Q1 2014 Earnings Call

Company Participants

- Eduardo Noronha, Chief Operating Officer
- Wilson Olivieri, Investor Relations Vice President

Other Participants

- Bruno Giardino, Analyst
- Carlos Macedo, Analyst
- Matthew Pascale, Analyst
- Rafael Frade, Analyst

Presentation

Operator

Good morning, ladies and gentlemen, and thank you for waiting. Welcome to Qualicorp's Conference Call to discuss the results of the First Quarter of 2014. We have with us today Mr. Seripieri Junior, the CEO, Mr. Wilson Olivieri, the Investor Relations Vice President, Mr. Alex Oreiro, the Financial Vice President, Ms. Natalia Lacava, the Superintendent of Investor Relations, and Mr. Eduardo Noronha.

This event is being recorded and participants will be in a listen-only mode during the company's presentation, after which we will begin the question-and-answer session, when further instructions will be given. (Operator Instructions)

I would now turn the floor over to Mr. Wilson Olivieri, who will start the conference call. Mr. Olivieri, you may proceed.

Wilson Olivieri {BIO 17325685 <GO>}

Thank you very much. Thank you all. Good morning. We appreciate you all being here with us today for this first quarter 2014 results. And we will start with Noronha giving the introduction. So, please, Noronha.

Eduardo Noronha {BIO 15227354 <GO>}

Thank you, Wilson. Good morning everyone. I would like to thank you again for participation in our conference for the first quarter of 2014 results.

We started 2014 following the trends of continued improvement of results, which we have already been shown in 2013, especially in the second half of the year. We have achieved adjusted EBITDA margin of 40.2%, 500 basis points better than the same quarter of last year, and an increase of 22.6% in revenues. We had efficiency gains in direct costs and expenses, especially in bad debt level, which returned to the historical level of 5% of our net revenues. Remember that our worst figure was 9.3% in the fourth quarter of 2012. You all can clearly see the evolution of the bad debt recoveries as the collection actions we implemented through this 2013.

Another highlight is the net additions, 20% better than the same period of 2013, resulting from the combination of 9.7% higher gross adds and 6.8% for churn. This also shows the results of our efforts with this churn, even in such challenging environment, we have face in this period.

Now, as usual, I will turn the word to Wilson Olivieri, who [ph] will detail this results, and immediately after that, I will come to speak about our future challenge. Wilson, please.

Wilson Olivieri {BIO 17325685 <GO>}

Thank you, Eduardo. So, as usual, if you are following the presentation, we posted on our website. I kindly ask you to please move to page four, because we have seen the highlights already that Eduardo has made. I'll try not to be comparative [ph] because I think Eduardo has touched the main point, but I'll give you some details on each one of this points, so we can better qualify the results we have this quarter.

So in page number four, you see the evolution of our portfolio slide. So as you can see, we're now managing more than R$4.6 million in total, out of which 1.9 million comes from our Affinity business that actually as you know, and we will see shortly, especially on this first quarter represented 92% of our revenue. This total number of lives has grown in the past few years by a CAGR more than 15%. But I think more important than that is, that the growth in Affinity for this very same period is being almost 26%, while the growth in our Corporate and Others is about 9.4%. So if you look at the pie chart to your right, you would see that right now we already showing Affinity representing 41% of the total number of lives, which is the highest level we have reached on this indicator in the past -- since the IPO.

So if you could please move to page number five. We give a little bit more details on how those lives have performed. So it's of course, it's easy to read it here. But the points that I want to highlight is, in total, with more than 4.6 million lives on our portfolio, we had grown better than same period last year, a rate of 4.1%, out of which this growth in Affinity specifically is 9.2% showing that we are in the trends that we have indicated to everyone here on an annual growth rate.

If you look at the gross sales, as we've been discussing with you, we are looking at an average for the quarter of about a little less than 33,000 last month, which is an important indicator and that keeps us in the good track to meet and Eduardo will talk about it shortly, it keeps us in right track to meet our targets for this year in terms of gross adds.

But most importantly, the growth that we seen in churn. It is interesting if you look in this slide, we see our gross adds growing at a 9.7% level, while our churn is growing at 6.8%. So we see a leveraging on those indicators in such a way that our net adds as it was mentioned, grew by 20% on that indicators specifically. It's not here in the presentation, but it is on the earnings release. If you look that on per regional basis, you would see that Sao Paulo, Rio have increased their participation a little bit when you compare to the prior quarter, mainly due to the sales of our (inaudible) lives in Rio de Janeiro.

And another region in Brazil that is performing a little bit better than expected is what we call the others for the Southeast region, especially in Minas Gerais and Espirito Santo, they are representing a better portion of our sales today.

So moving to page number six, the net revenue slide. As Eduardo already mentioned, we had grown sales revenue, but almost 23% rate when you compare to prior year. And being 23% out of Affinity and it's still not as high as 23% better than 15% rate to describe reasonable, growing Corporate and then others reaching almost R$26 million of revenue on that segment. If you see the comparison versus prior quarters, you see that we have reduced about 2%, but most importantly, if you remember, we had a few more lives in the fourth quarter that if we were to exclude those, we'd have seen growth of about 7% in the quarter as well.

In page number seven, we take a closer look at cost of services. And as you can see here, we continue showing our leveraging capacity. We had grown those expense lines by a little less than 20%, so even less than what we had grown sales, so leveraging on margins. Essentially the gross profit margin for this quarter has closed at 74.4%, which is about 70 basis points higher than what we had at the same quarter last year. And if we disregard the one-times that we had last year, we are seeing fourth quarter '13 margins at this very same level showing that we kind of stabilizing at this new gross profit margin higher than 74%.

In page number eight, moving to administrative expenses. We also see growth lower than 20%, it's about 18.4%, it's still maintaining our leveraging strategy. And if you were to look at this expenses as a percentage of net revenue, you will see that last year, there was -- at the same quarter, those expenses represented 29.1% of our revenues, while this quarter, it is representing 28.1%. So all of these gains that we are showing this quarter in the margin, we have about 100 basis points coming from leveraging administrative expenses.

Going forward that's probably relevant to highlight here is the line called third-party services, where we saw an extraordinary growth there, but there are a few reasons for those. As you recall, last quarter we announced the acquisition of a few units of Tempo. And for that, we had to hire lawyers and consultants, and part of those costs are already build into this line. We also have some success fees that we paid out of some successful events we've had in the fourth quarter.

If you remember, where at least two non-recurring items last quarter related to taxes that we actually paid the gross [ph] open this quarter. So that's why you see that specific line a little bit higher than others. But in over long-term, total administrative expenses is still helps margins for this quarter in about 100 basis points versus first quarter '13.

Selling expenses in page number nine, are growing in line with our revenue when you compare with prior year at a 23% rate. And more important here is to highlight two points; number one, the line called publicity and advertising that is actually marketing for us and if you all know that's a very discretionary line. So we have not invested much this quarter, but we do have a budget for 2014 total year. And we might be investing some of those budgets in the future quarters. So it was a low investment this quarter, because we felt (inaudible) already off the quarter would not require much. So therefore, you might see that line increasing a bit for the next few quarters.

And another line here that we're showing called other selling expenses that show a R$8.7 million of expense. It's basically growing due to as you all know, we're going to have the Soccer World Cup here in Brazil this year. And there are a lot of companies investing on that segment and we are not different than everybody else. So we did made some investments in World Cup. It's not related to the mass media like going to TV or radio, but it's related to a few specific actions that we are making to some of our VIP customers that if you are important. So part of that investment is here in this line called other selling expenses.

In page number 10. We actually take a closer look in two very important indicators, bad debt and other operating income/expenses. So talking about bad debt, which I believe is probably a star of this quarter. We were able to reach a level of 5% of net revenue with R$16.5 million of expense on that line.

And more important there is, what I'd like to highlight, we've always said to you our investors, that 5% of net revenue for bad debt is about the historical rates we've been discussing in the past few years, I would say back from 2011. But if you look at the current 5%, it does not have the same representation as historical 5%. Why is that? Because in the last couple of years, we have, as you all know, we've been still seeing a very challenging macroeconomic environment. So, reaching 5% on the challenging macroeconomic scenario at this point in time, it is a great achievement and it was a great challenge that we believe we have overcome. If you compare to the same 5% in the past, where we had no actions for recovering debt to that.

So if you look on the second group of the information, we called bad debt breakdown, you'll see that only for this quarter, we have been able to collect R$4 million worth of debt through that, bringing our total bad debt at R$16.5 million and this R$4 million represents 1.2% [ph] of our net revenue, which if we had not added we'd be looking at 6.3% worth of bad debt. So therefore, these actions we have been taking are really paying off looking at our results.

On the other operating income/expenses, we are not seeing anything different than what we have already seen in the past, meaning that we have reversal of some contingencies because they actually matured here in Brazil, which represented a credit of R$4.3 million. They were partially offset by some operational losses mostly coming from the constellation [ph] we have on payables or receivables with operators that amounted for 1.2 million, that in bottom line gave us a credit of R$2.5 million on this line of expenses this quarter.

In page number 11, our financial income and expense review. As you can see, nothing much to add here, the R$9.5 million that we see an income from short-term investment is higher than what we have seen in the past for mainly two reasons, higher level of cash that we carried throughout the last quarter and also high levels of interest rates demanded by the government.

The second line is interest and fine on late payment, basically follows the trend of our portfolio. So no new things there. I think that is important to highlight is the R$25.5 million of monetary adjustments coming from the call option especially from Alianca. If you remember last quarter, that amount was about R$50 million, because we had two adjustments building there. One related to adjustments of the projections of new (inaudible), because their performance better than expected. And the other is adjustment that basically called monetary adjustment, which is a recurring one.

So all of this 25.5 million, if we were to extract that, 17.7 approximately comes from monetary adjustments, deal of the 60% that we own from Alianca, which we only paid in the second quarter. So it still affects the first. So if you were to look at this number on the future basis, it should be a much lower pace, because we are now going to have projects monetary only for 40% of the acquisition, no more for the 60% we had to pay.

Talking a little bit more about EBITDA, which I think Noronha has already mentioned to you. Our EBITDA for this quarter was higher than a R$130 million, reaching a very interesting margin of 40.2%, which represented a growth of more than 40% when you compare to the same period last quarter. And although, we show here a slight reduction when you compare to the previous quarter, if you exclude the one-offs, out of this 135 million, we'd be looking at 130 -- and 122 million for recurring margin -- EBITDA for the last year, meaning that we will be showing growth higher than 7% on a quarter-over-quarter basis for that indicator as well.

Page number 13. If you look at adjusted earnings, I think we're very happy to say that our net income this quarter of positive at R$26.4 million, especially if you compare to the first quarter last year, it was 9.4, we show a very relevant growth there. And we don't have any extraordinary items at this quarter. If you look at the total cash earnings, which would be including controlling and non-controlling participation, we are shown here a R$112 million of this cash earnings, which represents growth of 48%, actually more than what we had growth in EBITDA that would be an EPS of about $0.40 per share.

Finally, getting close today, we're looking at CapEx condition, you see in page number 14. We have a regular ongoing CapEx investment for IT that would be exceptional for this quarter is the R$15.4 million of investments, it was the biggest (inaudible) coming from the change of our headquarters offices. As you know, we are in the process of moving. So we will for the first time in the history of this company have the ability or having all of the employees of Qualicorp, works [ph] in the building, which will -- in our field [ph] that increasing significantly efficiency among the department.

On the capital structure side, this is the second slide -- the second piece of the slide. We see our net debt growing a bit by 10% and the main reason for that or I would say, there were two main reasons. Number one, the Alianca adjustment, which comes out in the bad debt line. And also we did have a few extraordinary payments that we used our cash in the first quarter that we highlighted on our net earnings, but I'd like to highlight here for you. We had a payment for Golden Gross exclusivity agreement that we fluctuate [ph] last quarter of about R$40 million that we believe it will bring a lot of results in the near future, especially on our gross adds line.

We also have to pay, if you remember, Alianca results in the fourth quarter last year was fairly significant, because we're able to reserve a few taxes on the results. So the payable of that dividends for Alianca actually happened in the first quarter. And operationally, it will also help Unimed Paulistana with some advancements higher than what they used to have. So all of this together kind of used a little bit of our cash on the first quarter, they are not supposed to be repeated in the near future.

Finally, I'd take a new item that we are recommending everyone to look at, which is the return on invested capital. If you look at page number 15, you'll see that we have been consistently growing our return on invested capital stream second quarter last year, reaching levels at this moment higher than 30%. We've been considering all of the investments we have put it in together in our intangibles. So we should be looking at that indicator in the near future to make sure that the investments we are making in intangibles are actually reverting in good conditions for the company.

A couple of final comments that we highlighted on our earnings release. First of all, we had the (inaudible) announcement in last quarter. As you all know, we requested those to divest [ph] another 40,000 lives, which at the end of the day was a very good results based on our expectations. And we also announced Tempo acquisitions, and I think both of these cases we had specific calls, in a specific details, so no need to highlight regarding [ph] that at this point.

So I'd like now to turn this call over to Noronha for his final remarks, prior getting to the Q&A session. Noronha, please take it.

Eduardo Noronha {BIO 15227354 <GO>}

Thank you, Wilson. When we had that conference call for the fourth quarter of 2013 results, I talked about some expectations for the year. After a few months, I think it's worth to getting back to some of them. We talked about gross adds of 40,000 lives per month, and although, we have not yet reached this level in 2014. We are confident that we will reach at these averages this year with the implementation of the several sales strategies, we had already designed for this year. For example, regionalization on our strategy to implement some challenges and things like that.

We are maintaining our expectations for the net adds around 8% to 9% with the reduction of churn and with this is gross adds. We are very optimistic with our 100 basis points or more of EBITDA margin improvement. Although, we have started this year with higher than 40% margin, we will experience in this year paralysis of some expenses, for example, we will have to deal with two IT platforms and higher leasing expenses for the implementation of the headquarters, new headquarter office, as mentioned by Wilson, and with at least three months of duplicated [ph] account and the higher recurring monthly expenses. Once we are increasing our occupancy area, we need to accommodate our expected growth.

On the other hand, we have efficiency gain already captured in price adjustments of our portfolio, which should improve our margins. But we were comment to be careful, once this price adjustments may have reflects in churn and bad debt, it's a seasonal in our business.

We still talking about efficiency. We had our plans concluded to capture the gaps met during this EBB [ph] process that we mentioned before that we will implement in this year. And we should start getting these results during the second half of the year as planned.

And (inaudible) our biggest challenge in the short-term is our annual price adjustment management, which even though brings a positive impact in our short-term margins, it reduce our clients capacity to access the healthcare treatment. Even so, we understand there is still enough space to expand considerably our Affinity portfolio through our regionalization strategy, which will allow us to reach market with very good opportunity.

In parallel, we are advancing with our strategies in Health Management segment with the acquisition of health solution units for Tempo. We understand that there is a huge demand for those in efficient management models in the healthcare sector and then we are preparing ourselves to offer them to the market.

And finally, I would like to comment about the notice to the (inaudible) published last night. I'm leaving the executives team of Qualicorp to join the Board of Directors. This strictly related for personal reasons that prevents me from the voting a 100% of my time to Qualicorp. Therefore, we understand that it would be more appropriate, if I keep giving my contribution to the company via Board from where I will closely follow all the improvement projects that are being implemented. For now, the position of COO will remain open and the six Vice Presidents will report directly to CEO, to Junior.

And I will also take this opportunity to thank you all for your support and partnership during [ph] the time, I was in this role, wishing you all health and success. Thank you all. Wilson?

Wilson Olivieri {BIO 17325685 <GO>}

Yes. We may now go to the Q&A session. Operator, please.

Questions And Answers

Operator

Thank you. We will now start the question-and-answer session. (Operator Instructions) And our first question comes from Carlos Macedo of Goldman Sachs. Please go ahead, sir.

Q - Carlos Macedo {BIO 15158925 <GO>}

Hello, good afternoon gentlemen. Thanks for the opportunity. Congratulations on the solid results. Couple of questions, first, the ANS just suspended another 160 plans, I know it's very preliminary, but that'd be great if you had any insights on whether that can or cannot affect your results or your organic growth going forward over the next 12 to 18 months?

Second, you were -- Wilson spoke about a length [ph] about the bad debt expense and the recoveries. Quick question here, I mean, where should we expect this to settle? I know we're going into a more difficult macro environment here that should typically lead this to increase, you have the price increase midyear, which could be anywhere from 15% to 20%, which should affect organic growth, can increase churn. How do we expect these numbers both on the actual churn side and on the recovery side to behave through the end of this year? Should we expect a decline on the recovery side or should we expect an increase in the churn side? If you can give us some insight it'd be great. Thanks.

A - Wilson Olivieri {BIO 17325685 <GO>}

Hi, Carlos, good talking to you. Thank you very much for being here with us and for the question. Well, regarding the ANS, to be honest, two will be so involved in this call here that we had not an opportunity to look at, we know our sales team and our express, are already looking at it. Preliminary speaking what I could see was the few products from Unimed Paulistana, which we are currently selling, but I'm not sure they have the same model to sell. So it takes us even though we have fairly sophisticated expertise on that front. There are so many different products and so many different way, it takes us a couple of days until we can actually figure out what the main effect we have, and if we do have products to replace those specific products and regions. So I don't have any preliminary feeling to share with the investors, right now.

But as usual, we come in as soon as we have any news, we definitely let you know. So it's too early to say that it was good or bad, sorry, it's very fresh news at this market.

Q - Carlos Macedo {BIO 15158925 <GO>}

Okay. Wilson, then maybe a better question is in the past when this has happened now you've address, when there are plans that you can't sell anymore. How has been your experience in adjusting for that?

A - Wilson Olivieri {BIO 17325685 <GO>}

Well, great, thank you for the question, it gives a opportunity to explain. Then of course, it depends on the products and the region mainly. So let's say, when that first -- ANS first started doing that, one of the few companies that was hurt to us Unimed Paulistana. And we were selling Unimed Paulistana and the products that were suspended. But because the products were all here in Sao Paulo, most of them in the capital, we had several other choices with our operators like SulAmerica, Amil [ph], Bradesco. So we quickly replaced Golden Cross, we quickly replaced those products from Unimed in that region.

Now, we had a different experience end of last year when ANS suspended products from Golden Cross, where there were a few regions and one of the reasons why we end up cutting that deal with Golden Cross last quarter. A few regions where Golden Cross had products that we were marketing had no replacements at all. So you would only find comparing with that what we call the single Unimed, they are very region and very difficult to deal with. So we had no replacements on that -- those areas.

So, a direct answer to that question would be that depends a lot on the product and the region that the product is suspended. So if we do have all the choices of products in the region, we definitely recover that both sales fairly quickly. But if we are like Golden Cross, if you are talking of products in the regions that we don't have other choices, we may take a while and very candidly too, there were regions that we have Golden Cross, especially in the center of the country that we have no replacements of whatsoever (inaudible) release the products again. So it is a very broad answer, but that's how it works.

In terms of bad debt, as you mentioned, we have positioned ourselves, it hasn't changed. So if you remember, we are looking at 2014 would be only eight [ph] in the market, to be very conservative and we look at our bad debt as a percentage of revenue at a level around 8%. Even with that, we have committed an additional 100 basis points for margins this year. But considering that this quarter, we look at our bad debt rate about 5%, I would say trends for this year should be pointing out for probably lower number than the 8%. And whatever is lower than the 8% in each one of our projections, it could directly affect the EBITDA margin. So likely, we saw in this quarter, a 40% in EBITDA margin with the 5% bad debt level, if that remains the same then we could be potentially looking at margins increasing by 200, 300 basis points for the year.

Although, we are not only very conservative on our estimates this year, but we will comment the market to be conservative as well, because as we are properly said, we might see a price adjustment in the middle of the year that's higher than we have experiencing in past years. So therefore, we might have an impact in bad debt in churn that could be higher than our expectations. So considering those comments, I think we might be looking at probably lower rates than 8%, but if that comes to let's say 7%, that means our margins would have an additional 100 basis points of growth.

In terms of churn, that we have see a few advancements in this quarter, not only comparing with prior year, but also comparing to the prior quarters. We see that most of our strategies are paying out, most of our strategies are working well. But again, if we had to experience a price adjustment like 16%, 17% of our products that will be the third year in a row of double-digit price adjustments. So although we had benefits on our revenue, these are indicators especially churn that we should be more concerned.

So definitely you would not see churn growing at the same rate like we saw in 2012 and 2011. But they could grow at rates like they grow, if they grew in 2013, which was lower than the historic, but is still representing the effect of the price adjustment bring to our portfolio of lines.

Q - Carlos Macedo {BIO 15158925 <GO>}

All right. That's a great answer. Thank you so much, Wilson.

A - Wilson Olivieri {BIO 17325685 <GO>}

Thank you, Carlos. And if you need anything else, (inaudible). Thank you.

Operator

And our next question comes from the Mr. Rafael Frade of Bradesco. Please go ahead, sir.

Q - Rafael Frade {BIO 16621076 <GO>}

Hi, good afternoon everyone. Just maybe it's unfair to continue asking about this suspension in plans. But just give us a call on it, Wilson, from what I saw, it seems that most of your plans were suspended -- the plans that you sold from Unimed Paulistana. And if you could give us any idea of how much of your monthly sales came from Unimed Paulistana?

In addition, it seems that Golden Cross was not allowed to start selling again. So I would like to know if you already have another different plans with them to be able to sell?

A - Wilson Olivieri {BIO 17325685 <GO>}

Rafael, thank you again for the call. And again, this issue about the suspension is fairly fresh. But my initial reaction and please don't cause [ph] me in that, but my initial reaction. Yes, Unimed Paulistana, is the big issue of this time. I think you're fairly state, than we were like last call -- last time when there was Golden Cross, because Unimed Paulistana we have -- they're not good with products to replace those sales on a fairly good basis like we did it first time. So that should not be a major issue.

We are talking about potentially today anywhere between 2,000 to 5,000 lives depending especially in the first quarter, as you all know, softer than others. But if that is the only issue, I would not be concerned about it, Unimed Paulistana is probably one of the easiest providers we have to replace, because they have a lot of options in Sao Paulo.

In terms of the Golden Cross, yes, we didn't have two reactions in last quarter. Number one, a few products that ANS has released that we could good start selling again. And also a few new products that Golden Cross were out in the market that especially after we signed the agreement, we were allowed to sell and they are the part of our sales in the second quarter.

Q - Rafael Frade {BIO 16621076 <GO>}

Okay. Thank you.

A - Wilson Olivieri {BIO 17325685 <GO>}

Thank you, Rafael.

Operator

And our next question comes from Matthew Pascale of ShearLink. Please go ahead sir.

Q - Matthew Pascale {BIO 17304710 <GO>}

Hi, Wilson, how are you?

A - Wilson Olivieri {BIO 17325685 <GO>}

Very good. Thanks Matt. Good talking to you.

Q - Matthew Pascale {BIO 17304710 <GO>}

Sure. I had a question related to the new exclusivity agreement with Golden Cross. I know Golden Cross was suspended for some period during the quarter. Could you share with us a little bit about how many Golden Cross lives per month you guys were able to sell in Q1? And what this number could grow to under the new exclusivity agreement?

Also, are there any other agreements like this that you can talk about that will help us understand the bridge from around 33,000 live per month in Q1 and your target of 40,000 for the year. One thing I thought of was perhaps some benefits from the Clube de Saude brand?

A - Wilson Olivieri {BIO 17325685 <GO>}

Matthew, thank you. Actually, during the first quarter, we barely had sales for Golden Cross products. They were actually suspended, one of the reasons why our gross adds is softer than we would expect especially Golden Cross. If you look historically, Golden Cross, we were selling depending on the month, depending on our strategy, anywhere between 3,000 to 4,000 lives per month. And what we expect to do now with the exclusivity agreement, we know by fact they were also selling Affinity products to other minor competitors. But our expectations are to grow the Golden Cross, to use Golden Cross on our regional growth strategy. So therefore, we do expect to be able to grow that anywhere between 7,000 to 8,000 live by the end of this year.

So, this is surely part of our 40,000, because actually when we started talking about the 40,000, we do not expect to have this suspension from ANS. So the challenge that our sales teams is facing right now is actually not only to selling off, as we had already regional decline from the future quarters, but also to compensate somehow for the lives we missed during the first quarter. And we are pretty confident that with this agreement, we will be able to recover. Of course, we might not recover 100% of the lives with Golden Gross, but it might recover with other brands that we carry.

And especially in case that you mentioned Clube de Saude, which is our C-class product. We have already started selling in April, we do have a few sales. We have expectations that it should represent by the end of this year a potentials average of like more than 3,000 lives per month. So if you combine all of this the regional expansion, the Golden Cross products and exclusivity agreement, we included the Clube de Saude opportunities and a few others that we have already discussed in other calls, we are still confident that at this point that we could speak with the 40,000 lives per month average as a target for this year.

Q - Matthew Pascale {BIO 17304710 <GO>}

All right. Great.

A - Wilson Olivieri {BIO 17325685 <GO>}

Did I answered your question?

Q - Matthew Pascale {BIO 17304710 <GO>}

Yes.

A - Wilson Olivieri {BIO 17325685 <GO>}

Thank you.

Operator

(Operator Instructions). Our next question comes from Bruno Giardino of Santander. Please go ahead, sir.

Q - Bruno Giardino {BIO 15974970 <GO>}

Hi, everyone, good afternoon. Wilson, could you please share with us, what are your expectations on the new IT platform? Which activity is this new IT platform you perform? And also, do you have an estimate of how much in margins, you could save, how many bps you could have from this new platform? Thank you.

A - Wilson Olivieri {BIO 17325685 <GO>}

Yes, Bruno, thank you for the question, thanks for being here with us. And as we've been talking [ph] to the market just to have an idea, we are in the process during the second half of this year, so we're fairly close to that moment, that we will be able to migrate a -- we plan to implement this platform in three ways, let's put it this way. The first way, we have selected a few professional associations adding up to 17,000 lives, which will -- out of which we will test a few features of this new model. So that should happen during the second half of the year.

So not only I had mentioned, on this piece of this speech, during this period, we are going to have to carry two things, because one would be guaranteeing that the old platform still working, the new platform has an issue. And the other thing, we'll be working on the new platform. So once all of these features, the new features that we added for this 17,000 lives are up and running appropriately, we should come with the second way.

The second way, we should bring another 370,000 lives, out of our portfolio with specific new features that we should be adding to our gross profit. And then we would give those number of lives, another term, let's say, anywhere between (inaudible), as you will feel comfort about the new system is carrying appropriately all of these new lives and all of the features that we have added.

If all of that works appropriately, and if our (inaudible) works well, by second half of next year, we should be migrating 100% of our Affinity lives through the new system. In such a way that the way we'll be looking at early 2016, especially I would say second quarter, we would be able to gather the gains that this platform shall generate well.

And I'm just jumping the roofs directly to the end, there was the full system is implemented and up and running with no secondary systems around, we should be able to add another 200 basis points to our operating margins, mostly coming from operational activity, such as, call center, registration areas, billing process, collection process, these all should especially streamlining the sales cycle. So directly answer your question, we should be looking at second half of '16 generating this gains assuming that they would be growing slowly. But don't forget that during this past month, we have more like in cost increase than a cost reduction, due to that prior reason that we have to carry on the implementation front.

Q - Bruno Giardino {BIO 15974970 <GO>}

Okay, that's great and very clear. Just a follow-up, how much are these expenses for the second half, which I assume to be non-recurring, as I said?

A - Wilson Olivieri {BIO 17325685 <GO>}

Yeah. Actually there are two levels of expenses, one that is labor that you have to use in both systems. And the second group that would be under normal circumstances, they would be accounted for as CapEx, but because we have already -- making operation of few features, those CapEx will turn out to be expensive. So to the best of our estimates at this point of time, we would be looking an additional R$3 million per month approximately for the second half of this year increasing, in different line, they are now all allocated in one single department, but that's how we should look at.

Q - Bruno Giardino {BIO 15974970 <GO>}

Great. Thank you very much, Wilson.

A - Wilson Olivieri {BIO 17325685 <GO>}

Thank you, Bruno.

Operator

This concluses our question-and-answer session. I would like to turn the conference back over to Mr. Wilson Olivieri for any closing remarks.

A - Wilson Olivieri {BIO 17325685 <GO>}

So I'd like to thank you all again for being here with us in this call. And as usual, don't hesitate to call myself, Natalia, Jose and Gabriel. We are here to help for any answers you need. So looking forward for the next call for great results to come. Thank you all. Have a great day.

Operator

The conference has now concluded. Thank you for attending today's presentation. You may now disconnect your lines.