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SEER3.SA - Q3 2020 Ser Educacional SA Earnings Call

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CORPORATE PARTICIPANTS

Jânio Janguê Bezerra Diniz *Ser Educacional S.A. - CEO, Member of Board of Executive Officers & Director*

João Albérico Porto de Aguiar *Ser Educacional S.A. - CFO & Member of Board of Executive Officers*

PRESENTATION

Operator

Good morning. Welcome to Ser Educacional's conference call to discuss the company's results for the third quarter of 2020. With us today are Jânio Diniz, Chief Executive Officer; João Aguiar, Chief Financial Officer; and Rodrigo Alves, Investor Relations Officer.

We would like to inform you that this event is being recorded. (Operator Instructions) This event is also being broadcast live with audio and slides via the Internet at ir.sereducacional.com. You can also access the webcast, audio and slides through tablets and smartphones equipped with the iOS or Android systems. The replay of this event will be available soon after its conclusion for a period of 1 week.

Before proceeding, we would like to make clear that forward-looking statements may be made during this conference call relating to the business prospects of Ser Educacional as well as to its operating and financial forecasts and targets. Forward-looking statements are not guarantees of future performance. They involve risks, uncertainties and assumptions because they relate to future events, and therefore, depend on circumstances that may or may not occur. Investors should understand that general economic conditions, conditions in the industry and other operating factors may also affect the future performance of Ser Educacional and could lead to results that differ materially from those expressed in these forward-looking statements.

I would now like to turn the call over to Mr. Jânio Diniz, Chief Executive Officer, who will begin the presentation. You may begin, Mr. Jânio.

Jânio Janguê Bezerra Diniz - *Ser Educacional S.A. - CEO, Member of Board of Executive Officers & Director*

Hello, everyone, and thank you for coming to our results conference call.

Please go to Slide 4, where we present the main highlights of the quarter and recent events. We had an important third quarter of 2020 with our team dedicated to reducing the impact of COVID-19 on our company as well as working on creating opportunities to generate value for our shareholders, which we believe had very favorable developments to present.

Starting with plans to combat the impact of COVID-19, marked by the reopening of face-to-face classes in most of our institutional -- institutions, with priority to resuming practical classes since face-to-face theoretical classes could be applied via Ser Digital platforms, which made it possible to keep our students base solid during the year as well as fulfill their academic workload. We can consider it was a very positive result, supported by the relevant activities of supporting students with a very good credit profile, but with short-term financial difficulties.

In addition to the operational networks, we support the society, where we are establishing our qualities to service the educational institutes. We carried out various activities from donation campaigns, population awareness programs, partnership access, telemedicine, mass productions of hand sanitizers and even productions of respirators. I believe in the benefits that these initiatives generated for the society as well as the return to us in terms of recognition of our brands as they position themselves alongside our population in such a challenging moment.

At the same time, we took important measures for the company's longevity, such as reducing nonessential activities to produce cash if the operation situation had deteriorated, which fortunately didn't. And we ended this quarter, once again, without actually using any of the loans we contract to protect in case of negative cash flows along these years.

We also carried out an important real estate adjustment. In the first semesters, we made a wide renegotiations of our rental contracts. And in the second semester, we enhanced our operations with the reduction of leased space, and we reduced the 4 units in the cities of Recife, Manaus, Salvador and Maceió. It is worth mentioning that we maintained ourselves in all these markets, but now with a more adequate operation.

Another important step was to transform UNINABUCO and UNINABUCO Digital, transferring its [on-campus] activities to UNINASSAU and gaining a recognized brand to offer our new portfolio of course, what we are calling the digital class -- digital courses. With this, the UNINABUCO Digital, UNINASSAU Digital graduates and GoKursos courses were the programs of new forms of education that we launched this quarter. It was successful in its first quarter of operation, already surpassing the mark of 8,000 students enrolling.

Another highlight of 2020 will certainly be our new curricula, which is already in operation with our students being able to take advantage of the distance learning of up to 40% of total course workload, using the most modern education practice, which combines learnings through active methodologies with cutting-edge technology, allowing teaching through [Ser Digital] skills.

M&A is also playing an important role this year. As you could probably follow, because our proposal for the acquisition of Laureate assets in Brazil was passed over to Ânima Education. Last week, we received BRL 182 million as fine for terminating our agreement. In parallel, we also made an agreement with Ânima so that we have a bilateral option to purchase 5 educational institutions, which now are being evaluated by the company.

With that, we return it to our current business plan with the extra capital generating an extraordinary results for our company in a year that would only be year of challenges, and the year ended up become a year of positive results. And in terms of results, the quarter had a more pronounced seasonal effect as a consequence of COVID-19 as compared to previous years as it delayed academic calendar in this semester, driving a significant portions of the new enrollment and re-enrollment to move from September to October.

Even so, our operating cash generation was quite solid, reaching 106% of adjusted EBITDA. And our company continues with net cash of BRL 96 million. And probably, after the acquisitions and the Go Shop fine, it will continue with net cash or something very close to that.

In Slide 5, we show the next step. We are taking the launch of our digital course portfolio, which, as I said before, the success we reached in the first months of operations made us confident to bring more good news for you today. I would like to announce first-hand that as of November 2020, all Ser Educacional brands are offering digital course portfolio, which should drive new enrollment in this segment even faster due to the recognition of our regional brands.

Another highlight of the quarter was GoKursos, our open course market, which is following its innovation path. After the partnership with iG and [Barcelona], we are now in a partnership to distribute our courses in Magalu's marketplace. We are, therefore, a new type of distribution, that is the Brazilian retail e-commerce. GoKursos will be a very interesting platform in the future, and we are learning a lot from their potential to generate value and market potential of open courses.

On Slide 6, we show that we continue to take advantage of the intense acquisition pipeline that's happening in our sector. This year, we closed 2 transactions. The first one, FACIMED, an important institution in Rondônia state that has [7] medicine seats and a good student base in the health care segment, capable of helping us to increase our presence in the North region of Brazil.

The second is UNIJUazeiro, an educational institution strategically positioned in the Cariri region of the state of Ceará. This institution also has a good tradition in health care and is the second place in market share with good growth potential. I also highlight that the 2 institutions will become university centers in this coming semester. And for the next intake season, they will have a broader portfolio of courses to grow in these markets.

Our acquisition pipeline is to intensify in the coming months as we have some transactions in the due diligence phase and contract negotiations, some of which are at negotiation with Ânima.

Moving on to Slide 8. I am going to talk in detail our third quarter results, which, as I mentioned earlier, was a little achieved due to the calendar change as well as other side effects of COVID-19. To illustrate this effect, we put not only the result of third quarter trend in intake, but also an analysis comparing accumulated intakes between June and October.

As you can see, the improvement in face-to-face enrollment between September and October is clear. I believe that with our new curricula, we have a very solid classroom model for the coming years. The highlight of the quarter was our record distance learning intake, which was also boosted by the introduction of digital courses, reaching 75% growth when we analyze the results accumulated from July to October. We believe that we will be a recognized player in this segment due to the success of our strategy, quality of content and cutting-edge technology.

On Slide 9, we see the evolution of our student base, which continues to grow organically, driven mainly by distance learning and also due to the acquisition of [UNINORTE].

Highlight for the reduction of dropouts in September when compared to 2020 1st semester. In October, the re-enrollment base also improved significantly, which shows that, in fact, the greatest impact in terms of dropout was in the first semester. While in these semesters, we saw our students aiming to keep their academic activity.

Distance learning is no longer a promise. It is starting to become a reality, not only in intake growth but now significantly to our student base. The face-to-face segment remained strong, and we resumed growth in our view as of 2021.

Finally, we have analyzed our student base and average ticket on Slide 10. Let's start by analyzing the average ticket which is having stronger valuation due to stronger seasonal effects as a consequence and impact of COVID-19, which prolonged new enrollment and the re-enrollment season, increasing the impact of seasonal variation between odd and even quarters. This was also increased due to the higher share in out of pockets students in our total intake. We can also highlight the competitive environment, increase of student base in and the addition of UNINORTE that have lower average [registers the lower].

An interesting aspect is our student base is practically running out, and our health student is already 54% of the face-to-face student base, which is very positive from the point of view of the resilience and attractiveness of the course for the labor market.

[Official] comments. And now I will give the floor to João Aguiar to discuss the results for the quarter.

João Albérico Porto de Aguiar - *Ser Educacional S.A. - CFO & Member of Board of Executive Officers*

Thank you, Jânio. Hello, everyone. Thank you for the opportunity to present the results of the quarter.

On Slide 11, we present a summary of the quarter's results, which, in our view, are directing the company's results to something very in line with our expectations, with some seasonal and specifics generated by COVID-19 that are worth highlighting.

First, as explained by Jânio, the change in the seasonality of student enrollment and re-enrollment from September to October generated a transfer approximately of BRL 10 million in revenue recognition from the third to the fourth quarter. And it has a direct impact on the results between the quarters, but a [little] effect from the year of 2020.

Second, our operational discipline, which kept the cost and expenses structure well controlled for another quarter. In this quarter, we had a volume of nonrecurring effects greater than usual due to the return of 2 properties in the cities of Salvador and Recife. This is in line with our operational readjustment plan that we announced we would do since the beginning of the year. We also had a nonrecurring effect on payroll due to the same operational readjustments.

Third, no known impact in the increase in depreciation and financial expenses. Depreciation due to the impact of IFRS 16 on the acquisition of UNINORTE in financial expenses, mainly due to the raising of funds to protect our cash position by BRL 500 million.

On Slide 12, we have the breakdown of results between on-campus, new units, UNINORTE and distance learning. And once again, distance learning was the biggest highlight of the year in terms of adjusted EBITDA margin, but now becoming a line of business increasingly relevant to the company's results.

Distance learning is now representing 10% of our net revenue in the quarter and 8% accumulated, and more important, growing 37% year-over-year. All in all, it continues with an adequate pace of obtaining synergies despite Manaus being one of the cities most impacted by the effects of COVID-19 on our operations.

We believe that in 2021, we will have binding effect of generating synergies and [re-enrollment] base given that operations in general in each seats specifically started to respond more positively as of September.

On Slide 13. We include an analysis of our net income, segregating the effects of IFRS 16 from our results. See how this accounting effect ends up reducing our profit by BRL 23 million accumulated in the year, something that we believe is important to present because of these changes in accounting practice has been relevant. From the point of view of business, the [recurring] impact of net profit has been higher than demonstrated.

Moving on to Slide 14. We have analyzed our average collection period, which is a significant reduction in the quarter when compared to second quarter 2020. The average term of -- for regular students is now 100 days, already closer to the levels that would be ideal for an operation with our profile. Positive news that demonstrates that our credit recovery area is managing to collect a higher volume of receivables. And as a result, our provision, despite having been higher versus last year, is decreasing compared to the second quarter of '20. The average term of FIES receivables is higher than expected, but this effect tends to be reduced over the next quarter as cash economic at federal normalizes its operations, something that has not yet this year.

On Slide 15. We show our operational cash generation remains. As I mentioned earlier, it's due to the intense work that we carried out this year, aiming, on the one hand, to be flexible with our students in order to facilitate their permanent study; and on the other hand, quite in the process of collections collecting arrears.

It should be noted that this cash generation in the quarter was few, given by the increase in the FIES average payment term, which means that we have a favorable forecast for the next quarters when these payments will be regularized.

On Slide 16. We present our CapEx that just, as occurred with our costs and expenses, was reduced due to the impossibility of carrying out of works and certain investments, and thus, closed the 9 months '20 in about (inaudible) of the net revenue.

And on Slide 17, we have a more detailed view of financial indebtedness. We have another quarter which put the company in a very healthy situation, which will probably leave with cash even after the payment of recent acquisitions due to the cash inflow from the Go Shop fine, which will generate a very positive result this year.

Those were my comments, and now I will turn the floor back over to Jânio for the final remarks.

Jânio Janguê Bezerra Diniz - Ser Educacional S.A. - CEO, Member of Board of Executive Officers & Director

Thanks, João.

Let's please go to Slide 19 to summarize our short- and medium-term perspective. We are very confident with Ser Educacional's results for the first quarter as our activities are very much in line with our budget. We're now keeping up our distance learning, which showed strong growth this year, now helped by the digital course that are generating [course] initial results.

Another positive aspect is acceleration in the continuing education segment. And as you can see, both digital post graduate course and GoKursos courses are advancing consistently. Besides (inaudible), synergies of risk and acquisitions, UNINORTE, already has been positive to the results as of September, FACIMED and UNIUAZEIRO.

We also have a solid pipeline of acquisitions as well as maintained a very favorable financial position to take advantage of this movement.

Finally, we believe that the economic activity will return to its normal, and that 2021 is likely to be a year of recovery for the sector. And we prepare for it -- it will be ready to benefit from this recovery.

Those are my comments. And now we give to the sections of questions and answers.

Operator

(Operator Instructions) Thank you. That concludes the question-and-answer session for investors and analysts. I would like to pass the call back to Mr. Jânio Diniz for final considerations. Mr. Jânio, you may proceed.

Jânio Janguê Bezerra Diniz - *Ser Educacional S.A. - CEO, Member of Board of Executive Officers & Director*

Thank you all for participating in the disclosure of results. And our IR, relations investor, on hand to help you with further questions and information you need. Thank you, everyone, and have a good afternoon.

Operator

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

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