Conference Call Transcript

Operator:

Good morning, ladies and gentlemen, and thank you for waiting. At this time, we would like to welcome everyone to DASA's 2Q14 Earnings Results Conference Call.

Today, we have a simultaneous webcast that may be accessed through the website, www.dasa3.com.br. The slide presentation may be downloaded from that website as well. There will be a replay facility for this call on the website for a week.

Before proceeding, let me mention that forward-looking statements are based on the beliefs and assumptions of DASA and on information currently available to the Company.

They involve risks, uncertainties, and assumptions because they relate to future events and therefore depend on circumstances that may or may not occur in the future.

Investors should understand that general economic conditions, industry conditions, and other operating factors could also affect the future results of DASA and could cause results to differ materially from those expressed in such forward-looking statements.

Today with us we have Mr. Dickson Tangerino, CEO; Dr. Octavio Fernandes, VP of Operations; Mr. Marcio Fernandes, VP Administrative and Finance and Mr. Paulo Bokel, Investor Relations and Financial Officer.

Now, I will turn the conference over to Mr. Paulo Bokel, Investor Relations and Finance Officer. You may begin your conference.

Paulo Bokel :

Thank you. Good morning and good afternoon everyone. Thank you for listening to our earnings conference call. Let us start on slide number three, where we will cover DASA's growth, quality and return for our shareholder.

Our gross revenues reached R$743.8 million this quarter, up 6.5% from 2Q13. The largest increases were lab-to-lab with 10.8% and outpatient with 7.8%. This quarter we were impacted by the World Cup, with a high number of regional holidays during match days in host cities, part-time work hours on the days that Brazil played and the people major focus on the event, which led many people to postpone medical visits and examinations. We delivered eight renovated units, as well as four new MRIs and one new CT scan. We also opened seven new units.

We were represented with the speakers at the Main Radiology Event Worldwide including São Paulo Radiology Day, Magneton World, International Society of Magnetic Resonance and Medicine and American Society of Neuroradiology.

We continue to modernize the central lab in São Paulo with the conclusion of the New Pathological Anatomy Area, an investment in Analytical Chemistry and toxicology equipment, as well as molecular biology equipment.

This same lab was recertified by the College of American Pathology, CAP, which has been the renowned international reference for clinical laboratory best practice. In addition, at the Central Lab of Brasília, we completed the first phase of the Full Automation project, which consists of installation of a 100% automated conveyors. That equipment has already been successfully implemented at the Duque de Caxias lab in Rio de Janeiro, and the lab that serves the public market in Sao Paulo.

DASA doctors were responsible for 48% of all Brazilian papers and for five of all papers presented at the AACC 2014, the most important event of clinical analysis in the world. This reinforces DASA's position of excellence in the medical world.

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Regarding shareholder return, our EBITDA reached R$115 million in the 2Q14, 3.8% higher than second quarter last year, with a margin of 16.7%. The operating cash flow reached R$86.6 million and cash earnings reached R$38.3 million for the quarter.

Turning now to slide four, I would like to highlight that the following numbers are not adjusted by the World Cup effect. The Company's gross revenue reached R$743.8 million, up 6.5% in comparison to 2Q13, with 6% growth in image and 6.7% growth in clinical analysis.

Moving on to slide five, the units grew by 7.8% in 2Q14, with same-store sales reaching 7.4%. The growth of image totals 7.5%. 8% growth in clinical analysis. We continue to increase the average requisition price when compared to 2Q13, which was 18.5% higher or 13.8% due to the richer image mix with the modernization expansion of the technology part, mainly MRI and CT scan equipment, as well as increasing the number of clinical analysis tests per requisition, which also impacted the increase in average requisition price.

Moving on to slide six, hospital market revenues reached R$71.7 million, up 1.5% for the quarter. The average ticket increased 4.6%, reaching R$67.7 due to the last year's cancellations of less profitable contracts, as well as the entry of more profitable contracts during the last year, which affected the clinical analysis and image mix.

Moving on to slide seven, revenue from the lab-to-lab market reached R$81.6 million, 10.8% higher for the quarter. The growth of revenue per lab was 10.9%. We are continuing with this strategy of increasing capillarity, prospective new customers and opened new logistics routes, as well as seeking to improve the product mix for existing customers, with new service and higher volumes for certain specialties. Revenue per requisition grew 6.5% resulting from the richer image mix and increased exams per requisition.

Moving on to slide eight, in the public sector we achieved a revenue of 44.1 million, a 6.7% reduction from 2Q last year. We continue to be very selective in choosing new customers.

Moving on to slide nine, we are going to talk about expenses. In the 2Q this year, the cost of service totaled R$445.6 million, 8.7% higher than 2Q13, reaching 64.8% of net revenues. Personnel cost increased 16.4% from 2Q13 due to the hiring of new employees to support the operation and the collective bargain agreement in Rio and São Paulo.

Material costs increased 14.9% due to the strong growth in clinical analysis mainly in the lab-to-lab market in which the percentage end cost of material in the price of the exam is far superior to the outpatient market and also due to the greater complex of exams and the increase in input costs.

Services and utility cost declined by 1.2% due to the contract renegotiation. Under this line, we have the cost of medical reports, which were impacted by the 6% increase in image.

In slide 10, cash operating expenses were R$126.8 million, compared to the R$110 million in the 2Q last year, impacted by the hiring of employees and the collective bargaining agreement mentioned earlier.

Moving on to slide 11, our EBITDA reached R$115 million, 3.8% higher than the R$110.8 million reported last year. We reached a margin of 16.7%.

On slide 12, regarding income tax and social security contribution, we achieved a cash rate of 18.4%.

Moving on to slide 13, we have maintained our rules in the provisions for doubtful account where a 100% of the titles above 360 days of provision. The average collection period is 85.3 days. The level of provision for doubtful accounts and deduction was 1.3% of gross revenue this quarter, compared to 8.6% during the 2Q13. There is a downward trend in the area of

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deduction, due to the range of actions that we are implementing for this quarter, the magnitude of this decrease was larger due to recovery of specific credit.

On slide 14 we show our operational cash flow, which reached this quarter R$86.6 million.

On slide 15, we present the Company's debt profile. The Company's debt is almost entering CDI floating rent, ending that reduction trend in terms of cost. We have enough cash to meet the maturities of debt for the next 12 months. Our net debt table was a decline trend. Upon entry of the controlling shareholders, the Company could retain similarly financing from BNDES, with long-term and flat fixed rate, which will further improve the debt profile.

On page 16 we have our return on invested capital. This quarter we reached 10.7%. The Company is focused on maintaining our invested capital at levels above the cost of capital. This is the fifth quarter in a row that the Company is improving its return on invested capital.

In relation to the CAPEX on slide 17, we reached R$34.7 million with the opening of seven units and eight renovations completed, as well as four new MRI and one new CT scan. We will remain focused on opening and expanding for the rest of the year.

On slide 18, we have the final remarks. Considering the World Cup, the quarter had a strong growth for business sale of 15.7%. This reflects our goal of constantly in revenue improving the Company's performance. We have focus on improving the quality of operations, both for patients and shareholders seeking higher profitability. We are expanding the Center Lab of São Paulo in Brazil based in our piling process of total lab automation.

We continue to bring cutting edge technology to our Company. We have purchased new equipment for our Central Lab in Sao Paulo, installing the new equipment on CT scan and MRI, which show our commitment, quality of our operation.

We have faced big challenge, and other big changes still lie ahead of us, but we are gradually taking control of cost expenses and CAPEX of the Company, at the same time that we are modernizing our facilities in seeking price that is consistent with our service. We continue to see improvement on return on invested capital which reached 10.7% this quarter. In view of that, our net income decreased 3.2% in the 1H, increased by 3.2% the 1H14.

And now we will begin our question and answer session. Thank you very much.

Guilherme Assis, Brasil Plural:

Hi, good afternoon, everybody. Thanks for taking my follow-up question. My question is about the top line growth for the quarter, and looking forward what should we expect, I understand that the calendar impact in this quarter had a negative impact on volumes, so we should expect that to increase going forward, right?

But I would like to understand a little bit more on that, how the pricing policy has been for the company and the mix effect that we saw that led to rather healthy top line growth despite the weak volumes during the quarter, right.

So I like to understand how has been the pricing negotiations with the payers and what we should expect of mix going forward. We saw that there was a pickup in the emerging services growth this quarter, should we expect that to continue to have a positive impact on the average ticket for the Company. That is my question. Thank you.

Paulo Bokel :

The average ticket for requisition are basically influenced by the number of exams per requisition that is going up. The trend that we are seeing is basically ranging from 5% to 10%, it

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really depends where and which plan or which brand that we have, but it is going up and helps a lot of the average price.

Also in terms of mix, we invested a lot of money in new equipment and hired new doctors providing new services to the market, and basically MRI's and CT's are the most expensive exams that we have, and if we can increase the number of exams from this equipment, basically the price also goes up.

We have not started yet the renegotiations with the big players. So, basically we are going to see that in the second quarter of the year. What we can see about the price ranges that the price increase that we have to offer in the market, basically the ANS gave almost 10% for the particular plan.

So basically we don't know how much we are going to get, but 10% is what the client have to pay, a slight increase at least for the particular one.

In going forward the main driver of growth really is business day, it is very important, and basically this is going to be the main driver I think for the growth of the Company in the 2H on top of getting more exams per requisition, more image exams. There is a lot of image mix, you mentioned you have the mix from the brand, that we basically do not control, we have the mix from the payers, which is also hard to control, and also the segments that we operate.

Guilherme Assis:

OK. So going forward, if we have a positive impact from calendar from business days, and the carry, and the deposit carryover impact of the average ticket that you had, which was 13%, we should see better growth in the 2H14, is that what you are expecting there?

Paulo Bokel :

We do not give guidance. But we have been mentioning since last year that the 2H14 would be much stronger because of this kind of seasonality effect that the World Cup showed us. I think a lot of schools were on vacation earlier this year in June. So, a lot of people, instead of staying at the World Cup, travelled at the time of the year. So basically, it is going to very, very strong. The main quarter for us obviously is going to the 3Q14.

Guilherme Assis:

And do you expect any negative impact from the World Cup in the 3Q, related to July or do you think that the World Cup impact happened in June only?

Paulo Bokel :

We have some in the beginning of July, but basically the month of July proved basically normal because people just did exams right after, so we had a regular growth that we expected for July.

Guilherme Assis:

OK. So, no impact in the 3Q, right?

Paulo Bokel :

Yeah, it was not really anything meaningful.

Guilherme Assis:

OK. That is very clear. Thank you.

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Bruno Giardino, Santander:

Good afternoon, everyone. The level of cancellations reduced materially in the 2Q and I would like to know if this is a norm going forward. First, why did this happen and if you think this level could persist in the following quarters. That is my first question.

Marcio Fernandes:

The allowance we presented this quarter has been impacted by one specific negotiation with an important and large player, which generated reverse of provisions of bad debt.

Having said that, it is worth mentioning as well that we are now reaping the fruits of operational improvements in the receivable department and the results of such efforts eventually take some time to appear.

So, I would say that we are more likely to see figures closer to the average of the last six or 12 months than to see this quarter still going forward.

Bruno Giardino:

OK. Very clear. Understood. And my second question would be, recently the National Agency issued a new resolution saying that healthcare plans need to set a contract with providers establishing an index to reduce the prices and that this resistance need to be on an annual basis in the first nine days of any given year. So, do we expect this resolution to change the negotiations between payers and providers in the industry? Do you think this can be material going forward?

Paulo Bokel:

Bruno, basically, with the incorporation of our Company with MD1 we are basically negotiating a lot of things with payers and health plans, but it will help, but it really depends on which terms you are going to negotiate with the big plan. The small plan really you can basically put what you want, but the big plan does not work like that and basically we are negotiating right now with them. So, we do not have a specific answer for this question for you.

Bruno Giardino:

OK. Thanks.

Operator:

There are no questions at this time. This concludes the question-and-answer session. At this time, I would like to turn the floor back to Mr. Paulo Bokel, Investor Relations and Finance Officer for any closing remarks.

Paulo Bokel :

Thank you very much for you attention. We are looking forward to meeting you in the next earnings call next November. Thank you very much and have a nice day.

Operator:

Thank you. This concludes today's DASA 2Q'14 Earnings Results Conference Call. You may disconnect your lines at this time.

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