

Conference Call Transcript
1Q15 Results
Ourofino (OFSA3 BZ)
May 6, 2015

Operator:

Good afternoon, ladies and gentlemen, and welcome to Ourofino Saúde Animal 11Q5 Results Conference Call. Today with us, we have Mr. Dolivar Coraucci Neto, CEO and Mr. Fábio Lopes Júnior, CFO and IRO.

We like to inform you that this event is being recorded and simultaneously translated into English and all participants will be in listen-only mode during the Company's remarks. After that, we will start the Q&A session, when further instructions will be provided. Should any of you require assistance during the call, please press *0.

The audio-track and the slides of this teleconference are being simultaneously webcast by Internet at ri.ourofino.com. At this address you will identify the banner under the title webcast 1Q15, which will lead you to the presentation.

Before moving on, we like to make it clear that forward-looking statements made during this call concerning the Company's overall perspectives, operating and financial targets are based on the Company's beliefs and assumptions and as well as our information currently available.

Forward-looking statements are no guarantee of performance. They involve risks, uncertainties and assumptions because they refer to future events, which may or may not materialize. Investors should have in mind that general economic conditions, industry conditions and other operating factors may affect the Company's performance in the future and thus lead to different results from those expressed in these forward-looking statements.

I would like now to give the floor over to Mr. Dolivar Coraucci Neto, who will start the presentation. Please Mr. Coraucci, have the floor.

Dolivar Coraucci Neto:

Good afternoon, everyone. Thank you all for participating in our conference call to discuss the results for the 1Q15. In the 1Q15, we were consistent with our strategy of growth and value generation for our shareholders. When we compare the same period of last year, our net revenue from sales grew 16%, our net profit grew 34% and our EBITDA grew 14%, and we also launched two new products.

These good results make us confident that we have necessary stamina to face the challenges lying ahead this year. Also according to recent market information concerning the year 2014, and which were announced by SINDAN, we have confirmed our third place ranking in the industry, because of our growth of 12.33% in the period, which was a percentage above that of the market.

Our market share moved from 9.81% in 2013 to 9.93% in 2014. This happened even with the approval in May of Regulatory Instruction IN-13/2014 by the Ministry of Agriculture, which suspended the sales of long action avermectins and consequently made it

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impossible for us to sell important products in our portfolio, starting in June 2014.

We would also like to highlight the anullment at the end of March 2015, of the above mentioned Regulatory Instruction, which allowed us to resume sales of our Master LP product, which is a leader in the endectocide market. Our team is motivated and committed to deliver results.

I would now like to give the floor over to our CFO and IRO, Fabio Lopes, who will comment on the financial results for the 1Q15.

Fábio Lopes Júnior:

Thank you, Dolivar. Good afternoon, everyone. In the 1Q15, our results were in line with our plans, our projects. We managed to reach our goals and we grew in sales, EBITDA and net profit.

On page number three, we highlight the growth of our net revenue at 16% in the year, which moved from R\$75 million in the 1Q14 to R\$87 million in the 1Q15. On the same slide we have a breakdown of the contribution from different segments and production animals, companion animals and international operations in our net revenues.

In the 1Q15, the production animals segment represented 78% of our net revenues. The segment of companion animals accounted for 17% and international operations accounted for 5% of the total.

On slide number four, we have a breakdown by segments. As for production animals, our net revenue moved from R\$58.3 million in the 1Q of last year to R\$68.2 million in the 1Q15, and an increase of 17%.

As for companion animals, net revenues in the 1Q15 grew by 26.3%, moving to R\$14.9 million. One of the factors that drove that growth was the consolidation of launches at the end of 2013 and throughout 2014, including products at NEOPeto the Leevre dog leash.

As for international operations, we had a drop of 20.4% in revenue, when compared to the 1Q14, reaching the level of R\$3.9 million in the 1Q15. That segment was impacted by the fact that we could no longer sell to Venezuela.

On slide number five, we can see the gross profit and SG&A. In the 1Q15, gross profit grew 9.6% reaching the level of R\$51.3 million. There was a drop in gross margin of 3.4 p.p., which reflects a less favorable product mix in the quarter. Besides, in the same period, we had inventory adjustments.

As for SG&A, we had a dilution of 3 p.p. over net revenues, reaching an amount of R\$41.7 million. SG&A over net revenue remained at 50.9% in the 1Q14, as opposed to a level of 47.9% in the 1Q15.

On page number six, we will analyze the 1Q15. In terms of EBITDA, we see a growth of

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13.8% in that front, reaching R\$14 million. The EBITDA margin was practically in line with the 1Q14.

On slide number seven, we see net financial expense, income tax and social contribution expenses and continued operation profits. Our net financial expense showed an important drop of 75% in the 1Q15, which can be explained by the amount of capitalization coming from the IPO, which helped to reduce our net debt.

Our expenses with income tax and social contribution were higher in the 1Q15, reaching R\$1.4 million, an effective rate of 15.7%. Such expenses reflect an increase in taxable income also arising from a better overall result.

In the 1Q15, continued operations profits grew 33.9%, moving to R\$7.5 million, as opposed to R\$5.6 million posted in the 1Q of last year. Strong growth in net profit is driven in the first place by an increase in net revenues. And secondly, and materially, because of a dilution in SG&A, which offset that drop in gross margin. Besides that, there was a significant increase in the financial results coming once again from the IPO.

On slide number eight, we will be talking about our bank debt. In the 1Q15, net debt over EBITDA ratio, over the last 12 months was 1.27x, as compared to 2.16x posted in the same period of last year.

Our short-term indebtedness, half of which is referred to debt with Finep and BNDES, which were transferred from the long term to short term. The other half has to do with the working capital, which was contracted before the IPO and out of which R\$18 million have already been amortized in early April 2015.

As for this facility with FINEP, which was contracted in December 2014 at the amount of R\$107 million, the first disbursement has taken place at R\$42 million in early March 2015.

On page nine, we show results from investments in R&D and the launches which took place in the 1Q. We have two launches in the quarter; both antimicrobials in the segment of production animals. Lactofur is the first one, which helps to prevent infections in dairy and beef cattle and also in pigs; and the Ciprolac Dry Cow, which prevents and heals mastitis, an inflammation into mammary glands of cows.

On page ten, we have a picture of our daily performance of our share from the IPO until the end of 2014. At the IPO, we were at R\$27. On March 31, we closed the day at \$28.68, an increase of 6.2% in the period. Comparatively, Ibovespa dropped 5.8% in the same period.

In closing, on slide number 11, we would like to highlight our growth in net revenue, which was at 16%, an increase of 14% in EBITDA, and there also increase in net profit; it goes to 34% and the launches of two new products.

The performance in the 1Q reinforces our expectations that 2015 will be a year of good results for Ourofino. We are motivated to seek our target with determination, credibility and

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agility.

Thank you all for your attention.

Joseph Giordano, JPMorgan:

Good afternoon, Fabio. Good afternoon, Dolivar. Thank you for the call. I have a couple of questions actually. I would like some more color in terms of R&D, you launched two new products in the 1Q, but, as I understand, in the pipeline there were products to replace the long action avermectin.

So, what was the strategy you followed in the 1Q given the fact that now you have avermectin back in the game? You probably are focusing on that for their winter campaign. So, what can we expect in terms of that pipeline? Thank you.

Dolivar Coraucci Neto:

Good question, Joseph. Actually, we have different recommendations of management for producers. As the long action product is a strong tool to give a more rational management of the Brazilian productive system, which is a system where we use a lot of pasture, then we have with different scenario.

Before avermectin had been liberated, we were working with a scenery where we would need to adopt new management practices, but now we went back to using concentrated avermectin. So we go back to the management we used to have before.

So this way we have repositioned the product, which is a product, again, which is a very promising tool, which is a product that has a level of Eprino, which is very, very low. So, as an endectocide, it has a place in the Brazilian market. So our idea is to reposition that product to launch it as of August.

Joseph Giordano:

Thank you, Dolivar. Another question, if I may. Concerning the regulatory front and in the last month we saw the government giving more flexible signs in terms of safety rules. Do you foresee any change going forward? Do you think government tends to be less restrictive? What is your vision for the government going forward?

Dolivar Coraucci Neto:

Joseph, in our opinion, we believe that about perhaps the bio safety rules remain robust and strong, but what happened was, that there was a readjustment on the part of the companies which we have some kind of outstanding issue with the government. So what they did was to work towards eliminating any potential risk to human health or to the veterinary safety of the country.

So my belief is that we remain competitive and that the bio-safety rules are quite proper,

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quite adequate, for the moment we are going through. Looking ahead, looking forward, I think the more regulated, the more you are adjusted to best practice and safety, the better for everyone.

Joseph Giordano:

OK. Thank you, Dolivar.

Giovana Araújo, Itaú BBA:

Hello, everyone. My first question has to do with this revision for inventory, if you could share with us the amount concerning that inventory adjustment.

Fábio Lopes Júnior:

Hi, Giovana. It is a normal procedure for the Company, a couple of products which had expired in inventory, that is normal, nothing out of the ordinary for the Company. But because the value in the 1Q is significant, because of the low revenue level, it impacts a little bit. So, we just wanted to make that stand out, but it is nothing really out of the ordinary, but because it affected the gross margin, we made it a point of including that.

Giovana Araújo:

So, the main explanation for the drop in gross margin comes from the product mix? Am I right in understanding that? On top of the fact that you showed abroad?

Fábio Lopes Júnior:

Yes, the 1.5% comes from the inventory adjustment and 1.9% is driven by that issue with the mix, as you mentioned, because the external market accounted for lower volume, that of course affected the cost for the other lines. But that is not a source of concern for us, because, as I said, it is a seasonable occurrence for the 1Q.

Giovana Araújo:

And the second concerning your average rate, concerning to taxable income, your income tax rate was at 15.7%. Does that include the presumed profit too?

Fábio Lopes Júnior:

Giovana?

Giovana Araújo:

That 15.7% rate does it reflect or rather, going back our expectation was of a higher rate for 2015.

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Fábio Lopes Júnior:

Exactly, we do not expect that rate of 15.7% to last throughout the year. We consider that to be a low rate for the 1Q, but at the end of the year, our forecast is of a higher rate, closer to 23% or 24%, also because profit tends to increase in the coming quarters.

Giovana Araújo:

OK, thank you. And lastly, if you could give us some color on how you see now the impact of that fact that you have resumed sales of the Master.

Fábio Lopes Júnior:

Well, as I said in our last call, we are already selling the product. We are not formally positioned in that market as Dolivar has explained. We are waiting for the first campaign to close, but, in any event, the product has been well accepted by the market and we are still in the phase of quantifying the effect in the Company's numbers for the year as a whole.

Giovana Araújo:

OK. So for now, you are confident that numbers will be good for the year?

Fábio Lopes Júnior:

Yes, definitely. The 1Q reinforces our confidence that we will have good numbers throughout the year. In other words, 2015 should be a good year for Ourofino.

Gabriel Lima, Bradesco:

Good afternoon, Dolivar, Fabio, everyone. Congratulations on a good start of the year. I understood the remarks you made about the market share for 2014, when you compare it to 2013, but I would like to hear from you, what would be the perception that you have in terms of the competition, the market shares in the 1Q until April, and if you remain confident that Ourofino will consolidate those market share gains you have experienced in the past years.

Dolivar Coraucci Neto:

Hi, Gabriel. Thank you for the question. I think we have a strategic position, which is very much in line with the Brazilian agriculture advancements. It is part of our guidance to carry on with the work of taking technology to the field and that is why we are always concerned about launching new products, and as we do that, we are very careful in launching products that may make a difference at the Brazilian agricultural scenario. So that will consequently takes us to a very good competitive level and will leverage our position in the whole chain.

So we are, yes, to answer your question, confident in that process, but we are cautious,

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not just because we have enjoyed significant success in the past years, but also because we are trying to reach those initiatives that we still need to pay closer attention to. So, all of that gives us the confidence that we are working towards increasing even more our market share.

Gabriel Lima:

OK. Well, remember when you talked about market share of 10.5% at the time of the IPO was a one-off isolated figure and we close the year at 9.93%. That difference arises from the avermectin suspension would you say?

Fábio Lopes Júnior:

Gabriel, in the 1H of the year, if we analyze the 1H, we had a very strong growth. So, when we analyze the market share in the 1H14, our market share was a bit above that, but we like to see the picture including the whole year, and then we see, of course, an impact of the avermectin issue, especially the Master product.

This means that even without that product, which was our main product, we are still growing above market levels. In other words, if we have had the chance to work with that product, our expectations would be to have grown even more than we did.

Gabriel Lima:

OK. That is exactly what I thought. Thank you, Fabio. And lastly, I know this was asked, but just to make sure, why has the foreign market presented such a significant drop? Is it just because of Venezuela? Your expectations, as I see, are that that market will improve throughout the year, it is a market that presents good margins. So why do you expect it to improve? And also please explain a little more what the problem was leading to those results?

Fábio Lopes Júnior:

Yes, it was a one off isolated problem with Venezuela in the 1Q. We can no longer count on those sales for the half of the year, but we do believe that international operations are very important growth trajectories for the Company in the long run, in the next three to four years.

We may have some disconnect quarter-on-quarter, but when we analyze longer periods, an effort of concentrating more focus on countries such as Mexico and Colombia, makes us confident that that growth will generate significant growth.

Gabriel Lima:

OK. In other words, the focus will be on other countries, Mexico and Colombia for example, to offset the drop in Venezuela, am I right?

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Fábio Lopes Júnior:

Exactly, exactly right.

Gabriel Lima:

OK, thank you. Have a nice day.

Marcio Montes, Banco do Brasil:

Good afternoon, everyone. Thank you for the call. We are talking about taking technology for the field, helping Brazilian and agriculture and my question is referring to the plant. You are working on new technologies, you are complementing your product lines. So I would like to have some more color and the status core of the plant, as we speak.

Dolivar Coraucci Neto:

Thank you for the question, Marcio. We are totally in line with our development schedule concerning biologicals. Our plant has a schedule that spans for year or year-and-a-half. We are now concluding the first phase, which is the conclusion of the main building. We have already finished technology transfer center, they work with the preliminary phases of product development and then the plant where the final processing will take place is underway.

Marcio Montes:

OK. So you mentioned you are going to the preliminary phases, but you are enjoying a significant success in your new launches. Perhaps, if you do not have the plant ready to roll, would you expect some kind of delay in new launches because of that?

Dolivar Coraucci Neto:

All development processes have, of course, a series of phases which do not take place or cannot take place within the plant. You have to go through a series of preliminary phases. In any event, until you get to the final phase of plant construction, you can have a series of products that will reach the market and which are not produced at that plant. They are made elsewhere.

Marcio Montes:

OK, thank you.

Pedro Ferroni, CTM Investimentos:

Good afternoon, Fabio and Dolivar. Congratulations on your results. The first question has to do with the following; would you have time to analyze the National Plan of Agricultural Defense, which was launched this morning by the presidency? And if you did, do you see

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any new regulation arising or new rule arising that might benefit or harm the Company? We also see that that plan includes new regulations for veterinary generic drugs, will that affect the Company's development?

And the second question is, talking about the external market. How do you intend to grow in the external market, given the fact that you have high quality in distribution here in Brazil, you have people close to the producers? Do you plan to do the same abroad? How do you intend to expand abroad?

Dolivar Coraucci Neto:

Thank you for the question, Pedro. We are right now analyzing that National Defense Plan for Agriculture that was launched this morning. In any event, all topics which were addressed by the Minister and by the President are topics which are highly debated by the industry. So, we have been preparing and discussing all those issues which were announced this morning. There are no surprises for the sector in terms of the issues which were raised by that defense plan.

We do believe that our country does need some guidance in terms of development, in terms of safety, of security. And we like to see something happening, coming from the Minister, and Minister is showing a powerful position and we are now hoping that all of that really materializes. The biggest challenge that we have is when we do not have a guidance to follow.

So, when you have guidance, what I can tell you is that, as a whole, organizations and companies manage to display a much more competitive behavior than when we do not. But again, each one of those topics which were listed this morning, of course, impact different areas of the Company, of the industry, we are still analyzing how we can be affected by that, but, again, we have been preparing for that. Those topics have been the focus of attention and discussion for many years.

As concerned to international market, your question is very interesting. Our experience as an international Company up to the present has been and experience of an exporter. Our work would stop when we made the sale, we sold to a local distributor in different countries and our relationship with those countries fell short of what we are able to do in terms of distribution and services.

So, our strongest plan moving forward is to try and use Mexico and Colombia, which are two very interesting countries in Latin America, and are also the most important markets in Latin America, they are highly organized and they are inserted in relatively stable economies, and we are trying to establish a more technical presence, trying to somewhat replicate the model we adopt here in Brazil.

So, we will be, once again, providing technical services into health areas, because we have already identified gaps and technological opportunities in those markets.

Pedro Ferroni:

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A final wrap up. What contribution could you see going forward in terms of revenues for international operations?

Fabio Lopes Junio:

We have that forecast. Our base right now is very small for international operations. So, we are looking ahead to three to four to five years, and we believe in a very strong growth. We expect to increase our contribution coming from international operations.

Pedro Ferroni:

But how much would that contribution be? Would you say you would reach 10% for example?

Fábio Lopes Júnior:

We have different internal forecasts and those forecasts point to a very strong growth in the mid to long run.

Pedro Ferroni:

OK, thank you.

Operator:

Thank you. The Q&A session is now over. I would like to give the floor back to Mr. Dolivar Coraucci Neto for his final remarks.

Dolivar Coraucci Neto:

We would like to thank you all for participating at this conference call and throughout the quarter. I would like to tell you that we remain determined to work hard to provide the best return for our shareholders within very interesting and important plans for the Company. Thank you again. Have a nice day.

Operator:

Thank you. The conference call to discuss 1Q results for Ourofino is now over. You can now disconnect your lines.

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