

Conference Call Transcript
2Q15 Results
Ourofino (OFSA3 BZ)
August 12th, 2015

Operator:

Good afternoon, ladies and gentlemen, at this time we would like to welcome everyone to Ourofino Saude Animal 2Q15 Results Conference Call. Today with us we have Mr. Dolivar Coraucci Neto, CEO and Mr. Fabio Lopes Junior, CFO and Investor Relations Officer.

We would like to inform you that this event is being recorded and simultaneously translated and all participants will be in listen-only mode during the Company's presentation. After Dolivar remarks, there will be a Q&A session.

At that time, further instruction will be given. Should any participant need assistance during this call, please press *0 to reach the operator. We have simultaneous webcast that may be accessed through Ourofino's website at ir.ourofino.com.

At this address you can identify the banner webcast 2Q15. Before proceeding, we would like to mention that the forward-looking statements that will be made in the Safe Harbor and the Securities Litigation Reform Act of 1996 there beliefs based on the belief and assumptions of our Ourofino's management 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 future.

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

Now, I will turn the conference to Mr. Dolivar Coraucci Neto who will begin the presentation. Mr. Dolivar Coraucci Neto, you may begin your presentation.

Dolivar Coraucci Neto:

Good afternoon, everyone. Thank you very much for your participation. I'd like to thank you to take part of our video, audio conference of results of the 2Q and 1H15. The performance of the company has been consistent to our strategy of growth, profitable and also generation of value for its shareholders.

We launch in the first term four new products showing our commitment to innovation and continuity with investments in research and development to expand our portfolio. In addition, there is a successful return of Master product that fights parasites that are internal, external in bovines.

We follow optimistic regarding opportunities of market in which we act and we trust our planning for growth, preparing for a new cycle based on the expansion of our portfolio and the continuity of the process of structuring of our area of biological products.

I now would like to give the floor to our CFO and Director of Relations with Investors, Fabio Lopes, who will comment on the results of the period.

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Fabio Lopes Junior:

Thank you, Dolivar. Good afternoon, everyone. In the 2Q, first term in 2015, our results were in line with our planning. We are in line to reach our annual goals with product launches, growth in revenue EBITDA and profit

Slide on page three, we highlight the growth of our net revenue by 12.4% in the second quarter 2015, the total amount of R\$132.7 million. In the first term of 2015 there has been an increase of 13.8% with a total of R\$219.7 million.

On this slide we also present the contribution of production companion animals and international operations in net revenue compared to the same periods in 2014. We note that has been an increase in terms of the participation of large animals was in the quarter and semester moving from 80% first term 2014 to 82% same period 2015.

On the slide on page four we detail net revenue for each one of our business segments. In the segment of production animals, total net revenues in the 2Q15 with R\$112 million, an increase of 16%. In the first term 2015, the total amount was R\$180 million accounting for a growth of 16.4%. We highlight that this growth the sales of products for against parasites that are internal, external for bovines and the increase in sales in poultry and swine.

In the companion animals, the net revenue of 2Q subsidy was R\$15.2 million, a reduction of 5.6% considering 2Q15 which historically was stronger first term operating amount reached R\$30 million the growth of almost 8% regarding the same period last year.

In this segment of international operations, net revenues 2Q15 remained stable with a total amount of R\$5.5 million. In the first term 2015, there was a drop of 9.6% amounting to R\$9.4 million. This segment was impacted due to the impossibility of sales to Venezuela and also we gave continuity to the restructuring plan of the segment. With this initiative we believe in better results in the next term.

On slide on page five we analyze gross profit and SG&A. In the 2Q15 total gross profit was R\$72.8 million, a growth of 5% regarding same period 2014. The first term 2015, the total was R\$124 million, an increase of 6.9% considering first term of 2014.

When we analyze the first term 2015, the gross margin was reduced by 3.6 p.p. , and this was due to a less favorable mix and lower proportional participation of companion animals and international operations, in addition to greater revenue in poultry and swine and sales of vaccine for Food and Mouth Disease at lower prices.

2Q15, SG&A had a dilution of 1.1 p.p. on net revenue, reaching an amount of R\$49.7 million for the first term 2015 with a dilution of 1.8 p.p. and SG&A total was R\$91.4 million.

On slide on page six, we have EBITDA and EBITDA margin. 2Q15 EBITDA added to R\$28 million, practically in line with 2Q14, first term 2015 total EBITDA was R\$42 million, a growth of 1.9% on a same period 2014. We had a loss of 2.2 p.p. of EBITDA margin, which is explained by the drop in gross margin with partial offset by the dilution of SG&A.

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Slide on page seven, we present the net financial expense IRCS expense the profit from continuing operations. Net financial expense had an important reduction of 21.7%, 2Q15 and 51% first term 2015 explained by the amortization of funding linked to CDI as part of resources funding coming from the IPO.

Our expenses with income taxes have contributed with 52.9% lower in the 2Q15, with a total of R\$2.4 million and an effective rate of the 11.3%, first term 2015. These expenses were 28.3% lower with a rate that was 12.6% and the total R\$3.8 million these numbers reflects an increase in the use of *Lei do Bem* benefits with investments in R&D. Profitable operations grew in the 2Q15 by 16% with a total of R\$18.9 million. In the first term 2015, there has been a growth of over 20.5% compared to the first term 2014.

Slide on page eight, we analyze bank debt, net bank debt. The first term 2015 on net debt on EBITDA accumulate in 12 months was 1.63x, against a ratio of 2.2x first term 2014.

Our cash closed first term 2015 with R\$19.5 million with an impact of the amortization of R\$72 million in debt in the period. The debt cost closed first term 2015 by 5.75% a year against 6.27% a year same period 2014 with the result of debt amortization linked to CDI.

On page nine, we highlight investments in R&D first term 2015. We had in total R\$16.5 million accounting for 7.5% of the net revenues over the period.

On page ten we have launches for term 2015. We had four launches so far, three products for production animals and one for companion animals. The 1Q we had two antimicrobials drugs, Lactofur and anti-micro build for bovine and swine, and Ciprolac and inter mammal and for mastitis for bovine. 2Q we had Isocox, anti-oxidant agent for bovine, ovine and swine and Trissulfon SID, antimicrobials for cats and dogs.

On page 11 we demonstrate the daily performance of our shares since the IPO into June 30th 2015. The share was priced at R\$27 on 30th of June 2015, we close with a quota of R\$32, an increase of 19.54% in the period – comparatively at Bovespa, same period dropped 3.25%.

To close on slide on page 12, we want to highlight our growth of net revenue of 13.8% in the semester. Our growth in terms of net profit of 20.5% and the launch of four new projects. The performance of first term reinforces our expectation that 2015 is a year of good results for Ouro Fino.

We followed on motivated to seek our growth with the lot of the determination credibility and activity. I thank you all for your time. Now, we open up for questions.

Joseph Giordano, JPMorgan:

Hello good afternoon everyone. Good afternoon, Dolivar and Fabio and thank you for answering my questions. My question is regarding the pipeline, you have four products for the year that you have launched. What's your plan for the second term? you have more to

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come or reduce the pipeline is going to be concentrated close to the launch of the vaccine plant.

Second question is the growth of you had a production animal growth while Fabio explained what's happening to Venezuela, I'd like to understand what's happening to companion animals a growth that is well below average age group below the market in the semester. I'd like to understand what you see in terms of companion animals and production animals, especially with the return of Master. We have strong sales there, right? Thank you.

Dolivar Coraucci Neto:

Thank you for the questions. Regarding pipeline, our pipeline is very much in line with what we had planned and within our scope planning, we still have for this year products to be launched and absolutely within our planning to. They are not yet linked to the process of biological products because it's only going to be ready next year.

We have already launched one in August. Probably for the next month we'll have other launches, and important launches that are in line with a consistency of the financial results. We want to build within next term. And obviously along with the launch of the products that we have planned plus return of Master we are confident that what we're going to deliver in terms of results for the next term is something that is very much in line with the expectations that we see in the market as a whole and within our expectations.

For companion animals this is a segment that is more subject to the environmental changes we have or turmoil we have in Brazil. What is the political economic dissatisfaction affecting more directly the retail markets. What happens is that our customers in this next term, the base that we had this previous quarter was quite important. Our customers became bit more careful with the process. I can assure you that we have the situation that is very much under control and that we have the expectation of maintaining our annual growth above the market and two digits that we have historically having in our business.

Obviously, environmentally it will require great efforts on our company that I can assure you that we are quite optimistic in terms of maintaining our plans of growing above market rates, and about two digits.

Joseph Giordano:

Thank you. Dolivar. Regarding market share, can you update us on your market share and this semester of the Company, both in terms of companion and production animals?

Dolivar Coraucci Neto:

Thank you. In the case, well we don't yet have the market share numbers because that comes directly from the union and the update is only given after. The public, the disclosure of our results and after that they have some time to compile the data. We'll probably send

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you a position in the next two weeks. But you have felt that the Company has increase in terms of market share or is it a stable situation from what you have seen. What you have seen is that we are on patent of success and gross. We have noticed regarding the moves that we follow in terms of the market and the competition, we have done a good job. That's what we hear and that's what we perceive.

Joseph Giordano:

Perfect. Thank you, Dolivar.

Gabriel Lima, Bradesco:

Good afternoon, everyone. My question was also regarding market share that has already been asked. I'd like to comment, well benefits from the time and get an update as to the plant for biological products and vaccines that should be ready by late next year.

What about the construction work, the pipeline of innovation is everything is under, what expected in terms of the construction? Because this is important for you in terms of revenue expands and margin expansion.

Dolivar Coraucci Neto:

Certainly, Gabriel. We have this project as quite important project for the Company. And if we could actually give a degree of importance, three stages developed in the development of the same, certainly the project development, the regulatory and registry and plant registration and plant construction, we have everything in line with what we have planned for the project. This is a great news, actually, because there's no use having products have registry and no products, so we are implementing the project in a very consistent solid way.

And last time we had a chance to talk to you, we mentioned that you could visit the constructional works. We are growing quite fast, they are quite advanced. The next release we will show some photos to show you and the market how this project of ours is moving on that. Certainly, it's quite an important project for our company.

Gabriel Lima:

Thank you, Dolivar. And regarding spending with research and development that has been speeding up regarding first last year. Is there any change or something you expect to accelerate regarding sales? This term you add quite low tax rate. What can we expect in terms of tax rate?

This drop of that rate is related to the investment you made in research and development at first semester of this year.

Fabio Lopes Junior:

Well. Gabriel, we will be maintaining our investment base at around 6% a year. What

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happens is that, you have stages of project that sometimes require more resources at certain points, they're important cornerstone that we've retained, that required more investments, but our idea is to continue our level of around 6%. And regarding taxes, just a second, I can repeat.

As to taxes, we usually analyze quarters, we had a level of benefits of use that was higher. And our rate in this semester with lower, about 12%. But when we put at an annual rate, in terms of income tax and social contribution, we maintain our expectation of having an annualized rate of around 21%, 22% of income tax and social contribution for this year of 2015.

Gabriel Lima:

OK. Fabio. Thank you. Thank you, Dolivar.

Antonio Barreto, Itau BBA:

Good afternoon, everyone. We have seen that you have delivered SG&A, which you mentioned is quite strong. We've commented on that and it's above our expectation. I'd like to understand how much SG&A, this dilution, is scalable. If you can give us a detail on that. It has reached maximum dilution, from now on you have to invest more in SG&A to keep on growing or if you have more room. If you can give us more details on the fixed costs, I would be grateful.

Fabio Lopes Junior:

Hi, Antonio. We expected the dilution of SG&A continuous in 2015 and 2016. It is stronger when we analyze on projections and estimates. But it's offsetting the reduction of gross margin. We still have some room when we look at second term, increased revenue and consequently a dilution of SG&A. And when we talk about scalability and new levels, obviously, when this action plan starts operating we will have to make specific investments in marketing product launches.

When we look especially at 2017, sales team investment in commercial operations. When we think about internal costs we are not viewing the next two years change in terms of our level. The Company had set out this structure in the past years and we were counting on this dilution of the internal expenses of the Company with an increase in revenue.

Antonio Barreto:

Thank you very much, Fabio. Great.

Marcio Montes, Banco do Brasil:

Good afternoon, everyone. You have answered regarding the drop in the tax reduction. I would like you to talk about the international part. The Company has been impacted by Venezuela. And up to now I cannot see any grows regarding Colombia and Mexico. Can

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you talk a bit about the situation. What are your expectations now for the second term and 1Q next year?

Dolivar Coraucci Neto:

Certainly, last year. Colombia and Mexico are part of our strategic guidance and that is determined for everything we want to develop for the Company in the next few years, as well as the importance of these two cases which will be the internationalization of the company.

Colombia, we have decided to adopt situations repositioning there quite deep there. We have not managed to get a significant result this year, but we believe that in the next releases we'll share with you good news in this process. As to Mexico, we have been developing around market there. We've changed our operations quite drastically in Mexico as planned and it is within what we have expected within a development curve regarding previous terms.

We had a growth of 21.7% in Mexico pesos revenue and that support this strategy of our consolidating ourselves in the Country. It's below what we expected to be because the speed and the timing which we've adopted the measures have not yet managed to bring the results we expected to have and we are expecting them to have and we will be sharing with you in the next releases.

Marcio Montes:

OK. Thank you.

Pedro Ferroni, CTM Investments:

Good afternoon, Dolivar and Fabio. My first question is regarding launches. I'd like to know bit more about how does it work in terms of timing. How does the product reach its timing breakeven. You launch a product. How long do you take to make it go to all the distributors for customers to get to know the product?

Second question is regarding whether you can have more feeling for the second term, in terms of net profits and revenues if you can maintain the same dynamics you had in the first semester. Thank you.

Dolivar Coraucci Neto:

Excellent question. I think one of the competitive advantages that we have in our organization is that precisely the fact that we have great expertise to place products in the market. Our Company has capillarity and presence in the Brazilian market which makes it very easy for you, when you launch a product and put it in the market with great nimbleness. Consequently we start rolling that out very quickly. So, we are known. Actually, this is a great differential and competitive edge of our Company.

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The fact that we have this capillarity and the ability of placing products in the hands of farmers quite quickly. And consequently, I'd tell you that we enjoy the structuring products in the market in two, three years, taking the deep knowledge and the deep use of the product. This is a very advantageous to ramp-up.

Fabio Lopes Junior:

Regarding your second question, we expect the second term to have a relatively stronger dynamic as we had in the 1H. We have several situations for the second term and it makes you confident to put some expectations in the second term as regards to the first.

We have some points to set as examples. We had a price transfer in July of 6% in the Ouro Fino products, re-establishing the cost get this specially, the exchange gap and we have re-pricing and an improvement in gross margin for the second terms.

As Dolivar mentioned, we also have the return of Master, as you well know, it was a very important product and a main product of company until 2013. In the second term last year we did not sell the product and now we are starting this term with the product placed in the market.

At the last call, we mentioned that we did not yet have the sensitivity of the clear idea of what the product was like in the market. Now we can tell you that the product is very well placed, and we are confident of a positioning of it being one of the major products of Ouro Fino.

In addition, Dolivar have mentioned, we have already made a launch that was in August, it's another product that is doing quite well. And we have other launches for the second term that are quite important that bring even better contribution margin. And we are seeing growth. As Dolivar mentioned, there we expect to have over two digit for companion animals and pets. We'll have more favorable mix for the second term, re-establishing the EBITDA margin, actually making us have a second term in line with the forecast and budget we have in the Company.

Pedro Ferroni:

Great, thank you.

Gabriel Lima, Bradesco:

Great. Thank you for the follow-up. It's regarding the last comment you made, Fabio. This 6% of price increase you mentioned. You mentioned, July, I'd like to confirm that if you had increased the prices at the end of year. Just to understand, does this increase, is it to offset the new foreign exchange level that we see. That's why you needed more price increases or are you adding anything else to get profitability? And I'd like you to talk about price behavior of main competitors. They have imported products, more impacted by foreign exchange. That would be interesting. Thank you.

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Fabio Lopes Junior:

This price transfer or price increase that was set, yes, is to offset the USD level between R\$3.40 to R\$3.50, adjusted to offset the cost increase that we would have with the foreign exchange increase. The market cannot cope with a greater increase to get the margin but this price increase of 6% is getting back to the gross margins we had before. Regarding competition, we feel that competitors are following the increase that we have made, because the foreign exchange impact is for the whole industry, not only for our company.

Gabriel Lima:

OK, Fabio. Thank you.

Operator:

Thank you. This concludes the question and answer session. At this time, I would like to turn the floor over to Mr. Dolivar Coraucci Neto for closing remarks.

Dolivar Coraucci Neto:

I'd like to thank you for the attention and trust tell you that we are quite optimistic regarding the challenges we have for the 2H, and we'll keep on working hard to bring the best return for our shareholders. Thank you all very much.

Operator:

Thank you. This concludes Ouro Fino's 2Q15 results conference call. You may disconnect your lines at this time.

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