Operator:

Good afternoon, ladies and gentlemen. Welcome to Alliar – Centro de Imagem Diagnósticos S.A., 1Q19 earnings conference call. Present here Mr. Fernando Terni, CEO and Mr. Frederico de Aguiar Oldani, CFO and Investor Relations Officer.

The live webcast of this call is available at Alliar's investor relations website at ir.alliar.com, where the presentation is also available for download. As a reminder, questions will be taken by telephone and by the platform.

Also, this event is being recorded and all participants will be in listen-only mode during the Company's presentation. After the Company's remarks are completed, there will be a question and answer session. At that time, further instructions will be given. Should any participant need assistance during this call, please press *0 to reach the operator.

Before proceeding, we would like to clarify that statements made during this conference call related to the company's business prospects, projections and operational and financial goals are based on beliefs and assumptions of Alliar's Board of Directors, as well as information currently available to the Company.

Future assumptions do not guarantee future results as they involve risks and uncertainties related to future events that depend on circumstances that may or may not occur. Investors should understand that general economic and industry conditions, in addition to other operating factors may affect the Company's future results that differ materially from those expressed in such forward-looking statements.

Now, I will turn the conference over to Mr. Fernando Terni. Mr. Terni, you may proceed.

Fernando Terni:

Good morning, everyone. Thank you for joining our 1Q19 earnings conference call.

Before we begin, I would like to say that, as you will see in our presentation, even with a challenging sales scenario, we were able to deliver the operational leverage we have been proposing since 2017, with margin growth, profit and return. We also highlight our same-store sales, which grew 3% year-over-year during this quarter.

We remain focused with the purpose of increasing the Company's profitability through the maturing of investments already made and productivity gains with technology and innovation. This strategy allowed us to deliver the operational leverage we observed in this quarter.

I can also say that the Company is prepared for this more challenging market stage and ready for an accelerated expansion as soon as the formal employment market begins to react.

We used this cycle to reduce Alliar's financial leverage to more comfortable levels, which, along with lower investments compared to last year, has been important for the Company's free cash flow generation. Later on, Fred will go into more details on these points.

After the initial comments, I invite everyone to go to page three, where I will start with the highlights for the quarter.

But before we start, I would like to note that, as it is written at the top of the slide, we adopted the new IFRS 16 accounting standard as of January.

For comparability purposes, we prepared a pro-forma version of the 2019 numbers, excluding the effects of the IFRS standard so that you can compare numbers and better understand the results of this quarter.

Now let's start with the highlights. Beginning with shareholder profit, which grew 39% in this quarter. And, in the pro-forma numbers, growth was even more significant, reaching 67.6%.

EBITDA margin increased by 504 bps, reaching a margin of 27.7%, with an adjusted EBITDA of R$72 million, 21.9% higher, year-over-year. In the pro-forma numbers, growth was naturally lower, around 2.6%. Even so, there was a margin expansion of approximately 60 bps in the pro-forma numbers, characterizing the Company's deleveraging.

Same-store sales, as I said, stood at 3% and was driven by higher demand, mainly in the São Paulo market, as a result of the maturing of several mega units. Final revenue was stable at approximately R$ 262 million, and I will give further details on revenue.

Our operating cash flow generation was R$40.8 million in the quarter. And, most importantly, free cash flow reached R$24.5 million. ROIC reached 12.8%, an improvement of 69 bps, due to the strategy of maturing our investments.

NPS, an important indicator for patient satisfaction, was 63% at the end of 1Q19, an important increase by almost 250 bps versus the previous year, reflecting a continuous improvement in the patient flow management at our units.

Turning now to page four, I'll give a little more detail on the Company's gross revenue. Starting with the left chart, we provide a breakdown on the contribution of each growth channel. Starting with the same-store sales, which grew by 2.9%, increasing by R$8 million and, new units, which increased by 0.7% and almost R$2 million.

It is important to note that, in this quarter, we already excluded the São Rafael Hospital in Bahia, which was sold at the end of 2018 and reduced our numbers by 4%, as well as a few low volume units, which were shut down in the quarter when compared to the previous quarter.

As a result, we had a small decrease by 0.5% of the Company's revenue, practically flat, which is largely explained by the removal of the São Rafael Hospital in Bahia.

If we look at the chart on the right, I provide a little detail on where you this decrease was observed, mainly in magnetic resonance which was evidently due to the removal of the Hospital São Rafael, Bahia; results from images, excluding magnetic resonances, grew by 1.6% and clinical analyzes by 2.7%. Fred will give you lots of details on that.

This is a result of challenging tickets, especially in the region of São Paulo. Although there was a reduction in ticket, we had quite a large growth. The city of São Paulo has been a pleasant surprise for us. We grew same-store sales here by 7%. Always remembering that mega units have been operational for more than 12 months and therefore have been already considered in same-store sales. So, the city of São Paulo is doing very well.

Now I invite you to go to page five as I pass the floor to Fred, who will give you details on our numbers. At the end of the presentation, I will come back with my final considerations and we will then open the Q&A session. Fred, please go ahead.

Frederico de Aguiar Oldani:

Good afternoon everyone. I will start on slide 5, making a brief comment on the consolidated financial results. As Terni mentioned, since the end of 2017, when we presented our new strategy, we emphasized that we would see a different P&L model at the Company, we would have lower top-line growth, but top-line growth would come mainly from organic efficiency since we made significant investments in 2016 and 2017.

From then on, our main focus would be to grow our bases and, mainly, seek maturation of the new units opened from the end of 2016 and mid-2017. And, this is what we have seen.

It is important to mention that in this particular quarter we had a weaker top-line performance than before, even though we had improved same-store performance.

This is not something caused by us, it has to do with the sale of the São Rafael Hospital which is something that, despite taking some of our top-line growth, does not harm our total performance since what we received for the sale of the hospital and what we were able to reduce in debt practically compensates for what we had in EBITDA loss for this operation. So it's not an effect that worries us.

The important thing here is our organic top-line growth, as measured by the same-store sales, we continue to grow and improve compared to the performance we had in 2018.

When we go down to the other lines, it is important to note that we had an important change in accounting rule this year. This rule only changes from here onwards, that is, you do not change last year's results.

For this reason, we created a pro-forma comparison for the results in 2019, both with and without the new accounting standard to compare against last year's results if the same accounting rules had been applied.

We see that the rule does not make much difference in past numbers, that is, in both cases, we have operating leverage with EBITDA growth above top-line growth and with margin expansion, a little more in one accounting rule and a little less in the other.

The bottom-line, which is what we have challenged ourselves to substantially improve, had quite significant growth (i.e. 39% in the new rule and 67.6% in the pro forma numbers on a comparable basis). That is, in either of the rules, we delivered substantial improvements in the bottom-line result, that is, net income, which has been the Company's greatest challenge during this new cycle.

Going on to slide 6, I will comment a bit on gross profit and gross margin. Our pro forma gross profit reached R$70.4 million in the quarter. What is worth highlighting here is that we still have benefits to be captured from strategic plans and from better use of technology to gain more efficiency in the operation. Although on a smaller scale than we did in 2018, we expect significant benefits to be captured in 2019.

Here it is also important to emphasize that the comparison basis for the 1Q is our most difficult comparison base, both for gross margin and EBITDA margin during a 12-month period. When we look at 2Q and 3Q, based on a more favorable comparison than 1Q, which shows the quality of gross margin performance, EBITDA margin and the good costs and expenses control that the Company has been presenting.

Going to slide 7, we will comment on EBITDA performance. Here again, it is important to emphasize that, on the new accounting rule, EBITDA increases substantially compared to the previous EBITDA, that is, with the same accounting rule of last year, when the 1Q margin was 22.6%, the margin of this year reaches 27.7%.

Of course, this effect has to do with this new rule, but even if we exclude the effect from the new accounting rule, on a comparable basis, we had a margin expansion of approximately 60 bps, even in a scenario of no revenue or base growth when compared to last year.

It is important to mention that the improved efficiency and productivity gains are not yet fully captured. The main plans for our call center automation, wipe check-in at reception and other efficiency improvement fronts with the use of technology and innovation are still quite early in the process.

We still see enough potential to capture value from these fronts, not only in 2019 but also in 2020 and 2021. In other words, there is still a long journey ahead until we can capture all benefits that are possible to be captured by using technology.

So it's more of matter of when than if we are going to capture these efficiency improvements from technology. We are very optimistic about the outlook we see for improved efficiency and we have a very strong focus on capturing these benefits. In the current difficult economic and growth scenarios, they already have a significant impact on the Company.

When growth resumes, this will be even more relevant.

On slide 8, I will comment on EBITDA. The financial result was also significantly impacted by the new accounting rule. In IFRS 16, we have financial expense as leases. This effect was approximately R$5.4 million in 1Q.

As a result, we had a financial result that increased by 23.7% year-on-year. Excluding the effects from IFRS 16, that is, on a comparable basis, we had a reduction in financial result by 8.8% due to two main effects.

The first is a lower net debt in this new phase in which the Company generates much more cash, not only operating cash, but also free cash flow generation, combined with the lower financial costs due to the fall in Selic, and the reduction of the Company's cost of debt.

As a result, our net debt fell by 7.1% compared to last year, and our debt ratio improved to 2.24x of EBITDA in the new accounting rule. On a comparable basis, in last year's accounting rule, this effect would not be very different, that is, the Company's accounting leverage would be at 2.34%, a number very similar when using the current accounting rule. That is, the adoption of IFRS 16 has no material effect on the Company's debt.

On slide 9, I will comment on tax and net income. Here it is important to mention the good performance of net income in any of the comparison views, whether with the new accounting standard or the old one. Here, we would like to highlight the substantial improvement in rates of income tax and social contribution, something that was a concern perhaps a year and a half and two years ago because, the rate was above 34%, which would be the marginal normalized rate.

In this sense, we already had a very good performance during 2018. In 2019, we follow this same path. In 1Q, the effective rate of 25.3% was a very positive result. And, here, it is worth noting that we have not yet completed the process of simplifying the corporate structure, that is, incorporations are still happening.

When we conclude our technical report, we will have even greater room to reduce the effective tax rate as we account the distribution of profits through payment of interest on equity. That is, we already had a very substantial improvement in the effective tax rate, but there are still opportunities to improve it further after we end our incorporation process.

Going to the next slide, slide 10, you can see that in terms of investments, we had a substantial reduction compared to last year. Recalling that in 1Q18, the Company had acquired approximately 30% of RBD's stake, that is, in the PPP in Bahia we purchased our partner’s stake. This was the main comparison effect between this year and last year.

However, if you look only at expansion and maintenance investments, we have been able to further reduce investments over last year's first quarter, in line with our strategy to focus primarily on maturing existing investments and maintaining investments that are considered important, such as upgrading the park and renovating our units. This is to ensure that our park remains up-to-date and in good working order to adequately serve our operations at the level of excellence we are proposing.

So it's important to mention that despite all the substantial drop in investments, we keep the investments needed to continue to sustain the operation over time.

Finally, moving on to slide 11, the last slide of our presentation, in which we show both operating cash flow generation and free cash flow generation. Here, we point out that the Company follows a very positive cash flow generation moment, both in the conversion of operating cash flow and in the generation of free cash flow. It is also worth highlighting the effect from the change in accounting rules. It had a small effect in the free cash flow generation.

But, in any case, the important point here is the good moment for cash flow generation, and with this new moment in which we will generate a lot more cash than we use, along with the consistency of our operations, much of that free cash is being used to reduce leverage.

We recall that the Company aims to reduce leverage to levels of 1.5x, 2x over EBITDA by the end of 2020, and the Company remains committed with this goal. I think with that, we have illustrated that everything we committed to deliver in 2017, we delivered.

And now the Company is beginning to prepare itself for a possible new phase, hoping for a recovery of the economy. And we are likely to have a more relevant top-line growth in this new phase.

With that, I will now move on to the Q&A session, and then Terni will come back to make his final remarks. Thank you very much.

Marco Calzi, Itaú:

Hello everyone. Good Morning. Our question has to do with ticket. We would like to hear a bit more on the ticket scenario, especially in São Paulo. If we can try to separate between MRI and clinical analysis and breakdown this reduction we see in both segments, year over year, how much is downgrade and how much is related to a more challenging negotiation with operators? That is my question. Thank you.

Fernando Terni:

I'll give you a slightly more structured answer, and then Fred can provide more details. Last year, we had some important negotiations with some operators. And we preferred to invest more in some units that did not have the accreditation to argue for price.

Unfortunately, I cannot disclose the name of those plans in which we made these agreements, but we had a fairly important expansion of plans in new units, so it was our choice to prepare for the future with all units accredited in all modalities and all addresses, even if we sacrifice a bit of margin.

We also chose to do this at a time with low inflation and therefore we do not have significant cost pressure and the result is what you have seen here. Although we did not grow in revenue due to some ticket loss, we managed to make the Company's profit grow.

So that was a measure that, from our point of view, was correct. We were able to make accreditation grow in several units in which we still had some accreditation gaps, without a significant loss in margin. Quite the contrary, we have been able to recover this in costs.

So then, Marco, what we're doing here is preparing the Company to be lean and strong for when the market reacts. We are taking advantage of this moment to de-leverage the Company, from the financial point of view, to have all the accreditations ready, have all units ready, to receive more patients as formal employment begins to react in Brazil.

So, structurally, this was the decision we made last year, in the past and is now reflected in the 1Q figures.

Marco Calzi:

Very clear, Terni. Thank you.

Mariana Ferraz, Eleven Financial:

Thank you for taking my question. I would like to understand a little better what you said, about losing lives and plans. Where you are losing lives, especially in Bahia? I would like to understand a little better how the competition is there and to know, if you can tell us, who are the operators there. Thanks.

Fernando Terni:

Bahia, especially in Salvador, has a unique dynamic. There is a vertical operator, which is gaining lots of lives, given that it does not have economic growth once there is no natural migration to simpler, more affordable plans. So we saw, especially in Bahia, this migration of plans for larger coverage but simpler plans. And these simpler plans are with an operator that is fully verticalized.

We are currently discussing with these verticalized operators to offer other sales proposals, other than just fee-for-service so that we can also participate in this market.

Insurers are also going through a difficult time. This is widely known, you are aware. They have lost lives that have migrated, whether by unemployment or because they migrated to vertical operators, therefore, to simpler plans, and these operators are growing a lot. We already have good contracts with some of them, but not all of them. In the case of Bahia, it is where we do not have a contract with the operator that is growing there.

That said, in Bahia, on the other hand, there is an opposite phenomenon, which is our PPP, given that there is a relevant unemployment level there, and we have seen a very good result in the PPP, from the government and Company's operational point of view. All operations and hospitals are already in full operation. Some of those lives that were lost went to the lower segments (public hospitals), and we serve them through our PPP. This is overall, in terms of volume.

Bahia continues to be an important market for us. A stable market, but as it goes from one line to another (to PPP) where we have a fixed value and work hard with productivity, we end up seeing a reduction in the top-line that does not reflect in the Company's profit.

The reality is that these lives go from plans to the PPP. So, in a way, we do not lose as much. But in any case, it is the most challenging market today. It is the third largest market of the Company, first in the city of São Paulo, second in Minas Gerais, especially Belo Horizonte, and third in Salvador.

If we look at PPP, it is the third largest market. If we include PPP, it is the second largest market. So we pay close attention there to develop new products to serve this market.

Mariana Ferraz:

Great. Thank you very much.

Guilherme Palhares, BTG Pactual:

Good morning, everyone. Thank you for taking my question. I have three, actually. The first is regarding working capital. We saw yet another drop in the amount of days, looking at suppliers. I would like to understand a little bit how we can see this line going forward.

The second point I would like to understand a little bit about is the effective rate, which, in fact, came well below, at least of what we imagined. I would also like to understand to what extent we can look at this rate below 30%. And a third question is in relation to the NPS. Can you comment a little on the performance of this indicator? Given that, until recently, we saw it at a level closer to 69% and 70%. Thank you.

Frederico de Aguiar Oldani:

I'm going to start with working capital. Since the 3Q18, from the moment we entered a much more favorable period for cash flow generation, we made new negotiations with suppliers. We started working with common payment conditions, which are usually the deadlines with which you have the best cost ratio.

This has happened since the third quarter and deadlines have not changed much. So, you will see this effect in the 2Q. From the 3Q onwards, you no longer see this effect. But currently, if you compare from 3Q and 4Q, there are no big differences. And we do not expect relevant changes in working capital levels going forward. That is, current working capital levels are the normal levels for the Company's operation.

The second point, in relation to taxes, this level of around 25% is the new level for the Company. That is, with the actions we have taken so far, we have already been able to reduce to tax levels. Of course there may be some quarters with slightly higher or lower levels, but that level of 25% is the new normal level.

Why am I saying this is the new normal? Because, after all we had to do, pre-launches, this is the level at which we can run an "as if" operation. As we are undergoing corporate restructurings to simplify our structure, we are at a new tax level rate. Then, probably, we may be closer to 20%, or maybe a little less.

I think 20% is a good indicator as the Company manages to implement its restructuring, a portion during this year and another next year. So, sometime during next year, or in 2021, we should already run at even lower levels. The important thing is that this level of 25% is the level for current conditions, without the restructurings. The third question, regarding the NPS, Terni will respond.

Fernando Terni:

Guilherme, the 70% level you referred to was during 2017. You may not remember, but as of January 2018, in 1Q18, we changed the methodology for capturing information on NPS. Just remembering, and not wanting to stretch too long, but in 2017, we would capture this information when the patients left their exams.

It was done directly by the nurse, or at the reception, with tablets that were given to patients to respond. It is evident that the patient responded in the presence of one of our employees. So we understood at the time that we had to evolve to a more unbiased methodology and, as I said, from 2018 onwards, we send patients, via WhatsApp, SMS or email, the questionnaire to capture this information, giving them more freedom.

And we also increased our patient base. The result of this was that we evolved in capturing information, the number of patients responding to the survey multiplied by almost three - I do not remember the numbers exactly - but today we have more than 20% of patients responding to surveys.

It is taken after the patient leaves our unit, and we believe we have a much more reliable response. Because the truth is that we need this information to improve our services. It is no use having a beautiful number to show to the market if this is not reflected in the journey that the patient had in our units.

Today, we have, as I said, with more than 20% of patients answering the surveys after they leave the units and we have a very rich material to work from.

And the result is that this number has been evolving. Because we know exactly what the efficiencies are and what points the patient complains about, that is where we work to improve. With this, we reach numbers, as I said, above 77%.

Guilherme Palhares:

Perfect. Thank you, Terni.

Operador:

Thank you, we now conclude our Q&A session. At this time, I would like to turn the floor to Fernando Terni for any closing remarks.

Fernando Terni:

Thank you. I would like to thank everyone for the attention and time you have given to participate in this call. I would like to leave as a message for this 1Q that is, we are very happy in seeing that the strategy we adopted at the end of 2017, to increase profitability, has shown to be right one for this difficult moment that we imagined, back 2017, would come.

In 2019, we still have not yet seen a recovery of the Brazilian market. We have not yet seen the recovery of formal jobs, which are reflected in insured lives and increased patient movement in our companies. However, this move we made throughout 2018, and now in 2019, has given this kind of result.

So, we had a virtually flat growth in revenue and a growth of 3.0%, if we exclude the exit of the hospital in Bahia. Even so, we had quite significant numbers of net income growth. Another important information that we would like to leave with you is the ramp-up of the units, especially here in the city of São Paulo, which has given a very good result: a further 7% growth in the city, which is the largest market for Alliar.

It is also important to note that we have also seen increased productivity in magnetic resonance images. We've been seeing, quarter after quarter, the number of machine resonance exams increasing day by day. This is also a very important result.

Fred also did a good job in terms of tax rates. We have not yet completed the simplification of our reorganizational structure. But even so, we have already achieved quite expressive results compared to what we had two years ago. Tax rates are no longer a problem. We have fairly comfortable rates now.

With that, I would like to thank you, and we hope to see you again on our next earnings call in August. Thank you so much for your time.

Operator:

Thank you. This concludes today's presentation. You may disconnect your line at this time and have a nice day.