

Operator:

Good morning, ladies and gentlemen. Welcome to Hypera Pharma's earnings call for the 2Q24. We have with us Mr. Breno Oliveira, CEO; and Mr. Adalmario Couto, IRO.

This event is being recorded. The video can be seen at the Company's Investor Relations website, ri.hypera.com.br.

We would also like to inform you that all participants will be in listen-only mode. We will then have a Q&A session. Further instructions will be given at this time.

Before we proceed, I would like to reinforce that some information in this conference call may contain projections or statements about future expectations. This information is subject to known and unknown risks and uncertainties that may cause them not to materialize or to be substantially different from what was expected.

I will now turn it over to Mr. Breno Oliveira. Mr. Oliveira, you have the floor.

Breno Oliveira:

Good morning, everyone. I would like to thank you all for being here for our earnings presentation for the 2Q. I will begin discussing our growth on slide 3. Our sell-out went up 6.3% this quarter, boosted especially by our performance in chronic and preventive treatments, which is increasing its share in our portfolio.

We are strengthening our position in this category with some launches that will make our portfolio more balanced between acute and chronic use medication.

Performance in Respiratory, Pain and Fever, and Influenza medication, which is about 1/3 of our sell-out and 10% of our market sales was negative by 1% for the Company and 2% for the market. This was the only reason why our growth was below the average for the entire market this quarter. Our performance in these categories is a consequence of the high temperatures we saw in the 1Q of the year, still above the level seen in 2022 and 2023 due to El Niño.

Other categories unrelated to Influenza represent about 2/3 of our portfolio, and they represented 12%, which is in line with the rest of the market. Our highlights were Cardiology, Nausea, Women's Health, Gastro and Vitamins. Sell-out growth allowed us to reach a net revenue of R\$2.2 billion and a record operating cash of R\$624 million, which was also benefited by a significant reduction in our inventory, which Adalmario will discuss during his part of the presentation.

We are making significant investments in research, development, innovation and in expanding our production capacity. And of course, without forgetting shareholder payouts. We have invested about 7% of our net revenue into R&D, and this quarter, we have launched line extensions for leading skincare and consumer health brands, and also new product in Vitamins and Endocrinology, Respiratory system, Cardiology and Gastroenterology.

Our main CAPEX projects have been advanced in Goiás and São Paulo, internalizing some of the production for the acquired brands. We are also expanding our distribution center and building a new planned for oncological and biological products for the hospital market.

Our interest on owned capital was R\$185 million or R\$0.29 per share. We also published our 2023 annual report, which is aligned with the UN Sustainable Goals following GRI and Reporting Council guidelines. We would like to invite you to read our reports as they present our main initiatives and sustainability.

Finally, we were selected once again to the FTSE4Good Index Series. One of the highest sustainability indexes in the market. I will now pass it over to Mr. Adalmario, who will present more results from this quarter.

Adalmario Couto:

Thank you. Good morning, everyone. So let me discuss the main figures in our results and discuss our cash flow. This is one of the main positive highlights for the 2Q and for the year of 2024.

Our sales were close to R\$2.2 billion, a total net revenue of over R\$4 billion, around 47% of our revenue guidance for this year. I would also like to highlight that last year, we had strong revenue growth, about 18%. And with a lower sell-out level.

When we look at a longer timeline comparing the 2Q24 with the 2Q22, our net revenue growth was 16%, and our sell-out grew by 15.4% during that same time. So it was very close. This shows our portfolio's resilience even facing a more challenging scenario for anti-influenza, we have maintained a healthy portfolio and have had a significant increase from the new launches, which already represent 26% of our net revenue or 1/3 of our total revenue when we exclude the brands acquired in the 5 years.

Considering profitability, price increases in April and reduction in idleness in our plant were not enough to offset the negative contribution from the higher share of generics and the reduction in the 1Q. We also saw an increase in commercial discounts during this time. So despite our gross margins being pressured, we are more efficient in SG&A, especially in marketing expenses, making our EBITDA margin 34.5% this quarter.

Financial results had lower expenses by R\$45 million due to the Company's reduced debt and a reduced cost of debt, which cuts from the CDI rate and lower spreads in new issuances. So, at our bottom line, we had a net income of R\$491 million from continuing operations.

On slide 5, we see some of our highlights. First, an 8% growth in operational flow, representing 80% of our EBITDA conversion into cash generation. This is the highest level ever reported by the Company in a 2Q. This increase in cash generation came from better performance in working capital and our inventory reduction policy. In the last quarters, we have been able to reduce our inventory consistently. And this goes for finished goods and raw materials. We are close to 200 days inventory now.

Optimizing working capital in higher capital generation has allowed us to make all necessary investments to keep the Company growing sustainably investing in R&D, innovation, production capacity. And our free cash flow was nearly R\$460 million. financing cash flow included issuing debentures and new financing plans through BNDES and FINEP, coming to a total of R\$1.7 billion and payments of nearly R\$1.2 billion.

And the latest highlight was a reduction of R\$165 million debt this quarter. Our leverage is now at 2.4x the expected EBITDA for this year.

I will now pass it over to Breno again for his closing remarks.

Breno Oliveira:

Thank you, Adalmario. So the Influenza, Respiratory, Pain and Fever market, where we are exposed, had a very slight growth in the 1Q due to higher temperatures in the 1H24. El Niño has lasted from July 2023 to July 2024. And we are already seeing the market growing in July at about 10% versus 0% in the 1H. We are confident for the 2H24, which should have a higher sell-out than what we had in the 1H.

And so we are pursuing the guidance that we have published for 2024. Besides that, as I mentioned in our latest call, our goal for 2024 is to increase our operational generation at a significantly higher level and our operational results.

We have been very strong in our leading brands, our physician has been resilient, and our innovation pipeline is making us the best prepared pharma company to capture the growth opportunities in the Brazilian market for the next years.

We will now continue with the questions-and-answers session. Thank you.

Joseph Giordano, JPMorgan:

Good morning. Thank you for taking my questions. The first question I would like to ask you, is about how we should understand the comparative basis for the 2H24? You have just mentioned the guidance. So looking back, what was effect caused by the reduction in inventory levels? I mean considering the guidance is still the same. I would just like to know what we should expect.

And I would also like to ask about the new growth avenues. So what have you advanced in non-retail markets in sales and especially new products? What you have been developing? What has been approved? You mentioned immunoglobulin. These are major products. So I would just like to understand a bit more about that.

And finally, with cash generation and inventory levels, what should we consider about foreign exchange? We know that the BRL has reduced its value in the last months. So how does that affect your hedging policy? And what impact may that have on your results? Are your high inventories reducing that impact for the 2H24? Thank you.

Adalmario Couto:

Joseph, good morning. I will answer your first question, and I will let Breno answer your second and third questions. But referring to the performance that we had this year comparing the 1H and the 2H, it's what we mentioned in our call. The variation that we were going to see in the 1Q this year would be significant, especially because of our comparison.

Our comparison is much stronger in the 1H23, especially when it comes sell-in. And the 2H23 was much weaker, especially the 4Q, where we saw a double-digit revenue decrease. So we believe that if sell-out is at the levels we expect. And as Breno said, our levels in July are a good indicator. We are seeing some growth.

So this is a time where Influenza medication is still significant. So we saw there was some recovery in that category, which is very important for us. So July is in line with what we were imagining. The 2H24 is starting off on the right foot, and we will be able to resupply our clients' inventories throughout the 2H24, so that we can reach our growth guidance for 2024.

I will also answer your third question about cash flow and the impact of foreign exchange to our costs. The current exchange rate is above what we had imagined for this year. We had estimated it would be about R\$5.10. Differently from what we did in the past, besides hedging our purchases, we were also hedging our estimated purchases for the rest of the year. So that increased our hedging. And as of the end of last year, we stopped doing that because of our higher inventory levels.

Since our inventory levels are still above what we would like, we are seeing a smaller impact from foreign exchange to the results that we will have in 2024. But in 2025, we will probably see some more of that impact.

On the other hand, we have been seeing a reduction in USD costs in some of our main APIs, we are at a much lower level in purchasing these APIs, so that helps us to reduce the impact from the higher exchange rates. And if this level is sustained, we will need to adjust our prices for next year. So it is not a concern for 2024. And it will probably not impact us significantly. But the next year, we will see some other factors that may affect us and see what the impact will be.

Breno Oliveira:

Joe, let me answer your second question, which was about the institutional market. We talked about the institution are and the Company's planned during our Hype Day 2022. Since then, we have been following our plan. It continues our business plan, and we are very pleased with its performance.

Sales for portfolio products have been going as we expected. The portfolio we acquired from Takeda and Buscopan has some institutional products like injectable Dramim and Buscopan. So we have been able to standardize it in hospitals we were able to increase production capacity for Dramim, especially in our new injectables plant.

So besides that, we have also been expanding our team, creating a dedicated team for the public market for bid tenders and this market is doing very well. And considering new products, we are starting to see some dedicated and specific products for the institutional market.

There were projects that we started in 2021. We recently launched propofol and injectable parecoxib. Next month, we are also going to launch enoxaparin which is a very important molecule for the institutional market.

So it's all going according to plan. Our goal is to reach R\$1.4 billion in revenue by 2028 in the institutional market, and we have been on track. That might mean an additional growth of about 2 p.p. per year. So we are on track.

Joseph Giordano:

Great. Thank you, Breno and Adalmario.

Lucca Biasi, UBS:

Good morning. Thank you for taking our questions. We have two. The first is on working capital. What should we expect for your working capital, considering that inventory reductions were a bit lower than expected?

My second question is about plant idleness. If you could tell us what your idleness level is, and how much of your margin pressure has come from that idle capacity? Thank you.

Breno Oliveira:

Lucca, good morning. To answer your first question on working capital and reduced inventories. We have been working on this for some time. As we said, we are starting to see results this quarter. We had significant results, but we are still working on improving this.

This process will be adjusted by the 1Q25, but most of it has been captured this quarter or a good part of it has been captured this quarter.

About idle time. I think there's another factor that we need to comment on, which is the flip side of this reduction in working capital. By producing less to reduce inventory, we end up having a little bit higher idle times. So that's basically it. The plant has been running. We have been offsetting a part of the idleness with being more aggressive in the generics market. So this is a market that is very price sensitive.

And the plant occupation rate is about 70%. It's operating in 3 shifts depending on the production line. Of course, each line is different. But on average, we have 70% occupation rates.

Lucca Biasi:

Great. Thank you.

Vinicius Figueiredo, Itaú BBA:

Thank you for taking my question. I would just like to hear more details about your expected growth for Pain, Fever and Influenza medication for the 2H24? If I can ask specifically about other categories as well? We see that they had a higher level in the 2Q, offsetting the negative growth in Flu medication, but we see also that new launches have been helping. So if you could tell us a bit about the other categories, that would be great.

And I would also like to ask about your CAPEX. Besides this effect that you mentioned to working capital, you also had reduced CAPEX. So if you could tell us a bit about what you are expecting for the rest of the year, that would be great. Thank you.

Breno Oliveira:

Vinicius, regarding other categories, as I said, in the 1H24, our growth was about 12% and July has been strong. It's a bit higher than that according to our preview figures, 13%. So we believe that this performance will be healthy.

What I mentioned was that we saw a reversal in the Influenza medication market which had a big turnaround. But of course, it will depend on the end of winter. But the comparison is easier in the 2H.

And about CAPEX, I didn't mention this in our call, but we have some relevant projects that are ongoing. We are concluding our distribution center expansion plan. We have a plan for biological and oncological products for institutional clients, we have also been making investments in the scopolamine extraction plant. And we believe that our CAPEX will be close to what it was last year by the end of the year, if you add up CAPEX and intangibles invested in research and development.

Next year, we also expect to remain at the same level. And from then on, we will see a reduction as we conclude these main projects.

Vinicius Figueiredo:

Excellent. Thank you.

Tales Granello, Safra:

Good morning. Thank you for taking my question. I would like to ask you about your working capital. You mentioned that there will be an adjustment until the 1Q25. Do you think you will be at the same inventory levels as 2021? Or will it be higher than that?

Adalmario Couto:

Yes, that is our goal. So we started building up inventory to have a bigger buffer in the beginning of 2020. And we would like to go back to the same inventory levels we had then.

So this would be a total working capital of about 200 days or even below that and inventory levels below that as well. And when we are talking about the number of days, that's what we are referring to. But also when we look at the cost percentage, we would also like to go to 50% or 60% of our cost.

So that is still our goal. Initially, our plan was to reach this level by the end of 2024 but considering that the market slowed down last year, we will probably only reach it in early 2025

Tales Granello:

Great. Thank you.

Robert Ford, Bank of America:

Good morning, and thank you for taking my questions. Adalmario, can you tell us about the health of your inventory in your channel and what you are maintaining, what is the mix? And how well positioned are you for the 2H?

Breno, what is your perspective on the competitive environment for your main categories? Thank you.

Adalmario Couto:

Bob, considering inventory for the channel, we didn't change the policy. So we are still working on keeping the inventory at around 110 to 120 days, which is what we consider to be healthy.

Our portfolio is a bit more seasonal. So there are some demand peaks. They are difficult to foresee. So this is a level we consider to be healthy. As we advance and evolve, and as I mentioned, our main goal in our pipeline is to balance the Company's pipeline so that it can be a bit more for chronic medications.

So then we will reassess if we continue with that policy. But on the shorter medium terms, we think that is the appropriate level considering our portfolio, its dynamics, its capillarity, our distribution. We are basically reaching all pharmacies in Brazil. So I think that's the right level right now.

Breno Oliveira:

To answer that question on the competitive environment, we see that the competitive environment will remain competitive. So across the main prescription and consumer health categories, and also skincare will be at the same level. Our competitors are increasing their medical visit teams or at least they did last year, but we do not believe there will be significant changes.

But generics, and this is a market that we have been discussing for the last few calls. We do see high competitiveness there. Last year, by the 2H24, we have been trying to get more profits from this segment. We believe that this is temporary. The fact that it's more competitive, but it has been temporary for a longer amount of time than we expected.

So as we mentioned in the 1Q earnings call, we have been a little bit more aggressive with some selected generic molecules so that we can defend our market share. So for example, dipyron. In the past, we were the only player in the market. And then with time, other came in. So we adjusted our commercial policies so that we could be more competitive with the current scenario. And we did this for a few other molecules. And we believe that this will also be a good growth driver for the 2H due to the fact that we have an easier comparison and a more aggressive policy.

We do not believe that this will impact our margins significantly. Generics only represent 15% of our portfolio. But I heard many comments and reports that there have been commercial discounts that may affect our marketing investments between lines.

But when we look at marketing, overall, it is at about 22% of net revenue. That will not change, but these are some things that we can use according to the market. And right now, we see opportunities, especially in generics and biosimilars, besides an increase in the 2Q that we expect in Influenza-related drugs.

Robert Ford:

So what percentage of the portfolio is being impacted by this higher aggressiveness?

Breno Oliveira:

I do not know off the top of my head, but I wouldn't say it's more than 20% of our portfolio.

Robert Ford:

So that would be 3% of the total.

Breno Oliveira:

That's right.

Robert Ford:

Thank you.

Gustavo Miele, Goldman Sachs:

Good morning. Thank you. I have a couple of questions. The first one is about results. When we look at cash flow, there is a provision and Others line, And that looks like a one-off in comparison to the other quarters. I would just like to understand this effect. I would imagine that this is including some of the revenue from that tax break. But if you can help us understand what it means, that would be great. That would be my first question.

I remember also that in the 4Q earnings call, you mentioned a restricted macro effect, especially in credit, affecting smaller clients, so independent pharmacies and distributors. So if you could give us an update on how that has been going, that would also be great so that we can try to see how it affects the 2Q. That's all. Thank you.

Breno Oliveira:

Miele, I will answer your second question and let Adalmario answer the first question. These smaller distributors have stabilized, as well as independent retail. So there may be an additional contributing factor for a better sell-out in the 2Q. In the 1H23, it was still slowing down. So when it comes to credit, it seems to be stabilizing.

Some smaller networks also are going through board ordered reorganization. So in interest rates, we seem to be going to a more favorable scenario. We are still cautious, but we believe it will be more positive in the 2H24 than it was 12 months. So that might be a tailwind for the 2H24. I will let Adalmario answer your second question.

Adalmario Couto:

So I think the main factor in this line were the tax credits that we received from a subvention in previous quarters. You see that this impact is also in other revenues, and it impacts our cash flow.

There was also a reclassification between lines in our cash flow, but that had a lower impact. That was the main impact that we saw.

Gustavo Miele:

That was very clear. Thank you, Breno and Adalmario.

Mauricio Cepeda, Morgan Stanley:

Good morning. Thank you for taking my question. My question is about your long-term position. It's evident that for your portfolio, Pain and Influenza are very relevant, much more so than the market, and it will probably remain that way for some time. But do you believe that these changes in therapeutic categories will affect you? And will that lead to a change in your strategy?

Since they are providing lower margins as we saw in the 1H, do you think that you should change your promotional efforts? What I mean is, will you invest less in consumer products and more in biosimilars, generic or more traditional models? Do you consider repositioning yourselves that way? Thank you.

Breno Oliveira:

Good morning, Mauricio. So long term, what we have been doing, but of course, this is unrelated to the short-term effects, what we have been seeing recently has not been very typical. In the last 12 months, things were different, but if we look at the 2H21 and 1H22, this category performed very well.

If you look at the categories, we are mentioning on the long term that since the COVID pandemic, they are not performing very differently from the rest of the market. There's more volatility, but they are performing very close to the total market.

So this isn't a category that we want to reduce our investments in. In fact, we have been investing significantly in them. We see many line extensions that have a lot of potential, especially Benegrip, for example. We had 1 SKU in 2017. We expanded this portfolio, and now it is very relevant.

We are also going into cough medication, prevention, Coristina is a very strong brand, and we are also going into Coristina D Congest. So that's doing very well. Neosaldina, as well. We have plans to expand it into related categories, related to pain, but not specifically headaches. So this brings in a lot of potential, and it makes us much more efficient in our marketing investments. So 1 ad for 1 brand will allow us to have much better sales potential.

So despite weaker performance in some of these categories on the short term, we believe that this is just a one-off effect. We also see growth potential into the white spaces in our market. So continuous use medication.

Our portfolio has been historically short on that. That was due to how the Company was created. We were focused on other types of companies in our acquisitions. But now we are gradually increasing our portfolio for continuous use medication.

But we do not believe our marketing mix will change, they might for some time. Of course, it changes strategically. So as I mentioned, recently, we started providing commercial discount. But for the future, we should probably go back into traditional marketing, media, online media. We will focus on that for the next years. Increasing our share of the online market, medical visits as well. We have been gradually increasing our medical visitation team were seeking more efficient ways of reaching physicians. I'm sure that there are more efficient ways that we have been testing.

So we hope to expand these initiatives so that we can also talk to them online. There's a lot of potential in doing that. So we do not really see a significant change in our marketing mix for the entire Company.

I do not know if that answers your question.

Mauricio Cepeda:

It does. I just wanted to know if that was changing your strategy structurally, but that was very clear. Thank you.

Caio Moscardini, Santander:

Good morning. Thank you for taking my question. I would just like to ask about what share does Pain, Fever and Influenza have under sell-in. How relevant was it?

And if you can tell us a bit about your strategy for discounts in the 2H24. We see an increase year-on-year when you add up different kinds of discounts. So we would just like to ingress how that's going to go for the 2H24. What is your strategy? Thank you.

Adalmario Couto:

Caio, sell-in depends on sell-out. We have been keeping track of how that is going. So we always start with higher inventories before the season, look at the expected demand, and that's basically how it goes.

It's hard to talk about sell-in for the 1H because it depends on sell-out. But when we look at this entire basket, which is only Influenza, but also pain killers and things related to Influenza. So if you look at it historically, it's not very different from this 1/3.

But again, this is a category that has a lot of demand variation. And we need to see how the demand is going to go that we can tell you. We do not really have this figure right now because it will depend on our sell-in for the 2H24.

Can you repeat your second question, please?

Caio Moscardini:

My second question was on discounts. When we look at promotional and unconditional discounts, they seem to be going up year-on-year. Is anything going to change in that strategy? We know that usually the 4Q has higher discounts. So will that continue? What should we expect?

Adalmario Couto:

We will probably continue with higher discount rates. As Breno said, this will be mainly due to the mix. So we are being a bit more aggressive in generics. When we look at generics and similars, which have a more aggressive discount policy, we should continue being aggressive and maintaining our market share, even gaining market share with some molecules, and that will also increase promotional discounts. That's very specific for this area, generics and similars.

Caio Moscardini:

Great. Thank you.

Samuel Alves, BTG Pactual:

Good morning. We have a couple of questions as well. We have a couple of questions as well. The first is about your results. You mentioned working capital and inventory, but we would just like to get an update on suppliers. Do you also imagine it will normalize by the 1Q25? That's my first question.

And the second question is a bit more strategic. I would just like to understand your appetite for some inorganic movements. Even considering the idleness that you mentioned, will it make sense to have portfolio acquisitions, especially in chronic medication?

Adalmario Couto:

Let me answer your first question first. Yes, we intend to normalize the number of days in inventory. So as we normalize our inventory, we will continue to buy especially APIs that have a longer payment term for the Company. So we will probably go back to the pre-pandemic levels there. So that is our goal.

The reduction we are seeing is basically due to the policy that we have been following, buying less and having a lower average term.

Breno Oliveira:

Samuel, considering your second question on M&A, we are always paying attention to the opportunities. We believe that M&As are opportunities. We have a lot of expertise that can create benefits for our shareholders. We have been above what we have recently seen in these acquisitions. But on the long term, our focus is on deleveraging the Company. Interest rates have been slow to drop.

And this is different from the projections we saw when the acquisitions were made. At the time, we had 6% interest rates yearly. And now we are seeing that it's more than twice than that. So of course, with organic growth, we have already guided to some investments with the institutional market. Scopolamine, we have some major investments are still ongoing. But as leverage goes down and we see that happening in the last few years, even with higher interest rates, that gives us some space to consider other options.

This is a trend that will continue for international players. We are focusing on some therapeutic classes, some specific markets, and selling the more mature portfolios. And we see growth opportunities there, especially with strong OTC brands.

Samuel Alves:

Thank you, Breno and Adalmario.

Operator:

This concludes Hypera Pharma's earnings call. Thank you for listening, and have a great day.

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