



Conference Call Transcript 2Q21 Results

Hapvida (HAPV3)

Operator: Good afternoon. Welcome everyone to Hapvida's 2nd Quarter 2021 Earnings conference call. Joining us today are:

- Mr. Jorge Pinheiro, CEO;
- Mauricio Teixeira, Chief Financial and Investor Relations Director; and
- Guilherme Nahuz, Investor Relations Director and Sustainability Director.

We would like to inform you that this event is being recorded and all participants will be in listen-only mode during the company's presentation. After Hapvida's remarks there will be a Q&A session for investors and analysts only, when further instructions will be given. Should any participant need assistance during this call please press star zero (*0) to reach the operator.

Today's live webcast may be accessed through the Internet address at ri.hapvida.com.br/en/.

Before proceeding, let me mention that forward-looking statements that may be made during this conference are based on the beliefs and assumptions of Hapvida's Management and on information currently available to the company. They involve risks, uncertainties and assumptions because they relate to future events, and therefore dependent circumstances that may or may not occur in the future.

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

For those of you who are connected via webcast, you control the slide deck. Use the navigation keys in order to change slides.

Now I will turn the conference over to Mr. Jorge, who will begin the presentation. Mr. Jorge, you may begin your conference.

Mr. Jorge Pinheiro - CEO

Hello everyone. Thank you so much once again for joining us in our conference call. It is with great satisfaction that we share with the market Hapvida's results for 2Q 21.

I could not start this conference call without highlighting the efforts that were made during 2Q by our team to fight the Covid-19 pandemic. I am thrilled and acknowledge all the love, dedication, care and all professionalism put into the planning and execution of the several initiatives to fight the pandemic. We are very grateful for being able to fulfill our mission of serving, caring for and protecting our members. To our team my



deep-felt thanks, and to our clients I reaffirm our untouchable and unnegotiable commitment to serve you, giving true meaning to our existence as an institution.

2Q was an atypical and a challenging period, marked by the continuity of the second wave of the Covid-19 pandemic in Brazil. However, once we were getting close to the end of the quarter we saw the main Covid-19 pandemic indicators presenting strong reduction. Our Covid care numbers are going through a downward trend in all regions.

The daily volume of admissions that once exceeded 200 in one single day, dropped to about 20 recently. Yesterday for example, August 11 we had only 12 admissions. In some cities the volume of admissions is already stabilized at historical levels for some months now. The average length of stay also went back to levels that are close to pre-pandemic periods, with most recent values of around 3.8 days/admission. The number of beds dedicated to Covid-19 were reduced by about 90%, a bit over 100 beds today versus 1652 beds that we had during the peak. We now have around 600 healthcare professionals dedicating, dedicated to fighting the pandemic, a reduction of over 80% when compared to 3600 we once had. All of that, added to the vaccination pace in Brazil, makes us believe that we will remain in this downward trend in the number of Covid-19 cases.

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Ok? Continuing now, this growth came especially in the beginning of the consolidation of Promed in Belo Horizonte, an acquisition concluded in 2Q. We also added lives organically (130,000 lives in healthcare and 182,000 lives in dental). More recently, we have seen an active commercial pipeline with the addition of 23,700 lives in healthcare and 23,300 lives in dental in 2Q 21.

Our consolidated MCR in 2Q was of 66.6%, 5.5 p.p. increase compared to 1Q 21 due to the service and hospitalizations related to Covid-19. There was also an impact with a greater number of Covid admissions in the Central-West and Southeast regions, where we are still going through growing levels of verticalization.

In addition, there was also an impact of the MCR of recently acquired companies: Medical, São José and Promed. These three companies have MCRs around 85 and 95%. They are still operating at levels that are higher than Hapvida's; but they are already going through an MCR correction process.

It is worth mentioning that only with the entry of the acquired companies and their weights, without the Covid effect and without the impact of the negative readjustments of individual contracts, the consolidated cash MCR would have been 67.5%, and we delivered 66.6%. We were able to serve an exceptional demand, and at the same time deliver efficiency gains that were more than enough to absorb the one-off impacts in the quarter that we mentioned previously.

Our verticalized and integrated business model enables us to go through impacts like that much more than the rest of the market. We continue excelling in claims management. Digital transformation, automation and artificial intelligence are already part of the everyday life at Hapvida. Our operational technical center located in Recife,



in the State of Pernambuco, enabled us to continue increasing the number of tests conducted in our own network in 2Q.

Another novelty in the quarter was the launch of our ECG report center that is now using artificial intelligence. With machine learning we can now deliver 95% of test reports in up to 15 min. From March and July this year we had already interpreted and delivered over 53,000 tests with this new system. The use of artificial intelligence enabled us to implement this process in a safe and agile manner, indicating to experts the tests that may have some type of abnormality.

Our selling and administrative expenses level reduced by 0.5 p.p. when we exclude our long-term incentive plan, or ILP. Our SG&A level remains very well controlled with a stable index. So our ex-IOP EBITDA has reached 312 million BRL.

Now on **slide number 4** we closed the quarter with 465 care units between hospitals, emergency walk-in units, clinics and that diagnostic units, 27 more than 1Q 21. We opened Hospital de Maceió replacing another hospital in the same city; 2 walk-in the emergency units; 6 clinical, medical clinics; and 3 diagnostic units, in line with the modernization and consolidation process and new and large units for higher-complexity procedures that centralizes and expands the existing services.

In the inorganic front we concluded the acquisition of Promed, which became part of Hapvida in May, consolidating the results in June 1, on June 1, 2021 adding 2 hospitals, 5 clinics and 1 diagnostic unit to our structure. In addition, we now have 9 hospitals in different phases, some of them still under planning and other at advanced stages of construction. We are also expanding our hospital unit in Natal, where we are doubling our capacity. Thus, we closed the quarter with 3570 beds, 507 more than the same period the previous year.

The main addition of beds happened the following way: 103 at Hospital Sinhá Junqueira; 23 at Hospital Mário Palmério; 112 at medical; 99 in Grupo São José and 116 at Promed. We continue engaged to find the ideal size of our own network, which will enable us to achieve gains in verticalizing medical expenses.

Now on **slide 5** you can see the market share of the healthcare and dental segments in 2Q 21 compared to the same period in 2020. In healthcare we had a 1 p.p. increase in all regions where we operate. In dental we grew 0.3 p.p., fruit of our growth strategy.

Another major step was given as you can see on **slide 6**. We are advancing at yet another stage of our business merger between Hapvida and Grupo NotreDame Intermédica - GNDI. In June we received the official approval to take over GNDI's operator by the national regulator, or ANS. The next step is to receive CADE's approval. Our process was submitted to them in June.

On **slide 7** you can see that we continue committed to our sustainability agenda. We published in May our second annual sustainability report. We are advancing in our strategic planning for the area.

In the environmental sphere we celebrated for the first time the Environment Week, in which we implemented actions to foster the discussion our the topic at the company.



We have also announced 4 new hospitals in the network of green and healthy hospitals.

We also have a major work front with the project called Evolve, with several social responsibility actions with our employees.

We have also reserved the month of June to celebrate diversity and create a safe environment, free of prejudices, through programs that foster the practice of diversity in all its breadth and plurality. So we published a diversity and inclusion guide at Hapvida. The launch of the company was also accompanied by corporate talks and a remote learning course of 10 videos. We understand that we are in the beginning of this journey, and we are confident that the ESG agenda advance is key for the sustainability of our business.

We have also been taking all the opportunities created right now in the market for the buyback of shares in order to generate value to our shareholders, because we believe that the current price of our shares does not reflect the foundation and the opportunities of Hapvida's business.

The dedication of our over 37,000 employees and 30,000 medical professionals and dental professionals reinforces our belief in our business model.

Now I would like to turn the floor over to Mauricio Teixeira, our Financial VP and Investor Relations Director, who is going to give us further details about the numbers of the quarter. Thank you very much.

Mr. Mauricio Teixeira – CFO and IRO

Thank you Jorge, good afternoon everyone. Let us move on to **slide number 8**. Our net revenue in 2Q 21 grew by 15.7% when compared to 2Q 20, boosted mainly by the organic increase of 130,000 lives in our healthcare member base (39,000 in individual plans and 91,000 in group plans), and the organic increase of 182,000 lives in our dental member base, (with 38,000 in individual plans and 144,000 in group plans)... 5.2 million BRL in the quarter.

The consolidated acquisitions in 2Q 21 that did not exist in 2Q 20 also contributed to this growth: 48.8 million in Medical, 43.3 million of the São José Group and 43.3 million BRL at Promed. And we also had 12,000 lives coming from Samed and 13,000 lives coming from Plamheg.

Our dental segment had a decrease of 3.1% in the average ticket value because of the participation of urgency care plans; but even with the smaller ticket our revenue grew 11.2% because of the increase in the number of members.

On **slide 9** you can see how the Covid-19 landscape has been evolving at the company since the beginning of the pandemic. In 1Q 20 we had a peak of the second wave with 217 admissions in one single day. In 2Q 21 our care units were impacted by almost the same volume of service and admissions related to Covid-19 compared with 1Q 21. The difference is that this happened in a scenario with a downward curve. Just



like in 1Q, 2Q lead to a higher demand of elective procedures because of the flexibilization of mobility restrictions and the non-suspension of elective procedures.

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So there was a drop of 65% compared to the average of 2Q. In August the rhythm indicates a drop of over 50% compared to July. We project less than 500 admissions for the whole month. This trend, together with the advances in the vaccination phase, will give us an expectation of normalizing our operations.

On **slide 10** you can see the MCR for the quarter and for 1H TY. Cash MCR in 2Q 21 was of 66.6% and in 1H 21 it was 63.9%, increases of 14.1 p.p. and 9.8 p.p. respectively, and this is mainly due to the Covid scenario that was explained previously with an impact of 153.5 million BRL in 2Q 21 alone, against an impact of 47.6 million BRL in 2Q 20. And there was also a higher level of MCR in the acquired companies Medical, São José and Promed, which was not, which were not present in the comparison period.

We had cash MCR and the IBMR constitution because now we have a return of elective procedures in our accredited network, and the normalization of these as reimbursement provision, with the new ABS that are now being sent by ANS after being interrupted because of the pandemic. There was also an increase of 4 million in depreciation and amortization in 1H TY because of the increase in care units coming from both organic and inorganic growth. The reduction of 5.4 million BRL in 2Q 21 is due to a reflex of the amortization and RPPA, which is actually reflecting lower amortization in the period.

On **slide 11** you can see the breakdown of the SUS reimbursement provision. In 2Q 21 we received a new ABI lot, number 86, and because of the acceleration of the number of invoices sent in previous quarters, the historical percentage sent by ANS suffered changes; but the provision of ABI has been kept stable.

Interpreter

The speaker has become disconnected once again. Please hold while we established the connections. Please hold while we reestablish the connections.

Okay, reestablishing the connection now. We can hear you, go ahead.

Ladies and gentlemen, please hold while we reestablish the connection with the speakers, thank you very much.

Ok, connection has been reestablished.



Mr. Mauricio Teixeira - CFO and IRO

On **slide 12** we continue to present the percentage of representativeness of the SUS reimbursement provision value that has been dropping compared to the total claim of the company. We calculate using the ABI amount divided by the quarter to which the ABI refers. There has been a sequential drop in that level and we have received the ABIs for procedures that happened in 2Q 20, and the nominal value is similar to our historical levels; but since the claims of 2Q 20 was much lower because the elected procedures had been suspended, which is the number that goes in the denominator, there has been a dramatic increase in this index - but we should go back to normality in the next quarters.

On **slide 13** you can see an additional slide showing what our cash MCR would have been in 2Q 21 if we disconsider the additional expenses with Covid, which were 153.5 million BRL and the higher level of MCR in the acquired companies: Medical, São José and Promed. Our index would have been 59.7%, which is well in line with our historical MCR for 2Qs.

On **slide 14** you can see our operating expenses. The selling expenses rate was of 8.1% in 2Q 21 and 7.1% in 1H 21, a reduction of 0.6 p.p. and 0.9 p.p. compared to the same periods of 2020. This reduction can be explained mainly by a lower rate selling expenses in the acquired companies; reduction deferred, of deferred expenses of net commissions due to the cancellation of plans; and reduction in the level of delinquency in individual plans, both in 2Q 21 and in 1H 21. Compared to 1Q 21 there has been a 1.9 p.p. increase and the level of administrative expenses was of 9.9%, both in 2Q 21 and YTD. So this is stable when we deduct the long-term incentive plan effect. We had some positive and negative variations that offset each other, so this indicator has remained stable.

On **slide 15** you can see our ex-LTIP EBITDA of 312 million BRL in 2Q 21 and 778.8 million in 1H 21. The EBITDA margin of 2Q 21 was 13% and 16.5% in 1H 21. This reduction can be explained by the second wave of the pandemic, since our SG&A as a percentage of the revenue was practically stable. Excluding care costs coming from the Covid-19 effect, we would have had 153.5 million BRL for 2Q and 247.1 million BRL for 1H 21.

Net income totaled 269.8 million in 2Q 21, a reduction of 29.5% compared to 2Q 20 and 569.4 million in 1H 21, a reduction of 11.8% against the same period of the previous year, impacted by the reduction of the EBITDA because of the pandemic as we are ready explained, and an improvement in our net financial expenses and effective rate.

Slide 16, the ex-acquisition free cash flow was -202.4 million BRL, impacted at 420 million BRL by the working capital variation of Promed that had in its opening balance sheet 669 million BRL of net liabilities, and that after we took over was reduced to 248 million BRL through the payment to many suppliers. It is worth mentioning that this will be offset by the price adjustments for this transaction.

The cash flow was positively affected by the lower balance in our income tax and social contribution, explained by deductible expenses that did not occur in the comparative



period. There was also an impact of the EBITDA reduction that was 316.1 million BRL lower, and our cash consumption for the quarter was 115.5 million BRL against 92.4 million in 2Q 20 due to the increase in Capex investments and the expansion of our own network.

We are now available for the questions-and-answers session.

Q&A Session

Operator

We will now start the question-and-answer session for investors and analysts only. If you have a question please press star one. If at any point your question is answered you may remove yourself from the queue by pressing star two.

Questions will be taken in the order that they are received. We do ask you that when you ask your question pick up your handset to provide optimum sound quality.

Please hold while we pool for questions.

There is a question from Vinicius Ribeiro from UBS.

Mr. Vinicius Ribeiro – UBS

Good afternoon everyone, thank you for taking my question. I have actually two questions about the same topic. I apologize if you have talked about this during your presentation because we had some connection issues.

So first I would like to know about organic additions in new locations, especially in the countryside of the State of São Paulo. How is your vertical structure in those locations? I know you are planning to launch new products in these locations that needed higher-level of verticalization. Considering the investments that were made during Covid, when do you expect to accelerate this in the new locations?

Now my second question is about negotiation with clients. Last year we had an indication that the competition was a bit more aggressive, and I wanted to have your take on that.

And in addition to this macro situation is there any catalyst on your side to accelerate organic growth? Thank you very much.

Mr. Jorge Pinheiro - CEO

Hello Vinicius, thank you for your questions. About the infrastructure, you know that our team is very disciplined when it comes to all the initiatives that will increase the level of



verticalization and integration of operations. Even in the regions where we already have a high level of verticalization like in the North and Northeast of Brazil.

We are expanding the Hospital of Natal - that is also actually a duplication that is now ready; we have a pediatric hospital to be opened, and in the coming weeks we will have a new pediatric hospital in Recife; we opened a hospital in Maceió that is twice as large as the previous one we have. So we always want to offer the best to our customers, and this is very well aligned with our foundations.

Now about the recently acquired companies we have several initiatives. For the Center-West we will deliver in the coming days the first walk-in emergency unit in the region, and we are also building a hospital in the region that might be ready by the end of the year or beginning of next year.

In the countryside of the State of Minas Gerais we just acquired a property and we are now going through the regulatory process to build a hospital in the city of Uberlândia. In the city of Uberaba we had already leased parts of the largest hospital in that region, Hospital Mário Palmério, and we are also investing in imaging clinics, emergency units and so on. These investments have already been made and are already operating.

Still in the Center-West region we are building a hospital in Campo Grande. We just opened a low-complexity hospital in Rondonópolis and there are another three walk-in emergency units for the region, involving Mato Grosso and Mato Grosso do Sul. We also acquired a property in Brasília and we will soon start construction of a unit there.

Now for the Southeast starting with Belo Horizonte, the whole verticalization plan of these two acquired companies (Promed and more recently Premium) we are expanding the number of beds in existing hospitals. We are also building new hospitals and leasing hospital units and building and outpatient network. We have already devised a plan. This is a very robust plan that is now being executed, our expansion area is working very hard on this.

Now for the countryside of the State of São Paulo we are still working on the inorganic and organic fronts. In some regions, not only in the countryside of São Paulo, we have M&A projects that will help us increase the verticalization level in the hospital segment for São Paulo and the countryside of the State of São Paulo. We are also building 3 hospitals there. In total we have 9 hospitals under construction, not to mention those that will be added inorganically.

So there are several fronts and this is what is going to support us, because we do not focus only on verticalization; but also on complete integration of all of the services that give us a great competitive edge, sustainability and that will help us grow in the future.

Now about the competition, for now there is nothing very surprising to us. For 2Q as we said the company is resuming organic growth. 3Q is even more exciting. I am really excited about retail that has been exceeding our sales target in June -and August has started well as well, so we think our product is very well fit and we are very confident that we are on the right track. We are expanding our market share in general and we have the possibilities to grow and expand market share at the same time.



In the regions where we operate I do not see the competition offering and new competitive edge or anything that can threaten our consolidation. Thank you for your question.

Mr. Vinicius Ribeiro – UBS

Thank you for your answer, Jorge.

Operator

Our next question is from Mauricio Cepeda from Credit Suisse.

Mr. Mauricio Cepeda - Credit Suisse

Hello Jorge, thank you so much for your time and for taking my question. Talking about the commercial area, I have a few questions about things that have been happening in the field. Do you see any signs of economic recovery for your corporate clients? Do you think that they will increase the number of lives? Also do you see willingness from other companies to change their healthcare plans? Do you think that you have the possibility of attracting new customers because of that?

Now I would like to hear a bit more about the cancellations that you mentioned. What has been motivating those companies to cancel their contracts? Thank you very much.

Mr. Jorge Pinheiro - CEO

Thank you for your questions Mauricio. About the inclusion of lives in existing contracts, we see that this movement is already happening; but we are not back to pre-Covid levels yet. I think that the companies are resuming activities on the one hand; but I think that the main factor here is that the companies are now reestablishing their expansion plans - but not all of them are in force yet. But we have positive signs and we believe that soon we will go back to the level of hiring and the number of headcount that companies had before the pandemic.

So this is a very healthy growth for us when we talk about companies that are already our clients. When they rehire their employees and go back to the headcount to pre-Covid levels that is going to have a great effect for us. So yes, we see some growth there; but we are not yet back to pre-Covid levels in existing contracts.

Now about the dynamics and the possibility of offering new corporate products, in times of Covid it is harder to do that. Many companies started working remotely and it is harder to get in touch with them. Thankfully, we are going through the pandemic very well, and once this is over with think that we are going to have a great semester of



growth, and based on the expectations of our commercial area we believe we will go back to normal levels of growth.

And finally about the cancellations it is natural to have a bit more cancellations in periods of economic instability - but we are overcoming that. 2Q already had net growth and 3Q we will have an even more robust number. I think that when it comes to economic landscape the worst is behind us.

So I do not see any, I do not see a negative outlook for that, on the contrary; our product, especially during these challenging times that we are going through, is the product that Brazilians want the most. It is a dream of all Brazilians to have a healthcare plan, and we are ready to make the most of the economic recovery and of that desire of the population to have high-quality healthcare available to them.

Mr. Mauricio Cepeda - Credit Suisse

That was very clear, thank you very much.

Operator

Our next question is from Fred Mendes from Bank of America.

Mr. Fred Mendes - Bank of America

Good afternoon everyone, thank you for your call. I have two questions, the first one is about an important topic. In the macro scenario we are talking about almost 400,000 lives added. So I do not know if organically you had some specific contract that added that to that. I would say that you are now way above historical levels; can you confirm that?

Now about MCR if you exclude the Covid effect you would be within your historical MCR range as well, without a large impact of elective procedures, which we would expect to have a higher impact. But the point is, I believe that from now on we would go back to historical levels without any stronger impact of the elective procedures?

Mr. Jorge Pinheiro - CEO

Fred thank you for your questions. When it comes to organic growth, in the last 12 months - provoked by us - we canceled four significant contracts, and I think we mentioned that in our last conference call. But these are contracts of acquired companies that had a sprayed presence in regions where it would not be appropriate for us to invest in verticalization. Our verticalized model would not make sense for that; these were all corporate customers with very high MCR rates, about 90 to 120% all of



these contracts, and they accounted for 80,000 lives; but we were the ones that wanted to cancel those contracts.

Maybe some of them might make sense in the future if we implement a verticalization strategy there or a co-responsibilization, co-participation model; but the way that it was it did not make sense for us to keep the contracts, in which we would have no remedy but to transfer the prices to our customers. So we thought it would not make sense to keep these contracts.

And during such challenging times of the pandemic our company had relevant growth. In the end of last year from 3Q to 4Q we had had robust growth already after the first wave of the pandemic was left behind, and now the second wave is ending and we expect to see the same growth phenomenon in 2H TY.

About MCR that is a great question. I know that we had connection issues, so I would like to explain that to you once again. What I was saying is that if we made a simple merger of Hapvida that has around 60% MCR, with all of the acquisitions that we made in recent months: São Francisco, Promed, Limeira, América, RN, São José and others, the MCR of Hapvida at 60% in all of the acquired companies that varied from 70 to almost 100%, the combined MCR would be 67.5%, and a scenario without Covid-19 and without negative readjustment for individual healthcare plants.

But our operational discipline to capture synergies and correct assets that were acquired only a short while ago, we were able to achieve 66.6 of cash MCR, which is lower than the simple combination of Hapvida's MCR and the acquired companies' MCR ex-Covid, as they were able to offset all Covid-19 related service with a balance of 1 p.p.

So I reinforce: this is a spectacular result, and we kept MCR at around 60%. So it is important to mention that we see the whole market struggling, it has been challenging for everyone; but our business model enabled us to keep the MCR at around 60%, and to offset the major volume of admissions and the Covid-19-related care provided. We absorbed all that with efficiency gains, capturing synergies as well in the acquired companies, and they are now relevant considering our member base and our portfolio.

Now looking ahead at 3Q as we tried to show you in the number care provided, admissions, number of employees dedicated to one thing or another, we would say that 2Q was very much affected by Covid-19 and 3Q is now going through a strong recovery with a dramatic reduction of Covid-19-related service. June, July was less impacted than June, August much less than July; so there is a downward trend and we believe that in September we will have almost no Covid-19 effect, considering the reduced number of hospitalizations and the demobilization that we have done.

In terms of elective procedures we have not stopped, but of course some procedures were not conducted in 2Q; but they will be done in 3Q and I think that the backlog will be over in 4Q - but we do not think there will be a major impact, and that is because we have a very resilient business model. A surgical procedure of our network costs infinitely less than in the rest of the network, because around 70% of the cost has been prepaid in terms of salaries, property leases and so on. So we can buffer those costs



and considering the Covid-19 landscape our business model has proved to be very resilient, even in spite of all the challenges that we went through in 2Q.

Mr. Fred Mendes - Bank of America

Thank you so much Jorge, that was very clear. Now there is one thing that I did not understand: if we look at gross sales only, almost 400,000 in 2Q, now if we look at 2019 I see that the numbers were close to that, right? Or was that lower?

Mr. Jorge Pinheiro - CEO

Well Fred, I do not have the 2019 numbers here; but what I can say is that sales targets for corporate plans and individual plans are much higher than for 2019, and in 3Q we see great indicators of economic recovery, and the targets are now higher than those that we had for 2020 and for 2019 - but if you want further details about that we can forward them to you later.

Mr. Fred Mendes - Bank of America

Okay Jorge thank you so much, that was very clear.

Operator

Our next question is from Leandro Bastos from Citibank.

Mr. Leandro Bastos – Citibank

Thank you, good afternoon everyone. I would like to talk about M&A a bit more. A first question about the recently acquired assets, Promed as the most relevant one. Can you show your first impressions there and your attempt to capture synergies with them? That was one, my first question.

Now the second question do you see new opportunities to acquire assets? We know that we have the Covid-19 challenges; but do you see any M&A opportunities in the industry? Thank you.

Mr. Jorge Pinheiro - CEO

Thank you Leandro, these are great questions. About Belo Horizonte I am very impressed with many actions. After Promed we also received Cade's approval for PN, so in Belo Horizonte we already have a relevant portfolio, and that is really important



for us because we will be able to fully implement our business model there, and as I was saying our philosophy guides us to implement a large healthcare network, present in the most important regions of the greater metropolitan area around Belo Horizonte, where we need low and medium complexity units, where we need emergency units, imaging clinics, diagnostic units.

We are also expanding our hospital network. The plans have already been devised, they are ready and we are planning to implement our systems and integrate the whole network. You know that our systems have great intelligence, standardization of operations, medical protocols, prevention programs. So after all of that is implemented we are going to have a huge, competitive edge, not only to win markets, to gain new market shares; but also to create new market segments, and we will be able to reach locations that are out of the private healthcare market.

We were very well received by our customers and by the medical class. We have had over 96% - I am not sure this number is correct - but I think it has been over 96% of the contacts with physicians from the Belo Horizonte area have been made, which reinforces a solid partnership with the medical class in Belo Horizonte to make this product a financial reality, and also a reality in terms of high-quality healthcare offered for the population of Belo Horizonte. We are very happy. We have been doing a lot; but the market is huge and there are many opportunities to be explored.

Now about your second question yes, I see that the scenarios that we are going to face in the coming months will create organic and inorganic growth opportunities, and that is because many companies in the country depend on individual healthcare plans, and the negative readjustments will impact their operations strongly.

So two things may happen: on the one hand this type of company might have to transfer this readjustment through other sales channels, and this could bring us organic growth opportunities; but this could also create some fragility to those operations, which could be reverted into opportunities for acquiring those companies.

Our portfolio of acquisitions, our acquisition pipeline, is going strong. A few weeks ago we announced the possibility of acquiring one of the major operators in São José do Rio Preto, we also acquired a hospital in the countryside of the State of Bahia. So this year we are going to see a lot of activity in the M&A area. Our team has been working really hard, and we know that this can be boosted by the regulatory scenario as well.

Mr. Leandro Bastos – Citibank

Thank you Jorge, that was very clear.

Operator

Next question is from Gustavo Miele from Itaú BBA.



Mr. Gustavo Miele - Itaú BBA

Good morning everyone, thank you for this conference call. I have two brief questions, first I would like to talk about MCR from the Covid-19 perspective. It is clear to us that there is a positive message when it comes to the drop in Covid-19 admissions in the beginning of 3Q, as you already mentioned; but can you tell us about the unit cost of Covid-19 admissions in the beginning of 3Q 21 compared to 3Q 20? Is there any relevant changes here in terms of medication costs, medical costs so that we understand what the costs are? Maybe, will be lower admission rates be translated into lower costs or not?

Now another question is I would like to understand how the selling expenses fits into this context of healthier or sounder gross sales. We have seen that selling expenses usually go through variation in recent quarters. It is now going through a positive trend; but if we look at the organic portfolio of the company today, do you think that you have, you are at risk of having more volatile selling expenses because of these higher gross sales? So these are my two questions, thank you very much.

Mr. Jorge Pinheiro - CEO

Thank you Gustavo. Okay, I will try to give you a bit more detail about Covid-19 costs. What items have impacted Covid costs for us? Well, first of all, the second variant causes more severe cases than the first variant we had. This led to longer lengths of stay than in the first wave of the pandemic, and that affected not only the elderly and patients of risk groups as happened in the first wave; but also younger patients during the second wave. So we had a higher volume of Covid-19-related admissions as our charts show, and also lower lengths of stay.

But the excellent news that we are sharing with you is that in August we demobilized all Covid-19-dedicated premises we had. During the peak of the pandemic we had medical material inflation over 30%, and in the last month that number was below 8%, and it was focused on some specific items. So we see that this important cost indicator has already been, is already changing.

Now about medical fees there was a shortage of physicians, and we had to pay up to 80% more to some specific experts. That was also a temporary inflation that has zeroed down. And the month of August has just a little bit of that cost remaining; but we do not expect any more of that for September. The number of Covid-19 tests has decreased and the number of professionals needed, nurses, physical therapists, this has all been reduced by over 80%.

But I would like to emphasize that our team was a very agile opening units and making beds available, so that we would not have any shortage of beds or services to any of our members, not even in terms of materials, PPE, drugs and beds. We were very agile to open and make the best conditions available to all of our members, and we were also very quick in making demobilizations. As the numbers decreased we demobilized those assets, so that we can return to normal operations.



I would like to congratulate our team. We acted according to our needs and the operations are now going back to historical care levels.

Now I would like to turn the floor to Mauricio so that he can answer your second question.

Mr. Mauricio Teixeira - CFO and IRO

Thank you for your question. So talking about commissions I do not see any type of volatility in commission expenses, first of all because they are deferred by the duration of the contract. We had a benefit in 1Q to increase the average duration of the deferral of commissions of contracts, which is a good sign. This creates customer loyalty and the customers remain with us for longer.

And the acquired companies have an average cost of sales that is lower than ours. So yes, there are gains of scale, gains of scale in selling expenses. So I do not see any volatility. We can actually gain efficiency in the part of commissions.

Now we saw a decrease of the delinquency rates in 2Q 21, and 1Q as well - but we should look into this in the long-term after the end of the pandemic; but private healthcare is now at the top of the priorities of both individuals and companies, so when they have to choose what to pay the healthcare plan will be one of their priorities. So I think the delinquency levels will continue to drop.

Now for bad debt I do not see any type of changes from now on.

Mr. Gustavo Miele - Itaú BBA

Thank you Jorge and Mauricio, that was very clear.

Operator

Next question by Gustavo Tiseo from Bradesco.

Mr. Gustavo Tiseo – Bradesco

Good afternoon Jorge, Mauricio and Nahuz, thank you for taking my question. I only have one question about the merger with GNDI. We know that there is a relatively long period until we get CADE's approval, like seven to nine months; have you been working with a consultancy company? Can you capture any type of synergy in these seven to nine months that we have ahead of us? I just want some update about the merger with GNDI, thank you.



Mr. Jorge Pinheiro - CEO

Thank you for your question Gustavo. Well yes, we have been advancing in everything that we can do for now - respecting all regulatory requirements. Yes, we have hired a consultancy firm. We have put teams together, these teams have been meeting very frequently. We have listed all the main gain fronts that will have larger impacts in the short and medium terms. All of this is going to become initiatives, and the teams are working to devise and define everything that will be done after the merger takes place. Up until we get the approval none of the initiatives will be implemented, we will only plan the activities and other critical information that unfortunately cannot be shared with you.

We are keeping a high level of compliance in this area; but whenever our teams work we get more excited, because we see many opportunities. All of the fronts that have been identified are very solid and there will be clear gains. So on our side we have been working the best way we can, and I am very excited about all the fronts, the gains and the synergies that will happen in the future, either in the commercial area, G&A, MCR. There are many fronts for us to work on to bring gains to our members and to both companies.

Mr. Gustavo Tiseo – Bradesco

Great, thank you so much Jorge.

Operator

If there are no further questions I would like to turn the floor over to Mr. Jorge for his closing remarks.

Mr. Jorge Pinheiro - CEO

We would like to thank you all once again for joining us today. We would like to thank our members. They are the reason we exist, and we are still committed to offering them high-quality healthcare and efficiency.

I would also like to thank all of our employees for fighting so hard, and to congratulate them on the results that we have achieved in fighting the pandemic. I would like to thank also the Board of Directors and all of our partners and our shareholders, who believe in this beautiful mission of taking care of people. Thank you very much and see you next time.

Operator

This concludes Hapvida's earnings conference call. We thank you all for joining and have a nice afternoon. You may disconnect your lines now.