Conference Call Transcript

Hapvida

1Q25 Results

Operator:

Hello everyone and thank you for holding. A warm welcome to Hapvida's first quarter 2025 earnings call. Joining us today are Mr. Jorge Pinheiro, CEO, Mr. Luccas Adib, CFO and Mr. Nahuz, IRO. For those requiring simultaneous English interpretation, the feature is available on the platform. Simply click on the interpretation button and select English.

This event is being recorded and will be made available in the company's IR website along with the full earnings materials. You may download the presentation by clicking on the chat icon. Please note the disclaimers related to this release at the end of the slides.

During the company's presentation, all participants will remain in Listen Only mode. After the company's presentation, we'll open the Q&A session to submit questions. Click on the Q&A icon at the bottom of your screen and enter your name, company and language preference to join the Q&A.

I'll now turn the call over to CEO, Jorge Pinheiro to begin the presentation. Jorge, please proceed.

Jorge Pinheiro - CEO:

Hello. Good morning, everyone. Thank you for joining our first quarter 2025 earnings call. We're gathered here in New York, myself, Luccas and Guilherme Nahuz at the Itaú conference and together we'll walk you through the key highlights of our results.

We begin 2025 in a very favorable position with our operations fully integrated and unified. Since the start of the year, we've been mobilizing our team's resources and efforts towards a new strategic agenda, always keeping our members at the center of our actions. By the end of the first quarter, we completed. The full integration of NDI, including its managed operations. This milestone allowed us to optimize admin structures, for example, consolidating the Vice presidencies, overseeing our own network into a single VP of operations. To strengthen the strategic focus on technology and innovation, we also merged to finance and IT Vice Presidencies, now jointly led by Luccas. During the first quarter and the beginning of the second quarter of 25, we opened, reopened and expanded 3 hospitals located in Fortaleza, Sao Paulo and Belem. In the coming weeks, we expect to open another hospital in Recife. Meanwhile, our two new hospitals in Sao

Paulo and the Rio de Janeiro hospital are progressing with the Sao Paulo units already in the project development phase and we remain committed to our verticalization strategy.

In late April, we announced another capital markets fundraising round, our 9th debenture issuance, raising R$ 1.5 billion at the cost of CDI plus 1.05%. This issuance also received the highest investment grade, AAA. Our gradual and organic deleveraging process continues with our net debt to EBITDA ratio now below one time, a very comfortable level.

Now moving to our financial results.

On slide two of the presentation, I will give you an overview of the highlights that Luccas will dive into later on. I would like to comment on some of them.

Our net revenue rose 7.3% year over year, driven by necessary price adjustments and contributions from new sales. We recorded a net loss of 70,000 health plan members in the quarter, which was expected due to seasonality. Historically, early year periods see lower sales of mass plans as consumers prioritize other expenses.

In corporate plans, we face some impact from NDI Sao Paulo systems integration and greater exposure to Brazil's retail sector, which typically sees negative turnover early in the year. For the remainder of 2025, we expect a return to organic member growth supported by commercial initiatives that will support that. For example, we are making improvements in our internal processes and system changes to reduce churn. We are also increasing sales incentives in regions with new hospitals, such as Fortaleza, Recife, Manaus and Sao Paulo and in many other Brazilian cities.

Our cash MLR stood at 68.6% in the quarter up 60 base points year over year. Adjusting MLR for litigation expenses, which are now classified as healthcare costs starting in 2025, the ratio would have been 67.6%. That is a 4 pp improvement Vis a Vis the first quarter of 2024 and 3 pp Vis a Vis the fourth quarter of 2024. This is a relevant gain in our view, as seasonality typically drives 1/4 a quarter over quarter MLR increase.

Adjusted EBITDA reached a bit over R$ 1 billion this quarter, up 5% year over year, despite rising litigation pressures in recent quarters.

We are enhancing our governance to accelerate high-tech deliveries, including AI, automation and robotics and back office and care workflows, aiming to reduce expenses and costs, improve care quality and enhance speed.

Our investments in improving care quality have already started to bear fruits. We now have faster scheduling for appointments, tests, procedures and shorter result turnaround times. This led to a 33% reduction in complaints, the so-called NIPS from January 24th to

March 25. We also achieved improvement in IGR Group wide. IGR is the official regulatory complaint index. NDI Saúde NIPS have returned to pre system migration levels.

Now a clinical research update. We now have around 580 patients enrolled in trials across oncology, nephrology, endometriosis, endocrinology, mental health and neurology. This new vertical has attracted strong interest with 50 plus clinical trial proposals for our in-house research centers.

We also had progress in the education field. In March, we launched Connectomed, our online medical education platform now with 14,000 active physicians with access to over 200 video lectures. This content was fully produced in-house on different topics such as emergency medicine and AI in healthcare. The focus is on continuous physician upskilling and enhancing care quality across Hapvida's network.

Before handing over to Luccas for a deeper dive into our financials, I'd like to wrap up by emphasizing that we remain highly disciplined and focused, tackling challenges while seizing opportunities and working hard to advance the strategies that we launched last year. We continue investing in operational strength and sustainable margins.

A special thanks to our employees, doctors, dentists, brokers, suppliers and the strategic participation of our Board of Directors and above all, our clients for their trust. Luccas, over to you.

Luccas Adib - CFO:

Thank you, Jorge. Good morning, everyone. Thank you for joining us. It's a pleasure to be with you for another Hapvida's earnings call.

This quarter's call is technically more straightforward than last quarters, so be more concise with the explanations and focus more on our outlook for the year. On Slide 3, we see total revenue reached R$ 7.5 billion in the first quarter of 25, an increase of 7.3% compared to Q124. This growth is mainly driven by our policy of regular price adjustments and financial balancing of existing contracts. This strategy has more than offset stability in medical hospital services revenue, which remains under review for credit risk exposure, as well as lower demand in the areas with higher idle capacity and a reduction in the number of lives considering the net losses we had in the first quarter.

So on this topic, moving to slide four, we saw a net decrease of 70,000 health plan members in the first quarter. As Jorge mentioned, it's important to highlight the typical seasonal effect in the first quarters, which impacts 2 variables related to net growth. First, the declining gross sales of mass market plans influenced by factors such as the Brazilian

Carnival festivities, along with financial obligations like property and vehicle tax, taxes, school enrolment fees and others, and negative turnover in corporate plans resulting from layoffs of temporary positions hired for the holiday period. Remember, we have significant exposure to the Brazilian retail sector.

Regarding cancellations in the first quarter there was a marginal increase associated with the system migration during this. Which we believe is a nonrecurring event and at a much lower level relative to our other systems integrations. We should recall because there have been many challenges, but we just completed the largest system integration in our history, indeed in the country's history. It was not a simple integration with market systems, but a complex process involving proprietary systems, legacy applications, standardization of VRP versions and more.

It was an extremely complex move, but we achieved significant results in the rapid conversions of customer service and NIPS as you've seen from the public data released by ANS to all quarter along with stabilization of cancellations which were marginally higher. As mentioned, despite the net loss of members in the first quarter of 25, we're confident that the year of 2025 will be of net growth with a more robust outlook for the second-half. This expectation is based on investments we've made to improve and expand our network. Our current pipeline also looks promising as we see many corporate accounts with contract anniversaries in the second half of the year now seeking quotes.

And we know that the economic environment makes it appealing for companies to migrate their contracts to Hapvida with potential cost savings for them. On the right side of the slide, we observe the evolution of average ticket up 9% year over year. This growth is primarily due to a 7.7% increase in net price reflecting the necessary price adjustments and coparticipation increases on existing contracts, including the unification of revenue transferred rules between health and dental plans following system integration.

The second block: mix, which represents the net difference between the average ticket of new contracts, gross sales and cancellations contributed with a 1.3 pp increase driven by revisions to our commercial tables. We remain positive about 2025 in this aspect as we expect more moderate average price hikes compared to 2024. An ongoing trend that our business model continue continues to mitigate, enabling us to apply price increases below those of our competitors, yet sufficient to recover and expand margins. This movement aligns with the gradual convergence of MLR, reinforcing our commitment to technical balance and business sustainability.

Now on Slide 5, we report a cash MLR of 68.6% in Q125, up 70 bps from the fourth quarter of 24 and 60 bps from the first quarter of 24. So 70 from the fourth quarter and 60 from the first quarter of 24. This increase is primarily due to the change in accounting for legal demands. Until the end of 24 judicial claims were fully recognized under contingencies within admin expenses. From January 25 onward, we began recording the healthcare cost of procedures performed under judicial demand as claims.

We're referring solely to the judicial deposits that were dispersed during the quarter. We separate healthcare expenses from admin costs. Therefore, the MLR for this quarter, including at least one percentage point about R$ 75 million of this new approach, is considered now more accurate and fair. To make comparable figures, we must subtract this one percentage point, which indicates that comparable cash MLR would have been 67.6%, a decrease compared to the same quarter last year and even lower than the fourth quarter 24. In other words, we gain from the inherent seasonality of first quarters versus year end. Additionally, for the first time on the slide, we present the per capita volume metrics for some of our services such as appointments, tests and admissions. It's important to note that the utilization has increased since the first quarter of 24 across all of these services and yet we've managed to dilute MLR. This improvement in efficiency mentioned by Jorge has allowed us to reduce the number of NIPs to end by 33% March 25 versus January 20 and to improve the Group's overall IGR.

This progress results from our commitment to operational efficiency, maintaining high levels of vertical integration, price revisions and the strategic negotiations with our provider network alongside strict cost control. Turning now to litigation or judicialization on Slide 6, we present here the evolution throughout the first quarter of 25 based on the latest data shared. Starting the top left corner of the slide, we see judicial deposits. We began with a balance of R$ 728 million at the end of the fourth quarter of 2H24.

In the first quarter of 25 new net deposits totaled R$ 136 million an impressive 33% decrease compared to R$ 204 million in Q424 and R$ 199 million in Q324. This decline results from intensive efforts, enhanced governance and embedded technology aimed at reducing blockages and their impact on results. We also had disbursements R$ 89 million, slightly lower than in the previous quarter with potential for further improvement through new strategies under way. The total civil judicial deposit balance at the end of the first quarter of 25 was of R$ 790 million.

On the top right side, starting from a provision imbalance of R$ 754 million at the end of the fourth quarter of 24, we see new net provision reversals of R$ 88 million, including R$ 15 million for legal costs. And to make things clear, we segregated R$ 11 million of provisions from acquisitions that are the responsibility of the sales teams, which reduces the retained amount without affecting our results. Payments of R$ 53 million for contingencies, including R$ 15 million for legal costs and R$ 37 million of monetary restatement now applied uniformly across all of our groups operators. Thus the total provision at the end of the first quarter of 25 reached R$ 838 million representing 106% of the deposits.

Moving on to the lower left chart, we display contingency expenses which include R$ 40 million related to labor tax and ANS fines, R$ 89 million in disbursements from civil judicial deposits which I just mentioned, R$ 88 million in new civil provisions and combining these last two, we have R$ 177 million somewhat below the figures of the fourth quarter 24. And as previously indicated, we are also reclassifying medical procedural costs amounting to R$ 75 million in the quarter into claims rather than contingency expenses. Finally, in the lower right corner, we show the evolution of contingencies relative to net revenue. This indicates that the first quarter of 25 is below the fourth quarter of 24, reflecting the sequential reduction in labor and tax contingencies as provisions and adjustments for 20/24 were made last quarter.

Moving on to Slide 7, covering cash, admin and sales expenses compared to the fourth quarter of 24, you'll recall that in our accounting certain one off events impacted the quarter such as the ANS fines agreement and past blockages totaling R$ 506 million which did not occur in the first quarter of 25. Excluding those effects, the fourth quarter of 24 expenses would have been about 10.4% vis a vis 10.3% in the first quarter of 25 before the reckless reclassification of medical procedures from lawsuits into claims. As I mentioned earlier, the reclassification was of R$ 75 million representing 1% of net revenue and admin expenses in the first quarter of 25 was brought to 9.3%. Essentially, this is a reallocation of 1% from G&A into cost.

Some highlights among recurring admin expenses R$ 14 million related to consulting for integration efforts, which negatively impacted the fourth quarter of 24 and that was not repeated the first quarter of 25, although we are still under assisted operations and stabilization. And we also saw a reduction of nearly R$ 5 million in travel post integration. In contingencies in addition to accounting for judicial claims as care costs, there was a R$ 29 million decrease in tax and labor contingencies reflecting the seasonal nature of these provisions and prior years cyclical adjustments. Regarding personnel costs, we allocated approximately 200 employees around R$ 15 million to sales expenses personnel offset by a similar increase in vacation and bonus provisions. With Hapvida and NDI drums integration completed, our organization is embarking on a new journey prioritizing technology and innovation.

We're focused on process optimization and hyper automation, applying cutting edge technology to become more efficient and reduce back-office turnaround times while improving user experience from appointment scheduling to outcomes of treatments to be provided by our more than 40,000 physicians. This team is advancing rapidly worldwide and we are actively testing tools to enhance patients lives and transform our operational model enhancing the care provided. Sales expenses in the upper right corner of the slide remain stable at 7.4% as a whole, but we'd like to highlight two points for the quarter. First, PDD provision for doubtful debts for the first quarter of 25 was higher than the fourth quarter of 24, primarily due to a higher volume of cancellations in the period and lower recovery performance on overdue credits.

It's important to note that the PDD calculated based on the portfolio's loss perspective considering historical credit non recoverability and individualized credit assessments for the largest clients in the receivables portfolio. This model provides a more forward-looking view of loss probability rather than a purely retrospective. 1.2, in personal expenses, there was a reclassification as I previously mentioned of approximately R$ 15 million and that's due to the system's migration and it was completely expected. These impacts were partially offset by a R$ 20 million reduction in advertising and marketing, reflecting the concentration of campaigns in the second quarter and fourth quarters of 2024. On Slide 8, you can see that our Adjusted EBITDA reached R$ 1 billion in the quarter, which is naturally more pressured compared to the first quarter of 24 as it reflects the impact of increased litigation which escalated significantly throughout 2024. Nevertheless, it remains a strong result, demonstrating that we are on track to continue expanding margins.

Our IFRS 4 adjusted net income reached R$ 416 million with a 5.6% margin below the first quarter of 24 for the same reasons. Now turning to cash flow on slide nine. In the first quarter of 25, we recorded a net cash increase of R$ 695 million. This variation was primarily driven by positive free cash flow of R$ 570 million and R$ 240 million generated from financial expenses of financial investment story, which were partially offset by seven R$ 117 million consumed in M&A activities and R$ 34 million in interest payments.

Breaking down the free cash flow starting from R$ 1 billion in adjusted EBDA, we have R$ 93 million in variable compensation payments related to 2024 and R$ 12 million in net provisions and civil deposits consisting of R$ 177 million in write offs and deposit expenses which impacted adjusted EBDA but have no cash effect. R$ 133 million in new net civil judicial deposits, R$ 53 million in actual payments of provision lawsuits R$ 19 million and SUS provisions and deposits not of monetary restatement. These deposits are required for the company to defend itself in court without incurring in penalty fees and charges, and R$ 86 million from the company's operations, mainly consisting.

Of R$ 171 million in provisions for medical bills payable due to receiving invoices at the end of the quarter with payments scheduled for the second quarter of 24 a seasonal movement and R$ 24 million in IBNR with a negative effect on EBITDA, but no cash impact. And R$ 19 million and inventory and suppliers partially offset by R$ 129 million and accounts receivable. And finally R$ 197 million and CapEx continuing investments in IT and in our own healthcare infrastructure. We also had R$ 103 million and income tax and social contribution.

Please refer to the chart below to help reconcile cash taxes and current taxes. As previously mentioned, the companies making monthly payments under the annual real profit system as well as taxes withheld. In March 25, after assessments, we made interest on equity payments from the operating companies to the hold in reversing part of the current tax and crediting R$ 55 million disburst in advance which will be offset throughout the year.

This will be replicated monthly and we expect a reduction in current taxes over the year as mentioned in the last call, in total we generated R$ 872 million and cash that is 86.4% EBITDA to operating cash conversion, a level above historical averages primarily due to the previously mentioned increase in medical bill provisions. On slide 10, M&A activities consumed approximately R$ 120 million in the first quarter of 25, consisting of R$ 50 million related to the arbitration agreement mentioned in previous calls and R$ 70 million in amortizations of retained installments from other acquisitions. Regarding financial activities, there was a generation of R$ 243 million with the following highlights.

R$ 280 million in financial income representing 102.4% CDI return on the average applied cash balance and 34 million in interest in derivative payments during the quarter. We closed the quarter with a net debt of 0.98 times EBITDA, consistent with our gradual deleveraging strategy, primarily driven by strong free cash flow generation. Finally, completing Jorge's remarks at the beginning of the call, we are conducting a net fundraising of 1.5 billion through our 9th debenture issuance. The operation was structured at a cost of CDI plus 1.05% with a bullet maturity in 2032.

In settlement in the coming days, the proceeds will be used for the early amortization of the second debenture issuance, which carries a cost of CDI plus 1.45% and maturities in 26 and 27. This extends our duration while reducing the weighted average cost of that. Thank you once again for your patience and attention, and we'll now open for questions. We're happy to address them. Thank you very much.

Operator:

We'll now start the question and answer session for investors and analysts. When your name is announced, a prompt to activate your microphone will pop on your screen. Please unmute your mic and ask your question. Please limit yourself to two questions per analyst and ask all of your questions at once.

Our first question is from Joseph Giordano, sell side analyst at JP Morgan. Joseph, please go ahead. Your line is open.

Joseph Giordano – JP Morgan:

Hi, good morning everyone. Good morning Doctor Jorge Luccas and Guilherme. Thank you for taking my question. I would like to talk about growth. You said that the income for the year was a bit better with moderate price adjustments.

So can you tell us a bit more about the competitive landscapes, especially in Sao Paulo, we see a more aggressive player. So what is your strategy to tackle this? Now we see improvements in MLR in spite of enhanced fixed costs. So, can you tell us about the acceptance of the new product and the new network and the locations? Where your footprint is greater. Now and have you seen any type of seasonality?

That is weaker this quarter. When we look at the industry, the MLR has dropped significantly because of the carnival festivities and the vacation period. So do you see any type of seasonality here because we would expect a less relevant seasonality in this context? Thank you very much.

Jorge Pinheiro - CEO:

Hi, Joseph, thank you for your questions. So to start off, I would say that we continue happy for having finally concluded this long journey with great time and money invested in this integration. So this hard work is now behind us and our teams. Our commercial teams, product and pricing teams were devoting a lot of attention to systems changes that were being deployed and we had to explain to them how to use the new platforms and the new apps.

But now this is all behind us and we are starting on a new journey. And therefore, we can now look at expanding our own network and we can now focus on organic growth. Such organic growth will happen gradually. We expect it to gain momentum throughout the year, but we have a positive outlook for growth for the remainder of the year and we've been implementing actions for that.

We have been opening new units and we have some idle bads. So we have the possibility of being more competitive and more aggressive from a commercial perspective. And we have a very good and well controlled MLR which gives us margins to be sustainably more

competitive. And additionally, we've been taking actions to review our portfolio readapt products and prices of our network.
This is being done continuously and we now have new internal governance to attract brokers, multi brand or mono brand brokers to come work with us. So we wouldn't be closer to all of these brokers and we believe that this is going to lead us to successful results. So this new journey has been of expanding and upscaling our own network, organic growth, and digitalization of our operations with great use of technology. So our momentum now is focused on all of that.

With the integration now behind us, we have been focusing on this new agenda. And yes, we do see one or another player being more aggressive in the market. That is only natural. But our main concern is to have a cost structure that allow us, allows us to be competitive at the right time, not being irresponsible.

We want to be sustainable when we have margins for that where we are present and the investments we've been making will enable us to be even more accurate in our decisions. So we have a very positive outlook for the year. Now I'd like to turn the floor over to Luccas to answer your second question. Hi, Luccas.

Luccas Adib - CFO:

Giordano, sorry, thank you for your question. What we have been seeing is that the number of lawsuits discussing this topic in the judicial environment has been stable since the second quarter of 24 up until now. So we did not see a seasonality in the number of care related lawsuits. So it's hard to talk about a seasonality here because we have a short historical series and it's the first time that we have a 1st order with our teams focused on this governance and things are working much better now.

But our feeling is that, no, there is no seasonality here in the first quarter. And I think that we have data to illustrate that. And once again, we are constantly evolving in this area and this is quite dynamic. But the April numbers, for example, are very close to the first quarter's average.

So if there was any type of seasonality here, we would be seeing some things moving around and that's not what we're seeing. So the short answer is no, we don't see any seasonality here, although this is the first historical series with our team focused on the first quarter. So let's see how this unfolds. And the number of lawsuits has been stable since the second quarter of 24, and we see a similar monthly average all the way up to April 25.

So there doesn't seem to be any seasonality related to the first quarters.

Joseph Giordano – JP Morgan:

That's very clear. Thank you very much, Jorge and Luccas, have a great day.

Operator:

Our next question comes from Leandro Bastos, sell side Analyst at Citi. Leandro, your line is open. Please go ahead.

Leandro Bastos - Citi:

Good morning, everyone. I have two questions here on my side.

The first question is about contingencies. I just heard what you said about April and that you don't see major oscillations or seasonality. In Q1, we saw contingencies over net revenue improving to 2.9 and the coverage index is also improving when we look at deposits and balance provisions. And considering all of the governance you have in place for this topic, do you have a clearer vision on how this 2.9 can evolve from now on?

What can we expect here in this line? Now my second question is about GNA excluding the contingencies line, which has been a bit more volatile, the first quarter seems to be a bit better and you were just completing the NDI integration. So can you tell us about the levers for the year? So if we look at NDI X contingencies, what are the factors that we can expect from now on? Thank you very much.

Jorge Pinheiro - CEO:

Hi, Leandro, thank you for your questions. I will start with your G&A question. We started now in the second quarter of 25 a journey of capturing synergies related to G&A, which is fruit of this integration with NDI.

We are leaving legacy systems behind. We have mapped all of our outsourcing contracts and we now have a timeline in place and throughout the year of 2025, we will be executing our plan based on our expectations. I mean, we know that some of these contracts may take a while to be left behind, but we believe we're going to finish this by the third quarter of 25 and the fourth quarter will be cleaner, making the most of all of these synergies. So yes, we have great possibilities to capture synergies on different fronts and we have a group tracking all these synergies.

Luccas, would you like to talk about contingencies?

Luccas Adib - CFO:

Sure. Hi, Leandro, thank you for your question. This is an opportunity for me to explain what I said about April, which is exactly what I said in the fourth quarter.

I'm talking about new net deposits. When I look at the new net deposits in April, it's similar to the average we had in the first quarter. Now when we look at contingencies, things are a bit different, not in terms of what we expect for the remainder of the year because we do expect this to be diluted throughout the rest of the year because of the many initiatives that we've been implementing. But the 2.9% of contingencies take into account civil labor tax in US and others.

So we have different vectors that may not evolve hand in hand. Now when we look at the remainder of the year, we have to think about how to model this looking ahead, right, considering the information shared in the first quarter, The first quarter shows great strength and we have ways to control this internally without a mismatch in our MLR. If we exclude this effect, our MLR was great and we've been working hard to control net deposits and expenses and the needs for higher provision for all of that. So we have a positive outlook for the coming quarters because we've been doing everything we can, mapping, negotiating, gaining speed whenever we have to negotiate with our members and including new providers, bringing many of those providers in house.

So we see positive things happening here. We have a great team focusing on that with people from legal, people from operations, people from registration, people from regulation. So this is becoming more and more mature here. But of course, this is a living Organism.

There are always adjustments to be made month after month, week after week, but we have a positive outlook for this considering the positive results we had in Q1 and what we expect to achieve in the coming quarters.

Leandro Bastos - Citi:

Thank you, Luccas and Jorge, have a great day.

Operator:

Our next question is from Vinicius Figueredo, sell side Analyst at Itao. Vinicius, your line is open. Please proceed.

Vinicius Figueiredo - Itaú:
Good morning, everyone. Thank you for taking my question. A common question I heard in my interaction with investors was about cost internalization related to litigation and their impact on MLR.

So just to make it clear, when we think about the delta between gross deposits and net deposits, how does that impact your results? Because I see recovery duplication and others. So we were wondering whether this is somehow included in the R$ 75 million or if that is separate. So if it's separate maybe it could indicate that the claims acts litigation is better than 77.6.

That's my first question. Now my second question about price adjustments, you have a relevant price increase for small and medium businesses. What can you tell us about this readjustment or pass through of the litigation related costs and how does that aligned with your growth expectations for 2025? Thank you.

Jorge Pinheiro - CEO:

Hi, Vinicius, thank you for your questions and thank you for having us here in New York for this great event. No, thank you. OK. I'll answer your question about the price readjustments and then Luccas will take your second question.

This year, our pricing strategy will bring us an average readjustment that is lower than last year's. So this is something close to two percentage points below last year's average. So these two percentage points already include a 1.5 percentage point increase related to the lawsuits. So our MLR is very well controlled as you saw and the verticalization measures we have taken and the integration itself, which brings us a very large number of tools that can help us reduce costs and expenses.

And all of the measures we have adopted re renegotiating with providers and clients will allow us to have adjustments, price adjustments that are lower than last year's, but that are sufficient for us to continue diluting our costs and expenses. The small and medium businesses readjustments that you mentioned, if you compare to all of the other companies, this is actually at a low level. Some companies increase 4/5. 6 percentage points more than us.

No other company had lower readjustments for small and medium businesses. So this can actually vary around 10% on average for this portfolio, maybe a bit. More or a bit less depending on the year dynamics. And Vinicius like we said, considering that we have our own network units opening up and new hospitals opening up, we can be more aggressive this year in situations where we have margins for that and fixed costs for our own network. And as a result, we'll be able to be more aggressive at the right locations and at the right time this year. Now Luccas will take your other question, have an issues. Thank you for your questions.

Luccas Adib - CFO:

The 75,000,000 that we highlighted as judicial claims is the only risk related to deposits that are out of our control, those that we cannot negotiate on and that the judge has ordered to free up the resort, the resource for the other party. So this is not related to the recovery of our own network service. So like you said, and you're right when you say this, the MLR could have been better than what we delivered because the R$ 75 million something that we were not able to negotiate. And as part of this MLR, we also have this whole recovery of the gross to the net that we did in our network or that we paid to our third-party network.

But we have duplicated deposits every month we have a significant amount of duplicated deposits that we recover. And it's only natural you have 345 bank accounts blocked. And so we have the amount that is duplicated being freed up after some time. And so we also have issues in I mean situations in which we are able to negotiate with members.

There are situations in which we gain the lawsuit and the money comes back to our cash. So we have the gross deposits that need to be decreased and we have to be able to do the recovery and clean up the duplicates. So the R$ 75 is only the amount that was dispersed in blockages and the MLR that we also served in 3rd party operators. So your analysis is correct.

Vinicius Figueiredo - Itaú:

Thank you, Jorge and Luccas for your answers and have a great day.

Operator:

Our next question is from André Salles, sell side Analyst at UBS. André, go ahead.

André Salles - UBS:

Hi, good morning everyone. I have two questions on my side and they are about capital location. My first question is we see an average leverage below one time and the company continues to generate a lot of cash. So what can we expect? Are you close to this optimum leverage level or not?

And what can you tell us about how you plan to use this cash? And my second question is about your sales of the Maringa asset. Was that something timely or can we expect similar actions from the company from now on?

Jorge Pinheiro - CEO:

Hi, André, thank you for your questions. I will start talking about the Maringa asset. We had plan to do that. We did not do a systems integration there in that unit because we had an insignificant number of lives there, less than 1000 lives, fewer than 1000 lives. And the hospital was only selling services to third parties.

So it was not in line with our philosophy since we didn't see opportunities for growth there in the medium term. So it was part of our strategy to sell the asset. Of course, we consider selling services in addition to selling plants in a verticalized network. So we'll be opening hospitals in Sao Paulo and Rio and in Recipe and all of them have specific wards to sell services to PPOS.

But we don't want to have hospitals that sell services only. So since this was not aligned with our strategy, we decided to sell this asset, which helped us somehow to reduce our leverage. Now about capital allocation, I'd like to turn the floor over to Luccas. But before I do so, just a philosophical comment.

We want to continue in spite of making. Greater and greater. Investments, we're going to exceed 1 billion in CapEx this year, but our strategy is to continue deleveraging the company. And we expect to go back to a net cash position, which we believe is best for the company, but we're not going to relinquish organic and inorganic growth opportunities. So we want to keep this deleveraging trajectory, but still making the most of the growth opportunities that may arise. Luccas, yes, thank you for your question about capital allocation.

Luccas Adib - CFO:

And you asked about the optimum level. Optimal is what is mathematized in a specific modelling. So an optimal level for capital structure was something that was not studied in a country of 14.15% of risk free rate. So when we look at capital location, an enhanced leverage level would be close to the tax shield that I have an appropriate debt level.

The company has a great premium on the holding. So we don't have to have a gross debt level in order to have this tax shield because of the premium we have available for amortization. And we also have our operational profit in the operating units and at the holding. So if we don't have deductible expenses with that, I won't be close to an enhanced leverage situation because of my tax Shields.

So our idea is to incorporate the entities into the holding in a way to control our cash income statement. That's what we've been doing this year with some tools so that we look at the optimum tax shoot level in order to become net cash. The company has been generating a lot of cash and we want to be net cash and this gives us a, you know, robust deleveraging position so that we don't need to have such a high-risk free rate. So that's our main goal.

Now about the Maringa asset, you asked about other assets that we wanted to disinvest from and we keep on looking at the different locations and opportunities. But for now, that's the only asset we had to sell, but we'll continue reviewing and modeling our fixed assets elsewhere as well.

André Salles - UBS:

Ok, great. That was very clear.

Operator:

Thank you very much. Our next question is from Mauricio Cepeda, sell side analyst at Morgan Stanley. Mauricio, please proceed.

Mauricio Cepeda - Morgan Stanley:

Hello, good morning, Doctor Jorge Luccas and Nahuz. Thank you for taking my questions. I have two questions. The 1st is about the judicial MLR now being allocated into cash.

For small and medium businesses, I know that you already had that in place, but for corporate, I think you can adjust in the negotiations. Now what about individual plans? You have controlled readjustment prices, but you also have no sales. So considering new sales, what do you expect in terms of rebalancing for the judicialization situation in this portfolio?

How long will it take for you to achieve this rebalancing? And my second question is about the industry as a whole. The industry was working hard on the excess of litigation, excessive lawsuit. So can you give us an update of what is going on in the industry there?

Jorge Pinheiro - CEO:

Thank you very much. Great questions. Cepeda, let me start by talking about the industry, the work that has been done through our institutions Abramge and Fena Saúde are starting to bear fruits.

We can now see through the events that were conducted. There are several reports clarifying those to the population, meetings with the regulators, with the judicial and the executive branches of power. And we've been clarifying these issues with, you know, more reasonable practices to comply with the regulation and so that users can have more affordable health care plans. This is a gradual work, but we start to see that the population and business owners now understand that abuse and use of procedures without coverage are reverted back to them through higher prices.

Of course this is not going to happen in the short term, but the results have been relevant. We've been working with the regulator, the executive, the judicial branches of power, and also providing clarification to the population through new species and events, informing the population about the best practices so that they can have access to high quality healthcare that is affordable to them. Because we don't want to have to have high price adjustments. Only 1/4 of the Brazilian population has access to healthcare plans and we want to be able to offer good products to the rest of the population as well.

About prices, you probably remember that at the end of last year we announced that our new tables would already include readjustments and we did that for the individual portfolio, for small and medium businesses, for corporate plans. We did that in all of our sales channels. And twice a year we review our tables and we don't have to make extraordinary adjustments anymore because we already considered all that we needed in the table that we published last year. And now since we are incorporating legal expenses into costs after this one year journey, this is going to be captured not only by the regulators when they calculate the readjustments for the individual portfolio for the year of 2026 and 2027.

And for small and medium businesses and corporate channels, this has already been incorporated in costs as of the beginning of 2025, which will affect the pricing and readjustments from now on. Thank you for your questions.

Mauricio Cepeda - Morgan Stanley:

Thank you, Jorge.

Operator

The Q&A session is now concluded. This marks the end of Hapvida's first quarter 2025 earnings call. The Investor Relations team remains available for follow-ups.

Thank you all for joining us today!