

International Conference Call

PagSeguro

4Q17 Earnings Results

March 9, 2018

Operator: Good morning everyone and thank you for waiting. Welcome to PagSeguro's 4Q17 and full year results conference call. This event is being recorded and all participants will be in listen-only mode during the company's presentation. After PagSeguro's remarks there will be a question-and-answer session. At that time further instructions will be given. Should any participant need assistance during the call please press star zero to reach the operator. This event is also being broadcast live via webcast and may be accessed through PagSeguro's website at investors.pagseguro.com, where the presentation is also available. Participants may view the slides in any order they wish. The replay will be available shortly after the event is concluded. Those following the presentation via webcast may pose their questions on PagSeguro's website.

Before proceeding, let me mention that any forward statements included in the presentation or mentioned on this conference call are based on currently available information and PagSeguro's current assumptions, expectations and projections about future events. While PagSeguro believes that their assumptions, expectations and projections are reasonable in view of currently available information, you are cautioned not to place undue reliance on these forward-looking statements.

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

Mr. Ricardo Dutra: Hello everyone and welcome to our 4Q and full-year conference call. Today I have here with me Eduardo Alcaro, our CFO and Andre Cazotto, our head of investor relations.

Before we go through the main operational and financial highlights I would like to reinforce our vision as a sim tech company focused on offering products to disrupt and democratize financial services in a concentrated and underpenetrated

market providing a complete digital ecosystem that is simple, mobile forced, self-service, safe and affordable to enhance consumer and merchants experience.

We have a unique ecosystem combining cutting-edge in this cable platform, disruptive and complete online and in-store business model, 100% focused on user experience and with a huge online audience.

We believe that our market is just beginning and we still have a long way to go, constantly putting into practice our vision to disrupt and democratize financial services through technology and innovation.

Once again thank you all for joining us today and I will turn the call over to Eduardo Alcaro, our CFO.

Mr. Eduardo Alcaro: thank you Ricardo and good morning everyone. We would like to start our presentation on slide number three comparing the guidance shared with investors during our roadshow with the reported results.

Top line outperformed to the top of the guidance range reaching 2.5 billion BRL; our net income reached 479 million BRL, at the top of the range of our guidance from 460 to 480 million BRL. This reiterates our commitment in delivering profitability with strong growth.

Now I would like to pass the word to our CEO Ricardo Dutra to comment on 4Q and full-year operational highlights.

Mr. Dutra: thank you Alcaro. On slide four we start with our total purchase volume that reached 13.6 billion BRL in 4Q, an increase of 8.8 billion up 183% YoY.

Considering the full year of 2017 PagSeguro reached 38.5 billion BRL in TPV, an increase of 24.4 billion BRL, up 172% YoY. This growth is the result of a greater penetration of our ecosystem in the long tail combined with new innovative products and solutions offered to our clients.

The net take rate excluding sales of devices ended 4Q in 5.2%, a decline of 61 bps YoY mainly due to the mix of products, following the market trend of increasing debit card transactions; even though important to highlight that this trend has been quite stable given that quarter-over-quarter our net take rate contracted only 8 bps.

On the right side of this chart we see the number of active merchants. Just to explain the criteria used internally, the active merchants are those who made at least one single transaction in the last 12 months. We ended 4Q with 2.8 million active merchants adding 1.4 million new merchants in 2017 representing almost the double of the base we had in the previous year.

Now I will pass the word to Eduardo Alcaro again.

Mr. Alcaro: thanks again Ricardo. On the next slide we highlight the main financial metrics. On the first chart our top line reached 831 million BRL in 4Q, up 118% YoY; in the full-year comparison we ended 2017 with 2.5 billion BRL in our top line, an increase of 1.4 billion BRL or 122% YoY.

First let me talk about our main revenue streams composed by transaction services or mainly MDR collected from merchants, terminal sales and financial income originated from the prepayment on sales installments to our merchants.

In 4Q transaction services represented 52% over the total revenue stream followed by 34% from financial income and 13% from terminal sales. Terminal sales are becoming less representative in the mix when compared to the previous year. In the full-year comparison transaction services represented 49% followed by the financial income line, which represented 32%, and terminal sales revenue representing 19%.

On the chart below we present our total expenses figures. I would like to point out here our lean cost structure that allows us to have a highly scalable business model. Our total expenses declined 2.1 p.p. ending 4Q at 1.1% over total TPV. In the full-year comparison total expenses over TPV reached 1.3% or 1.2 p.p. lower than the previous year.

Related to admin expenses over total TPV it reached 0.3%. In the full-year the same metric reached 0.4% compared to 0.6% in 2016.

Moving to the next slide we show our net income growth that as said before reached the top of the guidance range. In 4Q we reached 189 million BRL, an increase of 150 million BRL and up 391% YoY.

The net margin reached 23%, an increase of 12.6 p.p. YoY. In the full-year comparison our net income reached 479 million BRL, an increase of 352 million BRL, up 276% YoY. Net margin ended in 19%, up 7.8 p.p. compared to the previous year.

Our commitment has been delivering strong top line growth with profitability.

Now I would like to hand over to Ricardo who will comment on new products recently launched.

Mr. Dutra: on the next slide we present our shared POS functionality launched during Carnival in Brazil. PagSeguro launched this new functionality for its Moderninha Pro and Moderninha Wifi devices enabling multiple merchants to share a single point-of-sale device. With this new functionality each terminal can serve up to six digital accounts handling sales transactions for each account separately and allowing entrepreneurs and merchants to manage multiple businesses using a single device.

The launch of this new functionality, innovative and unique in the Brazilian market, furthers our continuous process of democratization and a greater penetration of our payment terminals for micro-entrepreneurs and merchants with all types of businesses, and the inclusion and verification of digital accounts continues to follow our rigorous QIC process.

And finally on the last slide we introduce minizinha chip, our pocket POS, a new concept of point-of-sale combining all the high-end functionality such as Wi-Fi and GPRS connection with a complex hardware that literally fits in our merchants' pocket. Ideal for small merchants and micro-entrepreneurs seeking for morbidity and convenience, our pocket POS no longer requires smart phone impairing like other traditional mobile POS, since it comes with Sim Card and free data plan improving the merchants' experience.

Minizinha chip can be purchased for 12 installments of 24.90 BRL, which is around 8 USD.

Now we finish our presentation and we will start the Q&A session. Operator please.

Q&A Session

Operator: Ladies and gentlemen we will now begin the question-and-answer session. If you have a question please press the star key followed by the one key on your touchtone phone now. If at any time you would like to remove yourself from the questioning queue press star two.

Our first question comes from James Friedman, Susquehanna.

Mr. James Friedman: hi and congratulations both on the IPO and these exciting results. I had a couple of questions, first financial and then I want to ask you about slide five. I am sorry do not know this; but does the company plan to provide guidance and was there guidance given today or how should we be thinking about that?

Mr. XXX: thanks James. At this point we do not expect to provide any guidance for the year.

Mr. Friedman: okay. I also want to ask you about the share count. So the press release is using - correct me if I am wrong - but the press release I think is using 262 million; but that was the pre-IPO share count. How should we be thinking about the share count now?

Mr. XXX: the total share count right now is around 315 million shares that account for the 262 pre-offer. We also had primary shares issued and we also have a small amount coming from the long-term incentive plan.

So the total share count as is right now is around 315 million shares.

Mr. Friedman: got it and then maybe my last one about this slide five with the net margin of 23% and it is a helpful slide that shows the trajectory of expenses, the ratio administrative expenses and the 100 bps change. Just my question is how should we be thinking about that changing over time?

Mr. XXX: James obviously our business is a volume business and is a business that leverages expenses as we grow volume. As I said before we are not setting any specific targets here; but as volume continues to grow we should see leverage coming from expenses - because again it is a business, a volume growth business.

Mr. Friedman: okay thank you Eduardo all the best.

Operator: the next question comes from Jorge Kuri, Morgan Stanley.

Mr. Jorge Kuri: hi good morning everyone, congrats on the results as well. A couple of questions from me. I noticed that your net sales fell 5% QoQ and grew only 15% YoY, which was well below the growth in active merchants of 14% QoQ and close to 200% YoY.

What was the driver behind this? Why are POS sales down sequentially when you are adding so many merchants? Is this an issue of mix of devices, of prices, other? Anything you can help us, anything you can give to help us understand that would be great.

On the prepayment business can you let us know what was the volume prepaid and the average interest rate... in the quarter please so we can understand the drivers of that business?

And finally what is your expectation for TP growth this year? Thank you.

Mr. Alcaro: well let me... I will let Ricardo answer the first question and I will go through your last question. So again as I mentioned to James, Jorge, we are not providing guidance in terms of operational metrics this year.

In terms of further metrics as you are asking about prepayment volume and other specific metrics we are updating all the metrics that we provided in our F1 during our roadshow and during our IPO. So at this stage we are not providing guidance or any specific metrics beyond active merchants and CPV. And I will hand over to Ricardo to talk about the sale of devices.

Mr. Dutra: Jorge I guess the conversion between the quarter-over-quarter, year-over-year there are some things that happen through the year that we can at some point anticipate the sales, for instance we launched minizinha last year and with that we anticipated a lot of sales.

So when you compare 4Q with 4Q that is not something we are concerned about because we launched minizinha at the beginning of the year and then we anticipated the sales; and also there is this mix shift that we used to sell devices with higher price and now minizinha is an entry-level device.

So when you look in absolute terms it may be a little bit lower; but as we look at the number of merchants we doubled year-on-year from 1.4 to 2.8 million active merchants.

Mr. Kuri: thanks. Just let me just even then ask you a bigger question just understand where you guys are coming from. So there is any or you going to provide significantly less disclosure than what your peers do and no guidance is based on what I am sorry?

Mr. XXX: Jorge I think... let us think about it. We are disruptive, we grow extremely fast and we operate in markets that everybody wants to be nowadays. I understand what you are saying; but as a tech company we believe to the company's best interest to not disclose any further information beyond from what we already disclosed in the F1 and it was already available to our investors.

Mr. Kuri: all right thank you guys.

Operator: the next question comes from Gabriel da Nobrega, UBS.

Mr. Gabriel da Nobrega: hi everyone thank you for the opportunity. I just wanted to get more details and understand your views on the competitive landscape. Are you feeling any pressure at the bottom of the pyramid? And also as you begin to offer your solution how are seeing the movement of other acquirers? And I will make my second question afterwards.

Mr. XXX: thank you for your question. We believe we are well-positioned. We have a unique ecosystem that combines this cutting-edge and scalable platform. We know we are disruptive, 100% online. We have a strong brand in Brazil, we are well known.

But we... as you said competition should come at some point. We believe there is going to be competition, everyone is looking to us. They saw the IPO, they saw the business model; so there is going to be some competition but on the other hand there is so much room to grow that we also think that we are well-positioned and we will take advantage on what we have built so far.

Making long story short yes there is going to be more competition. Payment is something that everyone is looking for; but again we are well-positioned and accelerating to keep the growth and keep the results that we have got so far.

Mr. Nobrega: okay that is very clear and for my second question over the past few months we have actually seen that the central bank has been talking about updating and maybe even changing some regulations for the sector and more specifically the substitution of the D+30 to D+2 and I just wanted to get a bit more color from you guys on the possible impacts for your business if this change happens.

Mr. XXX: well first just a quick summary about what the central bank is doing in Brazil. The central bank has been doing a good job fostering competition. They are looking for more players in the market and that brings competition and of course we are one of them. So they see us as a company that is helping to fostering competition down here in Brazil.

The change from 30 to D2 we do not see that affecting our results because we already offer that for merchants. The change is not clear how the change is going to happen, if there is going to be the change in the interchange and other stuff and everyone could increase the price; so there is a lot of things that could happen with this change - but we do not see that affecting our results because we already offer one day for the merchants that desire to receive the money in the next business day.

Mr. Nobrega: all right that is very clear thank you.

Operator: the next question comes from Gustavo Lobo, J.P. Morgan.

Mr. Gustavo Lobo: hi everyone. I have two questions as well, the first question is if you could share with us how 1Q 18 is tracking, more specifically if POS sale has been increasing with the rollout of the new products and with the beginning of the year it is more likely that merchants switch from one acquirer to the other. So it would be interesting to see, to understand what should be the trend for now, and then I have a second question.

Mr. XXX: Gustavo the company believes that there are no structural changes in the business plan in the short to the midterm and as we mentioned before we are not sharing guidance at this stage, so prefer to do not comment how is trending and how 1Q or any forecasts in terms of TPV our sales of devices.

But what we can anticipate to you there are no material changes in the company from a structural standpoint.

Mr. Lobo: but have you already felt any change in the aggressiveness of competitors since the IPO in January until now?

Mr. XXX: of course as Ricardo mentioned before it is a competitive market. Players are looking in entering in the market, in fostering more competition; but again we do not see any material change from what we have seen in 4Q.

Mr. Lobo: okay understood and my second question is regarding selling expenses. On one hand there should be some scalability as top line grows and this is not directly linked to the top line; but on the other hand in order to continue growing you need to keep up with brand equity and brand awareness and so on and so forth.

So I just want to understand what is the strategy in terms of selling expenses, particularly as in 4Q 17 we saw decline vis-à-vis 4Q 16.

Mr. XXX: we know that our marketing is important; but as time passes by we see that our brand equity that we built the past years helps a lot for us to get new merchants. So I would say that marketing is part of our customer acquisition strategy - but it is not the main one as people think.

We focus 100% in user experience and we are having more and more people getting to us due to word-of-mouth and things like that. So we could see some leverage there and we do not believe that we need to keep investing in marketing if we want to new merchants.

Of course we are going to need to invest some, make some investment in marketing; but that is not the core. We have seen more and more word-of-mouth and people coming to us organically.

Mr. Lobo: that is clear thank you very much.

Mr. XXX: thank you.

Operator: our next question comes from Jason Kupserberg Bank of America Merrill Lynch.

Mr. Jason Kupserberg: hey thanks guys. I just wanted to pick up on a point around competition. It sounds like you are obviously seeing some of that and maybe it will intensify. I know you are not giving specific forward-looking guidance; but generally speaking how should we think about the implications for take rate over time? I mean do you see the prospect for a material deterioration of take rate as you look out over the next 12 to 24 months?

Mr. XXX: talking about MDRs we do not see that going down. If we compare 3Q with 4Q we were almost stable. It is also worth to say that in 4Q we have this high season in Brazil and people may use more debit during the Black Friday and even the Christmas season, and the MDR was almost stable.

Part of that is explained that we had more... When we compare year-over-year part of the 61 bps decrease in net take rate is due to the mix of debit cards that

we had more in 2017 as we had more Elo transactions, Elo cards transactions. So we do not see take rate going down as it has been stable in 2H 17.

Mr. Kupserberg: okay what is the mix now in your TPV of debit versus credit and within the credit piece how much of it is installments?

Mr. XXX: we are not disclosing that Jason but I would say to you that in terms of mix shift between debit and credit although we are only two or 3% of the market depending on the way look, we already have such a large size that we reflect the industry.

So you can use the breakdown of the industry as a whole for PagSeguro, it is 60% credit in 40% debit approximately the whole industry in Brazil and you can use the same figure for PagSeguro.

Mr. Kupserberg: okay and lastly a clarification on the regulatory side. In terms of what you are hearing from the central bank is the potential here to regulate or cap MDRs or inner change rates, or potentially either?

Mr. XXX: we do not see big changes for big bangs in this. The central bank is talking to everyone, we did not hear any caps in MDRs. Even in the interchange what the central bank is trying to do is to bring the interchange down - but not exactly through the cap, right?

The central bank wants the industry to work together to bring the interchange down; but not necessarily using caps. So still it is a long discussion; but going back to your question we do not see caps in MDRs being discussed at this point.

Mr. Kupserberg: okay very helpful thank you guys.

Mr. XXX: thank you.

Operator: the next question comes from Tito Labarta, Deutsche Bank.

Mr. Tito Labarta: hi good morning thank you for the call. Some questions I guess. In terms of the growth figure in merchants you doubled the size of the merchants going around 300,000 per quarter. I know you are not giving guidance; but is that a reasonable number to continue to assume, can that accelerate at all from here or with competition do you think the growth in merchants should slow down at least for this year?

And then on the back of that in terms of the average spent by merchants it looks it has been going up as you maybe go a little bit higher in the size of the merchants can that continue to increase? How do you see the... merchants evolving? Thank you.

Mr. XXX: hi Tito. As I mentioned before what we can say at this point we do not see structural changes in terms of our business plan and our business model.

Again we decided to not provide any specific guidance on those metrics and again, what I can say to you at this stage is there are no material changes in the business comparing 4Q to 1Q or what we foresee for 2018.

Mr. Labarta: I guess I understand that. Maybe thinking about Brazil in general with the economy recovering, things getting better I mean is there room for the market to get larger than we have seen in the last few years or... and offset competition? Or do you think the market is a kind of is big as it is going to get and this is a kind of the growth that is sustainable?

Mr. XXX: Tito you can see that Brazil is an underpenetrated market in terms of card transactions when you compare it to developed economies like the US or the UK. The growth of card transactions even during the worst years of recession in Brazil grew almost... Around double-digit figures when we had the worst recession ever.

So making a long story short what we see here is when the economy picks up - and it is picking up - we see Brazil coming out of the recession with a 1% growth in 2017, and we have a good forecast and the forecast for 2018 depends who you talk to could be between two and 4% - and as the economy recovers and the economy grows that will help everyone and will help PagSeguro as well.

Mr. Labarta: okay thanks that is helpful and maybe just one follow-up on the expenses just to understand what drove the big drop in selling expenses in the quarter compared to last year - 38% drop, I just want to understand what happened there.

Mr. XXX: it is really our size in terms of leveraging expenses, leveraging our costs. So again in our business model as the business continues to grow we should expect leverage coming from expenses.

Mr. Labarta: okay and given that... that is a little bit more up to you in terms of controlling expenses to some degree, even if just on the administrative and selling expenses and the cost of services and... let us say minus volumes; but is there room to continue to sort of control the growth there in the selling and administrative expenses and keep costs under control from that perspective?

Mr. XXX: well when we compare 2017 to 16 being more specific here, our operating leverage was concentrated mainly as you said in selling expenses, I mean call center. We have operating efficiency and greater penetration of mobile transactions versus web. In mobile transactions we have a natural reduction in call center demands and in automatic answers to our customers.

In terms of connectivity cost we also had a renegotiation with main suppliers and again, our business does not grow... As the business grows we do not go personnel as the business grows. So we continue to see leverage coming from personnel expenses.

Mr. Labarta: okay thank you.

Operator: the next question comes from Craig Maurer, Autonomous Research.

Mr. Craig Maurer: hi thanks. I was hoping you could talk about capital allocation going forward. I know you are going to take the IPO proceeds to fund prepayment; however there are a number of sim tech startups, other companies in Brazil that could prove interesting if... grow in an inquisitive mode? Thanks.

Mr. XXX: I am not sure I followed your specific question. If you could rephrase I would appreciate.

Mr. Maurer: I am just trying to understand how you view capital allocation going forward. I understand that most of the IPO proceeds will go into lowering financial expense for prepayment; however could PagSeguro be an acquirer of smaller companies in Brazil that might further... penetrate in financial services?

Mr. XXX: all right I got you. Let me start with the second question. We constantly look at new companies and new technologies in terms of M&A; but on the other hand we do not see anything transformational from an M&A standpoint.

From the IPO proceeds as we anticipated to our investors the majority of the capital will go to the prepayment business and the amount of the primary proceeds will be enough to fund 2018 and 2019 in accordance to our business plan, and after that we will be basically self-funded.

Mr. Maurer: okay thank you very much.

Operator: The next question comes from Tiago Euzier, Goldman Sachs.

Mr. Tiago Euzier: hi gentlemen good morning, congratulations on publishing your first set of results and thanks for taking my question. So first I understand you are not providing guidance at this stage; but conceptually how should we think about seasonality in 1Q for your line of business?

And secondly could you please comment on the opportunities you are seeing ahead in terms of products, particularly with your new lending platform Biva where do you think that can take you? Thank you.

Mr. XXX: I am going to talk about Biva first. We acquired Biva, a lending company, it is a small business still. We look into that very carefully, we have got to understand about this business - but a good point or the positive point is that we already have the platform with us, we acquired the company.

I mean we are still evaluating how we will go forward with this type of business. At this point we are focusing on the core, which is to acquire new merchants and keep doing what we know how to do. We do not want to have any huge distractions at this point of time. That is the general answer about Biva.

1Q as we said we are not giving any guidance; but I would say that things are going as we expect. We do not see any big changes according to our business plan, according to what we expected for. So even with competition and so on that we know that we are going to have, we are having and we are going to have in the future; but things are doing well at this point and as we expected.

Mr. Euzier: perfect thank you very much.

Mr. XXX: and Tiago into your last question we do have seasonality in 4Q. 4Q is the strongest season in terms of sales for all the retail if you take Christmas, the holiday season and also the Black Friday in November.

Mr. XXX: thank you very much.

Mr. XXX: thank you.

Operator: This concludes today's question-and-answer session. I would like to invite Mr. Ricardo Dutra to proceed with his closing statements. Please go ahead sir.

Mr. Dutra: Yes we would like to thank you all for the time spent with our management team. We would like to reinforce our commitment and focus on delivering solid results aligned with governance and best market prices, and see you all in the next conference call, thank you very much and have a good day.

Operator: That does conclude PagSeguro's audio conference for today. Thank you very much for your participation, have a good day and thank you for using Chorus Call.
