
Operator: Good morning. Welcome to the TOTVS conference call to discuss the results of the second quarter of 2016. We have with us Laércio Cosentino, CEO and Gilsomar Maia, CFO and IRO.

Note that all participants will be on listen-only mode during the presentation. After that, we will have a question and answer session for investors and analysts when further instructions will be given. If anyone needs assistance during the call, please press *0 to reach the operator.

The audio is being simultaneously webcast at ir.totvs.com

Before proceeding, we wish to clarify that any forward-looking statements that may be made during the conference call, related to business outlook, operational and financial projections and targets of TOTVS are based on beliefs and assumptions of the Company's management as well as information currently available. Forward-looking statements are not guarantee of future performance. They involve risks, uncertainties and assumptions as they refer to future events and, therefore, depend on circumstances that may or may not occur. Investors must understand that general economic conditions, industry conditions and other operational factors could affect the future performance of TOTVS and could lead to results that differ materially from those mentioned in these forward-looking statements.

Now, I will turn the call over to Mr. Cosentino, who will begin the presentation. Mr. Cosentino, please go ahead.

Laércio Cosentino: Good morning everyone. Thank you for attending the Company's earnings conference call regarding the second quarter of 2016.

I wish to kick off with the main recent events, shown on **slide 3**.

On May 11, the Company paid to its shareholders the dividends approved at the Shareholders Meeting held on April 26, 2016, in the amount of R\$66.6 million, related to fiscal year 2015.

On August 1st, the Board of Directors approved the distribution of interest on equity related to the first half of 2016, in the amount of R\$43.6 million, equivalent to about R\$0.27 per share, which is 49% higher than the interest on equity paid related to the first half of 2015. Said interest will be paid on August 24 to shareholders of the Company as of August 4.

Also on August 1st, TOTVS sold its Human Resources BPO operation to Propay, a company that has been providing this BPO activities for over 15 years. With this movement, TOTVS reinforces its strategy of specialization, bringing a focused partner in this activity to boost sales of TOTVS solutions and provide greater value to its clients.

In May, TOTVS signed a partnership agreement with National Computer Corporation (NCC), the biggest technology company in Russia, to set up National Platform, a company that will develop and market in Russia a new management system that will be

developed based on TOTVS' technology platform. With this project, TOTVS is testing a new way of exploring opportunities in the international market, without losing focus on Brazil.

Also in this quarter, we took an important step in the reorganization of our organizational structure, with the election of Gustavo Bastos and Marcelo Eduardo, that together have over 30 years of TOTVS, and will be responsible for the macro-segments of Supply Chain and Services respectively.

These management changes are part of the Company's strategy, which established a divided organizational structure in macro-segments through core-business solutions integrated with back-office solutions, which contribute to the integration of the major value chains.

Finally, on **slide 4**, we started our investments in the facilities of our new head office. As announced to the market on October 16, 2013, the Company signed a built to suit agreement for its new head office. It is a 10-year agreement starting from the delivery of the building, scheduled for February 2017.

In addition to tangible and intangible administrative synergies to be captured with the concentration of the main Company's administrative, development and sales departments in the São Paulo area in just one place, this new campus will contribute to a faster spread of our culture between employees, especially between those that became recently part of TOTVS, like Bematech.

The new campus will also have an exclusive area of client service and will provide an innovative environment to help reinforcing mobility and cloud, which are essential elements in our strategy. The total investment in facilities is estimated at approximately R\$90 million.

I now turn the presentation to Maia for his comments on the results of the quarter, starting on **slide 5**.

Gilsomar Maia: Thank you Laércio. Good morning everyone.

Before starting my comments, I wish to remind you that to preserve comparability, we have presented the consolidated pro forma unaudited figures of 2Q15, which include the results of Bematech during that period.

This quarter, total revenue decreased by 2% year on year and by 1% quarter on quarter, mainly due to the decrease of 15% year on year and 4% quarter on quarter of non-recurring revenue, shown on the chart to the left.

Recurring revenues grew 8% year on year and reached 61.7% of total revenue, which represents an increase of 5.8 percentage points over 2Q15.

When analyzed by business, as the chart on the right, we see that the drop in total revenue was concentrated in hardware and service revenue. On the other hand, the decline from 1Q16 was concentrated on the 3% drop in software revenue, which I will comment now on **slide 6**.

Software revenue remained stable year on year since the growth in recurring revenue from maintenance and subscription offset the 32% decline in non-recurring license fee revenue.

The 17% growth in subscription revenue in this period was largely due to sales to new small and medium clients under the TOTVS Intera model, which completed one year last June.

In this first year of TOTVS Intera, the growth in subscription revenue exceeded the decline in revenue from the licensing model, represented by license and maintenance revenues, as shown on the chart to the left.

Compared to 1Q16, the 4.2% growth in subscription revenue was not sufficient to offset the decline in revenue from the licensing model, especially the 23% drop in licenses revenue.

In fact, the decline in license sales in earlier periods, combined with the suspension of maintenance agreements due to higher default levels and partial cancellation of maintenance due to layoffs at clients, resulted in a 0.6% decline in maintenance revenue during the quarter.

Despite all these short-term effects on software revenue associated with the transition to the subscription model, the Company did not reduce its R&D investments. Actually, TOTVS has made new investments in client service and support, involving adjustments in internal routines, teams and software solutions.

As a result of this combination, software contribution margin fell by 4.4 percentage points year on year. In the quarter-on-quarter comparison, apart from all that I just mentioned, the 2.8 percentage points drop in contribution margin mainly resulted from the incremental revenue of R\$10.7 million from the corporate model reported in 1Q16, as shown on the chart to the left on **slide 7**.

Excluding this incremental revenue from the corporate model, the quarter-on-quarter decrease in licensing fee revenue came to 3%, mainly due to the 9% drop in new client additions during the period.

As already commented in previous quarters, the decline in license sales has mainly been the result of the economic downturn in Brazil and the partial migration of the sales pipeline among new clients to the subscription model especially smaller ones.

Despite this market momentum, we added 847 new clients in the licensing model, 900 new clients in the subscription model, and 440 new clients of Bemacash in the quarter.

The Bemacash solution combines TOTVS' management software for microenterprises (Fly01), under the subscription model, with commercial automation and fiscal solutions of Bematech.

It's worth mentioning that sales of the Bemacash solutions did not affect the subscription revenue in 2Q16, since new clients of Bemacash become software clients from the 8th month of hiring the management solution, when they start paying the subscription.

To conclude our comments on software results, we share on **slide 8** an exercise carried out internally, which simulates the impact on growth in software revenue if the Company had chosen to sell its software solutions exclusively through the subscription model since 2013. In this hypothetical exercise, the quarterly license revenue was deferred in 16 quarters and any impacts of churn, inflation adjustment and migration fee were not considered.

In short, if the Company had chosen to sell its solutions only through the subscription model since 2013, the growth in software revenue in 2Q16 would have been 11%, which reinforces the med/long-term financial benefits of the subscription model.

I now invite you all to move to **slide 9** to discuss services and hardware.

The chart on the left shows that service revenue fell 4.8%, compared to 2Q15, and remained stable quarter-on-quarter. The year-on-year variation is mainly due to the 7.8% decline in software implementation services in the period, which accounted for 62% of the service revenue in the quarter, chiefly due to the lower pace of sales in recent quarters.

As in 1Q16, service contribution margin increased from the previous quarter, growing 140 basis points in 2Q16. This recovery in service contribution margin is chiefly due to the reduction in recurring personnel costs resulting from the cost and expenses structure adjustments carried out by the Company during the second half of 2015.

In the case of hardware, shown on the right side of the slide, the 7.8% drop in revenue compared to 2Q15 chiefly reflects the economic downturn in Brazil and the changes in tax legislation, especially in the state of São Paulo, where fiscal printers were replaced for the S@T equipment, which has a lower value per unit, but in the other hand helps drive the growth of recurring revenue from fiscal software solutions.

Apart from the decline in revenue, hardware margin was adversely impacted by the year-on-year comparison by the reduction in tax subsidies in the state of Paraná.

In the quarter-on-quarter comparison, the 7% growth in revenue reflects the seasonality of hardware sales and the price adjustments related to FX rate, which also helped drive the growth of 190 basis points in the contribution margin.

For comments on selling and administrative expenses, please move to **slide 10**.

Starting with the chart on the top left, selling expenses and commissions jointly grew 3.6% year on year and 0.4% quarter on quarter.

This increase mainly reflects the higher volume of software sales under the subscription model, since the transition to subscription does not impact the sales team compensation.

On the top right, advertising and marketing expenses corresponded to 2.2% of total revenue, versus 3.1% in 2Q15 and 1.5% in 1Q16. The year-on-year decrease is chiefly due to the revision of the general marketing plan and the integration of the marketing activities of TOTVS and Bematech. The quarter-on-quarter growth reflects the seasonality of this expense line.

Expenses with allowance for doubtful accounts, on the top left, corresponded to 1.3% of total revenue, compared to 1.6% in 2Q15 and 1.4% in 1Q16.

Note that considering the current level of defaults in the market and the increase in the balance of accounts receivable past due, the Company will follow closely this matter and will work on the recovery of the debts already under provision.

And finally, on the lower right corner, general and administrative expenses plus management fees and other expenses increased 7.5% year on year, mainly on account of wage increases, net of layoffs.

Moving now to EBITDA and Net Income on **slide 11**.

The chart on the left shows that EBITDA in 2Q16 totaled R\$96.9 million, down 20.8% year on year and 15.4% quarter on quarter. EBITDA margin in the quarter reached 17.8%, down 420 basis points year on year.

The year-on-year decline in EBITDA was chiefly due to the drop in contribution margin from software and hardware, both already commented before.

In the quarter-on-quarter comparison, the decline in EBITDA is mainly due to the drop in software revenue, largely reflecting the reduction in licenses revenues.

In the case of net income, shown by the chart on the right, the year-on-year decline was largely due to the negative financial result in 2Q16, primarily as a consequence of the reduction in financial revenues due to the payment of the transaction with Bematech in 4Q15.

In the quarter-on-quarter comparison, the decline in net income compared to the drop in EBITDA largely reflects the increase in the Company's net debt during the period, as shown on **slide 12**, where I will make my comments on cash flow and debt.

Gross cash decreased by R\$60 million in the quarter, mainly due to:

- (i) the payment of dividends regarding the 2015 fiscal-year; and
- (ii) the partial amortization of the principal amount of the BNDES loan hired in 2013.

Net debt totaled R\$493 million in 2Q16, equivalent to 1.2 times pro forma adjusted EBITDA in the last 12 months. It is important to remember that the remaining R\$48 million regarding the principal amount of the debentures issued in 2008 will be amortized in this month of August, 2016.

I now turn the presentation back to Laércio for his closing remarks on **slide 13**.

Laércio Cosentino: Thank you Maia.

In short, the additional revenues from the 17% growth of subscription revenue exceeded the decline in revenues from the licensing model and kept the software revenue stable in the year-on-year comparison.

In June this year, TOTVS Intera completed 1 year of its launching, the subscription model in which clients define and manage the number of identities they will be enabled to gain unrestricted and simultaneous access to all management, productivity and collaboration software solutions from TOTVS.

This first year has shown that we are on track. We already have more than 600 clients in the Intera model, which corresponds to more than sixty-five thousand identities using our management systems and collaborating with our subscription revenue growth.

It is also worth mentioning that the 2Q16 subscription revenue did not reflect the Bemacash sales recorded in 2016. Bemacash, as mentioned by Maia, combines TOTVS management software for micro-companies "Fly01" in the subscription model with automation hardware and fiscal solutions of Bematech.

In this quarter, Bemacash sales for new clients reached 440 units, a 48% increase over the amount sold in 1Q16. This growth is mainly a consequence of the Company's hard work in training its resellers in order to increase subscription sales among smaller companies.

In summary, these two initiatives brought over 1,000 new clients and shown that the subscription is important for our growth and for increasing the efficiency of our operations, especially in a more adverse economic scenario, in which the combination of subscription and cloud can be an alternative to clients and prospects to reduce costs and, at the same time, increase their operations productivity.

Despite these impacts in revenue associated with the transition to the subscription model and the Brazilian economy momentum, we did not reduce our investments in innovation. On the contrary, we carried out new investments to innovate support to our clients, and we were recently elected by Valor Econômico newspaper as The Most Innovative Company in the IT industry.

We are close to moving from a mostly B2B for a B2C company, directly connected with individuals and in a much more relevant way with things, through sensors that will integrate our technology in various environments. That is, we are developing solutions used by clients of our clients.

We also raised our services and hardware margins quarter on quarter and started to invest in our new headquarters, reinforcing our strategy on cost discipline and on the continuous search for efficiency gains in our operations.

We are working to make TOTVS and our clients much more prepared for the recovery of the Brazilian market. We have seen some initial signs of market activity recovery, that

hasn't translated into sales yet, but we are confident that Brazil will come out of this much stronger.

Now we are available for the Q&A.

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 please press star two.

Our first question comes from Daniel Federle, Credit Suisse.

Daniel Federle: Good morning everyone. My first question regarding these signs of improvement mentioned by Laércio. Can you add some color as to what indicators you have noticed and what types of clients should start showing the first signs of sales recovery? Are these big clients or small clients?

My second question is regarding the churn rate. Going by the maintenance numbers, it seems that churn has increased in recent months and I wish to know if you consider it a trend that should increase over the rest of the year or if it has already peaked and should decline going forward. Thank you.

Gilsomar Maia: Good morning Daniel, it is Maia speaking. Starting with the churn rate. Indeed, in terms of financial churn, we are facing a higher-than-usual level, even compared to the fourth quarter and the first quarter. There's a component related to the level of delinquency itself; and just to remind you that in general, if a client delays more than three monthly maintenance payments, the maintenance service is suspended and consequently the collection for that service is also suspended - and this impacts my recurring maintenance revenue.

There are cases related to the cancellation of users, which would be partial cancellation of maintenance contracts, which is very closely related to the headcount reduction in some companies.

I think the two questions you asked are related, because this scenario I described for the churn rate - even to give you more elements to consider whether or not we've reached the peak of churn - when we talk about the subtle signs, they come mainly... for some quarters now, there has been a significant volume of accounts, especially larger accounts that have been frozen in recent quarters, at least last year or year and a half.

And for some we hadn't seen any form of activity in several of these accounts. More recently, we started to see some clients or even prospects coming to us again to talk about the project. None of this has been converted into sales but at least it's a start for reactivating these talks which, in my opinion, depending on how the political scenario unfolds in the coming months, could create a more favorable environment and this reestablishment of talks could lead us further on to close some sales deals.

This improvement in market sentiment would also help me here in terms of maintenance churn.

So, these initial signs lead us to believe that, in theory, the worst is behind us. Now, of course, we can't let our guard down and think everything is resolved. I think a topic such as churn is still a key aspect that deserves our attention and we'll continue to monitor it.

Laércio Cosentino: You asked – it's Laércio here – about the segments. In the service segment, we can already greater movement. Like Maia said, no deals have been closed, but truly an increased search for solutions.

Several proposals are on hold, so at least the resumption of negotiations, "let's go, let's talk again, let's see what you can do for the proposal you made some time ago".

The small business segment, when you talk about 440 Bemacash clients, an increase of 48%, this shows – you're right that this is TOTVS – but as an increase in activity at the bottom of the pyramid.

And 900 subscription clients is a very interesting number when you talk about when where we are picking up activity, with smaller tickets, because you don't have the license value, but if you look at the numbers, the average ticket of our clients, you'll see that it increased. So there would be an increase of nearly 30.9%.

This shows that small and medium businesses have already started resuming their demand for services, and the question of small manufacturers has also been evolving.

Gilsomar Maia: Daniel, if we compare the beginning of this quarter with the business volume we generated, sales of services, for example, if we compare April to June, we see substantial improvement.

It's true that this sort of behavior has become constant in the IT industry as a whole. A greater number of deals is closed at the ends of quarters. But excluding this seasonality, which I think has become somewhat typical in our sector, we saw that overall sentiment has improved.

So, if we compare the mood of our sales team, even the volume of interaction with our clients at the end of the quarter compared to the beginning of the quarter, there was a clear improvement internally.

Daniel Federle: Great, thank you.

Gilsomar Maia: you are welcome.

Operator: the next question comes from Marcelo Santos, JP Morgan.

Marcelo Santos: Thank you for taking my question, good morning to everyone. Can you shed some light on the adjustments to customer service that are currently underway? That is my first question.

And, second, with regard to the capturing of synergies with Bematech, what is the current status? What can we expect going forward? Those are the two questions.

Gilsomar Maia: Good morning, Marcelo. Starting with the synergies with Bematech. From the end of last year until now, what we've done and was perhaps more clear in the last few quarters was, first of all, the administrative integration. That was quick, I think it's a more obvious integration too.

Next came the integration of the commercial areas, with offerings to clients and the unification of the pipeline. And, finally, we worked faster on the aspect of bundling solutions, joint offerings that could be differentiated, also with more immediate effects.

In this regard, some solutions we had already started working on together have created a lot of opportunities for us with some clients, but perhaps from everything we discussed in the conference call, what is more significant to me, for instance, is Bemacash, which is an offering that Bematech already had last year but which registered significant growth in sales volume now in the first half of the year, more specifically in the second quarter.

And this happened when we unified our systems focused on this target group of smaller companies that were part of Fly01, with automation equipment in the format of Bemacash, which is a type of more modern mobile POS, based on a tablet platform.

When we unified these two offerings of TOTVS with Bematech – and this was done in a segmented manner with this target of small businesses – we saw that sales of the offering really picked up.

So, to me, more than talking about other aspects, I think this really materializes this part of the synergies with Bematech, which is less related to cost because this is the moment we are going through and we are starting to create more synergies in sales.

For next year, as I mentioned last quarter, we are already planning to work with a second wave of administrative synergies that will be related to standardizing management systems of Bematech with those used by TOTVS, and then we'll have a resulting opportunity to have a new wave of synergies as a result of this standardization.

Right now, I'd say the synergies are more closely related to creating offerings and to sales synergies.

With regard to the adjustments to the helpdesk that you asked, a few years ago we had already made some changes in the service and technical support team serving our clients and since then, in light of everything we've also done to unify other operations, even some that we acquired, and of all the changes we've seen in the user experience of our clients, social media channels, mobile devices, clients today interact with us in several ways.

So we felt the need to modernize the tool itself, the systems used by our customer service team, so it can capture these interactions with the client through these different communication channels, and that also requires the team to have a different profile that can interact with clients in these diverse fronts.

So, this implies training, changes in the team configuration and even redesigning the customer service flow so we can really provide our clients with good service, more modern technical support and more proactive service.

Laércio Cosentino: I think it's important, when we talk about having solutions for our clients, to broaden the number of profiles that can use our software. So, system users that used to interact with us to get support, to get better service, we end up encompassing a much wider array of people.

So when you talk about working, for instance, in a university, it's not just interacting with the system users from the faculty, the administration of a university, but also students.

So this change we are promoting is important for us to be able to capture any need, any channel of communication. Our clients are increasingly more connected and especially the clients of our clients. This is the work we're doing.

Marcelo Santos: Perfect, thank you for the answers.

Laércio Cosentino: Thank you.

Operator: the next question comes from Diego Aragão, Morgan Stanley.

Diego Aragão: Good morning everyone and thanks for taking my question. Laércio, Maia, going back to the aspect Marcelo mentioned about margin, I'd wish to understand the topic of synergies. I'm asking this because margins reached a relatively low level and we see the volatility quarter-over-quarter somewhat increasing since the integration of Bematech.

So, can you add some color to the topic of synergies. You mentioned the topline, synergies in sales and sales structures, but what should we effectively expect from now on, especially in terms of margin? And even looking by business line, the contribution margin in each of them fell year over year. So what should we expect going forward? Thank you.

Gilsomar Maia: Good morning Diego. Regarding the question of margin, I think it's important to note that Bematech's business itself faced some seasonality that is specific to the hardware market. The software market also has some seasonality, which in TOTVS's business model has always been attenuated by an element called the corporate model.

It's very common in the global market to see, for instance, a weaker first quarter in terms of software sales and in this sense the corporate model has always played an important role in complementing revenue in the first quarter and reduce this volatility in revenue. Other than that, the market in general has some volatility between quarters.

I understand that, when we combine the businesses, this could cause some additional difficulty for everyone to follow our margin on a monthly basis. We must also take into consideration that today, forecasting in the Brazilian market as a whole is a bit more difficult.

In any type of business today, you can see higher volatility than you used to see in the past. So, in several sectors, including banks, we saw some volatility in quarterly margins. Of course, here we are talking about a business with a high level of recurrence, which should make forecasting easier.

We will always have quarterly volatility. At the end of last year, when we discussed margins, we reminded you that the Company, especially in a moment like this when it concludes the first year of this cycle of transition from the license to the subscription model, it would be prudent not to give the market any guidance on margins, especially when consider the volatility of the Brazilian market.

In my opinion, it would be irresponsible for us to share any type of internal projection, because the market in general has very little forecastability. But even without giving any guidance on margins, we already knew - and we shared that sentiment with the market - that the first year would be the most challenging one in terms of margin because you still haven't fully reaped the benefits of the sale of subscriptions but have already stopped earning an upfront licensing revenue.

So I can't make any surprises with this type of volatility in margins that we've seen and the volatility between quarters has always existed in our business. In my opinion, if we close this year at a level, perhaps not equal but close to the level at the end of last year, and considering all this volatility we are seeing in the market, that would be an achievement for the Company.

This is not some guidance. I'd say it's more of a feeling I'm sharing. I'm not saying it will happen, but I think the Company must always pursue greater forecastability, margin expansion etc. But we must also understand the ground reality.

I can't, first of all, go against the numbers nor can I deny the reality that everyone is facing in the market.

Laércio Cosentino: Good morning, Laércio speaking. As Maia said, this is the first year of the subscription model and this is something relatively new for almost all software houses, and so I think it's important that you adjust the cost of clause, the sales team, and implement smaller projects, also because when you talk about subscription, you're based on the assumption - we joke about this a lot - that it's a give and take. I mean you sign something, you implement it, it's OK, and you subscribe to something else, implement the rest and so on.

So, there's a phase of learning and adapting. Even if TOTVS actually put into practice all that we planned for subscription, we still depend on people, people who sell the software, people who implement it and people who consume it.

So, what we've been seeing is exactly the behavior of each of these links in the software distribution chain. It really has changed.

And, on the other hand, unfortunately - or perhaps fortunately - we live in Brazil and particularly this year, while there's no clear definition of the country's path, whether we'll have an increase in taxes, which I personally believe we won't, but then how will we overcome the country's primary deficit, how will the Temer administration act, if he will indeed stay the next day after they say "you're now official".

And this really leads to uncertainty in a series of businesses. So, when we look at Brazil, the issue of the subscription model and the company itself, you're always going to innovate, you're going to invest, you're going to have opportunities for improvement, and of course TOTVS is being able to address these three aspects.

We are a company focusing on the medium and long terms, so I don't think we could have higher margins. Did margins fall this quarter? We could simply stop a series of investments, but that could jeopardize the future of the Company. We believe in what we are doing. Of course we must be careful with the Company's costs and all that.

But when we look especially on the slide that we mention subscription licenses, if we had started subscription since 2013, we would be recording growth of almost above 11% between the quarter in 2015 and in 2016.

So, I think we're moving in the right direction and must not forget the scenario we are operating in and the scenario in the information technology sector.

Diego Aragão: Perfect Maia, perfect Laércio. Just a second question: I'd like to understand what you think in terms of leverage. It's currently at 1.2, if I'm not mistaken, as cash generation has been suffering in recent quarters, or at least it has been decreasing.

At the same time, you just announced an investment of around 90 million on the new headquarters. According to my calculations, you'll be very close to reaching a debt covenant.

Is that right? Just to know if I'm looking at this the right way, thank you.

Gilsomar Maia: In relation to the covenant, I believe you're talking mainly about that tighter one, of 1.5 times. It's important to note that this is not the only indicator that triggers this covenant. There's also an issue related to own/loan capital and in relation to the company's total assets.

Even if we reached this level, I'm not settling my debt early. The only thing I have to do with BNDES is provide security interest, a bank guarantee or any form of security interest. In this case, a real covenant we would be talking about is 2 times EBITDA. I don't see this scenario happening. So, I don't see this happening in this scenario.

Diego Aragão: Perfect, Maia, very clear, thank you.

Gilsomar Maia: You're welcome.

Operator: the next question comes from Susana Salaru, Itau.

Susana Salaru: Good morning everyone. I'd like to go back to the topic of synergies of Bematech. Could you add explain how utilization is and how Bematech's sales channels are developing, and when you expect to be able to fully use it.

And can you also discuss a little about the dynamics of payroll tax and the increase in social security tax (INSS)? Are you already transferring it to new contracts? Are you able to transfer it? How's the discussion of this topic evolving? Thank you.

Gilsomar Maia: Good morning Susana, this is Maia speaking. Well, to start with Brasil Maior, as you asked, this was a topic that really started to have an impact since December last year when the new INSS rate of 4.5% came into force.

Since then, we've been working this theme with clients. As we predicted, we wouldn't effectively be able to transfer the entire impact to clients, because of the situation we've seen in the companies.

And when we talk about churn, since the end of last year, as I mentioned, in some quarters it's hard to associate, for instance, the reduction in a maintenance contract to an adjustment of this kind because generally when this happens the client links this to a reduction in its operations.

But I personally attribute a portion of this reduction in maintenance to this type of adjustment too, which was caused by the increase in the INSS rate of Brasil Maior.

If we isolate the transfer of the adjustment under Brasil Maior, we were able to transfer most of it, almost all of it, but when I look at the figures for maintenance churn and I see that the churn rate has been relatively high, I also attribute a portion of this churn rate to this adjustment.

It's hard to determine how much, Susana, because as I mentioned, the client usually doesn't use this type of argument to reduce the scope of a contract.

With regard to the Bematech channels, I would break them down into two types: the software channel, which is the origin of the acquisitions, especially by Bematech. These channels are already highly integrated with Bematech's software channels, which are often our own channels too, with their own franchises and so this part of the software operation is already working together.

There's another specific aspect that we are fine-tuning right now, which is related to the offerings that we're working jointly with Bematech. But there are business opportunities, for instance, a client we can serve with both Bematech and TOTVS solutions. While we don't have a joint offering, in some specific cases, the channels are already working on these opportunities together.

So, there aren't two points of interaction, let's put it this way. You have both teams working together and serving the client as one.

In terms of the channels that are more closely connected with hardware sales, these Bemacash sales we've seen have taken place through these channels to these Bematech resellers. So, this is already a joint offering, as I explained previously to Daniel, where we bundled the TOTVS software together with the Bematech equipment, fiscal software solutions and equipment also of Bematech and formatted this Bemacash offering.

Of course, since it is a different solution from that traditional Bematech hardware, it has required some training of the reseller channels, and this has been a part of the integration process since the beginning of the year. We have trained a significant number of Bematech resellers every month and a part of this growth in Bemacash sales also reflects this increased number of reseller channels we've been training.

So, every month, we have been training a significant number of resellers and I believe the trend is that the more channels in this Bematech distribution network we train, the higher will be the growth in sales volume.

Susana Salaru: Perfectly clear, Maia, thank you.

Gilsomar Maia: Thank you Susana.

Operator: Our next question comes from Valder Nogueira, Santander.

Valder Nogueira: Good morning. Back to Daniel's question that is very important, you mentioned the beginning or perhaps a light at the end of the tunnel of a recovery in services. The market is divided as to whether this recovery of Brazil will be driven by services, by consumption or by investments in capital goods or even manufacturing. Laércio mentioned small manufacturing.

Can you give us a little more color of how this is with you? Because if there's really a stronger recovery in manufacturing, whether small or big, it could be an opportunity for you to improve sales.

And, coupled with that, do you believe this time the recovery of Brazil, some external factor could help the company, like Sped did last year? We now have the issue of the electronic invoice, some external factor you think could help improve this situation? That is my first question.

Gilsomar Maia: Good morning Valder. In relation to external factors of this nature, there's always something new. In the last year, what we've seen, and which is still under way because usually these new requirements from the government don't come all at once, they usually start implementing in bigger companies and scale down until they reach micro-companies.

This was the case with the electronic invoices back then, then with the fiscal Sped system, the accounting Sped system and more recently with e-social, which hasn't reached the public completely yet. So this is an external factor, as you said, which is still impacting the market and for which there are not many options because it is fiscal compliance, it's something you have to do.

And now, more recently, we had the Block K, which at the end of the day is the name that was given to production and inventory control of industries, especially. So, this is will be implemented, the timetable is under discussion, the government has already postponed the implementation of this Block K.

But for the beginning of next year, it is already expected that companies of a certain size - which I can't remember right now but based on gross revenue, which was a threshold set by the government - they will have to comply with this obligation starting next year - which ends up revealing to tax authorities the entire cost structure of a product.

So, if you combine all that together with the electronic invoice, the government could already track everything the company purchased and sold, they were only lacking a vision of the middle of the way. "OK, the company purchased a lot of things and sold a lot of things, but from what it purchased, how did it get to a final product that it sold?"

So, Block K actually reveals to the government the structure of the production cost of each item of each product sold by a company. So, this is where you connect purchases with the cost of production and you arrive at the composition of the cost of sale of the goods sold.

It's a very complex item. It has required many companies to revise their systems because the level of detail of information required by the government is quite high and so several industries, for instance, which in the past developed proprietary production control systems - which is quite common in large companies and companies that use market solutions - many of them often prefer to maintain the tailored proprietary solution to cover this sort of activity.

The thing that a lot of these companies have faced is that, with this new demand for Block K, the systems that were built back then are not ready to provide all details of information that the government is requiring now. So, many of these companies have set as one of their requirements the replacement of these proprietary systems by modules of market solutions they already use.

So, this could be an external factor that may help us and everyone in the market working on this type of solution because, like I said, this is the sort of demand that doesn't leave you with much of an option.

Laércio Cosentino: Valder, good morning, thank you for your questions. When I mentioned that we were already seeing a subtle improvement in the market and I stressed the part of services and the part of small companies, small manufacturing companies, TOTVS adopted a strong positioning in recent months to understand this entire crisis.

And, first, in terms of retail, a total of 110,000-120,000 stores were shut down. So, we understand that the recovery will come from smaller players and then with Bemacash and with our strategy of simpler things, subscription and all that, we will address that and, as soon as we have higher demand, new store openings, we believe that small things will be reborn.

It's not major retail chains opening new points of sale, because they were all more or less committed to shopping malls, already committed to areas they had negotiated before and which were postponed.

When you talk about supply chain with Intera, we see that we can strongly address this growth of small manufacturing companies that are coming up in various corners of Brazil.

And in terms of services, we see large construction companies facing increasing problems and small and medium construction companies taking the place of the former as soon as infrastructure investments start to sprout everywhere in Brazil, and most of these companies are TOTVS clients. So, we are very close, very alert to be able to capitalize on this recovery of small companies, especially in the construction and infrastructure industries, which will certainly benefit. That's it.

Valder Nogueira: And you consider this more important than capital goods, large manufacturers? Do you think the driver could come from this side than from large manufacturers?

Laércio Cosentino: I think the number of clients will certainly come from the bottom, and when we say we're working to make TOTVS increasingly more of a subscription company, it means we had a recurring revenue of over 60% from maintenance contracts and now we will increasingly expand this recurring revenue.

And that will come precisely from this fragmentation... we believe the resumption will be fragmented. And from large companies with pent-up projects, but also with several licenses that they had acquired that they simply deactivated or stopped using.

Valder Nogueira: My second question is related to inflation: you have a 12-month IGP-M that benefited your maintenance contracts. On the other hand, we've never seen this tailwind effect benefiting revenue so much this quarter. What is the dynamic behind it?

Laércio Cosentino: What you have is exactly this: at the moment you see most of the companies trying to reduce their costs, the cost of a high IGP-M is negative, because it impacts the discussion of any discounts based on the IGP-M.

Last year, it was a higher IPCA against a lower IGP-M, and so there wasn't much discussion. Now that we can benefit from a higher IGP-M and a lower IPCA, often the client wants to reduce something so that they will really have a contribution from their suppliers to reducing their total costs.

So, we believe an improvement of the market mood and with the economy gaining strength, this negative agenda of cost cutting will become less relevant, giving place to revenue growth. We are working in this direction.

Valder Nogueira: OK, thank you Laércio, thank you Maia.

Gilsomar Maia: Thank you.

Operator: As a reminder if you would like to pose a question please press star one.

This concludes today's question-and-answer session. I would like to turn the conference over to Mr. Cosentino for his final considerations. Please go ahead sir.

Laércio Cosentino: I'd like to thank you all for participating in this conference call and wish you have a nice day and that in the next few days we can really see the definition of Brazil's direction.

We here at TOTVS are everyday much more optimistic. Good morning everyone.

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