Operator:

Good morning. Welcome everyone to TOTVS's 2Q13 results conference call. Today with us we have Mr. Alexandre Dinkelmann, Executive Vice-President of Strategy and Finance, and Mr. Gilsomar Maia, Corporate Finance Officer.

We would like to inform you that all participants will be in listen-only mode during the Company's presentation. After TOTVS's remarks, there will be a question and answer session for investors and analysts, when further instructions will be given. Should any participant need assistance during this call, please press *0 to reach the operator.

Today's live webcast may be accessed through TOTVS's website at www.totvs.com/ir.

Before proceeding, we would like to mention that during this conference call, forward-looking statements may be made relating to TOTVS's business prospects, operational and financial estimates and goals, based on the beliefs and assumptions of TOTVS's management and on information currently available. Forward-looking statements do not guarantee performance. They involve risks, uncertainties, and assumptions because they relate to future events and therefore depend on circumstances that may or may not occur.

Investors should understand that general economic conditions, industry conditions, and other operational factors could also affect TOTVS's future results and could cause these results to differ materially from those expressed in such forward-looking statements.

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

Alexandre Dinkelmann:

Good morning, everyone. Welcome to TOTVS's 2Q13 results conference call. Firstly, I will start talking about the acquisition of RMS, announced last July, presented on slide two. RMS develops enterprise management software for retail and supermarket industries and was appointed two times in a row as the first software company in the "Top of Mind" ranking published by the Supermercado Moderno Magazine, a standard publication in the Brazilian industry.

This is another acquisition that addresses our specialization strategy, strengthening our position, in this case in the retail segment, especially for supermarkets. We see a very interesting potential in this segment, especially in the integration of the value chain comprising Manufacturers, Distributors, Wholesalers, Cash & Carry, and now supermarkets. Today, TOTVS has a dominant and unique positioning in all these stages of the value chain, and we want to explore this huge potential.

Besides this M&A transaction involving RMS, we also had two acquisitions made by TOTVS Ventures since the 1Q13 earnings release. First, an investment of US$16 million in GoodData, a company based in San Francisco, California, focused on providing solutions for business analytics in the cloud, with Big Data technology offered in the SaaS model.

It is important to highlight that, in addition to the investment made, TOTVS now has a seat on the Company's Board and the distribution exclusivity of GoodData solutions in Latin America, bringing this new technology to the region and TOTVS clients. This operation reinforces TOTVS Ventures' capacity of adding value through synergies in every transaction made, since TOTVS Ventures goes beyond the role of being just a financial investor. In addition, it also confirms on a global basis the value of our presence and distribution capacity.

Second, Zeropaper, a company focused on providing cloud solutions for individual entrepreneurs. We do believe in this kind of solution that addresses the base of the pyramid of the Brazilian market, where the market is still fragmented and with a very attractive growth potential.

Before presenting our financial performance, I would like to reiterate that we remain focused on executing our strategy of enhancing the specialization by industry and by company size, organically and via M&A, with additional surgical investments made by TOTVS Ventures in initiatives related to the TOTVS's core business strategy.

Going now to the financial performance on slide three, we highlight the total net revenue growth of almost 16% year on year, higher than the last 12 months growth and the last five years CAGR. I highlight here that this faster growth came from all revenue lines. We continue to expect an adverse year for the Brazilian economy, which may affect the potential of doing business as a whole. This leads us to predict the year with a good degree of caution.

However, we also reaffirm that we will continue to seek, through a broad portfolio and strong presence in the region, the maximization of opportunities in regions and industries that show higher business potential.

On slide four we will drill down a little more, relative to the license revenue growth, which exceeded 12% year on year. This growth in license revenue came from the combination of the 18% growth in number of sales with the average ticket decrease of 5%. The larger number of sales was mainly driven by sales to existing clients, which grew almost 23%.

The downturn of average ticket was more concentrated in sales to new customers, which was almost 11% lower. However, on the other hand, in the last 12 months there was an increase in the average ticket to new customers of more than 23% and a 7% decrease in the average ticket to existing clients.

I reiterate that short-term fluctuations in average ticket are common, because it represents the average size of projects sold in the specific period. In our view, the last 12 months show more clearly the market dynamics.

Moving to Service Revenues on slide five, this line of revenue had the highest growth of the quarter, with a 19.5% growth. In the last 12 months, the growth reached 13.6%, exceeding the last 5-year CAGR. This line's performance was mainly due to the partial productivity recovery of implementation services, besides the higher number of working days in the quarter.

Going to the maintenance fee revenue on slide six, we see that, for another quarter, this revenue line overcame 15% of growth year on year and 13% in the last 12 months. This performance reflects our focus on customer loyalty, which is reflected in the consistency and in the recurrence of this revenue line.

By the way, talking about recurrence and consistency, on slide seven we present the total recurring revenue, which grew 12.6% year on year, accounting for more than 56% of total revenues in the 2Q.

It is worth mentioning that the changes of this line, as a percentage of total revenues, is due, among other factors, to the growth pace of other lines of non-recurring revenues, which in the 2Q had a faster growth, especially in licenses and implementation services, changing the revenue mix in the quarter. For this reason we focus on the growth rate of recurring revenue, period by period.

Recurrence is part of TOTVS's business model and strategy. In the short term, recurring revenues can reduce the average growth rate of total revenues, given the flow of monthly recurring payments. But on the other hand, it brings more predictability and sustainable growth in the longer term.

Now, I invite Maia to proceed from slide eight.

Gilsomar Maia:

Thanks, Alexandre. Good morning, everyone. Now, talking about the costs and expenses on slide eight. The group of license cost, service cost, and R&D grew 2.9 p.p. as a percentage of net revenue in the year-on-year comparison. Approximately half of this increase is due to higher investment in R&D. We understand that even in most adverse scenarios like this, we must maintain our investments in innovation in order to enhance our competitiveness in the future, making our growth sustainable in the long term. The other half is due to lower margin of services, reflecting the lower level of efficiency of service team in 2013.

In the quarter-on-quarter comparison, this group of costs and expenses fell 0.4 p.p. This decrease is partly due to the better margin of the 2Q, but still below the levels seen in 2012, and the lower relevance of third-party solutions reflected in the cost of license fees.

Moving forward to the second group, which concentrates advertising, sales, and commissions expenses and allowance for doubtful accounts, the increase from 19.4% to 21.1% between the 1Q13 and 2Q13 was mainly due to the seasonality of the marketing campaign, which is intensified in the 2Q, and due to the allowance for doubtful accounts, which returned to the level of 2012.

It is important mentioning that in the 1Q13 the decrease was mainly due to the overdue credit recovery that was accrued in previous quarters. In this line of allowance for doubtful accounts, we still notice a concentration on few clients facing financial difficulties.

On the third and last group, representing G&A and management fees, the reduction, both in the year-on-year and quarter-on-quarter comparison, is mainly due to the efficiency gains in this structure and the search for productivity. We emphasize here that we keep seeking efficiency gains in this group of expenses.

Moving to slide nine, the EBITDA increased 6.7% year on year, amounting R$98.9 million in the 2Q13, with EBITDA margin of 25%. In short, this reduction of 2.1 p.p. on the margin, when compared to the 2Q12, was mainly due to the maintenance of investments in R&D and advertising, and the decrease of sales and profitability in the period. We reiterate our commitment to preserve investments in R&D and to keep improving the efficiency of the servicing teams given the marketing potential.

We also reiterate that over the years, the EBITDA margin may fluctuate, that the combination of TOTVS's business model and its target markets leads to margin expansion in the long term. This fact is highlighted in the last 12 months EBITDA presented in this slide.

On slide ten, we highlight the net income growth, in line with the net revenue growth, in both quarterly and last 12 months comparison. In the 2Q13, the net income reached R$54 million, 14.3% higher than the EBITDA, mainly due to the lower level of both financial expenses and the effective tax rate.

Moving to slide 11, the net cash position changed from R$84.5 million in the 1Q13 to R$18 million in the 2Q13. The main reason for this reduction are the dividend payment, the GoodData investments reflected in intangibles, and the generation of operating cash flow of R$86.3 million, corresponding to 87% of EBITDA in the quarter. Here, it is also worth noting that the increase in gross debt is mainly due to the obligations from acquisitions.

Now the conference returns to Alexandre, to proceed to slide 12.

Alexandre Dinkelmann:

Thanks, Maia. On slide 12, we would like to close the presentation by referring to the three strategic pillars of growth, loyalty, and margin that guide the management's agenda, aiming to value creation for the Company in the long run. Regarding growth, we highlight the 16% growth of net revenue in this quarter, besides executing the specialization strategy, combining organic investments with the most recent acquisition of RMS.

At loyalty, we emphasize the growth of 15% maintenance revenue and the recurring revenue growth of almost 13%, both in the quarter. And for the margin pillar, we highlight the EBITDA margin of 26.1% in the last 12 months, in order to see the trend in margins for the Company in recent quarters, minimizing the natural margin volatility on a quarterly basis.

Regarding the margin, we continue to seek efficiency and cost-discipline, with emphasis in the service and administrative areas, as well as maintaining our investments in innovation, reflected in the R&D line, which are key elements for TOTVS to capture sustainable and long-term growth in our market. We understand that in times of crises or in more adverse scenarios, we must invest in our business with the proper discipline to capture all market opportunities.

The management reiterates its view on the relevant potential of the Brazilian market of management systems, especially amongst small- and medium-size enterprises, and keeps deepening the specialization strategy with the goal of increasing the Company's ability to capture market opportunities, even in adverse economic scenarios, such as the one in the beginning of the year. Thus, increasingly we are becoming stronger, both internally and externally, for the next cycle of growth in our markets.

From now on, we are available for the Q&A session.

Daniel Federle, Credit Suisse:

Good morning, everyone. My first question relates to acquisitions. I wish to know whether you could inform the contribution of PRX in 2Q and whether PC Sistemas, given that it was consolidated at the end of January, had a greater share in 2Q than in 1Q.

And my second question is related to R&D: do you see this slightly higher investment in R&D as something that will bring above normal growth in the future or is it only intended to sustain the current growth levels? Thank you.

Alexandre Dinkelmann:

Good morning, Daniel. Thank you for your questions. Starting with the second question on R&D, we don't see the figures this quarter as something outside the curve. This is a trend; we believe this is the best investment we can make to create value for TOTVS' shareholders as it is directly related to revenues in the medium term. So, when we talk about margin volatility, it is obviously affected by decisions on investments in the medium term.

About acquisitions, both PRX and PC follow the historical standard of disclosing consolidated figures. This has been our standard historically. In our history, the only three acquisitions where we made pro-forma adjustments were Datasul, RM and Logocenter – at the time, each represented 40% of the Company, so it was quite relevant. Later acquisitions are at a level we consider insignificant to give a breakdown.

PC did not change its share compared to 1Q. Basically, PC brings a lot of recurring revenue. Its revenue model is primarily based on maintenance, whereas PRX is 100% services. So, it brings neither maintenance nor licenses to our figures.

Daniel Federle:

OK. Thank you.

Suzana Salaru, Itaú:

Good morning. Could you describe the improvement in productivity in services? If that is already concluded, can we expect some margin gain from it?

And my second question is: which segments do you think are doing well that you are trying to direct sales in order to decrease their connection to the "pitch". Thank you.

Alexandre Dinkelmann:

Good morning, Suzana. In terms of service productivity, we informed you all that 1Q broke a historical series of gradual improvement in service profitability, and we had a localized problem in our operation with regard to software implementation services.

In 2Q, we improved performance once again, although still not sufficient to close the gap we had in 1Q, but we believe the trend is to improve.

As we always say about the services area, it is a vast area and is important for our future profitability, but the gains will be recognized in a cycle of two to three years. The hitch is it is a big area, and we are doing it in a disciplined manner, without creating expectations of achieving extremely short-term benefits.

So, it is in line. We are back on track and confident that, by the year-end, we will be able to close the gap we opened in 1Q.

In relation to segments, all segments in which we operate – we are basically talking about 10 verticals - are very important. That is why we are in them. But they have their own nuances and I will try to add some color on that.

When we talk about segments that, on average, generate greater potential to sell new licenses, we generally believe these sectors are more closely related to what we call non-tradable sectors. These are sectors more related to services.

I could give a few examples: education, retail, logistics, services, construction. These are segments in which we have betted heavily and which have performed very well for us. Quite well. I would go so far as to say even positively differing from the figures you see here.

On the other hand, when we look at other sectors, they are equally important, but on a different tone. For example, the manufacturing industry: it has the capacity to generate new licenses, especially in some specific niches within manufacturing, but what is most important to us in this industry is the question of recurrence it brings, and the unique capacity we have here in Brazil to connect value chains involving manufacturing, logistics, distribution and retail.

The more we strengthen our position in all these stages of the value chain, the greater is our competitive advantage. So, manufacturing is very important to us. We have seen this potential of manufacturing migrating to logistics, to retail and we are working to capture this.

So in terms of segments, it is in segments linked to non-tradable sectors that we want to grow organically, mainly, complemented by a few acquisitions.

Suzana Salaru:

Thank you.

Diego Aragão, Morgan Stanley:

Good morning, everyone. I have a question about revenue and another about M&A. About revenue: could you give us an idea of how a calendar with more business days impacted year-on-year growth in 2Q?

Alexandre Dinkelmann:

Good morning, Diego. This is a variable that affects the operational side of a company such as ours. To give you an idea, even the recent demonstrations in all major Brazilian cities affect business flow and the agenda of the software implementation services team; even the decision-making process at companies gets delayed. All this has an impact.

I wouldn't say that it is the main point, but certainly when we compare 1Q and 2Q this is a factor that explains the difference. It is not the only or most important factor, but it should certainly be considered.

Diego Aragão:

And my second question, TOTVS became somewhat more active this year in terms of M&A, although that is a part of the Company's DNA. I wish to know if there is a maximum number of acquisitions you can absorb in a year, in other words, is there a fixed number of companies that you have as target and is there any restriction, considering the whole of process of integration and capture of synergies.

Alexandre Dinkelmann:

You are absolutely right when you say M&A is part of our DNA. Historically, we have been very successful in combining organic growth with M&A, so that is a part of our ability. I would even say that perhaps TOTVS is the company best positioned to capture synergies from M&A in Brazil and Latin America, given our distribution network, our technology platform, the platforms we dominate, and the broad portfolio of products. All this generates important synergies.

We operate under the concept of a shared services center, which is the most efficient in Brazil. This is also highly relevant.

When we look at the pipeline, we are highly disciplined, especially during the initial stage of giving priority to deals that have a strategic fit. And then, obviously, during due diligence of a negotiation, we test the financial fit.

But what originates the entire operation is always the strategic fit. This is we see a share increase in some specific niche that is interesting in the long term, or an addition of some component to our technology portfolio. This is what guides us.

In this respect, when we see that TOTVS is already organized by segments, where we are increasingly organized in each vertical, the process of integrating companies is very natural. It fits exactly within that vertical we are operating in. This makes business absorption much easier today.

The second point that makes absorption a lot easier has an important premise for us and is much appreciated during the negotiation process and when the deal is structured, which is maintaining the leadership of all acquisitions. Leaders, of course, who we respect and want close to us.

In so far as we can maintain the leaders, the absorption process becomes much easier. We maintain companies as expertise hubs and for us it is interesting to maintain the regional focus, their regional base. This is quite useful even from the viewpoint of access to manpower and talent and local leaders.

This combination of fitting into TOTVS' segmentation model - preserving this regional spirit of the local expertise, the hub of talents and maintaining of leaders - all this makes it so much easier for us to manage acquisitions.

Diego Aragão:

Perfect, Alexandre. Thank you and good day.

Luiz Fernando Azevedo, Bradesco:

The first question is related to acceleration of sales, especially of licenses now in 2Q. What is your take on that? Has there been a better conversion of the pipeline? Has the pipeline improved? How do you see it in the second half of the year?

Alexandre Dinkelmann:

Good morning, Luiz. Even with a weak 1Q, what we have always said was: there is a pipeline. This gives us confidence that there exists a minimum level of activity. However, in certain cases, the cycle in fact canceled itself out. This premise of a longer cycle to close sales deals and negotiate is still valid, especially for new projects and new clients.

The decision ends up a little more thought out and an environment which, we believe, has a greater effect on this type of decision. That is why this quarter, we saw a much stronger base, because the base already knows its needs and the process of conversion into sales is much faster.

However, without giving any guidance for the second half whatsoever, our message is still the same as the one given during the 1Q conference call: caution. From a macro viewpoint, confidence indicators, whether of consumers, business or executives, have not seen a major turnaround.

We look to the end of the year with the necessary caution and our feet firmly on the ground. What we are pleased about our performance in 2Q, in light of this complex environment, is that we showed TOTVS is capable - thanks to its continental presence, we are in all corners of the region with a very local presence and operations in a wide range of segments of the economy, in terms of client size – of find deals wherever they are even in an adverse environment.

This is one of our strengths and it is extremely valuable for us in the long term, because the “guy” who is the owner may have a different dynamic - contractions or expansions – but we have been addressing that very well. In 2Q, I think this was the tone, but it doesn’t change our caution for the rest of the year.

The struggle continues in converting this pipeline we have into sales for TOTVS.

Luiz Fernando Azevedo:

Thank you. My second question is about acquisitions. What do you feel? Is the environment competitive? Has the economic scenario brought more feasible value perceptions for takeover targets? What do you think? Because the level of conversion of acquisitions really improved.

Alexandre Dinkelmann:

It is a competitive market. I think there is no acquisition today in which we are alone, none whatsoever; there is always someone together, at least someone. We don’t see a reversal in this scenario because, just as TOTVS believes in the potential, other players also believe in the more structural potential of the Brazilian and Latin American markets. We and other players still believe this market has much potential.

Of course, we, and probably other players as well, take decisions looking at the long term. We don't see a slowdown in competition or any significant change in this scenario.

Of course, TOTVS' style of making acquisitions is to work very closely with the entrepreneur who is there. It is to show that we actually don't want anyone to retire. We want to bring people to a bigger project, a bigger dream. This has always been our philosophy, the way we treat acquisitions and I think this is one of the pillars of our success.

In a more troubled scenario, I think there is a subjective side that entrepreneurs perceive, which is it is better to join forces with a strong group such as TOTVS, which, in the long run, increases their chances to capture value. That is why we like the earn-out model, because we remain their partners in the future.

Luiz Fernando Azevedo:

Great. Thank you.

Suzana Salaru, Itaú:

Thank you for taking another question from us. Could you comment on the competition? We saw SAP, which has a strong presence in SME, posting license revenue growth of 107% year-over-year. I wish to know whether you feel that competition has somewhat deteriorated the environment. How do you see it? Thank you.

Alexandre Dinkelmann:

In terms of competition, the reality of 1Q and 2Q is fully in line with what we saw in 2012. We did not see any deterioration in margin. The market is already competitive, so it is not a walk in the park for anyone.

We divide the competitive environment in three major groups: when we look at the high-end market, made up of large Brazilian companies, we compete directly with SAP, an obviously strong company that has been historically linked to this high-end market worldwide. It arrived in Brazil basically following the multinationals that came here. So, its DNA is in operating in the high-end market.

Today, it is a market in Brazil and the world - and those who follow the software market around the world know this - that does not hold very significant prospects for license growth. This is the case all around the world. In fact, companies around the world, the large software multinationals, also suffer competitive pressure in the United States, exactly from the new cloud models. This is the debate out there. This is a market that has more to do with loyalty than strong top growth.

When we look at the large portion of the market, which consists of small and medium companies – i.e. companies with 10 to 500 employees, including all sorts of companies of diverse requirements - the competition continues to be about specialization.

Smaller, regional companies, some very sound and strong, and which compete fiercely in this market. TOTVS' weapon for this is to specialize even further and invest organically, and some of these companies could be a natural target for TOTVS, as was the case of RMS and PC Sistemas.

And, despite announcements by SAP, we don't see anything in this market. In fact, it did not enter this market. It announced that it could be investing in channels but we don't see SAP in this market for small and medium companies.

And when we look at the base of the pyramid - micro-companies – it is still a large and highly fragmented market, where each player is pursuing a niche or even a unique positioning. So, you have multinational companies entering more in the accounting segment, you have a few interesting startups, and then we also are in this market. It is a market that still has much room for consolidation.

And about SAP's growth percentage, announced in newspapers, of 107% year-over-year, our understanding, our reading of the market - and we follow this closely as is our duty – it been making intense efforts to push the HANA solution worldwide, which is a solution more closely related to infrastructure and databases, where the competitive map is basically different. We have nothing to do with that.

We could even be partners of SAP if we wish to sell HANA. This is a competitive issue for IBM, for Microsoft and for Oracle. And it has indeed been a driver for SAP, which has been announcing to the capital markets that its growth driver is HANA. I think this has somehow been a success here, and perhaps is the company's flagship product in the market, from what gather.

Suzana Salaru:

Perfect, Alexandre. Thank you for your answer.

Bruno Mendonça, Santander:

Good morning. I'd like you to talk a little about this dynamic of new clients, which is still negative. My question is: are these smaller clients or are these smaller projects for clients of more or less the same size and profile as of last year? That is one question.

The second is about selling costs. My question here is: is it more expensive to acquire clients, or will these costs, growing more than licenses, are structural investments that will be diluted in the future? What should we expect from this selling cost dynamic? Thank you.

Alexandre Dinkelmann:

Thank you, Bruno, for both questions. Good morning. Starting with the first question about new clients, we are obviously talking about smaller projects, not necessarily about the clients being smaller.

It has to do with that point I mentioned earlier: it is indeed somewhat related to the general aversion to risk at this moment in the economy. And our strategy, of course, is to work under a concept of smaller projects at times and then after they become existing clients, the selling cost is much lower.

So, even if the project, on average, is smaller, we must go after it. And when we look at the future, more so because of this intensive specialization effort we have been doing, this is a variable that will obviously bring us much return in the long run. As for the relevance of new clients in the long term, we always work towards to make them more relevant.

Regarding selling costs, I think you touched on something that is exactly what guides our investments. The increase in selling costs is related to projects we consider structural, which will convert into lower selling costs moving forward. We have indeed made some investments here in what we call "sales intelligence", in order to scale up our proprietary distribution model even further.

Initially, we will be impacted by this increased cost. It is a conscientious investment that we are making in this intelligence to have a scaled model that is increasingly high-impact with a broader presence and reach. And then, in the future, this converts into lower selling costs. This is the thesis of our investment and it is a highly strategic investment.

Bruno Amorim:

Great. Thank you.

Operator:

There being no further questions, I now turn the floor back to Mr. Alexandre for his final remarks.

Alexandre Dinkelmann:

I wish to thank you all for listening in and for your time. Basically, I wish to thank the TOTVS team. The TOTVS team is gathered here. In 2Q we showed that even in an adverse environment we are capable of finding business wherever they are.

I want to underline one message that is very important: The Management and Board of Directors of TOTVS are here to think of the medium and long term. Our decisions are to increasingly add more value, capturing growth cycles in our market in the long term.

So, for us, key decisions such as maintaining and strengthening our capacity to invest in R&D, for instance, reflect exactly this. We will not focus on the concept of margin and percentage in the short run, knowing that it could affect the long term. For us, it is more important to make investments in both brand building, and now increasingly more segmented, as well as in R&D, which reflects in the medium-term revenue – and this revenue does not show here – than eventually worrying about short-term margin.

And when we look at the bottom line, we are delivering in the quarter, EBITDA of nearly R$100 million and net income of over R$54 million. So, despite the long-term decisions, all reflected in expenses, we did not capitalize any R&D within the Company and still managed to deliver a solid bottom line.

Thank you and we remain at your disposal to clarify any doubts you may have in the near future. Warm regards.

Operator:

The TOTVS conference call is now over. Thank you for participating. Have a nice day.