

Operator:

Good afternoon. Welcome everyone to TOTVS' 2Q10 results conference call. Today with us we have Mr. José Rogério Luiz, EVP, CFO and IRO, and Mr. Gilsomar Maia, Planning Officer.

We would like to inform you that all participants will be in a listen-only mode during the Company's presentation. After TOTVS' 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' 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 business prospects, operational and financial estimates and goals, based on the beliefs and assumptions of TOTVS 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 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. José Rogério Luiz, who will begin the presentation. Mr. José Rogério Luiz, you may begin your conference.

José Rogério Luiz:

Good morning and good afternoon everyone. Welcome to TOTVS earnings release 2Q10 call. First of all I would like to remind you that due to our corporate governance and respect for the market, the figures

of today's presentation take into consideration only TOTVS organic growth, since we added 2005 data of all the main acquired companies from TOTVS, allowing you a better and clearer vision of our performance, that is, acquisition pro-forma figures.

The 2Q10 was once again a period of growth, TOTVS reached records in several lines of its P&L statement, obtained outstanding acceleration in the number of new clients as well as in licenses revenues, and the Company reached the 18th consecutive quarter of double digit growth in revenues. At the same time, the Company kept the volume of investments in our longevity.

So, now I would like to invite you to go to slide on page two. We have mentioned a number of times that TOTVS is not a short-term player, therefore our actions are structured to bring the best possible result to the Company in order to get the opportunities of this low penetrated market.

In the past 12 months, TOTVS worked in several areas of its core business in order to strengthen its growth and improve scale. In the technology sector, sales is not only achieved because of the quality of the product but also because of the brand recognition. Therefore, since the 2Q09 a new investment period in TOTVS brand started. The objective was very clear: to improve volume in licenses sales, since it is the one that drives forward other revenues and services.

Keeping the same objective, strengthening and consolidating distribution channels, is extremely important to enable an intensive market attack ability, as we have a very low penetrated management software market in Latin America.

Based in this idea, gain in scale is fundamental. In the business model, more sales means fixed costs dilution. So, the improvement in internal processes and the pursuit of a unified technological base are essential to a consistent and growing margin development. The investments in R&D also enable the product improvement, and therefore presenting future sales positive effects.

Let us see some results of the mentioned actions. Please proceed to slide on page three. In terms of market share and taking into consideration all sizes of companies, I mean micro, small, medium and large companies, according to IDC in data published to the market in the 2Q10, TOTVS ended 2009 as

the leader in the Brazilian market, with market share of 42.7%, as you can see it highlighted at the left-hand side of this slide.

To your right-hand side we see Gartner figures for the same period, which shows 49.1% of participation. According to Gartner, TOTVS is the leader in the whole Latin American market. TOTVS presents wide and growing leadership in relation to the three main global management software players.

On slide number four, we present updated small and medium companies market-share data, and TOTVS, according to IDC, has enlarged its participation to 65.6%, a large market share in an underpenetrated market.

Still concerning brand perception, during the 2Q10 the Company has received several awards, so proceeding to slide on page five we would like to highlight the following: Bloomberg Businessweek publication has elected the TOP 100 Tech Global Company, and TOTVS has been ranked the number 56th, being the highest ranked in relation to the five Brazilian companies in the list.

The British World Finance Magazine, taking into consideration all continents, has elected TOTVS as one of the 50th companies which can most influence the market in the Future. TOTVS has also been considered the 22nd most valuable brand in Brazil, according to Istoé Dinheiro Magazine and BrandAnalytics.

TOTVS has also been awarded a distinct award of value creation in IT industry by ABRASCA, the Brazilian association of public companies. And, in a research performed by Agência Estado, TOTVS ranked number 1 in return to shareholders in 2009 in all companies in the Novo Mercado and 2nd among all public ones. The mentioned awards have been influenced by the consistent results of the Company, which, again, occurred in 2Q10.

Proceeding to slide number six, we can see some important highlights of these results.

The 18th consecutive quarter presenting double-digit organic growth, something reached by very few companies, in the 2Q10 the quality of the growth shall also be highlighted.

Historical records in total revenue and in other lines, pointing out the strong growth in software licenses revenue, 18.9% over 2Q09; significant growth in the number of new clients, 31% higher than 2009; and net profit approximately 30% higher than 2009; EBITDA was R\$62.8 million.

In this quarter we also had the TOTVS Day, the first results from partnership with American Universities of Stanford and San Jose as well as some M&A transactions in order to improve areas of future growth of the Company.

This growth can be easily noticed on page seven, to your left-hand side you can see the organic income growth line in the past six years, to your right-hand side, the base of the rolling 12 months, new software clients growth. That is, in the 12 months ended in the 2Q09, TOTVS was well-succeeded in adding 2,332 clients to its base. In the past 12 months ended in the 2Q10, this figure reached almost 3,000 clients, an increase of 25%.

Slide number eight presents another way to see this growth. To your left-hand side, the strong growth in the number of new software clients, 31% over the 2Q09, as well as the volume of more than 3,500 base clients served in the 2Q10, this increase stimulated growth of almost 19% in license sales, as demonstrated to the right, presenting a new historical record in this item, resulting in revenue over R\$70 million in terms of new licenses.

License sales are fundamental for future service and maintenance revenues. Proceeding to slide number nine, still without reflecting the accelerating effect of license revenues, we see record revenues in service to the left-hand side and maintenance to the right-hand side.

Slide number 10 presents a dynamic comprehension of the revenue lines. The marketing campaigns combined with the channel consolidation were important to accelerate revenue from new licenses, which in comparison to the same quarter in the previous years were over 5.4% in the 4Q09, 8.8% in the 1Q10 and almost 19% in the 2Q10, a clear acceleration in the process. This acceleration effect does not occur right away in service revenue, which presented an increase of only 12.1%, negatively affected by

less number of working days in the quarter, especially because of the interruptions on the days Brazil played in the World Cup.

Maintenance revenue grew 12.3% in the 2Q10, being affected by the lower number in license sales in previous quarters and also by the low IGP-M index in the first months of 2010. Recent data presents an increase in license sales as well as IGP-M index which may result in a positive effect in maintenance for the following quarters.

On page 11, the slide of revenue structure presents once again a picture of a very balanced revenue and business model with a very good visibility of the future flow of revenues, given the amount of recurring revenues of TOTVS. License revenue reached 23.6% of the total, service with 30.4% and maintenance more than 46%, despite the low IGP-M index in the last 12 months.

In order to follow up with costs and expenses, I would like to invite you to proceed to page 12. At the lower left corner, we can see that TOTVS remained keeping a strong control in term of G&A expenses; in the lower right-hand side corner, we see that marketing investments are in the same level when compared to 2009, however the increase in cost of services and the investments in R&D resulted in a faster growth in the total costs and expenses when compared to revenue increase, resulting in pressure on the Company's margin.

The effect over the margin gets clearer on slide 13. At your left-hand side, there is a comparison between the 1H10 and the 1H09, in which we notice TOTVS gained 3% margin in G&A plus marketing expenses, but lost 4.8% due to increase in both cost of services and R&D, resulting in 2% of margin loss when comparing both periods.

TOTVS management is working in order to reduce costs. For example, in the cost of services item, the productivity is still below the previous levels recorded before the process of distribution channels consolidation. It is important to mention that among several actions to attack this, we have the improvement in process and internal systems in order to increase implementation efficiency, reducing working hours in each project to allocate professionals in new clients. The goal is to have the implementation faster, with better quality.

Concerning R&D, the conclusion of FDES incorporating process from Datasul, at this point in time in due-diligence final phase, will help us achieve reduction in expenses with no loss to effectiveness in TOTVS solutions development. The costs with R&D are also temporarily higher than the historical average due to the equalization actions in all software tech bases, especially in Datasul one in order to reduce third-party software dependency.

At your right-hand side in the same slide there is a chart with the 12-month moving average revenue and costs plus expenses. In a long-term perspective, the Company has been having a very clear trend: increase in profitability.

Proceeding to slide 14, we can see the traditional financial dashboard in which we highlight EBITDA over R\$62 million in the period, and also the historical record in net income.

We started today's presentation approaching the past 12 months. On the slide on page 15, we provide you with a brief summary of what has been achieved so far. Marketing campaign plus the consolidation channels enabled increase in license sales which shall influence positively other revenue lines of the Company.

Concerning margin growth, some actions have already reached positive results, such as the internal processes improvement with the consolidation of the shared-services area, but some other areas in TOTVS are still in process of being rearranged. The investments in R&D in order to unify tech platform and the Franchisee of Developments incorporation are also in progress, resulting in a perspective of margin contribution for the coming quarters.

Proceeding now to slide 16, we can see our fundamentals reinforcement, which once again enabled the Company to face a period of growth. Execution keeps being essential, so that we can keep our historical growth sequence.

Finally, on slide 17, our commitment is to keep this line of success. I appreciate your time with us and we are available to answer your questions. Thank you.

Marcelo Gonzales, Credit Suisse:

Hi. Thanks. My first question is about the development franchises, the acquisition, is the due-diligence process already over? Do you have a date when you believe it will be finished? And do you believe there could be any adjust to the price that you first released to the market? And also how much do you think this could reduce your R&D expenses in the future? Thanks.

José Rogério Luiz:

Marcelo, the first thing, we have just finished the due diligence, there is no significant price adjustment and we expect to have it ready, that is, contract signed etc. up to August 15th. And what we have and what we expect to have this in an annual base to impact our fingers are something about around R\$10 million in terms of our EBITDA.

Marcelo Gonzales:

OK. Thank you. And just on license, the average revenue per license actually declined for new licenses during the quarter year over year, do you think this is because you are having smaller projects? Well, if you could give more details about this decline in average revenue per revenue. Thanks.

José Rogério Luiz:

Although we have been having, sequentially having new records in terms of license sales, what we have been seeing is that the smaller clients have been buying software. We are having an additional volume now of mid and mid-high companies in the pipeline but the huge majority of our sales has been to smaller clients. This seems to be a market very active at this point in time, while we have been seen the larger clients returning in a more soft way. Although it is important to mention that in relation to the 1Q10, we have already some increase, it was a timid one but some increase in terms of the average size of our clients.

Marcelo Gonzales:

OK. Perfect. If I may, just one follow-up question, do you believe your margins with larger clients are better than margins with smaller and medium clients? Thanks.

José Rogério Luiz:

Look, what brings to us the highest margin, Marcelo? In fact it is the time that the client spends with us. What do I mean by the time? Because the longer is the time the client remains with us, they remain paying maintenance and as you may remember maintenance is what brings to us the highest margin.

One thing that is a fact is that the margins, when I see a project, the margins for smaller clients are higher and bigger than when you have the comparison with high-end clients, but when you have a sale to a high-end client, they bring to us in a short term a certain amount of licenses and these additional amount of licenses, as the cost of licenses is a kind of marginal cost, so it bring to us in the first moment a temporary better margin when we make the comparison with the smaller clients.

So, trying to summarize, it is good for us to have larger clients, they provide to us a short-term impact. But in the longer term, thinking in the long term to have smaller clients is better. Is it clear?

Marcelo Gonzales:

Yes, totally clear. Many thanks. Perfect.

Andre Rezende, Goldman Sachs:

Yes, hi. Thanks for taking my question, actually I have two. The first one regarding the average ticket per client, do you expect to continue to recover in the 2H of the year due to a better client mix? The second one, would you be able to maybe point where the weakness in the channels is coming from? I am just trying to get a sense if it is coming from the franchises or the proprietary channels or both, and also which operational and technical actions are being taken to try to address those issues? Thank you.

José Rogério Luiz:

OK. The first thing, again, the average ticket of the client for us is more than a financial aspect, it brings to us the idea about the size of the clients that we have been having, or that they are active in a certain period. So, what do I mean by that? That we do not see the average ticket going down as a bad thing, and why? If I am having this going down but at the same time if I am increasing the number of new clients, so the combined equation seems to be good for us, because in the longer term is going to bring to us more margin.

But, trying to address your point directly, Andre, as we have been having some more mid and mid-high clients in the pipeline, it is natural to think that this growth in average ticket is going to occur in the next quarters. So the answer to you is are taking in consideration that in our pipeline the number of mid and mid-high clients is increasing so it makes sense to think that this average ticket is going to grow in the future.

Then, you asked me about the channels, what is weakening the channels. Let us think what happened, in the middle of the last year, we started to merger the Datasul franchises into the TOTVS franchises, not only in our own areas, but also in the third-party areas. Well, we created somehow a kind of mess doing this, because in the third-party franchises they had to talk to each other, to enter in accordance and in an agreement in order to go forward in this transaction of merger in certain areas.

What happened is that we saw a kind of slowdown in sales coming from the franchises in the last quarter of last year and in the beginning of this year. And it has been a step-by-step process, so nowadays they are more OK in terms of being together, their structure is working better. So the first phase is to cause an impact in selling more licenses, so you can see in our revenues that the amount coming from new licenses is growing.

And if you go to our commission expenses, you are going to see that the commission expense is growing a little bit and this is because the stake of the sales coming from the franchises is increasing in relation to what we had like six to seven months ago. Well, if they are selling more now, they are entering in another phase that is being better structured in terms of providing services of implementation.

So, we still have to support some of them and it adds to our expenses while implementing some of the products they had in their pipeline months ago. What do we expect? That as it is a process and it is getting better and this is going to allow us to be even more focused in our own areas.

At the same time, we know that the fast growth that we had in recent years provoked some disruptions in terms of our internal processes and even in some aspects of quality during our implementation process. So even within our own team here we had some cases of rework and we had some cases of loss of efficiency.

What have we been doing? We are going through our own structure in order to enhance the efficiency of our implementation team in order to reduce the pressure in terms of costs of our service area. So, when you asked me about what was wrong, in fact it is a process and we are working in order to fix this.

Andre Rezende:

Alright. Thank you very much.

Tatiana Feldman, Morgan Stanley:

Hi, Rogério, good afternoon. A couple of questions actually, one, I just want to understand what happened with the management fees in the quarter, because last quarter you guys reduced as a percentage of sales given the sort of the let us say less than satisfactory results and I was under the impression we should have seen something similar this quarter and sort like saw that back up, I just wanted to understand the rationale behind that. And then I have another small question.

José Rogério Luiz:

In some areas of the Company, as you could see that we had some acceleration in our license sales, some of the areas are already reaching their goals so we have to go in an accounting aspect to save some money to pay for these guys if we reach the global targets and the global goals of the Company.

Tatiana Feldman:

OK. So potentially, depending on how the rest of the year goes this could increase or decrease in the next couple of quarters.

José Rogério Luiz:

Yes, totally correct.

Tatiana Feldman:

OK. Perfect. And then the other question I had was about working capital, I tend not to look at this so much but it has stayed a little bit high and we continue to see an increase, specifically account receivables, you know, the numbers and so have not come down or anything and it is increasing sequentially, so I am sort of wondering what is going on there.

José Rogério Luiz:

Look, it was increasing so we managed this in a better way in the end of the 1Q, but we had some sales in the 2Q that required from us to provide some additional tenor, this occurred not only in Brazil, but also in Mexico. Mexico is facing, in fact and Argentina, the economy is getting a little bit better in Mexico in the volume of sales is increasing there, but we in order to follow some of the market moves we had to provide some additional tenor there.

Tatiana Feldman:

OK.

José Rogério Luiz:

Tatiana, just to end this specific point, we are already working not only in Mexico but also in Brazil in order to provide some additional instrument to our sales teams, if they need to provide some tenor, we are working some instruments that are going to be out of our benefit.

Tatiana Feldman:

OK. So we could potentially see an improvement towards the end of the year from what we are seeing.

José Rogério Luiz:

We are working on it.

Tatiana Feldman:

OK. Perfect. And just one final question if I may, I think the most positive thing to me in the quarter was sort of seeing license sales really coming back to a healthy double-digit number year on year, 20%, and even understanding the issues in maintenance and services, but assuming given what we have seen in licenses sales this quarter and the adjusts of inflations that we should expect in the 2H, is it fair to assume that we should see something a little bit more symmetrical or a little bit more in rhythm with the other segments in the 2H of the year if we continue to see license sales at this rate, is that fair?

José Rogério Luiz:

I think you have a correct reading.

Tatiana Feldman:

OK. Perfect. Thank you so much.

Operator:

There are no further questions at this time. We will now turn the floor back over to our host for any closing remarks.

José Rogério Luiz:

Thank you very much for your support, and again in the name of the senior management of TOTVS I should tell you that we think that we had some positive aspects in this quarter but we are not fully happy with the results that we have been achieving. We know that we have potential to increase not only our volume of sales but also to increase our margins and it is a compromise from the senior management to work in order to meet our own expectations that are higher than what we delivered in the last months.

So, thank you very much for your support, and my team and I are always very pleased to receive any questions and also your visit. So thank you very much.

Operator:

Thank you. The TOTVS's 2Q results conference call is now over. You may disconnect your lines at this time, and have a great day.

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