

**Operator:**

Good morning, welcome everyone to TOTVS' third quarter of 2006 results conference call. Today with us we have José Rogério Luiz (Vice-President and IRO), Cláudio Bessa (TOTVS' Group Marketing Officer) and Rodrigo de Q. Cabrera Nasser (IR Manager).

We would like to inform you that this event is recorded and 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.br/ir](http://www.totvs.com.br/ir).

Before proceeding, let me mention that forward-looking statements are based on the beliefs and assumptions of TOTVS management and on information currently available to the Company. They involve risks, uncertainties and assumptions because they relate to future events and therefore depend on circumstances that may or may not occur in the future. Investors should understand that general economic conditions, industry conditions and other operating factors could also affect the future results of TOTVS and could cause results to differ materially from those expressed in such forward looking statements.

Now, I will turn the conference over to Vice-President and IRO, Mr. José Rogério Luiz, who will begin the presentation. Mr. José, you may begin your conference.

**José Rogério Luiz:**

Good afternoon. I would like to thank all of you for participating in this 3Q06 conference call. It's a pleasure to bring forward the results of another period of growth and expansion of our activities. I would just like to remind you that, for comparative purposes, the figures we will show today include RM Sistemas and Logocenter Data in the group's results since January 2005, allowing us to better identify organic growth.

On page three, I would like to provide you with the highlights of this quarter, and we have, as I said, another period of growth in terms of revenues, and I would like to point out the growth in terms of gross service revenue, with almost 22% in the 3Q. And, with this, we have the gross and net revenues for the nine months ending in September reaching over 20% of growth in terms of revenues.

Another important thing that we have is the adjusted EBITDA, that grew 19.4% in comparison to the nine months of 2005. And, at this point in time, we are reaching almost R\$ 51 million in terms of EBITDA. So, in nine months, we are reaching the same level of EBITDA that we got in the whole year of 2006.

Therefore, during the next three months, October, November and December, we are going to work in terms of the growth of the company.

I would also like to say that the EBITDA in the 3Q, we had a growth of over 11% in relation to the 3Q05, reaching almost R\$ 16 million.

The EBITDA margin is around 18.4% in the last nine months and the adjusted net income reached a level of over 42% when we are comparing with the nine months of 2005. All of this growth was supported by the operational performance. And this operational performance was based not only in terms of new clients and again we reached over 300 clients at this point in time, 370 new software clients in the 3Q. And, in terms of 2006, we have reached, at this point in time, over 1,060 new software clients. Of them, just in the 3Q we have over 50% in terms of new clients in the corporate model.

One important operation that we have nowadays is, of course, Mexico, and we are going to see in the next slides the growth of Mexico, that is over 60%, bringing to us over R\$ 11 million in terms of revenues.

Another important thing that happened was that RM Sistemas was chosen as the best software company in Brazil by one of the most important IT magazines. And it is the 3<sup>rd</sup> year in a row that RM Sistemas is chosen as the best one.

So, moving now to page five, I would like to say something about the market and, during the last month, what we had was a research from Gartner that was published, and what we would like to point out is that TOTVS presented the biggest growth in terms of license sales in 2005. And we were, in terms of growth, the number one in the ten most important Latin American companies.

Also, in terms of Latin America, I would like to say that we are number three after SAP and Oracle, but in some specific segments we are already the number two, as Gartner pointed in terms of the manufacturing segment.

Also, IDC presented some new information and they published the market share data referring to the 1H06. In terms of Latin America, in 1H06 in relation to 1H05, we went up from 10% of market share to 12%. And, in terms of Brazil, especially in the small and medium business, we grew from 44.5% to 51.5% - so, in this segment we are the market leaders.

As you can see on page six, in the pie chart, we had the possibility to grow and, while growing, we could see the reduction of the share of all other competitors. And even the case of SAP, SAP in the whole market grew their market share, but this was basically in the high-end companies. So, this is something very important to us which brings lots of responsibility.

At the same time, one thing is having 51% of the share of this market, but we have to keep in mind that this is a very under-penetrated market, so we have a lot of opportunities.

In the slide of page eight, what we have here is an very clear picture about TOTVS. What do I mean by that? Quarter after quarter we presented growth. If we had here no pro forma, this growth would be even higher. Even in the pro forma data you see that, quarter after quarter, we have been working in terms of growth. And this growth has been based in one thing, that is, for instance, new license, because this new license will bring the seeds for the two other revenues: maintenance and service.

And we have been consistent in this growth. In order to build this growth, of course, we are always working in terms of managing our costs and expenses. You may remember that when we had the transaction whit RM we said "look, the first gain that you are going to have is going to be in G&A expenses". And then it is natural that we go to the other lines of expenses.

And we expect, and we are working hard in order to, not only have this growth, but also to have a better management in terms of our costs.

On page nine, I would like to call your attention in terms of, first thing, that we are keeping the path of growth of 20%, as we have in the figures for the nine months of the year. We had, in terms of adjusted net profit, and what I mean by adjusted net profit, I mean that is the profit without the IPO expenses, the one-shot once, and also the amortization of the goodwill generated by the acquisition of RM and Logocenter, that, in relation to 2005, we had a significant growth of over 40%.

In terms of EBITDA margin, we are keeping the same path in terms of the pro forma figures, but you should keep in mind that, at the end of 2005 we had an EBITDA of 15.7% in a non-pro forma data. Now, taking a picture of our company, 18.4% and, as we said to the market, our expectations are that in 3-5 years after the IPO, that we would go to a range of between 20%-25% of EBITDA margin. So, we are in the route to achieve this goal.

Slide ten now, I would like to say, in this chart, especially in the two last columns in the right side of this slide that, first, we've been able to grow, keeping the type of growth of around 25% in terms of new licenses, in terms of license fees and, as you may remember, this is the key for our growth, because license bring the seeds of the two other revenues, I mean, maintenance and implementation. Therefore, keeping this growth, in terms of this percentage of 25%, means that we are building up a future.

Another thing that is important to say here is that our ASP structure brought to us this year almost R\$ 4 million in terms of revenues and these are recurring revenues and they are based in contracts that they have around 36 months. So, this is the key, again, to build our future.

Going to page 11, talking about costs, investments and expenses; in the left side of the chart, you have research and development and this is to show that we are keeping our linearity in terms of investments in research and development. In terms of general and administrative expenses, of course, we are getting the synergy from having the three companies together. RM

Sistemas, Microsiga and Logocenter. Therefore, we have been able to get the synergies and reduce not only in terms of percentage, but in absolute figures.

On the other hand, on the right side, we have the total costs and expenses that now we are entering a new phase, in terms of controlling the other expenses and costs and this was already in our plan, because we have been working in terms of savings in order to get the synergies.

One thing that has happened, is that the advertising expenses grew in this year even in a faster speed than we had, in terms of net sales and in this case, I invited my colleague Claudio Bessa, the Marketing Director, with us today here in this call and he is going to say something about not only our structure and strategy of marketing, but also our strategy that we had in 2006.

In terms of operational performance, first thing that I would like to point out is, again, that we are growing in terms of new clients, that is, over 1,000 new software clients. In terms of corporate clients the growth reached almost 200 new clients in 2006.

On page 13, operational performance, this is to show that in every quadrant, what we have here is that our average ticket is growing in relation to 2005. So, we have been able to do better sales to our clients even in the corporate side, which is on the lower right part of the slide that reveals we are going down 17%, this is a positive message. And why? Because we have smaller companies buying our software, in terms of the corporate model and as this corporate model is linked to the revenue of these companies as they are going to grow, they are going to bring us more revenues.

So, on page 14, in order to close this segment of this presentation, we have the international market. We are clearly the largest Latin American software company and Mexico is the jewel of the crown in our strategy and, as you can see, not only in Mexican pesos, but also in reais, we have been growing not only in terms of gross revenues, over 66% in terms of reais but also in license fees and license fees they are key because of course, they are going to bring us future. License fees over 80% in terms of growth.

Well, I would like to invite you to go to page 16 now and I am going to ask my colleague, Claudio Bessa, that is the Director of Marketing, Partnership and New Businesses of the group, with a large experience not only in the IT business but also in the marketing business; he is responsible for our strategy in terms of marketing. I would like to invite him to say some things about our market strategy.

**Claudio Bessa:**

Good afternoon, I would like to explain a bit more about our marketing strategy and I invite you to the slide 17, that the idea is to provide you how we work in terms of our differentiations for TOTVS. So, as you see, our main differentiation is focus in terms of products, technology, distribution and commercial flexibility,

so, the whole strategy in terms of marketing is to provide and emphasize all those differentiations.

If we go to slide 18, I could explain to you a bit more in terms of how we work in terms of marketing. So, normally we work with four main topics. One is the marketing intelligence, the other one is the events, advertising and spontaneous media. So, the idea here with the marketing intelligence is to try to understand as much as we can the IT markets, the software markets and also the ERP market.

If we go to slide 19, I think I could explain in a better way what information we try to understand in terms of marketing, so, we are normally using two types of sources, not only IDC, for instance, but also Gartner and the idea here is try to provide a comparison in terms of how those researches understand the markets for the next year. So, as we could see, we tried to understand the worldwide IT, Brazilian IT market, Brazilian software market, Latin America ERP market and so on. And also, as Rogério mentioned in his presentation, we tried also to understand how it is going to be, I mean, in terms of goals, the other regions in Latin America like Argentina, Colombia, Mexico, Venezuela, Brazil, Chile and Peru.

If we go to the slide 20, we are also going to see some understanding in terms of new licenses by sector. So, here you can understand in which segment we have to be focused for each branch, so, you have a better understanding of what it is going to be in terms of retail, education, government, services, manufacture and so on.

If we go to the 21<sup>st</sup> slide, you are going to see a lot of opportunities that those sources try to present to us for the next year, so, the important thing here is the ERP, which is the base for all the probable demand generation for the next year. You can see here not only the ERP opportunity in mobility, in BPM and RFID, VoIP, Security and so on. So, with all information, the idea is to try to provide a better understanding in terms of emphasizing on how we are going to be in terms of strategy and CAPEX for each branch and for the business plan for the next year.

If we go to the 23<sup>rd</sup> slide, we are going to see that the idea here is to try to present to you how we work in terms of providing as much suspects and prospects for those branches. So, the whole strategy that we are working here are one too many strategies, so, that one too many strategies are very based in three points: public relations – that is the spontaneous media exposure, and the idea here is to focus very much in terms of credibility for the market and, especially, when we talk about the SMB market, this is something that has to be very important.

And also we work in advertising, and the idea here is to focus on brand fixation and better explain what mission each brand is going to present to the market; and also translate all those points that I mentioned in the events, and the idea here is to try to drag as much suspects and prospects as we could for each brand.

If we talk about the understanding of what happened this year, we actually could see, in the 1Q, that we are only focused in terms of spontaneous media. So the idea, in the 1Q, is to emphasize the whole presence that the IPO gave to us during that quarter. And after the 1Q, in the 2Q and 3Q, the idea is to maintain all the presence that we already had in the 1Q, having a very strong investment, in terms of marketing, to provide, as much as we could, a consolidation of all the brands that are working for TOTVS, and also provide the necessary volume of deals for each month.

Going to slide 24, you have some examples of the advertising that we are working during this quarter. The idea is to provide very strong information about how we operate in each brand. So, if you see, for example, Logocenter, the slogan we are working with is "Tailor-made management". So the idea here is to provide, in the best way, a construction of any type of solution that a customer may need.

If we go to Microsiga, we are going to see the slogan "Simplifying your life", and the idea here is to provide flexibility and simplicity for every kind of customer that desires that type of product in their own company. And if we go to RM, the slogan is "Everything in place", and the idea is to provide products in a very quick way, practical and accessible for the market.

If we go to slide 26, we are going to see some examples about how we work in the spontaneous media generation. As I mentioned, TOTVS is our anchor in terms of providing information that we could work with for all and each brand that are very targeted to the market – like, for example, Logocenter, Microsiga, and RM. And one of the examples that you can see on slide 26 is spontaneous media in TOTVS, that was focused not only in publications that much more cover in the middle or high markets, but also we have some publications that cover our target market, which is the SMB market, to provide a better maintenance of each brand that we already have, in slide 27, for Logocenter, Microsiga, and RM.

So, if we go to slide 28, we are going to see also an example of how we work in terms of advertising for each brand. So, for each brand we have a specific instrument, not only in terms of electronic media, but also a press media, to emphasize and to provide as much people as we can with an understanding of the focus of each brand we are working for.

In slide 29, you can see the whole transformation that we work, in terms of spontaneous media and advertising; we had to convert, in terms of prospects and suspects that we invite in all those events that are very different from one brand to another. For example, Logocenter: we are normally asking for a very famous speaker, who provides a much better level of executive for the company. So the idea here is to target the CEO's from the companies. As for Microsiga, the idea here is to work in a much wider way; so not only working in a business forum, but also covering some exhibitions and some seminars. As for RM, they are much more focused in vertical exhibitions, and also we have some seminars and congresses that we invite those companies to.

Slide number 30, you can see some examples of those events from Logocenter, TOTVS, Microsig and RM.

Thank you.

**José Rogério Luis:**

Thank you, Cláudio.

Well, in order to wrap up our conversation, and before your questions, I would like to say, first of all, thank you very much, and that we have three major dimensions here at TOTVS. The first one is the market – and we know that we have the market, the market is there, and it is an under penetrated market. The second dimension is the products' technology, and we do have the product technology. The third thing is our challenge, which is execution. So that is why we do know that we have a lot of work to do, a lot of market to gain, and we have, of course, a lot of things to work on, in terms of our costs and expenses, in order to leverage our growth.

Thank you very much.

**Mario Edelbaum, Artha Capital:**

Hello, Rogério and everybody. I have a couple of questions; the first one goes to the revenue in the 3Q. There appears to be a slowdown related to your growth rate, if you look at the 2Q and the 1Q. I just wanted you to comment if you think that the slowdown is permanent, or if you think it has some quarter issues, etc. – especially when you look at new licenses, right? Because new licenses, I think, grew 14%, or something like that.

**José Rogério Luis:**

OK. In terms of revenues, if we look at services, services are going up, and this is, somehow, a trend that we were facing some months ago. So that is why, in the 2Q, we kept counting, in terms of service, because we had the perception that this would increase.

In terms of maintenance, we have been able to, especially in the absolute figures, not only keep our base clients, but also include the new clients that we have been selling new licenses to. And in the case of licenses; the first thing, in terms of the number of new clients, we had in this quarter a very good number 370 new clients. Just to provide you an idea, this was 28.5% higher than we had in the same period of 2005. Then, in the 2Q, we had 378, but we were just 11% higher than what we had in the previous year.

In fact, if we had closed two accounts that would account for almost R\$ 1 million from the 3Q to the following quarter, we would have a better figure, almost 19%-20% growth in terms of licensing. So, objectively, we do not see as a trend what happened in this quarter. And again, this thing about, as you may remember, was almost a prevision when I was talking to the market about that:

remember that 80% of our sales happened in the last four days of the month. Therefore, when we have some accounts flowing from one month to the other, no problem at all. But when we have this in between quarters, this also will occur.

I would just like to point out a positive thing that happened. I am not putting this as an excuse, in terms of the 3Q revenues, but we had the world cup and the elections that also inferred some of the closing deals. But, again, if three deals that we had scheduled had the chance to be closed before September 30<sup>th</sup>, so, we will have a 30% growth.

**Mario Edelbaum:**

So, just to summarize, you have told us there is a volatility in revenue growth, so, I appreciate that, but, should we expect that when we get going to the next quarters and again into 2007 that your license growth will stay between your range of 15% to 20% or do you think when we look forward, we should start thinking of slower growth?

**José Rogério Luis:**

It is not going to be lower than 15% and higher than 25%. So, every time that we have something far higher than 25%, we think that some accounts from the quarter jumped to the other quarter. If we have this below 15%, again, it is not natural. So, at this point in time, we see no changes in the environment that are not going to put us in this range between 15% or 25%. Outside this range of 15% and 25%.

**Mario Edelbaum:**

I have a second question. You did talk a little bit about it in terms of expenses and margin. What would you say of the 3Q margin, were you disappointed or do you think that we could see, we were getting to the 20% and above that you are talking or it is always going up or are we going to see any new expectation maybe going down next year and then finally making it up. How do you see that progression?

**José Rogério Luis:**

I see our progression on a step-by-step base. First thing, talking about our perception about the quarter. We saw this quarter as a good one, but we are not happy, we could and we can do better, for sure. Not only in terms of revenues, but again, the market is there. I am very confident that the market is there; we have the product and we have always this thing of reaching the market and being able to close the deal. The pipeline that we had was the same pipeline that we had in the previous quarters. So, it is just a question that hasn't really had the opportunity to have it signed.

In terms of the margins, remember that I always invite the market to take pictures from us and see that we left from a margin, not a pro forma, a real

margin of the group of 15.7% in the end of 2005, and we said that, 3-5 years after the IPO, we would reach the range between 20%-25%.

So, if you take a picture now from us, we are in 18.4%-18.5%, and it is our strong expectation and we are working on it in order to have a step-by-step way in order to reach this 20%-25%.

**Mario Edelbaum:**

So, it would be unlikely that we would see more quarters in the 16.6%?

**José Rogério Luis:**

No, I am not telling you this, I am telling you that every time you close a period you are going to see in this period of 12 months our EBITDA going up.

**Mario Edelbaum:**

OK, I appreciate that, thank you.

**José Rogério Luis:**

That is exactly what we are working on, so that is why I am always inviting people to take the pictures and see how we are doing in terms of growth. Just one last point that I would like... As you can see in our page eight of our presentation, this is really a picture of how we see ourselves. I mean, quarter after quarter, doing the job in terms of growing the top line and, at the same time, we have to speed up some aspects of the synergies that we have to do in order to get... Again, not only better margins, because we are growing in terms of sales, but also because we are managing in the right way our profit in that sense.

**Mario Edelbaum:**

Thank you very much.

**Operator:**

There appears to be no further questions. I will turn the floor back over to you for any further or closing remarks.

**José Rogério Luis:**

So, I would like to say thank you to everybody for, again, supporting us as well as always saying things that we can work on. Again, I would just like to make it clear that we see the under-penetrated market and we have the structure and distribution to reach this market. So, we have another thing that is also the aspect of execution, execution in hand of the management that we have, of course, not only reach to the market in terms of sales, but also to control our margins and our costs.

We are working on it in a very hard way; we, again, think as a picture as a whole as a very positive one and we think and we expect to count with your support during the future. Thank you very much.

**Operator:**

Thank you, that thus concludes today's teleconference. You may disconnect your lines at this time and have a wonderful day.