Operator: Good morning. Welcome to TOTVS second quarter of 2018 conference call. Today we have with us Gilsomar Maia, CFO, Eros Jantsch, Vice-President for Small Businesses, and Sérgio Sério, Investor Relations Manager.

Note that all participants will be on listen-only mode during the presentation. After the presentation, we will start the 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.br.

Before proceeding, we wish to clarify that any forward-looking statements that may be made during the conference call, related to the 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, hence, depend on circumstances that may or may not occur. Investors should understand that general economic conditions, industry conditions and other operational factors could affect the future performance of TOTVS and could lead results to differ materially from those mentioned in such forward-looking statements.

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

Gilsomar Maia: Good morning everyone. Thank you for participating in our conference call. I will begin the presentation by commenting on the main recent events on **slide 3**.

The first event is the increase of Bematech's interest in RJ Participações by the incremental acquisition of 20% of the capital stock of RJ for R$4,3 million. As a result, Bematech now holds an 80% interest in RJ and the remaining 20% call option was extended to 2021, based on RJ's business and succession plan.

The second event to be highlighted is THE MAINTENANCE OF THE IT SECTOR IN THE TAX RELIEF OF PAYROLL until 2020, based on a Federal Law enacted on May 30, 2018. The Law establishes that, from 2021, the employer's social security contribution will no longer affect the revenue at a rate of 4.5% and will again be levied on the payroll at the rate of 20%.

We focus this theme on the services operation, given its predominance of payroll as a cost component. The deadline established by law contributes to prepare the service operation, both in terms of efficiency and in pricing, in order to mitigate possible effects from 2021.

And, the third event is the Board of Directors approval for the distribution of DIVIDENDS AND INTEREST ON CAPITAL for the first half of 2018 in the total amount of R$32.7 million, corresponding to R$0.20 per share, of which R$18,0 million refers to dividends, corresponding to R$0.11 per share, and R$14.7 million refers to Interest on Capital, corresponding to R$0.09 per share. Both, dividends and interest on capital will be paid on October 3, 2018 to the Company's shareholders on August 1st, 2018.

Turning now to **slide 4**, we also highlight the study "Enterprise Application Software" released by Gartner in June, which reiterates TOTVS leadership in the ERP market in Brazil, with a participation of 50.5% in 2017, which represents an increase of 0.9 percentage point compared to 2016, and 0.2 percentage point from 2014, which is the last year before switching to the subscription model.

The same study also points TOTVS in the first position in Latin America with a 31.6% share of the ERP market, which represents an increase of 0.7 percentage point compared to 2016.

I now turn the presentation to Eros, who will comment on revenues in the quarter on **slide 5**. Eros, please go ahead.

Eros Jantsch: Thanks Maia. Good morning everyone.

The 2% quarter-on-quarter growth in net revenue was driven by a seasonal increase in hardware sales and the progress of service projects in the second quarter.

In addition to the seasonal evolution, the increase in service sales in previous quarters also contributed to a year-on-year growth of 11% in service revenue, which added to the increase in software revenue, led to a 4.4% year-on-year growth in net revenue.

On the other hand, the quarter-on-quarter reduction of 3.9% in software revenue was mainly due to the 33% drop in license revenue shown on **slide 6**, particularly related to the incremental license revenue from corporate model in first quarter, that is also a seasonal element as shown on the year-on-year growth of the quarter and the last 12-month period.

And, by the way, year-on-year comparison shows that software revenue growth has been generated by Subscription Revenue, which grew 31% in the quarter and almost 35% in the last 12 months.

In the chart on the left of the **slide 7**, it becomes clearer. We can see that the blue bars in the chart, representing the sum of licensing and maintenance revenues, have not grown in the past 3 quarters, and all software revenue growth has come from subscription revenue represented by orange bars.

Subscription revenue grew 2.7% this quarter, rising from R$94.6 million last quarter to R$97.2 million this quarter. This performance of the subscription was negatively affected by the higher concentration of sales in June, due to the strike of truck drivers in the last week of May. The sales of June will contribute to the third quarter revenue and are included in the annualized subscription exercise on the chart to the right of the slide.

Additionnaly, revenue growth and subscription ARR were also negatively impacted by two factors linked to adjustments in the Bemacash sales model: (i) higher volume of cancellation due to delinquency coming from units sold before first quarter of 2018, when sales by credit card were implemented; and (ii) the reduction in sales resulting from the change in software chargeability from the first month of subscription.

Despite these factors, subscription annual recurring revenue (ARR) totaled R$425.6 million in the second quarter, an amount that represents 40% growth year-on-year and 5.7% growth quarter over quarter.

I now turn the presentation to Sérgio Serio, who will comment on the software result on **slide 8**.

Sérgio Sério: Thank you Eros. Good morning everyone.

The year-on-year reduction in the Adjusted Software Contribution Margin is a result of the combination of R&D and Support Costs.

Despite the reduction in recurring costs with personnel performed in 2017, the growth of these lines reflects the wage increase resulting from collective bargaining agreements, in addition to the new investments in innovation made by the Company in the period.

The quarter-on-quarte reduction in the Adjusted Software Contribution Margin is associated with the reduction in Software Revenue commented by Eros and the increase in costs due to the higher volume of participants in holidays in 1Q and the additional costs of Support to meet the demand from new customers added in the period and from the existing customers, due to new regulations that came into effect in the first half of this year, such as e-Social.

Turning now to services, on **slide 9**, the Adjusted Service Contribution Margin grew 600 basis points over 2Q17, and 310 basis points over 1Q18. The growth in Service Revenue was mainly due to the higher pace of service sales observed in recent quarters and the higher allocation of service professionals in the quarter.

When we use the comparison of the last 12 months, the reduction of 2.1% in service costs is a consequence of the adjustment of the structure promoted throughout 2H17. This reduction led to a margin of 5.6% in the last 12-month, or 340 basis points higher than in the same period of last year.

Turning now to hardware, on **slide 10**, the Adjusted Hardware Contribution Margin was 580 basis points lower than in 2Q17 and 570 basis points lower in the comparison of the last 12-month. The main elements that resulted in this decline were the increase in R&D, as a result of expenses with the institutes hired to comply with the IT Law and the drop in sales of tax solutions, which have a higher gross margin.

The 240 basis points quarter-on-quarter increase in the Adjusted Contribution Margin reflects the increase in sales of fiscal solutions in 2Q18, due to the maintenance of tax solutions in Minas Gerais and the incentive by the Government of Santa Catarina to regularize the use of fiscal printer, and also the recover of sales volume due to the negative seasonality in 1Q18.

Such negative seasonality of the 1st quarter can be seen in the chart on the left on **slide 11**. On the chart to the right of the same slide, we show the increase in the share of fiscal solutions in the product mix caused by the demand commented on the previous slide. The increase in sales of tax solutions, as shown, which have a higher margin, led to an increase in the margin of hardware results in 2Q18.

In addition, in 2Q18, Bemacash sales totaled 691 units, compared to 1,093 in 2Q17. As commented previously by Eros, this reduction is a consequence of the changes in the sales model of Bemacash, which aim to simplify the sales process and reduce delinquency.

To talk about selling and administrative expenses, please go to **slide 12**.

In the quarter, selling and commissions expenses as a percentage of net revenue declined in relation to the previous quarter, due to the mix of sales between own channels and franchises and the revenue mix.

Year-on Year, the reduction of 5.7% in selling expenses is explained by the reduction in recurring costs with personnel in 4Q17 and the deferral of variable compensation as a consequence of IFRS-15.

Regarding general and administrative expenses, management fees and other expenses, the year-on-year reduction is mainly associated to the provision for contingencies in 2Q17 being lower than the quarterly average of the same year, and also to the additional expenses with the incorporation of PC Sistemas in 2Q17 and the integration of Bematech's administrative operations during last year, both contributed to the reduction of recurring costs with personnel in 4Q17.

Turning to the advertising and marketing expenses, the year-on-year and quarter-on-quarter variations reflect the Company's annual marketing plan.

And, the allowance for doubtful accounts represented 1.9% of Net Revenue in 2Q18, compared to 2.3% in 1Q18 and 1.4% in 2Q17. This provison reflects the higher level of current delinquency, which resulted in a negative effect of R$3.2 million with the adoption of IFRS-9. Excluding the IFRS-9 effect, the provision represented 1.4% of net revenue, the same level observed in the second quarter of 2017.

I now return the presentation to Maia, who will comment on EBITDA on **slide 13**.

Gilsomar Maia: As we can see in the charts, the quarter-on quarter reduction in Adjusted EBITDA was due to the reduction in Software results, partially offset by higher service and hardware results and reductions in commercial and administrative expenses.

Year-on-year, Adjusted EBITDA increase came from software and services results that more than offset the decrease in hardware results.The change in the product mix continues to reduce hardware results, with the discontinuation of fiscal printers in a more advanced stage than the development of higher value-added solutions such as Bemacash and smart devices for the Internet of Things.

In the last 12-month comparison, the increase in software and services results, even partially offset by the reduction in hardware results, has not yet resulted in EBITDA growth, due to the amount still required by the allowance for doubtful accounts, part of the commercial expenses, and by the provisions for contingencies, part of the administrative expenses.

Moving now to **slide 14**, the EBITDA performance is the main element that, even with the improvement in financial results and income tax and social contribution, led to a reduction in net income quarter-on-quarter.

In the year-on-year comparison, the 7% increase in net income came mainly from the EBITDA improvement, since the reduction in amortization expenses, linked to lower expenses related to intangible assets arising from acquisitions of companies, was more than offset by the higher net financial expenses, and the higher effective tax rate in this quarter.

Now, I'll move to cash flow and debt on **slide 15**.

Free cash generation grew 20% year-on-year, mainly due to the growth in earnings before Income Tax and Social Contribution and the reduction of funds invested in working capital.

Quarter-on-quarter, the free cash generation grew 66% and the operating generation grew 53%, mainly by the reduction in working capital investments, and the lower volume of interest payments, given the interest amortization of debentures occurred in 1Q18; and also the lower CAPEX level.

Additionaly, net debt fell almost 50% year-on-year and 23.5% quarter-over -quarter, even with the payment of dividends and interest on equity reflected in the 2Q18 financing flow. This reduction led net debt to the level of 0.7x last 12-month Adjusted EBITDA, which is the lowest level since 2Q15.

I'll now turn to **slide 16** for the closing remarks.

Throughout this conference, we saw that:

Net revenue grew 4.4%, driven by software and services revenues that grew 4.4% and 11% year-on-year respectively

Subscription revenue grew 31% year-over-year, already accounting for more than 25% of software revenue.

Adjusted EBITDA increased year-on-year by 4.5%, with stable margin.

Free cash flow generation grew 66% and net debt fell by half year on year, reaching 0.7x EBITDA.

We are now available for the Q&A session.