Cerved Group S.p.A.

"Nine Months 2019 Results Conference Call"

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OPERATOR: Good morning. This is the Chorus Call conference operator. Welcome and thank you for joining the Cerved Group Nine Months 2019 Results Conference Call. After the presentation, there will be an opportunity to ask questions.

At this time, I would like to turn the conference over to Mr. Pietro Masera, Head of Structured Finance and Investor Relations. Please go ahead, sir.

PIETRO MASERA: Hi, good morning everyone. Thanks for joining the call today, Pietro Masera speaking, and I am here with Andrea Mignanelli, CEO and Giovanni Sartor, CFO. The call today will deal with the results to 30 September, 2019.

And at this point, I'll leave it to Andrea.

ANDREA MIGNANELLI: Hello everybody. Thank you for participating in the call today. Before getting into the details of the presentation, let me give you some initial comments to put Q3 into context. As you may recall, in the H1 call we made in July, we said that these [ph] results would have been backhanded due to a number of changes in the go-to-market and, as well as, to the contribution of M&A that we were just about to close.

Now, fortunately that's exactly what's happening. So Q3 is good and it's in line with what we expected and also I may say that we would expect Q4 to be on the same trajectory. Given the fact that we have some other initiatives that we are chasing in terms of M&A, as well as, the full deployment of the new initiatives that we are currently launching, they clearly…does not affect the guidance we gave in June '18, we still work along this guideline and the new guidance will be coming, let's say, in Q2 2020 as we used to do every couple of years…every 2 years given the fact that we gave the last guidance in June '18.

Now, let's give a look to the basic indicators that we show on Page 3. Revenues are growing 11.6% of which 4% organic, adjusted EBITDA growing at 8.3% of which 3% organic, operating cash flow up by 13.2%, adjusted net income up by 16.3% and leverage again decreasing to 2.4 times EBITDA. This is also thanks to the early termination fee of Monte dei Paschi di Siena.

Also just a quick flash on strategic initiatives, there are a number of things going on. The few key elements are the fact that finally the corporate credit information segment is running at a pace that we like, and this is mostly due to the fact that the merge of the 2 sales network is providing the expected results. And at the same time we launched a Cerved Money &Go which is a digital lending platform to…for our clients to sell their trade receivables. Again, clearly we are not doing balance sheet investments, we are using third party funds, but we are fully exploiting our analytics capacity, our credit assessment capacity and this is something that we think our clients will like a lot, and we have some initial contracts that back up this idea.

Also as you probably read in the press last night, our board decided to go ahead with the process of, let's say, evaluation of strategic alternatives on the credit management division mainly related to the possibility of sell the division or make strategic alliance with other players. So a disposal or a combinations, this is what the board has decided last night.

Now, let's go into more detail, and I will actually get to Page 7 where we see the divisional results. So some good news here as well at the divisional level. As you can see, the corporate information revenues are up 4.8% and this is good finally as a number, I have to say that it's made of 2…basically 2 effects, first Q3 was a solid 5% organic growth. There is also a strong contribution from the acquisition of MBS Consulting which revenues are mainly in the corporate business as they rely heavily on insurance at the moment. And as I told you in the last call, what we plan to do with this company is to take them to other vertical segment…client segments such as banking and telecom and media and so forth.

On financial institutions, still I don't like the minus 0.9, but I have to say that it is improving compared to the last quarter and especially we would expect a number of new initiatives in the advisory and advanced analytics space to bring these results back to a more like a positive trend by Q4.

Also in terms of adjusted EBITDA, still minus 1.6% but this is improving versus the minus 2.4% in H1, mainly due to the corporate revenues and the consolidation of MBS. So here as well we plan to recover and do well as well in Q4.

Marketing Solution I would say nice, back to a decent shape I would say compared to the awkward Q2 where we had positive revenue increase and negative EBITDA, now finally both indicators are in the positive side and this is mainly due to like, as I expected, the new organization that is actually putting some higher management focus on their division.

Finally, credit management doing very well, plus 29% in revenues and 43% in EBITDA. This is quite…it's quite important because, it's mainly due to performance, and I will get back to this in a second. So, all in all, results plus 11.6 in revenues, plus 8.3 in EBITDA.

Now, if you want some more details on the various divisions, let's go to Page 8 on the Credit Information. There's more contraction of minus 0.9% in Q3, it's due to the fact that the business is rather stable and in the past used to be compensated by real estate, and in this quarter real estate was not so strong as it is used to be in the past. And at the same time, the new businesses and mainly Atoka, the marketing platform and advisory and advanced analytics are well received by banks. But clearly, they do not deploy revenues yet. So, we have a number of conversations in place with large banks. We will expect the benefits of this conversation coming in the next few months.

Revenue in the Corporate business are up, and let's say sales in Q2…sorry, we have, you know, strong increase in sales, and this will, as you know by now, this will convert into revenues with a bit of a delay. So, in order to match the guidance that we gave for year-end, we expect to do a very strong Q4, may be stronger than Q3 in Corporate segment only. And so, we believe that we are on track to meet the guidance for the year.

As I said, MBS is contributing strongly to these results. We are very happy with the acquisition we made. They perfectly fit with our mindset and values and clients are receiving very well, the fact that we go to them with a double, let's say with a double approach and data and technology on our side and advanced analytics on their side. So, we are very happy about this acquisition.

In terms of EBITDA margin, you see there is still a bit of a contraction from 52.9% of last year and 50.9%, you know, clearly very good margin, so we can't complain too much. The thing is, by growing in businesses different from the pure data, there is a certain dilution because MBS, it's a consulting business so typically runs in the range of 30%, 35% EBITDA margin. But I…as I also had the chance to comment in the past, I'm not too concerned about the margin per se as long as it comes from a dilution. In the past, a little bit of margin compression was more coming from let’s say negative productivity leverage in the sense that we were growing sales more than…sorry, cost more than sales. I think this is under control now, we made a lot of work during the year to understand what are the key cost drivers and that we are assessing properly the way go forward. So, I would expect costs to be more under control going forward in the Credit Information business. So, we'll see the benefit of this let's say tighter cost control in the next few quarters to come.

Marketing Solutions Page 9, as I say, finally looks normal, revenues are up and EBITDA is up. I have to say that this is mainly I guess due to 2 or 3 events**.** First, we are changing the organization, so now we have one of our Directors fully in-charge of the Marketing Solution space, which helps to have a better view on revenues and costs. And also, we made some, you know, cost control initiatives, especially on the legacy system, which was quite soft in the first 2 quarters. And that's then the first thing.

The second thing is, the acquisition of our Web…sorry, Web marketing optimization company is doing very well, and this is more than compensating the softness of the legacy business. And also, the jump in EBITDA reflects this fact. And so, we expect this trend to be even stronger in Q4. So, I would say that on this one as well, we are delivering on the promise we made in Q2.

Finally, if you go to Page 10, you see the Credit Management, you know, it’s still doing very well, also because the growth in 2019 is robust growth, it's an organic growth. We also did a couple of very good acquisitions, although small but very interesting, one is Cerved Property Services in Greece, which has exactly…is actually delivering results better than expected, where this company is…was purchased by us from Eurobank, and now it's a leading local player of real estate services and the trust [ph] real estate management. Also, we finalized the acquisition of Euro Legal Service, which is a small collection company, which fits very nicely into our Cerved Credit Collection business and it's already merged into it and it's…is providing good results as well. So all in all, EBITDA margin is still growing more than sales at 43%, this is due to operating leverage and due to the fact that most of the growth is coming from performance in the banking business, meaning that, we are actually collecting more than expected and therefore the company there is doing very well.

So I am over with the business overview, and I leave the space to Giovanni Sartor, our CFO, to comment on the financial performance.

GIOVANNI SARTOR: Good morning, everybody and thanks Andrea. Moving on to Slide 13, let's take a brief look at the income statement. Capitalizing on 7% increase in EBITDA, the adjusted net profit increased by 16.3% versus last year, this represent an acceleration compared to the 12.5% in H1, and was achieved, thanks to a number of factors, but I'd say mainly it's the increase in EBITDA. Given, however the significant portion of the growth coming from Juliet, the increase in adjusted net income net of minority is lower for sure, but still 8.5%.

Regarding taxes, we continue to benefit from the "Patent Box" initiatives. I remember on a yearly basis its worth about €10 million of deduction, so the saving in terms of taxes will be about €2.5 million. Note, however, that for now this only apply to 2019. And we are not sure about receiving further tax break in the future even if we will apply soon before the end of the year.

Slide 14, provides the customary breakdown on net working capital. And as you can see net working capital increased to 12.8% of revenues adjusted to reflect of course the 2019 acquisition on a full-year basis. There is an increase compared to the 9% of last year and this is almost entirely due to the higher working capital interest segments of the targets we acquire, in particular, MBS and the Euro Legal Services. In any event, we are also providing the relevant working capital contribution i.e. €19 million.

Skipping on the Slide 15, the operating cash flow was still very positive, growing by 13% versus the prior year. And this positive result is based probably in 3 considerations. Firstly, growth we are achieving in the Credit Management Division is very, very efficient from a working capital perspective. Second, we have lower CAPEX than last year. And third, the impact from the recent acquisitions. Overall for the full-year, we can still reasonably expect operating cash flow growth to be roughly in line with the underlying EBITDA growth.

Last but not least. Moving to Slide 16, the financial indebtedness as of 30 September, 2019 was 2.4 time the EBITDA, based, of course, on LTM EBITDA, which is…which on a pro forma basis also includes the full P&L impact of the closed deals and clearly all is based on the IFRS 16. So despite the payment of €58 million dividends and other €50 million for M&A, we are still below our 3 times long-term leverage target, so we can also continue to benefit…continue to benefit from saving in cash and interest rates.

So I have finished. Thank you for your attention. And at this point, we have completed the presentation. So let's open the Q&A session.

Q&A

OPERATOR: Excuse me. This is the Chorus Call conference operator. We will now begin the question and answer session. The first question is from Andreas Markou with Berenberg. Please go ahead.

ANDREAS MARKOU: Good morning, everyone. Thank you very much for the presentation and congratulations on the results. I have 3 questions. The first one is on the performance of the Credit Management Division, I saw in Q3. This was especially strong. Can you mention whether there is a one-off element there if there is anything extraordinary? That's the first one.

The second one is on your AuM increase, again for the Credit Management Division comparing to Q2. So I see that the NPL AuM is up by around €1 billion to €1.5 billion. Can you just explain where this increase is coming from?

And the third question is a bit more generally on the kind of a bit medium to long-term growth of the group. So if we look at you know, your EBITDA growth over the past couple of quarters, this has been pretty much entirely driven by Credit Management Division, which now you are selling. And you did mention about the several initiatives you are taking on the credit information side. What is your conviction and your confidence about stimulating growth in the Credit Information Segment assuming that you sell the Credit Management Division? Thank you.

ANDREA MIGNANELLI: Yes. Thank you for the questions. First, performance and credit management; as you know, credit management has several business lines under the same roof banking NPL, small receivables management, legal services, master servicing, performing loans management, real estate, advisory, and so forth. So every time when we look at performance it's a combination of different drivers. Looking at the strong performance in Q3 and most of it comes from higher collection performance in the banking business both in Juliet and in our…and the rest of the group. So the banking business is doing particularly well and because it's a business where we have mostly variable revenues in mostly fixed costs. Clearly, when our performance is very strong, the impact of EBITDA is very good.

The other part of the businesses are doing well, and on track I would say. So nothing special, just very strong collection performance on the banking loans business.

The second question was about AuMs. We got normal business, as you remember we discussed the fact that we have many, many clients. We do not rely on a single client. Let's say the top 3 clients in our business accounts for about 20%, 23%, 25% of total revenues and in order to get to 50% of our revenues we need to take at least 25 clients which means that our portfolio…client portfolio is very well diversified so we…you know we normally grow by taking portfolios. In the specific case in the last few months, we boarded a portfolio from UniCredit, €1.2 billion and another small portfolios of…you know couple of smaller portfolio for €0.3 billion and master servicing agreement for portfolio €0.5 billion. So it is…I would say business as usual, nothing special, just normal clients that keep awarding us new portfolios.

And finally, you question, I understand clearly…I understand the question because if you look at the numbers now it looks like, you know, credit management is the key driver of our growth, but I have couple of…we have a couple of thoughts on this. First, the credit…what we currently call credit information and marketing solutions, I think can do better than this, and the way to do better than this is to enlarge the pie meaning that we understand and this is the base of our strategic review and the change in the organization we think that we can…we should call our, let's say, arena services for growth and services for risk management, not just marketing solutions and credit information. These are 2 subsets of the business we can do.

When I look at that data we have, when I look at the technology we can deploy, and when I talk to clients, I understand that they want to grow their businesses whether they are banks or large corporates or institutions in general they wasn't to grow, and they want to be protected from risk and that's what we do. So it is way more than credit info and marketing solutions. And so, the strategic outlook for Cerved will be to be stronger in these 2 businesses that I mentioned. And if you look at the broader perspective, for example, at risk management you don't have only credit risk but you also have antifraud, anti-money laundry, regulatory risk and we actually, our data and technology can support clients in all these new types of risks. So I believe we can do better than what we are doing by enlarging the competitive arena as I say.

Now, on credit management, the credit management is doing very well. I totally, you know, as you can imagine I am well aware about the performance of the group and the quality of group. We just…we are not in the process to sell as you say. We are in the process to evaluate strategic options and these strategic options include the potential sale or the potential merge or joint venture with other industrial players. Why? Because we believe that there is a certain consolidation trend in the market and let's say size matters in this business going forward and also we do not buy NPLs and more and more, let's say, the ability to buy credit it is a competitive advantage.

We made a living in the past out of being an independent servicer and we did very well in the past 7 years with this strategy. Now, we need to face the reality that things are changing in the Italian market, and more and more banks want to sell, as well as, to outsource. So will be for us to have some sort of alliances or joint venture or just to dispose the division and put it in a context where the credit management can be combined with credit acquisition.

ANDREAS MARKOU: Okay. Thank you very much. That's very helpful.

OPERATOR: The next question is from Andrea Lisi with Equita. Please go ahead, sir.

ANDREA LISI: Hi, thank you for the call. Just one question from my side, I want to ask you if you can provide the data what percentage of the increase in sales points that we have seen in second quarter was effectively converted into sales in the third quarter. So what is the percentage that remains potentially to be converted in the last quarter? And if you have the data, if the trend at this point that we saw in the third quarter…in the second quarter is also visible for the third quarter as well. Thank you.

ANDREA MIGNANELLI: Yes, let me just…it is a very technical question. Give me one second to retrieve the information, please. Yes, I don't have like exactly the answer to your question, I can tell you that last 12 months the sale of prepaid points was up 9.5%, and let's say year-to-date it is about 5%. And therefore, I think we have a bit of a tailwind and obviously a bit of seasonality, but the numbers look good, because clearly we haven't fully exploited of the sales yet, okay. And we are slowly kind of…we observe slowly a convergence of these 2 trends which means that the business is healthy. So it's selling pre-points and coins are converting this pre-points in revenues with a bit of a delay, okay. So, these are…I hope I was clear enough.

ANDREA LISI: Yes, yes got it. Thank you very much.

ANDREA MIGNANELLI: Okay. Thank you.

OPERATOR: The next question is from Rajesh Kumar with HSBC. Please go ahead.

RAJESH KUMAR: Good morning, gents. Just very quickly, can you give us some color on the extent of growth you have achieved on the real estate business? It looks like it performed very well in that division. Secondly, on the price negotiation term discussion you are having with the banks, it looks like you have renegotiated long duration contracts again. Can we get some more idea on the duration of the new contracts, you have renegotiated early? The final one is this is the more interesting one. You clearly are trying evolve from a data to full service analytics business, can you give us some color on what type of services which can you develop. I am aware you are doing fraud identity, those kinds of businesses which are quite interesting, but other than that are there any new segments which one would identify from global credit bureaus.

ANDREA MIGNANELLI: Yes, thank you for your question. But, first on real estate, yes, I mean, although not like a super results, I think Q3 was still decent given the fact that there are still quite a few renegotiation of mortgages in Italy due to lower interest rates. So, the demand of these services from banks is stable I would say, and we keep doing our fair share of work. We are probably still the largest provider of real estate appraisals in Italy and quality is good. So, you know, let's say we don't see anything major there. We honestly don't expect a huge growth, but at the same time, we keep doing our business. So let's say no surprise both ways there.

Your second question was on the duration of…the duration of contracts we have done, we only have one major contract expiring in 2020, towards the end of the year. And…but I have to say that it's a very relevant client and we already…I believe will start sooner rather than later to discuss the renewal with the client and that's why it's so important for us to change in the mindset of our clients their perspective on Cerved. We want to see the client, we want to…the clients to see Cerved as a partner for growth and risk management beyond the pure data providing. And what's why we started already specifically with this client conversation at your level to show what our tools can do for them in order to achieve their industrial plan. And we can help them to achieve…to gain new prospective clients in the SME business, we can help them to increase the issuance sales within their banking clients. We can help them to increase the penetration of wealthy clients in the private banking division. We can help them to reduce the capital absorption in the corporate credit departments, and I will keep going okay.

So, yes, there are renewals coming and I believe that we will tackle these new renewals with a much, you know, robust client relationship in the banking business. Anyway, back to your…just to give you a straight answer to your question, the duration of our contract is still 2023, the duration. So, you know, we feel comfortable there.

Now, going to your very important question is, how you know, what are the names, you know, of these new initiatives that we mentioning. So, as I said, the news is that we are reshaping the company from an organizational standpoint and from an strategy standpoint around 2 business units. One is called growth and the other one is called risk management. They are just…vaguely resemble the current Marketing Solution and Credit Information. As I said before, they are much broader than this. And just to give you an example, when I think of growth, currently we are already offering some business lines to our clients such as master…market and customer insight, service design, so we are making a project in a bank to help them to draw a new instant credit tool for their small clients with the immediate lending up to €100,000, artificial intelligence for sales and marketing, digital marketing solutions to improve clients' reach, as well as I say, as I have discussed before, advisory, advanced analytics especially in the insurance segment and also an academy. So, we offer training because we understand our clients are seeking for services to retrain their workforce. And that's why we use our knowledge to provide training. So this is just to mention a few business lines that we are currently doing in the growth business units. And if I look at the future, I see the digital lending, as I discussed at the beginning, coming up very strongly as a potential value driver for the company, for Cerved.

And when I look at risk management, we move from the concept of credit information, credit risk management to a broader view. And clearly, I have to mention the credit rating agency, which is doing very well and what we call in Italy Finanza Agevolata [ph], which is the support to SME clients to obtain funding with the guarantee of the government or special funding from European Funds. And this is something that is, it's an acquisition we made during the year, and is actually doing quite well and clearly fits perfectly into our business.

Real-estate risk, as I mentioned before, analytics in general, monitoring system for credit management. And when I look at the future, the new business lines that we want to develop either through M&A or internal make [ph] would be clearly KYC, anti-money laundering and anti-fraud. Very strong ESG solutions that our clients are asking at all levels support in the ESG, and as you know, we are a rating agency and we developed an ESG rating and an ESG score. So we are able to offer ESG rating on the top 400 names in Italy as well as the ESG score on the other thousands of small enterprises in Italy. And we're also thinking of launching an initiative in the PropTech retail business.

So as you see, we have a pretty good roster of initiatives in these 2 big realms of growth and risk management. I will keep you updated on what is an existing business line and what is a new business line arising.

RAJESH KUMAR: Thank you. That sounds very exciting.

ANDREA MIGNANELLI: Yes.

OPERATOR: The next question is from Michele Baldelli with Exane BNP Paribas. Please go ahead, sir.

MICHELE BALDELLI: Hi, good morning, everybody. I've just a question, how much of the growth in EBITDA in the Credit Management division is driven by Jupiter or the other way around, how much Jupiter increased the profitability? Thank you.

ANDREA MIGNANELLI: Yes, I guess you meant, Juliet.

MICHELE BALDELLI: Juliet. Oh, I'm so sorry.

ANDREA MIGNANELLI: Now, I know Juliet…Jupiter was the original name of the venture when I set it up in 2005. Now, Juliet is the company that we own together with Quaestio. Yes, profitability is driven, as I said before, mainly by performance. The performance is coming from the banking division and within the banking division, the NPE, the NPL banking division. And within this, Juliet is playing a strong role. Because especially because the contract with Monte Paschi, although unfortunately being early terminated by the bank, is actually doing very well. We doubled the performance compared to last year. Last year, we started to work on the on the Monte Paschi portfolio in May, boarding about €4 billion in a few months and taking up 200 people from the bank, with their own…we had to work on their system for a while. So, the initial startup was clearly very complex. In less than one-year, we are doubling performance. And in this business, when you double performance, you clearly have a strong benefit for the bank and also for the services. So most of that performance is coming from that contract.

MICHELE BALDELLI: Okay. Just to follow-up on this, because looking through the minorities' line, it seems that there is a €5.7 million of higher minorities. So it should be a better joint venture, which means that even that you have 50% stake, you should be roughly 10 and over a €1 million improvement of net profit in Juliet, which can lead to an EBITDA growth of roughly €14 million probably. So, if I'm looking to the EBITDA growth of the Credit Management, it seems that all the EBITDA growth is coming from Juliet, is it something that you can agree on or am I wrong or something?

ANDREA MIGNANELLI: No, you're roughly right. Although, we…as I discussed before, we…remember that Juliet is not managing only the Monte Paschi transaction. Actually, Juliet is managing roughly €18 billion of assets, out of which 4.5 billion, 5 billion are from Monte Paschi and the remaining part is from Atlante, and from another, it's divided into 4 different vehicles. So, Juliet as a whole is doing very well. But it's not only related to the Monte Paschi transaction.

MICHELE BALDELLI: Sure. Thank you very much.

ANDREA MIGNANELLI: Yes.

OPERATOR: Gentlemen, there are no more questions registered at this time.

ANDREA MIGNANELLI: Okay. Well, then thanks, everyone, for calling and we look forward to speaking again for the next quarter. Thanks. Bye-bye.