Stone Co 4Q23 Earnings Conference Call

May 13, 2024

Operator:

Good evening, everyone. Thank you for standing by. Welcome to StoneCo's first quarter 2024 earnings conference call. By now everyone should have access to our earnings release. The Company also posted a presentation to go along with its call. All material can be found online at investors.stone.co.

Throughout this conference call the Company will be presenting non-IFRS financial information including adjusted net income and adjusted net cash. These are important financial measures for the Company but are not financial measures as defined by IFRS. Reconciliations of the Company's non-IFRS financial information to the IFRS financial information appear in today's press release.

Finally, before we begin our formal remarks, I would like to remind everyone that today's discussion may include forward-looking statements. These forward-looking statements are not guarantees of future performance and therefore you should not put undue reliance on them. These statements are subject to numerous risks and uncertainties that could cause actual results to differ materially from the Company's expectations. Please refer to the forward-looking statements disclosure in the Company's earnings press release.

In addition, many of the risks regarding the business are disclosed in the Company's Form 20-F filed with the Securities and Exchange Commission, which is available at www.SEC.gov. I would now like to turn the conference over to your host, Roberta Noronha, Head of Investor Relations at StoneCo. Please proceed.

Roberta Noronha – Head of Investor Relations

Thank you, operator, and good evening, everyone. Joining me today on the call is our CEO, Pedro Zinner, our Chief Financial and Investor Relations Officer, Mateus Scherer, our Chief Strategy & Marketing Officer, Lia Matos and our Head of Credit, Gregor Ilg.

Today, we will present our first quarter 2024 results and provide an updated outlook for our business.

I will now pass it over to Pedro so he can share some highlights of our performance. Pedro?

Pedro Zinner – Chief Executive Officer

Thank you, Roberta and good evening, everyone.

I would like to begin by briefly talking about our first quarter 2024 results, which I believe are the kickoff for a great year ahead of us.

Our business continued to grow strongly, while we kept on delivering our strategic priorities.

In financial services, we performed well across all of our client offerings.

Starting with payments, we posted strong TPV growth (including PIX) and nearly matched the same volumes from the holiday shopping season in 4Q. This quarter, we launched instant payments in Ton – fulfilling a key request from our micro merchant clients.

In banking, we continued to show progress in onboarding new and existing clients to our bundled banking and payments solution, and today, approximately 80% of our active client base has our bundled offering. A couple of highlights I would like to make are the start of our pilot with credit cards in Ton and the evolution of the banking solution for SMBs in Stone, with features such as "PIX em lote" for our clients to simplify their workflows around paying their employees.

And finally, our credit solution continues to grow according to plan. We maintain our conservative approach but are testing different client profiles to grow while making sure we balance our credit models. We have set up a specialized desk to offer credit to larger clients with TPV above R$500 thousand per month, and this is just getting underway.

Now let me shift to our software business, which performed well this quarter, showing progress versus our previous quarter results, and in line with our strategic priorities.

Our vertical software grew well in 1Q with an annual revenue increase of 12% which was purely organic. Our enterprise software remains a detractor, moderating our total software revenue growth considering that we are not emphasizing this part of the business. However, the strong performance in our vertical software combined with our efficiency efforts continue to drive up total profitability in this segment.

As we discussed in our investor day, we will continue cross-selling financial solutions into areas of our software client base and evolve on creating software and financial services bundles. In 2024, we are focusing on the retail and gas station verticals – the latter being a highlight in the quarter.

In summary, I was pleased with the direction of our first quarter 2024 results and I think we remain on track to deliver our guidance for the year.

Now I would like to pass it over to Lia to discuss our first quarter 2024 performance and strategic updates. Lia?

Lia Matos – Chief Strategy & Marketing Officer

Thank you, Pedro and good evening, everyone.

As Pedro mentioned, we made progress in the first quarter across our strategic priorities, advancing on critical areas as we progress towards our 2024 and long-term goals.

Before we start discussing our main financial highlights, I would like to remind you that from 1Q24 onwards we have changed our internal accounting methodology for membership fees revenues. From now on, membership fees revenues will be deferred throughout the expected life of the merchant, instead of being recognized entirely at the time of the acquisition of the merchant. The materials we are presenting incorporate this new internal accounting methodology as of 1Q24. For this quarter, we will also present growth metrics using the previous methodology since this is the first and most impacted quarter.

As you can see on slide 4, our consolidated Revenues grew 14% year over year, which combined with lower other and administrative expenses, led to an increase of 75% in Adjusted EBT, despite an increase in selling expenses due to the seasonality of investments in marketing and provisions for loan losses. These factors resulted in Adjusted Net Income increasing by almost 90% year over year, reaching an Adjusted Net Margin of 14.6%, up around 650 basis points.

Now let's take a look at our financial services segment performance on slides 5 to 9, starting on slide 5 with the performance of our Payments business for MSMBs.

Our Payments active client base **increased 33% year over year**, reaching almost **3.7 million active clients**. Sequentially, this represented a net addition of **205 thousand clients**. The lower addition of clients compared to the previous year is primarily a result of the fact that we have caught up to the growth levels in the micro segment. As you will see in the pages that follow, besides optimizing our commercial strategy for growth and market share gains, we are also putting a lot of focus on improving our payments and banking bundle offerings to new client cohorts, both in Ton and Stone, as well as driving more engagement with our solutions for older cohorts of clients.

As you can see on slide 6, this approach has resulted in profitable TPV growth and market share gains in the MSMB segment.

MSMB TPV including PIX P2M increased **24% year over year**. Excluding PIX P2M volumes, which were more than R$8 billion in the quarter, MSMB TPV increased more than 18% year over year. We achieved this strong growth while also increasing take rates by **15 basis points year over year, to reach 2.54% with material contributions from all our financial services solutions.** We are continuously evolving our pricing and bundle strategy, to achieve higher levels of client engagement, and we believe these strong numbers are the result of our competitive advantages in distribution, superior service and our increasing ability to offer more complete solutions to our clients.

Moving to slide 7, let's discuss our Banking performance.

Our Banking active client base **nearly doubled year over year, to around 2.4 million active clients**. This growth was a result of the launch of "Super Conta Ton" in the beginning of 2023 and the continued activation of banking for Stone clients through our bundle offers. The decrease in growth rates compared to previous quarters is mainly due to the completion of our migration of Ton clients to our full banking solution. Going forward, we expect our banking active client base to grow more in line with the sequential increase in payments gross adds, as we continue to effectively bundle payments and banking.

This growth in our client base also helped drive a **53% year over year growth in client deposits, which reached R$6 billion in the quarter.** Despite the seasonal grow-over effects from the fourth quarter and the lower average CDI in the period, ARPAC increased to R$29.3 per month, driven by higher average deposits per client, as a result of increased engagement with our banking solutions. As Pedro mentioned, this quarter we made good progress in our product roadmap, starting to pilot credit cards for Ton clients as well as launching features that help our SMB clients to simplify their cash management workflows, such as paying suppliers and employees.

Moving to slide 8, I will talk about our credit performance.

This quarter, we disbursed around R$295 million, reaching a portfolio of almost **R$532 million, an increase of roughly 72% quarter over quarter**. Provision expenses for working capital expected losses totaled R$44 million in the period, resulting in accumulated provision expenses of R$106 million, as we are still constituting provisions in the amount of 20% of our portfolio. Although we are doing this conservatively, the performance of our vintages is above our expectations, **with NPLs between 15 and 90 days of 2.2% and NPLs over 90 days of 1.5%**. As we have highlighted before, this is still a recently launched portfolio, so the ratio of past-due loans should increase as our cohorts mature. This year, we will continue with disbursements without changing our approach towards risk evaluation and close monitoring of market conditions.

To summarize the performance of our financial services segment, the first quarter was again marked by strong TPV growth and higher take rates, resulting in Financial Services revenue growth of 16% year over year in the first quarter, reaching R$2.7 billion. As a result, our Adjusted EBT reached R$529 million with an Adjusted EBT margin of 19.5%, which increased more than 600 basis points year over year.

Moving to slide 10, let's talk about Software performance and strategic evolutions.

Quarter over quarter, the payments TPV of clients that use both financial services and software solutions, **decreased 13%, primarily due to the seasonal effect in our retail vertical which is strongly impacted by the higher volumes of the holiday shopping season of the 4Q.** However, our

Gas Station vertical, which has been a priority focus since last year, had a positive performance quarter over quarter. These SMB clients have been increasingly receptive to our efforts to provide an end-to-end solution that combines management software, payments and banking.

On page 11, you can see the highlights of the performance of our vertical software business

As you can see, vertical software revenue grew 12% year over year. The priority verticals, where we are focusing our initial strategic efforts to integrate financial services, now account for 47% of total software revenues. Our software solutions in other verticals also had a strong quarter across different products. As a result, our vertical software now accounts for 76% of our total software revenues.

In slide 12, you can see that total software segment revenues reached R$369 million but grew slower than our vertical software. This is because overall software includes our more mature Enterprise business. However, as a result of our focus on vertical software and our efficiency initiatives, our Adjusted EBITDA in the software segment increased to R$66 million in the quarter, up 65% year over year, improving our Adjusted EBITDA margin by over 650 basis points to reach 17.8% in the quarter.

As Pedro mentioned, the first quarter marked the beginning of an important year of strategic advancements for our business trajectory.

Now, I want to pass it over to Mateus to discuss in more detail some of our key financial metrics. Mateus?

Mateus Scherer – Chief Financial and Investor Relations Officer

Thank you, Lia, and good evening, everyone. I would like to begin on slide 13, where we discuss the quarter on quarter evolution of our costs and expenses as percentage of revenues, on an adjusted basis.

- **Cost of Services reached R$810 million, increasing 12% year on year and staying flattish quarter on quarter.** Sequentially, Cost of Services increased 160 bps as percentage of revenues, as a result of (i) higher transaction, logistics and D&A costs as we grow our client base and (ii) higher provisions for loan losses which amounted to R$44 million in 1Q24 versus R$39 million in 4Q23.

- **Administrative expenses decreased 12% year on year, leading to a 220-basis points reduction** as percentage of revenues when compared to 1Q23. Sequentially, administrative expenses decreased 16%, down 100 basis points as percentage of revenues due to seasonally higher personnel expenses in the fourth quarter and lower third party services expenses in the first quarter. We remain committed to our guidance of spending less than R$1.125 million in administrative expenses for 2024, which implies a growth of less than 7% for the year.

- **Selling expenses increased 36% year on year and 17% quarter on quarter**, up 320 bps sequentially as percentage of revenues. This increase is mainly attributed to higher marketing investments as a result of a planned sponsorship for a reality television show, combined with higher investments in our sales team.

- **Financial expenses decreased 2.2% year on year leading to a 470-bps reduction as percentage of revenues.** Quarter on quarter, financial expenses decreased 5.5% and remained flattish as percentage of revenues.

- **Lastly, other expenses decreased 58% sequentially and 230 basis points as a percentage of revenues**, as a result of (i) lower share-based compensation expenses, which includes a non-recurring positive impact of R$40mn from the net effect of the cancellation and new grants of incentive plans and (ii) lower contingencies.

Turning to slide 14, our **Adjusted Net Cash** position was R$5.1 billion, reflecting an increase of **R$1.2 billion** year on year and **R$87 million** for the quarter, lower when compared to previous quarters as we continue to deploy capital towards the expansion of our credit portfolio and also as a result of seasonally higher cash consumption in labor and social liabilities in the quarter.

As we kick start the year, I believe our first quarter results demonstrate we are executing on our plan and we remain well on track to deliver our 2024 guidance.

With that said, operator, can you please open the call up to questions?