

Vitru

A tad above us! Q4 proves the resilience of DL market

Strong Q4 on the back of solid top-line growth and execution

Vitru (a Brazilian pure distance learning player) reported a strong set of Q4 results, a tad above us, marked by another round of top-line expansion (implying impressively resilient pricing), propelling it to the high end of its previously disclosed guidance. More precisely, the company posted net revenues of R\$136.5mn (+16.5% y/y; 2% above us and 0.5% above the high end guidance) and gross profit of R\$80mn, up 19% y/y. Reflecting a normalized level of PDAs at 15% of net revenues (R\$21mn), optimization of personnel costs and overall gains from scale, VTRU's adj. EBITDA virtually doubled to R\$39mn (27% above us), yielding a 29% margin (above the high end guidance of 27% and also 570bps above us). Finally, its accounting net loss was R\$2mn (vs. last year's -R\$45mn) on higher financial expenses. When adjusting for the share-based compensation plan, restructuring expenses and business combination expenses, adj. net income would have been R\$19mn.

Avg. monthly ticket resilience is impressive! Student base continues to expand

In line with the company's successful positioning in DL, the company once again saw its student base expand in Q4. More precisely, the DL undergraduate student base grew to 257k students (from 243k in Q3; +5.7% q/q), driven by a solid intake increase of 23k students in Q4 (vs. 12k in 4Q19). Meanwhile, Vitru's undergraduate avg. ticket was a very positive surprise, growing an impressive 3.5% y/y (very differently from other listed postsecondary peers). In terms of consolidated student base, Vitru posted 301.5k EoP students (from 289k in Q3; +4% q/q). Finally, we note that it now has 709 DL hubs (vs. 662 in Q3).

Solid adj. CF generation in Q4

Meanwhile, the company also reported a solid adj. CF after capex, which came in at R\$27mn (vs. R\$8.4mn in 4Q19), implying a solid 70% EBITDA to cash conversion. The increase in CF generation mainly reflects: (i) the strong improvement in cash flow from operations; (ii) continued discipline in receivables management; and (iii) lower capex in Q4 (R\$10mn vs. R\$11mn in 4Q19).

Impressive resilience + solid execution = Buy reiterated

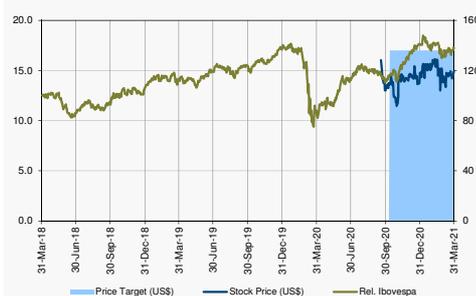
As a pure DL player, Vitru couldn't be better positioned to play the ongoing shift from onsite undergrad courses (particularly in the low-quality niche) to the distance learning market. With brighter earnings momentum ahead, we believe Vitru's pursuit of high growth rates has relatively low execution risk, hence our Buy rating.

| | |
|-------------------------|-----------|
| Rating | Buy |
| 12m Price Target | US\$17.00 |
| Price | US\$14.85 |
| RIC: N.A., BBG: VTRU US | |

Trading Data and Return Forecasts

| | |
|--------------------------------|-----------------|
| 52-wk range | US\$16.10-11.45 |
| Market cap. | US\$342m |
| Shares o/s (m) | 23.1 |
| Free float | 60% |
| Avg. daily volume('000 Shares) | 19 |
| Avg. daily value (US\$ m) | 0.3 |
| Forecast price appreciation | +14.5% |
| Forecast dividend yield | 0.0% |
| Forecast stock return | +14.5% |

Stock Performance (US\$)



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| Valuation | 12/2018 | 12/2019 | 12/2020E | 12/2021E | 12/2022E |
|----------------------|---------|---------|----------|----------|----------|
| RoIC (EBIT) % | - | - | 5.2 | 8.1 | 10.8 |
| EV/EBITDA | 25.2 | 23.5 | 16.7 | 13.7 | 10.8 |
| P/E | 42.2 | 40.5 | 29.1 | 25.9 | 17.5 |
| Net dividend yield % | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |

| Financials (US\$m) | 12/2018 | 12/2019 | 12/2020E | 12/2021E | 12/2022E |
|--------------------|---------|---------|----------|----------|----------|
| Revenues | 383 | 461 | 517 | 657 | 777 |
| EBITDA | 108 | 118 | 138 | 167 | 205 |
| Net Income | 55 | 58 | 80 | 90 | 134 |
| EPS (US\$) | 2.40 | 2.50 | 3.48 | 3.91 | 5.80 |
| Net DPS (US\$) | - | - | - | - | - |
| Net (debt) / cash | 378 | 427 | (32) | (52) | (127) |

Source: Company reports, Bovespa, BTG Pactual S.A. estimates. / Valuations: based on the last share price of the year; (E) based on a share price of US\$14.85, on 31 March 2021.

Table 1: Summary of Q4 results (Financials)

| P&L, R\$m | 4Q20E | 4Q20A | 4Q19A | 3Q20A | A/E | Y/Y | Q/Q |
|------------------------------------|--------------|---------------|----------------|---------------|----------------|----------------|----------------|
| Net Revenues | 134.1 | 136.5 | 117.1 | 126.1 | 1.8% | 16.6% | 8.2% |
| Total COGS | | (56.7) | (50.1) | (58.8) | | 13.2% | -3.6% |
| Gross Profit | | 79.8 | 67.0 | 67.3 | | 19.1% | 18.6% |
| Gross Margin (%) | | 58.5% | 57.2% | 53.4% | | 1.2 p.p | 5.1 p.p |
| SG&A | | (73.7) | (107.6) | (55.5) | | -31.5% | 32.8% |
| as % of net revenues (%) | | -54.0% | -91.9% | -44.0% | | 37.9 p.p | -10.0 p.p |
| Selling expenses | | (32.0) | (33.7) | (17.5) | | -5.0% | 82.9% |
| G&A | | (19.1) | (47.8) | (17.5) | | -60.0% | 9.1% |
| Net impairment losses + others | | (22.6) | (26.1) | (20.5) | | -13.4% | 10.2% |
| EBIT | | 6.1 | (40.6) | 11.8 | | -115.0% | -48.3% |
| EBIT Margin (%) | | 4.5% | -34.7% | 9.4% | | 39.1 p.p | -4.9 p.p |
| Depreciation and Amortization | | 14.1 | 16.3 | 13.1 | | -13.5% | 7.6% |
| EBITDA | 25.3 | 20.2 | (24.3) | 24.9 | | -183.1% | -18.9% |
| EBITDA margin (%) | 18.8% | 14.8% | -20.8% | 19.7% | | 35.6 p.p | -4.9 p.p |
| Stock option / non-recurring items | | 19.0 | 43.8 | 7.4 | | - | - |
| Adjusted EBITDA | 30.9 | 39.2 | 19.5 | 32.3 | 26.9% | 101.0% | 21.4% |
| Adjusted EBITDA Margin | 23.0% | 28.7% | 16.7% | 25.6% | 5.7 p.p | 12.1 p.p | 3.1 p.p |
| Financial Results | | (20.0) | (13.9) | 3.4 | | 43.9% | -688.2% |
| Financial Income | | 8.0 | 3.9 | 19.0 | | 105.1% | -57.9% |
| Financial Expenses | | (28.0) | (17.8) | (15.6) | | 57.3% | 79.5% |
| EBT | | (13.9) | (54.5) | 15.2 | | -74.5% | -191.4% |
| Income taxes | | 11.8 | 9.4 | (13.4) | | 25.5% | -188.1% |
| Net Earnings | 1.0 | (2.1) | (45.1) | 1.8 | -319.0% | -95.3% | -216.7% |
| Net Margin | 0.7% | -1.5% | -38.5% | 1.4% | -2.3 p.p | 37.0 p.p | -3.0 p.p |

| Revenue Breakdown | 4Q20E | 4Q20A | 4Q19A | 3Q20A | A/E | Y/Y | Q/Q |
|---------------------------------------|--------------|--------------|--------------|--------------|-------------|--------------|-------------|
| Net Revenue Breakdown (R\$ mn) | 134.1 | 136.5 | 117.1 | 126.1 | 1.7% | 16.5% | 8.2% |
| Digital Undergrad | 103.6 | 113.7 | 85.4 | 105.6 | 9.8% | 33.2% | 7.7% |
| Digital Graduation | 15.2 | 10.6 | 13.4 | 8.7 | -30.3% | -21.0% | 21.7% |
| On-campus Undergrad | 15.4 | 12.2 | 18.3 | 11.8 | -20.9% | -33.6% | 3.0% |

Source: Vitru and BTG Pactual

Table 2: Summary of Q4 results (Operating)

| Operating metrics | 4Q20E | 4Q20A | 4Q19A | 3Q20A | A/E | Y/Y | Q/Q |
|---|--------------|--------------|--------------|--------------|--------------|--------------|--------------|
| Digital Student Base (000s) | 286.3 | 301.5 | 231.6 | 289.0 | 5.3% | 30.2% | 4.3% |
| Undergraduate | 248.1 | 257.0 | 195.6 | 243.0 | 3.6% | 31.4% | 5.7% |
| Graduate | 38.2 | 44.6 | 36.0 | 46.0 | 16.8% | 24.0% | -3.1% |
| Number of HUBs | 662.0 | 709.0 | 545.0 | 662.0 | 7.1% | 30.1% | 7.1% |
| <i>Digital Student /HUB</i> | <i>432.4</i> | <i>425.3</i> | <i>424.9</i> | <i>436.6</i> | <i>-1.7%</i> | <i>0.1%</i> | <i>-2.6%</i> |
| Digital Education Tuitions (R\$ mn)* | | 177.4 | 130.9 | 163.4 | | 35.5% | 8.6% |
| Undergraduate Ticket/month (R\$) | | 263.6 | 254.6 | 263.1 | | 3.5% | 0.2% |

Source: Vitru and BTG Pactual

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The figures contained in performance charts refer to the past; past performance is not a reliable indicator of future results.

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|--------------------|---|-------------|----------------|
| Buy | Expected total return 10% above the company's sector average. | 63% | 51% |
| Neutral | Expected total return between +10% and -10% the company's sector average. | 36% | 33% |
| Sell | Expected total return 10% below the company's sector average. | 1% | 0% |

1: Percentage of companies under coverage globally within the 12-month rating category.

2: Percentage of companies within the 12-month rating category for which investment banking (IB) services were provided within the past 12 months.

Absolute return requirements

Besides the abovementioned relative return requirements, the listed absolute return requirements must be followed:

- a Buy rated stock must have an expected total return above 15%
- a Neutral rated stock can not have an expected total return below -5%
- a stock with expected total return above 50% must be rated Buy

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Moreover, at present, there have been certain isolated cases of market consolidation in the K-12 industry in Brazil. In the event that such industry consolidation intensifies, a trend that has been and is currently taking place in the post-secondary education industry in the country, Arco may face increasing levels of competition in the markets in which it operates. If Arco is unable to maintain competitive position or otherwise respond to competitive pressures effectively, Arco may lose market share, profits may decrease and the company may be adversely affected.

Valuation Methodology

Arco Platform Ltd. [BRARCE] (Primary) - Our 12-month target price is based on a 10-year DCF model with a wheighted average cost of capital (WACC) of 10.5% and perpetuity growth (g) of 6.5%, both in R\$ and nominal terms.

Company Disclosures

| Company Name | Reuters | 12-mo rating | Price | Price date |
|--------------------------------------|---------|--------------|-----------|------------|
| Arco Platform 1, 2, 4, 6, 18, 19, 20 | N.A. | Neutral | US\$25.34 | 31-3-2021 |

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Arco Platform



Source: BTG Pactual and Economica. Prices as of 31 March 2021

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