

**Operator:**

Good morning, ladies and gentlemen. At this time, we would like to welcome everyone to Smiles 2Q14 Results Conference Call. Today with us we have Mr. Leonel Andrade, Chief Executive Officer, and Mr. Flavio Vargas, Chief Financial and Investor Relations Officer.

We would like to inform you that you will be in listen-only mode during the company's presentation. After Smiles' remarks are completed, there will be a question-and-answer session. At that time, further instructions will be given. Should any participant need assistance, please press \*0 to reach the operator.

We have a simultaneous webcast that may be accessed through the company's website, [www.smiles.com.br/ir](http://www.smiles.com.br/ir). The slide presentation may be downloaded from this website, please, feel free to flip through the slides during the conference call.

Before proceeding, let me mention that forward-looking statements are being made under the Safe Harbor of the Securities and Litigation Reform Act of 1996. Forward-looking statements are based on the beliefs and assumptions of Smiles' 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 Smiles and could cause results to differ materially from those expressed in such forward-looking statements.

Now, I will turn the call over to Mr. Leonel Andrade, Smiles' Chief Executive Officer. Mr. Leonel, you may begin your conference.

**Leonel Andrade:**

Hi, good morning, everyone. It is a pleasure to share with you Smiles' results for the 2Q14.

I would like to start with a few highlights for the period on the slide three. First is that Smiles presented a net profit of R\$64 million that represents a net margin of 42% in the quarter, were similar to the previous year. It is good that we have maintained flat our margins in a good level.

Other great highlight is our, excluding Gol gross billings that grew 25% compared to the same period, quarter last year and almost 10% compared to the last quarter, it is a sign of a good relationship with our financial partners.

The growth in international partners' redemptions is another important factor. We have been preparing ourselves by seeking new alliances. It is fundamental to our share or high income customers in the upscale segment in the banks — especially in the bank. We grew almost 200% comparing to the year and our redeemed miles of that represents almost 17% of our redemptions.

In other words, we are enhancing our process attributes and diversifying our redemptions. Our focus on customer experience is to generate value and we launched our new Smiles Shopping platform. Now, we have full management of our e-commerce

for product and this Shopping will allow our customers to redeem their miles for more than 500,000 options.

Another great highlight was the issue of our debentures. Seeking the capital reduction, with the proceeds of R\$600 million at 115% of the interbank rates in Brazil, we have maintained our commitment of maximizing value to our shareholders.

Going to slide four, I would like to highlight our miles gross by billings and accruals. As mentioned before, we are aligned with the banks and all of them keep a very strong program with us with plenty of initiative.

All of them value us and we are always aligned. The examples we had this quarter with Banco do Brasil and Itaú, which offered very positive incentives to Smiles. We are very proud to present this growth for the miles that we accrue at this moment represents the revenues in the future.

On the slides five, we can see the growth of our redemptions. There was some seasonality and impact from the World Cup in Brazil. This season has passed fast and redemptions came back strongly after the World Cup, when comparing to the 1Q this year.

In terms of customers, we reached 10 million customers, considering Smiles exclusively. We had a huge coalition operation with Netpoints, the biggest in Brazil and we will discuss that ahead in the presentation.

On slide six, we continue pursuing new partners. In the 2Q, we implemented Aerolíneas Argentinas and it has brought us great results. Argentina is the second most important international destination for Brazilians, and Aerolíneas is performing strongly as a redemption option.

We will soon implement two new partnerships. The first one with TAP, the Portuguese airline and the biggest operator between Brazil and Europe. The second company is Alitalia, also important in Europe. Together, with Air France, Alitalia, Iberia, KLM and TAP, Smiles will offer a great availability to customers seeking European destinations.

These partnerships are very important for high-end customers and it gives us great advantage with the banks. It reflects on accrual numbers with banks, it is not a coincidence we grew 25% with banks. We keep our commitment to continue expanding that, probably two or three this year — we are going to announce three or few — two or three new partners this year.

On the slide seven, another great highlight for the quarter was the agreement with Cielo. More than a simple alliance, this business will potentially bring Smiles to all Cielo terminals. Cielo's technology and commercial strength will definitely bring us closer to retailers. The main focus is tourism and entertainment, restaurants, inns, hotels, and we are very satisfied to have this alliance with the biggest acquirer in Brazil.

On slide eight, an update on Netpoints. We remain focused on expanding our operations with Netpoints. We made an excellent investment. Together, Smiles and Netpoints have 18 million customers, more than 18 million customers, certainly the biggest loyalty coalition in Brazil. Our number of exchanges grew more than 400% over last year.

It is important to mention that Marisa stores had already added up in the program successfully since June. Soon, we will be partners with C&C, Casa e Construção, on the retail, and with São Vicente Supermarkets, a good supermarket on the countryside of São Paulo. We have no doubt that these will be the biggest retail company in Brazil in the future.

On slide nine, the next slide, the New Smiles Shopping platform launched this quarter. It gives our customers a lot more choices and it is important for our strategy. You can redeem your miles for products on online stores of Smiles, Wal-Mart and many other important partners.

Just to have an idea, we have 500,000 products available, redemptions grew 87% comparing to last year. So, we remain in line in terms of strategy, seeking growth and market gains, while maintaining positive margins, with a great agreement for retail and value in this integration with Netpoints.

I am sure that our past remains strong and very confident in the future of the Company, and now, Flavio Vargas my colleague, our CFO is going to explain and to talk a little bit about our financial results. Flavio please.

**Flavio Vargas:**

Thank you, Leonel and good morning everyone to participate in this conference call of our 2Q results.

So, jumping to slide 10 and continuing our presentation, we explained the composition of our gross margin. Our 100% miles redemptions kept margins 2 p.p. higher compared to last quarter, generating a gross profit 9.5% higher compared to the last quarter, and more than twice of what we presented last year, mainly to the legacy miles effect.

Our Smiles & Money margins were up almost 10 p.p. higher compared to last quarter. The lower volumes experience allowed us to consume more classical fares and therefore, increasing their share, which lowered unit cost of redemptions and increases margins.

Even though separate Smiles & Money and 100% miles redemption, we can analyze consolidated redemption results in direct margins by the spread between miles and money net revenues and direct costs. On the 2Q this year, we obtained a 45.1% margin, 3.7 p.p. higher than the previous quarter.

Now, jumping to slide 11, breakage revenue was very similar to the last quarter, with the exception of the real expired miles revenue, which were not recurrent with the same intensity this quarter. Our breakage rate remained stable at around 16.9%.

On slide 12, we see the net profit breakdown. Our operational expenses remained under control with an increase of R\$3.1 million mainly due to consulting services provided and marketing costs.

It is worth mentioning that within the R\$33.9 million reported as income taxes, there were R\$3.6 million worth of expenses that will not have a negative effect on our cost

positions, due to the incorporation, operation of these miles of G. A. Smiles that happened last December.

We closed the 2Q14 with R\$64.1 million of net profit, representing a margin of 42.1%, in line with the margins presented on the previous quarters.

On the slide 13, we comment on our stock performance compared to Ibovespa, adjusted for the dividend as a capital reduction that occurred on July. I take the opportunity to mention that the capital reduction was concluded with the distribution of R\$8.17 per share, which is aligned with the commitment to maximize value to our shareholders.

So I thank you all for participating on the conference call and now I open up the floor for the Q&A session. Thank you.

**Catherine O'Brien, Deutsche Bank:**

Good morning. Just had a quick question on the year-over-year increases on airline redemption rate — excuse me — on the airline redemption rate that went from 6 to 16.7 this year, we thought that was very impressive. We were just wondering how much of that was driven by the implementation of your redemption partnership with Aerolíneas Argentinas and if there are any other such partnerships in the pipeline?

**Leonel Andrade:**

We have different coming in the pipeline, we are going to implement Alitalia and TAP that we had announced months ago or weeks ago. And we expected to have two or three new alliances this year. Probably in the next weeks we are going to announce at least one more.

Specifically about Aerolíneas Argentinas, this is a very good partner, we presented something like 20%, 23% last month, and you know Argentina is very important for us as a destination, and we are very positive that this number — we continue increasing this number.

We do not have a guidance, but I think that this is very important in order to bring customers from the bank, because the customers from the banks — the upscale segment — they like to go abroad. So, this is very important for us and this is totally aligned with our strategy. Thank you.

**Catherine O'Brien:**

OK, great. And then if I can just ask one more. How large of an impact do you think your commercial partnership with Cielo have in the 2H14 and 2015. Any numbers you could put around that or any color you can give will be helpful?

**Leonel Andrade:**

I think it is very early to say how much the miles can come from this Smiles partnership. Probably this year, we will be working more in the pilot phase mode. So we will be trying to touch the waters and see what is the kind of products that we can sell, how we can reach the sale, how we can make this sales force engaged.

So, there is still a lot of challenge that we have to face together, to put that together, but we are very optimistic because we have been definitely working on the two very important fundamentals to make the partnership work, which is to use the sales force, so that provides scalability in terms of the roll out of that partnership in the future and we have built the right incentives in terms of how we are going to share the reserve of Cielo.

So, we think the underlying conditions are in the right direction, but I think it is still too early to say how much they are going to represent, we do not expect that to represent a very big impact on the gross billings in the short-term.

**Catherine O'Brien:**

OK, great. And if I could just squeeze in one last quick one. Looking at your new e-commerce platform that offers product redemption as well as the 100 miles or boost redemptions and how would you say that margins on redemptions are on e-commerce platform compared to margins you make on air and travel redemptions and obviously I know it is very early stages, but just kind of, first blush results would be really great. Thank you.

**Leonel Andrade:**

Kathy, thank you for the question. When the e-commerce platform, in fact, we have revamped it, we have launched that one year ago, but after one year in operations we thought that we would have to enhance the platform and try and even to change the business model with the commercial partners.

So, in terms of the actual cost for redemptions, we are pretty much agnostic. We make pretty much the same margin on the products redemptions then with the air redemptions. In fact, considering the amount of the efficiency that we have gained over the last quarters in pricing in the air ticket products — the air ticket products, they represent an even lower per mile or cost on a per mile basis — but our principle here is that we want to be pretty much indifferent, whether the clients chooses an airline ticket or product and the client will have the free will to choose whatever we wants for the redemption.

**Catherine O'Brien:**

OK, great, thank you so much for all the time.

**Participant:**

Yes, good day. Can you please give me an indication of the money revenue or Smiles amount, what the pickup has been of that after the World Cup and what you guys expect for the rest of the year?

**Leonel Andrade:**

Thank you very much for the question. Well, if we look at the results this quarter, we recognize the Smiles & Money was soft, especially when you compare with the 1Q14, which was very, very strong. The way that we have positioned the product, Smiles &

Money, it is like a cyclical product, because when you have a lot of redemptions and a lot of demand, Smiles & Money is a very great value option for the clients and then you would stimulate the redemptions.

What we have seen over the 2Q is that this was a soft quarter in terms of the demand. On top of that, we had a lot of promotional activities, probably more than 35% of the tickets we sold during the quarter were promotional tickets, so that reduces the value proposition and how the clients perceive the value of Smiles and Money and that has led to a softer result.

What we are seeing over this July and we expect that to continue this quarter is that the amount of sales on the Smiles & Money have resumed to what we consider to be a more normal level — probably not what we have demonstrated in 1Q, but still very decent result and at a different level than what we had in the 2Q.

**Participant:**

Thanks.

**Participant:**

Hi, there. Thank you. Just to follow up on the earlier question on the redemption for your international partners. Could you give a rough sense of how the breakdown between Iberia, Air France etc.? Is it roughly split evenly? And then could you also elaborate on the discounts implied in those tickets, if you could share any information on that that would be helpful.

**Leonel Andrade:**

OK. We do not provide a breakdown of how much each of the Airlines, but a very decent assumption is, that amount of redemption is proportional to the size of the flights coming in and out from Brazil. So, probably, we have to rank Delta, Air France, KLM, and Aerolineas are at a different level than Qatar and Iberia.

What we have in pipeline and Leonel mentioned during his presentation, TAP is going to be a very important partner because they have most of the flights from Brazil to Europe, they are operated by TAP.

So, we are very optimistic about the potential of having this new partner with us.

In terms of the amount of spreads that we are able to comment on those redemptions, they are probably in line with what we have with Gol. We have recently, in fact, as of today, we have raised the prices for the consumers for the redemptions on the international carriers, because we realize that we have a better demand, but still, we do not control all the supplies, so we recognize that this was an opportunity.

But in terms of the general margin that we can comment on this product, the value for the client is good, but we have a very competitive cost on the other side to allow us to provide this value for the consumer.

**Participant:**

Thank you. That is very helpful. If you do not mind, just a quick follow-up on that topic, can you give us a sense for what perhaps the average ticket price was for your international redemptions or what the actual market price would have been for the ticket?

**Leonel Andrade:**

Unfortunately not, but probably we can try to give you a number. We were selling our ticket from Brazil to the US for 25,000 miles and we could make a margin similar to what we had with Gol. So, probably you can reverse and calculate what is the actual price of a ticket. We have the confidentiality on the conference that we cannot disclose.

**Participant:**

Understood. Thank you.

**Operator:**

As we have no further questions, this concludes the question-and-answer session. At this time, I would like to turn the floor back to Mr. Leonel Andrade for any closing remarks.

**Leonel Andrade:**

Thanks a lot. I would like to give just some comments. I think that we have a very good 2Q, especially considering the margins. We remain sustaining our margins. The accrual was very good, especially considering the gross billing from the banks. And the international partners, in terms of redemptions, was very good news.

On the other hand, we know that we need to improve our performance in terms of the Smiles and Money which was very impacted by the World Cup and the good news is that in July we had recovered this performance, now we are in line with the previous performance.

July was, in fact, a very good month considering the accrual, redemptions, Smiles & Money performing, which is good. And we need to pay attention in terms of promotions in order to sustain and increase our pricing to the banks and to the markets in terms of miles issued.

But I am very confident in our future. I know that we are going to have a very good performance in the next quarter, and I am very confident with my team. Thanks for the support from you, the shareholders and the analysts. So, you can count on us.

Thank you very much again.

**Operator:**

Thank you. This concludes today's Smiles 2Q14 results conference call. You may disconnect your lines at this time.

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