dLocal Q2'23 Earnings Call

Webcast Presentation

Q2'23 Earnings Call Prepared Remarks August 16, 2023 8:00 am ET

Slide 3

Good morning everyone and thank you for joining the Second Quarter 2023 Earnings Call today. If you have not seen the Earnings Release, a copy is posted in the Financials section of the Investor Relations website. On the call today, you have Sebastian Kanovich, co-Chief Executive Officer; Sergio Fogel, co-President and Chief Strategy Officer; Diego Cabrera Canay, Chief Financial Officer, Maria Oldham, SVP of Corporate Development, Investor Relations and Strategic Finance and Soledad Nager, Head of Investors Relations.

A slide presentation has been provided to accompany the prepared remarks.

This event is being broadcast live via webcast and both the webcast and presentation may be accessed through dLocal's website at investor.dlocal.com. The recording will be available shortly after the event is concluded.

Before proceeding, let me mention that any forward-looking statements included in the presentation or mentioned in this conference call are based on currently available information and dLocal's current assumptions, expectations and projections about future events. While the Company believes that our assumptions, expectations and projections are reasonable given currently available information, you are cautioned not to place undue reliance on those forward-looking statements. Actual results may differ materially from those included in dLocal's presentation or discussed in this conference call for a variety of reasons, including those described in the Forward-looking Statements and Risk Factors sections of dLocal's filings with the Securities and Exchange Commission, which are available on dLocal's Investor Relations website.

Now I will turn the conference over to Sebastian Kanovich. Thank you.

Slide 4 and 5 - Sebastian Kanovich, co-CEO

Good morning, everyone. Thanks for joining the call today. Before we start the call, let me thank all of you who joined the Investor Day back in June. For those who couldn't make it, the material is available on our Investor Relations website.

Let me also add that we have in the call Pedro Arnt, who will be joining me as co-CEO. We are extremely excited to have Pedro joining the team. We are proud of the great talent that we have at dLocal and bringing Pedro is the ultimate example of this. Pedro will bring new energy and leadership and a highly complementary set of skills to the company, helping us to continue scaling the business at pace and to realize the enormous opportunity that we have ahead of us. I would now like to invite Pedro to introduce himself.

Pedro Arnt, co-CEO

Thanks Seba. Greetings everyone. We thought it would be useful for me to introduce myself today, and share with you what led me to join Seba, Sergio, Jacobo and the rest of the great team here at Dlocal. They will then walk you through dLocal's strong business performance, as they expertly do every quarter.

Having worked in Latin American tech over the last 25 years, I have obviously been aware of dLocal since its inception, merely 7 years ago. However, upon being approached by the Board and undertaking my diligence, what I found was a set of business success drivers even more remarkable than I had initially anticipated. I'd like to spell some of those out for you today: 1) A vast untapped Total Addressable Market (TAM) of 1.4 trillion dollars within the rapidly expanding markets that we currently serve. 2) An exceptional opportunity for growth alongside these markets, as well as the potential to extend our reach to numerous additional markets, and this allows us to increase our TAM by over 2.5 times over the next five years. 3) The product and technology stack is fantastic as it serves many of the world's leading, and most demanding Mega Cap tech companies. 4) This is an entirely customer centric organization that is obsessively dedicated to our customers' success, and continues to pile up client win over client win, growing clients by 41% CAGR and TPV by a phenomenal 126% CAGR over the past 3 years. And last, but certainly equally important, an extremely attractive financial model characterized by a Revenue CAGR of 101%, Adjusted EBITDA over gross profit surpassing 70%, and an annual conversion of free cash flow to Net Income exceeding 90%.

So, in essence, large TAM, great product and tech stack, a winning, customer focused organization, and a free cash flow machine. An investor's ideal vision realized, right? Absolutely!

BUT, like with any young successful company, there is always more work that can be done, so as to further, and fully realize, the extraordinary value inherent in the exceptional business I have just described to you.

That work is already underway, and it is also where I hope to contribute the most in phase one of my journey here. I am confident we will find ways to accelerate even further the pace at which we are rolling out additional processes, deploy more, and even better systems, and adapting our organizational design to prepare dLocal for the future. I am excited to see how all this will complement the extraordinary product and customer success work that is already being done on behalf of our clients, to further build a formidable company at scale.

And, as all this happens, I firmly believe that as we undertake these measures, we will propel dLocal's trajectory and further unlock returns for all stakeholders involved.

I look forward to engaging with you as we carry out this journey.

Let me know turn the floor over to Seba again to go deeper into the results of this quarter, that already show the positive direction things are headed in.

Sebastian Kanovich, co-CEO

Thank you Pedro and once again, welcome to the team.

I am pleased to share that we had another quarter of outstanding results. Our performance once again proves the distinctive strengths of our business, which we continue to build, focused on long-term profitable growth. These strengths combine:

- One: superior technology, that is driven by our commitment to make the complex simple for our merchants with our one API and one integration, what we call One dLocal;

- Two: a well diversified business across verticals, products and geographies, with vast geographic coverage of over 40 countries;

- Three: relentless execution of our merchant growth and cross-sell strategy across products and geographies;

- Last but not least - our lean and disciplined culture. We deliver all the previous strengths with a lean team, continuously striving for excellence. Our culture is key to continue delivering our long-term ambitions.

These factors underpin our continued success in building the best payments ecosystem across emerging markets based on our One dLocal, navigating the complexities of payments in these markets on behalf of our merchants, so they can remain focused on their core business. We have a proven track record in leveraging these factors to deliver robust dollar growth of TPV, revenue, gross profit, adjusted EBITDA and net income.

Slide 6 - Sebastian Kanovich, co-CEO

Moving to our financial highlights of the quarter, this success was reflected across all metrics. TPV grew 80% year-over-year and a strong 22% quarter-over-quarter, surpassing for the first time the 4 billion dollar mark. To put this in perspective, this quarterly TPV is more than double our TPV for the whole year of 2020, the year before we went public.

We continue to focus on growing our business in absolute dollar terms. Revenue, gross profit and Adjusted EBITDA all increased at double-digit rates both year-over-year and quarter-over-quarter. We recorded the highest contribution in gross profit and Adjusted EBITDA of the past 8 quarters, increasing $9M in gross profit and $7M in Adjusted EBITDA quarter-over-quarter.

We remain firmly committed to profitable growth at scale. In Q2 2023, our ratio of Adjusted EBITDA to Gross Profit remained stable quarter-over-quarter at 74%, which is best-in-class.

Slide 7 - Sebastian Kanovich, co-CEO

Moving to the next slide, we continue to invest thoughtfully in expanding our global team. We have hired new talent to pursue the opportunities we see in the market, also strengthening our foundations to face our long-term ambitions.

We grew our team to 806 employees, this is an increase of 174 FTEs compared to the second quarter of 2022, or by 28% year-over-year. We continue to recruit talent globally, combining specific experience and skill sets, as well as on-the-ground knowledge. We reached 202 FTEs in Africa and Asia by the end of Q2 2023. This now represents 25% of our workforce.

We will continue to invest in talent in a disciplined way, staying lean and always ensuring that we onboard talent that has a strong cultural fit. We are proud of our team and believe it is stronger than ever.

Now I will pass on to Maria to discuss our execution on our growth strategy.

Slide 8 - Maria Oldham, SVP of Corporate Development, Investor Relations and Strategic Finance

Thank you Seba. Hi everyone.

Let me remind you how we view our growth engine. We have 3 axes of growth: 1. Products, 2. Merchants, and 3 Geographies.

On Product - during the quarter we continued to focus our efforts on deepening our presence in the countries in which we operate, with a particular focus on Africa and Asia, by establishing more direct connections with payment methods and acquirers and continuing to enhance our solution. During the second quarter of 2023, we saw strong traction on our platform solution, in particular from marketplaces.

On merchants - we delivered strong revenue growth both from existing and new customers. Net retention rate continues to be best-in-class, at 148% in 2Q23. New merchant revenue reached $11M in Q2 2023. We have very close relationships with our merchants, which enables us to grow together with them. Our top 10 merchants continue to show very high growth, totaling $94M revenue in the quarter.

Our 3 axes of growth compound to deliver rapid growth. All of our merchants, products, payment methods and markets are linked to one API. This means that merchants can access all of our products and payment methods without any additional work, generating high value to our customers while growing our business.

Slide 9 - Maria Oldham, SVP of Corporate Development, Investor Relations and Strategic Finance

Let's deep dive into one of the dimensions - Geographies.

In Latin America, where we have our largest scale, we continued to experience strong growth across the region in Q2 2023, this proves that we still have ample room for growth in Latam, both with existing and new merchants.

In the last twelve months to Q2 2023, revenues in Mexico increased by 85% YoY and in Brazil by 50% YoY. Growth in both countries has been driven mostly by merchants from commerce, advertising, streaming and ride-hailing verticals. We have been operating in both countries since 2016, so these sustained growth rates are a true indicator of the hyper-growth potential that we still have in Latin America even in our most mature markets.

As you know, Brazil is where we started, 7 years ago. It is also a highly developed market in terms of digital payments penetration and technology. But this market is far from mature from a growth opportunity standpoint. This high growth in a large and competitive geography such as Brazil underscores the quality of our solution as we continue to gain share in the market. We continue to see strong growth opportunities in Brazil going forward.

In Q2 2023, TPV and revenue in Brazil doubled year-over-year and increased by around 80% QoQ. Recent growth has been mainly led by merchants in the commerce, advertising and streaming verticals. In Brazil we also proved the success and robustness of our local-to-local solution. Brazil is a market with higher local-to-local share, and we have seen favorable trends in both cross-border and local-to-local flows.

Slide 10 - Maria Oldham, SVP of Corporate Development, Investor Relations and Strategic Finance

Moving on to Africa and Asia, our merchants continue to signal strong demand for our solution in the region. Egypt, Morocco, Indonesia and Philippines, are growing triple digit year-over-year and have the potential to become a significant part of our business.
Our business in Africa and Asia continues to grow very fast; in the last twelve months to Q2 2023 revenues in Africa and Asia increased more than three times YoY. Excluding Nigeria, this region grew 78% YoY in the last twelve months to 2Q 2023.

In 2Q 2023 Nigeria revenues increased by more than 4 times year-over-year. The quarter-on-quarter deceleration was driven by the Naira devaluation in the last 15 days of the quarter. Nevertheless, Nigeria continues to present similar net take rates as other markets and is a key geography for dLocal. We continue to see great growth opportunities in this market. Excluding this effect, revenues would have been in line with Q1 2023. Sergio will shed more light on recent market changes later on in the presentation.

Slide 11 - Maria Oldham, SVP of Corporate Development, Investor Relations and Strategic Finance

Moving to the next slide, this case study illustrates the powerful combination of our 3 axes of growth.

We onboarded this merchant, a global e-commerce platform, prior to Q2 2021. We started processing volume for this merchant outside Latin America, in one country, and only one product. Over the last few years we have been able to successfully cross-sell new geographies, products and services.

The outcome speaks for itself: TPV has grown by more than 100 times since Q2 2021 driven by a combination of: organic growth of our merchant; increased share of wallet; and additional payment methods, solutions and geographies. We now process volume for this merchant in 7 countries across Africa and Latin America and on top of processing pay-ins and pay-outs, this merchant uses our platform solution in some of these geographies. We have seen strong growth coming from the platform solution as we developed tailor-made solutions at scale, including: 1) a white-label seller onboarding KYC and 2) a split payment solution to ensure full flow compliance throughout the process and best user experience.

This example is a testament to the fact that our business is built on the great relationships and customer service we have with large, global merchants, who continue to choose our solution and grow together with us.

Sergio will now discuss our emerging markets focus in more depth and share a few updates on some of our key markets.

Slide 12 - Sergio Fogel, co-President and Chief Strategy Officer

Thank you Maria. Good morning everyone. As you know, I have co-founded the company and have been serving as a board member. Since June this year I have been part of the executive team. I am delighted to join this earnings call today and look forward to continuing meeting many of you.

dLocal has been fully devoted to emerging markets since its inception. Where others see complexities, we see underserved markets with high growth potential. Buyers and sellers cannot transact due to the lack of infrastructure, and the magnitude of lost opportunities is overwhelming. We are going after a very large market, and after 7 years of strong growth, we are still only scratching the surface of the opportunity.

Our markets enjoy structural tailwinds: a young, growing population; an urban, connected middle class eager to consume and merchants that are only starting to customize their products for their needs and tastes.

Emerging markets are complex. Our mission is to solve payments complexities for our merchants, including technological, operational and regulatory complexities. Our ability to adapt to changing circumstances is one of our key operational strengths and underlies our value proposition of taking the complex and making it simple.

Now I’d like to update you on recent developments in 3 specific markets.

One such change in market conditions occurred in Argentina, as we stated in the filing, in late April. The Government and the Central Bank established new procedures to obtain foreign currency for the settlement of certain services.

We have been operating in Argentina for many years now, and we have seen many, many changes in regulations. This is only the latest change, and will not be the last. We will adapt to the new rules just as we have adapted to the previous ones. Our ability to do so is a competitive differentiator and an example of the value we add to our merchants.

Given the magnitude of our business in Argentina, as we announced in a press release in June, we committed to show additional economic substance in the country. On June 14, we acquired with our own funds $48M dollars worth of Argentine dollar-linked Treasury bonds. We acquired an additional $49M by the end of July. We plan to use these funds in the following years to fund our local operations and investment opportunities in the market. We continue to collaborate with local authorities in Argentina, to ensure that despite the macroeconomic situation, Argentinian consumers are able to access international services.

Moving to Nigeria, in mid-June, the Central Bank implemented a free-floating policy of the Naira, leading to the devaluation of the local currency, as Maria mentioned. I would like to highlight that we see the unification of the exchange rates as a positive for the country and for our business, as it promotes transparency and efficiency and it increases liquidity. This removes a lot of the friction that some of our customers see when expanding to Nigeria. We continue to operate normally in the country where we serve some of the world’s largest technology merchants.

We do not expect the depreciation of the Naira to have an impact on our gross profit. The negative impact on gross revenues, will be offset by lower expatriation costs.

We continue to have a bullish outlook on the operations in Nigeria for the long-run and continue to onboard and grow with merchants in the country.

Last but not least, Brazil.

Shortly after the end of Q2, we reached another milestone in our evolution in the country. At our investor day, we shared that we applied for a payment institution license in Brazil. I am thrilled to share that we were granted this license in July. We can now offer more payment methods and solutions in Brazil and participate directly in Brazil’s payment systems. We expect this to increase the efficiency of our operations in the country. Becoming a payments institution carries with it a higher level of scrutiny by Brazil’s Central Bank. We welcome such scrutiny (in Brazil and in other countries), as it helps boost the level of confidence of global merchants doing business in EMs, and also increases our competitive advantage. This is a clear example of our ongoing efforts to further strengthen our compliance infrastructure across emerging markets.

Being well diversified in 40+ emerging markets allows us to continue benefiting from very high growth regardless of the specific circumstances in any given geography. This is a key strength of our business.

Diego will now review our financial highlights.

FINANCIAL HIGHLIGHTS

Slide 14 - Diego Cabrera Canay, CFO

Thank you Sergio. Hi everyone.

We had another quarter of strong growth across our products and services. In terms of products, during Q2 2023 pay-ins increased by 70% YoY and by 27% QoQ and pay-outs increased by 114% YoY and 10% QoQ.

The contribution from pay-outs has increased YoY, as we have been successful in providing last-mile payment services to financial services companies in emerging markets. Moreover, we continued to position ourselves as the payments services provider of choice in emerging markets for global payroll, social media, ride hailing and on-demand delivery companies.

During this quarter we also saw strong traction both in pay-ins and pay-outs through our platform solution for marketplaces, particularly in e-commerce in Brazil and Mexico.

In terms of services, our cross-border and local-to-local volumes showed solid growth YoY and QoQ. In Q2 2023, we increased by 33% our local-to-local volume QoQ, mainly driven by merchants from commerce, advertising and ride-hailing verticals. This resulted in growth in our local-to-local share, reaching 49% in Q2 2023.

We are product and vertical agnostic - all our products and services bring incremental profit and when we combine them, they bring synergies both for our merchants and for us. Depending on which merchants we onboard in a given quarter, as well as the relative growth rates of each merchant, there may be fluctuations in the share of pay-ins vs. pay-outs and cross-border vs. local-to-local. Overall we see a positive growth outlook across all our products and services and see this diversification as a key strength.

Slide 15 - Diego Cabrera Canay, CFO

Revenues also reached a record high of 161 million dollars in Q2 2023, growing 59% YoY and 17% QoQ.

During this quarter we saw strong quarter over quarter revenue growth particularly in online commerce, ride hailing and on demand delivery, and from a geographical standpoint, revenue grew quarter over quarter mainly from processing payments in Brazil, Mexico, South Africa, Egypt, Colombia, Peru and Costa Rica.

We remained focused on growing absolute gross profit dollars which is the key success metric of our business. Our gross profit reached 71 million dollars in Q2, up 43% YoY and 14% QoQ, with net take rate at 1.6%. Processing costs over TPV remained stable at 2.0% QoQ.

Slide 16 - Diego Cabrera Canay, CFO

Gross profit margin and net take rate remained almost unchanged quarter-over-quarter, even with a high increase in the share of local-to-local volume.

The waterfall chart on the left shows the main changes in our gross profit margin QoQ. Gross profit margin was positively impacted by changes in merchant mix, particularly in Brazil. This was offset by the higher share of pay-ins and local-to-local volume and lower share of revenues in Argentina.

Moving to the right hand side of the slide, the slight decrease in the net take rate from 1.7% in Q1 2023 to 1.6% in Q2 2023 was driven by similar factors, particularly by the higher share of local-to-local volume and by country mix, with higher share of revenues in Brazil and Mexico and lower in Argentina.

Slide 17 - Diego Cabrera Canay, CFO

Profitability remains a top priority. During the quarter we were able to grow our Adjusted EBITDA to 52 million dollars, up 36% YoY and 14% QoQ.

Adjusted EBITDA margin was 32% in Q2. Our Adjusted EBITDA over gross profit remained stable QoQ at 74% as we continued investing in our people, both in terms of compensation and expanding the team.

Net income totaled 45 million dollars during the quarter, growing by 46% YoY. Sequentially, it increased by 26% QoQ.

Net income for the quarter includes 7.5 million dollars of net financial gains. These results were driven by our funds held in interest bearing accounts and money markets partially offset by the financial cost of hedges across the markets.

We also observed an increase in our effective income tax rate, from 11% in Q1 to 16% in Q2, driven by a higher share of profits in local markets, as a result of higher local-to-local TPV and financial gains.

Slide 18 - Diego Cabrera Canay, CFO

Let's move to cash generation.

During the first six months of the year, we observed strong cash flow generation.

The main drivers of our cash increase were our net income, which substantially converts to cash, and an increase in net trade payables, particularly as a result of the growth of our business with negative working capital and higher average settlement periods to our merchants. This resulted in an increase of $141 million dollars.

We invested 61 million dollars in completing our share repurchase program and 48 million dollars in Argentine dollar-linked treasury bonds, as part of our commitment to increase our economic substance in the country.

We believe our strong cash position remains a competitive advantage as it allows us to continue investing in the business.

Seba, the floor is yours.

Slide 19 - Sebastian Kanovich, co-CEO

Thanks Diego. We are very proud of the strong set of results we delivered during the first half of the year and we are even more excited about the runway ahead of us. We see continued growth of our business in the second half of the year.

Given the outstanding first 6 months performance, we would be on track to over-deliver on our guidance on Revenue whilst being in line on EBITDA. However, due to the currency depreciation in Nigeria (which will reduce Revenues with neutral impact on Gross Profit - In other words, it won't affect our gross profit dollar amount), we expect to end the year in line with guidance in terms of both Revenue and EBITDA - Revenue between 620 and 640 million dollars and adjusted EBITDA in the range of 200 million dollars to 220 million dollars. We have a truly diversified business that can deliver on our goals under changing specific circumstances in certain markets, and we are very very pleased to be in such a position.

We remain dedicated to building the best financial infrastructure for global merchants in emerging markets. The value proposition of our One dLocal platform is clear - to help our merchants navigate local complexities in receiving and sending payment in emerging markets. Everything that we do is focused on further improving this value proposition.

I want to send a big thank you to our global team, our customers and our investors for their continued support.

I'll now hand back to the operator to open up for the Q&A, which Pedro will also be joining.