Q3 2024 Earnings - Transcript

Webcast Presentation Q3 2024

Earnings Call Prepared Remarks November 13, 2024 6:00 pm ET

Good afternoon everyone and thank you for joining the Third Quarter 2024 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 Pedro Arnt, Chief Executive Officer; Mark Ortiz, Chief Financial Officer, Maria Oldham, SVP of Corporate Development, Strategy and Investor Relations; and Mirele Aragão, Head of Investor 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 dLocal. Thank you.

Pedro Arnt, Chief Executive Officer

Thanks everyone for joining us today.

Let me begin with a quick overview of our main highlights for the quarter.

We are encouraged by how we see the business evolving. After an admittedly soft first quarter, we see ourselves consistently gaining momentum. Despite a tough 2023 comparison, driven by extraordinary gains in Argentina, we have once again returned to delivering a quarter of record results in Total Payment Volume and Gross Profit. Our margins, cash position, and cash conversion have all improved quarter after quarter throughout 2024. A year that started off admittedly weak, has gained positive momentum.

Let me go into greater detail now, starting off with our top line results. We continue to deliver significant growth, with TPV re-accelerating to over 40% year-over-year, driven by our continued ability to expand our share of wallet of our existing global merchant base, as well as onboard new merchants. Both things underscoring our position as a trusted partner for global companies seeking to do business across emerging markets. Our performance this quarter was strong across diverse verticals, countries and products, notably:

- We ramped up operations in more countries, offered more payment methods and gained share of wallet across important logos in the financial services, SaaS, on-demand delivery, advertising, ride-hailing and commerce verticals.
- We increased payments volume in Argentina, Mexico, Egypt and Other Latam - mainly in Colombia and Peru - as well as Other Africa and Asia, with strong performance in South Africa.
- We reported record volume in our higher take rate cross-border (XB) business, surpassing the $3 billion quarterly mark in flows for the first time.

Our pipeline remains robust, including both growth opportunities with existing merchants as well as new merchants. During the period, we successfully integrated major players, including MoneyGram, one of the largest global providers of money transfer and payment services, and other significant remittance companies to serve them across countries in Latam, Africa and Asia. We also continued to ramp up volumes with one of the main Asian commerce players, expanding the regions in which we serve them, and have now gone live in Brazil with one of the largest global fintech companies, also out of Asia.

Moving on to profitability, this quarter's results showcase the resilience of our business model. We reached record gross profit of $78 million with net take rate stable at 1.2% since Q1 2024. This is a consequence of our differentiated value proposition, continuous pursuit of cost efficiencies such as renegotiation with processors, and the real value in solving complexities across emerging markets for our global merchants, which grants pricing power and differentiates us from more commoditized payments offerings in the developed world. We achieve those results despite weakness in most emerging market currencies. From a currency perspective, applying constant currency growth rates across our main markets - Brazil, Mexico, Argentina, Egypt and Nigeria - our gross profit would have been approximately 6% higher during the third quarter 2024 or over 18% quarter-over-quarter growth and TPV growth would have been 14% quarter-over-quarter.

Our Adjusted EBITDA reached $52 million, despite continued investments in our engineering team, back-office capabilities and our license portfolio, all crucial for our long-term success. Although Adjusted EBITDA was down year-over-year, this represents the second consecutive quarter of increased operational leverage, with adjusted EBITDA over gross profit margin now at 67%. This demonstrates the operational leverage inherent in our business model, general philosophy of expense control and disciplined investment to deliver our long-term growth ambitions.

Cash generation, another strength of our financial model, was also solid. During the past 3 months we had net cash from operating activities, excluding merchant funds, less CAPEX amounting to $26 million, a cash conversion of practically 100% to Net Income.

Now I would like to cover some technology and product development deployments during the quarter, that shed further light on what our core offering is, and how we differentiate from competitors. For context, always remember that the backdrop of where we operate is an emerging market landscape where payments are still characterised by three main factors: fragmented, costly, and lower performing.

During this quarter, we have launched our Smart Requests functionality, boosting our transaction performance, thereby improving conversion rate by an average of 1.22 percentage points. This may sound minor but this actually represents in practical terms 1.2% additional revenue to our merchants. Smart requests rely on per country machine learning models that optimise routing and chaining so as to maximise authorization rates.

We have also continued to develop increasingly advanced real-time cost calculation models to optimise processing costs, which also contributed to our gross profit achievement and stable net take rate.

A third area of innovation has been our launch of new and promising alternative payment methods (APM). As part of our ongoing efforts to deepen our infrastructure in various countries and add more value to our merchants, we have successfully deployed integrations with Nupay in Brazil for global merchants. This represents an expansion of our payment method footprint with this widely adopted and advanced feature-set APM.

Finally, we launched a new product to our suite of offerings, a stand alone Payment Orchestration option, which allows merchants to retain our Smart Routing, fraud detection, and unified reporting, while obtaining their own licences and contracting directly with processors in each market. Although this model may result in a lower net take rate net of acquiring costs, it enhances our ability to capture share of wallet with relevant clients, and continues to add value to merchants through our single API connection and product functionalities, while delivering optimised conversion and cost results.

All of these improvements to our platform, as well as the development of new solutions, serve to deepen our competitive advantages in our markets, enhance the stickiness of our products, and potentially bring future revenue streams.

Lastly, we continue to invest in expanding our licences portfolio, obtaining (i) International Money Transfer Operators licence in Nigeria; (ii) Financial System Auxiliary Services licence in Ecuador; and (iii) Payment Service Provider and Payment System Operator licences in Uganda. We continue to see this growing portfolio across complex and volatile emerging markets as very valuable IP, and adding to it every quarter as a deepening of competitive advantages.

Wrapping up; we are delivering on the outlined plan for sequential performance after Q1, consistently hitting record TPV, holding the line on take rate declines, best gross profit ever for a quarter and improving margins through reduced absolute dollar OPEX. In short, things are trending in the right direction.

With that, I'll hand it over to Maria to take you through a more detailed overview of our third quarter results, and then to Mark to walk us through key financials.

Maria Oldham, SVP of Corporate Development, IR and Strategy

Thank you Pedro. Good afternoon everyone.

As Pedro mentioned, despite some softness in Brazil, our third quarter results show healthy growth and momentum. We achieved TPV of $6.5 billion, up 41% year-over-year and 8% quarter-over-quarter.

From a business line perspective, our cross-border flows grew 12% quarter-over-quarter and 35% year-over-year, reaching $3 billion in TPV, mainly driven by the commerce, financial services, on-demand delivery and SaaS verticals.

Our local-to-local TPV increased by 4% quarter-over-quarter and 47% year-over-year, with strong performance in Mexico and Argentina. We experienced sequential slowdown in growth in Brazil driven by a loss of share of wallet in credit cards with a top commerce merchant, as they were granted a payment licence and were required to connect directly with acquirers in order to remain compliant.

On a positive note, we see potential to reignite growth with that specific merchant through a pipeline that includes alternative payment methods and onboard them to our new standalone Payment Orchestration option that Pedro described earlier. Excluding the impact of this merchant, TPV in Brazil would have been up 8% quarter-over-quarter, driven by the advertising and commerce verticals.

Our pay-ins business grew 8% quarter-over-quarter and 35% year-over-year, with strong performance in Mexico, Colombia, Argentina, South Africa and Egypt across various verticals.

Our pay-outs business grew 7% quarter-over-quarter and nearly 60% year-over-year, driven by financial services and remittances.

Revenue

Moving to revenue, we achieved $186 million in Q3, representing a 13% year-over-year growth. This is driven by:

- Egypt, with volume growing over 90% year-over-year;
- Mexico, with positive performance in the commerce and financial services verticals;
- And Other markets, particularly Colombia and South Africa with strong growth across commerce, and ride hailing verticals.

These positive results compensated for lower revenues in Nigeria due to Naira devaluation in February 2024 and in Brazil, as previously explained.

On a quarter-over-quarter basis, revenue followed the TPV trend, growing 8%, driven by the performance in Argentina and Egypt, with volumes increasing by over 30% in the period; as well as positive results in Other Latam and Other Africa and Asia.

Gross Profit YoY

Now moving to gross profit dynamics.

During the quarter, gross profit reached a record level of $78 million, up 5% year-over-year despite the hard comparison with Q3 2023.

Starting with LatAm, gross profit was $56 million, down 6% year-over-year, mainly driven by: (i) Argentina, due to lower FX spreads following the currency devaluation in December 2023; and (ii) Brazil, given the repricing with our largest merchant which occurred in Q1 2024 and share losses on credit cards.

This was partially offset by Mexico, where gross profit grew over 60% year-over-year, due to volume growth and lower processing costs from renegotiations with processors in Q1 2024.

In Africa & Asia, gross profit was also stellar, with almost 50% growth year-over-year, mainly driven by (i) our overall TPV growth in Egypt as discussed above; and (ii) TPV ramp-up of our commerce merchants combined with cost optimization in South Africa.

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Gross Profit QoQ

On a quarter-over-quarter basis, gross profit increased by 12%.

In LatAm, gross profit increased by 4% quarter-over-quarter, driven by Mexico and Other Latam markets - where we experienced $2 million growth from widening FX spreads, that may eventually fade away in the case of currencies devaluation. These positive factors were partially offset by (i) Brazil, given the share losses on credit card payments of a top merchant; and (ii) Argentina, as we had higher expatriation costs.

In Africa and Asia, gross profit increased by 39% quarter-over-quarter, due to the same factors just discussed in the year-over-year comparison.

As you can see by these results, Q3 continued to build on the growth of Q2, and delivered record Gross Profit despite the softness in Brazil, demonstrating increased diversification on a geographic and merchant basis. As our business continues to scale, we expect to reduce volatility on our top and bottom line.

In addition, please note that we provide detailed information, on a country-by-country basis to help you better understand the drivers behind our results. That said, it's important to emphasise that our business is ultimately driven by the volumes our merchants entrust to us and the unique dynamics of each of our markets. We encourage you to view our performance holistically, as this perspective best reflects the quality and resilience of the business as a whole.

Let me now hand it over to Mark to continue discussing our financials.

Mark Ortiz, Chief Financial Officer

Thank you, Maria. Hi everyone.

As discussed in previous quarters, we continue to invest in our capabilities and innovation to drive efficiencies across various areas of our business. We have maintained investments in key areas critical to our future growth while balancing out other expenditures given our top line path.

With this, for Q3 our total operating expenses reached $37 million, a 6% decrease quarter-over-quarter and a 61% increase year-over-year. Most of the OPEX growth continues to be mainly allocated to Product Development & IT capabilities, with these expenses increasing by 88% year-over-year while combined Sales and Marketing and G&A expenses grew by 35%. Pedro highlighted in his opening remarks some of the projects our tech and product teams have been working on during the past few months. We expect this allocation tilt toward Product and IT to continue in the future.
The 6% decrease quarter-over-quarter is a reflection of our continued disciplined approach to expense management after weaker than expected results in the first semester.

Through re-ignited growth and cost management, we delivered an Operating Profit of $41 million for the quarter, up 36% quarter-over-quarter, and Adjusted EBITDA of $52 million, up 23% quarter-over-quarter, representing an Adjusted EBITDA margin of 28%. This marks the second consecutive quarter of increasing Adjusted EBITDA and Adjusted EBITDA margin. The ratio of Adjusted EBITDA to Gross Profit followed a similar trend, reaching 67% for the quarter, up 6% percentage points quarter-over-quarter.

Tuning now to Net Income, Net income was $27 million for the quarter, down 42% quarter-over-quarter and 34% year-over-year. The earnings presentation provides a detail of the quarter-over-quarter evolution of net income which was mostly impacted by lower finance results, more specifically:

- The positive $23 million non-cash mark to market effect related to the Argentine bond investments in Q2 2024, as mentioned last quarter; and
- Higher finance costs this quarter mainly driven by exchange differences and higher cost of hedges.

Adjusted Net Income, which excludes the impact of the Argentina bonds and intercompany loan was $43 million for the quarter, down 5% quarter-over-quarter.

Our effective income tax rate decreased to 8% from 18% last quarter, primarily driven by lower pre-tax income in Argentina. On a year-to-date basis, our effective tax rate stands at 18%.

Moving on to cash flow for the quarter, net cash from operating activities, excluding merchant funds, less CAPEX amounted to $26 million, up from $19 million in Q2 2024, representing a 37% increase.

With that, we continue to hold a strong liquidity position of $320 million, including $208 million of available cash for general corporate purposes, and $112 million of short term investments, even after the $100 million share buyback executed this year.

With this, let me hand it over back to Pedro for closing remarks.

Pedro Arnt, Chief Executive Officer

Thanks Mark.

Before we conclude our presentation, I would like to state that our guidance remains unchanged in light of our Q3 2024 results and what we have seen through Q4. However, it is important to reinforce that Q4 results are heavily weighted towards the next 3-4 weeks, given the expected seasonal lift in commerce volumes and Black Friday.

Now, let me wrap up our earnings call by emphasising our long-term optimism, driven by the strength and resilience of our business model.

dLocal is a young and dynamic company, less than eight years old, and yet, during this period, it has delivered extraordinary growth. We have expanded our roster of sophisticated enterprise merchants, increased our share of wallet with them, and built operations across the most relevant emerging markets globally, adding products, new APMs and licences over these years.

Our growth underscores our success in serving and supporting these most demanding digital merchants with tailored solutions that meet their evolving needs. We navigate the highly complex and changing payment landscape and regulatory environments across emerging markets with one of the most complete emerging market processing ecosystems. Our best-in-class orchestration layer, competitive forex liquidity and rates, robust fallback and redundancy features, efficient fraud prevention engines, and

KYC, regulatory, and compliance layers are built to suit each market we serve. The comprehensiveness of our One dLocal solution allows our merchants to add new markets and payment methods at a marginal incremental implementation cost, providing cost-efficient and speedy go to market strategies. This value supports the resilience of our business, despite operating in the volatile global south.

The quarter we have just closed exemplifies both the volatility mentioned and, more importantly, the increasing resilience of our business. Despite softness in our largest market we have delivered record levels of TPV and Gross Profit. We have rebounded from weakness in Q1 to deliver two consecutive quarters of consistent growth in these metrics, as well as in Adjusted EBITDA. This type of sequential growth, when compounded over many quarters, shows the extraordinary potential of dLocal.

Secular trends also favour us. We have a huge and growing TAM underpinned by shifts towards payment digitalization, the growing importance of emerging and frontier markets, and surging demand for cross-border and instant payment methods. Industry forecasts predict the cross-border payments market will reach $65 trillion by 2030, and we are well-positioned to be capturing a reasonable portion of the growth in this immense addressable market. Our ability to innovate and capitalise on these trends, coupled with our financial model characterised by operational leverage and high cash conversion, will fuel long-term value creation for our shareholders and merchants. We are just beginning to realise the compounding nature of this strategy, and we remain steadfast in our mission to deliver on this promise, in all the relevant geographies that our merchants present needs.

Thank you to those who have shown us continued support and confidence. We look forward to updating you on our progress in the coming quarters.

With that, we can now take questions.