



MELI Q2'13 Earnings Conference Script

Date: August 1, 2013

MERCADOLIBRE 2Q13 EARNINGS CONFERENCE CALL SCRIPT

Part I: Introduction and Disclaimer – Investor Relations

Hello everyone, and welcome to the MercadoLibre earnings conference call for the quarter ended June 30th, 2013. My name is Martin de los Santos and I am the head of Investor Relations for MercadoLibre. Our senior manager presenting today is Pedro Arnt, Chief Financial Officer. Additionally, Marcos Galperin, Chief Executive Officer, will be available during today's Q&A session. This conference call is also being broadcast over the Internet and is available through the investor relations section of our website. [PAUSE]

I remind you that management may make forward-looking statements relating to such matters as continued growth prospects for the company, industry trends and product and technology initiatives. These statements are based on currently available information and our current assumptions, expectations and projections about future events. While we believe that our assumptions, expectations and projections are reasonable in view of the currently available information, you are cautioned not to place undue reliance on these forward-looking statements. Our actual results may differ materially from those discussed in this call, for a variety of reasons, including those described in the forward-looking statements and risk factor sections of our 10-K and other filings with the Securities and Exchange Commission, which are available on our investor relations website. Finally, I would like to remind you that during the course of this conference call we may discuss some non-GAAP measures. A reconciliation of those measures to the nearest comparable GAAP measures can be found in our second quarter 2013 earnings press release available on our investor relations website.

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Now let me turn the call over to Pedro

Part II: Overview & Financial Results – Pedro Arnt

Good afternoon everyone, and, as always, thanks for joining us.

I would like to start today by providing an overview of the solid progress we made during the second quarter of 2013, resulting from a set of well-defined and executed initiatives along different aspects of our ecosystem. Marketplace sold item acceleration for the second consecutive quarter, combined with strong results across the board suggest that the current investment and product cycle around these initiatives is returning positive results. Furthermore, as these initiatives continue to come together, we are increasingly able to deliver what we have said is our primary objective: to deliver a continuously improving trading experience for our users that consequently generates further growth for our business.

I will update you on the specifics that have seen the most progress during the quarter. But first let's take a look at some of our key metrics, showing the results these initiatives are having on our business.

In the second quarter:

- 4.5 million new users registered on our site, growing our base of registered users 23% year on year.
- Successful items grew 27%, reaching 20.1 million, and, we believe, increasing our market share of overall units shipped via e-commerce in Latin America.
- Number of payment transactions grew 35%, to 7.4 million;
- Gross Merchandise Volume was \$1.7 billion, growing 33% in USD.
- And Total payment volume reached \$578 million, growing 40% in USD.

Bear in mind that we achieved these USD growth rates despite currency headwinds in the quarter. In local currencies, Gross Merchandise Volume grew 45%, and Total Payment Volume grew 54%, both year-on-year in the second quarter.

These results illustrate the vibrancy of a business driven by constant optimization on our part, and the positive impact of secular trends that continue to favor us strongly. This combination has allowed us to overcome what we understand have been slower macro conditions present in our markets during the last quarter. Put another way, solid innovation, execution and the continuing shift from off-line to on-line purchasing continue to be the driving forces behind our ability to capture the tremendous opportunity presented to us. With this in mind, let me now walk you through some details on the initiatives we understand had the most significant impact on our strong results.

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Our marketplace is a great place to start, showing vibrancy in both supply and demand. We saw accelerating growth in buyers, sellers and listings, outpaced by even faster

acceleration of sold items growth during the second quarter. More notably, this acceleration occurred across our largest countries.

Three key factors, in addition to solid execution of the overall business, are worth mentioning as important drivers of operational strength: our branded marketing campaign, the continued mix shift into newer non-consumer-electronics categories, and additional UI enhancements carried out.

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Our TV campaign launched in the quarter centers on our brand, on our mobile capabilities, and on the benefits of buying on-line versus off-line. It is primarily a brand marketing campaign, and as such, is an initiative out of which we expect long term impact. Ultimately its success is measured on its ability to maintain MercadoLibre as the Top of Mind e-commerce brand in Latin America. However, we have also seen positive immediate results in terms of improved traffic to our sites during the quarter, as we are seeing incremental visits to our sites since launching the campaign, and have experienced a positive impact in our mobile efforts.

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In the meantime our efforts in non-consumer-electronic products yielded above average growth rates in categories as diverse as apparel, home & garden, industrial and office supplies, toys and games, and autoparts; with some of these growing units sold at nearly 2x the average rate.

In addition to the way in which an increased vertical focus is improving trading volumes, we also saw positive impact from certain horizontal features launched in all categories during the quarter. We deployed a series of search optimizations aimed at improving the relevance of search results surfaced, added features that improve deal and product discovery, and continued to perfect the UI for providing both a more simple and faster to download visualization of product pages, while at the same time surfacing more and better product information.

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User interface improvements were also extended to our mobile initiatives, where the right adaptations are turning smartphones and tablets into buying tools on MercadoLibre at a remarkable speed. Mobile continues to make its way towards double digits as a percentage of total GMVe, with certain markets already exceeding that level during the second quarter, gaining share of device mix yet again. Clearly, our mobile efforts continue to exceed expectations for such an early stage, and show no signs of slowing down.

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Steady penetration gains also characterize our early stage shipping initiative, MercadoEnvíos. In Argentina and Brazil combined, more than 10 thousand unique shippers sent at least one parcel during June through our system. This still entails a very small share of our total volume in those countries, but share gains over sold items and GMVe are consistent month after month. In the meantime we are bringing new carriers on-board as shipping options, and innovating with a local twist in each country. Last month in Argentina we launched a beta version of a same-day delivery service through a deal with a local courier that is available in the city of Buenos Aires for a very reasonable flat fee. We are making it available to professional sellers meeting certain criteria with regard to volume and level of service provided. This is just an example of how we are improving shipping not only for the sake of our buyers, but also to help further differentiate quality sellers. We look forward to reporting further progress as shipping continues to become a reality on MercadoLibre in quarters to come.

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Next, let me very briefly cover payments. We continue seeing traction in our payments business, as our total payment volume grew 54% in local currencies in the second quarter, while we posted near record low levels of fraud loss provisions on that volume, thanks to improved execution and newly deployed technology for our fraud prevention efforts.

During the quarter MercadoPago re-launched in's brand and logos, with the intent of generating a more explicit connection with the MercadoLibre umbrella brand. Let me remind you, that the strongest competitive advantage we have over competitors is our ability to leverage MercadoPago usage on our marketplace for our off platform efforts.

Additionally, MercadoPago's check out interface was updated once again during the quarter. Improvements included:

- streamlined buying flows,
- increased features such as recurring payments, additional marketing tools, one click purchasing for off platform merchants,
- and improved seller financing options

In all, a quarter with sustained growth, and an active pipeline of product improvements and launches.

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As one final update on our initiatives, we continue to see steady traction in our platform approach. In addition to a growing number of third party developers and other retailers that are integrating with MercadoLibre through our API's, we have launched a fund to invest in

companies that leverage our platform as a core part of their business models. So far we have committed investments in businesses focusing on diverse business models, all leveraging our API's. Among current portfolio projects are company's in the micro loans space to help fund working capital needs of MercadoLibre sellers, business intelligence solutions for sellers of our platforms, and ERP solutions that focus on making trading on our platforms more efficient. These are primarily early stage investments, typically in the 50 to 100K range, that, if successful, will add significant value to our users and generate both greater engagement and loyalty on our platforms. Additionally, they serve as important early phase users of our public API's, giving us valuable feedback so as to continue improving on that front.

Wrapping up my review of the quarters progress, we are pleased with the level of execution on most fronts, and the growth of our business. Now let's move on to our financial performance for the second quarter. As usual, during my review of our P&L I will call out year on year growth rates unless I specify otherwise.

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In the second quarter of 2013:

- Net revenues were \$112.2 million, accelerating in local currencies and also in USD despite foreign exchange headwinds. Revenues grew 38% in local currencies and 26% in USD.
- Gross profit margin was 72.3%, down only 81 bps YoY
- Income from operations was \$35.4 million, with an operating income margin of 31.6%. Year-on-year, operating income grew 11% in USD and 23% in local currencies.
- Net Income before Income/Asset Tax Expense was \$40.7 million, growing 16% in USD and 28% in local currencies.
- Net income was \$30.0 million, growing 18% year-on-year in USD, and 30% in local currencies. This resulted in EPS of 0.67 cents for the quarter.

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Topline growth was led by an accelerating core business.

New users in the quarter were the highest ever, and sold items accelerated versus the prior quarter in all our key countries, primarily in Brazil, outpacing user growth, a sign of increased user engagement. The resulting acceleration in GMVe also drove core marketplace revenue acceleration, though at a slightly lesser pace resulting from listing type fee mix, as growth in free listings accounted for an increased % of our GMV versus prior quarters.

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Non-marketplace revenue grew slightly faster than the core marketplace, driven by

- Off platform revenues that continue to grow at a faster pace than all other revenue sources,
- financing revenues that grew at a similar pace to the core marketplace
- both of these, offset by Motors and Real Estate growing at a slower pace than the core marketplace, given the strong FX headwinds faced, resulting from Venezuela's higher share of these classified revenue streams.

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The positive revenue trends we've just covered for each of our business units resulted in healthy growth for each of our largest countries. In the second quarter, consolidated revenues in local currencies grew: [PAUSE]

22% for Brazil, despite 33% sold item growth, on lower ASP's and a slowdown in non-marketplace growth, 66% for Argentina, 19% for Mexico, and 68% for Venezuela.

[LONG PAUSE]

Advancing down our P&L:

Gross profit grew 25% in the second quarter, to \$81.1 million. Gross profit margin was 72.3% of revenues, versus 73.1% in the second quarter of 2012, and 72.1% in the first quarter of 2013.

Both comparisons, year on year and sequential, show positive management of our gross margin profile as investments in our platform and our customer experience both showed scale. With payments penetration relatively equal quarter on quarter, gross margins actually improved sequentially, while a higher proportion of payments processing volume year on year was largely offset by efficiencies of scale in our variable costs related to MercadoPago. In fact, while payments growth and its efficiencies are practically a wash, the 81 basis points of year on year gross margin contraction are essentially driven by further investments in our fraud prevention and trust & safety efforts, generating benefits that I will cover shortly further down our P&L.

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Operating expenses for the period totaled \$45.7 million, 38% versus the second quarter of 2012. Operating expenses as a percent of revenues were 40.7% in the second quarter, versus 37.2% in the same quarter last year, and 44.3% in the first quarter of this year. Year

on year margin contraction basically arises from a higher accrual of our long term retention plan, yearly wage adjustments, a 10% increase in headcount and increased brand spending; all of these partially offset by efficiencies in chargebacks and bad debt. Within this frame, let me address each of our expense lines in greater detail.

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Sales & marketing, which remains our largest line item, grew 24% to \$20.8 million, or 18.6% of revenues, vs. 18.9% for the same period last year.

Increased offline marketing accounts for 349 bps of margin compression, as we aired our new TV campaign during the second quarter.

This step function in our brand spending was offset primarily by 2 factors also impacting within Sales & Marketing:

- First, we saw 255 bps of scale in our chargebacks line. This resulted from a steady improvement in our rate of chargebacks over TPV, as well a non-recurring recovery that accounts for 86 bps of the total effect.
- Second, once again we delivered a sequential improvement in bad debt, yielding a year on year reduction of 93 bps when measured as a percentage of revenues.

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Moving on to Product Development, expenses grew 59% to \$9.8 million, representing 8.7% of revenues in the second quarter versus 6.9% in the same period last year.

Salaries and wages are the principal driver of growth in this line as we added more engineering talent through hirings as well as small scale acquisitions, and took an 81 bps margin hit as a consequence of increases in LTRP accruals.

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Finally, G&A grew 49% year-over-year to \$15.1 million in the second quarter, or 13.4% of revenues versus 11.4% a year ago. Once again, salaries and wages explain most of this growth, and long term retention accrual alone accounts for 172 bps of margin compression.

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As a result, operating income for the second quarter of 2013 was \$35.4 million. Operating income margin for the quarter was 31.6% vs. 35.9% in the second quarter of 2012. Below Operating Income, we benefited from \$2.2 million of interest income, down 26% year on year as a result of lower interest rates on our investments.

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We saw a \$3.6 million gain in our forex line, almost \$3 million more than a year ago, as the USD holdings of our subsidiaries appreciated, a natural hedge that we generate as part of our treasury management.

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As a result our pre-tax income was \$40.7 million, 16% higher than in the second quarter of last year in USD, and 28% higher in local currencies. In the second quarter income tax expense was \$10.7 million, resulting in a blended tax rate of 26.3% versus 27.7% in the second quarter of 2012.

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Net income for the three months ended June 30, 2013 was \$30.0 million, 18% higher than last year's \$25.4 million. Net income in local currencies was 30% higher than last year's second quarter.

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Net income margin was 26.8% in the second quarter versus 28.6% for the same quarter of 2012, resulting in a basic net income per common share of 0.67 cents.

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Payments for the acquisition of property, equipment, intangible assets, and acquired businesses net of cash acquired for the quarter totaled -\$35.2 million. The ramp up in PPE was primarily driven by the purchases of additional offices in Argentina to accommodate future growth in headcount, and purchases of commercial real estate in Venezuela as a strategy to preserve the value of assets in Venezuela that would otherwise be exposed to devaluatory risks. Consequently, for the period ended June 30, 2012, net cash provided by operating activities less purchases of property, equipment, intangible assets, and acquired businesses net of cash acquired totaled -\$6.2 million, versus \$33.5 million last year. Cash, short-term investments and long-term investments at the end of the quarter totaled \$261.9 million.

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Concluding today's remarks, we are confident that the strong performance we've just reviewed further validates the strength of our ecosystem and highlights our ability to execute on our strategic initiatives. We are very pleased with these results, with the increasing strength of our balance sheet, and the strong momentum our business is experiencing. I look forward to further updating you on our progress over the remainder of the year.

With that, we will now take your questions.