Q2 2019 Earnings Call

Company Participants

- EugÃªnio De Zagottis, Corporate Planning & IR Officer and Member of Executive Board

Other Participants

- Joseph Giordano, Senior LatAm Healthcare Analyst

Presentation

Operator

Good morning, ladies and gentlemen. At this time, we'd like to welcome everyone to RD People, Health and Well-being conference call to discuss the Second Quarter results. The audio for this conference is being broadcast simultaneously through the Internet on the website www.rd.com.br/ir. On that address, you can also find a slide show presentation available for download. (Operator Instructions)

Before proceeding, let me mention that forward-looking statements are being made under safe harbor of the Securities Litigation Reform Act of 1996. Forward-looking statements are based on the beliefs and assumptions of RD management and are information currently available to the company. Forward-looking statements are not guarantees of performance. They involve risks, uncertainties and assumptions because they are related to future events. And therefore, depend on the 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 RD and could cause results to differ materially from those expressed in such forward-looking statements.

Today with us, we have Mr. EugÃªnio De Zagottis, Investor Relations and Corporate Planning Vice President; and Gabriel Rosenberg, IR and Corporate Planning Director. Now I will turn the floor over to Mr. De Zagottis. Sir, you may begin your conference.

EugÃªnio De Zagottis

Hello, everybody. Welcome to the Raia Drogasil conference call. I will start by apologizing as MarcÃlio unfortunately could not join us today as he's traveling abroad for us, the company. But here we are, Gabriel and I. So I'd like to start by saying that this was an excellent quarter for the company. After two years, posting mature stock comps below inflation or even negative in the case of last year, we were very successful this quarter. And we were finally able to beat inflation. And overall, we certainly did better margins, better working capital and other sort. So we ended the quarter with 1,917 stores all across

Brazil. We opened 47 stores and closed 3 stores in the quarter. Our market share reached 1.6% gain -- we had a market share gain of 1.6percentage points, with 2 points of gain in SÃ£o Paulo. Our revenue reached BRL 4.4 billion, 17.1% of growth, which is a very good number for the company with 4% mature-store sales growth. We posted a gross margin of 29.1% below the same quarter last year. And finally, we had an EBITDA of BRL 363.7 million, an increase of 14.9% with a margin of 8.2%. I will only comment on the previous accounts criteria, I'm not referring to the presentation to the IFRS numbers, although, they are here for whoever is interested. We had a total net income of BRL 160.5 million, an increase of 13.2% and a 3.6% on margin. And finally, we generated a positive free cash flow of nearly BRL 43 million, with BRL 53 million of total cash consumption in the quarter.

On Page 4, we can share more details about our expansion. So we ended the quarter with 1,917 stores. Through this year, we have opened 109 stores. And we have closed a total of 17 stores. If you look at the quality of the growth, I think it has been very good. As you know, we generally shoot for marginal internal rate of returns around 20%. Whenever we calculate where we are for stores opened in the last 12 months, we're generally somewhere between 17 and 20. If we look today's figures, we are 20.1%, 20.2%, something like that. So we are in the up area of the rate. So very consistent performance. And again, this is net of cannibalization. Finally, we ended the quarter with 24.7% of store still maturation versus 65.3% mature-stores. So there is more growth momentum contracted from maturation.

Page five is probably one of the most important charts in the deck. And I think this explains what's happening in the market and why we have been able to improve our comps so dramatically. So obviously, we have seen through 2017 and 2018, a cycle a very intense store attrition by competitors. Obviously, '17 was even stronger than '18. But these 147 stores opened in the Third Quarter '17 and 166 opened in the 4Q '17. And new stores, they affected only part of '17. But they affected dramatically '18. So when you put these stores open by year-end '17 with the number of stores opened through '18, which were lower. But still a significant number. I mean, obviously, this actual competition affected our comps and it posted negative mature-store sales. As we enter 2019, it's very clear that we see a huge reversion in terms of industry cycle. So we see now way less store openings and we see way more store closures, which basically is a recorrection of mistakes made.

Well on our side, we maintain a very consistent growth base. So I think this chart of this quarter, the fact that we are very high regional interferers in this market that can't be underestimated and the complexities of delivering an accelerated growth program that really creates long-term credit for the company, as we have done. But it's not an easy thing to be done, as the reversion of this bubble for traditionals. Then when we look up at the chart in the upper part of the page, I mean, our growth is starting to become more from the other plays. This is all Abrafarma data. So this is only about the large chains. This is not about the full market. But this is really the most relevant comparisons we made. So we see that Abrafarma keeps posting lower growth and we are accelerating. So our performance is decoupling from the market. I mean in the end this means market share gain made the company.

So on Page 6, we can talk more about this part on the right side of the page. So in terms of share gain, we reached 13% national share, 1.6percentage point share gain in one year.

This is a record gain. This is the highest number ever reported by RD since the merger in 2011. And I think even better, is the fact that we gained 2percentage points of share in SÃ£o Paulo, our main market and probably the market that saw the biggest pressure in recent years. We have gained market share in every single market. But I also like to point to our 7.9% share in the Northeast, which is already in line with the South and close to Southeast, not to mention that we have a huge growth momentum here because most stores are not mature yet and they have a lot of new stores coming. And the fact that we recently added in the North region with 3% market share already. And we will see way more growth here as well. One other thing about -- when we talk about SÃ£o Paulo, as I previously mentioned, this is especially -- this is even more interesting.

If you look at the bottom of the page and you see that our share of SÃ£o Paulo, the total expansion has been declining at a very steady pace. So SÃ£o Paulo in the 1Q '17 used to represent nearly half of our openings. We now represent only 27.6% of our openings. If you think in absolute numbers, we used to open 100 stores a year. We are now opening 67 stores last 12 months, still with less growth in a more upending market, our share gains have accelerated as I mentioned.

Then when we look on the left part of the page, I mean, it's clear that we already have a pretty national presence. I'd like to highlight that we already have 28 stores in ParÃ¡ and we'll open more. We are entering Amazona, the city of Manaus. This is not an easy entry because there are no freeways into Manaus. So we have to ship by air, which is expensive. So this is a higher execution risk proposition and we'll open a more conservative number of stores to begin with. And then we'll see where it takes us. So in addition to that, I also would like to point to the fact that we already have more than 230 stores in the Northeast, nearly 1,000 stores in SÃ£o Paulo. And when we think about our growth, the Northeast has been until now a very significant portion of the program. Every -- almost every year, we have a new state on average cycle of two years, a new state taking a lot of stores, like Bahia early on. And then Pernambuco and then Gerais and more recently ParÃ¡.

When we move forward, I mean, there's no new market in which we can come and open 20, 30 stores from scratch in a single year. So this means that our expansion will be more distributed than it has been until now. And the fact that when you look, for example, markets like Porto Alegre, Belo Horizonte, Rio, we are much better off now, they are than we were in the past. So this market can take more stores than before. So this is allowing us to maintain a significant growth pace moving forward.

On Page 7, talking about revenue growth. We posted a consolidated revenue growth of 17%, where 16.7% for our retail business and near 25% for 4BIO. When we look at the mix, the largest growth was OTC 18.8% before it keeps gaining the revenue mix. But for me the most impressive performance is really generics. We grew 18.2%. So slightly below OTC. But let's remember that we made very, very significant price investments here, starting the Second Quarter of last year. I think second Q and third Q last year were really the peak for margin investment. So when you look today at generics, our average price is not growing with inflation yet. It's actually below 0. But the volume growth has been so dramatic that the overall figure is already good. As we move forward and as the comp base, the tef comp base phase off, this means the generics will be the fastest-growing category in the coming quarters. But also like to point that the performance has been consistent all over, with 17% growth in HPC, 50% growth in branded.

On Page 8, we talked about the comps here. So for the 17% total growth was driven by same-store sales growth of 8% and mature-store sales growth of 4%. This is already -- this represents real growth as we beat an inflation of 3.4% to generate 0.6% real growth. So I think this is a big number for the company. This is an improvement that we expected to see by the end of the year. And we're happy to see that it already happened in the Second Quarter. And this is even more impressive because when we rank month-by-month, April was a challenging month. April was not an easy month for us. But May and June were reasonably upstanding months and we see the momentum maintaining as we enter the Third Quarter. So we remain very optimistic. And we believe we will post more real growth this year and very likely next year.

On Page 9, our gross margin totaled 29%. This represents a 10 bps pressure. This 10 bps pressure came from 4BIO, which was faster with a lower margin, which means that the retail margin was flat. But let's remember that this is the quarter in which we posted inflationary gains on inventories. And this year, the price increase was higher than last year. So we have a 40 bp margin gain. But through the fact that the price increase was high. So this is a cyclical -- a seasonal mix, sorry? And this seasonal gain was consumed by 30 bps commercial pressure, which is a reflection of the price investments and the taken net of all the commercial gains like trade allowances and so on. Then we have 10 bps of net present value.

But the challenge that we have is that in the coming quarters, there will be no price increase and here we will carry some kind of gross margin pressure, as we already see here because of the commercial initiatives we have been taking. The excellent sales momentum also translated in a cash cycle reduction. So our cash cycle is nearly 1 basis lower today than the same day last quarter. This is a nice reversion following several quarters of pressure, even though earlier on we had massive reductions. But retail is a very simple business. If you sell well the expenses will dilute well, cash cycle will behave well, margins will be great. And if you don't grow then it's the opposite. So growth is the most important driver and everything that comes in place when growth is anemic.

On Page 10, talking more about expenses. So our total operating expenses represented 20.8% of our revenues. So we were flat, 4BIO diluted 10 bps. We retained pressure 10 bps and the main sources of pressure were rentals because of the IGPM situation. The IGPM is already coming now. Well over the last 12 months, 2 points of inflation. So this represents 20 bps pressure. And finally, there is a healthy inflicted pain here of logistics. Let's remember that we're opening to see 3 new DCs. So 1 is a relocation. So we closed 1 DC in the countryside of Rio and we are now opening the DC in the metropolitan region of the city. This will take a very nice price gain next year because we are shipping from the countryside, all 130-plus stores and now we start shipping from the countryside. Sorry, we are shipping from the countryside, now we'll start shipping from the metropolitan region. So it's one hour less transportation time and cost. But because we had 3 DCs coming all at once because one of SÃ£o Paulo's largest companies, we are already booking fixed costs. So we now see logistics pressure. But we believe we'll hear good news next year from Frank. And finally, I think we will diluted 10 bps in labor, as we had a higher operating efficiency here and several other like acquiring fees, for example, another 10 bps. New store performance another 10 bps.

On Page 11, this resulted in a total quarterly EBITDA of BRL 364 million. This is 14.9% EBITDA growth. So regardless of what happens in the market, which is a 20 bps pressure. Our absolute annual growth grew 15%. So I think this is a very good quarter by any means.

When I think about net income on the next page, net income increased by 13.2%, also a very solid performance with a 10 bp margin pressure. We moved to the quarter nearly BRL 40 million of nonrecurring expenses. And the bulk of this is related to the relocation of the Barra Mansa distribution center and to consulting, advisory and restructuring expenses, most of which were related to the Onofre acquisition that I will talk more in detail by the end of this presentation.

On Page 13, we see that we posted positive free cash flow generation. This is also a result of lower cash cycle investments than we made last year, also higher level resource of operations. So positive free cash flow and somewhat negative total cash flow of BRL 53 million. But this is also -- this is mostly driven by interest on capital, interest on debt actually. So when you look at our share price. Obviously, the long-term performance is very good, 26% the internal rate of return for whoever invested in our IPO. But when you look in the year, the share price has grown 33% against 14.9% from BOVESPA. We're very happy for having generated alpha for our investors.

Then on Page 15, summarizing what we did in the quarter before we move to the one-off acquisition. So this was a quarter of very solid revenue growth, strong market share gains and which points to positive momentum ahead. We still see -- as we enter the Third Quarter, the mature-store delivering really well. And I think this will sustain this coming through the next quarters. Market share gain, again, 1.6percentage point. I mean, I think that's a big number. This is related to a combination of things. This is related to the fact that the capacity addition in the market was reverted. The bubble is now being cleaned up. So this is what we think. We never had a more competitive price positioning than we have today, driven by generic investors. But not only generic. Generic was the main line. But we're also invested in branded and even somewhat in OTC. So we have a competitive price today, as I think we never had in the recent past. And also the fact that we have done an expansion which has been phenomenal, which has been delivering very strong marginal returns. It's a fast expansion. But it's a high-quality expansion that creates long-term value.

Then -- when we think about margins, I mean, obviously, the gross margin was very good in the quarter, flat for retail driven by the seasonal effect from the price increase. So we have a gross margin pressure for the next quarters. But also, it's very good to see that we maintain expenses nearly flat as we sold -- as mature stores performed really well, I think, we started reverting the loss of operating leverage we observed in previous quarters. So as we maintain a good growth momentum, I mean, we may see operating leverage coming forward. This has more to do with sequential improvements from where we are than with the comps per se because the current expense level represents a certain level of revenues per store. If our comps increased just because of the comp base, I mean, that doesn't change. But if we get sequential increases, then maybe we can see more margin dilution that may or not offset these gross margin pressure we should face. And finally, when you look ahead, we are very optimistic because of the growth momentum because of our competitivity, as I mentioned.

I think I have also to mention that we are progressing really well along with our additional strategy, which you'll see very early promising results. Frankly, I don't think they are an explanation as of yet for the performance we had. But I think we have a very rich pipeline. And these efforts will start combining to start driving our numbers ahead. And this should be another source of competitive advantage. This should be -- this should increase our hedge versus our main competitors not to mention that it should dramatically improve the customer shop experience. But we're moving pin point, especially the pharmacy counter but not only the pharmacy counter. And this translates in a much higher engagement for customers, really being able to not only be a retailer, which deliver medication. But being a partner in promoting health care for promoting prevention, driving a derisk of the treatment, healthy habits. And I think with an app we can do this very effectively. So we want to have a broader role in health care. We are traditional retailer who sells a health care product. We want to become a health care provider who retails.

And finally, I think we have good news for expense coming forward. As I mentioned, freight dilution from the Rio relocation and also from the CearÃ¡ DC, which will reduce transportation just in the North and also in utilities. We are preparing the migration of up to 1,700 stores to renewable and distributed energy generation. So according to the pilot we have done, we could save 20% of electricity costs in those stores. I think it's difficult to generalize what it needs for next year because we had to understand how fast or slow the rollout to be. The other thing is that the 20%, that this relates to stores that were piloted, depending on the region where the stores will be rolling out. It could be higher or could be lower. But the direction of where EEG expenses will be growing, beginning next year.

Okay. Moving to Onofre now, Page 16. So this is, obviously, not just obviously. But happening in the quarter. So this is subsequent information. We concluded the transaction on July 1. So July 1, the company was -- became officially ours after CADE's approvals and other stuff. Then we had a channel sampling on August 1 to approve the legal incorporation of Onofre. So when we got the approval, we had a leader cooperation taking place in the same day, which means that Raia Drogasil and Onofre become a single legal entity. So this is very important for us to proceed with the integration. What this means is that next quarter, the July financial statements, they will be consolidated. But from August onwards, the numbers are part of the numbers that we'll be reporting. We don't need consolidated -- there's no consolidation to do here.

So let me talk about our integration strategy here. So what we're doing here. We are transferring every Onofre remaining assets to our platform. So all the stores are migrating to the Raia Drogasil platform. The e-commerce business will be migrating for the Raia Drogasil platform. So this means more efficiency. This means better operation. We're also optimizing the store portfolio, which means closing stores which are redundant or which we believe will not be able to create value. And we're rebranding ever single Onofre store and Raia or Drogasil, depending on where the closest store is and so on. So we have social technical criteria to decide on which brand. But Onofre will survive only as a pure-play e-commerce brand. There'll be no physical stores anymore. But by leverage in the high end as you scale and structure, Onofre will become a price leader in the market, playing on a national level, no longer only in Campinas and a couple of other states. And being able to do faster local deliveries in every single market. So I think we can really change the dimension of Onofre.

Onofre is already the second player in the industry. Onofre more than doubles our digital e-commerce sales and the fact that we have to absorb Onofre means that we're already preparing our stores to just assume the logistics of Onofre, starting to see which things then by Onofre DC which will be shut down. And this structure allows us also to accelerate neighborhood deliveries for Raia Drogasil. We have one hour delivery pilots and we should certainly expand on that. So Onofre will help us here. So we have a very clear integration schedule. A lot has already happened and the rest will happen in the coming months. So as I mentioned, we consummated the transaction on July 1. Already on July 7, we closed 8 underperforming or redundant stores. There will be more stores closed. But right now, we need to operate them as Raia Drogasil to understand what the potential is and reach towards can survive or not.

On August 1, follow a general assembly, we have already migrated all the 42 surviving stores to RD's platforms and structures. And we have fully absorbed the Onofre staff, blended them with our store chains. This means that if Onofre we were only a direct store chain without an e-commerce operation, the transaction -- the integration would have been already concluded. So this is really important because, as I mentioned on the next page, Onofre today will be generating losses that have to be accretively reverted. And we want also to minimize the distraction it caused on our structure. So the quickest integration is the quickest we will move ahead and go on to further things.

We're also rebranding the stores. So each store is already rebranded as Raia Drogasil with a CapEx of BRL 250,000 per store. So we deemed the most settled stores to make sure that the look, the view is good to validate them. And now we're starting to rebrand other stores. So the renovation work are undergoing. And we believe, by October, we may have closed some more stores and maybe we have rebranded all stores to Raia Drogasil. Additionally, between August and October, we're preparing Raia and Drogasil, are key to receive the e-commerce operation. These means preparing our distribution network and this means preparing our e-commerce systems because Onofre has functionalities which we can't lose. That also something related to maintain search relevance. There's a way to do the transaction that maintains such relevance. If shut down this way, the whole indication is lost. And we -- and search relevance, which is very important here, would just go -- it would just disappear. So we're preparing that. And in October, by the end of October, we expect that Onofre e-commerce operation will be fully absorbed by Raia Drogasil. And finally, this will allow us ramp up to shut down the operation, shut down sites, shut down the systems, transferring accounting balances and then the transaction will be completely finished.

On Page 17, we can discuss the economic outlook and expected synergies from this integration. So I'm not allowed to talk about historic EBITDA based on their sales contract to CVS. So what we have here is the projection that we have today for the Onofre operation going forward in the absence of integration. And this means that Onofre today projects an annual burn of BRL 100 million in EBITDA. That's not a small money. But this is a money that -- this is a loss that we expect to reverse very quickly through the integration synergies. Our expectation here is that by the end of the year, Onofre will be at break-even. Obviously, on a consolidated basis on the year, the profitability of Onofre will generate to be negative. But by the end of the year, Onofre should be at breakeven and then starting to create value next year.

Let's remember that the outlook is very favorable here because we had no acquisition price to be paid to the seller. And more importantly, we have a lot of assets in the company. In the company, there should be enough to absorb the cash pressure from the operating losses, actually, more than enough. Our expectation is to generate a surplus, meaning that the assets that we will convert in cash or minimize our CapEx and so on should be enough to absorb the cash losses from the operation. And which assets are these?

First, we have BRL 124.5 million in working capital. This working cap includes excess cash and a lot of other assets with significant release potential. So for example, as we eliminate these things, as we close stores, we will reduce financial liable. So overall, accounting efficiency gains and accounting also that the excess cash already existed, we believe that we can release 2/3 to 3/4 of these amounts to cash. And this should be enough to pay for any losses. This is a company that has no financial liability, absolutely clean. We also have commercial properties with an expected sales of annual BRL 30 million. The book value is even slightly higher than this. But we believe that we can sell these locations for something like BRL 30 million. We have also existing tax assets which exceed the liabilities that we project. And we have, as I mentioned in the beginning, fixed assets in DCs, headquarter and fulfillment centers, that we can relocate toward this, reducing future CapEx. Like conveyor belt to DCs, like consumers can store, things like that.

And this is my ending. And finally, we are completely protected from the existing arbitration proceeding involving Onofre's office and its former owners. We have no upside or downside potential payments. There's no upside or downside from the transaction and any potential payments, Onofre will have to make are fully collateralized by the seller, okay? What are the main synergies here? First and foremost, revenue increase. As we rebrand all the stores to Raia and Drogasil, as we leverage our system, the platform, retail execution and Univers institutional contracts, we believe these stores should be able to sell in line with the company average. They're not bad today, they sell around -- the surviving ones sell around BRL 500,000 per store. I think they could be selling north of BRL 700,000 based on using our brands and based on improving our execution.

We have also a very obvious and significant gross margin gain already quantified, based on our superior buying terms. So this is really, really relevant. All have very strong expense dilution, actual expense reduction by taking RD's existing logistics infrastructure, the IT infrastructure, the whole corporate support area and then they will simply prepare. And we will have a very interesting e-commerce business, which will be a pure-play-- Onofre becomes a pure-play national player, a price leader leveraging our buying combined terms. Our-- They will be able to do local deliveries on a national level using capillarity and scale structure and so on. So this is a very strategic asset for us.

And finally. And this is a nice surprise, I mean, as we started, no embedded people and how Onofre operated. I mean they are what we call in first synergies, which are improvements that Onofre structured. And people can't do for RC. So for example, Onofre has a digital marketing team that we lacked. We used an offsite agency and the team is much better than operating agency here. Onofre was fast when introducing services in stores beyond what we have done. So we are taking the example here. They do well in manufacture services, which is a very interesting profitability line for them and we also leveraged that structure. They have some store signaling solutions that are better than the ones we have and we can roll out for the whole chain. The operator call center, way better than we operate ours. And the call center leader is already -- Onofre -- the call center manager.

And finally, we're very happy to see a very strong team in Onofre that -- and we're absorbing a lot of people from Onofre to strengthen our corporate structure and to oxygenate our culture as well. So just for you to know, we have started hiring new people, that they would close Onofre transaction. We had 70 openings in the company which we are filtering through Onofre people. And we're also bringing more people because of the quality that we bring, because of skills that they bring, which, as I mentioned, will strengthen our corporate structure. In total, we are bringing 131 people from Onofre into RD. This is something like 50% of Onofre's structure. But this is not related to Onofre, it's related to improving our execution. That is an expected investment in corporate structure between 0.05 and 0.1% of margin. This will be easily diluted in the coming year or years. But I think that this will immediately strengthen our execution and we're very happy to pursue it.

We issued debentures. We raised BRL 300 million in the issuance of a single 8-year maturity tranche amortized in the last two years with a cost of 106.99% of the CDI. This is the cheapest corporate issuance ever done in Brazil with this 8-year maturity. We want to invite everybody who can come to Brazil to our Market Day, which will be place October 4 in SÃ£o Paulo. Then our next call will be October 29 to talk about the Third Quarter. And finally, we have 3 scheduled investor conferences that we are attending. So we have Santander in SÃ£o Paulo; We have Morgan Stanley in London, which I'll be attending; and then we have Bradesco New York in November, which MarcÃlio and Gabriel will be attending. So these were our prepared remarks. Now let's open for Q&A.

Thank you very much.

Questions And Answers

Operator

(Operator Instructions) The First Quarter we had is from Joseph from Banco JPMorgan.

Q - Joseph Giordano {BIO 17751061 <GO>}

Actually I have like few of them. So first of all, like, in this context of competitors kind of shrinking operations or slowing down the expansion plans, here I'd like to understand if you guys are seeing like a more benign environment for M&A. So maybe like some of those guys may have a higher willingness to merge in this context, if you are really looking for that? Like you have like an opportunistic purchase on and off. But eventually, there are some like regional change that would add value for the company? Then the second one, goes into future margin gains, right? So as you flagged, we still have like a very young store base. And here, we have a potential dilution of expenses as we mature the portfolio. My question here is if -- like we could be seeing the company investing a little bit of those operating gains expected into further competitiveness to retrofit that into additional growth

A - EugÃªnio De Zagottis

Joe. Thank you for your questions. I mean obviously, I mean, we see a competitive environment, which is much more favorable now. If you look this year, every single month we have opened ourselves more stores than all of the rest of the chains in Abrafarma. Obviously, there is some level of pain in the market. It's difficult for me to speculate on who will or will not sell or not. We are focused now on doing Onofre. And I think Onofre can provide us with a lot of expertise that maybe we can leverage in the future. So the fact that we are integrating the whole retail operation in one month it's something very important. As we understand what the gross margin gains are, you can also project in other transactions where we could be.

Sensing with expense reduction, same thing with revenue growth. So we have a good small lap here to learn about M&A to give us references, even to model future opportunities. And obviously, we have our eyes open. We are always receiving assets, potential targets to look at. But it's true, I mean, we have a certain level of bar that has to -- we have to believe that whatever asset we buy under our systems, under our brands, under our scale can deliver a profitability in line with what we do. That's not always the case. I mean depending on what the profitability of the company is, even if you add 3%, 4%, 5%, 6% of gains of month, speculation, I'm not saying what we gained with Onofre. But let's say, we had 3, 4, 5, depending what the company is, it doesn't take us to where we need to be. So we used to be selective. But we're opening -- we're looking more stuff. And I think the Onofre transaction sets a good precedent, that brings a learning experience that can be leveraged in the future.

In terms of margin gains, I mean, obviously, I think as we get back to real growth, as we have expense opportunities for dilution next year. I mean I'm positive that next year will be a margin expansion here. Then what we do with that additional margin, if we driving the prices or if we maintaining the margin, I think, this is a day-to-day decision. It depends on how the markets are doing and depends on where we're doing. Sometimes we're investing some regions and we are divesting other regions. So I mean, the message is as we -- last year and this year, we invested very significantly in prices. We are sacrificing short-term profitability. But I think it's obvious now how it improves our long-term potential.

The mindset is still here. If we need to do this again, we will do this again. But right now, we feel comfortable with our prices where they are. So under the current environment, I think, we have never been more price competitive than we are today. And when prices are out of the equation for the consumer then I think our execution shines. Then I think all the differentials that we have in terms of store look appeal, brand preference, people and so on, experience and so on. I think they deliver the full potential.

Q - Joseph Giordano {BIO 17751061 <GO>}

Perfect. Just one additional question, if I may. And here you're touching on the competitive landscape. And recent expansion, right? So we have an offeree ahead of us. But in the recent past, the company entered into agreement to acquire some point of sales from the former big bank chain in the North region. So here, I'd like to understand how are you seeing the competitive environment in the core market of some of the chains that we're actually expanding the Southeast region. So what I want to understand is like how strong they are in their core markets and how you're evolving there?

A - EugÃªnio De Zagottis

Okay. I think it's difficult to institutionalize this discussion. What I think is that growing on a national level is not an easy thing. Each market is a different story. Turning from branding that nobody knows into a new market. It's very difficult. I think when you look at Brazil, I mean, every market is now very populated with and even other chains. So I mean, I think what the numbers show is how difficult it is to grow on a national level at a high pace. And obviously, this is one of the things. The other thing is that every chain has to be -- has to remain relevant in their market. They have to be strong because otherwise, if a new entrant comes and the new entrant operates better, it's very easy to see a disruption. So I think the chains which will be successful in the future, the chains which will be around for the next decade, they're the one who deliver very strong execution and have a very relevant leadership in the core markets and the ones which have found opportunities to grow in new markets in a profitable, sustainable way.

Q - Joseph Giordano {BIO 17751061 <GO>}

Perfect. If I may, another one. So thinking on the regulatory front, we have this provisional measure, 881 the economic freedom one, that sets forth some potential regulation change in terms of pharmacies requirements in the drug stores and also the digital prescription system, which is something that may be integrated to your universe PBM platform. So here like I like to understand from you guys, what are the potential gains that could arise from this provisional measure? Then my second question, initially, there was a discussion about allowing OTC sales in other types of retail, particularly here, supermarket and convenience stores. So also, if you could touch upon on what, if it's a potential threat to your business or to the OTC sales?

A - EugÃªnio De Zagottis

So I'll start to further talk about the second. I think there are a lot of good things being introduced. When you think about digital prescription, I think this is an advance for the market. There was a discussion of allowing virtual pharmacists. This is something that -- as you know, I am the Chairman of Abrafarma. This is something that we are against. I don't think this improves care, I think this limits care. So we are against it. And in the end, it's not getting implemented. But there are other good things, for example, the economic freedom promissory measure. It allows us to open our stores any working hours. While we have in several cities, local laws litigate working hours and so on. So obviously, there's still some controversial -- some controversy about if the local law supersedes the national law for that matter or not. He hasn't sold the product in every single market but he sold the product already in many markets. So there are a lot of good things being introduced.

In terms of what you see is of the market. I mean, I think the first thing is talking as a cooperate office Abrafarma. Abrafarma is pro market. We are pro competition. We don't defend -- any protection is mechanism for anyone. Having said that, it's important to mention that the law expects than any medicine that is sold, is through pharmacy support. There is also the expectation that to sell medicines, I mean, there's certain licenses that must be held. So I think any company has the right of selling pharmaceutical products as long as they are in agreement with those legislations because they have to do with the customer's security. What you see is a pharmaceutical product. You have in Brazil a big issue with literacy, for example, how many people can read the package of a medicine, can read the -- I don't know the name in English. The small paper that comes inside with all the technical information. So pharmacist supervision gives something important, Otherwise those products, they could be reclassified like vitamins have been, for example, from the pharmaceutical product to being a supplement or anything like that. But I think that whichever retail format, if they have pharmacists, if they have the license, I think we should compete in the market. So this is one consideration.

The other consideration is that who do you see represents 15% of what we sell. If you look at how supermarkets have done in this industry. They have reasonable market share and the market share is going south because the purchase location is different, because this is a specialized -- this is an industry with specialized execution. So how much sales will they get. I don't know. I have a lesson in exercise. And that says they get a 10% market share. This is 1.5% revenue. I mean it's not negligible. But it's not disrupting that number. And let's also assume that if this pain is getting introduced it's a feature for the whole market, where Agencyport 13%, which Spartan can be 30%, sometimes even more than that. So in the end, it's another source of pain that could be introduced to the market and that could lead to weakening of the competitive environment and in some way, we can even capture that has an offsetting benefit, for example.

Operator

(Operator Instructions) It appears to be no further questions. Now I will turn the conference back to the company for any final remarks.

A - EugÃªnio De Zagottis

Okay. So first, thank you all for attending our conference call. And thanks for our shareholders, for your long-term support. This was, I think, an excellent quarter all over in terms of sales, I think in terms of margins, in terms of cash cycle, in terms of market share. We finally see after two years mature stores, again, beating inflation and with very good momentum ahead. I think this is a result first of the price investments that we have done. As I mentioned before, we have never been more price competitive on a relative basis than we are today. This has also to do with the reversion of the store opening bubble. Today, we see way less openings and way more closures than we have ever seen. So this is also a much more benign environment for us, which has resulted in a very fast shutting and should result in seeing going forward as well. So we keep -- we have a very good position to see the consolidation of this industry.

I think our growth on a relative basis has been stronger than before. On an absolute basis it's probably catching up of the numbers we saw in the past. So from a much lower, much smaller company back then. And finally, I think it's also important to mention that we the importance that will have in the short-term as a new growth lever for the company, as a new source of competitive -- a relative competitive advantage, as a new source of improving the customer's experience in the store, the customer's engagement in his own health care journey, being more proactive, for helping us driving health promotion, health prevention. So again, we have an ambition of becoming a health care player, of becoming a company that helps consumers maintain their good health, not only dispensing boxes of pharmaceutical products. And I think -- when in 1 or two years I think this huge pipeline of initiatives that we have, they'll start unfolding. And I think they'll take us from being in new space in terms of competitive positions.

I'd also like to highlight the fact that the integration of a novel offering will bring faster growth next year, to bring accretion here. And in the end, I mean, this all has to do with the fact that our relative competitive positioning in every way, we see prices, locations, digital, we have never been stronger on a relative basis again than what we see today. And I think this can only mean, this can only translate in good trends for the future. So again, thank you for your support. We remain available to meet you in conferences, roadshows, through calls or through visits to us. Thank you, again. I like to renew the invitation to everybody to attend our Investment Day in October. So thank you very much.