

Q3 2018 Earnings Call

Company Participants

- Fabio Abrate, Chief Financial Officer

Other Participants

- Franco Abelardo, Analyst
- Gustavo Oliveira, Analyst
- Julia Faga, Analyst
- Olivia Petronilho, Analyst
- Richard Cathcart, Analyst
- Tobias Stingelin, Analyst

Presentation

Operator

Good afternoon, ladies and gentlemen, and thank you for standing by. Welcome everyone to B2W's audio conference [ph] Digital Company to discuss the results relative to the third quarter 2018. Here with us today, we have Mr. Fabio Abrate, CFO of B2W; and Mr. Carlos Padilha, CFO of Lojas Americanas.

To better follow up on the conference, we suggest that you use the presentation, which is available at ri.b2w.digital. We also would like to inform you that this event is being recorded. And all participants are connected in listen only mode and with the conference presentation. After that we will start a Q&A session when further instructions will be provided. (Operator Instructions) A replay facility of this event will be made available right after the end for one week.

Before moving on, we'd like to mention that forward-looking statements made during this call confirming the company's business outlook, operating and financial projects -- or projections and goals are based on the company's assumptions and beliefs and also on information currently available. Such forward-looking statements are no guarantee of performance. As they refer to future events, they involve risks, uncertainties and assumptions and, therefore, depend on circumstances that may or may not materialize. Investors should have in mind that general economic conditions as well as industry conditions and other operating factors might affect the future performance of B2W Digital and lead to results that will differ materially from those expressed in these forward-looking statements.

Now I'd like to turn the floor over to Mr. Fabio Abrate to start the presentation. You have the floor, sir.

Fabio Abrate {BIO 17940993 <GO>}

Good afternoon, ladies and gentlemen. Thank you for attending our teleconference. We will be talking about results and operational highlights of Q3 2018. Right after the presentation, we'll have a Q&A session.

Let me start our presentation. Once the transition phase was concluded in 2017 of our 3-year strategic plans between '17 and '19, the company initiatives in 2018 are focused on the growth of total GMV through a hybrid digital platform model, 1P plus 3P plus services, with continuous growth of the Marketplace. As a consequence, Q3 2018, our total GMV grew 3x more than that of the Marketplace, 23.7%, and market 8%, according to e-Bit, with 3.7% market share gain, ours was 29.1% compared to 25.4% in Q3 2017. And we had continuous evolution in cash generation.

The Marketplace is quickly being developed, reaching BRL 6.6 billion in GMV in the LTM, growing about 84.4% in Q3 '18. Marketplace reached four new records for the quarter since its launch in late 2014: the greatest sales, BRL 1.8 million [ph] compared to BRL 1.7 million -- or billion, rather, in Q4 of 2017, with greater market share of total GMV, 52.2% against 47.2% in Q2 of 2018. For the third record, the largest number of connected sellers, we connected over 3,400 sellers compared to 3,300 in Q2. The fourth record was the largest assortment for a quarter, 1.2 million new SKUs compared to 1.1 million SKUs in Q2 connecting.

As the result of this new business model, the company has evolved significantly its cash generation, reaching BRL 58 million in Q3 2018, a 31% increase or BRL 14 million when compared to the BRL 44 million booked in Q3 2017. In the first nine months of the year, cash consumption amounted to BRL 454 million, a reduction of 69% or BRL 1,011,000,000 [ph] when compared to BRL 1.4 billion booked in the first nine months of 2017. In the past 12 months, cash was positive and BRL 56 million.

B2W and Lojas Americanas, LASA, had been adopting important initiatives, O2O, Online to Offline, through LET's, a shared management platform to manage assets of both companies, in late Q3. The services Click & Collect and Click & Collect Now are now available in over 1,000 physical stores, Lojas Americanas, in every Brazilian state, overcoming the targets established for year's end.

Innovation and Future was developed to create disruptive businesses for both companies, be in charge of the construction, creation, incubation and speeding up of these new businesses. They will be able to be structured -- or integrated through the structure of both companies. IF is also in charge of the synergy between the two companies' digital labs and to lead the way in this digital transformation.

AME Digital, one of the IF initiatives, keeps on evolving, showing outstanding indicators. We official launched with Americanas.com in June 2018, and we expanded to Shoptime, at the same time, in Submarino in September. The digital payments account has been generating a lot of traction in our brands, offering discounts to our customers, cashback, generating more recurrence and increasing spending. AME app has over 800,000

FINAL

downloads in only five months. The most recent introduction is the acceptance of AME Digital as a means of payment of physical stores in LASA. Back in October, we started a pilot project with six stores, 5 in Rio, 1 in Sao Paulo, and by year's end, several new introductions will be announced. In 2019, we're going to speed up the rollout of AME's acceptance for every LASA stores and to other store owners in the physical world.

Finally, I would like to point out that the entire company is prepared and motivated for Black Friday, the largest sales event of the year. In that sense, the fourth edition of the Seller Day, a preparation event for Black Friday conducted in August, was a huge success and had more than 3,500 participants, sellers, suppliers and strategic partners.

Among the new releases, we have Credit Seller, 100% online platform to offer credit to sellers, and the integration of Promo Seller, a promotional tool for B2W Marketplace with AME Digital. Now sellers can invest in the cashback offer that is additional to those customers that pay with -- using AME.

On to Slide 3. Let me talk about the highlights of Q3 2018. The total GMV amounted to BRL 3.6 billion, a 23.7% growth compared to 8% growth in the market. So we have a greater market share, 3.7% moving from 25.4% in Q3 '17 to 29.1% in Q3 2018. Marketplace's GMV registered BRL 1.9 billion, growing 64.5%, reaching 52.2% market share in our total GMV.

B2W Digital platform has attracted more customers and sellers. We have connected over 3,500 sellers in the quarter, breaking a new record. B2W Entrega connected 3,700 sellers in the quarter, and we are supporting 15,000 sellers, amounting to about 80% of the entire seller base in our company.

On Slide 4, I'm talking about the cash generation. In order to capture all these effects, cash generation is measured based on the variation of the net debt, not considering capitalization operations. In Q3 '18, the company generated BRL 58 million, an increase of 31% or BRL 14 million when compared to Q3 2017.

On to Slide 5. We're now highlighting the cash consumption in the past nine months of the year. As a consequence of our business model, the company consumed BRL 454 million year-to-date, a 69% increase when compared to cash consumption of BRL 1.5 billion. And year on end, the reduction was about BRL 1 billion.

On Slide 6, I will highlight the cash development of Marketplace. In the first nine months of the year, Marketplace booked BRL 4.1 billion [ph], a 77% growth, accounting for 48.8% of total GMV. In the past 12 months, Marketplace's GMV reached over BRL 6.6 billion and 84% growth when compared to the same period a year before.

On Slide 7, I point out the sellers base increase. Ever since the beginning of the operation in late 2014, B2W Marketplace connected over 18,500 sellers. This quick evolution is a consequence of the attractiveness of our digital platform. Sellers are more and more excited in being part, because we offer the access to the largest CapEx and the top brands with this very quick expansion. We are very stringent in selecting those who can

Bloomberg Transcript

FINAL

sell in our platform, because the reputation of the quality of our partners are very important factors, and they have to be aligned with our objective to create the largest and the best marketplace in Brazil. We're proud to support service so that they can grow with us. It's a partnership relationship, which is a win-win situation. Customers, sellers and the company can benefit. Marketplace B2W combined the top sellers in the marketplace in a reliable platform in which consumers can purchase their preferred products, knowing that their origin and quality are guaranteed.

On to Slide 8. That's the evolution of the assortment of B2W sites. In the past four years, we had exponential growth in our sellers base. As a consequence, the assortment of products, SKUs, have or they've been extended. 800,000 we had back in December 2014, now to BRL 7.5 million in late September 2018, an expansion of 6.7 million single items in that period. This assortment expansion is the key pillar in our value-generation cycle, consolidating the perception that our customers can purchase just about anything. We have become a one-stop shop operation. With the growth of the number of items that are offered, we have to give customers visibility to the entire assortment in our website. By doing so, in the first nine months of the year, we have encouraged marketing actions to obtain or to reach that goal. We've had great returns, greater traffic, purchase frequency and the number of items per purchase.

On Slide 9, I point out AME Digital, one of the first IF initiatives. AME is our digital payment means that will revolutionize the way people relate with money. Digital -- AME Digital customers can purchase over the Internet and in physical stores with greater benefit. They can transfer, receive resources using their smartphone using QR Code technology. With this new means of payment, all transactions are conducted in a practical, modern and safe fashion. Our app has been downloaded more than 800,000 times in only five months.

On Slide 10, I point out the quick expansion of AME Digital. Official launch was in June 5 at Americanas.com. The goal was to be the best payment means for both cash purchases and also on installments. And these results have exceeded our expectation. In June 28, we introduced AME also for Shoptime using our TV channel to show live the benefits of AME. On August 24, we have integrated AME Digital and Promo Seller. That's the promotional tool for Marketplace B2W. This new feature allows sellers to use Promo Seller to invest in the additional cashback offer for customers as they're using AME. On September 21, we introduced AME for Submarino's website. AME has getting a lot of traction within B2W brands, optimizing discounts for customers, cashback, generating more recurrence and increasing spending. Back in October, there was an important move. We expanded AME to the physical retail. We started a pilot project using 6 Lojas Americanas stores, 5 stores in Rio and 1 in Sao Paulo.

On Slide 11, I point out that by year's end, many new features will be introduced. And in 2019, we are going to speed up the acceptance rollout of AME for all LASA stores and also to other retailers in the physical world.

On to Slide 12 (sic). Let me talk about Credit Seller that was introduced in August 2018 during the Seller Day. That's a financial product for B2W Marketplace sellers. B2W started to offer credit, loans quickly, safely and simply in a 100% online experience. Platform allows sellers to have access to a new financial source. This is a better alternative than

Bloomberg Transcript

those traditional ones found in the market. Credito Seller is a powerful tool to speed up sales of sellers in B2W Marketplace. Sellers have had contracted out the product and invest in stock, in inventory and competitiveness and also in their operations to better support their growth. The criteria are defined based on sales history of those sellers at B2W, combined with credit and risk information available in the marketplace. Loans can be up to 12 months, and installments are discounted from future sales within the platform.

On Slide 13, I'll be talking about O2O initiatives. B2W and Lojas Americanas keep on speeding up these important initiatives using LET's, a shared management platform of logistics and distribution assets for both companies. Click & Collect is available in over 1,000 stores. We had 580 stores in late Q2 2018, surpassing the previous goal of 800 stores by year's end. It's the only Click & Collect model present in every state in our country. Click & Collect Now, today, it's a system that allows the picking up of the product in one hour after the online purchase. And it's now available in over 1,000 stores and by year's end, will be available in all Lojas Americanas stores, current and those that will be opened.

In late 2017, Lojas Americanas started to sell using B2W Marketplace, making their products available in the states of Rio, Sao Paulo and Minas. In Q3 2018, the operation went on to support all states in Southern and Southeastern Brazil, and the assortment available in the program reached over 12,000, we had 10,000 in Q2. By year's end, deliveries will be expanded to all states in Brazil, and assortment will reach 14,000 items.

On to Slide 14. I will talk about the B2W Entrega, a platform that operates and controls deliveries in Marketplace B2W. The service, introduced back in March 2017, has 15,000 connected sellers, accounting for 79.8% of our total base of sellers. In late 2017, B2W Entrega was integrated to the Prime royalty program. Sellers can now sell their products to members -- program members, free while delivery free of charge, quick delivery and top-level service.

On Slide 15, B2W keeps on being recognized as the best service provider to customers. B2W was a champion in two categories of epoca Reclame Aqui award. Americanas.com has been awarded for the sixth time in a row in the category E-commerce Major Operations with twice as many votes as the second -- as the runner-up. Direct has been awarded for the third time in a row in logistics and transportation categories. The award is based on customers' voting. In customer service, the Reclame Aqui, we have the best assessment. 1P has an average score of 7. Competition has 5.5. The 3P of B2W has a 5.9 score, and the marketplace of our competition is or received 4.9.

I would like to point out that our Americanas place score has been improving, but it's also lagging behind when compared to our Direct sales. We believe this is a great opportunity for improvement to offer services to sellers so that they can improve their operations, and it can also reach good customer service levels. In that sense, I would like to reiterate that B2W Entrega has been growing quickly, contributing to improving 3P service level.

Finally, I would like to thank the dedication of every associate part of the best digital team in North America. We would like to thank our suppliers, to the sellers of Marketplace for

choosing our platform, our shareholders for their trust and, of course, customers for their business.

These are the highlights about our performance in Q3. Now we move on to the Q&A session so that we can answer any question. Please be brief when asking your questions.

Questions And Answers

Operator

Thank you. Ladies and gentlemen, we will now start our Q&A session. (Operator Instructions) Our first question comes from Tobias Stingelin from Citi.

Q - Tobias Stingelin {BIO 18290133 <GO>}

Good afternoon, Fabio, and everyone. I'd like you to please give us some color on the sales performance of growth, specifically, if we know that the market has slowed down somewhat. But if we look at last year, the expectations for GMV for this year or for Marketplace would be to grow 80%, 85% in the first half of the year, that happened.

In the second half, we see that growth is still there, but at a slow pace. You also mentioned that you're offering some credit for the sellers, which might have addressed isolated problems or issues. How do you see that slowing down going forward? What can we expect going forward? What do expect in terms of growth? Thank you.

A - Fabio Abrate {BIO 17940993 <GO>}

Thank you, Tobias. Thank you for your question. Well, the total growth, the total GMV, we have been growing at 24% rate. There was a slowdown in the market. The market grew 12% in the first semester of 2018, and in Q3, it grew 8%. We had been growing twice as much as the marketplace during the first half. And now in the quarter, we grew 3x than the market, actually.

We have gained 4 points in market share in the quarter, 25.4%, and we are now at 29.1% in Q3 '18. That growth was boosted by the Marketplace. We grew 65% in the quarter, and year-to-date, we've been growing nine months steadily. We have broken four new records in the Marketplace, the largest number in sales BRL 1.9 billion, breaking our previous record in Q4 2017. The Marketplace participation is at 52%, which is substantial. We have managed to connect 3.4 million new sellers, which is very relevant when we think about the growth of Marketplace from now on. And we have improved assortment in more than 1.2 million new SKUs. It's clear to us that sellers need more and more support to keep on selling more using our platform. On these lines, we have three important fronts.

Number one, logistics and distribution. Our B2W Entrega reflects that. In a little over a year, the server has an 18% penetration in our sellers base. This will help us in future growth. The second front is the commercial, the support of our sales planning relationships with our customers and our -- to have the right negotiations at the right

prices. Our commercial team is working closely to the sellers teams. And the third front, the one you mentioned, which is credit, one of our latest introductions, Credito Seller. In a nutshell, we believe there is a lot of opportunity to support sellers even more so that they can grow their business and, of course, generate more GMV to repeat with us.

Q - Tobias Stingelin {BIO 18290133 <GO>}

Starting in November from 90% to 65%, it's a very strong slowing down. So is there anything happened which we not see in the numbers. What are the reasons behind that slowing down? Or do you see that those -- because that's time to grow, but they simply cannot grow with the same speed. Because during this time that there was a slowing down in the industry, there's a hope, but the numbers really dropped. We like everything, it's all clear, it's all good. But I'd like to understand the sales trends to have a better picture of the health of the market as a whole.

A - Fabio Abrate {BIO 17940993 <GO>}

Thank you. I believe you're right. If I were to highlight one thing about the growth of marketplace, is that they lack stamina. It's volume-based business. The platform can deliver a lot of traffic. And we believe that sellers need more fuel, more oxygen to keep the pace, the growing pace we have.

Let me remind you that we already had a financial product we offer to sellers, that is receivables discount based on their sales. And now we're introducing a second product, that's the Credito Seller. Our sellers can now have access to a new financial means, which is very beneficial when compared to traditional offerings you find in the market. We believe that this is a powerful tool to boost sales internally. Those sellers that have already taken out loans, the operation of this service is only two months, so they have been investing in the inventory and competitiveness. They've been investing in their own operations to better support sales growth domestically. I believe this is very important initiative. It's a very timely service because we are getting close to the Black Friday, the number one sales event.

Last year, Marketplace performance was just outstanding. The best performance was that during the Black Friday sales. So everyone is getting ready to have enough inventory, and we believe performance will be outstanding, too, both for Marketplace and Direct sales. Let me just remind you that last year, marketplace sellers sold 20x more than a very good sales day. So this is very substantial. So we are counting on that sales. And Credit Seller is a very timely solution to give them this oxygen, this fuel so that they can keep their inventories very high.

Q - Tobias Stingelin {BIO 18290133 <GO>}

One final question. Thank you. Did you say that this new -- with this new credit line, would you expect GMV to speed up this coming quarter? Of course, you have other investment made in logistics and distribution. But what's your expectation about the growth for the next quarter?

A - Fabio Abrate {BIO 17940993 <GO>}

Well, we are very hopeful for Q4. The semester accounts for 35% of sales in the year. And we have a very specific event that presented very good performance last year. So we are working sellers -- we're working with sellers so that we can both be very successful. There are 3 fronts, as I said: logistics and distribution, which is peak; commercial activities, planning, buying the right item at the right volume and at the right price; and now, Credito Seller. We'll help them to have that oxygen, that additional oxygen so that they can keep their inventory levels very high.

Q - Tobias Stingelin {BIO 18290133 <GO>}

Thank you.

Operator

The next question comes from Olivia Petronilho from JPMorgan.

Q - Olivia Petronilho {BIO 19090195 <GO>}

Good morning, everyone, thank you for taking my question. I would like to go back to the marketing expenses line. Fabio already explored, but I can -- I'd like to understand those numbers a little better. If you could explore a little more, what you're seeing in terms of growth of GMV in those categories and which might be less developed, if you will. For example, the automotive side, I'd like to understand. Maybe you won't have a number, but if you have a trend around those less relative categories for Americanas. Thank you.

A - Fabio Abrate {BIO 17940993 <GO>}

Hi, Olivia. Good afternoon. Thank you. This is a 3-year cycle, 2017, '18 and '19. Last year, it was a transition year. We're moving on to the 3P. 2018, it is a growth year already, and we are also reducing cash consumption. In the first nine months, we have reduced about BRL 1 billion when compared to the first nine months of 2017.

I have to point out that right after the Marketplace was created back in late 2014, the assortment moved up from a little less than 0.5 million to 7.5 million SKUs. So this assortment expansion happened because of the number of sellers increasing, too. We now have about 19,000 connected sellers. B2W is now operating new categories, selling items that customers did not have, that reference. That requires some marketing effort, especially at the start. Certain customers are aware that those rents can be found in our marketplace.

As a percentage of GMV, when you take into account SG&A at the first half of 2018, we had 10.7%, which was a record in the year, just like I said in the last call. In Q3 2018, it's now 9.9% of the total GMV. What do I mean? We're always looking at every possible variable. When you take into account the results, and the consequence is consuming less cash. The reduction was outstanding back in '17, and in 2018, same thing. As to the categories, we have noticed that some new categories have performed very well. Let me give you an example. Automotive products. We know that this is a very important category, which is not -- traditionally, at B2W, we didn't sell it. Now we do.

FINAL

And more than just having a good assortment, we have been working very hard to provide a good customer experience. We have the digital spotty shop. So we provide a very good experience to our customers. And some customers can file the brand -- car brand, year of manufacturing, every data of his or her car, and our algorithm can provide a customized packaged products that can be used in their cars. This is just one example of a new category. We are doing it differently, providing that good customer experience, and the performance, the results are very positive.

Q - Olivia Petronilho {BIO 19090195 <GO>}

Okay. Just to follow up, if I may. When we look at those expenses at that line in the P&L, they had been growing, almost doubling from quarter-on-quarter or half-on-half, and now we see that it had grown -- but not to 100%, but if it's seen of 50%. Can we expect that pace to continue, despite the logo design of the first half? Would you say we are coming close to the optimal level? Thank you.

A - Fabio Abrate {BIO 17940993 <GO>}

Thank you. As I said, when you look at GMV percentage, we had the peak, 10.7%. Now we are below 10%, 9.9%. And we expect something below 9% for Q4. So it has been improving consistently throughout the year.

Q - Olivia Petronilho {BIO 19090195 <GO>}

Thank you so much. Thank you.

A - Fabio Abrate {BIO 17940993 <GO>}

Thank you.

Operator

Next question comes from Julia Faga from Itau BBA.

Q - Julia Faga {BIO 20865300 <GO>}

Hello, everyone. Good afternoon. I'm going to talk about once again the growth line. This slowing down of the market, how do you see that going forward? Why do you think, that happened? What can we expect for the fourth quarter? What do you expect in terms of last year when compared to last year? Should we believe that the slowdown is related to isolated issues, the World Cup and their events? Or can we expect this to be related to some more underlying market dynamics? Your loan market, investments, how do you see that slowing down of the marketplace platform? Is it because the investors left marketing, left to be slowing down? That's it. Thank you.

A - Fabio Abrate {BIO 17940993 <GO>}

Hi, Julia [ph]. Thank you, thank you. We cannot determine what actually happened to the marketplace in Q3. There was that slowdown, as I said, and it's directly connected to the economic scenario overall that reflects consumer confidence levels and maybe the World

Cup effect. People ended up buying more in Q2, and they may have run out of money to keep on purchasing on Q3.

Well, this is in the past now. In Q3, the situation is very different. Now on to Q4, Julia, and we keep on very optimistic. Q4 accounts for 35% of our total sales. And we are just on the brink of a very important event, which is Black Friday. In 100 hours, we sell about one month's worth of sales, so it's a very important event. And we have been preparing ourselves for quite some time, especially with the marketplace sellers to brand sales to provide support in logistics and operations and with this new credit product.

So the environment as a whole is better. We have bluer skies, and we are ready to have an outstanding Q3 or quarter of sales. And it's not directly related to the marketing dynamics that you mentioned. I don't think so. If our marketing investments ramp up, it hasn't planned before. As I said in answering your previous question, there was a peak in the first half of the year, and according to our plans, as a percentage of the total GMV, SG&A is going down and it's going to happen in Q4 as it did in Q3, something below 9%. And traffic, the attractiveness of our platform, which, of course, goes hand-in-hand with more sellers and more assortment, something that has been growing substantially, this is important to give or to reach the goals of Q4 and the year, of course.

Q - Julia Faga {BIO 20865300 <GO>}

All right. Thank you.

Operator

Next question comes from Franco Abelardo from Morgan Stanley.

Q - Franco Abelardo {BIO 17416219 <GO>}

Hello, everyone. Good afternoon. I have two questions. Number one, I want to go back to the growth of the marketplace, which is the most relevant point to discuss. You broke down some of the interesting figures that you had. And we saw a little robust growth in the seller space. But when we did the math, the average sales per seller has dropped significantly, 30% year-on-year. What's your take on that? Would you say those new sellers are trying to introduce items with lower average ticket? Or we have just too many sellers under the same category and then we have individuals being affected? Or still, if you go back to share, the growth of GMV on a compared basis among sellers, we see the same slowing down across the board when we compare the base year-on-year. That's the first question. Thank you.

A - Fabio Abrate {BIO 17940993 <GO>}

Hi, Franco, thank you for your question. I believe that the marketplace growth can be explained by giving you two factors: first, the old sellers, those that have been in the platform for over a year; and the new sellers. It's only -- it makes sense to believe that new sellers are smaller than the old ones, right? The average ticket in -- for new sellers is down, and that's why we need to have more and more sellers to deliver on that growth of marketplace.

FINAL

As to the old sellers, I think it has to do with what I said before. We have to provide these sellers with every support they need, so that they can take the best out of the platform that I need in terms of growth. We've been working closer and closer with this group, B2W Entrega, a very new service, in well over a year. We service -- or we serve over 80% of the base. The adoption curve is very good. The other example is the commercial team. Let me remind you that in the past, our commercial team operated 1P, purchase, stock and sell. It was a 100% relationship with suppliers. The scope of this commercial team has been extended. So this team talks to suppliers, supplied they did. But they have also started to work with sellers directly to help them plan better, supplying the right product to help them negotiate with suppliers to get better prices, the right volume. So we have been supporting them, too.

So the thing that was lacking, and we bridged that gap back in August, was credit. We had a product when Marketplace was created back in 2014. It started out offering receivables discount that was a demand on the part of sellers. And now we have yet another product, that's the Credit Seller. The performance has been very interesting in the past two months. This will be not only a tool to boost the growth of Marketplace, but also another revenue source for B2W.

Looking into the future as to new sellers, we expect to keep on attracting more and more new sellers. The number of sellers is 3,400 new sellers in the quarter. Looking ahead, there is a lot of opportunities we can bring in, those that start -- that already operate online and also those physical stores. We have been putting in place means to bring sellers directly from physical retail to online retail, removing every obstacle they would find.

Let me give you some figures. The online market in Brazil is about BRL 60 billion. When you look at physical retail, the market is BRL 1 trillion. Online, it's about 30% market share. In physical, we have less than 1%. So that's exactly what we are looking at the other 99%, and we believe the Marketplace is the place to go to bring these physical owner -- shop owners to be online.

Q - Franco Abelardo {BIO 17416219 <GO>}

Okay. Very good. My second question has to do with cash generation. And the good news is to be that you are continuing to expand cash. But the expectation for the fourth quarter and for the year as a whole, is it to have a more relevant cash generation? Or should we expect to remain at the same level with a slightly higher cash generation year-to-date? And then for 2019, do you see potential to increase cash generation? And what would be a leverage level that you would see as comfortable for next year, since that -- when we look at the net debt-to-EBITDA ratio, the leverage level is slightly high, 5x. So in your view, is there any goal or target in terms of leverage, maybe to reinvest term of that cash generation back into the business? Thank you.

A - Fabio Abrate {BIO 17940993 <GO>}

Hi, Franco. Thank you for the second question. In terms of cash generation, in 2017, we had a transition year. We had an e-commerce model, and now we have this hybrid model, because we believe the combination of 1P and 3P, and even in a transition year, we had an

improvement in cash consumption. In 2016, it was BRL 1.6 billion. It's less than BRL 1 billion last year, about BRL 670 million.

From '18, it's a different year, we're back on the growing trend, and we are gaining market share, especially driven by 3P. And we keep on looking at that improvement in cash consumption. For the first nine months, the improvement is about BRL 1 billion. And we believe in Q4, things will remain the same. Historically, Q4 was better when compared to the previous 3, and this is going to be the same.

And in 2019, our third year, this is going to be a cash-generating company. That's our goal. And we are very optimistic that we are going to deliver on that promise, just like we have been doing so far. As to leveraging, well, we are comfortable with our leverage level. And the previous metric leverage would be 3x EBITDA. And by adopting a new financial model for this and next years, we'll be able to deleverage the company. So we are very comfortable in that regard.

Q - Franco Abelardo {BIO 17416219 <GO>}

But any target, any concrete objective? Why do you say 3x in the old metric? Can you explain a little better, please?

A - Fabio Abrate {BIO 17940993 <GO>}

Yes, no problem. We operate with the 3.5 EBITDA ratio. When you look at top indicators in the market, this is the leverage level as a ceiling, 3.5x, right? When I say we're operating at 3x, what I'm trying to say that we are below that theoretical leverage level, which will be the market's expectation. Looking onwards, when I'm reducing cash consumption and I'm shifting to a cash generation system, the trend is to maintain that level. So that's why we are that comfortable.

Q - Franco Abelardo {BIO 17416219 <GO>}

Okay. Perhaps, go, be proving to that issue offline. Thank you for your answer. Thank you.

A - Fabio Abrate {BIO 17940993 <GO>}

Thank you.

Operator

Next question comes from Gustavo Oliveira from UBS.

Q - Gustavo Oliveira {BIO 15129435 <GO>}

Hello, good afternoon. I have two questions. The first has to do with logistics. I would like to have some more color on the following. I remember the Sellers Day that you have -- that you organized back in August. You mentioned the fulfillment level that you were expecting for some sellers then, that would be a fee as an incentive to sellers. I want to understand a little better how things have evolved since then around that celebration for

sellers, how they see that? Do you already have more capacity to make that facility more available to sellers? And how is that going to play out going forward?

And number two, still based on what you presented in August, you mentioned you were creating a new index to measure sellers' performance, which was based on lead times, order canceling, customer complaint, remedial work for servers issues and so other attributes. All of that would be in the new algorithm. Has that led anywhere? Has that impacted GMV's growth in this quarter? In other words, can we see sellers which performed better under the index performing better across the board? So I'd like to understand those still a little better, please. Thank you.

A - Fabio Abrate {BIO 17940993 <GO>}

Hi, Gustavo. Thank you for your question. Let me answer the first question. It's linked to our service B2W Entrega introduced a little over a year. In late March 2017, it was introduced. 80% of our sellers base use this service. And within that service, there are four options. One, we do everything, that's the fulfillment. We stock their merchandise, and we're also in charge of the last mile.

A second option is, when we go to the seller, get the merchandise and do the last mile. A third alternative is that when sellers comes -- or come to one of our hubs, we have over 200 hubs all over the country, and they make the dropoff, and we are in charge of the last mile. The fourth option, that's the latest, sellers make dropoff in one of our stores, Lojas Americanas stores. So within B2W Entrega, we have several services to serve different sellers that we have in our platform, depending on their maturity level. So it's a very comprehensive service, in other words.

In April, we announced that we would make one of our DCs in Sao Paulo over -- about 100,000 square meters for sellers to store their merchandise free of charge till year's end, and our goal was to apply credit. And it has been very successful, indeed. Once products are in our DC, our delivery times are way better than that of the market. So it's been a very good experience on our end. Sellers can deliver more quickly. It's been good for everyone, for the company and sellers and our end consumers. Your second question about the seller and of course --

Q - Gustavo Oliveira {BIO 15129435 <GO>}

Going back to fulfillment, If I may. Those sellers who embrace fulfillment, have they shown a higher GMV growth when compared to the company's average? Can that be identified if I have a control group or not? In other words, they might be selling under different modes other than this one, but can you identify a difference between those who adopted the fulfillment way and the others one -- others?

A - Fabio Abrate {BIO 17940993 <GO>}

Okay, I got it. When we compare service levels is when we compare that to the 1P. During my presentation, I talked about Reclame Aqui. The score we had in 1P is 7. The average score, it's 5.9. For these guys in fulfillment, we start the merchandise into DC and also provide the last mile. Service levels are much better and it reflects on their sales. Delivery

FINAL

times and service levels are two key elements for customers to make that purchasing decision. And it has to do with your second question, which is the seller index. It's an indicator that combine several performance variables. Delivery times, service levels, these are two of those variables that make up that index. At the end of the day, that index is part of our buy box index.

Let's take into account several variables: price, installments, delivery times, freight costs and customer service level of that seller. So this algorithm is run 100% of the time, and it defines what the best offer to consumers are considering all variables, and seller rating is one of them. And, of course, the seller that gets the buy box has a much better performance when we compare to those that did not get the buy box. On a day-to-day basis, you have very tough competition to get the buy box, to be awarded that buy box. And in order to be awarded that buy box, service level is a very important indicator. And those within fulfillment stand out from the crowd.

Q - Gustavo Oliveira {BIO 15129435 <GO>}

One final question then. Do you have any plans in the pipeline to increase capacity under the fulfillment functionality in the short run? Anything for the fourth quarter, perhaps the first quarter of '19, anything in the pipeline, and distribution center, or modes where they see what you have, either capacity, something like that?

A - Fabio Abrate {BIO 17940993 <GO>}

I understand. Of course, with that expressive growth of Marketplace, and the seller support is mandatory to us. Yes, we do have plans to provide more capacity. I'm not going to mention any DCs. I can give you some areas. We have 100,000 square meters allocated. In 2018, we are going to at least double that capacity. That is to say 200,000 square meters for ourselves.

Q - Gustavo Oliveira {BIO 15129435 <GO>}

All right. Thank you.

A - Fabio Abrate {BIO 17940993 <GO>}

Thank you. Take care.

Operator

Next question comes from Richard Cathcart, Bradesco.

Q - Richard Cathcart {BIO 16457807 <GO>}

Hello, good afternoon, Fabio. I have two questions about the cashback. The first question is the following, just to realize how much was spending in cashback. Early on, the idea was to spend something close to what -- you already spent when you provided discounts. And I'd like to ask if that's still going on and if you are still spending money with the discounts. And the second question is how is that cashback being accounted for in the P&L? Thank you.

A - Fabio Abrate {BIO 17940993 <GO>}

Thank you, Richard, for your questions. Let me remind you that AME is one of the first initiatives of IF, Innovation and Future. The goal is to create and accelerate disruptive businesses, not only to B2W but also Lojas Americanas. AME Digital is one of these initial initiatives, as I said, and a digital payment means that will revolutionize the way people relate with money. It's very recent initiative, about five months old. Initial indicators are just outstanding. The number of downloads is just incredible, 800,000 downloads in only five months. And when we compare that to other market initiatives, this is just outstanding.

There are so many players out there trying to operate in that business. They haven't had the number of downloads that AME has hold up in its initial five months. Yes, it's a more intelligent platform to provide discounts. Let me remind you that we have budget allocation to promote, to give customers discounts. As I said, we use the boleto, the payment slip, but this is somewhat different because this is returned back to customers' account. And when they use that cashback, they end up spending more. We have that lock-in process, so you boost loyalty rates. These are more frequent consumers. When they get cashback, they come back and they purchase again and then they come back to use the next cashback. So you have that virtuous cycle in place. And by using that cashback, spending is bigger. So in the end, it's a win-win situation for everyone. And even with that, AME expansion is just a consequence of the initial results we have been getting.

All indicators that exceeded our expectations, number of downloads, PPD average ticket, the participation and the sales of company brands, frequency, spending, everything. Every metric has been exceeding our initial expectations. We started out at Americanas.com back in June and then Shoptime with the spread, with the support of a TV channel. That was very positive to us to explain consumers the dynamics of this new tool. And then we introduced Submarino. And now we're expanding to the physical world. We started out 6 Lojas Americanas, and in 2019, we are rolling out to all stores. As to the way it's booked, it's very similar to that of the boleto, the payment slip. If you give a BRL 100 cashback for a BRL 1,000 purchase, you book BRL 900. A -- the BRL 100 cashback is booked in an advanced payment to customers, and the money used, you record it.

Q - Richard Cathcart {BIO 16457807 <GO>}

Okay. Very good. Thank you, Fabio.

A - Fabio Abrate {BIO 17940993 <GO>}

Thank you.

Operator

Ladies and gentlemen, we now close the Q&A session. I would like to turn the floor back over to Mr. Abrate for his final remarks. Please, Mr. Abrate, you have the floor.

A - Fabio Abrate {BIO 17940993 <GO>}

Thank you for attending our teleconference. I'd like to take this opportunity to invite you to check the offerings of the -- there is a lot brands, Americanas.com, Submarino,

Shoptime and Sou Barato. If you have any questions, please get in touch with our IR team. Thank you.

Operator

B2W's audio conference is now over. Thank you all for participating. Have a nice day, and thank you for using Chorus Call.

This transcript may not be 100 percent accurate and may contain misspellings and other inaccuracies. This transcript is provided "as is", without express or implied warranties of any kind. Bloomberg retains all rights to this transcript and provides it solely for your personal, non-commercial use. Bloomberg, its suppliers and third-party agents shall have no liability for errors in this transcript or for lost profits, losses, or direct, indirect, incidental, consequential, special or punitive damages in connection with the furnishing, performance or use of such transcript. Neither the information nor any opinion expressed in this transcript constitutes a solicitation of the purchase or sale of securities or commodities. Any opinion expressed in the transcript does not necessarily reflect the views of Bloomberg LP. © COPYRIGHT 2022, BLOOMBERG LP. All rights reserved. Any reproduction, redistribution or retransmission is expressly prohibited.

FINAL

Bloomberg Transcript