Q2 2012 Earnings Call

Company Participants

- Eugenio de Zagottis, IR, VP
- Unidentified Speaker, Unknown

Other Participants

- Guilherme Assis, Analyst
- Juliana Rozenbaum, Analyst

Presentation

Operator

Good morning, ladies and gentlemen. At this time, I would like to welcome everyone to Raia Drogasil Earnings Conference Call to discuss its results for the Second Quarter of 2012. The audio for this conference is being broadcast simultaneously through the Internet and the website, www.raiadrogasil.com.br/ir. In that address, you can also find the slideshow presentation available for download.

We inform that all participants will only be able to listen to the conference during the Company's presentation. After the Company's remarks are over, there will be a Q&A period. At that time, further instructions will be given. (Operator Instructions)

Before proceeding, let me mention that forward-looking statements are being made under the Safe Harbor of the Securities Litigation Reform Act of 1996. Forward-looking statements are based on the belief and assumptions of Raia Drogasil management, and on information currently available to the Company.

Forward-looking statements are not guarantees of performance. They involve risk, uncertainties and assumptions, because they relate to future events, and therefore depend on 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 Raia Drogasil that could cause results to differ materially from those expressed in such forward-looking statements.

Today with us are Mr. Claudio Roberto Ely, CEO, and Mr. Eugenio de Zagottis, Investor Relations and Corporate Planning Vice President. Now I'll turn the conference over to the directors. You may begin your conference.

Eugenio de Zagottis {BIO 7193695 <GO>}

-- to the Second Quarter conference call, Raia Drogasil. On page three, I'll go over the highlights of the quarter. We ended the quarter with 807 stores in operation. We opened 26 new stores, igniting the store opening through this year, and foreclosures in the quarter.

We achieved BRL1.4 billion in gross revenues, 18.8% of growth over the previous year, which also represented 11.5% of same-store sales growth for the Company. We achieved a gross margin of 28.1%, a 1.7 percentage point increase, which consisted basically in the delivery of the cost synergies we have been talking for so long.

As a result, our adjusted EBITDA amounted to BRL100 million, an increase of 22%, and an EBITDA margin of 7.3%, a 0.2 percentage point margin expansion in the quarter. Finally, our adjusted net income amounted to BRL53.8 million, 3.9% of net margin.

On the next page, I'd like you to highlight that we already have 807 stores in operation. We opened 26 stores last quarter. And we also closed four stores. This was the beginning of I'll say of a cycle of redundant store closures, which actually consists in one of the synergies.

And these closures consist of shutting down one of two redundant stores, which are generally super stores. And we increased the total results, because the gross profit transferred from the closing stores to the surviving one. Generally far exceeds the operating margin that the closed stores had until then.

So we are very happy with the initial results of the score. And we will proceed to the strategy over the next few quarters with some more store closures to help our numbers coming forward. As of now, 35% of our portfolio consists of yet two mature stores. So we have a significant growth momentum ahead of us.

On page five, I'd like to give more details into our growth program. We have aimed to 130 new store openings over this year. We have now at the Second Quarter of the year opened a total of 35 stores. This is more than the total number of stores opened by the last quarter -- by the Second Quarter of last year where we reached a total store development program of 99 stores.

So in terms of our operations, in terms of our store development, we were absolutely on track to meet the 130 new store guidance that we have set. Each giving more details on that, but considering today we have already 47 stores open. So in the last 40 days alone, we opened 12 more stores. So we are really on a full-fledged basis here with our growth.

Then we have already signed 73 additional contracts that would assure 120 stores already this year. Furthermore, we have several contracts in advanced stage of negotiation. Still that, by the end of this month, we would have the full 130 new stores that would be open in our guidance.

We also have 26 additional stores that we acquire from Droga Raia Santa Marta in the state of Goias. This company is undergoing Chapter 11 restructuring. So our purchase depends on granting legal authorization so we don't run into any contingency risk from that. This is taking some time. So most likely, these stores were not part of this year's program. Rather, they will help us next year.

We have -- we have release yesterday a material fact, disclosing our coming incorporation of Raia by Raia Drogasil. The main reason for the incorporation is for us to effectively transform into one company, and as a result, be able to integrate IT, logistics, and all of our operations so that we can achieve the benefits of the merger. We can get for the synergies. We can get the best of both companies implemented in a single operation. So this is a paramount step for us to proceed with the integration.

The only collateral effect that it brings is a temporary suspension of the opening of new Droga Raia stores, which haven't yet get licensed. What happens is that today is like a cutoff date. So every store already licensed is today, but under Raia, they will have their disco and sanitary licenses migrated to Raia Drogasil. This is a very complex and time-consuming process. And so starting today, we start transferring those licenses to Raia Drogasil.

What happens, however, is that all the new stores that will be open, and that haven't been licensed yet, these stores will be licensed already in the Raia Drogasil. And as a result, they can only be open after the incorporation is completed.

From the legal point of view, we could, today, open a Raia store, the Raia Drogasil already. The problem is that we don't have systems for managing different Raia stores at different companies. So we really need the corporation to finish before we can resume operating. Nothing happens to Drogasil development program, as Drogasil's already within Raia Drogasil.

We expect the corporation to be finished by the end of this year. So we are setting a new store opening guidance for this year of 110 stores, and we are setting our next year, 130 new stores to be open as well. So it's important to be very clear about that, that we are always very frank in the way we speak. There's no issues for us as far as having the stores, and being able to open the stores and deliver the guidance.

This change is only to reflect the incorporation of Raia Drogasil, of Raia into Raia Drogasil, which is a step that would have been -- is paramount to that.

On page six, talking about market share. We increased our market share to 9% on a national basis. And the main highlight was the state of Sao Paulo, main market, where we came from 20% to 21.6% of share. What happens here is that significant part of our store development in the later years, especially on the Raia side, happened in Sao Paulo.

So we have a huge tailwind in terms of maturation of existing stores. And we continue to open new stores in Sao Paulo, and always very successfully. So it's a privilege to be able to open so many stores in a mature market where we already had more brand, our brand's very, very strong.

We have also grown in most states where we compete. In couple of ones we remain flat, Minas Gerais and Rio de Janeiro. And we got a decrease in Goias. What's important to mention here is that first, we stopped growing in Goias for some time. So we have virtually no maturation momentum here to achieve. And as the markets grow, and we are not opening any new stores, automatically, this means market share loss.

Furthermore, if you remember, Drogasil, one year, half ago, but stores from Santa Marta in Brasilia. But the market, which is now under Chapter 11, used the cash, and improved the inventory levels of their stores. So they were almost run down on the stores, somehow recovered, and they affected everybody in the market.

We are now finishing the process of buying 26 of the Marta stores, which would consolidate our absolute leadership, not only in Goias, but also the whole Midwest region of Brazil.

We also point the entry in Santa Catarina, which happened last year. And we have already consolidated 2.5% of market share, and also, our entry into Mato Grosso that happened late last quarter. Mato Grosso is located on the Midwest of Brazil.

We just opened last Wednesday, two days ago, our first stores in Mato Grosso do Sul, another small state in the Midwest of Brazil. And finally, yesterday, we opened our first store in Bahia, in the southern city of Itabuna. And this entity -- this new store is the start of a big cycle of store openings in the years to come.

So in reality, not only are we getting to Bahia, Bahia is our gate to get into the northeast region of Brazil, which is the major region with very high growth rates, and significant economic improvement taking place. So this is part of our short, middle and long-term growth. And we believe that we'll be successful in these new states, just as we have been in every single state where we have entered over the last 12 years.

On page seven -- I apologize for my voice. I'm recovering from a cold. On page seven, we achieved for mature stores in the Second Quarter of this year, 7.8% of growth. This is in line with the previous quarters, with the exception of the First Quarter of this year, where we had grown by 10.8%.

At the last conference call, I had mentioned that that 10.8% was a one-time benefit, and we would go down over the next quarter. And this is exactly what's happening. Out of the 10.8%, 1.2% is the positive effect of the Leap Year. This would have an extra day of sales this year, compared to the last year.

And the second, and probably most important part of the difference here, is the fact that we are dealing now with a significantly stronger comp base than the one we had at the

First Quarter. Important to mention, especially in the case of Raia, Raia completed its IPO late 2010.

The beginning of 2011, we increased significant inventories of the stores, reduced stock-outs. Over last -- through the extra quarters of last year, we increased our staff deployment of the stores so that Raia comps that start, that had ended 2010, a low basis, it increased something like 6% in the First Quarter of last year, and then to a level of 9% to 10% for the last three quarters of the year.

So in the Second Quarter, we were dealing with the easier comp base of 6% in the case of Raia. And now we are dealing with a 10% comp base, which is a much tougher one.

On the next page, it gets more clear as we depict the growth by brand. So Raia, that was facing a 6% comp base. Now it's facing a 10% comp base. And as a result, decelerated to 6.4% of growth. Drogasil, which is too facing an easy comp base of the early part of last year, was managed to deliver 9.1% of (inaudible).

If we combine the last two years of growth, so we'll have a two-year stacked growth for Raia, north of 16%, and for Drogasil, north of 14%, which is -- both numbers are good numbers, they now believe. And Raia has, over the long term, more growth momentum, because of global revenues per store. But this year's specific, we're dealing with a very different comp base.

On page nine, talking about the product mix, generics was once again the highlight of the quarter. And this is great news, because as you know, margins in generics were much better than everything else. So we increased from the previous quarter our generics contribution to the product mix from 10.8% to 11.5% from a significant advancement in the beginning of this year. And it's a lot due to our execution of our stores, there is somehow probably new products, but at this point, I would say the execution that is driving these generics grow.

Hygiene, personal care, they're slightly better than the total growth of the Company. And OTC is the lowest category, and has been so for a while.

On the next page, talking about gross margins. Gross margin was really the highlight of the quarter, with an improvement of 1.7%. This is basically delivery of the cost synergies. We have been talking, this whole year, after we announced the transaction with Drogasil.

Important to mention that we have two special effects in this number, but that offset one another. One is the fact that this year, we have a less favorable forward-buying season because prices increased by only 3% as opposed price increases of 4.8% last year. However, we also had an untimely allocation of trade allowances that relate to the previous quarter, at this quarter. And this affects -- they almost offset each other.

What happens is that our -- we are developing annual action plans with our main suppliers. But we are setting margin targets, we're setting volume expirations. And as a result, our trade allows our negotiator for the full year. As some of these negotiations not end in the First Quarter, in the Second Quarter, we allocated the part relative to the First Quarter. But that compensated for the loss of forward-buying gain, because of a slower price increase.

We still have a very strong, a very -- I would say a high cash cycle this quarter, an increase from the previous quarters, and that we are facing the need for logistics rebalancing across the distribution centers. What happened is that two years ago, both Raia and Drogasil had only one distribution, each of us had one distribution center. So total of two. And we have now moved to six distribution centers.

So all new distribution centers, they take a lot of additional inventories. And over time, the mature distribution centers, they get down in inventories as they start serving less stores. And this takes time to happen. So this is a progressive process. And that has pressured our cash cycle.

We also have some part of increase due to roof purchasing. There is a specific negotiation that, in which we lower payment term and had a significant margin increase. I would say that part is structural. We were once again strong in opportunity.

Now as we are more pressured with our cash cycle, we are -- the most talked word at Raia, quarter, is certainly working capital reduction. Even if you have somehow to sacrifice opportunity, not structural negotiation, but opportunistic purchases, we do that in order to improve our cash position.

On page 11, our main pressure for the quarter was in sales expenses. If you compare the quarter with the previous years, we have 1.4percentage point expense increase. We have to break this in two different parts.

The first part, the second to Fourth Quarter, in which we had a strong -- people deployment increase at Raia stores. And also, we had a payroll increase last July, which was above inflation. So 0.8%, which is exactly the difference, was due to this labor rates, which especially in the case of head count, that was structural, and that has a very important role in the improving -- allowing Droga Raia to close the gap at Drogasil.

The second part here, from 17% to 17.6%, this is a specific pressure that is being exerted by new stores recently opened, as well as reoperational expenses of upcoming stores. The reality here is that our expansion program was running late. So a lot of stores that were supposed to be open the First Quarter were open on the Second Quarter.

They're just now getting in sales. And these delays mean a significant pressure for -- in terms of pre-operation expenses, because several stores we already pay salaries, we already pay rentals. And we still don't have any revenues to balance that. So the combined pressure of new stores and stores we had to reopen that are already book merchant expenses, is exactly this gap. And so I think this is a very, very high expense point that we're facing.

General and administrative expenses on page 12 has remained flat, at 3.3%. Then it's important to mention that we booked, in the last quarter, BRL1.7 million, which was a reassessment of our labor contingency provision. So that affected the number, but it's part of operations, part of the year -- more in the interest of disclosure that I mentioned it.

Finally, on page 13, talking about our EBITDA, we reached BRL100 million, improved 0.2% percentage point of gross margins. And this was impacted by the increase, especially due to the fact of the new store opening. Here, we have on the right, a very interesting analysis that shows how big is the impact of new stores, and stores yet to be opened.

We have two Raia Drogasils. One part is the Company that existed by the end of last year, that ended last year with 776 stores. The second part is the new stores that have been recently opened, and that are already in the process of opening. So the regional part of Raia Drogasil, the reason the 776 stores, and putting here 100% of administrative expenses and everything in, this operation turned the gross revenues of BRL1.38 billion in the quarter, so it's slightly lower than the total, because these stores have also generated some revenues.

BRL107.5 million of EBITDA, so the impact of the new stores and pre-operation expenses of future stores is BRL7.3 million in the quarter. So these existing operation, displayed an EBITDA margin of 7.9%. So and the impact of the delay in our store development is pretty major, I'd say.

And the main reason here is that we are entering in three new states. When you enter a new market, you -- because store licensing varies a lot from market to market, both tax and sanitary licenses. So in every new market, we have a steep learning curve in the beginning. So the first stores, we don't know our way around. We don't know how long the process takes. We don't know what exactly we have to do. So there are some delays caused because of that.

So one problem is taking on the opening store, another problem is not knowing how long it takes to open a store, which is a case in new markets because if you know, you take six months, for example, to license a new store, you start hiring at month three, and not at month one. But as we didn't know how that would evolve. We have hired in month one, and have paid salaries for six months in this example.

So we are in a peak of new stores' pressure this quarter. And that somehow penalized the quarter, and consumed part of the margin gain that we achieve in gross margins.

Next page, we achieved 3.9% of net margin, 0.5percentage points below last year's. The appreciation was stayed flat, but as we consume more working capital, we came from 0.6% of net financial revenues to 0.12% of net financially.

Page 15, talking about our cash flow. We generated BRL101.6 million in results from operation. We invested BRL113 million in cash cycle. But we got a benefit of BRL28 million in other current assets and liabilities. The main line here was the beginning of the recovery process for accumulative taxes.

So we already reduced taxes to be recovered by BRL18 million in this Second Quarter of the year. So our operations generate BRL70 million. We invested BRL50 million, the bulk in new stores, and generated the quarter, a negative free cash flow of BRL33 million.

On page 16, we show how our stock has performed over the last five years. Drogasil, this quarter, completed five years as a relevant, public company. Drogasil's offer took place June 2007, Drogasil was already a listed company, but with very low liquidity. So effectively, Drogasil became a relevant listed company, exactly five years ago, counting from the beginning of last quarter.

Over this time, the investors that have the persistency to stay in the Company, they multiplied the amount invested by 4 times. 4 times. This is very, very significant number, I would say. And the investors who joined us at higher IPO one year and a half ago, they multiplied by 1.2 times in only 18 months. So this has been a significant, very gracious cycle for our company which we believe will continue in the years to come.

So summing up all we have said so far, this is the five-year anniversary of Drogasil as a listed company. We have investment -- the value of the investment, multiplied by four times for those persistent investors that entered the IPO and stayed until now.

This quarter, we also started our synergy delivery that we have been talking for the last year, as shown by the gross margin increase that we achieved. We have also ignited our strong store development for the year, after a low First Quarter and new openings, we have now 47 -- counting today, 47 new stores opened. And we have a very strong pipeline ahead of us.

So that in the two-year period, between 2012 and 2013, we'll open a total of 240 new stores. This is a number I would say, unseen in our industry, especially at the bulk of this is pure organic growth. Besides the 26 stores in Goiania that should be available, first open by the beginning of next year, all the remaining stores should be pure organic growth, where which are the each of those stores with the potential. And we estimate the returns of each of those stores.

So it's the safest investment, plan around. Generally, our mature stores, they deliver an intern -- of 10 year internal rate of return in excess of 25%, Rio. And the new regions, that is north of 20%. It cost us 2 times EBITDA to open new stores. And we are opening 240 of these over this year and next year combined.

We entered three new states, two in the Midwest, and then Bahia, which is our gateway to the Brazilian Northeast. And it will be an important part of our growth program in many, many years to come. We started the recovery of accumulated tax credits after a four-year struggle. So we now have a clear path. We started transferring credits to suppliers. And we're just starting to -- the substitute tax collectors for ourselves. So until now, whereby at our distribution centers, and our suppliers will pre-pay our taxes.

Now, they are no longer prepaying our taxes. We only pay our taxes when we ship from one distribution center to our store. So as a result, not only this is a path for recovering the tax credits that are already booked, but also we have a working capital benefit here, because an important portion of our working capital, of our -- especially the value of our inventories, is taxes pre-collected. And we're now taking credit of those taxes, and we'll be recovering those taxes over the next two years. So this will be a significant cash generation for the Company.

And finally, last but not least, we are now preparing the corporation of Raia, which is a key pillar to the full integration of Raia Drogasil and the full construction of a single company with integrated logistics, IT, store managers, and everybody, everything else.

So this is what we have for you. And we're now open for questions.

Questions And Answers

Operator

(Operator Instructions) Our first question comes from Guilherme Assis at Raymond James.

Q - Guilherme Assis {BIO 16143141 <GO>}

Hi, Eugenio. Hello, everyone. Thanks for taking my question. I have actually two questions. The first one is regarding the difference in the same-store sales growth that we saw for Raia Drogasil in the quarter. You mentioned that Raia's relatively lower since Drogasil's growth was related to the higher base of growth that Raia had been quoted in the past few quarters. And Drogasil's in the opposite side, right?

I would like to understand like how the two companies stand in terms of sales per store, and what we should expect going forward in terms of same-store sales growth? My feeling is that Raia's still lagging behind Drogasil as the Company was actually coming from a much lower base before the IPO and the merger. That's my first question.

Second question, regarding the sales expenses that we saw. They're reaching something like 17% of the sales. And in the past, they were actually below, at around 16%. I'd like to understand that, with this ramp-up in the sales per store that we expect to have both at Raia and Drogasil, we should see it coming back to 16% of sales at some point after you complete all these investments that it has been making to improve the operations. Those are my two questions. Thank you.

A - Eugenio de Zagottis {BIO 7193695 <GO>}

Guilherme, thank you. First of all, we really credit the slowdown in Raia growth to the strong comp base. So if we stayed flat in sales from one month to the following month, in March, we're talking about 6, or something like that, comp, and suddenly, April we're talking about a 10 comp. There is no way in one month you could make that leap and keep the constant growth ratio that we were sustaining.

Raia has something like 10% lower revenues per mature stores, when compared to Drogasil. So yes, this is a significant gap, and a significant opportunity for us. If you look, the two years gap, same stores, mature stores sales growth, Raia is growing above Drogasil.

This year, it's not because of strong comp basis, although, Drogasil had a pretty easy comp base. But on the two-year, you should look, the two years together, it's undeniable that Raia is starting to reduce the gap.

Has the gap every been bridged? I don't know. I think not. I think there is an opportunity to reduce the gap. But I think Drogasil tends to be bigger revenues per store for mature store than Raia. Drogasil is a stronger brand in Sao Paulo. This is clear for me today, they're much more than it was when we were separated. Our customer service showed that in a very clear way.

When you compare Raia and Drogasil, two stores with similar potential, Drogasil generally sells more in Sao Paulo. Another issue is that Raia is more concentrated in Sao Paulo. So you take one neighborhood, like Muema, Raia has five stores, Drogasil has two stores. So there is no magic rule that says that both companies have to have different assets, actually have identical sales per store.

But yes, there is an opportunity to close the gap. And we will work on that. And that's our multi-year endeavor, and not a quick fix that we can do from one quarter to the next quarter.

As for sales expenses, it would be very simplistic to assume that a growth program like this doesn't have consequences. So it bring huge expense pressures. It could be higher sometimes, like we believe it's now. But even in a normal quarter, that expense is always built on. At some point, which I hope is not -- it takes a lot to happen, that pressure will ease off. But that means that we won't be opening new stores, or nothing material at least.

This is what happens to the American drug stores. You look, Walgreens, they now add 200 stores a year over 8,000-store base. So then, they have very little pressure from new stores. So the bad news is that we will have that pressure going on for a very long time. But the good news is that we're creating tons of value by doing that.

Another important point is that margins and expenses are not completely separate stories. We have inflationary pressures that not only for us, but for all retailers. And we're here to stay. So even without any growth impact, our expenses would be pressured. Last year, we had an 8% salary increase versus an inflation, I don't know of 5.5%, something like that, or 6%.

So it's -- this pressures our expense. But at the same time, as every retailer in the country feels that pressure in the same way, everybody is more inclined to work with better gross margins. In the end, the bills that are put on any company, either by the government if it's a tax, or by the economic situation of the country, is that inflation, for any builder who pays those bills are always the consumer of the product.

So I don't believe our sales expenses will get down to 16%. But a big portion of the loss between the 16% and the point at which sales expenses remain flat once again, the gross margins based for that. And that's part of the natural cycle of the business.

Q - Guilherme Assis {BIO 16143141 <GO>}

Just a follow-up if I may. Correct me if I'm wrong, but I think you mentioned that there's a difference in the performance from the brand, sometimes due to geographic locations, and distribution of the stores. But if that is the case, would you be considering like changing or converting stores from one brand to the other in order to ramp up sales?

A - Eugenio de Zagottis {BIO 7193695 <GO>}

Then the issue, Guilherme, is marginal economics. Because let's assume that we turn a Raia store into a Drogasil store. Potentially, yes, that could increase the revenue. And in specific places, we can try to do that. But overall, the world is bigger for two brands. So if we dropped one brand, we would be having a lot of self cannibalization of stores. We wouldn't be able to grow.

Before the merger, we wouldn't open stores any closer than 500 meters from each other. Nowadays, because we have two brands, sometimes you can open a store 200 meters, 300 meters of a pre-existing store, as long as a different brand.

So you can be right, but over a much smaller store base, which is not the strategy we're pursuing.

Q - Guilherme Assis {BIO 16143141 <GO>}

Okay. Thank you, Eugenio.

A - Eugenio de Zagottis {BIO 7193695 <GO>}

Thanks.

Operator

Our next question comes from Juliana Rozenbaum at Itau BBA.

Q - Juliana Rozenbaum {BIO 2155607 <GO>}

Hi. Good afternoon, everybody. Just a follow-up question. I'd just like to make clear why you can and cannot do, before the incorporation of Raia. So after you incorporate Raia, you'll be able to change brands among each other, so you need the incorporation to be able to do that. And if you also need the incorporation to use each other's distribution centers, and also if you also need incorporation to use -- to potentially use the good will from the merger? Thank you.

A - Eugenio de Zagottis {BIO 7193695 <GO>}

Juliana, first things first. So why incorporating? Because if you want to share distribution centers, if you want to have a single accounting, if you want to really unify and integrate processes, and do, and deliver the value proposal, this merger, which is bringing the best skills from both sides, the best competences, to do -- to build a truly distinguished company, we must be a single company to do that. I mean, no doubt about it.

There are costs direct and indirect of being two different companies. One of those is in my previous example. Right now, if you wanted to -- let's see in a company -- in a certain city, we have a Raia store that should be converted to Drogasil.

Nowadays, we will close the Raia store. We would lose our license to sell controlled medicines. We would lose our license to be in the pharmaceutical program. And there, we will have to reopen and reclaim those licenses, and be operating without them for a long period, and having the store close for a long period.

So after the incorporation, we can change stores from one brand to the other, and that's only like a center remain change. The end, it's the same legal entity. So to do all those things in a consistent way, we need to incorporate. So that's the first part.

The second part, why do we need to interrupt the opening of unlicensed Raia stores? Because we have to migrate every existing license from one company to the other company. This is a very complex and time-consuming process. So we have to have a cutoff at some point, and that point is now.

Because otherwise, by the time we incorporate a store that has been opened by Raia, would have to be shut down because Raia no longer exists, and be reopened. The market impact of closing a store in that situation is terrible.

So we are stopping with new unlicensed stores because from now on, those existing licenses will be migrated to Raia -- to Raia Drogasil. And that takes time. And all the new stores would be already opened, Raia Drogasil. Could we open now a Raia, a Raia Drogasil? Yes. From the legal point of view, we could open. But the Raia system is not able to sustain operations of the same brand within two different companies.

So we would spare a lot of effort changing our systems, in order with a lot of risk involved in that, in order not to interrupt stores, and to forego the opening of 20 stores. If you look over a long-term perspective, the value of 20 stores over the 900 that we'll have by the end of this year, something like that, I mean, this is dismal compared to the benefits of the incorporation.

As far as good will goes, good will has never been the goal or the reason for this transaction. The reason for the transaction was to build a distinctive company by two companies with shared values and visions, and have complementary assets, and keep abilities. The reason now for incorporation is really to allow our integration to happen.

So as far as good will, anything we will see further down the road.

Q - Juliana Rozenbaum {BIO 2155607 <GO>}

Okay. Great. Thank you. Just another follow-up. Is there anything that could go wrong in the transition from the existing stores into the new licensing? Is that a risk at all? Or just takes time, but it's easy to do?

A - Eugenio de Zagottis {BIO 7193695 <GO>}

We don't believe in many major risks, of course, that any human endeavor has risks. (inaudible), the walls and the ceiling can get down. We don't count on that. And we're planning, and do all we can for that not to happen. Could that be disturbances in one city, or another city? Could be possible, but that would not be relevant.

We have a huge concentration of stores in capitals. And in capital is one process for many stores. So before we actually initiate the merger, the corporation, which means say on the day for the general assembly, things like that, we'll have clarity that the bulk of the bulk of our stores will be on a clear migration path.

Q - Juliana Rozenbaum {BIO 2155607 <GO>}

Okay. Thank you, very much, Eugenio.

A - Eugenio de Zagottis {BIO 7193695 <GO>}

Thank you.

Operator

This will be the final announcement. (Operator Instructions) It appears to be no further questions. Now I'll turn the conference back to the Company for their final remarks.

A - Unidentified Speaker

Well, thank you all for attending this conference call. We remain very, very excited by the future we are -- we are building. Certainly, our perspective is always a long-term perspective. We don't disregard the short-term, but we don't take the seasons based exclusively on the short term.

So we remain excited by our store development prospect. We remain excited by what we can achieve, improving our operating standards, as a result of combining those distinctive competences in Raia and Drogasil brings to the table. I think structurally, the numbers of this quarter are good numbers, because the clear signal, the benefits from the cost synergies, although, somewhat affected by the expense surge from pre-operational expenses.

But I mean, we believe we are absolutely on path to bring this company from one level of profitability to the next level of profitability. And thank you very much.

And we'll remain available through our investor relations department for any context for any of you. Thank you, very much.

Operator

The conference has now concluded. Thank you for attending today's presentation. You may now disconnect.