Q3 2015 Earnings Call

Company Participants

- Marcelo Rizzi de Oliveira, Investor Relations and Strategic Planning Officer
- Peter Estermann, Chief Executive Officer

Other Participants

- Andrea Teixeira, Analyst
- Bernardo Cavalcanti, Analyst
- Gustavo Oliveira, Analyst
- Joao Mamede, Analyst
- Robert Ford, Analyst
- Tobias Stingelin, Analyst
- Unidentified Participant

Presentation

Operator

Good morning, ladies and gentlemen, and thank you for waiting. Welcome to the Via Varejo Conference Call to discuss the results for the Third Quarter of 2015. This event is being broadcast via webcast, which can be accessed at www.viavarejo.com.br/ir with the respective presentation. The slide selection will be managed by you. There will be a replay facility for this call on the website.

We inform you that the Company's press release is also available at its IR website. This event is being recorded and all participants will be in a listen-only mode during the Company's presentation. After Via Varejo's remarks are completed, there will be a question-and-answer session. 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 beliefs and assumptions of Via Varejo management, and on information currently available to the company. They involve risks and 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 Via Varejo and could cause results to differ materially from those expressed in such forward-looking statements.

Now, I would like to turn the floor over to Mr. Marcelo Rizzi de Oliveira, Investor Relations Director of the Company.

Marcelo Rizzi de Oliveira {BIO 21142716 <GO>}

Good morning. This is the call of the third quarter '15 earnings presentation. We will give you a presentation of the results and then a Q&A session. I would like to ask Peter Estermann, CEO of the Company.

Peter Estermann {BIO 15380447 <GO>}

Good morning, everybody. On behalf of all the management, I would just like to thank you for participating in yet another call of Via Varejo. Ever since the second quarter of this year, we have observed a very difficult environment for consumption in Brazil and particularly referring to that of durable goods. And the results of Via Varejo which we will present today have reflected this reality. Consumption activities in the third quarter has been very similar to that, which we have seen before in the second and there has been no additional deterioration in sales. These results have been in line with our expectations. So what I'm trying to say with this, is that the results have been no surprise to the company.

With this scenario in mind and facing this reality, Via Varejo's management has continued with all initiatives to readjust the structure of costs of the company. A great effort has been made to reduce personnel costs leaving to a leaner structure, which is more adequate to our current structure. We also have renegotiated events [ph] reducing our marketing expenses, optimizing logistics, optimizing our storage spaces in our distribution centers, so as to make the company adequate to this new sale level. And particularly, making the company better prepared and protected for a greater and more unstable environment.

I would like to underscore that we are continuing with our plans and we will step-up all initiatives and implement necessary actions with method, discipline and sense of urgency, so that we may guarantee even more significant improvements in the short and medium term. In this way, the adjusted EBITDA margin of 4%, which we obtained in this quarter does not yet reflect all the gains, which we expect to have with initiatives and adjustments, which I have mentioned before.

We expect that the results of the next quarter will already reflect all these efficiency gains implemented and which we are implementing in the company. We will also continue in our commitment to strengthen our brands and improvement of sales level. I will talk more about this later on.

As an example of our commitment, I would like to mention to you that we closed at the beginning of this month, an agreement or a negotiation with a global network of television for football or soccer package of 2016. This is one of the most relevant sponsorship packages in Brazil.

Before I ask Marcelo Rizzi to take the floor, it is important to mention also the commitment of our Company to soundness in production of our balance sheet. This is a necessary and determining condition, so that we maybe winners in this difficult and very challenging scenario, particularly for the durable goods consumption sector.

I would now like to ask Marcelo Rizzi to take the floor and he will present the Company's results and then I will come back at the end for some final remarks. Thank you.

Marcelo Rizzi de Oliveira {BIO 21142716 <GO>}

So the results of the Company on Page 4, the net sales of this quarter were 4,095 million and with the result of -- down 22.7% and unless -- because of the better performance of the Company and the drop was of 23 [ph] -- and in the nine months 16.8% and also the growth of 10 percentage points better than the Ponto Frio, which follows our strategy of Casas Bahia Banner, which is being relevant in the Ponto Frio stores.

In the quarter, we have opened five stores, which reflects our strategy with much more selective store openings and in this way, we will focus on greater value projects and we -- and the revitalization of concept telephony stores, 56 stores were opened under new furniture concept and 53 banner conversions, Ponto Frio to Casas Bahia. So we have been able to implement important initiatives to improve competitiveness and much clearer and improved sales in September and in October.

On Page 5, we have the gross profit. We totaled 32.8% and regarding the same quarter in 2014 and this was offset with gains in services, credit and merchandise margin and freight and assembly revenues. SG&A expenses, 28.5% and impacted by the increased inflation and dilution of fixed expenses. We must mention that this didn't fully capture initiative to reduce the cost structure. These expenses were realized during the third quarter and the benefits should be better observed in the next quarter, because we have had no time yet to show these and these initiatives leave us more prepared to face the markets better. With the reduction of consumption scenario and also the recovery of growth and the adjusted EBITDA -- the EBITDA margin of 4% under the nine months, year-to-date, we have a margin of 6.4% and adjusted margin of BRL887 million.

In working capital, we have an improvement of BRL3 million and minus two days of improvement of COGS, but we must mention that the Company is very well structured in terms of inventory for (inaudible) and the Company has no problem regarding supply, because of its sound balance sheet and credibility vis-a-vis its suppliers.

On Page 7, we will have the financial structure, where we show that we deliver a very strong position of cash and cash equivalents and we are prepared for the fourth quarter, where there is a seasonality with generation of cash and the cash position was BRL1.7 billion and we have a debt -- been in debt. We have a solid net cash position of -- a determined position necessary for -- to face up to uncertain positions and in spite of retraction in consumption in the third quarter, the company has kept the same cash level of the second term of -- second half of 2015. So we have had less receivables with a significant reduction of interest expenses, despite the increase of SELIC over the quarter.

Last but not least, on Slide number 8, we show adjusted net income, 33 million which was positive, despite the scenario to maintain adverse consumption reaching 237 million. At nine months 2015, a net margin of 1.7%.

I'll turn the floor back to Peter Estermann for the final remarks now.

Peter Estermann {BIO 15380447 <GO>}

And considering the three priorities that we consider to be crucial to our business, I'd like to make some remarks now.

First remark. We will be giving total focus on all commercial initiatives in order to guarantee and ensure our sales growth. And in this case, I would like to underscore a couple of points. First of all, our pricing policy with even stronger focus on specific competition at each and every region and also media and offering policy that supports this strategy over September and now in October. We foresee stronger response from our customers in terms of price elasticity and this has encouraged us to move forward with this strategy. On a weekly basis, we test for elasticity, we adjust our pricing policy in order to boost our sales, something very key in this area, which we follow-up on a weekly basis in order to boost sales but maintaining our cash market.

Second point, we want to continue have an adjustment of cost and expenses required to assure our competitive edge. We want definitely to improve our operating efficiency and what I mean by operating efficiency, relates to three key aspects; first of all, improve the level of service of our customers and in this case, the focus will be on shortening our product delivery times and also improve the quality of assembly services.

Second point, we also to focus our efforts to supply our DC levels and in this case, we'll be strongly focusing on reduction in our store counts and improve our assortments, adapting to each and every region in question and we're also going to focus more often on regionalization, significantly improving our sales conversion rate.

We're opening now the question-and-answer session.

Questions And Answers

Operator

So now we'd like to go onto Q&A. Please ask all your questions at once and await the replies. (Operator Instructions) Mr. Robert Ford from the Bank of America has a question.

Q - Robert Ford {BIO 1499021 <GO>}

Thank you and good morning. I have two questions. First, how can you save annually with the closing of 31 stores and the improvement of rents in the third quarter?

And second, do you have a disclosure about the operating expenses, but as Peter said, what about the sales level and what can you do so as to not to effect the service level and what can we do in the stores to have a greater value, but not affect the service and there was an improvement in September and October in the sales, but can you give us the figures, please?

A - Marcelo Rizzi de Oliveira {BIO 21142716 <GO>}

Good morning. Your first question has to do with the savings generated by the great or a more lean structure. The potential is at least BRL1 billion, with our initiatives since the second quarter of making the headcount leaner logistics marketing and renegotiating rents and the effects have not yet been mirrored entirely by our balance sheet. Possibly in the next quarters, we will have them more reflected.

We don't disclose specific monthly data, regarding your second question, but we know that sales are improving. These are the former quarters. There is still a drop in sales regarding last November, but it is improving and we hope to keep steady until the end of the year. This revision of the structure is to maintain the gross margins steady to make the Company competitive and to allow the Company to gain structural market share until the end of the year and for next year.

A - Peter Estermann {BIO 15380447 <GO>}

I would just like to add a little bit to what Marcelo has said. You asked about the adjustments to the stores without affecting the service. I would like to mention that any adjustments that the Company might make and there are adjustments to be made, that they will always take into account the customer service level. We do have productivity adjustments and store-to-store, we have the head count adjusted to each store and we have some flexibility to be able to serve or adjust to any demand. And if there are any additional things to be done, there always are, and we follow this weekly very carefully and we will keep the focus to have an adjusted structure -- cost structure to a reality, which allows this to be more competitive.

Q - Robert Ford {BIO 1499021 <GO>}

Thank you, Peter. Thank you, Marcelo.

Operator

Mr. Bernardo Cavalcanti, he's from Goldman Sachs has a question.

Q - Bernardo Cavalcanti {BIO 19852901 <GO>}

Thank you for this opportunity. I have three questions. The first is very simple. Do you intend to give us the guidance about the opening of stores in the few next years.

Second M&A, how do you consider the situation of your smaller competitors and what about sales from the closing of stores and what about selling off of stores lower price than historic and do you have any strategies which might be relevant to you? And what about keeping cash et cetera in the balance sheet whilst the crisis is developing? And what about your ideas about unemployment? And that's about M&A.

Second credit, we've seen a relevant increase of delinquency seen from the point of view of provisioning -- quarterly provisioning and last quarter to this quarter and in spite of all of this, and the credit portfolio of paybooks being set up. The sales through paybook today has maintained -- has kept stable. So is there a possibility of closing this profit [ph] 15% of sales carried out through playbooks, if the delinquency level, which is a level which makes us unseasonable in spite of the high rates of interest? Thank you.

A - Peter Estermann {BIO 15380447 <GO>}

Thank you for your questions. First of all, the guidance regarding expansion. We are being very much careful of course, times are more challenging. And we have 70 stores and we have greater focus on investment, which generates much more value and at this moment of less consumption. Obviously, the opportunities will crop up, but the greatest focus of the company -- if opportunity does come up, we will consider it carefully. There has been a deterioration of companies in the -- regarding credit, especially when we talk about the credit programs. We're adjusting 25% of past due payments and we will improve the session [ph] of assignment of credit to the client. And this will be better controlled due to the very poor scenario that we have now in the third quarter.

Q - Bernardo Cavalcanti {BIO 19852901 <GO>}

Thank you for your answers. At current levels of delinquency, which obviously are not sustainable, the credit today and yesterday, is it viable? Thank you.

A - Marcelo Rizzi de Oliveira {BIO 21142716 <GO>}

No, thank you.

Operator

Mrs. Andrea Teixeira from JPMorgan has a question.

Q - Andrea Teixeira {BIO 1941397 <GO>}

Hello, ladies and gentlemen. Just adding something to the gross margin, some questions, at the beginning of the call, but it was not very clear to me. Basically I understand that in September, there seemed to be an improvement of (inaudible) so is this improvement of -- does the reaction has really improved, will it continue in the fourth quarter and the same-store and will it continue? What's going to happen because of the holidays that we will have and that leads to the second question regarding advertising.

With your agreement with Globo, based on my calculations, you would have about 3.5 historically of revenues and -- in advertising with a lot of revenue, this will be heavier. So you -- I think, that this is -- advertising has to deal with the products. You will have two practice the same prices and the turnover. And I'd like to know, what you're thinking about the gross margin and expenses in marketing?

A - Peter Estermann {BIO 15380447 <GO>}

Andrea, thank you very much. Regarding the gross margins, it's very simple. We have defined the gross margins. We want to be competitive and close any deal [ph] in the store. A store is a place to do business. So we have defined the level of gross margin, where we have to be competitive and sustainable in the next month. We have defined this margin and we must reach it -- achieve it. We believe that we are the only ones in the market who can achieve this competitiveness. This has been the strategy of the Company and as regards --

Q - Andrea Teixeira {BIO 1941397 <GO>}

Well, wait a minute, excuse me. Well, you have the same online brand offering more competitive prices. So this assumption that the people are going to go into your stores to negotiate, it's not realistic at the moment. So my question is, well, six months ago, we also thought that the world wouldn't be so competitive. So it's valid to think that a year ago, this strategy perhaps could be working, but today it doesn't.

So this idea with Black Friday around the corner, with a very much more competitive scenario, we have just had third quarter, September which has just gone by. So it's not realistic to think in past terms. Things have changed.

A - Peter Estermann {BIO 15380447 <GO>}

Well Andrea, the margin will not continue at the level which you are thinking about. We have defined what the margin is to compete. So any competitor in the market compete with any competitor. So we look at the total market and so, considering everything in online and supermarkets, we define margin to be competitive and to close business and we will be competitive from now on.

And with this margin in mind, we are re-analyzing all the costs of the Company. And then the soccer package, this is part of the strategy as well. Why? Because the Company has implemented a methodology and it allows us to being very much more assertive regarding investments in advertising and these packages, soccer packages have also brought us greater value. This package has -- we will be able to deliver better investments in marketing, even with this package, which was a result of this new methodology of return on investment, which we have optimized and regarding the investment in media next year -- this year and next year.

Q - Andrea Teixeira {BIO 1941397 <GO>}

But what is the source of saving to invest more in advertising? Where is money coming from? On the bottom line, will this be more next year or not? Will it be the same 600 million, that's what my question is?

A - Marcelo Rizzi de Oliveira {BIO 21142716 <GO>}

Well, we have -- what's going to finance the soccer package. We've managed to reduce the total marketing expenses of the company and even though, agree to the soccer package and invest more in marketing. So we can invest in the soccer for next week, next year. So we are expecting more sales, not only for the next quarter, but for next year.

Q - Andrea Teixeira {BIO 1941397 <GO>}

So you are expecting an inflection in sales in the fourth quarter, is that it?

A - Marcelo Rizzi de Oliveira {BIO 21142716 <GO>}

We are expecting a better result than September and October. Yes, we still have a drop in sales, but it is at a different level than we have in hand [ph] in the former courses, yes but still with the risk of drop, right?

Q - Andrea Teixeira {BIO 1941397 <GO>}

But you still have a risk of a drop?

A - Marcelo Rizzi de Oliveira {BIO 21142716 <GO>}

Yes, from the current level.

Q - Andrea Teixeira {BIO 1941397 <GO>}

Okay, thank you.

Operator

Tobias Stingelin from Credit Suisse has a question.

Q - Tobias Stingelin {BIO 18290133 <GO>}

Good morning, Rizzi. Good morning, Peter. I'd just like to understand something better. In the third quarter, the commercial margin went down 150 bps like you said and sales were still very poor. You're saying that naturally things are improving just by they're still negative. So the question is, what kind of margin is necessary to resume sales, because 150 led to 25 in the fourth quarter, I assume that well, you did the math about sales, but I assume the impact has to be very strong. So am I right to assume that?

What about the fourth quarter and what about the adjustment? Should it be protected by the cut down on expenses that you did? And that will also lead to a stronger result later on?

A - Peter Estermann {BIO 15380447 <GO>}

Tobias, hi. There are two things here as of September. We are working on some initiatives, not only in terms of price, the level of margin reduction for instance is slightly higher compared to what you saw in our earnings release. But we also see more elasticity this quarter. And above all, we are improving our store efficiency, so the conversion response has been also decisive to boost our sales. Price is an important lever, an important driver, but conversion also consider a more intelligent strategy, pricing and better service to customers. These are important drivers we're working on too. Naturally, price has a very strong relationship with sales, but we're also focusing a lot on store efficiency.

Q - Tobias Stingelin {BIO 18290133 <GO>}

Okay, let me see if I've got that correctly. So you had an aggressive reduction in expense of BRL1 billion, then sales were going down over 20%. And now you stop and said, okay, we're going to be more price aggressive, because you want to close deals. So the question is, what about the cut down that you did? Did they already allow you to work on the level of margins that you expect to see to boost sales or would you have to be even more aggressive in terms of breakeven in order to run with this level of gross margin. I know that once you recover sales, it will also have an impact on the operational leverage, but what about expenses, cut down expenses, how do you get to these numbers?

A - Peter Estermann {BIO 15380447 <GO>}

We're adapting the cost structure naturally allowed us to have significant competitive edge, but our daily management and very surgically is in the cash margin of the Company. For instance, think about addition of sales considering our investment -- margin investment and then monitor this daily as a company. So if we have more sales, we invest in margins and we keep on doing it.

Q - Tobias Stingelin {BIO 18290133 <GO>}

Okay, so the question is, under the current breakeven, what do you have to the current breakeven point if sales keep on going down 10 or 15, you have to work even harder on the breakeven point, does that make sense? Maybe closing another DC or more stores or you'll have to close more stores to do that?

A - Marcelo Rizzi de Oliveira {BIO 21142716 <GO>}

In terms of stores, if you have store problems or problems that are underperforming, not contributing to a reasonable adequate margin, then possibly we'll be closing more stores. And by closing these stores, we improve profitability and we can finance competitiveness. So chances are that we'll be closing more stores over the fourth quarter or next year if these stores underperform and are not profitable to the company.

A - Peter Estermann {BIO 15380447 <GO>}

Tobias, just adding to the comment -- to Rizzi's comment, one of the initiatives that we decided to embark on very recently is to separate under-performing stores. So today for instance, we are very much oriented to these stores that are underperforming or that are negatively performing and we also have extremities start of action plans to recover the result of these stores and I'll tell you more.

We also have opportunities to improve the results of these stores, focusing on aspects that depend on our own concrete actions. So in terms of reduction of stock out adjustments in store assortment, better supply levels, and reduction of product delivery times at these stores, so we already have thorough analysis of underperforming stores and we have been very assertive in terms of recovering the result of these stores.

We've been following up weekly the performance of these stores. Like Rizzi said, after everything is done, we understand the stores are still under-performing. Naturally, we have to do something about them, but we are pretty much focused on trying to bring these underperforming stores to the game again.

Q - Tobias Stingelin {BIO 18290133 <GO>}

Perfect. Maybe just one last question. I know it's very hard to say, maybe you don't want to give a specific guidance. It's hard to tell what will happen over 2016, but if you consider scenarios and I believe, other companies also tell in the conference call that everybody expects 2016 to be even worse.

We also have the payroll tax benefits that came to an end, a lot of pressure from suppliers. So there are some variables that lead to assumptions.

Is it reasonable to assume working on 5% or 10% drop next year and then there are other impacts that I've mentioned before tax benefits. And with the price reduction, we will try to have a stable margin vis-a-vis this year. I know there are so many variables, but we just want to have some direction, maybe things may improve and there may be upsides, but you're trying to consider a more pressured scenario?

A - Peter Estermann {BIO 15380447 <GO>}

Tobias, Peter speaking. Like you said, it's too early to say anything. We are just in the middle of our strategic planning, discussing our budget. We have already managed to quantify all the variables that you mentioned. To be very candid with you, considering everything we have already done at the Company level and everything that we still have to be implement in the short-term, I would say, we are confident to face 2016. We are not ready to talk about 2016 yet, but rest assured that we're working on it, we are addressing all these variables and analyzing the Company's current circumstance.

We are confident that we will be able to face -- or we're very determined to take the challenges for 2016. As the cash, this will be decisive to win the game and to be much better off next year. You touched upon that very critical point, which is a provisional measure, the payroll tax benefit, these are very important points and if you have a solid cash balance, this will help the Company to get stronger, despite this challenging scenario or slowdown in consumption or even to be stronger to rebound next year.

Q - Tobias Stingelin {BIO 18290133 <GO>}

Thank you, Rizzi. Thank you, Peter.

Operator

Joao Mamede from Santander has a question.

Q - Joao Mamede {BIO 15265292 <GO>}

Good morning, everyone. I would like to talk more about discount of receivables. So this quarter, you did not have this discount and that will have a significant impact on expenses in the future quarters. Maybe you just hold up in order to have more favorable cost over the next quarter. So this quarter, it's clear to me that circumstances are not expected to improve and maybe costs will be even higher compared to what we have today. So I would like to understand the rationale or why you did not discount this quarter.

And the second question is about the negotiation with suppliers by year-end. You mentioned in the presentation, that you have high inventory level, expecting a better year-end with Black Friday, Christmas season. So it is challenging for retail or maybe even worse for industry as a whole. So what is the order of magnitude to improve negotiations in terms of price and terms and conditions with suppliers in general? These are my two questions. Thank you.

A - Marcelo Rizzi de Oliveira {BIO 21142716 <GO>}

Hi, Mamede, how are you?

Q - Joao Mamede {BIO 15265292 <GO>}

How are you, Marcelo?

A - Marcelo Rizzi de Oliveira {BIO 21142716 <GO>}

Good. Let me start answering about inventories. If you look at our inventory position today, it is similar to the inventory levels last year at nine months. So with the slowdown, possibly inventory levels should be lower compared to the previous year. But this is if you look backwards, but if you think about projections, you look to the future. So we project and expect to have better sales compared to previous quarters. So this position is very strong for Black Friday, Christmas and to our big sale.

And plan B, if projections don't meet our expectations, then we have these three sales events and then you can always buy less in December, January, and then, you can adjust your inventory levels, but we always have an over-projection compared to the initial strategy. As to receivables discount, with the high SELIC rate, the Company has decided to use more cash to owner short-term commitments. I think you're familiar with our treasury operation. Anyway, the company will have to discount again to set the cash level to meet the minimum levels.

So this strategy provides better control of financial expenses, 1.7% of net revenues vis-a-vis 2.8. Now if we don't use this strategy in the fourth quarter or next year, well, it's too early to say anything. That will depend on the cash needs and requirement, SELIC progression. So it's too early to tell the strategy for the fourth quarter.

Q - Joao Mamede {BIO 15265292 <GO>}

Thank you, Marcelo, just a follow-up question about the first point about negotiation with suppliers. What about the improvement in negotiations achieved. Did you manage to have more discount, more -- or longer terms? What is your focus right now?

A - Marcelo Rizzi de Oliveira {BIO 21142716 <GO>}

We have a solid partnership with suppliers as you know and this year, our relationship became even more intense. In times like these, we have a lot of joint strategies. So in terms of price improvement, terms and conditions, everything is in the package now, we cannot disclose the strategy, but certainly, we can tell you that this year, things are harder for everyone, but we are having nice conversations with our suppliers, with a very well set strategy.

Q - Joao Mamede {BIO 15265292 <GO>}

Great, thank you, Marcelo.

Operator

Mr. Gustavo Oliveira from UBS would like to ask a question.

Q - Gustavo Oliveira {BIO 15129435 <GO>}

Good morning, Marcelo, Peter. I would like to start with costs. These extraordinary expenses of restructuring and then I would like to ask some questions about the top line and BRL119 million of restructuring in this quarter were higher than the ones that we saw in previous quarters, but you make some very large readjustments and you had cut 5,000 previously in expenses. As most of these costs have dropped in the third quarter, but are they part of adjustments which already started in the third -- in the previous quarter or not or are you focusing only what is happening in the third quarter, with -- and that the closing of 30 stores. First, I'd like to understand that.

A - Marcelo Rizzi de Oliveira {BIO 21142716 <GO>}

Well, it has to do with the expenses of the quarter, yes. But obviously, it is also the continuation of our efforts to cut costs and always improving margin assets, but also the improvements of competitiveness and commercial competitiveness of the Company, because we want to establish a competitive level which is lasting, not only just one month or another. But we really want the company to have a lasting strategy as far as competitiveness of the company goes.

Q - Gustavo Oliveira {BIO 15129435 <GO>}

So my question is the following. I'm asking this because with your reply, I believe that the closing of a store costs more than just to send -- just to lay some people off, you have -- and also you will have to pay the fine of -- resuming [ph] your rent contract. So do you have any estimates regarding how much on average it will cost to close a store?

A - Marcelo Rizzi de Oliveira {BIO 21142716 <GO>}

Well, the expenses with headcount and with personnel is the largest component of this expense and the closing of the store also is important. It's an important expense, but even so, it's very different.

Q - Gustavo Oliveira {BIO 15129435 <GO>}

Well, that doesn't make sense Marcelo, because if it was this, the expenses in the second quarter, the extraordinary expenses would also be similar expense to that of the third, the same number of people. I think we're closing off stores, must have a higher component than that -- just that of people.

Well, just to remind you that a lot of the expenses -- most of the expenses of stores of people. It also has a -- it comes into the cost of headcount and not of stores. But it was more than 11,000 people in the last two quarters. So in fact, it is not proportional. We closed 36 stores in the last two quarters, 36 stores. So this is where the difference lies.

Well, then I'll follow up here, but just to understand a bit more, going back to the question of opening stores. You want to expand your company, but you're closing some stores, you're still trying to recover some, but will you be able to recover these stores until Christmas and continue closing next year? Have you got any numbers that you can give to the market in terms of specific plans of stores with performance as well below the desired, so that you would consider keeping them open?

A - Marcelo Rizzi de Oliveira {BIO 21142716 <GO>}

Well, obviously. We have a priority to avoid closing stores, but should it be necessary, we will have to take -- make quick decisions. We have today a group of stores. I don't want to give numbers yet, but we do have a group of stores whose performance is below average and some will even have a negative performance, but we have been through this analysis in depth and we also have some concrete medium to long-term opportunities, which can leverage this situation more.

We have stores that have a similar competitive situation, in similar region to other stores who have very different performance levels. And we have to look at these things in greater details, (inaudible) this performance and find out the root cause of the very deviation.

We are optimistic that we will be able to recover sustainably the performance of these stores, so to be determined [ph] in a project of this kind, you do a weekly, monthly follow-up of the effectiveness of actions implemented, you carry out your corrections and you will have to make a decision sooner or later. I would say that you need at least three months. It would be a relatively fair period to have the possibility of what have to be done and if we think that our internal result is running out, we will decide to close.

Q - Gustavo Oliveira {BIO 15129435 <GO>}

Thank you, Peter. Peter, now the business of top line and concentrating on the Company and you have told that the focus was on sales. The strategy is very different from what you have had up to now and it's still not clear to me, how or why you are seeing these more optimistic signs of demand elasticities, just consumption or the consumption trends are worsening and probably will continue to worsen. I think this is very much in keeping with the fact that you really have to give up a lot of gross margin or not. What do you think is changed and why the demand elasticity -- I mean, this is just not very clear to me at all.

A - Peter Estermann {BIO 15380447 <GO>}

I think that there are some important components here to consider. First of all, this has to do with our positioning strategy. I'm not going to go into details on this of what we have implemented and our strategy of pricing, but we believe that by the reaction that we have had of sales that we have found a point of the margins that we have found a situation where we can leverage sales and this will help us to restructure our sales and improve them.

We are more competitive in terms of structure and costs and we have found a margin level, which has leveraged our sales. So I would not say that we are optimistic, but we trust that we have found the right level, which will allow us to continue to grow protecting the Company's margins.

Q - Gustavo Oliveira {BIO 15129435 <GO>}

When you think about margin, you were thinking of gross margins. Okay, but before you were working between 9% and 10% of margin EBITDA in a more balanced scenario to have a more lasting scenario for the Company, where you could have a better market share. Do these numbers continue at the same level, 9%, 10%, should that just be margin or what?

A - Marcelo Rizzi de Oliveira {BIO 21142716 <GO>}

Well, this is Marcelo, again. Obviously, with this new sales level, it's very difficult to obtain this EBITDA margin that we achieved at the end of last year. But we do think that if you have a sales recovery with the cost reductions that we have had and the prices at the same level of 2014 or more, we will have -- even have higher levels that we delivered at the end of 2014, but obviously, with less sales that we had at that year, because of recoveries, the restructuring has been very deep in the Company.

Q - Gustavo Oliveira {BIO 15129435 <GO>}

Well, going back to the agreement with a Globo network, what is the fixed and what is the variable component of this contract for next year?

A - Peter Estermann {BIO 15380447 <GO>}

Well, we do not disclose this. This is very confidential to the Company. Well, it's just that because the impact will be huge and if it doesn't come through, the impact will be huge. The marketing cost will be reduced according to sales reductions. We have readjusted all the marketing costs, the football or the soccer package is one of the marketing costs, but it will not alter the structure.

Q - Gustavo Oliveira {BIO 15129435 <GO>}

And the last question is, what are the initiatives of Click & Collect. So is this your sale or is it the turnover sale and today, what are sales in the Click & Collect?

A - Peter Estermann {BIO 15380447 <GO>}

Peter speaking. We have two modalities of joint work with e-commerce and one modality that we could call the traditional Click & Collect, is when e-commerce itself, it's inventory, so it's the e-commerce inventory sold in e-commerce and the client can pick-up this merchandize at these brick-and-mortar stores, that is one modality. We have about 500 stores that operate under this model and it's a significant number, it's very relevant and this model is approved and tested and is working well. And then we have another model, which is what we call marketplace. When the e-commerce sells the inventory of us brick and mortar stores and in this model, we already have more than 1,000 stores with e-commerce selling our inventory, and in this case, also the client chooses which store you wants to pick up his product.

Obviously this model as a whole, still have an important maturation product, but the greatest gain that we have deferment is operating -- operational wise and in terms of systems. The model is implementing and -- implemented and working and we are working on the efficiency and effectiveness of sales conversion and added sales and value to the stores.

Q - Gustavo Oliveira {BIO 15129435 <GO>}

And the sales conversion, is that coming from e-commerce? Is it significant?

A - Peter Estermann {BIO 15380447 <GO>}

As I have told you, we have focused significantly to begin with and the implementation of the model and we will start working now and we have started measuring the efficiency of the model. Our expectation was very positive regarding added -- adding revenue to the brick and mortar stores in this model.

Q - Gustavo Oliveira {BIO 15129435 <GO>}

That's very clear, Peter. Thank you.

Operator

Mrs. (inaudible) from the Citibank has a question.

Q - Unidentified Participant

Good morning. I would like to elaborate a little bit more on these investments in gross margin, that you have made in the third quarter. Was this proportional regarding categories of products over these specific products that you wanted to offer special discount or what's going to happen from now on particularly on special dates like Black Friday or Christmas, my first question.

Second question, yesterday you advertised in Cnova. They said yesterday in there that they will be talk about sustainability et cetera. I would like to understand, if this is going to benefit the sales of the Via Varejo et cetera?

A - Marcelo Rizzi de Oliveira {BIO 21142716 <GO>}

Hello, (inaudible). Regarding the categories question, we obviously have better and worse categories. We have a portfolio of categories and we manage according to elasticity of each one. What we have noticed is main highlights, smartphones, but also a category that has been very positive is air conditioners and this is seasonal. This penetration is growing and Brazilians are buying a lot. So we adjust things according to the elasticity of each category.

Now these are the highlights, these two categories. And the others are performing more or less at the same level. So these two are more outstanding and will be more aggressive. They are the ones that has had a better performance as far as sales goes.

And the question regarding Cnova, the strategy of Cnova does that benefit or affect generations? The two teams are aligned and they know what strategy they should adopt, so that both companies can have a better performance in the fourth quarter and focus then on for next year. So the Cnova strategy besides we discussed pricing and product with them, but these two companies are very important for the Via Varejo and well aligned as well. Thank you.

Operator

This concludes the question-and-answer session. I would like to give the floor back to the Company's management for the final remarks.

A - Marcelo Rizzi de Oliveira {BIO 21142716 <GO>}

Thank you all. Good afternoon. Don't hesitate to contact us if you have any further questions about our earnings. Thank you very much.

Operator

This concludes Via Varejo's Conference Call. The Investor Relations Department will be at your service for any other questions you may have. Thank you all for joining us today. Have a good day.