Q2 2019 Earnings Call

Company Participants

- Andre Correa Natal, Financial and Investor Relations Executive Officer
- BRDT
- Rafael Salvador Grisolia, CEO
- Unidentified Speaker

Other Participants

- Andre Saleme Hachem
- Bruno Montanari
- Christian Audi
- Gustavo Allevato
- Regis Cardoso
- Ricardo Schiavinato
- Thiago Duarte
- Vincent Falanga

Presentation

Operator

Good morning ladies and gentlemen. Welcome to the Petrobras Distribuidora Webcast and Conference Call with analysts and investors to present our results for the Second Quarter of 2019. We inform you that, participants will attend the webcast and conference call as listeners-only. The presentation will be followed by a question-and-answer session, when further instructions will be given. (Operator Instructions).

Today, here with us we have Mr.Rafael Grisolia, CEO; and Andre Natal, CFO and IRO. We'll remind you that this meeting is being recorded and ask you to pay special attention to slide number 2, which contains a warning for shareholders and investors.

This presentation may contain forward looking projections. These projections are merely the expectations of company executives about future economic conditions. In addition to the sector, we operate in the performance and financial results of the company, amongst other things.

The terms projects, believes, expects, forecast, intend, plan, project, objective, should and other such terms are used to identify such forecast, which, of course, involves risks and uncertainties seen or not seen by the company and, therefore, do not provide an assurance as to company's future results. Future results of the company operations may differ from current expectation and readers should not solely rely on the information set out herein.

The company undertakes no obligation to update the presentation and projections in the light of new information or future development. Figures informed for 2019 onwards, are estimates or targets. Financial and operational information set out in this presentation are rounded. And the total amount is presented in graphs. Therefore, could differ from numerical aggregation of the preceding numbers.

We point out lastly, that this presentation also contains certain financial indicators that are not recognized under BR GAAP or IFRS. These metrics do not have standardized meanings and might not be comparable with similarly describable indicators used in other companies. We disclose these metrics because we use them to measure the company's performance. They should not be used separately or as a substitute for financial metric that have been disclosed and under BR GAAP or IFRS.

The second quarter earnings presentation for Petrobras Distribuidora will be delivered by the CEO, Mr.Rafael Grisolia. After that, another officer will be available to answer participants questions.

We will now pass the floor to Mr.Rafael Grisolia.

Rafael Salvador Grisolia {BIO 16673583 <GO>}

Good morning, everyone. We're there week after the privatization of BR we continue to be very happy and motivated for such an important time for the company. This is the first earnings release conference call, after the privatization process, but we've been here for a week, so it's important to highlight that the second quarter has specific point that we will comment on, but obviously, the entire discussion for the follow on everything we discussed with investors.

For this moment of the privatization, that was being based on figures of 2018 and knowing that for the first quarter there were our comments that were not recurrent in terms -- were identified in the value proposition for the follow-on.

It's also important to remind you that during the follow-on in order to address our value proposition for the short and medium term and our plans, we had that list of 10 initiatives. They are valid both for the gas station, network, as well as B2B. So -- and the second quarter validates that in terms of planning. How we will address that to transform the value of the company by following those 10 initiatives. We are very enthusiastic about them and working to implement all of them, of course with the different timing, but all of them are important and they have a reason to make a consistent value creation process and seeking the optimum profitability and balancing its market share.

I would like to remind you that the 10 initiatives are driving the idea of changing our pricing system, our mindset, working with the different sourcing, culminating that with effective logistics cost also correct balancing of people expenses. Our value proposition for customers both resellers as well as in B2B market, how much we can bring in an effective marketing value that allows customers and suppliers to recognize the value of our proposition to create value.

Meaning that, we have a strong brand of premium products and reinforcing our relationship long-term relationship, we must have with the entire network of customers and resellers. Also, we'll continue to work on portfolio, on legacy systems focusing on our business and working within our view of where BR had plans to grow, and following its aspiration to grow.

In terms of developing new businesses, especially in the area of convenience, lubricant and means of payment and loyalty program. So during the entire road show process and follow-on the year of 2019 and '20 are years of execution. And we'll work very hard to deliver the 10 initiatives altogether. So that as of 2021, we can see the results of such an enthusiastic and strong effort that we will make now with since the privatization of BR.

In May, I was talking to the market about the earnings results of the first quarter of BR, and we were already talking about what had happened in the first quarter, regarding some strategic decisions that were made previously and that remained in the second quarter about searching higher volumes, a stronger presence. And what is the right-balance for selling purposes, in terms of our market presence.

And this remains in this period as well, and we made some internal discussions, and with our presence now and reviewing with managers and the board of directors, we changed the strategy a bit to make it in sync with the 10 initiatives.

So only change in pricing was not adequate. That's why in the follow-on process we addressed the 10 initiatives together, it's not only one thing or the other, but the whole process. There's logistic costs, the market value proposition, so this has been our value proposition during the follow-on, so we start to work on that in order to deliver the first results and the first reflections of that in the next quarters.

The second quarter in addition to having the impact that the previous strategy, the strategy that was implemented before we entered the company. It has things that are opposite to what we saw in the first quarter. In the first quarter when we presented the results to the market and we didn't give the disclosure as to the size, but we had reflections from inventory gains, that the prices of the refinery is going up, which is very common in our business. The second quarter had a symmetric reflection, the prices at the refineries, especially in June going back. Especially gasoline, and it's always seasonal reflection, in inventory regarding ethanol, because when you start the harvest season, it has an impact on that.

So you have effects in the quarter regarding previous strategy that was not aligned to our propositions made in the follow-on and the 10 initiatives that together will be able to address improving profitability, differently from our competitors that say where BR should be. Now more than ever that is being privatized. But in this package of the 10 initiatives together, we have to be able to address scale but -- metrics in our market share and presence in the business.

And the final message, it's important to see the accumulated the year-to-date results. When we look at EBITDA year-to-date BRL70 per cubic meter, we want a good indication, a recurring level of EBITDA per cubic meter where the company is working today. 85 is the recurring level, which we believe is what we have worked as the follow-on, which is based on the figures of 2018.

So this is why we're so enthusiastic and inspired to create value. So again, the reference is what we see in our largest private competitors. They have a higher profitability than us, so everything we did is planned on the pillars of BR, its staff, its presence in terms of logistics and scale and how much potential it has, and now it will deliver after the privatization process. These are the main messages. Now I will let Andre talk about the financial aspects and then we'll move to the Q&A.

Andre Correa Natal {BIO 21073585 <GO>}

Good morning everyone. That's the main message, privatization, this is the main event of the quarter. And again, just talking about the figures again, when we look at the long-term windows, they are better or a better representation of where we are. For example in margins when you look at isolated quarters we mentioned that as a follow-on.

86 of the margin of the first quarter was not a good reference. As well, we don't understand the BRL 74 and the EBITDA margin for this quarter is a good reference either. So looking at semester or even annual windows is a more intelligent way and better way to see the company and from now on we're looking at figures at the end of 2018.

So just to resume when we look at the average EBITDA, which was BRL62 per cubic meter, when we look at the average for the first quarter of '16 -- or the first half of 2018 was BRL64, which is a similar figure. We had problem problematic events such as the truck drivers' strike and despite all that it's a good average, so this matter we had BRL70 accumulated year-to-date margin. So in this semester, we already conveyed the IFRS effect, so it has a difference from measures. So making this adjustment BRL76 per cubic meter in comparison basis to last year, so you're talking about BRL62 or BRL64 as compared to last year for the first half and full year versus BRL76. So this is the figures we're looking at when we see challenges ahead.

Then in addition, I would like to highlight the fact that we make variations from quarters to the next quarter are not always a significant information. In this particular case there is a major difference from BRL86 in the first quarter to BRL54 now in terms of margin. It's important to highlight the following. And in the release we provided more detailed information about that to try to help you.

Although, we don't want to get into a discussion of detailed about the inventory effect in one quarter or the next, but we would like to help you understand these sequential gap. And when we made that in the release, we emphasized, especially in the areas of largest different resale -- resellers and largest consumers we had a high margin. And the main differences were in resellers as in large consumers. So we tried to help by showing the variation in the non-recurring items.

So this variation of inventory effect for example was too high and too concentrated in these two areas. Rafael already mentioned that, due to prices of ethanol, gasoline in June et cetera. But the main point here is that when you look at resellers, for example, this effect of BRL80 per cubic meters, because the same effects that happened in the first quarter happened in the second quarter. So BRL44 that was the difference for the March EBITDA margin, BRL30 where it could be understood as non-recurring effects, such as accounting or booking effect.

So and another part of it that could be understood as more of recurred items that refer to replacement margin, or sales margin, explains that it dropped during the quarter as compared to the first quarter or the quarter before. But there's something very important to bear in mind, we were in a test due to the losses in ethanol and diesel in January, as compared to the previous month.

We had a loss in market share 1.7% in diesel and 1.8% in retail, so these were concentrated fast and significant losses. So back then we understood that the replacement margin was the a bit higher than the stability level. The company made a decision to reduce that margin and go to recover the market share.

So that happened in March, April and May, but that was reverted as of June. So May, was the peak of these movement to regain market share. So the message is that, even here we could understand as a more recurring effect which has to do with the margin of the everyday business. It's not necessarily current, because it was based on a decision made at the time to regain market share and decreasing margin at that time.

So the message in addition to everything it Rafael said, is that even this recurring factor does not represent the value driver. This is not how we intend to create value, we understand that we have more to gain based on a consistent price policy rather than this type of positioning.

So I would like to stop now and open for the Q&A session. But these are the main messages. And we remain here together Rafael and I, and we are very excited about all the possibilities, events and the follow-ons. And we're able to answer your questions. Thank you.

Questions And Answers

Operator

(Question And Answer)

Thank you. Now we'll start the Q&A session. We request each respondent -- each participant to ask two questions at the most. Slowly, and in a sequence so that they may answer -- be answered after that. (Operator Instructions) ri@br.com.br for the company to reply at a future date.

The first question comes from Andre Hachem from Itau.

Q - Andre Saleme Hachem {BIO 20209966 <GO>}

Congratulations on the privatization, Rafael and Andre. I would like to understand how do you expect to release value after the privatization? What has changed? For example, at how energy do you see the new contract? And if you were to list a series of actions for the next month or quarters, what would be the first action to be taken and how fast they will have effect?

A - Rafael Salvador Grisolia {BIO 16673583 <GO>}

Andrea, thank you. This is Rafael speaking. Thank you for your question. We are so enthusiastic because it's so clear for us. What actions we should take. We have these 10 initiatives. They all have been addressed, and every week we have a group where the key executives of the group and we follow -- we make a follow-up of each initiative. We're working very hard on that. Immediately after the privatization, there are things that's already changed the company. Last week -- as of last week, the procurement system does not follow the sales methodology of state-owned companies. So now, we are working on how to purchase items? How to make agreements and contracts and engagements and hiring people, not following the state-owned companies law.

This has been changed already, now company is working with the negotiations and agreements and following the best market practices, which is connected with our initiative to manage expenses, which is to review and revise all the agreements we have signed, because now that we are free from the more older system. Let's say there was more slower because it had lots of paperwork to be followed in the older state-owned system, now we gained agility. So all discussions all discussions about pricing, gross margin, Marcelo Braganca in operations and logistics is talking, deciding on trading imports, all the decisions for the best procurement in office is already being taken care of. Our marketing program is being revisited.

The new proposal to work on their station imaging. We need all the initiatives to take place at the same time, to deliver a consistent package. So, we won't be prone to reactions in term of, market share loss or gain. So, we're working on creating cards as means of payment, it's a new stage now everything is going on, and now we are very disciplined in terms of management, involving all the executives as the key executives in terms of people management which is so critical.

The main value of the company are our staff, our people. So we need to redesign what we plan in terms of careers for everyone, how to hire new people? We have engaged consultants. After the follow-on, we have defined these engagement contracts for them.

So my due date is yesterday, but of course, we have a one and a half years for them to implement everything here 2019 and 2020.

Q - Andre Saleme Hachem {BIO 20209966 <GO>}

Very nice. And second question is, I would like to understand, how is initiatives after the offering? Do you look for people to -- for the new board? How would that gets developed in the following months?

A - BRDT

Yes. Investors are taking part, they are suggesting names. Petrobras is also doing that, recommending some names. So in one or two weeks, we will propose discussing with the current Board of Directors, these -- to call a new shareholders meeting, that must take up to 40 days after the privatization. We must call a meeting of shareholders. So that investors can vote on the new board members, according to the new by-laws of the company. So we are personally involved in that process, talking to investors, Petrobras, with the board members. And there's some names that are very interesting and would -- could contribute to the value proposition of BR and we'll soon announce that to the market.

Q - Andre Saleme Hachem {BIO 20209966 <GO>}

Okay. If you could have a profile for the people for the new board. Would you rather invite people who are technical financial?

A - BRDT

In everything in life, balance is the optimum, we should seek in life. So, I think we must have all kinds of profile. The current profile is very good. But in terms of board members profile, we have to have people with experience in fuel distribution, this is important today. We don't necessarily have that person and financial experience. Finance is always important, strategy profile is also important always. The profile retail and technology is also important for our aspiration of growth and further development. So these are the types of profiles we would like to have at the board.

Retail I mentioned, technology and means of payment, so the combination of these profiles people in financing, retail, fuel distribution, IT and means of payment are key profiles that we look for. And we're talking to investor and they are providing names, IT and means of payment are key profiles that we look for. And we're talking to investors and they are providing names.

Q - Andre Saleme Hachem {BIO 20209966 <GO>}

Okay. Thank you very much and congratulations on the privatization transaction.

Operator

Our next question comes from Gustavo Allevato from Santander Bank.

Q - Gustavo Allevato {BIO 18933135 <GO>}

Good morning, everyone. Good luck Rafael, Natal for the new team. We'll see a major change going in, on in the following month. But the first question to try to understand the pricing, there has been a drop of margin throughout the first half of the year. What could we expect for the next quarter, next half of the year, in terms of gross margins without considering inventory effects?

So, we are -- we don't know exactly what is the starting point. And the second question is, looking at the consolidated figures income. What is faster to implement among those ten initiatives? As Rafael mentioned, some changes have been made, but what are the things that we could see some actual results already in the second half of this year?

A - BRDT

Hello Gustavo. Well again, what we always look at of course we don't give guidance in terms of results, so don't take this as an indication, But what happened was the share movement, that was tough in January, market share data, there's always a lag in it as it is published for you as for us. You know the market share of January at the end of February. So you're almost in March, and the movement was strong enough to cause us to make a decision back then to try to regain that share. We already had a previous history of loss of market share and it became stronger in the beginning of the year. So back then, that led to a decision that margin should be used to regain that market share, and that was made by lowering them. In June that changed, July looks a bit more like June.

So Gustavo, we also don't want to be going up and down, , like a roller coaster effect. What we'll have consistent in the limit, you could exaggerate your margin to the top, and you lose share, then you let go of your margin to recover share and then you have to do it again. So you don't generate any consistent effect in the short term and it deteriorates the business in the long run because, you generate an inconsistency in your value proposition for resellers, for consumers. And this is not what we look for and what we have proposed in our value agenda with the initiatives.

So, we don't want to come to July or August and go back to the level of January now. So, we want to do it in a more consistent way, in time, more detailed, already in compliance with the proposals we made. Of course, later we can discuss that with you in further detail of having a more centralized pricing data-driven, detailed by region with all the questions and detail we commented on during the follow-on period.

So, as to how it will look from now on. In the future, we don't want to make any major movements like that, like those that have been in the past. So when you look at the average figures for the quarter, maybe that's a better reference for you to look at, in terms of where we would like to be, In the future. We don't want to be as high as we were in the first quarter, neither as low as we were in the second quarter. So that's for the starting point. So until our initiatives jointly are bearing fruit, you should think of something closer to the average of the six-month period and not any individual quarter separately. But this again, I emphasize should not be taken as a guidance. It's more of how we see this issue.

As about as for your second question, I'd say that in terms of gains of efficiency and I'll let Rafael comment more about that later, but just linking it to the previous question from Hachem, something we worked in parallel with the follow-on was the redesigning of the procurement process of the company. Today, we engaged several services and equipments and -- from buying a pencil to buying complex engineering services, everything used to be part of that state-owned bidding process and a major win-win When of our process is -- something we made operational immediately, now we are free.

We no longer need to go through that long, lengthy and complex process of procurement. That at the end, didn't allow us to choose the providers or the suppliers or the best prices and it's not very efficient and it was a very lengthy process that ended-up resulting in longer-term contracts and agreements, that we would regularly -- because we do not want to make bidding processes every three months, so we ended up signing longer agreements that we would otherwise do.

So, as I already mentioned, we no longer rely on that state-owned bidding law, now we have defined the new tool that's being implemented and will be operating soon in a month or so. So in terms of our running rate for agreement, that's BRL1 billion per year only for activities not including freight. In that package of BRL1 billion, we understand that this new procurement process and tool, especially the new freedom to negotiate will make us more efficient, to engage higher procure those BRL1 billion, in contracts. And finally, there's this other side that Rafael mentioned, that we can do immediately to which is to renegotiate existing contracts. Today, we have a balance of BRL3 billion and some contracts, that are highly concentrated, we did a screening of them.

40 contracts that account for 70% of the value and we're now speaking to vendors and sitting down to rediscuss them looking at the exit clauses. So that we can have efficiency gain immediately with those contracts. The due date of half of it was yesterday as you said, but of course the implementation process of some of these initiatives may take some months. But we're talking about things that are immediate, as well as others that would take months, but nothing will take several years at least as we see them today. Thank you.

Q - Gustavo Allevato {BIO 18933135 <GO>}

Thank you for the answers.

Operator

The next question comes from Bruno Montanari from Morgan Stanley.

Q - Bruno Montanari {BIO 15389931 <GO>}

Good afternoon. Thank you for the question. I'd like to explore a bit more pricing versus volume. It's very clear what happened in the beginning of this year. So what we have proposed at the end of the second quarter, would have a very interesting effect on the margin in a normalized term?

My question is, with this normalization of the margin, does the company actually expect to increase its market share significantly. So if we think in the medium and long term. What do you have in mind in terms of market share gain? Or, is the company satisfied to being -- with being a bit smaller in the industry or growing less industry and prioritizing a healthier margin? So I would like to understand this balance between pricing and volume.

The second question is about capital allocation. Especially now that you are a private company. How do you see opportunities for verticalization in refining. And the third quick question is there any update?

A - Unidentified Speaker

Mr.Bruno, can you hear us? Your line is mute.

Mr.Bruno, we cannot hear you. Please make your net connection. We'll move on to the next question until you can reconnect to the call.

Operator

The next question comes from Regis Cardoso with Credit Suisse

Q - Regis Cardoso {BIO 20098524 <GO>}

Good morning, Rafael. Good morning, Marcelo. I think we have discussed in detail the topic of the change in margins in the last two quarters. I would like to address a more specific point. It seems that the dynamic of this quarter was less, related to loss of inventories, but most likely related to replacement margin, which is what you and Natal explained in one of your previous answers to questions. So I would like to understand how much of this dynamic, which in our point of view, was the reduction in the replacement margin, during April and May and a recovery in June. How much of this dynamics do you attribute to the fact of increasing prices at the refinery with a reduction in June and how much comes from a decision of the company.

And also on that topic, it seems to me that the exit rate and the less margin in June was quite above the average of the second quarter of 2019 as a whole. So if you could comment on those two points? And then the second question relates to road maps from now on. How much, do you believe will be the next items on the agenda of the special shareholders meeting, like approving the by-laws, allowing you to work more as a private company. And if there is any previous case of privatization with the electrical companies or telecommunications company, there you're using to -- as a source of inspiration.

A - Rafael Salvador Grisolia {BIO 16673583 <GO>}

Okay. This is Rafael, thank you for your question. As for pricing strategy, we are trying. Remember that I joined the company in May. In the first call we had this comment on that, there was a decision of the previous company, regarding trying to find a balance, in terms of market size. Using only pricing and selling as a tool. So without judging their decision, the fact is that we're trying to find this balance.

Of course, all fluctuations, when you buy a by-product or ethanol, there are tactics to implement the selling and based on these variations. But the decision made was regardless of the fluctuation, that we internally call replacement margin, the commercialization margin. That's the margin we work with, regardless of effect of inventory and commodities prices. So this margin,-- we tried to go to market and saying what would be the margin to regain market share? So it was a new way of doing.

So we decided to reflect and we discussed this with the Board of Directors and with our Managers, that was translated to the market in the follow-on, on that 10 initiative, so the 10 initiative together, we believe will be the key. We look at what our competitors do and try to do better to deliver those 10 initiatives and activities because if you look, they are very well connected. They are the key to distribution joined with our aspiration, to get at the end of this stream up, until the convenience stores, even out of the stream, in the means of payment and loyalty programs. So by making that reflection in June, we started working on that. So, something that you mentioned in the previous question, that's also very important.

We in this return, in this consensus that we reached that the plan that we present now to implement the 10 initiatives. We now must be very careful to avoid any stress relationship with the resellers. Because when you try to go and make adjustments to return very quickly reaching an integrated margin balance, especially when you talk on stations network, in terms of our prices and the price at the pump at the station. So this is a point of change, and the main point here is to try not to use only this tool, but to find the balance point.

And how the 10 initiatives can have an impact on the two main segments, which is the network of gas stations and B2B, as for the special shareholders meeting, this will be based on the new board members. I propose that to bring the new team, a team of Executives because the new team of executives is certainly aligned with our vision, and how we believe we can transform BR based on our value proposition.

So it's important to be aligned with the Board, and that's why we are working with investors to have a name that they agree on. So, going back to your previous question, in one or two weeks we will be able to announce the special meeting of shareholders and their names. We'll invite -- we have on the board. As for long-term compensation. This is also important to discuss with the new Board of Directors, because investors have prepared -- made some proposals during the road show. Well, we -- as for your next question, we are discussing the entire -- with the entire network.

We have some privatization in several other sectors, so they're bit older, but BR has some specificities that we mentioned at the IPO. So there is a movement, a learning movement in terms of value creation, growth all the people management we did, since the IPO to have goals, training leaders. There's an entire path that is very specific to BR, but of course, we're getting a lot of information, bringing consultants that onboard that have worked in previous privatization process. As well as in private companies, that follow the same dynamics. So it's a holistic view to capture all possible experiences, so that we can do the best possible process for BR, people and investors.

Q - Regis Cardoso {BIO 20098524 <GO>}

Okay, excellent. Thank you.

Operator

(Operator Instructions) The next question is from Bruno Montanari, from Morgan Stanley.

Q - Bruno Montanari {BIO 15389931 <GO>}

Thank you. I had a connection problem. I don't know if you got the questions or if I should repeat all of them?

A - Rafael Salvador Grisolia {BIO 16673583 <GO>}

This is Rafael, Bruno. Thank you for -- I was starting to answer. I had noted them down. Let's see if you dichotomy if this is what you asked. You made a comment about what we expect in terms of pricing and initiatives, in terms of size of market share, capital allocation and how could that reflect our plans for refinery and an update of the convenience stores.

Q - Bruno Montanari {BIO 15389931 <GO>}

Okay. That's it, perfect.

A - Rafael Salvador Grisolia {BIO 16673583 <GO>}

So Bruno, regarding your first question there's no -- or option, we want the highest profitability with the largest market share, and it's not a joke. I mean every company because this dichotomy of either/or is preverse. So we want to seek both. Of course, if you reduce price, you can get a certain volume, if you maximize prices too much, you won't get -- have any shares.

So you must find the balance for the "and" option to take place, and this is a management decision we are trying to find the best point there. But in our segment, thinking more in strategic terms, when you think about the station's network, the 10 initiative should be looked at together as a joint effort, because this value proposition of BR today, is the best possible in the market. We have a strong brand, BR Petrobras, is a very strong brand. We have all the logistic capacity to have the best sourcing in Brazil. Our import capacity, capacity to negotiate.

We have an interesting value proposition in terms of convenience stores, lubricant. So the consistency of that is important, so we want to reinforce the trust or the confidence of resellers. Ipiran with its relationship experience. So maybe, we lack this element of reliability, of confidence at the network of resellers, who have real partners there.

So that -- it will be a win-win situation for both. So, we're trying to get that back because today, we have a value proposition for an unbranded gas station, that is very interesting. So, we do believe in that value proposition and we must reinforce and strengthen our relationship, so that this value proposition can be recognized by resellers, that are, today, have their own brands or are unbranded gas stations.

So all these initiatives aim to get that. So the growth of gas stations based on attracting those who do not have our brand, is key to me. And in the B2B segment, these are segments related to the economic growth of the country. So transport industry, road transport, aviation market. Brazil is a continental country, so there is a lot of air coverage to be developed still, and we believe, it's an important recovery moment, we've been in a recession for a long now.

We know that there's a cycle, so I believe that now there's an important growth movement in our B2B business for gas stations and B2B. Our inspiration is to maximize profitability. There are two large competitors showing us that we can be more profitable and we will be, now that we are a private company, and this dynamic of growth in several segments to have gas stations with our brand.

And something for capital allocation, something that's very clear. It's very important to understand that our location of BR to be a distribution company. We don't have the aspiration or knowledge to enter the production arena such as byproducts, ethanol production or refining. This is not our expertise, we do not aspire to do that. We want to develop for example, convenience stores as a true retail business. Working on lubricants, working on means of payment which is a large ecosystem, that works in entire business.

With the networks of people and the loyalty, the 3 million people enrolled in our loyalty program. So from the gate of the refinery on, the entire business belong to us. We are a distribution company of fuel, Ethanol and byproducts. So everything that happens after the refinery, in terms of logistics, and the role of a distribution -- of fuel distribution company, is to do that, we physically bring the products from the refinery and to the gas station.

So we do inventory management, we do logistics delivery. So this is the role of the distribution company and also, we financed that market, and funding also gives -- we add the financial dynamic that this market needs. So this is our role as a distribution company, being the largest fuel distribution company in Brazil we will continue to invest in that model. Because we already have the largest logistics network ready for that, with marginal need for investment.

So we'll look at opportunities outside the refinery, after the Gate of the refinery. And we expect that new opportunities may arise because today, we are the largest customer of one refinery company. So what can we have in terms of advantage? What are opportunities we can have for future, new negotiations with new refiners maybe, so that should make it clear how we work.

As for convenience stores, we have a potential to grow in that area. We have at the model that exists and in addition, we continue to believe that we could actually develop this business in Brazil. Because it's not like you see in Canada, United States convenience as a retail business, we're looking for partnerships, we have some formal proposals, very robust, and we're working with them. And now in a private environment, we can create a method and we could accelerate that.

A - Andre Correa Natal {BIO 21073585 <GO>}

We don't know just adding to the answer. I would like to make a brief comment on capital allocation, for your second question. Everything that Rafael mentioned is important in terms of how consistent this plan is, in terms of what we can do. What is our true location and we're not proposing any geographic diversification. We don't want to become refinery or doing anything like that. We are focusing on doing well and better, what we already do, as a base business. But the opposite of that is not only to think about capital allocation, but also possibilities, we'll have a higher freedom to release capital.

The -- being a state-owned company, there are several difficulties for us to sell a subsidiary or a plot of land for today, we own hundreds of gas stations, in which we own the real estate this value could be significant and we could become more agile to structure the sale of those assets. So we're not only thinking of how to best allocate our capital focused on our base business, but also in areas in which we could release or some of this capital that are in land for example, associated to the base, a real estate of gas stations. So in terms of capital allocation, we'll try to work on those two leverages and the privatization process makes it easier to work within those two fronts.

Q - Bruno Montanari {BIO 15389931 <GO>}

Okay. Thank you for your answer. Wonderful.

Operator

The next question comes from Christian Audi from Santander.

Q - Christian Audi {BIO 1825501 <GO>}

Thank you Rafael. And Andre, congratulations on your operation. I have two questions, in the conversion of white brands or unbranded. How is that working? I mean, I understand you probably working -- thinking of a high return on capital. Would you please say what it was in the past, in terms of the level and what you expect for the future? And quantity versus quality in terms of conversion of stations.

If you have any target, one thing is having a target of a net number of conversions in the year, and also differently could be lower conversions at a higher profitability, and the next question is in the competitive dynamics. What do you see in terms of competition in the market right now? With the potential improvement in the economy, a more aggressive number of unbranded stations and/or other private companies. How could that impact your strategy? Thank you.

A - Rafael Salvador Grisolia {BIO 16673583 <GO>}

Hi Christian, this is Rafael. Thank you for your question. Our conversion plans, that we have called IPO Conversion at the IPO, I think we want to enforce to strengthen our relationship more than goals and metrics. We always work on the net conversion 200 to 300 stations per year. But you touched an important point; quality, with the average cost of each station, I also have this concern and we're working with Flavio, discussing their true strength in the relationship, because -- coming back to BR, I have said in many things, and there's something that's very interesting, because if you look at the distribution such as BR, given its solid logistics presence capacity, we have all the elements necessary to provide the best price, sourcing, logistics costs.

We have a strong brand through Petrobras BR. So there is a convenience store proposition. That's very cool, very modern. So we have all the quantitative or tangible elements. Because in anonymous and open conversation with any reseller in Brazil, I believe that we could make the -- our brand more attractive, but we must strengthen the relationship with them, giving advice, because our sales team should do more than they do today. And also giving some advice on how to deal with the sales, based on what's going on in each market, in each region.

So I believe in that very much and I believe we should follow that path and improve. And for competition, It's very important speaking now as a Brazilian, as a society, we should reflect and think that if competition follows, everyone following the same rules, everybody paying the same taxes and following complying with the law, competition is most welcome. It only makes the market better, encourages participants to be more efficient, lowering cost, having the best prices. But it's really a problem in the competition environment as a whole.

You see the agency, the oil and -- agency as to non-conventional practices and that, in general. So the distribution market reflects the behavior of society. So, I think the solution to that involves several players, that are important. Everyone must look into that when you talk about the evasion and tax of pipelines. I mean, this is a competitive environment that doesn't favor anyone, but considering a healthy competition, everyone paying taxes, new participants, newer players, that will be good for the market, we believe in that.

And also very confident in our presence, in our strength, in terms of presence or logistics presence. But we welcome the competition, and we'll had to work with that to support that. I mean, had to bear that. But any practice that we will almost bear to be a crime. And in tax evasion, for example. As a company and as Brazilians, we must be absolutely against.

Q - Christian Audi {BIO 1825501 <GO>}

It's clear. Rafael, and just one final question. As for compensation, what do you plan, structure and think about in terms of how much compensation should be linked to the share price? Or being linked to operating target by segment. What would be the optimum solution, based on your discussions with the board?

A - Rafael Salvador Grisolia {BIO 16673583 <GO>}

Well, Christian. We're discussing that with the current Board, investors and consultants. What are the best current practices? Based on the stock option plan with the traditional ones, up to new solutions, we're looking -- we're trying to find the best balance between short -term fixed compensations, in the short and medium-term or long-term. Of course, it will be linked to the share price that it won't be a stock option because, there's been a dilution and so modern practices don't lead to in that direction.

But metrics are good. And we'll -- we're discussing the design with our the stakeholders. You mean your current board, the new board, investors and we're working with that, with Petrobras as well to find the ideal package for all investors. And also, we designed not only the executive teams and the statutory directors but other players as well, such as -- for the employees that remain with us.

Q - Christian Audi {BIO 1825501 <GO>}

Thank you very much.

Operator

The next question comes from Vincent Falanga from Bradesco BBI

Q - Vincent Falanga

Good morning, Rafael and Natal. I had two questions. The first one is -- derived from Bruno's question. I understand that Brazil, potentially entering a virtual cycle from now on. And we believe that in this strategy of prioritizing margin versus a share increment, you will be able to bear -- to really have as many fruits from that. How much of that strategy is not dependent on macroeconomic conditions? If, for any reason Brazil's economy doesn't launch in 2020, will you continue with your gradual price strategy?

And my second question is regarding convenience stores. You had different profiles, based on what we saw in the media, in a more attractive, financial proposal that's important, but the know-how is also important. Having said that, is there any partner profile, that you would rather have? Maybe someone who can bring logistics assets to the partnership, or a company that knows more about retail. So you also talked about recurring margins between BRL 70 and BRL 75. I believe it's under FIRS. Thank you.

A - Rafael Salvador Grisolia {BIO 16673583 <GO>}

Thank you for your question. As for your first question. Our value agenda and everything we presented in follow-on, recognizes above all, that in the current situation, it's not only about sales and increasing prices, it's a value proposition that we're able to have a partnership and find a balance with our customers, by implementing the 10 initiative. But acknowledging that the macroeconomic environment at this moment, something good about the BR, that we recognize that. Despite being the largest distribution company in Brazil, and the highest logistics assets, we're not profitable. Some competitors, have a more -- are more profitable than us.

So B2B is very closely related to the economic activity and the stations network as well, but the value proposition for those who are not branded gas stations, we believe in it very much. But we are -- if you look at figures from 2018, it was BRL72 per cubic meter. And you see the results of net our main competitors, they're working with BRL40 per cubic meter and we should seek that we have -- with the privatization, we could accelerate our initiatives to deliver a profitability. So if the economy recovers and we have a further cost reduction, we could be stronger in that area. But our case is that we're lagging behind so much in terms of profitability. And we need a joint combination of those 10 initiatives.

Understand above pricing, the dynamics of our resellers. What it takes in terms of sharing, understanding the need of our B2B customers, but there are also smaller costs, in terms of buying products, such as Ethanol byproducts. I should be able to reduce my SG&A, have a reduced cost. All of these elements will act jointly and together. So that's why, we're so excited at this moment, because we have all the tools and we know what to do. And now we can work more freely because we were no longer a state-owned company.

The second -- the other question was also very good. It will take some more time because, it's like a start-up, because it doesn't exist as a convenience business. So, of course, there are names we're working it as candidates. That have very traditional profiles as retail companies, and also, there's combinations of fast food.

So we're trying to balance that, to find the best solution. Of course, we are limited in terms of -- we have confidentiality agreement for the proposal. But we are very anxious to make that happen and we'll work on that strongly. So that in the next one or two months, we can communicate that to the market.

Q - Vincent Falanga

Thank you Rafael. And the BRL70, BRL75 is IFRS?

A - Rafael Salvador Grisolia {BIO 16673583 <GO>}

Could you repeat that question?

Q - Vincent Falanga

The recurring margin that you mentioned, BRL70 to BRL75?

A - Rafael Salvador Grisolia {BIO 16673583 <GO>}

No, I said that based on what we said, year-to-date, it's BRL70 per cubic meter, EBITDA margin. Last year, we ended at BRL62 per cubic meter. It's a reference that as we see the company today, that our recurring is BRL75 to BRL70, from BRL65 to BRL70 per cubic meter. That will be equivalent to the year-end figure of last year, adjusted by the FRS.

Just a quick comment on your question about margin question. Something interesting that Brazil growing in the dynamics of our products. We are associated to the history of Brazil. Our products grow in line with the GDP. So it's obvious that when Brazil starts to grow again and the demand for our product grow, that will be favorable and help in terms of margins, economy of scale and we would also have the competitive dynamics.

Because the entire industry grows and competition becomes more interesting for everybody, but it's interesting to note that, even in a decreasing demand for fuel, since 2014 until today, it was possible for part of this sector to maintain a certain consistency in terms of margins. So, I would like to highlight now, that if Brazil starts to grow again, It will help us even more. But there is an endogenous component in terms of gaining efficiency, efficiency in capital allocation, reduction of costs, that could allow us to grow despite any macro-economic boost. So this is the part of the beauty of our case.

Q - Vincent Falanga

Okay. Thank you very much.

Operator

The next question comes from Thiago Duarte from BTG.

Q - Thiago Duarte {BIO 16541921 <GO>}

Hello, good afternoon. Thank you for the question. I would like to explore three points if possible. First, this was addressed in previous calls, but I would like to understand from you. How do you see the resilience of unbranded stations or the smaller brands, or white brands? Some period ago, when imports became more relevant that reduced the competitive advantage of the prices of imported goods and unbranded stations had a bit more flexibility. Then substitutes came and the truck drivers' strike, and still, this becomes -- still remains latent. This is a window in terms of a performance for the smaller brands.

The second question from the 10 actions. The first action, I would like you to help us build the rationale for that, because it's very clear. You said that the company leaves some market-- some money on the table for that. When you talk about sell-in. When we look at sellout. And the market share that was lost by the company in recent years. If we could infer intuitively that has -- that is related to price, we're under the impression that your price policy is not so good in the sell-in, but it's very good for the resellers and the sellout. Do you agree with that?

When we talk about pricing policy. We see BR reseller with the higher margin, that they might or could operate with. And my last question regarding downstream movement that Rafael mentioned. Those measures, ANP and suggested for the industry, allowing the verticalization of distribution companies, with the gas station for you to be able to operate gas station. How do you see that possibility? Thank you.

A - Unidentified Speaker

Thank you for your question. We can have another call, I'll try to be brief, because we are running out of time now. But I'll try to address the point so that. You can have an overall answer. Actually, I'll insist in the point that's very important, okay? The 10 initiatives have to happen at the same time. All of them are equally important, there is not one that's most important than in the other one because, it is this consistency of the whole package that brings the answer to your first question.

Because today, we could discuss what happened in 2016, regarding the profitability gap that was due to import, or the strategy of Petrobras at that moment and what happened later, but right now that BR was the last one to start to import. But now as we speak, your question in terms of the gas station network, this resilience, not being able to act so quickly to attract an unbranded station.

Is because in our execution, if we're not able to deliver on this execution of these 10 initiative, because if we are able to deliver a set of -- a package of offers and lower cost, higher efficiency with a nice convenience store, a modern solution for, say, means of payments. And we should communicate that. We should again regain the confidence, the trust of resellers. Although we're very close to them, but there is a partnership relationship, the advice.

As for your second question, I don't agree with the general statement people make that as resellers, we are in sell-in and efficient in sale-out. I think this is a complicated general statement. It's not exactly like that, it changes according to the region. The important pricing is the mindset, we have all these systems, these tools, lots of information. So the issue is not only the tools, but the mindset of our sales area. It's not only of having money on the table, but there are times in which our pricing strategy to work with cost, with margin, leads to situations in which the dynamic of a macro region is very competitive.

The cost-plus margins, doesn't reach the market because I thought that a cost that's not so optimized. And when you work with cost-plus margin you end up with an end price that's not competitive for that region. So this view is complex. You must work with the price that market supports, either it's down or up. So this dynamic has changed. That's what we are proposing to do. It's a dynamic as Flavio said, that was implemented many years ago, and we must have a transparent relationship with resellers, because we must understand, what is the right proportion between what stays with the distribution company and with resellers.

So relationship is important in our pricing initiative. Again, I would like to emphasize again that according to understanding of the board and the management, all those initiatives should happen at the same time. It won't work if they're not all implemented. We won't be able to provide a correct offer package. As for the possibility of verticalization in the gas station, it's okay for it to exist, but this is not the main area in which I believe will add value to BR.

Today, resellers are entrepreneurs, they know in detail that their macro region -- mixed micro region, what they add value in discussion, they bring inputs to the business. The verticalization of owning gas station, operating gas stations may be won't interest us, it maybe -- we believe that resellers are more efficient than -- for us to -- as big as we are to enter into micro management of retail selling point.

So of course large retailers, they calibrate what is franchise and their own stores. Working with an ideal store, but the efficiency of retail is not having our capital at the point of sale. That already exists. So economic decision is present, because resellers, they work as major franchisees. So therefore, I don't believe that verticalization, it may be a possibility, may be approved, but for us, it's not a window, value window that we consider so much.

Q - Thiago Duarte {BIO 16541921 <GO>}

Thank you.

Operator

Next question comes from Ricardo Schiavinato from JP Morgan.

Q - Ricardo Schiavinato

Hello Rafael. I have two quick questions. First, regarding aviation. You mentioned in the release, that volume dropped during the third -- the quarter. There's a fourth company in the market. There's a whole discussion about their capacity. How do you see the impacts on your segment? How much that could improve or not, in terms of what you have spent.

And the second question is based on what Natal talked about earlier. He talked about the non-core assets, gas stations, but now I understand that the account court ritual? How do you think about the non-core assets? Do you think something will happen in the short and medium term, or it should -- will take a bit longer?

A - Rafael Salvador Grisolia {BIO 16673583 <GO>}

Hi, Ricardo, thank you for your question. This is Rafael speaking. In terms of aviation. I'm a major fan of aviation business in general. I think that BR has been operating this market for a long time. Brazil has a very small area of coverage, given the continental side of our country. I've been in 30 years -- in this market for 30 years, 20 in distribution, we've seen so many things in aviation. But today, domestic companies, some are more sophisticated, they are very sophisticated.

They have consistent plans, one of them left the market. Which was not a happy ending for that player, but the natural vocation of BR is very large in this market. So entering generic terms, I could say that the need for coverage is very high, and I am present in 99 airports and my second competitor which is not small, he is present in half of these airports.

So we are -- have a strong vocation for this market and we will help this market as best as possible. This is how I can answer you. As for the comment of Natal, which is very right. And your question. We could only accelerate that process, because now, there is the -- because we had to follow the systems of Petrobras et cetera. That for Petrobras, negotiated assets, they have this series of formal formalities, that should be followed. But now BR has much smaller assets, but we have to follow that law. But now with this transition, we tend to act much faster than we used to.

The fact is I remember cases in the follow-on that will take us so long to sell a plot of land, that because as a state-owned company, you have to have external consultants to add value to that, and then a public bidding process, and then it has to reevaluate again, and then you end up giving up, because the cost involved is so much It's so high that sometimes it doesn't make sense to sell. As a private company, the retail price is the price that people have to pay. If you may decide not to sell, but that's the price that was presented in the bidding process. So now the dynamics is much more agile, and we expect it to improve.

Q - Ricardo Schiavinato

Okay. Thank you.

Operator

Thank you, ladies and gentlemen. We now end the Q&A session. This webcast. Now Rafael Grisolia for his final comments.

A - Rafael Salvador Grisolia {BIO 16673583 <GO>}

Thank you all. We ended up extending the length of the call. If there is any question that was not answered or someone who was not able to stay until the end, please talk to Flavio, Andre or with me. And thank you all for attending, and I reinforce that it is a fantastic moment for BR, we're very enthusiastic. It's not a hundred meters race. It's a marathon, but we'll continue with our efforts. Thank you all very much.

Operator

Thank you. Ladies and gentlemen, the audio of this conference call as well as the slide presentation will be available at the Investor's site of the company at www.brir.com.br. Thank you very much for attending. Have a good day.