

Q2 2019 Earnings Call

Company Participants

- Carlos Mauad, CEO
- Jose Roberto Meister Mussnich, Chief Executive Officer
- Noel Prioux, Grupo Carrefour Brasil CEO
- Sebastien Durchon, Chief Financial Officer

Other Participants

- Gustavo Oliveira, Analyst
- Irma Sgarz, Analyst
- Joseph Giordano, Analyst
- Richard Cathcart, Analyst
- Robert Ford, Analyst
- Thiago Macruz, Analyst
- Tobias Stingelin, Analyst

Presentation

Operator

Good day ladies and gentlemen, welcome to Grupo Carrefour Brasil's Second Quarter and First Half of 2019 Conference Call. At this time, all participants are in listen-only mode. Later will conduct a question-and-answer session when further instructions to participate will be provided. (Operator Instructions) As a reminder, this conference is being recorded and broadcast live on the investor relations website at www.grupocarrefourbrasil.com.br. A slide presentation is also available on this website. Slide selection will be controlled by you.

Before proceeding let me mention that forward looking statements are being made under the safe harbor of the securities litigation reform act of 1996. Actual performance could differ materially from that anticipated in any forward looking comments because of macro-economic conditions, market risks and other factors.

It is now my pleasure to turn the call over to Mr. Noel Prioux, Chief Executive Officer to start the conference call. Please Mr. Prioux, you may proceed.

Noel Prioux

Good morning and thank you for joining us on this call to present Grupo Carrefour Brasil's second quarter and first half 2019 results. I am joined on this call by Roberto Mussnich

CEO of Atacadao , Carlos Mauad, CEO of Banco Carrefour and Sebastien Durchon our Chief Financial Officer. Daniela Bretthauer our Head of Investor Relations is also with us.

I will start with a brief overview of the key highlights of our performance in the period. Sebastien will detail our financial performance and Roberto, Carlos and I will present the key performance highlights of our different businesses. Those who could not join us for today's call, so Sebastien will present our digital highlight. After my concluding remarks we will then open the floor to your questions. Our presentation is available for download on our investor relations website.

The first half provided a demonstration of the stress of the ecosystem theme that we introduced at our investor day back in March. Even in a challenging consumption environment, Grupo Carrefour Brasil posted double digit growth in both sales and profitability in both the second quarter and the first half of the year. Thanks to a solid execution of our strategy. I'd like to mention some of the key advances of the first half as we continued the development of our omni-channel strategy with a focus on connecting the physical world and the digital one. Click and collect is now available in all stores of which 50 operate with their own inventory with two hour pick-up.

We now have drive for online food order pick up available in 17 stores and we also have three side-stores in operation in Sao Paulo. Our marketplace continues its Rappi ramp up and we now have 2,600 sellers in 2.4 million SKUs in our platform at end of June. We introduced Carina, our artificial intelligence enabled virtual after-sales assistant which we introduced to you at our Investor Day and which I will comment on in greater detail later.

Our ecosystem concept goes hand in hand with partnerships to speed up our digital transformation and enhance our service offering and we continued to make progress in the first half. The last-mile delivery service Rappi is now available in 88 stores in 22 cities nearly twice Q1 figures. We also launched at the end of June of a pilot with Magazine Luiza for store-in-store sales as home appliances in two stores and a similar partnership with Swift for meat sales in 12 stores. The goal of the ecosystem is to multiply touch-points with customers and to offer them increasingly personalized offers. We now have 15 million registered users whose data we can leverage and we also increased connections through new stores.

In the first half of the year, we opened nine new Atacadao stores in line with our target to open 20 this year. And we continue to develop the proximity segment with two new Market stores and one new Express store, bringing our proximity network to more than 130 at end of June. Speaking of innovation, Banco Carrefour will launch and ensure tack in insurance marketplace which Mauad will comment on.

Finally, we are advancing in the digital payments area where Scan&Go now available in 15 Express stores, payment via QR code through the app, and the soft launch of an NFC Digital Wallet. As you know the Carrefour Group has set itself the global ambition of being the leader in food transition for all, bringing healthy food to consumers at affordable prices.

And on Slide 4, you see that we took new steps towards that goal in the first half of the year. Healthy food aisles are now rolled out in 59 hypermarkets at the end of June, and the target is to complete the roll out by the year -- by the end of the year. In the first half, we increased a healthy product assortment by 32% with 500 new SKUs. The organic food segment is increasing even faster with sales increasing 82% on the back of a 34% increase in assortment with another 300 SKUs added. We are working closely with suppliers to increase our offer even further.

We are also advancing in our aim of increasing the share of private label products in our food offer. They now represent 13% of total food sales, a two percentage point gain over Q1, and we target 20% penetration by 2022. With 516 new products launched in the first half, our private label sales have increased 33% in the period. And we have added new features to CyberCook, the Foodtech we acquired at the end of last year, including nutritional and price, data and functionalities to search for recipes based on food restrictions or using leftover ingredients from previous recipes thus contributing to avoiding food waste. We recently hosted an Act For Food event in Sao Paulo and launched our new media campaign, which I hope you have all seen on TV or web to reinforce Carrefour's public commitment to healthy eating.

I will now hand over to Sebastien to comment on our numbers in greater detail.

Sebastien Durchon {BIO 20242758 <GO>}

Thank you, Noel. And good morning everyone. On Slide 6, you see how this strategy translates into our numbers, both in the quarter and the half year. I will present to you the key numbers for the quarter and the half year. My comments are on numbers prior to the implementation of IFRS 16 for the sake of comparability.

Let's start with our Q2 performance, our gross sales rose 12.9% to BRL15.3 billion. Adjusted EBITDA grew in line with sales to nearly BRL1.1 billion for a margin of 7.6%. Adjusted net income, Group share rose 11% to BRL419 million equivalent to a 3% margin, broadly stable year-on-year.

If we look at the half year performance, the pattern is very similar. Gross sales were up 10.9% to BRL29.4 billion. Adjusted EBITDA was up 14.5% to BRL2 billion with margin of 26 basis points to 7.6%. Adjusted net income, Group share at BRL832 million was up 19%. Our net debt was BRL1.1 billion excluding discounted receivables, a leverage of 0.3 time.

Let me now focus on the context in which these results were achieved. Slide 7 provides a backdrop to this performance, indeed, the headline numbers that I just presented are all the more remarkable as they were achieved in a challenging consumption and macroeconomic environment. As you know, the Brazilian economy has underperformed expectations due to delays in implementing key reforms despite some advances recently. This has led economists and the government to lower their growth projections for the Brazilian economy for the year and unemployment remains persistently high.

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At the same time, we have operated in a somewhat volatile inflation environment with food inflation rising in Q1 and Q2 as shown on the first graph on the slide, and then gradually easing most notably in June suggesting more moderate inflation for the rest of the year. This combination of a weak economy and high food inflation has impacted retail sales.

As you see on the graph on the right of the slide, as per Cielo's broad retail index, the ICVA, it shows a decrease in consumption that began at the end of the first quarter and continued in the second quarter, but with a gradual pickup again towards June as inflation eased. I wanted to highlight this as something important to have in mind as we comment on our performance in the period.

On the graphs on Slide 8, you can see consistent year-on-year growth in sales both in Q2 and the first half. Our total gross sales in Q2 of BRL15.3 billion were up 13.5%, which marks an acceleration over the 9.9% growth recorded in Q1. Beyond our solid performance, Q2 was also boosted by a positive calendar effect of 0.8% as Easter was in Q2 this year.

The graph on the left hand side shows that we have added BRL1.7 billion in gross sales in Q2 '19 versus Q1. Atacadao's contribution to our gross sales has grown in the period, reflecting its steady pace of expansion. Similarly in the first half actually, our gross sales reached BRL29.4 billion, a growth of almost 11% or BRL2.9 billion year-on-year.

On the right hand side, we'll look at the breakdown of sales. You see that quarter after quarter, the pace of like-for-like growth has increased and reached 7.7% in Q2, the best performance in the past three years. This was driven both by Carrefour Retail, whose like-for-like growth of 8% in the period constitutes its best quarterly performance in the last five years, and by Atacadao, whose is like-for-like growth in Q2 accelerated over Q1 to 7.6%. The contribution of expansion has also risen quarter after quarter, largely thanks to Atacadao's sustained pace of store openings with a Q2 contribution of 5%. This growth in the context I described earlier is clear evidence that our strategic choices are paying off and are producing sustainable results.

Let's now turn to look at our simplified P&L on Slide 9. Our net sales in Q2 posted a strong quarterly performance up by 12.6% and by 10.6% in the first half. Gross profit was up in double-digits, both in Q2 and first half, increasing by 12.4% and 12.5% respectively, driven by growth in all of our business units. Gross margin was up by 36 basis points in the first half and was broadly flat in Q2 at 21.7%. Margin improved at Carrefour Retail by a strong 31 basis points in Q2, but was down 24 basis points at Atacadao. Roberto and Noel will discuss this in greater detail shortly.

Selling, general and administrative expenses were up in Q2 in line with sales growth. However, as a percentage of sales, they were stable, reflecting productivity, gains and our continued financial discipline. Our EBITDA increased 12.7% in Q2 '19 to BRL1.1 billion and 14.5% in the first half to BRL2 billion. Pursuant to the material factor disclosed on May 12, we recorded in this quarter and ICMS provision for staple basket items posted under other operating income and expenses. This extraordinary provision does not impact the calculation of adjusted net income or dividends. Excluding a one-off foreign exchange gain

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of BRL45 million in Q2 financial result remains basically stable. Our adjusted net income group share was up in double digits, both in Q2 and the first half of the year, up by 11% and 19% respectively, which constitutes a very solid performance.

On Slide 10, I will conclude this quick financial overview with some information on the 2019 interest on equity payment scheduled. This was approved yesterday by our Board, we remind you that our dividend payout policy is to pay 25% of adjusted net income. In 2018, we made a total payment of BRL470 million with an advance payment in December 18 of BRL380 million and a complement of this payment in June 19 of BRL90 million.

Similarly, we have decided this year to anticipate the total amount of BRL470 million in dividends in the form of interest on equity, the payment will be in two equal instalments of BRL235 million. The first in September, the second in November, a special complement may be paid out in 2020 depending on the final net income of 20 -- final net income for 2019. Let's now look at our performance by business unit, and for that, I hand over to Roberto to speak about the Atacadao's performance.

Jose Roberto Meister Mussnich {BIO 18298845 <GO>}

Thank you, Sebastian, and good morning to all for the fourth consecutive quarter. Atacadao recorded double-digit growth in its total sales. Demonstrating the strength of its low price every day image and of its commercial strategy. This growth also reflects our decision to significantly accelerate our expansion with 12 new stores year-to-date, including now the first half of the year. Atacadao gross sales grew 14.8% in Q2 to BRL10.3 billion. Like-for-like sales accelerated over the previous quarters already strong growth, rising by 7.6% in Q2 after a 6.8% increase in Q1.

We saw growth both in the number of tickets and average ticket in the second quarter. In a challenging consumption environment as Sebastian mentioned, our gross margin was 15.2% as a result of our strategy to maintain the concept of the cash and carry model. So let's comment on what happened in the second quarter, a tough comparable base Q2 '18 gross margin benefited from a positive exceptional impact during the May truckers' strike. This is a nonrecurring event, greater focus on the merchant, B2B customers with a extremely positive impact on sales of famous day in April and the ramp-up effect of new stores.

Our park [ph] of new stores reflects 15% of the total park of stores, excluding expenses related to the expansion of the last two years, distribution costs as a percentage of sales would be 7.9%, 40 basis points lower year-on-year in Q2 reflecting our strong productivity gains and the strength of our model in a more mature stores. Despite all of that, our EBITDA grew in double digits, both in Q2 and in the first half of the year. On Slide 13 now please. We'll take a more detailed look at our expansion strategy with nine openings in the first half and another three in July. This brings our total openings year-to-date to 12 new stores in line with our goal of 20 new stores this year.

We surpassed 200 locations throughout Brazil. As you know, and as we always address, Atacadao is a wholesaler with a truly nationwide presence in Brazil and our openings were

well distributed in eight different states in the first six months of the year as you can see on the map on the left. Our model has proven once again to be resistant and resilient to market dynamics, we managed to maintain our value proposition and low price image, while delivering higher and sustainable results in absolute terms.

With that let me hand over to the Noel to comment on Carrefour Retail, I'll remain available for questions later.

Noel Prioux

Thank you, Roberto. On Slide 14, you see the main performance indicators for Carrefour Retail. The strategy we have been executing over the past couple of months is clearly showing up in our results. Carrefour Retail turning in its best quarterly like-for-like sales performance in five years posting an 8% growth in the second quarter, accelerating over 6.1% in the first quarter and marking a very sharp increase versus 3.8% like-for-like growth recorded in the second quarter of 2018. Gross sales in Q2 were up by 9%. The strong sales growth validates the strategic decisions we have taken over the past year, including the decision to re-position hypermarket prices to improve their competitiveness on going food transition initiatives and enhance the value proposition in our steady ramp up in e-commerce sales.

Gross profit rose in both Q2 and first half of the year and then accelerated in Q2. Gross margin was also higher. This improvement reflects a better margin at Carrefour as a result of commercial initiatives as well as better gross margin in our e-commerce. In the first half of the year, gross margin grew both in Carrefour Retail and e-commerce. Our distribution costs at 20.5% of net sales were broadly stable year-on-year, reflecting our continuing efforts to maintain financial discipline to fund investments linked to the roll-out of Carrefour Retail omni-channel strategy.

In Q2 adjusted EBITDA pre-IFRS 16 was up 14% to BRL183 million, a sharp improvement over Q1. Let me now hand back to Sebastian who will present our e-commerce advances and then Carlos Mauad will comment on the bank's performance.

Sebastien Durchon {BIO 20242758 <GO>}

As Noel mentioned at the start (inaudible) today will comment on our digital initiatives. I will do my best to speak with the same passion and energy as she always does, so that she won't be mad at me when she returns. Reflecting our growing emphasis on building an omni-channel ecosystem, e-commerce was once again the fastest growing segment within Carrefour Retail and GMV share of total Carrefour Retail sales in the first half reached 11% versus 7% in the year ago period. The percentage is even stronger in non-food, which represents 32% of Carrefour's total sales. Due to another strong performance with GMV rising by 59% more than five times the markets growth rate of 11% according to EBIT.

Orders were up 56% and visits increased by 89%. Our average ticket rose 6%, which is a very strong performance considering that the market average ticket was down 13%. A key

part of our e-commerce growth is the development of our marketplace, which continues to expand rapidly. We added another 400,000 SKUs in Q2, bringing the total to BRL2.4 million, nearly three times more than one year ago. And the number of sellers also grew to 2,600 from 2,000 in the previous quarter and 374 that we had in the second quarter of '18, a seven-fold increase in one year. As a result, the marketplace now represents about 17% of our e-commerce GMV.

On the following slide, I'd like to highlight two of our many recent omni-channel initiatives. So first is our virtual after-sales services assistant Carina, which we launched in April enabled by AI Carina gifts car for one of the most advanced after-sales services in Brazil retail through WhatsApp messages, Carina can answer customer questions on a broad variety of topics, such as store locations and promotions. She can also track e-commerce orders, provide invoices for Carrefour and Atacadao cards and a host of other services. By the end of June, we had approximately 300,000 interactions with Carina and July is not ended yet, but we believe we will have the same amount of interactions in July, we are working on upgrading Carina further, so she can do the Q&A session in the next earnings call.

The second focus is on the development of food e-commerce. As you know, we have set ourselves the ambition to be the leader in food e-commerce in Brazil and we have a very focused strategy that relies on developing the service infrastructure. The Carrefour app already accounts for one-third of our online food orders and we are quickly rolling out services to make delivery and pickup fast and simple. The Rappi delivery service is growing rapidly with a presence now in 22 cities and in 88 stores. Drive is available in 17 stores and it has a net promoter score above 75%.

In addition, with three side-store. We are growing our capacity to make orders available in the short time frame, which is key in online groceries. These are just two quick examples of the strategy that is clearly gaining momentum. Let me now hand over to Mauad to talk about Banco Carrefour.

Carlos Mauad

Thank you, Sebastian. Once again, Banco Carrefour stands out with strong growth in its results, Carrefour card total billings or the Atacadao card total billings still an expansion rose by 54.4% on a year-on-year basis. The Carrefour card despite being a much more mature operation also grew by 20.8% as a result of investments we have made together with Carrefour and Atacadao since January. Banco Carrefour total billings reached BRL7.8 billion. In the growing trend, the loan portfolio grew 36% of total BRL9.5 billion in the period, despite a robust growth of the loan portfolio credit indicators continue to improve on a comparable basis under the Central Bank methodology credit provision totaled BRL946 million with a coverage ratio of 11.2%, such performance stems from a credit management dynamics, which includes Carrefour acquisition of new customers database allocation and review of credit limits and an increasingly efficient digital collection and invoicing system that keeps cost under control. Growth of adjusted EBITDA accelerated reaching BRL252 billion in Q2, up 19.4% in relation to the same period of the previous year, driven by growth in net interest margin and diligent cost management.

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On the next slide, I would like to share with you our cultural transformation and work dynamic taking the customer through the heart of the bank's business decisions. All projects are closely linked to each phase of our customers' journey ensuring an increasingly solid experience by strengthening the customers or the customers relationship with our ecosystem investments in our promotional platform, start communication in the (inaudible) initiatives have proven to be powerful tools for customer engagement with store in credit cards. Another important initiative is the decision to accept the Carrefour card in the Atacadao store network, which should bring additional revenue in 2019 of almost BRL300 million.

Banco Carrefour establishing a marketplace for the sale of insurance, the main insurers in the Brazilian market are integrated on this platform and deposition process is totally digital with full customer empowerment, we will have products completely customized for our customers. We started selling through our own employees and after this soft launch, we will open the platform for all our ecosystem customers with special conditions for Banco Carrefour cardholders. I can assure you that the bank is now experiencing a true revolution, all areas are proud of the journey and are responsible for our customers. We transform the structures, previously working in silos to self organized and multi-disciplinary teams responsible for improving our customer experience throughout their cycle. Currently, 62% of the structure of the bank are in the agile model and we want to reach 100% by December '19. Given this new reality, all our products are connected to the experience that will be provided to our consumers, strengthening the culture of test and learn. Coupled with the transformation of work dynamics, Banco Carrefour has been building a strong pillar linked to data, data capture, architecture and application for meeting higher customer journey by constantly improving communication channels and content as well as improving the operations credit risk management.

Finally, at the end of the second quarter, we developed the technology chassis that will transform all of our channels, PWA, progressive web applications. The experience our customers will have in our app and self services stores on web platforms both mobile and traditional will be unique, we will have more flexibility development cost efficiency and more performance. This new platform will enable Banco Carrefour to optimize both customer service and cross-sell products for its customers. So there is a lot more coming in the next month, the Banco agenda full of new initiatives and we will surely have a lot more news by the end of the year.

Let me now hand back to Noel for his closing remarks.

Noel Prioux

Thank you, Mauad. To conclude, I think you could see through today's presentation that the Carrefour Brazil ecosystem is at work and advancing. Our growth even in a challenging consumption environment is the consequence of well thought out and well executed strategy. The multiplication of touch points is clear with over 500,000 new Atacadao cards and 480,000 Carrefour cards issued in the last six months, more than 90 million visitors in our e-commerce, more healthy SKUs, more transactions and an increasingly omni-channel approach. All these are elements of the interconnected at the system that we are building to drive more sales and more profitability.

With that, I conclude today's presentation. Thank you very much for your attention and we can now move on to the question-and-answer session.

Questions And Answers

Operator

(Operator Instructions). Our first question comes from Joseph Giordano with JPMorgan.

A - Carlos Mauad

Mr. Giordano, good morning.

Q - Joseph Giordano {BIO 17751061 <GO>}

Hello. Good morning. I have three questions, the first goes to Roberto. I would like to understand the very positive dynamic that we've seen at Atacadao. I would like to understand what you're thinking Roberto in terms of how do you see the competitive landscape, competition is illustrative. I want to try to understand whether the model be more mature in more regions of Brazil. If you're seeing a change in the maturation curve of the stores? So they're reaching maturity earlier and finally applied to understand what you have in terms of contracted pipeline for the rest of the year? And for next year. Have a guidance of 20 stores, I would like to know what you have done so far. And how do you see the food inflation?

Now to Noel. Talking about retail, I would like to understand more Rappi, and if this does bring to Carrefour customers who were not the traditional ones. How is this evolving over time? And regarding CRM and what Mauad mentioned about big data. How are you capturing card data and collecting data on retail checkout to improve in-store execution and value proposition? Thank you.

A - Noel Prioux

Hello, Joseph. I'm fighting not to have my head in the market, but what we see in the market is a growing competitive environment. This is normal. Although some of our competitors do not have the sustainable competitive advantages that Atacadao has. We saw inflation a little higher in some months of the first quarter and that caused a somewhat higher internal food inflation at Atacadao, but that has eased in June. And in July, inflation has shown to be relatively well, which leads us to think that we are going to have inflation at around 3.5% to 4% until the end of the year. In terms of expansion, well innovative market is ready to receive our model, the Atacadao brand is extremely strong where we are going.

We have a map of these eight stores opened in the second quarter and they were very assertive. Our pipeline expansion is extremely strong. We have started to build 10 stores to open next year, this normally happens until the month of June, August, but this year, we started working on 10. So that we're going to have a balanced set of openings. In terms of the projects for next year, these remain as strong as and the strategy remains the same. In other words, getting into markets that are ready.

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For our distribution, we want to work with merchants B2B customers as strongly as working with end consumers. So we want to have a wide array of services in the cities where we operate. So we continue with the same strategy, we are getting into new markets, we are tapping into new markets. We are strengthening our position in markets where we've been for a while with extremely strong stores that are quickly maturing and the result is shown in extremely consistent like-for-like sales, in line with our strategy.

Although, if you look at the mature park of stores, we only have 15% of this park with less than three years of existence. This means that 15% of the park is presenting a more positive ramp up within the rest. But 60% of our store park is mature and 60% of our park has been attacked constantly and even being attacked consistently, the model remains very, very strong, and this is very good because it shows that we have to be better, day after day and we change our tactics in our technical plan day after day, so that we can execute on our macro strategy. We remain alive, my head is not on the line. My head is still linked to my body, and it continues to think very, very well.

Regarding the Rappi strategy we have, Rappi, we also have click and collect, drive and many other possibilities that we offer to the client. But to answer by about Rappi, we do have an impressive conversion we have an organization that is dedicated that allows us to offer a spectacular level of service. I believe the best in Brazil. And with that we can offer a good service and we have an important base of new customers, new to Carrefour because if you offer a service with a good quality we end up attracting new customers and this is the case of Carrefour. So we are doing well and we are going to accelerate.

Q - Joseph Giordano {BIO 17751061 <GO>}

Regarding CRM and the evolution of clients?

A - Carlos Mauad

Thank you for the question. What we have two converging agendas in our group regarding data. Of course, the bank environment is used in terms of data capturing architecture and modeling applied to loans because this is part of the core business of a bank activity and this is a business that is very well developed, gaining more and more quality given the information that we capture from our own ecosystem.

So today the bank has 100% of the data of what we call in-house buffer ticket, which is nothing but the shopping cart of the client whether they're identified or not. In many cities, we identify them by tax payer number in check out. This is a law in some cities, in other cities there are customer incentives for customers to provide their tax payer number. We just want to identify customers, when they check out and this applies to Carrefour and Atacadao. So regardless of consumer and customers having the card, this information is captured when they check out in our stores, and this information is used to improve our credit modeling activity, so that we can have approval indices, which are more and more competitive at the point of sale.

Considering Carrefour structures, we have a data initiative, which is picking up very fast and very much linked to consumption. How can we build an engine of recommendations

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particularly considering food e-commerce linked to the app? When you have very little space for offerings. So we have to have a recommendations engine for our customers so that the experience will be always fluid and so that you can have a high conversion level in your funnel, given the power that the data give you. So when you look at the group from this structural standpoint in whatever is related to data, we are very advanced in terms of data capture, all of the information in our ecosystem is being adequately captured.

We have been working strongly from the standpoint of modeling, so that we can turn data into customer engagement and turn data into communication with a high level of return in terms of content. And so as to make this a big asset in our ecosystem. So you see these are two converging initiatives, i.e, how we can bring more and more customers to us and how we can improve the assortment of product for customers that are in our ecosystem.

Q - Joseph Giordano {BIO 17751061 <GO>}

Perfect, thank you very much.

Operator

Next question from Robert Ford with Bank of America. Mr. Ford, go ahead.

Q - Robert Ford {BIO 1499021 <GO>}

Good morning, everyone. Congratulations on the results and thank you for allowing me to ask a question. There seems to be a lot happening in Carrefour Retail. It's not just the ester effect, so could you speak about what drives the improvement in Carrefour Retail perhaps a streamlined cost structure and how sustainable do you think this improvement is?

A - Carlos Mauad

Regarding retail, I think it's easy to understand. Firstly, we are obsessed about sales. For the last two years we wake up every day thinking about our stores to break away from traditions. We want to change the store, the categories, the project, and this path is already bringing impressive results. And again, we have other initiatives that bring this spectacular growth. Again, is this new dynamic that we started two years ago -- about two years ago and that is now giving results and we have e-commerce which is the door to new customers, particularly click and collect the customers, they prefer to pick up their products at the stores and this gives us an opportunity to show them a store that is totally changed considering the last two years and also the quality of products.

We have a good image in terms of quality of fresh projects. The prices were lowered and we lowered the prices again in the end of May beginning and June, because we want to offer our customers a spectacular level of quality with affordable , so we think about that every single day. In addition, there are other things, our private label products, we had two percentage points of growth in one quarter, I mean this is spectacular. And this shows us that number one, our products are good at affordable prices and the clients or customers who like this private label products. And the same for fast-moving consumer goods and perishable. So all of these are trends. But we want to be leaders in for

transition. We are not going to stop every month we have new initiative and it's difficult to the competitors to keep up with us. This is what is interesting, every week I go to the stores every single week and I speak with our customers and every week we take our new initiative. This is what is giving us this accelerated rate of improvement and we believe we will sustain this. This is indeed going to be a model to show that hypermarkets have a great potential of particularly in Brazil.

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Q - Robert Ford {BIO 1499021 <GO>}

Understood Noel, thank you. Are you now making money with your proximity model, is there a material acceleration in this model?

A - Noel Prioux

Yes, last time we spoke about this. Until the year ago, I wasn't convinced about this model. But now I'm totally convinced after one year we have a strong growth of more than 20% happening every month, we maintain the pace. So I don't think that it's a sufficient, we are already working on a version, which would be say a little more aggressive. We have some ideas that will allow us to provide strong growth for next year as well. Based on this, I am convinced that we have a winning model and that we can do more now.

Q - Robert Ford {BIO 1499021 <GO>}

Thank you, Noel and congratulations again on the good results.

A - Noel Prioux

Thank you.

Operator

Next question from Thiago Macruz with Itau.

Q - Thiago Macruz {BIO 16404924 <GO>}

Good morning. My first question goes to Roberto. In the end of last year you had a favorable decision based on the ICMS resolution in states other than Sao Paulo. We had an expectation that this could flow through Atacadao results in 2019 and it seems that this did not happen in the second quarter, is it reasonable to suppose that you had to invest part of this benefit in prices, given the competitive landscape that you mentioned and Joseph question -- this is my first question. The second question to Sebastian. Could you give us an update of your strategy, in-house strategy to make these ICMS-ST benefits or cash benefit and not accounting benefits any progress in that direction? And my final question, you said that you're gaining more on the lines. I'd like to understand, when you say this, do you include users that buy from Carrefour through Rappi and if there is a migration from Rappi customers to the Carrefour cap that you mentioned? These are my three questions and thank you very much.

A - Jose Roberto Meister Mussnich {BIO 18298845 <GO>}

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Great Thiago, it's always a pleasure to have you on board. Let's speak about investing in price. It's funny when you speak about advantages based on ICMS-ST as if we have this kind of visibility on our data today, but we don't -- but this is main. It means that the market is alive. The market changes every day and we have to adapt to these market realities, as we always insist. Atacadao is top line. We always work to perform in the same way and we want to have a steady performance, our track record actually shows a steady performance, obviously, we have to use all of the possibilities we have at hand to gain more, but still a price investment is a day to day decision.

According to market into the conditions for our procurement and according to what the market requires, so that we can have the same model everyday low price. Once we have the price store and once we have the cost control discipline that we work strongly in-house on to maintain low cost every day, simple and with a very lean model. Once we control those variables, we work day-to-day to maintain the flame alive and we've been able to play this game well, but price investment is not something that we do in the way they overlaps lower prices to do this or that, no.

We work according to market -- to the market requirements. And this has been very efficient for our model. I hope I have answered your question.

Q - Thiago Macruz {BIO 16404924 <GO>}

You have indeed. Thank you.

A - Sebastien Durchon {BIO 20242758 <GO>}

Regarding your second question about ICMS-ST and how to monetize these credits? There is a very strong point here, ICMS before the favorable decision we had from the Supreme Court. We already had ICMS credits and ICMS-ST credits and there is no consumption issues here, we can consume every year. These credits with a value of credits generated while created a different decision -- a different situation was the Supreme Court decision regarding ICMS-ST credit based on presumed margin and the credit that all companies had when they regularized presumed margin from real margin, with that we had access to more credits.

And we waited this year to take the initiative and consume the credits, I cannot give you a lot of details, because this is very technical, but we have made changes in our logistics routes to avoid generating more credits. Because there are changes from one state to the next. We have initiatives to sell part of these credits and there are some changes in the legislation. Here in Sao Paulo, the technical rule Atacadao 17 is changing to another to 42. And with this new norm, it will be a lot easier to use credits for direct offset of sale -- of purchase, actually.

But everything is unfolding well. And another topic in our radar will be the tax reform. We have heard a lot of positive things about a possible upcoming tax reform and this will bring changes. We look at this with very good eyes very positively. We believe that it will even end this kind of system, we will have to pay a tax initially, we won't have to pay a tax and have a refund in the form of credits, this will be avoided. You also asked about the

customers, where we gain with Rappi in migration -- the possible migration to the Carrefour app.

As Noel mentioned with Rappi. I have a lot of new clients and a lot of new customers that we can identify with our CRM, these were customers that didn't used to buy from Carrefour and they are now buying. So we are gaining a very relevant number of new customers. Migration to the Carrefour App, this is only getting strike, it's a very few, but both are growing. We have a new customers being faster through Rappi and we have a growing number of customers using the Carrefour app. I don't know whether the game will play out exactly in this way. Customers use Rappi and then use Carrefour app, of course, we have initiatives to encourage that. But still we have growth regardless of Rappi, our e-commerce, our app and our website are posting relevant growth.

Q - Thiago Macruz {BIO 16404924 <GO>}

Perfect Durchon. Thank you very much.

Operator

Very well. Next question from Richard Cathcart with Bradesco. Mr. Cathcart, go ahead.

Q - Richard Cathcart {BIO 16457807 <GO>}

I have two questions here, one about e-commerce. You mentioned in the release that you launched three set stores in this quarter. Could you tell us more about the experience, you had? I know it's very little time, but it would be interesting to understand whether you can improve the efficiency of Rappi in your own delivery system and what is the impact on hypermarket sales. And the second question to Roberto, you also mentioned in the release about your focus on merchants. I just want to understand if you see any economic recovery in the clients, I'm thinking about food service clients?

A - Sebastien Durchon {BIO 20242758 <GO>}

About the side-stores, we have three, the goal is to have a spectacular level of service. The most important thing is when a customer asks for 10 products, they need to get 10 products. We have a level of service of 96% considering the world market. This is one of the highest. In terms of level of service considering Carrefour and some of the competitors. So this is due to the sites that are offering good level of service with dedicated inventory and with people dedicated to that. The first ones have been operating for a couple of months only, it's very little, but they're already giving us an outlook for the future. By the end of the year, we want to have 15 and we are working to see when we can get to a 100% capacity of the side-store so that we can open new ones.

We already have connection with all of the players, Carrefour, Rappi, the side-store and the dark store that we also use for Rappi. So it's a dedicated organization that allows us to offer a good level of service naturally if we want to open these in other cities. Well, that's why we have the ambition to be leaders in food e-commerce in Brazil and I think that we are on the right track.

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A - Jose Roberto Meister Mussnich {BIO 18298845 <GO>}

Regarding your question Richard about focus on consumers indeed in our focus on B2B and merchants is a focus to serve B2B clients, not only B2B clients but the industry, they are our partner and where we have a great capillarity throughout in Brazil, we can get to every single corner of Brazil in the north and in the south and that makes the industry -- give us the chance to work to improve the efficiency of the model. In food service in general, what we see in food service is a certain stability. I don't envision a great expectation of growth in this sector in particular. And what we hear from B2B clients and the industry is that they're waiting for the mood to change a little, because we are all waiting for key political decisions that will bring more money to the market.

Yesterday, we heard that we're just compensation fund, a part of it can be released for workers and this could drive consumption. So our expectation is that this will change from stability to optimism. This is how we see this matter. I hope I have answered your question.

Q - Richard Cathcart {BIO 16457807 <GO>}

You did. Thank you.

Operator

Next question from Tobias Stingelin with Citibank. Mr. Stingelin, go ahead.

Q - Tobias Stingelin {BIO 18290133 <GO>}

Thank you. I would like to know, perhaps you could give us some color on how the e-commerce margin evolved, perhaps comparing gross margin of e-commerce with second quarter of last year and the second quarter of this year, just so we can have an idea of how this is evolving? And do you still have a lot of SG&A expenses envisioned for this project? Because I don't know if you still have a lot of investments that you're expecting to make in the segment. And my last question regarding the like-for-like sales growth in Carrefour Retail, of what you reported removing e-commerce this should be close to 5% of same-stores is a like-for-like sales. Could you break down, how the segment really grew?

A - Carlos Mauad

Thank you. I'll start with second question. Yeah, yeah, your calculation was perfect. Like-for-like sales of 8%, excluding the contribution of e-commerce, you would get to 5% in our brick and mortar stores. We don't break down this information in terms of food and non-food. We don't do this here, we don't do this in the group in France. What I can tell you is that we have a very positive trend in non-food. The trend is also good in the food segment, but it is even greater in non-food with all of the changes we implemented in the end of last year and beginning of 2019. We had two double-digit growth in non-food. And the other part of your question was about e-commerce merchant, it is the same trend that we had before that we mentioned in the prior quarters.

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We started our e-commerce operation three years ago with a gross margin that was so low with very attractive prices. Over time, the margin is gradually improving. There is not a significant change, but it is improving gradually for two reasons. One, we already have a relevant operation how our e-commerce has sold BRL1.5 billion last year and will be a lot more this year. With that we don't need to be as aggressive in terms of price and that's the first reason. The second reason, the growth of our marketplace. That's why we say that for us it is very important to have a faster growing marketplace, because the cost structure and the revenue structure totally different. And this helps the e-commerce operation.

So the margin is improving gradually with e-commerce and you probably noticed that in this -- in this quarter. Looking at e-commerce and the brick and mortar stores. Our gross margin increased 0.30 bps. And this is also driven by e-commerce. So the margin at the stores increased more than 0.30 percentage point. So it came to a point and I think that we mentioned this in the past, it came to a point where we can perfectly pay for the investment that we made any comments. Without having such a strong pressure on the gross margin of the whole operation.

So looking ahead, there are more investments in e-commerce. The non-food part is done. So now the name of the game is to grow to break-even and to be profitable. For food, we have just started. So you will entail some more investment. The second quarter in terms of investments, it was not that different than the first quarter. So the whole margin increased, so we can develop food, e-commerce, even having in the short term, some investments to gain it. We understand that it is necessary to do this now, so that we can have sustainable growth of our results. This is what we aim to have and this is what we've been delivering so far.

Q - Tobias Stingelin {BIO 18290133 <GO>}

Okay. Excellent. Thank you very much.

Operator

Next question from Gustavo Oliveira with UBS.

Q - Gustavo Oliveira {BIO 15129435 <GO>}

Thank you, Sebastian. My question also has to do with retail. To continue what you were saying the growth of food or e-commerce, what kind of mix that you have in terms of channel because if you use Rappi accounted for 45% of your sales perhaps your margin will be a little higher. But from what I understood in prior answers, there's a certain strategy to migrate to other delivery forms to home and click and collect, please correct me if I'm wrong, but I think that they have a somewhat lower margin than what you would have with Rappi?

A - Sebastien Durchon {BIO 20242758 <GO>}

It's actually the other way round. It's the other way round because Rappi for us is very interesting, it's a good way to attract new consumers. But to us it's an additional result

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because there's practically no cannibalization, these are additional customers. And we have to pay them a take rate with our app. We have our own logistic costs, but our gross margin is a lot better. So Rappi is not necessarily the most profitable method for us, it helps us develop to food e-commerce operation. And it is exactly because of that we want to develop all delivery channels at a time. The side-store, we are going to start using it with the Rappi to facilitate our operation, but we are going to use the side-stores for our own delivery system as well.

Our strategy is to open the food e-commerce market, we have to convince customers about the quality of service and to that -- to do that we have Rappi. We have our delivery to home service and our drive and we intend to develop everything at the same time, and the customer, it's up to the customer to choose.

Q - Gustavo Oliveira {BIO 15129435 <GO>}

Thank you for the clarification, it's very clear. But if we think that you could have more similar to what we saw in non-food retail where your margins evolved, your gross margin is evolving in the retail operation. Can we even imagine that this level of margin that we currently have would be a lower level of margin and that the margin looking forward should be growing, if this what you're thinking in your business model?

A - Sebastien Durchon {BIO 20242758 <GO>}

It's what we've been saying over and over. Last year when the gross margin of Carrefour declined, a lot of people complained and we already told you at the time. These are short-term investments merged with all of the initiatives we can improve the gross margin at the stores and online, e-commerce, and this is exactly what's happening now.

Q - Gustavo Oliveira {BIO 15129435 <GO>}

Is there more room for the gross margin to grow?

A - Sebastien Durchon {BIO 20242758 <GO>}

Yes, there's a little more room. Yes.

Q - Gustavo Oliveira {BIO 15129435 <GO>}

And I have one final question, to Mauad. In the press release you say that there is an increase to frequency of Atacadao card and it is an increased consumption out of the stores, of course, in this quarter, you had I believe you had increased sales given the campaigns that you had. The campaign Usou zerou. So how are you thinking an opportunity of -- an opportunity out of your stores network because you're going to see an increase of sales out of the Atacadao network and that decision of accepting Carrefour cards had an impact. I want to know how this is influencing the frequency of card use?

A - Carlos Mauad

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Thank you for the question. But let me make a quick correction, Usou zerou is an exclusive dynamic for Carrefour card, the Atacadao card still the charges an annual fee as the card was conceived in 2016 and implemented in 2017. But let's speak about frequency. So what's happening specifically with the Atacadao portfolio. It is a portfolio to say -- to say product. Well, customers are standing to understand the product more in depth as the life cycle of the product advances. When you sell a product such as Atacadao card at Atacadao stores, sometimes this is the first card that consumer will ever get. We are doing financial education, the customer thinks that their payment form can be used exclusively in the Atacadao stores, but little by little we inform consumers that is a brand card, it can't be used at any point of sale that have US terminal available.

So you will probably see something very similar to what we see with Carrefour card where they ask us, share everything that is spent outside the Carrefour and Atacadao ecosystem is gaining more share. And the half-year numbers for Atacadao card we have something around 50/50, 50% of customers spending is Atacadao stores. The other 50% is off us, when you look at a mature portfolio, such as Carrefour is this number is around 25% in stores, 75% to off us. So it's about financial education and communication about the product to educate consumers to know that they can use the cards outside our own stores.

Now this is a business which is specifically important for the bank in terms of P&L because the transaction has a totally different economics than a transaction that happens in Carrefour and Atacadao stores and also because of the consumption profile. This is the information that we're collecting about customers to understand their spending profile, what they consume, what they buy, and if there is any opportunity in terms of communication to attract to appeal to customers to consume a certain service or SKU in our ecosystem. So these are the two major advantages of having off us spending growing and gaining share in our portfolio.

Q - Gustavo Oliveira {BIO 15129435 <GO>}

And this 50/50 ratio, do you think is stabilized?

A - Carlos Mauad

No, it is not stabilized yet. The trend is that spending off us will gain share. It does not cannibalize on a spending, but it should gain more share, because we are reviewing the Atacadao portfolio because every month that goes by in this portfolio, we capture more data, more information and we can expand the credit limit of these consumers and naturally they are trying to say that they can use that all off us. So I believe that Atacadao cards will not get to what we see in the Carrefour card to 25%, 75%. But I believe that off us will continue to increase its share.

Q - Gustavo Oliveira {BIO 15129435 <GO>}

Okay, thank you very much.

Operator

Our next question from Irma with Goldman Sachs.

Q - Irma Sgarz {BIO 15190838 <GO>}

Good morning. Thank you for the opportunity. I have two questions. Two follow-up questions. In terms, there was a lot of (inaudible) trucker strike last year, the World Cup, Easter. So it's kind of difficult to understand what is the underlying factor in like-for-like sales. So when we think about 5% or 8% including e-commerce, how should we think this number for the second half of the year, obviously there will be other impacts -- impacts from the economy in the expectations. In addition to inflation -- the inflation move that has -- the inflation rate that has eased a little. So what are your expectations looking forward?

And my second question is a follow-up question of one of the first questions asked about the data strategy. I just want to clarify, do you have an integrated view of CPF's or taxpayer numbers, individual taxpayer numbers to basically understand consumers' journey, the full consumers journey of the omni-channel customers that sometimes buy online with the app, through the website or they go to brick and mortar stores to different formats of stores or perhaps through Rappi. Do you have a unique customer view, that's how they call it?

A - Carlos Mauad

Regarding like-for-like you are right, every quarter we have many events that make it hard to compare, but what I can tell you is that we can look at the trends, every quarter, there are different events, Easter in one quarter, in the following year Easter is in another quarter. But if we look at retail trends, there is a very clear trend. Since the first quarter of 2018 initially, okay, we had deflation, inflation started growing again and we had a lot of inflation at a certain moment, this year this didn't really happen. And there was an acceleration of retail this year, the fourth quarter of last year posted like-for-likes of 13.5%, 6.1% in the first quarter of this year, 8% in the quarter -- in the second quarter and the underlying reason are not events that happening in the quarter, because this quarter unlike last year, we had a reduction in consumption.

So a very difficult and challenging environment, despite that retail accelerated. It is about Noel said all of those initiatives made last year. A move that we mentioned last year of repositioning our prices in the hypermarkets, the work we did on assortment healthy food isles, a lot of efforts regarding our private label, our private label has a 13% share in food sales. Two years ago this number was 7%. In two years, we almost doubled our private label product share. So it's a set of initiatives in our view that explain the current performance. And again this -- in this good performance happened in a challenging environment. Had we not made these decisions last year, we would never have achieved the current positive performance.

And with the assumption that the economic environment will not change. We don't -- we don't envision a very different performance in the future. Now, as you said it yourself at the end of your question, there are initiatives release of the FTTS workers compensation fund and PIS/Pasep. if this happens, it will help. Regarding your second question regarding our data strategy. We have an area in the Carrefour Group and integrated data area, and this is exactly what we're doing, we are collecting all of the data that was spread in

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different business units, we are putting it all together and we are -- we are trying to use data with the omni-channel strategy, Mauad said Usou zero is an omni-channel initiative that was very interesting, it was a decision of the bank that helps the bank, because it brings in new customers to the bank. But at the same time, it is one way of acknowledging customers loyalty and give them an incentive to buy more. The decision by the bank and by Atacadao of accepting the Carrefour card is the same reason, why did we make this decision because we analyze the data. So we have a lot of initiatives to drive and to build on this lots of data that we have.

Q - Irma Sgarz {BIO 15190838 <GO>}

Thank you.

Operator

(Operator Instructions)

A - Carlos Mauad

If there are no more questions, I will end today's call. I hope it gave you greater insight into how Grupo Carrefour Brasil omni-channel ecosystem strategy is developing. All these advances are the result of strategic decisions and investments in the past year to build an interconnected ecosystem and ensure continued sustainable profitable growth ahead. Thank you very much for your attention, and have a great day.

Operator

This concludes today's question and answer -- this concludes Carrefour's conference call for today. Thank you very much for your participation. Have a good day.

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