

Y 2019 Earnings Call

Company Participants

- Fabio Adegas Faccio, Chief Executive Officer and Interim Chief Information Officer
- Laurence Beltrao Gomes, Chief Financial Officer and Investor Relations Officer

Other Participants

- Gustavo Oliveira
- Irma Sgarz
- Joseph Giordano
- Richard Cathcart
- Thiago Macruz

Presentation

Operator

Good day, ladies and gentlemen, and thank you for waiting. At this time, we would like to welcome everyone to Lojas Renner's Fourth Quarter and Year-end 2019 Earnings Conference Call. We would like to inform you that today's live webcast, including the slide show, may be accessed at Lojas Renner's website at www.lojasrenner.com.br in the Investor Relations section at the webcast platform and MZiQ platform. As a reminder, questions will be also taken by telephone and by the platform.

Also this event is being recorded and all participants will be in a listen-only mode during the company's presentation. After that, there will be a question-and-answer session when further instructions will be provided. (Operator Instructions).

We would like to remind you that questions from journalists can be directed to our press office by the number 11 3165-9586. Before proceeding, let me mention that forward-looking statements that might be made during this call relative to the company's business perspectives, projections and operating and financial goals are based on the beliefs and assumptions of Lojas Renner's management and an information currently available to the company.

Forward-looking statements are not a guarantee of performance. They involve risks, uncertainties and assumptions, because they relate to future events and therefore, it depend on circumstances that may or may not occur in the future. Investors should understand that general economic conditions, industry conditions and other operating factors could also affect the future results of Lojas Renner and could cause results to differ materially from those expressed in such forward-looking statements.

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Now I'll turn the floor over to Mr.Fabio Faccio, CEO. Mr.Faccio, you may begin.

Fabio Adegas Faccio {BIO 19664887 <GO>}

Good afternoon. This is Fabio speaking. And I would like to thank all of you for participating and for your interest in the company. With me, we have Laurence and Paula. Before turning the floor to Laurence, I'd like to speak about the year, the past year and the opportunities ahead of us.

2019 was a transition year. In addition to Gall's succession and my taking over as CEO, we also work on the main deliveries of the digital cycle, structured around three main strategic fronts that prepared us for the transformation of the company. In this journey, we had important evolutions and achievements that make us confident that very soon we will have the best retail omni experience in Brazil.

I will mention just a few examples of important deliveries that we had along the year. We already have four different ways to pay for purchases at the stores, which really helps reduces queuing. In addition to traditional takeouts, we have mobile sale available in 100% of Renner stores in Brazil, where the employees specific devices can finalize purchases at any time in the selling area. We're also installing self-checkouts ready available in some units. And digital post payment is reviewed by the client, by the customer through the Renner app that they download to their own devices. This is available in 30 stores.

Also, we have digital sales to reach e-commerce are sold in brick-and-mortar stores. Still in 2019, we started testing using store's inventories for click and collect in 75 stores for now. And we have now a 100% autonomous journey from purchase all the way to the pickup. In addition, we have same day delivery, in Rio de Janerio and next day delivery for So Paulo. As a result of these initiatives, we have achieved a record levels of delighting the customers, including in December, which is the period when we have the highest flow -- the highest of foot traffic at the stores.

We had a very high number of customers saying to us, we're happy or very happy in 2019. We also implemented RFID in 100% of the stores. And though what that was impossible to increase the frequency of inventory count and expedite the replenishment of items to the selling area. This increased productivity and reduced stock-outs. For the Omni transformation, RFID is an important step for online and offline integration. We will allow us to use storage inventories for e-commerce sales with more safety.

With that we're having quite improvements for customers who will receive their orders faster sent by the closest store in addition to being able to count on the whole inventory of the company. As for e-commerce experience, we implemented improvements in usability and platform content and in omni-channel processes, making the channel growth for one more and consecutive year by around 50%. And again, above 3 times the online apparel market in Brazil, gaining market share -- gaining a share in our total sales.

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And also the Renner app is a highlight. Downloads grew significantly. We have 2.3 million active customers in 2019. The app gained relevance in our online experience, creating repurchase, representing 33% of sales and 45% of e-commerce accesses. As a result of the initiatives implemented, we will recognize with the award of favorite store in the apparel and accessories category. At Realize, our financial entity, we also had a lot of improvements adding convenience and improving customer experience.

In the year, we launched Meu Cartão. with immediate issuance of co-branded card in the brick-and-mortar stores. And turning to amounts of friction at the moment of payment, we also included AI, artificial intelligence tools. We have virtual assistance in the Renner card section. In the app we made available some functionalities such as renegotiation of purchases and contracting of services, removing more than 10 million excesses from the cards department. We also started a new relationship program, as benefits, improve customer loyalty.

Now looking at 2020. According to the capital budget presented, we're going to invest R\$910 million, which includes the opening of 25 to 30 Rebber stores, three Camicado, seven Youcom and two Ashua.

We will also be investing in technology systems and in a new distribution center with 150,000 square meters, and that will bring us more speed, more synergy among our companies and efficiency gains in the logistics operation with greater accuracy of product location at the stores and customer deliveries in addition to flexibility to serve the omni experience and to support the company's growth in coming years.

As planned, we reviewed our expansion plans for Renner in Brazil, and we renewed our target. We should maintain the level of store openings at 25 to 30 stores per annum, at least until 2025. In this period, we are going to have more openings in countryside cities, with street shops, and we will continue to explore possibilities of stores in shopping malls so that we can reach about 520 stores in operation of the Renner brand by 2025.

Regarding external factors, it seems we'll have an improvement in consumption environment with favorable interest rates in addition to more employment. In addition, we believe that with the improvements that we are implemented in terms of product quality, reducing lead time and improving purchasing experience, we'll be able to maintain our good pace of sales growth and we will maintain our gross margin.

This year, we intend that for the omni transformation, given all of the improvements and advances will use our leverage in favor of our strategic projects and to consolidate our position as the main fashion courier. The amount invested will be gated to improve e-commerce experience, particularly regarding delivery services and the omni-channel with greater speed and autonomy for customers during their purchasing journey. We also believe that we will have opportunities in extracting, capturing value from a potential combination of our businesses in one single platform.

To form our ecosystem, we'll continue to structure our data and technology teams that will be distributed to our business areas, and we will also invest to consolidate our operations

abroad. As for financial products, we will also be investing in hiring data and technology resources to move forward with the transformation of this business.

We are defining our strategy that include renewal of portfolio of products and greater offering of solutions and utilities that will impact positively the lives of our customers. Rest assured that we are paying attention to transformations in this segment and there are many opportunities ahead of us.

In the context of a more and more than responsible fashion, we will invest in heading in achieving our commitments of sustainability for 2021, with efficient eco management of our operations, responsible suppliers, sustainable products and services and engagement of our audience around sustainability.

I turn the floor now to Laurence, who will get into details about the results that we disclosed yesterday.

Laurence Beltrao Gomes {BIO 15361799 <GO>}

Good afternoon, everyone. This is Laurence. I will comment on our performance both in the fourth quarter '19 and full-year 2019. Fourth quarter of '19, was marked by an increase in customer traffic at the stores and the good acceptance of the high summer collection in this context.

we had revenue increasing 10.7%, of same store sales of 6.2% -- up 6.2%, generating the same-store sales of 12% in the fourth quarter of '18. When we compare, it shows that we continue with a good growth pace along the full year between January and December.

Net revenues grew 13.2%. Same-store sales up 8.7%. As for the gross margin, the fourth quarter expanded 0.6 percentage points, which reflects our commercial management and good quality of inventories.

For the full-year, gross margin was 56.3%, in line with 56.5% in 2018, which reflects foreign exchange pressures in the first-half and recovery of margins in the second-half of 2019.

Regarding operating expenses, excluding IFRS16, which totaled R\$875 million in Q4, we maintained the SG&A over net revenue ratio at the same level of Q4 '18. For the full-year, operating expenses totaled R\$3.1 billion -- R\$3.7 billion, 0.4 percentage point dilution in 2019 despite expenses with the strategic projects for the digital cycle. So retailing EBITDA net of IFRS for Q4 '19 posted a 14% growth with a 0.9 percentage point expansion in the margin. Full-year EBITDA increase was 14% with margin remaining flat.

Another highlight that I'd like to mention was the performance of financial products as a consequence mainly of the use of Meu Cartão, the co-branded card and the good quality of our loan portfolio. The result had a R\$99.4 million and in the year R\$391.5 million, up 12%.

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And so total adjusted EBITDA, net of IFRS was up 16%, R\$861 million in Q4 '19, 1.4 percentage point increase in the margin. In the full-year, total EBITDA was R\$2 billion, up 13.5%, an all-time high margin of 23.8%.

I also highlight the net income R\$513 million in the quarter, 17% up in the year. Net income of R\$1.1 billion. And in the pro forma, net or ex IFRS, we posted a 10% variation, which allowed our annual ROIC to be 21.4%

These were my main highlights. Our initial remarks are over, and now we can move to the Q&A session.

Questions And Answers

Operator

(Question And Answer)

Thank you. Ladies and gentlemen, we will now begin the question-and-answer session. I'd like to point out that question for the Portuguese will be taken first and subsequently, we will open space for questions in English. (Operator Instructions)

Mr. Joseph Giordano with JP Morgan will ask the first question.

Q - Joseph Giordano {BIO 17751061 <GO>}

Hello. Good afternoon, everyone Fabio, Laurence. Thank you for taking my questions. Actually, I have two questions about the digital cycle that we see happening in the company in recent years. So the first quantitative question. I don't know whether you can share this with you, but what would be the share of e-commerce to the same-store sales of the company?

I'd like to understand, is it a trend -- a growing trend in your opinion looking forward and looking at the format of the stores? The company will maintain the same pace of store openings in the coming years. So I'd like to understand, how will this store format evolve now that we have all of the digital tools, AI supporting the operation, as well as sales and interactions with the customers, will the stores be marginally smaller?

How do you see productivity of the new stores? And finally, looking at the gross margin. You spoke about a flat margin for the year. I would like to know whether looking forward, will you have marginal gains due to efficiency, perhaps lower promotional activities and more availability online? Should we start seeing the investment of potential gains to add more competitiveness, given the pricing strategy for the company?

A - Fabio Adegas Faccio {BIO 19664887 <GO>}

Thank you, Joseph, for the question. This is Fabio speaking. I think I have done three parts in your question. If I forget anything, please remind me. Regarding e-commerce share.

We showed you sales increase, which has been at the same level as the recent years. So it tends to increase. It's not so relevant in terms of total same store sales. We've had good growth of sales in our brick and mortar stores.

What we understand is that, online and offline together will increase same store sales. But we do expect constant growth of online sales, given the initiatives that we still have to implement this year. Among the things that we mentioned, a lot of things happened more towards the end of 2019 and there's a lot to happen in 2020.

So undoubtedly, e-commerce will have a greater importance in our business, particularly in terms of omni-channel, online and offline works together. As for the format of the stores and the expansion plan as you mentioned, yes. I guess that we would have a marginal reduction in the store size. And also because we will open some street shops and stores in countryside cities so there will be a marginal reduction in the size of the stores, but marginal, no change in the store format. But these stories will have a lot, particularly given that we don't have the physical presence in some cities, and this will add to our sales. And it will drive our online sales, in terms of omni-channel. So we need to be physically present in different cities.

So physical stores will drive also online sales. We believe that even with good online sales growth, we can increase the popularity of our physical network. As for the gross margin, we have to work to maintain our gross margins. Of course, we can offer little bit, given that there are many factors impacting it. But we have many initiatives to help us potentially have even more gain. We understand,

but we have a very high margin level -- a good margin level. And we have potential gains in terms of sales productivity, sales per square meter, more than gains and margin. Of course, we can grow both line items, but where we see greatest potential would be an increase in productivity of our sales. I don't know, if I was able to answer all of your questions. If I left anything else, please let me know.

Q - Joseph Giordano {BIO 17751061 <GO>}

You did answer all of my questions. Thank you very much, Fabio.

A - Fabio Adegas Faccio {BIO 19664887 <GO>}

Thank you, Joseph.

Operator

Thank you. Next question from the Gustavo Oliveira with UBS.

Q - Gustavo Oliveira {BIO 15129435 <GO>}

Good afternoon, Fabio and Laurence, I'd like to understand from you, how you see the impact of Coronavirus, impacting your supply chain, particularly now that will get into the winter collection when you import more items? Could you perhaps give us your opinion

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on that -- the country? How much is coming -- how much of the collection is coming from China? How much from other countries and the percentage of your imports that would be relevant in your winter season -- in the winter collection?

A - Fabio Adegas Faccio {BIO 19664887 <GO>}

Well, thank you. This is Fabio speaking. Well, actually, currently regarding production, we don't have any impact now. Because this has been scheduled -- all actions have been taken to contain the virus. And everything was already now planning. We have scheduled shipments and deliveries, considering the Chinese New Year. And we have to remember that after the Chinese New Year, the resumption as well, also the impact for now is zero.

Now of course, what could happen, if the situation extends for many months, that could cause an impact later, but not now. 30% of our total imports come from China. China is a very important country, but we have imports from many other countries, not only from China.

Now future production, if China doesn't go back to producing, which I think is very unlikely. I mean the country cannot be stopped for so long. But we have both the Brazilian suppliers and suppliers in other countries that could also replace the Chinese production. So in terms of direct impact on our metrics, the impact would be low.

We always worry about the global impact on the economy, but the impact on our network today is zero and future possible impact can be mitigated. We could shift our procurement to other partners. We have a very long group of partners and suppliers.

Q - Gustavo Oliveira {BIO 15129435 <GO>}

Thank you very much.

A - Fabio Adegas Faccio {BIO 19664887 <GO>}

Thank you.

Operator

Next question from Thiago Macruz from Itau.

Q - Thiago Macruz {BIO 16404924 <GO>}

Hello. I would like to understand the characteristics of online sales that you have disclosed, is the index similar, lower, higher? Could you share the margin of the sale? Is it similar to brick-and-mortar stores? Secondly, customers who buy online, are these customers there to do recurring purchases? Or are you getting new customers? If you could share this kind of percentage with us, it would be very helpful. Two questions then. Thank you.

A - Fabio Adegas Faccio {BIO 19664887 <GO>}

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Macruz, this is Fabio speaking. Thank you for the questions. Content mix assortment online is the same as in the brick-and-mortar stores. And sometimes we have some inventory volume that is concentrated more online. In the future, we can have a longer tail and then we could have a bigger mix than we have online. But there are many actions that we can take over time to maintain our e-commerce growth at very high level.

Regarding the margins of products, well, they are similar, depending on the sales mix. For example, Black Friday, on online had a different mix of products sold, but the margin -- it is a corresponding margin. We have a very healthy profitable operation with profitability increases over the year, not only increase of sales, but also increase in profitability. That's for who's the customer on and offline,

we have a online and offline customers who are great. We have new customers buying from us every year. And every year, e-commerce brings new customers on board, just like the offline channel. The biggest difference is the group of how many customers. Customers who came exclusively online, exclusively offline, and we compare with customers that buy on from on and off channels. These are the omni customers. These customers have a very strong frequency of purchases. They buy a lot more frequently than customers who buy only online or only offline and they have a higher average ticket.

They buy more than customers who shop exclusively online or offline, and that's why we believe that the strategy to integrate the channels is going to bring us more gains, considering online and offline shoppers, typical year.

Q - Thiago Macruz {BIO 16404924 <GO>}

If I can ask one last question, please. When you look at the economics of the new stores in smaller cities, do you take into account the base gains of these stores -- and the online? Or is this an upside to generate the expected results for the stores. This is my last question. Thank you in advance.

A - Fabio Adegas Faccio {BIO 19664887 <GO>}

It's an upside actually. As we still have many opportunities, we concentrate on the brick-and-mortar store opportunities. And online sales would be an upside. Perhaps that in the future, we could consider stores that would be complemented by online sales, but we still see many opportunities with the brick-and-mortar stores.

Q - Thiago Macruz {BIO 16404924 <GO>}

Excellent. Thank you very much.

Operator

Next question from Mr.Irma Sgarz with Goldman Sachs.

Q - Irma Sgarz {BIO 15190838 <GO>}

Hello. Thank you for the explanations and further guidance regarding store openings. I have two questions. First, regarding the expansion plan, you mentioned that you're going to have more street shops and more stores opened in smaller cities. Could you give us more color in terms of how comfortable you are with a sufficient pipeline

for the existing -- for stores in existing malls and stores in future shopping malls to support the 25 to 30 new stores to be opened per year, because we see that during the crisis,

of course, some shopping mall operators held back their plans to build and open new shopping malls. I do know that there is a pipeline of shopping malls, where you could open your anchor stores. I just would like to have more color in terms of how you see this evolving in coming years?

My second question is about Camicado. I know you've been making some adjustments in inventories and adjusting your product mix, could you give us more detail in terms of what's happening and how you see the margin evolving looking forward because for two years you've had some pressure on the gross margin? Do you see room for the gross margin to recover to levels closer to historical peak anything more structural changing in this market? Thank you very much.

A - Fabio Adegas Faccio {BIO 19664887 <GO>}

Hello, Irma. Thank you for the question. I think that regarding the stores expansion plan, we mentioned the stores of the Renner brand. We have also stores to open in the countries where we operate. We also have stores of Youcom, Camicado. But I think that your question comes at a very timely moment, because in recent years we saw a deceleration in the opening of new shopping malls. When we have many new developments, many shopping malls, we took advantage of that.

We opened many stores during this period at these new malls. But when the pace started decelerating, we took advantage of opportunities in existing malls. We still have about 40 shopping malls that are already there, where we can open stores. So we still have a few new shopping malls expected for the coming years, we're considering that in the plan.

When we made our calculation, we are considering six to eight new shopping malls per year in the coming years. Perhaps when the economy picks up again, we might have even more in the future, but we are not counting on that in our plan. And that's why we made it very clear that this is the moment for us to intensify our presence in cities, where we could be present, but we were enjoying these opportunities at the malls. And now that we don't have many new shopping malls in the pipeline, we can open some street shops. And if we have more shopping malls being built again in the future, we will be looking at those opportunities, and that will be an upside. It's not considered in the current expansion plan. So if they -- these opportunities arise, there will be an upside. Regarding your second question about Camicado.

I think that for Camicado, we have some of our own problems. They were not market problems. We had a management problem in our product mix along 2019, and we made

a decision to do purging of some of these products, and that's impacted our margin in Q4 '19. And this had have been impacting our sales in prior quarters.

Now of course, we are not 100% recovered from that, but the most important work has been completed. So we expect gradually to recover Camicado's position. It's too early to speak about results, but I can tell you that we are very optimistic about Camicado's performance in 2020, so just nothing structural about Camicado.

Q - Irma Sgarz {BIO 15190838 <GO>}

Thank you very much. If you're comfortable that when the economy picks up and the market picks up, the market is moving online, but you're comfortable that this is not the main reason for pressure?

A - Fabio Adegas Faccio {BIO 19664887 <GO>}

No. We believe that -- so we were not impacted by any external factor. Indeed, we have some management issues. We had some important changes in the management of the company and this was strategic and we're still seeing the good results of that little by little, we are recovering our . I think we're still some way to go to get to the best margins but sales have been better than in the last quarter, margins as well. And it's exactly what I said, we still have a little over a month ahead of us.

And we will have many initiatives at Camicado that should start generating a lot of return to us -- at the marketplace, which is at a very incipient phase.

We have the online initiative presenting a lot of improvement opportunities at Camicado. We can improve the lead time for all of our brands of the group, but Camicado has the biggest possibilities and opportunities in terms of lead time, deliveries, et cetera. So we can grow on and off channels for Camicado. It's a great opportunity. If it doesn't happen, it's not because of the market, it's because we need to make some improvement, but we're doing our homework. And I think that very soon, we're going to have good news about Camicado.

Q - Irma Sgarz {BIO 15190838 <GO>}

Okay. Thank you.

Operator

Next question from Mr.Richard Cathcart with Bradesco.

Q - Richard Cathcart {BIO 16457807 <GO>}

Hello. Good afternoon. Fabio, my first question is about the communication of all e-commerce tools. You did a lot in very little time. So I would like to understand, to what extent are you communicating this to customers at the brick-and-mortar stores or in the main media? Can you be more aggressive in 2020, 2021 to bring more people to the e-commerce channel?

And my second question. In your initial remarks, you mentioned the consolidation of Renner's presence abroad. I would like to understand in more detail, your plans for Uruguay and Argentina for 2020? Thank you.

A - Fabio Adegas Faccio {BIO 19664887 <GO>}

Richard, thank you for the question. Regarding communication of e-commerce features, functionalities, et cetera, well, we know, that analysts and the market believe that we don't communicate that well. But the thing is we prefer to do more than talk about it.

We have to make sure that things are well consolidated. So yes, we deployed a lot of new things for e-commerce, so many new features and functionalities. And we're testing these things, we want to evolve them. We don't want to communicate and cause frustration for customers. We want to communicate to them when we assure that things will work really well. We don't want to frustrate our customers. And yes, I think we have an opportunity to communicate these features more. It's actually something we've been discussing in-house.

There are a lot of things that we have deployed and that we will start talking more about them to customers. And this will definitely drive sales online and in the Omni channel approach.

Regarding consolidation abroad, we don't have to stabilize our operations and enjoy the opportunities that arise. Of course, marginally we can have another store opening here and there, but this is not where we're going to be investing a lot. When we consider the international operations, we want to consolidate our stores, where we are already present.

Q - Richard Cathcart {BIO 16457807 <GO>}

Excellent. Thank you, Fabio.

A - Fabio Adegas Faccio {BIO 19664887 <GO>}

Thank you, Richard.

Operator

(Operator Instructions) We are now closing the question-and-answer session. I would like to turn the floor to Renner's management for their final remarks.

A - Fabio Adegas Faccio {BIO 19664887 <GO>}

Well, we would like to thank you all for your presence on this call and for your interest. Be assured that we are working strongly on many opportunities that we have. And very soon we'll give you more detail and color on some opportunities that we are working on.

Thank you very much for your attention. We remain available for further clarification through our Investor Relations team, Laurence, Paula, and the whole team. And I'd like to remind you that on April 16, we are going to have our shareholders' meeting and we will

be available through a secretariat of corporate governance to help you with that. Thank you very much for joining us and have a good day.

Operator

This concludes Lojas Renner conference call for today. Thank you very much for your participation and have a good day.

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