

Q2 2013 Earnings Call

Company Participants

- Frederico Trajano Inacio, Chief Sales and Marketing Officer
- Marcelo Jose Ferreira e Silva, Chief Executive Officer
- Roberto Bellissimo Rodrigues, Chief Financial Officer

Other Participants

- Alice Fernanda, Analyst
- Fabio Monteiro, Analyst
- Fernanda Faria, Analyst
- Irma Sgarz, analyst
- Pedro Pessoa, Analyst
- Raquel Rodrigues, Analyst
- Ricardo Boiati, Analyst
- Tobias Stingelin, Analyst
- Victor Pascoal, Analyst

Presentation

Operator

Good morning and thank you for waiting. Welcome to Magazine Luiza's conference call to discuss the results related to the second quarter of 2013. I would like to inform you that this event is being recorded and all participants' will be in listen-only mode during the Company's presentation.

After the presentation, we will initiate the Q&A session, when further instructions will be provided. (Operator Instructions) A replay of this event will be available after it is concluded for a period of one week.

We would also like to stress that any statement made during this call related to the business outlook of Magazine Luiza, projections, financials, and operating goals are based on beliefs and assumptions from the management of the Company as valid information currently available in the market. Future considerations are no guarantee of performance, because they involve risks, uncertainties, and assumptions and therefore depend on circumstances that may or may not occur.

Investors will understand that general economic conditions, conditions of the industry and other operating factors may affect the future performance of Magazine Luiza and may

therefore lead to results that differ completely from those expressed in such future considerations.

To start this conference call, I would like to give the floor to Mr. Marcelo Silva, the CEO of the Company, for the presentation. Mr. Marcelo, you may proceed.

Marcelo Jose Ferreira e Silva {BIO 2096569 <GO>}

Good morning, and I would like to thank you all for participating in this conference call where we will discuss the results for the second quarter of 2013. We are just anticipating ourselves because this comes from the consolidation of our stores that we initiated last year.

So, I will start taking with our revenues. Total revenue has increased by 11.2% when compared to the same period of the year before. We reached R\$2.2 billion. I would like to highlight growth of same-store sales of 9.3%, when compared to the same period of the year before. I would also like to say that this comparison base is very strong, because last year same-store sales we had already managed to increase for conventional stores 9% and e-commerce 45%.

In addition, in this last quarter, more particularly in June, our economic environment was more challenging, the economy is slowing down gradually, and in addition to that we had some demonstrations on the streets, there were a lot of Brazilian soccer games on Saturdays, and all of these factors affected our sales in June, but nevertheless, we do believe that we had a very satisfactory performance in the second quarter of 2Q13. And at the same time we maintained the margin, and in fact we were able to increase by 0.2% and consolidated our sales especially in the areas where we have been present for longer, and we were also able to increase our gross margin in the Northeast stores due to the integration.

Today we have controlled, we have ways to monitor and follow up, and we were able to introduce the same procedures and the same comparison basis that we have with our stores in the South and Southeast. So, the Northeast gross margin has been increasing gradually, and now we'll elaborate further on. But I would like to make a special highlight, which is the profitability of LuizaCred.

LuizaCred improved its gross margin, so delinquency levels are absolutely under control, thanks to our credit card policy, which is very conservative, and it was inherited from Itau/Unibanco, and also we promoted a very important effort to reduce operating expenses. And LuizaCred's EBITDA went from 3.1 in the second quarter of last year to 10.2 in the second quarter of 2013, and as a consequence net margin went from 1.2 to 5.6. This is an important highlight, we had already talked about several initiatives that were undertaken with Itau to improve LuizaCred's profitability. And all of that paid off, and in the second quarter we are happy to say that LuizaCred's profitability has increased.

There was an exceptional fact that it was already in the pipeline, because we solved our stake holding and our distribution center in Louveira, at Bandeirantes Highway. Magazine

FINAL

Luiza had 76.7% of stake and the remaining of around to the holding of the Company. With that sale, we were able to include 205.5 million in cash and that gave us 205 million in net operating gains. And the purpose of that sale was to be aligned with what we had thought about before, which is to capitalize the main business of the Company and in turn to increase returns to our shareholders, which is the main purpose of the company.

All of these actions, like growth of revenue, increases in gross margin, and the profitability of LuizaCred, and the additional sales. In turn, our consolidated EBITDA reached 160.1 million, producing our extraordinary operating gain. Our adjusted EBITDA is 94.8 million, which represents 5.1% over the net margin. And therefore this is way above the first quarter of 2013. I think you might recall that we said before that our purpose is to present positive results throughout the period in a consistent base.

In the first quarter we had 3.0% EBITDA, and now that number has jumped to 5.1 million in terms of adjusted EBITDA. We were also able to reduce our SG&A sale by 0.7 percentage points even though we did not have such a significant contribution from e-commerce and also the increasing effort in our marketing portfolio because of all of the events that took place in June. So, we will also talk about sales performance after June or after the second half of this year.

Our consolidated net income was R\$54.7 million and this represents 3% net margin and interests of adjusted consolidated net income that is 11.5 million, with a net margin of 0.6%, which is way above what we reported in the first quarter of 2013, still in line with what we said in terms of achieving gradual performance increases.

Now, to talk a little bit about more of the financial KPIs, I would like to call Roberto, our CFO, to talk about the main economic highlights of the Company.

Roberto Bellissimo Rodrigues {BIO 17269312 <GO>}

Good morning. In the next slide, talking about the of the stores. Well, we showed that we inaugurated three stores in the half of the year, we closed one in the entire year, we inaugurated five stores. And when compared to the year before, our sales area increased 1.5% and once we compare that to the 11.2% growth in total revenues, it shows that we were able to achieve important sales figures in keeping with our concept of same-store sales.

In the chart below we show growth of same store sales the base was 9% on conventional stores, and total growth including e-commerce, still in the concept of same-store sales, 9.3%, considering a base of 13% on the second quarter of last year, which is a significant growth. We were able to expedite growth vis-a-vis the first half of the year and we are still gaining more market share. At the top right, we show our investment plan. We are still investing; we invested 34 million in the first part of the year, and then 61 million distributed between new stores, refurbishing, IT and logistics, and we still have 275 stores.

Approximately 38% of our total numbers of stores are still in the process of becoming more mature. When I say mature, they should contribute to a gradual improvement of our results as same stores become more mature.

FINAL

In the next slide, we talk about our finance sales mix. That was very important to the overall result of LuizaCred, as Marcelo already mentioned. It was another very good quarter, it was the third consecutive quarter where we experienced still a consistence growth. This also shows the strategy to change the mix of finance sales that was initiated early last year, was very assertive, and it brought about enforce new results, the share of CVC went from 18% to 20%.

Luiza Card, due to our conservative position went from 22% to 16%, but that was offset by an increased share of third-party credit cards that went from 32% to 36%. And that was the first level of the previous quarters. Therefore, cash sales is very much stable. And LuizaCred, even though it had a decrease in terms of total sales, the revenues are increasing; it grew by 9.5% in terms of total revenue, due to direct credit to consumer and also on our stores, which really helps us to activate more clients.

In the next slide, I show the base of cards, and due to our conservative position, the numbers have shrunk a little, and it is now at 3.6 million, but I would like to say that 90% of this base refers to active cards. And the more active and mature they are, the more profitable they become in terms of our card base. Our portfolio is also increasing, we grew 5.4% when compared to the same period of the year before; it is becoming more stable at around 3.6 million. And as this is a stable portfolio and as the results are improving in terms of LuizaCred, the return on investments will be greater and therefore, we will be able to distribute more dividends, and the dividend payout will be higher.

In the next slide, we show you how this portfolio has evolved. The quality of LuizaCred's portfolio is still very sound and good. The delinquency KPIs in short-term are improving, are getting better, MPL 90 days is better than the year before, it is just 1.6 percentage points lower than the year before, non-performing loans. And LuizaCred's results reinstate that this is the improvement that we expected to see. And in terms of allowance for loan losses, these expenses experienced a decrease from 48.4% in the second quarter of 2012 to 45.7% in this quarter. In expenses also we had a decrease which also helped LuizaCred to experience an EBITDA margin of over 10%, a two-digit EBITDA. And then we had 3 percentage points of improvements of EBITDA at LuizaCred.

Now, going to the next slide, I will talk about our revenue growth. On slide ten, in the second quarter our total gross revenue increased 11.2%, total net revenue grew 11.3%, so it grew more because of tax reduction of smartphones, Internet sales increased 13.3% in that quarter, and here today, it's around 17%. I would like to say once again that the base is high, the profit margins of the channel are still maintained, and our websites was awarded a prize of being the most innovative website this year.

Next slide, we show the evolution of the gross profit. It grew 12.2% in the second quarter, year to date we experienced a margin increase of around 30 basis points and if we continue experiencing this gross margin of around 29% until the end of the year, I believe that we will see an evolution on a year-on-year basis of more than 50 basis points vis-a-vis a year before.

FINAL

Next slide, on page 12, we show the evolution of operating expenses. Sales expenses were in keeping with those of the year before, a little bit lower due to tax reductions in our payrolls, both of them together accounted for 24.7% of net revenue, 0.7 percentage points lower than the first quarter of this year. I would like to remind you as well that most of the dilution of expenses that are expected should take place particularly at the end of the year.

In terms of other operating expenses and revenues, we have some non-recurring items. The gains what came with the sale of our stake at the Louveira distribution center, R\$205 million in non-recurring tax provisions, and non-cash, 45 million, and also accounting write off stemming from the immigration process of the former Lojas Maia, as amounted to 16 million.

So, the net figure gave us gains of R\$65 million to the total EBITDA of the Company.

The next slide, I show you equity income, LuizaCred was the main highlight in terms of increases in equity income, we increased the gross margin, we reduced provisional expenses and operating expenses, and in turn we increased the efficiency level of LuizaCred.

The profitability of LuizaCred has already superseded returns on net income of over 5%, and the expectations are still quite positive. We say that LuizaCred had the best first half of the year of its entire history; still in keeping with its trajectory, we should have the best year of the Company thus far.

In the next slide, we show EBITDA evolution. Total EBITDA was 160 million this quarter, adjusted by non-recurring factors it was 95 million with a margin of 5.1%, growing 15% vis-a-vis the year before. And I would just like to make a comment, in that previous concept that we were consolidated after last year, proportionally 50% of our joint venture's EBITDA grew more than 20%, reaching a growth of 24% this quarter when compared to the year before.

Next slide, we talk about financial expenses, we were able to dilute financial expenses, they came from 3.2% to 2.9% in that quarter, mainly due to CVI reductions. And in the following slide, I show you net income, which was 54.7 million in that quarter. And in adjusted terms it was 11.5 million, with a margin of 0.6%, and that was an evolution both vis-a-vis the first quarter of this year, and the before, and also in terms of recurring net income in that same quarter of the year before.

So, we may say that this improvement in the final net income figure went through almost all of our lines, therefore it is very consistent, going from growth in sales, increases in gross margin, dilution of expenses, improvements in the LuizaCred results, extraordinary gains, reduction of financial expenses, and also reduction of net debt, as we will show you in the following slide.

We have here that we were able to maintain working capital, discounted receivables increased due to growing increases in sales, because of third-party credit cards, and

indebtedness level decreased both in nominal terms, as well as in terms of adjusted EBITDA, reaching 2.1%.

And with that, I would like to give the floor back to Marcelo. Thank you.

Marcelo Jose Ferreira e Silva {BIO 2096569 <GO>}

Very well, then. I would just now like to refer to our expectations for the next quarters. We still maintain what we said before that we will deliver more robust results and consistent results throughout the period. And, as we saw in the first quarter, lower net income, but better in the second quarter, and it will be even better in the following quarters.

Our sales expectation is maintained, so we maintain our position in terms of the budget for the second quarter. July was the best month of the year so far, and we heard opinions from other retailers in this regard. There is one exceptional point, which is a Government program called Minha Casa Melhor, which was recently introduced by the Government, together with Caixa Economica Federal, and this program involves the industry, retail, wholesale, and we must also say that Luiza Helena Trajano, our Chairman, had an important participation in this program; therefore, we have a very good growth expectation throughout the following months. This program tries to include, as part of the program, a new social class bracket that in the past did not have access to furniture and to things to refurbish their houses.

That we already talked about smartphones, this is a category that is reportedly increasing in the second half, smartphone sales increased substantially because this is what everybody desires or aspires to have, and we will hope to increase sales in the second half of the year. In terms of gross margin, we will maintain and grow our gross margin in the South and Southeast, and gross margins are still improving further in our Northeast stores.

As I said before, we are still adopting the same incentive programs to the managers of our stores in the Northeast as well, and we were also able to extend that to the salespeople; not only we will give them commission on sales, but also they will get a participation on the total margin. We believe that, throughout next year, the Northeast will be very close to the

margins, both net and gross, that we experience in the Southern part of the Country. We also introduced a pricing project, I talked about that in the previous quarter, and the purpose of this project is to add intelligence in the pricing structure per channel, region, and family of products, so with all of that we do believe that we will be able to keep our gross margin and yet improve it further.

In terms of costs and expenses, and we expected more significant gains in the first half of the year, we had a reduction of 0.7, but we still have to invest more in marketing, but with the introduction of zero-base budget, or ZBB, that we are introducing in the second half of the year, and we are, again revealing our entire price structure, which is a very important part of our costs and we are also investing in the DC, the DC here delivered

FINAL

Bloomberg Transcript

straight to the Southern stores, and we have one in the North, and this will expedite delivery of products to our consumers in that part of the country. And, equally importantly, we have the maturity of the stores by 2014. We said that one-third of our stores are not yet mature, but as time goes by we are introducing our models and systems, and I just talked about our new projects for the sales area, so the stores in the Northeast are beginning to mature, they will increase the profitability, and I believe that in about one year they will be in keeping with the other stores of the Company.

With all of these things, I must reinstate that we are totally convinced that we will deliver better results as we are already delivering good results to our investors.

Now, I would just like to say that we are very pleased with the results of this quarter. Here we have all of our executive officers; Roberto, Frederico, Isabel, Tatiana from Investor Relations, Marcelo Ferreira, LuizaCred's officer. So, if you have any particular questions related to LuizaCred you can ask him.

Then we have Marcelo Rodrigues, our IR team, so everybody is here, and we are very pleased with the results for this quarter. And we are at your disposal to answer your questions or to clarify any doubts that you may have concerning the results of the second quarter.

Questions And Answers

Operator

Now, we'll start our Q&A session only to investors and analysts. Questions that come over the web will be answered later on by email and we will be available to clarify the questions. (Operator Instructions) Ricardo Boiati from Bradesco has the first question.

Q - Ricardo Boiati {BIO 16528742 <GO>}

Good morning. My question is related to your expectations for the remaining of the year. If we normalize the comparison base, some of the programs that are benefiting some sectors, like Minha Casa Melhor, and the tax reduction of smartphones, if we can eliminate some particular effects, the economic environment or the demand environment leads the margin to improve or to be reduced in the second half of the year, considering all of the other variables related to consumer revenue? And I would also like you to comment a little bit about the competitive environment and whether you see more aggressiveness on the part of the market.

A - Marcelo Jose Ferreira e Silva {BIO 2096569 <GO>}

Thank you, Ricardo, for your question. You talked about two very important points, I would like to say that at the end of last year and early this year on we said that we would try to deliver on same-store sales a very high one digit, and two digits for the total of the Company.

FINAL

That despite everything that happened to the economy, and we managed to deliver what we promised due to improvements in our processes, and we also invested a lot in our team, we motivated our people, we have a very good communication system, which in our view is very important to our staff. And as we did not see changes in unemployment levels, we were able to keep our growth pace for the second half of the year.

July, last month, July was a motivating factor, a motivating month for the other six months to come. The first half of the year was also very important, because we were able to overcome our goals, in almost all the stores we were operating above expectations. In June there were some setbacks, but if there is no growth in unemployment and if inflation is under control, because what really affects the retail market is when inflation grows and consumers begin

to lose trust.

And despite everything that happened, inflation was still low, unemployment remained at the same low level, so we are not going to look at the cup half empty but we will look at it as half full, and we will deliver according to our proposal. This is our main goal. Magazine Luiza, even though there may be difficulties, we keep on going, and we have important competitors in the market as well, they invest in media and marketing and the market, and we try to work along the same lines.

Therefore we have to look at the glass half full, and that is why we are still keeping our same sales projects to the second half of 2013. And we are very confident that we will be able to reach our goal at the end of the year.

Q - Ricardo Boiati {BIO 16528742 <GO>}

Thank you very much for the answer.

Operator

Mr. Fabio Monteiro from BTG Pactual has the following question.

Q - Fabio Monteiro {BIO 3711690 <GO>}

Good morning. I have a question about Minha Casa Melhor program, and I would like to hear your views and expectations, particularly considering is that market bracket that you have today, whether you believe that you should increase your share due to that program and also in view of your sales in July, whether you could give me, an overview of what happened after that program and what is the average ticket. Could you give me like a general overview about it? I know that it is still in its very beginning, but I just want to hear your views about Minha Casa Melhor program.

A - Marcelo Jose Ferreira e Silva {BIO 2096569 <GO>}

We see that project as something very positive. The average ticket is relatively high, because it encompasses products like refrigerators, televisions, etc. In the North if our

Bloomberg Transcript

FINAL

expectation is even greater because Brazil is a large country, and there are still many families that do not own an LED TV or do not own a smartphone, and as people increase their income, they aspire to have better products. So, there is an expectation that there will be about a million products that will be sold due to the Minha Casa Melhor program. I mean July started sales slow in August we see an increase in sales, we see that also maybe happening in other companies.

I do not think that currently I can tell you about any figures, it is still too soon. I believe that in the third quarter I will be able to give you some more concrete figures about this program, but we are -- when I say that we maintain our budget for the second half of the year, it means that we are still considering this Minha Casa Melhor program, and we see this program with good eyes.

The Northeast is a region where we believe we will be able to have a larger growth, especially comparing to the South part of the Country. It is still too soon to tell because the program was introduced only a month ago, we prepared ourselves, Magazine Luiza, we involved all of the areas of the company to be able to cope with the project. Our Chairman or Chairperson, Mrs. Luiza, was personally involved, and we are really betting on this

program, because it will be able to include a lot of families that had no access to credit before. Once they acquire their home through Minha Casa, Minha Vida program, now they can furnish their home. Therefore, this is a very positive thing for us, and it is included in our budget for the second half of the year.

Q - Fabio Monteiro {BIO 3711690 <GO>}

Thank you, Marcelo. One more thing about expenses, I know that you talked about it when you referred to your results, but I would like to learn something about the zero-base budget and the multi-channel delivery system. I would like you to just give me an idea of the impact of these two plans in the second half of the year and even next. And whether you could give me an idea on the

EBITDA margin that, in your view, will be sustainable for the next two or three years, already incorporating the benefits of your plans?

A - Marcelo Jose Ferreira e Silva {BIO 2096569 <GO>}

We have been talking about 5% or 6% of EBITDA ever since the IPO, and we did that, we accomplished that in the 2Q, and we will continue to work towards improving that. We do not disclose things for the future, we only talk about concrete figures, but by the end of the year we will certainly increase or grow EBITDA. This quarter it was 5.1, and we also said that we will work between 5 and 6 million, but we have to do our best to push that number upwards. We will conclude the pricing project, and currently we are doing a very encompassing freight program from the South all the way to the Northeast. In second, we'll deploying ZBB in the second half of the year.

FINAL

Last year what we did was some work in the sales area. Now we are giving support to LuizaCred. LuizaCred has already initiated some work, and we are doing that together with our support area, just as we focused the immigration of both networks, and the entire management of the Company was working on that. All of our initiatives aim at improving results. And what do I mean by that? Well, once we improve results, we will increase our share through sales, we will be able to keep gross margin despite the competitive environment, and despite the fact that, at times, we have to work with setbacks in the economy, but we are succeeding in growing and, as a consequence, we will be able to deliver these numbers. We are growing gradually and consistently. We certainly believe that results of 2013 will be much higher than those posted in 2012, and by 2014 we will be able to report a better result, stemming from all of the projects and new programs that are being introduced by the Company now. So, we are just putting into practice all of the things that we said before, so in all of the different areas we are putting things into practice.

Also, when we talk about the profitability of the stores, we review all of the expenses, we are looking at everything in our stores, distribution centers, freight, and also the admin part of the Company is being revisited. Even in a period of low economic growth, we are posting good growth. It is very difficult to integrate two networks, and we did that in two years, but we are, at the same time, delivering good results.

Now the focus is results, and we will deliver good results in a gradual fashion. We will not have spectacular quarters, we will grow gradually quarter after quarter. We said that last year and this year as well, when we talked about the results for the year 2012.

Q - Fabio Monteiro {BIO 3711690 <GO>}

Excellent, Marcelo, thank you. Just one last question about LuizaCred. I have been looking at improvements in delinquency rates and, despite a growth of direct credit to consumer, I would like to see whether you see any optimum level of losses in CDC or direct credit to consumer. It is still at 28%, I want to know whether you have any internal goals in that regard, whether you see any deterioration in terms of the quality of credit in the short and mid-range, because maybe consumers will have a deterioration of their income.

A - Marcelo Jose Ferreira e Silva {BIO 2096569 <GO>}

This is Marcelo Ferreira, from LuizaCred. First of all, I would like to refer to credit control. Well, the portfolio is under control, there is a good alignment between the two partners, and there is a very good technology coming from both sides, Itau with the technology and LuizaCred with account origination. Our President every Monday looks at all of the KPIs related to losses, so everything is under control. We look at it with magnifying lenses.

The other question, related to direct credit to consumer of the card, our strategy is to offer the best finance structure and conditions to customers. The products that we have available at LuizaCred allow us to do that. You have direct credit to consumers, preferential credit card, and gold. And I can also tell you that we are training our sales team so they will be able to understand the customers' need and to offer them the best possible product. To offer the credit just to finance a sale does not make sense, so I offer direct credit to consumers.

And if, further on, they wish to have the card, they will already have a credit history and therefore it will be easier for us to approve the credit card. We do not have any fixed number, but our aim is to give customers the best possible financial conditions.

Q - Fabio Monteiro {BIO 3711690 <GO>}

It's was very clear, Marcelo. Thank you.

A - Marcelo Jose Ferreira e Silva {BIO 2096569 <GO>}

Thank you all very much and thank you, Fabio for your questions. Thank you.

Operator

Raquel Rodrigues from Itau BBA would like to ask the following question.

Q - Raquel Rodrigues

Good morning. My question refers to e-commerce. Could you, please, tell us what explains the increase in multi-channel sales in addition to the fixed base that you talked about last year? I want to know whether there have been changes in the e-commerce strategy or whether you were choosing to have maybe less growth but more profitability, and whether you could talk about the profitability of that particular channel. Thank you.

A - Frederico Trajano Inacio {BIO 17269235 <GO>}

Good morning, Raquel, and thank you for your question. Here it's Frederico Trajano, the Operating Officer of the Company. Well, talking about e-commerce, the main reason of a slowdown of this year vis-a-vis the year before relates to the fact that last year we grew 45% in the first quarter of last year that was the second quarter of 2012. And then, we grew 40% more in the second quarter of 2011. So, we had a top growth, and probably that was the main reason. We had two very good months, April and May, we were very optimistic in terms of e-commerce sales in that quarter, but June was very bad, it was a very poor month, and I think that was related to all of the public demonstrations on the streets.

So, we are now very comfortable with the numbers for the year, we are keeping the budget for e-commerce for the year. In July we had the best month of the year for e-commerce, we grew more than all of the other months, and August is very promising, even though the month just began, it is a promising month.

So, I believe that was just an isolated thing, and the comparison for the next quarter should be better, because we grew less in the third and fourth quarter of the year before, that is why I'm very confident in terms of e-commerce. We have not changed our strategy vis-a-vis the margin. The margin for last year was healthy, it was profitable last year, and it is still profitable this year, so there is no change in terms of the margin and pricing, so we will keep on growing with a sustainable margin.

Q - Raquel Rodrigues

Thank you very much.

Operator

Irma Sgarz from Goldman Sachs. Would like to ask the next question.

Q - Irma Sgarz {BIO 15190838 <GO>}

Good morning. I would like to revisit LuizaCred. I saw that you improved the delinquency on year on year, but looking at the numbers quarter-on-quarter, or maybe since March, and looking at the slowdown or the reduction level of delinquency over 90 days, there was a decrease of 25% year on year, and now here the decrease was lower.

And now I look at your provisions, and your provision level is lower when compared to the year before and also lower when compared to last year, and because of that the coverage went from 147% or over 150% at the end of the year, coming down to 126%.

I would just like to understand what are the drivers behind that, and what were the drivers that you chose to decrease that initial coverage, and if you believe that 126 or 120 is a comfortable level where you want to remain. And later on I have another question. Thank you.

A - Roberto Bellissimo Rodrigues {BIO 17269312 <GO>}

Good morning, Irma. This is Roberto. Let me just explain. First of all, I must say that we monitor delinquency levels short-term delinquency levels, and these levels are much better than they were a year ago. Talking about NPL, it has to do with portfolios that are being negotiated and that decreased a little bit due to our conservative position and also due to some seasonality. But this does not alter the results of LuizaCred because we have provisions for all of this credit under negotiation, so the provision and methodology is related to expected losses and that takes all of those elements into account, it is a methodology that has been applied by Itau. So, there was an excessive provision from the past and this did not affected the results for LuizaCred.

So with this methodology, this is what we achieved R\$20 million. And even that result, there is another figure that we posted in the release, which is LuizaCred's result if delinquency were to be measured this year according to the Central Bank law, which reports to the delinquency period bracket. And LuizaCred's result was R\$29 million, so this is a result that will be posted to Central Bank. And in the entire quarter R\$ 58 million it was more than IFRS, so we had more provision than was required by the Central Bank, according to the law 2682.

They only measure 90 days delinquency days, which the methodology considers more things like the risk per customers, the delay per bracket of delay, not just before 90 days or after 90 days. So, in that sense, we are very comfortable, both with origination, with the new credit levels and also the quality of the current portfolio. And also the conservative position of the results are still conservative, even excess provisions are

above the level required by the Central Bank, according to the law 2682. And we do not see any deterioration of these KPIs. The coverage ratio is just a consequence of all of that, it is a consequence of the methodology and not a target per se. So, the calculation of the provision that is then posted in the result line is based on the credit score on customer risk, delinquency period, and it is a more complex thing. So, the coverage ratio and everything else is just a consequence of that.

FINAL

Q - Irma Sgarz {BIO 15190838 <GO>}

Okay. And thank you for the explanation. Do you believe that in the future, as you feel comfortable with your delinquency levels in the bracket below 90 days, from now on allowance for loan losses should be year-on-year lower, and then the coverage ratio would be comfortable at that level? And because I think usually your coverage ratio is a little bit higher, right? Thank you.

A - Roberto Bellissimo Rodrigues {BIO 17269312 <GO>}

We are comfortable with our current coverage; the trend is that the portfolio will improve even further the results, in terms of the results. We believe that LuizaCred will cause consists results and higher figures, with expensive level and provision -- proportionally low. So, we are confident with that idea.

A - Marcelo Jose Ferreira e Silva {BIO 2096569 <GO>}

We believe that in 2013 LuizaCred will post very good results as we get in the last half of the year. Despite all of our conservative approach that we inherited from Itau/Unibanco, therefore we are very comfortable with LuizaCred's performance for this year.

Q - Irma Sgarz {BIO 15190838 <GO>}

Thank you. And my second question, a very brief one, is about the impact of the tax reduction on smartphones, and this is probably aligned with the previous question. Can you separate that effect in the second quarter of this year and after your good performance in July and expectations from now on? Do you think that have a relatively high effect in the mix? Should we take that into account? Or you think that is not very relevant?

A - Marcelo Jose Ferreira e Silva {BIO 2096569 <GO>}

Our commercial department, the performance in the first half of the year was exceptional. The projections from our commercial department is still very good for the second half of the year, it's even above average. And we are also increasing our market share in that category; it is only a category among so many others. And I can't just say that this is a determining factor, it is contributing to the overall scenario. What contributed the most was our sales team, is also Minha Casa Melhor program, smartphones and also the maintenance of the other categories, because they are performing at good levels of a year before, and they are growing overall. It is just a whole set of things.

I talked about smartphones, because this is what most people aspire to have. And the sales of that item is growing above average. But on average, its gross margin can be

compared to the other products. The gross margin from smartphones is higher than the average of the company.

Operator

Tobias Stingelin from Santander has the next question.

Q - Tobias Stingelin {BIO 1557190 <GO>}

Good morning. I have a question to Frederico, because he talked about e-commerce. Could you, please, give me some guidance, nothing changed your projection of the year is the same vis-a-vis e-commerce? Can you tell me what do you want to do? Do you want to grow in keeping with the market, above the market growth? Because my question is: to grow in the market, and do you think your margin will be pressured? We saw many companies stepping on the break, they are changing the strategy, they are reducing growth to improve margin; can you please elaborate a little bit more on that?

A - Frederico Trajano Inacio {BIO 17269235 <GO>}

Good morning, Tobias, and thank you for the question. So, let us talk about e-commerce. Reinstating what I said, e-commerce, I mean, we grew way above the market in the last two years. In the first half of last year, we experienced almost 50% growth, and the same thing happened in 2011. So, we are gaining market share in a consistent fashion, so now things are a little bit more difficult, as difficult than the second half of this year.

As I said before, in July we experienced a significant growth, but we are talking about 20% to 30% growth for e-commerce this year, considering a comparison base which is difficult. And I say that I am totally convinced that this will happen, already considering the fact that we grew 17% in the first half of the year now when compared to a difficult base. The trend is to have a better number than that in the second half of the year, and this is what we said before, that we will have growth of about 20% to 25%. We do not see any pressure in our margins; we have always been very rational in terms of e-commerce gross margin. The expenses of Magazine Luiza are much lower than gross margin in the market because we share an entire chain of supply of our conventional stores, so be that marginal expenses related to people.

So, we are very comfortable vis-a-vis the expenses of the channel, the multichannel product. The same truck that delivers to conventional stores follows I mean the e-commerce product as part of it is included in all of the routes of the company.

In the past, there was another transporting company that would leave Louveira, the DC, to deliver to Caxias do Sul down south, and then we had a DC that is closer to Caxias do Sul. But with the multichannel project that was reported earlier on, we are sharing the routes and we will have improvements in the delivery timing and also we would be able to reduce freight expenses.

One of the most impacting elements is freight in our e-commerce strategy. What we had was a quarter that was more difficult to compare with the other previous quarters,

especially due to what happened in June, but in Magazine Luiza I must say that July was very good, August is very promising.

Q - Tobias Stingelin {BIO 1557190 <GO>}

Thank you. I have another question related to working capital. What is the guidance from now on in terms of the vendors and supply?

A - Roberto Bellissimo Rodrigues {BIO 17269312 <GO>}

Good afternoon, Tobias. This is Roberto. What we can say, I mean working capital as a whole, starting with inventories or our stock base, we are working hard to improve the turnover of our inventory. And with the integration of the Northeast stores, we are already making improvements because we are adopting the same systems and procedures that we already had in the Southeast and Midwest, therefore we expect improvements. And we also expect a gradual improvement in the turnover of our inventory in terms of our vendor base or supply base. The numbers are good and high compared to the market average, and it has been around the same time line and this covers our inventory. Therefore we do not have any need for additional working capital to cover the inventory turnover, because that is covered with our suppliers. As we improve the turnover of our inventory those negative working capital gets better. So, our working capital requirement comes from two areas, third-party credit card, part of it with discount, and the other part is kept in our balance sheet, and also taxes to be recovered. That is another item in our balance sheet and this line has increased a lot in the last few years due to the process of tax replacement.

And we expect to revert that in the next two to three years. We are already doing that in the State of So Paulo, as of June, adopting a new way to collect that tax credit. So, we hope to see improvements in our working capital performance and also it will be gradual as we are able to introduce that special regime in all of the other states. So, in the next two to three years we expect that these changes and improvements and inventory turnover in terms of suppliers and procurement. We do not see any changes.

Q - Tobias Stingelin {BIO 1557190 <GO>}

Thank you, thank you all very much.

Operator

Fernanda Faria, Banco Espirito Santo has the next question.

Q - Fernanda Faria {BIO 21060928 <GO>}

Good morning. I would like to know whether you can quantify in terms of percentage of revenue, how much that payroll reduction has to in terms of further expenses, and how much more do you intend to spend in marketing and what could we expect for the next coming quarters?

A - Roberto Bellissimo Rodrigues {BIO 17269312 <GO>}

Good afternoon. What we can share with you is that the decreases in our payroll certainly did vary, but on average that should represent 30 basis point on the net revenue, tax reductions on payroll. And in terms of the marketing part of your question, I believe that that is just a set of expenses that, if you look at SG&A variation, you can see how much we were able to save last year, and this saving in tax reduction that we are able to promote in our payroll.

Q - Fernanda Faria {BIO 21060928 <GO>}

Thank you.

Operator

(Operator Instructions). Mr. Pedro Pessoa from GQI has the next question.

Q - Pedro Pessoa

Good morning. Could you, please, talk a little bit more about non-recurring expenses in Lojas Maia integration, and what is in your provision for 2Q13 expenses and what is that line all about?

A - Roberto Bellissimo Rodrigues {BIO 17269312 <GO>}

Good afternoon, Pedro. Let me begin with the integration of Lojas Maia. They were not cash expensive with the integration. We concluded the integration last year, and so we no longer have integration expenses. And in fact there is nothing else posted that relates to that integration. What happened is that as early this year we are now operating under the same system, and we had just to incorporate the accounting figures and the balance sheet of Lojas Maia. And we applied the same methodology for several accounting taxes, including inventory count. And we then identified that there were some differences and then we did the write off of that. And we do not believe that we will have any more expenses related to that merger, but that had no cash effect.

Q - Pedro Pessoa

I understood, that was an one-off.

A - Roberto Bellissimo Rodrigues {BIO 17269312 <GO>}

Yes, also in terms of tax provisions or fiscal provisions, we took advantage of the momentum and, still on a conservative note, we now have a very conservative balance in our liability line, on the liability side, and there hasn't been changes in the risk level of the company because, as you know, we are very conservative and responsible.

It is worth mentioning that we have an auditing committee, they audit risk and they have to report to the Board. And we also have a fiscal board or Tax Board with members appointed by minority shareholders. And then, we also have legal consulting, therefore we are very comfortable with our provision, and this has no cash effect, not in a short run or not even in the mid-range, because we are still being very conservative with all of our projects.

Q - Pedro Pessoa

What about the gains from e-commerce operation? Now you have multiple DCs, some of the risks has been eliminated?

A - Roberto Bellissimo Rodrigues {BIO 17269312 <GO>}

It has nothing to do with our e-commerce operation; it has to do with taxes, particularly ICMS. We already explained that before that the company is now participating in a special program that was made available by the State of Sao Paulo, and because of that we decided to be more conservative vis-a-vis the other processes, but it has nothing to do with e-commerce.

Q - Pedro Pessoa

Just one last question. What is the company feeling vis-a-vis the repurchase of stocks? That now have accumulated profit, there is space for repurchase?

A - Marcelo Jose Ferreira e Silva {BIO 2096569 <GO>}

We do not have anything to say about that, Pedro. If there is anything to that end, we will certainly communicate it to the market. But currently, we do not have anything to say about it.

Operator

Alice Fernanda from Credit has the next question.

Q - Alice Fernanda

Good morning. In terms of the result of the quarter on the half year, what was the impact of the sale of your stake at the Louveira DC? And if you had not sold, what would be the results?

A - Roberto Bellissimo Rodrigues {BIO 17269312 <GO>}

Okay. Good afternoon. The sale of our stake at the DC, the Distribution Center, represented R\$205 million in cash in terms of results. R\$126 million and the net from other non-recurring expenses that we mentioned from the incorporation of Lojas Maia and tax provisions, we had a gross effect of income tax of R\$65 million, net about R\$40 million. So, our result, looking at the recurring line, was between R\$11 million to R\$12 million when compared to R\$54 million or R\$55 million, which was the total. So, R\$11.5 million.

A - Marcelo Jose Ferreira e Silva {BIO 2096569 <GO>}

That was the part from the operation of the company.

Q - Alice Fernanda

Thank you.

Operator

Mr. Victor Pascoal, Itau BBA has a next question.

Q - Victor Pascoal

Good afternoon. It is a very specific question, still talking about LuizaCred and what Beto said on a previous answer. I remember that Beto said that there was a lower level of negotiation. Now, why did you decide to reduce the number of renegotiations, and what should we expect for the future?

A - Marcelo Jose Ferreira e Silva {BIO 2096569 <GO>}

Victor, thank you for your question. In fact there was a reduction, which was proportional to that portfolio. In terms of renegotiation, we do not report the results of Luiza according to the Central Bank every quarter, but in general we have to report the figures for half of the year, so you will see the LuizaCred's results in Central Bank with the evolution of LuizaCred's portfolio by level of risk of each customer, and also the balance of the portfolio that is being renegotiated and the balance.

In fact, the reduction in the balance has a little to do with seasonality and also something to do with the fact that we are renegotiating with customers that have a greater likelihood of paying that bill. But it is nothing that is extremely relevant, and once again we are very confident with the quality of the credit. We had more than enough provisions to cover that and we are still posting provisions with our higher than the minimum required, and in keeping with the methodology of the bank.

Q - Victor Pascoal

Okay, very good. Thank you.

Operator

If there are no further questions, I would like to give the floor to Mr. Marcelo Silva for his final remarks.

A - Marcelo Jose Ferreira e Silva {BIO 2096569 <GO>}

I would like to thank you all very much for participating in this conference call. And together with my colleagues, I would like to reinstate our position that we will deliver gradual and consistent results, positive results. At the end of this year we will post figures that are much better than those presented at the end of last year, and certainly we will fulfill the promises in terms of results by 2014, according to what we said before. We are confident in what we are doing, the customer is number one, comes first, and then next comes the results of the company, which is what we are demonstrating to you now. So, I would like to thank you all very much and I hope to see you next time when we have another conference call. Thank you.

Operator

This conference call related to the second quarter of 2013 of Magazine Luiza is now concluded. Thank you very much for participating and have a good day. You can disconnect now.

FINAL

This transcript may not be 100 percent accurate and may contain misspellings and other inaccuracies. This transcript is provided "as is", without express or implied warranties of any kind. Bloomberg retains all rights to this transcript and provides it solely for your personal, non-commercial use. Bloomberg, its suppliers and third-party agents shall have no liability for errors in this transcript or for lost profits, losses, or direct, indirect, incidental, consequential, special or punitive damages in connection with the furnishing, performance or use of such transcript. Neither the information nor any opinion expressed in this transcript constitutes a solicitation of the purchase or sale of securities or commodities. Any opinion expressed in the transcript does not necessarily reflect the views of Bloomberg LP. © COPYRIGHT 2022, BLOOMBERG LP. All rights reserved. Any reproduction, redistribution or retransmission is expressly prohibited.

Bloomberg Transcript