

Q3 2020 Earnings Call

Company Participants

- Eduardo Galanternick, Executive Director of E-commerce
- Fabricio Bittar Garcia, Commercial and Operations Vice President
- Frederico Trajano Inacio, Chief Executive Officer & Member of Executive Board
- Roberto Bellissimo Rodrigues, Chief Financial and Investor Relations Officer

Other Participants

- Andrew Ruben, Analyst
- Daniela Bretthauer, Analyst
- Gabriel Simoes, Analyst
- Irma Sgarz, Analyst
- Joseph Giordano, Analyst
- Luiz Guanais, Analyst
- Unidentified Participant
- Victor Saragiotto, Analyst

Presentation

Operator

Good morning, ladies and gentlemen, and thank you for waiting. Welcome to the video conference of Magalu about the results of the third quarter of 2020. We would like to inform you that this event is being recorded and simultaneously translated. And all participants will be in listen-only mode during the company's presentation. At the end of the presentation we will hold a Q&A session. Questions may be asked by phone and the questions received via webcast will be entered up towards by the IR team.

Now I would like to turn the floor over to Mr. Frederico Trajano, CEO of Magazine Luiza. You may proceed, Mr. Trajano.

Frederico Trajano Inacio {BIO 17269235 <GO>}

Good morning. Thank you very much for participating in our call about the results of the third quarter of 2020. Once again, we are doing a video conference and here we have all the executive directors gathered in the room, and they will all be available to answer your questions. And we will have quite a lot of time to answer your questions. We intend to have a very self-explanatory presentation, but I think you will have questions. I would like to start by the first slide.

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It is the toughest moment of the pandemic, this photo. When we closed our stores and at the beginning of the second part of March and we had to shut down overnight all our stores, a 100% of over 1,100 units. So we had to remove all the security equipment and we send them all to our DCs and this is one of our managers, Maria Ernie [ph], she works in this store. She's shutting down her store and she put the Brazilian flag here and she is very sad and afraid and very frustrated in the expectation of what might come and I think this photo is very good.

And for three months or even more, almost five months, in fact, we had part of our units closed March, April, May, June and July. And we are reopening the stores and the second quarter of 2020. I have been in the company for about 20 years, we have always placed our bet on the multichannel model and here we are a mono channel model here. And we have always believed that summation of the channels, would be our challenge and the path and over this period, we resumed the opening of stores and after the second quarter, which was practically mono channel then we resumed the model and the consequence of this model.

So in the third quarter, we had the reopening of the stores and all the benefits from multichannel, which is basically putting together exponential growth, a digital company, so Magalu was able in this quarter to show the model, the model that is being streamlined and refined over two decades, consequences the superior multichannel model (technical difficulty) 80% of the overall business and once again we have been -- we have never left our physical stores by side, so to say. We have never neglected them. What is important is the whole of the business and of course e-commerce due to consumer behavior and the digitization of countries is the major factor, but we do not do digitalization to the detriment of the physical stores. So the whole business grew 80% and we had the words comparison base of the whole market in the previous year.

Competitors grew zero or less than 30%, but nobody grew 47% such as we did in the previous year. So we had a very expressive growth and considering a very high basis of comparison. And even in the first nine months of the month, we were able to sell exactly what we showed in the 12 months of last year in spite of having almost five months with all our physical stores closed, either partially or totally.

And this is a very important point, because for the first time ever we had share gain of GSK, durable goods category, which is a very important category. Although we are winning share in other categories as well. We gained 5.4 percentage points of share during this quarter vis-a-vis last year. Our growth is not based on the coronavirus voucher, of course, it is helping everybody not only Magalu. So this helps everybody at the same level, but when you gain share, it is almost -- gaining share and historically, we have always gained share in crisis.

So in this context, Magalu always exits the crisis better than the others. So it was even better than the growth of the fourth quarter of last year and the professionals and the team they are reinvigorated and they create new competencies in moment of crisis so this share gain was excellent. Multi-share online, many people are leaving physical stores, but we continue to insist on this model, which is a multichannel model because we firmly believe that it is superior, okay.

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Now talking about profitability (technical difficulty) 20.3% operating expenses and this result shows that we can grow with operating leverage, when you have a result that comes from the increase in gross margin, your competitive position is very fragile because it is based on opportunity and if you get a lower gross margin and in spite of that you increase your net income, this means that you are efficient, you are competitive and you are giving the best possible price to your end customers.

So, our gross margin dropped in the quarter, not because we slashed prices because nobody needs a price war, the market is very heated up now. So you can tell with high margin, but simply we went from 40% to 66% of e-commerce participation and the margin of e-commerce is lower, but the expenses are lower, and this is driven by the past platform of the physical stores. So having a lower expense places us on a very interesting competitive position and where necessary, where it was not the case in this quarter, but this -- the efficiency of this model is the highlight of the company and this is why we celebrate this net expenses over net revenue result. And theoretically, it could even be lower because the GMV is not here in the net revenue. If you include the GMV, it will be even more significant. So, this is a very interesting figure for the company.

So BRL216 million in adjusted net profit, so 70% growth year-on-year. So I do not see e-commerce operation growing as much as we are growing. And this is a figure to be celebrated and this was achieved because of the consistent work with focus and discipline on the part of our whole team.

Once again, this is a quarter -- this is a very positive quarter in terms of cash generation BRL884 million. We have a very efficient working capital management. We had the best inventory turnover ever, 60 days, very high efficiency, and which has to do with our physical and of course, good negotiation with our suppliers, everything combined previously. (Technical difficulty) will be show you how this is consistent over time.

Now, I would like to talk about this growth in detail. We had 18% growth (technical difficulty) total sales in stores. And in spite of many stores closed in July and part of August, and only in September all the stores were opened and same-store 7%, same-store sales increase. And if you look at the same stores sales on the same days, it was even higher, 18% is a lot. So, the store is very well supplied and the inventories are very good and people are very motivated. And we have learned how to sell without the client being present physically in those stores via mobile, 30% comes from mobile sales.

So the sales person sells by means of a digital platform that allows us to sell remotely to the clients. Facebook or Instagram or WhatsApp, whatever. So -- and of course this revenue comes to the store that is to say, because they have their efforts rewarded. So, to say we put these revenues -- revenues from the physical stores and last year, we had already had a very good performance in physical stores. And I would like to remind you that it is margin and price of the physical stores with the margin of physical stores, Thank you for the reminder.

Next slide. (Technical difficulty) a very major growth in e-commerce as well. The next slide, 148% increase year-on-year. As slight deceleration vis-a-vis the second quarter and there

is a difference because Netshoe got into our base in the third quarter of last year. So without considering Netshoe the growth was very similar to the second quarter in spite of the reopening of the stores and e-commerce -- the e-commerce team and this we'll be talking about that later, did a very great job with excellent results for 1P.

And I would like to mention our growth. We grew 148% over 96% growth of e-commerce last year. The growth of e-commerce was major in 2019, the third quarter of 2019, 150% over 96% is really a big achievement on the part of the team and they are doing a great outstanding job, they're very competent.

And next slide please, I would like to mention here, the growth of 1P, it was much higher than what we estimated at the beginning of the year end. We understand that looking ahead for the relative opportunity of growth in marketplace in this moment of pandemic. Some had not planned very well for a resumption of growth and after corona voucher, and we have good planning. We had the necessary inventories and our logistics are much, much better than the other competitors and because of all that, we were able to gain share in 1P. We have a very positive sequence here for 1P. I believe that looking for the next two years, 3P tends to grow faster than 1P, but we also celebrate the result of 1P and we are agnostic regarding channels.

Next, 145% growth in marketplace sales and we had the strike on the part of the Postal Op service. So, 250% increase in marketplace sellers and we increased the number of categories and we are focusing on that. And the average ticket is higher, it is not only going to add GMV, but also frequency of purchases. So we focus on 3P to add to Magalu, a higher frequency of utilization, a higher recurrences or repurchases. In high average ticket, we are already the leaders in 1P. So, this brings about not only GMV, but frequency a new categories and higher tickets [ph] for our Superapp. So this is a work we done by (inaudible) and the whole team of marketplace.

And very much driven in the last two quarters by the per sale of Magalu, the Magalu partner, which is the platform that we launched at the beginning of the pandemic in order to help small -- to help small analog sellers who are analog and we have been doing quite a lot of work in this regard. And for the next few years we believe that the major driver for growth in the company will be in the 3P. and we are improving our systems and services and platform consistently over time.

I would like to highlight our Superapp, 75% of the sales were via mobile, mainly by our Superapp. Mainly in Magalu 30 million MAUs, this is a very expressive figure. And in the context of Superapp, besides 1P, 3P, new categories, we are going to talk about categories afterwards in the market, but the consumer looks at our Superapp as a one-stop shop and we created a digital account within the Superapp and in less than three months, we reached 2 million customers who opened accounts showing our success.

And our big difference here in the Magalu Pay, is that we do not have another app. It is embedded into the retail app, so it takes advantage of the audience and along the lines of the Chinese payment apps that grew based on app such as Alibaba for instance. So they grew within the app, but the beginning was always natives, that is to say the payment

app embedded in the retail app. So now we have operating 2 million and this creates a virtuous cycle. The client get into the Superapp in order to integrate with the app, no friction. And we made the right decision in terms of growth, but tomorrow we might have another app for Magalu Pay, but until we gain this kind of traction, we will keep it this way. So we see a very good evolution in the apps and the highlight being the Magalu Pay.

I would like to highlight, in terms of new categories. We had fantastic performance on the part of the Zattini, Netshoes and Epoca Cosméticos. So, these were the performances that the company -- of the companies that we acquired in the past and organically, we launched the market line, the mercado line or the grocery line, which we call mercado. So that people don't have to go physically to a supermarket, we have over 5 million items sold in this quarter. And this is the largest category in terms of items. So then it is being driven by the grocery model. Hundreds and millions (technical difficulty) 1,100 stores, most of them have their inventories. So we know logistics, we know e-commerce. So we are driving this to this model, this is 1P for the time being. And it started organically, it grew very fast and we are very pleased with the market performance of this category. And I'm sure that it will further develop in the future and it contributes more than GMV. This is a huge strategic challenge and this is one of the categories that will contribute a lot.

So, now couple of words on our logistics. Logbee, is a start-up company that we acquired two years ago. When we acquired Logbee, it was 100% of deliveries in Sao Paulo, two years later 50% of Magalu's orders, all over the country, exponential growth. And it shows how we managed to have a start-up company with a very cool technology and they could bloom in our ecosystem. So that's extremely positive and it helped a lot our customers to increase the share in up or within 24 hours.

In September, 44% of orders placed by Magalu was delivered in one day. So the fastest delivery in Brazil, excellent level of service. I'll tell you more about it later on. So, we're truly very happy with this growth and obviously this number is still for 1P. We have a huge challenge to have fast delivery for 3P as well and later on I will tell you more about acquisitions and the focus for the future, but truly in 1P, it's very hard to beat our level of service and the multichannel operation that we have.

What about 3P, we had some progress in the quarter, nearly 30% of everything we sell on our platform is collected by ourselves and it goes through the so-called Magalu run network and this number is expected to grow. We have about 1,200 sellers in cross-docking and 240 stores enabled with marketplace products for click and collect. So we are going to change that logistics differential in 1P now with a multichannel approach. We want to replicate it in 3P. So that's the big challenge everywhere in the company in future quarters. There was evolution in the second and third quarter, significant progress vis-a-vis last year, but we are only just beginning. We have a huge potential and we had two acquisitions and we are going to work on others and also investment in IT, in order to allow our partners to have the same benefits that Magalu enjoys with its operation in terms of fast delivery and low delivery price.

So the focus of the company for the future will hugely be on using our logistics and enabling it to 3P. There was a progress and the opportunity is still huge. So these numbers were not even higher in Q3 because 1P growth was so significant that part of the capacity

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plan for 3P eventually was used in 1P this quarter. So naturally, we're going to have more predictability of demand in the future. Nobody expected e-commerce to be so fast in the curve with the pandemic and certainly we have more predictability and invest more accurately in the future in order to evolve with delivery times and delivery cost to our sellers.

Now, I really want to highlight, I was very clear last conference call and during some interviews in the sense that we had slightly lost our excellent service in the second quarter. By the way, I never expected to see this increase of 150% in e-commerce in the second quarter. The pandemic, well all Brazilian consumers had to rely fully on e-commerce to buy products, the products we sell. And for some time, we lost the RA1000 CU in the second quarter, but now we are back in the third quarter with a CU, the quality CU, despite the significant growth of e-commerce in Q3. I really celebrated it and now we are the only company of Reclame Aqui reporting together 1P and 3P. And therefore the only company that can have the level of service in Brazil, which is so outstanding at Magalu and we want to continue having in the RA1000. We're doing all we can not only to have faster delivery, but in time. So I do celebrate it and I think in Black Friday, we will be very well prepared. We did massive investments hiring, more than 3,000 people to work in these operations in call center, DCs. We also invested to increase the fleet, acquisitions with a goal to have high level of service in Q4. When it comes to billing, it's even higher than Q3. And therefore we have to ensure we have a great Black Friday operation with good level of services to our consumers.

Now, I would just like to wrap up this cycle on the results of the third quarter by saying that the result celebrates a multichannel model. We made a big digital transformation very successfully at Magalu and the next step is to share it all with the market. Having a digital ecosystem that enables small and mid-sized retailer to go digital as well, generating digital inclusion in Brazil. I cannot consider social inclusion with our digital inclusion, so we acquired a number of companies that were recently acquired in the third quarter. I said before that we could acquire different kinds of companies, so these companies that have three important pillars in our strategy.

One of them is valuation. It has to make sense from the financial viewpoint. The company assesses very well the companies and the potential to be added to our ecosystem, but very stringent financial discipline. The second pillar, we do technical due diligence assessing the whole team -- the technical skills and also the quality of the IT architecture. If our team does an approve, we don't do it either. And thirdly, people should share our values, people who trust the same values, people who like people thinking out of the box, simplicity, customer at the top. So, we have the privilege to find amazing business people in all these companies we acquired and many of them spent most of their time, now being part of the Magalu team and they are here with us, joining us to go digital in Brazilian retail.

So I'm just going to briefly touch upon each one of them, before I turn it over to Roberto. So, I just want to highlight, like I said before, our strength in expanding logistics to our sellers. We have two acquisitions with this go in mind. GFL is a logistics operator that used to work nearly all our collection processes, the 30% seller collection, amazing job, a very new company increased a lot the level of service. And increasing by 50% of Logbee

capacity compared to what we had. So that's a company that will greatly support us to grow even more going forward in the South and Southeast, but also growing now in the Northeast. So we truly believe this team is going to power our capacity to increase our network and help with sellers and SincLog is an IT platform that used to be used by GFL and it has another 30 logistics operators that make use of its platform and it certainly helps logistics operator to work very efficiently, in terms of taxes, basic things and routing and even tracking. So it's this amazing team that is joining our efforts in logistics. So, I'm very excited with these companies and I'm very confident they will bear fruit in Q4 already and more significantly next year.

I would like to talk about two acquisitions in Magalu as a service, Stoq may be one of the most interesting companies of POS in the market, 250 million transactions in 2019. The SaaS model, which makes it easier for small and mid-sized retailers to sell both in brick and mortar stores and online, integrated with apps, orders and it addresses, retailer options that will add to Magalu partner, a very good team, passionate by POS solutions. The idea in Magalu that Stoq turns out to be our POS solution in the future. Today, we work with third parties and we want to work with Stoq. We believe their system is very consistent with what we do in our platform and we also want to convince our sellers to use Stoq because it will be a more natural integration between Magalu partner and our system.

And ComSchool is a business school, focus on e-business, e-commerce and the focus is to sell courses. We only started selling online courses on our digital platforms and we intend to sell our own courses of ComSchool on our app, which is an interesting segment for Superapp education. But ComSchool, will also help our sellers to better manage their business and to prosper in Magalu platform and outside, for digital inclusion you need the connection gadget and knowledge and ComSchool is adding with knowledge. It's an amazing team that will add a lot -- thousands of people to go digital in Brazil. So that's a very important step at Magalu.

About the Superapp concept, we have one of the four largest food delivery apps in Brazil, AiQFome. Pretty much focus in the country side, not so well known in metropolitan systems, but 350 cities in Brazil about to get to 600 cities by year-end, BRL700 million in GMV and the big secret for us is three times monthly frequency. So AiQFome was acquired in this context of being an integrated to our Superapp and improve our monthly frequency of purchase. I believe this frequency can increase a lot and therefore, help our general frequency at Magalu. So that's another amazing team from Maringa city will join Magalu and I'm confident we'll grow a lot in the number of cities with aggressive expansion very positively, it's financially balanced company. I know, this is a red ocean in the market, but in this case we are managing to follow their model, which is also franchise allowing to grow in a very sustainable manner. And other highlight for us, how they ever do it by operations that are not sustainable or cannot generate results for the future. We do like diligent entrepreneurs and AiQFome is part of that universe.

And finally, all the acquisitions at temnomagalu [ph] extensive her to all started this year in a super important category, which is books, NetShoes is also growing. Balance results or high balance results, we could have a break-even point in the operation very fast in less than one year, showing that we managed to have positive integrations. And Epoca

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Cosmeticos, three-fold [ph] digit growth, a very core performance positioning very well in Epoca's channel and also in Magalu. I'm very happy with the results delivered by these companies. They are growing a lot for this year.

The year of temnomagalu [ph] helping us to be more well known and relevant, not only in durables, but other categories as well. We have several different moves in these new categories, but I consider to have a very important progress. So now, basically this is the ecosystem. I always say, it's a puzzle and we are choosing different pieces that can match. At first it sounds or looks complicated, but every piece plays a role, has a function in our ecosystem. So managing to have a very solid model, one plus one is more than two in our arithmetics. These companies benefit from the ecosystem and the other way around. There is a synergy that is so cool and I believe we will reap a lot of fruit from the past. A lot will come in the future. But it's also important to start seeding right now.

Now what about other figures. So we are coming back with our stores. We opened another in the Federal District, 65 Marisa kiosks in Q3, 116 for Magalu and we want to accelerate next year, because our multichannel model is a winning recipe. We want to keep on growing in new markets, new states, new cities. We will keep on accelerating this context. I would also like to highlight that Magalu was just awarded as the best retail company to work at by GPW, a Great Place to Work. For 20 years we are among the top 10, second in Brazil. Despite the pandemic and shutdown of stores, we really have this amazing group, they love to work at the company, they share the same values at and despite the crisis, it has proven to be very resilient and anti-fragile. Sometimes consumers don't see it, but I think that's the big secret of our success. I'm very happy about it.

And we also have the greatest grade in GlassDoor, 4.5 in GlassDoor 2020 and that's a very strong number and anonymous evaluation from our workforce showing that a company people like to work at. People want to come to help Brazil to go digital via Magalu and this brand also had exponential growth. Many research institutes considered as perhaps the major brand of pandemic, a lot of sensitivity, a lot of innovations, Magalu partner, the button to talk about violence against women, don't dismiss your workplace. So it's truly a company that had 360 management and consumers today really value this. We are the most valuable retail company in Brazil for the first time in the story of BrandZ and we also had 1 million followers in TikTok [ph] in three months, the first retail brand. And total followers in social networks, more than 20 million. So we have a very strong brand equity. Our digital presence is very significant and also helping us to build our brand in this new century.

I would just like to close the first part by addressing a program that generated a lot of noise in social networks, which is our trainee program. I simply have to mention it. I mentioned this in our management letter, but we launched a trainee program this current quarter or last month. The focus of the trainee program is to fix and correct a problem we have. Today 54% of our employees at Magalu are of African descent, and only 16% of our leaders are of African descent. I consider this to be a problem we have.

Operator

(Technical Difficulty) We ask you to please standby. We are waiting for the sound to resume. Thank you. Could you please standby. Because we are waiting for the sound to resume. The interpreters are not getting any sound. (Foreign Language)

Roberto Bellissimo Rodrigues {BIO 17269312 <GO>}

We are back we apologize. good morning, everybody. Thank you very much for participating in our video conference and I will be talking about the financial highlights. Fred has already talked about the sales growth over BRL12 billion in total sales, a very strong cash generation. Adjusted net income BRL216 million. And I would like to mention that before taxes it grew 115% this year reinforcing our gross margin went down, associated to the (technical difficulty) diluted our SG&A at the lowest level in our whole history. The interpreters apologize because they are getting a very bad sound. So we are doing what we can. We diluted depreciation and we more than doubled our gross profit.

On the next slide our working capital from June to September, we improved our working capital in over BRL200 million. We had an inventory turnover around 60 to 70 days. In September, we reinforced the inventories preparing ourselves for the year-end sales, 70 to 75 days, inventory turnover and an average term of 80 days, very healthy for our app purchases. We maintained this coverage up. (Technical difficulty) taxes recover (technical difficulty) our short-term assets and liabilities were improved and we evolved in the quarter and adjusted net cash position of BRL5.9 billion. We generated BRL100 million in cash net, but starting from BRL900 million respectively, this quarter we paid BRL300 million in dividends, BRL200 million in share buyback. We invested over BRL100 million in the quarter and we made all these acquisitions. So in the quarter, we generated BRL100 million in net cash going from BRL900 million of operating cash.

On the next slide. We showed the history of the last 12 months. In the last 12 months, we had BRL2.7 billion, the highest cash generation in our history and we invested, we paid interest and we invested. We did the follow-on, and we bought back and paid dividend, BRL7.6 billion for the quarter. So this means that we are very sound. On the next slide, we show a consistent evolution in this regard. Over the last three, four years, we have been able to grow with profitability, with cash generation. Next slide please about Luizacred. This was a major highlight in the quarter as well. In the second quarter, we had decreased the basis because the stores were closed. And in the second quarter, the focus was collection mostly. In the third quarter, we made a transition from this focus of collection going toward sales. So this quarter we resumed growth and we are selling very consistently and with levels that are similar to last year and the sales of Luizacred had decreased in the second quarter ended, bounced back in the third quarter with the reopening of the market. The sale of new cards, we resumed growth in our sales as well. Not only on the evolution of the Luizacard base and this is very important for our retail, the medium and the long run.

On the next slide. We have another highlight, which is the result of Luizacred, receiving is a highlight. So we went to the next level in fact, and we are receiving today much more than we received that the beginning of this year and the emergency aid has been healthy. But besides that, we also improved quite extensively our collection process and the credit and collection centers playing a fundamental role and with that delinquency dropped, NPL

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over 90 days past due dropped one point practically and long-term non-performing loan is provision for and the short-term NPL is what generally requires more provisions and as we improved our short-term portfolio in terms of NPL and to the lowest level ever in our history. As you can see we needed less provisions this year and with that it was record in Luizacred, (technical difficulty) BRL152 for the 9 months, and we had more provisions in IFRS than BR GAAP. Last year BR GAAP had been much higher than IFRS, however, this has been reverted this year. Now, we resume growth. We are growing of sales. We're growing to our card base. Delinquent to you can see that has been improving with a very good level. So I would say that these were the highlights of Luizacred.

And now I would like to give the microphone back to Fred.

Frederico Trajano Inacio {BIO 17269235 <GO>}

I'll be opening for questions, but I would like to talk about the fourth quarter a little bit. Of course, we cannot give you guidance, but in the fourth quarter, we are very well prepared as I said before. In terms of result capacity in most of the contracts that we signed (technical difficulty), our implementation of the fourth quarter -- the fourth quarter. So we will have a very good service level some deceleration vis-a-vis the third quarter will happen, not because of our supply, we have very sound planning for product and for, and for the fourth quarter as I said before. But because the corona voucher went from BRL600 to BRL300. So because of that a degree of deceleration should happen in the fourth quarter, but we do not believe it will be significant.

It will continue to be strong, higher than the market and the physical stores performing very well in spite of the drop in the corona voucher aid (Technical difficulty)

Operator

We are receiving a very bad sound (Technical Difficulty)

Questions And Answers

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

It's a marginal cost so as companies in stage, we don't have. For instance, I'm not speaking out there, but Rio de Janeiro (inaudible) when I see companies and the truck route are lower than the marginal cost of delivery to the market. So we have to do that, soon we have to grow a lot in 3P in our business. If you think about expenses, we cannot only think about the net revenue, but GMV because 3P will definitely grow a lot. So have to check the index for the future. As for Q4, we expect to increase our expenses a little because bulk of the agreements were made in 4Q for. So we're going to have another 3,000 employees. We expect to have a growth with a very strong operational leverage. So I do believe in our multichannel model as we open more stores, we keep on diluting e-commerce costs in the area where we made deliveries without having to worry about store pickup or deliver with the same truck route.

Q - Unidentified Participant

What about new temporary benefits, rents and salaries. I couldn't hear, did you have any temporary benefit of salaries, not this quarter. Okay. What about recent acquisitions particularly advertising?

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

These acquisitions -- these eight recent acquisitions, the vast majority are start-up companies as if like, particularly IT company so they add very little fixed cost or variable cost to the organization. They have the potential to generate gain with a platform model. So logistics operators grow as our volume grows or they gain internal share and advertising is going to add revenue -- topline growth to our business with higher margins compared to the market. Higher margins, so I don't believe there will be an impact on expenses. And we continue in our acquisitions, Bob, to privilege, where I'm not saying that we are only going to do that, but we are keeping an eye on asset like business. So we are privileging in our strategies, companies that are oriented to the growth of our digital platform, not as we did in the past that was just about by brick and mortar retail.

Q - Unidentified Participant

Thank you. Congratulations again.

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

Thank you, Bob. Thank you for the question.

Operator

The next question is from Luiz Guanais with BTG Pactual.

Q - Luiz Guanais

Good afternoon, Fred and Roberto. I have two questions. You mentioned at the end about the path for growth in 2021. Could you tell us more about growth in new categories? You've been speaking off cosmetics, apparel, grocery stores, could you tell us more about it? And what about the growth in services expected for next year owing to the acquisitions that you did in recent months? As far acquisitions again what do you consider to add to your ecosystem in terms of acquisitions of services for future quarters? Thank you.

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

Luiz, next year undoubtedly, well, I'm not only speaking of 2021, I'm speaking of future years. I believe we are getting to a level of penetration of developed countries when it come to durables. We did a great job in Brazil in the penetration of durables. If you look at other categories penetration rate is lower. If you think about fashion, beauty, foods the penetration rates are very low in Brazil in this category. So the big opportunity for growth lies in the other categories. So our efforts in investments are basically related, but not exclusively we will keep on becoming leaders in our own category and cash call. We have to continue to investment in the main categories, but now the major focus is on these

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new categories. So I firmly believe that the sporting goods area of NetShoes and fashion, Zattini and Epoca will keep on growing a lot.

Recently we hired (inaudible) had been CEO of Arezuo [ph] to lead our fashion and beauty sector. She is an Executive Director, a heavyweight and she is adding a lot to the team. We already had Chris and Zatti [ph] she go into address both areas. Zatti was not NetShoes focus, but we have a big market and penetration rate of fashion in Brazil is still very low. So we have a good avenue for growth in e-commerce. Another line that is also in the structure. Our structure, organic for the moment is grocery stores. We started very well. Like I said, the May category, and we'll keep on investing very heavily. The model was very successful. It's a focus right now, so fashion, beauty, sporting goods. So these new categories like I said are going to have a very significant share of future growth, both in 1P and 3P going forward.

And Hubsales, we acquired -- well, it is an F2C business, but pretty much oriented to fashion. So today, it is in Franca in the footwear industry, but we are going to work in other hubs, so footwear or clothing manufacturers sell directly to end consumers. So in the strategy obviously [ph] team, this is very important. We see a very important opportunity to grow in 3P. And also POS for multi-brands, sometimes products to our platform, so I bet heavily on fashion, beauty and also grocery stores. What about books? It's also a very good category, but in terms of size it's not so representative as the rest Estante Virtual is digitizing a lot of old book stores. So the big market certainly are beauty, fashion and consumables and foods. So these are markets that will get even stronger going forward.

Now, it's important to say, they are not only drivers for -- drivers for GMV growth, we also have to check purchase frequency. Consumers in Brazil don't keep an eye on that, they only keep on GMV topline and when we are digital, frequency is very important. So to me, even though these categories don't bring such a high GMV, they are going to bring a lot of frequency and stickiness to our operation. So strategically, they are very important to the company.

Q - Luiz Guanais

Perfect Fred. Now just a follow up, when it comes to services. When it comes to frequency that you mentioned, services is also very important drivers in (inaudible) and logistics, so how do you see the evolution of the portfolio and also considering new GMA moves?

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

There are services and financial services. Financial services, the bulk in the short term when it comes to adding result to our Group, to our balance sheet this is Magalu Pagamentos, Magalu Payments, that's a business that we launched this year. We've moved already BRL4.5 billion in the first nine months of the year, so BRL2 billion in the last quarter, Magalu Payments in last year as a reminder this receivable -- this move was through a partner stone last year and this year we created our own sub-acquiring business Magalu Payments and we anticipate seller receivables with a very robust revenue and it will grow a lot. So penetration of Magalu Payments and the use of revenue advance, that's in the short term. And we also talked about Magalu Pay.

Tomorrow, there will be some revenue of services provided so at the end of the day it will generate advertising in the short term and I firmly believe that. When it comes to logistics, we will generate revenue do in fulfillment, even if it's only cross docking for the seller, but we are not keeping an eye on profitability. So logistics more than making money or charging or having profit. In addition to costs, we want to provide the same level of service that we have in 1P. It's not going to generate gross income in the bottom line in the short term, so the financial component is very important.

As for the future, undoubtedly we have a word on any big acquisition that's a segment that has opportunities to be explored, new category in grocery stores, for instance, or even fashion we acquired Zattini, but that was a smaller operation in NetShoes, focus on sports. So once again don't be surprised (Technical Difficulty), it also in traditional categories maybe we can do -- make acquisitions in order to continue with our leadership. So once again I repeat, don't be surprised with the company. It will be in this strategy of being the system of retail in Brazil and the five strategic pillar, but that's very broad.

Operator

Joseph Giordano from JP Morgan, you may proceed.

Q - Joseph Giordano {BIO 17751061 <GO>}

Good morning, everybody. Fred and Roberto, thank you very much for my question. I would like to go back to M&A. You mentioned vertical -- in consumer goods, you already have a very good presence. You already have a very good service on the platform for that as well as home product. So, I would like to know about the retail ecosystem. What is your view from now on the one that you are building? Would it make any sense to get into brick and mortar for food retail or maybe establish a partnership in this regard or would it be difficult for you to find a partner for the full country for the whole country? And regarding Magalu Pay and the rollout, how should we think about your strategy in the short and the medium run, because it does not seem to be very sustainable in the long run. So how do you see this as a factor for activation for this platform? Thank you.

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

Well, it's very difficult to talk about acquisitions. I really cannot give you any clues about it because it has to do with our strategy. So we have nothing against bricks and mortar or e-commerce. We operate all kinds of channels and there could be some strategic moves regarding the increase in the presence of some categories, digital or not. Omnichannel, for instance, it could be -- and all the options are open. It has to make sense for one specific asset. So I cannot really give you a general answer. But the possibility does exist and we, of course, we look at both. This is part of our array of options and we are very much up focused on 3P and the platform. You can see the recent acquisition, they have characteristic in common because they are digital platforms and they drive this part of our business. So most of the acquisitions will have this kind of connotation. We don't have anything specific to talk about, but they will be more or less along those same lines.

And the other question, Magalu Pay, 2 million accounts, 30 million people in MAU and the focus now is to increase our base and then we will be make your best endeavors to

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increase this base and the acquisition costs will be lower because the account is integrated into the app. So less friction and less investment to activate the account 2 million in one month is a very important number and we are going to add features to our wallet in order to differentiate our product and cash back is important and it is important in our accounts.

I don't know, what you see in the market. Sometimes you have players that are not be very smart in this regard. We're not very good planning on their part. But we have always been very rational and in terms of our growth and I think we need to have discipline always, but it is very strategic for us to have this kind of payment and we make investment in the short run that are more expensive, but you're going to reap the fruit, having millions and millions of people using the app in the future on a daily basis. So some benefit, we are going to derive from this investment.

Q - Joseph Giordano {BIO 17751061 <GO>}

Talking about competition, Fred, many people are capitalized in your industry in may be new entrants as well. How do you see the evolution of the competitive environment, mainly now. Do you think there will be more steroid in the economy, maybe in terms of 1P?

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

I think we have all the calls, the previous calls that are available in our website. This is my 20th quarter as a CEO and we always get this question. Well competition has more money, they made a follow on, competitors so and so, this and that, but this is what we get all quarters in all quarters, this segment is very competitive. So our D&A come from durable goods, retail and we have always had hundreds and hundreds of competitors and we even compete with people who are bigger than our, sometimes in one specific area. And if we do our job every single day, we do our homework and have a good strategy in place and having discipline in terms of our capital structure and treating very well, both our employees and our client, if we do all of that because we did though that when people were very aggressive, in e-commerce, we were able to gain 5.4 in e-commerce.

We are very competitive and when the expenses are as low as ours and the very high cash generation such as we have, it's very difficult for people to compete with us. If we compete against a company that is as efficient as we are, this is different. Of course if you have a very high service level as well, so what I mean is that I respect all our competitors, but our focus is not on competitors, our focus is on our end customers, and this is what we have on our radar screen all the time.

Q - Joseph Giordano {BIO 17751061 <GO>}

Thank you, Fred.

Operator

Irma Sgarz, Goldman Sachs.

Q - Irma Sgarz {BIO 15190838 <GO>}

Good morning. Thank you for the opportunity. I would like to go back to the grocery category, what are the major hurdles that you are seeing in this category because it's not very easy to execute. So what do you need in order to attract companies to sell by means of your platform and regarding the assortment as well. You already offer some fresh produce, what about the room that you have or the space that you have for produce, for fresh product in this category, the overall grocery gateway?

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

Irma, thank you for the question. I'm going to try to distribute the answer and my colleagues will be helping me answer (inaudible) for instance will be helping me. Okay.

When I talk about the difficulties, we have been able to sign the contracts with the main suppliers and we've created this in March and we are learning every single day and we have already reached a new level in this regard. And I believe that next year this category should be playing a much bigger role. I think one of the difficulties, one of the hurdles in the market as a whole is the delivery cost because the ticket is low so you have high delivery cost and as we have the product physically present in the stores, we can have the ship from store is an important difference that we offer, we can be more competitive in this context and of course we have to make significant adaptations in our infrastructure in the store.

Because we have the inventory in the mezzanine, for instance, and let's say the product is very heavy. And then you have a struck through point or issue or a point of attention, but it fits very well into the model. And also we are doing this in a balanced fashion. We do not have a huge investment in the category so far. It will be sustainable and strategic for the company. This is what I can tell you. And about the products that need to be refrigerated, fruit and vegetables. Well, so far we don't have an answer to give you. We are still studying the category. It should be important in the future, but with our current infrastructure some adaptations would be necessary. So this is the reason why we are focusing on products that are not vegetables and fruits. Gabriel Simoes from Itau BBA

Q - Gabriel Simoes

Sorry I was muted. Thank you for taking my question. You posed a significant growth in Magalu Pay this quarter. Since it's integrated to the main asset, you've also mentioned your plan for an open platform and now we have fixed educated consumers in digital payments and QR codes. So despite this moves, do you think we can also get closer to the Chinese super app models? What others structural changes you expect to see in the formats and if not, what is the decisive driver in China that is absent here in order to replicate the experience here? Thank you.

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

Superapp one of our bets, very much inspired by the Chinese model, no doubt about it. We don't have super apps with the same Chinese characteristics in the US. It was not a success everywhere, but we believe we can do it well in Brazil. It will be an experiment. We're not so sure yet that we'll make it. Within this context everything you bring to the

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app, which brings frequent use like I said before AiQFome with food delivery or new categories that will bring in and also the market expectation of a more frequent purchase, so to increase customer loyalty, but there is no doubt that payment is also very important. The penetration of Luizacred at brick and mortar stores is 50%. So we have been an operator for decades with consumer credit payments, so we have robust knowledge for consumer credit. We also have a team that has been doing that for a long time and trying to take this expertise to the digital world and it makes sense to have very robust penetration rates in the app for our own financial products in brick and mortar stores. If I have 50% Luizacred penetration in Luizacreds, why can't I have it for 30,000 monthly users in the app.

So we still have a long way to go in this context. There are many decisions. We don't have a silver bullet to answer, but I believe it is possible and as for fix, it levels the playing field and it makes it easier for new entrants to join the financial system on equal footing compared to those that have been established for a while. I'm not going to share strategies or details on our strategy, but I am confident, we have the right knowledge. We have (inaudible) to do the job, (inaudible). So, I'm confident that we will become a relevant player.

Q - Gabriel Simoes

Perfect, Fred. Thank you.

Operator

The next question is from Daniela Bretthauer with Eleven.

Q - Daniela Bretthauer {BIO 13380169 <GO>}

Good morning, everyone. Congratulations on the earnings results. Many of my questions were already answered, so perhaps, I would like to address two topics. Firstly, I would like to talk about the cash back policy. Is it reasonable to assume that, now that you're probably developing and growing and increasing your own financial service platform like Magalu Pay, does it make sense to continue having other partnerships or if everything will be inside your own Superapp? That's my first question. And the second question is for Roberto. I would like to know more about Luizacreds because the results were really surprising?

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

Thank you for the question, Dani. Eduardo, can you help me answer this question about cash back and partners?

A - Eduardo Galanternick {BIO 20410320 <GO>}

Dani, thank you for your question. With regards to cash back, undoubtedly, we have this in our platform. (Inaudible) and other partners that we have, we see them as acquisition sources. We try to bring new customers through our channels and every order is placed and closed in our platform. We don't list our catalogs in any other platform to close orders -- to take orders. So we take these opportunities as media sources, equivalent to other

media and always take into account investment profitability and acquisition cost. So that's how we see it the cash back strategy YoD [ph] retention will always take place in our platform. That's very clear very clear. So it's more about the ROIC of the investment that you take into account as a long-term strategy, that's it.

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

Okay. Thank you Edu. Now back to back to Roberto.

Q - Daniela Bretthauer {BIO 13380169 <GO>}

Luizacreds result was really positively surprising, but what really amazed me was the revenue went down about 36%, but expenses went down much more about 78%. So it really boosted the result of Luizacred. So my question is, okay, I understand what you said about the harvest, the season of provisioning old timers versus new ones, but what about Q4 and going forward, do you think the result will be more similar to the level of Q3 because there is a structural change in profitability, if Q3 is the new reality for Luizacreds. It really multiply the income by five, though it's challenging to see how to work on projections for Luizacred in the future.

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

Roberto, I think you are muted.

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

Good afternoon, Dani, thank you for your question. So let me explain it better. The current quarter is a quarter of change of level. It won't necessarily be the same in future quarters, but to give you a backdrop, the financial revenue was lower because it was a time in which we didn't work so much on loans, funding. We were more conservative in terms of credit and customers have more cash and we're not so much on revolving credit, not so delinquent. So the revenue or deferred revenue went down, interest revenues were lower precisely owing to the quality of the portfolio that was greatly improved.

Now, when you say that expenses went down dramatically, it did happen and in net expenses, there is another right that is continued -- is going to continue to increase in our card base and also the growth in sales, et cetera. So the trend for the future is gradually to grow in that days sales, leading to fee income and necessarily will generate also more refinancing, financing loans and bringing in more revenue of financial transactions. So these were cycles and the trend is to start growing again in those lines and the level of provision will not necessarily be equivalent to this quarter because we had a change in the level this quarter. We greatly improved. So the expected losses that were made last year was changed owing to the new reality.

And now, we should go back to work on provisions, owing to this growth, growth brings provisions and we have an increase provision for customers who pay on time, limits. But we believe the level of provisions will be lower compared to last year, so it's a new normal, a new circumstance, a new level of profitability. Having said that we expect to start growing again. We are very bullish, very confident with Luizacreds results and also its contribution to retail and increasingly more to e-commerce.

Q - Daniela Bretthauer {BIO 13380169 <GO>}

Thank you. It was crystal clear.

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

Cool Dani, thank you.

Operator

Our next question will be in English, Morgan Stanley.

Q - Andrew Ruben {BIO 18834624 <GO>}

Hi, Andrew from Morgan Stanley. Thanks for the question. Two items here, first on physical stores. Can you talk about how you're thinking about the growth pipeline for 2021? And then second on the marketplace, what kind of view do you have in terms of the marketplace supply? What kind of visibility do you have for seller inventories heading into the fourth quarter?

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

Thank you for the question. I was asked to enter -- the first part of your question will be answered by Fabricio and then I will come back and I will talk or I will answer your other question.

A - Fabricio Bittar Garcia {BIO 17269261 <GO>}

About the pipeline for the opening of stores. Thank you very much for your question. We should be opening a few additional stores still within this year, ending with about 45 stores opened and the 100 and some kiosks at Marisa. Next year we should keep the same pace and we should be going to the Federal District to the Marisa kiosks that should be around 250 overall.

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

Well, adding to what Fabricio said, entering your question about marketplace. Yes, I do believe that the market is under-supplied and the small and medium players suffer more than the big players because of supply and we add new sellers and new SKUs, new items in order to offset this thereby improving the overall process. I do not see anything affecting 3P materially for the fourth one and same seller sales. I don't think there will be some additional effect and maybe you will have some stock out in some small ones, but as we are adding more sellers, there should be no material impact. And I have already mentioned the deceleration from the third quarter to the fourth quarter, I have already explained the reason because of the aid from BRL600 to BRL300.

Operator

Gabriel Desero [ph] from Santander.

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Q - Unidentified Participant

Good morning, everybody. I have a few doubts. You have already talked about competition, but do you see any different competition because some players and including your company, you are bringing forward the Black Friday sales and they should bring about some lower inventories so, do you believe in any stock out because of that of the early Black Friday sales?

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

Well, we have already planned for the full year to have an extended Black Friday in order to avoid a very big concentration on Black Friday, although I believe there will be a very good sales during the full month and also on Black Friday. So the market already expected that. So what we are trying to do is deconcentrate the purchases on Black Friday, the shopping on Black Friday and I see a very positive evolution of demand for the Black Friday products. The strategy is less aggressive than everybody is thinking

You need to make promotions but not at irrational prices. Black Friday's regulate that mind you. We have the consumer protection agency that keep their eyes turned to Black Friday all the time. The fourth quarter, will have less money from the corona voucher from the aid from the government as we have already said. But we are having very good growth. We have very good inventories and we have -- we do not like to work with a high coverage because the turnover of our inventory is very quick. And we receive all the time the products that we need and we have a very fast Inventory turnover. So we are very well supplied and we made a very good planning with our suppliers only. A few lines have some kind of stock out because most of the lines are very well prepared to have everything ready for the fourth quarter and also to start the first quarter of 2021. We have an excellent relationship with our suppliers and if the product is -- there is a shortage of the product in the market, then this is a situation that everybody would face. Thank you for the question.

Operator

Next question, Victor Saragiotto with Credit Suisse.

Q - Victor Saragiotto {BIO 19504427 <GO>}

Good morning, everyone. Thank you and congratulations. I would like to understand the 1P and 3P dynamics Fred. Over the last quarters, we saw 3P growth close to 1P growth, so if we consider other players in the market, some competitors didn't have investment in 3P and now everything is doing the opposite. They're getting to 1P, those who are no players are getting to 1P, players who were in 1P are getting to 3P, so maybe that has surprised many people, so what happened? What were the pains with marketplace over Q3? I understand, it's very hard to predict anything for market growth next year, but what should we consider channel wise? Should we consider that 1P will remain strong?

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

Thank you for your question, Victor. I mentioned that a couple of times. First of all, Magalu is a company with a very strong balance in results. So we don't compromise e-commerce

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for brick and mortars or the other way around, 1P or 3P. So the three channels are doing very well, outstanding performance in Q3. 3P did great, 1P as well. So 1P was outstandingly great. I'm not saying 3P was not good. We grew 145% in 3P, a lot more than the major marketplaces in the market from 11,000 to 40,000 sellers, the operation is getting better and better. The pain of running 3P, I have pains, just as I have pains in brick and mortars and pains when we run 1P. So nothing outstanding. Now the thing is that, this year with the pandemic, the market heavily (Technical difficulty)

Operator

Ladies and gentlemen. Please remain connected (Technical Difficulty).

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

So there was a shared gain that was not proportional in my opinion compared to 1P. So going forward, I believe 3P will keep on growing. That's the big growth lever. But do we have a goal for 1P, 3P, brick and mortar we are channel agnostic, we want to grow them all, but considering the market trend and opportunities growth in the future will be stronger in 3P compared 1P and compared to brick and mortars. In the sense of gain in scalability, gain in scale, we cannot get one quarter and projected for the future. It's not as simple as that.

Operator

This concludes the Q&A session. I would like to give the floor back to Mr. Frederico Trajano for the closing remarks. Over to you Mr. Trajano.

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

Once again, I would like to thank you all for joining us on our conference call. These are very long calls, a lot of information. We are very confident about our company and for the coming quarters. And if you've been through all, we've been through such a complex and challenging situation and you get out stronger will increased our confidence, but we are still very humble, we still -- there is a lot of things to improve. But I'm very confident about the team, I thank everybody for their efforts. The executives, directors, employers at Magalu for such an amazing result, despite all the challenges. So thank you very much indeed. Enjoy the rest of the week.

Operator

This concludes Magalu's Earning Conference Call. Thank you all for joining us. Enjoy the day.

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