

Q1 2020 Earnings Call

Company Participants

- Eduardo Benjamin Galaternick, E-commerce Executive Director
- Frederico Trajano Inacio Rodrigues, Chief Executive Officer
- Marcelo Jose Ferreira e Silva, Vice Chairman of the Board
- Roberto Bellissimo Rodrigues, Chief Financial Officer, Investor Relations Officer, Member of the Executive Board
- Unidentified Speaker

Other Participants

- Analyst
- Daniela Bretthauer
- Luiz Felipe Guanaes
- Richard Cathcart
- Robert Ford
- Thiago Macruz

Presentation

Operator

Good morning, ladies and gentlemen, and thank you for waiting. Welcome to Magazine Luiza's First Quarter of 2020 Earnings Conference Call. 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 presentation. At the end, we will hold a question-and-answer session, when further instructions will be given.

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

Frederico Trajano Inacio Rodrigues {BIO 17269235 <GO>}

Good morning. Thank you very much for participating. In this call, it's a very non-typical situation in this call because we arrived in the middle of a pandemic internationally and in a very sensitive situation in Brazil.

So we are holding our call 1 month after our original disclosure of our results. But it took us some time to give you a better preparation with more information -- more concrete information and a clear -- a more clear view of our situation. So as you can see, we have a different format for this call. In fact, it is a webcast, not a conference call. There is some --

there are some advantages because the audiovisual resources are better, and we are going to show you big news. And as usual it is another differentiated manner because we are holding this remotely. So all our executives are present, each one in their own homes or at their own home offices, and they are available. Should we have the necessary time, they are all available to answer any questions that you might have. So once again, we would like to thank you all very much for participating and for your interest in our company.

Well, the first thing that I would like to mention and I'm going to the presentation already, Magalu is a company that since the beginning of March, we already started to take these things very seriously. Up to February, our view of the pandemic was limited to the supply of our chain up to the -- up to February. But after March, after the carnival, we understood that this was going to be a serious situation here in Brazil, such as was already the case in Europe. So we had to tackle the situation very seriously.

We canceled a meeting for 3,000 people that we were going to hold in Campinas. Everything already paid for and we had to cancel it. And we were very much worried about the situation already. So we started to organize home office right at the beginning of the second part of March. So we took the decision of closing the stores and the company took it very seriously trying to adapt as quickly as possible to this new reality.

So we set a new management model, digital crisis management. We created 12 committees for strategic fronts because we said, "Well, if we do have a lockdown and social isolation should this come here and should be -- should this be extended, what should we do?" And I have a video that I usually show and I say, "Well, if you sail, this has nothing to do with the wind. It has to do with the person who is in the boat. And you can even go against the wind if you adjust your sails. So you have to take the whole crew and you have to have a very good reading of the situation. You're right in the middle of the storm and you have to adjust the sails. So this is what we did. We took our crews, so to say. And the crew that I have on my boat is outstanding, exceptional people who share our culture. They are totally committed to the business to the company. And they are very talented and they have the, I would say a very special kind of knowledge to deal with this specific storm so to say. So the digital part is very important for this type of crossing.

So these committees have their objectives. They have targets, and they are all strategic and they are transformational. And we've made very quickly the necessary adjustments and we crafted a very well defined accountability of the leaders and very fast decision-making process. And of course, we had first of all to preserve our cash and human lives.

I see that between the middle of March and the full month of April this reorganization of the company's management led us to create many actions that we put in place and they were very intense and decision making was -- well decision making that it would take us a much longer time we had to be very fast and that was a record in terms of delivery of platforms and the adjustment of our sales and a very intense one. And at the beginning of April, we made a -- we gave an interview to folio Newspaper and we said words at present to (inaudible) said that we did 50 weeks in 5.

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So what are we going to do strategically? So what kind of categories will be important for our consumers? We will not be able to have click and collect maybe and store pickup. And on the 20th, we already had a film with on global with free shipping and in global, at global when all the stores in Brazil were closed, only Magalu platform will have the closed stores to sell online. And the autonomous people who were at home also could sell online. Many deliveries, very significant and very short time for us to do this 50 weeks in 5 so.

So these 5 weeks were weeks of definitions of safety protocols and the implementation of our safety, strategies and a very big evolution and a very major adjustment in our sails because of this storm, winds coming from everywhere. And in May, I think I'm going to say so many things during this presentation. But by far the most relevant is this figure here. Up to May 20, we were growing 46%, including 1P, 3P, brick-and-mortar stores and 60% of the brick-and-mortar stores still closed, we are -- in spite of all that, we're growing 46% vis-a-vis last year.

So I think this figure alone shows very objectively and very clearly and puts in evidence the quality of the work done by our team, our crew during this storm and the sail that we adjusted in March and April coming from a many years of investment in digital and in the culture of our teams, a very strong team.

So we have a whole history. It's not only the last 5 weeks. So you cannot really make a difference overnight. So this has -- and what happens is that we are really collecting all the fruits of everything that we planted.

First of all it comes from our accounting. This is a figure that is not something abstract. This came from our accounting. And GMV is a very important figure, and we wanted to have KPMG verifying this figure. Second, we have not changed the number of last year. Last year was the one that we reported last year a very high basis for comparison. So what happens is that, we start already with a very high comparison base and this figure is higher than before the pandemic and we reported GMV growing 35% in the first quarter, and we're growing in May, and everything points to the fact that we are going to close May, we still have a few days but they are very good. And we will probably have higher growth rate than before the pandemic. So this shows how fast we are in terms of going against the wind. And I think what is very important is that, we -- this number is real as I said. This is concrete, and we are not making any trade-offs.

We are not releasing sellers that do not wish invoice, no. The degree of strictness on our part is the same. So we demand that they have a digital certification and we are helping them to have the certification so that they may issue their invoices online. So we do not waive anything in this moment of pandemic that will go from offline to online retail or government. We will be paying even more attention to tax evasion that happens in marketplaces.

So formal electronic retail is our responsibility. And the platform they cannot waive this responsibility. And as far as I'm concerned, the most important thing is that we are achieving growth respecting the health and the safety of our employees at the same

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time. We only accelerated after we put in place all the safety protocols after, we made all the investments to guarantee that our people in the DCs and our partners and the stores that were reopened after April 20, after we were certain that they were all working with total safety in our workplaces. They have more safety in our places than outside the workplaces.

So we didn't make any trade-offs. We didn't waive anything. And I'm going to publish an article this week saying that, "For me, the only way to consolidate economic development is by means of digital transformation and preserving the health of everybody." So I believe this figure is very inspiring for all the other companies. We are not making concessions. We are not having any trade-offs, we can consolidate these things that seem to be very antagonistic but by means of digital, we can do that.

And the countries that had a higher digital participation felt the crisis less than the others and we have very encouraging figures regarding our economic recovery here in Brazil as well. So you could say "Well, this only works for a very large company like Magazine Luiza." No, we are making this available for very small and medium sized partners as well. When you are in the middle of a crisis, you have to have principles that are more north. So you have the whole process of decision making and the principles have to be on north in our daily decisions.

First, health and safety. This is the basic principle: looking after the health of our people, our clients. And we are not talking about the protocol for IT, for governance in order to waive any legal responsibility. No, we're talking about a structure of health and safety in practice hands-on. And I'm going to say a few words about that as well.

Amazon had disruptions in their operations. And because their safety protocols in the U.S., were not as well adapted to, and they had some situations in their DCs that we are trying to avoid as much as possible. But when the crisis is very serious, this is very difficult because you have to guarantee that in the workplace people are safe. So we are always measuring whether people are safe in our DCs, in our stores and any other situation.

And the second is the preservation of cash of the companies. Because if you do not preserve your cash, you cannot preserve jobs. And when you preserve cash you preserve jobs. And I'm going to talk about that. We got into this crisis with a lot of cash. But this did not lead us to lower our guard. So we worked as if we had no cash whatsoever. Because we didn't want this surplus of cash to shift our attention. And so we work as if we didn't have any cash. So this is the way we worked in terms of renegotiations of contracting. And we raised these funds with investors last year in order to make investments, in order to grow the company and not to spend this in a crisis. Of course, this gives us a very high degree of comfort.

Well, the slide is slide number 5. We have cash for a long, long time and we could have 2 years of all our stores closed with the amount of cash that we have. But when the wind comes back in a favorable fashion, we want to have enough cash to place ourselves in a comfortable leadership position in all the markets that we operate. And the other point is, job maintenance, and we had a lot of help from the federal government.

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And together with the government, we made a fantastic job. And with this new NP allowed us to use some resources extensively with a lot of support to our teams and we are going to talk about that and the continuation of our operations and the radicalization of that which was part of our strategy. Our company is already digital, but now we want to make the Brazilian retail digital. We accelerated all that with the pandemic. So I'm going to say a few words about that.

I'm going to slide number 6 first. Talking about health and safety. We define safety protocols in the DCs mainly or first because the stores were closed. So 20,000 people on vacation, so we had time in order to work with our store safety protocol. So we started with our DC and the disinfection of our DCs and disinfection of all the workplaces and the use of masks and hand sanitizer and measuring the employees' temperatures outside. That is to say before, they -- their means of transportation to go to the DC.

So we started to do this monitoring and auditing, because sometimes, the person remove the mask and this. And so we are monitoring all that the same regarding the stores that were reopened on as of April 20 in some places, some locations where we can open stores and I'm going to talk about that. In some places, we believe that the decision on the part of the government of the city administration was not correct. But as far as our standards are concerned, we do not believe it is safe enough to open the stores. But we placed the infrastructure for all these issues of measuring temperatures and the safety infrastructure and we are doing this more. And more in order to guarantee the safety of all our teams

With a lot of support to our people, home office. And we prepaid the meal ticket. We prepaid the 13th salary, and we lowered the target for sales. We created a channel of telemedicine so that our employees didn't have to go to a hospital or a clinic unnecessarily. So we placed this for free, free of charge for our people, over 2,000 consultations in the last month. And in some cases that we tracked they were contaminated by COVID going to a hospital et cetera. And of course, if necessary, you have to go to hospital, I'm not saying that telemedicine totally avoids this or replaces this.

Okay. So then ever since the beginning, our whole analytics team produced information about risk scores since the beginning of April per municipality so that we could know where we could open the stores and where we shouldn't open the stores. So we created a risk score per thousand inhabitants, the degree of infection or the rate of infection per million inhabitants and ICU, occupation, the situation of our partners for the health plans that look after our population.

So a lot of information from our team, our analytics team, so that we could know whether it would be safe to open a store or not in that specific location. And Rio Grande do Sul, they are doing an excellent job in this regard. And we already have some stores that have already been reopened, but we opened or we used this risk score. And I'm going to show you a logistics video tape in order to show you the situation of our standards regarding safety in the DCs

(Audio-Video Presentation)

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About the reopening of stores, we have 40% of the stores already opened today. On May 26, 420 stores were opened. And we are going moderately optimistic about the reopening of stores. Because of the natural geographical hedge that we have, our characteristic in our whole history has been regarding the locations where we open physical stores. And most of our stores are in small cities. When you look at the COVID map and I'm on slide number 8 now. You can see that most of the death and most of the cases of COVID, and they are located in the bigger cities. Over 400,000 inhabitants, almost 50% of the cases.

And we have a distribution of our stores, 70% of our stores are in cities that have less than 400,000 inhabitants and 90% of these stores are in -- we only have a handful of stores in shopping centers. Most of them are street or standalone stores. And this is a characteristic of our stores. And because of that, we have a degree of optimism because we believe that a major part of these stores will be reopened in June, and maybe all of them reopened in the next quarter in Rio Grande do Sul, as I said. So Paulo is along the same lines, and the government will liberate first the smaller cities. And the stores, besides being very important for us in terms of revenue, they are profitable. They are very interesting from the viewpoint of profit generation and I will talk about that.

Now slide number 9. Preservation of cash and jobs. We got into the crisis with a comfortable cash situation. But we had to take an attitude, as if we didn't have any cash whatsoever in order to be even more austere, more frugal. And so we issued debentures at a fantastic rate, 1.5%, CDI plus 1.5%. This is one of the best in the market. And we discounted a lot of receivables as well in order to reinforce our cash.

We might even go to the market again and do some other operations, although we are optimistic. Sometimes what happens in other places in the world is that you reopen and then all of a sudden you have an increase in the cases and then you close again. So I believe that this is a very delicate and very sensitive situation. We have to pay a lot of attention to that.

From the viewpoint of the control of the pandemic in Brazil, I'm not very optimistic. And we renegotiated and we postponed many contracts with our suppliers in direct and indirect materials. And we renegotiated some payments with our partners. And they have been recognizing this and they will certainly recognize this because they can see that we were very strict. And we were very supportive in this regard and we privileged the smaller players and the small carriers and smaller transportation companies. And we made loans to them. And even for small sellers, we gave them 3.99, which is practically a subsidized rate.

And we do not want to have profit from prejudice. When we use the provisional measure 936 for most of the team, many people were covered by this 936 provisional measure, and we made very detailed studies about that. And we're benefiting from this measure and our employees as well, so this helps us reduce this. If you didn't have this provision to measure, it would be very difficult to hold on to the job. So it was fundamental why.

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I would like to congratulate the government for this measure that was very well implemented and I'm renegotiating contract and we are reducing the opening hours and the working hours and the CEO 80%; VPs, 80% reduction in salaries, 50%; members of the board, and because we have to give the example. So first, we reduced our own salaries. And we believe that everybody in the company contributed. We had a reduction in the working hours for instance of 10%. And I thank everybody for their cooperation and for understanding the difficulty of this moment, and thinking about the collective aspect and not the individual aspect. So you can see that everybody was very involved.

We have some real estate that we lease to stores and we reduced the rent, of course to help the stores. And also our social engagement, we made donations. And later, I will talk about that the controlling family Magazine Luiza is making some important contributions to sellers, mainly for the small suppliers and employees, many benefits for society, in general. The controlling family really took this from their own pocket and this is proof of the serious governance that the company has. And regarding every -- and now we're talking about digital and this is the main topic. And we digitalized Magalu.

And for some time already, we started the cycle 2 years ago, and you can see that at least for 2 years, we have been doing this and now we radicalized, we accelerated many of the projects of our strategy, exponential growth. And I would like to highlight the revenue from the physical stores, we have to have a platform to make the whole retail digital, the countries that digitalized a lot they had platform that contributed to digital inclusion I'm on page 13 and then I'm going back.

So we have a very fast exponential growth, new categories, we radicalized new categories because some categories were not scheduled for this year market and the Superapp which delivers everything to the end customer with faster delivery and Magalu as a Service MaaS. That was done for 1P alone. And we're doing for 3P as well, payments and deliveries and other services like the issue of invoices and back office. And we are delivering a whole package of our technology and making it available to our sellers, because we want to be the best solution for them. Not only the ones that already sell online.

Let's go back to slide number 12.

One of the characteristics that happens in countries that have been through the pandemic, the most emblematic case is China. Here you can see that in these countries, there is a change, a change of in the profile, purchase behavior and also the channel that drives the purchase. Think about China today. You can see in China, there are some industries that after pandemic are going very strongly. One in offline, the orange dots. Foods for instance was very resilient in the crisis and remain stronger.

And the same goes for beverage and what they refer to home care -- not home care, but hygiene and cleaning home products. So they're all at a very strong level both in one and offline, so we have different access here. And the same goes for communication processes and products, like smartphone and tablets, they are just as important as foods,

slightly behind foods, together with beverages. But these communication products we can see a strong boom.

People who are at home, they need to connect. And these elements we can see this boom with a very important driver, not only in e-commerce, but also in the stores that are open with a positive performance, like beauty products, and electronics, and home appliances, not only smartphones but home appliances, they are being recovered in China, the black dot, particularly online. So the driver of this growth is particularly online.

So the thing is by and large, what I want to say on this slide is that electronics categories and consumer goods and foods are doing fine. They are resilient. It's only natural to reinforce them and by and large these categories are growing very well and powered by digitization. That's what I wanted to say just to give you some context and then we can talk more about it in the Q&A.

Now speaking of category on page 14. Now from the very beginning, we realized there would be a lot of demand for consumer goods online. We accelerated exponentially all our deliveries to the market. It was not a focus category for the company for this year, but we decided to do it. So we were very much focused on sporting goods, fashion and beauty products. And then we accelerated a lot with staple goods, staple foods, beverages, including hygiene, products, diapers. We are one of the best sellers online on washing powder and diapers in Brazil and also the largest number of purchases in this category, generating all purchases per month. And this category is key to Magalu when it comes to DAU. We talk a lot about MAU in app. But the focus of any super app is DAU, the daily user. We don't publish this number, but it's growing a lot.

The daily number of customers in our app and certainly in the market was only in the first steps of the journey. There is still a lot of room to grow and this is helping a lot. This is not a category that is profitable yet. We are working a lot in order to have a break-even point, but it's very strategic to us. When it comes to frequency of use, frequency of -- well, the increase of MAU, DAU and one of the main KPIs early in the year, and it's going to be a point of no return, not only the pandemic. We'll be investing very heavily in these categories.

And I firmly believe that in some cases, if you think about for instance (Panda, San Carlos,) maybe even Carrefour, they have a good online experience and happy working in 17 of the 5,500 cities in Brazil. But when you go to the countryside, smaller towns in Brazil, the delivery time when you buy a product online it takes sometimes 2 weeks to have at home with a queue rate of 70%. It's a very poor experience. And we want to use our digital mobility to get into these categories in 1P, buying products and having them in our stores, which is direct store and ship from store.

We want to have products in 600 stores in the market, in the stores' warehouses in order to have the dark store model same day using our own room, our stores. And also via 3P through Parceiro Magalu. Not yet, but we want to go digital with small retailers, particularly for foods now and also support the payments and logistics in the future. So these are the plans. And this category has come to stay. It's the beginning of a long journey, a long

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marathon. And we'll be very much engaged using most of our cash power, funds, the digital ability of our business team and labs to make it all happen.

We have important partnerships top-to-top with most of these companies Ambev, Coca Cola via distributors. We also have Heineken, P&G, Unilever, I'm speaking a lot, NIVEA, L'Oreal, Kimberly, Johnson, Diageo. So we have great partnerships with the key brands, very selective at 1P with a higher ticket. We believe this is right along the chain but with significant programs and commitments of partnership -- a long-term partnership, very open, trying to add value, provide good service and naturally also make it in a very sustainable manner.

When it comes to the rest of the assortment, Netshoes is doing great, surprisingly good. Because in other places in the world, the fashion line and sport goods were affected. However, Marcio and his team job is amazing during the crisis. After April, with reorganization of in house, May is being great, contributing a lot in our growth as well with good margins. And we managed to close very significant deal with Adidas. There's type of deals, I mean, partnerships that we can sell now via market would be premium products of these brands, Adidas, Mizuno, ASICS, which is also a former effort by Marcio. So brands that are adding to our portfolio at Netshoes. Zattini is also doing very well.

They also have a winter collection. So the fashion category in Brazil as a whole is suffering. That's true. But people keep on having to buy things. And when they buy, they buy online. Because Zattini is important online, it's growing a lot. We have several partnerships with Pernambucanas, Marina -- Marisa, Besni, VR, Hering, Anacapri several brands that are part of Zattini's portfolio and also those that allow to be in Magalu's mini worlds.

Whenever our partner allows, we have negotiations then they improve our apps. They have their own apps, but when brands allow would have the same catalog in Magalu's world. And Epoca is doing great as well with cosmetic growing 150%. Several significant brands, the greatest portfolio on the web now, very global and surprisingly well. So the growth is really amazing. Men and women are still taking care of their beauty, even though they are at home. So they're buying online today.

Now, I'm going to show you a video. We have a very strong campaign and we benefited from our cash to invest in marketing, investing in brands and to make these new categories better. So how are you going to be known as a company that sold only home appliances for 60 years? That's why we are trying to build these new categories. And we have a video now about Magalu with a very good song and jingle, I just want to share with you. So the campaign -- the digital campaign is huge in addition to the video, but I think it can make everything very tangible in our position.

(Audio-Video Presentation)

Good. So just a short video. This is a webcast, right? So obviously all these worlds are part of our SuperApp. So we keep on insisting on our SuperApp. 70% of Magalu sales come from mobile GMV is mobile from Magalu MAU increased 111% vis-a-vis last year, BRL21 million. Like I said, we're increasing a lot of DAU, BRL26 million of install base. And this

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number also is in Net and Zattini's apps, but the bulk is Magalu. We are investing in growth. So the most significant number is GMV. It is not DAU nor MAU. We have to sell. If I want to spend my cash to have 50 million MAU I can do it. However, we always do the maths in terms of audience, installations, facilities bonds.

So I just show you this figure, just to give you some fundamentals of our path. But what really matters is 45% to 100% growth and not necessarily MAU. So that's just a number that shouldn't be more projected than it is. As for faster delivery time, the crisis make us work up. To some extent, I believe we are accommodated with store pickup. 40% of our customers would have store pickup. And with the crisis, the stores were shut down. We would even have authorization to open some modalities for store pickup. But we thought in order to contribute to social isolation, I would even have this available store pick-up negotiate with a mayor, I could do it at a store entrance right through, but we wanted to deliver have home delivery, so we benefit from the crisis and we modeled our strategy. And now we benefited from the crisis to accelerate ship-from-store, so we can have the delivery the next day and possibly the same day. It's our dream. We'll get there somehow.

So we shifted our focus, particularly considering Net's products, our products, 40-plus in order to have it home delivered. And store pickup is still a more inexpensive option for Magalu but ship from store is less expensive than the DC. When we shut the stores, we lost this option that was very cheap for us. The truck would take the product to the store. So we decided -- and by the way, we started to ship the product from the DC to the customer's home paying a higher rate for 150% of online sales. It was growing a lot. Logistics account was very high.

So we said, "Let's shift everything to ship from store and let's enable the stores to open as DCs not only for store pickup but also ship from store." So we use Logbee. We created a plan, an exponential growth plan for Logbee in 2018 when we acquired was one store in one city. And now we are operating more than 600 stores or 90% of our cities.

And today, we are having a significant share, close to 20% of ship-from-store trying to get even higher. It's a long way to go to reach 40% doing well. We are going to have both in the future store pick-up, ship-from-store. But the bulk of our logistics chain will be hyperlocal.

We want 1P goods and 3P goods in the future but let's focus on 1P only first. We wanted to get close to customers. Our whole intelligence area, supply area, we want to avoid the good to travel too much because the less the travel, the lower the cost. We need the right product, the right store. So when you buy, I deliver close to your home, maybe the same day or next day. Today that's our focus.

Logbee in more than 600 stores a whole system to make it happen. So the whole system process. Well, the store is running as a DC. The stock clerk is like a checking inspector. He beeps the products, sends to the inventory. They do the counting all the time, inventory management. The customer buys. It is delivered. So the whole tracking is there.

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A lot of labs delivery to make it happen. It's far more challenging in practice than it might appear. And the most challenging of all, which is our challenging, is to have the right product or the right supply for these branches that we're working very hard to have the product in store and in the right DCs that supply to these stores.

So we can raise the bar to an even higher number of ship from store. And store pickup was 40%. If we add them both in the future, we want to have more than 50% of our sales. So Logbee 60% of courier deliveries of 1P and Malha Luiza 90%. So we don't rely so much of market carriers. Carriers are having a high volume as e-commerce grows. Some are having a hard time. So it's very important to have your own network right now so you can have some assurance.

Unfortunately, I depend to some extent or luckily, we have our own network. However, unfortunately to the market some carriers are having an excess volume unable to deliver places like Rio for instance. They have a serious problem in the postal service delivery times owing to COVID-19. Many people have to be isolated. The post office guys are hero. I think they're doing fine considering the problems, but they have a guidance that also depends on the market context.

The evolution well was tough in Rio in Pernambuco at the coastal service and also Sao Paulo. So it's nice to have your own network, but naturally also depend on other third-party carriers, important partners of ours. By the way, I wish we could use a lot be -- more often to 3P, later on I'm going to show you that the current rate is 20%. Malha Luiza 20% of total 3Ps. There 1P increased so much that it beat some part of the additional capacity of Logbee and Malha Luiza. But we increased from 0.3% to nearly 20% in a short time frame. I would say for 2 years, we launched this modality already 20% of the total. We want to expand Logbee and Malha Luiza to grab a lot of share of 3P.

Now on page 21. The previous number was the number, the figures for 1P. So we want our own network to have a larger share in the total 3P. We are working to do that. Magalu Entregas is 80%, but sometimes it take products or the seller ship to third parties and not with our own network. Magalu Entregas from the total 3P that goes to our network is 20%. We want to increase. We don't increase more now just because we increased a lot in 1P. 1P is growing 200% in May, so it's eating the additional capacity that we're beating in Logbee and Malha Luiza.

Anyway, we have a firm commitment, we're going to accelerate investments to also provide to the seller our own network, which is very efficient and inexpensive. Anyway, if we need to count on third parties we'll do that.

And as for physical stores, brick-and-mortars, what is the performance? On Slide 22. We used to have more than 10,000 sellers, enabled with mobile sales, a system fully integrated with our inventories, integrated with the payroll, with everything. And we only enable to use mobile sales, and we have products and services being sold and is integrated in all social networks. And I have sellers with amazing numbers with remote selling.

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I'm not going to give you many details. Sometimes 600,000 per month by a seller. One in, another in Franca, selling more than 300 per month. And mobile sales gets to the store not to e-commerce. At Magalu, our rationale is that the sale is originated, so it is necessary in this modality to work with a closer margin to the store in e-commerce.

In addition, well, you're paying the seller cost, so if you pay with the e-commerce margin. Pay in the seller cost, your result will be lower. So we firmly believe that they will help us sell us more in the physical stores. We book in the physical store. So we are breaking it down.

So just highlighting again, all the sales to mobile sales remotely are in the physical store and not to the website. The project is doing fine, accelerating a lot. Nearly 2,000 people selling and we increased a lot in June. From the moment, people move from -- we want to make sure they have a good pay, BRL40,000 or BRL50,000 per month average. Naturally, some are outliers, so they can have a good compensation and earn more. So if they migrate remotely, they have to be with a good performance, good conditions.

So on the next slide, slide 23 a couple of words on the results for the physical stores that we open again, amazing results. These physical stores, even though we open but we only have 40% open. We have 60% fewer physical stores open compared to last year. We have only 55% of the sales below last year the number reported. So we have positive same store sales of these stores vis-a-vis last year, low-single-digit for the stores. But our result is surprisingly good, I would say, considering all the restrictions. People are afraid on walking down the street.

We don't know if that's a trend in the long-term. But in this month of May we started opening and have good results. We are not trying to do too many campaigns. We don't want too many people crowding in the stores. We opened without any noise, very carefully with the whole safety protocols and infrastructure, but the team is working fine.

Anyway, we believe like I said before, part of the natural hedge we'll have more stores opening in June. I cannot mention their importance to our results because they bring more positive contribution, but also to the website when it comes to a store pickup.

We are rolling it out from the moment we know this is not going to bring trouble to our customers, but we are also rolling it out with store pickup. Ship in store was already running but without the presence of customers. So finally, I would like to close my part of the presentation with marketplace, the main highlight of the company's result in the first quarter in April and May. Well, we have our partners, our sellers, who had an additional leap here because the sellers we were approaching until last of -- the end of May were already digital. 5,000 retailers in Brazil, only 50,000 were online, and we were searching for them.

But in the pandemic, we decided to accelerate an important project. We have Parceiro Magalu and we want the small and mid-sized retailers to close their stores. We wanted them to sell online. So we built a very easy, friction-free system. Naturally, the seller needs to comply with many regulations, have to be reliable, so we did an amazing job. And in

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one day, the guy can be running the store if everything is regulated. Otherwise, it takes longer.

Some sellers are in the process to be according to the regulation. We have many notaries that are closed. So the process is slower, but now we're trying to accelerate by going digital to have more than 20,000 taxpayer -- corporate taxpayers being enrolled. And the platform also have people who used to be self-employed, individuals. They can sell and have their own little store and have a commission. We have more than 300,000 people in this new platform. Everything very easy to use supporting 2 significant parts of all the population that were alone, with a hard time to survive economically speaking, owing to social isolation and the pandemic.

So once again, I firmly believe that digital transformation is a means to put together the economic activity with respect to the government measures of social isolation. I think we can put these things together. And now we are going to have Magalu partner video, just to show how they support us. And there are a lot of testimonials that make us very proud so we can generate and foster digital transformation. (Audio-Video Presentation)

My investor relations people are saying that I have to stop. Well, one milestone that we had in April. As you know, we launched Magalu Pagamentos last year, and we have this portfolio that belonged to one of our clients. And in April, we generated BRL500 million in TPV that went through the platform of Magalu Pagamentos, which already enables us. And automatically, we filed with the BACEN, the central bank, a request to be a means of payment company -- a payment company.

Most of our sellers are -- they are anticipating their participation in the platform and this is increasing the take rate for the company coming from this prepayment. We have the prepayment and the seller can have that increase in both cases increasing our revenue. So the marketplace is improving its economics this way. This is an important way to increase the revenue of marketplace. That will be the big revenue generator in the future.

We believe that the value of the company, the result of the company will come a lot from the growth of marketplace that has very positive economics. I don't understand platformS that do not give a good result because they should. But in our case, we believe very deeply that this is a platform that we will have a very good economics for payment and the average of services and the take rate et cetera. And we believe that this will give us great joy in the future in terms of cash generation from our marketplace. And the payment is very important for that, and Beto will talk about the FDIC.

On slide number 27 now. We have been growing much more than the marketplaces and market, e-commerce growing much more than the market but mainly our 3P. We see that 185% was the growth that we had in the first quarter, 430% in sellers. So you can see everybody issuing invoices not waiving our extreme care in terms of the correctness of these companies. And they work -- all of them work formally. And we -- at the same time we are keeping the service level. There was a drop in April and May because there is a very big reliance yet on third-party for transportation, not because the -- there are so many people -- new people in the market and a sudden increase in the volumes. And we

want to improve the level of service of the marketplace. But in terms of growth, the growth of our marketplace is outstanding.

It is much higher than everything that you see in the market. And it is in our strategy, digital platform. This is a digital company for a digital platform. This is the focus of the company. We have already a Magalu digital, and we want to digitize retail as a whole by means of Magalu. So this, I have already talked about growth. I'm no longer going to talk about that. E-commerce 138%, 430% in May.

In Slide 28. You can see that this is based on a 50% growth in the first quarter of '19, 65% in the first of '18. So this -- you can see that the comparison base is high, so we multiplied six-fold our e-commerce in the last 6 years. If you take the revenues published by the major players in the market, you add their GMV and you take the share of each one regarding this amount you will see who is gaining share or not. This is very simple. Only Magalu has been gaining share in the last few years in the Brazilian e-commerce, if you consider the top 4. It's very easy.

GMV published and then you can see who is gaining share and who is not. So it's very -- you take the first quarter. You add GMV of everybody, have the result of the first quarter of 1 year ago, 2, 3 years ago. And you can see who is growing more than the average, who is gaining share. This becomes much more clear and objective as information for you with no narratives that are not material or not real, I would say.

Okay. On page number 30, we have our donations, the families that have been donating ventilators and mattresses and for Hospital Emlio Ribas, Amigos do Bem, NGO. Now we are working with zero profit for the students of the public education system of Sao Paulo state with (Jay Ibero's) NGO. He was the creator of that, and we are embracing this cause. And we have launched this plan for the students. We wanted the students of the public network of schools to have the same conditions of the private ones. We helped over 38 institutions in over 10 states and we will probably roll this out and extend this.

The family will probably increase the amount solidarity that came with the crisis. We will not give any step back. We are very happy to be able to contribute and we want to intensify our contribution. And before giving the floor to Beto, I know that I have exceeded my time, but there is so much that I wanted to tell you. I cannot really say all that in 30 minutes. But we have been recognized as one of the most appreciated or most recognized brands by the client in terms of helping this solve the crisis.

We are very happy with all this recognition. This is not our objective. Our objective is to help, but what companies are doing will be forever engraved in people's memories. And people are more and more aware of that, and they will be buying more and more based on the value of the company in terms of solidarity.

We will probably make many mistakes and we have many challenges that Beto will be talking about. Roberto I apologize for exceeding my time.

Roberto Bellissimo Rodrigues {BIO 17269312 <GO>}

Good morning, everybody. Thank you very much for participating in our first video conference. I will try to go fast in order to recover the time. I would like to start with the highlights on Page 29. We have already grown 34%, as was said before, reaching BRL7.7 billion. With the temporary closing of our stores, we had a loss of about BRL500 million. And minus 4% here, then probably it would be 8%, and we lost in 10, 15 days as you can see an 8% -- over 8% last year.

You can see a high growth in physical stores, marketplace, e-commerce, big highlights. Talking about the EBITDA. We had already talked about that and we continue to invest in service level, logistics and service the acquisition of new clients, seeking a much higher growth than we said in our last letter. And in EBITDA, we have a little bit of this effect of the increase in expenses because of our improvement in level of service, the integration of Netshoes that has not been integrated yet. And we will be doing this over time.

And mainly during this quarter, about the temporary closing of the physical stores, our dynamics regarding results of the physical stores is the following: we bring -- they bring a much higher gross margin, much higher than our average. And in e-commerce, the margin is lower. And of course, the fixed expenses are much higher in physical stores. And when you shut down the stores at the beginning of the month or the middle of the month there is nothing you can do about that because you had already contracted all the expenses.

So if you estimate the sales lost, the gross margin and some variable expenses that could be avoided then you have a very high contribution margin in physical stores. And the EBITDA would be higher than -- so without debt, it was BRL274 million. It went from 8.9% to 5.2% margin. Probably, it would be 1.5 or 2 points more without the closure of the stores.

Dilution of financial expenses. We had a net profit of BRL31 million: adjusted loss of BRL8 million. In terms of capital structure, I would like to reinforce that we have almost BRL4 billion in net cash, adjusted net cash, one of the best capital structures in the market certainly. And when we put total cash and the current issue or recent issue, we have BRL5.4 billion with the new debenture. So you can see a very sound net cash position.

Now let's talk very quickly about -- on the next few slides, let's talk about -- on slide number 30, we show the very quick growth of the number of users, active users, MAU. We reached 20 million as I said, active customer base also growing 26 million active customers, growing 43% year-on-year, e-commerce client almost doubling visa-a-vis last year, very positive figures. Physical stores opening almost 200 physical stores.

In the last 12 months, accelerated growth. And also, we invested over BRL100 million in the 4 -- first 3 months of the year, growing by 31% year-on-year. We showed the evolution of sales. As you can see in this quarter, we sold BRL2 billion more than the same quarter last year. It would be BRL2.5 billion more if it were not for the closing of the stores, so this is a very high growth, e-commerce also growing a lot. 73% for a market that grew 23%, 24% according to the official figures. The evolution of the gross profit, a drop because of

the increase in the participation of e-commerce because the margin is lower and the closing of the physical stores also hitting it.

The gross margin would have been higher if it were not. And the same rationale about the expenses because it was not possible to dilute the expenses in this quarter. And the equity income line we had been going up and up. But this quarter, we have this BRL5 million in Luizacred which is BRL2 million in equity income here. We will be talking about Luizacred in detail later on. On the next slide.

We show the quarterly evolution of the EBITDA, which was one of the factors that we have already referred to. Financial result, diluted financial expenses, 0.5 percentage point if you remove IFRS 16 and the figures about the lease and the drop would be 1.8 percentage point to 1 percentage point, so a low financial expense. And what you have here is the situation of the prepayment of receivables minus the financial revenues.

Working capital. I would like to explain this. We had a variation of minus 1.8% to BRL500 million, BRL2.3 billion variation, totally associated to the reduction in the balance of the suppliers' inventory increase in the last quarter as we sold a lot in the last quarter, it usually drops afterwards minus BRL1,800 million and then you have payment to suppliers that usually happen in the following quarters. So we decreased this by BRL1.8 billion this quarter. So we reduced our cash because of that. But as of now, the accounts payable balance is much lower, BRL4 billion only, and for in inventory. So in this quarter, we have a balanced situation, whereas normally the -- it's usually BRL500 million, BRL1 billion better than the inventory.

And in this sense, the BRL500 million in working capital, normally, it would be minus such as happened in March last year. So this variation of BRL1 billion is basically associated to the inventory increase that we did strategically since the beginning of the year, we started to see the risk of supply and we decided to increase our inventory by BRL500 million. And in the last days of March, then we do not -- we did not sell about BRL500 million, so all that led to the increase in the inventory levels proportional of almost BRL1 billion.

From 70 days to 90 days turnover, so this is not normal. We usually have 70 days of turnover, inventory turnover. And this has already started, this is a very big advantage that we have. We are multi channels. So with the growth of e-commerce, we are already selling a lot of products from the DCs and our turnover is improving quite a lot. And the balanced suppliers, we paid a lot in the first quarter as we said. So we are already improving this position. And we already have this contribution in terms of working capital. And for the next 2 quarters, this will probably happen. And by the end of the year, we'll have a position similar to last year's.

Working capital is seasonal. We did this strategically. We took advantage of one situation. We reinforced our inventories at a low dollar rate and we used capital as we have a very good capital, we are very liquid. We wanted to make this investment. And as a consequence, it is really helping us boost our sales in this quarter. And the adjusted cash flow is very much proportional to the working capital that I have already referred to.

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On the next slide, we show the evolution of our cash. You can see BRL4.4 billion without considering the improvement on working capital and the net income, adjusted net income.

I would like to turn now to Luizacred. Up to March, we were growing very fast. We went from BRL4.4 million to BRL5.3 million, 22% of revenues going up, reaching BRL7 million in expenditures on Luiza Card, 8% increase inside the store and it's inside Magalu stores and 28% outside Magalu Luiza which is a sign of very big activation, 30% increase in the portfolio reaching BRL11.6 billion. And the pace of growth of new cards slows down because of the stores closed. So credit assignment goes down, and we also have a more conservative approval process. And people are spending a little bit less outside because of the pandemic.

From now on what we will have around the middle of the year, it will be more difficult for Luizacred, partially due to the slowdown in the growth rate. When we go to the next slide about portfolio, looking at short-term delinquency, it was 3.3%, a very low level. Well, improvement over last year. So over last year, the credit policy of Ita is very conservative, and it was further improved.

So we had a trend of improvement in delinquency levels. And this reinforces the importance of the partnership with Ita because they are in charge of a part of credit and collection and also the cost of capital of Luizacred which is low and with a guarantee of the Luizacred funding.

Now going to the long-term delinquency, it should be seen vis-a-vis the recent quarters and not last year. It was stable vis-a-vis December, very much under control. And I would like to remind you that it went up in the middle of last year and the percentage of new clients was going up very steeply. And then we had -- well the maturity of the base, we had the maturity of the base. And with the closing of the stores, the impact were not strong, because also we closed the stores in the last 10 or 15 days of March. And most of the impact on Luizacred and other -- any other similar operation, it starts to be shown in these indicators in the first quarter. And good news is that we have a high provisions level.

But we would have to track this crisis and the performance of our payments. If you look at this quarter, there has already been an increase in our provision level. At the beginning of last year, there was a mismatch because Luizacred in the first quarter of last year had BRL36 million -- BRL35 million in profit, but they were already provisioning much more because of IFRS and because of losses. And in the middle of the year, the situation changed. And at the end of last year Luizacred was already giving more profit in IFRS than in BRGAAP. This should be a trend or at least a balance this year with a positive trend.

But what happened in March was that the level of provisions became much higher than before because of the crisis. And because of that, we saw a reduction in the net income in IFRS and we had to a reinforcement in the level of provisions. And should the crisis continue, if delinquency continues to go up, there will be a difference between the GAAP and IFRS because in IFRS you'll see this later.

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So ever since the beginning of the crisis, we have about BRL5 million. Between 2, 2.5 million paid every month at the stores. And it was very difficult for them to make their payments because they went physically to the stores. And we communicated with these clients in all possible ways encouraging them to pay digitally, so that they shouldn't leave home. And with all the assistance on our part and with people who worked at the stores helping them some of the -- well some in home office and some already with the reopening of the stores. And we put in place many initiatives in order to better serve these clients and also to decrease this delinquency level and in order for them to keep their good credit score.

In April, collection was more difficult because most of the stores were closed. And we started to reopen the stores only around the 20th of April on, and other stores were open only to receive payments. Today, we have about 60% of stores open for clients who come and pay physically. So the performance of accounts receivable in May is better than it was in April.

It is not still at the pre-crisis level because I think this is the situation for everybody. Because the finance companies and banks will have an increase in delinquency depending on the size of the crisis. But in our case, the good news is that we are very well provisioned. There could be an additional reinforcement of provision over the quarter, but this is just temporary because Luizacred is very well positioned and our client base is very loyal. And most probably during the second half of the year until the end of the year the situation of Luizacred should go back to normal, such as it should go back to normal for the physical stores.

I think these are the main messages regarding the results and also Luizacred. And now I believe that we could open for questions. Thank you very much.

Questions And Answers

Operator

(Question And Answer)

A - Unidentified Speaker

Thank you very much. We'll start the Q&A session. (Operator Instructions). Our first question comes from Robert Ford, Bank of America. You may proceed, Mr.Ford, Bank of America. Please ask a question.

Q - Robert Ford {BIO 15127836 <GO>}

Good afternoon. I would like -- could you please talk about your view of the pandemic and how it impacted your business model? And what about the development of your stores in the medium and the long run? Could you talk about the impact on your marketing and investments? Because your growth at this time was incredible. And could you talk about the variables underlying this?

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

Bob, thank you very much for your question. As I said at the beginning, if you look at our strategy that we just say Magalu wanting to make the Brazilian retail digital. And if you look at the strategic pillars of this process, I would say that this is more a radicalization and acceleration in the implementation of the strategy. We accelerated many things: The executive committee and the whole team. We are all working in this direction.

I would say that this is more a radicalization. It's not really a change. Because we want to be the operating system of the Brazilian retail, not only for my physical presence, but also the physical presence of third parties, that is to say Magalu partners, I'm using their physical presence, their physical facilities with my operating system. So I do not see a change in the vision. It's more an acceleration of the strategy, that is to say, making this faster, doing this faster and making investments faster so that we may gain scale faster.

So we decided to accelerate and we want to continue to use our cash in order to accelerate and with consolidated and sustainable moves. What is important here is that for the long run, our view is a view of platform. There will be an important displacement. This new cycle of the company is the next cycle that we want to grow with the help of other companies and vice-versa. The previous cycle that we had, we had to go alone. There were no other companies.

And when I talk about the marketplace, I'm talking about the platform which means you helping other companies to be digital and to generate volume and doing this with a high level of service with the necessary economics. So what you have been seeing in our results is a strong trend and the store itself playing a more strategic role for 3P and not only 1P to date. It's very important strategically for 1P, but it will also be an important point of support for small sellers and store pickup, so that the sellers can ship their merchandise.

And I would say that this is totally in line. What happened is that the pandemic is generating more digital countries. Our boat, our sailboat was already prepared to face this reality. All you have to do is adjust your sales, but no big changes. In terms of marketing, we are investing in marketing with more organic accesses than in the past. Because people need to buy online, that is to say they don't want to go to the streets and they want to stay at home.

So there are many people who want to be at home and they do not need encouragement to buy digitally, to buy online. So Edu's team has been doing an outstanding job. And his whole team, marketing people, everyday, and the whole team of Eduardo Galanternick, they're doing a great job. They are very technical. And in our investment in marketing, Bob, has very -- been very precise. I can generate a lot of reach with proportional investments.

Our people are very technical in this area. So we make investments aiming at the long run and not only to look good. In my whole life in digital marketing, I have been seeing people who were not technical. And Edu is too technical sometimes. He doesn't let us spend more. ROE is important. It has to be sustainable, and he is totally right. And you can see

the campaign is online, but it's offline as well in globe. And the other networks and we are using our cash.

I think this is the right time for the company such as the Gulf War for CNN. This has to do with the opportunity. And we are tapping into this opportunity to show how useful we are for the consumers. Of course, I'm not celebrating because the situation is extremely sad. But we know that we can help directly and also looking ahead more and more platform, more and more marketplace. And this is something that we are going to do based on very sound decisions. And this is our view to grow and with everybody's help.

Operator

Our next question is from Luiz Felipe Guanais with BTG Pactual. Please go ahead, sir.

Q - Luiz Felipe Guanais {BIO 19933939 <GO>}

Good afternoon Fred and Beto. My question Fred, you have mentioned a little bit about an increase in the number of active customers. Could you also tell us more about the increase in frequency of the website, particularly April and May. And what about the performance of the cost of acquisition of customers. If we believe the bulk of the stores are closed, possibly there is a higher conversion in the website, which hits into other aspects. Could you tell us more about it, please?

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

Luiz, thank you for your question. I would just like to answer another question, Bob's question about Epoca. And I would also like to invite Edu to help me answer. Edu, could you use a microphone and talk to Luiz?

A - Eduardo Benjamin Galaternick

Luiz, Bob, thank you for your questions. Just coming back to the question about Epoca, Bob. Epoca is already with a very strong growth pace, 60% for a couple of years. And it was pretty much driven by the fact that there is a largest assortment in the market. So we are not connected to any specific group. So we have the possibility to work with the broadest assortment in the market. And if you consider everything we did in terms of the organic performance, we worked on this growth without a cash burn. We have to rely a lot on organic traffic. So when you have such a move where there is a much higher demand, when the customer goes for organic, you have this.

So answering your question Luiz about the customer base and the frequency, what we can see is an increase in all dimensions. We have an absolute number of new customer growth something unprecedented, much higher than in the past. The frequency is also increasing. So you have a multiplier in fact so to speak. So if we exclude new customers, we are going to have an even significant or a greater growth owing to what we've been doing with new categories.

And it's only natural that if we consider an increase in the share of organic sales, then our CapEx is reduced and also allows us to invest in the campaigns that we do with Parceiro

Magalu. And we have to consider our strategies in terms of the market, Magalu and Parceiro Magalu.

Q - Luiz Felipe Guanais {BIO 19933939 <GO>}

Excellent, Edu. Thank you. Can I just ask another question? Fred talked about FDIC. Beto didn't have time enough to talk about FDIC at the end of the call.

Roberto, could you tell us more about the structure of and the evolution for the credit for seller in the platform of Magalu Pagamentos.

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

Good afternoon, Luiz. Thank you for your question. In reality, the focus of Magalu Pagamentos was to do the split in the transactions and advance of receivables, prepayment of receivables. It's been happening since the beginning of the year and we accelerated the rollout ending it in March. And as of April, has is taken off following our marketplace and the natural path is to begin adding financial products to our sellers.

We know that most of them are small companies and they need working capital, they also need some financial support and sometimes they have a hard time to get it. So we have this whole relationship, all the data, in-house data, the whole experience of the seller on the platform with our customers. We believe we can help to some extent, help to generate a score that is better for them, so they can be funded like where they can do today.

In FDIC, there is a BNDES initiative, which is very interesting also to invest in FDIC. So we are considering this possibility as well. But if it's BNDES or our own FDIC, it makes no difference. The trend is the same. We increasingly want to create financial products and services to the seller so the seller can be in our system. So that's why we decided to request to have this regulated. And once it is regulated, you can have different connections at different levels and offer other services that you cannot have access to today. So this is only the beginning. We've just launched Magalu Pagamentos, Magalu Pay. So there is a number of initiatives that are related to Magalu Pagamentos. And they will support our sellers to sell more and that's the goal behind Magalu Pagamentos.

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

Just adding to Roberto's answer, this is Fred speaking. There were several measures made by the government that worked fine like BRL600 as a surplus ink or extra index for self-employed or people who need it, the provisional measure that I mentioned, which is important to prevent layoffs. And many companies are using these. Also many retailers. And one didn't happen, which is the credit at the store level.

So actually most of the lines available by the government for small companies never got to small companies. And because we have a lot of information by sellers, we know how much they're selling, we believe we can help them through these lines, particularly now supported by the federal government. So we have the money, with the information and all the relationships we have. So these measures unfortunately didn't happen yet by the

government. And we hope we can help in our ecosystem to make it happen, preserving credit, but also giving access for those who need it. Those sellers need it. They're growing. And the more money they have to invest to improve their operations, the better it will be for us to support them.

Q - Luiz Felipe Guanais {BIO 19933939 <GO>}

Excellent, Fred. Thank you very much, everyone.

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

Thank you, Luiz.

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

Thank you Luiz.

Operator

The next question is from Thiago Macruz with Ita BBA

Q - Thiago Macruz {BIO 16404924 <GO>}

Hello, everyone. Good afternoon. My question is about marketplace. On the one hand, you have an increased exposure to more frequent levels and lower tickets. So I believe you want to improve your cost of acquisition of customers. It's a clear advantage of migration. On the other hand, logistics can be a challenge. The ticket of these products is slightly lower. So Fred, what about economics of your marketplace considering this migration for more frequent items with lower ticket?

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

Thiago, thank you for your question. I think your question is very timely not only for marketplace but also 1P. 1P part of the market, we are selling our inventory low ticket. The secret behind e-commerce is price over volume. The higher the price the lower the cubic meter, the better the logistic will be. So the diamond is the best product to be sold by e-commerce because you have shipping fee over the price of the product which is low. The shipping cost is a fraction of the cubic volume. So that's the secret. You have low price, and sometimes you have a lot of cubic meter, you have a serious problem in e-commerce. The secret is to be hyperlocal. My view of logistics chain is closer to China than the logistic U.S. long-haul view. Amazon for instance buying airplanes with huge fulfillments, there the aircraft and flight network, you can to do these long moves not so efficient but at least more efficient than Brazil.

In Brazil, if the product has to travel too much, we have a serious problem in results because the cost of shipping and freight will be too high. So my vision to implement locally is based on what I saw in China, which is the short haul, the right product, right place. So my bet is more strongly in a hyperlocal chain privileging the inventory. There are many complex things about geolocation. So there is a little bit of long haul, but benefiting from the local inventory to sell to locals and make these goods travel less.

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So that's a very different approach compared to what I see with some players in Brazil. And that's where I place my bet. But we still have a long way to go we could have 1 hour just to talk about this topic. But I want to sell the product that is closer to consumers, and naturally it takes a lot of infrastructure, IT. Fátima's team is doing an amazing job. They have a great team at labs, and it's very complex to make things simple down the road. And they have a great Magalu is going to bring inventory from the Analog Local World into our platform. And the Superapp -- the advantage of the Superapp is that you know where the place -- the place where the person is and you can have the product exposure accordingly. So the chain is fully tied to make the product available, the product that is closer. And the secret is to have low ticket products with interesting logistic costs and making the product travel less.

Q - Thiago Macruz {BIO 16404924 <GO>}

Great. Thank you for your answer.

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

Thank you.

Operator

Olivia Petronilho from J.P. Morgan.

Q - Analyst

Good afternoon. Thank you for the question. I have three questions. One has to do with the short run when we look at the stores still closed and of course, there is a cost. Can you tell us the monthly cost of your operating the company with this situation? The other one has to do with Netshoes and Zattini. How much total GMV, how much were growing? And the other one is a long run question. Do you see any possibilities for M&A during the crisis? Do you think there will be new opportunities for acquisitions in the market? Thank you.

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

Thank you, Olivia. Three very different questions, and I would like to ask Beto to answer your first one. Beto, could you talk about this quarter and related to the first question of Olivia?

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

Olivia, good afternoon, and thank you for the questions. It's difficult to answer without giving you a guidance. What we can say is that in physical stores most of the expenses are fixed. So in the physical stores, they are personnel with rent and other expenses related to occupancy. And the percentage of marketing and shipping is less than online. And in online, marketing and shipping are much higher.

And most of the expenses are variable differently from the fixed of the brick-and-mortar stores. So if you break down our SG&A based on our sales and these indicators, maybe

you can get to the cost of the brick-and-mortar stores. E-commerce is growing. It is evolving in all aspects that we mentioned. And the physical stores have this scenario. They were closed in most of April and they are gradually being reopened in May with good sales performance, but we still have many stores that are closed.

So in terms of fixed expenses for all retailers that have physical stores, this is difficult because of the situation.

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

So we try to convey this message during the presentation and there is no magic trick. You can have creative accounting, or reversal of provision, or something non-recurrent but recurrent. As we make decisions, for instance, now laying off anybody in the next quarter probably all of them will be opened.

So it would be nonsense to have layoffs and then having to contract or hire people afterwards again. So we have the capacity, we have the necessary cash. We are going to hold on to this and we are going to report this in a very transparent fashion. So there will be an impact on our result, of course, because you will see this in our management report. And this has already impacted as you can see, the first quarter of this year.

The contribution margin of a physical store, Olivia, is high teens, So you can do the math yourself. We made endeavors in terms of reducing expenses, we renegotiated our rents and we use the NPE, the provisional measure. But we have to give a contribution as well, 80% drop in the sales of physical stores, we cannot reduce 80% of the expenses. This would be totally impossible. So you cannot pay zero rent for instance or zero salaries or 80% reduction in salaries.

So we decided to hold this back in spite of it being a more difficult quarter. And it's going to be difficult quarter now. So you should not expect -- well, you have to expect a difficult quarter in terms of bottom line. Top-line, much higher than we expected, but I want this to make very clear. Related to Netshoes, I would like to give the floor to Marco. But all over the world including online, the categories that he works with are suffering in terms of the home fitness market.

Categories as a whole, they are not growing in the same proportion. 3P is very good. 1P growing more than the market numbers but higher than the plan that we had. And with a very good balance in all senses, margin et cetera, and he's going to talk about that. I'm very comfortable and very pleased with the work being done by the Net team. But Marcio, I would like to answer -- ask you to answer.

A - Marcelo Jose Ferreira e Silva {BIO 20220206 <GO>}

Good afternoon. Ever since we came on board, we are working a lot for integration. And giving you a highlight about the integration. The back office areas are going very well, very smoothly in June. We have an important point which is the unification of the DCs and with that Net will be gaining logistic capacity of all the DCs. And this is going to make a lot of difference in terms of logistics as Fred said as far as we are concerned at Net.

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And also the back office migrating slowly and getting together with the Magalu team. So we have a very strong plan so that in the third quarter or from the third quarter on we may really make a difference at the bottom line. And talking about the JV, both Net and Zattini are growing. And also, we intend to put all our expertise within magalu.com. So as Beto said, we had been growing higher than the market. And when the pandemic hit, we had a drop. But we have already recovered from this drop, and we have reaccelerated in Net as it was one -- a very beloved brand.

We are very happy with this acceleration, the recovery of the base. And the margin that is going up because of the good renegotiations and the partnerships that we have with the most important brands and Net having the biggest -- the bigger share. And on the other hand, our products are practically all replicated in magalu.com, almost all the brands in Zattini and Net.

And many brands coming on board on Zattini and Net, at the moment the physical stores are closed. So during the presentation we showed you important brands. And we have the magalu.com selling in Net, which is big news, almost 6,000 products reinforcing and all part of the integration. And we see an acceleration of GMV and at the same time an increase in our margin, top and bottom as well.

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

In Comercio and about M&A of course, there is nothing we can tell you about our intentions. And once again, we try to preserve cash in order to be prepared for the opportunities that will arise in the market.

The digital profile companies, they were not devalued. Quite the opposite, they have appreciated. So we do not see a mega deal in our radar screen, but maybe there will be some other assets that might help us, companies that are not so digital, but could give us a contribution in the future. I cannot give you any hints, but we're ready to make intelligent acquisitions such as was the case of Net.

Q - Thiago Macruz {BIO 16404924 <GO>}

Thank you very much. Very clear. Thank you.

Operator

Richard Cathcart, Bradesco.

Q - Richard Cathcart {BIO 16457807 <GO>}

Good afternoon. I have two questions. First about the 3P logistics. You already have 20% cross docking, very quickly. You got to this number very quickly. So what about the remainder of this year? Fred, you said that 1P is growing very strongly as well and this could be a limitation. But how do you expect this to evolve over the remainder of the year?

And the second question has to do with the market category. I would like to know about the consumer behavior in this category. Are they trying to set up a basket? Or are they buying products individually? And about having the products at the stores for ship from store, have you done this only temporary because of the COVID crisis or do you intend to keep it this way?

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

Richard, good afternoon. Thank you very much for your questions. They are very relevant. And as I said before, as I said during the presentation from 0 to 20, it was a very big job done by the teams and I would like to be at another level. I think this is super important and it's very important to share Malha Luiza with our sellers. And 20% is a figure that does not satisfy us here, but it was possible because we had this boom in sales and we grew very fast and we had to build capacity for Malha Luiza mainly Logbee. And this is being consumed by e-commerce and part of reduced sale. And we have to protect this.

And it's simpler now to execute. I really cannot tell you from now on about the growth dynamic and to which extent this will be when all the commerce is open again. So it's very hard to foresee and to be precise. But if the acceleration continues to be the same, it will be difficult for us to increase this 20% significantly in the short run. I'm being very honest and very pragmatic. If we continue to see this growth base, it will be very difficult to go much beyond 20%.

So we do have a target. This is our intention, but we have to meet the capacity. And it's important for the company to generate cash. So, so many things involved and we have to find solutions that maybe I do not have right now in order to explain to you differently from other players that are only marketplace. We have 1P. As far as consumers are concerned, they want the product to come to their home very quickly regardless of being 1P or 3P.

In terms of our Superapp. And our competitive advantage in -- it's a little bit different in terms of economic because at the 3P gives us a higher ROIC. But for our strategy of growing and having a leadership in the formal market of e-commerce, I think our logistics is correct. And it can support us and give us this possibility of following this relevant growth in total GMV. In relation to market, the idea is to be at the stores, that we have to be at the stores forever.

So it is here to stay. We are setting up the necessary structure at the stores in order to have the system in place. 1P, we have a possibility of a leaner 1P SKU's and profile more wholesale than retail. It's higher ticket, not so many items per basket. Although we do have the development in the app. All the UX done by our products team and the labs team, Edu's team and everybody's, (inaudible) improving UX, and this is a very good experience today already.

But it still has a lower number of items per basket. And we want to supplement this with 3P. And we'll have a different experience there. There are some challenges how to put together 1P with 3P. But our team is very creative, and I think they will find the necessary solutions to conciliate and to put these things together. So it will be a combination of 1P of

store -- of the stores, current stores with 3P. If we need to increase the stores and have more storage area, we are discussing this. Today, we do not need this yet because this is -- we have a very lean line and I have some images to give you as well. We can show you the stores in this new model and you can see this, okay? I can tell -- show this to everyone.

Q - Richard Cathcart {BIO 16457807 <GO>}

Thank you very much.

Operator

Next question, Ruben Couto, Santander.

Q - Analyst

Good afternoon. Could you tell us more about the behavior for this acceleration in April or May? There was a first move to increase demand for specific products like home office, but it may change owing to this high demand of new customers and the acceleration of new categories available. Any insights on the levels of accelerations to understand what is a trend or just transient? Thank you.

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

Ruben, thank you for your question. I'll answer your question based on my opinion. I have Magalu data, but not market data by category at the level I wish I had to give you a more scientific base or more fundamentals. But what is my opinion right now? Firstly, facts. The market of office migrated, one. So you have many people buy in physical stores and now buy online. And online, Magalu's share is higher than offline. I have more competitors, small local regional players and only in one category which is electronics and home appliances, but even in that category half of the marketing is small and mid-sized, so we have more options there.

When the guy goes online, they have few players. Three platforms, three or four larger platforms for the guy to buy. So you have - Magalu has a higher share online than offline. So migration from offline to online overall speaking explains part of our sales growth. More people buying online, my share in online is greater, so naturally the growth happens at a higher rate. And our share is share as effect, high share online.

With regards to categories, if you think about Alibaba's results published on Sunday, this is so interesting. You will see that there was a slowdown in the quarter because it was the peak of the pandemic, unlike ours. We accelerated even more than Alibaba in our online. I think we have a lower digital rate, so migration was different. But if you focus by category, and they had a disclosure in their reports, the best performing products were supermarket, both home care, personal care and electronics as well.

So they mentioned several times in the release that electronics performed greatly. And my theory is that there is a universe that is limited to your home today. You're moving entertainment at home. You're eating more often at home. You're studying at home. You're working at home. So your home is your universe today. And in that universe, you

need the right parts and tools to work with. So if you have five people at home, I know many people who bought five notebooks.

Because the husband and the wife are working from home and their three kids are attending classes online, everybody needs a computer, everybody would have to do his own share. So people are via streaming channels and lives are popping up, everything at home. It takes investments. You have (inaudible) at home. You need a stove, a fridge. So there is a boom in countries that are going through the pandemic.

And home appliances, everybody thought they were not so important. They are nearly staples today, and I would say that today they are important, even more important. Well, if you think about fashion today, I'm speaking of published in Chinese company that I've been following on. However, this is just intuition. It's a theory, no evidence in practice. I think we have to wait a little. We have evidence based on our own numbers only.

Q - Analyst

Clear. Thank you. Thank you, Fred.

Operator

The next question is from Daniela, Eleven Financial.

Q - Daniela Bretthauer {BIO 13380169 <GO>}

Good morning, everyone. Good afternoon. We've been here for a while. Fred, the first question is addressed to you. Fred, what's your opinion about the strategy, Magalu strategy, considering the high complexity of the pandemic? Because it brought some constraint at the store level like you said before several times during the call. So how do you envisage Magalu's ecosystem with this additional level of complexity? That's the first part of the question. And then I have another question for Roberto about Luizacred.

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

Hello, Danny. It's a pleasure to answer your question. Good afternoon. I believe the store will have to have an even more significant role for the ecosystem. The current role is important in store pickup and also in ship from store becoming more and more significant. However, I think there is room for more. You can have an even more significant role for 3P. That's what I usually say. And I believe, I imagine it will be just like those XP self-adviser. So that's the role of being like a hub in the micro region, a hub to the platform. So that's the best example I can give right now.

The store is as significant as you have these advisers for XP, that's a general question or answer. Just to give an example, stronger in the ecosystem not only as a sales channel, but an important part that contributes to the whole. This thing about having independent parts being together. I think it has to be accelerated. I wouldn't say it is more complex, I hate complexity. But maybe it's something fuller, more complete to the system as a whole.

Q - Daniela Bretthauer {BIO 13380169 <GO>}

Has it changed? Do you think it would inevitably happen regardless of the pandemic? Or did it take some adjustments to the strategy.

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

I wouldn't say it changed. However, it greatly accelerated the need. Many things are projects that are still ongoing. But the vision, the vision is stronger in the current context in the sense of turning it into more relevant to the ecosystem as a whole and not only slightly relevant and isolated. This time more integrated to the ecosystem and the pandemic accelerated it. I wouldn't say it changed it, but it made the rationale more intense.

Q - Daniela Bretthauer {BIO 13380169 <GO>}

Got it. Roberto, my question is about Luizacred. I was positively surprised. I even thought or I thought that Luizacred's performance was good this quarter, particularly when we compare to what happened at (inaudible) or Carrefour. In other words, you did have a robust growth in the portfolio, even the on and off performance of Luiza Card. However, there was not a need to make more provisions or stronger provisions. So what about the second quarter? You said that this quarter was very challenging. But what level are we speaking of in terms of adjustments at Luizacred?

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

Hi, Danny, good afternoon. Thank you for your question. Luizacred was going through an improvement process. There was a trend to improve the results since early last year. Like I said, it increased a lot with many new customers and then the margin became more mature. By the end of the year, the results began to improve, go back to better levels, more similar to the historical figures. And this year, it was about to continue or to follow this trend.

So when you look at the result in the first quarter compared to the first quarter of last year, the bottom line was better but it should have been much better. And it was only slightly better because last year it was negative. For the future, the trend in the industry is to get worse. Today, provisions are already very high, IFRS, BRL1.6 billion provisions, about BRL900 million overdue portfolio, 175% coverage index. But the point is that Luizacred's result result or any consumer operation.

If you think about it now, the drop in concession brings down revenues and sales. So everybody will have a curve, a slowdown curve just as we see with physical stores. Maybe a little bit milder, but the impact is still there affecting results and also the impact of the difficulty, the hard time for customers to pay. And we are trying to minimize it with all the actions that we're mentioning and reopening the stores. But even when stores or where stores are open again, performance are not back -- is not back to normal yet.

So if I could give you a range just to give an idea, when it comes to receivables, the percentage of receivables vis-a-vis what we expected in April for instance was 90%. In May, it is close to 94% or 95%. It's not about the total. Some customers didn't pay, some

asked for additional funding, et cetera. So it's just to give an idea. May is better than April but not 100%, which is what we had before the crisis. So we still have some level of efficiency and we don't have all the stores reopened yet, and it made (Technical Difficulty).

Anyway, we have to welcome the customer, try to help him, minimizing impacts. We are getting all the stores involved in the process to improve our service in terms of reminding customers to pay. And just physical stores, the second quarter will be so difficult and slightly better in the following quarters trying to go back to the same track. So once again, I believe the good news is just for a short time frame. For Luiza in the long run, we are going to move away from this crisis even stronger than before, more digital, more connected, et cetera.

Q - Daniela Bretthauer {BIO 13380169 <GO>}

Great. Thank you. Thank you.

Operator

Now we have come to an end of our Q&A session,. And now I would like to give the floor back to Frederico Trajano for his closing remarks. Thank you.

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

Yes, I think our call has already been quite long, and I would like to thank you very much for your patience. You have been with us for a couple of hours already. And I would like to thank our people in the back office and our financial team that gave us our presentation and our accounting team, everybody who have contributed. Plus the 35,000 employees of Magalu who are, like all Brazilians, suffering and languishing because of this pandemic and all the consequences of the pandemic.

But we are now adjusting the sails of our boat in order to continue in our trajectory. And we're so thankful to everybody who works for us and very happy and very thankful for the performance that they are delivering. A lot remains to be done. We have already mentioned to you all our difficulties. There will be many but not bigger than our confidence on our team. I have always said that my focus is to get Magalu to 100 years and very fit. It is not a focus on a year, it is a focus on the long run. So we have already celebrated 63 years and we have a lot of room, a lot of time until we reach 100. Thank you very much.

Operator

Magalu's conference call has come to an end. Thank you very much for participating. And we wish you a good afternoon. Thank you.

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