Q1 2015 Earnings Call

Company Participants

- Eugênio de Zagottis, Director-Investor Relations & Corporate Planning
- Marcílio D'Amico Pousada, Chief Executive Officer

Other Participants

- Guilherme Assis, Analyst
- Joseph Giordano, Analyst

MANAGEMENT DISCUSSION SECTION

Operator

Good morning, ladies and gentlemen. At this time, we would like to welcome everyone to Raia Drogasil Conference Call to discuss its First Quarter of 2015 results. The audio for this conference is being broadcast simultaneously through the internet and the website at www.raiadrogasil.com.br/ir. In that address, you can also find the slideshow presentation available for download.

We inform that all participants will only be able to listen to the conference during the Company's presentation. After the Company's remarks are over, there will be a Q&A period. At this time, further instructions will be given.

Before proceeding, let me mention that forward-looking statements that are being made under the Safe Harbor of the Securities Litigation Reform Act of 1996. Forward-looking statements are based on the beliefs and assumptions of Raia Drogasil management and on information currently available to the company.

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

Today with us are Mr. Marcílio Pousada, CEO; Mr. Eugênio De Zagottis, Investor Relations and Corporate Planning Vice President; and Gabriel Rozenberg, IR and Corporate Planning Director.

Now, I'll turn the conference over to Mr. Marcílio Pousada. Sir, you may begin your conference.

Marcílio D'Amico Pousada

Thank you very much. Hello, everyone. Welcome to Raia Drogasil's presentation for the first quarter 2015. As always, Eugênio will present the results and me I will talk with you a little bit about the results. Okay, Eugênio?

Eugênio de Zagottis

Well, thanks everybody for the presence. It's a great pleasure that we announce another set of strong results in the quarter. We sustained a very strong momentum that a company has had since we completed the implementation of our corporate systems in the beginning of last year. So this was another strong quarter, we opened 19 stores and closed one. We achieved revenues of R$2.1 billion in the quarter, 19.4% revenue growth, 11.3% same store sale growth what we think is a robust number. Our gross margin reached 28.8%, 1.5% margin expansion. We booked R$152.4 million in EBITDA, a margin of 7.4% and a 1.9% margin expansion versus 1Q 2014. Our adjusted net income reached R$81 million, net margin of 3.9% which doubled the figure. And our cash flow was negative R$31 million in terms of free cash flow and negative R$24 million of total cash consumption but if you compare it with the previous, with the same quarter last year it's a much, much better number we have to consider here that the fourth quarter in every year is by far the strongest quarter in cash cycle with the seasonality. So any quarter when compared year-to-date we'll likely show a negative result but on a comparable basis apples to apples it's a very good quarter in anyway which I think is (4:07).

On page four, it's important to mention here that starting from 2015 our financials do include the effect of net present value adjustments. Basically, we're reclassifying from net revenues and from the cost of goods sold interest income and interest expenses that is embedded in our days of payable and days of receivables. We are also reporting 2014 on a pro forma basis so the figures are fully comparable and we provided in our website there is even a link to the earnings results along financial history, since the first quarter 2012 also with pro forma adjustment. So, that you can update your historical basis and use it as you sense it.

Another thing is that we readjust that days on the Interbank deposit range. So, it's very conservative kind of adjustment and in the end what this provides is full comparability to other retailers in Brazil. So, pretty much almost all the recent retailers do pursue net present value adjustment. I could mention a few here Lojas Americanas, Renner [Lojas Renner], Magazine Luiza and many others. So, now our numbers become fully comparable to them.

If you should take a look on the bottom table in this page; you can see what the effects are on the 2014 number. In average for the year, we increased our EBITDA margin by 0.4% based on this reclassification depending on the accounts payable in the quarter the number can move slightly more, slightly less, but that was the average and this figure is reclassified to the interest expense. So, it doubles up but interest expense will also double up in a way that net income is not affected by these adjustments.

Back to the business page five, we ended last year with 1,109 stores last year, so a strong number. We opened 19 stores in the first quarter versus 18 stores in the first quarter of the previous year. So we signed off in the same pace. We intend to accelerate the pace, this is still not an ideal number for us. Right now our numbers have been highly geared towards the end of the year. Operationally, this is not the ideal thing. So we are getting ready to try to make it as linear as possible. Otherwise, I don't think we ever be 100% linear to the quarter but I think we can do much better than this and we also closed one store in the quarter.

We are now have 66.9% mature stores in the base, 33 stores are yet to reach the potential of revenues and profitability. We can see our updated geographic footprint. We haven't entered nor we intend to enter any new markets this year, our focus will be based on existing markets, let's not forget that we are present in 19 states that account for 89% of the Brazilian pharmaceutical market. Our expansion focus has been in Sao Paulo and all of them are (7:32), let's remember that in the Sao Paulo metropolitan area with two brands Raia Drogasil, we have the excellent number that Drogasil Sao Paulo alone has of stores.

So this kind of shows how bigger we can be in Sao Paulo, this is our native market with the safest openings you can pursue anywhere. And the Northeast grows on a very successful entry story. We are very happy with every market there. Our new stores have been amazingly successful so we'll see more and more of that.

So overall the quality of the store has been outstanding and we have maintained kind of what we saw last year. And finally, an important notes here, we switched brands, a unified brand in Rio, Drogasil had entered Rio just a couple of months before high Raia and Drogasil merged. So, last year Raia had already north of 70 stores, Raia was the clear number two brand in Rio second only to Pacheco, while Drogasil had only nine stores. So Drogasil didn't get the visibility required with the help of brand awareness required so we decided to switch Drogasil to Raia. So, we're unifying, we're now competing a single brand in Rio and this also makes us stronger because Raia becomes more prevalent, we increase its presence and those shifted stores, they now have much bigger potential because the operations under a much stronger brand locally. So, this is another highlight of the quarter. We ended the quarter as I mentioned before with 1,109 stores of which 540 with Raia, 569 were Drogasil. If you take out, 22 Farmasils they are classified under Drogasil, the brand that almost an identical size because you'll have seven stores more than Raia.

And on the right side of the page, if you think about market share, we gained market share on a national basis but we also expanded our share in every market where we compete. So, our national share, they reached 9.7%, a 60 basis points increase. In San Paulo, we increased from 20.5% to 21.6%, in the rest of the Southeast we're talking Minas Gerais, Espirito Santo and Rio de Janeiro. We came from 6.7% to 6.8% so a light gain here. In the Midwest region 11.9% to 13.3% very, very strong performance in the every market here. In the south 4.3% to 5%, on the Northeast we are ready to reach 1.7%, and this the total Northeast region so there are many sales here in the region we are not pricing yet. So if you consider the market in the Northeast where you compare is much better number than that, it's a very good beginning for our operations up there.

On page seven discussing our revenue growth, we reached 19.4% during the quarter, same-store sales growth total of 11.3% while mature stores grew by 6.9%. We consider this a very good number much better than our budget especially when you consider the high comps of the 1Q 2014. So we grew same-store sales less than 12.7% and we did mature stores 7.6%, so I think it's a very, very good number. And as you reach the second quarter the comp base becomes much easier so even if you maintain the current revenue level this will be a much better growth so of course the comp base bring some noise to the figure but overall we're very happy.

Another thing that's happening is that Raia Drogasil is decoupling from Abrafarma when you think about sales trend. Let's remember Abrafarma the Brazilian Drug Chain Association equivalent to NACDS in the U.S. so it will be a list of the drug chains in Brazil who were part of Abrafarma and if you will consider last year and similar trend also happened in this first quarter were Raia Drogasil grew something like 18.5% if memory serves me. The rest of Abrafarma taking out our number from the base grew slightly north to 11%. So our numbers are de-coupling and there is a big gap between Raia Drogasil and Abrafarma, so I think shows the current stage in terms of competitive to Raia Drogasil.

On page eight we then discuss the gross margin, which were really the high level in the quarter and the main driver for the tremendous margin expansion we saw. We increased gross margins by 1.5 percentage points from 27.3% to 28.8%, 0.7% actually 0.8% of that increase had already happened through 2014 so we will focus here on what happened since 2014, what happened in this quarter versus the previous quarter which was a gross margin gain of 70 basis points. Where did this new expansion come from? We have several elements here to consider, first there is a net present value adjustment difference of 0.1% which helped the margins because we have longer payment terms now than we have in the end of last quarter. So this is one thing.

The second thing is that we had in the fourth quarter a peak in inventory losses due to a change in the accounting criteria for inventory terms to our suppliers, (13:34) but the reality is that now as things normalize there was a tiny bit (13:38) improvement over the 4Q 2014. So the expansion of the 4Q is really slightly bigger than it was actually was, so this is 40 basis points of commercial improvement achieved in the quarter and main reasons were pricing, let's remember that we significantly upgraded our technical management area from four people to nearly 20 people. This was done for the dunnhumby projects but even before the benefits from dunnhumby kicked in, I mean these are not people who are idle there, they are working and they are very creative value. So just by having more people looking more detail and separating smaller CapEx with the – by the category manager. I mean people can be much more assertive and they set up opportunities much faster and act upon that and we are benefiting from that in pricing.

Another thing is that, as we re-negotiated our commercial terms in the beginning of this year with our suppliers, we also saw significant improvement. Let's remember, as we are decoupling from Abrafarma and we are now the fastest horse in the race. So our suppliers who need to grow they are more likely to invest in the fastest horse. So we're seeing more investments because our supplier who gain share within Raia Drogasil feels assured something like 20% or more revenue growth from us. So this is a strong starting point from them and we can compensate for the lack of growth in other clients. So the growth also helps in getting better terms.

And finally, we're also doing a lot of opportunistic deals. We have supplied especially those who service supermarkets, who were not been able to fulfill their targets. So they come to us, they ask us to take extra inventories beyond what our demand would allow us to buy and as a result we – if we can get extra financial benefit in the form of more discounts, in the form of better terms. And also if we get the additional inventories financed by high accounts payable we'll do it and we have made some money like that and I think that's likely to continue. The reflection of that can also be seen on the cash cycle. We have very strong inventory level, 95 days, we have a very strong forward buying in anticipation of the price increase so this is sustaining us for a very strong quarter margin wise and I think overall as well. Another thing is that the opportunistic views they are also increasingly better but they also generate the financial benefit for that.

Accounts also while increased nine days of inventories, we increased 19 days of accounts payable. So, the forward buying is fully financed within the month. These opportunistic views have been fully financed as well and another thing is that historically, we had the seasonality issue on the first quarter in which significant purchases of cyclical merchandize at the end of the year were paid in a lump sum in the end of the first quarter. So we have been able to change the commercial model and to remove peaks and valleys that arise from that purchasing model, we are talking basically about sunscreen. So, there's also on a stretch improvement here and another thing is that the comp base of the first quarter of 2014 was also depressed, so this also helps to make the gains even bigger. So, as a result cash cycle reduced by 9 days and this has a tremendous impact on our cash flow.

On page nine, we diluted operational expenses by 50 basis points. This operating leverage was achieved part in sales expenses which diluted by 20 basis points and general and administrative expenses in which we achieved a 30 base point dilution. So, going one by one on the sales expenses we achieved the 20 basis points dilution in logistics, we're basically talk about distribution centers. We have a planning a new distribution center this year. We have one program for next year but nothing this year. And another thing is that as we integrated our distribution footprint, and as old distribution centers which used to be fully dedicated to Raia Drogasil, and as we starting to service in both brands, those are big reshuffling of stores from one city to another and this generated peaking of expanses next year. So this is another issue why, another reason why we spend 20 basis points where we diluted 20 basis points of distribution center expenses.

Another thing is that the new store results are better. We have 10 basis points better than last year which was already good. So this shows the quality of the growth program. And I am talking both of the results of the store that we have already opened, but also the three operations expenses related to the stores that are in the opening process. And then when we resume within the store we saw pressure of 10 basis points. This pressure arose from 10 basis points in rentals, 10 basis points of pressure in electricity, partially mitigated by 10 basis points in dilution of other store expenses. So the net effect of the store was minus 0.1. The net effect for sales expansion was plus 0.2. And then on generic it is a 30 basis point improvement, but this is due to the fact that last year we over-provisioned (19:43) compensation in the first semester. And then we doubled (19:49) the effect in semester. So we are comparing to a base that was kind of artificially flavored last year. These numbers figure is good I think that it may give the trend for the year. But the comp base is very – the expansion of the comp base was very high.

So we know our EBITDA reached R$152.4 million, 7.4% of gross revenues. Let's remember that we don't have a single adjustment in our expenses and this is also testament to those places in the integration and we reached our margin expansion of 1.9% in the quarter. This was driven by 1.4% in the gross margin and 0.5% in expense dilution. Another thing is that the stores recently opened in this year, they generated a negative profitability around R$7 million. So if you had modeled any single stores, we have had R$159 million of EBITDA which would be 7.8% when considering the respective revenues of the previous store without the revenues of the new store. So this is a small example of the effect of store growth in our figures. The full impact goes beyond the initial losses of the reopening stores or even of store one year or two years they are still not performing the full revenue and profitability potential. So we estimate that our EBITDA would be 150 basis points higher if we had a fully mature company.

Next page income, we increased adjusted net income by 1.5 percentage points we basically doubled over last year R$40.7 million to R$81 million and what happened here is EBITDA increased 1.9% depreciation, we got pressure from the 0.1%, interest expenses, we got a 0.2% pressure and then on taxes you had another pressure of 0.1 percentage point. What happens here is that these kinds of margin expansion that we achieved should have resulted in a much bigger negative tax effect. What happens is that we increased significantly our interest on capital which is highly tax efficient and that mitigated that effect. So, just to exemplify we booked in this quarter R$61 million in interest on capital to be paid for future and versus R$7.7 million last year. And another thing that a big portion of these interest on capital that we booked is related to last year, you remember that we announced one week before the fourth quarter last year an extra interest on non-capital payment related to last year, so it is within the figures. And just you remember that our commitment this year is to return the maximum amount legally possible in interest on capital to leverage its full efficiency to our shareholders.

Page 12, talking about free cash flows, we generated R$116 million in resources from operations versus R$80 million last year. Operating cash flow after working capital was R$28.4 positive versus R$62 negative last year. We invested R$7 million more so far and we reached a free cash flow of R$31 million negative versus R$115 negative last year and our total cash flow of R$24 million negative versus R$129 million negative last year. Any quarter when compared to the fourth quarter will be negative because the fourth quarter has a very strong cash flow seasonality it's positive but these trends when compared apples-to-apples in the first quarter, it's really a very good number fueled by operational improvements and fueled by working capital efficiencies.

On page 13, the total shareholder returns achieved so far in the year have been 13%, if you consider the total-the average total returns in the new IPO the have been 24%, we're talking almost eight years and since the Droga Raia IPO 26.8% total return per year. So these are very good primary equity tax returns and I don't know what the numbers would be but I'm sure we'll keep seeing stronger returns in our future.

On the next page, just to highlight the investor relation activities that we have in schedule. As you have observed, this year for the first time we are reporting in every quarter, we're just doing now and we did that, you do that in the second, third and fourth quarter. We are reporting the quarter results, we've seen in the consecutive months. So this is a big achievement for us. Closing the accounting for our retailers for 1,100 store is highly complex but I think it shows the level of process maturity that we have reached and our goal from next year remains to be seen if it's real or not, we'll beat the (25:39) on that, maybe one it is difficult but certainly for sure moves next year, so we have a high commitment to shorten the window between closing the numbers and reporting those numbers and other thing is that the Raia Drogasil Day will be held on December 4 in Sao Paulo. This is the consecutive day a very important conference in Brazil for whoever is expected to come to the conference please program another day and stay at our Investor Day we're sure you'll make good use of your time. The time and venue is yet to be determined and the next conference is that we will attend will be the Santander Conference in London on May 11 and 12. I will be there. And then May 13 and 14, the Itau conference in New York, Marcílio and myself will be there. Finally, we have another conference in Brazil on June 24 and 25, which Gabriel and I will attend, which is the Citibank conference.

Before passing the torch here to Marcílio for his summary, I'd like to highlight a couple things. The performance we achieved in this quarter which was very strong was really based on three pillars, market growth, strong capital structure, strong execution capacity. So we have a resilient market, a market that grew 14% according to IMS in the first quarter. It will maintain double-digit growth it can grow slightly better, slight growth but will maintain double-digit growth. So we have a very strong foundation for our growth here.

The second point is capital structure. The current capital structure that we have which is very strong, allows us to keep our investment program intact without any forethought about international markets, about the credit availability about interest rates or anything of the sort. Another thing is that we are able in adverse macroeconomics scenario like we've seen in Brazil to leverage that to a favor in order for us to gain market share. We have a lot of competitors who are highly leveraged some national ones, a lot of regional ones. They have very low investment capacity right now and they are becoming vulnerable in the operations and as they have to increase prices, as they have to cut inventories, as they have to cut people and service. So, we are taking advantage of the market environment. The market environment is proving to be an advantage and not a disadvantage. We already saw this at a much bigger scale in 2008 and 2009 due to credit crisis. And finally the third pillar, the execution, we are now a fully integrated company. We have combined assets and competences in a very unique that were brought by our brand and shared them across Raia and Drogasil and with that we achieved an even execution. So Marcílio will now do his final comments before we go to Q&A. Thank you very much.

Marcílio D'Amico Pousada

Thank you Eugênio. I think we are very proud of the results, we know how difficult it is (29:03) but we know the number of work that we (29:07) this acquisition how important is the (29:15) business, the vendor business and I had three process that here as show you how we improved these numbers. The number one process that I would stress it we have achieved the best lowest historical store cost level in our company in March. Okay, why we did that, we used our by now the expense (29:37) for all the stores which has helped us to do this and we know how to do this very, very well. We increased our delivered (29:49) for the stores also and we are using better our management algorithms to understand better what methods has be put the merchandise in the stores. When I listen for example, when our competitor also told (29:57) they reduced the stock. I thought it might be easier let's go to increase the stock near the region where (30:05) the customers, okay. Then the stock is very, very important for this business, for the daily business.

The other process is people. We hired a new VP of Human Resources people just one year ago, we then hired two new Directors and we worked very, very closely to normalize all the processing of people. We have now 23,000 employees in this industry this is very, very important how to manage, how to train, how to hire the people, and how to take care of these people for these people to take of our customers. This helped us to achieve our best historical number is the Net Promotor Score, we call this Asset Employment Group. We have to hire in the Raia Drogasil right now and we know we can have the customers happy where you can sell better then it helps us a lot to achieve the sales numbers in this quarter.

And the third process that we would like to share with you is to hire people in the end of 2013. The category management is very, very important in the business, our store is too small. We choose the items for the customer (31:24). Then you have to hire the best people to make this process very, very well. Not only with the assortment, layout and pricing, but in what the best item in which different regions in Brazil or even in the big cities like Sao Paulo where business right now using a customer's profile that you have and we know this is very important for the future growth because we just hired dunnhumby and dunnhumby is working right now in this process also but we didn't – that you consider it could be next two years 2016, 2017. The first improvement that you see right now is only pertaining, I am sure that you have the best category measures you need from a system in Brazil right now here in Raia Drogasil. This helped us a lot to increase the 1.5% in margin in this quarter. The last message that I would like to focus with you is we are focused in the long term, we are investing people, process and platforms increasing our productivity and improve the customer sales. We really believe if you have a good process, good platform and good people to sell to customers we will increase our results and return on investment capital we are working in future also.

Thank you for your (32:46) and we're now ready for the questions.

Q&A

Operator

[Operator Instruction] Guilherme Assis from Brasil Plural would like to make a question?

Q - Guilherme Assis {BIO 16143141 <GO>}

Hi, good afternoon, everyone. Thanks for taking my call. I have actually a follow-up question from the Portuguese call, can you guys elaborate and talk a little bit about the comparative landscape in Brazil, I think given the strong margin results that you posted and the strong growth, I'd like to understand how you are seeing the competitors from what we see from the latest competitors like (33:45) with their own turnover issue and also from among your peers like (33:52) and even Sao Paulo Pacheco and the international players can you talk about how you are seeing the competitive landscape in your traditional markets and also in the new markets and how is that playing out in terms of your expansion and margin and so on that's my question? Thank you.

A - Eugênio de Zagottis

Guilherme thanks for the question. This is a competitive market always was always will be but at the same time a rational market we don't see the irrational activity we don't see the predatory activity. I think over the last two years probably, the level of competition intensified with players like DPSP (34:38) for example entering the markets with other players maintaining strong growth programs. But we were able to assimilate that. We managed our portfolio of markets just like our investment managed portfolio of companies. So whenever you have a new entrant in the market, you may have an initial pressure, sometimes you have to reduce our margin to defend ourselves. But you can compensate in other markets I will give example, you have the markets in the South they used to be very tough markets in the beginning and now there are main markets and the margins has been growing up and up. So we are able to balance the portfolio in a way that we're defending ourselves we're doing whatever needs to be done, these defenses have been affective. But the numbers keep going up and even the next year after the new entrants, the new entry, we start seeing like normalized margins growing, growing up again and things like that.

I believe the crisis changes a lot of those things, I mean of course there players that has good financial capacity basically they don't need to change their plans, but we've not seen Brasil Pharma grow, we've not seen a lot of regional players grow, slow growing. And we have lot of players who are gaining on top of not growing, they're very vulnerable as Marcílio I think he defined it very well. When a competitor cuts people and cuts inventory, we add people and we add inventory and the numbers show what's happened. So we take advantage of the vulnerability of players who are leveraged.

I come from Raia, I know how tough it is to operate with leverage. I know that without leverage we wouldn't be here today, but it's not an easy life, and it's a life full of tradeoffs and we are now in the other side of the situation and we are really leveraging that. In terms of you mentioned specific players I think we see a lot of players with issues but you see a couple of players also doing well and maintaining normal lives. And we are increasing the number of people in the category management this help us out so not only defense but also to attack the market, okay, these guys work very, very closely to the operations guys but it's an opportunity to increase price or reduce price we have more competitive in some region. I don't know (37:09) and very healthy work, store-by-store, region-by-region within the competitive environment.

Q - Guilherme Assis {BIO 16143141 <GO>}

Okay, guys if you can just elaborate a little bit more on the international players specifically can you talk about how you are seeing like international players that are already like CVS (37:36) like from information that I have here that they are selling off some stores, on the (37:45) and also can you talk about if you are seeing any international players coming down to Brazil to look at the market and maybe give the depreciation of the BRL and you know if they are looking to making any move in to Brazil I have you see anything in how do you think they are looking at Brazil at the moment.

A - Eugênio de Zagottis

Well thank you Guilherme first of all the interest on global players is huge. That people are looking to Brazil and have been so far for quite some time we have huge respect for the global leaders they are leading operators in their market but in the end the capacity for global players to succeed in Brazil depends on what they are doing, what they are able to do locally. This is not a globalized market, this is a market with local formats, local regulation, local supply chain is very difficult or if not impossible to leverage a global supply chain, global brands.

So in the end I think a global player may be made well if he buys a strong asset and if he manages well the strong assets. The reality of this market is that this market has not been generous to new entrants when you look back in history. I will give a couple of examples. Farza (39:11) in the South of Brazil something like 10 years ago, complete disaster they got bankrupt in Brazil and they went out of the country. (39:22) bought Pharmalife de Mexico, huge disaster in negative, they sold it for nothing to Profarma. Brasil Pharma I think it goes without saying and the most recent news is farma (39:35) who belongs to Silazro (39:37), who belongs to Marchesa (39:37) who just announced the sale of their assets in Brazil.

So being a strong player outside of Brazil doesn't necessarily mean being a strong player in Brazil. We are ready for competition, we are working in doing our homework, we're investing in our format, we're investing in our strategies, we're investing our operational efficiency and to the end if the global provider strong asset manages it well to be a good player, but then it's the same stores we compete now it's the same brand we compete now. So there is doesn't represent much. For me, the thing that concerns me is to see a huge growth organic growth. Because organic growth will add capacity to the market. So you have a new players and when existing player enter new markets there is the result of being on pressure. We did well but the pressure is there. But just an existing assets changing hands this doesn't mean increased competition.

Q - Guilherme Assis {BIO 16143141 <GO>}

Okay. That's good insight. Thanking you Eûgenio.

A - Eugênio de Zagottis

Thank you.

Operator

. We go to Joseph Giordano from JPMorgan would like to make a question.

Q - Joseph Giordano {BIO 17751061 <GO>}

Hi good afternoon, everyone. Good afternoon Marcílio and Eugênio. First of all congratulations on the strong results. I have a question concerning the market weakness, like you did mention that several smaller competitors that are facing difficulties given the current macro. So I was wondering if you see any kind of assets similar to the Santa Marta operations, where you acquired the point of sales, so basically another shortcut to be scaled in a certain region. So that's my first question. Thank you.

A - Eugênio de Zagottis

Joseph, we receive a lot of offerings, we look at everything we are offered. We are always paying attention. Conceptually we will not be against doing something like Santa Marta again, but realistically, we see, we think it's very unlikely that a similar deal could happen. Most assets that we look we're absolutely not excited about the asset quality and I don't believe in buying a cash flow stream, if you don't, if you don't think the underlying asset is good, what it means is that that cash flow stream is negative, so it start, let me finish, that this cash flow stream may not be sustainable. So we have seen this time and time again, so we only buy things that we like and then we only buy things that we like and we think the price makes economic sense for us, so I would say buying a full asset that we had to integrate that's something that we are not ready to do. But buying a small asset that we could plug on, it's almost like an extend of organic growth, if it exists why not? But I don't think it will likely happen to be very frank.

Q - Joseph Giordano {BIO 17751061 <GO>}

All right, thank you, Eugênio. So, concerning the system, I guess like an integration basically about one year ago you completed the full rollout of the-like upgraded commercial system that is developed after merging the two companies. So, I wanted to know how the stage of the implementation of all the features particularly on the geographic brand in terms of pricing and loyalty card. Thank you.

A - Eugênio de Zagottis

We are concluding the rollout of the POS system in Drogasil probably August this year. So, we're very close to that.

A - Marcílio D'Amico Pousada

We had to take 211 stores Drogasil with the same people and hire alittle bit, okay, check our POS (43:29).

A - Eugênio de Zagottis

So the foundation is there, let's remember that we are ready, did a lot of things, so for example the pharmacy counter system that Drogasil uses is the same system as Raia and has been strong for since February last year. This itself is a huge advantage in terms of improving the process and in terms of having full visibility all the offers of generic substitution of pharmacy (44:02). It's a regular system and we followed a much better execution in Drogasil. We have been renovating the new stores and by the end of this year every store will be either renovated or born in the correct format. This is not a cosmetic intervention, many consumers don't even realize there is a renovation happening. It's a big functional change from the start. We are taking OTC from behind the counter into the transfer. We are opening up the store by removing a big check out island that we have and putting the check out to the side. We are removing diapers from the entrance of the store to the back of the store. So those things they translate to a lot of improvement and if you look into our comps in this quarter they were really good. The comps were identical for both lines.

A - Marcílio D'Amico Pousada

But I think the number one churn that we considered was (49:59) okay. The number is very, very important too that we have right now in Raia and we don't have in Drogasil and we are really believing 2016 can help us, how to manage the store and how to serve it better operating. We will have those a lot in the future. So the natural (45:17) enters automatically the pure season.

A - Eugênio de Zagottis

So those 200 stores will have already rolled out, were already rolled out in the system you see they already got the device for us to start managing the store in the same way we do with the Raia stores.

By the time also this rollout is done we were able to do CRM driven off the Drogasil. We don't want to do in an identical fashion to Raia. We want to use the same system and concept but to deliver value to the consumer in a different way otherwise it will be run back making the brands identical and we won't do that. So this is very long for us to decide and implement how we'll do it. But another thing is that as we enter with a new POS system, we got much more flexibility in generics prices especially in price (46:12). So Drogasil has seen tremendous benefits with the season growth in very good pace and there is still more to do at Drogasil. So this is one of the (46:24) for 2016.

Q - Joseph Giordano {BIO 17751061 <GO>}

Okay, thank you guys and also I would like, if you could comment on the Omni channel opportunity that Marcílio he usually comments on conference calls. I would like to know at the stage such initiatives, so how you leverage the large card and the online? Thank you.

A - Eugênio de Zagottis

Okay, we are looking for the Omni channel, a bigger percentage of that in future, okay, we finished the ERP for the e-commerce here in the beginning of the year okay which cover new, we are looking for a new platform right now. We believe we are working very well with this in 2016 to 2017 together with the loyalty card for, modeling card for Raia, I think all these new season in retail will be much better, much best only in 2016 not right now.

Q - Joseph Giordano {BIO 17751061 <GO>}

All right, thank you, Marcílio and Eugênio.

Operator

It appears there should be no further questions now I will turn the conference over back to the company for their final remarks.

A - Eugênio de Zagottis

Well, thank you very much for yours presence and for attending this conference. We started 2015 in a very strong note actually a huge leap in profitability which resulted from belief in execution and we also planted a very strong second quarter. We will have a price increase of pharmaceuticals north of 6%. We did a very strong forward buying. So, we have tremendous inventory to leverage. We have an amazing a very good phase trend in April that keeps that follows the trend set in the first quarter and we think it's likely to continue and the structural margin even the besides the price increase effect is also in very good shape. So, by any means you see a very strong second quarter. I would say this is already contracted. But the moment of truth will really be the second half of the year.

We did last year 7% EBITDA margin in the second semester. So, we have a huge comp base against which we have to perform. So, in our view where we'll be in the second semester is very important because it also sets a trend for the future. We're very optimistic, if we can maintain the great momentum in margins and in sales, I think we can do really well on the second semester but that cannot be taken for granted, it's not a given we have to keep working, we cannot be complacent and this will not happen automatically.

So, to finish I would like to point to the fact that this industry and this company has an amazing compounding capacity. So, by growing top line slightly below 20%, 17%, 18%, 19% by expanding margins – we don't expect to keep expanding margins 1% a year like we did last year. This would be another year of some margin expansion, the next year to be probably more modest that still even if you expand margins 10 bps, 20 bps to 30 bps per year when you put together with 17%, 18%, 19% top line growth the numbers will clean very fast and they compound very, very quickly so this is an industry that multiples don't capture the true value, because EBITDA number will be completely different in two to three years and the multiples shifts if the price is maintained very quickly.

So, if you look back in history at any moment you can think of whoever bought our shares and maintained it for two to three years made a ton of money and I don't think that will be any different in the future. So, we keep working, I think we are in a great shape right now. We are working in our future. We are really focusing our strategic agenda in terms of store openings in terms of new formats, in terms of management CRM, we are training people, sites, processes, platforms so there are few things done in Drogasil that will show which fruits we will collect in the future that is healthyso we remain very positive in the future and don't just be led by multiples. Thank you.

Operator

Thank you. Raia Drogasil's conference call is finished. Have a nice day.