FINAL

Bloomberg Transcript

Q3 2020 Earnings Call

Company Participants

- Ruy Kameyama, Chief Executive Officer

Other Participants

- Alex Ferraz
- Analyst
- Andre Mazini
- Bruno Mendonca
- Daniel Gasparete
- Gustavo Cambauva
- Jorel Guilloty

Presentation

Operator

Ladies and gentlemen, thank you for standing by. Welcome to BR Malls Conference Call to discuss results regarding the Third Quarter of 2020. Today with us are Mr.Ruy Kameyama, Mr.Frederico Villa and Mr.Derek Tang to discuss the results. We would like to inform that the participants attending the conference call will be in listen-only mode during the company's presentation. We will then open the question-and-answer session and further instructions will be provided. (Operator Instructions)

Before proceeding, we would like to clarify that any statements that may be made during this conference call regarding the company's business prospects, projections and operational and financial goals constitute beliefs and premises of BR Mall's management as well as information currently available to the company. Forward-looking statements are no guarantee of performance. They involve risks, uncertainties and assumptions since they depend on certain circumstances that may or may not occur.

Now, I would like to turn the call over to Mr.Ruy Kameyama. Please Mr.Kameyama you may proceed.

Ruy Kameyama {BIO 16672412 <GO>}

Good morning, everyone. Thank you for attending our 2020 third quarter earnings conference call. We will start the presentation on Slide number 2. Since August 8, 2020, all 31 malls in our portfolio have resumed with their operations and today their doors are open to the public again in spite of some restrictions on some activities. The quality, strength and breadth of our portfolio ensures that the processes of reopening our assets and recovering sales was structured and more solid.

Throughout the third quarter 2020, we will observe the consistent capital utilization of the opening hours of our malls. Until the second quarter, with our portfolio operating for only 30.5% of regular business hours and this percentage gradually evolved, reaching 45.7% in July, 64% in August and 74% in September. This scenario becomes even more positive when we look at the percentage recorded in October. That operated for 89.7% of its regular operating time.

On Slide 3, we present some indicators that show that despite the scenario restrictions in the operations of our assets, it's possible to observe a gradual and consistent evolution in these portfolio metrics. In April, our malls operated for the month only 1.5% of the operating time of 2019. And this percentage increased gradually. In October, it reached a value of 89.7%. This performance followed this improvement with assets as indicator progressing from a level in April from 19.4% of the value recorded and 2019 to 86.5% in October. These numbers show that with the reduction of restrictions, people are returning and consumption happening. When we compare the parking flow in the third quarter '20 with October, we observed an increase of 19 percentage points, up to the average of 65% in the third quarter to 74% in October.

Finally, time spent at the malls also improved significantly with 85.5% of the number presented in 2019, an increase of 11.3% when compared to the indicator given the same metrics in the third quarter 2020. In addition to this upward trend in sales, we show the strength of the assets and habits of consumers. On the following slide, we present the map of Brazil from two perspectives. The map on the left shows the percentage of households favored by the emergency aid offered by the Federal government and on the right the map containing the same store sales performance in the BR Malls' portfolio.

When analyzing the share of households that were favored by this aid in individual regions, it's possible to notice that the northeast region had greater reach of benefits. However when we compare the same store sales data of BR Malls for the portfolio by region, we notice that north and northeast were the ones that reported the best results.

On the other hand, south region was the one where the households received less aid in percentage terms and at the same time, it was the one that presented the worst assessed performance in the quarter. Finally, in the Southeast, and Midwest regions, around 40% of households received assistance and both had about 34% reduction in the same-store sales levels when compared to the previous year. Although in the short term the north and Northeast regions have some greater resilience due to the aid, we cannot guarantee that this will remain in 2021. We know that we have very diversified portfolio and making a new profile increase our exposure to dominant of properties that we call tier one and two. And the geographic distribution is much better.

On Slide 5, we show the monthly performance for March through September of the number of commercial proposals received compared to the same period of 2019 ex sales. We were able to see a constant recovery in the leasing activity with a number of new leases proposals received by the company returning to pre-crisis levels. When analyzing the consolidated figures of the third quarter, and the (inaudible) variation was minus 8.4%. However we recorded a gradual growth month over month until in September when the variation became positive. In addition, 104 proposals were executed this month, a record number of signatures in ex sales since October 2018. This line will also show important brands with which we signed contracts in addition to relevant names of segments that became stronger in the current situation such as iPlace, Camicado, (inaudible) Pacheco.

We also noticed that demand coming from branded segment were hit harder during the pandemic, such as Mamma Jama and TT Burger in the food segment, Foxton, Levi's and Arezzo in the apparel and footwear segment. Despite the challenging scenario, the company was able to continue strengthening strategy segment and further boost the segment that have gained relevance in the current context.

On Slide 6, we present some operational indicators for the third quarter. Those figures are the core portfolio of the company decreased by 34.8%, a total of BRL2.9 billion in the third quarter. However when compared to value of total sales of the second quarter, we recorded a growth of 277% in sales. Same-store sales decrease by 32.6% in the quarter. When we compare to indicator of same store sales of the second quarter, we have an increase of 38.5%. The occupancy rates reach 95.5%, showing the strong demand for our shopping malls.

In the release, we have broken down information on a monthly basis and we see that August was an important point to be studied in terms of occupancy rate.

The occupancy cost reached 10.5% in the quarter with a reduction of 0.4 p.p. when compared to the third quarter 2019 and 14.02 p.p. when compared to the second quarter. The preservation of the occupancy level and the reduction of the occupancy cost of tenants showed a strategy that we have adopted in the past few years with the strengthening of the mix, the recycling of the portfolio and the development of solutions, digital solutions to enhance the performance of retailers.

On Slide 7 we show the evolution of the delinquency rate of the company and PBD expenses. Regarding to net late payments, we saw an increase of 4.1 pp compared to the second quarter. And in the release, we provide more information. So it's nearly 4% in August and September. With the reopening of our malls and the improvement of the tenants' credit risk, we evaluated the provision metrics again in total on the third quarter, BRL27.8 million in the constitution of the PBD. Out of this amount, BRL11.3 million resulted from the increase in the overdue receivable, while BRL16.5 million was due to the increase in payable receivables. That is due to in anticipation of the fact that the provisions for expected losses from tenants. It's important to highlight that out of the 71% of the total provision, they've referred to -- doubtful accounts refer to overdue receivables.

On Slide 8, we present the main performance of our financial indicators. There was reduction -- 34.9% reduction in net revenues, a total of BRL207.8 million and a reduction of 35.6% in the NOI of the quarter in ex-sales, a total of BRL183.7 million. Adjusted EBIT reached had a reduction of 51%, considering the third quarter of last year in ex sales and an increase of 138% when compared to the second quarter this year. Our total adjusted totaled BRL45.9 million, a decrease of 76% in the quarter when compared to the same period of the previous year. When we compare to the second quarter of this year, AFFO increased by 151.7%.

On Slide 9, we present some data regarding our parent's capital structure. We ended the quarter with a strong cash position, BRL930 million, 25.7% higher when compared to the position in the third quarter of last year. The coverage ratio recorded in the period was 3.3x. That demonstrated our commitment to the payment of financial expenses. The leverage indicator returned to levels experienced before the crisis, reaching 3.9 for 2020 and 2021. The company's totals, respectively, BRL33 million and BRL266 million in debt amortization, which shows that we have no relevant obligations for the next two years.

In addition, we have a clear strategy of renegotiating debt and extending the amortization schedule in order to maintain the strength and solidity of our balance sheet. Therefore, as the sequence of events of the third quarter, we renegotiated CCB Itau debt, changing final maturation from March 2020 to October 2025, with the change of the CDI rate of 1.82% per year to CDI plus 2.23% per year. Fitch agency reaffirmed the BR Malls' national rating at AAA, showing the robust capital structure and the maintenance of a solid liquidity position.

On Slide 10, we show the evolution of our digital initiatives. During the second and third quarter, we managed to expand the presence of the integration and the delivery centers, logistics hubs to more than 12 malls. In October, we opened 3 more hubs in the portfolio. And by the end of the year, we will open 3 other hubs, complementing all the 26 malls managed by BR Malls to accelerate the expansion of new delivery center units to new cities and improve the operations technology, and we made a new investment in October in the amount of BRL9 million. In August, the company signed through the delivery center, a partnership with Google, reinforcing the expansion of one-stop to sell strategy of the company. With that, today BR Malls' tenants integrate in the delivery center are integrated to different marketplaces such as Google, B2W and BR Malls.

Regarding our own marketplaces, in October, it grew by 830% in sales when compared to the last three months, and our results represented the total online sales of the delivery center and 25% of the sales online in the Goods segment. In addition, we increased the SKU base by 165% after designing an acceleration plan with short term, short and medium-term gains. This shows the importance of our strategy. We have noticed the preference of our tenants according to the availability of those new solutions.

Now moving on to Slide 11, we presented the reopening after the third quarter 2020. Although we have postponed our planned investments and postponed the opening of retrofitting and expansion project due to the COVID-19 pandemic, we maintained investments in the retrofitting projects that were in their final stage. With this, important in operations to strengthen our portfolio are the following: Norteshopping taste lab in Rio de Janeiro is a gastronomic space that harmonizes several regional flavors, providing a unique and differentiated experience for our customers. Even in challenging scenario, of course the space was 100% sold and has 22 gastronomy operations, including relevant names such as TT Burger, Grand Gru, and Katmandu.

The second one is the pet shop of the Mooca Plaza in Sao Paulo. It's an integration took place November 8 and reinforces the positioning of pet friendly, which is part of this structure of the company to receive our customers in the best possible way. It has a pet park, a place that allowed consumers to interact with their animals and enjoy pet shop services. With the pet square, it will also be possible for customers to stay close to the animals at meal times.

On Slide 12, we show the construct construction potential of the core portfolio. Based on internal studies, the company estimates that it has an area with potential to expand its own GLA of 212,000 square meters with a private area of 454,000 square meters. BR aims to accelerate studies and development of multi-purpose projects to gain synergies for our shopping centers and creating shareholder value. We inaugurated the commercial tower at the shopping center Campo Grande, and we expect to open the second tower in the third quarter '22.

A key delivery to diverse tower happen on the 20th of August and the building has 25 stores comprising commercial rooms measuring 42 to 395 square meters. We expect to open Bourbon Hotel at shopping Catuai Maringa. The hotel will have 14 floors containing 120 apartments and this will be the best hotel in the region. In the long run, we believe that the fundamentals of our business will remain unchanged, and our malls will remain the destinations sought by major retailers and consumers. On the following slide, we show our main objectives and the value of BR Malls in short and long term.

BRML3 share end the third quarter of '20 -- approximately finished 42% lower than the closing amount in the third quarter 2019. When compared to the equity value, the market value showed an upside effect of 67% [ph] when compared to the fair value. It showed an upside of 130% at the end of the third quarter 2020. Operationally, we remain focused on resuming activities. And the strategy of the company in the past 3 years is to show more than ever how important this is. Today, we manage to consolidate the qualified portfolio consistent with a robust balance that provides us with peace of mind to go through this period. In the long run, our fundamentals will remain unchanged. We are confident that shopping malls will continue to be the best option for retailers in Brazil.

And the consumers and tenants will be even more selective, opting for assets that have excellent performance and offer new solutions. This is sustained by people. We are working hard to consolidate the culture of the company with attributes of long-term cooperation and provide more attention to or clients. These values are extremely important in a challenging scenario like this, which requires an ability to adapt quickly to changes. And today, we are happy to have built such a company with a young and entrepreneurial team. We close here our presentation and we're available for any questions that you might have.

Questions And Answers

Operator

(Question And Answer)

We will now begin the Q&A session. (Operator Instructions) Our first question comes from Mr.Gustavo Cambauva with BTG Pactual. You may proceed sir.

Q - Gustavo Cambauva {BIO 17329406 <GO>}

Hello. Good morning, everyone. I would like to ask two questions. The first one is related to the third quarter and we see the mismatch of same-store sales. What computation is the differential of the anchor shops because the same-store sales was better, but in-store rent was worse. I would like to understand if this is related somehow to some negotiation that was harder for you, maybe you had with some specific tenant or was it more focused on some specific segments? I would like to understand what was at play here or if you see any harder pressure of those companies who have more power of bargaining during negotiation, maybe forcing prices down since the malls were closed for period?

And my second question is related to PBD that was very high, and you commented that you were provisioning for those tenants who hadn't even been able to pay the condominium. So now when I look at this quarter, I can see the recovery level. And I would like to understand how this happened. Why did this happen? So how do you see this in the future and how do you see the PBD behaving for the future? Thank you.

A - Ruy Kameyama {BIO 16672412 <GO>}

Cambauva, thank you very much for your questions. The first question is related to the performance of the anchor tenants in terms of rent and the differences as I said rent. You see that the major tenants are recovering in a consistent manner. You can also see that the performance is better than the satellite stores somehow. And what we note is that somehow they are facing good moment if they are capitalized their recovery and we don't see any major concerns. I believe that negotiations have been as usual.

And what we notice is that there is difficulty in the movie theaters that can influence in the distribution of rents. Movie theaters have restrictions for their openings, and we are waiting for the blockbusters, movies, and the studios are holding them back for better moments. So we see many segments recovery in terms of sales and a demand for major companies and in general, they are facing a moment in which they are very well or solidly capitalized and they are also accessing the capital market as (inaudible) and follow on there, even strengthening their debt balance. We see that this movement by those major tenants.

So this wouldn't be a concern for us. It may be something that happens a mismatch that happened temporarily. And we understand that the demand is very high for other areas for them to catch up. In terms of PBD, in the second quarter, as you already pointed out considering all scenarios, we adopted a more conservative attitude. In the third quarter, we even provided information in the release, we talked about all the breakdowns and information or the receivables of overdue receivables that we know that the criteria is a bit different from other companies. And we made it clear that we wanted to show this to you in case you wanted to make the right comparison apple-to-apple for example.

So in order to try to understand what's ahead of us, we have to understand what is happening in in the moment with mathematical correlation between default rate and net default rate and provisions. And what we see, and we broke down those intimation to the level of net late payments month by month, we can see that in the past two months, the level has reduced quite a lot. We had in July, we reached 10%, and now in August and September, we are at 4%, and this is about the level we had in October. And this is going to provide us with the predictability so that we can recover the credits, which -- and part of those provisions can be reverted to the company or reverse to the company.

Q - Gustavo Cambauva {BIO 17329406 <GO>}

Okay. Thank you. Have a good day.

A - Ruy Kameyama {BIO 16672412 <GO>}

Okay. Thank you. Next questions.

Operator

Next question is from Alex Ferraz with Itau BBA. You may proceed, sir.

Q - Alex Ferraz {BIO 19294308 <GO>}

Good morning. Thank you very much for the presentationI have a question related to the breakdown of performance by region. And we look at -- when we look at October and a little bit of what's happening this month, do you see any difference in the North and Northeast region in relation to the reduction in the payment of the aid by the government as of October? And the second question is more related to the expense specification. I think you've been talking a lot lately about retrofitting, and we understand that the projects have been postponed. And do you believe we will go back to this initiative or was it something just for talking about the potential of those retrofitting project?

A - Ruy Kameyama {BIO 16672412 <GO>}

I understand. Alex, thank you very much for your questions. As to the regional-related questions, we have received many questions, and this is why we opened all those pieces of information. Specifically, you asked about October, how we would see. And if we saw the same trend or if the difference was big. I think it's very similar in terms of distribution. Maybe the difference is that (inaudible) shopping mall in the beginning of the third quarter, it was not in operation, and since it's so important in the sales levels of the company, it pushed the results a little bit down in the Northeast region when we considered October (inaudible) shopping mall was already operating normally in relation to the other malls of the portfolio. So naturally this helps us a little when we try to understand this metric. We did not notice a major change in relation to the general distribution, the result or the reduction of the provisions of the emergency aid.

As to the construction potential, we provided the disclosure because we wanted to talk about retention because this is part of the strategy and we also have to use the multi-purpose potential. Sometimes when we see the malls as with the strength of retail but our shopping malls go beyond that. We see that the really safe categories are accelerating and some are holding back. And this construction potential -- effort is important because we identify them by the opportunity by means of the multipurpose.

In Campo Grande, the best tower, business tower and it's connected to the shopping mall and there's also the hotel in Maringa. It's -- we are just waiting for the right moment to open it, but this is going to be the best hotel in Maringa and it is going to be connected to the mall. We look at expansion in the medium and long term, yes. These multipurpose projects were already underway. This is part of the strategy that strengthened the shopping malls in certain synergy of traffic and sales and we have potential to be used in the years to come.

Q - Alex Ferraz {BIO 19294308 <GO>}

Okay, Ruy. Thank you.

A - Ruy Kameyama {BIO 16672412 <GO>}

Thank you Alex.

Operator

Our next question is from Andre Mazini with Citibank. You may proceed sir.

Q - Andre Mazini {BIO 20818108 <GO>}

Hello Ruy. Thank you for the call. First is a follow up on the multipurpose use in Campo Grande and the hotel. In Campo Grande, you developed together with construction company range, how is this going to be monetized? Is in the group is in the balance of your malls? Will you include investors or is it in the balance of the construction company and how was this monetization and will there be any standard in the monetization of the land bank that you opened, which is quite expensive?

And the second question is related to the commercial proposal. In September, the number is very good, better than September last year, and we also broke down by segment. I would like to understand that basically old segments do not -- you even included full segment which was surprising to me because there is casual dining and other tenant types. Are they safe to open their businesses now or is it more related to takeout food? We are afraid of the second wave of the virus. I just would like to understand the new commercial proposals. I don't know how much you can disclose in terms of information, but how about spread and prices? Thank you.

A - Ruy Kameyama {BIO 16672412 <GO>}

Mazini, thank you very much for your question. As to multi-purpose in the Campo Grande tower and Maringa Hotel, these were cases when we negotiated a swap operation with the counterparts, and we chose the partners after we understood what was the best product to complement our assets.

In Campo Grande, it was (inaudible) as you mentioned and in Maringa, the hotel will be operated by -- by some investors as owners of the property. They have a negotiator. They have been recorded in the balance of BR Mall, so they have already entered our balance sheet. And when we look ahead, we are going to continue looking for the best partner. What would be the product that would best complement our project in terms of synergy and positioning at use, and we choose a large number tied with the commercial type, residential area. We try to understand the needs region by region, mall by mall, and after the negotiation, we focus on the specific aspects to see what would be the best capital allocation and what would be the best kind of risk return that we can have considering each of the negotiations. And we always try to find the best partner for that specific region.

As to leasing, we accelerated quite a lot in the past few months, and this is due to a number of assets. First, we made a very important improvement in our portfolio over the last years. We have a more homogeneous consistent portfolio, and this makes our negotiations much easier. In the past, we had more fragile assets and this used to make the negotiations harder, and we have a portfolio that is sought by the tenants, making easier for us to negotiate. And in spite of all the COVID-19 scenario and the cost reduction pressure, there we have the largest commercial team in the area of key account is very significant. So we can provide very good service brand by brand. We understand this is one of our advantages, competitive edges, differentiators.

And we consider all this scenario, we understand that we are undergoing temporary moment and seems we go back to normal. We understand that the combination of the capacity of merchant execution in a stronger portfolio. And the new digital solution, all of this is perceived by the tenant and they understand how this is going to play out in the years to come.

I believe that we are being favored by interest rates, link rate, which is helping us and pushes finance to consider to reach or to develop some fuels. And this has an impact both for our 10 stores and for franchisees. In the franchise market, we've never seen such a good situation. So we've been able to capture this demand in a very effective manner. And we brought some examples of different segments, fashion, services or household items. So we have been able to capture this major demand. And this is, for us, is quite a journey. We have our business. It's a long-term business.

Of course, when you are looking at each quarter, but we have to ensure that we are on the right track, capturing the right movements for the long term, maintaining the malls' mix. The make it attractive updated and keeping the occupancy rate high, late payments, rate low. And this is the business cycle. So we bring more information in this regard so that you can understand how we negotiate the leasing.

Specifically related to restaurants since you raised this point, what is happening is we have to think of restaurants as a whole. But if you think about restaurants inside the malls, they offer some advantages. Naturally the advantage is that they are within a planned mix. And next brand of restaurants would attract a shared consumer, and they will attract the consumers to other shops considering all this and the tenants are understanding -- beginning to understand that the digital solutions help a lot when they operate inside our malls, they understand that they are going to be working in different segments.

So all the apps, the Google Food and other marketplaces that will be available, considering that needs of the current were food. And we also look after the logistics because it certainly should integrate it. So if when you think, I have the capacity to invest in another deli, where am I going to invest? Am I going to invest on the street, on the street store, on any mall or on our BR Malls. Why? They will consider gain consideration of all those factors. We understand that food segment is going through difficult moments, but we are taking advantage of all the solutions, and we are managing to bring in the right brands to our malls.

And we have had successful examples such as the greenfield integrated in -- and that became the main attraction for the shopping mall. It makes that was developed by us, the commercialization, the management is very different from the traditional fast food and it's a model that has been consolidated. And the not shopping, even during the pandemic, we had 100% of the units sold. And we are opening it 100% sold and with TT Burger and many other brands that we have already mentioned. And this shows that even doing endemic when we manage to do the right job, considering the project, the positioning that we can understand the trends of the consumers and it through the digital solutions, and we are going to offer the integrated delivery service.

Of course, this creates value to the tenants and brings about attractiveness, a demand that is converted in a more resilient occupancy rate that resists to difficult times. And it's translated into higher rent. We used to have a major concern in the beginning of the COVID-19 pandemic of the adjustment of prices. But because the occupancy rate exceeds 95%, this was a turning point.

If we look month by month, we see downward trend. And in the last months, we have stabilized and started growing. We grew a little bit in the month of September, and there was an improvement in October as well in terms of occupancy rate. So it's been two months since we started to grow. So tenants are beginning to look after us since we see those good perspectives. Then the assets are also bettering our portfolio, we're offering digital solutions that increase the potential of sales of those tenants. As we only say this is the law of offer and demand. We have growing demand and with low offer. So the spread is marginally positive, it's not negative, and we believe that when we look ahead as the demand grows, you can see during that COVID scenario, we will be normalized. We expect this spread to go back to a positive and healthy level.

Q - Andre Mazini {BIO 20818108 <GO>}

Okay, perfect. Very clear.

A - Ruy Kameyama {BIO 16672412 <GO>}

So the value of proposal for the restaurants, if I understood correctly and summarizing, they will have a healthy team and a physical point of sales. So we are prepared to operate in different channels.

Q - Andre Mazini {BIO 20818108 <GO>}

Okay. Thank you. That was my question.

A - Ruy Kameyama {BIO 16672412 <GO>}

Yeah. The proposal of value is the integration solution. Yes, just to add the segment will continue to sell, selling as it needs what we will push the tenant in different marketplaces so that the tenants can capture more sales and the integration solution with the next mile because the motor cycle, the couriers will be there near, and we will make the delivery quite quick. The difference is it's not in their kitchen or cloud kitchen which is separate. They will use the facilities of the tenants' own restaurants in order to optimize labor and activities will count on this demand and it will optimize the cost and the labor in the local operation.

Q - Andre Mazini {BIO 20818108 <GO>}

Okay, perfect. Thank you.

Operator

Thanks you. Next question is from Daniel Gasparete with Credit Suisse. You may proceed, sir.

Q - Daniel Gasparete {BIO 17999254 <GO>}

Good morning, thank you very much for taking the question I would like to understand the discount. I would like to understand how you see the process of removing the discount? And what about vacancy, do you think there will be any change in asset in crises or do you believe that demand will continue to be very high?

A - Ruy Kameyama {BIO 16672412 <GO>}

Gasparete, thank you for your questions. As to removing the discount and this is something that's happening gradually in a very careful manner. On the one hand, we noted is that there is an increase in sales and this higher as we advertised (inaudible) has also increased, and we see that the tenants are making effort. They are at a moment when things are better, but specifically compared to last year, and compared to the shortage impacts in the second quarter. So we have been very assertive when we remove the discount. And you try to understand them on a case-by-case basis, and we consider the operator, the quality of the asset.

So we are in the middle of the long-term gain and we understand that we have to have the best brand with the best operators. We have already helped them for many months with discounts and assistance and we are likely to be removing those discounts, and this is the guidelines, and this is what's happening. We have high sensitivity. We are looking into the long-term so that we can preserve the fundamentals of our business. The right brands, the optimum mix, and we recognize that it's very important to have the right operators and the right brands. So every month, we will remove the discounts since they have better capacity of sales and payments. So we believe that this is going to be normalize in the future months.

As to vacancy rate, this is something complicated with which I commented in question. These are all aspects that increase the attractiveness of our malls. We had one of the highest occupancy rates compared to the market. And we see that late payment rate is very low. And with a high occupancy rate with a high-capacity of leading negotiations so when we consider this composition, we understand that there is a seasonality level and this is characteristic of our business. However, considering all those factors, we believe that we are going to be able to improve and to make the controls, all the vacancy levels in the first quarter and make the necessary improvements in the second and third quarters on.

So we have a expectation of the vaccine for next year. So when we think of our business in the next quarters and the next year, we have no doubt. We are doing a preserve or correct mix. We're going to continue have a very good relationship with the brands applying introducing digital solutions. This will help us gain more share and will help us to maintain very high occupancy rate and helping the business of the organization.

Q - Daniel Gasparete {BIO 17999254 <GO>}

Okay, Ruy. Thank you very much. Thank you, guys.

Operator

Next question comes from Bruno with Santander. You may proceed.

Q - Bruno Mendonca {BIO 16313094 <GO>}

Good morning. Most of my questions are being answered. I have question related to digital initiative. The shopping you made to have those implemented. How do you see Sao Paulo and Rio de Janeiro? Is there -- do they have this in other places? There is -- people do not have the habit to buy from apps. Could you provide some information related to this?

A - Ruy Kameyama {BIO 16672412 <GO>}

Thank you very much for your question. This is a topic that became ever more important. We have been working on this for three years now and we had higher integration with the malls is the potential of the malls to meet the demands of e-commerce next mile and this has increased a very high speed. And during the pandemic, we saw how important this is, and we are going to roll out the solution, as you mentioned, to other units. So until the end of the year, our shopping mall, do have the solution. We started from Rio and Sao Paulo because these are regions where we were closer to. I think we understand the brands in a way and even the market place penetration was also deeper and now we're going to expand this into other regions.

We have redesigns in Goiania and Parana mall just started this month, and this has been a very positive surprise. It's not really a surprise in a way because we expected this to happen, but we see that this has been materialized. When we think about e-commerce in the mall, the delivery path is more than seven days. So the user experience is very frustrating. And when you consider the penetration level region by region, Sao Paulo is record higher levels than the rest of Brazil.

So Sao Paulo is a leader of penetration and the southeast come following suit. And we see that there's logistics (inaudible) in Brazil, and the penetration is very low. But when you get to those regions, then you can offer a solution, which can be same-day deliveries when their experience of delivery will take seven days. This will generate a very positive experience and a higher level of recurrence considering the traditional e-commerce that consumers used to. This is important to also in malls, but we believe that in the regions where the traditional marketplace did not provide satisfactory service it will be very interesting to be there considering how quickly we can make all deliveries. I believe this is something to consider.

As to food segments, considering we already have this service consolidated with the main network, the main change. And we understand that this has also to have the improvement of the sellers. So the value proposition is very consistent, both for sellers and for buyers outside Rio and Sao Paulo region, it's much more compelling. So we have this potential to reach high level of increased demand of consumers, but considering that the provision, the value is high. We are going to accelerate all those levels.

Q - Bruno Mendonca {BIO 16313094 <GO>}

Another question and look at your e-commerce, in relation to how you're going to charge the rent in the situation normal. What kind of the way of charging the rent? Could you provide some color on this and how we calculate sales from same store?

A - Ruy Kameyama {BIO 16672412 <GO>}

It's something that we have been talking in only recently. In the long term it's very important as those brands and we are all still learning how this operates and in principle, the way we understand it is that it's a sale that is coming from the shopping mall. It's originated and fulfilled by the shopping mall using the mall structure. So far, we have been calculating this in integrated from both the sale and rent. We are testing the model. We have to develop an equation that can work out for everyone in long term. So we want the e-commerce to happen through the mall, and together with the tenants, we'll understand how this value chain operates. And what is the value share for everyone.

I believe that this is so new and this is something that's going to be vetted more deeply in the months to come. And maybe years in future years. What is important is that in Brazil, we have recognized the future winning model is omnichannel. The make winners, the ones who have stood out in the market place. So we have to consider the on/off combination. It's a winning model and by means of all the strategies adopted by those who are in this direction will understand what's important from the operational viewpoint, from the logistics viewpoint. How we can make this easier.

What is very clear for us is that as we used our scale to help the tenants to execute to the omnichannel strategy. Obviously, we are going to create value to the tenant at the local at the regional level and creating this collaborative value, we can try to understand how we are going to reach upon when we are going to come to a consensus.

Q - Bruno Mendonca {BIO 16313094 <GO>}

Okay, thank you. That's it from me.

Operator

Next question Jorel with Morgan Stanley.

Q - Jorel Guilloty {BIO 18291521 <GO>}

Good morning. Thank you very much for taking my questions. First of all, as a comment generally speaking in the south and the southeast region I asking this because it's been three to six months that we have been operating below capacity and do you believe that the end of year sales can help? And if this can limit and can increase the default rate because it's a trend after Christmas? So my question as to your commercial strategy. The strategy in terms of the date of the rents would be more focused on having new tenants or renewing agreements, and we believe that your strategy is to improve the mix of logistics of the tenants or to reach tenants with higher capacity to pay rent.

A - Ruy Kameyama {BIO 16672412 <GO>}

Jorel, thank you for your question. The first question, you asked about the financial health of the payment. We do not see a regional difference among them. We don't see differences when we compare Brazil as a whole. And we have had lots of surprises because a number of reasons, of course, is by the efforts that we have made. Thinking of the rent extensions during this time when the stores were close. Reduction of condominium costs, reducing all the possible costs, we could remove the burden from them. We have a leading role to provide them with more breadth for them to go through the most difficult time. So it was a planned strategy because we wanted to preserve our business in the long term.

We thought about what is the value. The value is more connected to the long-term traffic than one or two months of sector size. So it was a strategy that was well thought about how those small tenants when they were facing more difficulties because we were aware that they would have the capacity to recover, they need some other tools.

Other tools have emerged in the past month and weeks. I'll give you some examples. The government -- financing of the government for MG. This has provided some strength to those mall tenants. The government has also created some credit lines together with the bank. They took some while to be granted but they finally arrived, and they have some tenants have access to working capital. So I believe that the government took a while, but it managed to provide some resistance to those tenants and the federal government also subsidize the capital resources. And this has helped to us in this fiscal time. Our third sector is the industry itself. It helps those mall tenants. The mall health, government also provided help and the production team has helped a lot from the franchisers thinking about royalty rates to help those who are in the other end and also suppliers operating in the industry.

Maybe payments earn and discount those mall tenants, or those mall retailers would positively subsidize their production change, so this combination of factors together with perspective of redemption. When you see that, it suffered a lot, there's an improvement every month. So you feel like (inaudible) in the operation, different from when you don't see any light at the end of the term at the end of the tunnel. The last and major recession, you had some much uncertainty that you would simply give up if you are not able to pay your debt. So what we see is something different. They understand that this credit system is coming from different sources, maybe as working capital or maybe with some loans.

I think, Jorel, the health of small retailers is very healthy, those who are in our core portfolio. The net late payment rate is at a level which is controlled; those for the quarter or need to consider month-over-month results. In Brazil, in spite of the fact that we have retailers or individual corporate tax payers, most of them are franchisers. And the franchising area has been improving to be quite resilient. Andre, who is the President of BF, said that the market of each of those franchise, it's the second largest market of franchise in the world. And in the beginning of the COVID pandemic, they thought that this base would be excluded by 10%. But it's materializing only 2%. So when we remove the anchors, we understand they are very, very well capitalized, they are solid.

And we see that when we considered the franchisee, we see that the mortality rate was much lower than we expected in the beginning, and now we have this working capital and funding lines and this will help more. This was a combination that was not very clear in the beginning of the pandemic, and we see that this is a very important combination. And with the perspective of having new solutions and the improvement in the malls will help them to stay on the job and paying their debt on schedule.

As to the commercial strategy, I believe it reflects a little bit of what we are saying in order to continue -- we're going to continue going after the best operators and the best brands. This is a crucial for the fundamentals of malls in the long term. BR Malls did a very good job of change in the profile. We sold the non-core assets that we believe wouldn't help us in the long term and we replaced them in the logistics mix. So we had several quarters of high late payment rates and we re-commercialized or renegotiated with the correct concept. So in the beginning of the crisis, we had the right portfolio, the right mix with zero default rate and highest occupation rate of the last five or six years. And this is what we saw in the beginning of the year. We had done our homework before, and there came COVID and hurt everyone.

So our commercial strategy is to help the right brands, brands who are already operating at the mall so our top priority is to preserve the mix, help with tenants who have been our partners for the long term. And if we have no condition is the brand does not make any sense anymore, if they are having problems with a mother brand or if they decapitalize and they are in no way they can stay in the business. And then only then, we are going to replace them. So we are going -- we are working hard. We are working in an active way, and we have a pipeline of assets that can enter our portfolio.

Q - Jorel Guilloty {BIO 18291521 <GO>}

Okay that's clear. Thank you.

A - Ruy Kameyama {BIO 16672412 <GO>}

Thank you Jorel.

Operator

The next question is Jonathan (inaudible) with JP Morgan.

Q - Analyst

Good morning. Thank you very much for taking my questions and my first question is (Technical Difficulty). I would like to understand the metrics.

A - Ruy Kameyama {BIO 16672412 <GO>}

Hi Jonathan. Thank you very much for your question. The covenant topic is not something that concerns us. As you have seen in the last pieces of information, the operational results have been better, ever better in terms of better provisions and level of revenues. We have been working in a very certain way to reduce costs. So this is something that does not concern us. The shock we are not worried. There's not much we can talk about the covenants.

Q - Analyst

Okay. Thank you.

Operator

There are no further question. We'll turn the call back to the speakers for their final comments.

A - Ruy Kameyama {BIO 16672412 <GO>}

Thank you all for attending our conference call. Derek, Freddie and I are currently available. Good morning, and have a good day.

Operator

The BR Malls conference has come to an end. We would like to thank for everyone's participation and for the interest.