

Q3 2016 Earnings Call

Company Participants

- Fabio da Silva Abrate, Chief Financial Officer and Investor Relations Officer

Other Participants

- Franco Abelardo, Analyst
- Guilherme Assis, Analyst
- Irma Sgarz, Analyst
- Joao Mamede, Analyst
- Joseph Giordano, Analyst
- Paola Mello, Analyst
- Tobias Stingelin, Analyst

Presentation

Operator

Good afternoon and thank you for waiting. Welcome to the B2W Companhia Digital Conference Call to discuss the Earnings of the Third Quarter of 2016.

Today we have with us Mr. Fabio Abrate, CFO and IRO of B2W; and Mr. Luiz Saraiva, CFO Lojas Americanas.

Please use the supporting presentation to follow this conference call, available at www.b2wdigital.com. We would like to inform you that this event is being recorded, and all participants are in listen-only mode during the Company presentation. Then we will begin the Q&A session, for which instructions will be given. (Operator instructions.) The replay of this event will be available at the end of the call for one week.

Before we proceed, we would like to clarify that any potential statements made during this conference call related to B2W business perspective, operating and financial goals, and projections are based on the beliefs and assumptions of Company management, as well as information currently available.

Such considerations are not guarantees of performance. They involve risks, uncertainties, and assumptions as they refer to future events, and therefore depend on circumstances that may or may not occur. Investors must understand that the overall market conditions, industry conditions, and other operating factors could affect the future performance of B2W Digital and could lead to results that materially differ from those expressed in such future considerations.

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Now we would like to hand over to our speaker who will begin the presentation. Mr. Abrate, please proceed.

Fabio da Silva Abrate {BIO 17940993 <GO>}

Good afternoon, ladies and gentlemen. I would like to thank everyone for taking part in this conference call.

Throughout the presentation, we will talk about the earnings for 3Q '16, the operating highlights, and investments made. After the presentation, we will hold a Q&A session.

I'd like to begin on slide 3, where we highlight the evolution of the main indicators of 3Q '16. Total GMV achieved BRL3.1 billion, up by 15.8%. Marketplace is still quickly developing, growing 117% and achieving BRL571 million GMV, a share of 18.7% of the total GMV, an increment of 8.7 percentage points year-over-year. In the past 12 months, marketplace grew 203%, achieving BRL1.7 billion GMV.

In 3Q '16, B2W has intensified its growth, the evolution observed month by month throughout the year. It makes us feel very optimistic about the fourth quarter, especially for Black Friday, the most expected event of the year.

In the 2015 edition we sold over BRL1 billion, with a share of 40% of this event. The platform is ready, and our team is very excited to establish a new sales record in 2016.

Now moving on to slide 4, I will detail the evolution of B2W market share. As a result of the investments made in the past years, B2W market share has increased 7.2 percentage points, going from 19.9% in the first half of 2012 to 27.1% in 3Q '16. With that, the distance of B2W to the second player in that period has increased 2.9 percentage points over to 13.2 percentage points.

On slide 5, we'll talk about the evolution of our value generation cycle. The best purchasing experience that customers have is a result of excellence in operations and commercial variable management. Sales success depends on many factors, such as having the right assortment that customers need, the right inventory levels, good payment terms, and good delivery.

The B2W brands have the largest and most qualified traffic in Brazilian e-commerce, attracting more and more sellers to the platform, increasing the assortment and number of offers, which consequently attracts more and more customers and generates a virtual cycle.

In traffic, we increased 28% in 3Q '16. Throughout the year, we've connected over 1,900 sellers to the platform, increasing the assortment 127%, and resulting in achieving 375,000 new customers.

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On slide 6, we can see the quick development of marketplace. As seen in the previous slide, marketplace has added over 1,900 sellers throughout the nine first months of 2016, leaving a base of 2,500 sellers at the end of 2015, moving on to over 4,400 sellers on September 30, 2016.

In the past 12 months, marketplace has presented a strong performance, growing 2.8 fold in relation to the same period last year, achieving BRL1.7 billion of GMV. In 3Q '16, marketplace achieved a share of 18.7% of the total GMV, a growth of 8.7 percentage points year-over-year.

On slide 7, we would like to highlight the new partnerships of marketplace. In line with B2W's strategy to integrate new stores of many different sizes and different industries, B2W marketplace has closed a partnership with important stores such as Ricardo Eletro, which has an assortment of appliances, electronics, and variety; Dell, IT and technology; Britania devices; Philco electronics; and Mahogany, cosmetics and perfumery.

Additionally, to continue to grow marketplace in an expedited manner, a new platform was launched which is focused on smaller sellers that sell a large variety of products, and therefore improving and increasing the assortment of B2W sites. After concluding registration and validating the sellers' main data, they can upload their products through an exclusive portal without having to integrate systems, where they can also manage all the stages of their sale.

On this new portal, we will continue to be very strict in selecting our sellers, as the reputation and quality of our partners are very important factors for assessment, and are in line with our objective to create the largest and the best marketplace in Brazil, consolidating the best sellers on a reliable platform whereby customers can buy their favorite products, knowing their origin and quality.

On slide 8, we'd like to present the evolution of the distribution and logistics platform for the Company. B2W Digital operates with 11 distribution centers that are completely adapted for e-commerce operations, and also counts on 176 hubs that are strategically located throughout the entire country, an evolution of 81% when compared to the 96 hubs in operation in 3Q '15.

The hubs are operating centers to consolidate cargo and make distribution of deliveries easier for our customers. Additionally, B2W is the only e-commerce company in the country that has its own distribution unit, the UND, which is the result of the acquisition of the two main transportation companies that are specialized in merchandise delivery in Brazil, which are Click Rodo and Direct.

To increase the capillarity of our distribution unit, in October 2016, B2W established an operating agreement with Vialog, the leading transportation company in e-commerce deliveries down south in the country. Through this agreement, B2W will take on, through Direct, the delivery operations of Vialog orders, which includes the use of 40 hubs.

Throughout 3Q '16, the share of the B2W distribution units achieved 94% in the total deliveries made by the Company, compared to 55% of share in the deliveries in 3Q '15.

On slide 9, we show the leadership position of B2W Digital in the migration from e-commerce to m-commerce. Throughout the third quarter, the traffic through mobile devices represented for the first time more than half of the total visits, reaching 52.2%, a 17.4 percentage point growth compared to 3Q '15.

I'm sorry, we lost the audio. (technical difficulty) the first nine months of the year, a 171% growth. The apps offer a more fluid and faster shopping experience, in addition to offering exclusive features like favorite products and tracking of orders. As a result, the customers that use the app visit the brands more frequently and by more.

Going to slide 10, we highlight B2W's services, the result of integrating 12 acquired companies, among which 10 technology companies and two transportation companies specialized in e-commerce. B2W's services offer full solutions in technology and logistic verticals to provide support to the sellers' operations in the marketplace and online operations of large partner brands.

On slide 11, we point out B2W Digital's position as number one in customer service in Brazilian Internet. As a result of excellent customer service, B2W was again leader in the most important categories of the Epoca Reclame Aqui 2016 Award.

Americanas.com won for the fourth time in a row on the e-commerce electronics category. Submarino Card won, for the third time in a row, banks and financial services cards and retail award. And Direct won for the first time in logistics and transportation. Also, the four B2W Digital brands are considered a reference in customer service, having the most -- highest level of reputation at the Reclame Aqui website.

Going on to slide 12, we highlight the evolution of B2W Digital and the financial metrics throughout the past years. Taking the cash generation and the future need for investment reduction, this made CapEx as a percentage of the total GMV reduce from 12% in 2013 to 4% in the first nine months of 2016, while CapEx coverage index by EBITDA evolved 60% to 129% in the same time.

As we could see throughout the presentation, investments carried out generated gains in scale and important returns to develop the marketplace and in leading migration to mobile devices. Between 2016 and 2020, B2W will continue to invest in a digital platform that connects people, products, services, and businesses, help making all the businesses profitable, and in that generating value to their shareholders.

I would like to thank all the employees' dedication that are part in building the best and most loved digital company in Latin America. We would like to also thank our suppliers for their partnership, marketplace sellers by their choice, our shareholders for their trust, and especially our customers for their preference.

These were the main comments regarding our performance in 3Q 2016. Now I would like to open for Q&A to clarify any questions you may have. So that everyone has the opportunity to participate, we will ask you to please be brief in your comments.

Questions And Answers

Operator

Ladies and gentlemen, we will now start our Q&A session. (Operator Instructions) Our first question is from Mr. Joao Mamede from Santander.

Q - Joao Mamede {BIO 15265292 <GO>}

Good afternoon, Fabio. I would like to know about two things. The first is about the sellers that joined the platform this quarter. 1,900 is a high number. How did that evolve throughout the quarter? Was it more concentrated at the beginning or the end so we can understand how this will be the share of the market share in the fourth quarter? The effect is already very relevant in this quarter. So, that's the first question.

The second question is the evolution of the profitability. Although we saw an improvement of the EBITDA margin year-over-year, due to the growth of the marketplace and presuming constant shares, I was expecting a little better than it was. So, is this more a reflex of very intense competition? Because the contribution margin in the 3P maybe wasn't that high. That's what we suppose when we look at the numbers of your competitor. I know that competition is very high, and this has been putting pressure on the profitability, preventing you from expanding your margin even more.

A - Fabio da Silva Abrate {BIO 17940993 <GO>}

Good afternoon, Mamede. Thank you very much for your questions. Adding the 1,900 sellers was throughout the year, so those are numbers from the nine first months of the year. In the quarter, we included 400 sellers.

But I think more important than looking at just the addition of these new sellers, we have to look at the sellers that we already had at the base, which is equal to our same stores. So, we do some very interesting work in bringing new sellers onboard that are interesting to us in terms of bringing more assortment, including no new categories, but also we work very close to the sellers that we already have with us because there are many opportunities there.

We connect a seller to our platform, and the evolution of sales for that seller is extremely significant on a monthly basis. So, we play a very important role in the development of that seller so that they can, more and more, sell more and also make more money. So, I would be more concerned on those two aspects, bringing new sellers onboard and also treat the sellers that we already have very well since they already are with us.

The share of the marketplace in the first nine months of the year was 16.3%. Just to help with your projections, our expectation for the year is at least 18%, which means that the

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share of the market share in the fourth quarter will be around 20%. So in fact, we have very high expectations for the contribution of the marketplace on sales of the last quarter of the year, considering the existing sellers and also those that we will bring to our base.

Your second question about the margin in this quarter, it's more interesting for us to look at the Company's margin through the controlling company, because last year we had still some effects of B2W Viagens in our gross profit. So, when we look at the margin of the controlling company in the percentage of net revenue, it's 1.8%. And when we look at the gross revenue, it was 0.2%. So, it was not very high.

So, with the strong contribution because of the competition in the marketplace, but showing also a strong competitiveness in our direct sales market. So, the market is still very competitive, and we have been able to reach a balance between the margin that we can bring in 1P and also the contribution margin from the marketplace.

Q - Joao Mamede {BIO 15265292 <GO>}

Thank you, Fabio. Thank you for your attention. Just to follow up on the first question, I'd like to understand better how you are in getting ready for Black Friday. I know that recently you had an event with the sellers to try to make things more professional and even guide the sellers for Black Friday because there's going to be a peak in demand. So, how receptive were they about that? And do you see any differences about the type of service that the sellers are providing to the end-user, to the customer, actually you become closer to them and carried out that event? Thank you. That was it.

A - Fabio da Silva Abrate {BIO 17940993 <GO>}

Thank you, Joao. Yes, in fact, we did have a Seller Day in September. The purpose was to train our partners so that they could sell more during Black Friday. And it's very important that they could be present during this event with us.

And the feedback that we received was that they're really excited. And we were able to support our partners so that they can improve their service level. And like I said, when they join the platform they experience much higher sales levels than they were used to. So, it's our duty to work closely with these sellers in a way that they will not have any issues as they sell much, much more than they used to sell when they weren't part of B2W.

So, our sales team has done -- has worked closely with them to exchange experiences and try to understand their difficulties, and also supporting the development of all salespeople. So here with us they can be more successful and they can make more money.

Q - Joao Mamede {BIO 15265292 <GO>}

That's great, Fabio. Thank you for your answers.

A - Fabio da Silva Abrate {BIO 17940993 <GO>}

Thank you.

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Operator

Our next question is from Joseph Giordano from J.P. Morgan.

Q - Joseph Giordano {BIO 17751061 <GO>}

Hello. Good afternoon, everyone. Hi, Fabio. Thank you for taking my question. About Joao's question about the competitive environment, how have you seen or have you already seen any types of changes as your main competitor is restructuring?

And the second aspect, when you look at the more -- or a larger market, you can see many business models like asset light pure or a hybrid, which is probably what you are looking into. I'd like to understand where you will find a point of balance between 1P and 3P in order to support cash generation for the Company.

And about the cash burn, I'd like to know if we should expect any capitalization in the next 12, 18 months, given that the cash burn hasn't improved much? Thank you.

A - Fabio da Silva Abrate {BIO 17940993 <GO>}

Joseph, thank you for your participation. Once again, the competitive environment is very tough regardless of how our competitors are. Some competitors are growing, some are dropping or falling. But as we've seen in the market, it's that the competition for the customers' wallet is very strong under all aspects; price, free shipping, and payment terms in more installments.

In addition to the business model, I think that the beauty of our platform is exactly the balance between 1P and 3P. So, throughout time, we were able to extract the best of what each model has to offer, so bringing assortment, bringing in new categories through marketplace, and helping our sellers to make good business, and focus on what the Company knows how to do best.

So, the Company has a very long relationship with its main suppliers. So, in fact, there are some categories that we will operate better in 1P than in 3P and vice versa.

So, that business model few people have in Brazil. We're going through a transition process. I'd like to remind you that marketplace is very recent, even though it's big in the past 12 months. We already have a business of BRL1.7 billion, so marketplace is already very big but it's still very recent. So, cash generation and the evolution of the financial model will come from our ability to extract what's best in each one of the businesses.

In relation to your last comment, it's worth noting that the Company's net debt is based on seasonality, so throughout the quarters of the year, and the best leveraging position is 3Q. In the fourth Q, the Company generates cash, as an example of what we saw in 2011, when in 3Q '15 we generated over BRL600 million in cash and leverage went from 2.5 to 1.5 back then.

So, we still have the fourth quarter coming. And we have strong expectations in relation to the upcoming events, especially Black Friday, which will be on November 25th. So, we have the best expectations in relation to that. And without a doubt, we will close the year with an indebtedness position which will be better than the one that we had in 3Q, and that's it.

Q - Joseph Giordano {BIO 17751061 <GO>}

Thank you.

A - Fabio da Silva Abrate {BIO 17940993 <GO>}

Thank you.

Operator

Our next question is from Franco Abelardo from Morgan Stanley.

Q - Franco Abelardo {BIO 17416219 <GO>}

Hello. Good afternoon, everyone. Hi, Fabio. About the take rates in 3P, I think we can do the math about the growth, merchandise and the rent from the Company, there was a drop a bit. It was from 12% to -- dropped to 10.9% in this period. I'd like to know -- understand why there was a drop with the new sellers, large sellers, entrants. Was that a lower commission or is that a mix effect?

And how about this new channel for the smaller sellers? Will the take rate be smaller than 11%, for instance, that we see for the whole business, or is it the same? That's the first question.

My second question is related to 1P. We've noticed that it started to grow again, about 4% or 5%, but there is a very negative impact on the gross margin. And you touched upon -- touched on the fact of the competition in Joao's question. What's the balance for 1P and 3P? Do you believe you're going to still grow 1P, or would you -- do you expect a discontinuity of some of the categories in 1P and focus them on 3P? Thank you. Those are my questions.

A - Fabio da Silva Abrate {BIO 17940993 <GO>}

Hi, Franco. Thank you for participating. The take rate did not vary. When you look at 3Q '16 and compare to 3Q '15, it's about 16%. So then we can go into more details and so we can understand where you saw that drop, because our take rate is not dropping.

In relation to the small sellers and the portal that we just deployed, it does have the higher take rate. It's public. It's 16%. So, we have very positive expectations to bring in all these types of sellers in terms of size. And consequently, we want to see a higher profitability.

In regards to your second question about the balance between 1P and 3P, this is a model that is being under transformation. And as I said, the more interesting is the combined model. We have been learning a lot with the marketplace, especially with this combination between marketplace and direct sales.

So, we're in the process of understanding how is this better balanced so we can get better margins in 1P and better margins also in 3P in such a way that, with the combined of the two, we have a model of profitability that is better than what we have today. But this is an ongoing evolution process.

As you could see, the marketplace has been gaining share inside the Company. It reached around 19% of share in the third quarter. In our business plan, we have expectations for the marketplace to become even more relevant. So, it's a model that is under development, and the margin will come from the evolution of the combination of the two models.

Q - Franco Abelardo {BIO 17416219 <GO>}

Okay. Just to follow-up. How much is the size of the drop of margin in 1P? And I think you already answered on the previous question. But expecting greater penetration of the 3P in the fourth quarter, can we expect it to have a growth in gross margin, with a more balanced gross margin? Or will the investment still make the consolidated margin to drop year-over-year?

A - Fabio da Silva Abrate {BIO 17940993 <GO>}

I will give you some references of our gross margin of the controlling company, which was 24%. The marketplace contributes about 3 percentage points. Last year the margin was 22.2% and the contribution of the marketplace was 1.5%. The margin of 1P was flat at 27.7%.

Q - Franco Abelardo {BIO 17416219 <GO>}

That is the net revenue. You said that in the gross revenue it dropped.

A - Fabio da Silva Abrate {BIO 17940993 <GO>}

Yes, it dropped just a little bit.

Q - Franco Abelardo {BIO 17416219 <GO>}

Okay. Thank you very much for the visibility.

A - Fabio da Silva Abrate {BIO 17940993 <GO>}

Thank you.

Operator

Next question, Tobias Stingelin from Credit Suisse.

Q - Tobias Stingelin {BIO 18290133 <GO>}

Good afternoon. My question is, there is seasonality in working capital. And everyone is more optimistic about Black Friday. How are you looking at sales? If you could split what is marketplace specifically and 1P, because the question actually is, there is a bet that Black Friday can help with the revenues of the year. But if it is not too much of a contribution, your indebtedness will continue to grow. So, what is your expectation? I know it's early, but are things going in the right direction?

A - Fabio da Silva Abrate {BIO 17940993 <GO>}

Hi, Tobias. Thank you very much for your participation. I believe that, yes, things are going in the right direction. The evolution of our GMV throughout the year shows exactly that.

We came from a very bad first quarter in which we didn't have any increase in sales. Our second quarter was much better. We grew about 7%, and reaching the third quarter where we grew 16%. And this evolution is also seen when we look at the monthly basis.

So, the expectations are the best possible for the fourth quarter of the year. Black Friday actually is a very important event for us. Last year we sold the equivalent of one month of sales in just a few hours. So, the Company is ready for this.

I think that's the most important. We did some very hard work, almost one year before the event operationally, commercially, and with the sellers in the marketplace. So, everyone is ready and excited to sell more than BRL1 billion this year, growing not only in our 1P but also our 3P business.

So, we had a Seller Day specific for Black Friday in September with our sellers. It was very interesting. Everyone is very excited. The sellers are very happy with us. So, we have the best expectations possible for sales at the end of the year, and consequently the earnings will have a more favorable balance. So, I think everything is going well.

Q - Tobias Stingelin {BIO 18290133 <GO>}

Okay. So, what are you expecting for 1P specifically? I think your 1P grew 4% to 5% now in the third quarter. It was negative and now it's positive. So, what are you betting on? Because you put together an inventory -- I know that the marketplace is doing well. It's helping you. But the consolidated balance sheet is still very tight on the margin per year. So, we do have the seasonality, so what type of bet are you putting your chips on? Is it to grow towards a scenario with your inventories? Are you ready for that?

A - Fabio da Silva Abrate {BIO 17940993 <GO>}

I think you're correct in terms of 1P growth. The expectation for the end of the year is to continue to grow in 1P and the marketplace have an even higher share in the fourth quarter.

We're working with an expectation in about 20% of the share. So, we're betting on both sides. I wouldn't call it a bet. I would call it very good planning to sell a lot with this

balance between 1P and marketplace.

Q - Tobias Stingelin {BIO 18290133 <GO>}

Another question, please. In the process of focusing more, you said that you're trying to understand the best mix between 1P and 3P, but you made it clear that you want to have fewer categories in 1P and operate as much as you can with 3P. How is this process of simplifying or reducing the number of categories focusing on less categories in 1P? How is it on the curve? Are you 50% of where you want it to be, 90%, 10%? Can you give us some idea?

A - Fabio da Silva Abrate {BIO 17940993 <GO>}

Tobias, this is a gradual process. The sellers, in fact, when they enter our base, in one month they sell almost the equivalent of what they sold in the other platforms. So, we work very hard to bring the sellers to the base, develop those sellers to the point in which we can think, if that is a category that we operate in 1P as well, what would be the best balance.

We have enough sellers to sell in 3P what we sold in 1P. That's the first question we have to ask. There are the categories, in fact, that we're doing better than all the other competitors in 1P. So, we want sellers that support our need for sales.

So, the first quarter of the year where we had a drop in sales, it was a clear sign for us that inventory is still a very important aspect, because we didn't have inventory at that time. And the marketplace sold very well, but not enough to -- for the companies sell the same as our expectations.

So, it's a gradual process to have a balance between 1P and 3P. It's not that complex. It's not that simple. So, there is a learning curve there.

Q - Tobias Stingelin {BIO 18290133 <GO>}

Okay, perfect. My last question. Can you give us some statistics of how many users you have in Prime, some numbers that you didn't put in the press release?

A - Fabio da Silva Abrate {BIO 17940993 <GO>}

Yes, actually. Prime is still a pilot. We have about 5,000 customers that are subscribing to Prime. It's still restricted to the state of Sao Paulo, but the first statistics are very positive in terms of frequency of shopping, average ticket, and profitability. So, soon we will have news about this.

Q - Tobias Stingelin {BIO 18290133 <GO>}

Okay. Thank you very much.

Operator

Our next question is from Irma Sgarz, Goldman Sachs.

Q - Irma Sgarz {BIO 15190838 <GO>}

Hello. Good afternoon, Fabio. I'd like to go back to the part that you mentioned in other calls, but I'd like to confirm once again. I'd like to understand your positioning. And could you talk about your position? Did you pay 25% of PIS/Cofins tax over smartphones and tablets? Because there is the deductions, and the tax rates have significantly increased throughout the past quarters and once again in this third quarter year-over-year. So, that confirms that you've started to pay that solely, these taxes.

And I'd also like to know if you're paying in terms of cash or if you're just provisioning that or accruing that, and given that many companies are operating in this segment with a court order or finding other ways to work around the PIS tax and Cofins tax comeback, so I'd like to know what do you think are your expectations for the future? Are you still in the current position, or is there any room for thinking of operating with or without a court order and not paying and then paying again? I'd like to know your opinion on that.

A - Fabio da Silva Abrate {BIO 17940993 <GO>}

Good afternoon, Irma. Thank you for your question. I'm going to talk to you to give some overall aspects of the tax scenario.

That increment of the tax rate is resulting from many changes in the tax scenario in the country, and significantly impacted our tax burden and consequently our bottom line. The main impact is resulting from the constitutional amendment, number 87, which changed the collection of ICMS tax between the origin and destination states and of the increase of the ICMS rate in practically 20 states of the country.

Just to put this into context, our tax burden in the nine first months of the year increased 32%, which translates into almost BRL300 million extra in taxes paid. And in that period, where that tax rate or burden increased 32%, our gross revenues dropped 3%. So, those are the major figures of the impacts that we had throughout 2016 in relation to the changes of the tax dynamics here in the country.

Last year our tax burden was approximately 14%, and this year we're at 19%. So, yes, we were negatively impacted in these figures. We're not happy at all about that, but we also believe that this is temporary and that it is important for all the necessary adjustments that have to be made in our country.

Q - Irma Sgarz {BIO 15190838 <GO>}

Thank you for your answer. Can I -- also that you mentioned temporary impact. Are you talking about the delta, or is the current rate something temporary? Because I believe that ICMS tax changes tax rate for -- the destination state changes, and that will impact the taxes in the next years up to 2019. So, in theory, the tax rate will continue to increase slightly because of that. Is that your opinion as well in going back to late obeying [ph]?

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A - Fabio da Silva Abrate {BIO 17940993 <GO>}

The temporary is in the sense that it's a movement that somehow was important for the country and it has to be done. We don't have any signs at this time that the tax burden will improve from now on.

And with all the movements that happened, even the late obeying the law of the good, we were very much affected. We paid just in taxes alone over BRL300 million in the first couple of months.

Q - Irma Sgarz {BIO 15190838 <GO>}

So, you're paying them fully for smartphone and tablets, 9.25%?

A - Fabio da Silva Abrate {BIO 17940993 <GO>}

Okay. Yes.

Q - Irma Sgarz {BIO 15190838 <GO>}

Thank you.

Operator

Next question is from Guilherme Assis from Brasil Plural.

Q - Guilherme Assis {BIO 16143141 <GO>}

Good afternoon, everyone. Thank you for taking my question. I'd like to know about your sales expenses. We saw a trend in the first quarter, especially in the first quarter, of a huge drop year-over-year. And in this quarter, it's more in line with the third quarter last year. So, I'd like to understand what we should expect about sales expenses from now on and what changed in the Company so that that gain that we were seeing is no longer taking place in sales expenses? That's my question. Thank you.

A - Fabio da Silva Abrate {BIO 17940993 <GO>}

Hi, Guilherme. Thank you for participating. Yes, in fact, in first Q and second Q we had significant operating leverage. The effect that we had, especially in the 3Q '16, in the expenses line with sales, was in the area of personnel and occupations.

So, it's getting the Company ready for Black Friday and Christmas, because this year we got ready for that earlier. So, as you mentioned, the expenses were flat, and we didn't see the operating leverage that we saw in the first months of the year. So, with the sales in 4Q, we expect without a doubt to continue to deliver operating leverage as we delivered in the beginning of the year.

Q - Guilherme Assis {BIO 16143141 <GO>}

But nominally you dropped a lot in 1Q and then a little less in 2Q, but still a little, and now you're pretty much flat. I understand what you said about getting ready earlier and having -- and being stronger, so you can bear more sales, right? I understand that. So, in 4Q the trend is the same -- should we expect the same level as last year, or do you think you can dilute that and then come back in having more leverage and the same level of expenses reduction?

A - Fabio da Silva Abrate {BIO 17940993 <GO>}

Our expectation is for 4Q dilution and operating leverage. So, it was just a movement of -- in doing things earlier. So, since we're going to sell a lot in 4Q and given that our framework overall is very lean and we've been showing huge operating efficiencies, our expectation is that we will in fact have good numbers for 4Q.

Q - Guilherme Assis {BIO 16143141 <GO>}

Okay. Thank you. Oh, and Fabio, just if you can go back to the take rate, maybe we can talk more about that. But I reached similar figures to what Franco mentioned. So, I'd like to understand is there something that we haven't seen? Because in my math, my average take rate -- considering the difference between GMV and revenues, mine was a little bit over 12% for 3Q '15 and then 2Q '16, and now my math says 10.9%. What do we have to adjust to achieve a more correct figure to the Company's -- according to the Company's reality?

A - Fabio da Silva Abrate {BIO 17940993 <GO>}

Guilherme, let's go from the math that you did, because in my math, it's flat in 12%. I can give you the figures and we can discuss better.

So, the contribution of marketplace was BRL69 million and, in 2015, was BRL32 million. So, maybe we can later sit down and see what math you did. But it's flat on 12%. The math is at BRL69 million. I get BRL62 million, so I think this might be the difference. And then we can talk later to find out how to get to your numbers.

Q - Guilherme Assis {BIO 16143141 <GO>}

Okay. Thank you.

A - Fabio da Silva Abrate {BIO 17940993 <GO>}

Thank you, Guilherme.

Operator

Next question, Paola Mello, Citibank.

Q - Paola Mello {BIO 17712227 <GO>}

Thank you for taking my question. I want to understand what are the scenarios that you're working with for leverage and what level of leverage are you comfortable with? We saw

significant reductions in CapEx, but on the other hand, this level of leverage is very similar to when you did an increase in capital. So, I would like to know what we can expect from now on in a pessimistic scenario. We might not have the growth that you were planning on initially or one that the margins are still tight because of the competitive environment. Thank you.

A - Fabio da Silva Abrate {BIO 17940993 <GO>}

Hi, Paola. Thank you for your question. Considering the capital expenditure that we had in June and in September, our leverage throughout the year in the first and second and third quarters is about three times EBITDA. So, the maximum level that we could reach is 3.5.

But as I mentioned before, the expectation for the fourth quarter is a deleverage. And last year in the third quarter, we were leveraged 2.5 times and we closed the year with 1.5 times. So, the 3.2 tends to get better now in the last quarter of the year. And the maximum level that we understand as being reasonable to operate our business is 3.5 times, and we're within that number.

Q - Paola Mello {BIO 17712227 <GO>}

Okay. Thank you.

Operator

We now close the Q&A session. I would like to pass the floor to Mr. Fabio Abrate for his closing comments. Mr. Fabio, you have the word.

A - Fabio da Silva Abrate {BIO 17940993 <GO>}

Thank you for participating in our webcast conference call. We'd like to take the opportunity to invite you to check today the offers we have for Black Friday at our website and also get ready to enjoy the largest Black Friday in Brazil at our website that will take place on the 25th.

If you have any additional questions, our IR team is at your disposal. Thank you very much, and have a good afternoon.

Operator

The conference call now is closed. Thank you for participating and have a good afternoon. Thank you for using Chorus Call.

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