Local Conference Call
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4Q23 Earnings Call Transcript
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Vanessa Papini: Good morning, everyone. Thank you for waiting. Welcome to Magalu's conference call regarding the quarterly results.

For those who need simultaneous translation, just click on the “Interpretation” button using the "globe" icon at the bottom of the screen and choose your preferred language, English or Portuguese.

We would like to inform you that this event is being recorded and will be made available on the company's IR website, at ri.magazineluiza.com.br, where the earnings release and presentation are already available, both in Portuguese and English. The link to the presentation in English is also available in the chat.

During the presentation, all participants will have their microphones disabled. Then, we will start the Q&A session. To ask questions, click on the Q&A icon at the bottom of your screen. Enter your name, company and question language. Upon being announced, a prompt to activate your microphone will appear on the screen. You can then activate the microphone to ask your question.

Questions received in writing will be answered later by the investor relations team.

I would now like to give the floor to Fred Trajano, CEO of Magalu. Please, Fred, you can get started.

Frederico: Once again I am here with the company's entire executive board, who will be available to answer your questions at the end of our presentation.

I would like to say that the result of the fourth quarter represents an extremely important symbolic moment, a turning point in results for the company. I took over the company in 2016 and there were 22 quarters showing sales growth, profit growth and increased cash generation.

After the pandemic, with the macroeconomic context, rising interest rates, rising taxes, we faced a very harsh reality and for 2 years we did not present results. And I, together with the entire Magalu team, have now established an absolute focus on making the company return to profitability, which was exactly what we delivered in the fourth quarter of 2023, and which we know will continue as from this year.

This was no small feat. To give you an idea, the increase in interest rates post-pandemic, the increase in taxes, mainly the return of DIFAL, added around BRL 3 billion annually to the company's costs, 1.5 billion in financial expenses, with an interest rate increase from 2 to 14, and practically another 1.5 billion with the increase in DIFAL last year. Managing to extract BRL3 billion from the operation is no small task, requiring a huge effort from all 35 thousand company employees, and above all its leadership.

We increased margins, reduced expenses, improved working capital, added services revenue that includes more revenue from the marketplace and revenue from financial operations as well, especially the sale of insurance, sale of financial products, and with that, in the fourth quarter of 2023, we presented BRL100 million in recurring net profit, with the highest EBITDA margin, 7.2%, of the last four years. To give you an idea, in 2020 it was 5.2%, it fell to 2.6% in 2021, it rose to 6% in 2022, but there was no DIFAL yet, and to 7.2% now in the fourth quarter of 2023.

It really has been a lot of work, of which we are finally reaping the fruits.

On slide number 2, we show the quarter, we had sales of BRL18 billion. If we look at the annual level, 63% of sales, a growth of 5% on the annual level and basically stable in the fourth quarter of 2023. As I said, the company was totally focused on delivering profitability, returning to profitability. In this quarter, the basis for comparison was a little polluted by the World Cup, which for the first time in history was in the fourth quarter of 2022, and we were sponsors of the match broadcasts here in Brazil. So, we had a very loaded base, especially for 1P physical store operation. Even so, we managed to keep sales flat, GMV flat in the fourth quarter and deliver a margin of 7.2 with a margin of 30.3 in the fourth quarter, even with Black Friday, which we also operated in a very different way from other years. It was the first Black Friday with a positive contribution margin and, for us too, it was an extremely fundamental and important change in strategy for delivering our results for the fourth quarter.

When we break down these sales, slide number 5, we can see, from the point of view of physical stores, even with the very high comparison base from last year's World Cup, and I think this is already a very real trend for this year, I wanted to highlight, then Fabrício Garcia will be able to detail a little about how the physical stores are at the beginning of this year, last year, in 2022 to 2021, physical stores had already grown 15% largely due to the effect of the World Cup and in the fourth quarter we managed to grow 4% over this 15% in 2022. So, really showing that, after a long period of difficulty in physical stores, sales growth in the channel is resuming.

We are now in January and February showing growth more in the double-digit line, with great potential for improvement ahead, because if you think about it, interest rates have not yet fallen significantly. So, a very big opportunity for this channel, whose market share is smaller than the online one. We have around 20% market share in physical stores in traditional categories and around 35% online. So, we still see a lot of room for macro improvement and significant opportunities for physical store gains in total. As I said, Fabrício will be able to give more details if anyone has a question about this in the Q&A.

On the next slide, I wanted to talk about e-com. In e-com, we had two different situations, 1P with a drop of 8%, 3P with a growth of 10%. For the year as a whole, we closed with approximately BRL46 billion in online sales. We are vice-leader in this segment, we have been investing in this channel for 23 years, BRL46 billion is considerable sales. In the year as a whole, online grew 5%. In this quarter, we presented flat sales in the GMV concept, a drop of 8% in 1P, mainly due to the World Cup comparison base, but 1P also had to recover around BRL300 million in DIFAL, because DIFAL, as I said, is around 1.2-1.3 billion at the annual level. If we divide this by quarter, it is BRL300 million in DIFAL which we did not have to pay in 2022, which we now have to pay in 2023. So, there was a very significant increase in prices, a huge focus on the 1P margin and, with the World Cup as a basis, we ended up showing a drop of 8%.

I see a more stabilized situation in the first quarter than what happened in the fourth quarter, last year we had already paid DIFAL, so we will have a slightly fairer basis of comparison for 1P, so I see new opportunities here for 1P in this year.

In relation to 3P, we continue to show 10% growth, but I wanted to highlight, can you go to the next slide, please, the revenue growth of 3P. We grew 3P GMV by 10%, but with the increase in the take rate that we made throughout the year as a whole, our 3P in the quarter generated an increase in revenue, which is booked in service revenue, 26% of increase in revenue, that is, 10% of GMV with 26% of revenue, further monetizing our operation.

3P, which contributed negatively to the company, to the company's EBITDA in 2021, started to have a zero contribution in 2022, and in 2023 it had a very significant contribution to our EBITDA, and this will tend to be the reality from now on, We are already at a good level of percentage contribution margin, we want to continue increasing 3P sales - and I'll talk a little about that later on.

In relation to 3P, we went from 260 thousand published sellers to 340 thousand published sellers, also increasing the number of different offers here from 91 million to 128 million offers.

Practically half of our online GMV does not come from traditional categories and 3P has helped the company greatly in this diversification. To give you an idea, 40% of all items sold at Magalu come from 3P. 3P has already expanded to a physical store in less than five years, we have been operating a physical store for 67 years. In terms of GMV and number of orders, 3P has already contributed significantly to the company and the tendency is for this to continue, looking to the future.

Regarding 3P, we are also seeing favorable winds, we have significantly improved our level of service, our delivery. The percentage of 3P products delivered within 2 days jumped from 43% in the fourth quarter of 2022 to 51% in the fourth quarter of 2023. Remembering that 80% of our deliveries go through Magalu Entregas. We currently have minimal dependence on the Post Office. If I'm not mistaken it is around 10% of the total volume of our orders, very low. Nowadays, in fact, after the acquisitions of 4 logistics companies, which are now under the Magalu Entregas umbrella, 80% of everything we sell in 3P goes through our own logistics platform. We are already making 51% of deliveries next day, and the tendency is only to improve because we are very positive and confident - can you pass to the next, please - in expanding our fulfillment, it took us a little while to do fulfillment because we I wanted to set up a fulfillment operation that was very different from the rest of the market. Our fulfillment is multichannel, unlike any other proposals on the market, sellers place products in exactly the same distribution centers as we have for 1P products.

And like our 1P operation, once inside these DCs, sellers' operations benefit from multichannels. To give you an idea of the 1P service level, the 1P NPS today at Magalu, stores plus website, is around 80 and the 3P NPS is 60. As more and more 3P orders go to 1P, we are able to significantly improve the level of service for our customers, simultaneously reducing our delivery costs and delivery times.

We now have 8 distribution centers enabled to receive products from sellers, with 3 of these distribution centers being incentivized. So, the same incentive that I have for 1P, we are passing on to the seller. We are very optimistic, especially with centers further away from São Paulo, because few companies nowadays have the capacity to provide these services to sellers in more distant centers. More than 2,800 sellers use these services. I believe that by the end of the year, this rate of 15% of 3P orders will be closer to 30%.

Sellers who place the product in our DC have a 25% reduction in costs compared to the costs of traditional logistics operators and a 25% increase in conversion. So, as we move forward with this fulfillment agenda, which is one of the main goals of my entire platform and logistics team here, we will certainly improve customer service levels, margins, conversion and sales growth. too. We are very excited here and very confident in this expansion.

I think there are some opportunities, not in the consensus of any analyst today, which I think are worth highlighting. I'm going to talk about some of them here - and Roberto and then Mauad can add more details later -, I'm going to talk about Magalu Ads. We really believe we have a great opportunity to monetize our 500 million monthly visits. Bearing in mind that Magalu’s properties include the website, the most visited sports e-commerce in Brazil, Netshoes, the most visited games e-commerce in Brazil, KaBum, one of the most visited beauty product e-commerces in Brazil, Época, in Brazil, in terms of number of monthly orders, we have the second biggest delivery, AiQFome, remembering that all the companies are making a profit, I wanted to reinforce this, not only the controlling company, but when these companies are making a profit, plus Magalu's own channel, we have in total, and the content channels we have, Canaltech, Jovem Nerd, 500 million monthly visits with a huge opportunity for monetization, and a good part of our efforts (and our CAPEX too) will be in developing the platform for advertisers.

We have already had several products delivered this year, but we have a very consistent roadmap and we have no doubt that Ads will contribute significantly to our EBITDA in the coming years, and we are also sure that this is not included in market consensus forecasts. We are very excited about this opportunity.

Another opportunity is Fintech, but I'll let Beto and Mauad talk about that, Beto in the presentation and Mauad in the Q&A, and also Magalu Cloud, the first Brazilian cloud with global, public scale, 30% of Magalu's operation is already in the public cloud. We already have 52 external customers trying out our service. André Fatala is also here to answer your questions. Several important products for the cloud will be delivered throughout the year and will, in fact, provide an option for Brazilian companies to be able to enter the cloud with local, low, cheap costs. I think now it's not enough to just have a cloud, you also have to have competitive costs because for internet companies, for technology companies, you are not only demanding growth, but also profitability, and we see the option of a local cloud, with costs in reais and not in dollars, as a great alternative, not only for us, as we have made this migration, but for many companies, especially small and medium-sized ones in Brazil. I think it is another opportunity that is not in the market forecasts and which I think will contribute significantly to the result in the coming years.

With that, I'll give the floor to Roberto Bellíssimo to talk a little about our short-term results and then I'll return here for the Q&A. Thank you very much.

Roberto Bellíssimo: Good morning, everyone. Thank you very much for being here at our earnings call. I'll go through the big numbers here first, the financial highlights, as Fred already commented, almost 18 billion in sales, 10% growth in the marketplace, 4% growth in physical stores, significant gain in market share in traditional categories.

Then we will talk about gross margin, since the beginning of the year we have been saying that our gross margin was evolving and changing levels and, once again, we reached more than 30% gross margin, growing 2.5 percentage points in relation to the past, an EBITDA of BRL756 million, an EBITDA margin of 7.2%, also the highest EBITDA margin in the last 3 years and a net profit of 100 million, very happy with this profit, 1% profit margin, a net profit here which is, which we talk about, recurring.

On the next slide, we show total published net profit was 212 million. In addition to the recurring net profit of BRL101 million, we highlighted here the extraordinary events, starting with the sale of LuizaSeg stake, which contributed more than BRL200 million to net profit. In the financial result, we accounted for the fair value of liabilities for company acquisitions, the portion payable in shares, this ended up helping the financial result, but we excluded it from the adjusted financial result. We account here for a deferred income tax and social contribution credit at Netshoes due to the fact that Netshoes had previous annual losses, as it had losses, it did not record this credit. As it made a profit in recent years, we started to record this credit here, reverting positively to Netshoes' net profit.

In addition to all these events, conservatively, we made a provision for the 2022 DIFAL in the amount of BRL370 million. This provision was made where, in our view, based on the opinions of our legal advisors, there is today a greater likelihood of loss than of gain. Although, it is worth highlighting here that the STF decision has not even been published yet, we will continue to dispute and keep you updated on this matter. It is a provision that, for now, has no effect on cash, and remember that we have almost BRL1 billion in court deposits relating to DIFAL for 2021 and 2022 on our balance sheet.

Continuing, we had other non-recurring expenses that were quite low, practically BRL35 million, which mainly refer to expenses and write-offs in relation to store closures in the first quarter of this year. We closed 23 stores and this closure of stores will not have any impact on the results of this first quarter, it was already fully provisioned at the end of last year, also including a change of a distribution center. And the income tax on all these effects comes to a net accounting profit of 212 million.

On the next slide we bring more good news. We re-presented the third quarter results and, this time, the balance sheet is fully audited without any reservations. When we released the third quarter results, the audit was not yet completed and, after completing all its work, we publish the results here.

No inaccuracies were identified in the initial recognition of the bonuses, therefore, it was not necessary to re-present the balance sheets from previous periods, as previously estimated. What we did was review the estimates for the bonuses released in previous periods.

We fully included the value of this adjustment in the third quarter's results and, we emphasize, it is the same amount that we disclosed in the November Material Fact and in the November results, so the balance sheet published on September 30th and all accounts, assets and liabilities as of September 30th, needed no changes. The recurring adjusted result for the third quarter did not change either. The only change was in the accounting result, because, again, the amounts we had recorded retroactively, we now fully recorded in the third quarter results without any cash effect, as we had already explained.

It is also important to highlight that since the third quarter we have been improving, and in the fourth quarter all campaigns were already registered in our new campaign management system, TradeLinks, and the results of the third quarter and fourth quarter have already reflect all these benefits of much greater control and much greater focus as well.

Continuing, we show the evolution of the EBITDA margin not only in relation to the past, but throughout the year as well, a very important evolution. A highlight for the main leverage of this evolution, with emphasis on the growth of the service revenue marketplace, which adds greatly to our results, the increase in the gross margin of goods and the transfer of DIFAL. Fred has already spoken about Black Friday, the expansion of fulfillment, market share gains as well as the recovery of profits at LuizaCred.

On the next slide, we show that the product margin, we not only managed to complete the transfer of DIFAL, which we had already completed in the third quarter, but to go further, in addition to paying the entire DIFAL this year, the merchandise margin still increased by 1.1 percentage points compared to 2022.

The services margin also greatly helped again, 1.4 percentage points. And this gross margin grew much more than the evolution of operating expenses. In fact, operating expenses remained practically stable, both in nominal terms and as a percentage of GMV, and the only variation here was in relation to net revenue due to the issue of the marketplace and equivalence also contributing again.

On the next slide, we show and talk a little more about the working capital. Here, it is important to highlight that in this quarter we saw an increase of around BRL500 million in working capital as a whole, so another positive evolution in working capital, with emphasis on the level of inventories; we managed to reduce the balance of inventories by 400 million from September to December, and also highlighting the net balance of taxes to be recovered on the balance sheet, which we monetized here, offsetting 325 million net, this turned into cash and is also a trend henceforth.

As we increase product margins and increase service revenue, we have been able to offset more ICMS, PIS and COFINS, so the quality of working capital has improved significantly. And one observation, the suppliers balance, specifically, did not grow this quarter, it remained the same value from September to December for several reasons: one, we bought less because we reduced inventories too; but we also anticipated payment of certain suppliers, we made the payment in the fourth quarter, so we won't have to pay in the first quarter.

So, the message here is that in the first quarter of this year the variation in suppliers balances will be much lower than in previous years. So, we have a perspective that continues to be very positive for cash generation this year and also for the evolution of financial expenses, which, on the right side we show, fell a lot, literally, from 7% at the beginning of the year to 6 %, to 5%, to 4%, and this drop reflects the improvement in working capital, reflects the increase in financial revenue, including financial revenue with advance payment of suppliers and the drop in financial expenses, also the CDI and accompanying a stronger capital structure.

On the next slide we show that in the quarter, again, we increased total cash by 1 billion, we increased net cash by 1 billion as well, there was no change in the debt balance. And this 1 billion cash, again, did not come from suppliers. Normally, in the fourth quarter the balance of suppliers grows by 1 billion, and in this quarter it did not grow. If it had grown by 1 billion, we would have ended up with more than 10 billion in total cash, but this was very positive due to the fact that we generated more revenue, reduced financial expenses and will continue to reduce financial expenses. In this first quarter, the trend of financial expenses, again, is one of significant reduction throughout this year.

Of this 1 billion, we can say that 100 million came from recurring results, 400 million from inventories, 300 million from taxes and 200 million from the sale of LuizaSeg, in summary.

On the next slide, we show our capital structure, again, 3 times total cash over short-term debt, 9 billion compared to 3 billion. We have already paid almost 1 billion, including bonds and interest on bonds in January, and we will reduce another 2 billion, and in the year we should reduce our total debt from 7.4 billion to 4.4 billion, maintaining a very robust total cash flow, counting on the year's cash generation and also on the capital increase we are undertaking this month, in the order of BRL1.25 billion.

Next, as Fred said, we highlight the subsidiaries all making great profit, Netshoes making a profit, with the marketplace growing very quickly, Época also making a lot of profit, KaBum making a lot of profit, growing too, also growing a lot with KaBum's marketplace too, AiQFome, and then on the other slide we show Fintech, LuizaCred made 18 million in profit, MagaluPay also very profitable in terms of payments and anticipation of receivables. We will soon launch the digital CDC (Direct Consumer Credit) and our digital account for sellers has greatly evolved; it reached more than 70 thousand points this quarter and a total volume of more than BRL800 million.

Moving forward, at LuizaCred we continue to grow TPV, a card base of almost 7 million active cards, reaching 15 billion sales in the quarter and 57-58 billion sales in the year, a portfolio of BRL20 billion, and best of all in relation to this portfolio, on the next slide, we show that default rates are falling significantly, NPLs falling significantly, both short-term and long-term, the level of provisions falling significantly, funding costs also falling, LuizaCred also reversing the result. This quarter was also a turning point for LuizaCred, entering a new phase, yielding 18 million in net profit in the quarter, with very favorable prospects, a reduction in funding costs and a reduction in defaults going forward.

Finally, we show the performance of recent harvests as well, with emphasis on the last few months, with very low performance in both CDC and cards. For cards, a default level of below 3% is historically low.

Finally, we talk here a little more about our capital increase. We announced the increase in private capital, 100% supported by the controllers and BTG, demonstrating the confidence of BTG's controllers in the company, in the strategy, in the business model. We talk about the use of funds, in particular accelerating investments in technology, the expansion of LuizaLabs and all platforms here with high added value, high profitability margin, including Ads, Fintech, fulfillment and the cloud.

And finally, we would also like to thank the participation of all our shareholders, who contributed and participated in the capital increase very impressively. We had participation of practically 86% in the priority offer, the controllers entered with 100% of their potential and the minority shareholders participated with more than 70% of the entire available volume and also requested very significant participation in distribution of the surplus.

We received at the beginning of the month, we have already settled the priority offer, 1.070 billion and we will settle the apportionment of the remaining 180 million this week, totaling a capital increase of 1.250 billion in the quarter.

So, I'll hand over to Fred, or we can go straight to the Q&A session. Thank you very much, once again, for participating.

Q&A Session

Vanessa Papini: We will now start the Q&A session. To ask questions, click on the Q&A icon at the bottom of your screen. Enter your name, company, and language of the question to join the queue. Upon being announced, a prompt to activate your microphone will appear on the screen. You can then activate your microphone to ask your question.

Our first question comes from Luiz Guanais from BTG bank. Luiz, please, go ahead.

Luiz Guanais: Good morning, Vanessa, Fred, Beto. I think two questions here from my side, First, if you could comment, Fred, also taking advantage of Mauad's presence, about the evolution of new services on the platform, then, the digital CDC, as you mentioned, fulfillment and advertising, and how can we think of these as drivers not only of growth, but also of margin for you over the next few quarters?

And then, appending a second question here, what can we expect for this growth and margin equation throughout this year? It is clear that you are seeking to increase the profitability of the operation and improve cash generation, but on the growth side, can we think about any additional investment to be made, including the capital increase that you also undertook? How can this equation work throughout this year? Thank you.

Fred Trajano: Good morning, Guanais. Thanks for your question.

Luiz Guanais: Good morning.

Fred Trajano: I'll start by answering, then I'll pass over to Mauad and then back to me. Well, from the point of view of margins specifically and contribution to operating profit, I think there are three main lines there, in which avenues for improving operating profit, for increasing operating profit, as I said, are not included today in the projections of most analysts, namely: Fintech, we have significant monetization of financial products offline, and online it is low, so Digital CDC and various other initiatives - which I will ask Mauad to explain to you - have a huge opportunity here to contribute and monetize our ecosystem;

Advertising, which I think I already talked about a little in the initial considerations, there are several companies from around the world having a very successful monetization agenda via advertising. Recently I myself was visiting some of these companies in Southeast Asia and India, all of them with very successful agendas of significant Ad monetization on their audience, and we have one of the largest online audiences in Brazil - I'll ask Edu talk about that.

And the Cloud too. I think Fintech, Cloud and Advertising, are three avenues here and significant monetization opportunities. Fatala is here, he can talk on this later, not in this question, but if anyone is curious to understand more.

Fulfillment is much more about improving service levels and increasing conversion. It is not an opportunity here for monetization, 3P is here and we have better deadlines, with lower costs and we do not need to charge the customer for shipping for Pickup in Store, for example. It ends up helping convert 3P growth, but it in itself is not an instrument for increasing profitability.

With that, I'll hand over to Mauad to talk a little about the Fintech opportunity, then Edu can talk a little about Ads, and I'll come back here to talk about this year's growth in margins.

Carlos Mauad: Good morning, Guanais. Thank you for the question. Here in our product roadmap, we have planned to launch Digital CDC early in the second half of the year, so we are looking forward to having this new payment method at our e-com checkout, both for 1P and 3P, and, given the company's expertise in granting direct consumer credit in physical channels, we see how this boosts GMV and builds contribution margin. We are very confident that - obviously, taking all precautions here because granting credit online is a little warmer than in our footprint for physical stores - we will be able to ramp up this operation, and when we look at the market as a whole, we see we can have a share of something like 5% share of checkout, specifically in Digital CDC.

As a result, as we are building a product from scratch here for digital, in the second half of the year stores also tend to benefit from a new product chassis so we can create more flexibility, create pricing that is more in line with the risk and obviously a more fluid journey within our store environment as well.

So, in short, the second half of this year promises much in terms of implementing new consumer financing products.

I'll hand over to Edu.

Eduardo Galanternick: Hi Luiz, good morning. Thanks for your question. Talking a little about Ads, I think last year was a year of evolution for our product matrix. We basically have three products in Ads: One is the sponsored product, those showcases that appear in navigation and especially in searches; We are developing a video display network, which still needs some final steps to be fully ready; and we have all the special content, be it content from our content portals, Canaltech, Jovem Nerd, Steal the Look, or Lu's own content.

So, it was a year of consolidating this product matrix. We enter this year with the focus on having good go-to-market. It starts with reinforcing our team. To lead the Ads department within the company we've brought a super competent person with great hindsight in this market, namely Célia Goldstein. She took on the position on January 23rd and she is basically leading this commercial team, and we believe that this year, although we had good growth last year, whether in advertisers or in revenue, our view is that there is plenty of room for growth and this year will be a year of even greater acceleration.

Over to Fred.

Fred Trajano: I think that, additionally, I think many of these inputs will generate even more significant outputs for next year, including the cloud, they will start to reap the rewards, they will be investing in inputs that will generate outputs in the medium and long term.

In the short term, Guanais, it is important to say that we have momentum in terms of margins in the fourth quarter that we did not have in the first half of last year. Bear in mind, in the first quarter of last year we had the DIFAL impact without passing it on in prices. So, we will have better images in 1P and in the physical store too, with sales growth and operational leverage. We are already in double-digit growth, this tends to greatly benefit the result, as the physical store margin, the contribution margin is very high.

3P, we started passing on prices to sellers, tariffs, in February, I think it ended in June, so I also think we have good momentum in the first half of the year, regardless of all these new initiatives, which I think will generate result outputs towards the end of the year, next year. So, we have a first half already benefiting from this momentum we were able to harness in the fourth quarter.

Now, compared to last year, we will see even more significant improvement, because last year, right at the beginning of the year, we had to deal with the increase in DIFAL without yet being able to transfer everything to price and we had not yet made the changes I mentioned. So, we have a good perspective for the first half of the year with initiatives that were undertaken back in the fourth quarter. Anyway, this is just complementary.

I think there is another point, so we don't spend too long on the answer to your question, which I will probably talk more about in the next questions, which is that we are investing a lot in user experience this year, so there is a significant CAPEX here our goal is to improve UX. We have added a lot of complexity for our customer, many new categories, many new services, we have grown a lot. These last two years, our agenda has been very focused in-house, reducing expenses, increasing margins. This year's agenda will be very focused on the consumer and improving UX and user experience.

We can elaborate more in other answers so I won't go on too long here, but I'm sure they will help with conversions and improving 1P and 3P growth for this year.

Luiz Guanais: Okay Fred, thanks for the answers.

Vanessa Papini: Thanks for your question, Luis. Our next question comes from Maria Clara, from Banco BBVA. Maria Clara, please go ahead.

Maria Clara: Good morning everyone, thank you for the opportunity. So here at Itaú, we wanted to explore the expected evolution of 1P and the physical store in the year a little better, given that we can already see an improvement in credit KPIs, our internal proprietary index also suggests a gradual recovery in the consumption of durable goods.

So you say you have already noticed an improvement in the physical store, but what about in 1P? I would like to hear a little about this, and also a little about the strategy for each of these channels in the year, which is potentially a turning point year in the cycle and how this also relates to cash flow and profitability perspectives. Thank you.

Fred Trajano: Well, Maria Clara, good morning. Thank you very much for your question. I'll start to answer quickly here, then I'll pass it on to Fabrício.

Quickly, physical stores, I already said, we are at a very good level, excellent prospects - and Fabrício will detail them. 1P, we recovered profitability of 1P in the fourth quarter of last year. It took us about 3 quarters to fully transfer DIFAL to 1P. At the beginning of the year we have a little basis for comparison without DIFAL transfer, so in the first quarter of last year we had not yet passed on the DIFAL, so we have this base, but it is already better in terms of growth than what we presented in the fourth quarter of the year.

So, I hope that gradually there will be an easier comp and we will continue to grow it, but always with more positive contributions. But I'll let Fabrício elaborate on the answer.

Fabrício Garcia: Good morning, everyone. Thank you for the question, Maria Clara. I'm Fabrício. As Fred already said, I think that in 1P, online, we still have the DIFAL issue here in this quarter, but we are doing better, performing better than in the fourth quarter. The most important thing is we are managing to perform while maintaining our margin. We have changed levels, so we are focusing a lot on profitability and we want growth again, we are also gaining share in this quarter.

So, I think that in 1P, starting next quarter, we should start to see growth in sales as well, maintaining profitability. So, this is an issue we have done a lot of work on here, and we are performing well in practically all categories.

In stores, we had very good performance in the last quarter. We have to remember, 2022 was the World Cup and stores benefit greatly when you have the World Cup. We managed to grow and increase the margin. And in the first quarter, we had a very good Liquidação Fantástica, which is very significant for us in the quarter, we grew sales and managed to grow margins too. In fact, the sale was very good in all 3 channels, 1P, 3P and stores. We are managing to maintain double-digit store growth this semester by maintaining increased profitability and I think this will be the keynote for the entire year.

The store must stand out in terms of sales growth, we have a huge opportunity in the market. So, I think these are the scenarios we have for the year in 1P and stores.

Maria Clara: Perfect, thank you.

Vanessa Papini: Thank you for the question, Maria Clara.

Our next question comes from Irma Sgarz, from Goldman Sachs Bank. Irma, please go ahead.

Irma Sgarz: Hello, good morning to the team here. I have just one more quick follow-up question to Maria Clara's question about 1P. Do you have any vision about which categories you think, whether in-store or online, will perform better this year, perhaps even given product cycles, etc. of recent years?

And the main question. Fred or maybe Fatala, I think the question here is a little about the opportunities of the cloud. If you could talk a little about the main customers and the first lessons you have been taking on board in this vertical and, obviously, the opportunities. I wanted to dive a little deeper there. Thank you.

Fabrício Garcia: Good morning Irma, Fabrício speaking. I will answer about the categories and then Fred will give some guidance or we will hand over to Fatala to talk about the cloud.

In categories, performance is great in white goods, both in 1P and in store. Screens have also been performing well, portable and otherwise, I think these are the categories that stand out. And the market that is having a little more difficulty is the telephone market. It has been falling throughout Brazil. We have been gaining share, but it is a category that is having a little more difficulty, I think the product exchange cycle itself, but this is offset by the growth in white goods, in particular. So, I think, in categories, this is the scenario. Both in store and online performance is very similar.

I'm going to hand over to Fatala now to talk about the cloud.

André Fatala: Good morning, Irma, and everyone. Thank you for the question. Just to also contextualize the cloud opportunity, firstly talking about the global market, the number expected by 2025, is BRL5 trillion, more or less US$1 trillion, and the CAGR of 22 to 25 is in the range of 24%. And when you look at the Brazilian market, in 2025 we have a market of approximately BRL91 billion and a CAGR that sells 41% from 22 to 25.

So, we see that Brazil and Latin America in general still have a gap in this part of cloud adoption in all layers, from SaaS to the infrastructure part, so there is a long way to go for this part of digital transformation of companies.

Within the cloud, after we made the public announcement in December, the journey so far has been very interesting. One of the things that made us very happy was that, in the following week, we already had around 1,500 customer leads generated through the Magalu Cloud website itself, and we started working to understand what their needs are and onboarding some of them.

Bearing in mind that we announced the cloud and stated we would still be in private preview for these customers, so it is not open to the public to enter and do self-service onboarding.

Just to correct, Fred said the number was 52, but we have made progress in the last two weeks, we now have 74 customers in the cloud.

We are learning a lot. We have talked a lot about the focus on small and medium-sized companies, and we see that the product choices are working very well for them, but we have already had interest from enterprise customers as well. Enterprise for us, we say that these are select accounts, with more than 1 million in cloud expenses per year. So, we have already started onboarding some of them and we are learning a lot about the needs part and it is also a way for us to really direct the evolution roadmap.

Now, this April, we will launch the first 3 products, which we talk about as availability for everyone to enter through the portal and contract. This will happen at the Web Summit event in Rio de Janeiro, where we will do a demonstration and there will be a lot of content based on the cloud. And we have 9 other products that will be launched by the end of the year, also available to the entire market.

So, what we hope to happen is, with these first products, we start to grow the customer base a lot. They are very specific in use, but as soon as we evolve into the second half of the year and enable use of VMs, kubernetes, database, this is where we believe we will have the largest number of customers doing cloud onboarding. And we expect to be more or less at a level of maturity as high as what we have built around mid-2025/early 2026, we believe we will then have the mature product on a larger scale.

Irma Sgarz: Perfect, thank you.

Vanessa Papini: Thank you for the question, Irma. Our next question comes from Erick, from Banco Santander. Erick, please, go ahead.

Erick: Good morning everyone, thanks for taking our questions. I think on our side, there are two. First, if you could comment a little on working capital. Anyway, you mentioned there that in the fourth quarter there were a little more advances for suppliers, which in the end will be beneficial for this first quarter. Are we to think that this is a new pattern of working capital dynamics for you, thinking about these seasonal cycles? And also, if you can explore where you see opportunities in the working capital line.

And the other point, looking a little at the focus for 2024, where you talk a little about enchantment there, understanding how we can see this in practice in terms of changes perhaps. I think you commented a little on UX, but I think more to understand in practice what we can observe throughout this year to monitor the evolution of this initiative and also what we can expect in terms of evolution, whether in terms of sales, conversion?

Anyway, I think having an overview here would be interesting. Thank you.

Roberto Bellíssimo: Well, good morning Erick, thanks for the questions. I'll start here by talking about working capital. Well, we first highlighted the reduction in inventories, in this quarter we reduced 400 million, in the year as a whole we reduced 200/300 million in inventory, we had already reduced inventory throughout 2022. So, I think that since 2021 we have reduced practically 1.5 billion, almost 2 billion in inventory. And I think that an important point about this reduction in inventory is we have managed to do so by increasing the gross margin on goods in a very healthy way, in a very sustainable way.

This year we believe we will continue to improve our inventory turnover. We are not giving guidance, but on average we expect to improve inventory turnover by at least 5 days on average for the year, and may even improve inventory turnover a little more. We even look at more turnover than the nominal inventory balance, because it also depends on growth. The best way to improve turnover will also be as sales grow again, accelerating and everything else.

On the suppliers side, last year we saw a very significant increase in the average purchasing period, comparing 2023 with 2022, significantly. And if we look at every quarter, at the end of the year, we, in a way, let's say, tactically, decided to anticipate suppliers, so the average accounting term ends up reducing a little, but if we look at the average accounting term in fact, the order was much higher than at the beginning of the year or at the end of 2022, and this decision to anticipate suppliers was very positive for our own results in 2022. The financial expenses we saw falling greatly from 2023, and the financial expense at the beginning of 24, we are seeing at a very low level, much lower than the beginning of last year.

The trend in financial expenses this year is, in fact, very positive, decreasing greatly, and that has a lot to do with this working capital management, it has a lot to do with the fact that in this first quarter we will pay much less to suppliers than what we paid in the first quarter of last year. Remember that in the first quarter of last year we had to discount 2 billion more receivables to pay practically 2 billion more to suppliers due in the first quarter. We will not have this effect in the first quarter of 2024, so we are seeing much better working capital at the beginning of 2024 and much higher financial expenses and cash position at the beginning of 2024.

So, this is the result of work we have done together with the commercial department, the supply department, throughout the year, improving inventory turnover, improving the average purchasing period.

I will even make an observation I didn't mention before, but for us it confirms - and it's not debt, you know, but there are people who consider it in some way -, the Confirming balance over the last year, we decreased by 1.5 billion , from 3.8 billion to 2.3 billion, something along those lines. So, we also significantly reduced the Confirming balance, passing on, in a way, some of the increase in cost, repricing some of this product, and this also generated more financial revenue from suppliers, which we account for within the financial result.

So, in addition to inventory and suppliers, I will just highlight the tax bill, which, as I mentioned in the last quarter, we offset more than 300 million net between generation, accumulation and offsetting, and this should also be a very positive trend for 2024, again, as margins are higher, services are growing and everything else, it becomes easier to offset taxes. This is in fact a trend for 2024 and so, in general, we expect working capital to contribute very positively to cash generation for the year as a whole.

Fred Trajano: Good morning, thank you for the question. Regarding the issue of the year, of the customer, we are calling Simplifica Magalu, Monetiza Magalu, and now it is the year of Encanta Magalu. I think we had an agenda in the last two years, as I said at the beginning of our presentation, absolutely focused on profit, results. So, it is a very internal agenda, focused on efficiency.

There was a reduction in expenses, increases in margin and we felt the need, this year, to resume focus, as is the company's history, on level of service, in what we call user experience, the art of delight in every interaction. It is an extremely... it's simple, but at the same time it's very comprehensive. When you say delight in each interaction, we are talking about hundreds, even thousands of possible interactions with the consumer, and I think that on these journeys we have a series of opportunities for improvement, from password recovery, to refunding money when a sale is cancelled, reducing cancellations, increasing the level of service, meeting the deadline within the promised period, the level of service that we talk about, improving CSAT and the call center.

So, we mapped out more than 40 OKRs here, which are specific objectives related to the level of customer service and conversion, and we are going to put a huge focus on Luiza Labs, Fatala's teams, and the product and business, improving service levels.

We entered this period with approximately 80% NPS 2 years ago. At that time, almost all questions were answered for customers who purchased at 1P, in store. We maintain a very high level of NPS at 1P in store, but the NPS at 3P is historically around 60. It did not worsen, but as 3P increased total share in the company, average global NPS decreased.

So, we have a huge challenge in improving the global NPS. We want to return to an NPS of around 80, which is a global benchmark. To do this we have to significantly improve several issues concerning search, checkout, after-sales and all these items that I mentioned here in the answer. It is a very comprehensive agenda, but very pragmatic.

We know exactly what we have to do and I am very optimistic that it will, without a doubt, generate an improvement in our NPS, which I think is the main indicator here to validate this issue. But it will also help our conversion a lot, and increase in the frequency of purchases as well, which ends up reflecting in sustainable growth in results, regardless of whether you are giving a discount or not.

So, I think that's the agenda. It's not possible to summarize it in one answer, it's a very complete agenda and it's the focus of the entire company. Magalu's 35 thousand employees will be thinking about user experience with a strong, but not exclusive, focus on improving the technological platform.

Erick: Perfect, thanks for the answers.

Vanessa Papini: Thanks for the questions, Erick. Our next question comes from Gustavo, from XP Investimentos. Gustavo, please, go ahead.

Gustavo: Hi, good morning everyone, thanks for taking the questions. My first question is more along the lines of cloud. You comment that 30% of Magalu's digital operation is already in the proprietary cloud and that this should continue to increase in the future. Just so we can understand whether there is any level of expense or cost savings through this expansion. I imagine it should reduce dependence on external suppliers, so just to understand whether there is any type of saving in this lever as well.

And my other questions are a little more about the short term. The first is about store closings. You mention 23 stores closed in this first quarter. Just so we can understand if we are going to see more stores closed throughout the year. And the second point, I understand that DIFAL has already been fully passed on, but we saw some states also increasing the ICMS (State Tax on Goods and Services) rate starting this year as well. So, whether this has any impact or has it already been passed on to price? Thank you.

André Fatala: Good morning, Gustavo, thank you for your question. This is Fatala, I'm going to talk here about the cloud part. Yes, there is considerable saving with this migration that has undertaken. On average, we are managing to reduce what we pay, which already has discounts from public clouds, by around 30-35% depending on the type of workload. So, the idea is for us to continue migrating, it should reach around 50% by next year and with that we have a, let's say, change from OPEX to CAPEX here. Thank you.

Fred Trajano: Good morning, thank you for the question. Well, talking about the two questions, about the ICMS of the states, so, this transfer was already being made. I think we had already dealt with the tax reform, we are calm about it, we have the capacity to see more contributions per state and we have already transferred practically all of them, so we don't have any risk in that sense.

We specify state by state, 1P store by store and physical store. So, we have this vision with a great deal of granularity, one of the by-products of having focused so much on contribution margin for two years, our bases are now very good for very granular management of our results. We invested heavily in these systems and this monitoring model.

Regarding the stores, yes, we may close more stores. If the stores have a more negative contribution and no prospect of generating results, generally stores are very close to others, or we were unable to negotiate rental conditions with the owner, if necessary, we will close them, but I think there will be little material in relation to the total installed network.

Stores, the outlook is much more positive for recovery now, as I have said, but still, if there is any specific need to close a store, we will do so because we want our units to contribute positively to our results, above all contribute positively to margin. So, there is a possibility, but I don't think it will be significant in relation to the total number in the network.

And the store perspective is much more positive than negative. Right now it is the channel with the most positive outlook that we are already seeing materialize in January and February.

Gustavo: Perfect guys, thank you.

Vanessa Papini: Thanks for the question, Gustavo. Our next question comes from Nicolas from JP Morgan. Nicolas, please go ahead.

Nicolas: Thank you, Vanessa. Thank you, Fred and Beto, team, for taking our question.

Here on JP's side, I had two. Picking up a little bit on what you said about the stores, Fred, I wanted to understand how you see the competitive environment in brick-and-mortar. And would it make sense, perhaps, to open some stores, some points to try to capture market share that I think is perhaps available considering the financial situation of certain competitors.

So, to understand whether there is space to maybe open stores this year. Thank you.

Fabrício Garcia: Good morning, Nicolas. This is Fabrício speaking. You are right in relation to the competitive environment, this is a very favorable moment for Magalu. We are much better prepared than our competitors in every way, products, pricing, but I think it doesn't make sense to open stores now because we recently opened in several new regions, including where we have a lot of strong competition. They are large markets, particularly Brasília and Rio de Janeiro, so we have a lot of work to do in these regions where our share is much smaller than the share in places we are already more established.

So, we have a lot of opportunity to capture share in these new regions. We also see that, in regions where we are already established, we are gaining even more share. So, we agree that we have to gain share, but I think we can gain that from the stores we have open today. So, we don't have any plans to expand the store network much, no.

Nicolas: Great, thanks.

Vanessa Papini: Thanks for the question, Nicolas. Our next question comes from Vinícius, from Banco UBS. Vinícius, please go ahead.

Vinícius: Hi, good morning everyone, thank you for taking my question. Just a question here also on taxation. If you could comment on the company's position in relation to potential taxation, talking more about subsidies for investment, wondering if you also see an opportunity here to pass on prices as well.

And a second question, whether you could exploit LuizaCred a little more. We have seen an evolution here in the results, so if you could give a little perspective here of what you are observing in the credit environment in general, here on the other side of demand and a little bit of perspective as a whole for LuizaCred. Thank you.

Roberto Bellíssimo: Good morning Vinícius, how are you? Thank you for your question. I'll start by talking first about subsidies. What we say is that both Magalu and the companies, our main companies, Net, Época, KaBum, all of them have incentives that can be classified as a subsidy for investment. And, in this way, we will continue to have deductibility for income tax and social contribution purposes.

There is an incentive part, just to give you an idea, last year, we counted the effect of government subsidy in the order of 160 million, or more or less 40 million per quarter. What we can say is that 40 to 50% of this amount can be classified as investment and, in our opinion, should continue.

And the other part, possibly, will probably cease because it was about extending this benefit, this subsidy to other types of benefits, which, according to the STJ's latest decision, are no longer eligible.

But, in any case, let's put it this way, 40-50% should continue from this effect of the subsidy with the benefit in income tax and social contribution. We have deferred income tax and social contributions on the balance sheet to take advantage, so we do not foresee any material impact either from the point of view of our results or from the point of view of our cash flow. We will continue to focus, again, on increasing profitability, as we have said so far, including all tax effects. As Fred also said, I think the biggest impact in terms of transfer to the product, to the price, I think the biggest impact we have already had; that of DIFAL, and we have already shown the ability to transfer more than 1 billion in a single year to the final price. Here, I think we do not foresee any effect of passing on the subsidy to the final price, no.

Now I'll hand over to Mauad to talk about LuizaCred. Thank you.

Carlos Mauad: Hi Vinícius, thanks for your question. We are very excited about what we have seen in the last 6 months within LuizaCred. When we look here a little more, at 10 thousand feet, we mainly look at 2 credit indicators there, we look at the harvested performance indicators, which have been improving for a long time, but they are not large enough to improve the company's profitability. But when we were able to see the improvement in portfolio indicator performance, which more directly affect P&L and short-term results, we began to see this reversal until net profit materialized in the fourth quarter.

In the first two months of the year, we also saw a positive balance in our consumer financing operation, despite it being a quarter that, seasonally, is worse from a credit point of view. When we talk about the evolution of credit results within the year, the first quarter tends to be the worst quarter and it improves throughout the year.

So, the fact that we are in the black here, that we are seeing consistent improvement both in the portfolio and in the most recent harvests, as we showed here in the presentation, gives us a lot of confidence that this year will be a year in which LuizaCred will not only be able to help with the result, but also, obviously, be able to help build more GMV, both online and in the physical store.

I hope I have answered your question. Thank you.

Vinícius: Perfect, thank you very much.

Vanessa Papini: Thank you for the question, Vinícius. Our next question comes from João, from Citibank. João, please go ahead.

João: Thanks, Van. Two questions here. I think you discussed a lot of growth, the physical stores seem to be starting the year well. I wanted to explore - and sorry, Mauad -, I wanted to do a follow-up on this credit question as well and understand when we should see a boost, accelerating granting of credit and driving this GMV.

So, I think the question here is a broader point, about the timing we should see if 1P reversing the trend, whether due to comp or other factors you have in your expectations here. I just wanted to understand better the timing to see this growth coming in a more relevant way, given that the expense issue in 2023 has already been largely addressed. So I imagine that perhaps in the second half of the year we will see more accelerated growth again.

And then about 3P, we wanted to understand a little about the dynamics of the seller base. We understand that you were seeking a very specific seller profile and doing onboarding there, you also saw staff, store managers, in short, I wanted to hear a little more about this strategy, how we should see the growth of this base of sellers and how much this maturation of this existing base will also drive 3P. Thank you.

Carlos Mauad: I'll start here, João. Thank you for the question. What should we see here from a growth perspective? We should see our credit card structure, which is a more sensitive structure, including to the environment we are still experiencing here, growing in line with the market, and we should see high yield products, such as the CDC, accelerating further. So, even when we talk about the physical store environment, about CDC, it was already accelerating very strongly in the second half of 2023 and we hope to see this continuity from a growth point of view, especially with the entry into digital, which is a 100% new volume, a new tool for us to improve checkout conversion and profitability of this business.

Returning quickly, here, to the topic of credit cards, the economics of credit cards are more challenged following the pandemic, it is a very large portfolio we have here and we do not want to take any type of risk of the result changing again. So, we're going to take one step at a time, we're revisiting the value proposition, we're revisiting the acquisition channels, we're revisiting pricing, the customer financing cycle, in short, we've changed a lot of things in operation to adjust to the current scenario, both from a macro point of view and from a product point of view.

Yes, it will continue to be a super powerful tool to boost GMV, but the most striking growth must come from higher yield products, as they are easier to maneuver when you still have some level of uncertainty on the radar. Ok? I hope I answered your question, João.

João: You answered it, yes.

Fred Trajano: Ok, João, good morning. It's Fred here. I will answer that last question. Regarding the seller base, we will obviously continue to grow the seller base. We have, in our seller base, some differences, we have many sellers at the top of the pyramid who are brands that have a reliable platform here at Magalu to sell products and here they are not competing with specified white label products, so for these big brands Magalu is undoubtedly a priority channel. And we also have at the base of the pyramid those sellers that are physical stores, which we introduced with Parceiro Magalu, which are also those the stores bring to the base, and they had a very good year from the point of view of cash margin, of profitability.

The contribution margin of these sellers has increased significantly and, in short, we continue to have a good offer for sellers at the top, bottom and also in the middle of the pyramid, who come here through e-commerce platform integrators. So, I think we have an opportunity to continue growing the base. Now, our focus this year is not just to grow sellers, but to increase the quality of these sellers' offerings and the level of service from these sellers.

Within the context of the Year of the Consumer, one of Eduardo Galanternick's team's most important agendas is to ensure we are bringing sellers with a good level of service, who generate good NPS here for our platform, low rate of cancellation, high level of service in relation to deliveries and also, and above all, bringing the best offers, because in the same SKU, in the same code, you can have 10, 30, 40 offers. We want to ensure we have very competitive offers, with low prices, low shipping and a good level of service.

So, we will be qualifying this growth in the seller base a little, focusing a lot on the quality of the offer and their level of service.

João: That's clear, Fred. Thank you.

Vanessa Papini: Thank you for the question, João.

We will now conclude the Q&A session. I would like to turn the floor over to Frederico Trajano for his final remarks. Please Fred, you can continue.

Fred Trajano: Well, exceptionally in this call, I wanted to pay tribute to our founder, Luiza Trajano.

I think the best way to honor those who have passed away is to preserve their legacy. And it's no surprise that we chose the year 2024 to celebrate the Year of the Customer. She was someone who introduced customer-first focus into our culture, so we wanted to close this call with her photo in our presentation and also with a lot of hard work throughout the year to delight our customers as she always enchanted in her time here at Magalu.

Thank you very much, have a good week everyone.

Vanessa Papini: The Magalu conference call is finished. The Investor Relations team is available to answer any other queries and questions. We appreciate everyone's participation, have a good day.