CONFERENCE CALL TRANSCRIPT
4Q16 Earnings
February 20, 2017

Operator:

Good afternoon, ladies and gentlemen. Thank you for holding. Welcome to Magazine Luiza's 4Q16 earnings conference call.

At this point, all participants are connected as listeners only. Afterwards we will start a Q&A session and you will be given instructions on how to join in. If you need any assistance during the audio conference call please press *0 to ask for help from an operator.

Now I would like to introduce Magazine Luiza's CEO Mr. Frederico Trajano. You may proceed Mr. Trajano.

Frederico Trajano:

Good afternoon everyone. Thank you very much for joining our earnings call. It's a pleasure to be here with you. I am here with all Magazine Luiza's other executive board members to present our results and answer questions at the end of the call.

I would like to talk about our Q4 earnings, which in my opinion consolidate and reaffirm the assertiveness of our initiatives, both short-term ones, such as OBZ and GMD cost cutting programs, and our focus on gaining market share, as well as our long-term focus on our digital transformation strategy.

We have posted considerable improvements on nearly all key indicators followed by the financial market: growing sales, improved gross margin, diluted expenses and net debt reduced by operating cash flow, while the highlight has been our improved working capital number.

I would also like to emphasize that we have evolved greatly on indicators that the market does not usually follow, but are just as important as the ones I have just mentioned, in my opinion. In particular, I would like to note the evolution of our organizational climate index reflecting votes cast by our own team that were then compiled for our ranking among the best companies to work for in Brazil. Our NPS is the main customer satisfaction indicator we are watching at Magazine Luiza. Not only the latter, but other indices too showed evolution in 2016, such as *Reclame Aqui* [consumer complaints website] and PROCON [state government consumer protection entity].

It's great to see these indicators evolving, but the things that made us most confident for the future were all the initiatives we took to deploy our digital transformation strategy. We are aiming to do something no other company worldwide has ever succeeded in doing, as far as I know at least: transition from an analogue company to a truly digital one.

This project is based on our five pillars and we have evolved on almost all of them, namely: digitizing our physical stores, deploying Marketplace, becoming multichannel, our digital culture and the whole digital inclusion effort for our Brazilian consumers. For example, all Magazine Luiza stores have Wi-Fi and we provide all Magazine Luiza salespersons with mobile devices.

Several salespersons also got a mobile Pin Pad, which is a checkout device that avoids customers having to go find a cash register. Our all-store rollout gave customers buying on our website the option of collecting their items from one of our stores and it was already a huge success in 2016.

We launched our Marketplace operation; we evolved the already successful mobile app and we received an award from Google for having one of the market's best five apps - overall, not just for retailing - one of the Brazilian market's top five Android apps. We were very pleased to get this award and the mobile side was important for our online growth too.

We have done a lot in a very short time but we are still moving ahead with our digital transformation strategy rather than letting it rest here.

I would like to emphasize that e-commerce in Brazil accounts for only 3% of total retail sales. We strongly believe this online Brazilian market will continue to show substantial growth regardless of the economic crisis. If there is one thing that you do not want to be caught wagering against, it is e-commerce growth in Brazil.

The feeling here at Magazine Luiza is that we will benefit not only from growth but also from everything else we are doing for our digital transformation strategy. We are sure we will be one of the key players in this market.

We have a lot to do in 2017, which is the company's 60th anniversary and we feel that we are ready and focused to scale up several aspects but perhaps the most important is our key strategic pillar, the Marketplace platform, for which we will be attracting more partners and building out our product offering.

We are working to ensure that both partners and consumers see Marketplace as Brazil's best platform and we are doing so while very carefully upholding the reputation of a 60-year company that has always been very concerned to ensure high quality customer service.

This is yet another among the many transformations that Magazine Luiza has made in its history. The only thing that remains unchanged over these 60 years is that Magazine Luiza is constantly changing. We have the soul of a startup in a body consisting of 20,000 employees.

I want to take this opportunity to thank all our team members who worked very hard and showed determination in this tough year of 2016. I would like to thank our customers, shareholders, suppliers, the analysts who have joined our call, our partners, and the community in general for their confidence in us and their partnership throughout 2016.

Roberto Belissimo will now highlight some more details from this year's numbers, and then I'll talk about our expectations for 2017 for the very brief overview that we always provide at the end of our calls. So we are here once again at your disposal for questions. Thank you very much.

Roberto Belissimo:

Good afternoon everyone. Thank you for joining in our call. Let's start with slide 2 showing 4Q highlights. We have grown gross revenue with sales 14% up on 4Q15, which was the highest growth number of recent quarters. Our physical stores same-stores growth number of 6% was also higher than in 3Q, which had also been positive.

And all of this together with higher gross margin too, so this market share gain was very sustainable and quite consistent, too.

IBGE reported retail sales down around 6% in this quarter, whereas we grew 14%; so we showed a 20pp edge in relation to the market as a whole. The biggest highlight was e-commerce, which grew over 40%. Our e-commerce share rose 5pp to 26% of our total sales from 21% in 4Q15. EBIT also rose 8% in the same period, so our e-commerce grew 5x faster than our EBIT.

We are also highlighting the operating expenses line. We diluted expenses more than in any other quarter with dilution increasing in the course of the year to 2.3 pp and we got SG&A down to 22% of net revenue. Thanks to the OBZ work at the beginning of the year and matrix management of expenses throughout the year.

As a result, we more than doubled EBITDA to reach R$227 million with a margin of 8%, against that in Q3, [thus] showing recurrence and consistency. This was one of the biggest EBITDA margins the Company has posted since our IPO. And we posted R$46 million net income.

We are also highlighting quarterly cash flow of over R$650 million and working capital up by R$570 million, so we were able to lower the quarter's net debt from R$750 million to just over R$100 million.

Our adjusted net debt to EBITDA ratio fell to 0.2%, so both indebtedness and this leverage ratio are at their lowest level since our IPO.

Finally I shall mention LuizaCred. In the year, our NPL index for [arrears of] over 90 days fell 3.2 pp to 9.5%. This is one of our lowest delinquency rates ever and LuizaCred posted R$25 million profit as well, which mean that return on equity held up at 19-20%.

The next slide shows the year's sales up by 8% whereas the market was down by 8%, so there was a very big market share gain. For the year as a whole, our e-commerce share rose from 20% to 24%, and our e-commerce grew 32% against the 7% for the market.

We diluted operating expenses by 1.3 pp, which means over R$120 million savings in the year. EBITDA rose more than 50%; we posted a 7.5% EBITDA margin and R$87 million net income. We improved our working capital in the course of the year and reduced our indebtedness lowering leverage from 1% to 0.2% and LuizaCred posted over R$100 million profit for the year as a whole.

Page 4 shows that our number of stores rose to exactly 800. We opened 20 new stores in the course of the year. We reduced investments to R$124 million for the Company as a whole, investing particularly in technology.

Next, slide 5 shows our quarterly sales revenues with their growth rate clearly higher in the last quarter for both consolidated and internet numbers, and physical same-stores clearly evolved, too.

Slide 6 shows gross margin evolving in every quarter, so it was very consistent. On the operating expenses side for the last quarter, for example, we were able to reduce expenses in nominal terms from R$645 million to R$630 million, so there was pronounced dilution and a fall in nominal terms despite [several factors including] inflation, higher volume sales, collective bargaining, higher payroll charges and all the rest. So we did a very consistent job of reducing expenses.

On the equity pick-up line, contributions from LuizaCred and Luizaseg were consistent across all four quarters at around R$15 - 16 million. We are also highlighting the main effects on gross profit, including more rational pricing for the website, physical stores, freight and installation charges throughout the year; our product mix was better too.

Page 7 shows EBITDA growing in every quarter due mainly to higher sales, higher gross margin, diluted expenses and e-commerce numbers. Nearly all of the Company's growth this year came from e-commerce and we have managed to raise practically all our margins, which also shows that our e-commerce is getting positive results for our business.

Page 8 shows the evolution of financial result. In this quarter we saw interest expenses substantially diluted from 5.7% to 4.5%, partly reflecting the beginning of a downtrend for Brazil's base rate, but mainly due to the Company's lower leverage and its cash flow, too.

For the year as a whole, we diluted financial expenses from 5.1% to 4.9%. Also worth mentioning is the fact that our financial expenses tend to closely follow the Selic base rate and will probably fall in the same proportion as the latter.

Below we show the evolution of working capital at around R$260 million in the year. We are also highlighting the importance of e-commerce, which posts better working-capital numbers since inventory turnover in e-commerce is better while its terms of payment are the same as physical stores.

Above we show net debt and leverage, closely related to the evolution of working capital. We have kept gross debt almost unchanged, but boosted our cash position. We ended the year with a cash position of around R$1.4 billion, which was the highest level since our IPO.

Page 9 shows quarter to quarter net income. Page 10 shows our comments on LuizaCred, which was another of the year's highlights with revenues growing 19% in the quarter and 10% in the year to reach almost R$12 billion, while highlight was growth in use of Luiza cards at Magazine Luiza stores.

Growth was 34% for the quarter and 18% for the year. Luiza cards obtained substantial market share gain which also helped our stores post good numbers throughout the year.

Page 11 shows our delinquency portfolio with indicators falling quite consistently throughout the year while the card's portfolio grew and took over space previously occupied by the shrinking CDC portfolio.

Page 12 shows LuizaCred's net income numbers, which were also very consistent. Note that LuizaCred grew 17% in relation to 2015 in terms of operating income, but net income was slightly lower due to higher total taxes, although the last quarter's number showed a much better as a trend than 4Q15's.

Next a few highlights from our strategic pillars, which Fred has already commented on. Page 14 shows the multichannel pillar and within it the "Collect website purchases from a physical store" project. We concluded this project rollout in January and it was a success. Deliveries are increasing month to month and we now have over 100,000 products being bought on our website and collected from our physical stores.

Next on page 15, our app has had 4.5 million downloads and earned a Google award for one of Brazil's best apps

Page 16 shows a sample of our current Marketplace's top partners and others in the pipeline. There are now several vendors and partners in the Marketplace; others have already signed contracts and will be connected over the coming days or weeks.

Page 17 shows our greatly improved assortment. On Magazine Luiza Day, for example, this slide shows there were 80,000 Marketplace SKUs, of which 30,000 from our own inventory. Now there are over 200,000 third-party SKUs in Marketplace so we now have over 230,000 SKUs available on the website.

Back to Frederico for his concluding remarks.

Frederico Trajano:

I would like to mention our outlook for 2017. As I said, we always end our call with these expectations. For 2017, as we have said, we have deployed several digital transformation projects, some of them rolled out at the end of 2016. So we will have a year in which we will speed up the pace at which we are deploying new projects, but will also be capturing gains from previous-year projects, many of them rolled out at the end of the year.

This year we will still be harvesting gains from past projects and continuing to deploy new ones for this transformation strategy. We are going to keep major focus on the Marketplace pillar, so a lot of our Labs efforts from our technology lab team, e-commerce team and support units that have to do a lot of preparation will be involved in growing the Marketplace platform, so we are going to deploy new functionalities for more accurate searches and a more user-friendly digital platform.

So there's a lot coming up for the Marketplace platform. We can answer questions about this later without detailed numbers. We are going to focus on strategy. We will also continue to gain market *share* sustainably as we did last year.

For this year, we believe we have all the right conditions in place to continue gaining market share in both physical and online stores. I just want to point out that for this year's physical stores, in addition to gaining market share, we will probably have a tail wind behind us by 2H.

However badly 2017 might turn out, there is no way it will be worse than 2016. I feel we will still have the benefits of market share gain but with a bit more help from the economy in general, especially for physical stores. As I said, e-commerce does not show so much sensitivity to hiccups in the economy.

We aim to continue cutting costs. We had a year in which our highlights included getting operating expenses under control at lower levels due to all the programs we were running last year, which we are going to repeat this year, although obviously the basis of comparison will be slightly more challenging since we did so well last year, but the whole process and expense management culture remains in place and we have learned a lot from this; we aim to retain these lessons learned and apply them even in coming periods when the economy will be less challenging than last year. So we are going to continue our cost-cutting initiative.

We aim to continue our cash flow efforts with a continuing focus on managing working capital and working on all cash-flow and debt-reduction related issues.

We are going to speed up new store openings; we believe the stores are very important as revenue and growth drivers, but also as part of the Company's multi-channel strategy to roll out initiatives in more markets and places where our "Buy on our website but collect from a physical store" facility is not available.

Physical stores are important for the Company's digitization strategy and as centers of opportunity for future revenue drivers, but we will open stores while keeping tight control over new points of sale to ensure very low costs per square meter without requiring "key money" payments or major construction work.

We also expect to reduce financial expenses as the Selic base rate falls and as I have already mentioned to reduce debt too. So these are our expectations for 2017. Now we directors are available to answer your questions. Thank you very much.

Fabio Monteiro, BTG Pactual:

Good afternoon everyone. I wanted to explore this Marketplace business more. You have already detailed higher SKU numbers, but I would like to know whether you can give us any indication or target for this year or the next few years, in terms of number of sellers and also how much you think the Marketplace may add to the Company's online GMV and total GMV, perhaps more of a medium or long term target.

I also wanted to ask about online numbers, if you could highlight some segments or geographical aspect, or product mix that shows worthwhile numbers, or if it were a very general business shows across the board numbers irrespective of mix and geography. Thank you very much.

Frederico Trajano:

Good afternoon Fabio. Thank you for your question. I'll answer the Marketplace part. As I mentioned, we are not giving GMV guidance for this year. The year's focus is very much building a robust, quality platform that sellers will like to work with and one that provides good consumer experiences too.

For this year I would rather not pose ambitiously big numbers, what we call vanity metrics, right at the beginning of our Marketplace platform because I want the team to stay very tightly focused on building a quality platform.

Since we launched it last year, we still have a lot to do in terms of improving functionality and user experience and before we start upscaling our major concern is to ensure that scaling ensures the same level of service, which is an aspect that platforms in Brazil still fail to make the grade because they have very bad numbers for complaints posted to *Reclame Aqui* [consumer complaints website]. We are trying to find different ways of scaling without letting go of this level of service.

The focus is on product rather than value. What I can say more for the long run is that if you look at the situation worldwide, the Marketplace has the potential for scaling up so once you get your main value proposition right and your platform is working well, it will scale up very quickly.

It's an exponential scale that we have not seen on any other channel. It grows very fast, really exponential growth once you get it right, but it's very important you get your core right first and this year's focus will continue on adjusting the core.

In the future, I have no doubt that it may be more than half of e-commerce sales; I would say that over a five years interval, that is a very audacious assumption. It's not *guidance*, but there's a possibility that this may happen.

Fabio Monteiro:

Just a follow-up on your comment, thinking about what you said, do you see today some limitation for your Marketplace business scaling up perhaps the size of your offline business or do you see marketing investment only to showcase Magazine Luiza for sellers and end-consumers too as a platform on which you can find any product.

This is still not the case today because there are 230,000 SKUs, but you will eventually be adding many more over time. I would like to know your view... you're clearly talking about maintaining service level, being very careful... but other than that, do you see any limitations or any challenges Marketplace would have to tackle in order to scale up to much higher numbers?

Frederico Trajano:

None. The biggest challenge is developing a robust platform that you can scale up with good customer experience. This is the biggest challenge we are facing. Once you can get this right, scaling up goes extremely quickly and organically without having to make major investments.

For example, we already have over 500 sellers waiting in line to join our platform. Everyone wants to be there since having their products available on the platform is a no-brainer. Rather than any external limitation, the issue is much more our need to very meticulously build and maintain a robust product, one that can be scaled up while retaining quality.

There are no external limitations; it is a total greenfield market, still a small one. As I mentioned, 3% of Brazil's total sales are through e-commerce and a small fraction of those are through Marketplace. This market still has a lot of potential for growth. There is a huge opportunity and as yet nobody can claim to have a dominant position.

There are some high GMV players but this market is still wide open and ready to be tapped. There is a lot of trailblazing work to be done in Brazil. The real focus and challenge is product, platform and scaling while ensuring quality.

On your second question, I'll let Eduardo, our head of e-commerce, answer.

Fabio Monteiro:

Thank you, Fred.

Eduardo Galanternick:

Good afternoon, Fabio. In relation to e-commerce growth, it has been well balanced. We were able to evolve this year both in terms of visits, conversions and average ticket. It was also well balanced in terms of categories, all of which were more or less in the same order of magnitude with telephony, IT, electronics as highlights in some ways.

On the regional dispersion issue you asked about. Yes, we had some dispersion, not too much, but there was a deconcentration out of São Paulo. São Paulo has always been very relevant and still is, but we had some dispersion and this dispersion was mainly to areas near our DCs where we have operations, to the extent we are increasingly evolving this distribution of inventory and making this multi-channel operational. But what we can say is this, it was well-balanced sustainable growth.

Fabio Monteiro:

That's great, Eduardo. Thank you very much.

Richard Cathcart, Bradesco:

Good afternoon. My first question is for Roberto. You had written there in the presentation about zero base budgeting, which you did this year and which helped your end -year numbers quite a lot. I just wanted to learn a little about how you may continue this zero base budgeting in 2017 or whether it is getting increasingly difficult. Thank you.

Roberto Belissimo:

It does get more difficult to the extent that we did a lot last year, but expenses were increasingly diluted over the past year. So there are projects that have matured over the past year that will have an effect on the 12 month numbers, which will help us continue to dilute expenses, when comparing to last year.

This involves productivity gains. We have said that in these last two years we have been able to reduce our headcount while regaining almost the same level of sales as 2014. So we did get a very productivity gain in terms of sales per employee.

Our headcount is lower than it was in 2014, but our sales are almost the same as 2014. This was due to automation processes in stores. Take mobile sales for example, sales are much faster; our salesperson can serve more customers.

There are more projects in the pipeline to be rolled out during the year and continue automating stores for productivity gains.

Other than that, several expenses, we are working on the expense management matrix throughout the year. Take our "buy online and collect from a store" project, for example, which leads to savings for the freight package, and freight is the main expense, with packages. Both personnel and freight, as well as electricity, credit cards, are several packages that are part of the expense management matrix and every month we discuss them, search for improvements, compare numbers between stores, across groups of stores, we try to get stores that are lowering budgets to locate bench markers and get ideas from stores that are performing best, and so forth.

So the potential is there. The expense management matrix is now part of the Company's culture and we will continue focusing on this productivity gain. Of course we captured a lot of this potential last year, so now we will continue working to gain some more.

Richard Cathcart:

Fine. Just one more question, you also talked about a more rational pricing environment for e-commerce. I just wanted to hear your vision for 2017. Is it likely to continue in the same way, given that your competitors are experiencing profitability and cash flow problems? Or do you think rationality may diminish when the market starts improving? Thank you.

Frederico Trajano:

What I see is that if I could do so, I would wager on maintaining rationality. I'll tell you this because even in the United States, which is where this "high growth despite losses" story started, all the American venture capitalists who financed this story are now much less aggressive. So they are picking out and reinvesting in companies that have more short-term potential for growth with positive cash flows, or that will tend to improve their margins over time.

So this is the real situation for all digital startups, not just Brazilian e-commerce. There is already much more pressure for them to evolve profitability more in the short term. I think this worldwide trend will be reflected in Brazil too. More rational investors have learned to distinguish digital companies, e-commerce or otherwise, that have prospects of making a profit from those who do not, and they are no longer willing to finance the latter. Neither VC investors nor listed-stock investors will finance stories that fail to create shareholder value.

This is a worldwide trend and I do not see much room for Brazilian e-commerce operations or startups to evolve in this respect, hence my wager. But you never how the financial market will see it. I suppose they could decide make what I would see as the same mistake.

Richard Cathcart:

OK. Thank you very much.

João Mamede, Santander:

Good afternoon. Two things. First, I would like to mention cash flow. I think it has been one of the biggest positive surprises not only in 4Q, but throughout 2016. Now you are in a deleveraged situation that I would call quite comfortable if not controlled.

Looking ahead, initially with your results following the trend you have captured in recent quarters, you should continue to generate cash flow and deleverage even more. What I wanted to know is this: what level of leverage level are you thinking of working with? What would surplus cash flow be used for? That's my first point.

Here's my second point, could you tell us how you are seeing this early part of the year... you ended the year very well by accelerating in relation to the previous quarter. At the beginning of the year you have a very important event, which is this fantastic sale liquidating inventory; if you could give us feedback on the outcome of this event and how you are seeing things now in early-February too, that would be excellent. Thank you.

Roberto Belissimo:

Thanks for the question. On cash flow, we can not give any sort of guidance. What we can say is that it was a major focus last year and will continue to be so. Last year we got a lot cash flow from the evolution of working capital. We will make every effort this year to continue improving working capital.

Last year we improved inventory turnover for example, but this year, with the economy picking up and sales recovering, we could improve inventory turnover even more. Last year we were able to lengthen average payment terms for purchases in an intelligent manner and we do not intend to walk it back. We intend to maintain healthy average payment terms for purchases.

So to the extent that e-commerce is growing and showing better inventory turnover, physical stores are growing again a little more significantly. Remember that physical stores carry inventory in their showcases and displays. So our physical stores' numbers were almost unchanged last year. Improving inventory turnover for stores with stable sales is difficult. To the extent that sales evolve, it will be easier to improve inventory turnover for physical stores.

E-commerce shows better turnover as its share of total sales rise, and we are improving inventory turnover for consolidated numbers too. By maintaining an average payment term for purchases and thus financing our inventory, we have been able to generate cash from this inventory versus suppliers relationship.

So we will continue to work hard; our financial area works very closely with commercial to constantly improve this working capital ratio. Also to the extent that financial expenses fall as the Selic base rate falls, for example, there will be more cash left for the company. Given the downtrend forecast for the Selic base rate, lower interest expenses will have a very substantial impact on our costs. Brazil's CDI interest rate is highly correlated with our level of financial expenses.

So what we can say is that we will continue with this focus. We can not give guidance, but our aim is to continue generating cash and reducing net debt. This is our aim.

João Mamede:

Thank you. If I can follow-up on that point, I believe most of your free cash came from working capital, but you also had a reasonable reduction in CAPEX, and if you pose that against sales growth it was even better. CAPEX was down too. For this year, you are thinking of speeding up store openings, which would require some CAPEX, but for the overall reckoning what should we see for CAPEX as a percentage of sales?

Frederico Trajano:

We will not be saying much about guidance on CAPEX, but you are right, it will be higher than last year's due to more plans for new stores, but not only for that reason.

Remember that we are very disciplined in relation to this investment in new stores. There are not going to be very big investments in this respect. But we will be using more CAPEX too, and more than proportionately it will be used for new stores and technology for investments in the platform as we mentioned earlier in the conversation.

From the CAPEX point of view, however, I do not see any material increase capable of altering our perspective of continuously reducing indebtedness. We believe every aspect of the operation suggests we will have lower debt despite more CAPEX.

I do not believe it is at a comfortable level. I do believe it is at a better level than the previous year. Let's remember that end-year snapshots always look better than full year numbers. You get different quarters, seasonality, there is supplier seasonality every year. So the 1Q numbers will be different as will the 2H ones too.

The important thing about last year's number is that it has improved significantly on the same period of 2015, comparing 2016 against 2015, and we want to do that again successively from quarter to quarter, but ab end-year snapshot is always better than a full-year average so we still want to reduce indebtedness... although the Selic base rate is falling, it is still the world's highest base rate and we are have the world's highest interest rate in real terms, so financial expenses are very high.

And we want to reduce that line and improve our EBITDA/financial expense coverage ratio, which is the indicator we will now start looking at more closely for this year too, because we want to reduce this expense. We want to have EBITDA reflect more net income throughout the year, and to do that we have to continue our effort to lower indebtedness.

As to your question about our fantastic sale, I will let Fabrício, our vice-president and commercial and operational officer, answer.

Fabrício Bittar Garcia:
Good afternoon. About the beginning of the year, we started the year well and the sale was fantastic, our best ever with better numbers than last year, too.

We've been doing well in almost every category. The heat is helping. We had a good January and we are having a good February. I believe we will see a good quarter compared to 2016. Telephony continues to sell very well in the technology category. The white line category has also sold well.

In e-commerce we had good numbers too, as Eduardo will show here.

Eduardo Galanternick:

Same thing here; we started the year well with the same focus on execution that we had throughout the previous year. These big sale events are very important for us so we make sure we have stocked up goods well in advance. So we were able to post very good numbers off that fantastic sale.

[In relation to] February, the month seems to be continuing the favorable trend. The market as a whole has reacted. The first number was a preview of January based on EBIT, and showed about 15% growth in the market. So we have a better market scenario this year with the same focus and execution we showed throughout the previous year.

João Mamede:

Excellent. That's great, thank you.

Thiago Macruz, Itaú BBA:

Good afternoon. My first question is about LuizaCred. In relation to these rounds of Selic base-rate cuts that we have lined up for 2017, how long will it take before rate cuts will be reflected in LuizaCred's spreads? In other words, when can we see this [new development] driving bricks and mortar channel sales? This is my first question.

Second question: we have seen signs of certain international players showing interest in buying assets available for sale in your sector. I would like to hear your opinion... if you think an international player is likely to show interest in Brazil and decide to make a move.

If this is the case, perhaps [you could give us] your opinion on the impact this would have for the competitive environment. These are my two questions. Thank you.

Frederico Trajano:

Thank you for your questions. For the first one I will let Marcelo answer on the impact of a Selic rate cut for LuizaCred. Then I will mention the impact for business, but he may deal with that too. And I will mention the second part of your question.

Marcelo Ferreira:

A lower Selic base rate will impact interest charges this year for sure. But compared to this... [sic] is increased lending. So in relation to revenues going forward we will be working in a different market compared to the recent past, but we are already familiar this type of market too. So it will be a natural development.

I believe that both LuizaCred and the market as a whole will be lowering their interest charges in the wake of base rate cuts.

Frederico Trajano:

The second question is a very difficult one. I would not like to comment and build scenarios on the impact of any outcome of an acquisition for one or another of the assets in Brazil. I think we are in a very solid operational position now with a tight focus on execution and we are starting this year in even better shape than last year from the point of view of the operation, our team, our know-how, our projects, [so we are all set] to operate very well. We will be tightly focusing on execution and I honestly do not want to comment but I can say that we are not afraid of anything that might come out of any acquisition. Not at all.

I think we depend much more on ourselves to continue a virtuous cycle of growth-driven earnings. I do not see much of a threat from the point of view of the competitive microeconomic scenario.

Thiago Macruz:

Fine. Thanks for the answers. If I may come in again, we have how Amazon entered Mexico organically and there is the lingering question as to when it might eventually make a move in Brazil. I think your e-commerce results are pretty impressive and maybe they're drawing attention [to your business]. What do you think is the main point preventing the player out there from entering Brazil? What is the main difficulty for them? More out of curiosity. Thank you.

Frederico Trajano:

Firstly I have a lot of respect for the company. We think they show very good execution. It is now the world's largest retailer in terms of market value with a very good level of service, especially for customers in the United States. So, it's a player for us to watch.

Their entering the [Brazilian] market is a never-ending promise. I have had analysts and journalists asking me when Amazon will be here for many years. I have been answering this question for at least ten years. I think they have a very tight focus on India. We are [sic] investing billions of dollars in India; it is a huge market that takes a lot of their energy. What you have just said... recently in Mexico, but not with the same aggressiveness as their move to enter India, which is a very large and promising market.

Here is what I see in relation to Brazil, specifically, if I have to pose something: Amazon's business model means that its growth is highly dependent on cash flow. So they do not have very high margins, in fact their margin is very low and they are growing with positive working capital, so they have more suppliers than stocks - 45 days suppliers, 30 stocks. Amazon has a positive cycle. In the United States, you get paid sight on all credit card sales on D+2 if I'm not mistaken.

Whereas in Brazil, we have the terms of payment known as '10 installments free of interest charges'. This innovative arrangement was one that that Brazilian businesses wisely devised for their customers, but it eats into cash flow. You have to discount receivables for e-commerce and you end up paying a lot of interest expense. So I think this is a formula people are not used to anywhere else in the world, but they would have to deal with it here in Brazil.

On top of that, delivering goods in Brazil is a high-complexity operation. Amazon is very disciplined in terms of quality of delivery and service levels, which we do not yet have here - I suppose that we will do some day and that this ecosystem will evolve - but our ecosystem for shipments is still at a low level of automation and has much potential to evolve. We still rely heavily on postal services and one or another delivery player so I do not think they would be able to apply that "high-level-of-service" model here in Brazil.

At Magazine Luiza, we are managing to grow while ensuring a high level of services. As I mentioned before, with customer NPS largely due to our transport network supporting physical stores. We have over 900 service providers for our physical stores who are also delivering our e-commerce sales and reaching a higher level of service than these large-scale shippers in the market.

So for a new player that does not have the same high level network that we have, for example, I think ensuring high levels of service would be difficult. In fact here in Brazil, Amazon is not getting very good ratings on *Reclame Aqui* [consumer complaints website]. Their numbers here are still below their levels in other countries. I think upscaling would be a major challenge because they are very customer centered. They have a very strong customer-obsessed principle in other countries, so I'm sure they will only be able to upscale here if they are able to apply this principle here, too.

Thiago Macruz:

Great, Fred. Thanks for your answers

Guilherme Assis, Brasil Plural:

Good afternoon everyone. Thank you for taking my question. I would like to talk a bit about the competitive environment. We can see that the market is currently extremely difficult and we are entering the year with an interest rate outlook that can improve. But so, when we effectively look at PNC data, we still see nothing materializing in the market, especially for headliners like you. Even so, you are delivering good results, with positive 5% same-stores in brick and mortar and a very big and important growth, far above the Market, in e-commerce.

Looking at the previous year and this year, we see a difficult competitive environment and the competition obtaining some tax benefits in 4Q - on the same level as you in a certain sense, I think. How did you guys see the competition during 4Q? Obviously you continued to gain market share, but what was the competition's behavior in relation to price? How do you see that going forward, since your margin does not seems to have been affected by any change there may have been? And how are you seeing this in your analysis of the competition's pricing? That's my question. Thank you.

Frederico Trajano:

Thank you for your question Guilherme. What I wanted to say about competition is what I've been telling you since the first call last year when we commented that our expectation was that market would become more rational. Incredible though it may sound, the crisis creates a market that is - I would say - less competitive. And I'll explain that because what I'm saying might initially appear to be contradictory, but it's not.

The market is less competitive because in a crisis you have much less liquidity in the market, many banks are not lending, suppliers are lending less and capital markets are less interested in finding proposals involving low profitability and high growth. So in a market like this, I think that what happened was that several of our less well structured competitors started to have much less access to capital due to the financial market's risk aversion, as well as suppliers who also work with the financial market for loan insurance purposes.

So I saw many companies that were less structured and less disciplined from the point of view of earnings, that ended up leaving the market and downscaling their operation due to lack of access to liquidity, credit, the stock market, etc. And what I see, as you rightly said, is this market is still very selective. Banks are selective, although the capital market has come back with our stock being listed. Investors are much more rational and suppliers continue to be very disciplined about selling to retailers on credit terms.

So I continue to see a rational market for this year, I do not expect major changes because the year is starting without any major acceleration despite the Selic base rate cut. For this year, I do not see much change in the competitive scenario.

Guilherme Assis:

OK. In this context, Fred, how should we see your gross margin? I understood what you said about there being some players who continue competing as they always have and others who are more debilitated, so the competitive environment is not really so bad, but going forward and given that the outlook for recovery is still some time in the future, how should we see the issue of gross margin, which seems to have held up at very reasonable levels despite the difficult market? How should we see the gross margin outlook?

Frederico Trajano:

I cannot say much about guidance Guilherme, but generally speaking, on a very global level, I expect a scenario in which last year's numbers will continue. This is not guidance, but I do think it's the most likely outlook given the market's current situation. This is something we have been talking about for a long time - if you look back at Magazine Luiza's gross margins over the last four years, you will see a highly stable scenario, so we expect continuity and we are working with a gross margin very close to the number we posted at the time of our IPO.

We expect continuity for every quarter because our entire team is focusing on sales with margins rather than just selling. So we say that buyers and sellers have to see things like the company as a whole, or like shareholders. So they have to generate sustainable growth, long-term growth. To take one example, a Magazine Luiza salesperson earns commission on gross profit. Purchasers' remuneration - both e-commerce and physical stores - is based on cash margin, which is sales x gross margin.

So we are very disciplined Guilherme; the best way of showing this is the case is to look at our track record of steadily posting high gross margins whether our growth was high or low, we have always had this concern. I am not saying that for this year, but for subsequent years.

If there is one thing that will tend to be of great help for our gross margin in the future, it is the Marketplace's growth, but once again, as I said in reply to Fabio, I think that this is not something for this year but for the next few years. As we scale up, this will improve gross margin and help ensure a healthy gross margin for us.

Guilherme Assis:

Good. I think that's fine. Very useful, Fred. Thank you.

Operator:

We are now ending the question and answer session. I would like to ask Mr Trajano to make his concluding remarks. You may proceed Mr Trajano.

Frederico Trajano:

Once again, on ending this call I would like to thank everyone, especially our team who worked very hard this year. It was another very challenging year from the point of view of the macroeconomic context. I do not wish to in any way underestimate the importance of the job they did and their hard work, which was very assertive from the point of view of the initiatives taken. Many of them are here for the call and listening to us now.

I would also like to thank our shareholders and investors who participated in the process and gave us their vote of confidence. Many thanks to our customers who have been loyal to our business. I hope to reward them even more with even higher levels of service and delighted customers, with good service on every level. So it remains to me to end the call with a context of gratitude and one - I would add - of moderate optimism in relation to 2017.

I think the Company is in very good shape and ready for this year. I am sure this year will not be as difficult as last year. Finally, I would like to end on a note of moderate optimism for 2017, which is our 60th anniversary. Few companies have the privilege of doing business for such a long time in such an uncertain setting as Brazil's. We are celebrating our anniversary with the high spirits of a startup. I like to boast that Magazine Luiza is a 60 -year-old startup and we want it to stay that way and never change for our company, which we are constantly changing.

Thanks and good afternoon to all of you.

Operator:

Magazine Luiza's conference call has now ended. We thank everybody who joined the call. Good afternoon and thank you for using Chorus Call.