

CONFERENCE CALL TRANSCRIPT  
**3Q17 RESULTS**  
**NOVEMBER 1ST, 2017**

**OPERATOR**

*Good morning, ladies and gentlemen and thank you for waiting. Welcome to Magazine Luiza's conference call related to results of the third quarter of 2017. Currently all participants are connected on listen only mode and later on we will initiate the Q&A session when further instructions will be provided. In case you need any assistance during this conference call, please ask the operator for assistance by pressing \*0. Now I would like to give the floor to Mr. Frederico Trajano, CEO of Magazine Luiza. You may proceed, sir.*

**Frederico Trajano - CEO:**

Good morning, everyone and thank you very much for participating in this conference call for the third quarter results of Magazine Luiza. Here with me are all of the executive officers of the company who will also be available to answer your questions at the end of the presentation.

Now, I will start with a brief presentation of the company's highlights during the quarter and then, Roberto Bellissimo, our CFO, will give you more details on the financial figures, and after that we will open for questions.

As we said before in our last call, we were very excited with the macroeconomic landscape for this quarter, already anticipated a possible pickup of the economy. And in fact what I can say is that the recession is over, we see here in the sector, mainly of discretionary goods, two years, 2015, 2016 of a high decrease, the sector fell 20% according to IBGE in those two years, even more in volume in those years, and finally the economic signals clearly indicate that the recession is over. And with the consumption that was dammed in those two years, we are very optimistic that what we found in this quarter there, in the third 'Q' of 2017, we will continue to find for at least three more quarters. I'll say that in the end. But we can affirm that the recession is over, the repressed consumption means a lot of people buying again, since the scenario is more favorable, with lower inflation, lower interest rates and the return of credit too, that we are seeing signs for all the places of increase of limit, of increase of approval, which leaves us quite confident with this matter.

Now I believe that, given the current exceptional moment of the company with a very winning and superior business model, we can say that in this quarter, in the third quarter of 2017, it was just natural that we add up to our growth of the last 5 years. So, if there were one highlight to be mentioned in this quarter, certainly a good reason for us to celebrate is our 27% growth vis-a-vis the previous quarter, remembering that we already had a very strong base in the third quarter of last year, and so we had to grow based on that very strong basis. So I imagine in this very competitive landscape and with a positive macroeconomic landscape this is very important to our results and this will certainly be the case in the next following quarters, rather than any change in this competitive landscape.

So, the macroeconomic landscape will be much more relevant for the company's mainstay and results of the next quarters, than any possible change in the competitive landscape. And I am very aware and sure of that.

I will just mention some of the highlights of our results, I think the most important is: we are implementing since the beginning of last year, with a lot of discipline, a lot of consistency, our vision to transform a traditional retail company with a digital platform into an e-platform with physical stores, based on five pillars: digital inclusion, physical store digitalization, multichannel, marketplace and the digital culture. Every quarter we present new and significant performances when it comes to the execution of this strategy.

I want to highlight our e-commerce first. We grew by the third consecutive quarter more than 50%, this quarter specifically 55%. And this without even considering the GMV of the marketplace, which we do not report yet. So, 55% compared to an already strong basis of last year, e-commerce reached 30% of total sales. I wanted to give two highlights to this growth: First is our app, that has reached 7.7 million downloads and all mobile devices, app and mobile site, already accounting for 60% of the traffic and 40% of the total sale of e-commerce. That bet we made on mobile devices two years ago has gotten paid quite a lot and it has been one of the driving forces of our growth. I also wanted to highlight the launch, 1P and 3P of our market Magalu, products of consumer goods that we launched in this last quarter also, such as personal care products, house cleaning, baby care, coffee capsules, chocolate, among others. A significant launch in the categories that, I believe will grow the most in the Brazilian future, are the categories that I call long tail, which are different categories from the ones we used to operate in Magazine Luiza. The Magalu Market is 1P and 3P. And for 1P products we are already making the purchase option available on the site and withdraw at the store.

We have seen a great success of this launch, I wanted to highlight because I also found important from the point of view of the company's future growth.

Our marketplace, also, from the numbers that we disclose, we spent less than a year to reach more than five hundred sellers in our operation, 1 million products available, coming from 40 thousand items last year, an exponential growth. The inclusion of partners such as Electrolux, Acer, Home & Video, Star 10, Clik Baby, Farmais, Kikos Fitness, among other partners who entered. I think the important thing is that even if we grow so much, the number of sellers and products, we are still the most selective marketplace in the market in relation to the inclusion of new sellers. We had almost 30% bounce rate for sellers who wanted to join our platform, because we do a credit score process, a very, I would say, in-depth analysis, to make sure that the seller that is entering will respect our standards, both ethical as well as standards of service level for the customer.

I think this is an important point, because our marketplace, for us, is a growth opportunity, we are very optimistic, it has beaten all of our internal expectations, but we will not do this to the detriment of our reputation, our quality, our level of service, our RA 1000 in 'Reclame Aqui', to the detriment of all the respect we have from consumers. So we are doing it in the most responsible, consistent way possible, and even so we are not letting it stop our growth and our internal goals.

I would also like to highlight the recovery, not from today, of our physical stores, which grew 15% in the same stores there, over a difficult comp last year of 6%, the total evolution of 19%, we are already benefiting from a process of accelerating the opening of new branches. Now besides the same store sales it is very important to look at the physical stores with total sales - a 19% growth, almost 20% in the quarter, we will continue to see good numbers because we are opening more stores and these stores will be incorporated to our total comp in the coming quarters. We opened 16 stores only in this quarter, making a total of 39 stores in the last twelve months. And as we have already announced, we must open 30 stores, 60 stores this year, 30 more stores are missing for the last three months of that year. So, we believe that it

will beat this number, that we have already released to the market and we have the use of proceeds of the follow on that we did, I will speak a little bit more about that later and accelerate even more this store opening plan.

I also wanted to point out that in these parameters of digital inclusion, our services' sales increased a lot, this is a number that we report separately in our balance sheet too, with a highlight there for the marketplace commission, as well as the sale of digital services, of digital inclusion in the store like 'Lu Conecta', which is a service of installation and help desk for the customer, that we are selling with great success in all the stores of the group. The 'Plano Controle', also, that is to sell the data plan of the operators, and buy back as well, all these services with a very good performance, as well as the financial services also, insurance generally, that are having a spectacular performance.

I also wanted to highlight, from the point of view of the physical store process, the initiation of the pilot of 'Carnê Digital' also, which I think was the missing leg for our check in and check out process in the store to be very fast. Today the consumer, with this tool Carnê Digital, allows the seller to approve a DCC in a few minutes, performing the scanning of the customer's document, capturing digital signature and also with a process of recognition of facial biometrics.

I think it's a more analogic process that Magazine is digitalizing and we're having a lot of these ads practically every quarter here, we see that the team is in a very good execution phase, both the business area and the "Luizalabs" that gives support to all this.

From the multichannel point of view, a fundamental pillar for the company, we saw a further dilution of significant expenses, even with e-commerce growth, showing that Magazine's multichannel model is a winning model, and for 1P and certainty will be for 3P too. The In-Store Pick Up has increased greatly with our offer, in two business days, for almost all categories of almost all branches. The number of orders In-Store Pick Up has grown 250% since the beginning of the year, an absolute success and we are strengthening the multi-channel pillar also with the introduction of the possibility of store sellers selling 3P marketplace product. We have ten pilot stores and over twenty licensed sellers and by the end of next year all sellers, all 3P categories will be available to all stores, all of the Magazine's 10,000 sellers will be able to sell 3P products as well, and will be properly commissioned for this.

So the seller that puts his product in Magazine Luiza, besides selling on our digital platforms, will be able to sell in stores also, through our mobile sales. Logistically I already talked a little about the In-Store Pick Up, but also we are evolving a lot in every way. The top rate today is 98% delivery in relation to the promised delivery time. Our average delivery time, which has already been promised to the customer, is already 25% shorter than the delivery time of the competitors as in the courier mix. And we are doing almost 30% of orders in Greater São Paulo and Belo Horizonte in less than one business day. So I think it's a very significant evolution of the delivery time and at this point we still have a lot to improve. I am very confident that we will greatly improve delivery time and, thus, offer significantly lower delivery times in terms of numbers of days, obviously, to key competitors in the market.

I also wanted to highlight the roll out of another application produced by Labs, which is "Mobile Entregas", which is already on the thousand carriers of "Malha Luiza" and with more and more functionality being incorporated into it. So now we've introduced the routing feature for drivers. We already have tracking, order tracking, low order management and with that the information for the customer gets much better, so the traceability of the customer's product is already much better, with push notifications, automatic emails, etc. And we are reducing the

level of contact per order, which has dropped by 56% our contact rate from last year. And so, with this, with all these evolutions of logistics, we keep a very high mark and the RA1000 label of "Reclame Aqui", which is a condition that we already have for some time and we are maintaining, even with the growth of the marketplace in the company's total revenue.

I also wanted to highlight from Luizalabs, the 1-Touch Purchase, which was launched, is the Purchase with 1 Touch and In-Store Pick Up so we can today by the app, buy with 1 touch and In-Store Pick Up and have all the geolocation to facilitate whole process; the launch of machine learning also for automatic pricing of 10,000 products; we were the only Brazilian to launch, the Brazilian retailer, Pay with Google this quarter as well; we've made a series of improvements, both for our Digital Wedding List, which is the "Quero de Casamento", which now has an app and the "Magazine Você" as well, which is a direct sales channel for social networks, and now the seller of the "Magazine Você", the promoter of the "Magazine Você" are able, we are in a pilot phase, to sell using a credit card machine, he can sell real time to his colleague by cell phone, using a credit card machine. This is a payment feature, that is now in "Magazine Você", and I'm sure it will further expand that channel's sales. So, a lot of innovations in all five pillars of our strategy.

I would like to emphasize, to conclude, that we were elected, one more year, for the 20th consecutive year, among the ten best companies to work for, being the best retail company to work for, an indicator that makes us very proud of us, perhaps what we most celebrated in the last quarter, the fact that it is the best company to work in retail and to say that at the end of September, in September, we completed our stock offer, our follow on, capturing R\$ 1.5 billion, more than R\$ 1.1 billion to enter the company's cash, which we will put in and then we can clarify more in the questions, as we put in the prospectus, for long-term investments, but basically to conclude, continue implementing the digital transformation strategy to implement this vision of the digital platform with physical points, take this vision to more and more Brazilian markets and deepen our competitive differentials. We feel that we are already well ahead in the implementation of a vision, a digital platform with physical point. In other words, a multichannel marketplace and we want to deepen that advantage with IPO's use of proceeds, investing in technology, logistics, physical network expansion, which is so important to us in the In-Store Pick Up concept. We are calling the stores now 'shoppable distribution centers', which are sales outlets that also function as distribution centers. So, all these investments are going to be made there over the next few years. And with the inventory offering we are also confident that we can, we have great chances of entering the main market indexes, the Ibovespa, IBX-50, MSCI, in the next revisions, we are very confident about the volume that we are having in daily negotiations, that there is a great possibility of entering those indexes.

To conclude, I want to reinforce what I said at the beginning, about my optimism in relation, at least in the next quarters, the next three quarters and the end of the year here tends to be strong. Again, consumption dammed, credit is more available now by the economy, lower interest rates, low inflation, so we are optimistic about the macro scenario of this quarter and next year, and I want to reinforce that we have the World Cup. Every year, if you look at our history, we had a very positive performance in World Cup years, for the year as a whole, especially in the first half, so we have a very positive outlook for the next quarters, in a macro scenario. And from the competitive point of view I think today our biggest competitor is our comp. Magazine Luiza's biggest competitor today is Magazine Luiza from the previous quarter, and that is, it's not a soft competitor, because we're doing a very strong quarter-on-quarter performance, the base comparison for the last three months of this year is a lot stronger compared to the comparison base of the last 'Q' of last year, both for the physical store and for e-commerce. And the same will happen with the first half of next year. Despite this, with this

favorable macro wind, which was not winding in our favor in the first half of this year, nor at the end of last year, I believe that we are able to continue presenting very positive numbers in the quarters, although of course I imagine a certain deceleration, but not very expressive due to this excellent operating moment of the company and also because of this favorable macro scenario.

With that I finish my initial speech. I'll be available for questions at the end, and I'll pass on the floor to Roberto Bellissimo to talk about the financial indicators. Thank you very much.

### **Roberto Bellissimo – CFO & IRO**

Good morning, everyone and thank you very much for joining us this morning. I will start on Page 3. Here, we show the evolution of our stores, we inaugurated 16 stores this quarter and we should open 30 more stores until the end of the year, fulfilling a plan of opening 60 stores this year. We show here the increasing CapEx, we are growing our total CapEx by over 60%, when compared to last year. And with the new offering, we tend to increase our investments even further. Most of the investment has been geared towards technology, and also strategic planning.

On Slide 4, I show the performance of our quarterly revenue. It's clear here that we are growing steadily in the last 7 quarters. This, I think was the highest growth rate in the last 5 years, over 27%. So we grew based on a larger base when you compare to the last year, we grew compared to the last quarter, as well we had a very positive sales performance both on brick and mortar stores, as Fred spoke about, as well as e-commerce, the physical stores grew 19% in total, 15% same store sales, e-commerce also we grew over 50%, 3 quarters in a row growing market share as well. E-commerce as a whole in Brazil only grew 9% whereas we grew over 50%. And retail figures according to IBGE grew around 11% this quarter, whereas we grew 27% and that means that we had a substantial market share gain in both channels.

Then on slide 5, we also show the evolution of gross profit, increasing gross profit, gross margin 80 basis points lower than last year, in line with what has happened in recent quarters, due to a very accelerated growth of our e-commerce. As you know, as a trend, e-commerce has a slightly lower gross margin, but we compensate this with a much lower level of expenses. So we ended up diluting almost 160 basis points in the level of operating expenses, we lose a little margin, but it saves a lot more on operating expenses. This dilution of operating expenses had a lot to do with the growth of e-commerce, but also of the physical stores, as well as of the expenses matrix management projects and the zero based budget - ZBB. This quarter, once again, we have greatly diluted personnel expenses and a lot of rental expenses. Our rent expenses per square meter, for example, grew very little and we diluted much as a percentage of net revenue, as we grew 27%.

Equity income, again, has shown great consistency, represented R\$ 21 million, or 0.7% of net revenue, also growing in relation to last year, both Luizacred and Luizaseg. Luizacred grew 33%, Luizaseg 10% and also contributed to our total result.

And then on slide 6, we show the evolution of EBITDA, also our highest quarterly EBITDA in history, our highest quarterly margin also, 8.8%. Totally influenced by the growth in sales, e-commerce, the dilution of operating expenses and the result of Luizacred and Luizaseg. We went from 8% EBITDA margin to 8.8% this quarter.

Then on slide 7, we also show a very significant evolution in financial expenses, we have diluted financial expenses by more than 200 basis points, going from more than 5% to less than 3% of net revenue. This had no effect yet from the follow-on that was settled in October.

So here the reflection was mainly the reduction of the company's debt, strong cash generation in the quarter and the last two years and the reduction of the CDI also helped. We have diluted both prepayment interest and the other financial expenses that are more related to the company's debt, which fell a lot, represented only R\$ 20 million in this quarter and tend to be lower from now on with the resources of the offer as well. We even announced yesterday at the board meeting that we approved the prepayment of four issues of debentures, so we tend to reduce our level of short-term debt and consequently our financial expenses. We ended the quarter with a lot of cash, before the offer we ended up with R\$ 1.2 billion, plus R\$ 1.1 billion of the primary offer, so we can reduce our debt and maintain a lot of liquidity. Commenting here on working capital, we again improved working capital indicators, improved inventory turnover and improved average purchase times at the same time, reduced the inventory turnover in 9 days, this also has much to do with the growth of e-commerce. And then, again, our model is fully multichannel integrated, all DCs are shared, so this tends to greatly optimize inventory turnover. And especially in e-commerce, we have turned inventories at a very fast speed. Adjusted working capital improved by more than R\$ 500 million in the year and adding to the profitability of the operation, plus the improvement in working capital, we reduced net debt by more than R\$ 700 million in 12 months, and in this quarter in more than R\$ 200 million. So operating cash generation has been very positive, cash flow from operations reached almost R\$ 1 billion in 12 months and in the quarter was also very positive. We are in a very good moment, both results and cash generation.

Slide 8 shows the evolution of net income as well. Here, again, increasing net income has not yet had an impact on the supply yet, but we have already achieved ROE of 43% and ROIC of 36% in the quarter, due to all these operational and financial improvements.

After speaking a little more about Luizacred, I think it's worth noting that it also grew 27%, that is, it grew at the same pace as Magazine Luiza, with a highlight for the Luiza Card within Magazine, which grew almost 50%, so I think which is a very important indicator of the loyalty of our client, of our Luiza Card. And we grew sales of new cards, grew active base, activated base, which is the base that buys every month, frequency, average ticket, all this contributed to the total billing of the card, in that house of 27%. Better still, we're managing to grow all this with a reduction in delinquency, so the NPL 90 hit the lowest level in the last five years as well, dropping to 8.3%. And the short-term NPL also fell sharply, to 3.1%, and at the same time we increased the coverage ratio, we increased surplus provisions. So this also demonstrates the quality of Luizacred's result.

Then, on page 10, Luizacred's net income evolution quarterly, also showing improvement in the third quarter compared to the second quarter, when we made the reduction of the interest rates. We grew our Luiza Card portfolio, at the same time as the CDC portfolio declined, but the total portfolio grew 20% to R\$ 5 billion. More than 3 million cards, with all these improvements and a return on equity of over 20% in Luizacred as well.

Now I turn the floor back to Frederico for the final considerations. We are available for questions. Thank you very much.

**Operator:**

*Ladies and gentlemen, we will now begin the question and answer session. To ask a question, please dial star 1 (\* 1). To remove the question from the list, dial star 2 (\* 2). Our first question comes from Luiz Felipe Guanais, BTG Pactual.*



**Luiz Felipe Guanais – BTG Pactual:**

Good morning Fred, good morning, Beto. I wanted to explore one point, you commented on the favorable environment for the economy over the next few quarters, but I also wanted to hear a little bit about how you have looked at the competitive environment, not only in relation to the level of service, which I think will be a very important driver, especially when we talk about growth in the marketplace, but also about price rationality and take rate. Thank you.

**Frederico Trajano - CEO**

Well, Luiz Felipe, good morning, thank you for the question. Well, so my point is this, I think the favorable macroeconomic environment will be much more relevant to the company's numbers than a possible change in the competitive landscape, which until now I have seen that no significant change has taken place, and I do not expect any significant change in the competitive environment for the coming quarters. I cannot talk in three, four years, but for the next few quarters I imagine it will continue very similar to what we saw, especially in the last quarter. I think the most correct way to put this is to incorporate the macro factors, which are very significant considering this consumption dammed for the last quarters of this year and considering World Cup for the first half of next year, which is usually a very positive season for the sector. So I see that it is more relevant and I do not see anything significant in terms of pricing. You see that our evolution of EBITDA margin, which is relevant here for the discussion, was once again positive in the quarter. The fact that we dropped gross margin in the quarter was specifically due to channel mix, the channels themselves presented similar results to the same quarter of the previous year, which shows that it does not have a very significant competitive dynamics. October is now over, I have not seen any major changes in terms of price changes, etc. and such. And we are managing to grow with very healthy margins, including in terms of EBITDA margin with our multichannel model, as a superior model, because we can grow e-commerce by diluting general expenses, we have one of the lowest indexes of SG & A in the history of the company, is a very low index, which shows that we have a very robust model to face any competitive scenario. But I say again that we are always paying attention to the competition, we respect all the competitors in the market, but I reaffirm my optimism with the macro scenario and with the company's business model, which I think is a winner both to the physical world and, above all, to the secular growth of e-commerce. I think that today we have one of the only models that can capture the growth of online with the result, and this I find very difficult to achieve in the Brazilian scenario, without being a truly multichannel operation like us. So I reaffirm my optimism there, at least in the coming quarters in this regard. I reinforce that our biggest competitor of this quarter will be our comp.

**Luiz Felipe Guanais – BTG Pactual**

That's great, Fred, thank you so much. If only I may ask a second question, in relation to the In-Store Pick Up pilot project involving the marketplace. Thinking about evolution over the course of next year, as you mentioned, would that involve the complete assortment of the marketplace or at first would it be more targeted to some specific SKUs?

**Frederico Trajano – CEO**

Just to clarify, Luiz Felipe, thanks for the question again, what we launched now was the product sale of the marketplace in the store. So, all of the ten Magazine Store sellers are selling products from twenty 3P sellers, and that we're going to roll-out to 100% of stores, 100% of sellers next year. That is, it is selling the 3P product in the store, delivery continues to be executed, for now, by the seller himself. For next year we will make the pilot of Fullfillment By Magalu, that is the pilot in which the seller will inventory his product or use our distribution network for the delivery of the product, which we commented, that people will probably be

piloting this next year and should have the definitive roll out over 2019. So that's a bit of our vision, Fullfillment pilot By Magalu next year with a roll out in 2019.

**Luiz Felipe Guanais – BTG Pactual**

Great, thank you very much.

**Frederico Trajano – CEO**

Thank you.

**Operator:**

*Our next question comes from Robert Ford, Merrill Lynch.*

**Robert Ford – Merrill Lynch**

Thank you very much, good morning everybody and congratulations for the results Fred and Roberto. In the Earnings Release, you indicate improvement and conversion across all channels. Let's talk a bit about this performance and the operational improvements you made, please.

**Frederico Trajano – CEO**

Bob, good morning, thank you very much for the question. Well, I think in terms of conversion, Bob, I wanted to highlight, in the online channel, specifically, our app. We have invested heavily in the mobile app in recent years, we bet that online consumption in Brazil was going to migrate to mobile devices and mobile devices, they historically have a lower conversion, but we managed with an app, I think, very well designed, with low friction, with enough personalization, use of big data, etc. and such, have in our mobile app a conversion even higher than our desktop, which is very rare for mobile applications, and with that we are getting a growth increase in digital channels. I think in the physical stores I think we have a whole job of supply, distribution of products, reduction of break even for the site, we reduced rapture. Even reducing the inventory level, you saw that we improved the inventory management greatly in this quarter, we reduced the level of rapture, with enough assertiveness. So the in-house areas that are working on this part of the supply are doing an outstanding job both in the physical store and in e-commerce, remembering how much our inventory is integrated, once we hit one, hit the other automatically as well. And the better distribution on regional DCs as well. So all this has been improving our conversions. And lastly I wanted to point out that maybe Eduardo and Fabrício could highlight an additional point, Eduardo Galanternick, of e-commerce, and Fabrício of physical store, which is the In-Store Pick Up. Our In-Store Pick Up offer is a very appealing offer for the consumer, because it is delivered within 48 hours without freight cost, for all stores in Brazil. And In-Store Pick Up, as I said, increased 250%, it is helping a lot the conversion of the site, because the consumer does not pay the freight and can withdraw his product in 48 hours, remembering that in Brazil we have problems scheduling deliveries, we have problems, delivery times are all very high, so In-Store Pick Up has also helped the conversion of channels. I do not know, Eduardo, Fabrício, do you have anything to add on the subject?

**Eduardo Galanternick –E-commerce Director**

Good morning Robert, it's Eduardo speaking. Just to add something, it is important to note that this conversion growth happened on all devices, and in the general device mix, as Fred spoke, pushed from the conversion improvement on the mobile. From the operational point of view, we achieved for the products of 1P the lowest level of historical breakdown and this is a lot due to a new system "customers to buy" that we implemented and also due to multi-channel management that we have commercial, we managed to have the lowest level of rapture improving the inventory turnover. Generally speaking the other points are the



deadlines, Fred talked about the In-Store Pick Up on our offer, but we also had a "last mile" average delivery time reduction, so an important component to the conversion. A general word for competitiveness, pricing, we are a little better than last year, but not very different, as we saw this rationality has been perceiving in the market for some quarters and this conversion growth still do not consider the conversion growth coming by the marketplace sale. When you put these orders on our visit basis, the conversion gets even bigger. Thank you.

**Robert Ford - Merrill Lynch**

Thank you. My last question: It indicates a much more rational competition, but my question: what implications does it have in the entry or expansion of Amazon Brasil, some for you? Or does it have a very short term impact in terms of value proposition?

**Frederico Trajano – CEO**

Bob, I think our vision for the business model, the pillars of our strategy, it remains completely unchanged. We trust that the best way to take advantage of the growth of e-commerce is through a digital platform with physical points, in other words the multi-channel marketplace. Given Brazilian structural problems, the physical store is a great leverage of our e-commerce market share. So the possibility of picking up from the store, returning it to the store, using the same logistics network of the store to deliver to the site confers us with respect to any competitor a competitive advantage that we think is solid and that we want to take to new markets, passing the store base now. So, as we have talked since the Offer and I think it is very clear in our prospectus, what we really want is to deepen the implementation of the same vision, without any change, because we believe that for Brazil, both the e-commerce as the retail as a whole, the best model to grow with profitability, and I highlight with profitability is the multichannel model. So we want to go deeper into it, but to incorporate the marketplace element, which is so important, and that we have done successfully.

**Robert Ford - Merrill Lynch**

I think an important return will be the reverse logistic. You have free shipping and I think in the long run you will have the free returns, and free returns to the marketplace. Let's talk a bit about the timeline for the marketplace in Brazil, please.

**Frederico Trajano – CEO**

Right. Reverse logistic is a big issue here, it's a great theme indeed. Today approximately 20% of e-commerce purchases are returned in the store, it's free, the consumer goes to the store and returns the product. The stores are, as I say, shoppable distribution centers, they are distribution points for e-commerce, I reinforce the importance of the multichannel model that we have been developing for 17 years, so we did not start it last year, the last year, we have been deepening this model for 17 years. The challenge we have now is to have more coverage, because today our coverage is for less than 50% of the Brazilian population, hence the importance of increase the pace of expansion. It may seem like a contradiction, a company that focuses so much on the digital open physical shops, but we think it is just the opposite, our great competitive differential of e-commerce is the physical presence for both In-Store Pick Up and reverse logistics. And I think that as we expand our capillarity of stores, we can achieve this as an even greater competitive advantage for the rest, the other 50% of the Brazilian population. So we're betting a lot on that, and I think with the Fulfillment by, reverse logistics will also be available for 3P. So, of course, we're going to put a lot of effort into implementing and roll outting, so our seller can use exactly the same distribution loop, both on the first leg and on the reverse leg, which our 1P uses very successful and very profitably. So everything we do for our 1P we want to make available to our 3P, and that is undoubtedly one of the top priorities of our strategic planning, which is the pillar of the marketplace.

**Robert Ford – Merrill Lynch**

Thank you very much, Fred. Again, congratulations.

**Frederico Trajano – CEO**

Thanks, Bob.

**Operator:**

*Our next question comes from Tobias Stingelin, Credit Suisse.*

**Tobias Stingelin – Credit Suisse:**

Hello, good morning, congratulations, Fred and Beto, everyone who's there. The first question is this: I know that you do not give guidance specifically in relation to the margin, but do you think that the margins should have room to grow beyond the levels they are now, or according to what you had already said in other calls, you are not looking to maximize the margin, that is, to pass the margin beyond a certain ceiling, and much more trying to focus on competitiveness, to make the market grow more. I think this would be the first question and the second, taking advantage of the questions that have already been asked about the marketplace, but can you give a little update on the initiatives that were done during this quarter, Fred? You have already spoken in the press release, you have already spoken a little more in the call, but could you just talk about how this business is evolving, you are not releasing numbers yet, but if you could give a summary I think it would help too. Thank you.

**Frederico Trajano – CEO**

Tobias, thank you very much for your question. I wanted to address the first issue of the margin. I think we keep it this way, the main focus of the company is on growth, and the margin, what has happened in terms of margin has been through, as we are growing a lot, we are managing to dilute expenditure, we have a basis of fixed expenditure still significant in our total expenditures, it amounts to almost half of total expenditure, fixed expense. So when you grow significantly above inflation, above the market, you have a great spending dilution power, so I believe we see with optimism the possibility of continuing to make gains in that direction. What we can do, what we have announced Tobias, is that we want to reapply part of that margin and then I can not even give guidance to this to increase the level of services. So it's more investing in DCs, investing more in logistical capacity so that we can reduce the deadlines that are already in the average better than the competitors and we want to make it even bigger. And invest a lot in technology too, expanding there our teams, both the marketplace and Labs to invest in this channel that tends to grow so much in the future. We believe that if we did not do this reinvestment in the service level, the margin could increase a lot, but as we are redoing it, I do not expect large margin increases, I expect a high growth and an improvement in the level of service. The company's focus, the drive I am giving here for my executives is: increased sales, increased level of service, but with a certain preservation of profitability. I do not believe in, I want to reinforce this, very significant investments in growth that represent very sharp declines in margin. I think in Brazil, we are having a good time right now, but in five quarters we have elections, and any scenario can happen. So, I think the most responsible for leaders that operate in the market as unstable as Brazil, is you preserve your margin, because today is good, tomorrow may be bad. So reinvesting a potential future margin gain on the service level is okay, now, greatly reducing your margin with that American model of growing up, giving up, I think it's not a sensible decision for the Brazilian market. About marketplace, do you want to give a highlight, Eduardo? About marketplace, please?

**Eduardo Galanternick - E-commerce Director**

I think in general the marketplace, all the work of the Labs' team with our business team has been doing throughout this year, they are in fact delivering everything that we expect, by far.

From a platform point of view, in addition to all the incremental improvements we made at Integra, which was the company we bought at the beginning of the year and that is allowing us to grow sellers as we need them. We had some important points, as Fred said, the implementation of the credit score for the entry of a seller, where we can filter through not only the documents but also some aspects of business, and try to preserve the suitability and the quality of the sellers that are on our platform. In general, what we realize is that we came with 500 sellers to more than one million SKUs, we believe that it does not have to have 10,000 sellers to have 5 million SKUs as the market has today. What we believe is that we must have the best sellers and go look for sellers that today do not sell within the platform, do not sell online to our platform and suitable companies. I think the other two highlights were the launch of our ad platform, so this is already inside the Integra for our sellers, they can buy directly in the Integra advertising space. This was released at the end of August, with more than 20 advertisers, including sellers and industries that are using this platform. And I think the best news was really the launch of the marketplace in store, and with that I think we have a great opportunity of growth.

**Tobias Stingelin – Credit Suisse:**

Wonderful, thank you. And one last question now, Fred: Specifically, I mean, you guys have fantastic results, I guess, I do not know how your budgets are, if they should be getting better or not, but of course, obviously very strong numbers. Any provision in relation to, for example, bonus payment, which is already being made from quarter to quarter, taking this into account?

**Frederico Trajano – CEO**

Yes, it is. We will not have any surprises in the 4th quarter.

**Tobias Stingelin – Credit Suisse:**

Wonderful, thank you. Good Morning.

**Operator:**

*Our next question comes from Rubem Couto, Itaú BBA.*

**Rubem Couto – Itaú BBA**

Good morning people. I think all the questions I was going to ask were asked, but if you can comment on the working capital I think the improvements continue to be quite successive from quarter to quarter. But does this level that we see now in the third quarter has some specific line that has some effect, perhaps not recurring, or maybe we can assume a stability at this level that has been running in these last twelve months?

**Roberto Bellissimo - CEO**

Good morning, Rubem, thank you. No, so it is totally recurrent, every quarter, in fact, we have been evolving very consistently. It's a trend in fact, we've been talking about it, which is also related to the growth of e-commerce. In e-commerce we have a much better turnaround than the market and maintain the same terms of purchase that we have in the physical stores, because we are a fully integrated company. And as the product is on the DC, all channels can sell, we optimize inventory turnover and e-commerce benefits from purchases made by physical stores and physical stores also benefit from e-commerce purchases, by optimizing inventory turnover, as e-commerce grows faster than physical stores in the future, we tend to continue pulling product inventories down, improving working capital, maintaining the average purchase. And besides these two important accounts, we have also managed to reduce the tax line to compensate, we stop accumulating, we have a special regime related to tax substitution not to collect more taxes in duplicate as it was in the past, and now we are reducing this line in a rhythm of about R\$ 100 million per year in the last twelve months. So, the main lines of

working capital, we have addressed in a very consistent way and the line of accounts receivable, is basically credit card receivables, this quarter we reduced the discount a bit, but it is a line totally manageable. So what's more important here is that the balance of suppliers is much higher than the balance of inventories, the supplier finances our inventory and as we grow we must continue to improve this. In the fourth quarter seasonality helps even more, so we should further expand that difference between suppliers and inventories, generate more cash, and we plan to do that going forward as well. And with the marketplace we can also do better yet, working capital related to the marketplace also tends to be negative. So we are in a very positive working capital management situation and we tend to improve.

**Fabrício Bittar Garcia – Comercial VP**

I think, good morning, Rubem, it's Fabrício who's speaking. I think the good thing about managing our inventory has evolved a lot this year, as Beto put it. I think our multi-channel OTB that we have implemented and rollouted for all categories has a positive effect on this management. The integrated store-to-e-commerce inventory helps a lot and the sale of the other channels as well, but I think one interesting point is that we have greatly improved our assertiveness of distribution to the store, this greatly improves the management of our inventory. We now have an assortment defined by store, we call it "common trunk", and that helped a lot. And we have a lot of management over the inventories, the quality of it. That is, we have a fairly strong store-to-store performance, and our inventory has been dropping quite a bit throughout the year. I think these three points, these three pillars that have made our inventory management much better, besides the negotiation of suppliers, the lengthening of deadlines, which we have already mentioned here.

**Roberto Bellissimo - CFO**

There is a point, with the In-Store Pick Up in 24 hours we have improved the frequency of supply in the stores. And by increasing the frequency of the supply you can have a smaller inventory in the store and supply the store more frequently, this has greatly helped our management. Without losing sales and without breaking store product inventory.

**Rubem Couto – Itaú BBA**

Very clear Fabrício e Beto, thank you for your answer.

**Roberto Bellissimo - CFO**

Thank you, Rubem.

**Operator:**

*Our next question comes from Guilherme Assis, Brasil Plural.*

**Guilherme Assis – Brasil Plural**

Hi good morning. Good morning, Fred, Beto, everyone, thank you for submitting my question. I have two questions, in fact, is that we have already explored a lot, you commented a lot, Fabrício was talking about the issue of inventory working capital. I just wanted to try to reconcile with a vision a little more short term, we saw there a significant reduction in the inventory level, and we are thus preparing for the fourth quarter, for the next few weeks, which are the two most important events industry today, both Christmas and Black Friday. I wonder, does this inventory reduction have anything to do with any expectation you're already seeing there in the fourth quarter, the sales position for these events, or does it just reflect that synergy efficiency gain from the models you're talking about? That is one question. And the second question is in relation to CAPEX, you said that you will deliver the 60 stores this year, the great part of CAPEX is being invested in technology, I wanted to know, looking ahead,

what we should expect in terms of CAPEX for the technology and also in the level of expansion of your stores? Those are my questions, thank you.

**Roberto Bellissimo - CFO:**

Good morning Guilherme. Thank you too. I will first comment on working capital. We have managed to improve the inventory turnover for operational efficiency, for all these processes that we have commented on, but nominally the inventory has grown, if you look at it like that in a sequence, September's inventory was higher than June's, and was higher than last year's September. But we managed to grow much more the revenues than we needed to increase inventories. So it was basically efficiency gain, improvement gain in these processes. And we're fully stocked with the quality of inventories, even better than we were last year, for the whole quarter, which is the best retail quarter for sure. You do not have to worry about that because, certainly, we are well-stocked and strong by the end of the year.

**Guilherme Assis – Brasil Plural**

That's ok.

**Roberto Bellissimo - CFO:**

And in relation to the future CAPEX, we do not give CAPEX guidance, what we can say is that we raised the resources with the follow on offer, we explained that 60% of the primary part will be destined to increase investments, including investments in technology, logistics, new stores and store remodeling and 40% is basically aimed at reducing the company's debt, optimizing the capital structure and at this point we just announced the reduction of close to R\$600 million of debentures, which we must now carry out this quarter by reducing debt. And the part of CAPEX will be invested there over the next three years, we have been saying that the pace of inaugurations has increased, this year is already an example of this, we should open 60 stores, compared with an average of 20 to 25 stores in recent years. We still only cover half of the population, we have a very large space to open new stores and now most of CAPEX, as has also happened in recent years, will be dedicated to technology and logistics. As we open more stores, we should open more DCs too, being closer to our consumers and this helps e-commerce as well. And nowadays almost half of CAPEX is being made in technology to support the growth of e-commerce, the growth of the marketplace, and all the multichannel projects that we have implemented within the digital transformation.

**Guilherme Assis – Brasil Plural**

It's good, it's great. Just on the issue of store expansion, I think you mentioned well, of course, that you have increased from a pace of about 20, 30 stores a year to 60 this year. Is this a pace that you think is sustainable for the next three to five years, that level of new stores opening?

**Frederico Trajano - CEO**

Guilherme, when we published 60 it was because we had a CVM's Notice, so we can not comment about quantity, but what I mean is that we have raised funds to accelerate investment, including opening stores. So we want to speed up store opening. I can not give you numbers or give any guidance on that.

**Guilherme Assis – Brasil Plural**

OK, it's great, thanks Fred.

**Operator:**

*Our next question comes from Maria Paula Cantusio, BB Investimentos.*

**Maria Paula Cantusio – BB Investimentos**

Good morning everyone. Congratulations on the results, thank you for receiving my question. I was wondering if you can give a little more detail on the store digitalization, you commented that now the emission of the “Carnê Digital” is now available for the salesperson to do. I wanted to know how the issue of credit analysis rolls out, whether it is done by the salesperson, and how this can benefit the dilution of expenses in the future, with even greater reduction of store staff. And my second question is about the same store sales growth in the quarter of 15%, if you could open up to us which regions that stood out the most. We've also seen that virtual stores continue to grow well above ordinary stores, if you can also tell us which regions and which types of stores you want to invest the most in the fastest expansion plan going forward. Thanks.

**Marcelo Ferreira – Luizacred Director**

Good morning Maria Paula, Marcelo Ferreira, from Luizacred speaking, how are you doing? I'll explore a little bit for you the issue of store digitalization, the credit issue. As you know credit is a super important leverager for the sales of Magazine Luiza. And the customer experience will be greatly improved, and we are already seeing in the digital CDC, as Fred said, a fairly large improvement in the customer experience at the time of approval. And more importantly, the integration between the credit system and the store's sales system, that is, runs out of friction for the customer. The next step is the card, so today we already have a process that we call "Crédito Certo", that allows the seller to identifies which customers are with pre-approved credit and we have a very great approval feeling, but we still have to make a separate purchase process from him for the issuance of the card. Next year we will have this process fully integrated with the sale, which will be totally frictionless, much better than we have today, and we are very excited about this process that will bring a lot more customers, and the customer experience will be much better than we have today. So for next year we already have this process starting in the stores here.

**Roberto Bellissimo - CFO**

Just to add something Maria Paula, we have already started the pilot, so as Marcelo put it, next year we will rollout all this and since it will be a pilot for “Carnê Digital” and is in the development phase of this pilot for the Luiza Card. And now the approval process does not change, it's still a credit score, it's still a decision of the bank, which only makes it easier for the seller to attend to a process that took tens of minutes before, and in the pilot, a few minutes.

**Marcelo Ferreira -Luizacred Director**

Yes, the credit policy remains the same, but the feeling for the customer is not a non approval, he will not have the feeling “I tried and failed”. I mean, we will have the offer, it will only get the yes, which greatly improves this experience for the customer. And we are much happier to be able to serve all customers with this credit approval.

**Fabrcio Bittar Garcia – Comercial VP**

Good morning, Maria Paula, its Fabrcio speaking. On the question of growth, actually our store growth was robust and one of the highlights of it was that we grew well in all regions. All regions grew more than double digits, the Northeast performed a little better and the highlight of the quarter were the virtual stores, which grew very well, as well. We had growth in all regions, in all types of stores.



**Maria Paula Cantusio – BB Investimentos**

And you can tell us, what are the opening focus of the next stores, if they are virtual stores because they have grown above average, what regions should you focus on, that kind of stuff?

**Frederico Trajano - CEO**

Good morning, it's Frederico speaking. We have, as a matter of priority, still many spaces to open in the present states, there are 17 states out of the 27 total, and we can enter into new states that we will not announce now. But we have already mapped dozens of cities and potential neighborhoods in today's cities, new cities and neighborhoods, we have opened enough virtual store to a city of up to 50 thousand inhabitants, we will continue to open. The proportion will depend on what we think, we have a very hard criteria here today to find points. The percentage of rent over billing, value of the investment in the property, attractiveness of the city, so we cannot talk: it will be 50% virtual, 50% conventional because it depends, we depend on finding it. But we have several potential mapped points with virtual and conventional opening, as long as we manage to balance the financial issue, that is, the rent versus investment in the point, size of the city, we are opening. So, we do not have to specify, we do not have a percentage target, but we have opened a lot of virtual and conventional store and we intend to continue opening the two without major changes of proportions.

**Maria Paula Cantusio – BB Investimentos**

Okay, thanks guys and congratulations for the results again.

**Frederico Trajano - CEO**

Thank you, Maria Paula.

**Operator:**

*Our next question comes from Irma Sgarz, Goldman Sachs.*

**Irma Sgarz – Goldman Sachs**

Hello, good morning. Most of my questions have already been asked, but if I may, quickly, if you can open for me how much of your sale is already being picked up in the store. I do not know if this was given somewhere, but I did not find it here. And I found your initiatives quite interesting to expand this also into the marketplace. And perhaps connected with that question, what is your idea, and I understand that it is a project to pilot in 2018, rollout in 2019, but thinking a bit, in your head, where would be the inventory of the top sellers of your platform in 3P, would it be potentially within your distribution centers or maybe part of that will be the exchange when the order is made? Thanks.

**Frederico Trajano - CEO**

Irma, please, can you repeat the second part of the question? I did not understand well. Please.

**Irma Sgarz – Goldman Sachs**

Sorry, the second part of the question is where in the model of fulfillment By Magalu where would be the seller's inventory of the marketplace? That is, do you have plans to have the seller's inventory, the marketplace within your distribution centers, or maybe a portion of the inventory, the part that has the highest turnover in it?

**Frederico Trajano - CEO**

Now it's clear, thank you. Well, on that last question, we imagine that the seller's inventory, ideally can be in any distribution center of the company, today we have ten, tomorrow we will

have more, obviously, because there is a plan to open new DCs ahead. So the seller will choose that distribution center that makes the most sense to him, the proximity to his DC. Remembering the fulfillment by, and in the future may even be in the store as well. I wanted to say that we are converting 30% of store space into storage area for e-commerce, this for 1P and in future for 3P as well. That's why we have called our stores 'shoppable distribution centers'. So we will make an investment in remodeling in all our stores to adapt the storage areas around 30% of the area of the store, both virtual and conventional, to also function as drop shipping points, cross docking points, and even store high turnover products. Remembering that it only makes sense to have high turnover products in turn, smaller spinning products you better have more centralized in centers, in full distribution center, which are the 10 that I said. So, answering your question, it could be in each of the ten of today or would be more in the future, and also in our 800 stores, which will be more in the future as well. So that's the vision, but we still have a lot of implementation effort ahead. We'll pilot seller inventory on one or a few DCs as early as next year or rollout for all DCs and stores over the next few years. Remembering that obviously only makes sense to be in store products of very high turnover, will be a small part of the total SKUs, is not relevant. About In-Store Pick Up , today there is much discussion about the methodology to indicate this number. Our current number is everything we sell on the site, 20% is picked up at the store, around 20% is picked up at the store. So that's our current indicator of all products, I'm not just talking about eligible, I'm talking about 100% of the website's billing, 20% is picked up in the store. So I think that's the number you can keep in mind, that number is going to grow a lot because it has grown 250% just in that year, from the first quarter to the third quarter, and we believe it's one of our big differentials. But since there is a lot of confusion about the indicator, from eligible, not eligible, it is: from everything that we sell on the website, 20% is picked up in the store today, it is a number that tends to grow a lot for the next quarters.

**Irma Sgarz – Goldman Sachs**

Perfect, very clear. Thank you.

**Frederico Trajano - CEO**

You are welcome.

**Operator:**

*We now conclude our Q&A session. I would like to leave the floor back to Mr. Frederico Trajano for his final remarks. You may proceed sir.*

**Frederico Trajano - CEO**

Well, once again I wanted to thank you for participating, for the confidence of all our investors, the new ones, those who were already with us and the new ones who joined in the follow on. I reinforce my optimism with the coming quarters, given the more favorable macro scenario and the excellent moment of execution of the company, in spite of our comparatives that are difficult for these next quarters and I am optimistic about the macro scenario. I am also grateful for the commitment, the work and the good execution of everyone in the Magalu team who made another positive quarter, the seventh consecutive quarter above market expectations. I hope to continue to meet the expectations that are placed for our company. So, good morning everyone. Thank you one more time.

**Operator:**

*Magazine Luiza's conference call is now concluded. Thank you very much for participating and have a good day.*