

## **CONFERENCE CALL TRANSCRIPT**

1Q17 Results

May 5, 2017

**Operator:**

Good morning, ladies and gentlemen. Thank you for waiting and welcome to Magazine Luiza's conference call for the 1Q17 results.

From this moment on all participants will be in listen-only mode during the Company's presentation. Then we will open up for our Q&A session and additional instructions will be provided. If you need any assistance during the call, please ask an operator for help by pressing \*0.

Now, I would like to give the floor to Mr. Frederico Trajano, CEO of Magazine Luiza. Please, Mr. Trajano, you may proceed.

**Frederico Trajano:**

Good morning, everyone. Thank you for joining our earnings conference call. Together with all our executive officers, I am here today to discuss our 1Q17 figures, which this quarter came well above the market expectations also above our expectations with very positive figures in almost all the fronts.

Putting into context current scenario, now we are dealing with an economic scenario less unfavorable than in 2016. This does not mean that the wind is in our favor, but at least, this is not a headwind. The sector slightly grew 2% according to IBGE in 1Q17. We saw a significant drop during same period last year. At the same time, we face a favorable competition scenario with large more rational players, both online and offline, focused on profitability. This was always Magazine Luiza's standpoint, which never changed, regardless of economy concern. Then, from the moment when large players become more rational, such scenario becomes more favorable to us, which structurally we always adopted such strategy, and small players face drawbacks from the product supply viewpoint, the credit to buy the product and credit to finance clients, allowing a scenario of consolidation and continued gain of market share.

Within such less unfavorable macroeconomic context and favorable from the microeconomic viewpoint, we are operating with a well-structured operation, a lined up, focused and motivated team, and well-standardized and well-defined digital strategy, we managed to report a favorable result in absolutely all the balance sheet accounts. Sales grew at physical stores and outstandingly another quarter at e-commerce. Expenses were diluted, delinquency decreased, profitability of Luizacred increased, we sold more financial services, we generated cash and used it to reduce our indebtedness level. Positive figures were seen in practically all the balance sheet accounts, and we are very pleased with global results achieved this quarter, as it is not common for a first quarter, when we usually see a difficult seasonality, then, it is not usual to report such type of result. Soon Roberto will detail the figures.

I would like to end my presentation talking a bit about the future. We are in full swing implementing our digital transformation project, our strategy focused on evolving the marketplace in 2017. We have five pillars. The platform pillar, which represents the marketplace pillar is the one we are highly intensifying this year. We saw a record entry of new Sellers in 1Q17, especially in April. The Company recorded the highest number of new Sellers entering in April, after closing the quarter, already reaping the benefits even from the acquisition of the startup company in Minas Gerais, Integra Commerce, which helps us. The main focus of this acquisition was to speed the integration of new Sellers and the year of 2017 exactly focuses on the expansion of the Sellers base and the platform maturation. We are not so focused this year on GMV, but on introducing new Sellers; we have several outstanding Sellers which joined our base and were mentioned by Management in our earnings release disclosed yesterday.

Looking ahead, I do not expect great changes in scenario, neither from the competition viewpoint nor from the macroeconomic viewpoint for the second quarter. I am expecting a second quarter in line with the first quarter in all the aspects I mentioned at the beginning of the call, but I can foresee changes in the second half of the year. There are few issues worth mentioning for the second half. We will have a basis of comparison more unfavorable compared to the first half, because we performed very well in the third and especially in the fourth quarter last year, then we will have a more challenging base both in e-commerce and in physical stores. In my opinion, we will also have more organized competitors, not a fierce competition in terms of price, nor in terms of profitability, because this is not an option for everyone, I think now this is an irreversible path of more rational operations, both online and offline, more organized and focused players, and let's say, hectic competition scenario. On the other hand, we will also have, I expect and we believe in a more favorable macroeconomic scenario and wind blowing in favor of our business, higher sector growth as a whole, also interest rate decrease, higher confidence index, which will be more relevant, to the extent the quality of reforms approved in the second quarter improves. But regardless of anything, we expect a favorable second half, and in our segment, it has been a long time we do not catch a tailwind. In view of such scenario, we intend to maintain our focus on execution, implementation of our digital strategy, the motivation of our team, our employees, who are essential for the success of our operations, and especially the customer enchantment.

Now, I give the floor to Roberto and afterwards we will start the Q&A session. Thank you very much.

**Roberto Bellissimo:**

Good morning everyone. I will start with our highlights on slide 2. Starting with sales, Magazine Luiza recorded total growth of 23%, one of the largest ones over the last years. Sales totaled R\$3.4 billion in 1Q17, the Company recorded same-store sales gain of 22%, also very high, pointing out the 12% increase in physical stores. Maybe this was the quarter the Company more gained market share. The market performance stood at 2%, the Company grew 23% and at the physical stores, growth was 12%. The market was going sideways.

Referring to e-commerce, this was an important highlight in the quarterly results recording a growth of 56% compared to 8% market growth. This was an extremely high market share gain.

The e-commerce share over our sales gave its highest leap also of the Company's history, from 22% to 28%, i.e., 6 points of share within one year, thus, a substantial evolution of e-commerce.

Referring to gross profit, the Company grew 22%, also a very high growth. Gross margin dropped half point, chiefly due to a mix effect. The e-commerce grew more than physical stores, but the Company managed to preserve gross margin in the two channels.

Then, referring to expenses, which was also a highlight in the quarter, the Company diluted operating expenses by 2.3 percentage points. The Company reduced SG&A to the level of 22% for a first quarter, which is also the lowest level of the past years. A solid sales growth contributed to such reduction in the operating expenses, allowing a very high operational leverage at physical stores; an accelerated growth of e-commerce, which has a level of expenses well below the average due to our integrated and multichannel strategy; and the maturation of zero-based budgeting (ZBB) projects, the expense matrix management. Several initiatives were implemented in 2016, which became more mature, thus, contributing to the Company being able to control expenses.

EBITDA recorded a substantial growth of 61% with a margin of 8.3%, our highest EBITDA margin over time, recurring and especially for a first quarter, which usually does not record the year's highest margin, due to seasonality. This was a very high margin for a first quarter and net income also jumped from R\$5 million in 1Q16 to R\$59 million this quarter, with a return on shareholders' equity of 32%.

The working capital improved by R\$380 million in the last 12 months, also we reduced adjusted net debt and accordingly, with very high EBITDA growth, we significantly reduced our leverage to 0.5x EBITDA, also one of the lowest leverage levels since our IPO, for instance.

And finally, pointing out here Luizacred, also recorded excellent results. Luizacred's profit grew over 50%. Luizacred's returned to a very high level, 28%, highlighting a very strong reduction of delinquency levels and sales growth, at the same time, portfolio growth, which is very good for the business as a whole.

On the next slides, in operating performance slide, we can see the evolution in the number of stores. We opened 18 stores in the last 12 months. We opened four stores this first quarter, according to the plan we commented in previous quarter to intensify the pace of stores opening. Thus, our investments were up more than 50%, especially in new stores and technology, in line with our digital transformation planning.

In terms of average age of stores, most stores are already mature, which is very good inclusive for the matured stores' profitability. In addition, the Northeast region, for instance, which is a mature region, continues growing in a very fast pace. Such region was also a highlight in terms of growth.

On the next slide, we can see gross revenue quarterly evolution. It is clear that this is the fifth consecutive quarter of sales growth in a pace increasingly faster. This was our highest growth rate over the past five quarters. The Company recorded sales almost the same level of fourth

quarter last year, which includes Christmas and Black Friday and R\$600 million more than the first quarter last year, which means a very high quarterly sales increase.

The Internet in the first quarter sold more than 4Q16 growing 56% over last year's growth which was very high at approximately 27%, 28%. In fact, this was a very good sales performance with very high market share gain.

On the next slide, we can see the evolution of gross profit and gross margin. I already commented that growth and the factors which justified such change in gross margin. I would like to point out here the expenses, which increased only 12%, compared to 24% net revenue growth, then, this was a very high operating leverage, a dilution over two points percentage. Practically in all accounts, the Company controlled very well fixed expenses, the administrative expenses increased slowly, the e-commerce contributed a lot, the ZBB, the expenses matrix management and also several projects referring to our digital transformation strategy, which also brought greater efficiency, more automation at the physical stores. Thus, the Company has been gaining productivity.

Referring to equity income line, Luizacred and Luizaseg recorded significant growth of profit, and equity income was 0.2 points percentage better than last year.

On the next slide, we can see the EBITDA quarterly evolution. This was the highest EBITDA over the past quarters, the highest EBITDA margin of our history due the factors already mentioned, sales growth, the positive contribution from our e-commerce, which we mentioned as a positive contribution to our results, the dilution of operating expenses, improved financial partnerships.

On the next slide, we can see the financial results: financial expenses were diluted, both interest rates from anticipation of receivables and other financial expenses. There was a dilution of 0.4 percentage point in the quarter and reminding that interest rates started to drop now. Then, the benefit of interest rates cut should be higher over the next quarters and it is worth mentioning that the cost of capital also started to decline. The Company just approved an issue, for instance, paying 109% CDI for one year, 112% for two years. Such level of spread this year is very low compared to two years ago. Thus, the Company has good prospects in terms of financial expenses dilution.

We can see here the working capital evolution. The Company now reports the adjusted working capital excluding receivables, which are practically cash. The best way of looking at the working capital is like this, and under this concept, the Company improved by R\$380 million in the last 12 months in practically all the accounts, which means, the inventory turnover substantially improved recording nearly 66 days, which is very good for a first quarter. The e-commerce growth also has been significantly contributing in this regard. This is another multichannel benefit, all our inventory is integrated and inventory turnover in e-commerce is naturally quicker, then, it has contributed to evolve the inventory turnover. At the same time, we managed to increase the average term of purchases in a very healthy, sustainable manner, without increasing our cost of goods sold, also we reduced the taxes accounts, we decreased other working capital asset and liability accounts, which are highly sustainable. Then, the Company generated R\$380 million cash deriving from working capital,

this plus the operation's results, the Company decreased the adjusted net debt by more than R\$415 million and leverage from 1.6 to 0.5x EBITDA. Again, this is one of the lowest leverages of our history.

On the next page, we can see the net income quarterly evolution. Again, the 1Q17 net income was the highest quarterly net income since our IPO, even higher than 4Q16, with ROI very relevant at 32% with a net margin above 2%.

On the next page, let's talk about Luizacred, which was also a relevant highlight. Luizacred's total sales grew 22%, a very important highlight for sales inside Magazine Luiza, which grew 45%. Luizacred's share from Luiza Card, especially in physical stores sales records its highest level in the company's history. In April, it came to 30%, for instance, added to over 10% from CDC (consumer direct credit), the Company manages to finance practically 40% of its clients and we managed to significantly increase Luiza Cards sales, at the same time reducing all delinquency indicators, pointing out the NPL above 90 days, which fell 3.6 percentage points, we also increased the coverage ratio, and reinforced provisions. The coverage ratio went from 121% to 132%, then this was Luizacred's result also very complete, with sales growth, portfolio growth, reduction of provision level by over 20%. It also started to feel the effects of borrowing cost decrease, thus, recording one of the highest quarterly profits of the past years. The Company grew 50% with return of nearly 30%.

Finally, the Company reiterates its expectations for 2017. The Company will continue capturing the gains of the digital transformation projects, significantly develop the marketplace platform, gain market share on a sustainable basis, continue focused on the SG&A expenses management as a whole, working capital, generating cash: a very important target for us, besides intensifying the opening of new stores, also benefitting from the cycle of interest rate cut in Brazil.

Now, I give back the floor to Frederico. Thank you very much.

**Frederico Trajano:**

Thank you Roberto. Now the Q&A session is opened.

### **QUESTIONS & ANSWERS SESSION**

**Operator:**

Ladies and gentlemen, now we will start the questions and answers session. To make a question, please press star 1 (\*1). To remove a question from the list, press star 2 (\*2).

The first question is from Mr. João Mamede, Santander.

**João Mamede:**

Good morning everyone. Good morning Fred. Good morning Beto. I would like to explore a little further on online sales performance, which called our attention in the quarter. Apparently, the first quarter was slightly positive for retail, as not seen for a long time, but taking into account such slightly improved macro, the Company's performance was impressive,

much above any justification that could derive from macro. We know everything you have been doing over the last years in terms of digitalization, all the initiatives, but I wanted to know a little more if in this quarter Fred, something particularly especial also contributed to such performance, as you mentioned a very strong basis of comparison of first quarter last year and despite such very strong basis, the Company managed to step up compared to the fourth quarter last year. Then, if you could explain a bit more on this issue, I would appreciate.

This is the first point. The second one, I also would like to talk about a comment you have made Fred, which is the issue of rationality, a rationality slightly higher this first quarter. What calls my attention is that, as of end of last year and beginning of this year, several competitors, at least, some of the largest competitors, also started to use the benefit of the Lei do Bem injunction. In my opinion, this could be a pitfall to the extent would create a cushion to a trend maybe a bit more aggressive from any competitor, in an attempt of gaining market share using part of such benefit. Apparently, from what you mentioned, this did not occur. I know it is difficult to make any conclusion on what competitors are thinking, but I would like to know if you have any opinion on this issue, what would have occurred for such trend slightly more rational this quarter. These are my two questions, thank you.

**Frederico Trajano:**

Thank you João for your question. I will elaborate a bit the answer, we have two parts of your question and maybe, in the first part, Mr. Eduardo Galanternik, who is our e-commerce executive officer may contribute with additional information. Broadly answering your question, specifically about the e-commerce, I think it is worth noting that the e-commerce growth, if you look at 2016, the last quarter was very good. The Company recorded a growth of approximately 40% in fourth quarter last year and now reached a level of 50%, then business is doing very well. We have a well-structured operation, a very good team, with also a positive result and I think obviously, and I like to say that, because it has a market component, besides our execution, the market is the one where all the players lost lots of money. There was a very high cash burn, which amid a scenario economically good with low interest rates is already difficult to sustain, but when you face a crisis when interest rates are high, the market is challenging and liquidity is not easy to raise money, the situation becomes unbearable. What I have been affirming for a long time here at calls, since the IPO that in a certain moment, the market would initiate a bias of rationality, even because the cash burn is unbearable in the long term. In certain moment, shareholder will want return on its capital. This moment finally came and I think this is an irreversible change. The online market, the operations which lost one hundred, two hundred, three hundred, even almost R\$1 billion in cash burn p.a., these operations will must review their strategies, and this is happening now, because the company needs to pay bills, needs to pay supplier, needs to pay expenses, needs to pay employee and needs to generate cash and we cannot always rely on the market to raise new cash. Then this change from online to rational is even more assertive than the offline change, which is also more rational. Then, when I am referring to higher rationality, I'm referring to this online market which is attempting to adopt a higher rationality, although the model I see, which is not a multichannel model, it is difficult to reach a level of rationality with a very high cost advantage compared to an online player only, because the online costs are shared with physical store and this multichannel model the Company has been developing for 17 years is

strategically, operationally higher. I can work and operate with levels of profitability at margin levels that the market which does not have this model cannot handle.

I will let Eduardo answer only to discuss more specifically about our management and then I will return to answer your second question.

**Eduardo Galanternick:**

Good morning João. Eduardo speaking. Referring to sales growth, this was well distributed into visit, conversion and ticket. Concerning visit, it was clearly a result of all efforts towards mobile we have been doing. The Company accumulated R\$5.4 million apps downloads. This is an application which has a good conversion, then traffic migration to such device has not been impairing our conversion. Conversion was also influenced by rupture reduction, by such price rationality we saw in the market, a decrease in delivery term, a result of all the efforts the Company has been endeavoring to well distribute the goods among our distribution centers, employ the delivery multichannel, also the impact of the Pickup in Store. Overall, sales results meant a combination of several factors. We also had a very strong calendar; we started with an amazing sale, which was a major vector for the first quarter. Our results came very positive. March was excellent with a very favorable calendar, without any holiday. The Company organized a successful computing fair. We have been doing a good job in the computing category. This is the second EBITDA with very high market share, over 20% in this category. This represents our team efforts as a whole, of getting all the details. We affirm that our business refers to execution, detail and we have been working on it.

**Frederico Trajano:**

Thank you, Eduardo. And João, just adding, in relation to the market as a whole, specifically tax issues, I see that same initial answer applies here. The market needs to adopt rationality. Several businesses were going through losses, maybe they benefited from a legal concept to reduce losses or to generate a small profit, but the market cannot make use of that and should return to a period of rationality. Then, I always had this view, I always believed that in certain moment, this path towards more rational operations which return value for shareholder is an irreversible path. I think this will continue this year; I don't think this will significantly change any company's action from the price viewpoint. What I think it is going to happen is from competitors' viewpoint, as I already mentioned, probably they will be more organized, with more structured operations, and maybe more liquidity will flow to small and medium enterprises. Then, in this regard, we can expect a fierce competition, not from very aggressive viewpoint of that game of reducing margin to gain market share. I think this game no one will play because it is too dangerous at this moment. I think the same for the future, besides being dangerous, it is not good from the viewpoint of generating value for shareholder.

**João Mamede:**

That's great, thank you for your answers. If you could, just a last and quick issue, the working capital. Roberto made few comments about the dynamics, how growth changes the working capital dynamics, considering that e-commerce grows quickly. There are other lines you also have been working, but I would like to know if you can attribute any weight to such change in



e-commerce, to such improvement you have been recording, because, at the same time, the company's super strong growth requires more working capital, but it has been declining due to initiatives, change of channel, that is to say, could you give us any idea, how much was such change of channel? Because from now on, the e-commerce only will gain more weight. Then, how much the e-commerce growth can contribute to the working capital dynamics looking ahead? Once again, thank you.

**Roberto Bellissimo:**

Thank you, João. Let me give you my opinion. We recorded a negative working capital, then receivables, we have more suppliers than inventory, managing to grow by generating cash. Then, the accounts receivables are seen almost as cash, we can rely on it. We improved such account, but we will focus here on inventory. The inventory turnover improved from 73 to 66 days in two channels. The e-commerce turnover improved a lot, it was already lower than physical stores. I think it is important to also mention that physical stores also improved the turnover of our inventory, because the Company returned to grow. Then, it is much easier to improve inventory turnover when sales are also growing.

In 2016, for instance, the Company did not record growth at physical stores, and you have the sample inventory, which is almost a fixed cost. If you do not record sales growth, you cannot dilute the sample turnover. To the extent, the company returned to grow in a two-digit pace at physical stores, it could improve inventory turnover, samples at physical stores and e-commerce had a significant growth, which also improved turnover, which was low than average, these factors positively contributed to improve turnover. Such seven-day improvement I cannot say how much came from e-commerce and from physical stores, but I may affirm that these two channels significantly improved the inventory turnover with a positive mix effect, which is the highest percentage of e-commerce, and as you said João, this is a trend. To the extent, the e-commerce grows structurally more than physical stores, we have the opportunity of continuing evolving the inventory turnover, and from supplier side, purchase is solidary. This means, the same term we have for e-commerce, we have for physical stores. Then, we try to maintain this trend, and if we have the opportunity to improve, to increase, but we already have a very healthy average term of purchase. Then, we try to expand such gap to the extent the e-commerce grows and contributes to the working capital dynamics. The working capital dynamics is already positive, our adjusted net working capital is negative and if could say anything else, the marketplace also contributes to such dynamics. We are very comfortable with working capital trend from now on.

**João Mamede:**

That's great and very clear for me. Thank you, Beto.

**Roberto Bellissimo:**

Thank you, João.

**Operator:**

Next question from Mr. Richard Cathcart, Bradesco.



**Richard Cathcart:**

Good morning everyone. I would like to make another question about sales growth, both online and at physical stores. I would like to understand if you have a conversion rate, if you have more customer traffic flow or if you have current customers buying more frequently. Just a more detailed explanation about such sales growth. Thank you.

**Frederico Trajano:**

Hi Richard. Thank you for your question. As Eduardo mentioned here, just to elaborate his answer, I would say all these factors contributed. The average ticket and conversion increased, also sales for new customers, then, in my opinion to reach such percentage of 56%, you have to be well positioned in all fronts. I would highlight mobile, we significantly invested in this platform, as we saw that the market changed from desk to mobile. We highly invested in our application, which recorded over five million downloads. Currently, this is one of Brazil's most downloaded apps and one of the leaders, undoubtedly, or 1P leader – and this is relevant. For us, right decisions and a good execution of daily routines by Eduardo's team generated such result. I would like to remind you – I think this is very important – that the e-commerce dynamics in the long term is positive, then I am not surprised with e-commerce growth, because this is a measurable trend. The e-commerce share over Brazil's retail still is 3%, 4%. If you observe the figures reported by free market last year in Brazil, the growth is nearly 60%. Those businesses which are well organized, with teams who know how to operate the segment very focused on sales and growth, will stand out. Not only Magazine Luiza, I think this is an inexorable long-term trend of e-commerce increasing the share over total sales.

**Richard Cathcart:**

Thank you. Just another question. Could you comment about the Pickup in Store, about its performance in the first quarter? Thank you.

**Frederico Trajano:**

Well, Richard, this segment is doing very well, 100% of our stores are accredited and the Pickup in Store share over total e-commerce sales has been significantly growing. This is our great differential, as consumer opts for picking up in store and does not pay freight, and has an improved delivery term. We also have been working for several stores to work with 48-hour delivery term. This is our target to have 48-hour delivery term for the Pickup in Store in all stores. This is not the case today, but we have been launching it at the stores. The Greater São Paulo, if I'm not mistaken, already has been working with such term as of April. This segment tends to gain a greater share and contribute as competitive advantage of the website, because, when competing with stores and chains which do not have such option, especially those players who are only online, we have a trump card with one of the most relevant components in consumer's decision, which is delivery term and cost of delivery. We have over 800 stores distributed in 17 Brazilian states, we have an unbeatable value proposal.

**Richard Cathcart:**

That's great, excellent. Thank you.

**Operator:**

The next question from Mr. Luiz Felipe Guanais, BTG Factual.

**Luiz Felipe Guanais:**

Good morning everyone. My question refers to the marketplace growth. You mentioned in the earnings release that assortment of the marketplace platform is 98% complementary to B2C platform and Magazine's physical stores. We also know that this implies an exponential growth in the number of the company's SKUs. I would like to understand and know a little more with you, Fred and Eduardo, how do you see the evolution of assortment between B2C and marketplace over the upcoming years, as the marketplace grows, and eventually do you think of leaving few categories of B2C to benefit few specific sellers in the marketplace platform?

**Frederico Trajano:**

Thank you for your question. The focus today is not to leave, especially the Company's core categories. We do not intend to exit, even because we have a very comfortable position, in which we have been gaining cash with 1P. We have been gaining cash with categories we buy and sell, then we have a good profitability in these categories. Different from few players, for instance, which had losses in category 1P and sometimes they need to speed up the marketplace to offset such loss; we have a situation of profitability. In these categories, we are ranked amongst second, third and in few cases, the top buyer of suppliers. Then, we have a competitive position in this commodity category, such as 1P, then becoming very difficult for a small seller defeating us. Sometimes, we will have a complement from any very specific line of product, inventory balance. This will be imputed to the platform, but in the core, most of items and sales, our 1P will continue the most competitive of the market. Leaving does not make sense but complementing, which is now our vision and focus. This is a complement of lines of category. We have suppliers selling directly, such as Brastemp, Electrolux and now also Multilaser... We have several suppliers selling directly. The focus now is in complementary categories, turnover is not very high, then we will not leave such category. Probably, we will leave few SKUs. The SKU has a low turnover, the working capital dynamics is not good, as well as the SKU profitability, then we tend to fully migrate to the marketplace, but this is not so relevant change as we can see in few market players.

**Luiz Felipe Guanais:**

That's great, thank you very much, Fred.

**Operator:**

Next question from Mr. Guilherme Assis, Brasil Plural.

**Guilherme Assis:**

Hi, Fred. Hi, Beto. Thank you for choosing my question. I think we already commented on sales issue, but not very clear to me the Company's strategy and competitive advantage. You commented on the last slide you also foresee a potential growth of stores. I would like to know if there is any specific region with higher market share potential. And you commented, if I'm not mistaken, 18 stores in the last 12 months. I would like to know if in your opinion this is a pace of growth you can have or if with economy upswing, you think it is possible to speed up the pace of store expansion.

And already linking to the second question, I think that amongst several results highlights, we also have the cost control. I think the Company's initiatives, also the SG&A dilution and revenue growth. I would like to know if the digital transformation strategy, with all these mobile stockist, mobile cash initiatives may bring greater productivity at store, such as headcount reduction or higher efficiency and sales per employee at store, if you have a plan for this. These are the two questions. Thank you.

**Frederico Trajano:**

Good, Guilherme, thank you very much for your question. In fact, we strongly resumed the pace of store opening. We are inaugurating today a store in Minas Gerais, Sete Lagoas. We also opened stores in Curvelo, Sete Lagoas. We have several points-of-sale contracted and we plan to open them in 2017. I think the store is important in two points. Reminding that our strategy is to become a digital platform with physical points-of-sale. The physical point-of-sale is a relevant differential component for our online proposal. We were mentioning here that with the Pickup in Store, we have delivery price terms and conditions very competitive in relation to the market. Then for us, to increase the physical store base makes sense, because the physical store has a positive contribution and it is an important differential of our model compared to our only online competitors. Then, we plan to resume the pace of growth. Our stores are relatively small compared to competitors' meterage. We are taking advantage of favorable market conditions, in these openings, we do not have to pay a non-refundable lump sum, you can get more competitive costs per square meter, then, we have been very disciplined to open a POS which may continue opened for 20 years, with very low rent cost, lean stores, small meterage, even because product is sold through seller's mobile. And this already answers the second question, because, with store automation, which is one of our strategy's pillars, which is the physical POS digitalization, we manage to gain productivity. We do not need a big store, because inventory is in the mobile phone. I do not require a big support team because seller receives cash in his mobile POS, then, not requiring a very big cashier team. Reminding that 40% of my store team is in the back office and looking ahead, we want to transform such back office in sellers, in revenue generation for the company and then we will increase sales per store employee, reducing the store SG&A, which still has lots of opportunities through automation. I am referring to mobile sales, we reduced customer service time. In January, we had an excellent month here at the company and chiefly due our sales. Our sales were successful, as all stores had the mobile sale which was closed in two minutes. Without mobile sale, this is closed in 40 minutes. Then store sellers gained more productivity on peak day, like sales where you have hundreds of people at stores. The

Company gained productivity and managed to increase staff even equal to last year. Sales grew in line with staff, then store automation is essential to reduce expenses and, when we invest in store automation, we have two points of focus: improve consumer's experience and reduce the store cost. We plan the store has a cost very similar to e-commerce for it to be competitive. I believe that, structurally, the best way of doing this is with all investments, all projects Luiza Eletro has been executing for point-of-sale automation. There are several other projects we have been implementing during the year.

**Guilherme Assis:**

That's good. Only two things, Fred, just to complement these two questions. In the first answer, you said you can see store potential, you can see synergy in your model? This means you should open other virtual stores or not. Do you think that the store mix you will have will continue highly with traditional and bit of virtual? In relation to dilution and strategy, could you try to quantify? I think you already gave very relevant information that is to attempt reaching productivity of store similar to virtual store, but would you have an idea which is the difference today and how much you can achieve on average productivity? These are the questions. Thank you.

**Frederico Trajano:**

Answering your first question, yes. We plan to open a proportion of virtual stores this year in relation to conventional stores. This is the company's strategy of increasing such opening percentage, but we will continue opening in these two formats. In this strategy, for instance, we are opening a conventional store and we already have several virtual stores scheduled which were inclusive opened in these last 12 months, but the proportion of virtual stores in relation to new stores, even because it has a model very compatible with we plan for a store in the future, it will continue high. Then, the answer is yes.

About the second issue, we cannot give any guidance, Guilherme. We can talk after the call, try to elaborate better, but this a type of information I cannot discuss now. But I think generally speaking, as I mentioned, it is very difficult because the e-commerce has... [sic] The main cost of the physical store is payroll, approximately 60% or 70% of operating expenses, depending on the store, derives from payroll and the e-commerce does not have such cost. Then, it is a very difficult work to reach the same cost base of the website, but we have been continually working on this, because retail needs to understand it must reduce such gap of physical store SG&A with e-commerce, in this regard, we will have several initiatives but I cannot quantify right now.

**Guilherme Assis:**

Ok, thank you, Fred.

**Operator:**

The next question from Mr. Ruben Couto, Itaú BBA.

**Ruben Couto:**

Good morning everyone. I have two questions. Could you comment on such mobile evolution, its share over total e-commerce sales? If you could also breakdown the percentage of application, how much is entering in the site via mobile and if there is a substantial difference in the average ticket, recurrent shopping by mobile user, sometimes, consumer uses the desktop. I think this is an interesting point and another topic, could you explain about the gross margin evolution and in these dynamics the e-commerce continues gaining share over total sales, but you could explain the evolution of each channel? These are relatively stable, such drop we can see, is it a mix effect of e-commerce growing or is there any change in each channel separately? Thank you.

**Eduardo Galanternick:**

Well, Ruben, good morning. Eduardo speaking. We usually release the traffic flow share, which exceeds 50% - 54% in the last quarter. Referring to sales, it already exceeded 30% of sales referred to as our B2C. Most of sales derives from app, although, traffic does not represent the majority. We also have several initiatives to improve our mobile platform, thus, we continue investing in the app, improving the mobile site platform, the expectation is such share continues increasing.

**Frederico Trajano:**

Referring to margin I will speak here, maybe Beto could help me, but there is no mystery. As we already mentioned Ruben the e-commerce works with lower margin than the physical store, even because expense is lower. Then, we could see that in our first quarter results: no change of margin individually per channel. The physical store margin came in line with same period last year. The e-commerce margin remained in line compared to 2016, even because the market is rational, and there is no reason for big changes. The overall figure changed because e-commerce gained higher share. Then, total gross margin went down due to e-commerce market share gain, but not due to each channel's dynamics.

On the other hand, EBITDA more than offset such reduction of percentage margin. Then, as e-commerce is a business with operational leverage, when the company grows and increases e-commerce market share, the SG&A decreases, because, as I mentioned, we do not need to hire to increase e-commerce sales, differently from store, because it is an asset-light model. The e-commerce is more productive from sales viewpoint for employee than the physical store. Marketing is also more efficient than the physical store. The e-commerce marketing return is higher than the marketing return of physical store, then what happens in this scenario is we have an increase of EBITDA margin with e-commerce growth and I think this is what we have to look at, the operating cash generation. Then, it tends to contribute to generate operating cash. Not to mention Ruben, this is a calculation I think everyone has to do also in return on invested capital, because, above all, the e-commerce, as this is an asset-light business, it requires less CAPEX than the physical store, therefore, this operation has higher possibilities. We have been managing to grow with CAPEX level historically low, due to these factors. Looking ahead, we can foresee a slight increase of CAPEX, because we plan continue opening stores due to our multichannel operation. We are a multichannel operation. We do

not have a preferred channel, we prefer the omnichannel model. We believe this is a winning model and the best alternative to capture the e-commerce growth here in Brazil. In our case, the e-commerce success much relies on physical store. These issues are very tied and vice-versa. The store benefits from e-commerce by means of traffic that the e-commerce generates for store, through a number of more available items. For instance, in certain moment during this year, the marketplace products will become available for seller to also sell at store. Then, we have the story that 1 + 1 equals 3 and not 2, do you understand? The sum of channels is very positive for the company as a whole, the old and known synergy.

**Ruben Couto:**

Got it, perfect, Fred. Thank you for your answers.

**Frederico Trajano:**

You're welcome. Thank you for your question.

**Operator:**

Next question from Mrs. Maria Paula Cantúcio, BB Investimentos.

**Maria Paula Cantusio:**

Hi, good morning. Congratulations for the company's results. Thank you for choosing my question. I would like to explore with you the marketplace issue. Could you explain about the number of Sellers which entered in the last 12 months, how much the marketplace is already accounted for in e-commerce sales and how do you manage to make the SKUs entering to be complementary to the company's portfolio, if you choose those players operating with different products of the company or only one item they sell part of portfolio in your e-commerce. Then, if you could disclose about the same-store sales, how much came from traffic flow and how much from price. I do not know if you provide this type of metrics. Then, I have another question about Luizacred.

**Frederico Trajano:**

First, thank you for your question, Paula. About the marketplace, the company recorded 220,000 third party SKUs, we exceeded the mark of 100 partners. In April, the company recorded more than 30 partners, 32 partners to be more accurate. Very interesting partners entered, such as Spice; Avon; air conditioning Clima Rio; Havan, which is a retail chain increasingly growing in Brazil; one the leading market's sellers, which is Connect Parts, a large seller of automotive components; Drogeria Onofre, entering this segment, Madeira Madeira, which is a category in the furniture segment; Lojas Mel; Saúde Já; Drogeria São Paulo; Pacheco... The company sold chocolate at Easter holiday, for the first time in 60 years of Magazine's history and a successful partnership with Mondeléz, Lacta chocolate. The business is booming, total focus, as I already mentioned, in the introduction of new sellers and in the introduction of new categories, notably complementary this year, but we want to become a full marketplace. We will have complementary producer, competing product, we will have any type of product at the website and, this year, as we must choose, we pick categories which

complement, therefore, then we have a high complementarity index at 98%. Then, we are in high spirits.

This year's focus is not GMV, we are not concerned with GMV. We are interested in quality, having the same care with customer service and improved platform. This is an easy platform, in which the entry of all these SKUs does not make browsing complex. Browsing becomes easy, fluid, a user-friendly experience, we are focused on executing this as best as possible, unhurried. Even because the marketplace must be built consistently, in an accelerated manner, but unhurried, not to the detriment of our service level or our skills. We are very focused on adding new Sellers and doing this so that to sustain the service level and shopping experience at the website. The marketplace is more focused on product, platform, when I say product, this is the platform – focused on having a solid platform, good for Seller and for end consumer. This is our focus in this regard. I cannot remember your second question.

**Maria Paula Cantusio:**

I would like to know if you could disclose the figures of same-store sales deriving from physical store or from traffic flow and price.

**Frederico Trajano:**

Unfortunately, we cannot give any guidance in this regard, but I can say that we recorded growth in two aspects: average ticket and traffic flow.

**Maria Paula Cantusio:**

Ok. Just another question about retail, what has been specifically done in terms of pricing policies that you mentioned in the earnings release for gross margin gains?

**Frederico Trajano:**

This was in e-commerce, Maria Paula.

**Eduardo Galanternick:**

We mentioned in our earnings release that the improved pricing index was one of the aspects which benefited conversion. Such improvement could be our assertiveness or higher conservativeness of our competitors. We could see a higher conservativeness, because our competitors approached more price balance than we could have and this contributed to increase our conversion.

**Maria Paula Cantusio:**

Ah, I've got it. Then referring to Luizacred, I would like if you could mention about the dynamics we can see from a substantial reduction in DCC and individual lines of credit, if you intend to continue reducing and even offsetting this with Losango partnership or if you achieved a level you deem good and from now on maybe slightly increase these portfolios.



**Frederico Trajano:**

Maria Paula, thank you for your question. Such trend at Luizacred is continuous. Luizacred's focus is Luiza Card, which is a loyalty card, you gain relationship, services and much more. Most of Luizacred's actions are concerned with Luiza Card, which by the way has been performing well. At DCC, for one year and a half, Luizacred significantly reduced the approval rate and allowed us to enter into a successful partnership with Losango, recently we have been leading this partnership and we started another one with Santander Financiamentos in a model similar with Losango. The idea in consumer credit is also to become a marketplace, i.e., we can sell products at Luizacred, but we can sell Losango's products, we can sell Santander's products and henceforth. Then, at Luizacred, these portfolios – DCC and loan– should not return to grow. We may increase these businesses with other companies, other partners, but Luizacred will continue focusing on Luiza Card growth. We also have room for Luiza Card to grow at physical stores, in the e-commerce. We have several growth opportunities here at Magazine as well. Marcelo will add, just a minute.

**Marcelo Ferreira:**

Maria Paula, here is Marcelo Ferreira. Thank you for your question. Just clarifying one issue. What you see as personal loan is a product referred to as "Grana Extra", this is a card. The single product contained inside that card is the personal loan. It is not opened to you, but the credit card also has a personal loan category, this we intend to continue expanding, but you cannot see in the portfolio. You can see the portfolio growth, but you cannot see inside it, then, it does not mean we ceased personal loan. The personal loan which is not linked to the card, this is focused on old client and we expand in the portfolio for cardholders.

**Maria Paula Cantusio:**

Great people. Thank you very much for your answers and good morning.

**Frederico Trajano:**

Thank you, Maria Paula.

**FINAL CONSIDERATIONS**

**Operator:**

This concludes the Q&A session. I would like to give the floor back to **Mr. Frederico Trajano** for his final remarks.

**Frederico Trajano:**

I would like once again to thank all those attending this call, the analysts for their questions and our team for their good performance in the quarter. I wish you all a good day.

**CLOSURE**

**Operator:**

Magazine Luiza's conference call has now ended. We thank everybody who joined the call, have a good day.