Multi

Conference Call Transcript
Multilaser
2Q22 Results

Juliane Goulart:

Good morning, everyone. Welcome to Multi's results of the 2Q. I am Juliane, IR Director, and I am here with Alê, our CEO, and Leo, our CFO.

Before turning over to Alê, I just have two things to say. The first is, if you would like to ask a question, you just click on the Q&A icon. If you wish to open your microphone to make your question, you can feel free to do so. Otherwise, you can just write 'no mic' on your question and we will read and answer.

Also, a reference to our disclaimer on the last page of the presentation. And that is it. Let us begin. Alê, you have the floor.

Alexandre Ostrowiecki:

Good morning, everyone. It is a great pleasure to be here. Thank you all for your interest. We will have some comments about the 2Q22 on Multi's earnings. We will start with some highlights of the 2Q.

As you must have seen, first of all, we really changed our brand. This is a historical moment. After 35 years in the market, a company that started, as everyone knows, in the laser printer cartridges, therefore the name Multilaser, and we made a historical change for a new positioning, shortening the name. Multilaser is now Multi. I will talk more about it towards the end of the presentation, but it is really nice. It is a movement that will add a lot of value to our brand and to our results as well.

Talking about the numbers, and I will talk about Multi, but the quarter's outlook was positive for us. We saw a recovery in revenue. We grew 20% in the Company's net revenue compared to the 1Q of this year, and even more important, 1.2% compared to the 2Q21.

So the big point of pain, the doubt that we had from the investors was that a company that tripled in size in a two year period, maybe this new level would not be sustainable, or would it be possible for the Company to hold its ground and continue to grow organically, even if at a small rate per year? Or will revenue go down to something in-between the pre-pandemic and post-pandemic levels?

That was always the big challenge, but when the 1Q came up, or came here on the call, it shoes that the 20% decrease was nothing that scared us. It was in line with the plan because the base of the 1Q21 was huge. It was the best quarter in the year, and historically, the 1Q is weak. It is the weakest in the year usually in our industry. But okay, 20% down, but now with the 2Q with we are plus 1%. It is small growth.

Of course we want to see more, but it is a good trajectory. We are optimistic with the future for the upcoming quarters to be able to deliver more than that, of course. But -20% and then two +1%, so now we will start delivering. If all goes well, better results, closing the year with an interesting figure.

So this mall growth, this reversion seems a good thing. Comparing the 1H21, it was very strong, the 1Q and 2Q21. 3Q21 was more difficult and the 4Q was very hard. It was the quarter where retail really tightened, and the atmosphere was worse in the 4Q21.

Now on EBITDA, we show an increase of 12% compared to the 1Q. That is also interesting. In line with this revenue, the margin was tightened at 0.9, but EBITDA is growing up.

And the fourth point here is that there was a lot of growth in new product lines that are not as traditional for Multi, but showed the diversification of the Group. We are going to see each category, but we grew a lot on screens and displays, TVs, networks for providers, personal computers for the government, and the new baby category is really booming. Pets, wellness, toys. So the Company is increasingly diversified, relying less in one or two segments only.

And an interesting point is that we are generating operating cash at R$80 million. We are consuming cash. So quarter by quarter, we have been using cash to fund our growth. We have receivables and inventories with the large accounts that really eat up the cash, but for a good reason. The Company's growing strong and now that the revenue base is more stable, we start to generate cash. That is also always something investors ask, and I think this is positive. Let us see in the upcoming quarters if we continue generating a lot of cash.

So bringing more details, net revenue, looking at the year over the last 12 months, we see an important growth of 62%. There is a compression of gross margin that is entirely expected due to the comparison base, the pandemic moment when everything was in our favor, people were still with a lot of money and buying and equipping their homes, not consuming from abroad. So all these forces have been discussed and really boosted national retail and electronics, but now the margins are more compressed. I believe the normal, stabilized long term margin is slightly above this. It is in between the pandemic level and the level of the last 9M, which is tighter, with a retracted retail.

Looking quarter by quarter, we can see this 1.2%, this small growth compared to last year, see the 20% leap that is very important compared to the 1Q, this margin compression here, the gross margin, and then 0.9 on EBIDTA that we will see next.

So here is the EBITDA. We see growth year on year, a 12% increase compared to the 1Q, and -23% compared to the peak of the good winds of the pandemic phase. The 1Q and 2Q21 were some of the best quarters in the history of the Company, and here we have that margin of 0.9%, basically due to the mix. But we may say this is a level that is below expected. We want to improve this.

We can work better on this percentage, and it is closely related to that tightening of the retail, more competitiveness, fighting to sell. It is a cyclic point of the market, in our view.

Net income here. This slide is very important to pay more attention to, because you will see a significant drop of 72% in net income, almost 70% compared to the 1Q. But we see this. As nonrecurring effects. There are three very important factors that explain this difference.

So, of course, it is frustrating to have an income that is below the previous quarter, but it is quite understandable, and it is nonrecurring. So we believe this will be quickly reverted. It is a one-off scenario.

So let us give you the brief history. In the year, we are growing 55%. We came from R$200 million, that is an astronomical figure. I think it is the highest income of the Company's history, R$200 million and a quarter, because it is more in a quarter than the income of the entire last year, and a margin of 17.5%. In 1Q, we came here and told you that this was nonrecurring due to foreign exchange aspects.

We saw 13% of EBITDA margin and the previous slide, 13%, becoming 17.5% of net income. The explanation is the strong drop on the USD. We had a positive exchange rate variation, but we told you, let us not get excited. This is not sustainable. We need to look at it carefully because it is way above the Company's normal levels. It was a tight quarter, with a lot of fight, and then we had R$171 million in net income.

But now the opposite occurred. We had three important effects that we must understand. The first one is the negative exchange rate variation offsetting the previous year, basically. What we made more in exchange rate last year, the USD went up, now it went down again. But maybe if the USD is maintained at this level, we may have a positive exchange rate variation in the next quarter, but we need to balance this. So this is very important.

Then we had another negative one-off event that was the tax review with Minas Gerais government. We reviewed many years back and there was a discussion of ICMS credits intercompany. Being conservative, we decided to have a one-off spontaneous report of the ICMS tax, cleaning up some potential contingencies that could come up since 2017, 2018, 2019. So nothing is related to the 2022 fiscal year. We also had an adjustment in that income due to the spontaneous reports.

So the first negative one-off effect is exchange rate of R$100 million minus RAD. To give you an idea, it is about R$70 million. So R$70 million, more or less, of exchange rate impact. Then we had this tax review, net of around R$45 million, R$50 million. This is just the major figures, but we have all the details in the notes. And finally, of course, we had a positive adjustment, a reassessment of our invested watch, because there was a new round of investment with a higher valuation. It seemed a fair valuation to us. It went up about 100% in the Company value, and it tripled its subscribers' base.

So per subscriber, it became cheaper. It was about 400,000 paying subscribers, and now it is getting closer to 1.5 million active paying subscribers. There has been a new round validated by audit, so we reassessed, and our share that was about 42% is now 49%. This is the limit we want to get to.

We have almost 50% of WatchBR, it is a TV company, a paid subscription TV service that sells services through Internet providers. It is growing a lot, and we have big plans for watch. And I will talk about Multi Mais when we talk about it.

So these are the three factors that explain the drop on income. There are nonrecurring aspects. There should be nothing in the tax scenario for upcoming quarters, and tax and exchange rate really depends. Our business really does fluctuate according to exchange rate.

If we look at the half of the year, we are talking about a company that is coming from an EBITDA of 12.5 13% with net income at around R$10.5 million. It is less than ideal, but completely explained by the very tight retail moment. There is a lot of competitiveness, it is difficult to sell, especially for large customers, as we will see. But net income, bottom line, at two-digit. It is a very tough sales moment, but it seems okay, in line with our plan.

Now per Channel, there is something very interesting here, and I think it is good news for Muti. Comparing to the base of last year, which is a robust sales based, excellent scenario and so one, we will see that there has been growth in most channels, led by a huge drop in large retailers.

See how interesting small retail, which our intuition will tell us that they would suffer more, small retailers with the pandemic, migrating to e-commerce, they would suffer. But no, we saw a small growth here, and in the 1Q as well.

Large retailers are struggling. We are talking about three names here. It is concentrated in three big names. The conversation with the CEOs of this major companies that you know better than I do is basically, “look, we are struggling with stock prices and so on, and we held on the purchases, and now we are starting to recover”. So what they have all been saying is that they have cleaned house, decreased inventory, but they are ready to start buying again. So we see large retailers with more appetite now on the 3Q. So this is a good perspective.

But the other operations of the Company have been showing growth. 11% in government, 7% in Internet providers, corporate with a small drop. But this is basically a memory for other manufacturers. They are also suffering in the sales of electronics, buying less memory from us.

And another thing that I think is interesting for everyone, everybody asks about direct to consumer, is e-commerce growing with DTC at 65%. So this is becoming a more and more important business for us. 7.3% of the Company's revenue today, and more than 10% of its margin comes from e-commerce sales.

And we are only beginning in this game, because now we have unified all of our e-commerce area. We had the Multi e-commerce, we had Obabox, the Company that we bought last year specifically to do that. And now they are unified, joining forces, joining teams, joining marketing budgets and we are working on strong investments.

I invite all of you to visit multi.com.vc, it is ‘Multi with you’. It has a new phase. Go there, shop, try it out and feel the logistics, the service level. I am sure everyone will like it. So it is a healthier mix of channels.

And the biggest suffering point is large retailers. And that is what tends to recover when we start to sell. Our relationship is good, everything is good. We are just waiting for the right moment and it is coming up. So it is going to be easier to revert this.

Now looking at segments, basically, there is greater diversification as well. We see Kids and Sports, which was the smallest segment of around 4%, this year already close to 8%. We are growing strong. We will see more details later. Home electric products growing at 16% due to TVs. Office and I.T. supplies going down slightly, that consumption from the pandemic of accessories, everybody was buying webcams, mouses, keyboards, accessories, but now the level is slightly lower, 4% down. It does not scare us; it is a post-pandemic level. Everybody has already equipped their home offices. Everybody is starting to spend money outside of the house again, traveling and going to bars and hotels. So 4% is acceptable.

And -10% in mobile devices is more concerning because it involves tablets and smartphones that really suffered in this half year. Smartphones was the big villain of the revenue, especially in large retail. But you will see that it is already 50% above the 1Q. It was a lot worse, and we will see on the upcoming slide. So we see a recovery.

Smartphones -10% compared to last year, but 50% up. Look at the 1Q. It was a disaster for tablets and smartphones and PCs, from R$500 million to R$300 million. But now we see a recovery, and the 3Q will see even more so, especially for smartphones. For the first time, we had some month with good news for smartphones, but this is something for the future. The 2Q has improved. It is still below the 2Q21.

Office and I.T. supplies. Basically, we see a stable revenue with small decrease recovering compared to the 1Q, basically led by Internet providers. So Internet providers are pulling it up. Computer accessories and peripherals, that was saturated. The replacement cycle is longer. People hold on to their mouse and keyboard for a year and a half, two years with an equipped home office. So that is a little less.

Home electric products. This is good news, growing 16% year on year, 2% quarter on quarter. The 1Q was already strong, but the name of the game here is basically TV. That is what we are talking about. Speakers are growing up slightly, portable appliances going ‘wow’, automotive going down, automotive is very weak. Health care, portables and audio and mobile accessories going up. But TV is a new market for us. We have 2% of market share in Brazil, with a lot of room for growth. TVs are coming up with a lot of consumption, a lot of demand.

Multi TVs are the entry TVs. We have the premium Toshiba TV brand, a brand that is very accepted, even more so than Nokia. We have Multi Smartphone that is very well positioned, Multi TV, very well positioned. Nokia smartphone is struggling with the competition, with the big global brands, but Toshiba TVs are winners. In Toshiba, we see greater brand acceptance and more room than on smartphones right now at this moment.

Finally, kids and sports shows this diversification because, in addition of diversify in products, it is also channels. We are talking about completely different sales channels. Toys is one thing, sports is another, baby is another and pets is another. So basically, we see huge growth rates, 71%.

Wellness is a little bit below that, with a supply difficulty, a difficulty of buying exercise equipment. Baby is meeting our targets, sports also meeting targets, toys meeting targets. And pets, which is new, we acquired Expet last year, the mat factory, and it is really going up, always with one month of backlog. Whatever we sell, good margins. Pets is a big point of surprise for us. We are investing in increasing production there.

In sports, what is new here is that we have launched the DJI drones. It was a huge hit last month. We launched Mini 3, selling quite well and pulling these numbers up. 72% comes basically from Pets, DJI as something new, and the organic healthy growth of the other lines, except for Wellness that is a little bit below due to supply issues.

So finally, we have here the three additional points to discuss: the brand revitalization, the existing partners evolution and the factory. In terms of partnerships, we have bots that we acquired in the beginning of the year, that factory for electric vehicles. So we combined all of the electric vehicles’ line of the Multi brand, our Atrio brand of the Grupo Multi, the Watts brand of electric vehicles, bicycles, scooters, etc. going very well. We bought Watts and combined the portfolio. So we are going to have Watts with a more corporate portfolio and Multi, with the Atrio brand, in more of a leisure portfolio.

And what is new here is the electric motorcycle. Watts already had a project approved for the E-bike motorcycle, already registered with all the licenses, they are being manufactured. They should be shipped in upcoming days. We are expecting a launch in the 4Q with the electric motorcycles, and they are a game changer. They will be imported first to test the market, but we are already putting the factory together in Manaus to start production in the 1Q23, producing domestically electric motorcycles.

It is a huge market, and we are very excited because it is the future, reducing the costs of fuels and the environment, ESG. It is very good for people to adopt electric motorcycles. So we want to be a disruptive player in the market.

DJI, we mentioned, we have the exclusive distribution. It is the leading brand for drones with more than 80% of global share. They are the major reference for drones. We have our entry level drone, Multi Atrio, and the DJI drones that cost 10x, 15x more, with more added value compared to Atrio's drones. It is a completely different market. They do not compete with each other. The launch was very good, we sold R$2 million in two days of the Mini 3 drones.

And the third, I do not even know what to tell you what the biggest potential is. There are three major points. We have a very good partnership with Hikvision, the greatest manufacturer of security cameras, image recorders, access controls, the whole security world. Hikvision is a leading brand worldwide, dominating all markets in the world except for Brazil. It is the vice-leader in Brazil, and we are already manufacturing and selling at this moment. The product is already in line. Some of the Hikvision product lines are being distributed to the market. So this is huge potential as well.

Taking more and more of their lines, we are bringing body cams, those security cams for the police, for example, Hikvision brands, access control, high performance hard drives for security, security cameras, DVRs. There is a lot of potential for us to increase our security line.

And the last point that I want to mention, which is very important, our sixth industrial warehouses ready in Extrema, Minas Gerais. 80,000 m², 14 meter ceiling height plus the factory. And this warehouse will be entirely dedicated to plastic injectors.

Multi is an electronic company. We have many industrial processes that are very complex, manufacturing memories and assembly lines, but we were not injecting plastic, we were purchasing it. But for our portable lines, with the high volume products that are heavy, voluminous, it is more competitive for us to produce our own plastic rather than importing from China, for example.

So we are starting already to produce fans. We are assembling them with plastic injection. The cost will go down greatly. The comps of these products will be more competitive and we will be able to grow in this billion USD market, R$6 billion per year for electrical portable devices that we have a small share.

With plastic injection, in addition to that market, we already have in the pipeline blenders, fans are already ready, the robot vacuum cleaners, air fryers, and we also have products for pets and baby lines with injected products. For example, car seats. Car seats basically have large plastic pieces, and the products are all imported in Brazil.

So as far as I know, we would be the only and first company to manufacture that here. We have a very important competitive edge in terms of costs, creating this injector industrial park, and it is a lot simpler than electronics. There is no big mystery, but teams already put together with experts in the area. We have three plastic injectors initially, being able to grow to 40 for this industrial park.

So without any further ado, let us go to the end of this presentation, talking a little bit about the Multi brand, the rebranding. The font has changed. It is younger, cleaner, the name is shorter. We started to see that we became more and more multiple and more multi and less laser. Laser refers to laser printers, and it does not respond to even 0.2% of our revenue. I do not know the exact number, but it is almost neglectable.

So we are also embracing this nickname. The Company already had this nickname, consumers called us Multi, retailers, financiers, workers, everybody called us Multi. So let us embrace that and show the new face of the brand. Younger, more democratic, more pleasant, closer. And it is a Brazilian brand.

Our mission has always been to democratize the access to the tech market. It is a market of desires, novelty. So we are in tune, innovative, democratic, making the Brazilian people be able to afford an intelligent option. Our quality products with guaranteed warranties and a nice design. It is not going to be heavy on their pockets. People will not need to get in debt or pay thousands of installments.

And this goes hand in hand with the current moment. As you know, it is a moment of economic retraction, small growth, inflation that puts pressure on everyone is wallets and encourages trade down from the consumer side.

So this change in the brand goes hand in hand with the Brazilian macroeconomic scenario and will help us boost the business for the future.

I will show you a brief two minute video, showing a little bit of this features for you.

Video:

So being Multi is being tack and going and beyond. Carlinhos, play that.

So leaving your comfort zone. Seeking more. Because we deserve more and more. Being Multi is getting it done. Showing the world that we are more than capable. Capable of choosing always what is best, and the best is Multi, of course.

Multi is Brazil. It looks like us. It feels like us. It does not matter if it is at work, studying or at home, chilling, then saying, looking good. Roll it and play with Multi. Always with Multi.

We are Multi everywhere, every day. Being Multi is being on even when we are off. It is connecting, interacting, enjoying, going round, exercising. It is having the power of choice and being sure of our satisfaction.

Being Multi is experiencing the future now, being ahead of the necessities, desiring and conquering. Being Multi is being experienced even being young. It is being bold, creative, leaving commonplace. Day to day, busy routine, chilling.

Being Multi is building a new brand for our country, bringing the desire and the possibility to all Brazilians. Being Multi as being proud of doing it and doing it well. Improving everyone is lives with a lot of technology.

So, let us go! Be Multi!

Alexandre Ostrowiecki:

Let us go be Multi!

So a little bit of our packages. Look how plain they look, how attractive, valuing the product, the product that we launched recently, the smartphone G-Max 2, we are now going on to G-Max 3, G-Pro 3. We are going to have a lot of very nice products in the smartphones. And just a curiosity, the average ticket for smartphones has been going up. In this category, we have been seeing great growth and specifications. Consumers want a product with large screens, good cameras, even at entry level.

So without leaving this entry level, we see that the ticket has been going up. And average ticket from R$400 to R$500, moving up to R$700, R$800 reais. So that is the entry level category.

Our PC, we are going to have an advertising campaign to strengthen the brand. That will be great to show the Multi technology as a way to make life Multi better, investments of around R$100 million rise in media trade, launches, new packs, actions at points of sales as well. And the plan is to have 1 billion impact. It is almost as if each Brazilian person was impacted 5x on average. There is more than 200 million offline impacts, 800 million online impacts, not to mention the influencer package that we recruited with a great host of influencers to advertise the brand and run campaigns and actions.

This is going to be widely communicated. It is the largest media campaign in the history of the Company, and with that we expect to change the perception of Multi and bring it closer to reality. There are companies that, in terms of structure, are relatively modest, but in terms of brand, they have a huge perception.

We were actually committing the opposite. We were ahead in terms of structure, when people look at it, close to R$6 billion in revenue, 6,000 employees, 6,000 products. So many products, so many points of sales, and people did not know when they associated to our name. And now, we want to make Multi's reality what we really are, for people to become aware of that, and it translates into perceived value and pricing power.

At the end of the day, it is a game of pricing power. They go to the point of sale or the Internet and pay a little bit more, a few hundred bps more for a product that they know and they trust, and this will have an absurd impact on margin. And we were leaving that on the table.

So what is the big mistake we are making at Multi? Maybe leaving on the table the power of building a great brand. And we are working strongly on that now.

So with that, I will move on to the Q&A. I think this has been a positive quarter overall, considering the one-off effects in terms of net income, and we are very confident there is a lot of business to be done, a lot of possible partnerships. So I am excited to face the next quarter, even if the macroeconomic scenario brings challenges with high inflation rates. We saw a small reduction in the fuel price, but it is still a point of concern. Unemployment is high, but it has been going down.

It is a single digit now, if I am not mistaken. And high interest rates, but also helping us with the trade down situation.

So it is a scenario we are used to face, and retail is also not as supplied. So that indicates that there may be a lot of good things coming in terms of sell in for large customers.

Dani:

Good morning, everyone. Thank you for taking my question. I have a few. First, about the perspective for the 2H22. Alê, in the release, you said that you were a little concerned with the capacity to deliver the growth of the year in the 1Q. And then, I do not quite understand, based on the 2Q, maybe the perspective for the 2H has been brought down. So just to understand what you are thinking about the growth for the year. You mentioned this recovery, the demand from large retailers. But I would like to understand a little bit what you see for the 2H, especially the 4Q, that there is a lot of expectation of the industry as a whole, especially with Toshiba going so well with TVs and the World Cup. It would be nice for you to tell us more about the growth for the year.

And my second question is in terms of profitability. I would like to understand what you see as sustainable profitability looking at gross margin and EBITDA margin, because at the same time you see some relevant dynamics that should help the margin, for example, decentralizing national retail, as you mentioned in the release, or the increase on the DTC channel. We see some margins still being pressured. So to understand what you see as a normalized point, linking with this point of the new warehouse, that I understand that is going to bring better margins or better price competitiveness. So if you can give us more color in profitability.

And if I can, a third question about the impact of the tax review that you mentioned. It was a one-off point. So, as far as I understand, there should not be any other adjustments like that. And on the tax aspect, there has been some news last month about the implementation of the IPI on some products that they consider relevant, including motorcycles, phones. So if you can tell us whether or not this has been reverted and how it affects you, and what other products you make that would be part of that basket. Thank you.

Alexandre Ostrowiecki:

Great, Dani. Thank you for your questions. If I skip something, please remind me, if I forget. So first, the outlook for the half year, for us, it is a lot more positive than the 1H22 has been. I was joking at the Company, when October, November comes everyone is happy meeting targets and bonuses, but I tell people that the rear mirror looks great, but looking forward, there is a storm coming.

The 1H was chaotic. But now it is the other way around. I am not going to say the skies are looking great, but when you look back, there was a storm. But looking forward, you may see clouds and the sun coming from between, poking through the clouds. But it is exciting to see that retailers are reporting smaller inventories.

We have the overstock report going down month by month. The government started to also drop the Renda brasil, the support of R$600 this month. This has also been a help. The emergency help in the pandemic was one of the big factors for the increase in consumption. Large retailers are supplied, and now they want to have more inventory.

We were talking a lot about delivering low double digits, but now, we are still targeting that number, but less comfortably so. Before we were comfortable, and now it is like, well, there are some good things coming up, but we are still considering low double digits in terms of growth for the year, or something very close to that.

Your second question, if we improved that distribution profile, why had not it reflected in the margin? The margin is tight because of the competitiveness. Even the smaller clients are tightening prices. If we compare with the 1H21, we saw things we never saw before increasing prices one week before the container arrive, and all retailers accepting it, including large ones, because there was no product available in the market.

The big three that everyone knows, they called and said, “I am sorry, we need to increase 20%. The cost went up”, and they agreed, no questions asked, but it is a lot tighter now.

EBITDA, I will ask for help here, but there is a percentage of nonrecurring also affecting the EBIDTA. It went down 0.9, but what is the nonrecurring?

Leonardo Dib:

The EBITDA effect, especially down to that self-reporting that we had, amounted to R$45 million on average. So that brings an effect of 2 to 3 points of margin reduction on EBITDA due to that, the tax review aspect.

Alexandre Ostrowiecki:

Excellent. So I am glad I did not say anything silly. But this 0.9 decrease, there is 2% that is nonrecurring. So it would be a slight improvement on EBITDA. It is not wonderful, but it is a recovery.

So continuing with what you asked, we have the IPI tax, that is very important. I think it is good news for our segment, although in terms of the country, if we discuss the macro scenario, it would be very good to see an overall IPI reduction. But looking strictly from the electro electronic industry, these comings and goings bring a positive result.

So, two messages. So what happens? Let us go back, so everyone is on the same page. We have IPI, which is the tax on industrialized products. You manufacture it at R$100, there is the IPI, 10%, 15%, 20% rate, and you have the final price to sell to retail.

Looking to reduce inflation and improve purchasing power, the government forced a decrease of the IPI very abruptly; overnight, actually. The news was released at the end of the night and then the next day it was already in force, reducing IPI in 25% for almost every product in Brazil. A while later reduced, it reduced 35%. And then, this became a factor of loss of competitiveness for those who have plants in the Manaus Free Zone.

The benefit there is that they do not pay IPO. So if IPI goes down for everyone and this Free Zone in Manaus, which was zero, continues zero, they lose competitiveness. The political forces and lobbying in that region went to the Superior Court and they were able to get a monocratic decision to return IPI to what it was. And that was a list for a while, typical Brazilian uncertainties, and yesterday there has been a third list released that I hope determines which products will have the fall IPI incidence.

So the final balance: I do not believe there will be anymore change. This seems that the status quo satisfies all stakeholders at this time. So finally, the products made in Manaus Free Zone, 100, 200 more or less, the list varies, I do not know the exact numbers, but TVs, cell phones, computers, tablets, all of these products will have full IPI. It goes back to 15%, a little bit more or less. 15% is the average. It is not 9.75% anymore, it is 15. And the other products that are imported or made in the rest of Brazil, they will have reduced IPI rate.

So that is very good for us, because all of Multi's imported lines, baby, sports, accessories, pads, all of it will have less IPI, less tax. The product will become cheaper, more attractive to consumers. So that is going to help increase the products share of wallet.

But the critical products, where we need the competitiveness of the Manaus Free Zone, we will go back to the IPO of 15%. So we go back to the status quo. It is very interesting for us at this time.

Was there another question, Dani? I cannot remember.

Dani:

No, that is. You answered all of them. Just a last follow up: any products made in the Manaus Free Zone will have the full IPI, or some specific product?

Alexandre Ostrowiecki:

The initial decision of Minister of Justice, Alexandre de Moraes, is that all products in Manaus, but there has never been a list of that. So what does the Free Zone mean? If there is a shack with someone making a product that is not related to electronics at all, does it count? It is made there.

So this uncertainty was a point of concern for the industry. So we wait for the Ministry of Economy to release the list. A month later, they released the list, it went back to the Supreme Court and they brought it down saying it was incomplete. And then yesterday they released a new list from the Ministry of Economy, including all the NCMs, all the categories that were missing. And today, we have to follow a list of NCMs, they are the tax codes. So we cannot guess everything that is being made in the Free Zone. There is a list that must be followed, including almost everything.

Dani:

Excellent. I had a mini comment that I think you forgot, about the nonrecurring tax situation. If you think this may happen again, or if you mapped everything that could possibly come up.

Alexandre Ostrowiecki:

In the ACMs, it has been resolved. We adjusted the entire procedure and from now on there will be no immediate financial impact. But it has been recognized and there is nothing else that we see.

But Dani, again, Brazil is always full of surprises. There is nothing that we see or have in mind, there should be no new impacts unless there is a new surprise, if it is something we are not aware of.

Dani:

Great.

André Salles:

Good morning. Thank you for the opportunity to ask a question. I would like to focus a little bit on the partnerships, two of the ones you mentioned, actually. When we look at partnerships with Nokia, what do you see is the biggest offender here for the growth of this partnership? Is it new players that are coming to the market, or players that are more adapted to the market?

My second question is about the partnership with Hikvision. You mentioned an interesting range of devices with Hikvision, but I understand that some of them may require a more specialized installation service. How does this dynamic fits with your main channel, that is the small and medium retailer?

Alexandre Ostrowiecki:

On smartphones, André, I think we made a mistake in the beginning, an error in assessment. When we came in with Nokia, we had that coincidence of the departure of LG. So I mentioned that a few times, LG had 10% of market share. LG announced it was going to leave the smartphone market worldwide, and then we said, well, if LG is leaving, retailers are avid for a third brand. They do not want to rely only on the two big players, the two that, you know, hold 90% of market share today. They had 80% of the time.

So will this 80% turn into 90% and the result will be at the hands of two? With Nokia, we found a brand that is well known, a traditional one, and we thought we could take LG's space. So since we already had a 2% market share with Multilaser smartphones, with 2%, 3% with Nokia, we would go to 5%, 6% market share. It would be an interesting figure to defend.

But since then, being quite honest, we were not competent enough in the premium smartphone market, which is completely different from the entry level smartphone market. You have the time to market of launching products at the speed and specification and updated according to the competition, while on Multi, we have the basic entry level products with great share, great margins, defending the market, but it is a small share. Entry level smartphones have a very small share. It is about 5% of the total market.

So this midmarket, which is almost 30%, the big money we wanted to embrace, the pace of launches and updates is very fast, and we were not able to keep up with Nokia. So we were always three, four months behind. We launched with the price, we needed to give a discount, we could not get margins. We are kind of chasing our own tails.

It was a lesson we learned. We are still fighting there. There are new lines coming up. We are going to break more rocks down than we imagined. Thinking in the beginning, "Oh, LG is leaving, everyone is going to embrace Nokia, it is going to be beautiful" did not become a reality.

But we are remaining in this plan, launching new things with Nokia to accelerate and clean house. But it was not a good entry.

Now, changing to the other question, about Hikvision, you are completely right. The retail channel has nothing to do with the specialized security camera channel. Since 2017, we have a separate division, which is Giga Security, which we bought in 2017, and this channel. It was very similar to the market leader that is also listed, everyone knows. It is different from retail. You need to sell the products to specialized distributors or dealers that are focused on specifically this channel of security and CTV, and they served the installers in the direct channel.

So it is more of driving sellout, you have to have marketing teams in the distributors, give a lot of training, a lot of material. You need to train and run campaigns to get the loyalty of the installers, because people do not tend to have a brand of security that they are going to impose. If you have an installer in a region, they work with so many brands. And then, today Hikvision is basically number two, 25% market share. Giga is number three with about 8% market share, and there are a lot of smaller brands. So the leader holds about 60%, 25% Hikvision 8% Giga, then smaller players.

With Hikvision together with Giga, we are talking about more than 30% of share, 33% market share. So that is already quite robust. Then we need to intensify this attack to distributors. Work strongly on distributors, give more trainings, more sellout, more campaigns, more incentives to installers so that they adopt and embrace our technology. That is what we are working on. We brought two senior professionals to this department to work on Hikvision. We are having good perspectives here.

André Salles:

Very clear. Thank you.

Marcelo Afonso (via webcast):

Can you already have a vision of sales for government in 2023?

Alexandre Ostrowiecki:

This year is quite strong, we will post a small growth in government. Remembering that it grew very strongly last year, from R$40 million to about more than R$1 billion. Unfortunately, government, we do not have a long term pipeline. It is not a recurring revenue for years, but part of this year's revenue will drop on next year.

I believe that the government now, with devices for education, they are here to stay. Government has distributed a lot of tablets and PCs and Chromebooks. This was really good for the teacher's community, parents, students. There is a budget for that, so the trend is to always have business with government, but I cannot give you an idea of size.

At the end of 2021, we projected 50% drop for 2022 to be conservative because we did not have the business on the table. If you were there at the calls, you remember we were quite conservative. And this year, fortunately, we are seeing a small growth compared to 2021. I hope we can repeat this next year, but we cannot count on it.

Marcelo Afonso:

The financial credit has been increasing quarter on quarter, and today is at R$382 million. Is there an estimate of how when this will stabilize or start to decrease?

Alexandre Ostrowiecki:

Yes, Marcelo. This is a big challenge for us, the financial credit. This is also related to what Dan mentioned about margin. Something that we struggled with this year was the high inventory levels. Our average inventory at home went from 3.5 months to about 5.5 months. We are talking about two additional months of inventory in house, paid for. And in Brazil, when you import a product, you must pay almost 100%, usually 80% then and there, at customs, 80% to pay for expenses, import taxes and all the handling, warehousing, PIS/COFINS. Everything is paid right then and there and credited.

So my estimate is that about 2/3 of this value is stocked. So as we bring our inventory down for the 2H22, we tend to consume this financial credit. And 1/3, of course, is the informatics line and credits generated from the PTB. But we can get the details for you later. I am just giving you the outline.

Robert Ford, Bank of America (via webcast):

Can you explain what seems to be ICMS fines of R$92 million?

Alexandre Ostrowiecki:

Exactly, Bob, that is what I talked about in the tax review. R$92 million minus some credits, there are some credits there, net EBITDA around R$40 million. That is what we have talked about there, spontaneous reporting, basically. A discussion of intercompany credits, whether or not we could take that credit, that was also raised since 2017. And we decided to be conservative, not to discuss, to spontaneously report it and liquidated within the quarter.

Robert Ford:

Should it be litigated?

Alexandre Ostrowiecki:

No. We decided to break down these value installments and get it out of the way. There will be no litigation. And the impact was 100% in this quarter.

Robert Ford:

Could you explain the quarter on quarter drops in the office and I.T. margins, as well as kids and sports?

Alexandre Ostrowiecki:

I do not have this breakdown here now, but we will get back to you.

Robert Ford:

Great performance on the DC, but still small.

Alexandre Ostrowiecki:

Yes, from 4 to 7, that we had on our presentation.

Robert Ford:

What is the expectation and plans for the direct to consumer business?

Alexandre Ostrowiecki:

Bob, we unified this area. Everyone is excited. We have excellent professionals. We have an office in Belo Horizonte focused on that with about 50 people there, a team in São Paulo as well. So certainly, these are the areas that have the highest growth targets. We have a very aggressive target to deliver more and more in direct to consumer, and more than that, improve margins, because the play so far has been on top of campaigns, promotions, and less on exclusive items. But now we are talking a lot about exclusive items working on better margins.

Guilherme Corazza (via webcast):

In the release, you mention a new inventory administration model. Can you give us more detail?

Alexandre Ostrowiecki:

Excellent, Guilherme. Basically, we had a model that was not working with the purchasing budget. We worked with the restocking value in terms of number of pieces. Our system looks at the past, looks at the day to day sale of each product, all this product selling three pieces, five, eight. And when those sales are zero and the inventory is zero, they take it out, and we create a number that we called algorithm. That is the average daily sales.

And we have been buying to replenish inventory at this algorithm. So we have this mouse here, Rapoo, selling 23.5 pieces per day. So the restocking is four months, securities inventory as well. So 23 pieces times eight months, 40,000 pieces of this mouse. We need to buy 40,000 of them.

And then we would restock. Since we had our working capital at a lower level, we had not had that lesson learned in the quarter. We would release it and restock to keep the inventories regularized so that we would not have a shortage. But it did not optimize working capital.

So what we implemented last year, and the Financial Planning Department did, we took family by family, manager by manager, and we created a beacon but close. It is actually a light post, red, green and yellow, and according to the color, we give them a purchasing budget.

If the line is green, they can restock on that same reasoning that I talked about, eight months and so one, or seven to reduce the inventory levels. If it is yellow, they can restock 50% of the COGS of the previous month. So they divide it and calculate the USD and so on. So the manager, the head of the business unit has a check applied to this rule, and the inventory levels will go down month by month.

I do not know if it is too many details, but I know you like this, numbers and management. It is really nice. So there is a power BI, they get their budget and they buy.

Guilherme Corazza:

So on Mulit's projections, the breakdown of sales for channels will be maintained?

Alexandre Ostrowiecki:

I do not think so. I think national retail will retake its fair share. It is going to bite a little bit of the others share. It is going to pressure margin, but the improvement of retail overall reduces discounts and it kind of offsets everything.

Francisco Rosset (via webcast):

Does the Company have a lot of debt in USD that required this exchange rate swap? Because the Company had a good operating performance, even a positive financial results, but this net exchange rate variation killed the net income. Could you explain that again?

Leonardo Dib:

The Company has protection for the exchange rate variation on debt, and we mark this effect here, but there is also exposure on suppliers, and we do not hedge the entire supplier base, since we have the concept that we can work on the transfer of that to the price. But the fact is that, since we marked to the market, the position at that moment generates a negative exchange rate impact. And last quarter, there was a positive exchange rate effect. It is not necessarily cash. One thing offset the other in the quarter. So with that policy, we see these effects of the exchange.

Alexandre Ostrowiecki:

The bank is all in BRL, right? It is only for suppliers.

Leonardo Dib:

Yes, it is only suppliers.

Robert Ford, Bank of America (via webcast):

How should we think of smartphones in the long run? Chinese producers seem to be aiming Brazil more aggressively. How do you see 5G?

Alexandre Ostrowiecki:

Multi smartphones, we are launching new products, increasing average price. We are seeing an acceptance. We were a brand that only sold the entry line, but we are selling more. F, F Pro, G. Multi has three lines: E, F and G. Entry, F is mid and G is mid low. That is what is really booming now. People are looking for smartphones from R$700, R$800. That is our brand, Nokia, we are also working on the brand, bringing in new products, repositioning.

Chinese producers are interested in Brazil, but they have barriers here for the local products. We need to see what their appetites is going to be like. Without domestic manufacturing, it is almost impossible to compete in Brazil. So one way or another, they need to make the investments, buy national memory, have the electronics plants. So until they come here and invest millions to manufacture, they will not be able to have a share outside of the gray market.

So we are excited with the smartphone perspective. It was a bad semester. We have been growing, this 1H22 has been quite painful, but I think it will improve. We see very positive signs because we are already halfway through the 3Q. The first half of the 3Q has been good, even for smartphones.

5G, I am very excited. That is the normal evolution of technology, and it seems a lot like what happened with 4G. It starts with 100% on 3G, growth in entry little by little, and that is the normal technology evolution. All of our areas have products that drops one type of technology and evolve to another one. For example, Wi-Fi, 56 Mbps, moving to the N line, 300 Mbps, C line, 1200. It goes up and we renew it.

And 5G brings a lot of opportunity. We have the first Multi 5G smartphone in the oven. It is going to be released by Christmas. It is an H 5G. H is ultra-premium, above G. We also have ZTE, our Internet provider partners for routers, 5G routers for people to have it at home. 5G is a game changer. You cannot route 4G to your house, but 5G will have a ZTE router, plug it in, put a chip, and the whole house will have high speed Internet. It is not as good as fiber, it is not going to replace fiber, but these technologies will live side by side.

Thiago Souza (via webcast):

If Taiwan is invaded by China, how would this event impact the operations and results of the Multi Group?

Alexandre Ostrowiecki:

Thiago, I really like this topic, but it is not my area of expertise. I imagine it is going to be a worldwide chaos if this comes through. Depending on the weapons, the impacts, the duration. We cannot compare it with the Ukraine-Russia case, because China is the world's greatest industrial power, Taiwan for semiconductors.

So if Taiwan is invaded by China, and it is not extremely briefly resolved, it would be chaos for the global economy as a whole. Everything depends on technology. All products coming from China, our biggest economic partner. It is a doomsday scenario.

I would love to say that we would migrate production to local, but it is not feasible for anyone. The components come from there. Nobody can manufacture all the components required. The silicon devices, semiconductors, there is no economic branch in the world that would not be affected by that scenario. It must be avoided at all costs.

Thiago Souza:

What are the three macroeconomic variables that are most relevant to the Multi Group's business? Why?

Alexandre Ostrowiecki:

Since 60% of our sales is consumption, consumer, the disposable income and the purchasing power of the C and D economic class population is our major driver.

So what moves disposable income? In my opinion, unemployment, inflation. What else? Come on, you can tell me. Interest rate. You? See. So unemployment, inflation and interest rates. If these three aspects get worse, that affects the disposable income, reduces consumer, offset a little bit with the trade down because of the entry level migration, but it is not sufficient to guarantee good sales.

Mateus (via webcast):

Congratulations on the marketing and rebranding initiatives. We are keeping track, very excited. A question about the hiring. It attracted attention in the sustainability report that more than 3,000 employees have been hired in 2021. Today, 60% of your employees have been in-house for under one year. Can you tell us, please, how the integration of this people has been and what are the main difficulties?

Alexandre Ostrowiecki:

We had a lot of expansion and this boom moment. We went from R$2 billion to R$6 billion, increased 3x, employees doubled. So we tripled revenue, doubled the number of employees, but mainly it is industrial personnel, factory to produce products. It is factory labor.

The second place is increasing logistics. Because of the higher inventory, we had to increase the number of DCS, more products, more goods, more people handling goods, and then in product areas with the launch of new lines, the business units' teams have been reinforced.

But it is a big challenge, Mateus, because it came along with the remote work condition. We have the hybrid system now, and Multi defenses this freedom with responsibility. That is our motto, of course, inspired by Netflix, who was the main disseminator of these words. But we practice that here and we have a strong feedback that this makes sense in the Company's day to day.

It is always a challenge to integrate people at home. We are running a lot of events and meetings from different departments for integration from the product area, IT area, even back office. We had that meeting with the accounting team here at the office to get more aligned. I feel that the atmosphere is really good. People tell us they are quite satisfied. Overall, they have the Multi spirit. It is a different way of being, very laid back, informal, things happen fast.

People say that, "oh, if you have one defect is that you go too fast, you stumble and then you have to make corrections and adjustments". But it is a company of doers, not a company where everyone is sitting on top of decisions, shifting things, one side to the other. It is very fast. We have a big room here if you want to come and visit. There is 200 people here every day. I sit there with directors, with reps and everyone, and it is it flows quite fast.

And we have been working a lot on those seven values of Multi, the culture, the freedom, responsibility, who decides, delegation, zero prejudice and all that.

Guilherme Corazza:

About electric motorbikes, how do you see the competition with Voltz, which started first deliveries last month?

Alexandre Ostrowiecki:

I would not know about Voltz. There is a lot of businesses. It would be reckless of myself to do that. But what I have been seeing with the business unit and the works with that, Rodrigo and Alexandre are the heads at Watts, and we know that Voltz had some struggles, being a startup, starting their business. It seems to be a serious company and we are going on top of them, as all markets. There is no market that has no competition.

So we are used to joining markets even that are completely consolidated, that customers tell us not to go there, and we go there and we take a share, like TVs now and so many others.

Thiago:

What are the mistakes that generated this spontaneous reporting and the ICMS?

Alexandre Ostrowiecki:

The mistake is that we have two companies in Minas, one that builds components and one that produces industrial products. The components exit is has incentives, there is no way ICMS, and in the other company as well. But we had an understanding that it does not matter which company imports. If you import from one and transfer to the other, you would be entitled to incentives.

But there is a technical detail that if you import, manufacture and sell, you have incentives. But if you import, sell to a brother or sister company in the same group and transfer to the next one, and you sell, you would not be entitled to incentive. And we had doubts if we should discuss this judicially or agree and we self-reports and not spend money with lawyers and fines.

So being a conservative, we decided in this case to spontaneously report, pay the ICMS intercompany with the two of the Multi Group's incentivized companies, and this is solved. It is not a very relevant value month by month and we will not have this concern.

There has been a lot of discussions that have been discussed in the past, but we decided that it would be better to do it like that, break it in installments and feel more confident.

Francisco Rosset (via webcast):

Last period, the high valued USD made the domestic line consumption to improve significantly compared to internal consumption, since imports important brands price went up too much. With a potential improvement in the economy and stable USD, do not you see a potential migration to other mid-quality brands affecting Multi's revenue?

Alexandre Ostrowiecki:

Let me understand better, because the USD is not going down, Francisco. It is stabilized at around R$5. It is a high level for the USD. So if the economic scenario improves and the exchange rate appreciates that, maybe there is going to be a flood of imported goods, foreign brands.

We saw that in the past, and it increases the share of premium global brands a little. There is some of that effect. But on the other hand, in this scenario we are looking at, you are talking about the valuation of the BRL. Probably interest rates will go down. The economic scenario will be of growth, low unemployment, consumption increasing.

So the pie increases for everyone, including us. People by brands from other countries, but for our share maybe it is not such good news, but in the top line we will do well. So there are scenarios whenever the economy is booming. In the first Lula administration, pre-Dilma crisis, it would go, Wow.

Thiago (via webcast):

How do you see small retailers who wish to sell only on the Internet? And how are you structuring to serve these players that only have an online store and not a brick and mortar store?

Alexandre Ostrowiecki:

Great question, Thiago. We have thousands of customers like that. We call them small sellers. And they are doing quite well, as incredible as that seems. They have a lot of advantages compared to the incumbents, the giant ones.

And why don't the top three players massacre the small ones with their scale, competitiveness and so on? Why are so many small sellers growing? We have examples that are not even that small anymore. The half year was so bad that today, I have small sellers buying more from us than some large retailers. We have some sellers that we considered small selling more than incumbents, because of the platforms where they sell. So they sell more on 3P through them than in 1P directly with a large player.

Because the seller is usually an entrepreneur that understands the product, choose the right product, can work on price actions. They may have a more advantageous tax scenario because they are small. In some cases, each company has their own engineering. Small companies in faraway regions may have tax plays that make them more competitive in that sense.

Geographically, they are closer to their consumers. A seller in Paraopebas, for them to deliver in the neighboring towns, it is a lot faster than if the client buys in the 1P with the inventory in Rio de Janeiro or São Paulo. They have these cities spread out in Brazil. A small seller in Acre, for example, is closer to them, and finds the opportunity. So they are doing quite well.

And we are very excited and investing in our e-commerce infrastructure in two ways: we have our own website. You go at multi.com.vc, or multilaser.com.br, it is still active, or you can go to the marketplace as well where we are plugged in. We are plugged in the large, medium and more than 30 different marketplaces, including bank websites, airlines, mileage programs, affiliate member programs.

So we are plugging our inventory to a lot of options that you can buy directly. And for small sellers, we created a project called Multi Line, Linha Multi. That is a free virtual store that they can upload free of charge overnight and choose what they want to sell. So you go to a neighborhood shop in Salvador and they have 200 products that they bought in their 1P, on the shelf, but they can sell more than 6,000 Multi products through a website that has their face. It can be the John store. You type johnstore.com.br, you go to a website that will have the customer's logo but Multi's structure behind it, and you can buy any product from Extrema, from our plant, it leaves Extrema directly to the consumer and the client gets a commission for working that.

Daniel (via webcast):

How are Multi's perspectives for the last quarter of this year for the sales of PCs, tablets and smartphones? Do you feel the market is more apprehensive with the uncertainties?

Alexandre Ostrowiecki:

Quite the opposite, Daniel. I see the market more excited than they were in the 1Q. Definitely, people are more excited. I see the sales in large retailers starting to grow. We have to break this down in two: in government, we have a robust delivery pipeline for the 2H, it is very strong, of things that have already been won. And on retail, I do not think it is going to be spectacular. I do not think it is going to compare to pandemic levels. I do not think it is going to have comparable margins, but it will be better than the 1H22.

I think we have covered everything. Excellent. If there are no further questions, Ju, let us go to the closing. I will turn to fortune. Juliane. Thank you all very much for the trust in our Company, for attending this call. Let us go to the 3Q.

Juliane Goulart:

Thank you all for your presence. If you did not see the whole meeting, we will make the recording available as well as the transcription of the call in our Investor Relations website. Thank you very much. Have a great day.