2Q20 Results Webcast

August 17, 2020

Mrs. Suzana: Good afternoon. Thank you for waiting. Welcome to the d100 Varejo Farma Webcast regarding the results of the second quarter of 2020. We inform that this event is being recorded and translated into English language, and will be available on our website. Questions will be received via chat and answered after the presentation. Before going ahead, I would like to clarify that any statements that may be made regarding the prospects of the Corporation's business, as well as its projections, are forecasts based on management's expectations. Such expectations depend on the sector's performance, the country's general economic performance and market conditions. Therefore, they are subject to changes.

Sammy Birmarcker, CEO of d1000 Varejo Farma, Marcos Santos, CFO and IR, Ana Cândida Fonseca, Marketing Director, Lívio Silva, Operations Director are with us today.

Now, I will give the floor to Sammy Birmarcker. Go ahead.

Mr. Sammy: Good afternoon. Before we start with the presentation numbers, I would like to update the staff with the latest information from July. In August 10, we had our IPO of d1000 Varejo Farma, DMVF3, and I think it's cool to be sharing some information here. Following the line of the market, in July, we had an increase of 12% in revenue, when compared to June 2020, already showing a consistent recovery.

We also had the creation of a new Sellout Board, dedicated to the RX and generic category.

Throughout the pandemic, we maintained our store opening schedule. In July, we had two openings and this will become our minimum level going forward. We also had four store expansions already contracted for the third quarter. Remembering that these expansions are focused on stores with less than 90 square meters and that usually or historically bring about 40% more sales.

All stores resumed operations. Some located in malls and sidewalks are still at reduced hours, but with an increasing flow, reinforcing the idea of a gradual resumption. And, with IPO funds, we have a reinforced cash flow for investments in network expansion and digital transformation.

As was widely reported during our roadshow, we have a strong presence in three formats: premium, standard and popular. Much of our expansion project is focused on the popular, this largest photo represented here through the Tamoio brand, but that does not mean that the popular openings will be only of Tamoio. It's just an example that we have of what we do in our popular format.

Now talking about digital transformation, also during the roadshow, we explained why we were a little late in this regard, due to the whole process of integrating the systems of the acquired companies, but, in June, we started to remove this gap that we had. By the end of the third quarter, all brands will already be operating in online sales. I think this is an important point and we started based, structured with all the strength that we have always had in the call center. We have been able to operate with a very satisfactory delivery time. This is going to be one of the differentials of our digital transformation strategy through online sales.

I also think it's cool to share that we have not neglected, at any time, all preventive measures in relation to Covid-19. Here is some material exemplifying the protection of both the counter and the cashier and also the furniture for the use of gel alcohol in our stores.

Now, Marcos, our CFO, will talk a little more about numerology, but I will continue to be here to help with the answers. Thank you very much.

Mr. Marcos: Thank you, Sammy. Good afternoon everyone. Regarding the financial highlights, remembering all the numbers present here count on the application of IFRS16. So, in the second quarter of 2020, we had gross revenue of R$ 230 million, a reduction of 24% versus the previous year. If we exclude mall stores and closed stores, we had an effective reduction of 4.2%. The gross margin of 30.6%, 1.6 percentage points higher than last year. EBITDA of R$ 14.5 million, an EBITDA margin of 6.3%, 1 percentage point lower than the same period last year. And a net loss of R$ 13 million, of this amount, more than 60%, 63% occurred in the month of April, which shows the dynamics of the evolution of the Corporation's results within the quarter. And we ended the quarter, during the quarter, with a free cash flow generation of R$ 8.1 million.

Now, going a little more through the details, our gross revenue is 230 million. It is worth emphasizing that it was strongly affected during the period, due to closed malls, remembering that in 18% of our store base are located in malls, which were closed most of the quarter. If we compare it with the 10 main players in the retail pharmacy, surely d1000 has the largest weight of stores in its network, in the portfolio of stores in malls. Removing that, removing the result of malls stores and stores effectively closed, I say again: the effective reduction in sales was 4.2%. Why is this number so important to us? Sammy already commented, in July, we had a 12% improvement in sales, when compared to the previous month, and the resumption of the mall was much faster than that. So, it also shows better the dynamics that we are currently experiencing and how it behaved at the end of the 2020 quarter.

With respect to our gross profit, we delivered R$ 70 million, a gross margin of 30.6%, an improvement of 1.6 percentage points compared to the previous year. We achieved this result thanks to the implementation of a new pricing strategy, especially focused on RX and generic, which proved to be a winner and a legacy for the coming quarters and for the future of the Corporation. When we go to operating store expenses, we had a total of R$ 46.6 million, which represented a weight of 20.3% of gross revenue. Most importantly, it is a 9% drop in expenses when compared to the same period last year. How did we achieve this reduction? Part of this is due to the smaller number of stores in our base, and the other half, due to our ability to respond quickly to a reality that we saw in stores, which was the drop in the flow of consumers, as happened in so many other segments. Our response was to relocate the staff of those stores that were closed to the open stores and to our call center, review the work schedules of our store team, part of the team on vacation and, very importantly, the application of Executive Order 936, which provided for the reduction and suspension, in some cases, of the employment contract of some of our employees.

So, back, when we look at the contribution margin, despite the significant reduction in sales experienced in the quarter, our efforts were able to mitigate this effect with a better gross margin, an important reduction in expenses and, with that, we were able to deliver a double digit contribution margin, reaching 10.3% in the period. It is also worth noting that the closing of the 10 stores we made within this quarter will bring an increase of R$ 3 million per year in our contribution margin from the stores and, consequently, in the other financial indicators.

In corporate expenses it was not very different, when we talk about expenses. We reached R$ 11.7 million, an even stronger drop, a 20% drop compared to the previous year. And here we have two main reasons. The first is a groundwork that started at the end of last year and was completed at the beginning of this year, which sought to improve the productivity of our entire back office. For this, we counted on the help of an important external consultancy, Proudfoot, which accompanied us throughout this trajectory and, in the second quarter, we start in this quarter of 2020, we start and see the first results.

On the other hand, once again, our ability to respond quickly, our agility, with application within a few days of Executive Order 936, for reducing and suspending employment contracts, for a good part of our corporate structure, as well as for reviewing and cutting general expenses. As a result, we landed a corporate expense of 5.1%, when, obviously, a dilution would normally be expected, but this happens, this dilution does not come due to the sales of the period.

Well, with all this, we reached an EBITDA of R$ 14.5 million, a margin of 6.3%. And here it is worth making a review. We had a 24% drop in sales and only 1 percentage point of EBITDA margin. We did everything we could and quickly to guarantee the Corporation's operating margin. The application of Executive Order 936, negotiation of rental contracts, not only of those stores that were closed but of our entire store portfolio, review, cut, reduction of expenses in general, recognition of 1.6 million of a tax credit by reason of the Supreme Court decisions, and other initiatives that contributed to keeping the EBITDA margin still in line with what was the first quarter of 2020, and just one point below what was the same period last year.

Moving to the bottom line of the Income Statement, we had a loss of R$13 million, which represents a net margin of 5.7%. As I said initially, very impacted by the month of April. Why the month of April? April was the month where we had the greatest impact on our sales and it was not yet possible to capture all the savings as they did in the months of May and June. For this reason, this concentration in the month of April, which also gives the perspective of the Corporation's results and profitability within the quarter.

It is also worth remembering that from EBITDA to our net income, we have depreciation, financial expenses, income tax. Depreciation in the period weighed 8.3%. Returning to the normal level of sales, the weight should be around 6%. So, it should generate a gain of 2 percentage points in our net margin naturally. And the financial expense, more than half of it, comes from interest that is linked to the loans that we have with financial institutions and banks in general. With the proceeds from the IPO, this will obviously be falling and improving our financial result, consequently, bringing benefits to our net margin.

Now starting to talk a little bit of cash. Our cash cycle in the period was 38 days. It is very much in line with the previous year, which was 37 days, but this indicator does not reflect all the efforts we made in the period to protect and improve our cash. And here it is worth highlighting some points. The first is the positive operating cash flow of R$ 17 million in the period. We managed to achieve this result with a reduction in inventory in the amount of R$ 14 million. Here, the supply team has a very strong job in rebalancing the stocks of those stores temporarily closed to the stores that were in operation, as well as from the stores closed to the stores in operation; an important work of our team is the commercial collection of our receivables from the industry, reducing the balance, this balance receivable; and we also took advantage of all the benefits given by the government arising from the Covid-19 pandemic, regarding the postponement of payments of some taxes. This also had a positive impact of approximately R$ 5 million on our cash flow within the quarter. Well, the positive operating cash flow enabled us to double investments in stores in the period. We went from 4 million to 9 million investments for store openings, expansions and renovations of our stores. I think this indicator is very important. In other words, despite all the circumstances, we do not give up our future, which is organic expansion. Considering all these factors, we achieved a positive free cash flow generated within the quarter of R$ 8 million and I think it is worth a last reflection on this topic, which is in relation to indebtedness. We closed the second quarter of 2020 with a net debt of R$ 203 million, but with the inflow of IPO funds, d1000 changes its net debt situation to net cash of over R$ 100 million.

These are the main financial points I had to share. Now, I will give the floor to Suzana, so that we can start the question and answer session.

Mrs. Suzana: Thank you. We will now start the question and answer session. To ask a question, please write in the Q&A. After the Q&A, if you have any questions, I and the Investor Relations team are at your disposal for clarification. Our email is ri@d1000varejofarma.com.br.

Let's go to the first question: What is the Corporation's expectation with the opening of malls and the reduction of social distance? Can we expect better results in the coming quarters?

Mr. Sammy: Good afternoon. Thanks for the question. Yes, we have seen, every day, every weekend, the movement in the mall improving, sales being recovered.

We have the perspective that between the third and the fourth quarter, it is probably already normalized, except for some big second cycle of contamination, something in that sense, but within what we are currently seeing, between the third and fourth quarters, this is already should be normalized.

Mrs. Suzana: The IPO funds are for an increase in the number of stores, in addition to a reduction in indebtedness. Do the plans include expanding the geographic area of operation? Is it possible to comment a little on this, even if generically? And how are you seeing these expansion plans? Considering the movement of other networks in the country, also in this sense, such as the follow on of Panvel and IPO of Pague Menos.

Mr. Sammy: Well, I think it's important that we emphasize the use of funds. 50% will be for us to fully pay the debt in the coming months, and the other half will be distributed between working capital reinforcement and the expansion plan. In the short-term, our expansion plan focuses on the areas in which we are already operating, subject to execution risks. This accelerates our capacity, including implementation, and we leverage the recognition of the brands in our portfolio.

In relation to competitors, I think we have it there ... the financial market has a series of different story options, but I think that, in relation to our project, it does not have much effect because the other two are also very regional, from the point of view of their expansion plans. At least, that's what we've been reading about. I think that it does not see an additional risk of execution for us in that sense. Panvel focusing on the South. And it seems to me, from what I've heard, that Pague Menos also focuses on the Northeast. As we are not in these areas, I don't think it changes much for us.

Mrs. Suzana: Good afternoon. Could you talk a little about the behavior of each brand? We saw that the popular model benefited this quarter. Can we imagine that Tamoio performed better? And how do you imagine the behavior by market in the second quarter of 2020?

Mr. Sammy: We will not comment on our releases by brand. I think we will concentrate much more on the format. In fact, the popular format demonstrated an even greater resilience. It seems to me that this is very much linked to a greater flexibility of the distancing rules in these regions. Again, our expansion plan focuses heavily on this popular format.

Mrs. Suzana: What level of gross margin or EBITDA do you aim to achieve in the restructured and mature units?

Mr. Sammy: I think that if we answer, we would be giving guidance. I don't think I can comment on that, but it is obvious that we aim at the market average, at the very least.

Mrs. Suzana: How much are online sales expected to be incremental and not substitute for physical sales? If possible, what expectation of online revenue to expect to reach total revenue?

Mr. Sammy: This is an interesting point. We passed the pandemic, much of it, without our online sale, 100% of our delivery was practically based on our call center. It had the same performance in relation to the sale of other market figures disclosed, we even had a 12% share in our sales. And it is important to remember that this structure that supports delivery, the polo stores, has also been greatly strengthened during the last few months and, with this, we have been able to perform our delivery quite efficiently, and this is being perceived by our consumers. I think that, for now, as long as we have this issue of distance and restriction of opening hours in some regions, we will maintain this greater weight in not face-to-face, whether call center or online. But, with things returning to normal, we imagine that there will be a setback in this participation, but not to the previous levels. I think we will have set a new level that will not be as high as it is now, nor will it be as low as it used to be.

Mrs. Suzana: Based on the values informed in the IPO, referring to the distribution of funds, will d1000 publish any guidance?

Mr. Sammy: For now, we do not expect to operate with guidance in d100.

Mrs. Suzana: I would like to know the positioning of d1000 regarding the phenomenon of the pre-rise in the price adjustment of medicines and how this positioning is reflected in the current stock level.

Mr. Sammy: I think that in view of all the uncertainty regarding the price increase, during, I would say, some days, there were doubts if we would have this price increase, and at the moment that the market was still very volatile from the point in terms of credit, we decided not to overdo this investment, this pre-rise. We will still have part of this gain happening in the third quarter, but we chose not to make such a big investment in d1000 this year, due to all the volatility. We had a very big change in the sales mix, we were afraid that a wrong bet would have some financial impact, in our opinion, it was risky at that time. So, it was a year that we invested proportionally a little less.

Mrs. Suzana: Can you comment on how the contribution and/or EBITDA margins are running now, July and August, excluding IFRS if possible, given the greater normalization of sales and the closing of the ten loss-making stores?

Mr. Sammy: We ... I don't think I can go so far in the statement regarding the third quarter, but Marcos remembered it well. Our loss-making stores contributed negatively, around 3 million per year. We are seeing a recovery, a return to almost previous levels of results, but we have a very optimistic outlook for the third and fourth quarters, when we already have the effect of inaugurations in greater quantity per quarter, and store expansions as well.

Mrs. Suzana: There being no further questions, we closed the question and answer session. I would like to thank everyone for the participation and say once again the Investor Relations area is at your disposal. Good afternoon.

Mr. Sammy: Good afternoon.