

Conference Call Transcript 1Q21 Results

Pedro Zemel:

Good morning, everyone. Welcome to the SBF Group webcast, where we will discuss the earnings results of the 1Q21 of SBF Group. I am Pedro Zemel, CEO, and I have José Salazar, CFO, Daniel Regensteiner, our Corporate Finance Director, and Luna Romeu, our IR Manager.

As you can see on slide two, today we will separate our presentation in three parts. First, an update of the current moment and the highlights, then we will comment on our results, and at last, we will have a Q&A session. Questions can be sent through this platform and they will be answered after our presentation.

So we will start on slide number three. During the 1Q21, our financial result was impacted by the increased restrictions of retail opening hours because of the pandemic in 2020. This impacted our operations in the first half of March.

We have been impacted during the entire quarter. This scenario affected our store sales, and in 2020, the drop in our brick and mortar stores caused deleveraging, and this damaged our EBITDA.

On the other side, the GMV online of Centauro is growing and it offsets partially. As stores go back to normality, something that we have been seeing, we expect a recovery of EBITA margin to levels pre-pandemic.

We do have some interesting figures to share. Number one is that the SBF Group grew 59% in revenue driven by the acquisition of Nike. But this is the business that we have right now, and one we have a challenging quarter, and the seasonality of the year. We have R41 billion in revenue. We believe in what we will be able to deliver when we open our stores and our margins go back to normal.

In addition to this, our online sales continue growing soundly. Entering the 1Q, they grew 138%, and this represents 30% of total sales, driven mainly by the result of nike.com.br, that in this quarter represented 25% of Fisia's revenue. In addition to the migration to the DTC channel, direct to consumer online, and now we already have put into practice initiatives that give us results. We have broadened our portfolio to sell through the Nike site, and we have optimized our online marketing to create more conversions. The gain of shares of online DTC to Fisia contributed for it to reach an EBITA margin of almost 10%, 9.8%.

We are highly satisfied with the speed of the implementation of the projects that will lever the value of this acquisition. During the 1Q, the first months of with positive results of Fisia, this shows you the opportunity that we have to broaden the profitability and penetration of Nike, especially with an assertive online strategy, in addition to have new initiatives that allow us to drop costs and optimize the profitability through our direct contact with our consumer.

Another important point, although with the worsening of the pandemic, the omnichannel sales of Centauro grew. And when the stores were open, we observed sound and healthy sales. During the last weeks of April and May, we continued observing good signals of recovery for the open stores, and we are already seeing a growth of same-store sales, especially in the G5 stores that continue

showing performance above the traditional stores, and even above what we had projected when we created the store model.

This behavior confirms that the customer is omnichannel, and the store experience is essential for the purchase process when you buy sports goods. This is why we continue with our long term plans to expand our stores in new cities, to broaden our national presence.

Although it is still fragmented, we evolved in our ecosystem so that all the business units work in an integrated format. This year, we are prepared to face the pandemic without deviating our focus on the projects that will give us value in the long term. Our technology team will give agility to these projects that will give us new value, and we will be able to give more functionality and a better experience.

We are also integrating with NWB, which is part of the Group and it started on March 1st. As a first integration experiment between the business' channels, we transferred the Brazilian Female Soccer Championship. And last year, when we face the great uncertainty because of the effects of the pandemic, we adopted restrictions, and also measures to protect our cash flow.

Now we are prepared to face a second wave, and we are focused on the projects that will add value in the long term. We believe that the reopening of brick and mortar stores, even in the middle of a pandemic, will allow us to grow the sales in our stores and to have more profit.

We will not change our investment plan and our growth plan, focused on the building of a new ecosystem and increase of national reach, and an improvement in the sports experience purchase. But we are paying attention to the short term to react quickly to any change in this scenario.

Now I give the floor to Salazar that will give you details regarding the financial highlights of the quarter.

José Salazar:

Thank you, Pedro, and good morning to everyone. Let us go to slide number four. During this quarter, in our release we present a table with all of these affects. The results that I will present in the upcoming slides are adjusted by the nonrecurring effects, and we will comment on the effects of IRFS. This is complete, where we include Fisia, and 2020 figures are only Centauro figures.

We will go to slide number four, in our main highlights of the quarter. We totaled R\$1 billion in gross revenue, an increase of 59% when we compare it to the 1Q20. We had an increase of 45% of GMV online in Centauro, and R\$126 million in the digital platform of Fisia. At the end of the quarter, we have a cash position of R\$412 million.

We can go to slide five of the presentation. When we see the total revenue, we grew 61% during the quarter.

We had a drop in Centauro because of the worsening of the pandemic during the quarter, when we had greater restrictions. In March, we had days of 93% of our stores closed, and in 2020, the second week of March was affected. Centauro had 39%, and GMV was 45%. This is result of the omnichannel investments, technology and marketing that we carried out in 2020. Even with the drop of markdown level, Fisia also represented good results, 24% of the net revenue. The second wave also went to the digital platform.

On slide six, we will talk about the gross income and gross margin. Gross income in the 1Q was R\$353 million, a growth of 43% when we compare it to the 1Q20.

A drop of 3.8 p.p. of Centauro's gross margin is a consequence of the promotional environment caused by the pandemic. The price dynamic was normalized, but with the worsening of the pandemic during the 1Q, the margin was stable and equal to the 4Q20.

Other factors also contributed to this drop:

1. mix of channels, with more digital platform's representative
2. mix of products, with the soccer channel below stock.

Fisia presented a margin of approximately 38%, driven by the gain of nike.com.br, the online Fisia channel that has the greatest gross margin of these three channels. This gain of share, as Pedro explained, is the initial result of the new marketing initiatives and the assortment since we adopted Fisia. The margin was also impacted by what we observed in the past quarter, when we assumed in the quarter the inventory, we assumed the operations of these merchandise, and now they were acquirer's in the distribution commercial agreement. And we continue expecting a drop of gross margin as we renew our inventory.

Now we go to slide seven to talk about operating expenses. The SG&A grew 54% compared to the same period last year. This increase is because of the incorporation of Fisia operations. And as we mentioned, the growth of Centauro created variable expenses. Freight and performance marketing, but the temporary drop of this revenue is not followed by the expenses, because of most of the expenses associated to this channel are fixed. By and large, the operating expenses grew 56%.

Now going to slide number eight, we will analyze the EBITDA. The EBITDA of the Group totaled R\$37 million, with a margin of 4.6%, a drop of 4.1 p.p. in comparison to the 1Q20. The EBITDA margin of Centauro was 0.9%, and Fisia was 9.8%.

The main factors that allowed this EBITDA margin to drop were the drop of gross margin and the operational deleveraging because of the closing of stores of Centauro during the 1Q.

On Slide nine, we have the net income. We had a loss of R\$28.1 million.

Now going to slide ten, cash flow was zero. The seasonality consumes more cash during the 1Q of the year because of the payment of Christmas, but the payments were offset by the Fisia wholesale. This cash flow was impacted by the acquisition of NWB. And last year we suspended investments to preserve the cash flow because of the uncertainties of the pandemic. Right now, we have to focus on the long term and maintain our strategic investments.

On cash flow from financing, we have the same strategy, which is the anticipation of accounts receivable to reinforce our cash flows, something that was not adopted in the past. We ended the 1Q with over R\$400 million of debt, of R\$200 million, a total net debt, including anticipation of R\$343 million.

Now we open to questions that can be sent through our webcast platform.

Question (via webcast):

Good morning. I have two questions, one about nike.com.br. The pandemic could have helped to increase the share of this channel, but do you believe that this accelerated the plan of the DTC of the Company? Which were the learning points?

And the second question is about the sports platform. You were talking about NWB and Centauro broadcasting female soccer matches. What was the experience?

Answer:

Pedro Zemel:

About the first question, we are highly satisfied with the results of Nike.com.br, and very reassured regarding the prospects. As you do know, this is an important part of the value generation. We expect this channel to give us better margin, and the prospect of growth is very interesting, in addition to a direct relationship with our customer.

The brand Nike is a loved to brand. People love it. I really do not have to prove this, everybody realizes this. And this is an important factor for people to use the direct channel of Nike.com.br. So this relationship with the consumer that is strong is an element that will drive the growth.

In addition to this, this is a channel that is underpenetrated, so the participation of e-commerce in Nike.com was lower. It was 10% when we compare it to other countries and other businesses. So we do believe that there is a possibility to grow quickly, and of course, this event helped us.

I think that the purchase that was created by an exceptional occasion, this is not the biggest factor. So regarding what we have seen in reports from the banks, as stores open, there will be a greater e-commerce penetration.

We believe that Nike.com is going to drive sales, but I believe that what is important is what our team is doing, and we are focusing on this part of the business, that is an integration of our technology platforms, and also analyzing the logistic network, focusing on this. We are excited with the first signals.

The second part of your question, this was an experiment. We have had seven matches. This was an experiment and we have to see it as an experiment. What excited us, was, number one, that we broadcasted an official match live from the CBF, and this opens doors for the future.

Number two was the tone of voice of Desimpedidos, which allowed the public to be greater on the Internet than it has historically been in terms of female soccer. There was an average of 300,000 views online on these matches, and there were matches with 15,000 people watching it live simultaneously. This is a long period of time in terms of broadcast.

So we are excited because our channels, in certain event, can also drive the amount of audience that we have, and this can also encourage partnerships. And also, these are the simplest layers of integration that we can use in order to drive the audience that watches our videos, and afterwards they can buy in our e-commerce platforms.

And as we already mentioned, during the first stage of our ecosystem, this is the main way of monetizing, that is to sell products. So we want to connect the audience of the NWB channels and affiliates which Centauro.

Now, going back to the beginning, this is an experiment. Of course, we are happy with the signals, but this is just an experiment.

Question (via webcast):

In the release, you said same-store sales positive in April and May. Do you have a base of comparison from 2019?

Answer:

José Salazar:

May is being compared to 2019, and our performance has exceeded the amount. We do not want to give you the precise figures, because this can vary throughout the month. Nonetheless, we do understand that our performance is positive when we compare our figures to 2019.

We had been observing this performance in the stores that had been opened during the pandemic. In March, we already saw that consumers wanted to go to the stores, and in April and May, we saw a stronger trend. And Fisia was impacted by the restrictions.

Question (via webcast):

Since Fisia's first quarter was impacted by those restrictions, what can we expect in a normal scenario?

Answer:

José Salazar:

We always had a target in our mind that we wanted to have a DTC mix, and this includes e-commerce, Nike Factory Store that are the outlets. We wanted to start from a level that was 30% and we wanted to go to a level between 50% and 60%.

Our objective is to do this in three years, and we believe that, unfortunately, with the pandemic, we will be able to anticipate the fulfillment of this target, because we can radically change the mix. The DTC may be more relevant than wholesale. And this, of course, will improve our margin.

Question (via webcast):

Does the site nike.com.br has gains of efficiency with SBF?

Answer:

Pedro Zemel:

Not yet. This gain is not because an improvement of services from the platform, or from logistics. This is something that we are just starting. Our gains, in regard to things that were done during the five first months, are mainly of two areas. One is regarding marketing performance, and yes, this is something that we adopted.

And we treat the Nike e-commerce with variable marketing with ROI, as you do with e-commerce. And we will not asphyxiate the e-commerce when it is growing, so this is very important.

And another thing that was very important was the possibility of focusing into expanding this channel, seeing it as a priority for us, and we are going to deal with it that way, and we have to consider it on our daily decisions.

In addition to this, the team had been doing an excellent job. There were things that had already been done, and we surfed on the wave that had already been created. I just wanted to add this.

Question (via webcast):

How can the SBF ecosystem increase the purchase recurrency of your customers? And how is the purchase process of the Nike products?

Answer:

Pedro Zemel:

I will answer the first question. The retail of our category is a low frequency retail. A customer buys an average two times a year, and there are customers that, of course, buy more. This is one of the main challenges to create an ecosystem.

How do we create and make the best the journey of sport to increase the frequency that we meet our customers? Because you cannot have a deep relationship with someone that you see twice or four times a year. This is why we want to increase the frequency of Centauro.

But when we include other assets and other types of business, with this, we want to increase the frequency. And this perspective in terms of sports gives us optimism because there is strong engagement with sports, people are frequently connected to sports. A great amount of people watches a match, or read an article about sports, or use some running app or practice sports or go to the gym every day. And what we have to do is to connect ourselves to our points to increase the recurrence. So this is one point.

There is another point, which is that the Nike brand provides us. We are in members day for those that are members, these products emerge and they are all bought. This is for members, and this is an additional purchase. The product that Nike brings to the ecosystem is not that a person bought sneakers because they needed it, they bought sneakers because the opportunity appeared, and this is something that they could have bought in another segment like wine. I am just giving you these examples, but I believe that we are placing assets that help us to have lps in order to increase the recurrency.

Female soccer was an audience that was watching other things, and we brought female soccer and they connected with us. We are really reassured because we are opening channels and we are creating more sporting engagement. And with this, we create purchases inside our ecosystem.

And before I give the floor to Salazar, during the first days of May, we are talking about 13 days of same-store sales. That is nothing relevant. We are going to break out the figures in a structured fashion. But we are excited because we saw a base of stores that were open. And despite the restriction of opening hours, and this is an additional challenge, we see same-store sales at 7% in stores during the first days of May.

So this is why we believe that, as stores will open, we will see growth, we will be able to sell products, which increases the gross margin, and we will go back to the pre-pandemic levels in terms of revenue. And of course, a higher revenue, higher than the 1Q.

Salazar, you can answer the second part of this question.

José Salazar:

Basically, it is the following. We generally negotiate the collections. There are four collections a year: Spring, Summer, Fall and Holiday. And we negotiate, and we prepare these collections and at what price we have to sell them in order to attain the desirable margin.

We do this nine months before. Just for you to have an idea, in March of 2021, we were starting the calculation proceeds of the sales volume for Holiday 2021. And during this moment, we realized what kind of demand we are going to have, and based on the expected demand, we also see the price of the USD, how much will it cost to buy this product in USD. So we price here the different products, and we provide the sales price to our partners. Everything is based on the USD perspective. This would be the future USD.

So what we basically do beforehand is to see the costs, or how much it cost to buy this collection based on the market demand. So we start to announce to Nike Inc. what will be our demand, and also, we already know at what price we have to sell to gain the margin based on the exchange rate of the market. And we do things nine months beforehand, and we have four collections a year.

Question (via webcast):

Now that the NWB acquisition has closed, what are your next steps? How are you going to engage with the e-commerce customer?

Answer:

Pedro Zemel:

Thank you for your question. This year, we have a number of priorities. We are evolving each one of the business units at Centauro, and the Internet is the preferred destination to buy sports goods. For Nike, it is to grow nike.com and to open a channel of direct sales through stores, so that we can grow in the direct channel to our consumer from here on, and to integrate, or to bring elements that can support and solidify our ecosystem, mainly through the ability to use our audience that we created in NWB, and to create some type of membership so that our customers come back more recently; CAC and we want to increase more frequency.

When we see the e-commerce consumer, and when we are talking about the omnichannel consumer, they have an LTV better than that from e-commerce, we have a CAC that grows in the industry, and we are maintaining this relatively low. But if you see a shorter period of time, like one year or more than this, it is based on the first purchase because there is low recurrence.

So here we have a major challenge of improving the e-commerce indexes, but to place elements that will drop the CAC. We have a proprietary channel of NWB to bring customers and to increase the recurrence, and to create articles, or to create partnerships to increase or to create advantages so that the consumer buys in other companies of the Group.

So these are a number of products, but these are new products, therefore, I want things to happen before I share all the ideas broadly.

Question (via webcast):

With the reopening of stores, have you seen a mix of sold products, or is it too early? In Centauro, is the gross margin going back to the historic levels, or are there things that will affect you for a longer period of time?

Answer:

Pedro Zemel:

Salazar, I will answer the first question, and you answer the second question. About the first question, Irma, there are oscillations because there are restrictions like soccer products, soccer shoes are suffering because we have less people playing soccer. Individual sports still are a highlight and collective sports are still suffering.

This is the main change that emerges. But we are closer to normality than one year ago. Last year, we sold a lot of home training equipment, but now things are going back to normal, of course, with the caveat of collective sports, because we have different profiles, and people that play soccer are suffering, and this is a business that is important for us.

José Salazar:

About the second question, I am going to extend my answer a bit and I am going to go back in time to give you context. And the answer is yes, we see that margins are going back to margins close to 2019, but there is a context.

This had already been observed since October last year, when we had a slowdown of the pandemic in September and we lived a "more normal" life in October and November, with open stores and things were working, or people were circulating more freely during this period. We saw margins recovering. So this was reassuring, because we saw people, things come back to normal, people go back to normal.

In December, before the Christmas period, until the 15th we also observed a gradual recovery of margins. Things were resuming month on month and the margins were improving in both channels. Then December came with the beginning of the third wave before Christmas, and we started seeing opening hours restrictions, and the movement of margin resumption was more restrictive.

But on the other side, during the second wave, we did not see what we saw in the first wave, that was a significant margin drop. In a certain way, everybody was prepared. Our inventories were not as high as in February before the first wave because people were optimistic. Nobody thought about a pandemic. And also, within this aspect, although we did not recover our margins, we did not record a significant drop vis-à-vis the last quarter.

And we changed a couple of things because, as the stores' operation resumed, we became more selective, and perhaps more intelligent in pricing, in markup. We focused the pricing on this aspect, the markup. We believe the people that were visiting the store were going to buy. If they left their house after a second wave, this person went to the store to buy. And we realized that we could be more conservative in the price marking. So we started to mark less.

And with this, our margins, mainly in brick and mortar stores, started to recover. The e-commerce margins are recovering slower because the market is more competitive, this is a market online, but we can also see the same margin recovery that we see in brick and mortar stores.

So the answer is, are we recovering our margins? Yes, but I wanted to give you a little background so that you could see what we did during this period.

And why this movement? When stores go back to the normal opening hours, and as we see that customers want to go to the stores to buy, and this is something that is going to happen, when stores go back to normal and e-commerce goes back to normal, we will see everything, everything reflected on e-commerce as well. Thank you very much.

Question (via webcast):

Regarding Nike, when do you expect the inventory to be consumed? And how much does the online represent of Nike's total?

Answer:

Pedro Zemel:

This consumption of inventory, this depends on the channel. There is a part of it, especially the part that isn't NFS, wholesale and online, that we finished this quarter and there's the other part that is NFS that will be expanded until the 3Q. And the third part that is online, we believe that we are in a

place where we doubled it. Even with the reopening of stores, we are reaching this point. So we are very happy. And we accelerated with the capacity of adding value with this acquisition.

Question (via webcast):

Regarding the sales of Centauro, can you give us your prospects for the future?

Answer:

Pedro Zemel:

Victor, we do not have a target here, or an objective. The growth of this number depends on the growth of Centauro, and it also depends on the growth of the Nike share in Centauro. We basically let the market resolve this. The Centauro team has their objectives, and they benefit themselves with the growth of Centauro, and they will buy Nike more or less, according to how this will benefit them. So we do not have an idea of how much they will buy.

Question (via webcast):

What about the remodeling plan for your G5 stores? Has there been a change because of the current situation?

Answer:

Pedro Zemel:

We continue doing this. We have not changed our plans. We continue remodeling stores. We have around 60-something stores following the G5 model, and what happened was that, due to movement restrictions and additional care with the circulation of people, we did not send teams, or IVMs, to cities where hospitals were overwhelmed.

And during this quarter, and I am going to ask Salazar to give you the figures, I cannot find these figures right now, I believe that Salazar has these figures and he can give them to you, but we have not changed our plans. In terms of cash. It was not necessary, but we replanned things because of the circumstances.

We are talking about 65 G5 stores, and it is important to say that these stores present good performance with a performance index that is better proportionally to the normal stores. It is better than what we expected. So we believe that this is an important avenue.

Question (via webcast):

Any restriction of Fisia in the marketplace?

Answer:

Pedro Zemel:

We believe that we have a number of avenues of growth and all channels can develop themselves. Our ambition here is to grow the Nike business in Brazil, and this is a possibility because we can work with products that have a margin that do not allow you to sell it wholesale.

There are players of the market that defined themselves and are as successful as a marketplace, and there is a growth priority in this channel. These are technology platforms, and they are not

necessarily interested in holding inventories. Of course, we can follow this model. Yes, there is an avenue of growth.

Pedro Zemel:

This basically concludes our Q&A session. These are all the questions that we received through our platform. So we will now bring to an end our Q&A session. Our IR team is at your disposal to clarify any questions that may emerge, or if by any chance we did not answer a question.

I would like to thank all of you for participating in our earnings results conference call, and to thank our team, our employees at SBF, everybody has been working strongly and has been totally dedicated to this bold mission, that is to build an ecosystem, and in the middle of a pandemic. The dedication of this team is moving.

We will pay attention to the short term, and we are prepared to react quickly, but without losing sight of the future in order to evolve our sports ecosystem. As we mentioned in our last call, our ecosystem is growing, and this is a challenge. We believe that in this quarter we placed an additional brick on the building of this ecosystem. We will continue with our investment and growth plan focused on delivering the best sport experience.

I hope that you continue following us. Thank you for your time, for your participation, and have a good morning.