Conference Call Transcript
3Q23 Assaí Earnings Results (ASAI3 BZ)
October 31st, 2023

Operator:

Good morning everyone and thank you for waiting, welcome to the third quarter earnings for Assaí Atacadista.

For those who need simultaneous translation we have this tool available on the platform, just click on the *interpretation* button through the globe icon at the bottom of the screen and choose your preferred language, Portuguese or English.

This earnings call is being recorded and will be available on the company's IR website at ri.assai.com.br where the release is currently available.

During the company´s presentation, all participants will have their microphones disabled, then we will start the questions and answers session.

For questions, click the #Q&A# icon at the bottom of your screen and type your #NAME#, #COMPANY#, and #LANGUAGE# to join the queue. When you are announced, a request to activate your mic will appear on the screen, then you must activate your microphone to begin asking your question. Please submit all your questions at once.

The information in this presentation and any statements made during the earnings call, regarding Assaí's business prospects, projections and operational and financial goals, represent beliefs and assumptions from the Company's Management, and are based on information currently available.

Future statements are not guarantees of performance. These involve risks, uncertainties and assumptions, since they refer to future events and, therefore, depend on circumstances that may or may not occur. Investors should understand that general economic conditions, market conditions and other operating factors may affect Assaí's future performance and lead to results that differ materially from those expressed in such future statements.
Now I will pass the floor to Gabrielle Helú, Director of Investor Relations at Assaí.

Gabrielle Helú

Good morning, everyone. Thank you for participating in our 3Q23 earnings call.

Belmiro Gomes, our CEO, Daniela Sabbag our CFO, Wlamir dos Anjos, our commercial and logistics VP and Anderson Castilho our Operations VP will participate in the presentation today.

As usual, I will pass the floor to Belmiro for his opening remarks.

Belmiro Gomes

Thank you, Gabi. Good morning everyone, good morning everyone, I also thank you for participating in our third quarter earnings call.

During the 3Q23, I think a great highlight that has been reported on the news and makes us very proud, was the fact that Assaí has become the food company with the greatest presence in Brazilian households.

Today, we reach 25% of Brazilian households, that is, 1 in every 4 households visits an Assaí store. This is due to the value proposition in our expansion plan, and the greater number of stores, but mainly due to the business model, and we will also talk a little later about the conversion projects, which allowed us to reach this important milestone.

And for a company that is in a very large expansion project, attracting new customers is what guarantees the assumptions for the project, and that it can, in fact, be achieved.

Other than that, we also had important recognition as the most admired Cash&Carry brand in Brazil, with an award granted by Estadão. Before starting the presentation, I would like to thank our customers for this recognition.

During the third quarter, we had a market scenario that was challenging, which we all know, but with numbers that are very positive in our view when it comes to sales evolution.

We reached a level of gross sales during the third quarter of R$ 18.5 billion, reaching a total level of more than R$ 70 billion in revenue in the past 12 months. As a result of our very strong expansion in the last 12 months, we opened 52 stores in the last 12 months and had more than 100 stores opened in the last 36 months.

Part of these store openings, as everyone knows, comes from the hypermarket conversion project, a project that required a series of adjustments within our business model. Within our value proposition, adding services, and changing the assortment and mix, which is something we were already developing in previous conversions or organic stores located in downtown regions.

So I wanted to thank our team, in all areas, our almost 80,000 people, for the numbers, and our results achieved within the third quarter.

During the third quarter, Assaí also experienced a corporate change with Casino exiting. Within the third quarter, we implemented the last change in the board of directors with the departure of the last member representing Casino, which was Philippe Alarcon, and Enéas Pestana joining. I would like to thank our board of directors for the support and the work we have been doing within this new phase in the company without a controller, as a True Corporation.

Operationally, the Company's performance remains very strong, we continue to advance with our expansion plan. During this third quarter, we entered another state in Brazil, Espírito Santo, with the store you see on the screen continuing the expansion plan in the company.

So about our revenue, in addition to the R$ 70 billion and the R$ 18.5 billion in revenues in the third quarter, this represents an evolution vs. the second quarter of more than R$ 1 billion. So obviously, we have a basis that it is complicated when compared to last year, when we started opening the extra conversions around August. So you have growth rates that will adjust over the period.

So we want to highlight the total growth rate vs. the previous year, but also look at the sequential growth rate, the evolution over the quarters in 2023. Within this third quarter, despite the very large number of stores, as we had announced an important achievement, the company reached the highest EBITDA margin in the year.

We are presenting the EBITDA margin with 2 views, despite the IFRS standards, we also believe that the pre-IRFS view provides a better perspective on the company's numbers.

So with that, in Q3 we are delivering an EBITDA margin that is 5.4% in the pre-IFRS view, which is exactly the same margin that was operated with in the previous year, before the beginning of this store opening process.

And when we consider the number of stores opened in the period, the pre-operational costs of many of these stores are still on a ramp-up, costs that we initially have until the stores are more productive, so in our view this is a positive number.

The same stores have a series of effects and one of the main ones is that we are experiencing a moment of deflation in food prices, some very important categories in the food market and perhaps even more important within our sector have had price deflations.

This is the case with soybean oil, with more than 20% deflation, meat with approximately 15% deflation compared to the previous year, milk and dairy products with more than 16% deflation compared to the previous year, as well as other important commodities, such as beans and some other categories.

Commodity fluctuations are normal in Brazil, and they are more related to agricultural factors and international external factors than actual demand issues.

But at the moment we have a deflation that is concentrated in several categories, because normally, the price increases and drops occur in one or two categories.

At this moment, however, we have at least five important categories experiencing deflation. This changes the dynamics of the business a little, especially among B2Bs, because when the price drops, they tend to be a little more cautious with volumes and the levels of stock they purchase. So this has an impact on our same stores.

Same stores are -0.9% and this is an impact as well, in addition to deflation and the significant price drops I mentioned, as well as group of stores that has a bit of cannibalization in the expansion project. With the almost 100 stores from the Extra conversions, at the moment when we closed the Extra stores, the entire market benefited from this group of stores closed.

So since the beginning of the project, we already expected that we would have cannibalization, either compared to our base in 21 or over 22, during the period when the Extra stores were closed.

And now as we reopen these Extra stores , there is an impact also with the same stores. This has an effect of approximately 2 p.p. when we compare the numbers of the same store base in this quarter of 2023 compared to 2022.

A great highlight this quarter is the expansion, which allowed the company to, despite the deflation with a negative product price factor, to have a R$ 3 billion increase in revenues compared to last year. We achieved 22% growth and this has been supported, as I said at the beginning by the increase in the number of tickets, the increase in the number of customers, there are 15 million more ticket during this third quarter compared to last year.

And when we consider the regularity of purchases that customers perform at cash & carry stores, this gives us an idea of how many new customers we have been able to attract within these new Assaí stores.

This is the result and it is what will make Assaí the company that is most present in Brazilian homes. And other points that I highlighted a bit earlier.

A positive point also in our view, despite this large number of stores from the Extra project which is still underway. We managed to maintain a very stable gross margin compared to last year, demonstrating that our business model, for food and especially Assaí's value proposition, is extremely resilient with a very strong level of stability.

Despite all of the movements, with the challenging economic scenario and the gigantic store openings cycle, we also reached this quarter with the highest EBITDA margin level of the year, with 7.1% and as I highlighted before, a stability of 5.4% in the pre-IFRS view, which is already comparable to the period before the conversions began.

About the Net Income, Dani will highlight this a little later, but obviously it has an impact on the levels of investments that the company has made and the cost of carrying this debt. So we ended the quarter with R$ 185 million.

And a highlight in our vision is our cash generation, historically Assaí grew by generating cash, we will talk about this a bit on the other slide ahead. Cash generation reached R$ 4.9 billion in the last 12 months, with most of our large investments made towards our growth. Supported by this strong cash generation, which is part of our Assaí tradition.

Dani will provide a better view on our debt, but when we look at our current debt, most of it still comes from the spin-off process with GPA.

And the highlight of the operating cash generation is that the company is perhaps carrying out one of the largest projects in the history of the Brazilian food sector, with the acquisition of the Extra store locations. This, along with our organic expansion, is part of the growth and expansion that the company has been demonstrating to the market.

So, when we look at a period, we are sharing a vision from the end of 2020 until the end of the third quarter now. At the end of 2020, we had a company with R$ 39 billion in revenue and 184 operating stores, at the end of September 23, we have a company with R$ 70 billion in revenues.

And R$ 70 billion is not yet stabilized because there are several of the benefits of opening stores, with other conversions and the ramp-up process that will still be captured.

But during this period, the company was able to go from R$ 39 to R$ 70 billion, which is an addition of R$ 31 billion in revenue and this added revenue, would already represent the revenue of the third largest player in the Brazilian food market most likely.

We had to make investments, but cash generation is our strong lever, as we generated R$ 9.4 billion reais during this period.

This supported the investment in store conversions, organic expansion of R$ 6.8 billion, part of the payments for the acquisition of the Extra locations, R$ 2.7 billion, our maintenance capex, it is a relatively stable capex with R$ 80 million invested during this period, which not only includes store maintenance, but also some new areas, and the expansion of some existing stores.

The Company distributed R$ 400 million as dividends in the period, but had a debt cost that is obviously above what we expected, especially when the hypermarket acquisition project was carried out.

There was another expectation in relation to Selic, but even so, with this R$ 3.3 billion, we had a variation in cash flow during this period of R$ 4.6, however, the R$ 9.4 were able to support most of the investments that the company made during this period.

Within the investments for the expansion, which already came from the organic stores, let's remember that Assaí is a company that only had 14 stores, when GPA bought it in 2008 / 2010. So the company has been generating cash and growing.

There was a need to make a stronger movement in our vision, which was the acquisition of the hypermarkets and we are not simply taking the same model to a new region, but also about modifying the wholesale model. Which is currently the channel with the highest penetration in Brazilian households.

Cash & Carry as a sector currently has one of the highest sales volumes, and our objective is to always innovate and differentiate ourselves. So I think the hypermarket conversion project is also not only about building more of the same stuff.

We had already developed this model before, with some new organic stores, and other conversions, that would allow us to enter the central regions of the cities, the model that would also allow us to service another level of income, a model that would provide a faster supply option for B2B customers , especially in the foodservice.

We all understand the logistical challenges in large Brazilian cities, and the high costs that makes it difficult for the industry to perform door-to-door deliveries. And to enter the central regions, the best solution we found was to buy these locations from hypermarkets, so this is the project that increased the company's leverage.

When it comes to execution, in our view, it is the most challenging project ever in the history of the Brazilian food sector, converting hypermarkets to the wholesale format.

But I believe that we also have at this moment, when performing this project and with everyone involved, witnessed a change in behaviors and in approach towards supplying the Brazilian population and businesses.

So we understand the importance of the project, and it is on a maturity curve. We had initially highlighted among our base of shareholders and potential investors, analysts, that the company's expectation was to triple the sales volume.

This multiple of sales has now reached 2.7x within that third quarter, even with some stores still averaging 10 months of operation. So we still have a maturity ramp-up, which is adjusted for each market and store by store.

Today these stores already deliver a gross revenue that is 13% above the average history of the company.

And when we look at the 47, the first batch of stores that were opened in 2022, the EBITDA margin in the pre-IRFS view, already delivers a historical level, that is, the same general level as the company. The 5.4% level still has a ramp-up to capture.

Because in the EBITDA pre IFRS, these stores have a different lease dynamic, than we had in the organic park where we mostly were prospecting, finding and building new units. In the post-IFRS view, the margin in the third quarter already exceeds 7%. So this shows that we are on the right path, it shows that the customer, especially, has visited, bought and returned.

Before the return on capital, which is what we need to deliver with the project. I need to ensure that our customer accepts the value proposition, likes the value proposition and returns to one of Assaí's stores.

Here we are bringing the 2 views of the EBITDA vision before and after IFRS, because it had this dynamic when considering lease levels, but in our view the 2 EBITDA margins, whether the lease is affected or not, show how much evolution the company has had even at a stage with many stores still reaching maturity, despite the pre-operational costs.

The adjusted EBITDA in the pre-IRFS 16 view, is totally stable compared to last year, but obviously it is not what it would be in a mature store network, because there are still many stores, whether organic stores or conversions, which still require a maintenance phase.

I would also like to highlight our discipline with expenses, because we have deflation, that is, the topline, for the same volumes, has a negative price effect, but many of the expense lines still follow the inflationary curve, with payroll, collective labor agreements, or a series of other expenses, with great discipline among the team to be able to maintain the EBITDA levels.

And I would like to thank you for the efforts with our operational areas because we have been tightly controlling the expense levels, keeping the operating costs low so that we can deliver the level of EBITDA presented.

And within the third quarter, I think that both in the pre and post views, numbers are a bit below what we expected, but considering the market context, and the number of stores, in our view we have had positive evolution.

And now I will pass the floor on to Dani, as we made some changes, and you must have seen in the release that we provide better visibility now regarding the company's obligations towards debt adjustments.

And during this transition, with the company no longer being a subsidiary of the controller, but a true Corporation. Dani, the floor is yours.

Daniela Sabbag

Thank you, Belmiro. Good morning everyone. So let's talk a little bit now about the financial results for the quarter. So, we achieved R$ 737 million, which is an important increase here, 67% impacting the company's earnings and an increase of almost R$ 300 million.

When we focus here on this blue part of this bar, that is, to address the financial expenses arising from the cost of our net debt. We have a level of R$ 506 million here, an increase of 61% compared to the previous year and this represents 3% of our net sales, which is an important level.

This result for the period was obviously impacted by high interest rates, but mainly due to a higher volume of debt. Because we have almost R$ 2 billion in additional gross debt here, compared to the previous year and also due to the expansion and funding that we carried out.

During the second quarter, we mentioned we issued a R$ 1 billion instrument, we had already announced this in the second quarter, but we completed the R$ 1.1 billion in funds raised, with a CDI cost plus 1.26%, which is lower than the average cost of the company.

And also during this quarter, there is an accounting effect, that I think is worth mentioning with the reduction in capitalized interest. So, during this quarter, this effect was only R$ 53 million, since last year this impact was R$ 247 million.

So obviously, this is linked to the progress with the expansion project, which is now in its final phase, and these values have been decreasing more and more.

Moving on to the second part of the slide, as we are talking about cash generation, Belmiro has already shared this highlight, but in the last 12 months, the company's operating cash generation reached almost R$ 5 billion. So it is a very relevant growth of R$ 1.7 bi year over year, which comes from this higher EBITDA in the company in the pre IFRS16 view, of course, as it grows more than R$ 363 million.

And also one of the best periods when it comes to working capital management, which had a 9 day improvement here, year over year. This strong operating cash generation looking here, was essential to support this intense level of investments, when adding the capex and the payments for Extra stores.

We have a total R$ 4.7 billion here, so these R$ 5 billion practically pay for the level of investments and, on the other hand, they have a negative effect on the interest level, which increased the cost of our net debt.

So the variation here in the net debt, going from R$ 7.3 billion to 8.6 billion is basically this effect of the interest, which did not negatively affect the debt. Thus, in the concept that we always disclose to you here, we reached 2.7x the EBITDA, in a high investment context as we highlighted here.

And during this quarter we are sharing a new concept, adding the receivables and the balance payable from the acquisition of the supermarkets, and we reach 4.4x the EBITDA. And then I will go through a reduction.

Before going through the next slide, where I will share a bit of the transition from one concept to the other.

The highlight here is the reduction of this 4.4x EBITDA, which in the previous year was 0.2x with a higher EBITDA. So we can move on to the next slide Gabi.

And here we bring this view of our leverage as you are used to seeing it presented with the R$ 8.6 billion.

We return the undiscounted receivables and add them here, with the total receivables and the balance payable from the acquisitions of the hypermarkets. So with this concept, as I mentioned before, we reach 4.4x the EBITDA and this reduction is already compared to the previous year, of 0.2x.

For the next slide, we provide a view of our leverage, the history, in fact, of this leverage, so, with this concept, on the gray line, we can share this as we have always presented it to you, and when we look here, eliminating the seasonality in the 4Q22, we have a level that has been very similar since the 2Q22.

The fourth quarter obviously has this seasonality, but the other quarters end up being very similar. And then in the 3Q23, this 4.4x is quite comparable to the 4.67x in the 3Q22.

I think we should also mention the completion of the conversion project. Here we also have an increasing cash generation, we have already highlighted that the cash generation grew 54%, representing R$ 1.7 billion.

And this is what will give us the necessary speed to continue deleveraging the company, even at a higher speed than this drop of 0.2x that we have observed here in the last 12 months.

So it is logical that along with this, there is the lowest cost of debt resulting from interest. And all this leads to this greater deleveraging trend that will happen for the company in the coming quarters.

I think these are the main highlights on this slide. And now I will pass the floor back to Belmiro, for his comments on our net income and the last few slides.

Belmiro Gomes

Net income has obviously been impacted by the cost of carrying our debt, in the project, but in our view, I think the project was decisive, as much as it has its impacts now at that moment. We are building a company, including our value proposition, customers, scope, and the company has been presenting very strong growth levels.

So within the quarter, the big impact is not coming from the operating performance, as is still reflects the high interest rates and the higher levels of debt than what we had estimated when we began the project. But it mainly shows the resilience of the model, capable of supporting these levels of investments, despite the interest rates and a deflationary scenario, as well as the purchase environment with consumers still taking on a cautious approach.

The company delivers a positive net result, and within this third quarter we have an impact of a renegotiation we had to make, due to the controller´s exit.

There were 2 relevant themes, and they are the only points as we no longer have any forward pending items related to the exit of the controlling shareholder of the company. Many stores required new contracts, since there was a clause that provided for the termination of these contracts if the controller exited the business.

And also a marginal impact within this third quarter, just as occurred in the second quarter with a ***waiver*** alongside the financial institutions provided for in loan agreements in case the controller exited the business.

About the net income, I think as we look at it now, considering that the conversion project is a project that has a beginning, middle and an end. The project is now approaching its final phase, we still have 2 relevant payments, one now in the fourth quarter and another in the first quarter of 24, related to the Extra acquisitions.

But the company still has a relevant number of stores, today we just opened our 60th Extra store, a conversion at the Boulevard in Rio de Janeiro.

And in October we opened the Foz do Iguaçu store, which was organic, as well as a new store in São Luís do Maranhão, one in Fortaleza in Ceará, and now we are reaching 19 stores opened during this year.

There is still a big challenge and within the fourth quarter, we even have some expenses on our administrative line, which also reflects the opening preparation for 11 or 12 more units that we should be opening during the fourth quarter.

And this will be the completion of the hypermarket conversion project and from then on, the company will obviously count on cash generation, either from the current store network, or with the growing cash generation from these new units.

Which is combined with the expectation regarding the interest rate and most likely a readjustment of the investment levels, allowing us to deleverage and return to the levels, from the point of view of our net income, that the company had previously.

I think this is it from an operational point of view. And now I wanted to move on to the next slide, where I will share some advances in ESG.

Assaí is a great reference for investors, and I recommend you schedule a meeting with our sustainability department and IR, as I think it is worth understanding the main advances that the company has achieved with this topic.

Within the third quarter, the company is the only player in food retail that has the B3 indicator, IDiversa, with more than 25% of women in leadership positions and 43% of our leadership positions and managers occupied by black people.

This requires constant work, it is a journey that is unending from an inclusion perspective, but the company is proud to be promoting it daily within our pillar of social responsibility, as the company has the largest presence in Brazilian households with the diversity within our store network, encompassing employees and customers, fulfilling our social responsibility.

There are a number of ESG highlights as well, but I think there are two advances in the Assaí institute I want to highlight.

During the third quarter, we launched the Sport Cidadania program, which we began through the institute and especially the Mais Escola Card we began operating with in Santarém, in the Amazon region.

Now, within the third quarter, it will benefit more than 2,000 families, within the Amazon and other socially vulnerable regions in Brazil with financial resources for food.

We also had an important advance, when it comes to waste, with the gold seal in the public registry for emissions in the Brazilian program and a reduction in scope 1 and 2 emissions versus the third quarter.

But for those of you who are listening to us and want to know a little more about ESG and its broad scope, you should read our sustainability report and learn about how the company's actions impacted this pillar of social responsibility.

So I finished my presentation and want to call Gabi so we can move on to questions and answers. Thank you so much.

Gabrielle Helú

Thank you, Belmiro. We can move on to the #Q&A# and continue with the question queue.

Operator

Now we will start the Q&A session, remembering that to ask questions you must click on the #Q&A# icon at the bottom of the screen and write your #NAME#, #COMPANY# and #LANGUAGE# to enter the queue.

When you are announced, a request to activate your mic will appear on the screen, then you must activate your microphone to begin asking your question. We kindly request that your questions be submitted at once.

Our first uestion is from Danniela Eiger Sell Side analyst from XP.
Danni we will enable your audio, so you can proceed.

Please proceed Danni.

Danniela Eiger – XP

Good morning, Belmiro, Dani, Gabi, thank you for taking my question.
I have two. The first one is from a perspective angle, mixing a bit of the short and medium term.

I would like you to give us some color on the dynamics of the evolution of the same stores or volume, in October, and if the trend you saw throughout the third quarter remained.

I think it would be nice to understand if this can already show an inflection on the consumer side with this issue of purchasing power, considering the deflation that has been pressuring the earnings for some time.

And also on the issue of lease renegotiations, how we can think of this regarding an impact on the profitability of the company as a whole.

Because we only have 28 stores, from what I understand, it's 10 to 20 beeps only of pressure over time, so do you estimate a slightly more relevant impact on the company as a whole?

And the second point is that you mentioned deleveraging, and the expectation of this accelerating after the first quarter, but you also mentioned the readjustments in the level of investments.

I think it would be nice if you can share if you already have some kind of discussion in this regard, and what would that be, in regards to opening stores.

You even mentioned the stores under construction, which I think are already planned for 2024. But we would like to understand what this readjustment would be.

And also other possible levers that you see if a scenario of dropping interest rates proves to be a little more gradual than I think we could be imagining because of other dynamics in the macro scenario. These are my points. Thank you.

Belmiro Gomes

Thank you, Dani. I think I will follow the order you mentioned.

I think September was a very positive month, I think during September mainly we had Assaí's 49th anniversary campaign, Regina Casé has been our brand representative, causing strong adhesion.

But what we have seen so far in October is the same levels in relation to the third quarter.

You realize that there is no dynamic change, considering you have greater price stability now, but if there is the same level of caution as B2Bs, when it comes to the purchase volume and the consumption patterns.

So at least what we saw so far in October is very similar to what we saw in the third quarter.

Obviously, there is an expectation that it will be more positive in November and December, during the end of the year period.

During the last end of the year, mainly, we still had impacts from the pandemic that affected some purchases. So, there is an expectation that is perhaps a bit more positive for December.

But we prefer to be a little more cautious.

For now, what we have seen is the consumer maintaining their level of purchases, and B2Bs are also cautious because they are also under pressure in terms of working capital, so we have seen a dynamic that is similar to the third quarter.

The leases from Peninsula were negotiated, and the impact on leases is for this group of 28 stores.

Obviously, when we look at these stores, they are very relevant, but when we look at everything about the company, the impact ends up being very marginal, it has an impact, obviously, but this 10 to 20 bps will drop, maybe to 0.02bps or something like this.

So it ends up not being relevant when you look at the company's numbers overall ahead.

Investments have a drop that will already be normal and natural, because we are finishing the largest project in the company with the hypermarket conversions.

And then we will more back to the organic projects, some stores for 24 are already under construction yes. Throughout the fourth quarter, we should review this better to confirm the number of investments for 2024.

But there is also a focus in the company on deleveraging, to be able to reduce debt if the interest rate remains high. But I think that even though the interests may remain at higher levels, there is a highlight here.

Which is Assaí's solid cash generation capacity, whether it is the store network cash generation capacity, among legacy stores, or also how much these new stores contribute with, and the EBITDA in the pre-IFRS vision.

Then, if you look at our history, our EBITDA conversion rate into cash is 100%, we have always been able to convert most of our EBITDA into cash.

If you look at our balance of recoverable taxes, it is dropping when we consider the sales volumes.

So these new stores also come along with cash generation and this cash generation above all, is the fortress that will allow us to deleverage the company.

Danni, I hope I have answered your questions.

Danniela Eiger

You answered them Belmiro, thank you.

Operator

Moving on, the next question is from Maria Clara Infatozzi Sell Side analyst at Itaú. We will enable your audio so you can proceed.

You can proceed, please, Maria.

Maria Clara Infantozzi – Itaú

Hi, Belmiro. Hi guys, thanks for taking my question.

Here from Itaú, we wanted to understand a little about the prospects for revenue growth in 2024.

On the one hand, food deflation should persist even in the first half of the year, the competitive environment is a little more difficult, but on the other hand, conversions are doing very well, ramp-up is evolving quarter by quarter from *the* sales uplift.

And I wanted to understand how we can think about the productivity *build-up* versus the area expansion next year, and with this we can also cover the issue of the organic expansion.

Can you also cover bit of which would be the main locations you plan to enter, after this opening in Espirito Santo for example. Thanks.

Belmiro Gomes

Thank you, Maria Clara.

When it comes to our organic expansion, as we said, there are already some stores that are under construction now to be opened in 2024, during the fourth quarter, and soon we will have a definition of the expansion stores for next year.

There are some regions and some of these stores that are under construction, are in areas where we are already present, among all regions.

We have work taking place in the northern region in several northeastern states, in the Southeast where we just opened a store in Foz do Iguaçu for example, so there is no target region we will concentrate on.

Even in regions where Assaí is already present, there are several cities, I will mention for example, Rio de Janeiro, where Assaí has one of the largest market shares I believe. We are building Angra dos Reis now at this moment, which is a very important city and we do not have any stores yet in the region.

And in São Paulo state we also have São José do Rio Preto, with a store under construction, so we also aim to complement and enter relevant cities that have 300 / 400 thousand inhabitants, and there are not Assai stores yet.

When it comes to revenue in 24, obviously it will depend a lot on how many organic stores we can build in 24.

I think about the deflation scenario and prices, Wlamir you can go deeper about if you believe prices are going to continue to drop or if we are already on a plateau; so you can talk about the issue of the deflationary part.

Wlamir dos Anjos

Hi Maria Clara. Good morning, everyone.

I think about the inflation issue, our expectation, in fact, when we look at commodities actually there is an issue.

These price fluctuations, in fact, we had the perfect combination that happened now, in this last quarter, and at the same time several commodities had price drops.

We do not imagine that this will happen with a price reduction forward, but it is very volatile because now we have the exchange rate situation, as well as the situation with the war itself, with the impact on the price of oil.

So there are other factors. So it is difficult to predict what will happen, but we have monitored this over the quarters and months, and there is a normalization in the average price.

When you look at the basket as a whole, you have pressures, for example with soybeans rising or dropping 29%, on the other hand, you have sugar rising a little, so there is a certain balance.

So we do not see much room even for large increases, or greater reductions in the price of commodities. On the other hand, we have an impact on the rest of the assortment.

So other than dairy, for the basic commodities there is a little inflation in the products, but we do see more stability in the average selling price from now on, and maybe there may even be something related to the war.

With what is occurring in Ukraine and in the Middle East that may impact commodity prices, but it is very uncertain. It's hard to predict anything.

In relation to inflation, its very complex. We imagined that at this time in the year we would no longer have the impact of deflation, we expected deflation in the first half of the year, but it occurred in the second half of this year.

We imagine price stability going forward.

Maria Clara Infantozzi

Perfect. Thank you.

I just wanted to take advantage and follow up to make sure we got the right message.
Belmiro, it is clear that the guidance for the expansion for 2024 is not yet confirmed, but today how many openings are you considering for this year.

Belmiro Gomes

For 2023, around 30 stores and for 24, we will wait for the fourth quarter, there are already approximately 7 that are under construction, but we will wait for the fourth quarter. Of course opening an organic store requires prior notice, especially in regards to approvals.

The Company has a relevant number of projects to continue expanding, but we will have a balance between deleveraging and the number of stores will have to wait until the fourth quarter so we can provide a definite number, Maria.

Maria Clara Infantozzi

Thanks. Thank you.

Operator

Moving on, the next question is from Vinícius Strano, Sell Side analyst at UBS.

Vinicius we will enable your audio so you can proceed. Please proceed, Vinicius.

Vinicius Strano - UBS

Good morning everyone. Thank you for taking my question here.
On working capital dynamics, if you can mention what you see as levers here to improve forward working capital.

And what would be a more normalized deadline for inventories and suppliers. I think that would be great.

And a second question too, if you can discuss the mix between b2C and B2B customers in the Extra stores converted. How would you see this mix evolving forward?

And also about the converted stores, if you can add a little color to the gross margin of this network of 47 stores that you mentioned. Thank you.

Belmiro Gomes

Thank you, Vinicius.

I think I'll go backwards, talk about the conversions and I'll let Wlamir talk about the working capital part, inventory levels, supplier level, and the expectation going forward.

The converted ones, they work with a higher gross margin, this was expected and we highlighted this at the beginning of the project, since you have a product mix there and differentiated purchasing power and they are ramping up, but they work with a higher margin level than the other stores.

There is a greater B2C share still within these stores, but they are stores that are still on a ramp, we think we still intend to move forward with them for a while to see the stabilization levels for some stores,.

And then there are unique aspects, and this network is not homogeneous, you have some stores that are in regions that we already knew since the beginning of of the project would have more adherence.

Especially for the food service customer, B2B food service and also the utilizers, as they now have a store close by to supply their needs.

We know how much more expensive it has become, and more complex to perform door-to-door distribution, I think it's even worth looking at, you must be following the changes in transportation laws underway in Brazil, at this moment that will make it even more expensive from a logistics point of view, with the new driver law.

This will make door-to-door distribution even more difficult, for industry or wholesale deliveries, especially in large centers. With changes in the rules.

This has made this store model become a quick supply point, for this b2b customer, because he has no minimum order, he can buy the quantity he needs, he has access to a variety of brands and quality and products, especially with the perishable goods.

Which allows us to have strong adhesion from this kind of client.

But they do have and we expected a greater share if end costumers and there is some ramp-up work that we have done, to attract B2Cs and B2Bs.

And I will pass the floor to Wlamir, so he can answer the working capital part.

Wlamir dos Anjos

Hi, Vinícius.

Regarding working capital, if you notice in our release, during the third and fourth quarters last year, we were operating with 8 / 9 more days of inventory, given the number of stores, and inventory information.

As we balanced this now it is a lot lower than in the passed.

If you look at it historically, we reduced between 8 / 9 days in our working capital, and our stock, let's say. And it has been kept at around 44 / 45.

This is a trend going forward, so we can keep stock levels and term negotiations, and they occur monthly and on a quarterly basis with the supplier.

For us to maintain a very healthy relationship and a lot of discipline in our working capital. We understand that as we invest in our expansion, we need to have a lot of discipline.

So you should not see big swings going forward, either in stock levels or in supplier term increase levels, we should keep the trend you have seen in these first 3 quarters of the year. This should be extended.

Obviously, now, in the fourth quarter, there is an increase in inventory levels for seasonal reasons, anyway, but there is a normalization and disclosure of the days that we must keep quarterly without much variation.

I think the team has been able to work in the commercial area, as well as logistics and operations with very strict discipline in inventory levels, not harming sales.

The levels of rupture are within a normal range we expect for the company, I think the stock issue is pretty peaceful at Assaí. I don't know if I answered your question.

Vinicius Strano

Great. Thank you, Wlamir. Thank you, Belmiro.

Operator

Moving on, the next question is from Joseph Jordano, Sell Side analyst at JP Morgan. Joseph we will enable your audio so you can proceed.

Please proceed, Joseph.

Joseph Jordano – JP Morgan

Hello, good morning everyone. Good morning Belmiro, Dani, Wlamir, team. Thank you for taking my question.

I wanted to explore this capex issue a little bit, in order to deleverage the company, with what would be the capex level for these new 30 stores.

I know it is still a guidance that is not so strong with these 30 stores that can be reviewed, but what would be the level of capex that the company believes is reasonable for 2024.

And then going back a little on this working capital journey, I wanted to explore what we can do to improve this a little still. Thank you,

Belmiro Gomes

Thank you, Joseph.

I think there may be an misinterpretation even. When we talked about the 30 stores, we are talking about the 30 in 2023, which includes conversions and organic stores.

For 2024, we have 7 stores under construction and now during the fourth quarter, we will define the amount of stores. And the volume of capex that we must consider as a consequence.

But for 24 it would not be 30 stores, we were previously working with a maximum of up to 20 units. 25 units, but now, throughout the fourth quarter, it will be reviewed.

When we talk about the 30, these are from 2023, there are 7 already in 2024 that are already under construction at the moment, mainly from distant regions such as Manaus and Macapá. The second store in Macapá, which is already under construction at the moment, Manaus, which is under construction at the moment.

But the total even for 24 will be defined throughout the fourth quarter, looking at the expansion, and the locations with the best returns, but also taking into account the company's leverage level.

And from a working capital point of view, I think Wlamir mentioned this a but during the last one. We've already made improvements.

Obviously, we are always looking for improvements in our working capital, opportunities, inventory turnover, and increases in supplier terms, but at this moment we are considering stability, so to speak, in the working capital, at the levels that we saw within the third quarter.

Wlamir dos Anjos

If I can add to this, Belmiro. I think it's important, because we have a concern, Joseph.

Of course trying to have longer terms with supplier, can interfere with competitiveness and reduce the inventory level a little more and can harm the sales with disruption.

So I think we found a balance, a nice stock / term ratio, and I think if we can keep this, the company will be in a very healthy condition going forward.

So, I think it's more about maintenance than gains. Obviously, we will work to improve the terms, in short, the days of stock, but I think we are at a very healthy level.

Joseph Jordano

Perfect, thank you very much.

Operator

The next question is from Eric Huang, Sell Side analyst at Santander.
Eric we will enable your audio, so you can proceed. Please Eric, you can proceed.

Eric Huang – Santander

Good morning everybody, Thank you for taking our questions. Here on our side, I think there are two more pretty much on the same topics.

You mentioned how you have entered the state of Espirito Santo, so I think I would like to understand how receptivity has been in the state, as well as the competitive environment.

And we could even consider a future potential expansion with more stores there, how can you imagine this environment?

And on the other hand, looking at these organic expansions, we want to understand what we can expect regarding the sales level for these stores.

Will this be more aligned with what we had in the legacy stores, a little more aligned maybe with the expansions, I think I am trying to understand a little more about the economics of these organic expansion stores. Thank you.

Belmiro Gomes

Thank you, Eric .

Well, Espírito Santo we should have already entered, we opened the first store in Serra, I'll pass the floor to Anderson to discuss our arrival at Serra and what we are already doing there in Espírito Santo.

And then I will come back to talk a little bit about the sales level.

Anderson Castilho

Thank you, Belmiro. Eric, good morning.

I think Espírito Santo was very positive, we really were anxious with the community there, the client welcomes us there very, very well.

I think that the value proposition is in relation to our store services and we are very careful about our mix as well. We always talk a lot about this issue of regionality.

To give you an idea, we started a store there with more or less 1,500 new SKUs, looking at the regional characteristics.

So we want to arrive in a region and deliver a differentiated value proposition, through our customer services and especially with regional products. So I think that was very positive.

The store has been a great success, and we are already inside this organic process for next year, and we have another store there in Vitória. And we are starting the construction work there.

So this should also strengthen the brand a lot more, so I think that as we are looking at the Serra store it's really fantastic, we really got it right with our opening there and the market noticed Assaí´s strong arrival.

We are no longer Assaí from far away in Rio de Janeiro but an Assaí that is in Espírito Santo, strong, with a second store now in Vitória, and this strengthens us even more.

And, mainly, with this regionalized approach. I think this was the main thing, having the local brands, having the local culture, the local team, I think this differentiated us, our caution and care, especially with our people close.

I think it's been a really great job that we've been doing with the team Eric. I think it's really positive. I think that would be it about Vitória.

Belmiro Gomes

So there is a complement to Eric's question, which I think is what is expected from the revenue of the organic stores, obviously much more linked to the legacy stores.

Obviously, you can't talk about all the stores, there are also some organic projects within central regions, which are analogous to be honest and even the conversion stores.

So we have, for example, a conversion spot which was an old Makro store in Vila Maria as well, with very high expectations here in the northern region of São Paulo and some other organic stores.

But in general, organic stores, due to their nature, should have more revenue than the legacy stores with one or another more exceptional store, whether we are buying locations within central regions that may have a higher level of revenue there.

Eric Huang

Perfect and thanks for the answers. Thank you.

Operator

The next question from Alexandre Namioka, Sell Side analyst at Morgan Stanley. Alexandre we will enable your audio, so you can proceed.

Please Alexandre, you can proceed.

Alexandre Namioka – Morgan Stanley

Good morning everyone, thank you for taking our question.

Going back to his point, actually about the openings, and looking a little more long-term.

I would like to understand how you see the expansion in terms of stores and markets, where there are no longer cash&carry formats, not necessarily with the Assaí brand, versus places where you already operate. At least with one store, at a city level. I think that would be interesting. Thank you.

Belmiro Gomes

Thank you, Alexandre.

Well actually there is no place today in Brazil that does not have a cash & carry store, so there is already some level of competitive activity, which is high.

Today there are many players operating within the Brazilian sector, in expansion projects, and there are important regions such as São José, Rio Preto or Angra dos Reis.

Among these two examples, which are in the States of São Paulo and Rio de Janeiro, we still do not even have a store in these two important cities.

As I mentioned the example from Foz do Iguaçu, which we opened last week in the southern region, even though we already had a store in Paraná, it was very far away, the store closest was Maringá, approximately 400 km away.

So we still have a large number of relevant cities, with 200 / 300 thousand inhabitants that we don't even have a store in, or for example, with cities that have 600 / 700 thousand inhabitants and we only have one store still.

So, within this pipeline of organic stores, we have been looking at the cost of implementation, and the returns on investment, defining which are the priority projects.

So it is difficult to define what and which regions this will take place in.

As well as the new store networks but openings are pretty much spread around all regions in Brazil.

There is an obviously greater focus on establishing our operations in states where we are operating but still have large cities that we are not present in yet, such as the São José and Angra examples I gave and I think maybe this would be a good focus.

I hope I answered you there Alexandre.

Alexandre Namioka

Perfect, thank you very much.

Operator

Our next question is from Irma Sgarz, Sell Side analyst at Goldman Sachs. Irma, we'll enable your audio so you can proceed.

Please go ahead.

Irma Sgarz – Goldman Sachs

Good morning: I just wanted to ask you a question which is in line with the question from Joseph, about capex in theory, I understand that there are only 7 stores that you have under construction and there will still be maybe a more specific definition about the plan for organic openings.

But what level of capex should we think about even just for those 7 stores? I understand that this is a small and specific store network and maybe there are a few points that deviate.

But I would like to get an overall view and the reason for the question is because of the strong inflation in the cost of stores in recent years, due to several external factors, and then I think it is important to keep investors on the same page regarding this.

And the other question is on the logistics side, if you think you have all the DC structure for the logistics network today, which you need to continue supporting this next wave of growth?

Do you have some projects that you are looking forward to, in the next few years, maybe specifically for 2024, but over the next 2 / 3 years.

Belmiro Gomes

Okay, I'll move on to Wlamir to answer the logistics part and come back to talk about capex.

Wlamir dos Anjos

Hi Irma, good morning.

Speaking about logistics, in fact, if we look at 21 / 22, given this expansion movement that we had, with the acquisition of the hypermarket stores, we have already prepared our logistics.

We made investments in Pernambuco, São Paulo, Rio de Janeiro, and Pará. In the last 2 years, what we do with the logistics is as our operation grows, we adapt our structure.

Today, for you to have an idea, we have a model where stores operate as a Mini CD. In fact, we have stores that operate 100%, receiving directly from the supplier.

This I think is a big advantage of the model, because unlike retail operations or other super or hyper operations, you rely on logistics to be able to operate.

In our format, we can open a store in any region of the country without depending on logistics. Obviously, as we grow, we invest.

We have some things that we are looking at in the midwest region, but we are still studying possibilities and we have nothing defined, but as the operation grows, we are investing in it.

The investment is very low, the capex is very low, because we do not build, basically, we rent DCs, and we do not invest equity in our logistics operation.

But we look at the operation as it grows and we structure it, but for 2024, we should have some investment in the Midwest region as we grew a lot there and we did not make a movement.

We have a small DC in Goiania and maybe we will expand in that region, but there is still nothing defined.

We are working on studies, just as we have not yet defined the number of stores, we have not defined an investment for logistics in 24 and 25, but we will have this definition soon.

But the logistics grow as the operation grows, and to give you an idea, what makes us very comfortable is the fact that we can grow and open a store in any region of the country, without depending on the logistics structure. This is a great strength in our business.

So, I hope I have covered your question,

Irma Sgarz

Great, thank you, very clear.

Belmiro Gomes

About Capex, there was an inflation of construction work especially at its peak last year, and maybe the first half of this year.

What we have seen is that some construction materials, especially cement and steel, remain at high levels, but there is a drop.

Today when you look at the cost per square meter of an organic store in relation to last year, there has been a drop of approximately 8%, compared to what it would have been in the same period last year.

So it is not that prices are cheap to work on, they have gone up a lot, as well as the food products during the pandemic period, but there is a normalization.

In these 7 that are in progress, there will be a maximum 450 / 500 million reais invested, which is obviously not all the capex for 2024.

Even then we will have to add maintenance costs, there is also an expansion in the services we are providing, and there is a carry-over from this year's stores, which will probably drop in 2024.

So as soon as we have the number of stores in the fourth quarter, we should still signal the level of investment that the company will make in 2024.

Irma Sgarz

Got it, thank you.

Operator

Our next question is from João Soares, Sell Side analyst at Citi. We will now enable your audio, so you can proceed.

Please, João, you can proceed.

João Soares - Citibank

Thank you. Good afternoon guys, two quick ones here from my side.

Belmiro, I feel you are a little more cautious now for next year's openings, I may be wrong here in my interpretation, but if I´m right then... What may be preventing you from nailing this or having a slightly clearer view here of the openings during next year? This here is related, maybe to some balance constraint, or the process is a little more difficult now and mapping out the openings is a little more difficult.

Anyway, if I'm right, which could be maybe hindering your visibility a little bit. And the second point is quick, just when we look at SG&A, I think there has been a very interesting level of control, in the last quarter it dropped 8% year over year, and this quarter it is flat.

Can we imagine a number here of about 200 million, annualized as a sustainable level, looking at the SG&A forward? Thank you.

Belmiro Gomes

Thank you, João. Going backwards.

I think that about SG&A we have been able to keep it disciplined, on the operational part there has also been the impact of having the conversions.

In the administrative area there is a drop when looking at the percentage of sales, not in absolute volumes, but mainly with the exit of the controller, board costs, and cost-sharing.

You can't nail it, and say this number is forever, the company always needs to be looking at new areas or projects etc. But there is a dilution of the administrative costs expected, which I think is the most relevant point. Because, as we grow, the administrative costs will not keep up with the expected sales growth rate.

For 24, we are more cautious because we will define it within the fourth quarter now, since the company is also operating as a true Corporation, and obviously, we are a little more cautious about how we disclose information with greater precision.

So the fact is that we do not have this decision made, so we actually have projects, this time what we are looking at for 24 is a balance between expansion and our leverage.

So since we have uncertainty about the interest rate dropping now, this also places uncertainty about the expansion investments. So one of the levers is holding our investments.

So, within this scenario, you have an uncertain curve. It could probably be a little more optimistic.

The investment in organic expansion is our decision, so the big costs, from the moment we decide to start a project we have to work on it until the end, because if not the costs can get pretty high.

So that's why it's simply a matter of caution and in the 4th quarter, we will disclose what the goal is, with the number of stores and the number of investments. João

João Soares

Ok Belmiro. About competition, we are noticing some markets that have become much more saturated, and we even heard that some players have changed their expansion plans, isn't this influencing this decision a lot?

Belmiro Gomes

I think it's no, the biggest decision is the level of leverage, along with your point about saturation. If you imagine that every cash & carry is the same, then yes it's saturated. That is not the case.

We do not have a quarter of the stores in Brazil, quite the contrary, I think we have 8% of the stores and we have a quarter of penetration among the Brazilian population.
So you have different propositions and there is obviously a market with a greater number of players, but actually, the decision maker is really the leverage level.

There were also impacts, as Irma also mentioned, on the cost of construction, I think we have also been able to reduce our costs and that is why we intend to disclose this number now in the fourth quarter.

João Soares

Great. Thank you, thank you, guys.

Operator

Thank you. We have closed the questions and answers session, and now we would like to go on to the company´s final considerations.

Belmiro Gomes

Thank you. I would like to start by thanking you for your participation during this earnings call. Also thank our team once again, with the total amount of stores which represents a challenge for many areas.

Looking ahead, we see a scenario with limited visibility when it comes to consumer purchasing power, but we can separate the external cyclical effects with the inflationary or deflationary issue at the moment. The company is keeping stable. I think it could even be expected to have a greater impact, either because of the project's great expansion or because of the deflation impacts now.

The company remains very resilient, very strong, very stable, very predictable from a sequence point of view, with the group and the company as a whole, all members, the employees who make it all possible.

Our goal is to keep moving forward, keep gaining market share, keep gaining share, keep opening new stores, and generating jobs and then after finishing this project, which I mentioned a few times and don´t want to be too repetitive.

But I certainly think it is one of the projects with the greatest challenges for execution within the Brazilian food market, whether due to the number of square meters involved, the number of galleries within these stores, the number of people involved, but they start to present their results, start to make this contribution from the point of view of sales, and cash generation.

This allows the company to become more solid, and stronger, in order to face 2024, 25, 26, 27, 28. We always work hard looking at the long term.

Historically an organic store takes up to 2, 3, 4, 5 years, often to approve the project. From the moment we make the decision until we can open the store actually.

So looking at the long term, looking at the medium term, when you look at the positive numbers of this third quarter of the short term, they make us estimate a very positive and solid expectation for the company, in the medium and long term.

So these were my final considerations. I want to thank the team that was together with me during the call, as well as the members of our board of directors, who have also been very supportive during this transition phase.

With all the changes and Casino´s exit, but we are on the right path to have an increasingly cash-generating company, with a higher volume of sales, conquering more and more households in Brazil.

Thank you very much, everyone.

Operator

We have finished the 3Q23 Earnings Call for Assai. The investor relations department is available to answer other questions and concerns. We would like to thank all of the attendees and wish you a great day.