

Conference Call Transcript
2Q23 Assaí Earnings Results (ASAI3 BZ)
July 27th, 2023

Operator:

Good morning everyone and thank you for waiting; welcome to Assaí Atacadista's Earnings Call for the 2nd quarter of 2023.

For those of you who need simultaneous translation we have this tool available on the platform, simply click on the interpretation button on the globe icon at the bottom of your 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 also already available.

During the company's presentation, all participants will have their microphones turned off, and soon after we will begin the questions and answers session.

To ask questions, click the #Q&A# icon at the bottom of your screen and write your #NAME#, #COMPANY#, and #LANGUAGE# to join the queue. When announced, a request to activate your microphone will appear on the screen, then you must activate your microphone to ask questions. We request that all questions be presented at once.

We would like to highlight that the information in this presentation and any statements that may be made during the videoconference, related to Assaí's business perspectives, forecasts and operational and financial targets, represent the beliefs and assumptions of the Company's Management, as well as information currently available.

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I will now pass the floor to Gabrielle Helú, the Investor Relations Officer at Assaí.

Gabrielle Helú:

Thank you. Good morning, everyone. Once again, we'll be participating in this earnings call for the second quarter of 2023 at Assaí. I'm going to present the executives present. We have Belmiro Gomes, our CEO, Dani Sabbag, our CFO and our VP's Vlamir dos Anjos, commercial and logistics, and Anderson Castilho with operations. Before we begin the presentation, I'll pass the floor to Belmiro for his initial remarks.

Belmiro Gomes:

Thank you, Gabi. Good morning, everyone. I'd like to thank you all for your presence at this earnings call today. And we'll begin by talking about our second quarter. The second quarter of 2023 of course has been very challenging with the numbers are going to present here.

First of all, I want to thank our teams and everyone in our stores. From different areas that have been working intensely throughout the first quarter to deliver the results that we have at this moment.

It's a very important moment for the company considering the expansion and the new stores Assaí has been adding to its base, especially last year and even for this year, which should be the second biggest year when it comes to store openings historically in our journey. So I want to highlight the main points in the second quarter. From a market point of view, it's been a quarter where everyone has probably seen the news regarding food deflation.

Some categories had a really big peak in prices in the beginning of the pandemic. And there's this movement towards a drop in prices, especially for commodities, which impacts the same store sale base especially.

From the moment when you have this drop in prices, it is natural that B2B customers, which represent about 40% of our sales, will reduce their level of purchases and stock as they see the prices and a growing trend. Just as we also perform some reductions whenever there is a drop in prices, and you have this contrary effect as well. We see consumers that are very pressured with interest payments, their income levels are still very low.

And so this is mainly due to the impact we had in same store sales in the second quarter and also the effect created last year with this movement performed by Assaí with the closing of the Extra stores at the end of the first quarter of 2022.

We had 105 hypermarket stores of the second biggest operator in this format in Brazil, which of course benefited most of the market, especially in Sao Paulo and Rio markets where you have the biggest amount of these stores. So of course there's a base effect that we'll notice now as we start reopening the Extra stores.

Besides this, the second quarter was very important due to many factors. We had a growth of 21%. Even with the deflation in food, we added a total volume of sales that represented R\$ 3 billion, and a total customer flow growth of about 25%. We reached 70 million tickets within this quarter which represents about 105 or 110 million people going by the Assaí stores. And this growth is mainly supported by the expansion and conversions and transformations. Because one thing is if you convert a store from one format to another and the other is if you transform it from a hypermarket to a cash-and-carry format.

You need to have this heavy-duty process to transform the physical structure of the store when it comes to construction, placing the equipment and really changing the entire concept of the store so that it can have the necessary stock capacity and meet the needs of customers as well as the B2B clients.

So these are stores that are very well located and as we had already mentioned initially, there was an expectation that there would be quick maturity in these stores and that there would not be a very significant impact on results.

But this is very visible when we look at the margins delivered in the second quarter even with a huge amount of almost 35% of our sales area representing stores open for less than three years, we can still deliver a gross margin that's about 16% with a variation of only 0.10% compared to what we delivered last year. Even with the impact of the provisional measure 1159 became effective as of the 1st of May, and also had a marginal effect on our margin pressure. So the margins have been very positive.

An important highlight this quarter is mainly in the expense lines as despite this amount of stores adding all these services, we had about 60 stores opened last year, almost 100 when you look at a three year period. Expenses were extremely stable with a variation of 9% to 9.3%. So this is because we've already included in this percentage of expenses, the cost of occupation in the stores that are still under maturity, personnel costs, and all of the trends and movements that are coming from this expansion process and maturing of the stores.

So the expenses are a big highlight and this variation of the Ebitda is about 0.4 p.p. compared to the previous period, keeping up the delivery consistency and being able to grow sustainably with our own cash generation and keeping up the levels of results despite the high growth rate.

So Dani will highlight this a bit more ahead, but about the Ebitda and the net income I will give you an overview. So we closed the period with a margin that even with the interest costs and the carryover costs and level of debt, as well as the investments the company performed to be able to acquire the Extra POS's and work on the transformations required, we were still able to deliver in this scenario of high interest. Now we are waiting on the minutes of the next Copom meeting as we believe there's going to be some relief in the costs of debts and this will help us of course, get back to a more normalized net income scenario.

Working capital management. So, a highlight at Assai is that we have strong cash generation capacity and along with some initiatives in our stock position that we will also highlight ahead, makes our debt indicator drop compared to the first quarter, which is very close to 2.8x and now it reaches 2.6x. Then moving on to the projects with the Extra conversions, we have at this moment 57 conversion stores opened. We're still missing 9.

If you can go back to the previous slide, you can see the Móoca store, and it's a building that was built in 1898 and we had some licensing impacts for the transformations of these stores that ended up taking longer than expected. Now the company currently has 20 construction projects underway, which allows us to have this estimate, as we had mentioned in the Q1 of approximately 30 new units this year.

With an important resumption of the organic expansion process, since our landbank of projects is still being set up and the company really has a set of projects for organic store openings, now in 23, but also in 24 and 25. We can move on to the next slide please.

So the sales uplift and performance of the Extra stores, as I mentioned in the first quarter, we know how people are very anxious for the sales, but these are stores that have even less than eight months of full operation. So it's still a very new project. The first store openings were concentrated from August last year onwards.

So next month in August, we're still going to have like the first stores completing a full year anniversary of operations and even with the impacts of deflation that we had, which of course will impact the same-store-sales as well as the new units, the stores already performed 2.5x as a sales uplift. And I think the main point here is that these stores continue to keep up their growth ramp with an evolution of almost 10% in the second quarter, compared to the first quarter, and especially delivering an EBITDA margin. In the Ebitda margin there is a degradation of 0.4 p.p. in the total base, meaning that the expansion already began very strongly with an Ebitda that's close to 6% even with this short period of sales.

So another topic we would like to also highlight within this group of stores that came around in the second batch of the hypermarkets, Assaí will go on to having a gross leasing area with stores of 220,000 square meters. To give you an idea, this represents probably the second biggest shopping in Latin America and it adds up to 1300 shop owners split between these units.

The focus in the company mainly last year, was delivering the part for our operation first of all. So, this year we're completing this gallery project within the investments. We already have about half of these galleries complete.

So this should help us when it comes to the revenue as the revenue from these galleries in the stores is not considered in our lease line. So we received some questions about this. The company looks at the revenue coming from these shops in the stores as a reduction in rent costs. But from an accounting perspective, the revenue from the galleries is classified gross profit.

So there's 1300 small stores and they are going to help these stores with a bigger customer flow when it comes to maturity, dilution of the rental costs and occupation costs that we have in the stores such as the property tax, water, sewer taxes and other fees. So it's a really intense project with 220,000 square meters of leasing space, and for those of you who invest in real estate I'm sure you know what it means, with a quantity like this that was included in the project and we received some questions about this. So it's important to highlight this point.

Now I'll pass the floor to Dani and she'll talk about our Ebitda, our earnings and cost of debt, and then after I'll come back up ahead. Thank you so much.

Dani Sabbag:

All right, Good morning everyone.

And now moving on to slide five, we're going to talk about the Ebitda. We have an important evolution in Reais, quarter over quarter, and also some important evolution in this second quarter compared to last year. And in the semester, with an increase of R\$ 334 million and an EBITDA that already reaches R\$ 2 billion.

So our margin had a little bit of pressure of 7% compared to 7.4% last year, and this pressure is mainly due to the maturity of the stores. An important point to highlight here is that we have a store network with over 1/3 of the stores still maturing. So 35% of these stores are in this maturing phase.

When we highlighted to you guys the evolution of the Extra margins, an important point to highlight is that if we exclude the effects of the conversions and the margins of the conversions, then the Ebitda margin remains quite stable year over year. So here we have the results that demonstrate the resilience

of the company, and this is a very important point, as it also reflects the maturity. And we have a very stable margin year over year.

So, if we move on to the next slide I'm going to talk about our financial results. And here from the R\$ 628 million, it's important to exclude some of the effects with the lease liabilities. So when we look at this part here that's blue on the graph, we can see the financial results pre IFRS of R\$ 221 million to R\$ 420 million and this evolution of R\$ 200 million year over year, is mostly related to the cost of debt, of course, and the greater volume of debt, coming from the fundraising initiative we performed in 2022 to be able to handle the expansion project in the company and support our investments for expansion.

So, to explain this variation, an easy way is to say that R\$ 100 million would be coming from this higher cost of debt and the other R\$ 100 million or so, is also related to the capitalized interest, which is already at a smaller amount than what it was before since we already reached 90% of our conversion project for stores. So this explains the variation in our financial results.

So moving on to the right side of our slide. We have a lot of stability in our net debt. R\$ 7.9 billion last year and this year, with strong cash generation as well, which is an important point here in this slide where we end the last 12 months with a cash generation of R\$ 5.4 billion, an improvement of R\$ 2.6 billion mostly coming from the management of the working capital. So, for suppliers and stock, we have significant gains and this strong cash generation is really what supported company's investments.

So when we take a look at the 1st and 2nd lines, of R\$ 3 billion of these investments, that in the past 12 months represented almost 60 new stores and a sales area that grew. And it's important to highlight that we grew 34% in our sales area and an additional R\$ 1 billion which are the payments related to the acquisition of the commercial real estate.

So, we supported this high level of investments, besides the cost of debt that we are disclosing here which adds up to a total amount of R\$ 1.3 billion, so with this, we have a net debt and leverage going from 2.72x last year to 2.6x.

And if you remember in the first quarter this year, we had 2.8x. So this is an important advance towards deleveraging the company.

And now I would like to also make another point here. Can you go back a bit? OK.

On this last chart here, on the right corner, we would also like to highlight our indicators and our debt ratios. On the blue line you can see how we present this in the release. We know that there are some analysts and investors that look at this indicator of 2.6x adding the payments to GPA. So if we do this, we would be adding on 0.8x to this indicator. However, for the contractual covenants that we have on our debt contracts, the number for these contracts is the orange line.

So, we're taking a look at a difference of 1.8x to 2.6x and the 1.8x is what applies to the three times covenant. So this slide basically intends to present to you how in regards to covenants, we are very comfortable with the levels that we have achieved at the moment. And when we look at the forecasts in the future for deleveraging the company and our commitments for payments with our cash flow, we will have this deleveraging occur through a very gradual process, but by 2024 and 2025 we should be at levels that are a lot lower. So we're very comfortable with these numbers up ahead.

Now moving on to the next one, we present our net income, and as we mentioned, some of the factors presented during the presentation. So we have our financial results and profitability, stores that are maturing, as I mentioned, and we end the quarter with R\$ 156 million. This evolution is very significant compared to the previous quarter because we ended with a margin of 1% and last quarter, we had a margin of 0,5%. So, we have an evolution quarter over quarter, and in the semester R\$ 228 million with a margin of 0.7%. So these are the main comments about these two slides.

Now I'll pass the floor back to Belmiro to talk about ESG advances. Please, Belmiro.

Belmiro Gomes: Okay, thank you Dani.

And of course, the company is the second biggest retailer in Brazil with 76 thousand employees, 105 million people going through our stores in the first semester, which is equivalent to the Brazilian population coming to our stores.

So we have an important social responsibility, especially due to the sector we operate in, and our target audience as well as the locations of our stores. So this is a topic where there's always something to do, there are always things you can improve and work with. But it is a topic we have an extreme responsibility towards.

And within this quarter with the exit of our former controller, our company now has 100% fragmented capital. So with this we have become a full corporation. So from a governance perspective there are some highlights this quarter. Assaí is recognized as a company that really focuses on ESG, we have 5.5% people with disabilities and we're probably one of the only large companies that are above the legal quota and some other important advances we've had.

We also had a reduction in our scope one and scope two emissions.

And another interesting project is the Assaí Academy which intends to train small businesses and B2B customers, with over 20 thousand people signing up this year, especially among informal businesses as they are searching for ways to professionalize and manage their activities. And so we've been able to train people.

An advance in the levels of waste repurposing reaching 44%.

We also had a special campaign to gather donations of blankets and clothes as well for a special campaign for winter with over 42 tons gathered.

And now with the new board, Assaí will now have two women in the board. We have a lot of work to do still because we have a total of nine members. But before we only had one woman, Josseline, and now we have Leila and Andiara.

We also have important advances also when it comes to our policy for diversity and equal opportunities, we have 43% of our people that are black or brown in leadership positions.

This is a topic that we're also advancing in constantly and in line with the concerns in society and over 25% of women in leadership positions.

I also want to highlight something that is not on the presentation, but the company was once again awarded by GPTW among one of the 10 best retailers to work at. This is something we're super proud of and this is a result of our work not only in HR but in the entire company since this classifies the climate.

Now the company has 100% fragmented capital. We had the election of the new board this quarter. So the new board is really fully independent. Among the new board members, five had never even been in contact personally or professionally with me. And so from a governance perspective the company will have some very recognized professionals, highly qualified professionals that can support management and give us comfort when it comes to governance, especially for our shareholders.

So having said that, we finished the presentation and would like to open up for Q&A. Thank you so much, everyone.

Operator:

Now we will start the Q&A session and would like to remind you that in order to submit a question 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 announced, a request to activate your microphone will appear on the screen, then you must activate your microphone to ask questions. We kindly ask that all questions be submitted at once.

Our first question is from Joseph Giordano and we'll open up your mic.

Please, Joseph, you can begin.

Joseph Giordano – JP Morgan

Hello everyone. Good morning and thank you so much for taking my question. We would like to explore three main points here. The first one is maybe a positive surprise in the quarter with the working capital dynamic, especially for the suppliers account with quite a bit of volatility. So if you could give us a little more color on what has been done to improve the terms with suppliers without leading to major impacts on the other side which would be the gross margin.

The second point is the occupation cost which has been growing a lot and so back then when we had the purchase of the Extra stores, you were mentioning something about like 1.5% of the revenue, as occupation costs. So I want to split this question in two parts. So the first question is if these 1.5% already consider the revenue from leasing the stores in the galleries and what would be the actual potential when it comes to revenue from leases coming from these gallery stores.

Then we would get into the governance issue. Belmiro mentioned the diversity of the board. We have a board member that was a related party in the company currently. So could you maybe talk about this, I want to hear from you guys about how the situation is with this board member, if he should continue to be in the company and if this would also be used to improve the diversity in the board as well.

Belmiro Gomes:

Thank you Joseph. I will switch the orders and let Vlamir, our commercial VP talk about the working capital aspects, but regarding the occupation fees, yes, when we considered the lease it already considered the net effect which is how we look at this daily.

So the lease of these properties, especially with the stores that came from Extra we have to pay for rent of the entire area occupied including the Assaí operation and these 220,000 square meters of leasing area, which is actually going to move on to almost 400,000 square meters.

So of course we already considered the net value. The focus last year was to finish the areas for store reopenings. There was an impact when it comes to licenses, so some people as why we didn't open everything at once. Because believe it or not, we could take even longer to open some stores, especially the ones with a huge leasing area, and the priority was to open the Assaí stores.

This year we have a huge effort from our construction team to complete this store gallery area. So 220,000 square meters of leasing areas represent approximately 40 Assaí organic stores basically in sales area. So it's a huge effort. We would not like to provide an estimate for revenue yet.

But in the first semester, although half of these galleries are ready, we have a big effort till the end of the year to deliver the rest. And they already did bring some revenue in the first period of R\$ 44 million. So there's a potential to at least double this amount of revenue. But, of course, this is a situation that varies from site to site. But we can't only look at the revenue from the galleries, because this also helps us with other costs such as the cost of occupation, the property taxes, which is a very relevant weight when it comes to expenses especially in major capitals. But it also helps when it comes to customer flow.

Most of these store owners also benefit from this and help our own store flows and traffic, especially in the downtown regions where you have levels of service and consumers have a different social level. And for these clients it's sometimes good to have extra support like a cafeteria, a snack, stand, a gym or other convenience stores.

So, from a board perspective, we had the exit of the controller. This is a topic that of course we're still going to be discussing. We just had finish the project, but it was one position among nine. So, I don't think this is going to be that relevant but if there are some changes that need to take place, they could happen in the next few months.

Now I'll pass the floor now to Vlamir to talk about the working capital.

Vlamir dos Anjos:

Good morning everyone. Thank you for the question Joseph. When we talk about working capital, we've been negotiating the increase of terms that are quite significant for quite a while and we just materialized and completed these negotiations in the first quarter. And this of course reflected on this gain in greater terms with our suppliers. But the improvement in the working capital is not only due to the adjustment in the terms, but also the adjustments in the levels of stock.

We had a period where we had the opening of many stores and we were structuring our stock and inventory, but now we're readjusting this. And so now we have a history of what the stores sell, especially the ones we recently opened and now we can balance out the stock levels a little better. And we also had some contributions towards the reduction of stock with the deflation issue, especially in commodities where we also reduce the levels of stock due to the deflation scenario. So up ahead what could take place is some variations between the quarters with the working capital, but nothing very relevant.

Now what could happen now as we talk about the 2nd semester with the working capital is that we'll enter an accelerated process for expansion with 20 stores under construction and we need to supply these stores. We have the anniversary campaign, as well as the seasonality in the second semester and we have the Black Friday campaigns as well, and Christmas.

But I can keep you at ease by saying that we always were very disciplined with the working capital and this is going to be kept, we're not going to lose this. We're going to continue to look at these aspects and adjust to the macroeconomic scenario.

If we keep up with a deflation pace up ahead, then maybe the strategy will have to change. So we're going to adapt, but I can keep you at ease that with the working capital will keep our discipline as always. I hope that answer was clear.

Joseph Giordano:

Yes, it was.. And just a quick follow up here with Belmiro to understand what would be the ramp up of these leases. So a lot of these stores have been open in the second semester last year, some now. And so how should we look at the leases in the future because this is going to lead to relevant impacts in the next quarters.

Belmiro Gomes:

When it comes to occupation costs, well, our expectation is that some stores even due to licensing and complexity issues, we will be completing around November or December. So, we should already have some evolution in the third and fourth quarters, but we should be capturing these effects in the first quarter of next year.

So for the leases, we always wait for the Assaí stores to be open and at a certain level of activity, because this also helps us negotiate the leases per square meter, but we should really notice the effects in the first quarter of 2024.

Joseph Giordano:

Okay. Thank you. Perfect.

Operator:

Well, the next question is from Vinicius Strano, sell side analyst at UBS. Vinicius we will open up your mic. You may proceed please Vinicius.

Vinicius Strano - UBS

Hi guys. Good morning, everyone.

Thanks for taking my question. I wanted to discuss how you're imagining the ramp up of the Extra stores up ahead. And today, for example, how do you expect these stores to be close to their full potential?

And could you talk about what the cannibalization levels are that you've been noticing? And then also about this topic, if you could just mention a bit of the expectation of how you're imagining the same store sales being impacted. Thanks!

Belmiro Gomes:

Well, Vinicius. There's no way out: cannibalization exists and especially when you look at the Sao Paulo and Rio markets, which is something I mentioned, and even in Brasilia where you have a huge amount of extra stores. So a point we have been highlighting a lot among investors and shareholders is that we have to separate what's cannibalization and what's just returning what was delivered last year.

So in the North and Northeast to Brazil, there were not Extra stores. So there wasn't like a positive effect for whoever was operating that region, which was not the case here in Sao Paulo and Rio where the overall market was benefited with the closing of the Extra stores, but as the new stores are reopened, the stores that received the store volumes will start giving back part of this volume.

There's also a bit of cannibalization, for example, if you look at the Congonhas store, we had customers there that would buy at our store on Marginal Pinheiros. But now there's a newer store that's more modern, closer to where they live and then they're going to start buying at this new unit.

So there is a bit of cannibalization, but there's also a part which is just like the temporary effect of the closing of the Extra stores. So to be honest, in Rio, Sao Paulo, Brasilia where you had the biggest concentration of these stores, the best method would be to use the same store sales looking at two years because then you can see the period where Extra was closed and also the period where the stores were reopened. But yes there is a cannibalization effect.

Part of this maturity and cannibalization was also a bit more contaminated by the deflation because B2B customers become more careful and they're controlling stock due to the visibility with the price. Normally B2B customers, when they see the oil prices are dropping, are not going to go out and shop for big volumes.

So when you have store maturity, for example, of course, this varies from store to store. But our expectation is that we'll have three times the amount of sales, we've already disclosed the number in the end of last quarter. In the first quarter this was quite stable at 2.2x because we had the effect with December and goes up to 2.5x. But of course we've been working on this as quick as possible. We should of course be looking at the final numbers in the project in 2024.

So the time to plant and a time to reap and now is when we're investing and we're starting this process with the activities where you have the biggest amounts of operational expenses, investments. But we're super satisfied and confident of beginning our work in these stores even with the amount of time they have. If you look at this total amount of flow and this increase of 25% that we highlighted of course this is

going to be levered by the opening of these units. So they continue to follow this maturity ramp and this is some work that we do month after month and week after week.

And so there's some stores with a potential to have a higher ramp up and of course there's stores where you have a reaction of competition also. But I think this is super visible when we look at the public numbers for the retail operation and we can see how this has been affecting the opening of these new Assaí stores. I hope that's clear Vinicius.

Vinicius Strano:

Thank you. Just a quick follow up here. Do you already see any kind of evolution with the sales? And what's been the progression throughout the quarter? What have you been noticing In July? Thank you.

Belmiro Gomes:

So yeah, we ended up well. We know how the market's very anxious about these stores and they go from 2.2x with a sales uplift of 2.5x. And so of course, there's some evolution within the quarter ever since we looked at this from the other period in March and now in June as well.

Operator:

Moving on the next questions from Daniela Eiger, Sell-side Analyst from XP.

Dani please you may proceed.

Daniela Eiger – XP:

Good morning, everyone and thank you for taking my question. These guys are starting to get faster and are now placing their questions before me! I always used to be the first one in the queue. But anyways a follow-up here on Vinicius question just to expand a bit to the broader store base.

So you talked about this in the release and how the same store sales were already positive and there was an important evolution throughout the quarter, but this calls our attention because the food inflation is quite weak and actually has been slowing down. So if you could maybe talk about this and show us a bit of the vision for July for the total base, not only the conversions and also some color on what the volume dynamic has been. Have you noticed any kind of recovery or trade ups at the stores?

And then my second question, going back to the conversions and talking about profitability a little bit, the 6% seems to be very strong. So I don't know if this is already in line with your expectation towards the ramp-up or if this is overcoming expectations of what you had planned and if you could talk about if this and if it is in line or above and where you're headed. It is really those 150 beeps above average or is there room to be even better than this. Thank you.

Belmiro Gomes:

So thank you. Dani, I thought you weren't on the call, I was missing your name, but great to hear from you.

Anyways, the ramp up of 6% is in line with the project. We highlighted this in the beginning, that there would be a ramp-up. It's a little more accelerated compared to organic stores considering the location of

these stores and even the level that they have with the category and public surrounding these stores with another level of income and a higher average ticket.

And this of course helps to dilute expenses. And so I wanted to highlight this because when we worked on the conversion project, you're going to remember that a lot of people criticized the services and how we were modifying the cash and carry model. This could of course impact the costs and you even brought this question during a call. So we look at the expenses and we see that they were actually very stable if you consider the amount of stores we had. And if the store is not good, then it's not going to start off with good expenses. So if expenses are very much impacted at the beginning, this demonstrates of course that you will have difficulties with the maturity curve.

So it's in line with what we expected. But the same store sales in April had some competition effects which also impacted this and in June we also made an effort, com a sales perspective. July is better than June from a sequential point of view, but July last year was also a strong month.

And now the same store sales with deflation should be a bit shallow. But when we look at this internally, the Extra effects and cannibalization we must also deduct. So of course we are concerned with the same store sales, but there isn't any other movements that can explain why it's dropping.

Unfortunately, we haven't noticed a recovery in volumes when it comes to consumers. So the difficult choices, the trade-downs customers had during the pandemic to face the food inflation that didn't come along with an increase in income, these purchase choices remain. So I'd mentioned that we expected there would maybe with the stability of food prices and that consumers could maybe go back to their original habits has not occurred.

So we've performed surveys and noticed that there were some new expenses added to the pockets of these consumers. So these are consumers that are really pressured due to high interest.

And believe it or not, now there is also a big market for sports bets that really take away a lot of income from these consumers. And so, they haven't been able to resume their purchase volumes. So they are totally stable in the 2nd quarter basically.

We have an expectation that's actually a lot more positive for the third quarter because naturally the third quarter is stronger and we can see this in July as we practically closed the month already.

So there is an evolution and we should see the market as a whole pressured with deflation and with the movement I mentioned about last year with the benefits from having the Extra stores closed so we should still have the same store sales pressured in the 3rd quarter.

Daniela Eiger:

Excellent! I hope the *Desenrola* will also help consumers a bit, let's wait and see! Thanks Belmiro.

Belmiro Gomes:

Yeah, our expectation is that this government program will help. We've been monitoring this closely and we see that the population is still suffering a bit, but some categories where there was an expectation, we still haven't seen happen actually. So as the interest rate drops, this is going to release a significant amount of cash in the market that could also be used for food.

So the good news is that we have a population that is not consuming what it should be consuming or would like to be consuming. So as soon as there's any kind of improvement in income or with other expenses such as interest or debt this cash should go back to the food market.

Daniela Eiger:

Great. Thank you.

Operator:

The next question is from Ruben Couto Sell-Side Analyst at Santander. Ruben will open up your mic so that you may proceed please.

Rubem Couto – Santander:

Hi, good morning, everyone. Thank you for taking my question. Could you give us an update on what the expectation is for Capex this year? Most of the conversions have already come through, but could you help us as we see there's a lot up ahead still? So what's the dynamic like for inflation in the construction expenses you have been mentioning for a while? Has this also been reducing along with the inflation headlines? Well, I wanted to hear from you about this topic.

Belmiro Gomes:

Thank you, Reuben. The CapEx expectation is pretty much kept for the year. So it's about R\$ 3 or R\$ 3.5 billion. The costs of construction are very similar to food. They went up a lot in the pandemic and they stabilized now. There's a little bit of deflation now in some products, but then I think the actual movement towards having 60 constructions or transformations of stores also generated an increase in market prices. And so when we kind of held on to this a bit to be able to handle the cost of debt, 40 stores to 30, we waiting on some organic stores, which helped us with some negotiations.

But the cost of construction is still at a really high level just as the food prices. So we haven't seen any signs or room for increases, but they did stick around at high price levels, especially when we look at steel and metal costs. And it is possible that will have a reduction depending on the level of the Dollar.

We did have some optimizations when it comes to project perspectives to search for ways to reduce costs. This is going to be even more visible in our organic stores this year and next, but there's no big expectation for an increase in Capex volumes compared to what we had projected and it is maintained. Thank you, Ruben. I hope I answered your question.

Rubem Couto:

Thank you. Yes, you did. Thank you very much.

Operator:

The next question is from João Soares, a Sell-Side analyst at Citibank. João we will open your mic so that you may proceed. João, you can proceed.

João Soares – Citibank

Thank you everyone. Good morning.

I have a question about expenses. I think it's clear that you mentioned that the margins of the converted stores which are in line with the plan. When you look at the operation as a whole, it seems like there's been quite a bit of work to reduce expenses, at least when we look at the SG&A year over year which dropped 8%. And I wanted to understand if there's any kind of broader plan to cut down on expenses and gain efficiency or maybe you can even revisit the soft guidance you guys provided about stable Ebitda margins for the year. Thanks!

Belmiro Gomes:

Well, it's a huge effort. As I mentioned the expense factor twice. There's an effect of the dilution. Maybe Anderson can talk about the huge efforts to control costs. Anderson has been leading this.

Anderson Castilho:

Well, good morning, everyone, and thank you so much for this question. I think that I always talk about expenses and how they are just like nails, you have to be cutting them all the time. And then there's a general approach especially in the operations team, which is store by store looking at each detail when it comes to power, water, safety, security costs, etcetera.

It's something that we really look at in a very detailed way, especially when we look at our daily operations. So we have been monitoring this from a general perspective and we always say that any R\$ 1000 saving is a lot of money when you look at 270 stores, right? So we're very careful about each detail and we have a team that's very much focused on expenses.

We're a low-cost operation and I always say that our cheap prices need to be based on lean expenses. So this is our team's discipline. Our team is very careful when it comes to this topic and we have major effort when it comes to administrative, operational and store levels and in our operation also with logistics when it comes to freight costs.

So the sum of all these factors really makes us perform these adjustments. So a lot of small factors or topics that altogether make a difference and regardless of any new topics we add to the business, expense control is always the focus. I hope that's clear. So it's really about our day-to-day discipline.

João Soares:

Well and for the year, do you have any expectation when you think about this, like maybe a magic number you can share with us that you think these projects could deliver when it comes to savings?

Belmiro Gomes:

I think it's still quite early to estimate this, but of course it's an effort to reduce expenses. Part of this is also because we have a dilution of administrative expenses because last year we were prepared to open up 60 stores. So the amount of temporary workers we had also was quite significant. This year we're opening 30. So naturally you have dilution due to the actual growth. But as Anderson said we're going to be always working towards reducing expenses. But I think mentioning a guidance at this point is not what we would like to do.

But you can believe that we'll be working to operate with the lowest expenses from an expense perspective. And I think it's important to highlight that we had many changes in our model. We had a lot of curiosity or anxiety about how this could maybe generate greater expense pressure, but this is not what we've seen. Just visit one of these stores and you'll see that there's better purchase experiences keeping low costs, which is such an important characteristic of our business model.

João Soares:

Great. Belmiro, thank you so much. Thank you, Anderson.

Operator:

Next question is from Luis Guanais, sell side analyst at BTG Pactual. Luis we'll open up your mic so that you may proceed. Please, Luis, you may proceed.

Luiz Guanais – BTG Pactual

Good morning, Dani. Good morning, Gabi, and Belmiro. I think I have 2 questions here on my side. The first one is if you could talk about this breakdown at these converted stores in terms of price and volume throughout the quarter and help us understand how this has been evolving. I know that there's a ramp-up for the store. And you also talked about the performance in June, which was better.

And the second question is still in line with the working capital point after the conversion process of the stores. Could you maybe talk about the differences in the working capital processes and dynamics in the converted stores versus the legacy stores? Thanks.

Belmiro Gomes:

Thanks Guanais. Well 100% of the growth that comes when you look at this from a sequential perspective is volume and traffic or customer flows because the price we measure according to the average kg and they've been stable for about 12 months.

The price on average of what you're selling compared to last year is dropping about 2%, which is what we see as deflation. So you have to operate with 2% more volume to be able to have the same sales value as last year.

So the evolution in the stores, comes due to volume and customer flows or traffic. So deflation also affects the ramp-up curves and if we had food inflation which is what we had expected for the project we would

have about four or 5% only and then it would be 4 or 5% more in sales. Not sure if that answers your question.

So then when it comes to working capital, yes, there will be an improvement which is not related to the fact that it's a conversion, but it's just because of the location they're in. So since most of these are in big urban centers and major states where the stock time for supplies is a lot shorter than what we see in stores that are in the north of Brazil, in the Amazon region or other remote locations. On this map here you can see how we're present all over Brazil. And it's really about a geographic aspect that makes them deliver a stock supplier ratio that's better than what we have compared to the legacy park that we had highlighted before. I hope that's clear.

Luis Guanais:

Excellent, thank you for the answers.

Operator:

The next question is from Vitor Pini, Sell-Side analyst at Safra. Vitor we will open up your mic so that you can proceed. Please Vitor you may proceed.

Vitor Pini – Safra

Good morning, everyone. Just a follow up here about the gallery issue. I wanted to understand if the 50% that are already complete have already been operating full and when the other fifty percent that are under construction should be ready? And could you give us some guidance about the expectation for sales with these 44 million that you had in the first quarter, can you already expect some kind of proxy or if there's a big ramp-up still compared to those that are under operation?

Belmiro Gomes:

Well, the guidance of course we have been avoiding but I think that the proxy is very good in my opinion. The other 50% have been delivered at this point and they should follow the sequence as we have the store openings and we'll be finishing the galleries till the end of the year. But we want to be careful about this. We'll bring some updates probably quarter over quarter.

Vitor Pini:

Okay, Perfect. Thank you.

Operator:

The next question is from Vitor Trevisan. Sell-side analyst at Itaubba. Vitor we will open up your mic so that you can proceed, Please Vitor, you may proceed. Hey, guys, actually this is Macruz.

Thiago Macruz:

So I wanted to understand this a little better. We have noticed some very interesting stability in the gross margin in the industry as a whole. We saw this with you guys and some other competitors as well. We've been receiving some feedback from regional players as well.

It seems that the suppliers have been good partners at this moment, but the deflation scenario is still being kept. So how have you been looking at this dynamic and if we look at the next quarter, is there room for suppliers to continue to be your partners regarding this? And is the stability of the gross margin something that we should look at as long lasting? I think that's pretty much the question.

Belmiro Gomes:

Thank you, Macruz. Well, the margins of course are a consequence of our model, we price this based on cost and the margin needs. So the company will always be searching for a way to be stable with margins. So unless you have any big effects from a competitive perspective. But it is necessary to make the sector continue to be healthy and generate cash. So the company will always be searching for stable margins, regardless of an inflation process or deflation process.

And that's why controlling the stock is so important for the stability of the margins. There could be an occasional situation where you have to invest, but the price of the cash and carry operation overall, especially for us as we have a lot of stores in new locations and people that are starting to buy in this format, our price represents a bit advantage compared to other retail channels.

So this allows us to have margin stability. So of course what can vary a little more with deflation that we felt this quarter is the volume of the B2B customers. So when you have a growing price trend, they stock up, right? Just like we do. And when you have a movement with a price drop, they're going to reduce their stock levels. And there's no point in having like a special offer because they look at the situation and say "well soy oil prices dropped and will go down even more, so there's no point in organizing a big purchase" so the special offers may even be unhealthy when it comes to attracting more volume.

So, this kind of explains the very good control of the margins. But of course, when you look at the margins and we have to keep our eyes open and look at the expense perspective. So if the store is not a store that has good performance expectations, the expenses are going to start off a lot higher than they should be. That's why we're being very careful with the efficiency and discipline of our expense controls and we highlighted this during the quarter.

Macruz:

Well, excellent Belmiro thank you for the answers.

Operator:

Well, now the next question is from Irma Sgarz , the sell-side analyst at Goldman Sachs. Irma we will open up your mic so that you may proceed. Please Irma, you may proceed.

Irma Sgarz – Goldman Sachs:

Well, good morning and thank you for taking my question. Just one more point here on my side from the converted stores that you're already operating with at a margin of 6% based on the comments you guys made before in the release. Could you maybe talk about how this margin would be if we were to take a look at the EBITDA in the pre-IFRS level considering the cost of occupation in these converted stores included in the margins, just so we can get a feel.

And also how you would compare this with the organic stores that are just as old? I think this was this kind of comparison was very interesting and useful.

And just another question about the market gains. Of course a bit of this also comes from the expansion in the store network. But when you look at the stores that are mature, do you also feel that there is a bit of a gain in these new converted stores from the competitors? Or maybe there's some market share or some segment in the market where you think you are gaining more market share either from the stores or regions where you're gaining more market share?

I think it would be very interesting to have this extra information. Thank you Belmiro.

Belmiro Gomes:

Thank you for the question. We presented a breakdown of our Ebitda and a pre-IFRS vision. And that demonstrates this variation in the pre and post IFRS which is 0.4 p.p., which is basically the same.

And the converted stores of course they're on a maturity ramp, so they have higher rent costs and they're going to have the gallery revenues coming in still. So of course, the Pre Ebitda is more pressured. So today we would have these 6.3% that would drop to maybe 4.5%. I'm going to confirm this later and it's important to talk to our IR team later as we can highlight this number better, but even in a pre-IFRS vision, the conversions are very positive.

So in our model that's a cash generator, they already started contributing with the earnings, and net income. So we wouldn't be able to operate with this EBITDA margin pre IFRS, because the entire lease is being paid now. So you already have a dilution of this expense as there's a ramp-up of sales from 2.5x to 3x.

But most of the galleries that we also wanted to highlight are in these stores. So most of these galleries 80 or 90% come from the conversion stores now that we recently worked on which are the big stores that Extra used to operate with, in the hypermarket format. So there's still like a normalization that needs to be done in the Pre-IFRS Ebitda Margin.

But in a post-IFRS we are keeping the guidance provided in the beginning of the project. And in the Pre vision they also have to deliver the Pre-Ebitda which is bigger than our organic store network.

Irma Sgarz:

Very useful. Thank you. And the second question was about the market share.

Belmiro Gomes:

Oh well, about the market share, it really depends on the store regions. So, we highlighted this throughout the project, due to the fact that Assaí was part of GPA we were avoiding to open stores close to Extra stores and Atacadão also avoided being close to Carrefour. But now we're entering the central areas where a lot of our regional competitors were very strong for quite a while.

So there are important gains depending on the region coming from other Cash & Carry players, as we have been noticing, within these expansion stores, but most of them have been coming from retail. So there's an important part that we always remind the market about which is how 40% of our market is B2B.

So the wholesale distribution market is still very strong but very fragmented, so we don't have a very clear vision about this and these stores are now provide these services. So they have some gains from different aspects, but there's also big variation from store to store. In some stores, most of the gains come from other cash and carry competitors and in others most of the gains come from retail operations. So I hope that was what you wanted to hear and that was clear.

Irma Sgarz:

OK Thanks.

Operator:

So the next question is from Vinicius Preto, sell-side.

Analyst from Bank of America. Vinicius we will open up your mic so that you may proceed.

Vinicius Preto:

Hi, good morning, everyone. Thanks for taking our question.

When you look at the performance of the Extra Stores that have already been converted for longer, what surprised you guys compared to the original plan and what was the expectation for returns and how do you see this compared with the acquisition for these stores? And also if you could give us some color of almost R\$ 1 billion in forfait operations and how we should imagine the payment of this in the next quarters? Thank you.

Belmiro Gomes:

Well Dani can talk about the Forfait operations and payments. I will talk about the Extra stores and what surprised us is the flow and about 25%, it's quite easy to perform this calculation right. And we can see how many people were added to the store.

So although we already had a series of projects in central regions for stores, of course there is always some fear towards if the customers will accept this kind of model. But we noticed this strongly. So we had some surprises that were positive in this area and also when it comes to customers that use the store to perform a monthly bulk shopping and but then they come for smaller replenishment purchases, which has been greater than what we had seen in organic stores

But this project is really new and the numbers show how we were very precise in bringing the cash&carry format to downtown areas. So not really about surprises but the fulfillment of our expectations.

There's still a lot of work and obviously we are presenting the project overall as there are stores that have better performance and stores that have more work to be done. There are some other competition processes as well, but the project has been within our expectations.

Dani Sabbag:

So yeah, about this forfait issue, because we receive a lot of questions about this and if we should add the debt or not. So our understanding is that the operations are quite normal for supplier discounts and the anticipations.

So the forfait operations for merchandise are considered in the supplier account and they're part of our cash flow for payments. We provide for these payments just as the suppliers and Capex. So the criteria is exclusive for these ones. This level of the CapEx forfait should be at a regular normality level about 300 or 500 million, that's our estimate. But it's important to mention that when you look at this guideline from the Central Bank, you can see that there are operations like this for suppliers that perform these with their financial partners, and we sometimes find out because we look at this data.

But this is subject to the supplier's exclusive criteria, and they manage their cash flow with their financial partners. So we don't always have the supplier asking us about this. So what I would like to say is that we should have a drop of about 500 million from the levels you see. But if you look at the history of the company, you'll see that there's always a percentage of merchandise and that's quite regular in the business.

So if you want to clarify any points on this, I'm super willing to help with more details.

Vinicius Preto:

Okay, great. Thank you.

Belmiro Gomes:

So forfait operations always existed and there was some disclosure due to what happened in the market. But this is up to the supplier entirely. Even from a Capex perspective, with some construction projects for 2024 we're already having expenses incurred now. So besides what we highlighted, there's some construction work that's going to be opened in 2024 that already started.

There are services like groundwork and other preparation work. And so this is normal, when you have a longer opening process you will ask suppliers for a longer term, and since they have a bigger level of these forfait operations, they will be keeping up with a higher level of investments due to the 60 stores last year, 30 this year, and the amount of stores that we're going to have for 2024.

Vinicius Preto:

Thank you. Very clear Belmiro.

Operator:

Well, moving on, we're going to head to our last question. This is a question in English from Andrew Ruben, Sell Side Analyst at Morgan Stanley. Andrew we will open up your mic. So you may proceed please. You may proceed.

Andrew Ruben – Morgan Stanley

Hi thank you.

ou mentioned the land bank and just mentioned some plans for 2024. I'm curious what kind of visibility you have for the organic openings, your latest thoughts on what the pace of new stores might be over the next couple of years? Thank you.

Belmiro Gomes:

Thank you for your question. Andrew. We would still not like to disclose this number for 2024. As I mentioned in the first quarter, we held on to some openings within our land bank and we have about 50 projects for about 50 new organic stores. But part of this level of leverage that the company has, as we hope for a drop in the interest rates, but we have been managing these debts by waiting on these investments. So we're still going to assess this a bit so that by the end of the year we can provide information on the exact numbers for 2024. But there are still a lot of stores in many regions still that we need to penetrate.

Next week, we're going to open our first store in the state of Espirito Santo. Tomorrow, we're going to have an organic store opening in Limeira, a market where we only had one small store. And it's an important city. So Assaí is continuing to expand. There's some cities where we're going to have our first stores still. Sometimes they're big cities with almost half a million inhabitants. So there's still a big amount of cities to enter, but we would like to wait and analyze this before we can disclose this information about the expectations for stores in the next years.

Andrew Ruben:

Very clear. Thanks Belmiro.

Operator

The Q&A session is now complete and we would like to move on to the company's final remarks.

Belmiro:

First of all, I want to thank our entire team, not only the directors that are present with us in this earnings call, but all of our Assaí team of 76,000 employees. We went through a challenging period in the past year with the amount of store openings, not only with the 60 units that we highlighted, but we wanted to bring these 230,000 meters of galleries, the amount of new services, butcheries and cold cuts etc. So huge movements.

So we're really at this investment phase and we know that this is what's going to guarantee our relevant positions when it comes to the growth of the company up ahead.

So the expectation now is that we already survived the most challenging period in the first semester. The 2nd semester always has a more positive perspective when it comes to income and stability in the economy, which has an important factor with the expected drop in interest rates. So of course the company has leverage and this weighs on our results. So there's a very positive expectation and most of these conversions were already performed.

So we have some final conversions such as Guarulhos with a very important opportunity there. And I want to thank the team a lot. Besides this, I want to highlight that this quarter is an important milestone for the full transformation of the company with the controller leaving and up until 2020 we were a GPA subsidiary and in 2021 we stopped being a subsidiary.

We started to report to the controller and then they sold their positions and the company started to be a publicly held company that's really a corporation. And this did not affect our performance, when you look at the stability of our margins, the company continues to generate cash and grow as always. And we want to thank the members of the new board for the support that they've been giving us within this transition process and also thank some shareholders that have been monitoring us and subsidized us with information.

So I want to thank our team especially that's been really making a big effort and it's a company that's made by 76,000 people that together delivered these results and have been working tirelessly to continue to deliver this in the 3rd, 4th quarters as well as 24, 25, and 26 with excellent performance. This is what I want to say thank you all.

Have a great day.

Operator:

The Assaí earnings call for the 2nd quarter of 2023 is finished.

The Investor Relations department is available to answer questions and concerns.

We would like to thank all participants and have a good day!