Julia Faga, Itaú BBA:

Hello everyone. Good morning. I'd like to talk about the supply issue you mentioned. What does your inventory look like? Were you expecting to higher your inventory? Because you still have some carryover stock from the winter collection, promotions and you're expecting to sell that in the next season. So, I'd like to have some more color on that because we see that your inventory level is slightly high.

I'd like to have a breakdown of that inventory, how much of that is coming from the fourth quarter, how much is carried over and is there any attempt of putting a mark down for the coming quarters to manage that high level of inventory? That's it, thank you.

Oswaldo Nunes, CEO:

Hello Julia, this is Oswaldo. Thank you for your question. As we mentioned earlier, of course the low sales in December brings pressure to inventory levels for January because it is an important month and it pressured not only same-store sales but also margins.

When you mentioned the winter collection inventories that were carried over, you are correct, and it's always important for us to remember that – and of course, we understand, we look at this as a learning curve coming from 2018 – the imported goods chain, especially the one around winter products, which cannot be met by our local apparel industry, it is a chain where you are gambling 8-9 months ahead, in advance.

As I said in previous quarters, we made a big bet for 2018, of course, whatever is seasonal was addressed, but there is also an important portion of nonperishable jackets or sweatshirts, knitwear, of black, grey, navy blue prints that you have to carryover to 2019, but we understand we need to pay closer attention to that process because that's not good for inventory and it's not good for our financial cycles.

Another lesson learned coming from 2018 is how to work with the seasonality of sales throughout the year, when we compare to a more linear production process of our own clients. Until last year, our policy was to anticipate production of basic products with longer lifecycles, denim, dress, shirts and so on and so forth.

But still we understand that that's not really positive, even if you're talking about different products where you predict sales more accurately, we are still betting in the future and we know that sales might and will vary, then when you get there, at the end of the road, you would not always have the ideal level that you wanted, and that forces you to have a larger carryover.

Again, lessons learned from 2018 that we plan to apply in 2019. And, as we look ahead, we have this work ahead of us of adjusting those mixes, and this is happening now in the first quarter. For the second quarter we only expect to see very residual effect, we should see no impact on margins in a more significant way. That's what we hope for.

Julia Faga, Itaú BBA:

Okay, thank you very much.

Operator:

Next question comes from Helena Vilares, from Bradesco BBI.

Helena Vilares, Bradesco BBI:

Hello everyone, thank you for taking my question. I'd like to first have some more color on the front of initiatives related to Midway Finance, you were approved by the Central Bank, so I'd like to have some more detail on how you see that operation this year, when do you expect the Central Bank to finally approve that?

And the second question has to do with productivity levels. We see that SG&A has been dropping consistently. Could you break that down in terms of lines and initiatives which are generating that operating leverage you mentioned?

And lastly, also in terms of SG&A, we have, for a year, been seeing a transfer of SG&A from retail to finance. Have we reached the base point? Can we expect 2019 to be more normal or should we expect some more transfer that will reflect on the consolidated results? Thank you.

Tulio Queiroz, CFO:

Helena, thank you for your questions. I'll start with the first one relative to Midway. First and foremost, to understand that process, the process by which we will transform our financial into a multiple bank, underneath all that we have the intention of placing customers at the center of our focus. Today, we are talking about a relationship which takes place through our card only, we want to expand that relationship including the possibility of offering bank account, a current account and other products. But most importantly, we are focusing this project on the customer profile that we have today, on the relationship that we have today, people who are today buying at Riachuelo.

The company operates with its own card, that has been there for over 30 years, and basically, all that relationship that the company has with customers comes from the fact that the customer perceives some quality and an environment which is much friendlier than the one offered by the bank environment. But, as we've seen several banks offering digital platforms and new Fintechs, what's happening is that those barriers that existed before brought in relationship or handling relationships between banks and customers they are collapsing. So, today relationship with digital bank is much more friendly and simple, so there is a new type of competition for our card operations, and we are paying close attention to that.

We want to elevate, increase that relationship with our customers, we have 2 operations which are quite mature, in other words, a financial platform with a huge active customer base and retail platform which is extremely wide, comprehensive and spread throughout Brazil.

The idea is that all of that combined will have created an ecosystem where the system will take center stage, as I said. Of course, Newton in the coming quarters will be sharing with you more detail about the development of that specific strategic plan, but in essence, that transformation follows along those lines.

As for your second question relative to productivity levels, here essentially and more importantly, we shouldn't emphasize one or other point, there is no silver bullet that helped dilute by 3 p.p. This is an ongoing work, as I said in my opening remarks, we started doing it in 2014 through a very detailed survey of productivity levels broken down by position, by store cluster and using specific productivity indicators for each one of those positions.

So today, the whole of the retail operation, which of course is the one with the highest demand in terms of personnel, all of that operation is modeled around productivity platforms and with direct connection with the physical volumes that flow through the stores. And we always have benchmarks emerging from those assessments and what we do in practice is to bring in the benchmark, try to understand what's new, what kind of knowledge was created, we discuss feasibility around standardizing a new process and then we replicate that across the organization. That has happened in different ways and in different occasions.

The main operating expenses of the group are: number 1, of course, people ; number 2 occupancy cost, so we are working around expanding the group, relationship with shopping malls, with real estate owners, property owners; and number 3, a deferred operating expense is electric energy, and here too we work around a new operating procedure to implement and we are constantly monitoring that in our stores, the idea is to achieve important savings in terms of consumption because we cannot control price, of course, we have to control consumption.

Those are the main pillars towards productivity. And it is, as I said, an ongoing effort. For the support areas, the same goes. We are constantly conducting surveys conducted by the support areas in terms of pricing, cost, and we're always assessing if those products are really necessary, if they are really contributing to value generating.

The secret, if I may, of this value generation pillar lies exactly there: Discipline in our efforts.

As for your third question concerning the transfer of operating expenses between Midway and Riachuelo, I'd say that the main difference in criteria took place late last year, the 2018 basis squared, so moving forward and not only 2019, but also the basis of comparison for 2018 will also be under control. So, with that we are talking about a pure comparison basis.

I think those are the 3 questions you asked, correct?

Helena Vilares, Bradesco BBI:

Okay, thank you very much.

Operator:

Our next question comes from Felipe Casemiro, from HSBC.

Felipe Casemiro, HSBC:

Good afternoon everyone. Thanks for taking my questions. My first question is about sales. Following up on Oswaldo's comment earlier on, I can think of the same-store sales level for the first quarter is not very much disconnected from the fourth quarter, in other words, a low number but still in the initial of the stock up. So, what can we expect for 2019 in terms of same-store sales given that the first quarter is not that relevant? But can we expect a recovery going forward? So, what do you think about that?

And my second question about results. I'd like to understand non-recurring expenses. You used that in the adjusted EBITDA, so it is clear that R$692 million refers to tax credits , but there is a difference of R$86 million expenses that you also have added to that, so I think that R$50 million financial, R$36 million on retail. I'd like to understand the breakdown of those non-recurring expenses and have a bit more color on that if you will please.

Oswaldo Nunes, CEO:

Thank you Felipe. As for your first question about the same-store sales coming at a low digit, when we look at the second quarter and we look at the recovery coming from inventory levels at the DC so that we can allow stores to bring in as many SKUs as they really demand so we will have SKUs that will be more efficiently allocated, we do believe that we will resume growth for same-store sales at a higher level than the average that we had for last year actually.

Tulio Queiroz, CFO:

Felipe, this is Tulio speaking now. As for your second question about the non-recurring expenses, I will give you a step-by-step disclosure of the main elements.

Let's start with the EBITDA effect. As I mentioned and you also mentioned in your question, the main non-recurring effect comes from the ICMS is PIS/COFINS, the main volume produced an effect of R$684 million. On top of that, we made a provisioning to pay lawyer fees concerning that case, a tax suit. Another non-recurring expense was a credit coming from employees.

As for the PIS/COFINS issue, what we also did was that we aligned the SELIC rates associated with that topic, and that had an impact on the financial results. So, R$684 million, as I said, for EBITDA plus R$483 million and the financial revenues lines which have to be with the update of the SELIC rates. Of course, this will generate PIS/COFINS, I'm not going to go into all the minutia.

So, totally, the EBITDA effect that I mentioned R$655 million and the total effect for the financial result at R$460 million, as I mentioned, and net profit R$ 795 million.

As for the Midway Finance specifically, what we did was that we did a PDD adjustment of R$60 million relative to the classification of clients and the risk base. This has to do with internal controls and risk controls that we routinely execute. So, any fine tuning that is needed leads to an adjustment in those numbers. On top of that, we have a positive adjustment for operating expenses referred to charge back or cancellations made using the branded card. So, for EBITDA the effect is negative, at R$49 million.

In the net income line, we have an additional effect which has to do with the change in the rate of social contribution, which was changed for financial institutions. At the end of the year, we moved from 20% to 15% starting in 2019. So, in practice, all the nondeductible expenses we use a 20% rate. When we change the rate and we change the year, we need to revert the base. So that's good news actually, that will affect results in the short run.

So once again, that affected the income tax of line by R$30 million. As I said, impacts in 2019 the company will benefit because we will have a contribution rate, which will be 5% lower.

If we add all these effects together, EBITDA, as I said, R$606 million, in the financial results an effect of R$460 million and for net income the effect is of R$737 million.

Felipe Casemiro, HSBC:

Okay, thank you. And, if I may, one final follow-up about e-commerce, I'd like to understand your strategy a little more, I'd like to understand for the year what is in your mind in terms of pick-and-collect and other omnichannel initiatives, and if you are working with the idea of using some kind of marketplace platform to increase your reach. That is my final question, thank you.

Oswaldo Nunes, CEO:

Felipe, our strategy for the digital channel is the following: We think that the natural way to go is to have a full-fledged, robust digital platform, a very low level of inefficiency that is able to maximize flows and especially conversion of average tickets. We are now investing on that. At the same time, the idea is to strengthen all omnichannel initiatives. The pick-and-collect is present in all stores varying from 25% to 30% depending on the month, but on average, surprisingly, there are a couple stores where that number is above 50%, quite impressively, because of location, different flows, easier access, the strength of the brand, that all contributed to boost that number in same stores.

And the question about marketplace platform, that's something we are discussing right now, trying to understand it a little better, trying to know what kind of competition that represents, trying to identify opportunities in those new ecosystems. We know that with that comes along a new challenge of how to better position the brand in a platform such as that.

As about becoming a marketplace, that is for the future, but looking at what we already have today, if we could offer the reach of our physical network to other retailers or other industries that could be an opportunity, yes. But that's something we will be discussing in the future. We are now trying to understand the specificities and trying to identify opportunities.

Felipe Casemiro, HSBC:

Thank you, have a nice day.

Operator:

The Q&A session is now over. I'd like to turn the conference over to Mr. Queiroz, CFO, for his final remarks.

Tulio Queiroz, CFO:

Thank you very for participating in our call. Just to make sure we remain available for other comments or questions you may have. Thank you again, have a nice day everyone.

Operator:

Thank you. Guararapes Riachuelo conference call to discuss results is now over. Please, you may disconnect your lines now and have a nice day.