BRAZIL RETAIL & CONSUMER GOODS / ECONOMICS

SEPARATING THE WHEAT FROM THE CHAFF: A SECTOR-DETAILED SENSITIVITY ANALYSIS FOR 2016

DOWNGRADING CBD AND VIA VAREJO; LOWERING YE2016 TARGET PRICES

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Net/Net: In light of the recent GDP estimate revisions by the market, we ran a sensitivity analysis on the potential sales performance of each retail segment in 2016 under three different scenarios. Our results show that the pharmaceutical category has the most favorable outlook; we have set HYPE3 as our new Top Pick and RADL3 as the second best option. In addition, despite the challenging environment for apparel, we still like LREN3 due to its strong retail execution. We also concluded that food retail may not be as resilient as we had thought, and we are downgrading PCAR4 to Hold from Buy. Lastly, we think durable goods should continue to be the lowlight, and we are downgrading VVAR11 to Underperform.

- **Digging deeper into each retail segment.** The recent round of releases of economic activity indicators confirmed a deep and persistent recession in Brazil. The shrinkage in retail sales has played an important role, and we do not expect a reversal of the retail downtrend in the short term, in-line with the expected further deterioration in labor market conditions, tightening of credit markets, and a political and economic environment full of uncertainties. Nevertheless, the different retail segments show varying responses to the dynamics of consumption fundamentals, in terms of magnitude and intensity, which means they require separate analysis, in our view.
- **Pharmaceutical segment—the most favorable outlook: high conviction on HYPE3 (our new Top Pick) and positive view on RADL3 reinforced.** Our exercise shows that pharmaceutical goods should perform better than other categories. Unless we see a significant additional downward revision in GDP estimates (to -6%), we believe market volume should increase in 2016. With GDP falling 3.7% (Santander's official estimate for 2016), for example, pharmaceuticals would be the only category to show positive sales growth (+1.2% YoY). *We remain positive on RADL3 and HYPE3, and we are setting HYPE3 as our new Top Pick.* Regarding apparel, we forecast a sales decline in 2016, yet less than in 2015, even in the bear-case scenario. *We remain positive on LREN3 given its superior execution and market share gains.* We recognize that the stock lacks a short-term catalyst, but we expect investor concerns on higher delinquency to be reduced as ongoing initiatives to improve consumer finance results bear fruit.
- **Food retail is less resilient than it looks; we downgrade PCAR4 to Hold from Buy, with a new YE2016 target price of R$50/share.** Based on our sensitivity analysis for 2016, we observe that the food retail market may not be as resilient as it looks (-2.8% growth with an estimated GDP of -3.7%). In our view, *CBD may continue to experience some difficulties* in offsetting changes in consumer behavior and market share losses. We see positively the company's efforts to expand its cash & carry footprint, yet it may continue to struggle with poor sales performance in super/hypermarkets (~65% of total sales at CBD Food) as well as at its subsidiaries Via Varejo and Cnova. **We also revised estimates for VVAR11 and downgraded the stock to Underperform (new YE2016 target price of R$3.70/share)** given the challenging sales outlook for discretionary goods in Brazil, which is also one of the main conclusions of our sensitivity analysis.

A SECTOR-DETAILED SENSITIVITY ANALYSIS FOR 2016

We ran a sensitivity analysis in partnership with **Santander's Macro Research team** and found that retailers will likely post very different sales growth results depending on each business segment. In order to run the exercise, we designed three scenarios—A, B, and C—with different parameters for 2016E GDP growth, ranging from -2% to -6%. Our main conclusions are as follows (see pages 3–5 for more details):

1. **Stick to pharma's resilience—Hypermarcas is our new Top Pick, and we also like RADL3**
2. **Food retail is less resilient than it looks—Downgrading CBD to Hold**
3. **Don't expect a quick turnaround for durables—Downgrading VVAR to Underperform**
4. **Apparel goods still expected to suffer, yet less than in 2015—We still like Lojas Renner**

Figure 1. Retail Market Analysis for 2016—Sensitivity Analysis of Three Main Macro Scenarios (% YoY)

Category	2014	2015	2016E—Scenarios		
			A	B	C
GDP	**0.1%**	**-3.8%***	**-2.0%**	**-3.7%**	**-6.0%**
Retail – Core Index	**2.2%**	**-4.3%**	**-1.3%**	**-3.5%**	**-6.2%**
Food retail	1.3%	-2.5%	-0.6%	-2.8%	-4.5%
Apparel	-1.1%	-8.7%	-2.7%	-5.2%	-7.7%
Pharmaceuticals	9.0%	3.0%	2.5%	1.2%	-2.3%
Furniture & Electronics	0.6%	-14.0%	-4.2%	-8.0%	-13.3%

*Santander estimated GDP for 2015. Sources: IBGE (PMC – Commerce Monthly Survey) and Santander estimates.

MACRO OVERVIEW

The recent round of releases of economic activity indicators confirmed a deep and persistent recession in Brazil, and we see no consistent signs of a reversal of the negative trend for most consumption and investment drivers in the coming quarters. Indeed, we believe some stabilization of economic activity will come only by the end of this year, which supports *our base-case scenario, in which real GDP is forecast to shrink nearly 4% in 2016, as occurred in 2015.*

According to our estimates, private consumption should subtract 2.2 pp from GDP this year, reflecting the worsening of labor market conditions, tightening of credit markets, and an economic and political environment full of uncertainties. Looking at the labor market, the unemployment rate should climb to 13% in 2016 from 10% in 2015 (eop, seasonally adjusted), according to our projections, driven by the widespread decline in the employment level across productive sectors and a faster growth in the labor force. With this, real aggregate wages should continue to shrink, heavily affecting retail sales, in our view.

Even assuming the monetary easing we foresee in the 2H16, we forecast that real interest rates should tend to remain high, which also undermines household consumption, particularly in the durable goods segment. Furthermore, we expect the turmoil in the macro environment (dismal performance of fiscal accounts and uncertainties about economic policymaking, among others) to keep consumer confidence at very low levels, postponing the recovery of retail-related segments.

Regarding the alternative scenarios, we assign a slightly higher probability to the pessimistic case (GDP -6%), which has assumptions such as a low commitment to fiscal adjustment, intensification of political instability, and a hard landing for China's economy (and high contagion to other countries). In contrast, the optimistic case (GDP -2%) assumes factors such as a rapid reduction in the risk perception of the Brazilian economy and an improvement in external demand. (See Figures 2 and 3 for details.)

Figure 2. Different Macro Assumptions for Each Scenario Designed for the Retail Sensitivity Analysis

Scenario	A	B	C
GDP	-2.0%	-3.7%	-6.0%
Unemployment (average)	10.2%	11.5%	12.7%
Unemployment (eop sas)	11.4%	12.8%	14.0%
Employed Population	-0.6%	-2.3%	-3.8%
Aggregate Real Wages	-2.4%	-4.6%	-6.7%

Source: Santander estimates.

Figure 3. We Identified Different Coefficients for Segments, based on Wages and Interest Rates in Brazil

Segment	Real Wages	Real Interest Rate
Retail	**0.5325**	**-0.0245**
Food retail	0.5482	-
Apparel	0.4391	-
Pharmaceuticals	0.2804	-
Furniture & Electronics	0.4518	-0.0836

Source: Santander estimates.

It is also important to notice different regression coefficient estimates generated by our statistical models for wage growth and interest rates in the country. The results underscore our thesis that sales of pharmaceutical and CF&T goods do not vary much with changes in wages, which supports our belief that the segment might be more resilient than the others. In contrast, furniture and electronics present a direct relationship with wages, yet an inverse relationship with interest rates: here, we first assumed that interest rates would affect discretionary business, and the results of our analysis show that high interest rates do affect the sales performance of durable goods, for instance.

Drawing Conclusions

#1: Stick to Pharma's Resilience—Hypermarcas Is Our New Top Pick

Taking into consideration the scenarios illustrated in Figure 1, we can see that no segment is wholly immune in times of macro turmoil. Nevertheless, our analysis indicates that even if there is a further deterioration in macro indicators—such as GDP, unemployment rate, and real wage growth—*the group of pharmaceutical and CF&T goods* (cosmetics, fragrances, and toiletries) performs better relative to other categories. We recognize that the definition of this group is quite broad and comprises different products with distinct demand elasticity; nonetheless, unless we see a significant additional downward revision to GDP estimates (to -6%, which is unlikely, in our view), market volume tends to increase in 2016, according to our base-case scenario, benefiting from (i) mix resilience—people taking care of their health, (ii) aging of the population, (iii) still lower consumption per capita, and (iv) easier access to information and treatments available on the market.

Thus, we believe that retailers and other companies exposed to the dynamics of the pharmaceutical business are the best vehicles for being in the market in 2016. Based on that outlook, we take the opportunity to set *Hypermarcas (HYPE3) as our new Top Pick* in the retail & consumer goods sector. We also have a *positive view on Raia Drogasil (RADL3)*, and the main reason we do not set the stock as our Top Pick is the already expensive valuation levels where it currently trades. We maintain Buy recommendations on both stocks, as we believe these companies should be able to successfully navigate the current turbulent waters in Brazil.

#2: Food Retail Less Resilient than It Looks—Downgrading CBD to Hold

On the surface, it is possible to assume that the food retail market has some resilience, though to a lesser extent than pharmaceuticals. Using a more in-depth analysis, however, *we think the segment has limited room for growth in 2016, mostly affected by (i) consumers' smaller "shopping baskets", and (ii) the down-trade phenomenon.* Besides reducing consumption—especially on superfluous goods—shoppers tend to migrate to cheaper brands when inflation hits their pocketbooks. As a consequence, sales growth in real terms is somewhat affected by down-trading, and we expect this scenario to persist throughout the year. As we discussed in our report *Change in Consumer Behavior: Shopping with Less Money* (March 31, 2015), down-trade behavior has been noted in developed markets during recessions, as consumers try to save money, and we believe that the same pattern can be expected in emerging markets.

On the flip side, we recognize that the cash & carry format still has room for growth and is not a temporary wave, being one of the best segments to invest in, in our view. More recently, the format has become stronger and more advantageous for monthly shopping, filling the space formerly taken up by hypermarkets (no longer recognized as the ultimate low-cost type of store).

Regarding specific stocks, we believe that CBD (PCAR4) has experienced some difficulties in adapting operations to the new consumer behavior. We remain positive on the company's efforts to expand its cash & carry and proximity stores footprint, yet CBD continues to struggle with sales performance in super/hypermarkets (still 65% of total food division sales). *We are downgrading PCAR4 to Hold from Buy and lowering our YE2016 Target Price to R$50/share* based on our concerns about sales recovery and results from CBD's subsidiaries (VVAR and Cnova). (For more details, see page 6).

#3: Don't Expect a Quick Turnaround for Durables—Downgrading VVAR to Underperform

The so-called "Brazilian middle-class boom" seen in the last decade supported high consumption levels until 2013-14. This was particularly true for durable goods manufacturers and retailers, which also benefited from industry tax incentives that ultimately allowed more affordable prices of electronics, for instance. In our view, the aforementioned development is the most vulnerable in a macro slowdown, given the discretionary nature of these products. Thus, the segment of furniture, electronics, and home appliances will likely continue to be the most negatively affected by deteriorating macro indicators, in our view, and may continue to post double-*digit sales declines in a deeper recession scenario. We have revised our estimates for VVAR11 and downgraded the stock to Underperform. We set our new YE2016 target price at R$3.70/share.* (For more details, see page 8.)

#4: Apparel Goods Still Expected to Suffer, Yet Less than in 2015—We Still Like Lojas Renner

In 2015, apparel retailers experienced a sharp decline in profitability levels. Based on our assumptions, *apparel companies will likely continue to experience sales declines, but with a smoother impact on a YoY basis.* Even in scenario C, where we use deeper recession parameters (as shown in Figure 2*)*, the scenario does not worsen. However, this does not mean it will improve and recover in 2016; indeed, we do not expect any recovery until mid-2017.

Given the current environment, *we see Lojas Renner (LREN3) as one of the best-positioned retailers in the market, with substantial room to capture market share gains* through (i) an improved value proposition over the past few years, (ii) benefits from push & pull logistics, including gross margin gains and lower inventory levels, and (iii) capturing share from retailers struggling with low working capital and some that are going into bankruptcy. Our positive view on the name is also predicated on the company's strong balance sheet position and proven track record in the retail business. Concerns regarding Consumer Finance results do exist, but we believe Lojas Renner is well positioned to offset high delinquency and funding costs by (i) improving revenue growth through a healthier credit portfolio, high collection rates, and high interest rates on late payments, as well as (ii) lowering operating expenses YoY.

CBD

HOLD

LIMITED VISIBILITY AND NO SHORT-TERM TRIGGERS

CURRENT PRICE: R$41.35
TARGET PRICE: R$50.00

DOWNGRADING RATING TO HOLD FROM BUY
LOWERING YE2016 TARGET PRICE TO R$50.00 FROM R$66.00

Net/Net: We believe that CBD has experienced some difficulties in adapting its operations to new consumer behavior—intensified down-trading, price sensitivity, and smaller shopping baskets (i.e., less disposable income). Although we remain positive on the company's efforts to expand its cash & carry and proximity stores footprint, CBD continues to struggle with sales growth in hypermarkets, postponing the recovery initially expected for 2H15. In addition, our analysis shows that the food retail segment is not as resilient as we initially expected. Our rating downgrade and target price reduction are based on concerns about (i) sales and margins recovery, and (ii) results from CBD's subsidiaries (VVAR and Cnova) in 2016.

- Sales reignition at hypermarkets is still the biggest challenge. We acknowledge the importance for CBD of its package of operating initiatives for traffic/sales improvement, especially in a challenging macro scenario. However, we have become more conservative on when exactly all the efforts will lead to sustainable improvements (postponing the recovery initially expected for 2H15). Meanwhile, we see CBD struggling to gain share over competitors, even though some players are shutting down stores (Wal-Mart is closing 60 locations, accounting for ~5% of local sales).

- Margins may have reached their peak in 2014. In our view, recent efforts to reignite sales growth (increase SSS and productivity levels) through promotional efforts could continue to pressure margins. Moreover, we think initiatives to control SG&A expenses on the corporate level may not be enough to fully offset commercial aggressiveness in the near term. Additionally, inflationary pressures may keep weighing on profitability, in our opinion. Thus, we expect EBITDA for CBD Food to rise "only" 5% YoY, leading to 20-bp EBITDA margin compression in 2016.

- Durable goods—underdogs for a while longer. In a nutshell, we think CBD's consolidated figures should experience additional pressures—on both top-line and margins dynamics—from its invested companies, Via Varejo and Cnova, given the vulnerability of their sales mix in a macro slowdown. Sales of durable goods in hypermarkets are not in a good place either, with a possible double-digit deceleration YoY, according to our projections.

Estimates & Valuation Ratios

(R$)	2014A	2015E	2016E	2017E
P/E	20.6	22.3	17.6	10.3
FV/EBITDA	6.4	5.5	6.8	5.3
FCF Yield (%)	18.6	(19.2)	4.3	7.6
Div Yield (%)	1.0	2.8	0.7	1.2
Net Debt/EBITDA	(0.3)	0.9	1.8	1.4

Sources: FactSet, Santander estimates and company reports.

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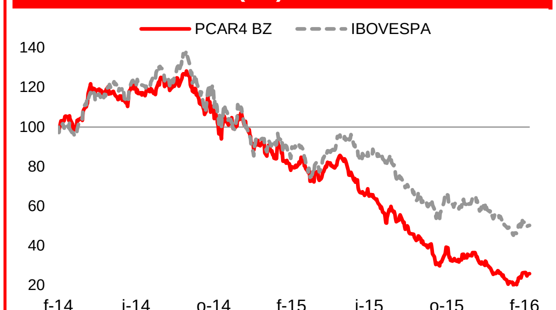
Company Statistics

Bloomberg	PCAR4 BZ
Current Price (02/15/16)	R$ 41.35 / US$ 10.36
Target Price (YE 2016)	R$ 50.00 / US$ 12.80
52-Week Range (R$)	32.90 - 102.69
Market Capitalization (US$ Mn)	2,753
Float (%)	58.7
3-Mth Avg. Daily Vol (US$ Mn)	11.9
Shares Outstanding - Mn	266

Price Performance (R$)



Sources: FactSet, Santander estimates and company reports.

CBD

Financial Highlights: P&L, Balance Sheet and CF Statement, 2014–17E in Millions

	R$				US$			
P&L ACCOUNT	**2014A**	**2015E**	**2016E**	**2017E**	**2014A**	**2015E**	**2016E**	**2017E**
Total Revenue	65,526	69,116	70,910	76,323	27,841	20,746	21,285	18,391
YoY change (%)	13.3	5.5	2.6	7.6	3.9	(25.5)	2.6	(13.6)
Gross Profit	16,947	16,358	16,361	17,753	7,201	4,910	4,911	4,278
YoY change (%)	12.2	(3.5)	0.0	8.5	2.8	(31.8)	0.0	(12.9)
EBITDA	5,370	3,409	3,478	4,416	2,282	1,023	1,044	1,064
YoY change (%)	19.7	(36.5)	2.0	27.0	9.7	(55.2)	2.0	1.9
As % of Revenue	8.2	4.9	4.9	5.8	8.2	4.9	4.9	5.8
Operating Income	4,002	1,920	2,286	3,191	1,700	576	686	769
YoY change (%)	35.8	(52.0)	19.1	39.6	24.5	(66.1)	19.1	12.0
As % of Revenue	6.1	2.8	3.2	4.2	6.1	2.8	3.2	4.2
Financial Results	(1,507)	(1,542)	(1,566)	(1,591)	(640)	(463)	(470)	(383)
Taxes	(734)	(136)	(190)	(433)	(312)	(41)	(57)	(104)
Net Profit	1,271	498	625	1,068	540	150	188	257
YoY change (%)	20.7	(60.8)	25.5	70.9	10.7	(72.3)	25.5	37.2
As % of Revenue	1.9	0.7	0.9	1.4	1.9	0.7	0.9	1.4
CASH FLOW	**2014A**	**2015E**	**2016E**	**2017E**	**2014A**	**2015E**	**2016E**	**2017E**
Depreciation & Amortization	(925)	(1,104)	(1,192)	(1,225)	(393)	(331)	(358)	(295)
Other Noncash Items	(1,861)	(3,282)	(3,484)	(701)	(791)	(985)	(1,046)	(169)
Changes in Working Capital	3,611	(1,341)	(4)	(33)	1,534	(403)	(1)	(8)
Operating Cash Flow	3,946	(3,021)	(1,670)	1,560	1,677	(907)	(501)	376
Capital Expenditures	(1,165)	(1,306)	(1,344)	(1,428)	(495)	(392)	(404)	(344)
Free Cash Flow	4,876	(2,138)	470	834	2,072	(642)	141	201
Other Invest./(Divestments)	0	0	0	0	0	0	0	0
Change in Debt	234	(1,093)	0	0	99	(328)	0	0
Dividends	(258)	(315)	(73)	(133)	(110)	(95)	(22)	(32)
Capital Increases/Other	0	0	0	0	0	0	0	0
BALANCE SHEET	**2014A**	**2015E**	**2016E**	**2017E**	**2014A**	**2015E**	**2016E**	**2017E**
Cash and Equivalents	11,149	5,414	2,327	2,327	4,197	1,386	596	554
Current Assets	24,133	21,004	18,607	19,679	9,086	5,379	4,765	4,685
Fixed Assets	21,367	22,720	22,872	23,074	8,044	5,818	5,857	5,494
Total Assets	45,500	43,724	41,479	42,752	17,130	11,197	10,623	10,179
Current Liabilities	23,848	22,763	23,450	24,488	8,978	5,829	6,005	5,831
Long-Term Liabilities	7,170	8,274	8,274	8,274	2,699	2,119	2,119	1,970
Shareholders' Equity	10,580	9,082	6,150	6,385	3,983	2,326	1,575	1,520
Total Financial Debt	9,728	8,635	8,635	8,635	3,662	2,211	2,211	2,056
ST Debt	6,594	4,246	4,246	4,246	2,482	1,087	1,087	1,011
LT Debt	3,134	4,389	4,389	4,389	1,180	1,124	1,124	1,045
FINANCIAL RATIOS	**2014A**	**2015E**	**2016E**	**2017E**	**2014A**	**2015E**	**2016E**	**2017E**
Net Debt	(1,421)	3,221	6,308	6,308	(535)	825	1,615	1,502
Capital Employed	21,652	20,961	18,029	18,264	8,151	5,368	4,617	4,349
Net Debt/EBITDA	(0.3)	0.9	1.8	1.4	(0.2)	0.8	1.5	1.4
Net Debt/Equity	(0.1)	0.4	1.0	1.0	(0.2)	0.4	1.0	1.0
Capex/Revenue (%)	1.8	1.9	1.9	1.9	1.8	1.9	1.9	1.9
Int Cover (%)	(7.8)	(4.0)	(5.5)	(7.3)	(7.8)	(4.0)	(5.5)	(7.3)
Dividend Payout (%)	24.5	24.8	14.6	21.2	22.5	17.5	12.1	21.0
ROCE (%)	21.9	9.8	13.7	19.8	24.3	11.5	13.9	19.8
ROE (%)	12.7	5.1	8.2	17.0	13.5	4.8	8.2	17.0
MARKET RATIOS	**2014A**	**2015E**	**2016E**	**2017E**	**2014A**	**2015E**	**2016E**	**2017E**
P/E	20.6	22.3	17.6	10.3	18.2	18.8	14.7	10.7
P/CE	11.9	6.9	6.0	4.8	10.5	5.8	5.0	5.0
FV/EBITDA	6.4	5.5	6.8	5.3	5.7	4.6	5.7	5.5
FV/EBIT	8.6	9.8	10.4	7.4	7.6	8.2	8.7	7.6
FV/Revenue	0.5	0.3	0.3	0.3	0.5	0.2	0.3	0.3
P/BV	2.5	1.2	1.8	1.7	2.5	1.2	1.7	1.8
FCF Yield (%)	18.6	(19.2)	4.3	7.6	21.0	(22.8)	5.1	7.3
Div Yield (%)	1.0	2.8	0.7	1.2	1.1	3.4	0.8	1.2
PER SHARE DATA	**2014A**	**2015E**	**2016E**	**2017E**	**2014A**	**2015E**	**2016E**	**2017E**
EPS	4.79	1.87	2.35	4.02	2.04	0.56	0.71	0.97
DPS	0.97	1.19	0.27	0.50	0.41	0.36	0.08	0.12
BVPS	39.88	34.18	23.15	24.03	15.01	8.75	5.93	5.72

Notes: EBITDA is adjusted and net profit is to controllers.

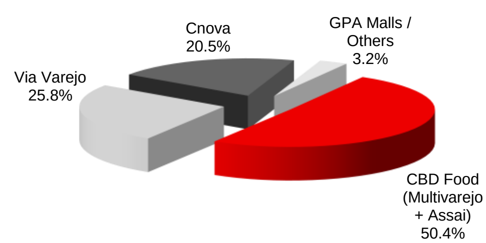
Company Description

Companhia Brasileira de Distribuição (CBD) is Brazil's largest multibrand, multichannel retailer, with net sales of R$65.5 billion in 2014. CBD Food (R$34.7 billion in sales) is the largest food retailer in the country, with 909 stores (3Q15), including hypermarkets (Extra), supermarkets (Pão de Açúcar and Extra), cash & carry (Assai), and proximity stores (MiniMercado Extra), as well as gas stations and drugstores. Through its 43% stake in Via Varejo, CBD is also the largest retailer of white goods, electronics, and furniture in the country, with ~1,000 stores (3Q15). Global e-commerce (Cnova) sales amounted to €4.5 billion, which helped position the company as the second largest player in Brazil. CBD is controlled by French retailer Groupe Casino.

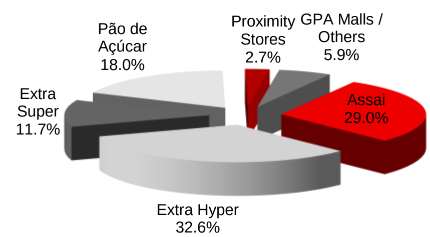
Key Personnel: Jean-Charles Naouri (Chairman), Ronaldo Iabrudi (CEO), Christophe Hidalgo (CFO) and Daniela Sabbag (Investor Relations Officer)

Web: www.gpabr.com

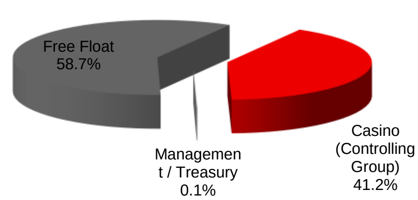
Sales Breakdown, 3Q15



CBD Food Breakdown, 3Q15



Shareholder Structure, Current



Sources for all charts and tables: Company reports and Santander estimates.

VIA VAREJO

FUNDAMENTALS DO NOT SUPPORT RECENT STOCK OUTPERFORMANCE

UNDERPERFORM

CURRENT PRICE: R$4.15
TARGET PRICE: R$3.70

DOWNGRADING RATING TO UNDERPERFORM FROM HOLD
LOWERING YE2016 TARGET PRICE TO R$3.70 FROM R$3.80

Net/Net: Based on our sensitivity analysis of the main retail segments in Brazil, we are tweaking estimates for VVAR. We believe furniture/electronics should remain the retail categories most hurt by deteriorating macro indicators, and they may continue to post double-digit sales declines in a deeper recession scenario. In our view, the company is making reasonable decisions to improve traffic in stores and maintain its leadership position in the market, but we are skeptical about the positive effects of recent measures such as commercial/marketing efforts, which are coming at the price of margins. Also, recent price action (+46% YTD) leaves no upside potential, in our view, which supports our downgrade.

- Intense promotional efforts only a palliative. We recognize that a sales recovery at Via Varejo may depend on a more aggressive pricing strategy to offer products that can fit the consumer's smaller pocketbook in 2016. This strategy seems sensible, in our view, but we expect margins to remain under pressure and SSS to stay in negative territory. We estimate a top-line decline of 6.8% YoY, along with 150-bp gross margin compression. We think SG&A expenses dilution may be limited on the weak sales dynamics, leading to an 22.1% YoY EBITDA decline and 100-bp EBITDA margin compression for 2016E.

- What else to expect for 2016? As management stated at the Investor Day in December 2015, VVAR's key focus will be: (i) improving sales in 2016; and (ii) maintaining a solid cash position. The main strategy will rely on a more aggressive pricing policy, but management noted the team is also working to increase service levels to clients, reduce ruptures in logistics/supply management, shorten lead times, and regionalize its pricing strategy.

- Our sensitivity analysis supports a more conservative approach. According to our exercise on the impact of GDP downward revisions on each retail segment, durable goods is the most affected category given slower economic activity (-8% YoY growth for a GDP of -3.7%). We continue to see a challenging scenario, which prevents us from taking a more bullish view on VVAR in the short term.

Estimates & Valuation Ratios

(R$)	2014A	2015E	2016E	2017E
P/E	9.7	6.8	23.1	14.1
FV/EBITDA	3.6	1.9	4.0	3.3
FCF Yield (%)	10.5	(137.6)	3.6	3.3
Div Yield (%)	(0.0)	15.8	(0.0)	(0.0)
Net Debt/EBITDA	(0.3)	0.8	2.1	1.7

Sources: FactSet, Santander estimates and company reports.

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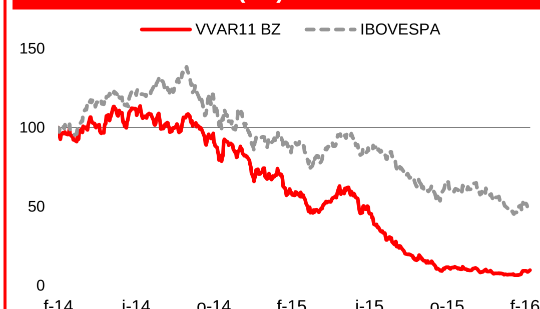
Company Statistics

Bloomberg	VVAR11 BZ
Current Price (02/15/16)	R$ 4.15 / US$ 1.04
Target Price (YE 2016)	R$ 3.70 / US$ 0.95
52-Week Range (R$)	2.90 - 19.75
Market Capitalization (US$ Mn)	448
Float (%)	29.3
3-Mth Avg. Daily Vol (US$ Mn)	1.0
Shares Outstanding - Mn	430

Price Performance (R$)



Sources: FactSet, Santander estimates and company reports.

VIA VAREJO

Financial Highlights: P&L, Balance Sheet and CF Statement, 2014–17E in Millions

	R$				US$			
P&L ACCOUNT	**2014A**	**2015E**	**2016E**	**2017E**	**2014A**	**2015E**	**2016E**	**2017E**
Total Revenue	22,674	19,267	17,957	18,686	9,634	5,783	5,390	4,503
YoY change (%)	4.2	(15.0)	(6.8)	4.1	(4.5)	(40.0)	(6.8)	(16.5)
Gross Profit	7,354	6,173	5,472	5,736	3,125	1,853	1,643	1,382
YoY change (%)	9.8	(16.1)	(11.3)	4.8	0.6	(40.7)	(11.3)	(15.8)
EBITDA	2,250	1,180	919	1,119	956	354	276	270
YoY change (%)	26.3	(47.6)	(22.1)	21.8	15.8	(63.0)	(22.1)	(2.2)
As % of Revenue	9.9	6.1	5.1	6.0	9.9	6.1	5.1	6.0
Operating Income	2,090	840	685	887	888	252	205	214
YoY change (%)	(6.0)	(59.8)	(18.5)	29.6	(13.8)	(71.6)	(18.5)	4.0
As % of Revenue	9.2	4.4	3.8	4.7	9.2	4.4	3.8	4.7
Financial Results	(679)	(597)	(564)	(714)	(288)	(179)	(169)	(172)
Taxes	(475)	(96)	(43)	(46)	(202)	(29)	(13)	(11)
Net Profit	926	208	77	127	393	62	23	31
YoY change (%)	30.2	(77.5)	(62.9)	64.2	19.4	(84.1)	(62.9)	31.8
As % of Revenue	4.1	1.1	0.4	0.7	4.1	1.1	0.4	0.7
CASH FLOW	**2014A**	**2015E**	**2016E**	**2017E**	**2014A**	**2015E**	**2016E**	**2017E**
Depreciation & Amortization	(179)	(233)	(234)	(232)	(76)	(70)	(70)	(56)
Other Noncash Items	0	(12)	(132)	(23)	0	(4)	(40)	(6)
Changes in Working Capital	738	(1,255)	2	(75)	314	(377)	1	(18)
Operating Cash Flow	1,853	(887)	182	261	787	(266)	55	63
Capital Expenditures	(601)	(314)	(182)	(261)	(255)	(94)	(55)	(63)
Free Cash Flow	940	(1,936)	65	60	399	(581)	19	14
Other Invest./(Divestments)	0	0	0	0	0	0	0	0
Change in Debt	(257)	(657)	0	0	(109)	(197)	0	0
Dividends	0	(222)	0	0	0	(67)	0	0
Capital Increases/Other	0	0	0	0	0	0	0	0
BALANCE SHEET	**2014A**	**2015E**	**2016E**	**2017E**	**2014A**	**2015E**	**2016E**	**2017E**
Cash and Equivalents	4,448	2,157	1,125	1,125	1,675	553	288	268
Current Assets	10,717	8,409	7,401	7,603	4,035	2,154	1,895	1,810
Fixed Assets	5,287	5,713	5,660	5,688	1,990	1,463	1,449	1,354
Total Assets	16,004	14,122	13,061	13,291	6,025	3,616	3,345	3,165
Current Liabilities	9,719	7,563	7,589	7,716	3,659	1,937	1,944	1,837
Long-Term Liabilities	1,570	1,746	1,746	1,746	591	447	447	416
Shareholders' Equity	4,715	4,813	3,726	3,829	1,775	1,233	954	912
Total Financial Debt	3,706	3,049	3,049	3,049	1,395	781	781	726
ST Debt	3,409	2,525	2,525	2,525	1,283	647	647	601
LT Debt	297	524	524	524	112	134	134	125
FINANCIAL RATIOS	**2014A**	**2015E**	**2016E**	**2017E**	**2014A**	**2015E**	**2016E**	**2017E**
Net Debt	(742)	892	1,924	1,924	(279)	228	493	458
Capital Employed	6,285	6,559	5,472	5,575	2,366	1,680	1,401	1,327
Net Debt/EBITDA	(0.3)	0.8	2.1	1.7	(0.3)	0.6	1.8	1.7
Net Debt/Equity	(0.2)	0.2	0.5	0.5	(0.2)	0.2	0.5	0.5
Capex/Revenue (%)	2.7	1.6	1.0	1.4	2.7	1.6	1.0	1.4
Int Cover (%)	(6.3)	(2.9)	(2.2)	(3.0)	(6.3)	(2.9)	(2.2)	(3.0)
Dividend Payout (%)	0.0	24.0	0.0	0.0	0.0	16.9	0.0	0.0
ROCE (%)	40.8	14.3	13.3	16.7	45.1	16.6	13.4	16.7
ROE (%)	21.4	4.4	1.8	3.4	22.8	4.2	1.8	3.4
MARKET RATIOS	**2014A**	**2015E**	**2016E**	**2017E**	**2014A**	**2015E**	**2016E**	**2017E**
P/E	9.7	6.8	23.1	14.1	8.5	5.7	19.3	14.7
P/CE	8.1	3.2	5.7	5.0	7.2	2.7	4.8	5.2
FV/EBITDA	3.6	1.9	4.0	3.3	3.2	1.6	3.4	3.4
FV/EBIT	3.9	2.7	5.4	4.2	3.5	2.3	4.6	4.2
FV/Revenue	0.4	0.1	0.2	0.2	0.3	0.1	0.2	0.2
P/BV	1.9	0.3	0.5	0.5	1.9	0.3	0.5	0.5
FCF Yield (%)	10.5	(137.6)	3.6	3.3	11.9	(163.4)	4.3	3.2
Div Yield (%)	(0.0)	15.8	(0.0)	(0.0)	(0.0)	18.7	(0.0)	(0.0)
PER SHARE DATA	**2014A**	**2015E**	**2016E**	**2017E**	**2014A**	**2015E**	**2016E**	**2017E**
EPS	2.15	0.48	0.18	0.29	0.91	0.15	0.05	0.07
DPS	0	0.52	0	0	0	0.15	0	0
BVPS	10.96	11.19	8.66	8.90	4.13	2.86	2.22	2.12

Notes: Adjusted EBITDA and net profit figures.

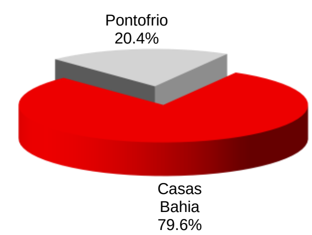
Company Description

Via Varejo is currently the largest electronics and furniture retailer in Brazil, with annual gross sales of R$25.7 billion in 2014. The company sells a wide variety of electronic goods, home appliances and furniture through a multichannel platform that includes more than 1,000 stores (3Q15) under Casas Bahia and Ponto Frio banners. The company also has e-commerce operations through Cnova (controlled by Casino through CBD).

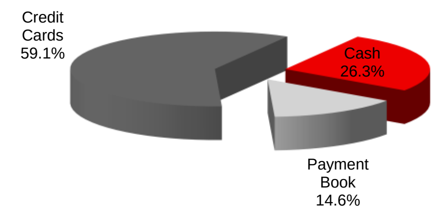
Key Personnel: Ronaldo Iabrudi (Chairman), Peter Estermann (CEO), Felipe Negrão (CFO) and Marcelo Rizzi (IRO & Strategic Planning)

Web: www.viavarejo.com.br

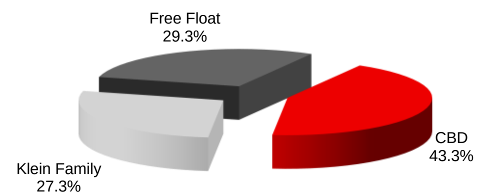
Sales Breakdown, 3Q15



Sales by Payment Type, 3Q15

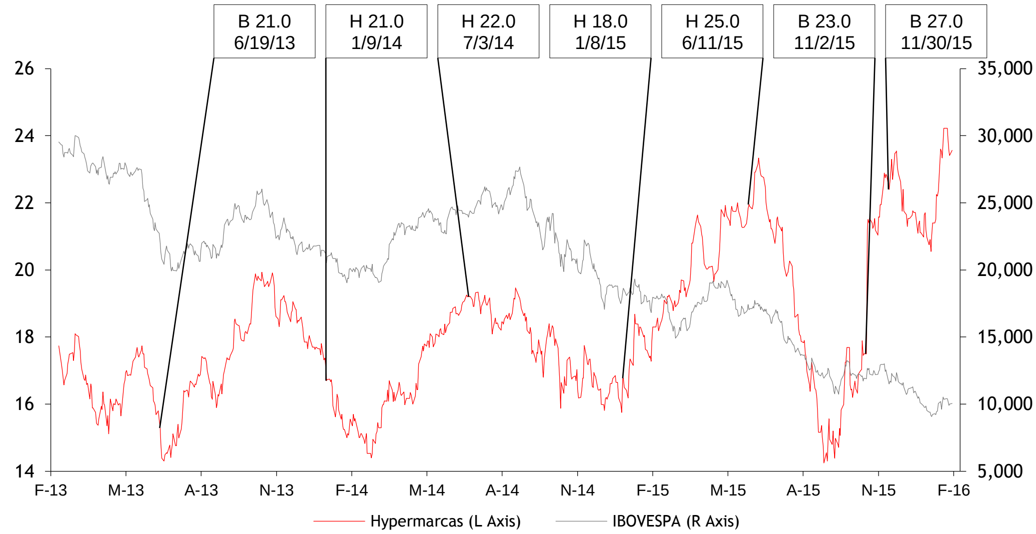


Shareholder Structure, Current



Sources for all charts and tables: Company reports and Santander estimates.

Hypermarcas – Three-Year Stock Performance (R$)

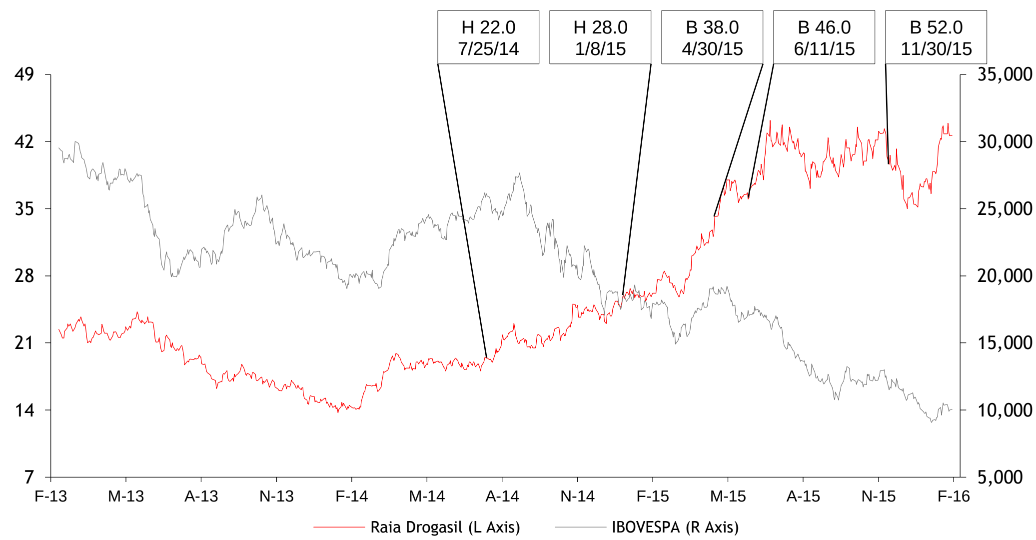


Sources: FactSet and Santander.

Valuation & Risks

Our YE2016 target price is based on a DCF analysis (in US$) for which we consider a Ke of 10.9% and a perpetuity growth rate of 4%. Main risks: (1) changes in the regulatory framework for pharma products, (2) elimination of tax incentives (i.e., ICMS), (3) divestiture of the Disposable Products division at lower-than-expected valuation levels and (4) increased competition in the market.

Raia Drogasil – Three-Year Stock Performance (R$)

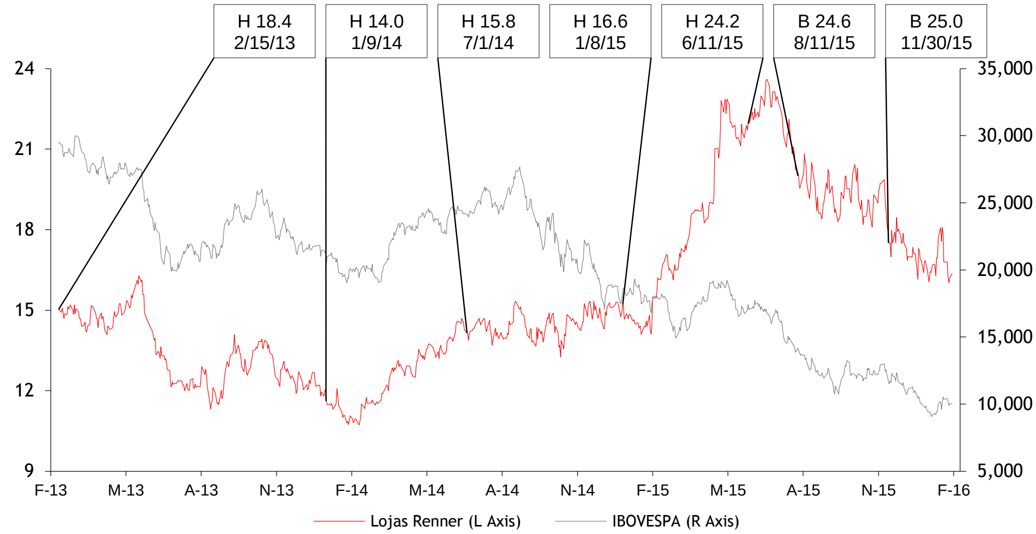


Sources: FactSet and Santander.

Valuation & Risks

Our YE2016 target price is based on a DCF analysis (in US$) for which we consider a Ke of 10.1% and a perpetuity growth rate of 4.5%. Main risks include: (1) increased competition, (2) changes in sales mix (lower-margin categories), (3) changes in industry regulations, (4) higher tax burden on medicaments and (5) a shortage of good locations (lowering new stores' IRR).

Lojas Renner – Three-Year Stock Performance (R$)

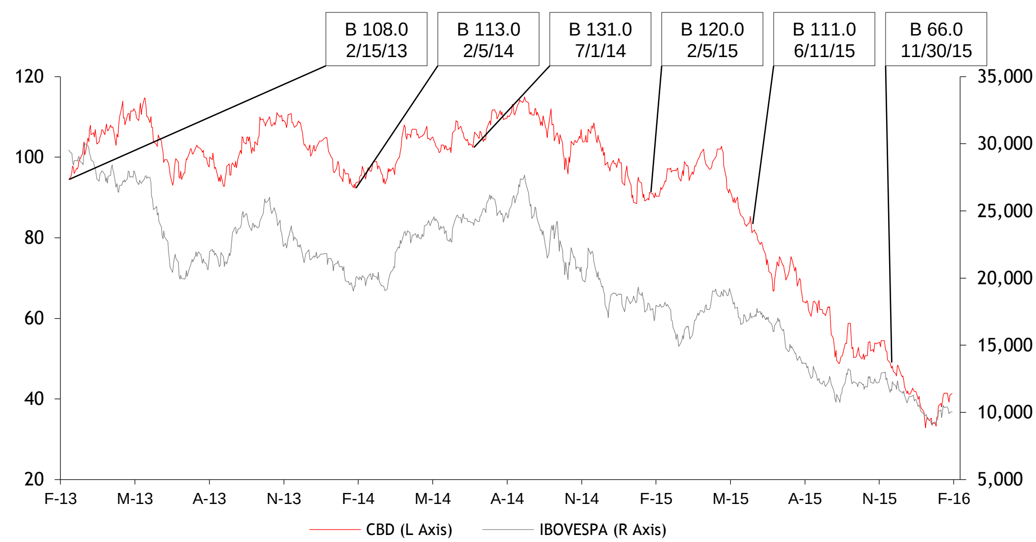


Sources: FactSet and Santander.

Valuation & Risks

Our YE2016 target price is based on a DCF analysis (in US$) for which we consider a Ke of 10.9% and a perpetuity growth rate of 4%. Main risks include: (1) lower-than-expected SSS; (2) increased competition; (3) deterioration in the Consumer Finance business, with rising NPLs and delinquency rates; (4) disruptions in push & pull logistics, leading to possible wrong orders or stock-outs at the store level; and (5) FX depreciation weighing on imported goods.

CBD – Three-Year Stock Performance (R$)

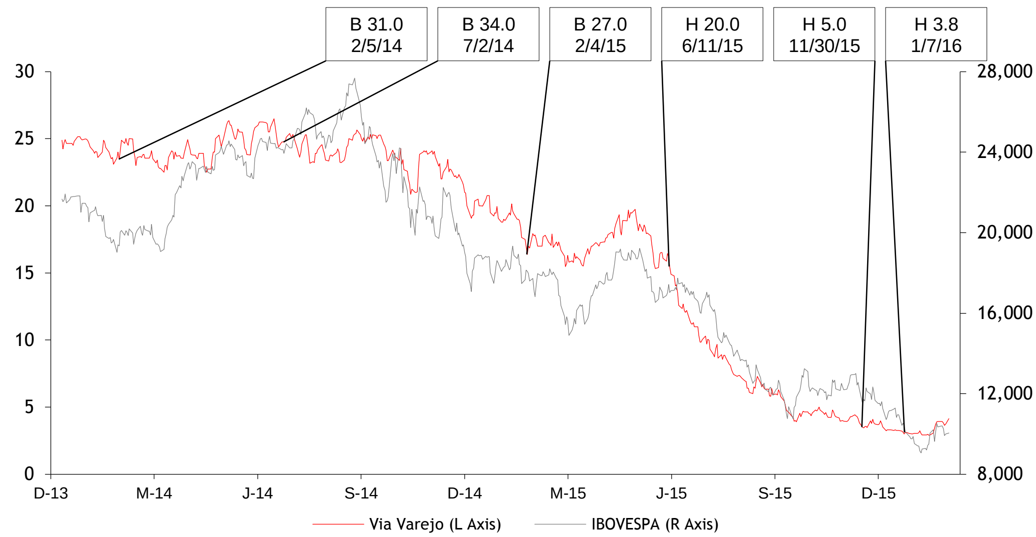


Sources: FactSet and Santander.

Valuation & Risks

Our YE2016 target price is based on a DCF analysis (in US$) for which we consider a Ke of 12.3% and a perpetuity growth rate of 2.5%. Main risks are: (1) further deterioration in macro indicators, (2) a delayed recovery in the refurbished stores, (3) deterioration in working capital, and (4) potential block trades.

Via Varejo – Three-Year Stock Performance (R$)



Sources: FactSet and Santander.

Valuation & Risks

Our YE2016 target price is based on a DCF analysis (in US$) for which we consider a Ke of 14% and a perpetuity growth rate of 1.5%. Main risks include: (1) further deterioration in macroeconomic indicators; (2) higher IPI taxes (government stimulus programs); (3) FX depreciation weighing on the cost of product components and raw materials; (4) aggressive pricing policies from competitors; and (5) block trades.

Companies mentioned:

Hypermarcas (HYPE3, target price R$27.00, current price R$23.56, Buy)

Raia Drogasil (RADL3, target price R$52.00, current price R$42.65, Buy)

Lojas Renner (LREN3, target price R$25.00, current price R$16.35, Buy)

CBD (PCAR4, target price R$50.00, current price R$41.35, Hold)

Via Varejo (VVAR11, target price R$3.70, current price R$4.15, Underperform)

IMPORTANT DISCLOSURES

Key to Investment Codes

Rating	Definition	% of Companies Covered with This Rating	% of Companies Provided Investment Banking Services in the Past 12 Months
Buy (B)	Expected to outperform the local market benchmark by more than 10%.	48.38	8.30
Hold (H)	Expected to perform within a range of 0% to 10% above the local market benchmark.	42.24	7.22
Underperform	Expected to underperform the local market benchmark.	9.03	1.44
Under Review (U/R)		0.36	0.36

The numbers above reflect our Latin American universe as of Monday, February 15, 2016.

For a discussion, if applicable, of the valuation methods used to determine the price targets included in this report and the risks to achieving these targets, please refer to the latest published research on these stocks. Research is available through your sales representative and other electronic systems.

Target prices are 2012 year-end unless otherwise specified. Recommendations are based on a total return basis (expected share price appreciation + prospective dividend yield) unless otherwise specified.

Stock price charts and rating histories for companies discussed in this report are also available by written request to Santander Investment Securities Inc., 45 East 53rd Street, 17th Floor (Attn: Research Disclosures), New York, NY 10022 USA.

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The benchmark used for local market performance is the country risk of each country plus the 1-year U.S. Treasury yield plus 5.5% of equity risk premium, unless otherwise specified. The benchmark plus the 10.0% differential used to determine the rating is time adjusted to make it comparable with the total return of the stock over the same period. For additional information about our rating methodology, please call (212) 350 3974.

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