Operator:

Good morning ladies and gentlemen. At this time we would like to welcome everyone to the SUBMARINO's 3Q05 earnings conference call. Today with us, we have Flávio Jansen, CEO; and Martín Escobari, CFO and Investor Relations Officer.

We would like to inform you that this event is being recorded and all participants will be in listen-only mode during the company's presentation. After SUBMARINO's remarks are completed, there will be a question and answer section. At that time further instructions will be given. Should any participant need assistance during this call, please press *0 to reach the operator.

There will be a replay facility for this call for one week. We ask the Press to get in touch with Submarino's Press Agent for further information: RP1 - (+5511) 5501-4655 – Rosely Santiago.

Before proceeding, let me mention that forward-looking statements are based on the beliefs and assumptions of SUBMARINO management, and on information currently available to the company. They involve risks, uncertainties and assumptions because they relate to future events and therefore depend on circumstances that may or may not occur in the future. Investors should understand that general economic conditions, industry conditions and other operating factors could also affect the future results of SUBMARINO and could cause results to differ materially from those expressed in such forward-looking statements.

Now, I will turn the conference over to Mr. Jansen, the Submarino's CEO, who will start the presentation. Mr. Jansen, you may begin the conference.

Flávio Jansen:

Thank you, good morning everyone, thanks for joining us. I am glad to announce the 3Q results, another quarter of solid growth and increase in profitability.

First highlight is our top line growth. We were able to accelerate our revenue growth from 58% in first semester to 71% in the 3Q.

Our growth continues to be driven primarily by the growth of our customer base 54% year-to-year as Internet users (…). This rate of customer growth has been helped by our offline market campaign. Additionally, average ticket grew 15% year-to-year mainly because of the increase of (...).

Profitability improved. EBITDA year-to-year, year to date, R$ 28.3 million, representing 75% growth when compared to last year.

Net income was R$ 8.6 million reais this quarter, R$ 6.1 million reais year to date. Our net income margin of 10.5% of net sales in the quarter shows the profitability of the company after the IPO in the deal captured (…). And this is the first quarter that we do not have portions of IPO expenses.

We are ready for Christmas. During the 3Q we expanded the capacity of our order system; we also implemented a new CRM system and we finished the expansion of our warehouse. We keep the plan to move to a new warehouse in 2006 we have already pre-selected a site, we agreed on all commercial services with the new facility factor and, right now, we are in the process to obtain the final permissions to start the construction.

We are very excited about the acquisition of Ingresso.com and our new campaign. We will talk a little bit more about this in the next slides.

Within our growth initiative, I would like to highlight that our new (…) category has already reached breakeven and also we are in the final process of selecting our trainees for 2006. The selection process was (…) more than 600 thousand applied encouraged by the fact that young graduated were employed by our company.

Going on to the next page, page number 3, just to give you some highlights on the offline marketing campaign.

Results, so far, (…) and our historical customer acquisition costs are lower than marginal contribution from the customer's first order. We are clearly under investment marks. In the long run, we believe that the market will become more competitive and certainly, acquisition costs should increase. So, that is a good time to increase and try to stress the growth of our customer base. We believe that (...) on the growth rate in the 3Q results of the offline marketing campaign.

The campaign (…) enforce with promotional products; everything is looking (…) you very (…). We plan to keep our offline efforts in the 4Q and evaluate the results as we are considering the right level of investments in 2006.

Finally, I would like to welcome (…) Submarino, (…) and Mauro, the founder, are great entrepreneurs and did a great company. We are really excited about both companies working together, and I will ask Martin now to speak a little bit on the acquisition.

Martín Escobari:

Thank you. Good morning everyone, thanks for joining us. We are very excited about the ingresso.com acquisition, in many ways an example of the type of business model expansions, which we may pursue.

What is ingresso.com? Ingresso.com is primarily a technology company, it started 10 years ago as a software automation company for cinema theaters throughout Brazil, it grew very rapidly, and today, basically the automation software empowers close to 900 theaters in Brazil, which represents about 80% of all movie tickets sold in Brazil.

This technology platform allowed ingresso.com to become the leading and today the only company to sell movie tickets online. The acquisition allows us to enter a very attractive and growing market, the sale of online ticket. The sales of tickets in Brazil is about R$ 1 billion industry, only 1% is online, and we believe it is an opportunity to increase that dramatically in the coming years.

The primary driver, in addition to the normal comfort to being able to buy online, is the fact that, you know, Brazil is relatively under-penetrated in terms of numbers of theaters. It is very frequent, particularly in big cities in Brazil, like São Paulo, Rio, Salvador and Curitiba, that you face long lines and frequently sold out when you go to the theater over the weekends; buying online is a way to avoid standing in line when you go to the theater during the weekend. It is a great service to customers, and it is a service that from now on will be enjoyed by around 1.2 million active customers.

When we think of how much to pay for an acquisition, we very carefully evaluate how much it will cost to build a competing platform for such service. In the case of ingresso.com, the math was very simple: it would have been prohibitively extensive to develop a competing technology transfer platform to enter this segment, so the choice of our acquisition was the right one. And we believe the price paid was very attractive.

We are also very excited with the fact that we have retained the entire team of ingresso.com, and the two founders will be now leading the efforts in ingresso.com and other things that we will launch using the Ingresso.com platform.

The purchases of our consumers, in terms of what movies they buy, give us a lot of insight about their taste. We intend to use those insights to (…) Submarino products overtime. Moreover, we think that in long run it is very important Submarino develop a very differentiating position relative to our online and offline competitors.

The sale of tickets online is clearly a long step forward in terms of a differentiation offer.

Moving on to the financial results, on page 5, as Jansen mentioned, we saw an acceleration of our growth in the 3Q. We grew 71% in the quarter, up from 58% up to the first semester. It is an important step-up. As we think of our market share, we think that we've continued to increase market share, our market share will record, during these 9 months period, 24%, compared to 21% from the year before.

Our gross profit for the year to day is about 28%, on page 6; is in line with our long-term and short-term targets. During the quarter, however, we saw a rapid increase in the sale of consumer electronics.

We believe that the increase in consumer electronics is due to a combination of a stronger real, that makes these products more affordable, but, more importantly, the beginning of a cycle of lower interest rates for Brazil.

The consumer electronics line has a slightly lower gross profit margin, as a percentage of net sales, but significantly higher gross profit dollars per order, particularly because the average ticket of the consumer electronics is R$ 500, where for media groups the BMV line is about R$ 50.

So, the higher ticket item yields a much higher gross profit dollars per order, which is the right way we should measure the attractiveness of that category. So, in long term, we think this shift in mix is (…) to a long-term profitability.

In terms of expenses, we would like to report that, unfortunately, selling expenses did not improve, on page 7. They went, year to date, about 15.8%, whereas last year it was 14.6%.

Why did they go up? We believe we are under-investing in marketing, so we decided to begin to expand our margin expenditure moving into (…) offline marketing in the world.

Our gross marketing expenditure went from 2.4% in net sales to 3.2% of net sales. We believe the return on that extra 1.6% was very positive, as Jensen said. However, two things true: one, I think we can improve the productivity of marketing expenses, as we know how to do that better. We are only at the beginning of that learning curve.

And secondly, we think what is the right level of investments, of incremental investments in marketing, we want to assure the market that our incremental investments will be measured and defined in a way so that we don’t sacrifice the guidance profitability.

The other effects on the selling line will be much smaller, as an increase in fuel cost lead to higher freight cost, and more importantly, we are experiencing inefficiency in the warehouse; even though we expanded the warehouse in our existing facilities by taking over some additional space. In the short term, we are trying to maximize capacity and not maximizing efficiency, since we are going to be moving to a new warehouse next year; and that, of course, has an impact on profitability.

In terms of G&A, it is better than our expectations, G&A cost (…) of net sales are 1.8%, compared to 3%; we continue to see dramatic gains from scale on our G&A line.

What this translates in terms of EBITDA, on page 8, is the EBITDA growth of 75% year-on-year, and EBITDA margin of 10% for the year to day. In terms of the balance sheet and our working capital ratio – which is something we monitor closely -, we did not see any significant changes.

Our accounts receivable base worsened slightly, from 85 days to 93 days; inventory went up slightly, from 40 to 43 days. But that was more than compensated by an improvement in payable days, which went from 55 to 65 days.

None of these changes are permanent, they reflect seasonal fluctuations, we have not seen any change for the better or for the worse in our working capital ratios.

In terms of cash flow, on page 10, they are just a product of our working capital ratios; we did not see a change from our expectations or from our targets since our working capital ratios have not changed.

In terms of guidance, once again, we decided not to change the guidance metrics for growth and profitability; probably I would like to reiterate them and continue to say what we have been saying that we remain confident on our ability to meet guidance.

Finally, as we look at 2006, I would like to highlight some of our priorities. It will grow 45%-50% next year; capacity will be one of the priorities. As we have discussed the new warehouses (…) but will lead capacity expansion runs across all processes in the company. We have been doing that for the last six years, so we believe we are on track on this.

We also believe that there is a great opportunity to create differentiation and increase frequency through different tools. The major area we believe there is an opportunity is personalization. We will be announcing something in this area pretty soon. And without giving too much info to the competition, I just want to go through the drivers of our growth next year.

The first one will be the increase of the customer base through Smart Market. The second driver will be new categories, we will keep adding new categories next year. We also plan to enter in new service areas, something similar to what we did with ingresso.com this year.

We have talked with many people and we see a great opportunity in customer finance, and we believe there is an opportunity to monetize our ability to generate financially. At the moment, the only thing we can say is that we are discussing with some banks to partner in this area. When we have something concrete, we will be disclosing to the market.

And the last thing is the commercial program, it continues to grow, and we expect it to continue to grow in 2006.

That would be all, so I would like to open to questions.

Operator:

Thank you, sir. The floor is now open for questions. If you do have a question, please press *1 on your touchtone phone. If at any point your question has been answered, you may remove yourself from the queue, by pressing #.

Our first question is coming from Tania Sztamfater, with Unibanco.

Tania Sztamfater:

Good morning, Flávio and Martin.

Martín Escobari:

Hi, Tania.

Tania Sztamfater:

My first question is regarding the sales of electronics and white goods. As you commented, it was one of the (…) growth. I want to know how you see your competitive landscape right now on that (…) business.

And how do you see your (…) products evolving now for the (…), I mean, how much of your products you expect (…) to response for with the expectations of the declining interest rate in the long term?

Martín Escobari:

Sure. The competitive landscape in electronics has changed over the last decades. I mean, those of you that follow Brazilian retail will remember names like Arapuã, Mappin or G. Aronson who went bankrupt in the mid 90's. So, that actually (…) a lot of competitors.

Today, who we compete against in the electronics, at low end, are Casas Bahia, who is very high price but very high financing, primarily to class C citizens. SO we do not bump into that that much, and at the middle and high end, which is where we are, class A and B, we compete against Ponto Frio, Fastshop, and to a lesser extent Lojas Americanas (…), and more so Lojas Americanas online.

I would say, compared to other categories, it is, perhaps comparing, or perhaps less competitive than some of the other categories in which we are in. In terms of how our mix has improved and our offering, Americanas.com was earlier in the game in terms of focusing on electronics, back in 2000, because they saw this is a way of generating quickly cash flows and revenues. We prioritize the lower ticket items to maximize the growth of our base; that was the right decision. Since then, we play catch-up.

Today, in terms of product mix and offering, we are as good or better than the rest of the competition, offline and online, where there is tremendous room for improvement is the price in which we buy (…), and more importantly on the supply chain (…). The one advantage that we have in this category, unlike the books category, where, in a very fragmented, very informal, the electronic suppliers are very high-tech and they understand supply chain management. And I think that as we continue to grow in this segment, we should be able to further integrate our supply chain without our suppliers unless you have drown down some of our inventory days.

In terms of magnitude, I think we have been pretty consistent about not giving quarter-by-quarter guidance on the revenues, the revenues flipped by category, but this is significant enough that I think we should disclose something, and what we are (…) the disclosure (…) whereas consumer electronics, which encompasses an array of things, you know, the durables line that you are (…) to be about 1/3 of our sales; it is now more than half of our sales.

Tania Sztamfater:

This quarter, you mean the 3Q?

Martín Escobari:

In the quarter, yes.

Tania Sztamfater:

OK. And do you expect it to stay at that level, Martín?

Martín Escobari:

If it continues to grow faster on the rest of our business. So, to what extent this is a long run boost in durables, it could continue to grow; but it is hard to know what the drivers are, I mean, lower interest rates is clearly a factor, and it remains to be seen how long it will last; and so far we haven't seen a slow down in consumer electronics.

Tania Sztamfater:

My second question is regarding consumer finance and part of the last comment. We know that differently from the other retailers, (…), I have more customers on the higher income classes, we know that those (…), they have (…) different (…) what type of they can pay, or how much they will finance. In your recent conversation with banks, do you have, you know, drivers could give us, figures you could give us in terms of credit card usage, in terms of rollover rates for credit card and type of interest (…) being paid by this type of customers. We know that they also use this type of credit line, just at what levels compared to classes C and D?

Martín Escobari:

Sure. I think it is very early to get into a lot of details about what this could mean to Submarino, and we are just beginning the process, we surely don't want to create the expectation among investors, an announcement is imminent and we are going are going to be seeing a huge (…) for the cash in the short run. I will tell you specifically about the appeal of a consumer finance operation for class A and B customers; we are very excited and so is the bank we are talking to. There are two drivers, which determine the attractiveness of (…) what percent of your customers would be willing to migrate theirs purchases from their existing credit cards to Submarino credit cards, or Submarino private label product.

If you look at benchmarks in the US, guys like (…), which are clearly in class A consumption, those department stores are able to migrate 50%, or close to 50%, of their revenues to their local card. Lojas Renner closer to (…) has about 70%. So there is enough preference, given our plan and given some of the rewards program that we are defining we should be able to get reasonable migration from sales from other credit cards to our own credit card, so that is one driver and we are pretty optimistic and I believe to do that, and there is enough benchmark outside and inside that gives us confidence.

In terms of how much money that customer yields to the owners of the credit card. In consumer finance there are two types of business, there is the low end, which is what Casas Bahia does, which is relatively low consumption per customer very high spreads; and the high end, which is significantly higher, 5x to 10x more consumption per card but lower spreads.

As the high end, which is our business, our target is in the short run, it is very attractive. From what we see in the market, about 20%-25% of gross billings going to rollover rates on the rollover, rollover financing charges are about 6% to 8% per month; what that yields, in terms of (…) fantastic, we need only to look at the transaction where the banks (…) credit cards to the second largest issuers in Brazil, they pay about US$ 150 per card holder.

So, clearly it is a lucrative segment, and it is the one in which we are going to be focusing in. But, again, (…) we have no cards today, and we will announce something in the first semester of next year, and we are optimistic, but I think we want to be measured and not create expectations at this point.

Tania Sztamfater:

And just one last question on your marketing expenses lines, you commented that we can see that the acquisition cost lower than (…) give us a sense of the short term impact of this investment. But I wanted to know what is your view of the long-term impact of the current investments, how you see your competitors investing in marketing, how do you marketing expenses evolving for the long-term with increase in competition and along with this analysis, how do you compare your current customer acquisition cost and acquisition initiative with your customer maintenance cost (…)?

Martín Escobari:

OK. Tania, you are correct in your question, we think, today, we are able to pay the acquisition of the customer with this first purchase, we do not believe that we that it will be the case in the future, in the long run, the cost to acquire a customer will increase, so we will need more effort to acquire customers.

And what we start to look in, I mean, part of our strategy today is to prepare the scenario and we believe that the way to prepare will be creating some differentiation with the competition, and also to use to increase the frequency.

One thing we believe will be a key factor in the future will be personalization, we are looking this area, we plan to invest in this area, and that will allow us to, we think it will allow us to keep growing with lower marketing costs in the future.

Flávio Jansen:

You can think of two phases, while marketing costs are reasonable, we will spend more in marketing, not too much to sacrifice the guidance profitability but there is low (…). In the medium term, as the marketing costs go up, our focus will move away from clients acquisition and move towards, you know, differentiation and loyalty, and if you look at the frequency today is (…) opportunity, so I think there are clearly two phases: one is now, while the marketing costs are reasonable, and then in about probably two years, as all our focus becomes on farming as opposed to hunting.

Tania Sztamfater:

So you mean that right now your effort is in customer acquisition, and probably you do not have a lot of cost regarding customer maintenance or initiative, and then you move to, let's say, customer maintenance initiative, and as time passes by and marketing expenses go up?

Flávio Jansen:

Yes. I think you should read into the current expenditure level as a permanent level of marketing expense, it is not. It is an opportunity in the short-term; it is not the long-term trend.

Tania Sztamfater:

Do you have any guidance regarding where you see your marketing expenses, as percentage of net revenues, going to in the long-term?

Flávio Jansen:

Historically, we have said it, if you look at the semesters, the gross, you do recognize that there are allowances that…

Tania Sztamfater:

Sure, I mean the gross marketing expenses.

Flávio Jansen:

The guidance we gave during the road show about 2% of net sales, or slightly under that, seems reasonable.

Tania Sztamfater:

OK. And the last question is, do you see your competition doing something similar or different from the guide, how do you see the competition is moving right now, the positioning and marketing efforts?

Martín Escobari:

Yes, we believe they have similar plans, I mean, our main competitor. The same way we believe that there is an opportunity to grow and increase the customer base; it is very likely that they are seeing the same opportunity, because it is clearly a growing market with low competition, so I think both are using similar strategy.

Tania Sztamfater:

OK, thank you and congratulations for the results.

Martín Escobari:

Thank you.

Operator:

Once again, ladies and gentlemen, to ask a question, please press *1 on your touchtone phone at this time.

Our next question is coming from Daniela Bretthauer, of Santander.

Daniela Bretthauer:

Hi, good afternoon. Actually, I want to be more straightforward. Can you quantify how much of your marketing expenses you plan to invest during the 4Q, meaning, is it 250 basis points of net sales, is it more, is it less? Of course, there is an effect of the higher sales also in the 4Q, but can you just quantify that, that is the first question.

And, secondly, how confident are you that you will be able to meet your guidance for the full year 2005, that calls for an EBITDA margin of 11.5%, given that you have decided to invest more in the offline marketing.

Martín Escobari:

Thanks for your straightforwardness, and I will be purposely evasive, we don't want guidance quarter-by-quarter about marketing expense, but my answer to the second question, I think I will give you a hint (…).

We feel very confident in terms of the R$ 46 to R$ 50 million EBITDA contribution, so when we say about how much extra we want to invest in marketing, and not scarify the long-term profitability, we do not want to sacrifice the EBITDA in terms of real terms.. Obviously, to the (…) margin we are investing more in growth, the margin might suffer slightly, but I think the right way to think about the incremental margin is, we will invest more, but we want to still deliver the EBITDA guidance, which, as we said all along, and if you look in page 11, it is reais terms, which we think is the right way to look at it.

In terms of the marketing expense, it will not be more than it was in the 3Q, it is in line with that, and, seriously, the disproportion of seasonality in the 4Q is a percentage of net sales that also affects the math. But I think we do not want to give too much information at this point other than to say we will deliver the guidance in real numbers.

Daniela Bretthauer:

OK, Martín, thanks. And in terms of your freight costs as a percentage of sales, you are basically in line with the year-ago quarter, but higher than what we have seen from Submarino on the first two quarters. Can we expect also something like that during the 4Q, given the seasonality, or is it an one-off thing, and you should go back to around 1% of sales?

Martín Escobari:

Daniela, we believe that we will be similar to the 3Q, I mean, Christmas promotions and all to react to the market, it might change a little bit that, but we really believe we will keep same level of the 3Q.

Daniela Bretthauer:

OK. And last question: I could not really catch what Martín said that the average ticket for BMV is around R$ 50, and what was your average ticket for consumer electronics?

Flávio Jansen:

R$ 500.

Daniela Bretthauer:

R$ 500. And how do you see your sales mix as you are heading in to the 4Q, compared to what you had in the year-ago period, can you comment a little bit on that?

Flávio Jansen:

As we said, durables and consumer electronics are growing faster, they are more than half more sales, they were less than 40% last year on the same quarter, so we do expect durables to be around that range, more than 50%.

Daniela Bretthauer:

OK, thank you, guys.

Flávio Jansen:

Thank you, Daniela.

Operator:

There appear to be no further questions. I would like to turn the call back over to Mr. Jansen for any final comments.

Flávio Jansen:

Thank you everyone for the attention, also thank you for the questions, and I just want to invite you to meet us in the next call that will be in the beginning of next year. Thank you and goodbye.

Operator:

Thank you, ladies and gentlemen, for your participation. That thus concludes Submarino's conference call. You may now disconnect your line.