Transcription of Natura's 2Q05
Earnings Presentation
July 29, 2005

Operator

Good morning ladies and gentlemen. At this time we would like to welcome everyone to Natura's 2005 second quarter results conference call. Today with us we have: Alessandro Carlucci, the CEO, José Davidd Uba, the CFO and Helmut Bossert, the Investor Relations.

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 Natura's remarks are completed, there will be a question and answer session. At that time, further instructions will be given. Should any participant need assistance during this call, please press *0 to reach the operator.

We have simultaneous webcast that may be accessed through Natura's IR website: www.natura.net/investor. The slide presentation may be downloaded from this website; please feel free to flip through the slides during the conference call. There will be a replay facility for this call on the website. We remind you that questions, which will be answered during the Q&A session, may be posted in advance in the website.

Before proceeding, let me mention that forward-looking statements are being made under the Safe Harbor of the Securities litigation reform act of 1996. Forward-looking statements are based on the beliefs and assumptions of Natura 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 Natura and could cause results to differ materially from those expressed in such forward-looking statements.

Now, I will turn the conference over to Mr. Helmut Bossert, Investor Relations Manager. Mr. Bossert , you may begin the conference.

Speaker – Helmut Bossert

Good morning everybody. First, let me welcome you all to **Natura's** conference call to discuss our results for the second quarter of 2005.

I'm going to present the slides and then Alessandro, Davidd and I will be glad to answer any questions you may have.

Now let's go directly to slide 2.

Slide 2 – Historical figures: CF&T Target Market and Natura's Market Share

This slide shows the nominal compound growth for this target market between 2000 and 2004 which grew by 17%. In real terms, this amounts to 6.8% per annum.

The graph on the right shows that Natura's market share rose from 13.9%, in 2000 to 18.9% in 2004.

Let's now move on to slide 3, which shows market figures for the first four months of the current year.

Slide 3 – CF&T Target Market Growth in Brazil – First four months of 2005

The chart on the left shows the first four months of 2005 target-market net revenue growth of 18.1%, while the one on the right indicates that Natura's net revenues grew by 30.3% in the same period, followed by an increase in our market share from 18.6% to 20.5%.

This substantial market growth is based on the dynamic of the industry, strongly influenced by innovation and changes in the population's demographic parameters, for example the growing presence of women in the workforce and the gradual aging of the population.

In addition, there is no hard evidence at the moment that leads us to believe that these factors, considered industry's drivers, will run out of steam in the short and mid-term.

The next slide deals with growth per product segment.

Slide 4 – CF&T target market growth in Brazil per category (First four months of 2005)

In the cosmetics and fragrances segment, Natura recorded year-on-year growth of 33.3%, versus 18.7% growth for the market as a whole, and our market share climbed from 32.2%, in the first four months of 2004, to 36.2% in the same period of 2005.

In the toiletries segment, we grew by 24.3% in the same period, versus 17.7% for the market, and our share increased from 10.0% to 10.5%.

The fact that our growth outpaced that of the market can still be explained by strong innovation, a commercial model based on a constantly sales channel growth and high consultant retention and productivity rates. Also, there is our brand, which this year, was ranked fourth as the most valuable brand in Brazil, in a recent study by Interbrand published by *Isto É Dinheiro*, a well-known magazine in Brazil.

Let's now move on to slide 5.

Slide 5 – Gross Revenues and total number of Consultants

This slide shows that Natura's gross revenues recorded a growth rate of 28.5%, in the second quarter and first half of 2005.

On the right, we can see that at the end of June, 2005, the consolidated figure stood at 484 thousands of consultants, up 21.1% over the same period last year.

Let's now go to slide 6, which deals with the Brazilian sales channel in more detail.

Slide 6 – Sales Channel in Brazil: growth and productivity

The graph on the left shows that the number of consultants in Brazil totaled 454 thousands consultants at the end of the first half 2005, 20.2% more than at the end of June, 2004. It is also worth noting that the average growth for the last two years was 15.1%.

The chart on the right shows that productivity, in the second quarter, increased by 7.3% year-on-year, reaching R$3,085 per average active consultant. For the first half as a whole, productivity amounted to R$ 5,637 per average active consultant, a growth of 7.1%.

Slide 7 deals with our Latin American sales channel.

Slide 7 – Sales Channel in Latin America: growth and productivity

Our Latin American operations have also been expanding consistently, with a compound annual growth rate of 35.1% over the last two years. At the end of June, 2005, there were 29,9 thousands consultants, 35.9% growth over June 2004.

In the second quarter, productivity measured in US dollars grew by 8.4% year-on-year, reaching US$693 per average active consultant.

In the first half 2005, productivity was of US$1,252, up 7.0% growth over the first half 2004.

And now some comments on our innovation process, moving on to slide 8.

Slide 8 – Continuous Innovation

Investments in innovation continue to play a strong role in the company's growth. In the first half 2005, these investments totaled 3% of net sales, in line with our strategy.

It is also worth noting, in the graph on the right, that we recorded a first half total innovation index of 69.7%, versus 61.3% in the first half of 2004.

Now, with slide 9, I'd like to briefly say something about corporate responsibility.

Slide 9 – Social corporate Responsibility

This slide shows the sales figures for our *Crer para Ver* product line, which in this first half of 2005 was of R$3.8 million, up 46.2% over the same period of 2004.

Regarding environmental field, our first-half packaging impact index averaged 10.2 milipoints.

Now let’s move on to slide 10.

Slide 10 – Financial Summary – Quarterly figures

This slide summarizes the main quarterly indicators:

- Products for resale moved up 17.0% year-on-year, accompanied by net revenues growth of 30.1%.

- Gross revenues climbed to 35.6% year-on-year, while our gross margin increased by 2.8 percentage points, from 65.9% in the second quarter of to 2004, to 68.7% in 2005. This was due to lower promotional efforts in the period and better management of seasonal products margins (such as Mothers Day and Valentines Day).

- EBITDA grew by 25.9% year-on-year, while the EBITDA margin narrowed from 23.9% in first quarter of 2004 to 23.1%. The decrease in the EBITDA margin was essentially due to the company’s structural changes, aimed at ensuring continued business growth, such as: our ongoing international expansion – this year we have entered Mexico and France and we are preparing to enter other markets in 2006 and 2007 – and the previously-mentioned upturn in innovation investments.

- Net income climbed by 11.5% year-on-year, while the net margin fell from 18.4% in the second quarter 2004 to 15.8% in 2005, chiefly due to:

- the reduction in the EBITDA margin;

- a lower financial result;

- higher net expenses abroad related to the international expansion process, which do not reduce the taxable income base in Brazil;

- the lower relative share of goodwill amortization on the income tax and social contribution calculation base, in the second quarter of 2005.

Now let's go to slide 11, which summarizes our first-half financials.

Slide 11 – Financial Summary – First-Half figures

Net revenues increased by 30% year-on-year, the gross margin widened by 1.2 percentage points and the EBITDA margin decreased by 1.6 points.

In short, the benefits from improved gross-margin management and the gains in scale from higher output partially offset the upturn in expenses from strategic investments in the international expansion process and in innovation

Now for slide 12.

Slide 12 – EBITDA and margin

Here we can see that first half 2005 EBITDA which totaled R$224 million, 21.3% higher than in the first six months of last year.

Second-quarter EBITDA stood at R$129 million, 25.9% up year-on-year.

The graph on the right shows a comparison between first-half and second-quarter EBITDA margins for 2004 and 2005.

Now let's move on to slide 13, which deals with our Latin American operations.

Slide 13 – Operations – Latin America (Argentina, Chile and Peru)

Net revenue growth continued to outpace growth in Brazil and totaled US$6.6 million in the second quarter of 2005, a year-on-year growth of 55.3%.

The next slide deals with our international expansion process.

Slide 14 – International expansion

International expansion has continued as planned and initial achievements in Peru (which is already profitable) show the model is vigorous, in spite of operating losses in our other operations (all of them still in the process of consolidating their structures).

Here you can see total net expenses from our international expansion process, which totaled R$18.6 million in the first half 2005 and refer to operating losses from existing operations (Argentina, Chile and Peru) plus those from new ones (Mexico and France).

For 2005 as a whole, we estimate such expenses at R$41 million net, R$28,8 million higher than in 2004.

Now slide 15.

Slide 15 – CAPEX

We invested R$ 53.1 million in permanent assets in the first half of 2005, most of which went to the acquisition of new machinery, software and molds. In April 2005, we inaugurated our new vertical warehouse facility, doubling storage capacity in Cajamar (SP). In the third quarter, our third automatic separation line (Picking) will begin operations.

It is worth reiterating that our 2005 annual investment program totals R$120 million, focusing on increasing production capacity, intensifying automation and making the logistics process more flexible.

Slide 16 compares cash generation in the first half of 2005 and 2004.

Slide 16 – Cash Flow

Gross cash generation in the first half of 2005 stood at R$ 184.9 million, 27.2% up year-on-year. Of this total, we invested R$40.5 million in working capital and long-term receivables and liabilities.

Investments in permanent assets, as mentioned previously, stood at R$53.1 million, giving free cash generation of R$91.3 million.

Finally, slide 17 brings us to dividends.

Slide 17 – Dividends and interest on capital, net of taxes

The Board of Directors has approved the payment of dividends and interest on capital related to the first half of 2005 and this proposal will be put to the AGO in 2006. The net total comes to R$101.8 million, equivalent to R$ 1.20 per share and representing 64.6% of first-half net income and 111.5% of free cash generation in the same period.

That brings us to the conclusion of our presentation and we are now at your disposal for the question and answer session. Thank you all very much.

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Question and Answer Session

Operator: Ladies and gentleman, we will now begin the question and answer session. If you have a question, please press the star key followed by the one key on your touch-tone phone now. If at any time you would like to remove yourself from the questioning queue, please press star two. Our first question comes from Daniela Bretthauer, from Santander. Please, go ahead with your question.

Ms. Daniela Bretthauer: Hi, good afternoon everyone. The first question is if you could just give us a little bit more clarity on the financial results, meaning how much was the effect of the market to market on your financial results? I'm just trying to get to ... If that was the main reason why your financial results were lower than expected. That's the first question.

Mr. David Uba: Hi Daniela, this is David Uba speaking. Actually, we had two effects on these financial adjustments, one for this current quarter and another one for the same quarter of last year. Let's start for the last year, which this explanation will help you understand why we had such a big difference between our results of second quarter of 2004 and the current second quarter. Last year we had a capitalization of some convertible bonds by BNDESPAR and that resulted in a decrease in our expenses, financial expenses, for that period. Actually, we had made some provisions for an extra cost for those debentures that, when we went public, those extra expenses didn't apply anymore, so we canceled those provisions in that particular quarter, so that had a net effect in that quarter of R$3 million. This year we decided to swap 1 million term finance for another one at much better, with much better conditions, with a lower cost and when we decided to anticipate the liquidation of that operation, that loan, the market to market calculation of the net payment to be done, resulted in a financial expense of R$2 million, so those two effects together represented a effect total difference from those two quarters of R$5 million.

Ms. Bretthauer: OK, so this basically on the financial results, would it be fair to say that the lower figure it is more a reflection of your working capital needs going up, rather than the market to market? Because it is a very small impact, I was thinking maybe was a bigger figure, so I guess the lower financial result has to do with the increase in working capital needs. Am I correct on that line?

Mr. Uba: Almost. I would say that the impacts are similar. We estimate our excess in inventories in this first half of the year as something around R$20 million, which we do not expect to reduce until the end of the year, by the way, so if you take the impact of this excess in inventory at, let's say, an average cost of 10% per semester, would mean an impact in this semester of R$2 million or in the quarter of 1 million, while the market to market adjustment meant R$2 million for the semester and 2 million for the quarter alone. So they are similar.

Ms. Bretthauer: A combination of both.

Mr. Uba: Yes, yes.

Ms. Bretthauer: And the second question is, you provided us with the total amount, or the total cost of your internalization, or international expansion for 2005, which is a pretty substantial amount, R$41 million. What can we expect for 2006 and going forward? Similar levels, or ... I am just trying to sense when will that figure peak and when will it start to normalize? Or that will not happen anymore going forward? If you can give us a little color on what to expect for your expenses in the international expansion going forward, that would be great.

Mr. Uba: Daniela, as you know this internationalization process is deep rooted in our strategic planning for the coming years. We want to create a new route of growth for the company in the coming years and we believe that if we do not expand abroad we might jeopardize the growth of the company, let's say from 5 to 10 years from now. So, this is ... the company is strongly committed to this internationalization expansion, but with a limited impact in our results. This internationalization expansion is always reflected in our results, since they are operational losses in the startups in other countries, so we are also committed in putting a cap on these expenses as a percentage of our EBITDA. We are right now in the process of making a new long-term planning including this stronger expansion abroad and we still do not have precise figures for the coming years, but what I can advance to you that we are very concerned in putting a cap on the impact of this internationalization in our results.

Ms. Bretthauer: Can you share with us what this cap, as a percentage of the EBITDA may be at current levels?

Mr. Uba: No, not currently. We are still in the process of discussing this with our board of directors and it is going to take a few months before we have a better picture of what we are going to do in the coming years, but what is important here is that we are going to limit this impact and I would even say that at a very reasonable level. We wouldn’t let this to have a too relevant impact in our results.

Ms. Bretthauer: OK, thank you very much, David.

Operator: Our next question comes from Robert Ford, from Merrill Lynch.

Mr. Robert Ford: Hi, good morning everybody. David, my first question had to do with some of the expense pressures that appear to be resulting from your domestic operations and I was wondering if you could share with us a little bit more color in terms of what is pressuring your logistics expenses internally in addition to just simply fuel costs? And what may be the portion that you can address and the portion you can't address? And I would like to have a better sense of some of the investments that you appear to be making that I think will yield greater productivity in future periods but for now maybe yielding greater costs?

Mr. Uba: OK, Bob. First of all I should start telling you that we do not have any specific pressure from raw material costs, they are very well balanced with the internal inflation here in Brazil. We had some pressures from plastic packaging, but they were offset by some gains on imported and other materials that are linked to foreign currencies here in Natura. So we for raw materials, we are in line with the internal inflation in Brazil. Now, the other pressures from logistic process that we had were more linked to what we call here the process associated with taking orders and shipping orders to our consultants. All these processes, as we had, suffered a little bit from the tremendous increase in volume we had in the last three years. Actually, that infrastructure was not well designed for this tremendous increase we had. We are redesigning all the infrastructure for conducting those processes and we expect these costs to decrease in the next year. This year, in the first half of this year, this loss of productivity in these processes represented roughly 1% of our net sales, which we expect to go on for the remaining of the current year.

Mr. Ford: OK David, in my perception, when people make reference to your working capital requirements means that not only is it in distribution, but also in manufacturing it seems as if you are carrying a little bit more finished product; you built up inventories, not just to hedge yourself, because if you take out that R$20 million in excess inventory that you referenced, you are still up 50%, your sales are only up 30, right? So, there too, it seems like you are bumping up against some of the capacity constraints, because of your phenomenal growth that you have had over the last few years. Is that correct? And if so, will you raise your CAPEX budget even further than the R$120 million to address some of these constraints that you appear to be bumping up against?

Mr. Uba: OK. Well, your supposition is partially correct, part of the problems we have in servicing our consultants came from some constraints in our manufacturing processes, some bottlenecks we have in manufacturing processes, but also from inadequate inventory policy we had until, say, the beginning of this year. As our portfolio increased in number of SKUs, all these logistics processes increased in complexity and we had to review all the processes. So, let me try to summarize what we are having right now at Natura. We, in the last two years, we have been losing some sales because of our lack of capacity of fulfilling 100% of our consultants' demands. We want to decrease these stockouts and the losses of sales derived from these stockouts and we believe that we can have two positive effects from doing that: the first one is the direct one, is the increase in sales from these lost sales by canceling those losses from the stockouts; and the second one is improving the quality of service to the consultants and giving them more stimulus for increasing their sales to the final customers. And this second factor may be even more important than the first one. We believe that by improving service to our consultants will help them to increase their customer base, or increase the share of Natura in these customers' expenses with cosmetic products. So, what we are doing now is investing in manufacturing process, giving more flexibility to the manufacturing process and at the same time to develop a much more intelligent, I would say, inventory policy in order to reduce the stockouts to almost zero and therefore to increase our sales. We are absolutely sure that this investment has a tremendous return for the company.

Mr. Ford: I have no doubts that you've got some good opportunities and they sound like they are very good ... very good problems to have, I would suspect. But is it going to cause you to raise your CAPEX? And because part of this is improving the quality of service to the consultants, then my suspicion is also you have been growing consultant base by so much, that we're also probably going to see some growth in terms of your further growth already from that first quarter base in terms of the ... that your managers, your promoters to the consultants as well, are we going to see further growth in terms of that level of the organization and, again, are we going to see CAPEX in excess of R$120 million?

Mr. Uba: No, I don't expect CAPEX to go much further beyond the levels, the level of this year, R$120. In this year no, and not even for the coming years. It should stabilize around those levels. That's our perception right now. We are going to eliminate some bottlenecks we have right now and for the coming years, of course it also will depend on the rate of growth we will have in our volumes, but our better estimate right now is that CAPEX should stay around those levels, R$100 to R$120 million per year.

Mr. Ford: OK and when it comes to promoters and people and also if you were to strip off fuel costs, because my guess is that on some of your freight contracts there is a component that may not to be easily negotiable, which will be their operating expenses. Are those things that will not be easily addressed initially meaning that you're going to have to kind of work through this period of higher fuel costs and probably make an investment initially, I would suspect, in building up a bigger team of promoters that, when you bring them on first, it takes a while for them to reach levels of productivity of your existing promoters.

Mr. Uba: Well, the new promoters we are bringing to the company, of course they have much less productivity then the senior ones, but at the same time, the compensation of those promoters are in line, roughly in line, with the contribution that they give to the company. So, actually we never saw any decrease in productivity or increase in sales expenses as a result of bringing new promoters to the company, because of this effect. As the productivity is much lower, their compensation also is lower in the first years in the company, so the net impact is, in terms of percentage of expenses, is nothing, they do not increase neither decrease the sales expenses as a percentage of sales. Did I answer your question or not?

Mr. Ford: You sure did, David. The only other thing was with respect to your freight contracts, because my perception in terms of logistics was there was an external component as well, it was not just picking internally and trying to fill demand or servicing the call centers, but there was a third party freight component, that they you're trying to work through as well. Is that correct?

Mr. Uba: The freight? Well, we might have some pressures from freight contracts. We will try to compensate that by offering larger volumes to our freight companies, the contractors, and see if we can compensate some increase in costs, in petrol prices for instance, or the fact that we are growing at higher rates at more distant areas from our distribution centers, which might add some costs, add some freight costs to the company. What we are trying to do, as I said, is to improve the negotiation with these freight companies and try to stabilize the cost around what it is today. We

... it is too soon for projecting or estimating any effect in the long term, but I would say that if we have a impact, a negative impact, it wouldn't be too much; very, very small as compared to the total expenses of the company.

Mr. Ford: Thank you very much David, that is good to hear.

Mr. Uba: OK, thank you.

Operator: Our next question comes from Julia Rizzo, from CSFB.

Ms. Julia Rizzo: Well hi, good afternoon everyone. I have two questions regarding the product development and the direct distribution channel. My first question is if Natura is developing new products out of the CST segment to be distributed through the direct channel? And the second question, following the same line, is if the company decides to get in a new product segment, for example vitamins or supplement tabs, what point or market characteristic the company considers, such as market size or penetration or returns, to add this new product to its direct distribution channel? Is there any color on that? Hello?

Mr. Uba: Just hold on one second, Julia.

Mr. Carlucci: Hi Julia, how are you? It's Alessandro speaking. Talking about the developing of new products outside the cosmetic industry, even though we are planning and studying the opportunity to develop products outside the actual industry, we are too far from this day to share with you some informations about. The important for you is to know that we are studying, we are planning, but we don't have now good informations about what we are going to do, what is the size of the market, which products, and what we ... how we plan to develop and launch and sell those products, so we don't have much more information about to share with you.

Ms. Rizzo: But could you please just provide like a figure, such as what kind of sectors or segments could be actually possible for Natura pick up and choose to develop and try to distribute through this channel? Like we considered outside the CST segment this and this, because of this and that? Can we just have a highlight on that?

Mr. Carlucci: Julia, like a said, we are far from the date that we are going to launch an outside, or a new category outside the cosmetic industry. But I think that, as you know, there are some new categories where direct selling companies do well, like - and are just examples - nutritional products, some lingerie products, products that can be sold by direct selling companies and we are studying among those categories. Maybe, the nutritional products are more related with our reason being, so you could think about the nutritional products, but as I told you we don't have a plan already done, so we are still studying.

Ms. Rizzo: OK, thank you very much.

Operator: Our next question comes from Robert Wertheimer, from Morgan Stanley.

Mr. Robert Wertheimer: Hi. My first question is on the price per unit and unit sales. Price per unit grew 10% year over year after a number of quarters are being flat to slightly down and I'm wondering how much of that planned for, did intentionally and how much was a surprise to you and why it happened?

Mr. Uba: Robert, this is David speaking. Actually, We had a 3% real increase in our average prices in the second quarter, differently from the first quarter when we had a real decrease in our average price. I would not say that that was a surprise to us, at the same time I would add that we were not planning to change this average price. We have, usually we have a certain degree of volatility in the demand among our categories; that also might be helped by our promotional efforts in a given period and by new products being launched and that is what we saw in the second quarter of this year. We had some very good new products being launched with a higher unit price, higher than the average for the company, and also some increase demand for some higher prices products inside each category. It’s a normal process in this business and it wasn’t actually a surprise for us, so with this increase in prices in the short term it is natural that the number of items sold decreases a little bit, since the commitment of our customers with our products might be considered fairly constant in the short term, so if in the short term we have an increase in average prices, the unit sold should decrease a little bit. Of course, this is an effect only for the short term. In the long term, we can have both effects. Average prices increasing as well as number of items and we saw that, we have been seeing that in the longer-term, if you look in the last three years, for instance. That is a summary of what happened in the second quarter.

Mr. Wertheimer: OK and if I can just understand the reason for the inventory build. Is that on purpose with more innovation in the pipeline and preparing for higher sales at the back half of the year? And you mentioned that inventories should stay high for the rest of the year and I just wanted to understand exactly why?

Mr. Uba: No, not really. The reason for the increase in inventory was that we were not happy with our inventory policy that prevailed until the end of last year. We were losing a reasonable portion of sales because of stockouts in our inventory. We decided to review all our inventory policy in order to decrease those stockouts and therefore to increase our sales. We ... in the first moment, the increase in inventories was higher than it should be because we are still developing, let's say, the details of the new inventory policy and we expect a certain excess that we have now to disappear by the end of this year. But the new inventory levels will be higher than we used to have before, because we were under invested in inventories until then. We were losing more sales than we should and you can see our gross margin is very high. So, any losses in sales can have a tremendous financial impact in our results and also, as I mentioned before to Bob, if we fail to fulfill 100% of our consultants' demands, we might have a very negative impact in our network of reps and also with an additional impact on sales. So, what we are doing now is trying to extremely improve the service we provide to our consultants. That's the real reason for increasing inventory right now.

Mr. Wertheimer: Great, and just one last. Did I understand correctly that the price increase was 3% real or about 9% nominal year over year?

Mr. Uba: Yes, you are absolutely right, 9% nominal and 3 real.

Operator: Our next question comes from Margaret Kalver, from Harding Loevner Management.

Ms. Margaret Kalver: Yes, hi. Just a quick question on the domestic competitive environment. Avon maybe becoming a little bit more aggressive, I read and do you expect to have higher promotional expenses or higher advertising costs in your Brazilian market going forward?

Mr. Carlucci: Hi Margaret, is Alessandro speaking. In fact, until now we didn't see any reasonable change in the competitive environment here in Brazil. We have important competitors like Avon, like Lever, like l'Oreal, like other big companies, like Nivea, but we didn't see any change until these days that should keep us planning more promotional investments in the next months. So we are running our plan as we started this year, so we are not seeing a big change in the competitive environment.

Ms. Loevner: OK, thank you.

Mr. Carlucci: You are welcome.

Operator: Our next question comes from Ms. Tânia Sztamfater, with Unibanco.

Ms. Tânia Sztamfater: Hi, good afternoon everyone. I have two quick questions. The first one regarding your small pilot on the bi-level Consultant Network. I'm wondering if you have any update on that, how were the results and if you are considering using that type of direct distribution in a larger scale?

Mr. Uba: Hold on a second, Tânia, please.

Ms. Sztamfater: OK.

Mr. Carlucci: Hi, Tânia, is Alessandro speaking. First of all, I would like to share with you that you have a lot of new initiatives on new kinds of sales models. We are trying every day to develop new kinds to reach the customer always by the direct selling system. We have, yes, we have a pilot, a project with a two-level system, among other projects that we have. We are trying to develop the actual one that we are using Brazil, but we still don't have results about this project, even though we are happy with the start of this pilot. But we didn't reach the point to share with you what we are going to do, if we are going to roll out, if we are happy with the results and when we finish this project we can share with you what we are going to do, but nowadays we don't have the final results.

Ms. Sztamfater: OK. Do you have like a timeline for discussing with the market this new product or this is still very premature?

Mr. Carlucci: I think that is premature. Maybe next year we could share something about this project, because if we change something it’s an important change in our model, so we are caring about, so before next year I don’t believe that we are going to have some better information about.

Ms. Sztamfater: OK, thanks, Alessandro. And the second and last question is regarding your new picking line. Since picking was one of your ... one of the most important bottlenecks in the production by the end of the last year and beginning of this year, I was expecting that with this new line starting to function in the third quarter, that would affect working capital needs and ... decrease working capital needs and might, and even might affect the costs of goods sold. As you mentioned that you expect the level of inventories at least to stay, at least in this level for ... still the end of the year, I wanted to know where are the impacts of this new picking line now functioning from the third quarter on?

Mr. Uba: Tânia, this is David speaking. We will have a small impact of this new line in our operational costs, not in the inventory. Inventory was increased not because we had a bottleneck in our picking line, but because we had some bottlenecks in our manufacturing process and also because of our promotional process and cycles. We need to be better prepared to face the volatility in our demand, mainly during ... for the items being promoted. So, the picking line, as I said, will have some impact in some sales expenses. We have more productivity in the picking process, no impact on the cost of goods sold, neither on the inventory level. And also we will be ready for facing new increases in sales, because we are almost doubling our picking capacity with this new line.

Ms. Sztamfater: OK, Thanks David.

Mr. Uba: Thank you.

Operator: Our next question comes from Daniela Bretthauer, from Santander. We ask you please to limit yourself to one question.

Ms. Bretthauer: Yes, I have a follow-up question, David. Can you share with us what level of stockouts that you are right now? I mean, you mentioned as a percentage of sales, but as a percentage of your inventories, what was the rate? And you said that you expect to decrease that and to what level? What level would think is a normal stockout for your business?

Mr. Uba: We, actually we do not disclose this information, but I can tell you that we wouldn't be happy if these stockouts were about 1%. We intend to work with these stockouts to be below 1% of our sales, but the level that we have today we don't share. Although it has a direct impact on sales, we are more concerned with the indirect impact, through the perception of our consultants in our quality of service, the service that we provide to them. There is where lies, probably, the best opportunity for improving our performance in the medium-term, by improving or by reducing the stockouts. Did I answer your question of not? Hello?

Ms. Bretthauer: ... question on the payout ratio for the first quarter, first half, excuse me. It was around 65% of earnings and I particularly was expecting a little bit more. I understand you already signaled another 10 million in July, but that is only for the second half of the year payout, which will only take place in April next year. So, I was wondering if the market can expect a higher payout during the second half of the year, so that for the full year the average payout could be around 75% or higher or if we are just expecting too much from the company on that front?

Mr. Uba: Daniela, actually we would prefer to compare our payout to the free cash flow generation for the period or for the exercise. We have been, we always declared that the company had no intention to build up cash, so that we would pay 100% of our free cash flow and we have been doing this consistently since our IPO. As we said in the first half of this year, our payout as compared to the net ... to the free cash flow was a little bit above 100%, actually 110%. So what we ... I can advance to you that that's our policy and we will proceed with it. By the end of the year, the beginning of the next year, we should pay that complement of dividends and income on net worth, juros sobre capital próprio, in order to keep with that policy, about 100% of the free cash flow generation in the year.

Ms. Bretthauer: So, in other words, we should really focus on the free cash flow payout rather than the net income payout? That is your guidance, right?

Mr. Uba: Yes, that is my guidance right now, because that is our policy, we should have our payout around 100% of free cash flow generation. Hello?

Ms. Bretthauser: OK, thank you.

Mr. Uba: Thank you, Daniela.

Operator: Excuse me, this concludes today's question and answer session. I would like to invite Mr. Bossert to proceed with his closing statements. Please, sir, go ahead.

Mr. Bossert: I would like to thank everybody who took part in our conference call and remind you that we are always at your disposal. I hope to see you again at our forthcoming meetings, so please check our event agenda on our investor relations site. Thank you very much.

Operator: That does conclude the Natura audioconference for today. Thank you very much for your participation and have a good day.

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