

Q2 2014 Earnings Call

Company Participants

- Emilio Fugazza, Chief Financial Officer and Investor Relations Officer
- Pedro Henrique Nocetti, IR Coordinator

Presentation

Operator

Good morning, ladies and gentlemen. At this time, we would like to welcome everyone to EZTEC's Second Quarter 2014 Results Conference Call. Note that this event is being recorded, that all participants will be in listen-only mode during the company's presentation. After the company's remarks are completed, there will be a question-and-answer session when further instructions will be given. (Operator Instructions)

Today's event is available through a live webcast that may be accessed through the EZTEC Investor Relations website at www.eztec.com.br/ir by clicking on the banner 2Q14 Webcast. The following presentation is also available for download on the webcast platform. All information are stated in Brazilian Reais and in BR GAAP and IFRS applicable to real estate developers in Brazil, except stated otherwise.

Before proceeding, let me mention that any forward-looking statements made in today's conference call, regarding business outlook, forecast, and financial results and operating targets is based on the beliefs and assumptions of EZTEC's management and the information currently available to the company. Forward-looking statements are no guarantee of performance. 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 the company and could cause results to differ materially from those expressed in such forward-looking statements.

I would now like to turn the conference over to Mr. Emilio Fugazza, Chief Financial and Investor Relations Officer, who will begin the presentation. Please Mr. Emilio, you may begin the conference.

Emilio Fugazza {BIO 16474296 <GO>}

Thank you so much. Ladies and gentlemen welcome to our presentation of the results of second quarter 2014. I am Emilio Fugazza, CFO and IR officer of EZTEC, and apart from myself, Mr. Pedro Henrique Nocetti, our IR Coordinator.

We have two highlights; the efforts, the operational efforts of the company to keep the margins quite similar to the last couple of years. And in order to compensate the investments of the company, and even in a challenging period for the sector despite of the diminish in the pace of sales and less visibility of the macroeconomic overview for the next couple of months. We have results we need [ph] and sustainable for the company.

I would like to ask you to refer the slide number three to talk about the first half 2014 highlights. From the operational side of the company, we have the launches. The launches reached R\$495 million in the first half of 2014 and contracted sales were R\$337 million in the first half; R\$204 million of the units coming from units launched in the previous years, which means inventory. We have been selling inventory in a very good price.

In terms of our Land Bank, the Land Bank position reached R\$5.2 billion by the end of the first half 2014, less than 13% the ratio cost for PSV. In terms of Land Bank R\$5.2 billion, we have the same amount of plant we had in the fourth quarter 2013. So we have acquired at least the same amount of launches we had in the periods. In terms of further financial highlights, we have the gross profit reaching R\$229 million in the first half 2014; 125 million in the second quarter with a gross margin of 53% in the first half.

In the second quarter, the gross margin reached 56%, we got in the very good performance of the sales in our interim target. In terms of net income, the net income for the first half reached R\$218 million with a return on equity of R\$22 [ph] million one of the highest in the real estate sector in Brazil. In terms of (Technical Difficulty) net debt position of the company was R\$78 million, we have to add in these account is the Performed Receivables of R\$344 million adjusted by IGP-M, less 12% per year, which is completely securitizable as we need this amount of money.

For now, we only keep these Performed Receivables in our asset just to compensate using IGP-M plus 12% legally [ph].

I would like to call for this conference call, Mr. Pedro Henrique to talk a little bit about the operational side of the company. Mr. Pedro, please.

Pedro Henrique Nocetti {BIO 20904123 <GO>}

Thanks, Emilio. Good morning, everyone. I would like to please turn to slide number four where we talk about the Land Bank, which as Emilio said ended the second quarter of 2014 with 5.2 billion in our PSV with an average cost of acquisition of 13%. It's very important to say that we are still finding good opportunities in terms of land acquisition and we brought in the second quarter two new lots, one of them in Sao Paulo and other one in Osasco in the Sao Paulo Metropolitan Area those two lots combined they achieved 200 million in our PSV.

So I would -- I would like to ask you to look at the chart in the upper right, where you can see the age of our Land Bank, you can see that 78% of that Land Bank was brought after 2011. You can see that this is not an old Land Bank, and this is a Land Bank bought recently with good margins which we provided at least 40% of gross margin.

Looking at the bottom left, you can see that 74% of that investment to the residential segment from the middle to the high end segment. And 25% to the commercial segment, which historically has higher margins.

Looking at the bottom right, you can see our Land Bank region in which 89% is in the Sao Paulo Metropolitan Area, that you can see that in the following years we will keep our region, our focus of operation.

Please turn to slide number 5, where we talk about EZ Towers. Here you can see the currently status of the project, you can see that our A is almost all of the facade installed and all of the facade because they are almost finished. The elevator they have already been installed in Tower A. In Tower B, you can see the structures vary. You can see that the facilities there, they're been installed and the external facade is installed in few days the 17th floor. It is very important to say that the estimated PoC curve we ended June 2014 with 67% of the projects complete.

We would still, we still expect to deliver Tower A by the end of this year and Tower B in the following year in 2015, very important to say Tower B is still in our inventory. Now, I'll ask you please to turn to slide number six, a slide which we showed you in the last quarter and we are keeping showing you in order to say how our projects are growing. How we are starting new construction and developing projects. You can see that compared to the last quarter to for the first quarter 2014, we increased the volume under construction.

It's very important to say that our construction cycle takes 13 months. So, projects which are initializing, they have less volume of construction being recognized and projects in which are for the half to the end of the construction, they have more volume occurring at the same time. And it's very important to say that for the year 2014, these volume of construction will increase because we are -- although we are delivering projects, we are starting new construction, we are expecting the construction of (inaudible) we will start the construction of projects that we have launched recently.

So I request to please turn to slide number seven where we talk about more operational figures, I will talk about the launches of the second quarter, 2014. In the second quarter, we launched two projects, one of the project was launched by the end of May, the Magnifico Mooca projects that [ph] to middle-high end segments with PSV of EZTEC's share of 48 million in which is 82% sold and we launched one more project by the end of June during the World Cup, the project Gran Quadra San Felipe with two phases, the phase Palazzo with 46 million of own PSV is now 51% sold, and the phase Giardino with 90 million PSV is 32% sold until this moment. Therefore, we totaled 184 million in own PSV launched in the second quarter and for the accumulated of the year 495 million.

So let's have to talk about sales but after that I will talk about launches in the third quarter 2014 and launches that you can expect for 2014. So in the slide number 8, talking about sales, you can see that we sold 119 million in the second quarter and 337 million in the first half of 2014, 60% of those sales, they come from units launched in previous years, units launched in 2013.

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As Emilio said, there was a very important share in terms of sales of units delivered, delivered units. Those were very important sales in the second quarter and they were very important in order, in terms of increase of gross margin. So you can see in the chart in the bottom right, you can see our inventory by delivery date.

You can see that most of our inventory comes per unit that we will be delivered from 2015 and on. I can also say that our inventory which corresponds to the unit delivered, it corresponds to 16% of the total inventory.

And projects which are under construction they're 81% sold and projects which were launched after December of 2013, they are 51% sold. So, we are very confident about our inventory. So we will sell our inventory with good margins in EZTEC, and at the speed that the company needs.

Also about sales, 75% of our sales came from Tec Vendas our own brokerage team, and almost all of the sales of units delivered they come from Tec Vendas. So, it's a very important brokerage and it's very important for the results of the company.

So finally, I request please to turn to slide number 9, where I would talk about launches in the third quarter of 2014 and upcoming launches.

In July, in the July 24, EZTEC launched the project Le Premier Flat Campos do Jordao in the countryside of the state of Sao Paulo. A project that to the -- a project which is located in winter station in the state of Sao Paulo that's going show [ph] the high-end segment, for the high-end residential segment.

We launched with own PSV of R\$119 million, it's now at this moment, it's 73% sold. We have also projects which are being prepared to be launched and will be launched when we feel that the demand is a good demand for EZTEC.

So, we have project like Legitimo Santana with 47 million of PSV, projects like Av. Morumbi with 88 million PSV, projects in Agostinho Gomes; 69 million PSV, all those projects we have in the city of Sao Paulo. Beside these projects, we have also one project in the Sao Paulo Metropolitan area with 120 million PSV. So, therefore what I'm saying is that beside the 640 million PSV launched until July of 2014, we have more than 300 million in projects to be launched, project that will be launched following the company's strategy. Therefore, I will hand back the presentation to Mr. Emilio Fugazza, who will talk about financial performance. Please Emilio.

Emilio Fugazza {BIO 16474296 <GO>}

Thank you very much, Pedro. Financial performance shown on slide number 10, let's talk about firstly net revenue on the top left, the chart you can see we had reached R\$435 million in first half 2014.

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In the second quarter 2014, R\$225 million, mainly because we have sold a lot of units in inventory and a lot of them performance units. Twice as much, the performance units we sold in the first quarter 2014. And I'd like to say in a very resilient prices, when you see on the top right, the chart of gross income and gross margin, you can see is more than welcome, these incremental margins in the second quarter from 51% in 2013 to 56% in 2014.

On average, in the first half the gross margin of the company was 53% comparing to first half 2013, 51%. Those numbers gross income, gross margin, net revenue, we are talking about the projects completely under control of the company, a 100% controlled by the company. And due to the IFRS 10 and 11, only 100% projects controlled by the company.

We are providing, releasing revenues and gross income. The other projects, where we have a share in the controlling group; obviously we're providing the results by the equity income. And on the bottom left, you can see G&A expenses as a ratio for net revenue and net revenue plus equity income. When you compare a net revenue plus equity income in ratio, you can see in the first half of 2014, 8.8% the ratio G&A over net revenues.

We know that this increment in the second quarter R\$29 million or almost R\$30 million, 9.4% is non-recovering event, it's non-recovering event because we have in the second quarter 2014 the program of owners with program of retention, the program to compensate the Board of Directors, the directors and the people working on the company.

We know that the size of that administration, the size, the amount of people working for the company was planned in a scenario that the volume of revenues were increasing in 2012 and 2013.

As you can see right now due to the distillation pace of sales we had in the first half of 2014, we are going to adjust the volume of G&A expenses; we have in the year of 2014. These are just the stake -- stake in our hands in the second half 2014, producing results over the second half of 2014 and the first half 2015.

In order to keep the ratio, G&A over net revenues plus equity income is around 8% to 8.5% overall.

In terms of selling expenses and with ratio, selling expenses over the net revenues, we have something close to R\$18 million, a ratio of 4.1%, decreasing compared to the first half 2013. The meaning of these is debts. We have less efforts to sell contracts completely under control of the company, a 100% control of the company than the projects we have coming from the equity income efforts. In that sense we're not forecasting an increment in this ratio to 4.5% as we had in the first half 2013.

Turning the page to number 11, keep talking about financial performance, on the top left, we have the financial results.

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The financial results in the first half 2014 was R\$37 million almost twice as much the first half 2013 financial results. The ratio and over net revenue is about 8.5%, due to the fact that we more performance units under our management using IGP-M plus 12% yearly which means something close to 17%, nowadays something close to R\$344 million using IGP-M plus 12% yearly.

And, also we have more gross cash debt we have in the past, due to a lot of projects we have been delivering, generating cash for the company. In that sense and increment into this space in Brazil over around 11% yearly, its providing more financial results than we had in the past.

Talking about the equity income and the results coming from equity income, as of we have in the first half on the chart on the top right, the first half 2014, R\$40 million.

This stake on average on the control of the company is about 54.9% compared to 50.9% in the first half 2013. Less results coming from an equity income mainly because of the commercial expenses as you can see we have provided in our earnings release of the second quarter.

It (inaudible) cost, we have projects mainly in the Metropolitan region of Sao Paulo, projects like Joaquim in Osasco, projects together, answering for, calling for more than R\$2 billion in on PSV in non potential sales value and the amounts of equity income coming from those projects can release a gross margin around 40%.

Nowadays, the R\$40 million coming from equity income calls for almost a 20% of the whole net income of the company in the first half of 2014. 80% of the net income of the company is coming from projects that are 100% controlled by the company.

Net income, talking about net income, on the top left you can see R\$218 million in the first half 2014 and the net margin, a rough over around 50%, 2 percentage of points more than the first half 2013, due to the target that we had, we have implementing gross margin and we have less commercial expenses and more weights on financial results in these results provided by the first half, 2014.

Finally, I'd like to say that the backlog margin and backlog results, you can see on the bottom right of this slide, the result we recognized over around R\$431 million and the backlog margin 54%.

The backlog margin of 54% is almost the same of one year ago. This is more than necessary to keep the gross margin of the company, we have been releasing in our P&L over 50% for the next couple of years.

Turning the page to slide number 12, let's talk a little bit about cash position. In terms of cash position, you can see the chart, the chart in the middle of the slide, you can see a net debt position in the first quarter 2014 of R\$94 million and gross cash R\$282 million.

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In the second quarter, an increment in gross cash R\$344 million in an decrement in the net debt position from R\$94 million to R\$78 million. It is important to say that we have been providing these increments in the cash position, this is particularly because we have been delivering a lot of Towers, lot of units and we have been bringing these contracts to the Bank receiving the money from the bank and through -- from the clients, through the banks.

It's important that you see on the bottom of this slide, just a comparison because R\$246 million of our debt, its coming from the EZ Towers' construction and after we delivered the keys to Sao Paulo [ph], our buyer for the first tower, we are delivering along with the tower, the total amount of debt coming from this Tower, nowadays in order of R\$246 million, thinking these on mind, you can see that the net debt position will turn in a net cash position of R\$168 million, an increment coming from the first quarter 2014 of R\$115 million, an increment of 46 to 45.9%. So only the EZ Tower is truly responsible for more than 50% of the total amount of gross debt we have in our balance sheet.

In these we will turn in a net cash position, probably in the first half of 2015. Turning to slide number 13, capital market, it's important that you see our net asset value statement. You can see at the bottom line of these statements.

In the second quarter, 2014, the total amounts of net asset per share we have is about R\$29 per share, accounting from R\$27 per share, just one year ago. It's important because it's an increment of R\$2 per share only in a period of 12-months even in a challenging scenario as we have been passing through. It's important to say that the total amount of debt we have provided by these statement is only just for production. We have no working capital, we have no debentures, we have no or the kind of debt but the debt for production, we have been paying this amount of debt bringing contracts to the bank in order to compensate the debt.

The total amount of receivables we have from a unit sold under construction right now is about R\$1.7 million, in terms of performed receivables, R\$344 million, the first one adjusted by (inaudible) monthly and the performed receivables adjusted by IGP-M plus 12% monthly. It's important to say all of the assets we have, this is by costs, when you see the Land Banking venture R\$594 million this is the real, the current cost over the Land Bank R\$5.2 million, Pedro mentioned before. On the right side of this slide, you can see the total amount of results we have been provided every first half of yearly since 2010 and the amount of written on equity provided by these results.

In 2010, our net income was R\$103 million. In the first half 2014, R\$218 million, it's important to compare in a network scenario without the increment provided by the selling of the EZ Towers in the first quarter 2013. So the volume of net income we've provided this half is quite strong.

Providing a return on equity of 22%, it's almost twice as much, the (inaudible) in Brazil.

Talking about it, I would like to call the slide number 14, this slide number 14, it's a slide which explain our mindset for this time we have been passing through. This time we have

been passing through, we can see ourselves as an asset management, when you put or when you buy a stock, when you buy a share of the company of EZTEC, you're buying a company that can provide a management with productivity and efficiency.

When you see our data compared to the sector, I only use the comparison from 2013 and the first half of 2014. On the top left, you can see gross margin. In 2013 and 2014, the gross margin of the company remains the same, keeping the gross margin over around 52% to 53% comparing to the sector around 24% to 26%.

Here, we are talking about how to generate, how to provide wealthy, wealthy because we have been increasing the volume of revenues of the company with margin, margin to observe any kind of scenarios we have been passing through or in a challenge outlook in order to provide discounts to sell quickly our inventory without any kind of problem. When you see the return on equity of the company on the chart on the top right, you can see 2013 is that provided 35% comparing to the sector over 7%. In the first half 2014, we have 22% comparing to 4% of the sector, here we have been talking about how to compensate the investments on land on G&A, on commercial expenses we have been doing in our new launches, we have to use the word success. When Pedro mentioned to you that we have launched in the first half, two products just in the middle of the World Cup, a project in Sao Paulo, projects in the countryside of Sao Paulo, the (inaudible) both project selling something close to 70% to 80% even in this scenario of the World Cup, the scenario when the economy is decelerating.

The scenario of a lot of the peers are making huge discounts in order to generate cash to pay their debt, we have been selling project to provide a return on equity all the 20% it's a quite success, it's a way to manage a company thinking about a long run. And all of it, we have been doing without wasting money.

This is very important, people please, it's important here to say that when you compare on the bottom of this slide, the balance sheet of the company, 3% net debt to shareholder equity compared to 78% net debt to shareholder equity of 16 publicly traded companies in the real estate sector, we can say that we have been providing margin, we're compensating our investments with a return on equity twice as much the (inaudible) in Brazil, results putting ourselves in a risk of raising money without sufficient cash to pay it and having to sell the merchandize with huge discount to provide cash, to generate cash.

Nowadays our seat is a better seat than the others; we are in a position among all the real estate developers in a better position than the others, it's specifically because we can manage our inventory, we can manage our launches, we can manage our Land Bank the way in order to provide the best results to our shareholders.

For now, our (inaudible) is how to increase wealthy in this challenging scenario? In this scenario in which this perspective, the outlook for Brazil is not quite sure, how to manage a deal to the sources with productivity and efficiency?

And I think we have been doing well. Thank you so much and we are completely open to your questions. Thank you.

Questions And Answers

Operator

Thank you. Ladies and gentlemen, we will now initiate the question-and-answer section. (Operator Instructions) Alright, as there are no questions at this present time, this concludes our question-and-answer session. At this time, I would like to turn the floor back to Mr. Emilio Fugazza for any closing remarks.

A - Emilio Fugazza {BIO 16474296 <GO>}

Ladies and gentlemen, I would like to say that in the Portuguese conference call, there were a lot of questions, answered by the Directors in this conference call. In that sense, we are providing the translation of these questions to provide you some kind of doubts people in Brazil have about the real estate market and about the company.

And we are more than open, we are more than welcome to answer any questions you may have in the future. Apart from myself, Mr. Pedro Nocetti, our IR coordinator and Mr. Erik Zarzur in terms of IR analyst. Thank you so much and see you in the next conference call.

A - Pedro Henrique Nocetti {BIO 20904123 <GO>}

Thank you so much. Have a good day.

Operator

Thank you. This does concludes today's presentation. You may disconnect your phone lines. Have a nice day.

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