Q1 2013 Earnings Call

Company Participants

- Elie Horn, Chief Executive Officer
- Jose Florencio Rodrigues Neto, Vice President of Finance and Investor Relations Officer
- Rafael Horn, Chief Operating Officer

Other Participants

- Eduardo Silveira, Analyst
- Luiz Mauricio Garcia, Analyst
- Marcelo Motta, Analyst
- Rafael Pinho, Analyst

Presentation

Operator

Good morning, ladies and gentlemen. Thank you for waiting and welcome to the Cyrela Brazil Realty Conference Call where the results of the first quarter 2013 will be presented. All participants are connected only as listeners. And later on, there will be a Q&A session for which instructions will be given. (Operator Instructions) This call is being recorded and the recording will be available at the company's website at www.cyrela.com.br/ri.

This call is being simultaneously translated into English and also through the webcast. Questions can be asked normally by overseas participants. You can access the earnings release disclosed yesterday, May 13, after close of trade on the BM&FBOVESPA Stock Exchange on the Company's website, that's www.cyrela.com.br/ri.

Before we proceed, we would like to clarify regarding the company's business prospects as well as projections, operational and financial goals concerning its potential for growth are forecast based on the expectations of the management for the future of the Cyrela. These expectations are highly dependent on domestic market conditions, on the general economic performance of Brazil and international markets, and are therefore subject to change.

Today, we have with us Mr. Elie Horn, CEO; Mr. Rafael Horn, COO; Mr. Jose Florencio Rodrigues Neto, Vice President of Finance and Investor Relations Officer.

Now, I'll hand over to Mr. Elie Horn. You may proceed.

Elie Horn {BIO 1823000 <GO>}

Good morning, everyone. Today, we'll disclose our results for the first quarter of 2013. These are consolidated and solid results, consolidated because it's a guidance to our company in the last few months and also consistent in terms of the results showing an increase of the gross margin for the ninth quarter in a row; consistent in terms of our financial policy always focus on consolidation and also to generate cash and also in terms of all the debt we'll be showing you today and also according to our strategy to strengthen our D&A and to go through better processes. In our D&A, we have the results of the quarter where we have an increase in the city of Sao Paulo and Rio de Janeiro and for the Mia Casa Mia Vida the program made from our partners. And we go on with our processes. For this quarter, we have in Sao Paulo a strong relationship for our clients and approval of credit lines. And our team is more and more focused with the business knowledge, focusing on entrepreneurship and technical capacity.

Consistency of our management of people with consolidation of the cycle of bonus payments based on their geography and on the cultural alignments according to our team's result that way we keep working day after day, developing innovative products with quality and within our budget, always focusing on enchanting our clients and focusing on our business. So we focus on our suppliers, partners, shareholders, all stakeholders that have consistently supported us. So I'd like to pass the word to Mr. Rafael, who will talk about the results that are consolidated for this quarter.

Rafael Horn

Good morning, everyone. On slide number five, we'd like to comment the Cyrela's consolidated results. For the first quarter of the year, we launched R$955 million, of those (Technical Difficulty) segment represented 21% of the total with the launch of R$200 million within Tier 1 through our joint venture with Cury. Cyrela's participation in the launches reached 59% in the quarter, compared to 65% of the previous quarter.

In this quarter, (inaudible) was launched with 28% of Cyrela share and on the part in Rio developing with 43% of Cyrela's participation. Together, this [ph] represents 30% of the PSB launched in the period. Geographically speaking, the launches for this quarter took place in Sao Paulo and Rio de Janeiro.

Now moving on to slide six, let's talk about our sales performance. In this quarter, contracted sales reached approximately R$1.4 billion including partners. This sales volume was 11% higher than the expected volume year-on-year. Sales in the economic plus MCMV program represents 38% of total company sales in the period. 3,922 units were sold this quarter, not including Tier 1 units compared to 3,516 unit year-over-year. Figures translate into an annual sales over supply of approximately 51%, 50% if we disregard Tier 1. The company believes that this sales beat of approximately 50% per year is within the new market dynamic and already uses it in the launch feasibility. The states of Sao Paulo and Rio de Janeiro represent together 70% of our sales.

Now, moving on to slide number 7. Excluding Tier 1, in the quarter inventory sales correspond to 71% of the total while product sales launched in the period corresponds to

29%. In terms of performance per season, we saw 56% of developments launch this quarter, 44% if we disregard Tier 1.

Project developments launched in the fourth quarter last year are already 61% sales; launched in the third quarter, 66%; and the second quarter, 76%; all with sales speed higher than forecasted.

Now, on slide 8 we'll talk about Cyrela's total inventory. At the end of the quarter, market value inventory totaled 6.3 billion reals, a 4.3% drop compared to the previous quarter. Our inventory movement can be seen on the chart on the right. In the quarter, we sold 821 million in inventory. Of these, 146 million were ready units. Ready units represents 13% of our total inventory, 11.5% drop compared to the previous quarter.

On slide 9, we can see the details of ready units. The concluded units represent 843 million reals, a reduction of 110 million compared to the previous quarter. Analyzing this inventory per delivery season, you can see that 58% was delivered during 2012. As said before, last year, we delivered 68 developments launched in 2007 to 2009. These seasons had more delays in the works and consequently more distracts, increasing our ready units. We can see that 40% of the ready units are focused on the northeast and in the state of the Espritio Santo. There's a reduced demand and we expect that there's going to be a slower sales speed from now on.

Now, let's move on to slide number 10. For the first quarter, Cyrela delivered 17 developments representing 5,186 units, representing a SGE(ph) of R$1 billion.

Now, I'm going to pass on to Jose Florencio who will talk about the financial results.

Jose Florencio Rodrigues Neto {BIO 17498585 <GO>}

Good morning. Before talking about the financial results for the quarter, I'd like to comment on the accounting standard change. As you know, as from this quarter, the consolidation rules are now following the IFRS recommendation. So, to understand the evolution of results and maintain historical comparability, all the explanations or variations in this presentation were made according to the formal rules and we've added the figures, according to the new rules for information purposes. As from the next quarter, we will compare according to the new rules as possible. Therefore, we believe that the transition can be easier to be understood by everyone.

Now, let's move on to the figures. On slide 13, we're going to talk about the financial results. Gross revenues reached 1.3 billion for the quarter, 14% lower than the previous quarter's revenues. The lower volume in revenues is for three reasons.

First, the reduction in the number of active work sites, from 203 work sites in the first quarter '12 compared to 181 in 1Q13. The high volume of delivery in 2012 and the lower level of launches in that last year also are a reason for that.

The second fact is the delay in recognizing the Tier 1 revenues from MCMV program. In the last quarters, we launched upon approximately 800 million in Tier 1, and recognizing these results only takes place after the works begin, which could be six months after the launch. That is still according to the formal consolidation rule.

The third one is a lower participation of Cyrela in quarter sales. As said before, in this quarter, Cyrela's participation was 70% in 1Q13 compared to 79% in 1Q12. We believe that percent should increase in the upcoming quarters.

Gross margin increased increased for the ninth consecutive quarter and reached 33.3%. EBITDA for the quarter was 254 million, 25% higher than the 200 million recorded in 1Q12. EBITDA margin reached 20.2%, a 6.4 percentage point increase compared year-on-year. In the quarter, net income was 179 million, 52% higher than 1Q12. Gross income was 14.2% high -- 8.2% higher than 1Q12 and 3 percentage points above net margin in 4Q12.

Now, let's move on to slide number 14. (Technical Difficulty) I think we had a problem here, so I'm going to start off with slide number 14. For the first quarter, the number of transfer payments was 1.2 billion, 47% higher than 1Q12 and 32% higher than 4Q12. In this quarter, we had an expressive volume of payments, total payments; 500 units than the average history, which represented an additional volume of -- and we would like to highlight the Nova America and Salvador shopping business developments, which represent 56% of units paid off.

On slide 15, we have information about indebtedness. The gross debt at the end of the quarter was R$3.9 billion compared to 4.5 billion in the previous year, a 6.7% reduction or 600 million. Of this total, 21% refer to financing of construction with SFH and 79% in the long-term. With the strategy adopted in 2012 to replace the SFH of development in the conclusion phase for corporate debt, which are more affordable with the longer term, the current corporate debt percentage is 69% of the total. This year, with the reduction of the finance rate, we can have -- we can use this type of line more intensely. Cash flow at the end of the last quarter was 1.7 billion compared to the prior quarter. And we still have a reduction of the net debt going from now reaching 2.4 billion for this quarter. Our net indebtedness in relation to P&L reduced again. So we have a leverage ratio now of 40%. The average debt is of 111% of CDI, which is lower compared to December 2011. And if we see the CDI of the period, there was a drop. And we are talking about an increase of the spread over CDI.

For slide 16, we'll be talking about cash generation for the quarter. We present 180 million, compared with a generation of 240 million from the previous one and a cash burn of 6 million for the first quarter of the previous year.

We must remind you that the generation of 240 million of the previous quarter about 100 million are from non-recurring event. The operational generation for the quarter was motivated by the strong volume of settlement and transfers due to high volume of delivery, which took place in the previous quarter. We are confident that we'll generate cash that is relevant for this year.

Now, we'll pass the session to Q&A. Thank you.

Questions And Answers

Operator

Ladies and gentlemen, we'll now start the Q&A session. (Operator Instructions) The first question comes from Rafael Pinho from Morgan Stanley.

Q - Rafael Pinho {BIO 15321539 <GO>}

Good morning, everyone. Florencio, you mentioned a bit about the reduction in terms of (inaudible) and that is important in terms of what has already been done. Can we expect some gain? We just want to understand a bit about what is a normal level after the whole work that you went through last year. Is there anything else that we can see for us coming?

A - Jose Florencio Rodrigues Neto {BIO 17498585 <GO>}

Well, good morning, Rafael. As I mentioned in the previous calls, our target for this year is to absorb the compensation rate increase established by the union. So we see 9% and we will absorb that during the years. So, we will keep the nominal value from the previous year. So, we believe we'll be able to reach that even at a better level, if we still find some improvements to carry out because of the consolidation of back-office as we mentioned in terms of charging transfer credit.

So, that's something that will carry out during the year, but I do not like to give you a specific number. So, if you understand as well keep the same nominal value, that's important. But we must focus also on the sales focus, which is bit more complicated, why because on one hand, there is a Phase II increase but we need to intensify to sell some inventory and it's not very clear how we're going to go about. But in any case, it has to be made clear to you that we're working hard on reducing sales expense as well.

Q - Rafael Pinho {BIO 15321539 <GO>}

Thank you very much, Florence. Have a good day.

Operator

The next question comes from Mr. Luiz Mauricio Garcia from Bradesco.

Q - Luiz Mauricio Garcia {BIO 17432519 <GO>}

Good morning. Good morning everyone. I just had two questions, the first one related to the outlook for future launch as I'm sure there is relevant pipeline there for the future to come. And in terms of a percentage of Cyrela to be more relevant that will actually contribute to the revenue, I'd like you talk a bit more about the pipeline for launches. Explain if the Cyrela percentage will increase and if that will actually give a good help in terms of revenue.

And the other aspect is related to cash generation. So, I know there are some scenarios that is variable, but I'd like to understand how this will keep being analyzed by the Company the extraordinary dividends, repurchase, or any other issues that is in the agenda as well to the counsel when it comes to the generation of cash. That should be an increase for the future also where we see probably a peak of delivery in 2014 that will be greater than 2013 when actually you have the transfer of the 2010 project -- developments, excuse me. Basically these are my points.

A - Elie Horn {BIO 1823000 <GO>}

Good morning, Luiz. In terms of launches, we expect to have an increase of launch for the next quarter. And we also expect to see a higher volume for the second part of the year and an indicator of our expectation of increase, therefore, the region of Sao Paulo, which was our ideal in the past. We expect by half of the year to basically have same level of launches that we did have throughout the whole last year so that would be our area of recovery that is relevant.

In terms of the Cyrela percentage or share, I expect yet an improvement, however, not expect to be at the same record level basically because of Tier 1. Tier 1 is something that we are actually taking advantage of, and it's through the Cury joint venture. So that already gives an idea of the percentage of Cyrela. In any case, we do expect an increase vis-a-vis what we saw in this quarter.

In terms of cash generation, it was quite strong for this quarter. We cannot say that we'll have the same for all the other quarters. It just varies a lot over to quarters depending on the purchase of lands and other factors. But we do expect a relevant generation of cash. In terms of what to do with the generation of cash, we mentioned that in the previous call and there are many things on the table in terms of what to do. So we already approved an extraordinary dividend. We will have surveillance of the generation of cash for the first few quarters, and if we keep having that we will analyze extra dividend or reducing debt ratios or even have a buyback program.

So that is something that is in the discussion table something that the Board will have to approve. In any case, it's very important to focus on the consolidation of the company. That is very important. Thank you.

Q - Luiz Mauricio Garcia {BIO 17432519 <GO>}

Thank you very much. Thank you, Florencio

Operator

The next question comes from Eduardo Silveira, Banco Espirito Santo.

Q - Eduardo Silveira {BIO 16201252 <GO>}

Good morning to everyone. I have two questions. First is a follow-up from what we've mentioned in terms of what to do with the cash. Is there a minimum leverage ratio that you consider that under that you would have an increase of dividends or buyback, or anything related to that? Is there a minimum ratio that you were considering in terms of extraordinary dividend also in inventory or ready units? Is it something that is not typical in terms of giving a discount? So how do you actually see a sale for this ready inventory? What's the outlook on that?

A - Jose Florencio Rodrigues Neto {BIO 17498585 <GO>}

Well, Eduardo, in terms of the leverage ratio, at the level which we have reached, which is about 40% is a good level to be at. We shall reduce a bit, but it's really close to what we expect to be good for the company. And yes, we will have good problems to deal with in terms of what to deal with or what to do with the extra cash generated, but we've done a bit of everything in the past. Just to talk about what we've already done, buybacks. We have already approved an extraordinary dividend. We have already purchased strategic plans and we have already reduced debt.

So, that is what we have in the agenda. So, we will over use of these options and what will be the decision of the Board in terms of how to distribute the generation of extra cash, we'll have to wait third quarter to see what the Board will define.

A - Rafael Horn

Now, Rafael here speaking. In terms of inventory in the northeast and in the state of Espirito Santo, we're not going to have lowering the price for here. So, get money and we want to have the best of returns. We can't pre-development, but what we're working on is to focus, focusing on sales force, media campaign and obviously we are not in the academy. There is a level of liquidity and you need to know exactly how you're going to sell based on that.

So, you need to really be patient and sell at the best price better. So, we don't want have a situation where we have no more inventory for the northeast and Espirito Santo. That's not where we're going be doing. That's not our profile. We're going to be able to remain there and hold ourselves. So, we do not want to generate expectation. In terms of short-term, we're going to have inventory of Salvador and Espirito Santo will be sold, but we're going to have to deal with that for few months to go and we'll reflect that in the next quarter.

Q - Eduardo Silveira {BIO 16201252 <GO>}

Thank you very much. Have a good day.

Operator

The next question comes from Marcelo Motta from JPMorgan.

Q - Marcelo Motta {BIO 16438725 <GO>}

Good morning. I'd like to know if you can talk a bit about Cyrela. We've seen some media news talking about different shareholder's structure. And I'd like to know a bit about you in terms of how we're going to see an investment also in terms of cash if there's something to do with these type of initiatives.

A - Jose Florencio Rodrigues Neto {BIO 17498585 <GO>}

Well, I don't really see opportunity to use the generated cash for some acquisition or getting into other segment to do that. We already have the land bank, it's something we do like and we're going to go organic step by step do not expect any mind-boggling action. It will be step by step and slowly but surely. We want to focus exactly on the segment we're in. Thank you.

Operator

(Operator Instructions) As there are no further questions, I would like to pass the floor Mr. Elie Horn for his closing comments.

A - Elie Horn {BIO 1823000 <GO>}

Ladies and gentlemen, cash generation, inventory sales, quality of construction, innovation, and construction, and entering the other sectors allows the company to last longer in time. There are many ways to work in this market and we've been present in almost all of them. And to make sure the company is solid and lasts long, we have to be consistent and use capital at least as possible very solid as always. Thank you for your presence and I hope to hear you in the next quarter with better days if God's be. Thank you very much.

Operator

The Cyrela Conference Call is closed. Thank you for your participation and have a good day. Thank you.