

Q4 2014 Earnings Call

Company Participants

- Eric Alencar
- Raphael Horn

Other Participants

- Eduardo Silveira
- Fred Mendes
- Guilherme Vilazante
- Luiz Mauricio Garcia
- Nicole Hirakawa

MANAGEMENT DISCUSSION SECTION

Operator

Welcome to Cyrela Brazil Realty Conference Call to discuss the Fourth Quarter of 2014 results. At this time, all participants are in listen-only mode. And later, we will have a question-and-answer session, and instructions will be given for you to participate. As a reminder, this conference is being recorded, and it will be available at the company's website at cyrela.com.br/investorrelations.

This call will be simultaneously translated into English and broadcast over the Internet. Questions will be asked by participants connected from abroad. The earnings release published yesterday, March 19, after the closure of the BM&FBovespa trading session, may also be accessed at the company's website.

Before proceeding, we would like to clarify that forward-looking statements that may be made during this call related to the company's business prospects, as well as projections, operating, and financial targets linked to the company's growth potential are assumptions based on the management's expectations about Cyrela's future. Such assumptions are highly dependent on domestic market conditions, on the country's economic performance and on international markets as well, and as such, they are subject to change.

With us today, we have Mr. Raphael Horn, Co-CEO; and Mr. Eric Alencar, CFO and Investor Relations Officer.

Now we would like to give the floor to Mr. Raphael Horn. Mr. Horn, you may begin.

Raphael Horn {BIO 19714328 <GO>}

Good morning, everyone.

Ever since the election last year, we have been seeing many news about adjustments in the economy the last few months. And in fact, the beginning of 2015 has already shown that it is very challenging politically, institutionally and economically. And this affected directly the economy. And these challenges may be overcome when the large (02:24) also in recovery which makes the attractiveness of Brazil even lower for investors from abroad.

In this moment of uncertainty, we have to be very firmly grounded. We have to be differentiated by our experience and we have to anticipate and be conservative and have a vision of opportunities. The financial culture of the company has given us the guarantee that we can take advantage of the good deals that might appear in the market conditions today. We need a very well qualified sales team, product by product management and differentiated market strategies, focused on inventory sales and assertiveness in the new launches.

In this end, it's important to stress that there are good launches with innovative products and adequate (03:20) for the regions are winners. In the fourth quarter, we launched 22 projects, (03:28) São Paulo, capital and interior (03:30) Rio de Janeiro and south markets. And with the assertiveness of launches in 2014, our focus on cash generation is BRL 277 million (03:40) in the year. And we've been generating only cash with operations but also some efficiencies in working capital as well, mainly with the decrease in the term of transfers vis-à-vis the banks and we use this cash prioritarily to be returned to our shareholders in mandatory dividends and repurchases, 10% yield over the company's market cap.

2015, we have 100% of the problems or the full performance vintages and the focus on inventory sales, especially the finished inventory will be maintained. Of course, we are going through a cyclical moment in that sector and we will be focusing this with a lot of caution and efforts.

Each area of the company has to have an ownership spirit and a commitment to its meritocracy. We have three pillars: consumers, people, management. And the result would come from all forces. We cannot count on luck.

And now we are going to talk about our operating results. On slide number five, we have the Cyrela results. In Q4, we launched BRL 2.3 billion vis-à-vis BRL 2.7 billion in Q4 2013. In the year, launches were BRL 5.8 billion and 12% lower year-on-year. The participation of the company in the product launch went from 70% in 2013 to 83% in 2014.

Net of swaps and launches of the MCMV Faixa 1 the volume launch increased 7% year-on-year. And in this quarter, we highlight the launches of Living Magic in Osasco and In Side Península in Rio with a good sales performance.

Slide seven, our sales performance in Q4 2014, sales were BRL 1.9 billion approximately vis-à-vis BRL 2.3 billion in the same quarter in 2013. In the quarter, we signed one contract of the MCMV Faixa 1 approximately for BRL 100 million vis-à-vis BRL 470 million in the same period in the previous year.

In the year – I apologize – the sales of the company were BRL 5.7 billion, 21% lower than with BRL 7.2 billion in the same period in 2013. And this drop was partially offset by the increase in the CBR participation in sales from 71% in 2013 to 82% in 2014. Net of swaps and sales in the MCMV Faixa 1, the sales decreased by 7% year-on-year. São Paulo and Rio corresponded for 81% of our sales in the quarter and 81% for the year.

On slide number eight, we are going to talk about our sales speed. Sales in the quarter led us to reach an annual SoS of 41% and excluding Faixa 1, 44.8%. Performance per vintage, 42% of the projects launched were sold in this quarter. And on the right, you can see the performance of sales per vintage. The projects launched between the fourth quarter of 2013 and the third quarter of 2014 have on average over 55% of the pre-sales.

On slide number nine, we are going to talk about the total inventory of the company. Market cap was BRL 7.3 billion, a 6.2% increase vis-à-vis the previous quarter. Inventory movement, so change you can see on the right with previous inventory 19% of the total inventory. And we have already been talking about that this refers to the delivery of high volume of inventory in areas where demand is low.

Finished units on the next slide. In this quarter, we were able to sell 22% of our finished units in the period and adding this the appreciation of the units with inventory further hike of 11% vis-à-vis the third quarter of 2014. We know how important this is for the company, and we will continue to focus our investments here. The Northeast and Espírito Santo represent approximately 40% of the finished inventory of the company, and that's now at (09:08) 76% of the Northeast.

And on slide number 11, we talk about the delivered units. In this quarter, we delivered 20 projects, representing 5,500 units approximately. And in the year, we delivered 81 projects with 20,800 units delivered. The units delivered in the quarter represented BRL 1.8 billion of PSV. And in the year, this amount was BRL 7 billion approximately.

I think now Eric will be talking about our financials.

Eric Alencar {BIO 18098474 <GO>}

Thank you, Raphael.

Good morning. On slide 13 we will be talking about our financial results next. Gross revenue BRL 1.6 billion, 4% lower than the last quarter, 9% higher year-on-year. Gross revenue was positively impacted by two factors, a higher evolution of work underway which generates higher acceleration and POC and a higher proportion of finished and semi-finished products. For the year, it was BRL 5.9 billion, representing a 7.5% growth over 2013.

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Gross profit BRL 495 million. For the quarter, 2.5% higher on a quarter-on-quarter basis and 8% higher on a year-on-year basis. For the year, gross profit reached BRL 1.9 billion, a growth of 6% over the same period last year.

Gross margin for the company was 32.3%, 2.4 percentage points higher than the 29.9% of the previous quarter and lower than the 32.9% of the fourth quarter of 2013, specifically in this quarter that's why a decrease in gross margin occurred due to the sales mix of the products. Q4 had a higher percentage of sales of finished and semi-finished products. And of the poor performance vintage, we typically have a lower margin for the year, 32.1% gross margin, 0.6 percentage points lower than the margin of 2013.

I would like to remind you that in 2014 the gross margin was impacted by the launch of two major projects, with a high percentage of swaps, Reserva Golf and Lead Américas. And these projects by accounting criteria has a gross margin which is more than the average of the company. On the lower left, we have the EBITDA. EBITDA for the quarter was BRL 256 million, 8% lower than the EBITDA of the previous quarter, and 10% year-on-year. For the year we have an EBITDA of BRL 1 billion, 5% lower than the BRL 1.1 billion in 2013.

Net income, BRL 150 million in the quarter, 16% lower than the net income of Q3, and 18% lower than the fourth quarter of 2013. For the year, the company's income reached BRL 661 million, a reduction of 8% vis-à-vis 2013. And the biggest impact in 2014 when compared to 2013 was BRL 35 million (12:39) increase in commercial expenses due to a higher effort to sell inventory provisions for litigation and the BRL 23 million increases referring to third-party services in the G&A. Thus, our net margin was 9.8% for the quarter compared to an 11.1% in Q3, and 13.1% in the fourth quarter of 2013. Margin for the year was 11.4% vis-à-vis 13.4% in 2013.

Now slide 14 talks about our profitability. In Q4 2014 we had our ROE measured as the net income of the last 12 months over equity of 11.9%. In line with the strategy of generating value for our shareholders, over 2014, we paid out BRL 500 million: BRL 171 million were the minimum mandatory dividend and BRL 329 million in share buyback. In 2015, we have already bought back BRL 46 million in financial volume. Earnings per share of the company reached BRL 0.39 in the quarter vis-à-vis BRL 0.46 in Q3 2013 and BRL 0.45 in the same period of the previous year.

Now slide number 15. That talks about the financial solution for the client. In Q4 2014, we transferred and paid off, and we had trust deeds of 17% lower than in Q3 2014 and 6% less than Q4 2013. In terms of units, 3.4%, 22.7% lower than the previous quarter and 23% lower than the same quarter last year. For the year, we transferred and we paid off and had trust deeds, BRL 3.8 billion. The volume of transfers and payoffs continued to be at healthy levels.

On slide 16, we will be talking about cash generation. The company presented in the quarter with cash generation that was record. In the quarter, the operating cash generation BRL 362 million and the strong cash generation is a consequence of three main factors: high volume of deliveries over the year; lower disbursement with land

acquisition; and operating efficiency to reduce the timeframe for transfers. BRL 867 million in the year vis-à-vis BRL 201 million in the same period of last year.

On slide 17, we will be talking about indebtedness. The gross debt at the end of the quarter was BRL 3.8 billion; cash position, BRL 1.8 billion. With that, our net indebtedness was BRL 2.1 billion in total of the gross debt, 58%. Our financing for construction is 67% long term. Our net indebtedness, vis-à-vis our equity was 32.8% vis-à-vis 37% in the previous quarter. And the low level of indebtedness, together with the cash generation delivered ratify (16:12) the principle of sound financials of Cyrela and place us in a privilege position to tap into the advantage of the real estate market.

Now we would like to open for questions.

Q&A

Operator

Our first question comes from (16:47) from Itaú BBA.

Good morning. Thank you for the call. I have two questions, basically focused on ROE. Taking into account that this is a more difficult year, what is the minimum cash in absolute terms? And what about the performance as you have been through many crises and many factors (17:10)? Do you think it's prudent for the size of the company to have on their balance sheet based in your - and what about - what are you doing with the remaining cash? I believe your strategy will be different for this year.

The second question is the falling discharge (17:27). What could we expect at cash generation for the first quarter and for the year? And what about the performance of transfers with the banks in the first quarter? What have you been feeling about transfers? Do you believe that mortgage loans will start to rise up or do you think that the Faixa (17:53) will decrease financing and what about the private banks? And how do you see this already in the first quarter of 2015?

Hello. I understand you're asking three questions, in fact: the level of cash of the company talking about performance then cash generation estimates for the next few months or quarters and then what we see in the speed of transfers with the new scenario. We have BRL 1.8 billion in cash in the company. BRL 0.5 billion is mandatory, so BRL 0.5 billion is in our JV, and so BRL 0.8 billion in cash is working capital because at Cyrela, our philosophy is to have a certain level of cash to really be able to have four years (18:50) of positive cash flow. So, we see no scenario to decrease this.

The only item could be the performed items, and this is not a long portfolio. And the other half - it wouldn't be worth securitizing 30% because we consider this as a cushion for us. And in our management, we do not see the scenario of securitization of the BRL 780 million or so in our long portfolio.

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For 2015, we believe we will have positive cash flow because the fundamentals of cash generation in 2014 will be repeated in 2015. You know us. We do not give a guidance for these items because of the volatility that we have here on a quarterly basis regarding the speed of transfers and what we see regarding credit.

Cyrela three years ago, we increased the level of interest charge, so we had some fat to be trimmed, so to say. And there is no fat to be trimmed now because of the increase in the interest rates on the part of banks. But there has been no impact on transfers yet because the clients were already going through a more limited credit situation with the banks quarter-on-quarter. We can talk about that. And so far, we do not see that there's been a big pressure on us (20:27).

Thank you.

Q - Nicole Hirakawa {BIO 18242556 <GO>}

This is Nicole Hirakawa, Credit Suisse. Good morning, everyone. I have two questions. The first is about the net balance of current accounts with partners with a decrease of BRL 200 million quarter-on-quarter and with a stronger variation than your historical levels. So what was different in this quarter?

And the second has to do with land acquisition. You acquired 17 plots in the second quarter and could you give us more details about the profile of the project that you're seeking mainly in São Paulo because of the city's master plan? Could you talk about the strategy? And we saw a percentage of swaps even in most centered cities was very high. What about the situation now regarding land acquisitions? Is it better? Are you having slower launches? How do you see this situation now and from now on?

A - Eric Alencar {BIO 18098474 <GO>}

Nicole, this is Eric. I will answer about the current accounts and Rafa (21:51) will answer about the land. In current account, you have the commitment regarding receivables between partners, and sometimes you have a total imbalance derived from that. And we had some eliminations in our assets and liabilities then the impact was between lines. There is no need. There is no event there for us to talk about. So Rafa (22:16) will be talking about the land and land acquisitions.

A - Raphael Horn {BIO 19714328 <GO>}

Good morning, Nicole. I believe that the land market will allow us to buy some opportunities because when liquidity is right in the market, you have less money circulating, and then you have opportunities. We're not very aggressive in this regard but we always seek opportunities. The bulk of cash generation will not go to acquisition of land. We have a good land bank already for 2016 and 2017. But we will be very careful with our cash. And the best proxy is this where you place your money if there is land, has to do with a swap, or whether it's going to be cash. We are going to be very selective and look after our cash. But if a good opportunity arises, then we will buy.

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Q - Nicole Hirakawa {BIO 18242556 <GO>}

And what about your strategy? Do you have some specific projects that you believe bring better opportunities for the company, mainly in São Paulo because of the new master plan of the city?

A - Operator

Well, we do believe some segments and some kinds of products are better than others however this has to do with our own internal intelligence. And this is not something that we talk about. But the message is that we are going to be very selective in the acquisition of very good plots (24:05) of lands. Thank you.

Lucas Gregolin here at Fators (24:13) Good morning, everyone. Could you please talk about demand in the first quarter of 2015? Maybe where you have a lot of finished inventories such as into Northeast and Espírito Santo? Thank you.

Good morning, Lucas (24:40). You're asking two questions, in fact. The areas that we call poor performance vintages and a little bit more complicated than the others is also very complicated scenario. So it's not new. But the good news is that as these areas - but competition is lower in these areas and for the last couple of years or three years, competitors have not been launching anything there. The scenario was difficult there and it continues to be difficult and it's difficult to sell inventory in the south (25:23) for instance. But it has not deteriorated because of the macroeconomic situation of Brazil. And it was not easy and it continues not to be easy.

Now talking about the other areas, other locations, January and February, I would say, we're in line with last year. But it's a little bit too early to evaluate the year. So the year has 12 months. So every month, we are going to reassess the market. And so far, we are in line with what we performed last year.

Thank you.

Mr. Fred Mendes from HSBC.

Q - Fred Mendes {BIO 17221617 <GO>}

I have two questions. Good morning. Provision, on your - you reclassified quite a lot during this quarter, BRL 48 million impact which is sum of the total of your other operating expenses. When we look ahead in order to project 2015, could we imagine or assume that the level will be the same or should we see a drop in this amount? This is the first question.

And when I look here at the FTE (26:49), I see that there was a contribution of 27% included in your earnings with the fiscal scenario that we see. I don't know if you can talk about that, but how do you include it and their contribution for 2015 and equity income?

A - Eric Alencar {BIO 18098474 <GO>}

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Good morning. This is Eric. I will answer your question. The first has to do with our provision. You said it yourself - you answered your own question. Every month, we provision for new action based on the possibility of losses and what we have decided to do about it. And yes, we see the balance sheet suffered a very big impact related to this item in this last quarter. For 2015, the level of deliveries for 2015 is quite similar to the delivery level of poor performance vintages in 2014. So you should expect a provision. At Cyrela, we believe it will be either the same level or lower than last year looking product by product.

So the trend is that these provisions will start to have a lower impact as quarters go by. Now talking about Cury, you are correct with your mathematics. That was the contribution by Cury in the quarter. For next year, we have the balance sheet income, and Cury is easing a lot of Faixa 1. So, they are positioned with about BRL100 million for this next year and it will continue like that in 2015.

Regarding Cury's strategy, Cury is a company that has a low construction cost. This is the difference, MCMV or without MCMV. If the fiscal squeeze hits MCMV, they will continue and then this middle phase (28:48) or level 3, they will go very well as well. And they are all working with the two scenarios, Fred.

Q - Operator

If you allow me a follow-up on your provision page, when you take the year, it has been growing, it started lower, then it started to gradually go up and when I look at 2015, what you have as nominal value in 2014 would be reasonably similar in 2015 or will it be more similar to the fourth quarter on an annual basis?

More the annual basis, Fred.

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

Luiz Mauricio Garcia from Banco Bradesco. Good morning, everyone. I have two questions. The first one has to do with your conservative stand regarding cash. Raphael said that you're going to hold on to your liquidity. What I would like to know is during the scenario, you also see some opportunity of JV. In the very successful JV that you already have, do you see any new opportunities and could this be one of the uses for your cash, optimizing your G&A structure? Do you think it would be feasible for you to go back thinking about new models or other models based on these that have already worked very well for you?

And the second question has to do with the market. You talked about the difficulty regarding inventories in some areas, in some locations. Do you believe you will be giving additional discounts given the scenario of cost of capital and the scenario of credits? Do you intend to further accelerate your sales? And what would that bring as an impact on your gross margins? So I think reaching a balance is a constant dilemma for the company. This balance between the base and the impact on your gross margins. How are you going to tackle this?

A - Operator

FINAL

Good morning, Luiz. Regarding JVs, well, we are always open to this possibility. But good JVs don't need a lot of cash. So a good JV doesn't need quite a lot of cash, I repeat. So this is where - but if a good opportunity arises then we will be doing this. Regarding additional discounts, I think it's a generic question, so to say.

And again, every month we reassess our inventory. We carry out campaigns. We analyze project by project. So every month - sometimes it's not just the price, sometimes it remains the same, sometimes it works, sometimes we spend more with media. So this is business as usual. Every month we revise our inventory and regarding impact on the gross margin, we believe there will be no big impact because of that.

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

Some companies are very clearly going towards the scenario of discount. So going back, could you talk about buyback and dividend, what is the impact on the company's liquidity?

A - Operator

I think it's now on the menu, our cash will be used either to lower our leverage or to continue buying back or to pay dividend. So we have the full menu, and this is the menu. And we have three options to use our cash. So we are going to analyze during the year how much we generate. And these are the three options. Probably, we are not going to buy a land. This will not be the use of our cash this year, most probably.

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

Thank you.

Operator

Guilherme Vilazante from Merrill Lynch.

Q - Guilherme Vilazante {BIO 15319271 <GO>}

Good morning. Talking about the use of proceeds, supposing 2015 will be similar to 2014. Although there is no guidance, we believe there will be some cash generation, and we would like to know about the company's appetite for the situation of cash generation, whether it materializes or if it materializes, will you continue your share buyback endeavors?

A - Eric Alencar {BIO 18098474 <GO>}

Hello. Good morning. The cash generation fundamentally repeat themselves, and the concept of use of proceeds by the company also repeats itself. The purchase of land will be on opportunistic basis. And indebtedness tends to drop slightly because may generate - cash generation is a transfer, and you have to pay the asset age on the first day, on day 1. And then you have BRL 100 million from the buyback program and our trend, as a company, to continue to close out the program that we opened. And after that, we will be sitting with the board to see what we do from now on - from then on. And our philosophy is to work with a lean capital invested. And as Rafa (34:44) said, as an

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answer to the previous question, we are not going to just let it be. We have to do something with this cash.

Q - Guilherme Vilazante {BIO 15319271 <GO>}

Does that include dividend payout?

A - Operator

Yes. Undoubtedly. It's on the menu. However, we cannot be more precise in our answer now because we have many other items on the menu but, of course, this option is one of them.

(35:18) from Banco Safra.

Good morning. About Minha Casa Minha Vida, MCMV, the Federal Government has been publishing that MCMV 3 will have 3 million units in volume or more than MCMV 2. You have been operating, as far as I understand, on Faixa 1 and 2 and 3, and the fiscal adjustment, the lower volume of investments on the part of the government. In my mind, I believe that this segment will be deeply impacted mainly Faixa 1. What about your relationship and the JVs relationship with that, everything vis-à-vis the segment?

A - Eric Alencar {BIO 18098474 <GO>}

Hello, Christiani (36:03), this is Eric here. Let me answer your question. There is a fiscal squeeze and even in this fiscal squeeze, our understanding is this MCMV is a counter-cyclical activity and that it will continue to exist in this new phase of Minha Casa Minha Vida 3. In spite of the fiscal squeeze, we believe that there will be some change in the rule.

The rules are not quite clear yet. They are still being defined and they will be creating Faixa 1 (36:33), which would be between Faixa 1 and Faixa 2 catering to stakeholders that were not really being catered to in Minha Casa Minha Vida and our row (36:49) in Cury, which is our JV that operates with MCMV, is to be ready to face all scenarios, and Cury is prepared because they can build at low cost.

If there is no MCMV, they will be catering to this whole demand because of the housing deficit outside the MCMV program. So this will be another channel. This is as far as we can go in our answer today, Christiani (37:16). Thank you.

Operator

Eduardo Silveira, Espirito Santo Bank.

Q - Eduardo Silveira {BIO 16201252 <GO>}

Good morning. My question has to do with G&A. We saw an increase year-on-year in your G&A, I know that you do not give guidance but could you tell about the trends in G&A and what explains the increase in Q4? Was it - you said three factors, so how do you see these three factors playing out in 2015?

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A - Eric Alencar {BIO 18098474 <GO>}

This is Eric again, Eduardo. I'm going to talk about G&A in the quarter. I'm going to separate this quarter from the year. The main variation BRL 6 million comes from JVs, that provision for employees' participation. And it's important to talk about the year. In the year, the biggest variation if you look at the release, our third-party services BRL 23 million, mainly lawyers' fees and also others, BRL 44 million in variation. Of this BRL 44 million, BRL 33 million, Eduardo, are increases in indemnifications, our fixed G&A. This is one that you have here in the office has been dropping in nominal terms. And on the other hand, the FTEs grow gradually our trend for 2015. As provisions tend to stabilize, the trend of course is of stability in G&A with a certain variation due to indemnifications regarding delays in deliveries.

And this is an important point of philosophy by the company. In our philosophy, we adapt the G&A to the size of the company, not the offices, not the other way around. So G&A is not the reason for us to launch either more or less. It's quite the opposite. Thank you.

Operator

As there are no more questions, I would like to give the floor back to Mr. Raphael Horn for his closing remarks.

A - Raphael Horn {BIO 19714328 <GO>}

Thank you all very much for participating in our call and we hope to see you in the next call. Thank you.

Operator

Cyrela's conference call is closed. We thank you for participating. Thank you.

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