Q2 2020 Earnings Call

Company Participants

- Miguel Maia Mickelberg, Chief Financial Officer & Investors Relations Officer
- Raphael Abba Horn, Co-Chief Executive Officer

Other Participants

- Analyst
- Daniel Gasparete
- Elvis Credendio
- Enrico Trotta
- Marcelo Motta

Presentation

Operator

Good morning, ladies and gentlemen. Welcome to Cyrela Brazil Realty Conference Call, where we'll discuss the Second Quarter of 2020 Earnings Results. (Operator Instructions)

And as a reminder, this conference is being recorded, and the audio will be available at the company's website, www.cyrela.com.br/ri. This call is being simultaneously translated into English and is being broadcast over the Internet. Questions can also be asked by participants connected (inaudible). The earnings release that was published yesterday, 13th of August, after the close of the B3 trading session can also be accessed on the company's website.

Before we proceed, we would like to mention that the forward-looking statements that may be made during this conference call relative to the company's business prospects and forecasts and operating targets related to its financial growth potential are predictions, which are based on the management's expectations about the future of Cyrela. These expectations are highly dependent on the domestic market conditions, the general economic performance of the country and international markets. Therefore, they are subject to change.

With us today, we have Mr.Raphael Horn, our Co-CEO; and Mr.Miguel Mickelberg, our CFO.

I will now turn the conference over to Mr.Horn. Mr.Horn, you may begin.

Raphael Abba Horn {BIO 19714328 <GO>}

Good morning, everybody. While the second quarter of 2020 was marked by the global adherence to socialize especially amid the coronavirus pandemic. And that seriously affected the performance of both the Brazilian and (inaudible). Even though the pace of our construction work did not slow significantly, sales fell sharply, especially in the month of April. As a result, we've postponed most of our launches scheduled for the second quarter. However, the real estate industry have recovered well in June, and the sector had a very good restart, driven by the interest rates at all times low and the partial reopening of the economy combined with good inventory sales and the launch of Ipiranga.

In terms of operation sales under Minha Casa, Minha Vida program were the main highlights during the quarter, once again, showing the resilience of the low-income segment during economic crisis.

Concerning our financial performance, we've recorded a strong gross margin of 32.8% and a net income of BRL68 million. Considerable uncertainty persists, but the strong sales of our launches and inventory units make us confident that the real estate industry will perform well in the coming quarters.

Now let's comment on our national launches.

Miguel Maia Mickelberg {BIO 20023910 <GO>}

Thank you. Good morning, everybody. On Slide #5, we have Cyrela's launches. In the 2Q '20, we launched 5 new projects, which is a PSV of BRL395 million, 81% less year-on-year. Excluding swaps, the volume launched in Cyrela's share in the second quarter was (inaudible) lower year-on-year. The company's share in volume launched in the second quarter of '20 was 73% compared to 80% year-on-year.

On Slide 6, we highlight the major release in the quarter that was 52% sold on that period, which was deeper on the level.

On Slide 7, we'll talk about our sales performance. In the second quarter of 2020, the pre-sales were BRL818 million, 58% lower year-on-year. The swap resales amounted to BRL1.5 billion, a 28% decrease year-on-year. The state of São Paulo accounted for 70% of our sales.

On Slide 8, we'll address sales speed. The company's annual SoS was 50.7%. Looking at sales speed by period, projects launched in the second quarter of 2020 have been 43% sold.

On Slide #9, we'll address Cyrela's total inventory. At the end of the quarter, inventory at (inaudible) value totaled BRL5.7 billion, down by 6.5% quarter-on-quarter. The change in our inventory can be seen in the chart to our left.

On Slide #10, you can see a breakdown of our finished units. And in the second quarter of 2020, we sold 8% of the finished units in the beginning of the period. Adding the inventory projects delivering along the quarter, pricing of units at market value, finished units inventory decreased by 5% quarter-on-quarter.

On Slide 11, we'll talk about delivered units. In the second quarter, Cyrela delivered 12 projects totaling almost 3,000 units and a PSV of BRL641 million. In the first half 2020, more than 6 units of -- 6,000 units were delivered, representing a PSV of BRL1.3 billion.

On Slide 13, we will address our financial results. The net revenue was BRL839 million and looking (inaudible), higher quarter-on-quarter and 10% lower year-on-year. In the first semester, the revenue was BRL1.6 billion, 9% lower year-on-year. The gross profit in the quarter was BRL275 million, up by 5% quarter-on-quarter and 6% lower year-on-year. In the first half, gross profit amounted to BRL536 million pretty comparable to 2019.

Our net profit totaled BRL68 million in the second quarter of 2020, with a net margin of 8.1% compared to a profit of BRL28 million quarter-on-quarter and BRL114 million year-on-year. In the first half year, net profit reached BRL96 million.

Now please let's go to Slide 14 to see our profitability. In the second quarter in 2020, our return on equity measured with the net profit of the last 12 months over equity ratio was a positive 6.9%, and our EPS was 18% -- sorry, 0.18 per share. On Slide 15, you can see our debts. Gross debt at the end of the quarter was BRL 2.9 billion. The cash position was BRL2 billion. Thus, our net debt was BRL905 million. 19% of the total gross debt are related to loans for construction and 71% is long term. Our net debt over equity ratio was 17.1%, 1.0 percentage points above last quarter.

Slide 16 shows the company's cash generation. In the second quarter of 2020, our cash used was (inaudible) BRL67 million compared to a cash generation of BRL13 million against last quarter and BRL196 million in the second quarter of 2019. And they have in the first half of the year, the cash yield is amounted to BRL 54 million.

Now Rafa and I are going to go on to the question-and-answer session.

Questions And Answers

Operator

(Question And Answer)

Ladies and gentlemen, we will now begin the question-and-answer session. (Operator Instructions) Our first question comes from Mr.Enrico Trotta from Itau BBA.

Q - Enrico Trotta {BIO 16742911 <GO>}

Hi, good morning, Raphael. Good morning, Miguel. Thank you for your presentation. Two very quick questions. The first one is just on, if you could comment and now looking forward in the third quarter of the year, based on what so far, we've been having our sales dynamics. If you could just give us a hint on what is the relative performance between the high end and the mid to low end compared to the pre-crisis items? And if you could please tell us a little on how the high management is intending to launch with the second half of the year? We can see that we have quite a few people pretty encouraged with the post-COVID response.

And the second question, and that is more on the dividends. And we have the (inaudible) with potential offers on short-term. And we have the second relevant area that could better foresee. What is the timing? Is this your intention to pay the dividends in the short-term or to hold the liquidity and wait a little bit to see how this economic scenario is going to build up along the next month? What is the expected timing of those dividends if those offers proceed? So, if you put a line with those two issues, that would be great.

A - Miguel Maia Mickelberg {BIO 20023910 <GO>}

Enrico, good morning. This is Miguel. Well, first with relation to those sales, indeed we had a pretty good month of July, was the best month of the year and it was good not only in the launches. We hadn't good launches and some launches, but also in our pre-sales and our finished units. And so we are indeed pretty encouraged to keep on launching and for the next quarters. And if the second half is good, we'll have no room to add a couple of extra products to the market. As for the high end Minha Casa, Minha Vida, well, (inaudible) Minha Casa, Minha Vida is more resilient with the smaller built, no market drops or falls in the high end or in the mid high-end, then we had most of the increase in the volumes and the sales volumes for both June and July.

This was the second question unfortunately, as you know, very well, all those offers are processes underway, and we won't be able to make any specific comments relative to those, Enrico.

Q - Enrico Trotta {BIO 16742911 <GO>}

That's all right, Miguel. Now okay. So if you allow me another second question, which is, if you could talk me about the competitive scenario in Sao Paulo, either for the low-income or high-income. I would say that the sales performance in the industry was a pretty good highlight amidst all those prices. And people were talking about accelerating launches and just launching a lot of finished units and in Sao Paulo, we are talking about 30,000 units, and now they are talking about 60,000 units. So I would like to know and to hear from you whether you have a mid-term concern with all this surplus offer or if you think the real -- interest rates are pretty low. So do you think the market can absorb that for the next 12 months? I'd like to hear anything about that.

A - Miguel Maia Mickelberg {BIO 20023910 <GO>}

Well, Enrico, yes, we are still at the very beginning of those cycle, but you see competition is competition. In other words, I mean, you just have to stay put and get your grip and you got to be careful, of course. I mean those are slips with SOL. But we are in the pretty in part pretty hard excited about the economic cycle. Let's see what's going to be the level of competition or size. So, I think this is pretty -- it's always in our radar. Yes, and it's really something that we can't -- we just we have to just have our heads up for that all the time. Thank you.

Operator

Our next question comes from Mr.Elvis Credendio from BTG Pactual. Please move on Mr.

Q - Elvis Credendio {BIO 20084266 <GO>}

Hi, good morning, Raphael. Good morning, Miguel. I have two questions here as well. The first one is with regards to the land plot. If you could give us an update on how the landowners are? Do you think that the [ph] and prices are tending to a recovery? And what do you see about the strategy from now on? Do you think it's for us to take the first step for the next side or is it too early?

And the other question is with regards to initiation requests from the clients. I would look do you have an update from you. What is the status of that and the portfolio? How it's been behaving.

A - Raphael Abba Horn {BIO 19714328 <GO>}

Good morning, good. Well, for the land and for the plots of land, it's a sort of a slower market. And then you see the prices that didn't fall in one or two months. And neither going to go up that badly and we are obviously going to have some economic recovery. But a couple of players buying you see (inaudible) there will be the prices are going to go up.

But we are not in land banks speculators that we are anticipating and just trying to make money out of that, no. We are developers. So, our -- we needed to have a positive cash flow and that's it. And we believe that the plots of land are a good part. And we think that our (inaudible) 2021. Now the main concern is now maybe 2022. We think that the market is not saturated if you will, so we can still do that.

Now with regard to competition, we don't know, but so far, it's not something that you can market this yet. It might come up, but it's just a matter of being attentive and keeping an eye on it. But we have been able to operate pretty satisfactory. Interest rates play a big role, but it's really the matter of being attentive to years, the competition will be.

A - Miguel Maia Mickelberg {BIO 20023910 <GO>}

Yes. This is Miguel here. With regards to the negotiations to net debt, we have had 11% of our clients have lasted the renegotiation of installments and a large share of them chose to pay it, because we were always obviously negotiating the interest rates. And then and third of them basically have been able to pay and all the others are sort of pretty advanced in their negotiations.

They remain like two to three months, in that but they are sort of, getting back. So, and this obviously going to be translated in. We think that maybe something like 5% to 10% of the estimates that we did in the forecast that we did for the years. But our renegotiation requests standing to zero and for a while now. So, we think the situation is very much under control.

Q - Elvis Credendio {BIO 20084266 <GO>}

Yes, thank you. That was pretty clear. Thank you.

Operator

Our next question comes from Daniel Gasparete from Credit Suisse. Daniel, please go on.

Q - Daniel Gasparete {BIO 17999254 <GO>}

Good morning, everybody. Thank you for the call. Two quick questions. And the first is more related to how that you see the interest rate scenario for the real estate because, I mean, we could envision that those drop was about to come. But do you see any additional drop, that is something that we can expect in the short run.

And the second question is, I would like to understand the dynamics of the real estate prices. How do you see the pressure for an increase in the prices at the final consumers? So, we have a scenario of potential growth and price raises in the short term.

A - Miguel Maia Mickelberg {BIO 20023910 <GO>}

Good morning, Gasparete, Miguel here. Well, this is the interest rate, and the current products, we still think that there is some room for fall because if you check the spot wages and it's much higher if compared to the background figures. And on the other hand, we have this mismatch between the offer and demand and that may hinder things a little bit.

So, we think that the structure of our products have to just evolve a little bit, that we can spread the offers. And so -- and we don't really have a lot of in on what should happen in the short term. But the banks are keeping an eye on this type of product and we think soon or later, this is about to happen. If you check the loans for real estate, they are growing in their margins and the companies are not delivering much. So offering supply are indeed helping us right now. So, it's a good opportunity for us to be more aggressive by changing products instead of just adding up on the spot rate for the existing product.

So, now linking this to the unit prices. And then, of course, the drop on the interest rates effects the affordability pretty markedly. And that is probably going to be much lower than the rent that they might pay. And that encourages buyers and this interest rate is a great mechanism of incrementing the offer and also for prices, so (inaudible) high. And especially in Sao Paulo the stock levels have gone down significantly. So, this has been a vision of positive dynamic for price raises and the interest rates are going to be one of the main drivers for that to happen.

Q - Daniel Gasparete {BIO 17999254 <GO>}

Okay. Thank you very much.

Operator

(Operator Instructions) Our next question is from Haiza Alonso [ph] from Citibank. Ms.Alonso, please you may proceed.

Q - Analyst

Hi. Good morning, everybody. My question is on the -- my apologies first if it is redundant. But Sao Paulo has represented 70% -- 77% allowances for the period. And considering Cyrela's participation, they only have 7%. And so how can we expect for the evolvement on this rhythm and also the competition perspective, and if you intend to sell your land banking areas, which are not that attractive.

And the other question is with regards to the cost. You think that you've seen by increasing the margin, do you know the margin of this project in front of the others -- in face of the others?

A - Raphael Abba Horn {BIO 19714328 <GO>}

Hi, good morning. Well, of course, Sao Paulo played a huge role in our market share and it seems that it won't change much in the future. Now here in Sao Paulo, the top brand in some segments for 2020-2021, I mean, they are very predictable for 2022.

So, segment, we have our -- some of them, the grid is full and some others not exactly. So, in some areas we might need to procure for 2022 and we do that pretty carefully without any rush and for -- and is this something that we do strategically, of course. And we left the areas that we didn't want to be. We are basically in Sao Paulo, Rio and Porto Alegre. We have a couple of small parts here and there, so we can monetize them. But -- and also within Sao Paulo itself and Rio itself, we might have some -- which are not exactly strategic ones. So, we might sell them and we to just have some liquidity, because they're not exactly very tragic. [ph]

A - Miguel Maia Mickelberg {BIO 20023910 <GO>}

So, Haiza, let me address your second question. With respect to margin, I mean, our margin is the mix with many different periods. And so -- and our units are going with lower margin. So, at the finished units, specifically they are coming with gross margins of 34%, 35%, and especially to consider what percent at the end of 2018, 2019, those projects they start to represent more of the gross margin. That's why it is going up a little bit and its sort of getting closer to the margins of the newest unit.

Operator

(Operator Instructions) Our next question comes from Marcelo Motta from JP Morgan. Mr.Marcello, please you may proceed.

Q - Marcelo Motta {BIO 16438725 <GO>}

Good morning. Two quick questions. So, on the margin, I mean, we've been hearing from some corporations that the sales for finished units have increased and people are sort of anxious to get themselves arranged soon. And Miguel said that this is a product that has a smaller margin than the launches, but -- and I just wanted to know what was the pressure?

And then the second question is on the revenues. Despite the COVID situation didn't really put many of Cyrela's projects on standstill. But still something that we must have to be careful on the third quarter and we might have some improving productivity. So, what do you envision as the rhythm for the following quarter?

A - Miguel Maia Mickelberg {BIO 20023910 <GO>}

No, we haven't really noticed anything in particular about selling more due to COVID. I would say that this is still low income, reshaping many years from crisis, hit margin historically low prices, high affordability, and this dynamic is just continuing. And we are getting back to the old dynamics and for our high-end landbanks and plot plan, I mean, we have been witnessing this segment slightly different with people buying more plots planned and houses.

But I hope this is the case, but I would be -- we don't have this as a real evidence. Yes, this is still normal good behavior in my opinion. The launches are going well. And this is nothing to do with COVID. So, it's nothing really. And then just the same that we stopped that in the landbanks and so on. And the developers not this much.

With regards to the acknowledgement of the revenue and the work, including the South, we have works that have to be suspended more to the end of the quarter. And for sure, if they hadn't been put in the and the standstill, we might have had some more million and of higher revenue recognition. So, -- but all-in-all, the work volumes are pretty satisfactory considering the pandemic in the second quarter. I would say that they are a driver for the third quarter to increase the revenues, increase the stock sales and it is so. Thank you.

Operator

(Operator Instructions) There are no further questions, I would like now to give the floor to Mr.Horn for his final remarks. Mr.Raphael? Mr.Horn?

A - Raphael Abba Horn {BIO 19714328 <GO>}

Well, once again thank you for your interest in Cyrela. And we are pretty confident in the future and this has been pretty for the both human and the corporate perspectives, we are getting back to work and either home-based or whatever for the market dynamics and the consumption and the real estate sales, there returning to normal faster than we expected. So, we are pretty happy that the whole industry executives from any sector are pretty encouraged with this upturn of this. So, let's keep on working and thank God that the COVID was a bit shorter than we thought it would so. Thank you, and let's just step ahead.

Operator

Well, that concludes Cyrela's conference call for today. Thank you very much for your participation. And thank you.