

Y 2017 Earnings Call

Company Participants

- Eduardo Fischer Teixeira de Souza, Chief Executive Officer Region II
- Leonardo Guimaraes Correa, Chief Financial and Investor Relations Officer
- Rafael Nazareth Menin Teixeira de Souza, Chief Executive Officer Region I
- Ricardo Paixao Pinto Rodrigues, IR & Financial Planning Director
- Unidentified Speaker

Other Participants

- Enrico Trotta, Analyst
- Luis Stacchini, Analyst
- Marcelo Motta, Analyst
- Unidentified Participant
- Victor Tapia, Analyst

Presentation

Operator

Ladies and gentlemen, good morning. Thank you for holding, and welcome to MRV Engenharia. We would like to inform you that all participants would be in listen-only. And we will start the Q&A session. (Operator Instructions) Now I would like to turn the floor over to Mr. Eduardo Fischer. Mr. Eduardo, please proceed.

Eduardo Fischer Teixeira de Souza {BIO 17580321 <GO>}

Good morning to all, Eduardo here. Thank you very much for your participation. I'm going to start talking about 2017, and what we're expecting for 2018. So starting by 2017, results were extremely positive. We were able to start to put into practice what we had planned 2, 3 years ago, the most aggressive purchases. If we get the fourth quarter, specifically the second quarter 2017 we launched and sold annualizing the 50,000 units. It was our proposal two, three years ago and we pursue in 2018 the consolidation of these figures. 2018 will be a year where we are going to look at the operation, MRV launching and selling during the year the 50,000 units. The year started well. We are moving to the ending phase of the first quarter. The demand has been growing. 2018 we are going to look at consolidation of the units -- of the 50,000 units that we have as a goal.

The consequence of this is that our expectation and our numbers will be better in 2018, as we're going to launch more, therefore sell more. Our revenue tends to be higher and we will have the dilution of expenditures and our expectation is to have a growing

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profitability during 2018. So in terms of comparison we -- in 2018, we maintain the strategy of continue to invest in bank. We should see the same investment that we saw in '16 and '17. And behind this, there is a reason that despite the market showing an improvement, higher competition in some locations, because of the purchase of land in most of the location the competition -- we are in hasn't arrived yet, the competition. So we think it is the moment to continue the strategic and important investment, which will be useful for good pillars.

2018 should be a year with great investments in landbank because this still makes sense in economic terms. Another important thing for this year, as we said at the end of last year, we're going to have in the second semester, probably our new product in the market, which is the premium product. And we will be able to increase the platform and the reach of MRV, in terms of dwellings in Brazil. As we had said it's going to be something complementary. This does not overlap our project 50,000, and the current operation. It's an opportunity of gains that we see, and our goal and our objective is that in the second semester this year we can have the product on the shelf.

Another important point is -- that we may follow in 2018 the implementation of our project, which is guaranteed income. It's important an objective. This project should be completely implemented during 2018. Looking at 2019 a company, that should have close to zero-distract [ph]. And it's a lighter and more agile company with less liabilities. So we see opportunities for gain in the operation during 2018 within this project of ours.

And to close we continue capturing gains in the implementation of our aluminum and concrete walls. This quarter we're finishing with 80, 85 of job sites with this process implemented but most important than this, we still see chances for a shortening of the cycle with our new building process. It was -- it's being implemented -- it's been implemented during the last five years, but we see a chance of really shortening of the cycle even in these 80% of job sites that are already using this technology.

So our perspective for 2018 is that we continue with a more efficient operation growing and delivering more profitability. Now I'm going to pass the floor to Leo.

Leonardo Guimaraes Correa {BIO 15387486 <GO>}

Good morning to all. I'm going to comment on the aspect which is so important for our business, which is the funding and financing for customers. I'm going to split the subject in two. First in regards to banks, and then we're going to talk about the fund for length of service for the FGTS. First talking about Banco do Brasil clearly considering a greater appetite for this site, they've been hiring entrepreneurships with -- enterprises -- with Banco do Brasil the partnership was very strong in the past. Suddenly it cooled down, but now it's recovering, recapturing. It has a long and strong balance sheet, strong base. So we see this partnership very well with Banco do Brasil.

Moving to the Caixa Economica Federal, it's been a greater to partner in the last years. It has a great percentage of our business. Now we are extremely comfortable with the Caixa Economica. We see the changes that have been taking place, they are positive and

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bringing more transparency and great governance for Caixa. We see Caixa focusing more and more in its operations, in a sense of real estate portfolio. And this brings great tranquility in terms of basal issues. It was held on the press, we've seen reporters talking about the results of Caixa being quite positive, especially in the fourth quarter. And this result also brings -- bring us space of -- in terms of basal for Caixa Economica. The forte of it is completely under control, very adjusted, it has a good guarantee which are the apartments, they were hired with a good loan to value. It brings good quality for the portfolio of Caixa Economica. From the point of view of MRV with Caixa the first quarter has been completely normal -- normalized from the point of view of hiring enterprises. It has been happening normally.

Change, -- moving to FGTS, another topic. Some people have a more conservative vision in terms of FGTS. We are looking at the cash flow for the next four or five years, we look not only at the budget of the first year, this year, where we see a budget that completely feasible, both from the point view of contracting volume as well as funds and resources to subsidize the 1.5 level. A very easy this year, other years. It's very important for us to have this planning -- multi-annual planning because the land, we're buying today we're only going to launch in 2 or 2.5 years' time in average.

The budget from the point of view of allocation from 1.5, 2, 2.5 and 3, we've seen it quite balanced. We have 70,000 units for 1.5, perhaps some increase, but it depends still on dealings with FGTS, and the budget of the union. The message is that we are seeing very calmly the account of FGTC [ph], the unemployment decreasing slowly. This should improve the cash flow for FGTS and availability of resources to be able to finance the market.

Now I'm going to ask Rafael to speak. So, repeating what Rafael, and Fischer said now, we saw a great result vis-a-vis delivering what they promised in the past. I would like to highlight the growth of the net profit of 180 million, a very robust growth. ROE reached 10%. Now it reached ROE which is very healthy. It hasn't reached the level we want. We're really targeting 15% to 17%. The ROE is very sound now. Revenues have grown 29% in regards to the last quarter of 2016, a billion [ph]. The EBITDA also had a great advance, spectacular advance at 68% in regards to the fourth quarter of 2016 EBITDA of 260 million, over the financial indicators, all of them had a great advance.

This is the result of a healthy operation, an operation that has been growing and very assertive planning that was made 3, 4 years ago. The company was able to preserve its size during the crisis, but left the crisis much more prepared, much more profitable and very ready to enter this type of growth and consolidating 50,000 units.

Now we're going to pass to the questions and answers.

Questions And Answers

Operator

(Operator Instructions) Mr. Victor from Bradesco BBI would like to ask a question.

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Q - Victor Tapia {BIO 20566083 <GO>}

Good afternoon. Thank you for the opportunity. First point I would like to discuss here is the dividends that you have announced, extraordinary dividends, you announced 55 million. So you have a leverage that is low and generation of cash should continue solid, very robust even with the issue of increasing the landbank in 2018. Given this when could we see this payout increasing? And another point that I would like to discuss is that we had recently -- we were recently in Brasilia and discussing with government representatives, they're very focused on the quality of the program. And they forbid individuals to access it. Given this view that are more [ph] spread in more than a 150 cities, perhaps the competition with these little ads, individuals maybe higher. How are you seeing this move during the two first months of the year? Is there an improvement in this competition?

A - Rafael Nazareth Menin Teixeira de Souza {BIO 16905756 <GO>}

This is Rafael, good morning. In regards to dividends first of all, we have a formal right. We have to go through GE, risk, the company should release, so make the payment of dividend during the start of the second quarter. It's important that our dividend payout was close to 50% in the last year, and gave a situation of the cash, low leverage, the economy moving better, political risk exists, but it's more under control. The company is more confident and perhaps growing -- perhaps going beyond 50%, where we say that the most difficult part is to make the money, make more profit, have a generation of cash that can be solid and continuous. This is the difficult part to distribute dividend or have rebuying program. This is easy at the right moment, the company will address this and return more capital to shareholders. I mean today we are comfortable than we were in the past and therefore we should see in the mid term, the payout of dividend going beyond 50%, which is a very healthy threshold already.

And being conservative with low level we see no problem with cash perhaps during the year. In the past we had strong investment in LOG and in our opinion it was very assertive and it will pay during this year. And looking forward, with less obligation, investments will be focused much more on MRV and this will open a space for us to be more aggressive at the moment in terms of dividend. In regards to the build -- and in fact the government or individual is looking at more sustainability for the program. The companies that were more irregularly or in a more informal manner, they face more difficulties today to capture the FGTS funds. There is no doubt looking forward this was a very correct vision. We see small companies with a bit more difficulty, but I think it's early to say that if the market -- if our market share will grow at a higher or lower pace. As simple and important as this difficulty with the -- we're using this little land, the landbank that was bought by us during -- I think it's very stratifies, very strong the MRV brand, what we do in terms of experience with the customer, experience, quality of the product -- MRV has been planting during the last years more and more round operations (Technical difficulty) This will make a great difference looking at the mid and long term.

Q - Victor Tapia {BIO 20566083 <GO>}

Thank you very much.

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Enrico Trotta, Itau BBA.

Q - Enrico Trotta {BIO 16742911 <GO>}

Good afternoon. I have two questions. The first one, looking at sales expenses in this quarter is quite stable in regards to the third quarter. And this increase, also we could see very clear the dilution. So I would like to understand how -- what can we expect in terms of sales expenses, given you have this target, this goal 50,000 units. Can we really expect this dilution that has been occurring during 2018? How are you looking at this? And the second question about the ready stock, raising in the semester because of greater rigor of strictness of the bank 4% of the total it was 2, if it's more concentrated or Minha Casa Minha Vida if you see any movement of this ready stock, if it should increase during 2018, given that the banks can continue -- should continue being working this. I would like to understand your mindset?

A - Ricardo Paixao Pinto Rodrigues {BIO 21232785 <GO>}

Enrico, good morning. It's Ricardo here. So the first point, in terms of sales expenses, we have been saying that we had a structure that was a bit more swollen than was needed. But in our growth plan, it would make sense to maintain this expense is a bit higher in percent -- thinking about the growth of the company. This growth is being delivered, starting to be delivered, where this threshold of 50,000 expectation, is really a dilution. The commercial expense which is linked to the quantity of sales, but it's an important portion. It's a fixed number, so we can see this during the year. In regards to ready stock went from 2 to 4, it's a very low number. It doesn't worry us and on a higher -- with enterprises, with Banco do Brasil, we don't expect this number to continue growing with the conclusion of these enterprises with Banco do Brasil or any other partner.

Q - Enrico Trotta {BIO 16742911 <GO>}

Thank you very much.

Operator

Next question comes from Morgan Stanley.

Q - Unidentified Participant

Good morning. I have two questions. The first is land -- your are Investing in this landbank. How do you -- where did you want to invest In other cities? Or you think you are close to universe [ph] at the bank. And second question is mission for 2018, hearing you speak today you have a quite an optimistic view. I would like to understand which are the things that worry you most, such as the risks that you are more worried about, what type of things may concern you? Thank you.

A - Eduardo Fischer Teixeira de Souza {BIO 17580321 <GO>}

Eduardo Fischer, landbank, as I said in the opening, we have some opportunities for the buying of Landbanks in some places where we operate. We have more competition in metropolitan areas, but if you look at our behavior of landbank purchase was stronger. We

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have consolidated this and today we are making a strategic move towards the cities in the interior of the country. We want to reinforce the purchase of this land in metropolitan areas and use the opportunities in very good conditions where conditions are much better. In August 2018, we have some points that are important. We had a great concern about electoral risk, political reason. What could happen in 2018, especially in the middle of last year. This was a worry that really bothered us. This risk today is smaller, we believe, we are more comfortable and we are more optimistic. This reflects an operation since the second semester last year, we're seeing much growth, higher growth in our standard sales, our communication channels with potential customers. This is a very important and positive point. The risk, the worry is always cash and funding. But looking at what happened in the last six months as Leo was saying in the opening, it is something that I consider that is mitigated and well balanced. I see 2018, I am much more comfortable in March 2018 than I was in March, 2017. March 2018 and March, 2017, so I think we have the condition to deliver everything we starting to -- we had started in second semester 2017.

Q - Unidentified Participant

Thank you.

Operator

Next question from Marcelo Motta from JP Morgan.

Q - Marcelo Motta {BIO 16438725 <GO>}

Good morning. Two questions. If you could comment on the land, we saw that it was a great improvement, threshold that was better. I want to see the tenant [ph]. If you would like to could comment on the free cash flow after one year with the normalized cash, without any stumbling to the end of the year. If we could expect a higher recovery in 2018? How you've seeing this scenario?

A - Leonardo Guimaraes Correa {BIO 15387486 <GO>}

Hello Marcelo, good afternoon. First, the equity income has been improving for two reasons. One the prime MMRO have been improving, operating selling at good price with very compatible prices. Some prime operations are even above the average of the consensus margin. This is clearly contributing. And with this operations are out of phase, where they can improve the generation of -- cash generation and as these are leveraged entities, the drop in interest rates can help a lot their operations, and diminishes the financial cost. It brought an important improvement that is continuing. So the two factors brought this improvement, we and see a continuation. It is slow but steady and this line will behave well.

In terms of free cash flow last year we generated a bit less cash than we would have liked. Or we had planned for series of reasons that are well known, the fourth quarter was lower.

We have been accumulating a volume of receivable and clients that is high. This cash will be stronger this year, 2018. And as Rafael already mentioned cash generation, good part

of it will go to our shareholders. This is our objective and we have mentioned this already.

Q - Marcelo Motta {BIO 16438725 <GO>}

Thank you. Perfect.

Operator

Next question, Luis Stacchini, Credit Suisse.

Q - Luis Stacchini {BIO 18717891 <GO>}

Thank you. I have two questions. You talked about -- in regards to sales, expenses, you mentioned that there is a fixed part of this. Could you quantify the -- parse all this -- share of fixed expenses, do you have any contracts, institutional expenses that have more fixed character? If you could try and quantify this it would be very interesting. And second point, I would like to discuss the interest, capitalized in stock. We saw the first, I think it's since 2012, if it makes sense to assume a stability or a drop at this level since the pace of growth have been faster. The company given the growth in debt could be larger. I want to understand the dynamic of this interest rate capitalization.

A - Ricardo Paixao Pinto Rodrigues {BIO 21232785 <GO>}

Luis, this is Ricardo, in regards to trade or commercial expenses more than half of it is fixed. And consequently, the rest is something in terms of variable expenses. It is an important expense since we are increasing funds. In terms of capitalized interest, yes, we reached a certain stability. It is important, it is a mathematical factor here, when in 2016, beginning of 2017 the interest rate was higher. Therefore in terms of number of reais, the capitalization volume with more reais being capitalized, with lower interest rates, the receivables are less. We have a level of cash that is quite high. So we're not going to increase the indebtedment to increase the cash volume. It could happen pinpoint situations, since we always try to have a longer and longer debt, longer and longer profile debt.

So when we have good opportunities, we are always going to try to stretch the debt. But we shouldn't change much what we have in terms of debt value we have. Some due in 2018, that should be amortized and the company will try and do this. We're going to see a balance in terms of quantity of interest maintaining the SELIC, the interbank rate at the same level and we're going to have more expenses, since the lands, the stock of interest we will see this coming near term. There is not a great change in terms of what we have now.

Q - Luis Stacchini {BIO 18717891 <GO>}

Leo, can just help me here. Would you be able to say how much is in land and how much is in stock?

A - Leonardo Guimaraes Correa {BIO 15387486 <GO>}

I don't have this in my memory right now. How much it is divided in terms of stock of land and stock of apartments.

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Q - Luis Stacchini {BIO 18717891 <GO>}

Okay, no problem, then.

Operator

Victor Tapia from Bradesco BBA.

Q - Victor Tapia {BIO 20566083 <GO>}

I have one more question in terms of the premium product, that you want to launch. You commented that this would be linked to the same model that you have with Minha Casa Minha Vida how are the talks going, these conversations with banks going on? Thank you.

A - Unidentified Speaker

We are talking to some banks and these conversations have been good. We don't necessarily dependent only on them. I can do it with Banco de Brasil and Caixa the same way we do it today. Obviously if you have more partners to develop the products of this platform, it's better. But it's not exactly attached to commercial banks entering the game. The expectation is good, the one condition for us to do this as MRV works with FGTS. In constructions with short cycle the model doesn't change. So regardless the banks that we're going to search the premise is that this model should work the way, it is doing now. Thank you.

Operator

(Operator Instructions) So as there is no questions, I would like to turn the floor over to the President for their final considerations.

A - Rafael Nazareth Menin Teixeira de Souza {BIO 16905756 <GO>}

First of we want to thank you all to be here, present at our DRE. We had 2017, it was very good financial indicators and operating indicators, very, very good. Our great project is MRV 50,000 is completely feasible as Fischer said, annualize the fourth quarter, the main objectives are at this level. Next year is really consolidating the project. We see that the demand is good and looking forward, we're going to have very relevant launches, strong entities with little competition. The economy is improving, consumers are more confident employment is slowly growing and improving. We are optimistic and we are sure that was made in the past will put MRV in a even more differentiated position. We made very robust investments in IT, people, landbank, we put MRV at a very highlighted position. And the next quarters or years we're going to let the benefit of these investments the last years. So it's important to emphasize that we continue comfortable with the program as it's being managed by the government, always with this sustainability, predictability, Fundo de Garantia FGTS, the same way, search for a better qualification of the industries, very important that formal companies do things right, being it in the hiring of hand labour, the delivery of products with guarantees.

I'm sure that the companies will have a competitive advantage over more informal. The Ministry of Cities has had said MRV as all other companies with -- have this long vision and

I have no doubt they are very well-positioned in an industrial sector that will have a strong demand for many years. So again thank you all for your presence and re-emphasize I am positive and optimistic, not only for the company, but also for the industry in which we operate. Thank you very much and see you next call.

Operator

The conference is closed. We thank you all for your participation and have a nice day.

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