Q4 2012 Earnings Call

Company Participants

- Leonardo Guimaraes Correa, Chief Financial Officer
- Rubens Menin Teixeira de Souza, Chairman and Chief Executive Officer

Other Participants

- Eduardo Silveira, Analyst
- Enrico Trotta, Analyst
- Javier Gayol, Analyst
- Luis Mauricio Garcia, Analyst
- Marcello Milman, Analyst
- Marcelo Motta, Analyst
- Rafael Pinho, Analyst
- Rene Brandt, Analyst

Presentation

Operator

Good morning. Welcome to MRV's Conference for analysts and investors that is going to discuss the earnings of the quarter of 2012. Today with us we have Rubens Menin Teixeira de Souza, CEO; Leonardo Guimaraes Correa, CFO; Ms. Monica Simao, Chief Investor Relations Officer; and Mr. Gerson Mazer, Investor Relations Executive Manager.

We would like to inform you that this event is being recorded and that during the Company's presentation, all participants will be in listen-only mode. We will then start with the Q&A session only for investors and analysts, when further instructions will be provided. Only after the Q&A session for investors and analysts, we are going to open the Q&A for journalists. (Operator Instructions) Today's live call can be accessed on MRV's Investors Relations website.

Before going on, we would like to mention that any forward-looking statements made during the conference call, relative to MRV's business outlooks, operating and financial goals, are based on the beliefs and assumptions of its management and rely on information currently available. They involve risks, uncertainties, and assumptions, because they relate to future events and, therefore, depend on circumstances that may or may not occur in the future.

Investors should understand that general economic conditions, industry conditions, and other operating factors could also affect the future results of MRV and lead to results that materially differ from those in such forward-looking statements.

Now, we will turn the conference over to Mr. Rubens Menin Teixeira de Souza, CEO, who will begin the presentation. Please, Mr. Menin, you may go on.

Rubens Menin Teixeira de Souza {BIO 15387481 <GO>}

Good morning, everyone. Once again, I thank your presence in MRV's call on the results of our 4Q and year 2012. What I think is interesting is that we have seen some negative analyses of our Company and of the market, which is understandable, but I would like to do something different.

The construction industry has been going through a different moment in Brazil. In 2005, we grew a lot, which was the new phase of civil construction industry in Brazil. It was very important for the economy, for the growth of the economy. And several companies as of that year started to work very hard to grow, and to occupy the space they deserved in our industry. MRV was one of them. It was a company that from 2005 to here grew more than 1,000%, and I would say that 2012 was an important year. Unfortunately, lots of companies were along the way and had unfavorable results. But MRV very proudly has reported along the year very favorable results.

And how do I analyze the year of 2012? After the very steep growth we had, we wanted to consolidate the Company in 2012, and that's what we did. We were able to do something unique, and I think this is important. The Company has five areas: budget, development, production, real estate credit that is very strategic and finally financial and administration.

In 2012, it was a year that all these areas in the Company were able to grow, to get to the level of 40,000 units a year, which is very important for the Brazilian civil construction industry in Brazil. So, we were able to get there, to go through very good growth, and to get to a stage that enabled us very good quality of operation, which was unique. We were able, today, to have a very good production machine.

Today we are the only company in Brazil that has capacity to produce that many units a year, a 100,000 units simultaneously. It is a landmark in the construction industry, and we did that in 2012. So, it was very important to build with quality, at good cost, we were able to review our processes, we have well-managed processes. So, I think that it is something that is really going to give pace to MRV in the future.

It is the first time in the construction industry where a company is able to build more than 40,000 units. This is something that we did -- that should -- that we did for the first time in the country, and we are very proud of our partnership with Caixa Economica Federal and others. So, we are working more and we are being able to improve our Company. Another thing that I would like to highlight is that administrative-wise, we have good revenue here within -- at a good cost with quality, our part of costumer services is doing very well, after sales. So, I would say that all this is being very well worked out.

Our sales were perhaps not as good, but it was a good year. I think that it is important. It was, I think, in short, 2012 was a year that completed a cycle. We consolidated in 2012 the Company, and in 2013 we are going to start this new phase of improvements for the Company, to improve all the areas. We are all going to be able to improve all our areas, to more and more have good results. Our production area is better, more efficient, sales are doing good. We are spearing no efforts to work well, so I can say that in all our areas we are going to work very hard to get to the best results. So, 2013 is going to be an year of improvement.

With regard to margins, we always had very good margins and we knew that in 2012 our margins were going down. There was series of factors so that -- as we published in our report, but margins are a continued process. We are at the bottom part of our margins, but that is the start of a process. The margins went down, but from now on we believe that they are no longer going to go down, and rather they are going to gradually go up.

So, what I see is that our worst result, which was in the fourth quarter on 2012, after very, very solid results in seven years, it was still

very good. I think that 90%, 95% of the companies wanted to have our margins. Sometimes the market thinks that this is not good, but to have a free margin of 13%, but EBITDA margin of 19%, it is very good. Some people say that it is not good, but if you compare us to the rest of the market, it was an excellent job. But anyway, I think that from now on things are going to be better. 2012 was not a bad year, it was a good year, but certainly 2013 is going to be better. Not being optimistic, I'm being realistic. We are going to see that along the quarters.

Anyway, to discuss the data more, I will turn the call over to Leonardo Correa, who has some interesting data to show you.

Leonardo Guimaraes Correa {BIO 15387486 <GO>}

Good morning to everyone. You can follow my comments with the presentation that is available on our website, as usual. I'm going to start with slide four, and perhaps I will be repetitive here, but I would like to start talking about our cash flow.

2012 was an year of inflection in terms of generation of operating cash. We consumed cash in the first quarter and then we had a neutral cash, and then we had a cash generation in the 4Q12. The evolution of our operating indicators show the sustainability of continued cash generation since the land bank will remain stable, the volume of production and transfers are also balanced. Along the last years, we grew pre-sales and production in a speed that was higher than the volume of the cycle of transfers, increasing our accounts receivable. Our cycle, as of now, our accounts receivable is going to be converted in cash to be used, first, to deleverage the Company.

On slide five, we show the evolution of our customer satisfaction levels, which is measured based on the percentage of customers that recommend MRV to their friends and family members. This has been growing exponentially. This is the reflex of the importance that clients have to MRV, and in a way it guides our operations. We have a very complex, fragmented operation, but we are already structured in all business areas, aiming to meet the expectations of our clients. We have a firm commitment of delivering our units in the right time, sometimes even before that and with the expected quality. In 2013 we are going to continue to focus on improving our operating quality and have a production level similar to the year of 2012. Finally, this year we are going to have an important growth in the number of completed units, the last operating indicator to reach the level approximately 40,000 units.

On slide six, I'm showing the main factors that pressured our gross margin in 2012 and some of the highlights are, well, we already talked about the TAC in Campinas that we had in the first quarter. We approached that in the conference call of the first quarter. We had greater efficiency in credit transfers, which is positive for cash generation from the Company, but the sooner you signed the agreement you have a negative impact in the gross margin, which is offset by the net margin.

We invested a lot in improvements and the monitoring of the work conditions of our construction sites to be a national reference in labor and social issues. There is not much impact of that in terms of numbers, but it is a plus that the Company has compared to the market. We also changed the process to deliver units in the end of 2011 to try to really exceed the expectations of our customers, especially in larger projects. Also not a very large impact, but it had some. I would also like to talk about the termination of agreements, marginally it was bigger than the third quarter, we had less amounts than in the year of 2011, and we expect to change this levels as for the future. We expect to improve, although not substantially in terms of differences of levels.

And finally, we finalized older projects that suffer the more negative impact in our growth process, which affected our statements. It is important to highlight -- the highlight to the focus of the Company generating cash, the focus of our management in 2013 will be to gain productivity, efficiency, and reduce the financial cycle. And the conditions that are pressuring our margins are already identified. We have to work hard to take our profitability to historical marks, correcting our prices but also talking about our costs, even if we cannot deliver

everything immediately in the next quarter. These are improvements will be seen in the year of 2013.

On slide seven, we show the impact of the change of the RET tax bracket and the amounts that are elected to that 1% fee. First, we had a reversal of the deferred tax in the fourth quarter. We expect an additional reversal in the year of 2013 first quarter. Additionally, perhaps the most important message is that we are going to have a gradual reduction of the Company's total tax percent because of the increase of the RET in our business. So, that was -- our tax percent is going to be around 4%.

Now, on slides eight and nine, I have just a very brief comment on LOG and Urbamais. The clear message is that MRV does not only generate value with its construction units, but also with other real estate opportunities it has. In LOG, the construction volume is accelerated, our portfolio is more than 1.4 million square meters of ABL and a growth of 31% compared to December 2011. We continue to expand geographically our operation to become a domestic player with commercial and industrial properties.

In 2012, we built approximately 200,000 square meters of ABL and 252,000 meters that were delivered to operations. It is an aggressive growth plan for the coming years, and LOG results are going to be more and more representative, they can generate value to shareholders. It is important that the value generated by LOG is still not being included in MRV valuation by most investors and analysts. But we are negotiating with investors that are interested to grow LOG and we will certainly will share the information with the market.

At Urbamais, it's our newest subsidiary, we already have independent professional management, very well defined business lines. In less than six months of operation, we already have a land bank with a PSV of a bit more than R$600 million, and with Urbamais growth and development we are sure that this is also going to be a company that generates values to its shareholders.

Before going to the Q&A, I would like to tell you that the Company is no longer going to offer guidance on its margins and sales. Of course, every now and then, we are going to be talking about our expectations of sales and performance, but we have decided to go for the change after we conducted several studies and benchmarks in our industry and in others, in Brazil and in the international market, and we realized that most companies do not offer guidance. I think that this is very important, especially for an industry that itself -- has very long cycles, almost four years, and then sometimes have guidance's in a specific quarter, we are not giving our listeners the best information.

Rubens Menin Teixeira de Souza {BIO 15387481 <GO>}

Well, this is Rubens again. I heard that my audio was not very good, so I would like just to go back to the main points of what I said.

First that differently from other market and some analysts say, MRV had a very good year. We performed in a balance area in all our five areas. They did very good in terms of real estate credit, production, and I tell you the following. For the first time that a company can do 40,000 units in Brazil and also transfer that in real estate credit. So the maturity of the Company, I said that MRV was the company that most grew from 2005 to today, more than a 1,000%, and differently from other companies that became along the way or had very poor growth; we had sustainable good quality growth with very few problems along that time. And for the future we want to improve our operations.

The results we will have in 2013, I said, I mentioned that the worst results were for the fourth quarter of 2012, so from now on we are going to improve. But even our results of the fourth quarter, some companies would love to have that. But they were our worst margins. So, we had a decrease in our results and we believe that we were in a valley, but from now on we are going to have an ascending positive movement. This is an industry that does not have a straight line; industries have peaks and valleys, but we want to go back to the results that we always had.

We are optimistic, we are confident, we have the best platform in the market, we have more than 100,000 units in production, we have a differentiated structure and that gives us the guarantee and the certainty that in the future we are going to produce well and yield good results to our shareholders.

And now we are going to open for Q&A.

Questions And Answers

Operator

We are now going to the Q&A session for analysts and investors. (Operator Instructions). Our first question comes from Rafael Pinho from Morgan Stanley. Please Mr. Pinho, you may begin.

Q - Rafael Pinho {BIO 15321539 <GO>}

Good morning, everyone. Rubens, Leonardo, I would like to understand something. We have been following your company and we have an account of what we think your cancellation rates are, and in the last quarter we had seen a substantial increase in the numbers was about 300 million. It was about 300 million but this quarter it went up again, above the 300 million.

I know that you are working to improve the quality of your portfolio and to avoid this kind of problem. So I would like to know what happened in the fourth quarter. Do you think you are going to keep this level of the 300 million? Do you think you are going to decrease the number and also I would like to understand how much this is related to the difficulty of the Company of generating more cash? I know there is an impact in your revenues and generation of cash because of course this number of cancellations was not passed on to your cash. So is that a correct analysis? Could you talk a bit about that?

A - Rubens Menin Teixeira de Souza {BIO 15387481 <GO>}

Well, this is Ruben. Well, were you able to listen to my part of the presentation?

Q - Rafael Pinho {BIO 15321539 <GO>}

Well, your part of the presentation was not that good. Also, when Leonardo was speaking, it was a lot better, but we could understand it. But we lost a bit.

A - Rubens Menin Teixeira de Souza {BIO 15387481 <GO>}

But anyway, Rafael, let me say something to you then. Well, in terms of cancellation rates, I have always said that and I'm going to repeat that. It's not bad for the Company, financially wise. Whenever you have a cancellation, you resell the units at a higher price and you have a margin gain.

So, I have always said that. When you sell a unit, you want to complete the sale. The Company wants that and the client wants that, of course. But today we lack units in Brazil. So, cancellation rates are high. We want the clients to continue with the agreement, with the purchase. But it may happen along the time something that escapes our control, the customer loses his job, or something happens, or a separation, and they cannot go on with the contract.

So, we understand that (inaudible) the program has a 10% rate, which is our average cancellation rate. Sometimes it is a bit higher, a bit lower, but this is about this number. What I think is interesting is that it is very hard for us to improve that. It is a whole process -- you sell the unit, then you have the financial agency, and then you have uncertainties, sometimes people are not ready for that.

Now, differently from cancellations and after end units, these units are sold very fast, so cancellations are not necessarily a problem, they might be a solution. So, companies have to try to complete the sale, to have the client along with us. But if it is not possible, we are going to cancel. And remember, whenever there is a cancellation; whenever there is a termination, there is an improvement of margins. And we are very efficient and basically the cancellation rate is about 10%. So, that's what traditionally is and I think that is it.

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

And Rafael, obviously, if you are taking a look at the inventory of units at market value, we are working very hard to recover margins and there was an increase in prices, and that explains part of the cancelations or the terminations. But anyway, in the fourth quarter we had cancelation rates about the volumes that we had in the last eight quarters, slightly higher but really I think it is more due to the change in prices that we had.

Q - Rafael Pinho {BIO 15321539 <GO>}

Leonardo, if you enable -- allow me a follow-on, could you give me a number of what your record position was above the INCC because then we can calculate better numbers. And also I would like to know the effective impacts on your cash generation. So you terminate this customer and then you generate less cash. Is that correct?

A - Rubens Menin Teixeira de Souza {BIO 15387481 <GO>}

No, it is not. It is very important that you understand that. What happens in the market today, in the levels 2 and 3 of Minha Casa, Minha Vida, you launch a project for R$100,000. Today we do not have an inventory of finished units, this is very important for you to understand because that's crucial for our business. You see that rents today are above the price of the installments for you to buy a property, it is R$900 per month. So, this unit that is ready to sell increases value very fast. So, the original price was R$100,000. When it is ready, it is worth 150,000, 180,000. There is an increase in price. And so you correct the price not based on the INCC, but at market value, and this market value is huge, it has not been historically such a difference.

So, what happens is the following, the industry in Brazil is building much less units than the demand. So, what happens, the demand is very heated, it is very high, so when the property is ready or semi-ready, the price goes up amazingly and then you have a reassessment of the asset. This is a market reality. If you survey the market, especially in small, medium, and even large towns, you are going to see an apartment of two bedrooms that is R$145,000, it is very expensive. But when you sell the project, it is R$100,000, so the first customer will pay a much lower price. But remember, we do not have ready units to sell. This is a really important aspect.

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

And you see the evolution of INCC, it is about 6% to 8%. FIPE, ZAP rates for real property that is ready, you are going to see that although it is an index that is above which is more restricted, you see that it evolves at a much higher pace, and that is what the industry recovers in terms of prices because of all the increase of cost, because of all the growth that the industry had.

Now, going back to your question, the point that you are asking specifically, you see when we transfer credits, let me try to say it this way, I can transfer a unit that is in the beginning or when it is completely finished. In the beginning, when I am transferring the credit, I receive less, but then along the contract I get to the installment. When I transfer the property when it is more close to its end, I receive more money. So, there is a certain volatility in what I receive quarter on quarter depending on the stage of my units, if it is older or if it is newer.

Q - Rafael Pinho {BIO 15321539 <GO>}

Okay, Leo. I do not want to extend myself in the question, just to give opportunity to everyone. But I thank you very much, and have a good day.

Operator

Our next question comes from Marcello Milman from BTG Pactual. Please, you may go.

Q - Marcello Milman {BIO 7252528 <GO>}

Good morning, everyone. My question is regard to margins. You already mentioned that one of the impacts that explains the margin of 2012 were additional expenses in the delivery of units. But I would like to know in, I would like to understand why you had an increase in other expenses. In the third quarter it was higher too, it was about 16 million. So, perhaps it has to do with the number of deliveries, and also you're increasing costs in the costs of deliveries because in 2013 you are going to deliver a lot more units. So I think it is very important to know the potential impact of that.

A - Rubens Menin Teixeira de Souza {BIO 15387481 <GO>}

Hi, Marcelo this is Rubens. Let me tell you something very important about what you are saying. There are two things that happened here. Our pricing in 2011 was not good. We think we sold in 2011 at a price that was lower than what we should have had, especially in the last quarter. In the last quarter of 2011, we had record sales, we had 1.600 billion, 1.580 billion [ph] that's for 2011. And at that time the price was very competitive, very low and I think we lost some margin there and we paid the price for that in 2012 a bit.

But anyway, another thing that is important is that we are in a new age of consumers. Today delivering an apartment is a lot more complex. After you finish the unit, you spend in that unit for another year. In the past you did not have that, but now we are including that in our budget for the new units. The launches in 2012 that we didn't have that, we had to absorb the cost after the units were completed. For the new units that are going to be delivered from now on, more and more this cost is embedded in our budget. So, we are not going to have as many complements of costs.

Once again, I would like to highlight two things that are important for you to understand. Number one, that we have been doing, we do not have expect costs, sometimes we have to have review our budget and we have to recompose them. We have very good budgets, so we do not have a mismatch of budget. What happens is that sometimes we have to review our budget, and that affected a bit our margins for 2012.

Now, another thing that is important is that we are conducting a very interesting study in terms of provisioning and maintenance, and we are very conservative because we have to deliver the whole condo and you have the maintenance for that. In 2012, we had almost 200 million provisions for maintenance, the cost that we would have in 2013. Perhaps that is a bit too much, for we are being more efficient in that. In the past, delivery was a bit more complicated. We were having costs that were not provisioned for. But now we are even provisioning less for maintenance because we know already what it is like.

But just for you to have a comparison with other industries, we provision 10% for maintenance, even less than that. So, again it shows that we are getting it right with the customer. We want customer satisfaction, we are delivering the units correctly, we are meeting their expectations, and we are providing good maintenance. So, that affected the margin a bit in 2012, but I do not think it's going to be that important for 2013. It is a fact that happened in 2012, it is important for us to highlight, but it was corrected. We also had 31 million in terms of maintenance, so it is something that we are doing our homework.

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

-- Yes, you also talk about other revenues and expenses. There are several smaller items we spent a bit more with legal issues in the fourth quarter 2012. We had -- rains in Rio de Janeiro, because of the rains that we had there that was very expensive, we have donations there. So, there were some smaller items but that all together increased this line of other expenses. So, this impact of other expenses has nothing to do with delivery.

Q - Marcello Milman {BIO 7252528 <GO>}

And talking about what Rubens mentioned, you are going to deliver more units in 2013, and these expenses are going to be higher, but they are going to be a bit offset because you are provisioning better for that.

A - Rubens Menin Teixeira de Souza {BIO 15387481 <GO>}

Yes, Marcelo, what I said is that more and more with these new units we have better provisioning. So, we are going to deliver more units but we are not going to have as many expenses because they are already inside the budget.

Q - Marcello Milman {BIO 7252528 <GO>}

Okay. I understand. Thank you very much.

Operator

Our next question comes from Luiz Garcia from Bradesco.

Q - Luis Mauricio Garcia {BIO 1827948 <GO>}

Hello everyone, good morning. I have two questions. The first is about your free cash flow. Along the quarter we saw an expressive improvement in some working accounts that affected your free cash flow. You increased the number of transfers and you have a higher purchase of lands, and you decreased your rhythm of expansion. You were doing 10,000 units per quarter, and now you are, in the fourth quarter with 9,100.

And another thing that called my attention was the advance of the receiving of customers, including swaps, that increased by 25% from the third to the fourth quarter. That accounted for 127 million in a quarter where we saw some stability in sales. And the number of advances to clients accounted for 25%, or 127 million. But your cash flow is 13 million above, which is a lower number that all these other items I mentioned. So, the receivables are not going down. So, I want to know what really affected your turnover. Where does it come from? You did have non-recurring expenses, but anyway we understand that why. So, why didn't you not have a higher free cash flow?

And the second question is about G&A. You had a growth of 27% quarter on quarter, especially wages, provisions for contingencies. And Rubens already mentioned some problems with maintenance, we have seen that increasing, today the Federal Government announced that there is probably going to have a new package for consumer protection, reinforce our consumer protection agencies that will probably impact several industries of the Country. So, what do you expect for G&A? Are you going to keep the levels of the fourth quarter that plus inflation? Or if you can reduce G&A? Well, these are my two first questions, and then I might have a third one.

A - Rubens Menin Teixeira de Souza {BIO 15387481 <GO>}

Hi, Luiz. This is Rubens. Can you hear me, alright?

Q - Luis Mauricio Garcia {BIO 1827948 <GO>}

Yes, perfectly.

A - Rubens Menin Teixeira de Souza {BIO 15387481 <GO>}

We are checking the audio, if you please have any problems with audio, it seems that in the beginning it was not good, but anyway. Luiz, it's very important for us to mention your questions in detail, because sometimes we have some distortion. Let me tell what happened in the fourth quarter, we are talking to Caixa and Banco do Brasil, we are very close to them, but there some changes in the system that sometimes can affect our business.

Caixa, specifically, had a change in the way it releases resources in the last quarter, which cost us about 80 million in reimbursement. If disbursements were made exactly the same that they were made in the previous quarter, we would have an extra 80 million in our cash, which, hypothetically, would have increased our positive cash. It would be close to 100 million, which would be exceptional, but it did not happen, because there was a change with Caixa. So, your question that was very well articulated, but it is not taking into consideration those change with Caixa.

And then, it is very interesting, Gerson can explain it better to you but Caixa is doing something like transient cash, so the client signs with Caixa, but it does not pass it on to us. So, this is something that we have been discussing with Caixa, they want to improve too, but what happened is that we lost almost a 100 million with that. And in this quarter, we are going to have changes as well. I know that we are going to have this amount that we still have to receive, the Government wants to improve the flow of the Minha Casa and Minha Vida program, but these are things that happen and we have to highlight to you.

Another important piece of information that I would give you and to hold off the market is the following. Today we have 4,000 units under construction, perhaps more companies are building that, we have 3,000 units in construction -- 4,000 units in construction. I think that we are one of the companies that most build in Brazil and yes, that was in Rio de Janeiro and I visited a construction site. It has 500 units with traditional masonry, the traditional masonry is faster and it is cheaper. So, these are the things we have to think.

We have to think of the metallic forms, we want to do better with technology, but today we are thinking about that and we think that structured masonry is being cheaper. It's not a matter of not knowing how to do or anything. Yesterday, we went to Rio de Janeiro to take a look at this construction site, we have 500 units with metal framework and the other with traditional masonry, and you see that masonry is better. And it's very interesting that you understand that, so 100,000 units in construction, we have to have a team to measure that. We deliver in time, we have the right to delivery.

So I think things are getting better. We can even talk more about that, but it is very important for you to realize, we are analysts, we have questions to ask, but we have very interesting things to tell you.

Q - Luis Mauricio Garcia {BIO 1827948 <GO>}

I think that we have the signature of the contract and now Caixa is not blocking that any longer in your account.

A - Rubens Menin Teixeira de Souza {BIO 15387481 <GO>}

Yes, they call it transient account, this is something that costs us R$80 million in the quarter, but we are working with them, all construction companies are, to try to improve that. And we will be able to do so.

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

With regard to expenses, Luiz, the G&A this year, as we mentioned, we grew the structure of the Company, the Company is well structured, we do not have G&A increases any longer, the G&A is just the pass on of INCC or inflation rates, wages. As for sales expenses, we had a higher volume in 2012 and sales expenses in 2013 are going to be smaller. We identified several areas to improve our efficiency and we have just to change the way we are doing things, to find a cheaper way of doing the same thing.

Q - Luis Mauricio Garcia {BIO 1827948 <GO>}

You're going to have a reduction in sales expenses and G&A is going to be more or less the current level plus inflation.

A - Rubens Menin Teixeira de Souza {BIO 15387481 <GO>}

That's correct. And if you allow me a last point about things that make sense in terms of the Company, we had bad surprises in older projects, but there was something interesting because the cost of land was cheaper in some regions, some regions still did not have a supply. And now we see some regions where the Company is operating, like Paraiba, Sao Luis, Vitoria (inaudible) where sales performance, not only of the Company, but of the market as a whole, is very bad. So, we do not see today, given the macroeconomic situation, inflation, others, to improve the purchasing power of people in a very fast way. It is probably something that is going to be very gradual.

Q - Luis Mauricio Garcia {BIO 1827948 <GO>}

Well, that said, we have seen several regions where you are not selling as good, you had a very strong launch in the third quarter in Paraiba, but you did not sell much, neither did you in Sao Luis. So, we understand that new projects could evolve, but as a counterpart some regions are not that good. What would be the strategy of the Company to leave these areas, to give up? How do you see the geographic situation given the dynamics very different gross levels?

A - Rubens Menin Teixeira de Souza {BIO 15387481 <GO>}

Well, Luiz, it is interesting. You talked about three regions, Vitoria had record sales in the fourth quarter, the Joao Pessoa had record sales, and Aracaju in Sergipe also had record sales. Sao Luis do Maranhao (inaudible) started, we started in December, we had five days of launch. It's very little. These are very good markets, Fortaleza, Recife, (inaudible) of the Country. That is what we expect.

The sales in 2011, there -- look at this, this is interesting. If you get the price of land in 2011 and you have INCC, the land in 2013 is cheaper. I told you that in other calls. I think that what we have to focus is that the prices of sales in 2011 were not good, we had a huge level of sales but with a bad price, but not anymore. We are really thinking that these markets are going to be very good. What you are saying I think they are stable markets and they are our greatest bet for the future.

In the last quarter, we sold in the Northeast, in Aracaju, 900 units in a month and a half, so they are very good markets. And what sets us apart is that we have no competition and we have a very efficient structure of production, sales, and credit. So, what you see as a problem, to us is quite the opposite. It is a good strategy, correct, and we are certain that this is going to be an asset for MRV.

Q - Luis Mauricio Garcia {BIO 1827948 <GO>}

Okay. Thank you.

A - Rubens Menin Teixeira de Souza {BIO 15387481 <GO>}

Thank you very much.

Operator

Our next question comes from Marcelo Motta from JPMorgan. Please Mr. Marcelo you may go on.

Q - Marcelo Motta {BIO 16438725 <GO>}

I have a question about margins again. If you could explain a bit what 2013 is going to be like. What happened to your EBITDA margin? You had expectations in the beginning of the year of 24 to28, when you announced your guidance. What really made things escape of the control? And for 2013 what factors are going to stay, what can you work with? Just for us to understand what the dynamic of margins is going to be like.

A - Rubens Menin Teixeira de Souza {BIO 15387481 <GO>}

Hi, this is Rubens. First, we have to admit that we had a better expectation and we were wrong. Now, the second point is, first, we had some setbacks. Setbacks, in our case, is that we expected something to happen and it didn't. We expected that we would have a better year, LOG did very well, it is going to have an important rate for MRV. And second, there were some factors that were bad for us. We had some setbacks, we had the problem in Campinas that affected our construction prices.

And in addition to our over optimism and the setbacks we had, we had things of the day to day that affected our results. I think that 2012 paid the price of mistakes we made in the past, but more and more this is not going to happen, and that's why we believe that we are very optimistic that our operation is more in place from now on. I think that we made less mistakes than the rest of the industry, but still we have to be honest to say that we did make mistakes. Our guidance was wrong. There were setbacks, but we also made a mistake in what we thought was going to happen. So, 2012 paid the price of our mistakes.

I think that the greatest price we paid was the sales that we had in 2011, we wanted to go after our guidance, we sold units at a very, very competitive price and that wasn't good. I will give you an example, we have 1.5 billion in units that are to be launched and we have not launched them, that comes from the fourth quarter. And why is that? Because we did not want just to meet guidance and margin at any price. So, we want to hold the launches, we decided to hold them in the first quarter not to just do anything and depreciate our margins. Differently from what we did in 2011, so we want really to have a more balanced company. We are going to sell well, we are sure of that. We are going to sell 6 million to 7 million? No, we want to sell at consistent margins and really settle all the inventory that we have in a consistent manner. 40,000 units is something that that we have to work very carefully.

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

Just to tell you, we could sold more. We didn't have that many sales, we didn't meet the guidance because of the macroeconomic scenario. Brazil grew less than expected, and we were affected as everyone else, we were more optimistic, we had an expectation that the prices on Minha Casa and Minha Vida would be corrected earlier in the year; they were only corrected in October, that also led to a difference in prices.

In commercial expenses, we spent more money than we should have. There is no other way to say that. We can be more efficient than doing more things with less money, to sell the same amount, we're spending less money. Commercial expenses also had an impact in EBITDA margin.

And finally, not finally but we had these other operating expenses, legal expenses and everything that also had a negative contribution to the EBITDA margin. Of course it was not our expectation in the beginning of the year. And finally the gross margin, which was slightly lower, completing then, the scenario of why we haven't met our guidance in sales or margin.

Q - Marcelo Motta {BIO 16438725 <GO>}

Okay. Thank you very much.

Operator

(Operator Instructions) Our next question comes from Mr. Javier Gayol from GBM. State your question please.

Q - Javier Gayol {BIO 17879480 <GO>}

Hi. Good morning. Thank you for the call. I have two questions. My first was -- first question would be, you mentioned in your press release you found comfortable levels of debt, your current levels that you are comfortable. Could you tell us where -- how much further could you leverage the Company until you reach an uncomfortable level?

And my second question is related to, are you comfortable with the level of inventories and the land bank that you have? Hello?..

A - Rubens Menin Teixeira de Souza {BIO 15387481 <GO>}

Can you please translate answer in press release so that are translated -- can translate into English? Tell me just understand that I understood your question.

Speaking English. The question was leverage. Is that correct?

Q - Javier Gayol {BIO 17879480 <GO>}

Yeah, my questions the leverage you say -- you were (inaudible) in comfortable levels? Okay. The second was your level of inventory to the land banks and do you find that you need to invest more, in order to secure your launches for 2013 and going forward? Or are you at more comfortable levels during the (inaudible)?....

A - Rubens Menin Teixeira de Souza {BIO 15387481 <GO>}

Okay I'll translate that. The --

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

For the first question, -- the first was with regards to leverage and cash generation and the second was with regards to the level of units that we have in inventory. So answering your first question. Now with regards to leverage, yeah, the cash generation of 2013, the allocation of resources, our first idea is to decrease the level of leverage of the Company. And our intention is to be close to approximately 30% net debt to equity.

And with regards to inventories, we are very comfortable with our inventory levels now. Once again, we are managing our inventory levels comparing them to the price of sales, speed of sales. This is something very important because that's what we have to have in mind. We have to maximize the amount that is sold in terms of volumes, but at a good margin.

Operator

Our next question comes from Eduardo Silveira from BES Securities. Please you can go on.

Q - Eduardo Silveira {BIO 16201252 <GO>}

Good morning, everyone. I have still a question about margins: I know you are not giving guidance, but when you accelerate the amount of deliveries in 2013, close to 40,000 units, can we expect a drop in margins because of the expenses of delivery that you mentioned. And if you can explain a bit better, you talked about a reduction of margin, can you tell us in 2011 how much you had in receivables and how much you have in 2012, just for us to try to understand this drop in gross margin that is offset by a better financial result?

A - Rubens Menin Teixeira de Souza {BIO 15387481 <GO>}

Well, I'm going to answer your question in two parts. You talked about two very important things. As we migrate to larger projects, you have less cost of delivery. If it is just 100 units, it is more expensive than if you have 300 units, relatively. So, we are improving deliveries and these amounts are going down. So, we think we are going to have two positive things here, first, in our budget we have all these deliveries of 2013, differently from what we had in 2012, and that the cost is going down for delivery and maintenance.

Yesterday, or just weekly once, we has to deliver condos in Mogi das Cruzes, in Sao Paulo. It's 301 apartments delivered on a day. It's

a condo of 400 units and we delivered 301, so the customer satisfaction goes up and the price goes down. So, our cost of delivery is going down, our maintenance costs are going down, they are going to have a much lesser weight in 2013 than in 2012.

And then, in terms of leverage, cash flow, MRV is being able to have positive cash flow, it's growing its operations, and perhaps it is a company that has the lowest leverage in Brazil, especially because our cost of assets. What is bad about this? Is that when you sign with a customer, you have to consider the INCC contract. This is bad because you are going to be paid in Reais at a fixed price, and that consumes margin a bit.

When we increase the associative expenses and we give increase them in 2012 because we are being more cautious with that but we have to be careful with that. And MRV is the only company in Brazil that is working at -- in this manner. We are optimizing our cost of capital, but sometimes you lose a bit of margin because you can no -- after you sign you can no longer take advantage of any increases that you might have. The money is not corrected as fast as the market grows.

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

But we think that we are on the right path. I'm going to tell you the amount of -- credit that we have because you have to think of accounts receivable on-balance but also off-balance, which can bring more impact for the Company.

Q - Eduardo Silveira {BIO 16201252 <GO>}

Okay. Thank you very much.

Operator

Our next question comes from Rene Brandt from Banco Safra. Please, Mr. Brandt, you may go on.

Q - Rene Brandt {BIO 17277802 <GO>}

Well, good morning, everyone. I have some questions about adjustments for the improvement of the quality of your products. You talked about the quality of your construction sites, do you have any reversal of revenues? Was that just additional costs? Did you review the whole of your budget, or just for the part that was delivered in 2012? So, I would like to try to understand exactly what you did.

And also about the deliveries for 2013, if eventually in the first quarter, we can expect a significant delta. What was delivered in this quarter? If you think of a period of construction of ten quarters, 30 months, you probably delivered 10,000 to 12,000 units. If you expect this volume for the first quarter of this year?

A - Rubens Menin Teixeira de Souza {BIO 15387481 <GO>}

Well, let me talk first a bit of the construction site. I have been working with civil construction for 38 years and it is impressive how working conditions changed along the years. The number of labor extents are going down, this has to happen. It is important that it happens and we invested a lot on that, a lot. Recently we did something that was very nice, we were the first life to the construction company that joined the national pact for negotiation. We have a trade union leader in each construction site to take care of that construction site. So, we invest on the quality of labor. It is nice to visit our construction sites.

Apparently, it can be expensive, but it is not. You improve productivity, you make a better work environment, so our construction site is a model construction site. I do not think anyone has anything like us. We have training, we have recreational areas, health services. It costs money, but this cost can be profitable to us, because workers profit from that, but the Company profits from that as well. So, this is very, very important.

As for delivery, as well I have a forecast for you, but it is the end of the cycle. Your first launch, then you sell, then you sign, and then you deliver. So we increased deliveries a lot in 2012 and we will do so as well in 2013. We are going to deliver more than 35,000 units in 2013. This is very interesting. Customers are satisfied, we are delivering on time, and this is something that you really should take a look at all companies, the number of deliveries, because the delivery is the end of the cycle.

We have the money, the customer is satisfied, we took an important step in 2012 and in 2013 we are going to close the cycle and we intend to be very successful, we want to go above 35,000 and get to the 40,000. So, this gives us the comfort that we are doing things right. I don't know if I answered your question.

Q - Rene Brandt {BIO 17277802 <GO>}

Yes. Thank you very much.

Operator

Our next question comes from Enrico Trotta from Itau. Please you may go on.

Q - Enrico Trotta {BIO 16742911 <GO>}

Good morning, everyone. Thanks for the presentation. I do not want to ask too much on margins, but you said that margin was impacted by the recognition of older projects with lower profitability. You talked about 2011, that the price was probably wrong. Can you talk about the gross margin of the projects for 2011 and these older units vis-a-vis the current projects that being launched now?

A - Rubens Menin Teixeira de Souza {BIO 15387481 <GO>}

Well, unfortunately this is not a number we can disclose, we cannot give you the guidance. But indeed, margin comes from two things, the price of cost and the price of sale. You can have a damage in margin if you have a poor construction, which happens to some companies, not MRV, but if you sell poorly, which happened to us in 2011. So, in 2011 we had less profitable projects, but they were corrected in 2012, and as of 2012 we are going to see the results in 2013, and margins went back to the traditional volumes that we had.

So, the combination of the price of your cost and the price of your sale is a lot more balanced. So, the margins in 2013 are going to be better than what we saw, more related or closer to the traditional or historical level of the Company.

Q - Enrico Trotta {BIO 16742911 <GO>}

Okay. Thank you very much.

Operator

Our next question comes from Marcello Milman from BTG Pactual.

Q - Marcello Milman {BIO 7252528 <GO>}

If I could ask just one more question, just a follow on a previous question. You expected to have better margins and sell more and avoid poorly pricing the product. What is your challenge now? You have more objectives and the costumer will also have to pay more? That may impact the quality of your sales. How do you see that? Try to sell more, at a better price from customers? But costumers cannot really afford much more.

A - Rubens Menin Teixeira de Souza {BIO 15387481 <GO>}

Well, Marcelo, our time is just about to finish. I will try to be brief. But it is what we said, our capacity to balance the price with the quantity of sales. If we make a product that is good and we believe that, and there is a demand, we have to price it well to balance the sales. I'm not going to try to take a wrong step in 2013, I want a very well balanced operation. If we sell less in 2013 it means that we did not get it right. I'm not going to lower prices. What you are going to see along the year is the following, if MRV is growing sales and the margins are getting better, this means we are doing it right, otherwise we are doing it wrong. What we have to do is to get it right; we have to sell more and adjust our margins. This is what we are focusing now. And I'm convicted that we are going to be able to do that in a consistent manner in 2013 and we hope to show it to you.

Q - Marcello Milman {BIO 7252528 <GO>}

Okay. Thank you very much.

Operator

Our next question comes from Luis Mauricio Garcia from Bradesco. Please Mr. Luiz -- Mr. Garcia, you may go on.

Q - Luis Mauricio Garcia {BIO 1827948 <GO>}

I had just a brief question, a follow-up. We saw project of the Company, specifically an SPE that is very representative with very high volatility, which is one of the projects in Taguaatinga, with a profit of 33 million and a -- in the third quarter and a negative contribution. I was drawn in terms of attention of this high volatility. Was there any recurrent effect that happened in the third quarter? So, it was very, very high volatility in a single project in the Company.

A - Rubens Menin Teixeira de Souza {BIO 15387481 <GO>}

I can't answer you right now. Monica is going to get back to you to talk about this specific project. I don't know what project you are talking about, I do not have the information. We are going to look into that, Monica is going to get back to you. Perhaps it's some non-recurring event in price or cost of project. Monica will get back to you and we are going to give you the information in a more organized manner. Okay.

Q - Luis Mauricio Garcia {BIO 1827948 <GO>}

Yes, certainly.

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

In the fourth quarter, I do not think we did have a negative result, but anyway, we are going to get back to you. It is a good project, it has been sold at a good price with a good cost. I don't recall all the projects by heart, but we are going to get back to you.

Q - Luis Mauricio Garcia {BIO 1827948 <GO>}

Okay. No problem. Thank you.

A - Rubens Menin Teixeira de Souza {BIO 15387481 <GO>}

Well. Thank you.

Operator

MRV's Q&A session is now closed. We are going to turn the call over to Mr. Rubens Menin Teixeira de Souza for his final considerations. Please, Mr. Souza.

A - Rubens Menin Teixeira de Souza {BIO 15387481 <GO>}

Well, we have two more questions but we -- that unfortunately do not have any more time. We had to follow the line of questions, but anyway we will get back to you. I would like to thank you very much. Once again our IR teams, Gerson, Monica, Leonardo, we are all here for you, if you want to ask more questions, if you need clarifications, because we want to discuss our operation with you, try to explain where we are, where we want to get to. I think this is very important to you and to us as well.

Anyway, we thank you very much, and we are going to continue working very hard in 2013. Thank you very much.

Operator

Well, MRV's conference call on the earnings release of 2012 and fourth quarter is now closed. We thank you very much for joining us and have a nice afternoon.