Q3 2014 Earnings Call

Company Participants

- Emilio Fugazza, Chief Financial Officer and Investor Relations
- Pedro Henrique Nocetti, IR Coordinator

Presentation

Operator

Good morning, ladies and gentlemen. At this time, we would like to welcome everyone to EZTEC's Third Quarter 2014 Results Conference Call. Note that this event is being recorded, and that all participants will

be in listen-only mode during the company's presentation. After the company's remarks are completed, there will be a question-and-answer session when further instructions will be given. (Operator Instructions)

Today's event is available through a live webcast that may be accessed through the EZTEC Investor Relations website at www.eztec.com.br/ir by clicking on the banner 3Q14 Webcast.

The following presentation is also available for download on the webcast platform. The following information is stated in Brazilian Reais and in BR GAAP and IFRS applicable to real estate developers in Brazil,

except or stated otherwise. Before proceeding, let me mention that any forward-looking statements made in today's conference call, regarding the business outlook, forecast, and financial and operating targets is

based on the beliefs and assumptions of EZTEC's management and on the information currently available to the company. Forward-looking statements are no guarantee of performance. 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 the company and could cause results to differ materially from

those expressed in such forward-looking statements.

Now I will turn the conference over to Mr. Emilio Fugazza, Chief Financial and Investor Relations Officer, who will begin the presentation. Please Mr. Emilio, you may begin the conference.

Emilio Fugazza {BIO 16474296 <GO>}

Thank you so much. Welcome everyone to EZTEC's conference call for the third quarter 2014 results. I'm Emilio Fugazza, CFO and IRO. And apart from myself we have here with us Pedro Henrique Nocetti, IR

Coordinator. For this quarter, this year 2014 and third quarter 2014 in one word, out layer for EZTEC. It's important to bear in mind, that it was growth prices in a market we have been trying to sale and trying to

launch a new projects. It's important to understand that this is our regular market now competitive for quality placed and delivers. It's important to understand, that left pace of sales is not a crisis but an adjustments

of the booming markets.

It's important to understand that the company on page number three, the company launches and reaches a R$899 million in the nine months 2014. Launching new projects of considering its stake acquisition of

projects launches by EZTEC, but EZTEC remaining only with 70% now acquired the remaining 30% of the project. Contracted sales reached a R$689 million in nine months 2014, considering its stake acquisition of

281 million of units launched in previous years. By previous years, I mean 2013, fourth quarter 2015 and even the second quarter, the first and second quarter 2014.

Land Bank position reached R$5.4 billion by the end of nine months 2014. And the cost of this Land Bank its about 14 to 15% of the potential sales value of this Land Bank, all in cash not swaps, not exchange

agreements. About financials, it's important to bear in mind, our gross margin reaching something close to 53% in nine months 2014 for the third quarter of 2014, 54% I mean it remains compared to the second

quarter. It's important to bear in mind, the gross drops of R$354 million in nine months, 125 million only in the third quarter 2014. Net income reached 343 million nine months and R$125 million in the third

quarter. Net margin reached a 51% in nine months, 54% in the third quarter 2014.

The annualized, the return on equity of the company its about 22.3% in nine months. It's important to understand that 22.3% means something close to twice as much the debt (inaudible) in Brazil which is now about

11.25%. And almost five times, four to five times debt average, return on average other sector. Net debt position of the company is about R$89 million plus performed receivables of R$227 million can be securitized, whatever

we want adjusted by IGP-M plus 12% per year which means something close to 15% this year. It is important to understand that when you see the net acquisition of R$89 million, this is because we have a strong use of cash to build that EZ Towers project and we are about to deliver this project in Sao Carlos by the end of 2014.

In 13 our net cash-- our net debt position by the first quarter of 2015. To talk a little bit more about our operational highlights. And now I will give the work to Pedro Nocetti now. Please Pedro , keep the bouncing the ball. Thank you.

Pedro Henrique Nocetti {BIO 20904123 <GO>}

Thank you Emilio. Please turn to slide number four, where we talk about the Land Bank. As Emilio said before, the Land Bank ended the period the third quarter of 2014 with 5.4 billion in owned PSV, it's important to say that in the third quarter we acquired two pieces of land which will provide something that is more than 500 million of all PSV. With an average cost of acquisition of 14.5% of the PSV. Therefore as you can see in the chart, in the top right you see that 79% of this Land Bank was brought after 2011. And we are very confident that we will keep the margin of at least 40% with these Land's acquired.

Looking at the chart in the bottom left, it's important to say that 78% of this Land Bank is debt mature the residential from the middle end income segment to the high end income segment, the 20% remain is the insure the commercial segment.

In the chart in the bottom right, its important you can see that Land's 2% of this Land Bank is located in the Sao Paulo Metropolitan Area. In the area and which are very focused and which we are very confidence about the demand and which we keep starting that we'll keep providing good profitability while operating in it.

I want to please turn to slide number four, where we talk about the corporate project EZ Tower's, as you can see the Tower A is almost finished with the -- it's important to say that we will deliver it, we are predicting to deliver it until the end of this year.

You can see that the facade is concluded, the Lob is about to be get finished and the parking spots, they are being definite (inaudible). Looking at Tower B, you can see that the facade enclosed to the top, the facilities there, the installation there and the progress and also the entrance is being down.

Until the end of September, we had 76% of the total cost of the project include.

Considering only Tower B, which is in our inventories by the cost. The cost of Tower B is 198 million. This is the cost of the Tower. We are very confident that we will be able to make this tower as profitable as we made Tower A.

Now please turn to slide number six, I will talk about the projects and the constructions and I see the slide, we have been showing, since the first quarter of 2014.Looking at the PSV under construction it's possible to see and maintenance of volume under construction between the quartered of -- which is the second and the third quarter of the year. And we are very confident that this volume we'll keep in the fourth quarter of the year because although units being delivered, we'll have more projects into the conservation being started. So you will see that their volume of projects under construction we will the same in the fourth quarter.

Now please turn to slide number seven, I will talk about launches, in the month of July after the world cup EZTEC launched the project Le Premier Flat Campos do Jordao, winter station in the country side of Sao Paulo. Our project estimate should very high end segment and our project in which we work very successful in terms of sales, at this moment we have 82% of the units of disclosures already sold which appear to be of 120 meters, so looking at the launches in the third quarter and the nine months of 2014 is very important to say that, on the first day of October is the second quarter 30% of the project Cidade Maia which was launched between the end of 2013 and the beginning of 2014.

This acquisition will provide R284.4 million of all PSV's launched in 2014. One thing that is very important to say although we are showing here is the launches and the sales of this sales acquisition, the finical impact of this operation we only busy in the fourth quarter of 2014. First we'll talk about sales after that I will talk about upcoming launches.

Please turn to slide number eight and we show in here at the sale of the third quarter and nine months of 2014. We ended the quarter -- we ended the month of September with accumulated sales of 689 million including 154 million of Cidade Maia, 41% of the sales referred to unit launches until 2013. Therefore we ended the third quarter with inventory of 1.3 billion, very important say 21% of this inventory becomes is -- comes from third party units, the units which are in the construct, we have 80% sold on average and projects that were launched since December 2013, we have 69% of them sold on average. One other important thing to say about sales, 78% of the sales were done by second vendors, our old brokerage team a very strong brokerage team which is responsible for almost all of the sales of performance units and which is very important for us and as scenario like this to keep operating.

So, I would like you to, please, turn to slide number nine, I'd talk about launches done in the fourth quarter and launches which we withdrawn in the following months, not necessarily in 2014.

In October, EZTEC launches middle end segment projects called Lazaro Suave[ph] Prime House Bussocaba located in Osasco in the Sao Paulo Metropolitan Area. The projects has an EZTEC PSV of almost 120 million and now is 42% sold. It's very important to say that, we have already reached more than 1 billion in terms of PSV launches in 2014.

We have projects approved or earned their approval which are -- able work to launch, the same amount we launch in 2013 or even more but we have our mindset is that, as this launch, we need to focus on what we have or what we have already launched. Therefore, what I am saying now is that, launches view we don't but they will withdraw under commercial decision and we are very confident that we will keep generating value with our investor if it's using our inventory or launching new projects.

So I'm saying that, in terms of projects, we have Legitimo Santana a middle-high end residential project in the North Zone of Sao Paulo with 47 million of own PSV. We have also a high end residential projects in the South Zone of Sao Paulo called Agostinho Gomes with almost 70 million of own PSV and we have a project in the East Zone of the City of Sao Paulo middle-high end called residential projects in the Biguacu II with an own PSV of 46 million.

Now I will hand back the presentation to Mr. Emilio Fugazza, who will talk about the financial performance. Emilio Please.

Emilio Fugazza {BIO 16474296 <GO>}

Thank you so much Pedro. Dear all, let's talk about financial performance on slide -- page number 10. Let's start talking about what's the net revenues on the top left. And you can see nine months 2014, we will kept something close to R$666 million of net revenues. It's important to bear in mind, that's net revenues are impacted by recognizment of the construction on our sites.

So as we has been delivering a lot of project and we are about to start further ones. We are in the moment of prediction between delivers and starting new projects, impacting the total amount of volume, we can release about net revenues.

One of the turns, we are going to see in the next quarter it's about Cidade Maia project. Cidade Maia project is a project of R$1 billion and we have in the past 70% stake of this project and now in the fourth quarter of 2014, we acquired the remaining 30% stake of this project, this R$1 billion project.

And this is so important because it's a project of 45% to 50% gross margin each phase and it's a project to compensate the decrement, the drop on net revenues for the cost. Nowadays, the results of this project is coming to our results, to our bottom-line and equity income.

And now with these acquisitions and the third quarter of 2014 you will see, a migration from their income efforts to the revenue line, increasing the revenue line, it's important to understand that on the side of the gross margin and the gross profit, nine months 2014 we boosted the gross margin by 1.1 percentage points. It's important because even in that different scenario compare it to nine months 2013, we have been selling, very good merchandize for very good prices and prioritize that can compensate the investment and the costs that we have to produce them. Nine months 2013, gross margin of 52%, nine months 2014, 53%. It's important to understand that 53% is a mix of commercial project and a gross margin of 60.7% gross margin and residential, the residential one was the gross margin of 47.9%. So it's a good mix, it's a flat record of margins belonging to residential. Overall in terms, on medium in terms of 47% to 48% and commercial projects 60%. On the bottom left you can see the G&A expenses.

The G&A expenses for nine months 2014, it's about R$78 million. Given this project, it is important to bear in mind that the company has workers to which much, more potential sales value every year then reached this year. 2012 and 2013, we has been acquired more projects, more lands to increase the volume of launches by 15 to 20% every year.

With this new scenario of last projects launches at Campos do Jordao something close to R$1 billion by the end of October. We have few, our SG&A structure to is new moment. And we have been backed in -- true, reanalysis of process and positive in our company. EZTEC doing some kind of jobs in terms of people. These all work overall, you're going to see the results impacted in our net income by the end of the first quarter 2015.

And overall by the fourth quarter 2015, increased this productivity margin G&A expense. In terms of the bottom right, you can see the chart showing the commercial expenses. The commercial is pretty left, the commercial expenses is pretty flat around 4.4 to more than 5%, and over net sales you can see something close to 5.6 to 5.7% of the net sales of the company, in the third quarter 2014. So remains flat.

In the next slide on page number 11, you can see it on the top left, the net financial result of the company, there was graph of financial results, specifically in the third quarter 2014,because the net financial result is made of, work of the cash position of the company -- compensated by the base into (inaudible) Brazil, which is something close to grow $11.25% yearly and the performed receivables we have been financing our clients in something close to R$226 million compensated by IGP-M plus 12% yearly.

This IGP-M, it means the inflation index, the last three months we will on -- a negative inflation index, impacting our financial position, our performed receivables, comparative to positive one in the third quarter 2013. And the compensated third quarter of last year, a R$11.5 million financial results, positive financial results compared to R$9.5 third quarter 2014.

Even think that it's important to see the nine months 2014 and the total amount of positive financial results it's about R$47 million which means 7% of our net revenues. Talking about equity income, the projects we have of shared controlling with our partners in those projects on the top right. You can see the total amount of outcome coming from these projects of about R$73.5 million compared to R$70.9 million nine months of the last year.

It's important to bear in mind, that the nine months 2014 gross margin of these projects its about 41.3% but when you see only the third quarter 2014, you can see a huge increment reaching 46.4% a huge increment compared to the second quarter 2014, to 46.4% in line with our -- with residential projects, 100% controlled by its debt.

It's important to understand that those projects are impacted by the volume of constructions we have. So, as we are going through in terms of construction you were going to see more equity income, outcome coming and margins in line with 46%, 45% pretty stable. On the bottom left let's talk about net profit. Net profit of the company is about 343%. In terms of margins, 51% of this year compared to 50% last year. It's important to understand this drop 20% drop compared to nine months 2013 is mainly due to two facts. First of all, because last year, we had a full recognizement of EZ Towers project in the third -- in the first quarter 2013 because we sold the tower in the first quarter and as we have percentage of completion methods to report our results.

In the first quarter of last year, 29% of the percentage of completion sold reported a huge volume of net profit in last year compared to this year, which is pretty stable in terms of all of the construction not selling the second tower of the EZ Towers project. The other kind of things it's about the drop in 10% of launches, impacting 10% of sales. So less sales, less launches and less revenue recognizment impacting the more line of the company.

But in terms of margins, you can see, it's pretty flat. So we are not filling the same prices, you could be haven't seen in the sector. The last cost on this page is about the backlog margin on bottom right of the page number 11. So the backlog margin is about 53% considering the project acquired at Cidade Maia, the 30% remaining of Cidade Maia projects, you can see this full recognizement, we are going to see by the end of the fourth quarter 2014.

So, the launch, the backlog margin of the company, will be something close to 50% increasing the volume of results, the backlog results to R$604 million and increment of 40% compared to the second quarter 2014. In this specific subject, it's important to bear in mind two kind of things upon backlog. One of them is tower split of EZ Towers .

As Pedro mentioned before, as Pedro has mentioned before one kind of thing is that, the inventory cost of Tower B is about R$198.5 million for this project and you know very well we sold one Tower of the project for close to R$600 million, for the same price for Tower B, would be outcome for R$400 million in net profits and we'll pass through straight to the bottom line. The bottom line not been considered in the backlog.

The second thing is about our inventory, when you see R$1.3 billion in inventory, one part of it, it's about projects ready to use, ready to live that is not fact in true the backlog margin it's going straightforward to the bottom-line.

In terms of projects and the constructions as we have in sales, we can see in the backlog results. So in terms of explanation, the backlog can showed to us, two kind of different things. So we are increasing the volume of backlog with a very good phase of sales for the next four, five or six quarters. And the margin remains the same, something close to 50% pretty much to support the gross margin of the company.

Let's talk about cash on slide page number 12. In terms of cash, sales for the fourth quarter of 2013, you can see on the chart, in the middle of the slide, we have been the same pretty much flat net debt position something close to R$8 to R$9 million. And these positions we'll turn in a net cash position again as you saw in the past for the company, by the end of the fourth quarter of 2014 or the first quarter of 2015 regarding the delivery of the EZ Tower's Tower A to Sao Carlos.

And the way to Sao Carlos paid back this tower, EZTEC is about making an assumption of this entire debt of the EZ Towers project. So this amount of R$295 million of EZ Towers that will be supported by Sao Carlos company by the end of fourth quarter this year or first quarter, the next year. And that's why we have these short-term debt of 349. So we do -- we did some change in the line from the long term to the short-term it is simply because we are about to deliver these tower to Sao Carlos. So we think that it's much more transparent into our -- for the shareholders, to understand better, what is coming in terms of cash position and booking this debt in the short term to be consider at that, to be assuming to by Sao Carlos.

So on page number 13, you can have seen debt net value statement. As always, you can see the position of net asset value of the company about R$4.3 billion. So on the stock price, and stock for share, price for share something close to R$29.43 per share of adjusted net asset value, adjusted net asset value. It's important to understand when you compare this price, this adjusted net asset value per share, with the current price of the share we have been trading -- traded of about discount of 67% which is gross to what happened in 2009, 2008 for this company.

And being a company, delivering every year something between 20 to 25% of return on equity, its seems like unfair for this company being traded for this price.

It's important to look at these net asset value statement, to understand that all the Land Bank inventory we have R$674 million can represent a potential sales value for new launches of up about R$5.4 billion in a gross margin, average gross margin of 40% to 50% as you saw, as you have been seen all of these years, something between 40% to 50%.

So in that sense, it's important to understand, that we can add something close to R$2 to R$2.5 billion in gross profit to add in this net asset value for the next maybe four to five years which can represent something close to R$15 per share more that have today so for a company being traded, almost 65 -- six times, the net profit of this year it seems to me quiet (inaudible) and for spent a little bit more about it, I would like to go through the slide number 14, the last one for this residential.

Look at this slide, we call this slide asset management, resource management with productivity and efficiency. Look carefully this slide. Let's talk about gross margin, gross margin for EZTEC on the top last it's about 53%, nine months 2014 and 52% 2013. So compared with -- all the companies in the sector, public traded companies, real estate public traded companies, you can see on average 24% to 25% gross margin.

So we are hoping about twice as much the gross margin of the sector.

On the top right, you can see, the return on equity of the company 22% this year 35% last year, 22% last year it's about four times the return of the average of the -- among all the companies, public traded companies in the real estate sector and compared with the base (inaudible) Brazil, 11.25%, it's almost twice as much debt into the (inaudible) and including that the last one, the last you the last chart, you can see doing that with a net debt position of only 4% of the shareholders equity, compared to 79% the average of the sector.

So all the land that we have been buying it, all the cost we have been seen constructed by our own team, 90% constructed by our own team, all the efficiency would have been releasing with our administration.

Regarding 53% of gross margin, regarding twice as much the sector, in fact in capital to that almost four times, they are the company's in the sector and doing that, we doubt with same risk of the sector, all using 4% net debt to equity, compared to 74% of the other players, keeping the sector so looked more riskier than its debt, specifically in this moment with last piece of sales, incremental base interest rate cost is much more expensive than that -- of them, so the only words we can say to you is that we remain, we are keeping confidence in the Brazil economy. We truly believe in the dynamic of the Sao Paulo Metropolitan region markets and we are supported by these new middle-income class, because here in Sao Paulo and Metropolitan region with 22 million people living here and only producing year-by-year 35 to 40%, 35 to 40,000 newly say less than 1% of the net warning rates.

We are in the best place ever to get all the advantage, to get all the efficiency and productivity.

To keep this company releasing these standards of results without pulling the company in necessary risks, so we are truly confident in Brazil now for keeping invest in our capital in new projects, in new piece of plan, in newly state acquisition for our projects in the next quarters. So, thank you so much for your audience and we are completely open for your questions. Thank you so much.

Questions And Answers

Operator

Thank you. Ladies and gentlemen we will now initiate the question-and-answer section. (Operator Instructions) Having no questions. This concludes the question-and-answer session. At this time, I would like to turn the floor back to Mr. Emilio Fugazza for any closing remarks.

A - Emilio Fugazza {BIO 16474296 <GO>}

Thank you all for your participation today. And let me remind you that apart from myself, Mr. Pedro Henrique Nocetti, Mr. Erik Kragegaard and then we completely open to answer any part of your questions in our office. Thank you so much.

A - Pedro Henrique Nocetti {BIO 20904123 <GO>}

Thank you so much. Have a good day.

Operator

Thank you this concludes today's presentation. You may disconnect your line at this time.