

Q1 2019 Earnings Call

Company Participants

- Antonio Emilio Clemente Fugazza, Chief Financial Officer and Investor Relations Officer
- Hugo Soares, Investor Relations Coordinator

Presentation

Operator

Good afternoon, ladies and gentlemen. And at this time, we would like to welcome everyone to EZTEC's First Quarter 2019 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's Investor Relations website at www.eztec.com.br/ir by clicking on the banner Webcast. The following presentation is also available for download on the Company's webcast platform. The following information is stated in Brazilian Real and in BR GAAP and IFRS applicable to real estate developers in Brazil, except where stated otherwise.

Before proceeding, let me mention that any forward-looking statements made in today's conference call regarding the business outlook, forecasts and financial and operating targets is based on the beliefs and assumptions of EZTEC's management and 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 would 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 would like to turn the conference call over to Mr. Hugo Soares, IR coordinator, who will begin the presentation. Mr. Hugo, you may begin the conference.

Hugo Soares {BIO 19772261 <GO>}

Good morning one and all this is Hugo Soares, Investor Relations Coordinator here at EZTEC's, and with me we have Emilio Clemente Fugazza, our Chief Financial Officer and Investor Relations Officer. So that we can discuss our operational and financial highlights for the first quarter of 2019. From the operational side at first, the first quarter 2019 was marked by very relevant new records.

It was a quarter in which EZTEC's sold a record amount of units in the past five years. We have 810 units commercialized. The quarter was also marked by all-time record by (inaudible) vendors, EZTEC's inhouse sales team, which was the protagonist for the sales of the quarter, both in terms of launches and in terms of inventory sales. (Inaudible) vendors managed the breakthrough the mark of BRL253 [ph] million out of the BRL322 million sold in the quarter.

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Now I'd like to move directly into Slide number 4, where I'll discuss EZTEC's landbank. EZTEC's landbank as of the first quarter 2019 has enough prowess to be able to deal with the beginning of a new operational cycle with very much comfort. When we point to the BRL6.1 billion in PSV accumulated in our landbank, we are dealing basically with 25 plots, they're very much well aligned. And on top of those 25 plots, we can mention the fact that we have 26 additional plots that did not attribute to any PSV at the moment, as they are still in the process of development, but will surely grant an adequate return for the Company over a longer period of time.

Among the projects that are already getting developed, we have the broad availability of something along the lines of BRL4.3 billion in plots located specifically in the South Zone of Sao Paulo. These projects from the South Zone of San Paulo will be the ones that will basically serve as the foundation for the pipeline that we have delineated for the next few quarters, and they have the focus to be -- and they are very much focused in noble neighborhoods within the South Zone of Sao Paulo. These plots already conceived within the new master plan of the City of Sao Paulo and they have the perspective to have quick returns.

Now regarding the operational performance of the quarter, if you could, please move to Slide number 5. So EZTEC has been able to reach success basically in every aspect of its operational front. We have had very consistent inventory sales, diminishing inventory cancellation levels as well as a very much man-made [ph] interaction as far launch and sales goes. The result of that is that by the first quarter of 2019, we have managed to break through the mark of BRL300 million in net sales for the quarter, which is the highest that we managed to achieve in the past five years.

This performance is the fruit of a very proactive management, very careful management that we have met -- that we have done over the course of the crisis and that has left us very well-positioned to deal with the beginning of a new cycle. From the site of launches, the Company has been able to consolidate the operational escalation that is rather assertive. It is suffice to say that EZTEC has launched more units in the past two quarters than it has done in the 17 prior quarters put together.

In 2019 in itself, we proposed to launch something along the lines of BRL1.5 billion as indicated by our guidance, which basically will double the volume that we launched in 2018. And we insist and accelerate launches exactly, because we have been able to consistently achieve a consistent and satisfactory sales speed for each launch sold. When we look at seven projects that we launched over the course of the past quarter [ph] of the past semester, we can point out the fact that four of those have already managed to surpass the 50% mark for units sold. This is the result of a very strong inhouse sales team effort and through various assertive projects at very competitive prices, as well as of an

increasing and improving demand and you have your presence in the Minha Casa Minha Vida Segment.

On the side of ready inventory sales, the focus of EZTEC's operations takes place basically in the second -- the sales central forces in the cities of Osasco and Guarulhos in the Metropolitan Region of Sao Paulo. If you combine those two cities, the net sales performance was for the first quarter 2019 was of 167 units, which is higher than the performance that we managed to achieve for those two cities in the past 15 quarters.

The fact that we are being able to channel that inventory is all the more relevant, if you take in consideration that usually you associate the first quarter of every year as in lower to a lower sales performance due to regular seasonality or -- and even -- and the performance is even more salient, when you take in consideration, you factor in the fact that we basically are dividing our attention among the process of channeling in the inventory and a record-breaking acceleration in new launches, which is basically the highest acceleration that we performed ever since the Company's IPO in 2007. The capacity to conciliate the sales speed -- the inventory sales speed and the launch of sales speed is an important attribute, an important asset for the Company going forward into the cycle.

Now, I ask you to move to Slide number 6 and number 7, where I'll discuss the project that have been launched as well as the projects that we have approved for further launches. We have, in the first quarter 2019, launched three new projects and they were the following, they were the Le Jardin Ibirapuera project, which accumulated a PSV of BRL72 million and it is very nicely located a few blocks away from EZTEC's administrative headquarters.

We have also launched Vertiz Club Home Vila Mascote project with a PSV of BRL99 millions, which has already managed to strike a 75% mark for its units sold, given the fact that it was launched in January. We have also launched the Fit Casa Rio Bonito project with a PSV of BRL142 million, at this point 66% sold, and it is the second project within the Fit Casa line of segment that goes into the Minha Casa Minha Vida program. Alongside those three launches, we have also carried it out an additional stake acquisition of 30% in participation for the Jardins do Brasil project. This acquisition basically represents again of inventory as well as a gain over the portfolio of receivables at the amount of BRL82 million. On top of that, the 30% acquisition also contemplates an additional share over the six phase of the project that is still to be launched, which basically adds another BRL102 million in the Company's Landbank.

With that being said, it is very useful for EZTEC to already have a pipeline of projects that is already approved this early on the cycle. Basically, we have a pipeline of BRL1.3 billion of projects that are already approved by the City Hall Municipality. In these cases, the decision of the timing, of when to launch a new project is subject upon the Company's commercial strategy exclusively. So it doesn't depend on any bureaucracy that they place, we basically choose when to launch each project at the time where we perceive that will have the best sales performance. That grants the Company very much flexibility to align the itinerary for its launches in a very organized and effective fashion, focusing always at the sales speed at the time of launch.

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Now, I ask you to move to Slide number 8 and Slide number 9, where I'll discussed the future launches. So in this segment, we show a series of projects that has already been approved and that we have the capacity to launch in the next months, and as I have already mentioned, we have the six phase of Osasco, Jardins do Brasil, which basically concludes the Jardins do Brasil mega compounds. Apart from that, the remaining projects, the remaining plots that we have were all of them acquired from 2017 on, in other words they are very recent acquisitions. At the moment when those acquisitions took place, EZTEC had a greater visibility over the type of projects that will be suited for this new operational cycle. So these projects are the type of projects that really give enthusiasm to new clients, they're very adequate products for this current market and they're very competitively priced and they're very much desired by our clients.

We believe that this is a lot of launches that is very much differentiated, that promises a good sale speed and a promising prospects for profitability. But it's worth highlighting the two specific projects, the Patrio Ibirapuera project and the Parque da Cidade project, which put together basically compose as much as half of the guidance foreseen for the year 2019. These are very iconic projects that will account on a unprecedented mobilization of commercial efforts, trying to mobilize specially the attention of real estate investors. And so these are projects that -- in which we'll act with various assertive prices, their projects in the high standard and in very desired locations and when we talk about real estate development and if you think of the five main point state, you have to keep in mind, at least two of them should be location and the location for this project -- these two projects is special. One of them is in (inaudible) where we have the central commercial projects of the city, and among those very many commercial projects we'll have a spectacular residential project that is 150 meters tall, will be very much differentiated and we expect a very great success.

We also have Patrio Ibirapuera with 95 meters of height, which is at the most notable piece of the neighborhood of Moema, their apartments has the largest 280 meter square and they're located at the best of Moema at the (inaudible) section of Moema. So they're very valued projects where we expect to get a good results.

Now I'd like to pass the word to Emilio Fugazza, so he can discuss about the quarter's financial results.

Antonio Emilio Clemente Fugazza {BIO 16474296 <GO>}

Thanks very much, Hugo. It's a huge pleasure to take place earnings results conference call for the first quarter 2019. Starting with the financial performance on the Slide number 10. Let's talk about net revenues. Net revenues came 62% higher than the first quarter 2018, BRL146 million, this quarter and compared to almost the same with the fourth quarter 2018, mostly because we are recognizing revenues coming from some new projects launched in the quarter and in the first quarter 2018, like -- such as the Pinheiros.

The Pinheiros is a project in the neighborhood of Pinheiros East Zone of -- West Zone of Sao Paulo, Vertiz Vila Mascote in the South Zone of Sao Paulo, middle income segment, and also with Sky Chacara Santo Antonio in the South Zone of Sao Paulo, but in this case with no such expressive amount of sales we have done so far. It's important to mention

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that another part of the revenues are coming from performing the units sold and performing the units especially from the project Cidade Maia was a very good surprise in terms of the volume of sales this -- specifically this quarter. And this amount of sales took place in a huge impact in terms of gross profit and gross margins. Cidade Maia was a project of 41% of gross margin in the first quarter 2019. In terms of gross profit and gross margin, gross profit came at 69% higher than the first quarter 2018 and the margin, the gross margin was 37%.

Let me remind you that when you think about the movements to have the gross margin at a standard of 37%, one important thing is, in Brazil, given that our accountancy we have the present value adjustment to do, so without the present value adjustment we could get something -- a little bit higher, like 3 to 4 percentage points higher than we are releasing now. So, it is highly expected that in the next eight quarters, two years, maybe we are giving back the volume of revenues that we took out in the first quarter of 2019. So there is going to be a part of this gross margin coming back to our earnings results.

So in terms of G&A expenses and selling expenses, we have mix of things. In terms of G&A, you can see we have been working on keeping the volume of G&A expenses at the same level in the last three years to four years. If you compare to the first quarter of 2018, even though we have a slight decrement of BRL2 million, but I would expect something higher in the next quarters. Is it simply because in terms of salaries payrolls, there will be some increment given that at the moment of engineering area is (inaudible). So in the last, let's say, two years, one year and a half to two years, the volume of sites under construction decreased a lot.

And now with the new launches, the new releases we are going to see sizes in the constructions coming up again. So, it is expected to have from seven to nine sites under construction right now, from nine to something around 15 to 17 by the end of the next year. So we're going to see a little bit of increment in payrolls, given the engineering team.

In terms of selling expenses, selling expenses is a little bit more complicated. First of all, it's important to understand that's the volume of expenses from units we are carrying on for now a reinventory, we have something around BRL4.9 million of cost. So -- well each into this cost, you can see it maintenance costs and property taxes, compare it to BRL6.8 million in the first quarter 2018. So, with the units sold in the last four quarters, we can see a decrement -- a huge decrement in the volume of expenses used by that.

But in terms of advertisement, sales stand we saw BRL16.9 million, BRL16.9 million means that we are investing on a lot of projects that we are -- we're going to launch in the next couple of quarters, such as the Parque da Cidade itself as Hugo has mentioned before, only in part of the Cidade, we spent something around the BRL2.6 million in the sales of stands and is not -- and there is much more to come. But apart from Parque da Cidade, Patrio Ibirapuera and all the projects we have spent a lot of money and the project is going to be launched -- are going to be launching in the next six months.

So for me, in one of my personal opinion we going to see (Technical Difficulty)

Operator

This is the operator speaking, it seems like the main line has cut out. Please stay on the line, while I attempt to reconnect. Pardon me, this is the conference operator again. We will connect the main speaker line in just a minute. Please continue to hold and we appreciate your patience. Pardon me, this is the conference operator again, I've just reconnected to main speaker line. Speakers, you may continue.

Antonio Emilio Clemente Fugazza {BIO 16474296 <GO>}

So coming back to slide on Page number 10, selling expenses is last chart on the bottom right of this slide. Let me talk about the BRL21.8 million. BRL21.8 million means that we spent BRL4.9 million in cost to carry the inventory ready to leave. So the cost includes, maintenance cost and also the property taxes. So you can, compare to BRL6.8 million coming from the first quarter 2018. So a drop of BRL2 million in cost to carry inventory ready to leave. That means that our job to sell the units from Cidade Maia from Jardins do Brasil. So units is ready -- are taking place in a very good expenses saving costs in the last quarter and in the first quarter 2019.

On the other hand the BRL16.9 million of selling expenses coming from sales stand and advertisement is getting higher and higher specifically because the volume of launches we have forecast for 2019 is about -- is up to BRL1.5 billion. So, which means that we have some sites under construction, some sales standard under construction such as Parque da Cidade, Patrio Ibirapuera and others that are consuming cash upfront, only Parque da Cidade in the first quarter took something around BRL2.6 million and sales stand in terms cash spend in order to get ready for up for the launch could be by the beginning August 2019.

So moving onto a Slide number 11. Let's keep talking about financial performance and this started with financial results on the chart on the top left, coming at BRL9 million -- only BRL9 million in the first quarter 2019. The main explanation about BRL9 million is because the majority of our financial result is coming from our book for the receivables.

So receivables we are providing mortgages to our clients. Providing mortgages to our clients, we charge something around IGP plus 10%, but this quarter, the first quarter 2019, IGP was a deflation, so minus 1.5%. So that's why the financial result is not the same off the third quarter or the fourth quarter 2018. So, for the second quarter -- to the second quarter and to the third quarter 2019, our forecast is something very close to what happened in the fourth quarter 2018, something around BRL30 million. So that's why, came in the huge drop compared to the fourth quarter 2018,

And we are going to talk a little bit more about financial result in the slide on Page number 12. For now let's talk about equity income on top right. The chart on the top right BRL8 million means that we are recognizing right now the project Fit Casa Bras, the very first project coming from Minha Casa Minha Vida, Minha Casa Minha Vida side we have 70% stake on this project and we start the recognition of this project by equity income in the first quarter 2019. For the next couple of quarters, my personal forecast is you see results coming from equity income side higher than in the past quarters simply because we are

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launching projects in partnerships much more than in the past. Net income; net income in the bottom left from this slide, only BRL17 million, I'm sorry about that, but BRL17 million is because it's a miss of BRL20 million from the financial results. We are going to see coming in higher in the next few quarters, but the good news is, first quarter 2019 came in 200% higher than the first quarter 2018, which is good enough specifically because a half of the net income is coming from the operational side, not only from the financial side. Now we are getting back to the financial -- the operational side.

And finally, in this slide is results to be recognized over the backlog, result in backlog margin came in 39%, a BRL144 million. So compare it to the first quarter 2018, was almost 100% more more results to be recognized with 3 percentage points more in terms of backlog margin. So which means that this is a kind of gross margin you could expect in the next few quarters. Let me remind you that again in Brazilian accounts, we have the present value adjustment taking a little bit, the margins from the very first moment and giving back the margin at the last moments of the projects, the moment -- very close to the moment that we deliver the keys.

Let's go to the slide on Page number 12, portfolio of receivables -- performed receivables. Let me show you that in the first chart on the top, we are keeping -- we are holding the same level of portfolio receivables in a BRL513 million. So BRL513 million, we could hold only because the acquisition, the stake of 30% in project like Hugo said the mega compound Jardins do Brasil of BRL15 million acquisition in terms of receivables -- portfolio receivables. But the true situation is, as the interest rates coming from the commercial banks are declining a little bit and now clients can get mortgages from the commercial banks at a rate of 8.2%, 8.3%, 8.5% yearly compared to EZTEC, which is charging 10% plus IGPM or IGP-DI, means that one part of our receivables are being transferred to the commercial banks. Nowadays those BRL513 million are representing almost 2,000 units under our management in EZTEC.

Let's move to Slide number 13. Slide number 13 is saying something about potential cash generation. Let's start talking about the cash burn, cash burn in first quarter -- cash burn of the first quarter 2019 was BRL51.1 million, which means that we have cash of BRL427 million and the debt, the debt of the Company only project debt of BRL76 million. So, let me remind you that the last public meeting, the general public meeting of shareholders took place on April 26th, was approved a payment of dividends of BRL23 million to be paid up to November 2019.

So, all in all, the net cash position is about it BRL352 million and performed receivables of BRL526 million. Taking out all the construction obligation, the remaining balance of this Company, allowing the Company to make some reinvestments, some acquisitions is about BRL845 million, including inventory at market value we could add BRL1.3 billion. All in all, the bottom line of cash flow generation in the next couple of years is about BRL2.2 billion, which tell you a story about EZTEC, which is safe enough to make some reinvestments. We doubt putting the Company in risk and that's the case for the moment as our Vice President told in our meeting before. So the volume of new piece of land, the volume of acquisitions, we are going to do in the next couple of quarters about to increase specifically because we have been watching some very good opportunities to

invest the money of EZTEC in order to take a very good return on equity in the next couple of quarters.

Moving onto slide on Page number 14, potential value for EZTEC is a summary -- is a conclusion about the balance -- about EZTEC's balance sheet, which means BRL3 billion -- BRL2.9 billion of assets and BRL338 million of liabilities. All in all, BRL2.6 billion of book value, book value, we're adding BRL100 million of backlog, BRL600 million on the gross margin -- gross profit from their potential inventory and BRL2.4 billion in gross profit from the landbank we could achieve BRL5.8 billion, which means BRL28 -- BRL29 per share in terms of book value. Let me remind you that all those numbers are taking in mind that the Company is not buying land -- buying land again, so only launching, only developing the projects we have bought so far.

So moving onto slide, on Page number 15, on a very quick explanation about what took place in the public meeting of shareholders, April 26th, 2019. The shareholders equity of this Company is about -- was BRL2.6 billion by the end of 2018. And divided into BRL1.3 billion of capital and BRL1.3 billion earnings reserve. So the Company took the decision of capitalized about BRL553 million, so taking all the capital of this Company of -- leading the total amount of capital for this Company, about BRL1.9 billion and letting BRL700 million in earnings reserve. So when we have done this capitalization, the main purpose was to issue about BRL35 million in new shares and those new shares with a cost per each share of BRL15.82, which was a ratio of 21.2 new shares to 100 shares kept by our shareholders. So the main goal to achieve that is in Brazil with specifically.

So, these for ordinary people, this can make, I'd say, at an average price to share and hold by our shareholders is specifically the ordinary people doing a very good planning of that savings for those who are with intention to sell those old shares and on the other hand, it is only to -- I'd say to send the message that for this Company to operate in the guidance of BRL1.5 billion or more in the next coming years. The minimum capital required to operate this Company is something close to BRL2 billion. BRL2 billion is easy to understand, nowadays is about BRL800 million in terms of a land by cost, something around BRL400 million in capital and in cash and the remaining in terms of inventory ready to leave our inventory under construction. So it's only a kind of management to provide the best planning for the Company in the next coming years.

Thank you very much. Coming back the word to Mr. Hugo. Please Hugo.

Hugo Soares {BIO 19772261 <GO>}

Thank you Emilio. Now, if I could address the development of the first quarter of 2019 in broader strokes, I would like to reaffirm our confidence in this new operational cycle. It is a cycle that we started with a lot of breadth and with the capacity to deliver growth in terms of launches, capacity to deliver rapid sales and differentiated margins. This operational uptake reached the fruits of what we have planted over the course of this strenuous years of the crisis and is important to remind that we have devised our business model to be able to striving a very proactive and intelligent fashion at the worst times of the sector, such that now we have a liquidity cushion that grants us the comfort to extract value from each opportunity that may emerge out of this transition.

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That way, we have put up a portfolio of ready receivables that is basically taking much of the space that would regularly be attributed to the commercial banks and we have over the course of this crisis -- we have managed to preserve the value of our inventory at that moment, at which it was the most threatened and now we have (inaudible) generate the cash from at a very healthy margins. We have also made several acquisitions in new plots over the course of the past years, that at the time when people were the most willing to sell. And now, we have the ammunition to make -- to reap the most benefits out of the moment of operational escalation. We have entered the year 2019 in a way that is both strong, organized and that opens the opportunities for a series of new cash -- new value accreting opportunities, from the Minha Casa Minha Vida program to the Parque da Cidade value project or even as far as the corporate project (inaudible) Towers. We have constructed the circumstances for a prosperous operational cycle that is compatible with the Company's history.

At this point in time, it's worth highlighting that our team of executive officers are working at their best performance. They are very much able and cautious that make judicious decisions that lead to the lucrative and profitable opportunities. They know what risks to take and how to perform it and not to mention the best sales in the City of Sao Paulo. In other words, the results will come, they will come gradually, but they will come strongly. So I'd like to transmit and reaffirm the confidence that we have in the upcoming good results in this new cycle.

Thank you very much.

Questions And Answers

Operator

(Operator Instructions) Seeing that there are no further questions, this ends -- this concludes the question and answer session. At this time, I'd like to turn the floor back over to Mr. Emilio Fugazza, the IRO and CFO for any closing remarks.

A - Antonio Emilio Clemente Fugazza {BIO 16474296 <GO>}

Thank you very much your audience today. We are completely available to answer any further questions apart from myself and Mr. Matheus Tubarao, and with Hugo Soares, we are -- it's going to be a huge pleasure to answer any further questions. Thank you very much for today and have a wonderful week.

Operator

Thank you. This concludes today's presentation. You may disconnect your lines at this time and have a nice day.

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