Q1 2016 Earnings Call

Company Participants

- Armando d'Almeida Neto, CFO, Vice CEO, EVP & IR Officer
- Franco Carrion, Manager-Investor Relations

MANAGEMENT DISCUSSION SECTION

Operator

Good afternoon. Welcome to everyone to Multiplan First Quarter 2016 Earnings Conference Call. Today with us, we have Mr. José Isaac Peres, CEO; Mr. Armando d'Almeida Neto, CFO and IRO; Mr. Marcello Barnes, CIO (sic) [CDO] (00:28); Mr. Hans Melchers, IR and Planning Manager; and Mr. Franco Carrion, IR Manager.

Today's live webcast and presentation may be accessed through Multiplan website at www.multplan.com.br/ir. We would like to inform you that this event is being recorded and all participants will be in a listen-only mode during the company's presentation. After Multiplan remarks, there will be a question-and-answer session. At that time, further instructions will be given.

Before proceeding, let me mention that forward-looking statements are based on the beliefs and assumptions of Multiplan management and on information currently available to the company. They involve risks and uncertainties because they relate to future events, and therefore, depend on circumstances that may or may not occur. Investors should understand that conditions related to the macroeconomic scenario, industry and other factors could also cause results to differ materially from those expressed in such forward-looking statements.

Now, I'll turn the conference over to Mr. Franco who will read the message in the name of Mr. Peres. Mr. Franco, you may begin the conference.

Franco Carrion {BIO 16449361 <GO>}

Good morning. As we disclose the results for the first quarter of 2016, I'd like to highlight some of the aspects that, in spite of the recessionary economic environment, encourage us to continue to move forward. Tenant sales recorded a compound annual growth rate of 10.1% in the last five years. This remind us that our activity should be constantly analyze with a focus on the medium-term and long-term.

Quick recall to what happened since the company's IPO in 2007, our gross revenue increased 280%, the EBITDA 307% and net income 1,570%. In spite the average tenant sales growth in the quarter of 3.1%, we call attention to some of our centers that had significant results. In São Paulo, MorumbiShopping grew by 8.3%, ParkShoppingSãoCaetano by 7.1%. In Rio, ParkShoppingCampoGrande increased by 13.2%, VillageMall 12.7% and New York City Center 10.8%. Parque Shopping Maceió in Alagoas continues to record a strong sales phase growing 15.2% in this first quarter. The occupancy rate remained at 97.9% and the rental revenue increased 6.7% while same-store rent grew 5.8%.

The quality of our assets continues to attract new tenants and we are taking advantage of the current scenario to improve the store mix. By the way, the country's prospect of recovery may lead us to new future expansions. As already mentioned, we have a clear focus on the long-term, and it's worth mentioning that, it takes from (03:48) buying a land to delivering a new mall around five years to six years.

When the economy goes through a major crisis, it highlights the company's solid financial stance. Multiplan holds a debt which corresponds to approximately 18% of its market cap and its net debt to EBITDA ratio showed a slight drop to 2.33 times. In Multiplan's 43 years, almost half a century, the company has been through equally difficult macroeconomic scenarios from where it has emerged stronger, more disciplined and focused on improving our operations.

In the stock market, we are happy with the significant evolution of our shares liquidity. In our early years, as a public company, it was trading at less than BRL 1 million per day and after our continuous improvement, it reached an average financial turnover of about BRL 40 million a day. As a result of our efforts in pursuing the highest standards of corporate governance and enhance interaction with the capital markets, we became part of the main stock indexes in Brazil.

Talking about growth, we continue to work on several projects, mainly the construction of ParkShoppingCanoas, which Multiplan's investments account for BRL 360 million. The construction works remain within schedule and the inauguration is planned for the second quarter of 2017. This is a greenfield which already has 72% of its area leased.

In addition to the ongoing structural works of this mall, the company made major enhancements in the area, including the extension and improvement of the Getúlio Vargas public park, which should be delivered in August this year right next to our future mall. I'd like to add that a crisis at least (05:43) create a destruction, new trades are developed, new tenants replaced old ones and intensive work is carried out, seeking to reduce cost and increase efficiency. Within this context, we expect to see another quality renewal. We have seen it countless times, the rise of new operations, innovative, more efficient, which anticipate customers yet to come with us (06:06).

Finally, I want to highlight that since our IPO, the company distributed to its shareholders around BRL 1 billion in dividends and interest on capital. As we mentioned in the previous conference call, the company has several projects underway, awaiting a more positive economic environment. Our expectation is that the economy will begin to react within a very short time, creating a favorable environment for new projects, which by then would be ready for the commercial launch.

We continue working hard to have the best malls projects and thus continue to deliver our contribution to society, the malls' customers, and investors. My sincere gratitude for the commitment of our whole team at Multiplan, and for the interest of investors, analysts and journalists, who hear us today.

Now, I'll turn the floor over to Armando, which will give you more details about our results. Thank you very much.

Armando d'Almeida Neto

Thank you, Franco. Thank you, Mr. Peres. Good morning, everyone. And thank you for being with us in the first quarter 2016 results conference call. This presentation is based on our management data. Please check our earnings release and financial statements for more details. I will comment on the main topics of the quarter but not necessarily in the same order of the presentation.

Let's start with the operations area. Moving in the opposite direction to the economy, our tenant figures increases 3.1% in the quarter. As a result of the tenant mix, the same-area sales grew 4.2% to a record spread over the same-store sales of 2.6%, benefited by 74 new contracts signed in the quarter, totaling 8,384 square meters or – of GLA, something like 90,245 square feet.

As shown in the last quarter, the company has increased the lease area participation with segments of Services, Miscellaneous and Food. Not a coincidence (08:12) we see these segments leading the quarter same-store sales growth, with increases of 7.3%, 4.3% and 3.9%, respectively. Even growing at a low – at a slower pace, this increase in sales resulted in sales of satellite stores of BRL 26,015 per square meter or $620 per square foot in the last 12 months.

It was almost BRL 200 improvement higher than the first quarter of last year and more than BRL 1,600 higher than the first quarter of 2014, a year that was of exceptional results for the company. The occupancy rate remained virtually unchanged to the fourth quarter of last year, 97.9% against 98%, while the occupancy cost increased 47 basis points, now at 13.9%. The increase in occupancy cost is caused by the higher rent increase when compared to sales and also by the effect of inflation in the common costs.

The rent delinquency and loss increased to, respectively, 4.5% and 1%. There are several reasons for the deterioration of those indicators that remained very well behaved. Some of the reasons are related to the macroeconomic scenario such as retail sales worsening, the high cost of capital and some retailers under financial stress. But we'll also remember specific issues such as the December double rent that was charged in the first quarter.

We are working together with our tenants to resolve these delays, but we have confidence that in some cases, recover the space, the store is the best solution making it possible to mix improvements or even allowing expansion. Remember, the theory of corrective destruction that Mr. Peres just mentioned. The net before IE (10:27) also considered the rent recovers during this quarter was up 3.6% well below the 4.5%

showing that we'll be able to recover more and more the delays showing that it was just delays.

If you look at the picture today, it will be closer to 3% showing a improvement through time. The rental revenue on our main revenue line increases 6.7%. We consider it an excellent result in this challenging environment we are going through, especially, when we take into account that the vacancy was higher when compared to the first quarter of last year, 97.9% versus 98.6% in the first quarter last year.

And particularly, we had in this quarter bigger discounts, rent discounts. All combined in this quarter, we could not pass the effect of (11:22) with the same store rent increasing 5% to 8%, but it is still again where it was. The parking revenue increased by 9.4% and services revenue increased 34.3%. The car flow, the people (11:38) flow remained virtually unchanged.

The shopping center expenses increased 39.9%, and this is in part due to the common charge provision and costs related to higher delinquency, the higher vacancy when compared against the first quarter of last year and also due to the functional costs of stores turnover.

On the other hand, the cost of towers for lease fell 39.8% as a result of a higher occupancy rate at Morumbi Corporate, which is 91.5% occupied. The G&A expenses increased 24.3%, but it's important to emphasize it was not due to higher cost overhead in the quarter, but to a provision reversal that occurred in the first quarter of last year, thus, reducing the G&A in the first quarter last year, the comparison base. If, for just illustration purpose, we exclude this one-off effect, the increase would have been of only 1.7%. That is well below the inflation recorded.

Now speaking about results, the NOI grew 4.6% even with a margin reduction of 226 points related to shopping center expenses. In the last 12 months, the NOI totaled BRL 944.9 million with a margin increase of 72 basis points at 88.8%. Consolidated EBITDA for the same trend growing 2.6% with a margin of 71.3%, lower by 188 basis points. The last 12 months EBITDA reached BRL 794.3 million with a margin of 72.2%, 273 basis points higher. Even with the higher financial expenses due to the base interest rate increased, with a reduction in real estate for sale achieved and higher expenses, the net income increased 0.7% in the quarter, totaling BRL 362.7 million in the last 12 months, 2.1% higher. FFO was unchanged at BRL 114.6 million, while the last 12 months was reduced by 1.6% to BRL 530.6 million for the same reason that I mentioned on the net income, basically, the higher financial cost in Brazil.

This strong cash generation allow us to have a comfortable capital structure as we will discuss shortly. And it's enough to amortize the 2016 and 2017 debt that is coming due. So we have a very tougher (14:42) balance sheet at this moment.

But before moving to the capital structure, just a quick highlight on the last 12 months margins that improved despite the challenges. Talking about capital structure now, we have no new relevant transaction this quarter. Net debt to EBITDA showed a slight decrease from 2.44 times to 2.33 times, far from the nearest quadrant, which is at 4 times net debt to EBITDA. The average tenure is a little bit over four years at 52 months, and the net debt represents just 11.8% of the properties' fair value. Mr. Peres mentioned about the comparison to the market value, but when you compare to the property value itself, it's even lower. The average cost of gross debt was 13.22%, 103 basis points below the Selic Rate, the base rate in Brazil.

Turning to development and again, as Mr. Peres just mentioned, we are developing ParkShopping Canoas that is on time and on budget with almost 72% of the GLA leased a year prior to the opening. We just opened the Barra Shopping Medical Center expansion now in April that will make the whole complex, not just Barra Shopping (16:08) even more complete, another greater options for consumers.

(16:19) expansions that we did last year. Let's talk about the performance of our stock. It showed a 10% increase in the average daily trading volume. And in four years, we more than doubled the number of shares traded in a daily basis. Even better, the stock appreciated in this quarter 41.3%, outperforming the Bovespa Index (16:44) by almost 25%. Despite this strong growth, the company's enterprise value continues trading at a discount of 30.4% to fair value of our investment properties.

I want to thank you all for your attention, and let's now move to the Q&A session. We have plenty of questions on the Portuguese session as well. If we have more questions here, we're going to just turn to the operator in a minute, but we will just share some of the questions from the Portuguese call.

Q&A

Operator

Thank you. The floor is now open for questions. I'll turn over to Mr. Armando d'Almeida Neto for final considerations. Mr. Armando, you may give your final considerations now.

A - Armando d'Almeida Neto

Thank you very much. But before just the final words, just to share, as I mentioned, a few of the questions we had in the Portuguese call, there are a few questions on delinquency. We're showing that, first of all, a clarification. Our delinquency that we published is the gross delinquency. We do not consider any recoveries from past quarters on that.

As I mentioned during the call, with the double rent charge that happened in the first quarter created a seasonal increase. Our delinquency is so low that percentage-wise created a significant growth. But when you look at it in terms of cash, in dollar terms or in reais terms currency, you're going to see the delinquency, and this was part of the – some analysts mentioned is very low.

Cost of funding is very expensive in Brazil, so we understand the reason why some of the delinquency happens in a model like this. But we are working with tenants. There are tenants that are going through this restructuring, so their indebtedness.

So, this we have to deal with the legislation and negotiate with the whole group. There are some models that we can basically get the space back, because we are very confident there are many tenants being very comfortable with the space we have, and we have many tenants leading to change or vary (19:48) locations or to increase their stores or open new stores with good locations. So on the short term, that might represent a little bit of costs, but on the long run, this is a tremendous opportunity of innovation, of improvement that we have for our properties.

Of course, the delinquency, this rent delinquency automatically triggers the common cost provisions. So the way we are comping (20:19) the company in a conservative way, when you have the tickets delays from tenants, so we just get the common cost and fully provision immediately, because we are not certain when and if it's going to be repaid. So this has a increasing cost that automatically goes to our shopping center expansions on the provision line.

Again, we are very comfortable with the value that we have in our space, (20:57) space back, it's a opportunity for long-term growth. We will get questions related to change in mix, especially because of the record spread between same-area sales and same-store sales. And we again showed the confidence that we have in attracting best-in-class tenants. We have the main new operations starting in Brazil. These are a moment of distress only in the moment of new opportunities, new products, new line of business that's been growing on in just a starting (21:35).

Yesterday, we have a very famous retailer in Brazil that opened their first store in our MorumbiShopping for the very first time. They were selling on the Internet, they were selling on door-to-door and they opened their first operation in MorumbiShopping of many they have plan to open. There are few international tenants that came to Brazil recently and are selling well and looking for high-quality space. So these are (22:10) opportunity that we see.

And of course, as we could not finish the call without a question like this, how we're looking at the – of the – our expectations on the Brazilian economy, our expectations with the political (22:25) news, so we are confident that we've seen improvement on its way. We are prepared to it. We have many projects that are ready to be launch both expansions and greenfield waiting just a better moments and this is – we're seeing as an inflection point to start the improvement at the moment that we are ready to take advantage of new expansion plan when and if we feel confident enough to do it.

More than that, I want to thank you all for participating in the call. I want to thank you all for the trust and interest in our company and turn back to the operator. We'll remain available for any questions that you might have in our IR Department at any time. Thank you so much.

Operator

Thank you. This concludes today's Multiplan First Quarter 2016 Earnings Conference Call. You may disconnect your lines.