Q4 2018 Earnings Call

Company Participants

- Ruy Kameyama, CEO

Other Participants

- Daer Labarta, VP
- Enrico Trotta, VP of LatAm Real Estate
- Jorel Guilloty, Equity Analyst
- Luis Guilherme Braga Stacchini, Research Analyst
- Luiz Mauricio Garcia, Research Analyst
- Marcelo Garaldi Motta, Research Analyst
- Nicole Inui, VP
- Unidentified Participant, Analyst

Presentation

Operator

Ladies and gentleman, thank you for standing by. And welcome, everyone, to BR Malls conference call to discuss results (for) Q4 2018. Today with us to present the results are Mr. Ruy Kameyama, Mr. Frederico Villa and Mr. Derek Tang. (Operator Instructions)

I'd like to say that forward-looking statements made during the conference call regarding the company's business outlook, operating and financial goals and forecast are based on beliefs and assumptions on the part of BR Malls management and also on information currently available.

Forward-looking statements are no guarantee of performance. They involve risks, uncertainties and assumptions as they refer to future events and, therefore, depend on circumstances that may or may not materialize.

I'd like to now turn the conference over to Mr. Kameyama. Please, Mr. Kameyama, you have the floor.

Ruy Kameyama {BIO 16672412 <GO>}

Good morning, everyone. Thank you for participating in our conference call to discuss results relative to Fourth Quarter. I'll like to talk -- to start by addressing the highlights of the Fourth Quarter. And then we'll go to the Q&A.

On Slide #2 we show that we had several challenges in 2018. Slight challenging for the retail area, the atypical events such as the truck drivers strike, the elections. But we the closed the year with high expectations in terms of important structural improvements. For BR Malls, the year was important in terms of evolutions. We took significant steps in strengthening our portfolio. We improved our operating indicators. And we also added liability management efforts to strengthen the company's capital structure. And we ended up showing advances in different financial metrics.

2018 was also an evolutionary year for our culture, which also led the company more client-oriented in the long run. Innovation has also been a very relevant topic for the company.

On Slide #3, we have a picture of the evolution of the company going back to 2017 in relation to the strengthening of our portfolio. In strategic terms, it decreased our exposure to noncore assets, smaller malls and smaller cities, where we do not have active management authority and increased our exposure in core access for assets. Acquiring larger malls in larger cities where we do have a more active management over those assets. We've sold stakes in 7 malls. And we acquired stakes in another 3 malls. And we opened the 11th greenfield of the company, EstaÃ§Ã£o CuiabÃ¡. So we closed the year with 86% of our NOI exposed to assets classified as Tier 1 or 2 as compared to 76% we had -- or that we have in the same categories in 2013.

We believe that the retrofit projects in our 10 malls will bring improvements in our performance for the coming years. 2018, we also spread up our NorteShopping activity. In 2019, we'll also advance our works Villa-Lobos, Tijuca, Plaza NiterÃ³i and same-store shopping over rent.

Now moving on to Slide #4, I will show a little bit about of our EstaÃ§Ã£o CuiabÃ¡ mall. The expectation is quite positive. We've had brief intakes since the start of the mall. And we see a trend of having important anchor stores, with food courts performing really well. And we have good and important openings restaurants into an outback in Coco Bambu. The outback opening was the second best opening in their track history. And for the same complex, it's the best in the state. So it was born as the strongest, more intense in the region, which shows that we're able to generate opportunities in areas where we have opportunities such as (inaudible), which has contributed to the company's long-term performance.

On Slide #5, we show why for the next years our expectations for operating results are even more favorable. On top of a macroeconomic recovery after the recession, we realized that for the coming years, very little growth suitable area will be opened in Brazil. And the same time, we realized an important rise in the land from tenants, either through expansion of the existing brands or by new brands. We also believe that in the demand/supply, we'll be more balanced through an increase of the occupancy rate and any recovery of the leasing spreads.

On Slide #6, we showed the recovery of our operating indicators. In the Fourth Quarter, we grew 7.7% in total sales, excluding the malls that we sold. And same-store sales, we grew by 3.7%, up 2.1% when compared to the Fourth Quarter of 2017. That growth is associated with a good pace of sales in the retail area and an improvement in our tenant mix. It's important to mention that all regions presented a positive growth in same-store sales with a highlight for the Mid-West region, which grew by 10.7%. This increase in sales in the past quarters has guaranteed higher percentage lease and an increase in inflation and a reduction in discounts, which is close to our historical average. With that, that indicates a healthy recovery having filed a growth of 4.9%, up 3.2% when compared to the previous year.

On Slide #7, we show how the execution of the strategy of replacing a relevant percentage of existing base of tenants with updated concepts of mix and better performance with mature company's collections allowed us to register the second lowest net delinquency of the company's history, 0.4%. The gross delinquency also showed improvement at 2.1% or 3.5% below Fourth Quarter of last year. Delinquency at lower levels has contributed to lower provisions. In this quarter, bad debt provisions stayed at BRL 14 million or 4% of net revenues year-to-date. The drop was 77.1%, moving from BRL 185 million to BRL 42 million. The execution of this strategy also allowed the company to obtain throughout the year, a recovery in terms of occupancy rates, which reached 96.7%.

On Slide #8, we present our NOI for the quarter, which moved from minus 0.8%, excluding the sold malls. And totaled BRL 317 million. The profit of replacement, defaulting tenants, exerted some pressure on leasing amounts and also NOI but with a healthy portfolio with a better mix, which seems to be going on. This is a proxy for cash generation, which saw an expressive growth in the year and the quarter.

On the right-hand side, we see the evolution of NOI extra sales for the past few years. With the lower delinquency and a higher level contrast level from the tenants, we are confident that we'll follow now a recovery path.

On Slide #9, we have adjusted EBITDA with solid growth of 6% disproving the malls that we sold, reaching the level of BRL 235 million in the quarter. The main contribution for the improvement was the reduction of bad debt provisions as mentioned. The EBITDA margin adjusted totaled 66.8%, up 4.1% when compared to the previous year.

In this quarter, we had an increase in SG&A, which were impacted by nonrecurrent events coming from the Fourth Quarter of the previous year and this year, 2017 and '18, having to do with reversals and structural reinforcement.

On Slide #10, we see the company's capital structure. We closed the Fourth Quarter with a cash position of BRL 935 million and a gross debt of BRL 2.8 billion, a drop of 16.2% when compared to the previous year. Though, the net debt at the end of the quarter was BRL 1.9 billion, which maintains a net debt-EBITDA ratio at 2x, the lowest in the industry. The average cost for the debt dropped from 9.2% in the Fourth Quarter 2017 to 8.8% due to our liability management actions, which reduced the cost of our debt in TR by 0.9percentage points.

Looking ahead, liability management actions along with a change in our debt profile in a more efficient portfolio management increased our capacity impact in the long run, which was proved by the receival of AAA rating from Fitch, the first time in the company history.

Looking forward with a defined electoral scenario, we have more opportunities going forward. The issuances of new debentures at 117% (sic) (107%) of CDI in March this year and also the refinancing of one of our TR-linked debt, which reached the lowest levels in two years. Our TR debt today accounts 59% of our debt. The debt profile is changing when going forward.

Now moving onto Slide #11. We see a growth of 25% in our AFFO in the quarter and 36% in the year-to-date numbers, reaching the level of BRL 168 million in the quarter and BRL 581 million in the year. It's the largest AFFO in the company's history, even after the sales of some assets. The combination of a better bad debt provision and our ability management efforts allows for that growth. About this metric, the AFFO, the main metric for value creation for shareholders, we grew 33% in the quarter, 31% in the year, reaching a total amount of BRL 0.68 per share year-to-date.

Moving on to Slide #12. We present the evolution of our culture. It has (inaudible) created our sense of purpose, which is to transform shopping malls in destinations of happiness and opportunities. And we updated our values so that we can reinforce long-term end clients. Those changes were planned, well thought out and were key for the long-run performance of the company. We have received promising feedback from our clients, tenants, consumers and associates or employees. In the change, we have obtained the highest satisfaction level measured by MPS and the best semester and worker turnover. It's important to highlight the effort and time dedicated to digital transformation. In 2018, we brought in new member to our board with a strong background in innovation and technology. And this topic has gained strategic importance. Our final objective's to develop new solutions to improve consumers and tenants' journey. And partnership with Cubo and the Delivery Center have been growing fast towards that goal.

On Slide #13, we have our focus for the coming years. We continue to work in strengthening our portfolio and to make them even more desirable by tenants and consumers. We'll keep the robustness of our balance sheet. And at the same time, we'll maintain our flexibility to return more capital to our shareholders. We continue to advance in transforming digitally. And we'll reinforce the long-term culture and excellence in people.

We now close our presentation. And we remain available for questions or comments you may have. Thank you.

Questions And Answers

Operator

(Operator Instructions) Our first question comes from Enrico Trotta from ItaÃº.

Q - Enrico Trotta {BIO 16742911 <GO>}

I have 2 questions actually. The first one, if we could go back to the main assets, the top 25, if you will. When you look at the assets in Rio, Plaza NiterÃ³i, NorteShopping, we see relevant drops in NOI in the Fourth Quarter when compared to the Fourth Quarter of the previous year. I'd like to have some more color on the reasons why that happened?

We see, of course, that the economic scenario in Rio is not very helpful. But what can we expect going forward? Mix replacements, what can we expect in terms of NOI for 2019? Mixing issues and other facts that impact those assets. And that impacts the company's top line.

Number two, if you could talk about G&A some more. We saw a growth year-on-year in G&A. You mentioned that you have brought in new people. So I'd like to understand, in terms of G&A, what areas were actually reinforced? How much of that G&A will be recurring for 2019? Are you expecting to bring in more people this year? And for BRL, if you could be -- BLR, if you could give us some more color for that metric for 2019?

A - Ruy Kameyama {BIO 16672412 <GO>}

All right, Enrico. Thank you for the questions. About your first point, well, the performance of our main asset, Plaza NiterÃ³i, specifically, we had an important change in the mix. We had a portfolio of delinquency, which was quite high. But for the past two years, we have replaced several of those delinquent tenants. We had significant change on that front, new stores, new tenant. And at the same time, that brought in a short-term pressure on our rent from leases. The level of new leases gained at lower levels because of the economic scenarios, difficult to bring in new tenants in this uncertain scenario that we have.

So that, as I said, pressure on our leasing rates. So that's why this line grew less in the others. But at the day, this was a deliberate decision that we took because we wanted to grow the bottom line of those assets, not only the NOI but the cash conversion, cash generation as well. So we'll be starting to remove delinquent tenants and bring in better-performing tenants, even if that would mean receive lower lease rates. So when we compare Tijuca with (TU) NOI, we see that retraction. But when we compare NOI with the bad debt provision for those 3 assets, the 3 grew in double digits, NOI plus bad debt provisions, which proves us that this was the right decision to take the replacement of those tenants.

When we look at those metrics, we have better indicators in terms of cash plus NOI. Looking forward, we expect to have some stabilization. We think that improvements will come gradually. That's the scenario we hope to see in the long or in the short term.

About G&A, we have some plans in the quarter, as you mentioned, we brought in new people, more expensive wages when compared to the previous years that amounted to BRL 4 million in terms of difference. BRL 3 million of those BRL 4 million are relative to the economization of some businesses and back-office expenses. But we have lost that number by revenues. So we brought in revenues of at BRL 3 million. Then started generating expenses of newer personnel at BRL 3 million. But that's a more transparent way of showing that number.

As for BLR, in the Fourth Quarter of 2017, the Fourth Quarter of the previous year, we have a reversal and an adjustment because we reimbursed part of the BLR. But that didn't happen in 2018. So on a comparative basis, we saw an increase, which was more significant.

In terms of structure, we make an adjustment throughout the past quarters to increase our team, especially in what's related to retrofitting activities. That expansion has been made. So looking forward, we do not expect other increases in terms of expansion of its structures. Still, under G&A, we had a nonrecurrent event. Our noncontingent expenses in the Fourth Quarter that amounted to about BRL 7 million. And at the same time in the Fourth Quarter for 2017, we had a contingency reversal of also BRL 7 million of nonrelated topics of different nature. But in practice, in the comparative basis, we see the same increase. So as far as an increase in the recurrent expenses, we had some nonrecurring expenses. In the long run, looking forward, we do not expect to have those events as recurring.

So now we're working around the bases, which better reflects what we can expect. So the First Quarter of 2018, it's a better base for comparison because we had none of those nonrecurring events. That would be our ongoing structure going forward.

Operator

Next question from Garaldi Motta from JPMorgan.

Q - Marcelo Garaldi Motta {BIO 16438725 <GO>}

Two questions. First one, the optimization of investment portfolio. For the past call, you mentioned that if you could not quantify your portfolio going forward. Any other of those noncore assets would be up for sale or not? And the second question, on the operational front, we've seen considerable improvement, leasing spread, could you also give us some more color on the current situation vis-Ã -vis past periods in the leasing spread issue?

A - Ruy Kameyama {BIO 16672412 <GO>}

Garaldi, thank you for your questions. About the first question, about the portfolio in the long run, we are now shaping our portfolio, scoping, if you will, our portfolio, meaning that we have been touching now -- reallocating capital in different parts of the portfolio. We have been decreasing exposure to certain assets where we do not have a more active management activity. They are relatively small. So we don't think it makes sense to allocate capital or energy on those assets. And we've been at the hand of other investors. Others will see more value than we do.

So we're going to an active process now in terms of recycling that portfolio. At the same time, we also say that this maintains our scale, our liquidity, our robustness because those assets account for less than 10%. So a reference in terms of volume, it'd be there, quantification, less than 10% of our NOI. So not that much of a burden in the company's NOI. But they will free up energy, free up focus. That will be important for us to dedicate to our main assets. As for our main assets. And when I say we are scoping our portfolio, that's what you're doing. You're trying to improve those assets. In some cases, we are having retrofitting activities, expansion activities, geared towards those main assets. That's part of our model. And now with a strong balance sheet, that option became a reality, a more attractive reality for the company.

About your second question, about the leasing spreads and discounts. Discounts have been dropping. We were close to about 3% before. Now we're getting close to 5%. And quarter-on-quarter, we see an improvement on that front. We haven't reached the level. We had 3 recessions. But we have been evolving towards that quarter-on-quarter. The same goes for the leasing spreads. Leasing spreads were negative during the recession. They have been improving as we move along. And we expect them to improve even further as we move forward. That's not a quick, in fact, when we look at our main malls with an occupancy rate close to 97% of our top 20, close to 98%. And when we look at the dynamics with our tenants, we see that tenants are behaving differently.

A year ago, they were looking for discounts or closing down stores. Now they're feeling, the climate is different. You probably know that. The main retail chains are expanding their portfolio. New brands are being launched. Investment funds, such as (the Madero), they're going back to invest in retail, getting -- tenants getting ready to a year round of IPOs and so on.

Well the supply-demand dynamics is much more favorable right now. So looking forward, I think we are confident that there is a trend, both for discounts and leasing spreads, it's first we see an improvement, not because of the macroeconomic tailwinds, better employment opportunities, low inflation and so on. But not only that but also the supply and demand dynamics. As I said, that dynamics would be much more favorable to shopping malls. We have no growth visible areas being opened going forward. So an increase in demand with lower supply will be favorable in terms of discounts, occupancy rates and leasing spreads.

Operator

Your next question Luis Stacchini from CrÃ©dit Suisse.

Q - Luis Guilherme Braga Stacchini {BIO 18717891 <GO>}

I have 2 questions. The first one, you just mentioned that to Enrico, perhaps, to discuss the issue of leasing per square meter, the lease for square meter dropping by 4%. Of course, you have some nonrecurring events and CuiabÃ¡ and Maringa. But I'm still under the impression that the replacement of tenants has not -- has it impacted effect? Yes. So how do you see lease level of the company on average? Do you still see a need for more turnover? With leases still going down, how much longer do you think that dynamics will last of lower-leasing rates?

Also, we saw that there was that negative contribution. Does that figure represent an initially loss for the Delivery Center? Or is it more of a cash burn related to the stake that you have in that asset? Or is there something you would mark-to-market? What can we expect in terms of contribution for 2019 for that specific line, please?

A - Ruy Kameyama {BIO 16672412 <GO>}

Luis, thank you for the question. About the rent or lease per square meter versus same-store sales, in this quarter, specifically, we saw an effect which dragged the numbers down, which came from EstaÃ§Ã£o CuiabÃ¡. It is a Greenfield. And being a Greenfield, it has a lower lease rate level.

And we also had a linearization effect. And that happened because the lease in December is doubled as you know for malls. But at the same time, we tried to linearize that throughout the month. And because it was open in late October, December had higher weight and that impacted on the stores and led to a negative effect. And it started at a lower level. We also had the opening of new anchor stores. And new anchor stores, of course, bring leasing rates down.

And of course, we also had effect coming from the leasing spreads. So all of that brought the minimum rent per square meter down for different companies. Looking forward, how do we see that dynamics playing out? On the one hand, we see same-store rent accelerating from the third to the Fourth Quarter, we saw some acceleration. And for the First Quarter, we see good signs already, January and February in terms of same-store rent. So we think, we are following on the right path going forward.

And at the same time, when we look at future leasing spread, when we look at the cost of occupancy for the company, it moves -- it went through a correction, through an adjustment. The level we are now is quite healthy. The cost of occupation closed the quarter at 10%. In 2017, it was 10.3%. And in fact in '16, it was 10.7%. So we're getting closer to a healthier level. And when we look at the sales performance and delinquency level at much better metrics than before, that reassures us that in terms of adjustments for mortality rates will decrease. Since we expect the economy to improve. And we're at an adequate level.

So looking forward, we expect to see improvements, both in same-store rent and also in new leasing. And with that, I can see an improvement in the leasing spreads as well.

As for the equity pickup front, it has to do with the Delivery Center. No other relevant events were at play. It is -- we do have an initial cash burn as it is the case with most startups. In the ramp-up phase, we do have cash bun. And we're trying to maintain a good level quality in the first steps. So we have a team, which was sized to take care of that, which was -- and we will -- we have to be going through the equity pickup. And they will depend on future capital raise or dilution and on the stabilization phase for that ramp up. It's difficult for us to foresee that now. But those are the main effect that will define the behavior asset in the future.

Q - Luis Guilherme Braga Stacchini {BIO 18717891 <GO>}

Okay. Just a follow-up concerning that mortality rate that you mentioned. It got my attention, the growth delinquency having dropped year-on-year from 9% to 6.1%. When you changed your mix at 7%. So it didn't drop further because you replaced tenants who are not delinquent? Or do you have some delinquency level you created within the portfolio?

A - Ruy Kameyama {BIO 16672412 <GO>}

Oh, the growth delinquency has been dropping -- has dropped significantly when compared with -- to this year. We also made a different criteria so the money coming in is allocated to the previous tenant. So when we have tenants who have the capacity to pay. But they have an outstanding month, the invoice is allocated to the previous month. So it is healthy, if you will, in terms of liquidity. But it is still behind -- a month behind. And when we issued 2 invoices, then we changed that. And after some months, that same tenant was recovered, if you will. We saw a net recovery and full fees. But not so much for the growth recovery. They are paying part of a previous invoicing even though they are paying new invoices in their full amount. So when you look at the net delinquency rate, it is quite important for the company's health, the portfolio's health. We see that number at 4% in a good trend. So we do believe we're going in the right direction. So in a few quarters, we'll be bringing that number down, that number relative to growth delinquencies. So when we see the number at 6%, that does not mean that the portfolio has a problem. I'd like to look at the issue from the net delinquency standpoint. For this quarter, something that stood out was the big delinquencies for -- coming from the bookstore industry and that's a specific issue for that factor, the library -- the bookstore, which is quite different in the dynamic of some of the other industries, other sectors.

Operator

Next question from LuÃz MaurÃcio Garcia from Bradesco BBI.

Q - Luiz Mauricio Garcia {BIO 17432519 <GO>}

Two questions about occupancy. You mentioned that you had a strong total sales level and you mentioned the revenue dynamics, you mentioned the new tenants coming in at lower leasing levels in accounting terms now. So the question is, looking forward, do they -- how are you going to extract revenue from that? In the following sense, I'm talking about those new stores coming in, in which you're selling well, do you have any kind of ramp up in terms of contracts linked to performance? Or not? We have to wait for the third year to start seeing those numbers going up. So how does that dynamic play out? How are you going to extract revenue from those stores? What's the time line for that? And the second question is the competitive environment. You have been mentioning that -- there we see the 2 important things for you, NiterÃ³i and Tijuca, have been targeted by greater big players in the case of Tijuca, Tijuca shopping mall as an example. So 2 questions, what's the status for the Tijuca TÃªnis Clube, the internal approval processes? And what are your expectations about that? And a second question about the competitive environment as a whole. What you'd expect in terms of new entrants, both for NiterÃ³i and for Tijuca? Big players are interested in those areas. How can you see that? How can you defend the company from that? How do you expect those new projects to materialize in those 2 regions?

A - Ruy Kameyama {BIO 16672412 <GO>}

Now LuÃz, thank you for your questions. About the cost of occupancy, we -- as I mentioned, the level was 10% better than the Third Quarter 2017 and '16. So the metrics are healthier now, which are also, on the one hand, to capture more advantages. But the minimum lease, as I mentioned, we suffered a little. But on the other hand, we have a better potential for percentage rent. We saw an improvement in that metric and at the same time, we see that as for any new lease, we have a lower level for the first year, which reflects the economic momentum. But most of those contracts also include real growth throughout the life of the contracts. So throughout time, we've been able to see improvements in terms of occupancy costs. So we still think that in time, with improvement, there are no pressures on that front. And when we see that the health level, if you will, is at a much more comfortable point, not only in terms of delinquency and discounts, you'll see that the business, as a whole, tends to become more stable. So this trend, in the long run, you still have missing rates following up on sales levels. So which -- we have an expectation of better sales. We have long-term expectations of better leasing rates as well. As for the competitive environment, Tijuca, as you mentioned, NiterÃ³i, those are very important areas, it is for any tenant, any retailer in Brazil. So those are areas that are very attractive. It's been difficult for tenants to invest significantly in those areas, because the low availability of areas and the great legal difficulties in terms of authorization and permits. So that, of course, makes their lives more difficult in terms of opening new stores. Still, we're always looking for new opportunities. And if we do identify opportunity that might generate good returns, good synergies, which might be the case for the TÃªnis Clube, as you mentioned, we'll look into it. But it's well widely known that we are now analyzing the possibility of building a mall along with the club, the TÃªnis Clube. We are looking into that. We are being very cautious there. This is, to me, an interest of the club members, of course. But right now, we cannot anticipate any more than that.

Q - Luiz Mauricio Garcia {BIO 17432519 <GO>}

So just to follow-up, speaking about the TÃªnis Clube. The TÃªnis Clube will have to approve that. Do you have any idea where that stands? Do you have a time line? What would be the next step inside the club, the TÃªnis Clube?

A - Ruy Kameyama {BIO 16672412 <GO>}

No, no. I would have nothing to comment at this point. What I can tell you is that we are taking very gradual and cautious steps with the club. And this will happen in the right time. We acknowledge the importance of the TÃªnis Clube. So it's very important to have (inaudible). So we need to be very careful, very cautious to be sure all steps -- all the correct steps have been taken.

Operator

Our next question comes from (Andriano Gini) from Citibank.

Q - Unidentified Participant

My question about the core assets. What do you consider core assets? In terms of size, population size, mall size, what would you consider a core asset? So what would be the minimum size of a mall to be considered a core asset? And as for acquisitions, what kind of portfolio are you looking into going forward on that front? Talking about a possible new acquisition of (5) portfolios.

A - Ruy Kameyama {BIO 16672412 <GO>}

(Andre), your sound is not very good. But we have an internal metric that we use for the size of the city. We do not look only at the population size, we also look at the environmental or the environment of the city, if there is competition, if the mall would be attractive enough to bring in people from around the city, from the larger metropolitan area. Of course, we also try to identify relevant competition. So there is no magic number, a cutoff line to determine. We look at it on a case-by-case basis. We look also at income levels. A 200,000 people city with a high income level is quite different from a city of the same size with a lower average income. So those are the main variables, the number of people, the population in the city, in the metropolitan area and the per capita income on average for the region and for the city. As for your second question about the portfolio, we are looking at portfolios, which was the case for -- (in Monte when) -- in 2017, we have -- it's a portfolio with a few malls, which proved to be adequate and others which were not (in that it sold). That's one of our characteristics. We are very proactive, both in terms of acquiring and in terms of selling up, which is -- gives us a good flexibility. We look at portfolios that perhaps 2 other players did not think to be that interesting, be it because of turnaround possibilities or other reasons. But now I will see some of those opportunities as more interesting. But our companies in Brazil do have good assets and also -- they also hold assets that they can be -- that can be sold in time. So it's difficult to find portfolio that only include core assets. Most portfolios do include core and noncore assets. So should we find opportunities where we mainly have core assets with 1 or 2 noncore assets, the strategy would be to absorb what's core and right after that, we would look into reducing the exposure of the noncore portion of such portfolio?

Operator

Next question from Nicole Inui from Bank of America.

Q - Nicole Inui {BIO 17757166 <GO>}

I have 2 questions. The first one, would you give us an update on the retrofitting activities? How much are we going to spend this year? What malls would be focused first? And are we also going to see an increase rent in growth applicable area with that and also the Delivery Center? If you could talk about the rollout of the Delivery Center in SÃ£o Paulo. Do you have a target for the end of the year, just to have a better understanding of the Delivery Center activity? That's it.

A - Ruy Kameyama {BIO 16672412 <GO>}

Nicole, thank you for your questions. About the retrofit, our plan is to speed up NiterÃ³i, Villa Lobos and UberlÃ¢ndia as we mentioned in the presentation. We, of course, want to keep a good pace at the NorteShopping, which we started last year. And for the other ones I mentioned, we went through a phase of approvals, licensing, permits. And we should speed that up this year. We -- our plan is to invest BRL 400 million in five years, which leads us to an average of BRL 80 million a year. Last year, the number was slightly below BRL 80 million. So for the next two years, it should be slightly above than average. And most of them does not create significant GLA, approximately the same GLA. No major expansions. But in the larger picture, we talk about the same GLA. So we have -- what we're doing is repurposing the same GLA, transforming the existing GLA of stores into restaurants. Oftentimes, we have changed the nature of the GLA from outside areas to indoor areas, playgrounds. So it's a change in the nature of the GLA rather than an increase in square meters. As for the Delivery Center question, we are quite satisfied with the results we have achieved. And in terms of rollouts, they are now (trafficking) 5 of our malls. And it started in SÃ£o Paulo. Until last year, we had 5. This year, 2019, we already are working with some malls in SÃ£o Paulo, in the MetrÃ´ Santa Cruz, Villa Lobos. So in the last year, the idea was to ensure a footprint in Rio for the Delivery Center and NiterÃ³i in 2019. This footprint is now reaching SÃ£o Paulo. So that's the plan for Delivery Center for 2019.

Operator

Next question, Jorel Guilloty, Morgan Stanley.

Q - Jorel Guilloty {BIO 18291521 <GO>}

I have 2 questions. The first about the tenant turnover. So it's above the historic average, the turnover. So that suggests that was you replacing tenants at a very fast pace. So where are you now in your time line in terms of replacing tenants? And also, do you expect to have -- expect that negative spread for new concept already flattening in the leasing rents or rates? Or do you expect something different for 2019?

A - Ruy Kameyama {BIO 16672412 <GO>}

Jorel, thank you for your question. As for this tenant turnover, we expect that we are now going through a downward trend. We were at 7.6% in the -- in Third Quarter. That number was up, was higher before. And that 7% level is higher than the historical average, as you mentioned. So our perception is the following. It's difficult to make an estimate. It also depends a lot on the tenants themselves. The recession was deep, intense and it led to a high turnover. For example, for a bookstore, as I mentioned. And it is still ongoing. We've got everyone by surprise. In 2017, not many people could predict that bookstores would be taking such a big problem. But that's what we saw. Then, of course, might lead to a higher turnover for that industry, that factor the bookstores. But -- so the perception that we have is that we still have some turnover. But that the trend is downwards. And how can I say that? Because we see that tenants are more confident vis-Ã -vis the new government, the expectations of a recovered economy. They are trying to analyze if it's worth their while staying. They know that if they leave, it will be more difficult for them to come back to the malls. If they do come back, negotiations would be more difficult for them. So in several cases, we see a will -- a very strong will on the part of tenant, even among those who are facing economic difficulties, a strong will to stay. Gambling on a better 2019, an even better 2020 and '21, that the worst is over. So retailers managed to survive throughout the recession, this would be the right time for them to leave. That's the perception that we have in our conversations. And it makes sense. It is a very rational approach to the situation. In terms of mortality, we could -- in terms of mortality, we hope to see a drop in that. We hope that, gradually, we see a lower turnover. And as we saw delinquency rates are down, which reassures us. So the installed basis, if you will, it's showing a healthier condition than before. As for your second question about the leasing strategy that later reflects the new rents, the answer is yes. I mean -- we do believe that. And going forward, we tend to see a recovery. Of course, it will also depend on the speed of the recovery of the market and that, of course, will depend on new leasing spreads. But the new installed bases will already reflect that. But looking forward, it will depend on turnover and -- as I mentioned. And also, it will depend on the speed that the sales are recovered.

Operator

Our next question comes from Mr. Tito Labarta with Goldman Sachs.

Q - Daer Labarta

A couple of questions also. Just on the other cost, it was around 34%. And that's mainly related to digital investments. So just curious, is (there anything) that could make the pressure decline? Or are you done with those investments? I -- can you maybe give us color on exactly what part is related to it? Then the second question, in terms of your debts, you talked about maybe you can reduce the cost a bit further. And so do you see moving to--(inaudible) and you refinancing of the higher cost that's compared to lower cost because of what you mentioned in your talk today? And how much could you -- how much more could you improve your financing costs going forward?

A - Ruy Kameyama {BIO 16672412 <GO>}

Could you repeat the questions, please? The line was not very clear.

Q - Daer Labarta

Sure. I mean, the first question was in terms of the other costs that went up around 34% on the year, most of them mainly due to some investments with your digital initiatives. So just curious if you're supposed to see more extensive risk? Or not? Is the -- are you there? Hello? Can you hear me? Hello?

A - Ruy Kameyama {BIO 16672412 <GO>}

Tito, if you can please repeat the questions.

Q - Daer Labarta

So okay. And I don't know if this is any better. But the first question was on your other costs, which went up around 34% on the year that mainly related to your digital investments. So this year, do you expect to see more pressure on expenses related to that and maybe you can give some color on what those investments are for? Then the second question is in terms of your leverage and in maybe refinancing from the event related to lower cost. And how much could you improve your financing costs going forward?

A - Ruy Kameyama {BIO 16672412 <GO>}

So I'll answer the second question. And then please, if you can, after that, repeat the first one. I understood for the second question that it's regarding the refinancing efforts that we're doing, how much we can still do and what are our expectations. So what I can say here is that on general terms, we believe that we have maybe about 25% of our outstanding debt that we can still renegotiate with the banks through better terms. So in terms of the liability management, we could say that maybe 3/4 or 75% has been done. And we have about 25% to be done. A part of that we're doing through the BRL 600 million debenture that is now for March, this month. And we still need to go through some TR links that are -- will -- is the effort that we're going to focus on the first half of this year. In general terms, what you can expect is that the percentage of the Selic exposure will increase while TR should decrease. And with that, we will try -- hope to reduce the cost of the average debt and also to extend the durations of the outstanding amounts. So that's the general term. We don't give specific guidance on the percentage that we expect to reduce. But this is naturally both reducing cost and extending the duration, the objectives of the efforts that we're doing.

Q - Daer Labarta

Okay. That's helpful. My first question was related to the other cost line, which went up 34%, that's like mainly due to naturalization of your digital media strategy. Could you talk about some -- what exactly -- can you give some color on it, those investments? And (other -- and do you) expect it to continue -- could we further expect is related to this going forward?

A - Ruy Kameyama {BIO 16672412 <GO>}

Okay. Thank you, Tito. I understood that the question's related to the other costs. That in 2017, the Fourth Quarter was BRL 10.6 million. And now they increased to BRL 14.2 million. So an increase of 34%. This is mainly related to the digital media implementation for the digital screens. This is a model whereby we have to account for some expenses on the leasing of those equipments. And because this is a new process, it was not fully reflected on the previous quarters. So it got to a certain accumulation during the Fourth Quarter of 2018. But looking forward to the Fourth Quarter of last year, it doesn't reflect what would be the ongoing for an average quarter of the future. So looking ahead, this should be more diluted or maybe the Third Quarter operating, there could be a better processing of the -- these costs on the NOI side.

Operator

(Operator Instructions) This concludes the conference call. I will give the floor back over to the speaker for his final remarks.

A - Ruy Kameyama {BIO 16672412 <GO>}

Thank you, everyone, for participating in our conference call. Myself, Fred, Derek and our IR team remain available for other questions. Have a nice day, everyone.

Operator

Thank you. BR Malls' conference call is now over. Thank you, all for participating. Have a nice day, everyone.