

Q2 2012 Earnings Call

Company Participants

- Leonardo Guimaraes Correa, CFO
- Rubens Menin Teixeira de Souza, CEO

Other Participants

- Adrian Huerta, Analyst
- Carlos Peyrelongue, Analyst
- Michael Olson, Analyst

Presentation

Operator

Good morning. Welcome everyone to MRV's Second Quarter of 2012 results conference call. Today with us we have Mr. Rubens Menin Teixeira de Souza, CEO; Mr. Leonardo Guimaraes Correa, CFO; Mrs. Monica Simao, Chief Investor Relations Officer; and Mr. Gerson Mazer, Investor Relations Executive Manager.

We would like to inform you that this event is recorded and all participants will be in a listen-only mode during the Company's presentation. After MRV's remarks, there will be a question-and-answer session for investors and analysts when further instructions will be given. (Operator Instructions) Today's live webcast may be accessed through the Internet at MRV's Investor Relations website.

Before proceeding, let me mention that forward-looking statements are based on the beliefs and assumptions of MRV's management, and on information currently available to the Company. They involve risks, uncertainties and assumptions because they relate to future events and, therefore, depend on circumstances that may or may not occur in the future.

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

Now, I'll turn the conference over to Mr. Rubens Menin Teixeira de Souza, CEO, who will begin the presentation. Mr. de Souza, you may begin your conference.

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

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Good morning, everyone -- everybody. I would like to thank you to be with us in this call of the Second Quarter of 2012 of MRV. We are very happy. The Second Quarter was a very good quarter; one of the best of the history of the Company.

The results we are showing for you, they are very good. They show the way the Company is running today. You can see that the Company is a very balanced Company. All the areas of the Company are working very well. It's very important that at this point we are beginning a new cycle. The last year we increased very fast.

Now, of course, we like to increase but not so fast. But the main is that we are going to make very good results. We are looking or forecasting to show of course good (marks), good operational views, but important, we are also doing positive cash flow. This is very important for us.

We -- now, at this point, we are beginning the new cycle and we will run the Company with good operational results, but with positive cash flow. This is the best position that you can find for a construction company. At this time, they have come to decide MRV is the first one of the Brazil's industries to get at this point.

Leonardo Correa is here with me and he will show to you very important views. And you can just then ask us in the Q&A session. Thank you very much, and I will pass the word to Leonardo Correa.

Leonardo Guimaraes Correa {BIO 15387486 <GO>}

Morning all. You can follow my comments in the presentation we posted on our website.

Starting on slide 4, I would like to comment on our performance in the quarter. We had a quarter where we expanded our land bank, set new records over -- in terms of numbers of units built, and also in terms of number of units transferred to Caixa and Banco do Brasil, resulting in the neutral cash flow in the homebuilding segment.

This development, specifically the volume of transfers, demonstrate the Company's ability to maintain a sustainable operation, combining growth with cash generation. This is our mantra.

On slide 5, we show the evolution of our SG&A. Our selling expenses increased primarily by continued investments in our own teams and by higher advertising expenses without a corresponding dilution since we didn't have gross sales as in the magnitude that we originally expected.

That's basically due to price adjustments on Minha Casa Minha Vida program. In relation to our administrative expenses, we expect to maintain the current volume reported for the coming quarters.

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Our profitability in margins, as I commented in our last call, will be growing from each quarter sequentially this year; data that can already be seen in this quarter results. We have a long-term commitment regarding our actions on our values and on continuous improvement process, seeking the satisfaction of our customers, the development of the communities where we operate and shareholder value generation.

On slide 7, I would like to start commenting on our new subsidiary Urbamais. We believe there is a great opportunity to develop new urban areas in order to meet the strong demand for these areas. Urbamais aims at the development of large areas for residential, commercial, industrial and all mixes for other developed and/or end customers, focusing primarily on the public of our class B, C and D.

The main executives that -- who will lead the Company have already been hired, eliminating any conflicts of interest amongst any of the important synergy between the companies of the MRV Group.

Finally, before I end, I would like to make some brief comments on LOG. The volume of construction continues accelerated and the expectation is that the GLA under construction is delivered quickly. The portfolio continues growing and totaled almost 1.2 million square meters at the end of quarter second.

The large potential market supports an aggressive expansion plan, consolidating the Company as one of the leading property players in the country. This operational growth with a yield on cost of around 17.6% of the project already delivered will increase the representativeness of the results of LOG, generating value for the shareholders.

Now, we would like to invite everyone to the Q&A session.

Questions And Answers

Operator

(Operator Instructions) Carlos Peyrelongue, Bank of America Merrill Lynch.

Q - Carlos Peyrelongue {BIO 4364319 <GO>}

Thank you for the call. Gentlemen, two questions, if I may. The first one related to pre-sales for this year. With renewed focus on profitability and the price increases you have adopted year to date, do you still expect to achieve pre-sales in excess of BRL4.5 billion?

And the second question is related to free cash flow. If I understood correctly, you expect free cash flow to be positive in the second half of the year. Is that correct? Thank you.

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

Okay. Thanks Carlos. The -- in relation to pre-sales, yes, we do expect to reach the BRL4.5 billion in sales despite the fact that we have been adjusting the price of our apartments.

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The focus on profitability remains and we think that we will achieve the BRL4.5 billion.

Regarding the cash generation, we clearly see that this is an inflection point. We were burning cash. This quarter was a flat. And we expect to generate cash flow on the second half, on the Third Quarter and Fourth Quarter. As a result of this continued process of transferring clients to Caixa, that has been working very smoothly.

We, at MRV, have been saying for many, many quarters that we have always believed in first that both Caixa and Banco do Brasil would be good partners and they would be keen in meeting the demands -- the growing demand from mortgages and financing. The cash -- we represent that cash generation on the second half of the year.

Q - Carlos Peyrelongue {BIO 4364319 <GO>}

Great. Thank you, Leo.

Operator

Michael Olson, (i3 Investments).

Q - Michael Olson {BIO 6742768 <GO>}

In this quarter, MRV reached a neutral cash generation. What should we expect for the second semester and for the next year? I mean are you going to increase dividend payout if cash generation keeps sustainable?

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

The -- I just mentioned on the previous call that we do expect cash generation on the second half of the year. And this is a result of many quarters. This is something that our Board has decided, again, many quarters ago and it comes as a result.

The first cash, if you will, that is going to be generated is meant to decrease the net debt of the Company. And although we're not as leveraged as some of our other peers in the market, we want to be on a lower level of investment than the current one. The second one would be for the increase in dividends.

Very clearly, what the view of our Board is that we should be a company that should be presenting simultaneous with some growth and cash generation. And of course, a good portion of that cash generation will go into dividends. That is clearly how they see it, let's say, the value generation for the shareholders.

Q - Michael Olson {BIO 6742768 <GO>}

Okay, perfect. I have one more question. I noticed in the notes that the Company is decreasing its exposure to MCMV program when compared to last year. The share of sold/launched inventory units eligible to MCMV funding is decreasing. Is there any problem with the housing program, or you are moving your focus to a different segment or something like that?

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

Good question. The -- let me explain one thing here. Definitely we have some units that are very close to the limits imposed by the Minha Casa Minha Vida program. Given that some of those limits have been fixed, if we adjust those prices by inflation, we end up going beyond the existing limits.

In that case, we have to move or to sell those units not, let's say, within the program but instead financed by the SBT, by the savings account. What we have seen so far that has given the drop over our own interest rates in Brazil, the number of things that happened through the savings account.

The bottom line is that the installment or the financing cost for the client for those that are very close to the limit is very similar if you are financing them to Minha Casa Minha Vida or through the SBT. So again, that has been the case. We have -- now that we are changing dramatically our product or et cetera, but we have been selling some of those units through the savings account.

Q - Michael Olson {BIO 6742768 <GO>}

Okay, perfect. And if I have time, I just want to ask here one last question. It's about selling expense. It came higher than I expected as your pre-sales were most stable. What should we expect for the coming quarters? Should that keep the same level or something like that?

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

We had increased selling expenses, and as we have two things, have invested more in home team. And second, we have a large-scale project where we had to place more investments in terms of mock-ups on -- for those launchings.

We -- as I had mentioned, we expected to have higher pre-sales in the Second Quarter than what we had. We are adjusting the selling expenses and that number should be stable to lower on the coming quarters.

Q - Michael Olson {BIO 6742768 <GO>}

Okay. Thank you, Leonardo.

Operator

(Operator Instructions) Adrian Huerta, JPMorgan.

Q - Adrian Huerta {BIO 1749060 <GO>}

Just a quick question. Can you elaborate a little bit further on where you're expecting the improvements on margins to come from in the second half in order to reach your guidance for the year of 24% to 28%? Thanks.

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

There are two things that we see occurring in the second half of the year. There's going to be an extension of revenues, given the pace of construction, also the pace of our higher sales in relation to the first semester. And second, as we have already mentioned, we expect higher gross margin as we move during the year. Those are the areas where we expect improvements on our results.

Q - Adrian Huerta {BIO 1749060 <GO>}

Leo, and the improvement in gross margins, why -- can you explain the reason for this?

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

We -- on the First Quarter, we are impacted by the agreement with the general attorney related to the continuous projects. We had some of -- to a much smaller extent but are remaining intact on the Second Quarter.

Also, in relation to the delivery of some projects, some adjustments we made on the First Quarter slightly impacted again to a lesser extent and also the Second Quarter. And we see those issues getting behind us. And given the prices that we have been selling and the control on costs, we expect a higher gross margin on the second half of the year.

Q - Adrian Huerta {BIO 1749060 <GO>}

Thank you very much, Leo.

Operator

(Operator Instructions)The Q&A session is now closed. I'll turn over to Mr. Rubens Menin for final considerations. Mr. Rubens, you may give your final considerations now.

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

Okay. I would like to thank you very much to be in this call, and hope you will be joining the next quarter also with good notes and good results as it is the tradition of MRV. Thank you very much. Bye, bye.

Operator

Thank you. This concludes today's MRV's Second Quarter 2012 earnings conference call. You may disconnect your lines at this time. Thank you.

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