Q4 2014 Earnings Call

Company Participants

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

Presentation

Operator

Good morning, ladies and gentlemen. At this time, we would like to welcome everyone to EZTEC's fourth quarter of 2014 and 2014 results conference call. Note that this event is being recorded and that all participants will be in listen-only mode during the company's presentation. After the company's remarks are completed, there will be a question-and-answer session when further instructions will be given. (Operator Instructions)

Today's event is available through a live webcast that may be accessed through the EZTEC Investor Relations website at www.eztec.com.br/ir by clicking on the banner 4Q14 Webcast. The following presentation is also available for download on the webcast platform. The following information is stated in Brazilian real and in BR GAAP and IFRS applicable to real estate developers in Brazil, except when 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 depend on circumstances that may or may not occur in the future.

Investors should understand that general economic condition, industry condition, 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'll turn the conference call over to Mr. Emilio Fugazza, Chief Financial and Investor Relations Officer, who will begin the presentation. Please Mr. Emilio, you may begin the conference, sir.

Emilio Fugazza {BIO 16474296 <GO>}

Thank you very much. Welcome, everyone. Welcome to our conference call for the results fourth quarter 2014 and the full 2014 results of the company. So apart from myself, Mr. Pedro Nocetti, IR Coordinator of EZTEC, and we are here today to release the operational and the financial highlights of the company. It's important to bear in mind that this time with the results of the company -- the results of the company were very good compared to the sector. In the meantime, we have lowered the national growth in a scenario, which is challenge for the real estate development in Brazil, especially in Sao Paulo and metropolitan region of Sao Paulo.

In that sense keeping margins on track, keeping margins on the same level of 2013 is a kind of situation which can show you that our strategy, our business model for the company have been rewarded with this moment with -- this moment we have problems in terms of governability [ph] and economic growth.

So in the slide number three, the highlights of the company for 2014, I would like to start about launches. Launches, we reached BRL1.1 billion own PSV considering the acquisition of the 30% stake in the Cidade Maia project. Cidade Maia project is a project located in the city of Guarulhos. Guarulhos is a city of the metropolitan region of Sao Paulo and it is important to say that 61% of the total amount of units in these projects are sold -- I'm sorry, 61% of the total units of the project launches in 2014 were sold; in Cidade Maia project more than 80% of the units are sold.

In terms of units sold, the whole 2014, we have reached BRL881 million considering BRL154 million coming from the Cidade Maia project. The Land Bank of the company end up the year with the potential sales value of BRL6 billion equivalent to five years of launches in the piece of launches we've seen since 2013.

So in terms of financial highlights we have gross margin, 2014 gross margin; 53%, with a gross profit of more than BRL500 million. It's important to bear in mind that we have sold units not only keeping the margins, but having the cost completely under control in our construction operation. In terms of net profit, we reached something close to BRL474 million with a return on equity of BRL23 million, by far the best return on equity in the developer's company, public traded companies in Brazil 2014.

In terms of cash, the company ended up the year with a net debt position of BRL272 million. We have to say that from the gross debt of BRL507, 367 of this debt, it's a debt coming from the EZ Tower's project. EZ Towers project, we are delivering -- we deliver the keys by the end of 2014 to the Sao Carlos, which [ph] is the actual coverage owner of the Tower A of EZ Tower. And in 2015, first half 2015 they are assuming 100% of this debt bringing from the balance sheet from EZTEC to Sao Carlos. So in that sense, we are going to turn a net cash position of close to BRL100 million possibly in the first half 2015.

So finally, BRL444 million performed receivables adjusted by IGP-M plus 12% yield. So those receivables are units already sold and we can transfer, we can securitize them whenever we want, but now they are using something close to 17% to 18% yearly. So this is a kind of bridge loan we do for our clients that they have no interest to get mortgages from the banks.

So saying that now I'm going to turn the presentation to Mr. Pedro Nocetti, who will comment on the operational highlights of the company.

Please, Pedro, go ahead.

Pedro Henrique Nocetti {BIO 20904123 <GO>}

Thanks, Emilio. Good morning, everyone. I would like to please turn to slide number four, where I will continue talking about the Land Bank. As Emilio said before, the Land Bank ended the year of 2014 with a potential sales value of 6 billion with an average acquisition cost of 13%. Very important to say, we were able to buy one piece of land in the fourth quarter of 2014, piece of land which can provide more than 600 million of PSV considering that the cost of acquisition was something close to 10%.

It's very important to -- we affirm that EZTEC in a scenario in which most of the companies are facing some difficulty, we are looking and we are able to find good opportunities to buy pieces of land. Pieces of land that can keep in the long term good results as we have been reported recently. So in order to say more about the Land Bank, I would like to you to see that this chart on the top right about the acquisition period of our Land Bank. More than 8% of that Land Bank was bought after the year 2011. So very important to reaffirm again, we are able -- we are buying good pieces of land with good -- which can provide good margins.

So looking at the chart on the bottom left, you can see that 74% of our Land Bank is (inaudible) to the middle to the middle-high-end, high-end segments and 25% to the commercial segment. Talking about region, we are keep -- we will keep the operation in the same region, because 93% of the Land Bank is located in the Sao Paulo metropolitan area. An area with a good demand, an area with different types of demand, an area in which we can offer good projects in different regions and obtain good margin. So our Land Bank is very well positioned.

So please turn to slide number five, I will talk about EZ Tower. The Tower A was levered in the last December. We are now transferring the debt 367 million to Sao Carlos, this -- that will leave our balance sheet. And we still have the Tower B in our inventory. Very important to say Tower B can provide the revenues around 700 million if sold. Nowadays, considering all of the cost of the project, pieces of land, construction permit, we have now 84% of the PoC of the total cost already incurred. So we are predicting to get 100% of PoC by the end of this year.

So, please turn to slide number six, I will talk a little bit about the volume of projects under construction. As you can see in the last three quarters, we kept the volume under construction in the same pattern that was we're expecting for these following quarters, because, although, we have projects being delivered, we have projects starting construction also.

So I would like to please turn to slide number seven, I will talk about the launches in the fourth quarter and in the year of 2014. As Emilio said we launched 1.1 billion in the year of 2014. In the fourth quarter, two projects were launched. The project of the middle-end, middle-end standard Prime House Bussocaba with PSVs present at EZTEC of 120 million with 63% of the units sold until this moment. And the middle high-end project Legitimo Santana with 50 million PSV and almost 60% of the units sold.

So this sort of volume launched in the year 2014, consider the acquisition of the Cidade Maia project with 284 million. Very important to say we are very comfortable about this volume launched in the year of 2014. Considering that all of the projects that we launched they are on average 60% sold.

So in the slide number nine, I would talk about launches in the year 2015. First, I will talk about sales in the slide number eight. EZTEC sold 881 million in the year of 2014 considering 154 million of the Cidade Maia project -- considering the acquisition of the Cidade Maia project. From these sales, 42%, they came from units launched until the year of 2013. And 85% of the sales they were done by the Tec Vendas, our brokerage team. So we ended the period, we ended the year of 2014 with 1.4 billion in inventory considering market value.

From this inventory, very important to say 25% of this, they come from units delivered.

From the units under construction, almost 80%, they are sold. And more than 60% of the units that they were launched after December 2013, they are already sold. So this volume of inventory is something that keep the attempt [ph], but this is something that we are able to work well and get good margins with this inventory.

So please turn to slide number nine, where I will finally talk about the launches in the year 2015. EZTEC is still -- is studying the markets very well. We are able to launch projects and we only launched projects if we feel that demand allows us to have good liquid in this project. So for example, in the first quarter of 2015, we launched in the month of February, we launched the Splendor Ipiranga project, with a PSV of 72 million. So if we think about that this project was launched in the last month, we have already 61% of these units sold.

So this is a good performance of sales, and every time we try to launch a project we try to reach at least 50% of sales after six months of launch. This is what we want to get in terms of demand when we launch a project. So we will not launch, we will only launch these other projects in these is like if we feel that demand goes well, so considering other projects, Massimo Vila Carrao with 45 million of PSV. These are the two pieces of Jardins do Brasil with 174 million of own PSV and the In Design Vila Mascote with 78 million of PSV.

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

Emilio Fugazza {BIO 16474296 <GO>}

Pedro, thank you very much. Let's go to slide number 10, financial performance, I would like to start talking about net revenue on top left. Starting about 2014, the whole year 2014, we accomplished BRL951 million in net revenues. It's important to say that lowering 16% from 2013 means that when you see it, Pedro said, less volume of launches something close to 20%, less volume of sales because we launched less, so we sold less, so merchandise is selling something low, less, 15%.

In that sense, as we have percentage of completion, the method to recognize revenues in our accountancy, so the bottomline was 16% less net revenues than in 2013, so nothing more than this explanation. But on the other hand, when you see on the top right, the gross income and gross margin, you can see 53% in 2014 compared to 52% 2013. Even comparing fourth quarter 2014 to fourth quarter 2013, the gross margin remains exactly the same, 52%. So even recognizing less net revenue, because of less sales and because -- also because we have in 2014 less volume of construction, less volume of sites under construction, in the same time we could accomplish the same pattern of gross margin, which is amazing given the scenario, given the economic momentum we have been passing through.

When you see on the bottom left, the chart for G&A expenses, you can see the company reached a BRL104 million, 2014 compared with 83.7 million, 2013. So it's important to bear in mind that the total amount of G&A expenses we have, we have because, we have to manage all the projects under construction for the company. Not only the projects, 100% belonging to EZTEC, but even projects that company has is in a stake of 30% or 40%; so projects we have shared the control of those companies, of those projects.

In that sense, so when we compare the net G&A expense with the revenues of the whole amount of projects, we have been managing to is about 8.3% G&A expenses of the total amount of net revenues. So it's important to bear in mind in this number, this figure increased from 2013 and the company have the mindset to keep that without increment in 2015. So the company is working on keeping or lowering the volume of revenues from 2014 to 2015.

In terms of selling expenses; selling expenses on the bottom right of the slide number 10;

selling expenses reached BRL58 million, 2014, 6.1% of net revenues. When you see the comparison; 2014, 2013, it's important to say that really we have a huge increment, an increment of almost two percentage points from 2013 to 2014. I have now the forecast to lower the volume of selling expenses or the ratio of selling expenses over net revenue for 2015. This is simply because we have been spending much more expenses to accomplish the volume of sales we have to accomplish. So in that sense, now using TVs, using radios, using newspaper, using all the possibilities of merchandise we can use nowadays, the new ratio for selling expenses is much more closer to 6.1% then for the 4.3% of the past.

Moving to slide number 11, the continuation of financial performance; on the top left we have the financial results. It's important to say that all the financial expenses we have, we have those expenses on costs. So, the financial results are coming from the amount of money the company has, and the company has this money, the money not used on the production, we are excluding the base into which -- base in Brazil which now is about 13% per year.

As 2014 we have much more money available including the higher interest rates used in bonds of the Brazilian government, we could reach more financial results, positive financial results than 2013. So, which means BRL60 million compare to BRL46 million in 2013. There is a trend; there is a trend to be a little bit more than 2014 in the year of 2015, because of the interest rates are higher than in the past and the volume of money we have available to invest fund is more than 2014, or it's going to be more than 2014.

In terms of equity income on the top right, you can see that the volume of net profit -- of the results coming from equity income, it's pretty much the same of 2013. Even buying that the stake of Cidade Maia project, which can means that so project -- the Cidade Maia project is moving from equity income results to consolidation in our net revenues. So for 2015, we have more projects to launch to be recognized as equity income. As Pedro mentioned before, the project in the city of Osasco is at fourth phase of Jardins do Brasil project. Jardins do Brasil project is a project of BRL2 billion EZTEC has in a stake of 27.5% and we're going to launch the last phase of this project. The last phase of this project will be recognized by the equity income as such keeping the volume of equity income at the same pattern to the years ahead.

In terms of net income, net income on the bottom left, you can see the company reached BRL474 million. Absolutely in line with the situation of launching less, selling less, so and a little bit more G&A expenses to hurt the results. But on the other hand, you can see the margins remaining at pretty much the same of 2015. So absolutely, by far 50% -- 51% is the most or the best net margin of the sector of the real estate or best [ph] among real estate developers in Brazil, public traded companies. BRL474 billion means 23% return on equity, which is return on equity can represent twice as much the volume of the basic interest within Brazil.

So, it's a minimal that we can see to compensate the risk, the chances we have to work on a sector that which is the real estate development, the residential and the commercial real estate development in Brazil. In terms of results to be recognized, it's important to see that the gross margin of this, the backlog margin of the results to be recognized, it's about 49%; 49% compared to 53% in the past. 53% because when we acquired -- at the moment we acquired the Cidade Maia project; Cidade Maia project is a project of BRL1 billion in potential revenues and a project of 46% to 47% of growth margin; 46 or 47, BRL1 billion of revenues.

So on average in our -- on a mix of results in our backlog, lower the backlog margin from 53 to 49 is nothing else [ph]. So we are not running out of costs as we are not selling for worst prices than in the past, no. It's exactly the same of the past, only the effects of the recognizement of the Cidade Maia project in our balance sheet as a consolidated project for EZTEC. So in that sense for the quarters ahead, the forecast for gross margin is about 49%, which means our backlog of margins.

Turning to slide number 12, cash position; cash position is very easy subject for EZTEC simply because we have something close to BRL507 million of debt and 100% of this debt is production debt. So production debt means that those debts are connected or projects that are connected with the construction of the projects and on average the interest rates of those project is like 20% less than the basic interest rate in Brazil.

It's because of this -- so this kind of debt doesn't hold our EBITDA margin or our net margin for EZTEC. In terms of cash and equivalents of cash, there was a drop from third quarter to fourth quarter 2014. And this drop means that we repaid BRL140 million in dividends last November. And we paid last October the 30% acquisition of Cidade Maia project, which means something close to BRL58 million. And we ended up the year with a net debt position of BRL272 million.

But from this debt, from this BRL507 million debt, 367 belongs to EZ Tower project. Belonging to EZ Towers project means, in this first half 2015, we are going to bring these amount of debt from the balance sheet, the EZTEC balance sheet, to Sao Carlos balance sheet, the ex -- the coverage owner of Tower A of EZ Towers project. In that sense our forecast is to turn from net cash (Technical Difficulty).

Moving on to slide number 13, about dividends referring to 2014 results, we have the net income, which was BRL474 million. The statutory reserve we have to keep is about BRL23 million. So the proposed dividends 25% net income after the statutory reserve, it is BRL112.6. So which is the dividend per share about BRL0.77 per share less than in the past, specifically because the amount of net income is lower from 2013, but by far one of the best of the sector.

It's important to bear in mind that in Brazil, we have by the law, we have a method to do capital increase, which is when you have a capital, an amount of capital and your earnings reserves surpass the capital of the company, so we have to capitalize or we have to pay as more dividends in order to keep both at the same level. So in that sense, the Board of Directors will propose in the next shareholders' meeting, a capital increase of BRL170 million from the earnings reserves.

But adding that an issuance of almost BRL10 million of common share at a cost of BRL16.47 [ph] per share, the BRL16.45 per share means the coverage price, the coverage value of the shareholders equity. So, it's nothing different than we have to do when the earnings reserve surpass the shareholders' capital, so that is.

Moving to slide number 14; then the slide number 14 we have in a statement of the net asset value of the company. The net asset value of the company reached BRL29.21 per share which means company value of almost BRL4.3 billion for this price of share. It's important to say that when you see this statement, you see cash, you can see debt, you can see performed, unperformed receivables, but you can see also Land Bank inventory. Land Bank inventory means that all the volume of the potential sales value in Land, Pedro mentioned before of BRL6 billion, which means five years of future launches for the company. The cost of those BRL6 billion in potential sales value is about BRL728 million. All of that in cash, a 0%, nothing, none percent of these amount of land earns what [ph]. It's important to bear in mind.

And as we released last December, in the public meeting we held in A EZ Towers, the gross margin of those project on average, something close to 47%. So and years ahead, we have a little bit more than BRL2.5 billion in gross income to add in this adjusted net asset value to reach something close to BRL7 billion in future net asset value for the company.

As we are going -- as we are launching the project, you're going to see the volume of net asset value increasing owing we ended up the year with a return on equity of 23%; 23% over BRL474 million, obviously is the best of the sector, is the bigger of the sector. And nowadays, we reached a point that our shareholders' equity is pretty much the same of the market cap of the company.

So, which means for the Board of Directors, for the executives of the company, almost no sense. So when you see, since 2010 company releasing a return on equity of more than 26%, 26%, 30%, 24%, 35% to 23%, a company with a market cap would think something close to the shareholders' equity means that our shareholders are (inaudible) the company almost nothing in terms of growth in this equity for the years ahead. Obviously, is not our opinion about that which we can show you on the slide number 15.

Slide number 15 can tell you something more about Asset Management. So the mindset of the company for these kind of moments in our economy is about although, about productivity and efficiency. So when you compare on the top left, when you compare the gross margin 2014 to 2013, you see the company operating something flat in terms of margin. When you see return on equity, you can see a huge drop but mostly because the base, the capital base is much more higher in 2014 than in 2013. And you could think that what possible situation is to increase the payment of dividend, the dividend ratio in terms of our net profit.

But unfortunately we have to think orthodoxically [ph] is to simply because we have nowadays -- we have been leaving to a governability crisis and in moment of governability crisis, we have no possibility to forecast what's going to be in terms of economy.

So, nowadays we have been launching projects. This the pace of sales of those launches are pretty much good, but when you see all the other operators in the sector, all of the other developers in the sector, they are facing problems, much more higher than EZTEC. And we don't know what is the amounts of hurt we are going to see in the quarters ahead, given the moment with this -- the moment that we have been passing through.

So for now we are taking the decision to keep the capital, to keep the earnings reserve at the same pattern. Two possibilities; one of them is to be opportunistic to buy some good assets in order to increase the production in the years ahead. The other situation is to keep a solid strength in terms of balance sheet to support whatever is going to come from this moment we have been passing through.

So the bottom line of it is when you see the shareholders, the net debt to shareholders' equity. So you see that we reached 11% in 2014; 11% in 2014 with the situation of turning from net debt position to net cash position in the first half 2015. So we are keeping the margins at the same level. We are working our best to keep the return on equity on the same level or mainly twice as much the base interest rate in Brazil. And we are doing that without increasing the risk of the company trying not keeping or not increasing the net debt-to-equity ratio.

Finally, I would like to say, I'd like to highlight (inaudible) in the governments we have been dealing in our company. So the company is closing its eighth year of public traded -- as a public traded company with almost the same executives and the same Board of Directors taking the decisions. So when you see that and you -- when you see all the information, all the disclosure -- all information and all the disclosure to take the decision to release to you what are the perspectives for the years to come, we are trying to be true and we are trying to be realistic instead of optimistic. In my personal opinion, nowadays, we are the best company prepared to face the problems issued by the government in Brazilian economy.

Thank you very much. And we are completely available to -- for the questions. Thank you.

Questions And Answers

Operator

Thank you, sir. (Operator Instructions) At this time we have no questions. This concludes the question-answer session. At this time I'd like to turn the floor back to Mr. Emilio Fugazza, for any closing remarks. Sir?

A - Emilio Fugazza {BIO 16474296 <GO>}

Thank you, everyone for the audience today. And apart from myself and Mr. Pedro Nocetti, Mr. Erik, we are completely available to further questions. Thank you very much, see you next time.

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

Thank you so much.

Operator

And we thank you gentlemen for your time today. This does concludes today's presentation. At this time you may disconnect your lines. Thank you and have a great day, everyone.