

Q3 2007 Earnings Call

Company Participants

- Leonardo Guimaraes Correa, Dep. CEO, IRO
- Rubens Menin, CEO
- Unidentified Speaker, Company Representative

Other Participants

- Alex Bartner, Analyst
- Carlos Peyrelongue, Analyst
- Gordon Lee, Analyst

Presentation

Unidentified Speaker

(inaudible) -- or on the Company's investor relations website.

Before proceeding, let me mention that forward-looking statements are based on the beliefs and assumptions of MRV's management from information currently available to the Company. They involve risks, uncertainties and assumptions. Because they relate to future events, they 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, CEO, who will begin the presentation. Mr. Menin, you may begin your conference.

Rubens Menin {BIO 15387481 <GO>}

Good afternoon. Thank you, to stay here with us. It's with much pride and satisfaction that we present exceptional results posted by MRV in the Third Quarter of this year.

As you can, MRV has demonstrated its immense growth potential and excellent operational capacity leading to the impressive operating results and margin. We will show that not only did we achieve quite easily all that we promised in our '07 guidance. But that our guidance for '08 shows a strong growth in operation resulting in a select margin and consolidating MRV's position as the largest Company of the low income segment in Brazil.

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First, I would like to say something about '07. Today, with the approaching year end, we can see the impressive growth in the Company's operation and, more importantly, that it is constant and sustainable. Note that all our indicators have heightened at above previous rates. All markets post showing an excellent operational level. And our backlog gross margin was an enviable 55%. We will provide a few more operational data in our presentation and (inaudible) later.

Now, talking about our future, I would like to highlight a few points I consider fundamental. The name of the game, team. First, guidance '08. Once again, we see high rates of growth and operating margins in the '08 guidance. Second, the MRV 40,000 project. This is our big challenge for '08 and the years that follow. We have prepared the whole Company to operate at the pace of 40,000 units per year in the near future. It's a complex process that will certainly require total commitment and a lot of work from our team. But the result will be exceptional. Without any doubt this project will be the foundation of our future growth and sustainability.

Third, the team. This is one of the aspects I consider the most important and which explains how MRV managed to reach this position and why it is confident about continuing to grow at this accelerated pace, delivering good performance in the future. I reiterate that this work did not start now. But many years ago. We now have a highly qualified and committed team that goes after the targets established by the Company management. Our success is the fruit of a great team effort. I can assure that we have the most experienced team in this industry. And with a very special operating partnership model, which I believe makes all the difference. We have been practicing this for 11 years.

Knowing how to align the Company's interests with employee interests have always been a goal we have endlessly pursued. Our Real Estate Development team has seven executives with an average tenure of 14 years at MRV, holding 8% of our shares and 0.2% of the stock option. No doubt it's the most experienced in the market. And as a result, our land bank may be considered to be of the highest quality, not to mention the efficiency of our projects, which always meet the needs of our clients.

Our Production team is very special. We have seven executives with an average tenure of 13 years of MRV, holding 1.3% of our shares and 0.5% of the stock option. This team has vast know-how about low-income housing and has the best track record in the industry.

Our Commercial team is 100% focused on low-income housing, as this has also been the Company's focus right from inception. This department has four executives with an average tenure of four years at MRV, holding 0.3% (sic; see presentation) of our shares and 0.2% of the stock options.

And finally, our Administration and Finance department is state of the art. This department has 10 executives with an average tenure of five years at MRV, hold 0.4% of our shares and 1.5% of the stock option. I must mention the quality of the team with regard to a few aspects like, IPO[ph], finance etc. The entire team, which is the backbone of growth, is ready and raring to go. It's true that really amazing[ph] the team. But what give us the confidence is that the base is solid, highly experienced and committed to our growth.

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To conclude, I reiterate that a long-term operation has to be integral, starting with a well executed development process, then moving to efficient construction and concluded with a successful sales process. Only with this, we'll be able to reach our targets and bring value[ph] to our shareholders.

Thank you, everybody. And now I will give the floor for Leonardo Correa, our Vice President and IRO of the Company.

Leonardo Guimaraes Correa {BIO 15387486 <GO>}

Thanks, Rubens. Let me continue our presentation. Let's go to page 11 and let's talk about the highlights of this session. The main highlights that we have here are the three-digit growth that we'll show you on our launches, on our sales and on our revenues, when comparing the Third Quarter of '07 to the Third Quarter of '06. Also, we'll show you the growth on our gross margin, on our EBITDA -- adjusted EBITDA margin, on our net margin and on our backlog margin. Finally, I want to show you the growth that we had on the number of cities and on our land bank.

Before I get into further details, let me deliver you two messages regarding Real Estate's client financing in Brazil on our number eight slide. The two messages are the following. The first one is that we're seeing a very solid growth on the funding for the low-income financing, both on the savings account and on the FGTS, which is the unemployment fund. The second message is that the commercial banks and Cash Economica[ph] are very interested and eager to grow their real-estate books and they have plenty of available limits to do so. In summary, we have very good prospects for client financing in the low-income segment in Brazil.

Jumping to slide nine. I want to talk about the G&A and I want to talk about the productivity of the Company. First of all, we have our adjusted general and administrative expenses. And here what we are doing is that we are excluding the non-recurring expenses related to the IPO on the Third Quarter.

Before I get into that, I want to call your attention to the fact that companies that are facing a very strong growth as ours, they have -- they are somehow penalized in the sense that the expenses come much in advance in relation to the revenues. And therefore, there is this gap between expenses and revenues. Because of these issues. And in order to keep track of that, we like to measure our expenses in relation to sales. Sales is always a key indicator for any company.

Our adjusted sales for the Third Quarter of '07 reached BRL14.1m. If I measure that. And when I want to start looking at our productivity, I basically have to divide that number by the pre-sales value. And when I look at these percentages, the comparison of the Third Quarter of '07 to the Third Quarter of previous year, for the nine months of the '07 in relation to the nine months of the previous year. And also the same percentage comparing the Third Quarter of '07 to the Second Quarter of '07. On these three percentages, on these three comparisons, I see them decreasing. I see them decreasing around to the level of 6.5%. And the message here is that we are on the right track. We're

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increasing the productivity of our Company. And that we will be increasing further the productivity of the Company.

If I jump into page 10, the point here is going to be very much related. Again, the issue of a very strong growth Company and the gap, time gap between the expenses and the revenues. And therefore when I compare the productivity of our selling expenses, if I look at the comparison of Third Quarter, both in relation to the previous year, both in relation to the previous quarter of the same year, I see my productivity increasing, going from 6% to 3.9% in the Third Quarter of '07. And going from 4.1% after the Second Quarter of '07 to 3.9% of the Third Quarter of '07. So you see that those BRL8.4 million that we had on the selling expenses on the Third Quarter, they -- basically, we are becoming a more productive, a better Company with a better productivity ratio.

If I jump to slide 11, I want to talk about the launches of the Third Quarter. They have reached BRL289m, a very robust growth of 473% in relation to the Third Quarter of '06. And even if I compare the Third Quarter with the Second Quarter of '07, you see a growth of, in this case of 14%.

If you look at the launch mix, if you look at our product mix of the Third Quarter launches, you see that 83% of the launches were for units up to BRL130,000. This is -- this represents the trend that we have on our land bank. This is very much our focus. And our focus is that we should be launching more products on the low end or more on the -- for the -- units with a lower price.

For the slide 12, we will be talking about the contracted sales. The contracted sales have reached BRL217 million on the Third Quarter. It's again a very strong growth of 261% in comparison to the Third Quarter of '06. If I compare quarter to the previous quarter of the same year, you also see a growth of, in this case of 38%. And as we launch more products and we increase our sales, the market is hot, the demand is very good and this is clearly not a barrier for our growth.

On the slide 13, we will be talking about our land bank. Here there are three main messages that I want to pass on to you. First is that we have added another estate on our portfolio. Second is that we have already increased the number of cities. We are in 51 cities. If I look at the size of the land bank, we have shown a very strong and robust growth of around BRL2.6b. They -- our land bank today amounts to BRL6.9 billion worth of launches. Again, a very strong growth when we compare to the last time that we report our land bank on July 31.

The last point I want to convey to you is that we have divided this land bank in two categories. The first category is that of state capitals and their metropolitan areas. And the second category is the other cities or the interior of the country. Basically, 40% of our land bank is located on our capitals and their metropolitan areas. And a larger part, or 60%, is located on the interior. And here, I think this is a show of our strength on the interior where we face less competition.

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If we jump into page 14, we'll be talking about our net operating revenue. It has reached BRL113 million in the Third Quarter, a very strong growth of 203% in comparison to the same quarter of last year. And again I call your attention to the comparison of quarter to the previous quarter, or to a growth of 41% in relation to the previous quarter.

On page 15, we'll talk about our gross income and our gross margin. The gross income has reached BRL45.9 million on the Third Quarter. It is an increase of, in percentage terms to the previous quarter, or to the same quarter of the previous year. Last year our margin was 38% and in this quarter it was almost 41%. Again, if I compare to the previous quarter, you also see an increase. And that is the kind of trends that you'll be seeing as we relay[ph] our results.

On page 16 we'll be talking about EBITDA and EBITDA margin. Here we'll be talking about adjusted EBITDA and the adjustment is that we're excluding the non-recurring IPO expenses. Our adjusted EBITDA margin on the Third Quarter reached 27%, which compares very positively to 20% of the same quarter of the previous year. If you look at the Third Quarter margin EBITDA -- adjusted EBITDA margin in comparison to the previous quarter, you also see an increase going from 22% on this Second Quarter to 27% on the Third Quarter. The point here is that, as we are growing our revenues in -- at a very good speed, we are diluting our expenses into higher revenues -- into larger revenues.

Jumping to page 17, now we'll be talking about adjusted net income and adjusted net margin. The adjusted net margin reached BRL37.8 million on the Third Quarter, which compares very positively in percentage terms. This quarter that margin was 33%, compared to 16% in the same quarter of the previous year. If I look at this quarter in comparison to the previous quarter, you also see a very positive trend. And here financial revenue coming from the proceeds of the IPO play a positive role.

On slide 18, we talk, basically, about our unearned results. And this is a very good emphasis[ph] of our ability to take advantage of a very good current market conditions. In other words, it's a very hot market and we know how to take advantage of that. Our unearned results, they reached BRL181 million on the Third Quarter of '07, a very solid and a very strong 55.5% margin. That shows, also, a very significant increase in relation to the previous quarter of the same year. This is clearly something that will be positively affecting and pushing our gross margin up on the quarters to come.

Jumping to the outlook and to page 19, I want to talk about our guidance. First, I want to talk about the '07 numbers and then I'll talk about '08. In the beginning of October we have already revised our guidance for the launch value in '07. So we have increased that on the beginning of October to the interval of BRL1,030 million to BRL1,100m. On the contracted sales, we are now -- we are today revising up our original guidance. We're revising it to the interval of BRL640 million to BRL690m. For the gross margin, we are revising the interval. And now our new interval goes from 39% to 41%. On the adjusted EBITDA margin for '07, the previous interval was 21%, 24%. We are revising it up 24%, 26%. And for our adjusted net margin, the previous interval was 19% to 22% and we're revising it up to 24%, 26%.

For '08, we'll be talking not about adjusted margin and adjusted net margin or adjusted EBITDA margin. But we'll talk about net margin and EBITDA. Our guidance for launch value for '08 is for the interval of BRL2 billion and BRL2,200m. Contracted sales is for BRL1.5 billion to BRL1.7b, gross margin to come on the interval of 40% to 44%, EBITDA margin to come on the interval of 24% to 28%. And net margin to come on the interval of 21% to 25%.

I want to thank you for the opportunity of talking to you all and let me pass the word back to Rubens.

Rubens Menin {BIO 15387481 <GO>}

Okay, Leonardo. Thank you very much. We're now ready for the Q&A and therefore on you[ph].

Questions And Answers

Operator

Thank you. The floor is now open for questions from investors and analysts. (Operator Instructions) Thank you. Our first question is come from Carlos Peyrelongue of Merrill Lynch.

Q - Carlos Peyrelongue {BIO 4364319 <GO>}

Thank you. Hello, gentlemen. Congratulations on the solid results. Two questions if I may. The first one is related to the backlog margin. On a quarter-over-quarter basis, your backlog margin increased from 52% to 55.5%. Can you provide some explanation for this increase, this fairly large increase in just one quarter?

And the second question is related on or to construction. Of your total construction, can you give us an idea of the breakdown between the construction that is done in-house and the construction that is done by third parties? Thank you.

A - Rubens Menin {BIO 15387481 <GO>}

Okay. This is Rubens. I will answer first the second question about construction and then, Leonardo, do you want to follow-up with the backlog?

Like I told in my explanation, I think that we make the whole process the best way to do. We have to make the construction, the operation, development and sales. And what we will make in there? And we (inaudible) of construction -- of production inside and we will make the easier lifting[ph]. But the (inaudible) sometimes we gave for the first part. But we think that the best way to do is to make everything inside. We have some orders with partners, some companies that you know very well. (inaudible), suppliers and backlog[ph] there. They'll produce with us. But they produce under our supervision. And the (inaudible) today is more than 80% we do by ourselves. And the other 20% is with partners.

About the backlog, I would like that Leonardo answer to the question, please.

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

The main explanation is that we have been raising prices and our recent launches that we have done, they have been sold with very good margin. And again it is a question of taking opportunity of the demand. The demand is responding very positively. And that is the reason why we have increased by such percentage.

Q - Carlos Peyrelongue {BIO 4364319 <GO>}

Understood. Thank you.

Operator

Thank you. Our next question is come from Gordon Lee of UBS.

Q - Gordon Lee {BIO 1551117 <GO>}

Hi. Good morning. And likewise, congratulations. Two quick questions just related on the growth. And one thinking more about the MRV 40,000 plan. The first question, obviously you're seeing a very large ramp-up in volume this year and you're expecting a very big one next year. And I was just wondering from a balance-sheet perspective if you feel comfortable with having enough cash on hand to go through all the launches for this year and next?

And the second question was, as you think about MRV 40,000, if there are any meaningful CapEx outlays that we should be aware of, either respect of systems or perhaps to any acquisition or further verticalization on the construction side that you think we should be aware of, at least for this year and next? Thank you.

A - Rubens Menin {BIO 15387481 <GO>}

Okay. Yes, okay. I'll answer the second question about MRV 40,000. MRV 40,000 is a very complex program and we have been working on this for more than one year. And we have been working hard. Of course, we have some spend with CapEx. We changed all our hardware and we put some money in programs and software. But it's not a very, very big money. You are talking about less than BRL10m.

The big key[ph] of the MRV 40,000 is to put every people into positive thinking and running at the same way at the same time. And I can assure to you that this is working. This year, you have very good improvement in the personnel more positive. And I'm very confident that next year will be very, very good for us too. And MRV 40,000 it looks positive for production[ph]. Hopefully, the production line for the backlogs and everything. To now MRV 40,000 is working very well and I expect it to work again and this will be the pillar of our increasing.

And I will ask Leonardo to answer about the other question.

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

Okay. Just to complement, you asked after -- you made a question also about verticalization. We see no need for specific verticalization on our program. There's no concentration of any investment on that front.

Regarding the balance sheet, yes we do have enough cash for running the Company with the launches and the construction of this year and of the next year. I just want to remember everybody. And I have been talking on our financial model, we contemplate some debt on the Company. And that is something that we'll probably accessing the debt market on the beginning of next year.

Q - Gordon Lee {BIO 1551117 <GO>}

Perfect. Thank you very much.

Operator

Thank you. Our next question is coming from Alex Bartner, of ESBC.

Q - Alex Bartner

Hello. Good afternoon. (inaudible) and congratulations for the results. My question is regarding the land bank. You guys have now almost BRL7 billion in the land bank. And I want to understand from you first what would be your comfort level in terms of land bank? You have now about three years of launches, if that is a sustainable level or if we should still expect some very relevant ramp-ups on the size of the land bank?

And also, if you could give us some color on the price and conditions of the recent land acquisitions that you guys have made? Thank you.

A - Rubens Menin {BIO 15387481 <GO>}

Okay. That's Rubens. Thank you. About land bank. Land bank is a key point in our business. Like I told in my presentation, we have a very good and experienced team working on that. Our kind of business needs around two years to have half and half in land bank. In the past you have two and two and a half. But with the growth we did (inaudible) now we have to have three to three and a half years. Of course, we have to ramp up the land bank.

This year we made a very good job. We began the year with more than BRL1 million -- BRL1 billion and we now have around BRL7b. And we will have at the end of the year, bigger than that. But the challenge in '08, we will have to move fast. And we are doing that. We are beginning the views[ph] for '08 now. But you have a lot of views that are coming. But some views delay[ph] three months, four months, five months to finalize the buying of the land. But I'm very confident that our team is a very good team and we will be able to buy the land that we need into the next year, in '08 year. And of course, the '08 year will be more mobile than this year. But (inaudible) to have in-house three and a

half years of land bank in the '08, we think. And all of this, you are dealing with in the MRV 40,000 project.

Q - Alex Bartner

Okay. Thank you.

Operator

(Operator Instructions) Thank you. I would like to turn the floor back over to Mr. Rubens Menin for closing comments.

A - Rubens Menin {BIO 15387481 <GO>}

Okay. I take this as the end of the Q&A. And like I told in the beginning, I'm very happy and very proud with Third Quarter of '08 -- '07 and the nine months of the '07. Did a good job. All the team are very, very glad with this. And of course we are planning good news for you in the future. I thank you very much to have the time to hear us and I hope we'll meet again in the end of the year. Thank you very much.

Operator

Thank you. This does conclude today's teleconference. You may disconnect your lines at this time. Have a wonderful day.

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