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Q2 2016 Earnings Call

Company Participants

- Armando d'Almeida Neto, Vice Chief Executive Officer and Investor Relations
- Franco Carrion, Investor Relations Manager

Other Participants

- Daniel McGoey, Analyst
- Ivan Enriquez, Analyst

Presentation

Operator

Good afternoon. Welcome everyone to Multiplan's Second Quarter 2016 Earnings Conference Call. Today with us, we have Mr. Jose Isaac Peres, CEO; Mr. Armando d'Almeida Neto, CFO and IRO; Mr. Marcello Barnes, CIO; Mr. Hans Melchers, IR and Planning Manager; and Mr. Franco Carrion, IR Manager.

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

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

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

Franco Carrion {BIO 16449361 <GO>}

Good morning. Thank you for listening to our call. Over the last few months, confidence started to be restored in our country, which is essential to bring the businessmen and the consumers back to investing and consuming again. In our view, this potential recovery is the result of the measures being taken by the country's new administration, even if it

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carries a transition status, an administration that shows an excellent economic team and is gradually managing to put Brazil in the right direction. The growing confidence, which is fundamental for the economic environment, is already observed in the stock market in the forecast made by the IMF last week and in the data published by important economic institutes.

I take this opportunity to point out that so far this year, Multiplan's share price appreciated close to 65%. These encouraging data started to be reflected in our malls, which kept growing in the second quarter, highlighted by the 4.1% increase of our Tenants' Same Area Sales over the same period of the previous years. This shows that despite the adverse scenario, Multiplan continues to maintain positive figures both in its tenant sales and in our company's net income, which reached BRL98.7 million in the quarter or 2.4% above the same quarter last year. Moreover, our rental revenues net delinquency rate fell from 3.6% in the first quarter to 2.4% in the second quarter.

Next, I would like to highlight some of the assets that recorded excellent sales performance. Shopping Analia Franco in Sao Paulo grew 7.1% in the quarter; Parque Shopping Maceio in Alagoas, 7.6%; ParkShoppingBarigui in Parana, 9.4%; and ParkShopping Sao Caetano in Sao Paulo reached double-digit growth of 11.4%. We also continue to seek highly efficient mall operating costs by improving the asset management and searching for more modern and efficient technologies. Our tenants' occupancy cost declined compared to the first quarter of the year and stood at 13.1% in the most recent period.

Throughout these times of adversity where Brazil's economy stopped growing and the national retail presented successive falls, we have not recorded negative sales in any quarter. We delivered in June, at BarraShopping in Rio de Janeiro, the expansion of Mall's Medical Center, an innovation created by Multiplan 20 years ago, which receives more than 10,000 people a day. The expansion has 3,500 square meters with 11 clinics, including a premium laboratory that brings together, in one environment, lab exams and a diagnosis center.

As of the last quarter, BarraShopping Medical Center has 41 clinics with more than 150 doctors. We are repeating the same strategy in RibeiraoShopping in the city of Ribeirao Preto, where we started the construction of a Medical Center, comprising 32 clinics and a day-hospital. I also wanted to highlight that although it does not represent an economic impact, but a great social one, and honoring our RibeiraoShopping's 35 years and the city of Ribeirao, 160 years, we delivered a true gift to the city, the renovation of Parque das Artes. It is a 68,000 square area adjacent to the mall, where we sanitized its tree [ph] lakes, built a one mile racetrack, delivered a new furniture and a picnic and Food Truck area. It is a true example of how Multiplan is also concerned with the well-being of the population living nearby our shopping centers.

Another intervention I would like to highlight is the integration we are promoting between Morumbi Corporate, a business center with 72,000 square meters of area and MorumbiShopping in Sao Paulo. We are completing the construction of a modern skywalk, 330 feet long connecting the two sides of Avenida Chucri Zaidan allowing pedestrians to have access to both Morumbi Corporate and MorumbiShopping without having to cross the busy avenue.

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With this, we'd benefit an entire developing region with the most modern buildings in Sao Paulo and the workplace of about 30,000 people. We are preparing a footbridge with air conditioning, escalator and elevator to be delivered to the population of Sao Paulo made by Multiplan in collaboration with the City Hall.

We are building the second phase of Patio Savassi, expansion II, in which we are incorporating two large stores, Renner and the BIG [ph] Supermarket. Still new projects, we have already started infrastructure works in the surrounding area of ParkShopping Jacarepagua project, preparing the land for the beginning of the mall's construction, which will have 42,000 square meters of GLA and is located in one of the fastest growing areas of Rio, the West Zone. This is a neighborhood with a predominant upper-middle class population with about 500,000 inhabitants and no significant shopping center operation.

Finally ParkShopping Canoas located in Porto Alegre, our second project in Rio Grande do Sul is in advanced construction stage and will open in 2017. We now have 73% of the GLA leased and in September, we will deliver our renovated park, Parque Getulio Vargas, a fully urbanized area that will likely be highlight for the region with new gardens and lakes. It will also have a lightened fountain that will offer an amazing water show not yet seen in Brazil.

To conclude, I would like to state that we continue to believe in Brazil and its growth. I'd like to thank our shareholders' and investors' trust in the company. I also want to thank our officers, the whole team at Multiplan for their dedication. And finally, I also thank the analysts and the journalists for their interest in the company.

I'll now pass the floor over to Armando, who will bring you more details. Thank you.

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Armando d'Almeida Neto

Thank you, Franco. Thank you, Mr. Peres. Good morning everyone and thank you for being with us in this call. Just a reminder, this presentation is present in our managerial report. Please see the earnings release and the financial statements for further details and information.

Let's start with the operational data. Tenants' sales exceeded the second quarter 2015, growing 2.7% this quarter. To-date and since the IPO in 2007, we did not present any quarter and not even a single mall with declining tenants' sales, despite the high comparison base of our malls. In this sense, sales resilience can be seen by the high level of sales per square meter of satellite stores of BRL26,000 -- BRL26,818 in the 12 months ending in June 2016, being 3% higher than the 12-month period of June 2015.

Another good result was to see the 2.3% growth in same-store sales, outpacing the growth in retail, but also higher than the 1.6% same-store sales in the first quarter 2016. It is too early to point out to a recovery. The mix change continues to add value to our malls, driving the same area sales growth to 4.1%, 189 basis points higher than the same-store sales of 2.3%.

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In this quarter, we signed 74 new lease agreements totaling 8,836 [ph] square meters of GLA. Once again, the services segment led the same-store sales growth with an 8.9% rise. We should also highlight the apparel and home and office segments, the latter resuming growth after a few quarters. The occupancy rate remained high at 97.6% and the occupancy cost was 13.1%, 46 basis points above the second quarter '15, but 89 basis points below the first quarter of this year. This additional room to our tenants was also demonstrated by the 56 basis points decrease in our gross delinquency now to 4%, but mainly by the net delinquency, which fell 120 basis points to 2.4%.

Rental losses remained at only 1% in the quarter. This -- it is an indication of the value of a good tenant location, the value of a good property, a high quality property. Gross revenue increased 5.2% and its main component, the rental revenue increased 4.9% driven by the 6.6% growth of the minimum rent in the quarter. The shopping center expenses rose to 32.3 million from 22 million in the first quarter of '15 and were in line with the 32.1 million incurred in the first quarter this year.

This higher cost is still related to provisions and common charges due to the higher delinquency and higher vacancy when compared to last year and also to investments in promotions and marketing campaigns that helped sales to have a good performance. Also important to highlight that due to the higher spread, higher -- faster growth of same area sales over the same-store sales, it means that we have a slight increase in turnover while temporarily vacancy creating common cost expenses for the good reasons we've seen, not just for good reason, for the long state reasons. So we have -- can better implement the mix change that will result in higher sales in the long run, so -- but you have an investment cost, initial cost to pay.

Just moving into headquarter expenses, they were up 12.8%, but taking into account a provision reversal -- provision reversal that occurred in the second quarter of last year. If we exclude this one-off effect that happened in the past year, the increase would have been a 6.7% below the inflation for the period.

Turning to results, the net operating income, NOI, was higher by 0.6% with the margin reduction of 287 basis points, mainly due to the shopping center expenses increase. In 12 months, the NOI totaled BRL946.3 million with a margin of 88.1% is still on very high levels, range that we'd been presenting. Consolidated EBITDA increased 5% with a margin of 72.4%, up 43 basis points. Over the last 12 months, EBITDA reached BRL803.6 million with a margin of 72.3 million -- 72.3%, 206 points higher. Even with all the challenges, with a higher interest rate and expenses, net income increased 2.4% in the quarter, totaling BRL365 million in the last 12 months.

The FFO was 1.5% higher at 140.5 million in the second quarter this year, but in the last 12 months, it reached BRL532.6 million. The margins remain at a higher levels and the consolidate EBITDA margin was the highest presented in the second quarter until now, we are working to improve it. Capital structure; this quarter, we invested BRL64.5 million and paid out a 115.8 million corresponding to the net amount of interest on capital announced in December last year. In June 2016, net debt compared to EBITDA was 2.43 times far from the nearest quadrant [ph] which is at four times net debt to EBITDA.

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The average tenure is -- of our gross debt is 52 months and the net debt represents only 12.9% of the fair value of the properties. The average cost of the gross debt was 13.23%, a 102 basis points below the Selic rates, the basic interest rates in Brazil.

Turning now to development, ParkShoppingCanoas construction is progressing within budget, with a 73.1% of the GLA already leased, one year before the opening. We launched in this quarter, the ninth expansion in RibeiraoShopping, an integrated Medical Center with 4200 square meters of GLA, in its first of two phases. And we are also developing a new expansion in Shopping Patio Savassi in the city of Belo Horizonte with 2300 square meters already leased to two key operations. Both sites are already under construction.

This -- in regards to our stock, to our shares, this was another quarter in which we presented a strong performance, rising [ph] 12.2% and accumulating 58.6% increase year-to-June [ph] or a 65% year-to-date. Despite the sharp increase that we've presented, the first time we saw the stock trading above BRL60 was in September 2012. If we compare the 12 months' NOI from June 2012 to June 2016, it grew 73%, moving from BRL548.5 million to BRL946.3 million, in spite -- in addition to the over BRL800 million that were declared in dividends and interest on net equity in this period.

In summary, this was another quarter where we presented resilient operational indicators and results that in spite of the economic atmosphere, grew and exceeded the figures from last year and the previous quarter, becoming in absolute numbers, the highest net income, the highest EBITDA, and the highest NOI ever presented by the company in the second quarter.

During this challenging period, we maintained our focus, vision and strategy, pursuing on a day-by-day to improve our malls, to improve the store mix and to promote marketing campaigns and events that could better attract and serve our consumers and therefore our tenants. We didn't stop at all. Also we didn't stop to look for growth opportunities, we prepared our properties and our capital structure for moments like this.

Opportunities emerge in every crisis and we are well prepared to analyze it and take advantage of them, but always taking into -- I'm sorry, always taking into consideration, the profitability and our ability to grow through expansions and new products. I want to thank you. I would stop here, I want to thank you for the trust and attention of all and move to the Q&A session.

Thank you very much.

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Questions And Answers

Operator

Thank you. The call is now open for questions. (Operator Instructions). Our first question comes from Daniel McGoey, Citigroup.

Q - Daniel McGoey

Good morning gentlemen and congratulations on the results. The question on area and same store sales, both segment and retail --

A - Armando d'Almeida Neto

Dan, I am sorry to interrupt, can you speak a little bit louder? We barely hear you here. Thanks.

Q - Daniel McGoey

Okay. Is that better?

A - Armando d'Almeida Neto

It's much better. Thank you so much.

Q - Daniel McGoey

Sure. I'm wondering, The better same-areas sales versus same-store, I'm wondering if you could talk a little bit about what segment of tenant or retail is producing that higher productivity?

And then my second question is, you know, your material showed that the inflation adjustment for rents would have been about 9%, but you only achieved 6%, so a negative difference of about 3%. How much of that is due to negative leasing spread or how much of it is due to tenant turnover or tenants coming in at lower rents than the outgoing tenants or perhaps some type of short-term release you're providing? Thanks.

A - Armando d'Almeida Neto

Thank you. Let me start with the second part or the latter part, Dan, and thank you for your question. This negative same-store rents comes mainly from discounts, from rent breaks, working with tenants to move along this challenging period in Brazil. Okay. The temporary rent breaks that can be reverted at any time.

In regard to the same area sales, same-store sales spread, we've been constantly adapting the mall to better attend consumer demands, bring in the best tenants operations. We've been showing, up to now, positive spread between the same area sales and same-store sales, so this is one of the reasons why we could see through all these challenging days, sales on the positive territory and we think this is a -- it's a great achievement.

And being specific on your question, the service segment was the one that presented the best performance and I have here, I can't unfortunately share in this call the spread sheet that I have, of course. But, looking at the different segments and the specific natures of business in the different segments, we get very impressed to see sectors growing 15%, 12%, 21% in terms of same-store sales, so it's not at all -- not entirely bad news.

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On the contrary, we're seeing many, many different segments and specifically, kind of operations growing double-digits in terms of same-store sales. And I believe that this ability to change the mix on a daily basis, this focus we have in the company, it's responsible for these positive results in this quarter and the past quarters that we presented.

Q - Daniel McGoey

I'm sorry, I'm not sure if I understood it correctly, those double-digit growths are in services segment you are saying over a broader (Multiple Speakers).

A - Armando d'Almeida Neto

No, within, within service segment. And you can see many orders and then the services was the leader in this quarter, in the high single digit, okay, with 8.9% same-store sales, but within budget is, you'd be surprised to see how many operations that go in -- grow in double-digit. That's what I meant.

Q - Daniel McGoey

I'm sorry, within services, can you just touch on some of the highlights, say for instance, you know what within services is working well?

A - Armando d'Almeida Neto

Well, pharmacies, telecom companies, travel agencies, some small clinics and many others.

Q - Daniel McGoey

Okay. Great.

A - Armando d'Almeida Neto

All right.

Q - Daniel McGoey

Terrific, thank you very much.

A - Armando d'Almeida Neto

Thank you, Dan.

Operator

Our next question comes from Ivan Enriquez, HSBC.

Q - Ivan Enriquez {BIO 17654188 <GO>}

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Hello, Armando, hello Franco. Thank you for the call and congratulations on the, as you were saying, resilient results. I basically have two questions, the first one would be within your gross revenue, there is a concept that is service revenues and I understand that you received a non-recurrent payment for managing marketing campaigns.

So can you -- I would think these are designed to bring profit to your shopping centers, but I would like to understand a little bit better, how they work and how would you profit from them, you recorded a 22.5% increase in that concept.

And in that same gross revenue, you have another category of other revenues, can you just remind me what is included in there? And finally, where do you see delinquency rate by the end of the year? Thanks so much.

A - Armando d'Almeida Neto

Can you just repeat the last part of your question, please?

Q - Ivan Enriquez {BIO 17654188 <GO>}

Yeah. Armando, the last one would be, where do you see the delinquency rate at the end of the year?

A - Armando d'Almeida Neto

Thank you, Ivan. Well, just one second, please.

Operator

Sure.

A - Armando d'Almeida Neto

Ivan, so just start with your first part of the question in gross revenue -- service revenue and so, we have a team dedicated to create campaigns, events and we are compensated by that, as you know, we are not owners of a 100% of our malls. So this is part of the service we render to the mall and to our tenants here.

Okay. This is a period of time in which we're investing a lot in creating marketing campaigns, grow more in the shopping center, attracting consumers, and so we got compensated. So, that's why we stamp it as a one-off event, because it was beyond the normal achievement [ph] we had.

In regard to orders, it was basically penalty fees related to lease agreements that hit the income statement in this quarter. In regards to delinquency, very hard to say, we don't like to make any forecast in terms of specific figures. Our view to the second half of the year is, it's positive, it's constructive.

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We take into consideration the quality of the products we have, we've been keeping occupancy very high in the company. So, we'll be keeping a well-balanced in terms of delinquency, in terms of the rental growth, in terms of occupancy rate. So we have a more positive view on the second half of the year, that's all I can say, but it is very hard to forecast specifically, if it's going to be lower or better than it is today, even though we saw an improvement on the first to the second quarter and we are working to improve it further, but depends on -- not just on us.

Q - Ivan Enriquez {BIO 17654188 <GO>}

Okay. Thanks so much, Armando and Franco.

A - Armando d'Almeida Neto

Thank you so much.

Operator

(Operator Instructions) I'll turn over to Mr. Armando d'Almeida Neto for final considerations. Mr. Armando, please proceed.

A - Armando d'Almeida Neto

Thank you. Well, just to share, as we usually do, to some of the question we have in the Portuguese call as well that just finished minutes ago, on top of the questions coming from Citibank and HSBC, in this call, we had some questions related to G&A. If this is the right level to be when compared to this 12.8% growth?

We explained that, that this is what we think G&A should be, but last year was below the normal, because the one-off provision reversal we presented and when you compare year-to-year, excluding this one-offs, we were going to be at 6.7% increase, so well below inflation.

We also got a question in regards and in line with the Citibank question in this call with the same-store sales, but were a little bit more specifically asking on the second quarter in a month-to-month basis. So our answer was that, we saw in the three months of the second quarter, an increase from April to June, being June the best month in terms of same-store sales. We highlighted that in all months we were positive.

So that's very good achievement. Once again, we're very happy to have achievements, on the positive territory in sales growth, especially when we compare the high productivity of our malls already present and we also highlighted that June, due to the temperature change in Brazil in most of the locations, of the regions, so we saw a maximum (inaudible) in terms of apparel, especially winter apparel that can be expanded by the 7% increase in Encore [ph] apparel stores.

We also had questions in regard to new projects. As Mr. Peres mentioned about the project we have here in Rio de Janeiro, in Jacarepagua, if NOI yield would be similar to

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other projects? So, our answer was that we haven't published, we haven't announced the formal figures for ParkShopping Jacarepagua. We haven't announced officially the project yet, but we're working with a 10% to 12% range of third-year NOI yield or yield on cost with a risk of upside potential in some cases. Some of the projects that we're working on, we see an upside potential to that.

And lastly, questions on delinquency and losses, the improvement it was -- any change in the way we collected? And the answer was no. There was no change in the way we collected rent here. But we assume that this improvement was related to a 50 basis point reduction in occupancy cost when compared to the first quarter this year and also through the higher quality of the properties we have, just playing a role here, so -- and being able to recover faster than we thought before.

But I think that's all from us. We remain available for any questions that you might have, in our IR team. Thank you so much for your trust and attention and interest on Multiplan and I wish you a great day and a nice weekend. Thank you so much. Back to you, Operator.

Operator

Thank you. This concludes today's question. Thank you. This concludes today's Multiplan's second quarter 2016 earnings conference call. You may disconnect your lines at this time.

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