Q2 2014 Earnings Call

Company Participants

- Armando d'Almeida Neto, Chief Financial Officer
- Rodrigo Krause, Investor Relations Superintendent

Other Participants

- Paul Jones, Analyst
- Unidentified Participant

Presentation

Operator

Good afternoon. Welcome everyone to Multiplan's Second Quarter 2014 Earnings Conference Call. Today with us we have Mr. Jose Isaac Peres, CEO; Mr. Armando Almeida Neto, CFO and IRO; Mr. Marcello Barnes, CIO; Mr. Rodrigo Krause, IR Superintendent and Mr. Hans Melchers, Planning Manager.

Today's live webcast and presentation may be accessed through Multiplan website at www.multiplan.com.br/ir. 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 Multiplan remarks, there will be a question-and-answer session. (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 circumstance that may or may not occur.

Investors should understand that conditions related to macroeconomic scenario industry and other factors could also cause results that to differ materially from those expressed in such forward-looking statements.

Now, I'll turn the conference over to Mr. Rodrigo Krause in the name of Mr. Peres. Mr. Rodrigo, you may begin your conference.

Rodrigo Krause

Good afternoon, everyone. Dear shareholders, it is with great satisfaction that we disclose our quarterly results, which are above our best expectation. We will make a brief analysis of our strategy and Multiplan's performance for the next years.

Firstly, I would like to highlight the most relevant main financial indicators. Gross revenue, this quarter increased 13.5%, reaching the amount of R$298 million. The EBITDA reached R$187.1 million, an increase of 25.6% over the same period last year.

Net income was 32.7% higher, reaching the sum of R$93.4 million. And finally FFO which presented R$143.9 million, a 31.5 increase greater than the same period in 2013.

Notwithstanding the difficulties we are living through in the macro economic scenario, we have plenty of days impacted by the FIFA World Cup games in Brazil, interfereing in the commercial activities in the main cities in which we operate.

Regardless to say, our sales didn't drop, start growing at a double-digit pace growing 15.2% on top of the second quarter of 2013.

Other noteworthy points are as follows. At Village Mall sales increased 92%. Furthermore, the ICSC considered it, Village Mall as the best project in Latin America in 2013, a fact to be proud of.

As Village Mall, other shopping centers recently inaugurated performed well in sales, 28.4% increase JundiaiShopping and 22.4% for ParkShoppingCampoGrande.

More consolidated shopping such as Morumbi and Ribeirao had significant sales growth of 20.4% and 16.5% respectively.

Results like these encourage us to continue to stick to our strategy of new Greenfield. We are currently developing another three new shopping centers, ParkShoppingCanoas with 48,000 square meters of GLA in the state of Rio Grande do Sul. ParkShopping (inaudible) with approximately 42,000 square meters of GLA in Rio de Janeiro. And ParkShopping Global with approximately 80,000 square meters of GLA in the City of Sao Paulo and should be built in two phases.

We have the potential to develop about 300,000 square meters in new areas for lease, which corresponds to roughly 53.3% of our own GLA. Half of this number will come from three new shopping and the other half from expansions in existing developments.

In Rio de Janeiro we are working on a future expansion of Village Mall, along with a new complex of office space and corporate floors. For these projects, we will disclose more details in due time.

These are some of the opportunities that are being developed. I will now address a part of our business that completes our core business and exploits the long and profound relationship Multiplan has in developing a mixed-use project.

In their great majority, these are projects mostly destined for sale. We included in our report this quarter, not only the Land Bank, but also the private area of each lamp flat, which will be integrated to our shopping centers. These projects are equivalent to about 1 million square meters of private area.

These properties are located around our shopping centers, most of which in contiguous areas of great urban development and guarantee appreciation. Just as an example, if we consider conservatively 8000 reais per square meter in sales, we have a potential value of approximately R$8 billion to be realized in the next years.

As you already know, we are not only a company that launches one real estate development after the other.

This is not the model we believe in, has been the best for Multiplan. We take advantage of opportunities as markets become receptive to our project. We continue to be prepared to do more, however, within the financial leverage limits we consider comfortable.

In this sense, it is with great satisfaction that we mentioned that Multiplan is one of the 11 national companies rated by Standard & Poor's as having a better risk rating than the sovereign rating of Brazil and the only one in the civil construction sector with an investment grade.

In 2015, we completed 40 years in business in Brazil and abroad. We were the pioneers and innovators in many projects we delivered. For these and other reasons, Multiplan will continue to invest in its strategy in search for new opportunities, with new lease projects in a creative and consistent manner, aiming to offer its consumers, clients and tenants and always inviting environment with Multiplan's quality standard.

Quoting a young consumer when asked why she comes to buy her shopping every day, she answered, and I quote because I can run all my daily choice here. Our shopping centers have become more and more true places [ph] in the middle of urban chaos, worsened by the lack of mobility in the main cities in Brazil.

Throughout the years we are becoming a solution to the big urban problems, especially when we implement mixed-use projects as are the cases of Barrashopping in Rio de Janeiro, of MorumbiShopping in the city of Sao Paulo, of Ribeirao shopping in the city of Ribeirao Preto and many others where we put together a single nucleus of activities such as services, leisure, trade, hotels, even a medical center, making sure that the quality of life continues to improve.

I will stop here, but not before I thank our executives, employees, the team with which together we dedicate ourselves to the growth of Multiplan, without losing one of our most important tenant that of quality and doing things as best as possible.

I also thank our shareholders, investors, analysts and journalists for their trust and interest in Multiplan.

I now hand the floor to Armando for a more detailed presentation of our results and to answer your questions. Thank you very much. Armando?

Armando d'Almeida Neto

Thank you, Rodrigo, Thank you, Mr. Peres. Ladies and gentlemen, good morning. We will start our presentation with the operational performance on slide number four.

Following in the steps of a strong growth in sales in the first half, in the first quarter, our shopping centers accomplished a growth of 15.2% over the second quarter 2013. The highlight goes to RibeiraoShopping with a 20.4% increase, strengthened by the expansions delivered and Morumbi Shopping after the change in mix, reaching a 16.5 increase in sales.

We started the second quarter with many uncertainties, among which the facts of FIFA World Cup on sales and the implications of company's economic growth also with their sales. In spite of the reduction in consumer flow during the Brazilian team matches, sales increased before and throughout the event, leading to the highest same-store sales in the last three years.

This was certainly a strong growth, but even stronger was the figure presented for same area sales of 12%, the highest mark growth since the fourth quarter 2010. The three shopping centers inaugurated in the fourth quarter 2012, Village mall, ParkShoppingCampoGrande and JundiaiShopping presented sales growth of 45.7% on top of sales last year, especially Village Mall with a increase of 91.8%.

On page five, we show on the chart to the left, the top left, the consolidation process of these developments, rapidly reducing the gap with consolidated shopping centers of sales per square meters to 38%, what was 112% in the first quarter of 2013, big difference from consolidated to new malls sales per square meter became 38% gap.

It is also worth noting that the sales per square meter in the second quarter 2014 for those new malls surpassed those of the fourth quarter '13, two quarters before which is traditionally stronger due to the Christmas season.

The strong growth sales lead to the reduction in occupancy costs as can be seen in the chart on the top right, falling 100 basis points when compared to the second 2013. Another topic to highlight is the occupancy level of shopping centers, which improved 80 basis points compared to the second quarter '13 and remain in line with that figure of the first quarter 2014 at 98.4%, in spite of the increase in GLA throughout the last few years.

Since I mentioned occupancy rates, I would like to say that Morumbi Corporate in the presentation here, Morumbi Corporate the twin towers we have across the street from

Morumbi Shopping Sao Paulo has already leased 65% of its GLA and contributes with a $10.1 million as rental income in the second quarter.

Speaking now of gross revenues and moving to page six, they increased 13.5%, together parking and rental revenues represented 75.4 of the total revenue, presenting a 21.6% and 25% growth respectively.

On page seven with more details regarding rental revenue, the campaign is related to the FIFA World Cup pushed growth of 32.2% in merchandising revenue, the specialty income. Both the fixed rent in average showed an important growth of 20.7% and 21.8% respectively, creating a positive impact in same store rent, which benefited from strong sales.

Growth in same-store rent was 10.1%, exceeding the adjustment inflation, adjustment effect 4.1%, a very strong real growth coming mainly from the contribution of the consolidated shopping centers.

Village Mall and I'm going to be back on the normal rental revenue. Village mall presented an outstanding performance with rental revenue up 46.1%, RibeiraoShopping with 35% increase in rental revenue and ParkShoppingSaoCaetano with 23% and last but not least, ShoppingBarigui were 18.3% increase.

On page eight and moving to the main expenses lines. Shopping Center expenses was 27.8% lower than in the second quarter 2013, as a result of the beginning of the consolidation of the new shopping centers.

In the first six months of the year, we reduced shopping center expenses by 15%, when compared to the same period previous year 2013.

It is worth mentioning that in that period we also increased own GLA, more GLA 7.6%, in which the natural effect would have been the increase in shopping center expenses. There is just an example of the (inaudible) of the company to having those malls consolidated and be more efficient, right?

Also G&A head quarter expenses fell compared with Q2 2013 by 1.7%, accumulating an increase when you look at the first six months figure of 7.9%, when compared to the year before. And was the G&A expenses was fully covered by the revenues from services, mainly mall management.

In a summarizing manner on results on page nine, the reduction in expenses combined over the increase in revenues, lead to a important margin improvement in NOI and EBITDA exceeded a 20% mark in the quarter.

Even though, this is not mentioned in this presentation we don't have a picture showing what we're going to mention now, it's only in managerial report, published in the earnings release. I call your attention to the compounded average growth rate for the last five years of EBITDA and we look at the last 12-month figures here.

They reached 21.4% CAGR and compare it to the growth of our shopping center on GLA in the same period. There was a 11.2%, that proves the strong value creation and we almost tripled the EBITDA, the last 12 months EBITDA which in June 2009 was of 160 million,

R$260.7 million and jumped to R$686.1 million in the last 12 month's figures for June 2014, almost three times what it was in the same period 2009.

Wrapping up my comments on results on page 10, FFO presented a strong increase in value of 31.5% and also in margin of 673 basis points, up to 52.8% and was assisted by the announcement of interest on shareholders' equity that we announced the end of June. And also due to the small deleverage of the company that will mention in a few slides ahead.

In the same analysis we use for the EBITDA the last 12 months of EBITDA, the last 12 months of FFO more than doubled in five years, even with strong investments made that we levered the company further for that, that moved from R$229.7 million in June 2009 up to R$487.2 million in this quarter.

Net income increased 32.7% in the quarter, accumulating R$175.7 million in the year, in spite of the non-cash impact, the non-cash increase of depreciation of 38.2% and also the increase in interest rates, the effect of higher interest rates.

On the following page in the number 11, a quick snapshot of the evolution of company margins during 2007 through the first half of 2014 that reflects the effort of our company to increase the results, to increase our own GLA and also to enhance our efficiency.

On indebtedness and leverage on page 12, we show that we reduced it slightly our leverage from 2.94 times net debt to EBITDA in the last quarter in the March '14, down to 2.81 times in the second quarter 2014. The company's net debt represents above 12.5% of the fair value of properties, not considering areas that are recorded as inventory and therefore not part of the calculation of fair value, most of the Land Bank will be classified as inventory.

An example just to illustrate how we managed indebtedness in the past two years. If you look at the picture below on page 11, on page 12, if you look at the fourth quarter 2011, the basic interest rate we call the Selic Rate in Brazil was also at 11% and average cost for the company was 8 basis points higher at 11.08%.

With the end of the second quarter 2014, the basic rate is the same 11% and the average cost now at 10.5%. So basically, 50 basis points lower than the basic rate.

So what I'm trying to show here is that we, in terms of average cost of gross debt, we were able to reduce 58 basis points in this period when compared fourth quarter '11 through the second quarter 2013 to an annual of course, right.

On the following pages we're going to show as mentioned by Mr. Peres, a few of the new developments. We shows sketches of our parking global project is the new announcement of our land swap in the city of Sao Paulo. We are excited about the development of this new project in the state of Sao Paulo that we plan to start with 16,000 square meters in GLA in a mixed used project that will provide us with opportunities to grow in this important city for a long period of time.

On page 14, we have also a sketch of ParkShoppingCanoas, our most recent product in the pre lease phase. We will have the 48,000 square meters of GLA in its initial first phase.

On page 15, you see pictures of the recently delivered VII Expansion in BarraShopping in Rio de Janeiro. There we added new important international national brand, in addition to underground parking area with over 600 new spots, with a better quality of parking spot. In the upper floors, we are expanding the medical center that we have in BarraShopping, an area that is quite demanded in space and by also by consumers and which combined with the retail operation and the VII Expansion make BarraShopping even stronger.

On page 16, there is a picture of BarraShoppingSul mall in the city of Porto Alegre with two new towers that are in finishing phase and will shortly add to the floor of consumers to the shopping centers.

Last but not least on page 17, as mentioned by Mr. Peres in our earnings release this quarter, we provide a better disclosure of our Land Bank for reservation and (inaudible), as part of our strategy to develop mixed use products. I hope that is additional details provided, made us issuing better understanding the company's growth potential.

We couldn't conclude this presentation without mentioning our satisfaction, you've seen the resilience of our properties.

Even in moments of uncertainties contribute with strong result and further stimulate us to pursue our development strategy. Due to many questions regarding the impact of the FIFA World Cup, we produced a brief case study of its effect on sales of our portfolio and can be found on our earnings release report.

We thank you all for your support and the interest and I'll now open the lines for the Q&A. Thank you very much.

Operator

Okay. Yeah.

Questions And Answers

Operator

Thank you. (Operator Instructions) Our first question comes from Paul Jones, AEW Capital Management.

Q - Paul Jones {BIO 17898473 <GO>}

Yes, thank you for taking my question. Just going back to the shopping center expenses in way you've been able to contain cost is worrying now. So the 11% or so, from 11, 12% of shopping center net revenue, is that a good ratio as I think about what the expenses relative to revenue should be going forward?

A - Armando d'Almeida Neto

Paul, how are you? I think we've been able to improve significantly the shopping center expenses margin throughout the quarters. But as the new malls get consolidated, I think we can do even better.

Don't forget and we're dedicated to develop newer shopping centers, so we might see more expenses coming in the future years to come above the very decent revenue base. So I look forward to see margins better than that, but I think we have to recognize the reduction in the shopping center expenses margin throughout the quarters.

Q - Paul Jones {BIO 17898473 <GO>}

Okay. So what you're saying is that where it is now, but as I'm thinking three or four years out, we could see continued improvement in that numbers as you consolidate more assets?

A - Armando d'Almeida Neto

What I try to say that I think on the short run, I think on the coming quarters, over next year at the new malls that were delivered in 2011,'12 and '13 getting stronger, more consolidated, the need which shopping expenses should reduce especially with the marketing, with vacancy, with common costs for vacant areas.

So I expect to see improvements on that, a lower shopping center expense margin. When I look four or five years ahead, our revenue base will increase a lot, I now see that the margin would deteriorate.

But we're just saying, we will have new shopping centers and those new shopping centers will consume some investments after it's opened. So shopping center expenses there should increase a little bit just to help consolidated. But I don't think that you will see on the margin a deterioration because your rental, your revenue base will be much stronger. So I think we can do better than that. That's my view.

Q - Paul Jones {BIO 17898473 <GO>}

Hey, great. Thank you.

Operator

Okay. Our next question comes from David Think [ph] First State Investment Management.

Q - Unidentified Participant

Hi, good morning guys. Just wanted to get some color about your development yield of the three developments you're currently doing, probably also getting in touch with say, some color when it's not going to be pre-leasing and how you are going to forecast pre-leasing. Thank you.

A - Armando d'Almeida Neto

David, thanks for your question. Well the -- we haven't changed our mind in terms of the expected returns. As you know, we like the IRS and on leverage as a way to measure returns on the long run and which you expect to see a 15% real and levered returns to the new developments, that's our goal, that's what we're trying to reach.

It's getting tougher, yes, it's getting tougher in Brazil nowadays, but we think as doable, feasible otherwise we wouldn't launch. What we announced, we announced that the acquisition or the land swaps in new sites, but the only project that we provided the detail so far was one turnover in the south of Brazil.

This mall is under the pre lease phase, we haven't announced the total investment in the shopping center yet because we are detailing the product, we had contractors. So we don't have the final budget for it, we will do as soon as we engage in the construction phase that we are not there yet.

The early results from the prelease phase be very exciting, very good and fast demand for space in the shopping center, but not an office due for us make us move and had contractors starting the construction work. We will do that. We normally try to get about 15% of GLA and a balance between anchors and satellites to start the construction before we engage in the construction malls.

But it seems good, I mean we've started with early results from turnovers. In regards to the other projects, we have a mall in Rio that is under approval phase. Another one is San Paulo, Parque Global also in approval phase, those are talking about new Greenfields.

So there is no much to say, we will address that after we get the approvals and as we start pre-leasing those new profits.

And also mentioned by Mr. Peres we have other product expansion of malls. We have some approvals, some under approval phase, but we are not touching that yet, we are waiting a little bit more.

Q - Unidentified Participant

Okay. Thanks,

A - Armando d'Almeida Neto

Thank you, Dave.

Operator

(Operator Instructions) I'll turn to Armando d'Almeida Neto for final considerations. Mr. Armando you may give your final considerations now.

A - Armando d'Almeida Neto

Well, just before my final thoughts, just to share, just a couple other questions regarding the Portuguese call, in regard to margins of new shopping centers, is there room for margin improvement and the answer is yes.

So one analyst asked us about what is the margin of the new shopping centers. And with that is on the range of 75 to 80%. So and the new shopping centers announced, (inaudible) and CampoGrande the ones delivered on the fourth quarter 2012, when you compare that with every margin of the company, that is closer to 90% 88 and change. So you see that we have room for improvement, and that won't conclude in the new malls, hopefully we'll boost further the average.

Another question in regards to occupancy cost is was there was -- the 100 basis points reduction in occupancy cost was due to lower common expenses in the shopping center. And we explained that the lower occupancy cost was mainly due to higher sales, was the impact of higher, stronger even than expected I should say sales effects on the both common expenses and rents as a percentage of sales.

So just to share that with you, that is also important to discuss on the macro economic scenario nowadays a seasoned company like us, Mr. Peres mentioned, we're going to be the four year anniversary of the company next year. So we're seeing a lot in Brazil and we saw the inflation was 67, 80%, but from north per year, not per annum.

And we saw there was no funding available. So what we're going through right now is much better than what we saw in the '80s and the early '90s in Brazil. And so we are confident that even in this more challenging scenario compared to a couple of years, a few years ago we can grow further, based on the quality of our portfolio, we try our best to make our malls better and better always focusing on consumers, always focus on consumers' needs and trying to anticipate the trends, new operations, as you saw recently in our malls mainly new comers to Brazil coming to our portfolio and creating a significant impact in sales, of course, its impacting sales.

So with that in mind on behalf of Mr. Peres, I want to thank you all for your trust and confidence and for your interest on our company and just say that thank you very much. We remain available for any questions in our IR department or myself if you need. Thank you very much and have a nice day.

Operator

Thank you. This concludes today's Multiplan Second Quarter 2014 Earnings Conference call. You may disconnect your lines at this time.