Y 2017 Earnings Call

Company Participants

- Armando d'Almeida Neto, Chief Financial and Investor Relations Officer
- Jose Isaac Peres, Chief Executive Officer

Other Participants

- Enrico Trotta, Analyst
- Gustavo Cambauva, Analyst
- Marcelo Motta, Analyst

Presentation

Operator

Good morning, ladies and gentlemen, welcome to -- welcome everyone to Multiplan's Fourth Quarter of '17 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, Investor Relations and Planning Director; and Mr. Franco Carrion, IR Manager.

We would like to inform you that the presentation that will be made will be available for download at ir.multiplan.com.br. We would like to inform you that participants will be in listen-only mode during the conference. Afterwards, we will have a question-and-answer session, when further instructions will be given. (Operator Instructions).

Before proceeding, we would like to mention that forward-looking statements that might be made during this call relating to business perspectives of the company, operating and financial projections and targets are beliefs and assumptions on the part of Multiplan's management as well as information currently available to the company.

Forward-looking statements are not guarantees of performance, they involve risks, uncertainties and assumptions. Therefore they referred to future event and therefore they depend on circumstances that may or may not occur.

Investors should understand that general economic conditions, industry condition and other operating factors may affect the future results of the company and lead to results that differ materially from those expressed in such forward-looking statements.

Now we'd like to turn the conference over to Mr. Jose Isaac Peres, CEO, and he will start the presentation. Mr. Peres, you may proceed.

Jose Isaac Peres {BIO 15388489 <GO>}

Good morning. Good morning, everyone. Ladies and gentlemen, it's a great pleasure to be with you again. I will try to read more slowly, because we have simultaneous translation. And I'm not going to leave my text. I have a few changes here, but afterwards, we will talk about that. And I'm just mentioning this, because normally for very often, I see things that are not in my prepared text, and that I being convenient. But I will have more discipline this time, and we will have a simultaneous translation in English to the benefit of our international investors.

So what I wanted to say was the following. 2017 as we had anticipated would be a year of recovery. Taking into account, the radical change in politics, much better structured before the rebound of the economy and fiscal equilibrium. Therefore or nevertheless in 2017, some business [ph] political fact happened. And they were published in a very sensationalized and reckless fashion in my opinion. And therefore, they hinder the economic growth that already was certainly some recovery, just to show you how the Brazilian economy was affected, I can mention the impact of that on the retail sector, in which, we include our sales, we started 2017 with two-digit growth or 12% in March and 11% in April.

And after the public prosecutor's office demonstration, the economy came to a halt and we dropped to one digit and we only started again to see an acceleration of the economy in the last quarter and in spite of all this turbulence in the sales in Multiplan shopping centers obtained a 7% growth and rental revenue growing by 8.4% and the company obtained net income amounted to BRL317 million, 18.4% higher than the previous year.

In spite of the major political crisis that had took the country by storm as of May. And for this year, we expect a more robust economic results due to the fact that we find ourselves in a more adjusted economy with an inflation rate of about 3% and unprecedented interest rate in the country that is to say 6.75%.

We are always seeking new investments new opportunities as you know. And in 2017, we invested BRL450 million in expansions and new project. And another important fact that I would like to mention is that for many years, we have already been developing a technology, seeking a higher operating efficiency and also looking for digital models. And to increase our efficiency in 2017, we started negotiations with an IT company, which is very much focused on e-commerce, and in that sense, we established a partnership by acquiring a 20% stake in the company, and we could go up to 30% and we are talking about Fulllab, a company that has as its main activity, the development of technological solutions applied to digital retail. We are integrating the expertise of Multiplan's digital innovation team with the knowledge, tools and technologies, developed by highly experienced professionals in e-commerce. And our objective will always be to deliver more convenience and more services to our customers and tenants as well.

And ultimately, what we wanted to bring to the homes of our consumers, all the retail array that we have in our shopping center, always focusing on Rio [ph] trade commerce. And we believe that growth of retail going from Rio to virtual could accelerate sales in the shopping centers themselves. Because technology and e-commerce will change the results that we obtain and we know that we are giving very important steps and that will bring more comfort, more ease to our consumers, and we understand that the shopping centers will sell more, because of this digital technology. And I would like to mention also that the model that we are building in Brazil or have been building in Brazil for a long time is a product, that is totally different from the others that exist abroad, mainly the United States. These are products that are focused on pleasure and give our consumers an appealing environment, making them much more of a meeting point or safe meeting point, where they can carry out many activities.

And we add more and more services. We recently -- in June last year, we inaugurated the Ribeirao Preto Shopping with 32 clinics and medical center, and we are renewing our vision applying all our current knowledge of the construction of ParkShopping Canoas supported by a tripod, nature, entertainment and shopping. And in Canoas, we inaugurated that with a spectacular success to the extent that we were awarded, [ph] because of the size of our parking facilities, and the first 30 days were fantastic sales higher than our estimates.

And now I would like to mention the fact that we started to build the shopping center in 2015, and we inaugurated in 2017, when we were braving the biggest economic crisis in the history of this country. And I want to mention that, because we want to reiterate that we opened the shopping center with 90% of the stores already in operation. And it was a record, when no shopping center inaugurated in this country in the last three years was capable of such feat. Thus motivated by the results obtained, we made a decision to start building [ph] 2017 as we had already announced, and I would like to reiterate that it was very good to start this in 2017.

But I want to say that in December, we already started to build these facilities, and we estimate this to be concluded in the next 24 months. And finally, my friends, I'd like to mention that in this country, if we were to wait for the crisis to go away, we wouldn't have done practically anything, because in the last 50 years, at least of which I have been living, we have had over 10 different crisis of different dimensions and proportions and nature. But what is really important is that Brazil continues steadfast as a nation and as a democracy growing. And thanks to the efforts made by the current administration, today, we find ourselves in a country that was able to recover the confidence of both Brazilian and international investors, and we hope that Brazilians in the next elections will be able to choose a new Congress and a President that are sufficiently sensible and committed to the development and also to the reforms that were and remain to be made in order to guarantee a sustainable economic growth and a socially more equitable society.

I would like to thank the Multiplan team for the very hard work done this year, which helped us to deliver this outstanding result. I would like to thank all the investors that have placed their trust in us. And now, I would like to give the floor to Armando, who will be talking about our figures. Thank you very much.

Armando d'Almeida Neto

Thank you, Peres. Good morning, everyone. With the announcement of the results of the fourth quarter, we realized that we are already in a new year and with the country resuming economic growth, and this brings us a lot of satisfaction, because we see the results breached in 2017. And by the way, with a lot of satisfaction, we see that sales in our shopping centers continue to grow in all quarters, even during the last few years when the country was braving a very strong crisis and the company remained profitable, delivered extremely high financial and operating margins and did not stop investing and improved even further property acquiring interest and developing new areas, looks like we've made it.

While many said that this could not be done during the worst of the crisis, Multiplan delivered a new shopping center plus five expansions between 2015 and 2017. We exchanged approximately 1,100 stores corresponding to an area of the 106,000 square meters, maintaining a high occupancy rate in our portfolio.

Recently in January 2018, we disclosed the preliminary data for the fourth quarter and we heard that growth was lower than expected, and we certainly respect everybody's opinion. However, I would like to present our opinion here. What would be better to have a lower comparison base in the fourth quarter of 2016 to show a higher percentage growth in 2017? Certainly, we do not consider this as right. As we said, we grew in all quarters in 2017, '16 and also '15, '14, '13. And this was what happened since we became a listed company in 2007. 43 quarters delivering, growing shopping center sales, and we are very proud of that.

And another point, we assess that, is that very often, analysts [ph] focus only on same-store sales neglecting the daily task of property management and change of mix, reflecting same area sales. In 2017, sales grew by 6.8%, same-store sales 5.2%, over 2.5 times what we had in 2016, and same area sales growing 6.6%, twice what was obtained in 2016. And consumer inflation was 2.95%, and this growth is real, it is strong. And it was obtained over a very high base already.

Our shopping centers had 97.4, average occupancy rate, opening 57.6000 [ph] square meters in the year, basically concentrated in the fourth quarter. And the occupancy cost was stable, 12.9%, delinquency went down and the gross revenue of the company grew by 3.9%, with rental revenue being the biggest part, representing 77.1% of the overall gross revenue.

Rental revenue grew by 8.3%, with same-store rent 7.1%, the real increase of the effect of the IGP-DI adjustment that was 6.5% in 2017, and this increase would be even higher when compared directly to the IGP-DI of 2017 that was negative by 0.4%.

In the fourth quarter, we had the biggest real growth, because this -- it went back to real growth, that didn't happen in 2016 that was 2% and expenses were 40.2 million higher or 12.9%, and basically the effect of the mark-to-market of Phantom stock option and expenses with new projects, as well. Here, concentrating in the opening of the ParkShopping Canoas, there are expenses related to the launch of new areas, as you know that cannot be activated causing a distortion in the quarterly result.

And the headquarter expenses and shopping center expenses were lower by 4.4% and 0.4% respectively. In relation to the shopping center expenses, I would like to remind you that we grew GLA by 7%, and even in spite of that, we were able to get a small reduction and commenting about the result, the NOI was 8.4% higher with the margin increased to 87.6%, exceeding BRL1 billion.

EBITDA 0.9%, due to one-off non-recurring expenses, as I said a while ago. If for analysis purposes, these expenses were to be excluded, EBITDA would grow 5.7%. FFO and net income grew very steeply, 15.3% and 18.4%, respectively.

In 2017, FFO reached BRL558.5 million, and net income as Mr. Peres said, BRL369.4 million, both with the good performance in our margin and the strong increase is due mainly to operating growth and the drop in interest rate and also the payment of interest on equity.

In 2017, we returned to our shareholders the highest amount ever paid out BRL440 million, representing also the highest percentage over the net income, which was 68.3%. In 2017, we invested BRL449.6 million, allocated mainly to the development of new areas.

Together with that, we had the distribution of results that I have just mentioned, and it is evident, our continued strategy to optimize capital allocation. And this is made possible due to the stable financial situation and strong cash generation that Multiplan has. Net debt corresponded at the end of 2017 to 2.34 times the EBITDA, very far from the covenant and representing only 11.3% of the fair value of our properties.

In the last two years, we accelerated our borrowings back [ph] to the CDI, which allowed us to better take advantage of the drop in interest rates, and the average weighted cost of our gross debt is 8.24% a year, with an average maturity of 49 months. The amortization schedule is distributed over the years with no major concentrations, and we are up to now -- we are up to now lower than the cash generation measured by the FFO of 2017, not considering our cash position that we have in our balance sheet.

We have an in-house evident [ph] which Peres speech when he inaugurates a new shopping starts with in spite of the price as well in Canoas this was more than deserved, and we are very proud for having launched and delivered a new shopping center during the biggest crisis in the country and what seemed almost impossible became reality, as a result of our strategy, our effort and the dedication and capacity to invest. We inaugurated the most modern shopping center in the country, integrated nature to entertainment and shopping.

We opened with 90% of the area already in operation, and this figure has already gone up and at the end of January, it was already 93.4%. And before closing, a brief note about the performance of our shares, going up 19.4% in 2017 with higher liquidity, with average daily trading volume of BRL52.1 million, 32% higher than in 2016. Entering these 10 years as a listed company, Multiplan implemented its growth strategy with a clear focus on what is best for the company in the long run.

Now, I thank you for your attention and your trust. And I would like to open for questions now. Thank you very much.

Questions And Answers

Operator

Thank you very much. Now, we will start the Q&A session for investors and analysts. (Operator Instructions) Mr. Gustavo from BTG Pactual.

Q - Gustavo Cambauva {BIO 17329406 <GO>}

Good morning, everyone. I have two questions. The first one is about how you see the possibility of increasing what you charge for parking. In 2017, you didn't make any increases in this price, and it was flat, so is there a possibility or intention on your part to increase the price for parking in some of your parking center -- some of your shopping centers?

And about Mr. Peres initial remarks, I would like to know your outlook for new greenfield today. I know you announced Jacarepagua, and on one hand, the economy is improving, but on the other hand, we see quite a lot of area being added to shopping centers. And now with the challenge of e-commerce, I would like to understand whether you are still bullish to continue building new greenfield shopping centers with this scenario. Thank you.

A - Jose Isaac Peres {BIO 15388489 <GO>}

Gustavo, good morning. I will answer your question. Parking is not the object of the company, and parking is only charged in this country. Nobody ever did that before, if I do not explain the context, you will not understand the answer. Parking lots were franchised, and we had a lot of problems with theft in the cars, and because of that we came to the conclusion that we had to have a higher control and give more security. And because of the situation that we have in the country regarding public security, we had to create parking facilities and charge for that, so that we could give our tenants and everybody a high degree of safety. And I can say to you that part of what is charged for parking is shared in order to reduce the cost of operation of the shopping center.

So I would like you to understand that parking is not an end, it's just a need and it would be great if we could not charge anything, and that Brazil were a country like some others that don't charge and they only have two security people, and we have about 200 people doing this kind of protection. So this is the first point.

About increases, there were some very small cases, but let's not give a bigger step, because we are about to leave a crisis. We are leaving the crisis behind, and for this year, we expect a higher recovery and the figures are improving. And I think this year will be better. And we have Jacarepagua that we include a shopping center for 40,000 meters of gross leasable area. And in Canoas, as you know, our focus was on entertaining, and nature, and shopping and this is a model to mitigate the fact that the current society mainly, youngsters are becoming more and more interactive, and they look for more and more interaction. So we have to think about shopping centers in a different way, because shopping centers are the place, where the person -- it was a -- it used to be a place, where people just went there to buy something specific, but now, it is much more of a meeting point, so people like to go there, and there are movie houses, and they go there to eat and to have fun. And this is the model that we are building in Brazil.

And recently, we had a workshop with some international consultants, and I was very pleased to hear from them that, the happy [ph] Americans made shopping centers like the ones that we are doing in Brazil, they would not be facing a crisis today. I don't know, whether I have answered your question, but we are going to do many things, expansions, we have not announced yet, but we will do this, I don't know whether I have answered your question or not.

Operator

Mr. Marcelo from JPMorgan.

Q - Marcelo Motta {BIO 16438725 <GO>}

Good morning. I have two questions. Could you give us some additional color about Fulllab, CapEx and relevant investments for the next few years in order to have this integration with Multiplan. And will this generate an increase in sales, and do you have a target for that? And could you talk about the scenario in Rio, I know it's too early to say, but have you received any changes in traffic -- in visitors traffic in your shopping centers?

A - Jose Isaac Peres {BIO 15388489 <GO>}

Marcelo, visitor flow has been increasing in the first month, exception made to February, because we had carnival in February, and last year it was in March. But in spite of carnival, visitor flow was positive. And Rio as everybody, knows is under federal intervention, and in a way it was positive for Rio. In spite of the fact that, Rio has not the highest criminality rate in the whole country, there are many other cities and states that have worst data than Rio.

Our problem in Rio is that the publicity that is given to criminality not always corresponds to the Rio fact, but those who are not in Rio, those who are outside Rio, they have the sensation that they will come to Rio and they will have to wear a bulletproof vest and a helmet, and that is -- there is a war they wage, but this is not the reality.

Even in the United States, there are wagons, where cities are more or less like that, but of course, with the economic crisis in Rio, this will became deeper and not paying policemen salaries is a big problem. I would like to tell you that we have already been through many crisis in the state with higher rates of violence. And I think that from now on, we will be recovering this and overcoming violence, and Rio will once again be seen as the beautiful city that it is, that's attracting tourist et cetera.

Today, traffic in Rio is better and subway comes to the Barra region much easily. And if it were not for this very unpleasant situation of safety in Rio. And also due to the fact, that the state is broke, it went down the drain, because of the oil situation when the barrel reached $40 in a way of the revenue of the state was reduced.

But this year, we believe that there will be a better level of fiscal equilibrium. And we hope the situation improves in Brazil. And our figures are not bad for Rio. And it is important to mention that when we talk about Rio, Rio has -- I don't know how many square kilometers. But we are concentrated on the West zone of the Rio, this is the fastest growing region in Rio. We will have shopping, we'll have VillageMall and CampoGrande. So maybe Armando could mention this.

But we want to show you that Rio is not as bad as people think. Rio grew more than our average in Sao Paulo and in Belo Horizonte and as an average -- when we look at the individual group, we see 10.3% in BarraShopping, CampoGrande 16.8%, so it's quite the opposite. Our performance in Rio was very good. In spite of what has already been said.

Last year, we started to talk with some people in e-commerce, and we have our digital innovation team in-house, and we have an independent company that work for third-party, and I look at this company, a profitable company. And so we decided to make this investment in this company initially 20% stake and possibly going up to 30%, it was an investment of 7 million, it was not the big one, but very important in terms of placing our team closer to e-commerce professionals, and bringing more knowledge, more market knowledge and the way it operate.

And my feeling about Rio commerce and virtual commerce is the following. Many companies started with e-commerce and they decided to go to Rio commerce, and it has to do with distribution centers, which is one of the big problems that some of these companies face, and many of these companies e-commerce companies present results much based on the expectation of future results.

And with the price profit ratio of 200 or 300. We understand that having Rio commerce is something very good, but human nature is not going to change the need for contact, the need for human warmth, and being together with other people, and we have the feeling that by having a cell phone, you have the feeling that you have lots of people around you. What I view now is that people are suffering in fact, and what we want to give is joy, is happiness, and I welcome the opportunity to tell you that, of course, we want to grow in Rio commerce as well, but with e-commerce, we want to bring to the homes of our consumers, the whole array of products and services that maybe later on delivering, but this will represent a real increase of about 15% to 10% -- 10% to 15% in our shopping centers. Of course, it's not going to be a quantum leap, this is not the way things happen. And it's easier to go from Rio to virtual than the other way around, okay?

Operator

Enrico from Itau.

Q - Enrico Trotta {BIO 16742911 <GO>}

Good morning Mr. Peres, and Armando. I have two questions. You talked about the maturity of contract, and looking at 2018, the expectation is that about 11% of the contract in terms of gross leasable area would come to an end. So how much do they represent not in gross leasable area, but in terms of revenues?

And could you talk about your expectation about renewing, when we talk about the rent per square meter. And the second question has to do with debt. You have about 35% concentrated in TR lines and the cost of debt is higher than the CDI line. So I believe you still have room to decrease your exposure from the TR or the reference rate to the CDR. So I would like to understand a little bit of this side of opportunity for further reductions, for the cost of debt.

Thank you.

A - Armando d'Almeida Neto

This is Armando speaking. Thank you for participating in the call. I'm sorry for the delay in my answer, because I was looking for the page, where you can find this information relevance of that. And in 2018, 52 of the 11.2% of the GLA coming to an end, 14.4% of our overall revenue. So there is no big distortion, and our expectation of contract renewal is positive. We see shopping centers quite full of consumers and some stores and some tenants with expansion plans. And I think you saw that thousands of stores are planning to open, and this is being announced by the tenants club of (inaudible)

And talking about major operators, we see that they want to improve the portfolio and increase space together with an occupancy rate, that during all of these challenging years remained very high. And as you saw in our presentation, and the renewal of these operators will be by means of new business models and new segments, such as we have been doing over the years.

In relation to borrowings, financing, your view is correct, when you look at average cost in base rate TR is 9.2% something like that, and when we look at the (inaudible) at 6.75, it seems to exist a very good opportunity. But when you look at the curve of interest rate and prefix for five years and seven years, they will give you a duration more similar to the contract that we have in TR [ph] and when you look at that, you can see that they are 9.7 -- 9.5 depending on the duration.

So the path is not so clear, if you take this into account. So if the company believes that the drop in interest rates will accelerate even further, and as you can see when you look at two, three years ago, the drop in financing, we were able to cross a period of high interest rates with our financing in TR, and so the average or the gross, the weighted gross average debt would be -- was lower than the CDI, and there we had a big gap between this and the CDI. And now with 12, 18 months duration, we were able to get a very strong reduction in this cost and taking advantage of the lower interest rate. We are always assessing opportunities, we are assessing many opportunities right now, but exchanging the TR [ph] for the CDI right now doesn't seem to be something that would be good and extremely short run. Thank you very much.

Q - Enrico Trotta {BIO 16742911 <GO>}

Thank you.

Operator

(Operator Instructions) Thank you very much. As there are no more questions, I would like to turn the floor over to Mr. Jose Isaac Peres for his closing remarks. Mr. Peres, you may proceed.

A - Jose Isaac Peres {BIO 15388489 <GO>}

Once again, I would like to thank you for your patience in listening to us, and I would like to stress that the fact that we have to speak slowly, sometimes, I think about things that I would like to say. And then all of a sudden -- because of simultaneous translation into English, I will try what we say with the written script could make it more difficult for simultaneous translation purposes, and I felt a little bit constrained due to the fact that I had to follow a prepared text. But anyway, I thank you very much for your patience and your attention.

Operator

Thank you very much. Multiplan's conference call for the fourth quarter of 2017 results is closed. Thank you very much. And please disconnect your lines now. Thank you.