



LOG COMMERCIAL PROPERTIES
3Q22 Results Conference Call
October 27, 2022

Operator:

Hello, ladies and gentlemen, good morning. Welcome to the video conference on the results of Log Commercial Properties related to the results of the 3Q22. With us today are Sergio Fischer, CEO; and André Vitória, CFO and Head of Investor Relations.

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During the Company's presentation, all participants will have their microphones disabled. At the end of the presentation, we will initiate the Q&A session. To ask a question, just click on the Q&A button and state your name and company. Once your name is called, a request to activate your microphone will popup on the screen, and you can then unmute your microphone and ask your question.

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To open this video conference on the results of the 3Q22, I would like to give the floor to Sergio Fischer.

Sergio Fischer:

Good morning, everyone. Thank you for joining us today for LOG's earnings release call of the 3Q22.

We reported a very strong commercial activity in the quarter totaling 171,000 m² of gross absorption in several projects, the highest in the last 4 quarters. This reflects the growing demand in several sectors of the economy. It is also important to highlight that 57% of the absorption in the quarter is linked to e-commerce related activities, reinforcing how the segment continues to advance strongly, along with the flight-to-quality movement.

In addition, we noticed the significant growth in the food and beverage sector, pharmaceutical and health and hygiene, which account for approximately 60% of this absorption in the quarter.

During the year, absorption totaled approximately 320,000 m² of leases in 10 Brazilian states, reinforcing the Company's business model's assertiveness of being present in strategic locations close to major consumer centers.

100% of the leases that expired in the quarter were renewed, reflecting the efforts of the property managed team and the commercial team to offer the best experience to our customers. Once again, we had record deliveries. There were 3 new assets totaling approximately 175,000 m² of GLA, 86% already leased in Betim, metropolitan region of Belo Horizonte, Itapeva, in the Extrema region, and Viana, in the metropolitan area of Vitoria. Year-to-date, we reached a total delivery of 415,000 m² an increase of 80% over the same period of the previous year.

We have seen a positive pricing trend, which has already been reflected in this quarter with these agreement increases, which were 1.4% above inflation. The stabilized vacancy continues at historical levels and reached 1.73% at the end of the quarter.

The pace of production is moving as expected. We are currently developing 7 projects in 7 cities, which together totaled 430,000 m² of GLA. Construction costs remained stable and development yields are on an upward trend. This quarter, we concluded the historic sales of 2 assets in the amount of R\$429 million, resulting in an average gross margin of 32.6%, being 3% above NAV.

In the last few years, we have sold R\$1 billion, totaling approximately 300,000 m² of GLA. There is a lot of liquidity in the market for high-quality assets such as blocks both from institutional investors and also large investment funds. The strategy of recycling assets will continue to be the main source of funding for our growth. I will now give the floor to André, who will elaborate on the financial highlights.

André Vitória:

In the 3Q22, we posted an adjusted net income of R\$112 million and an EBITDA margin of 78%. We also maintained during the 3Q, our ability to generate value through the development of greenfield assets. There were R\$78 million of value generated through new projects.

As mentioned before by Sergio, we continue pursuing our strategy of recycling assets, which is our main source of funding to promote the Company's growth, the liquidity and attractiveness of our assets remain high as evidenced by the sales made over the last few years.

Net debt will remain flat during this growth cycle of the Company, and the net debt over EBITDA ratio remains at 2x. The Company's operating performance is also reflected positively in the financial results we presented in the 3Q22. Our indicators remain solid. The recent deliveries of assets with differentiated levels of average rental ticket continued to reflect the significant increase in revenues. This quarter, net revenue stood at R\$59 million, representing a significant growth of 60% over the same period of last year. It is worth mentioning that we carried out contractual adjustments to the existing portfolio, 1.4% above inflation.

Accumulated net bad debt for the last 12 months remained low and stood at only 0.6% in the 3Q balance of admin expenses continues to grow at a slower pace when compared to the previous year and reflects our constant operating efficiency. The financial result was impacted by the increase in the average balance of debt in the CDI in the period. The equity swap transaction under the Company's share buyback program generated a positive effect of R\$16 million in the quarter due to the share price variation.

LOG continues to focus on several ESG initiatives. Currently, a 100% of the energy utilized in our projects comes from clean and renewable sources. And in this sense, 5,000 tons of CO₂ are no longer being emitted each year.

We certified our first inventory of greenhouse gas emissions, and in its first year, we were already awarded the Gold Seal of the Brazilian GHG Protocol program. Keeping up with our commitment to support the communities neighboring our developments, we inaugurated Log Social in Betim, in the metropolitan region of Belo Horizonte, aiming to contribute even more to the personal growth and professional qualification of the employees who work in the site as well as the region's residents.

Bruno Mendonça, Bradesco BBI:

Thank you for the presentation. I have 2 questions here. My first question is a bit more about the deliveries. We have seen a very high level of deliveries. And this is surprisingly well leased, even above expectations. Sergio, could you please elaborate a bit about the yielding cost? And looking on the cost side, how do you see this cost environment in the construction business? And what has been the average rental ticket?

And my second question is probably looking long term. It is probably a more strategic question. Maybe 91% of the landbank of that plan of 1.5 million already acquired. So what could you tell us about what will happen or what do you anticipate for the period after 2024? What do you have in mind in terms of what will grow further after your 1.5 million plan?

Sergio Fischer:

Thank you for your questions. I will start with that yield part. The deliveries that were concluded in this 1Q. I mean we just finished. We got 415,000 in GLF. That 415,000 was delivered with a good yield cost. All of the projects that were initiated in the second half to be delivered throughout 2023, we are seeing an improvement in that number, about a half percentage point.

This is how we anticipate deliveries will be for the projects that were initiated this year to be delivered next year. We see a stabilization of the construction costs. Construction costs have been flat and stable, and that might be a bit lower than we see a marginal decrease in construction costs coming next year.

And in addition to that, we have seen a very positive movement for pricing, the average rental ticket and that has been over R\$20 per m². This is quite positive, not only for the industry, but for our business as well because this will allow us to improve our yield costs going forward.

About the landbank, and answering your second question, we already have new acquisitions. We see a lot of new opportunities in the market. Some geographies that have reported high demand. And so we are going forward to deliver that 1.5 million program in 2024.

About the Company, we are still internally discussing about growth going forward. The Company now, in all of our departments, we are working with 500,000 m² a year. Land approvals, construction, commercial and everything else in the packet, everything is already running at 500,000 m² a year. This is just an idea of what we could anticipate next year and for after 2024.

Bruno Mendonça:

Very good. Thank you. So R\$20 per m², it is a much better level when compared to what we saw more recently. Thank you very much.

Gustavo Cambauva, BTG Pactual:

Good morning. I have 2 questions. My first question is whether you could tell me a little bit more, because I know you just sold some assets more recently, despite the general M&A landscape that has cooled down a little bit. But even then you were able to sell at a very interesting multiple for the Company. So first of all, I would like you to tell me what you see going forward or whether somehow you still see that the market is very heated up and whether things will remain as is or you probably see things differently.

And my second question is related to delay demand. When we look at e-commerce prices, in general, e-commerce prices or the pace of growth of e-commerce is slowing down a bit, and this has been one of the major drivers for GLA in your case. So what do you anticipate going forward? Have you also seen some slowdown in demand? Or do you believe that there is still grade appetite for e-commerce and also whether you are looking at other segments. So, can you throw some light about e-commerce status?

Sergio Fischer:

Thank you for your questions. I will start with the question on demand. We had a very strong quarter. The 3Q was the best quarter when compared to the last 4 quarters. And a great part of that demand comes from e-commerce, almost 60% of new leases came from e-commerce. We formally believe the penetration will continue to grow. I mean, of course, we come from a very strong base looking back 2 years. It is not growing as it did in the past few years. But even though it is very positive, we have been monitoring some recent studies that anticipate e-commerce penetration to be close to 25% in 2026. And if that happens, there will still be a lot of demand for warehouses, and this is what we are feeling right now.

In terms of our strategy of geographic pricing, we have been able to capture that e-commerce demand throughout the country. This year, we made deals on the e-commerce side in several geographies around the country, and this is a bit different from our business model because we have been serving in some geographies where there is very little competition.

Just one more point related to demand: 40% of all of the deals signed this year were related to flight to quality. We are noticing that some of our clients are now preferring more quality rather than price. And so Brazil invested a lot in this current landbank. So I think we will advance still a lot in e-commerce.

In terms of the sale of assets, this is a very interesting, very good transaction for the Company. There are still a lot of things in progress, things that were already initiated and a lot of liquidity for asset like towers. We see some funds, some large investment funds that have a pro and their express interest in some assets. And also, we saw interest part of institutional investors.

We are not going to do things in a hurry. We want to maintain, now in the long run, our position. We will continue to work on recycling because I think this is very important. We see some relevant opportunities. The scenario hasn't changed. And so we also have this move towards flight to quality. So we will certainly have new transactions, but we will do that with caution. And certainly, this will be our main source of funding to fund our coming growth.

Gustavo Cambaúva:

Thank you very much. Good morning to you all.

Ygor Altero:

Good morning. I have 2 questions. It is more like a follow-up on the previous question related to recycling. In regard to valuation, how do you see the market evolving? And even considering your side, maybe we could see other transactions at the same valuation level between 7.5% and 8%. Is that the way you are looking at the market? This is point number one. Point number one is about investor interest at this level of valuation.

And the second question is about the costs. I know that you are having some relief. So what impact should we see in terms of gross margins?

Sergio Fischer:

Ygor, thank you for your question. Recycling, we see the market pretty much in the same line of our 3Q, something around 7.5% and 8%. We can have a relevant spread because of that, and we will continue to pursue these transactions, as I said earlier.

About construction costs, certainly, this will have a significant impact in the improvement, especially in view of the new projects, because the percentage has been higher than what it was back in this year, 2022, and this will have an impact in the gross margin.

So this, together with a more positive landscape with lower interest rates in 2023, I think we will be able to increase the spread and bring those transactions closer to our historical levels, which today is close to 40%, considering the last 3 years transactions. So this is what we have in mind.

Ygor Altero:

Very clear. Thank you very much.

André Mazini, Citi:

Thank you for the presentation. My question is about your agreements with Amazon. It is interesting to see that the rent per m² was able to go up more recently. I think it went from R\$16 to almost R\$19 now in the 3Q. Probably, this relates to Amazon contracts, which became your largest customer. And then you have contracts of longer duration of your warehouses, a lot of TI involved. So, do you believe that this increase has to do with tenant improvement that you did for Amazon, and so they pay this back through the lease, or does it have to do with the amortization time? And so, after the tenant improvement, do you believe that the lease per m² for that client will then be amortized back into the Company? Is my reading right, or am I reading something differently?

Sergio Fischer:

Thank you for your question. Mazini, what we see is a very positive landscape. But it is across the board. New transactions are occurring above that R\$20 that I mentioned before. This contract with Amazon is different, the ticket is different, and it will be that ticket for the next few years.

But we have seen all of the other transactions and the cost of **Spec Log (19:59)** which is the modular warehouse with log specs, they have been traded above the average lease ticket that you saw today. So that there is an upward trend in terms of the average ticket. And we will see that coming closer to the R\$20 as we delivered new assets that are being rented now.

André Mazini:

Perfect, Sergio. And what is the duration of the agreements? Is it 10 years? Because I think, on average, the other agreements are for a 5-year term.

Sergio Fischer:

We have several agreements with Amazon. There is a large one in Recife, which was delivered in the 2H22. It is a very different agreement for a 10-year term, and they are also coming with a major funding in TI, and we will be reimbursed by the TI we did for them. And the rest is just speculation. I think we have about 4 or 5 transactions with Amazon in addition to this, and that is this backlog with a 5-year duration in the agreement.

André Mazini:

Thank you, Sergio.

André Dibe, Itaú BBA (via webcast):

Could you please comment on the pricing dynamics related to the actual increase that you managed to post in this last year? How was absorption in pricing, looking at different geographies? Which ones had a more positive dynamic that led to that increase, and which ones were probably lagging behind.

Sergio Fischer:

André, thank you for your question. This quarter, we had 100% of renewals of the agreements that ended in the quarter. That was a very strong year that really shows that our clients are not leaving the operations. It is a very demanding market.

And with that, we were able to renew agreements from existing customers. And this has been across the board. I would not highlight a particular region. Things are happening across the board in a linear manner, and we are seeing that this industry is booming, and we will try to push prices above inflation, if possible.

Rafael, Safra (via webcast):

My question is about your deliveries scheduled for 2023. How many of them are already pre-leased, and whether we could also expect the same mix of clients.

Sergio Fischer:

Thank you for your question. We started many projects in the 2H to be delivered throughout year 2023. We anticipate a very active year in terms of delivery. We do not have any deliveries for the 4Q or the 1Q23. They will start occurring after the 2Q.

We have a lot of things going on in the Northeast of the country, and probably the bulk of our deliveries, 50% of deliveries will come from that part of the country. And on all the projects that are initiating, we already have a large amount that is up for lease, and this really demonstrates the strength of our business model, which is to be close to consumer areas.

And we have a mix of a lot of things. We see demand coming from e-commerce, demand coming from flight to quality. We just closed a BPS in the Northeast for a large beverage player. There are 2 other deals being negotiated in the Northeast, the deal is about to be closed in the next few weeks. Therefore, this is a very interesting moment for Log's business model.

Our geographic positioning is very interesting in different regions, and we are able to capture demand coming from our clients, which are asking us for additional areas in new geographies.

Marcelo Motta, JPMorgan:

Good morning. Thank you for taking my questions. I have 2 questions. My first question, I think the operating side of the Company is very strong in terms of leases, in terms of price increases, but FFO was still impacted due to higher interest rates and financial expenses. So, on the side of liability management, do you see any possibility of doing something to improve the conversion of EBITDA into FFO?

And my second question, considering the demand, and the market is very promising and very good, probably the main idea for you to accelerate growth would be sale of assets. What would be on the way for further sales? How many other announcements will we hear from you in terms of that?

Sergio Fischer:

I will answer the second question and then André will answer the first. Motta, we are not in a hurry. The quality of the recycling is very important to us. We want to deliver spreads so that we can sell 1 m² and have 1.5 to build with that proceed.

We just completed a transaction. It was a record transaction of almost R\$420 million. It was sold to a real estate fund from Credit Suisse. You do not even see the full cash of that coming from that transaction in the 3Q, but it will come in the 4Q.

Our policy to focus on warehouses is still going on. We still have something in our portfolio. We just sold another plaza for R\$20 million, and this will be materialized in the 4Q22.

So things are in progress. We are not in a hurry. You will see some moves in that direction. But what we are pursuing is that we want to follow our growth plan, and also to maintain the stability of our net debt throughout the next year.

So as things are happening, we then proceed with recycling. Certainly, you may see in a quarter or another some variations of our net debt, but the trend is that by 2023, it will be a lot more stable due to recycling.

André Vitória:

In terms of the debt, whenever we talk about FFO and the margin, it is a bit under pressure right now. There is a big weight in terms of interest rate, and this should become better going forward, because we believe that the interest rate should be a bit lower coming next year. So the margins are 35% to 40%, but we will certainly throw that margin back to 45% to 50% because of the interest rate.

In terms of the debt, the trend is that we will have more stability in terms of our net debt. The main KPIs we have today, net debt over EBITDA, the leverage will be around 2x. This is a very important KPI for us because our growth plan will be based on recycling, and we have been demonstrating great quality in recycling despite more complex moments as the ones we faced in the past quarters.

Another important information is that when we look at net debt vis-à-vis the PL, in our LTV, it will be 35% to 40% at the most. Therefore, in terms of net debt and the leverage level, we will maintain stability during the conclusion of our growth cycle along the next 2.5 years.

Marcelo Motta:

Perfect. That is very clear. Thank you very much.

Steven Lam, Goldman Sachs:

My question is about different leverage scenarios of the Company. Taking into account everything that could happen, how do you see your leverage by the end of the next year, considering the number of assets that you have in mind or a more extreme scenario where you would not be able to have any recycling?

André Vitória:

Steve, let me start by saying that recycling will happen. We will, therefore, move on with our growth plan by recycling our assets. So as a consequence, net debt will remain stable throughout that period, as I said before. Therefore, this is a landscape that we anticipate for next year. Therefore, any possible change in terms of net debt stabilization that is not contemplated in our growth plan. So this is our strategy for the coming year.

Steve Lam:

Got it. Thank you.

Antonio Castrucci, Santander:

Thank you. I have a question related to your maturity schedule that is quite high for the next 12 months, for new contracts. How do you see the outlook of spreads for these negotiations? Are you still maintain IPCA + 1.4%? And how can you compare these transactions to that rental per m², considering R\$20 per m²?

Sergio Fischer:

Antonio, thank you for your question. This dynamic will depend on the geography, on the region. What we have been saying is that in the 3Q, we were able to renew 100% of our lease agreements, and in the 4Q, we anticipate something very close to that. We do not see anything new. Therefore, we were able to renew at an amount above inflation.

So, for the next quarters, we see some positive spreads, close to what we delivered in the 3Q. And again, every geography has a different dynamic, so it is hard for me to really tell you what the lease spread will be for the next contracts that are about to mature.

Antonio Castrucci:

Perfect. Thank you.

Operator:

The Q&A session is now concluded. I will turn the floor back to Sergio for his final remarks.

Sergio Fischer:

Thank you so much for your question. Thank you for joining us today. I would like to say that our growth plan is moving at full force, and we will focus on pursuing this plan and serve our demanding clients all over the country, and this will be funded through recycling.

So this is our plan. We have a lot of liquidity to continue pursuing this model. We have a lot of things in progress. And as I said before, we will stabilize the net debt of the Company as the Company grows, and so this will be funded through these recycling projects.

This is what we had for today. Thank you so very much, and have a good day.

Operator:

Log's video conference is now concluded. If you have further questions, please submit questions to the IR department of the Company, ir@logcp.com.br. Thank you so much for participating, and have a very good day.

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