1Q21 Conference Call – EZTec

Hugo Grassi:

Good morning, one and all, and welcome to EZTec's results presentation for the 1Q21. Please note that this call is being recorded and that all participants are in listening-only mode.

By the end of the presentation, we will begin a Q&A session when further instructions will be given. In case you need any assistance over the call, please let us know through the chat box. In case you have any connection issues, you may reuse the same weblink or ID to return to the presentation available on our website. You may find on that link an ID as well as the slides for this presentation on the address ir.eztec.com.br.

Before we start, we would like to mention that any statements during this call pertaining to EZTec's business projections, operational and financial targets are based on management's beliefs and premises, as well as recruiting available information. These considerations do not constitute an assurance of performance. They involve risks, uncertainties and premises. Investors may take into account that general economic conditions, industry or operational circumstances may ultimately affect EZTec's future performance and may cause the Company's results to differ materially from those expressed in those forward statements.

Now, I am accompanied by Emílio Fugazza, our Chief Financial Officer and Investor Relations Officer. I will get the presentation started and pass it on to Emilio as soon as we get to the financial portion.

Moving on to the first slide, just very briefly introducing the main figures and numbers that we will try to address more thoroughly during the course of the presentation. Operationally, the quarter was marked by net sales of R$236 million, launches significantly lower at R$28 million, a single project, landbank of R$14.1 billion with many acquisitions through the year. Financially, we had gross profit of R$83 million, accompanied by a gross margin of 42.5%. Our net income was R$73 million, with a net margin of 37% assisted by financial revenues.

Net cash of R$1.06 billion, alongside a R$529 million of performing receivables, much of that financed directly by EZTec in the portfolio of direct receivables of R$482 million. Here, we are talking about financing to the clients made through a set of aligned agreements directly from EZTec to the final consumer.

Briefly mentioning subsequent events that have happened already by the 2Q. We had yet another launch of the R$253 million, Dream View, launched as soon as sales stands were reopened. In our shareholders meeting at the end of April, we have also approved the payment of dividends of about R$96.2 million, about R$0.42 per share.

As an increment of the Company's governance standards, we had appointed an election of our Board of Directors with four independent members out of a total of nine members altogether.

Now getting started in each specifically theme, addressing EZTec's landbank, it is important to mention that despite the quarter itself did not have very many acquisitions, R$240 million in new acquisitions in the quarter, we have been coming from a full year of 2020 in which we had several acquisitions, basically fulfilling the full mandate that was given to EZTec by the follow-on, at which time we had approximately R$940 million of cash injected into the Company, and basically about R$1 billion already earmarked for acquisitions. Much of that was already deployed, some of it is still pending installments, but that money has been directed to landbank, that it is already within EZTec's landbank.

In the 1Q specifically, we noticed that there was a significant contribution coming from price provisions. We are talking about an average of 40% growth in price levels in our landbank, basically in line with actual price growth for practice sales to the quarter.

As you consider that we also have R$2.3 billion in option acquisitions, you reach a combined landbank of R$14.1 billion as we speak.

Just to keep that in proportion, out of that R$14.1 billion , we have approximately R$3.4 billion which is within EZ Inc, our commercial development subsidiary, while the remaining R$10.7 billion is within EZTec's residential operation, that basically represents something like 4.3x a sustained launching volume of R$2.5 billion, which implies that there is plenty landbank available at this time, already, somewhat signaling to a cycle, a few years in which we do not have an imperative need to buy additional landbank, and we may keep on acquiring just to the extents that we actually push forward the new launches.

Moving on to the operational slide, here is where we feel the direct effect, the toll the pandemic has taken on EZTec's performance for the past quarters, especially when you look at the fact that approvals for new launches coming from the city hall had been lagging relative to what we wished for, which means that launches have been significantly lower over the course of the year thus far.

Naturally, that has only the sale derived from the launches. But the sales themselves were also harmed in the 1Q by the fact that about 45 days out of the full quarter were marked by the red phase of the pandemic here in the state of São Paulo., The red phase of the pandemic means that all sales stands were forced shut over the course of 45 days, and that had a particular effect on ready units, considering that a client very naturally would prefer to visit the unit that he will live in prior to making the investment decision, and naturally we had a lot of clients that chose to postpone that investment decision, and lead to ready inventory units about 30% lower than the previous quarter. And actually, that in itself has had its implications in terms of revenue recognition.

Regardless, as soon as the sales stand reopened, what we have seen thus far in approximately three weeks is that sales speed at this time is 26% faster than the average weekly sales speed for the 4Q20. We are basically talking about a level of R$31 million sales per week.

Just quickly mentioning about cancelations, here we had a smooth convergence to a R$20 million standard of cancelations forced economically, and very important to remind that out of those R$23 million cancelations reported, 44% actually refers to transfer that were upgrades and downgrades where our credit recovery team tried to redirect a client to another unit as a way to prevent cancellation, and mutually to wait for both the Company and the clients. And that takes us to a net sales of R$236 million in the 4Q21.

Now, moving on to the next slide, we will talk about the outstanding inventory for EZTec. We notice that altogether we are spending at R$1.066 billion of available inventory at the time, and you notice that we have some 300 commercial units, but mostly we are talking about residential units within the city of São Paulo. There has been a marginal decrease in the inventory side in comparison to the 4Q, as a consequence of the fact that we do not have enough launches to replenish the volume of next sales we have had.

That takes us to a point in which we have the lowest inventory level for the past seven years, especially when you look within that inventory, you still notice that the ready inventory in itself is shrinking. The largest concentration we have is still in Cidade Maia, in the city of Guarulhos, where we have R$435 million available inventory.

Cidade Maia, always a good reminder, is still selling in this quarter at a gross margin of 49%. So that is a very strong year for EZTec's operations, and it has been so for the past three quarters already.

And naturally, we do not have many deliveries over the course of the past two years as a consequence of the fact that we also do not have many launches over the course of 2015 all the way through 2018. But those deliveries should pick up back again by the 2H21 and on. We are talking about some $500 million of PSV to be delivered in the 2H21. That should contribute with a larger portfolio of units available for EZTec's commercial assets.

Now, moving on to slide number seven, where we talk about launches, like we said, launches for the 1Q itself were only the single tower launched in ID Paraíso, that is R$28 million in PSV. It is actually a project that is combined with a previous launch called Signature by Ott, and if you take it all together, at this point it has 60% of its area already sold. The ID Paraíso is very much driven towards investors.

ID Paraíso was launched at a time in which we do not have our sales stands open, but given that it is a relatively small project, and investors tend to be a little nimbler in terms of being able to access digitally, that worked out fine for EZTec.

And as soon as sales stands reopened by the 18th of April, we also launched the Dream View Vila Prudente project as a subsequent event, adding another R$253 million of PSV to the quarter.

Moving on to our next one slide, number eight, it is very important to highlight EZ Infinity. EZ Infinity is the main project for the coming months, and it is also possibly the highlight for high income projects to be launched in São Paulo for the year as a whole. We are talking about something that could reach R$600 million of PSV by the time it is launched.

Just for just for reference, it is the project on to be built on top of IBM's current parking lot by the Paraíso region, a region where it is very hard to replenish, landbank is a very valuable asset, and a launch for the coming months.

Other than that, we also have Arkadio in Alta Vista. It is a smart living high income project for the Chácara Santo Antônio region of São Paulo that is still pending approval to be launched, but also hopefully we will launch for the coming months, and if we take those reports to mind, that basically represents R$1.1 billion of launches already in the coming months out of the two-year guidance of R$4 billion to R$4.5 billion that we have committed, basically where we are still left with an additional R$2.6 billion to R$3.1 billion guidance pending for the remainder of 2021.

I will pass the word to Emilio, our CFO and Investor Relations Officer, to comment on the financial performance.

Emilio Fugazza:

Thanks, Hugo. Let us talk about financial performance, slide number nine, starting with net revenues coming in at R$195 million in the 1Q21, coming down from R$262 million in the 4Q20. It is important to bear in mind that the piece of the construction nowadays is becoming a little bit slow compared to the 3Q and 4Q20, simply because of the of the problems regarding the sanitary conditions, the covid issues here in Brazil, specifically between February and March.

It is important to understand how we can come up with those revenues. Once we can sell one performed, obviously, we are going to recognize the revenues coming from these units. But units under construction, or units already launched, we are going to recognize only the state of the land over the revenues, and the construction part is going to take place in the miss of the construction.

So we are going to recognize by the percentage of completion method the revenues of the quarter. And the problem is, given the fact that we sold less performed units in the 1Q, and the pace of the construction sites were slower than in the past, we came up with less revenues than the past.

From now on, we do expect that the volume of construction can increase a little bit in the 2Q, but mainly in the 3Q20, given the incremental prices we have been facing so far, and obviously, the situation about the pandemic here in Brazil, specifically in São Paulo.

Talking about gross profit on the on chart on the top right of the slide, you can see R$83 million of gross profit for a gross margin of 42%, recovering a little bit from the 4Q20, from 40%. It is important to say that INCC, the index which is adjusting all the receivables we got in our balance sheet, can so far replace the incremental cost we are facing now.

It is important to understand that that we have been facing a lot of incremental costs, especially of raw materials like concrete, like a steel, specifically copper. So, so far, those incremental costs or delays in the construction sites are not harming the schedule of delivering those construction sites. And so far, the cost and the margin remain a little bit steady, over a little bit more than 40%.

Talking about selling expenses, nowadays they are coming at a pace of 40% of gross sales. That is important to mention. When you look deeply at the figures, you can understand that we are coming up with a lot of new sales stands to launch the projects Hugo told you before.

Apart from that, you can see an incremented branch of ready inventory, commission and others, specifically commission, because nowadays, totally different than the past, all the commissions are recognized over the selling expenses, because mainly of the sales are coming through digital ways. So digital ways mean that the brokers are not charging for the commissions directly to the clients, but also trying to do that directly to the Company, and that is a way to perform sales a little bit faster in this in this moment we have been through.

In terms of G&A, you can see R$25 million in 1Q21, compared to R$27 million one year ago. That is because we made a lot of adjustments in the 2Q20 and 3Q. Those adjustments in payrolls are even adjusting the whole teams of EZTec in the headquarter, and we have not recovered the number of people we actually saw before in our Company. That is like we can see a little bit less G&A expenses than in past.

Apart from that, it is important to mention that if you are going to look deeply at the expenses of the Company, tax expenses were a little bit higher than in the past. That is because of every 1Q each year, we can pay in advance the whole land and property taxes to the municipality.

And this year, only land has impacted something around R$12 million, counting on the lands managed by EZTec or in in partnership with other developers. And that is why we saw an increment on this branch.

Moving on to financial performance on page number ten, you can see on the top left R$45 million coming in the 1Q21. Let me remind you that it is solely because of the performed assets we have here on our own accounts. Nowadays, it is about 1,500 units we have been providing financing, adjusted by IGP + 10% yearly.

Only to bear in mind, only to understand what happened here in Brazil, IGP since January 2020, adjusted by something around the 35%, quarter by quarter is impacting our receivables on this branch.

If you look deeply at financial expenses, it is important to understand that, since 4Q20 and 1Q21, you can see a huge increment in financial expenses. It is not regarding that because we have no holding debts in our Company, but mainly given the questions I got from the Q&A in Portuguese an hour ago, it is important to understand that that is mainly because of three factors.

First of all, because many people are paying in advance installments that they were going to pay only after the permits of living. So these payments in advance are accounted with some sort of discounts.

Secondly, because in the 4Q, we have the living permits for one specific project in advance, and this project was Z Cotovia, but we only delivered the units to our clients between March and April. And we have decided about this specific project, instead of charging IGP + 12%, which was so high for this specifically project, we have targets only INCC.

So that was a huge difference, because INCC to on that specific time was something around the 3% yearly, and IGP + 12% was more than 6%. So the difference between one and another made an adjustment of financial expenses reported in those quarters.

And finally, only to understand, when we sell one unit, after we sell this unit, the client has three to four months to get the mortgages from the banks. But in between, the client has his debts adopted by IGP + 12%.

And in the majority of the cases, because of the units are performed, or because the units are in the middle income segment, it is barely possible to have these amount of adjustments only within two to three to four months.

And we provide a discount to them, and this discount mainly conceive 0.5% of this this adjustment of IGP, for instance. And that is why in the last two quarters, we went in an incremental financial expense.

Moving on to equity income, it is about R$6 million in the 1Q21, mainly impacted also because of the property taxes, something around R$4 million to R$5 million over this line. Obviously, we are going to expect less than that amount of results in the next coming quarters, particularly because many of the enterprises coming from this branch are starting the construction, or factoring the pace of the construction overall.

In terms of net income, it came at R$73 million, and a net margin of 37%, and obviously 6% of it impacted by financial results. We do expect that we are going to see a higher increment in revenues recognition in order to boost the volume of net income coming in the coming quarters.

And finally, that could be the highlight of these 1Q21 results, it is the backlog margin around 45%. For us, 45% means that all the adjustments we have got in the in the budget of constructions, or in the accounting because of the constructions, had not impacted so far the margins to be recognized in the coming quarters from the sold unit so far. That is very important to say.

So the main idea, the two mindsets behind this can be the fact that all the incremental costs we have been facing can be offset by the adjustments off the INCC so far.

On page number 11, you can understand a little bit more deeply the portfolio of performed units sold with financing provided by the EZTec. So far, 1Q, we are talking R$480 million, meaning something around 1,500 units under the management EZTec.

It is important to see the payments in advance we have already received, something around R$66 million this quarter, meaning that 182 two units paid that debt off, specifically trying to transfer the credits to the banks, taking mortgages from the banks.

This is highly possible right now because many clients that took finance from EZTec five to six years ago nowadays have loan to value off 60% or 50%. Nowadays, those credits for them are available in very good interest rates, something around 5% to 6% yearly compared to IGP + 10%.

The highlight of this slide is about the foreclosure, only 12 units. Let me remind you that, for the whole assets managed by EZTec in terms of performed portfolio, only 100 to 110 units are on default right now.

We have been managing, obviously, and you can expect something around 60 to 70 units to be taken back in the next coming quarters. So the foreclosure can reach something around 60 to 70 units in the whole year, meaning that is about 4% for the total amount of units, which is not a concern by itself.

On page number 12, financial performance, Fit Casa, our brand for Minha Casa Minha Vida, low income segments. It is important to understand that we have to reached something around 50% gross margin on Fit Casa, meaning something around R$8 million pounds of net income in this segment.

Let me remind you that R$8 million is already impacted by the tax property, or land taxes we have paid in advancement for still more than R$5 million. Even with that huge back in the 1Q, we could provide something around 10% return on equity. So we can expect a return on equity even higher for the next coming quarters, because as Marcelo Zarzur, our technical Director and the current EZTec CEO said in the conference call in Portuguese, two projects scheduled to be to be delivered by the end of this year or half of 2022, I gonna to be delivered in advance, six months in advance, and with some savings in budgets, we can provide an increment in the net profit, and also in the gross margin of Fit Casa as well.

Saying that, let me bring you to the end of this presentation, on slide number 13, talking about the common equity in this Company. 1Q ended up with R$4.1 billion shareholders' equity, which we can break up into cash and equivalents of almost R$1.1 billion. Finished units receivables of R$529 million. And the cost of the land bank, the land bank of R$11 billion guys has already boosted by almost R$1.2 billion.

But that we have to increase here, another R$3 billion, and we are going to do that in the next coming quarters, and it is going to add by something around R$300 million to R$400 million in land bank inventory.

In terms of liabilities, only to remind reminder that the dividends we are going to pay in the next coming quarters of R$96 million, and they are only carrying something around R$8 million of construction finance, almost nothing regarding R$4.1 billion shareholders equity.

All in all, that is our earnings for the 1Q21, and we are really open for the questions you may have. Thank you very much. Thank you for your audience today.

Nicole Inui, Bank of America:

Thank you for the call. Just a couple of questions. First, on launches, how are you thinking about your guidance for this year? We have had a difficult start of the year. We had another shutdown. We are already reaching the end of May. So, how strongly do you feel that you will be able to meet this guidance for the year? And if not, how do you think it will look in terms of launches for the year, given the recent lockdowns that that we had?

And then the other question, just in terms of your pace of construction, it has been slower this quarter. I saw some specific problems with Parque da Cidade. So if you can elaborate a little bit more on that, would be great.

Emilio Fugazza:

Nicole, thank you very much for the questions. A very good morning to you. Regarding launches specifically, let me say what Silvio Zarzur and Flavio Zarzur have already mentioned in the Portuguese call by now.

In terms of launches, obviously, we are fully committed to achieving the guidance. But, obviously, we have already missed something around 45 days in terms of launching process. So regarding the permits, specifically since the beginning of March, we have not saw a huge work coming from the municipality of São Paulo releasing the permits.

Hugo has already mentioned about the three major projects we are going to see in the months coming, specifically in terms of IBM, Arkadio and Alta Vista. All in all, we are talking about R$1.2 billion. Adding to the projects we have already launched, between something around R$300 million, it is meaning that up to July, beginning of July, we can reach something around R$1.5 billion of launches in the 1H21.

There is something around 15 more projects under the process of taking licenses, taking permits. And regarding what Mr. Flavio Zarzur said, he is fully committed to get the licenses for those projects up to the end of this year, in order to achieve the guidance at the end of this year.

But obviously, in terms of getting capacity, operational capacity enough to open the sales stands, to make the sales of those projects also in 2021, it can it be a little bit hard.

It is possible to see the launches coming at 80% of the guidance, something about that up to the end of this year, and watch the remaining projects being accomplished by January or February. All in all, depends on not having another stop, another closing of the of sales stands again in the next couple of months.

Making a long story short, we are fully committed to achieving the guidance. But obviously, we already know that we have at least something around two months so far.

In terms of pace of construction, it is important to understand that what we have been facing now is not something that is harming the schedule of deliver of the projects. That is important.

All the projects we are going to deliver in 2021 are going to be delivered on schedule, on costs, or even facing some savings on those costs. But projects with very large proportions, such as Parque da Cidade, we have our mentioned in our earnings release, or even Air Brooklin, for instance, are projects that are at the beginning, the cost of the construction is getting higher and higher, specifically the raw materials, and we are facing, obviously, some delays because of hiring people to work on those projects.

Saying that, I would like to address that everything about 2021 is not harmed. But 2022, I would say that we are going strong enough to achieve the goals. So we do not enhancements in the pace of the construction in the 2Q, as we are in the middle of it. We do expect something coming from the 3Q21.

Nicole Inui:

That is very useful, thank you.

Hugo Grassi:

Thank you very much, Nicole. With that, our conference call for the results presentation is over. We thank you all for the attention, and we remain available, all the investor relations team, for any further questions, at any timing.

Have a nice day.