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Q3 2020 Neinor Homes SA Earnings Call

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**Manuel Giménez**

## PRESENTATION

### Operator

Ladies and gentlemen, thank you for standing by, and welcome to today's Neinor Homes [Q3] 2020 Results Conference Call. (Operator Instructions) I must advise you that the conference is being recorded today, and that's Thursday, 29th of October 2020. I would now like to hand the conference over to your speaker today, Jose Cravo. Please go ahead, sir.

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### Jose Cravo *Neinor Homes, S.A. - Director of IR*

Hi. Good afternoon, everyone. I'm Jose Cravo, the Head of Investor Relations at Neinor Homes. I'm here with Borja Garcia-Egotxeaga, our CEO; and Jordi Argemí, our Deputy CEO and CFO. Today, we'll go over the results of the third quarter of the year 2020.

But before I hand over the presentation to Borja, let me give you a summary of what we will discuss. Firstly, we will start with a macro review. Secondly, we will review our business performance over the last 9 months. And in this area, we will provide an overview of Neinor Rental strategy and how we are approaching land acquisitions. Then Jordi will review financial results. And lastly, we'll move to the closing remarks and address any questions you may have. With this, I'll give the word to our CEO, Borja Garcia-Egotxeaga.

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### Borja Garcia-Egotxeaga Vergara *Neinor Homes, S.A. - CEO & Executive Director*

Good afternoon, everyone. Thanks for taking the time to join us. During the last 2 presentations of this year, we have started talking about the impact of the COVID-19, the big changes that the pandemic has brought to our civilization and the hard times that we are all going through.

After 8 months, the pandemic is far from ending, and my first thoughts

(technical difficulty) are extremely hard situations. Special remind for some of our employees and fellows who have gone through these situations. This COVID crisis is forcing us to face yet another one, an unprecedented economic crisis that will have major effect in Spain. Our industry, as we already mentioned a few times, has strong fundamentals and is much more resilient than in previous cycles. On top of this, this crisis has put our homes as the most important asset of our lives.

Today, developers are part of the solution to the current economic crisis. We are one of the few industries with capacity to generate millions of jobs going forward. We are constantly in touch with administrations to find ways to work together so that we emerge from this crisis stronger, supporting inclusive and sustainable growth in Spain.

Now we are going to move to the presentation. And before getting into the business, I will give back the word to Jose to do a step-back and understand the macro picture Jose, please?

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### Jose Cravo *Neinor Homes, S.A. - Director of IR*

Thanks, Borja. So if you please follow me to Page #4. Here, I'll just repeat what we always say. We only work in the 6 high-growth regions of Spain. Our footprint is established in the regions that drive the growth of Spain. And in these regions, supply of units for sale and for rent is way below demand. If you see 2019, we saw the peak of housing starts in the cycle. And even then, there was a housing production deficit of almost 70,000 units. This shortage of supply will compound going forward as housing starts in 2020 are almost 30% down

year-on-year.

Moving to the next page. We see how this virus has changed our lives and how this transformed the residential sector into a top pick within real estate. Where we live now became an office, a school, a gym, a leisure center. It's WiFi-connected. It's sustainable, and people just want more space.

People are fleeing from cities to the outskirts, which is where we have our land bank. On top of this, monetary policies have reduced mortgage costs. Fiscal policies preserved jobs and household income. And while some of these elements will change over time, most of them will become a new way of life. At Neinor, we are perfectly positioned to embrace all these changes. We have the best product and in the perfect locations, and it's all land that we bought at the correct prices.

So I think now, I will give the word back to Borja to go over our business.

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**Borja Garcia-Egotxeaga Vergara *Neinor Homes, S.A. - CEO & Executive Director***

Thank you, Jose. Okay. Now let's review our business and our achievements in this Q3. So please let's move to Slide #6. In Q3, we had revenues of EUR 96 million and EBITDA of EUR 19 million. And during the first 9 months of the year, we achieved an EBITDA of EUR 34 million. This is in line with our planification. As we always said, this year, we have a good number of deliveries in Q4.

On our commercial activity, we have presold 400 units in Q3. We have presold more than 1,000 units in 2020. And this represents an increase of presales versus last year even in these challenging times. Our construction sites have not suffered big delays nor any cost increase due to the COVID. Today, we have already reached all the final construction certificates for the deliveries of this year.

As we promised, we are very prudent with our leverage and cash position in these challenging times so we are in a very comfortable balance sheet position that will allow us to seize opportunities going forward.

Last, but not least, a very important acquisition in this quarter was Renta Garantizada. We will see in more detail later on, but it is the best rental operating company with 25 years of track record in a market where there is a clear lack of these platforms. This allows us to become the only residential platform that incorporates the full value chain of PRS.

So as a summary of Q3, despite the crisis, we are growing as a company. We are able to increase our sales, and we haven't suffered cost increases. All these allow us to have a comfortable balance sheet position, and we are able to keep growing our Neinor Rental strategy. With all this said, now let's go into a bit more details on the business.

Now a few highlights of our core and most important business in Slide #8. First, it is important to remark that we have the best land bank out there to produce more than 10,000 units. Going to the business as of September 30, we had almost 5,000 units under construction. We notarized 523 units. And we have gotten final certificates of construction for almost 1,900 units.

On our commercial side, our lead generation has suffered a drop of 40% during the month of March and April. Today, it's fully recovered, and we are exceeding by 18% year-on-year. Our order book has over 3,000 units, and it's over EUR 1 billion. Important to remark here is that we have presold keeping our pre-COVID prices, and we didn't have a spike in cancellations.

Going to the quality of our order book, more than 85% of it is under private contracts with an average of 17% down payment. And also, as we said last time, it is very important that 68% of our order book is covered by the Family Homes Protection insurance, which give us further visibility towards the notarization.

In the next slide, we give some visibility of our upcoming years. One of our current strengths is the visibility we have going forward. For 2020, we have more than 90% presold and as we said, with almost all of them under private contracts. We are fulfilling the planning. At this moment, all certificates of final construction have been achieved. And by September 13, almost 1,000 units delivered or in the delivery process. For 2021, we have over 55% presold, and all the sites under different status of construction in line with the planification. And for 2022, we have 34% presold, and we are awaiting only for 12% of the licenses and 49% is already under construction.

So now please let's move to Slide #10. As you remember, we took the correct view, and we decided to accumulate cash, keep a low loan to value and wait until we see very accretive opportunities. Today, every day, we see more and better opportunities coming to us. And today, we confirm that we are under exclusivity to acquire more than 2,000 units in top locations. We are also presenting this partnership that we are doing with a local land owner in a consolidated area close to Madrid. We are going to get fees for developing more than 1,000 units. And on top of this, we are getting a cheap option to acquire more than 4,000 units.

Now moving to Page 11, we will show how we are doing with our rental platform. We decided to put this platform in place more than a year ago. And it's never good to have competitors, but after seeing more than EUR 1 billion investments announced since April from investors targeting 12% to 15% IRR, it confirms that we took the right decision. Our 1,200 initial units are on track, with the first 100 units that will be delivered in the second quarter of next year.

On top of this, we acquired the best operating platform, something that is very tough to find in Spain. It is a company with more than 25 years of history with a very stable business that has been growing at 30% for the last 3 years. This company provides us a lot of synergies, efficiencies and allow us to create the only residential platform in Spain that incorporates the whole PRS value chain.

With this now, I will give the word to Jordi, our Deputy CEO and CFO, to walk us through financial highlights.

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**Jordi Argemí García Neinor Homes, S.A. - Deputy CEO & CFO**

Thank you. Vast majority of the data has already been commented by Borja. But just as a brief summary in Slide #12, you will see that we have closed the first 9 months with almost EUR 200 million of revenues, positive EBITDA of EUR 34 million and positive net income of EUR 22 million.

On the right-hand side, you have the comparison with Q3 of last year. Basically, we have increased revenues by 20%, EBITDA by 4% and net income by 17%. So we come today with a strong set of results. We all know that there is still a lot to be done in Q4 to fulfill the objective for the full year, but we are in a good path despite we are facing the COVID-19.

In terms of balance sheet, we have a strong cash position with EUR 115 million. And this number will significantly increase up to EUR 200 million roughly in the next couple of months, thanks to the deliveries we are planning to have. So basically, this company today is a cash machine that will help us to navigate in the current context and, hopefully, to even take advantage of it. Loan-to-value has not changed. Prudent, as always, with a 20% ratio, and it probably will go down at the end of the year.

And my last comment will be that in Q2, in a full lockdown situation, we signed EUR 250 million of new CapEx financing loans. And now in this Q3, we have signed additional EUR 125 million with no material changes in the conditions. With all these signatures, we have clearly derisked the year 2022. And the rationale behind it is that banks trust in both the execution capacity already proven of this company and also the financing policy and solvency of Neinor Homes. And as all of you know, leverage and conditions are critical in our business.

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**Borja Garcia-Egotxeaga Vergara Neinor Homes, S.A. - CEO & Executive Director**

Thank you very much, Jordi. So now I will give a few closing remarks. As stated initially, we see a sector that is much more resilient. We have very strong fundamentals in the 6 growth regions of Spain, demand of homes keeps increasing both to buy and to rent. Supply not only is not enough, but that gap keeps increasing. We also see that the residential sector comes out much stronger from this crisis as the home now plays a critical role in our lives, and the type of product being demanded is the one we have fulfilled. We feel comfortable that we will achieve our target of EUR 100 million EBITDA for this year.

As mentioned, we are one of the few industries that is not suffering from the crisis as it did not affect the demand for our product and did not increase our costs. Now we are facing the second wave of the COVID. Even though the number of positives in this second wave is bigger than in the first one, we haven't seen a drop in leads or visits as we did in the first wave as there aren't mobility restrictions that forbid people to go and see our assets.

On rental, we are confident that our bet was the correct one, and that soon will be translated into value for our shareholders. And last, but not least, there is plenty of noise out there, but we took a good read of the cycle and we were prudent. We maintained a low loan to value and protected our cash. Now we will finish the year with more than EUR 200 million in our bank accounts.

Today, we see new and better opportunities, and we have never been better positioned financially and operationally to tackle these good and very accretive growth opportunities.

So thank you very much for your time. And now as usual, we will open a brief Q&A session.

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**Jose Cravo Neinor Homes, S.A. - Director of IR**

Thank you, Borja. Operator, you can start, please, with the questions coming from the phone lines. And afterwards, we will address the ones that come from the webcast platform. Thank you.

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## QUESTIONS AND ANSWERS

**Operator**

(Operator Instructions) You do have a couple of questions from the phone lines. Your first question comes from the line of [Manuel Gimenez Jorge].

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**Manuel Giménez**

Can you hear me?

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**Borja Garcia-Egotxeaga Vergara Neinor Homes, S.A. - CEO & Executive Director**

Yes.

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**Manuel Giménez**

Excellent. I've got several questions, if it's okay with you, guys. I'll go one at a time. So the first question is with regards the sales figure that you published. I just wanted to be clear on whether this was a gross figure and whether the cancellation rate was around 95 units. Correct me if I'm wrong. I'm just trying to do the bridge in the order book from one quarter to the next.

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**Borja Garcia-Egotxeaga Vergara Neinor Homes, S.A. - CEO & Executive Director**

Okay. I will give the word to Mario, our CEO (sic) [CIO].

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**Mario Lapiedra Vivanco Neinor Homes, S.A. - CIO**

Thank you, Borja. No, yes, it's correct. It's 95. Out of that 95, we have 43 that have been done by ourselves regarding the rental buildings of the second portfolio that we are launching. So in that sense, we do not consider that 43 as cancellations or typical cancellations to be taken into account into the cancellation ratio. And then we have 52 cancellations or real cancellations that could be compared with that Q3 of 2019 that you can see that are basically the same. So we are comfortable. And on top of that, we can add that out of the 52 cancellations of Q3, we have 29 that are coming from the online presales that as we anticipated has a slightly higher cancellation ratio. So in general terms, we keep our below 1% cancellation ratio on a monthly basis and the order book with 90% of private contracts done. So we're really comfortable with our risk there.

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**Manuel Giménez**

Okay. Very useful. Next question would be with regards to -- you mentioned the asset-light deal, which, from what I understand, basically, you're going to let other developers sell their developments under the Neinor brand. So essentially, you're offering your commercialization services and taking a fee in exchange. I just -- I was -- I understand this is pretty risk-free. But I was just basically wondering how accretive this was and to what extent you intended to scale this new line of business.

**Mario Lapiedra Vivanco *Neinor Homes, S.A.* - CIO**

Okay. I take this one also. It's correct, but with 2 extra points. The rationale behind is that, on one side, we will lead the whole process. So we will have control over the development in that asset management contract. And the second point is that we will have the call option over 4,400 units that we will have that as a real rationale behind.

**Manuel Giménez**

Okay. And then my next question is with regards to your land purchasing strategy, which, as you know, is slightly concerning that you've been so long without buying land. You've mentioned that you have a pretty strong pipeline, which -- well, you already had it early on in the year before the pandemic. And I guess, that's back on track. I was just wondering if you could give us slightly more detail on whether this land in terms of urbanization, whether it's fully permitted, ready to build and whether any of it is earmarked for your rental platform or if it's all for your core business. That would be the question.

**Mario Lapiedra Vivanco *Neinor Homes, S.A.* - CIO**

Yes, I will take this one. Yes, we keep the pipeline, as you were aware, during the COVID impact on the contingency plan. What we did is to maintain that strategic deals or the ones that we really believe could make sense in the current environment alive. At that point, in the year where we have visibility on the deliveries and on the cash, the idea is to execute that pipeline. And regarding the distribution of these 2,000 units, we have 75% of it dedicated to the build-to-sell. Out of it, we have 50% in strategic lands, 50% in fully permitted lands. And the other 25%, it's, well, dedicated to our pipeline regarding the build-to-rent strategy.

**Manuel Giménez**

Okay. Very clear. And then just one very last question, and this is a bit -- we're talking about all these different new business lines, which is clearly indicating towards a diversification in your business model, which makes sense. But just for argument's sake, 3 years down the line, how do you see this diversification impacting your business model? I mean how much is each of these business lines, in a way, on your revenues and on your business model as a whole? I guess it's a pretty generic question, but how do all these different business lines fit into the investment case as a whole? And I guess, I'm also asking whether you've had any feedback from investors on this front.

**Jordi Argemí García *Neinor Homes, S.A.* - Deputy CEO & CFO**

I take this one. Basically, we have always said that with build-to-rent, we wanted to have optionality. So the case that we keep the assets, this would imply a recurring EBITDA of roughly EUR 14 million, and this is what you should consider in the potential business plan, let's say, 3 years from now. But we'll decide this. It's not the momentum today. Obviously, 3 years from now, but keep in mind that this is optionality because we can always sell these units once rented at a multiple EBITDA times, so we will decide what's the best decision. But the best decision would imply the best value proposition for our shareholders.

**Operator**

We will now take our question, and your next question comes from the line of [Fernando Abril].

**Fernando Abril Martorell *Alantra Equities Sociedad de Valores, S.A., Research Division* - Research Analyst**

It's Fernando from Alantra. It's about the EUR 200 million cash that you expect to have by year-end. So just what are you thinking with it? I don't know if you want to -- are you thinking on scale up your rental units or maybe do some cherry-picking land plot purchases? I don't know. What are you thinking about on -- with this cash generation?

**Jordi Argemí García *Neinor Homes, S.A.* - Deputy CEO & CFO**

Look, this EUR 200 million, it's important to understand that already considers the deploy in equity of what is in the pipeline. So it already assumes that we are going to buy plots. And as Mario has said, part of it can be for the build-to-sell and part of it can be for the build-to-rent. Let's see how we can execute that before year-end, okay?

And on top of it, obviously, with EUR 200 million minimum of cash available, for sure that if we find opportunities, we will jump. But we will decide where we put the money depending on the opportunities that we see in the market. So let's see. For sure that we see that there will be good opportunities in the next 6 months.

**Operator**

(Operator Instructions) And your next question, the line of Ami Galla.

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**Ami Galla Citigroup Inc., Research Division - VP & Senior Associate**

Just 3 questions for me. The first one in cancellations. Can you give us some color as to what are the reasons why these customers are canceling their reservations at this late stage? Is there a difficulty for them to procure financing to fund their purchases?

The second question is on the sort of land market. In terms of the sort of deals that you see in the market today, can you give us some color on what sort of margin -- intake margins are you really seeing coming through the sort of pipeline?

The third question I had was on -- it's already October. So if you could give us some color as to how the sales have trended into the October month as well as your 90% forward sold for 2020. When should we expect the remaining units to sell through for this year?

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**Mario Lapiedra Vivanco Neinor Homes, S.A. - CIO**

Okay. I'll take the first one regarding the cancellation side. As I was saying, apart from the effect of the one-off online presales, the reality is that the reasons behind are quite individual like in Q3 of '19, on Q4 of '19. Basically, there are some cases of financial problems, but the (inaudible) changing that type of cancellations. We have personal motives, divorce, that type of things. But we have not, apart from the online presales, additional increase in any type.

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**Borja Garcia-Egotxeaga Vergara Neinor Homes, S.A. - CEO & Executive Director**

Okay. I'll take the next question about the deliveries and licenses for this year 2020. Okay. As we have said in the presentation, we have more or less 1,000 units delivered or under the delivery process, and we are waiting for 340 -- 336 units pending first occupancy license. Okay. We have to remark from here that in these 336 units pending of first occupancy license, we are considering one of our biggest developments from -- for this year. There is Aura homes in Madrid with 250 units that really we have requested the first occupancy license, and we really expect to have this license like in a couple of weeks. Anyway, I want to remark here that if we wouldn't have or if we wouldn't achieve this first occupancy license in a couple of weeks, we could always activate the new regulation of the community of Madrid.

I just -- I don't know if you know, in the 15th of October, it was published a new regulation of the community of Madrid. This is a modification of "La ley de suelo", the land law, which are basically that allows to the developers is not to obtain, not to achieve the first occupancy license but to make the delivery process with declaracion responsable, a responsible declaration of the developer. This is the same as it's already working in Andalucia or Valencia and that we have been using it during the deliveries of this year. So we feel comfortable that, basically, we have more than 90% of the first occupancy licenses.

Regarding the occupancy licenses that we still don't have basically are located in the North area in the surroundings of Bilbao, and it's a couple of developments. One is Iturribarri III, and the other one is Iru Bide Homes, and both licenses have been managed with the local councils. We feel also comfortable that we will get them in the next weeks.

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**Mario Lapiedra Vivanco Neinor Homes, S.A. - CIO**

If I may rescue the second one that was regarding the margins of the pipeline. The blended margins of the pipeline are in line with the target of the 24% gross margin. We are having some extra margins on the strategic land and a bit more tight margins on the fully permitted. But the blended, it's in line with the 24% committed.

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**Operator**

There are currently no further questions from the phone line, sir.

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**Jose Cravo Neinor Homes, S.A. - Director of IR**

Okay, operator. We have here one further question on the webcast from an investor, which is asking us why do we keep preselling or why have we been selling better than our peers.

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**Mario Lapiedra Vivanco *Neinor Homes, S.A.* - CIO**

Okay. Well, I'll take this one. There is -- there is not one single reason. There are a combination, I would say, of 4 factors. The first one is regarding where and at what price we acquired the land. As we have been commented, it's very important to acquire at the right price and in the right locations. In that sense, as we incorporated in that presentation, you can see our 6 main regions concentrating the vast majority of the population increase and the GDP creation. And the second factor is you should design correct for the target demand that you pursue. You know that we have been always very focused on this type of product and common areas and space and terraces that today is the most demanded. And the third thing is the correct price strategy that, in our case, has allowed us to consolidate most of the developments with financing with gains, and this is helping in this environment. And the last one, I would say, the go-to market. So we did the homeworks with our Neinor stores. We did the homeworks with our marketing online and online sales. And we did the homeworks training the commercial teams and keeping the best sellers in the market in our sales points. So I would say this combination of 4 things, it's what really make us today be resilient in that environment.

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**Jose Cravo *Neinor Homes, S.A.* - Director of IR**

Thank you, Mario. I don't think we have any further questions on the line or online on the webcast. So I think we will close today's call. And I would just like to thank everyone and say that we are available. If you have any further questions, feel free to contact us. Thanks, everyone.

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**Borja Garcia-Egotxeaga Vergara *Neinor Homes, S.A.* - CEO & Executive Director**

Thank you very much.

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**Mario Lapiedra Vivanco *Neinor Homes, S.A.* - CIO**

Thank you.

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**Jordi Argemí García *Neinor Homes, S.A.* - Deputy CEO & CFO**

Thank you.

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**Operator**

Thank you. Ladies and gentlemen, that does conclude our conference call. Thank you all for participating. You may now disconnect.

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