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Conference Title: **PHD 3Q2017 Earnings Conference Call**

Moderator: **Mamdouh Abdelwahab**

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Operator: Good day and welcome to the PHD Third Quarter 2017 Earnings Conference Call. Today's conference is being recorded. At this time, I would like to turn the conference over to Mr Mamdouh Abdelwahab from PHD. Please go ahead, sir.

Mamdouh Abdelwahab: Thank you, operator. Good afternoon everyone, and good morning for those of you joining us from different time zones and welcome to our Third Quarter Earnings Conference Call. On today's call, I have with me Mr Yasseen Mansour, the Founder and the Chairman of the company; Mr Tarek Rahman, the company's Co-CEO; and Mr Ali Thabet, the company's CFO and myself, Mamdouh Abdelwahab, the Head of Investor Relations.

On this call, we're making a brief presentation of the key highlights and then the results. And then we'll open the floor to questions. And at this time, I would like to hand over the call to Mr Yasseen. Sir, please go ahead.

Yasseen Mansour: Thank you, Mamdouh. Good afternoon ladies and gentlemen and thank you for joining our Third Quarter 2017 Earnings Conference Call. I will briefly present to you, today, the key highlights. Then, I will hand over the call to Tarek to walk you through the financial results, and afterwards we'll open the floor for questions.

We have signed, in the third quarter, the co-development agreement of the Oasis project spreading 12.6 million square meters in West of Cairo – which we consider as one of the most important milestones in the company's long-term history of achievements, moving it from developing integrated communities to building small cities – with an option also of another 3,000 feddan, or another 12.6 million square meters as an option. We are currently finalizing the project's master plan in anticipation of launching the first phase during the first half of 2018. We will be meeting with our advisors in Germany to conclude the master plan next week.

We expect the project to offer anywhere from 35,000 to 40,000 units, of which around 85% to 90% will be apartments, and the rest will be standalone units. The government will be entitled to 26% of cash revenue, payable over 20 years in addition to an in-kind payment of residential, built-up area of 372,000 square meters of core and shell, to be handed over to the government between Years 9 and 12. As I've mentioned, core and shell, plus a commercial, built-up area of 50,000 square metres in Year 12. We agreed with the government that the total cash payment should equate to EGP640 per square meter, discounted at 16%. The project will be developed over 12 to 15 years, and we expect to generate revenue in the range of anywhere between EGP160 billion to EGP200 billion over that period after deducting the government revenue share. So, for us as PHD, the total revenue will range from EGP160 billion to EGP200 billion.

Now looking into the third quarter of 2017, it was a period in which we have seen healthy residential change, stable profitability margins and solid handovers, supported the ongoing demand and uptake of our projects offering across all operating regions, backed by our strong management team and healthy financial position. Looking at new sales for the nine months of 2017, new sales grew 44% year over year to reach EGP8.1 billion, supported by growth in volume and value of units sold in recently launched projects. This figure of 8.1 equates to total sales of 2016.

While the market is still going strong, we believe we are still getting – gaining market share with 1,663 units – residential units sold during the period. Despite the challenging market condition post-flotation and Egyptian Pound and the resulting inflation we will expect, we still expect sales growth during the rest of 2017, mainly by new launched inventory in Palm Hills New Cairo and The Crown on the West – in West Cairo, keeping us on track to achieve our full-year target of EGP9.5 billion.

We have built over 1,340 units, spent EGP1.7 billion on construction and generated EGP3.5 billion in cash flows from operations. We have completed all construction works in the Village Gate project, Village Avenue, PK2 and CASA project during the first half of 2017 and expect to conclude at the end of Y2 before year-end, as we previously promised. Our financial results for the nine months of 2017 reflected our operational excellence with revenue of EGP4.8 billion, gross profit of EGP1.5 and EBITDA of EGP938 million – a growth of 30%, 32% and 34% year on year respectively. Net profit after minority interest grew 16% year on year to reach EGP467 million. Our balance sheet maintained its strong position with receivables of EGP14.4 billion covering net debt 4.4 times. We'll continue to closely monitor our construction costs which increased by 20% since the beginning of full – of Year 2017 in comparison to our selling prices, which recorded a year-on-year growth of 40% for land, 60% and 36% for built-up area of standalone units and apartments respectively.

Looking at our recurring income and commercial real estate portfolio, we stopped sales at non-core commercial projects during the summer due to low demand and seasonality, nevertheless planning to resume sales soon to capture upside potential in selling price. Our core commercial assets contributed 17% to net profit in the nine months of 2017, in line with our strategy to generate 25% in net profit from recurring income and commercial assets by end of Year 2020.

With that, I'll hand over the call to Tarek to walk you through the results. Thank you.

Tarek Abdel Rahman: Good afternoon and good morning, everyone. Thank you for joining our call.

On the operational front, we were able to achieve new sales, as the Chairman said, of EGP8.1 billion, a growth of 44% year over year as compared to 2016. We were able to generate EGP7.6 billion from residential and EGP519 million from the sale of commercial units in The Lane, which is formally known as Palm Valley Mall, Palm Central and Village Gate Kattameya Mall. It remains a bedrock of our strategy to unlock value in our commercial real estate, whether through sale of units in non-core commercial real estate plots, or through recurring income in core residential real estate plots.

Palm Hills New Cairo project continues to be the largest contributor to residential sales in 2017, complemented by strong uptake in both Hacienda West and The Crown. During the third quarter of 2017 – the third quarter alone – we recorded new sales of EGP1.9 billion, an increase of 6% or translating into 365 units for the quarter. Yes, this was mainly fuelled by both, like we said, Hacienda West and Palm Hills New Cairo where – during the quarter. In terms of number of units sold in 2017, volumes grew by 23% year on year. We sold 1,709 up from 1,385 during the same period. Since the beginning of the year, we – although there was – due to the flotation of the pound and the removal of the subsidy, we witnessed construction increase by 20%. We were more than able to pass that to our final consumer with average selling prices rising by 60% and 36% for the built-up area for standalone units and apartments respectively, and 40% for the land.

We remain comfortable – of our contracting ability to the final consumer with demand still being high for our units. And like the Chairman said, we anticipate that we are gaining market share. If we look at the region by region – and we pride ourselves as being the only developer who diversified enough to be offering product in both East and West Cairo and the North Coast – let’s look at the regional analysis. So, in West Cairo, we recorded new sales for the nine months of EGP2.4 billion. That was basically driven by sales in The Crown, which was launched in 2017 in addition to sale of commercial asset – commercial – sorry – units in The Lane and Palm Central.

New sales for the quarter, however, decreased to EGP376 million of which EGP175 million was generated by The Crown. This is basically due to the seasonality factor. We generally, and throughout all the past years, see very little demand for standalone units in Cairo in the third quarter of the year where basically, most demand centers around the North Coast and apartments in Cairo.

But you see very little demand for standalone units in Cairo. And in West Cairo up 'til now in this year, we have very little apartment offerings – mostly standalone units.

Moving to East Cairo, new sales generated a remarkable 149% for the first nine months, to record EGP3.8 billion. And the growth was also very good in the third quarter of the year, increasing by 161% to EGP573 million, basically through the sale of apartments in Palm Hills New Cairo and Capital Gardens. We sold minimal commercial real estate in the third quarter of the year: EGP14 million in East Cairo, Village Gate Kattameya.

We want to just highlight that since the beginning, since the launch of Palm Hills New Cairo in December 2016, we were able to record sales of EGP4.3 billion or 1,000 units in that project alone. In the third quarter as well, new sales – in the North Coast – sorry – new sales stood at EGP1.9 billion for the nine months, an increase of nearly 20% over the same period last year. We witnessed a very solid performance in Hacienda West, where we were able to book aggregate sales of EGP980 million by the end of the nine months. However, we launched Hacienda West in June, and so some of the – nearly half – more than half – nearly EGP500 million of the sales was recorded in June as opposed to the quarter where we usually record the sales for the North Coast. For the quarter alone, our sales witnessed EGP976 million in the North Coast, which was a decline of 34% as compared to the same quarter last year. But only because the summer started early in June, and we were able to record EGP500 million of sales in Hacienda West in June of 2017 rather than July or August.

Looking at deliveries, we were able to deliver 1,340 units, including 445 – 455 units in the third quarter, and we're on track to meet our target of 1,600 units delivered. We also recorded construction of EGP1.7 billion for the nine months, and we're on track to record EGP 2.3 – EGP2.2 to EGP2.3 billion – for the year.

Now looking at our income statement, we continued our steady focus on enhancing the company's profitability while maintaining the quality for which we are well known, which translated into profitability margins improvement. During the nine months, revenue grew by 30% year on year to reach EGP4.8 billion delivered by the increased pace of handovers – mainly in Hacienda Bay, Village Gate, Golf Extension – in addition to the sale of standalone units in Palm Hills New Cairo, Hacienda West and The Crown. We also handed over commercial units in Village Gardens Katameya, and we had a EGP110-million contribution from our core commercial assets which are the three hotels and Palm Club in West Cairo.

Gross profit grew by a remarkable 32% to reach EGP1.5 billion with gross profit margin remaining flat at 31%. SG&A recorded 11.3% of revenue yet decreased as a percentage of new sales by nearly one percentage point to 6.6%. And EBITDA grew 34% for the nine months to EGP938 billion with a margin of 20% in line with last year. Our net profit after tax also increased by 16% for the nine months to record EGP467 million, despite us witnessing a significant increase in interest expense driven mainly by the Central Bank of Egypt increasing the interest rates. And we have leverage, but there's also interest calculated on the instalments on the land, for land which we bought in cash.

Looking at the third quarter alone, revenues – revenue and gross profit saw a minor increase of 3% while the gross profit margin was flat at 35%. This was mainly due to the change of units and projects sold, mainly towards chalets and apartments rather than standalone units. Also, we – the handed-over units decreased to 455 units for the year, which is a 27% decrease, basically because we've gone through the entire backlog. And we don't have much to hand over, especially – that the old projects are coming to completion, and the new projects have recently been launched.

EBITDA for the quarter decreased 16% year on year. This is mainly due to the increase in SG&A. Because of the improved sales figures for the first nine months and converting most of that into contracts, we paid a higher commission to our sales and outside brokers. In addition, too, we are spending a lot now ramping up for the launch of Oasis. So, we're spending a lot on master planning and on increasing our capabilities and capacities to be able to deal with such a huge project of EGP12.6 million square meters.

Net profit for the quarter was also negatively affected. It declined year on year, basically due to the increase in SG&A which we just discussed, but also the increase in interest expense driven by the increase in the base rate by the Central Bank of Egypt, and in addition to the small securitization that we've done during the quarter, in which we recognized EGP25 million of interest. As you well know in securitization, you recognize the entire present value of the interest, and you take a one-time hit which eases the interest expense going forward. Our balance sheet is still extremely healthy with net debt over EBITDA at 2.6 times down from 2.8 times, and we expect it to decline further towards the end of the year. And our receivables cover our net debt 4.4 times. We are looking forward, like the Chairman explained, to launching the 3,000-feddan project Oasis, which is going to be – to sort of transform the company completely and drive our results going forward for the foreseeable future. With that, we turn it over if there – if anybody has any questions. Operator?

Operator: Thank you. If you'd like to ask a question, please press star one on your telephone keypad. If you're using a speakerphone, please make sure your mute function is turned off to allow your signal to reach our equipment. Again, press star one to ask a question. We'll pause for just a moment to allow everyone an opportunity to signal. That's star one, and we'll take our first question from Rohan Shah with Deutsche Bank.

Athmane Benzerroug: Yes, hi, good afternoon. This is Athmane Benzerroug from Deutsche Bank.

Tarek Abdel Rahman: Hi, Athmane.

Athmane Benzerroug: Hi. So, a couple of questions, if I may, first of all on the price increases for both land and the residential, actually. Can you just remind us what have been the price – increase that you have passed year on year, I would say, and also the cost increase.

Tarek Abdel Rahman: Sure, okay. So, costs increased from the beginning of the year by nearly 20%. However, we were able to increase the price of land by 40%, and the price of standalone units – built-up area – we increased by 60% and apartments by 36%.

Athmane Benzerroug: Both these are increases year to date, or year on year?

Tarek Abdel Rahman: No, year to date, yes? Year on year.

Athmane Benzerroug: Year on year.

Tarek Abdel Rahman: Yeah, year on year.

Athmane Benzerroug: And – sorry, okay, thank you – and what about the construction costs?

Tarek Abdel Rahman: The – sorry, no, no, sorry – these are – since the beginning of the year, these are increases that have occurred since the beginning of the year, and construction cost is also since the beginning of the year.

Athmane Benzerroug: Okay. And construction costs are up – [inaudible] said it's 20%, did I catch it well?

Tarek Abdel Rahman: 20%.

Athmane Benzerroug: Twenty, okay. Just on the guidance, actually, end of 9M, you realized roughly 85% of your yearly target. Why – how are you comfortable to exit the – your 2017 figures at the guidance or how do you feel, actually, for the last quarter?

Tarek Abdel Rahman: To the – look, we've guided for EGP9.5 billion. We're very comfortable in reaching the EGP9.5 billion, maybe exceeding it, but we had – we were going to launch Alexandria before the end of the year. However, the licensing of it is – has been delayed, so we expect it maybe first quarter 2018. But remember, it's not a matter of exceeding our targets because we're controlling the targets, and we have increases. So, if we reach our yearly targets, we increase to the prices of next year because as you know, this is the entire sort of strategy of Palm Hills, of having very disciplined rollouts, especially in this inflationary environment at preset prices. And once we are able to consume that volume with that price, we launch new product at a different – at a higher price to fulfill our business plans and our return profile.

Athmane Benzerroug: Okay, okay. And just to follow up on the inflation, I asked you for the year-to-date increases for selling prices and costs. But what about the inflation, actually? I'm not talking about the official inflation, but the – sorry – the inflation that you witnessed year-to-date, do you think, overall?

Tarek Abdel Rahman: I mean what we've witnessed: our main cost component is construction, so we witnessed a 20% increase in construction up 'till now. We've obviously witnessed inflation from the interest rates rising, because we have debt and the – so that also affected us because not only do we have debt, but we have land instalments, especially for The Crown, to the government. So, with any increase in interest rates, it affects us.

Athmane Benzerroug: Yeah. No, I was more talking about the interest – sorry – the inflation in Egypt overall, I would say.

Tarek Abdel Rahman: Yeah.

Athmane Benzerroug: Just to see how the real estate is performing versus the inflation, actually, in the country.

Tarek Abdel Rahman: Like I said, our costs – we've only – the major costs we're going to spend increase in construction.

Athmane Benzerroug: Okay. So, I just wanted to better understand. It seems that the – for a while now, you have been able to pass new price increases despite a quite high inflationary environment. I'm just wondering where the money comes from, actually. How actually the prices can be so strong, and therefore the [inaudible] seems to not be hit? So can you just shed some lights with us, explaining – us what is triggering a [inaudible] to buy more and more units?

Tarek Abdel Rahman: Of course. Look we – yeah, the thing is –

Athmane Benzerroug: Wages are increasing also – that – my question is wages are also increasing at this level, so it's more people are easily leveraging[?], or I don't know.

Tarek Abdel Rahman: No, on the wages side we've seen – with all sorts of big, major companies and banks – we've seen a significant increase that everybody's done in the beginning of the year, to the – increase, to be able to deal with the inflation that was happening because of the flotation, and the increase in interest rates and the removal of the subsidy. So, most companies have increased their wage bills by anywhere between 25% to 30%, which is a one-off thing that usually does not happen. However, we've always explained that our ability to sell more and more is because the numbers we're selling are small in terms of total demand. Us and other developers, frankly, are small. It remains to be a completely under-supplied market. We sold, for the first nine months, 1,709 units in a country with 100 million people. We understand that's not our investible market. We figure our investible market is probably 70,000 to 100,000 units a year, and this not being fulfilled. All the developers are selling, combined, about 25,000 units a year. So, you see, you're only able to increase prices and sell because the numbers you're selling are just too small in terms of actual volume.

Athmane Benzerroug: Okay. It's very clear, thank you very much. My follow-up question is just on the land liabilities. In the third quarter, you had an impact on – in your P&S. So, I just wanted to get a clear – an idea of the number: how much do you pay to the government, and how much it should be, actually, for 2017 and '18 on an annual basis, just to get a sense of – yeah, what you – what we – impact.

Tarek Abdel Rahman: The land liability? The land liability, did you say how much we paid for the first nine months?

Athmane Benzerroug: Yes, or how much do you spend and how much do you expect for 2017 and 2018 full-year?

Tarek Abdel Rahman: Okay.

Speaker: In land liability [Arabic, 0.24.28 – 0.24.37].

Tarek Abdel Rahman: Okay. So, we've paid, in the first nine months, EGP500 million.

Athmane Benzerroug: In the first nine months.

Speaker: Yeah. [Inaudible], what's the land liability for 2018 and '19?

Tarek Abdel Rahman: We're getting – we're getting the figures.

Athmane Benzerroug: Can I ask another question, or should I wait?

Tarek Abdel Rahman: Of course. No, no, go ahead, and we'll get the figures.

Athmane Benzerroug: Yeah, okay, thank you very much. So, this is my last question, sorry. So just on the cash generation, actually, you are still generating negative cash flows. When do you expect, actually, these to reverse, first of all? And the additional question to this is – and we have the main shareholder also on this call – so when to you expect, actually, PHD to distribute dividends – to start to distribute dividends?

Tarek Abdel Rahman: Look we – on the cash flow, we expect to impact cash flow positive on operate[?], cash flow positive in 2018. That's always been the plan, where we were ramping up our construction capabilities over the last four years, or our construction activity over the last four years. We've been constructing much more than we've been generating cash consciously: number one, to finish the projects that were started, the old projects – which we call 'the old projects' – which should be done in the coming – this year or next; and to try and mitigate the effects of inflation as much as possible because the more you build on the old – with the old rates, the more money you make. So, expect 2018 to turn cash flow positive.

And I mean on the dividends, I think based on the 2018 cash flow, we've said that once we turn free cash flow positive, we're going to distribute 30% of that to shareholders.

Yasseen Mansour: Either distribute or have them buy back book. This is Yasseen. Just to add to what Tarek has said, the company Palm Hills should be turning – about EGP16 billion into free cash flow over the coming 11 years, okay? It will – a lot will depend on also the interest rates environment. As we had mentioned before, I mean now, because we have been delivering a lot of units, we have receivables that we can discount or securitize off balance sheet. It's up to us to choose the timing. As we have mentioned before, we were looking to achieve that. But due to the fact that, as soon as you discount or you securitize, you have the interest rate paid up front. We don't want to do it now with an interest rate environment of 19.25%. So, we're waiting 'til the interest drops, and then this is when we could afford to securitize for EGP1 billion or EGP2 billion, or even more, and either pay off dividends or more than likely, just have the buyback program.

Tarek Abdel Rahman: Sorry, on your land liability question? Hello?

Athmane Benzerroug: Hello?

Tarek Abdel Rahman: Yeah, you had a question on land liability. So 2000 and seven –

Athmane Benzerroug: No. Yeah, 2017, sorry.

Tarek Abdel Rahman: Yeah, 2000 and – the last quarter of 2017, we were supposed to pay EGP347 million, of which we'd already paid EGP270 million. 2018: we should pay EGP886 million; 2019: EGP561 million.

Athmane Benzerroug: Okay. And this is accounted in the accounts, no?

Tarek Abdel Rahman: Mm-hmm.

Athmane Benzerroug: Yeah, okay. Thank you very much, gentlemen.

Tarek Abdel Rahman: You're welcome.

Yasseen Mansour: Thank you.

Operator: As a reminder, if you'd like to ask a question, it's star one on your telephone keypad. For our next question, we'll go to Al Qureiyeh with RWC Partners.

Al Housein Qureiyeh: Hi everyone and congratulations on the number; a couple of questions, if you don't mind. Again, this is Al Qureiyeh from RWC Partners. Early in the call, we've talked about the new joint venture with the government but sorry, we've lost the connection for a while, so we couldn't hear, really, the expected revenue. And – so to confirm, the project is expected to be delivered on 12 to 14 years, and you said revenues are expected to be EGP160 billion after the deduction of the government revenues, is that correct?

Speaker: Yes.

Yasseen Mansour: Yes, it's – the – it's 12 to 15 years, and the expected revenue will be anywhere from EGP160 billion to EGP200 billion. This is Palm Hills' share of revenue, not including the 26% that goes to the government.

Al Housein Qureiyeh: And you said the government will take 26% of the cash revenue over 20 years, correct?

Yasseen Mansour: Yes, over 15 years.

Al Housein Qureiyeh: And you said how much was in kind – in-kind payment?

Yasseen Mansour: Sorry?

Al Housein Qureiyeh: Over 15 years. And the in-kind payment?

Yasseen Mansour: Yeah.

Speaker: They take it [inaudible].

Yasseen Mansour: The in-kind payment is 375,000 square meters of core and shell.

Al Housein Qureiyeh: Okay.

Yasseen Mansour: That – sorry, 372,000 square meters of residential core and shell, and 50,000 square meters of commercial core and shell also.

Al Housein Qureiyeh: 50,000.

Yasseen Mansour: Yeah. 50,000 commercial, 372 – 3-7-2,000 residential.

Al Housein Qureiyeh: Yeah, 50,000 commercial and 375,000 residential.

Yasseen Mansour: 72 – 72,000.

Al Housein Qureiyeh: 372, okay. Again – and sorry, I know – often asked the question – but again, if you can walk us through, again, the finance costs – the major increase in finance costs. So, the securitization of notes receivable, which is EGP24,715 on the financials – this is the discount, right, that you had to use on the receivables?

Speaker: Yes.

Al Housein Qureiyeh: Okay. And the finance cost, which is the EGP82,000, includes the interest rates plus what? Or it's only pure finance costs? It's jumping from EGP16,000, EGP17,000 in third quarter 2016 to EGP82,000. This is because of the devaluation?

Tarek Abdel Rahmin: Okay, the finance costs include – sorry – so the 25 – there's EGP116 million securitization and notes receivable. That's the cost for the nine months. And then the jump in the finance cost is mainly from – for the quarter from 16 to 82, is mainly the increase in interest rates and our payment – interest and principal – on the leases that we have.

Al Housein Qureiyeh: Okay, okay. Last question on the presales or the pre-orders, or you call it 'new sales,' the 9 Month is up 44%, which is very strong, though in the third quarter it was down 6% year on year. How do you see – I understand that you said you're still comfortable with our target – EGP9.5 billion by the end of the year…?

Tarek Abdel Rahman: Yeah.

Yasseen Mansour: Yes. Look, the reason – one of the main reasons that the third quarter was negative compared to quarter on quarter is due to the fact that, as we had earlier mentioned – due to the seasonality during the summer months. So mainly the sales in the summer – is in the North Coast. We are depleting our inventory in both projects in – on the North Coast, which are mainly Hacienda White and Hacienda Bay. And the only project we had was Hacienda West, which is a new launched project. But as Tarek had mentioned earlier on, we launched this project – usually we launch them during the third quarter. But due to the fact that Ramadan comes early every year, so the summer started a little bit earlier, and we launched in the middle of June. So, there is EGP500 million that we have seen as new sales coming into June from the North Coast. So, if this was not the case, and we had launched in July – the new project Hacienda West – you would add EGP500 million to our sales, which would put you in a positive territory.

Al Housein Qureiyeh: Okay, okay. And as you've said, you're going to delay the – and this is my last question – you're going to delay the securitization of the receivables 'til the end of quarter one where you expect trade coming down. In case, if they don't come down, you expect to wait until you get a reasonable interest rate, so you don't get a major discount like the one [inaudible].

Tarek Abdel Rahman: Right, yes. We – we –

Yasseen Mansour: Look, our – our –

Tarek Abdel Rahman: Go ahead, sorry.

Yasseen Mansour: We think that the interest rate will start to drop. There are two Monetary Policy Committee meetings during 2017: one is in November, and the other is in December – end of December, December 28th, to be exact. We think that probably November maybe we will not see an interest rate reduction, but we foresee an interest rate reduction probably on the December Committee meeting. This is not – it isn't – it's not really an assumption because this is what the government has been hinting from both the Governor of the Central Bank and the Ministry of Finance. So basically, this is what we've been hearing all along.

Al Housein Qureiyeh: Okay, understood. Thank you so much.

Speaker: Thank you.

Operator: Once again, it's star one if you'd like to ask a question at this time. That's star one on your telephone keypad. And it appears there are no further questions. So, at this time, I'll return the conference to Mr Mamdouh Abdelwahab for any final remarks.

Mamdouh Abdelwahab: Thank you, operator. And thanks, everyone, for attending the call. Please contact the Investor Relations team in case of any follow-up questions. See you soon, bye-bye.

Speaker: Thank you.

Operator: This does conclude today's conference. Thank you for your participation. You may now disconnect.