Brookfield Residential Properties Inc.

2012 Third Quarter Results

Conference Call & Webcast Transcript

Date: **Wednesday, November 07, 2012**

Time: **11:00 AM ET**

Speakers: **Alan Norris**

President & Chief Executive Officer

Craig Laurie

Executive Vice-President & Chief Financial Officer

OPERATOR:

At this time, I would like to turn the conference call over to Mr. Alan Norris, President and Chief Executive Officer. Please go ahead.

ALAN NORRIS:

Thank you. Good morning ladies and gentlemen, and thank you for joining us today for Brookfield Residential's Third Quarter Conference Call. On the call with me today is Craig Laurie, our Chief Financial Officer. I will provide some comments on the current markets and outlook going forward, and Craig will then discuss financial highlights of our operations and results. I would at this time, remind you that in responding to questions and in talking about new initiatives and our financial and operating performance, we will make forward-looking statements. These statements are subject to known and unknown risks and future results may differ materially. For further information, I would encourage investors to review my Letter to Shareholders and our interim report, which are available on our website.

Our performance remained very strong in the third quarter, building on the excellent results achieved throughout the year. We are well-positioned as we move into our, key, fourth quarter period. Given the nature and operating cycle of our business, our fourth quarter typically accounts for the highest proportion of the year's income before income taxes. Based on current backlog, we expect fourth quarter 2012 results will be similar to those seen in 2011.

For the nine months ended September 30, 2012, net income increased significantly to $37 million from a loss of $19 million during the first nine months of 2011. The net loss in the prior period was largely the result of a one-time valuation allowance taken against the Company's U.S. deferred tax assets on completion of the merger. As stated in my Letter to Shareholders, the comparative statements for 2011 do include certain one-time merger items. Throughout 2012 we continue to break out normalized and non-recurring items for 2011 so that you can better gauge our performance. We remain very optimistic about longer term growth prospects, as we are well-positioned for growth in the Canadian and US markets.

In Canada, a recent forecast issued by the Conference Board of Canada in the Metropolitan Outlook focused on Alberta. Edmonton and Calgary are expected to lead the country in growth over the next four years.

I would like to highlight two strategic achievements that transpired in the third quarter. We received area structure plan approval for 1,400 acres on the North Stoney Lands in Calgary, which now enables us to proceed to final land use and subdivision approvals, with a view to commencing development in 2015. As the Company already who owns 400 acres adjacent to this property, the combined parcels will support development of over 13,000 lots. Another key development was the acquisition of 370 acres located within one of the last large land assemblies in the popular Northwest Calgary, where land constraints have shrunk its market share. It is expected that entitlements will take up to four years, and development is set to commence in 2016. As a residential leader in Alberta, we feel that we are well positioned to capitalize on this growth going forward.

In the U.S. analysts are also providing a more positive view of the U.S. housing market, with housing inventories now reaching low levels and prices stabilizing. As indicated on the call last quarter, we have noticed that regional markets that we operate in are experiencing a shortage of new service lots on which to build. This is a very positive development for a company such as ourselves, as we have significant land holdings in key U.S. markets.

As house prices increase, we expect to see a substantial positive impact on underlying land values. Over the past several quarters we have been enhancing our corporate profile, which is posted on our website to provide information to better understand our business and our land investments across North America. Based on our current visibility and backlog for the fourth quarter, we are predicting that we will meet or surpass our guidance targets outlined for 2012. Our fourth quarter should be similar to what we saw in 2011, which would put income before tax for the fiscal year 2012 well ahead of the recurring income before tax of $80 million in 2011. We believe that the short and long term prospects of our business remains excellent.

I would now like to turn to the call over to Craig, he will discuss our financial performance for the three and nine months ended September 30, 2012.

CRAIG LAURIE:

Thank you, Alan and good morning everyone. Our results for the third quarter of 2012 improved over the same period last year. Net income for the three months ended September 30, 2012 totaled $15 million, or $0.15 per share, compared to $19 million, or $0.19 per share, for the three months ended September 30, 2011. Net income for the nine months ended September 30, 2012 totaled $37 million, or $0.37 per share, compared to a net loss of $19 million, or a loss of $0.19 per share for the nine months ended September 30, 2011.

As Alan mentioned, the comparative statements for 2011 do include certain one-time items, such as the valuation allowance against the Company's U.S. deferred tax assets on the completion of the merger in the first quarter of 2011, as well as other non-recurring items as a result of the merger that impacted revenue and net income. Specifically, the first nine months of 2011 included $58 million of income before tax from a non-recurring change of business practice. And the first quarter of 2012 included $9 million of interest on the transaction debt that was not included in the comparable period in 2011. Taking these items into account, income before income taxes for the three and nine months ended September 30, 2012, improved $13 million and $50 million on a comparative basis over the same periods in 2011, reflecting improved operating results.

Financial highlights from the reporting period are as follows; for the three months that ended September 30, 2012, land revenue totaled $62 million compared to $116 million in the same period of 2011. Approximately $43 million of the land revenue from 2011 was due to the non-recurring change in business practice for lot sales in Alberta. Taking this into account, normalized, land revenue decreased by $11 million over the same period of 2011. Canadian single-family lot closings accounted for $8 million of this decrease, and Canadian multifamily, industrial, and commercial parcel sales accounted for the remaining $3 million.

While selling prices remained relatively constant year-over-year, there was a marginally decrease of 27 lots and 7 acres in the current year period, reflecting the timing of closings. During this period, housing revenue increased to $183 million from $112 million during the same period of 2011. This reflects a 55% increase in home closings, and a 5% increase in the average home selling price. Sales activity continued to be strong in the third quarter, particularly in Canada, California, and the Washington D.C. area, with a 19% year-over-year increase in overall net home orders.

For the nine months ended September 30, 2012, land revenue totaled $215 million, compared to $359 million during the same period in 2011. Approximately $153 million of the land revenue from 2011 was due to the change in business practice noted previously. Excluding non-recurring revenue normalized land revenue for the nine months ended September 30, 2012 increased by $9 million, or 4% over the same period of 2011. The increased in normalized land revenue is mainly driven by the sale of multifamily and commercial parcels in Canada. Additional lot closings particularly in the Canadian and the Central and Eastern U.S. operating segments also contributed to the increase in normalized revenue. During this period, housing revenue increased by $125 million compared to the same period in 2011. This improvement reflects a 41% increase in home closings compared to the same period in 2011; the backlog of units also increased by approximately 35% to 1,095 homes from 813 homes, with this increase primarily reflecting stronger sales demand.

Moving to our balance sheet, as of September 30, 2012, our primary asset; our land and housing inventory totaled $2.3 billion, or approximately 82% of our total assets, similar to the prior quarters. Our land and housing assets include homes completed and under construction; lots ready for construction; model homes and land under and held for development. Total acquisitions in the third quarter were $76 million, consisting of $70 million in Canada and $6 million in the U.S. The Canadian acquisitions related to the 370 acres in Northwest Calgary described in the press release. Total acquisitions for the nine months ended September 30, 2012 were $187 million, with $129 million in Canada and $58 million in the U.S. operations.

Thank you for joining us in our quarter end conference call. I will now turn the call back over to the Operator who will moderate questions.

OPERATOR:

Thank you. Our first question today comes from Stefan Mykytiuk of Pike Place Capital.

STEFAN MYKYTIUK:

Good morning. Just a couple of questions, you talked about meeting or exceeding the guidance you gave on the last call about the number of homes you're going to sell in both the U.S. and Canada and the lot sales. If I got that right, it basically implies Q4 in Canada you're going to have maybe a 4% or 5% increase in home closings, and in the U.S., in California, your home closings are basically going to triple from last year, and be up kind of 50% or something in the Central and Eastern?

ALAN NORRIS:

I think we were giving some indications on unit counts, but now we've got pretty good visibility at the end with the number of lot sales that were going on, some bulk sales in the U.S., and some partial sales. Generally speaking we're really trying to outline that we think is going to be very close even from a bottom line point of view to where we were Q4 last year as well, from an actual dollars and cents point of view. We are expecting to be up slightly more on the closing side, but we will get a few other partial sales which are closing off on commercial and industrial this quarter in Canada, as well as a few bulk deals that we're working on in the U.S. So the combination is all positive.

STEFAN MYKYTIUK:

Okay, yes. What I was getting at, is assuming you are still targeting those kind of levels of housing unit sales for the year, it would seem to imply that your Q4 this year should be actually greater than it was last year, unless for some reason the land sales or the lot sales or the partial sales are going to be down year-over-year. Am I missing something?

ALAN NORRIS:

I'm just trying to relate back to Q4 2011 on some of the lot sales last year. Stefan, with respect to the actual mix of actual lot sales, Q4 2012 and Q4 2011, and house closings we are improving in D.C. and I mean we have obviously got the Bay Area, where we are going to have hopefully close to 60 closings in Q4 this year. We had nothing literally in Q4 2011 last year, because it's really some of the land that we bought about 12 or 18 months ago in the Bay Area now starting to come through to fruition that we have touched on in past calls. So, there's definitely an increase just on the Bay Area alone, with many of the projects that we have going up in northern California.

CRAIG LAURIE:

I can just add to that, Stefan. To your point if you were to look at last year, and then relate it to kind of the unit count guidance, as well as the dollar guidance that we have given, what you would see as you said, the Canadian home sales are probably similar to last year, up marginally. In the U.S. we have 123 in the fourth quarter of last year, and we've done 292 to date. So, to get to the 550, obviously that's a bigger quarter than the fourth quarter, and Alan commented with what would drive that. Obviously, there will be more acre sales in this fourth quarter than there were last year. I think we have done 26 or so to-date. I think the fourth quarter of last year we would have done roughly 28, and we had given guidance of 80. There'll be additional acre sales and in terms of the lot sales, in Canada they'll probably roughly track where they were the fourth quarter of last year.

STEFAN MYKYTIUK:

Okay. So, lot sales kind of flattish year-over-year; for Q4?

CRAIG LAURIE:

In terms of in Canada, yes it's probably flattish, obviously there's been better margins so far. The home sales in the fourth quarter will be roughly flat to last year, and then the U.S. will be up materially and the acre sales will be up materially. I'm just comparing to two fourth quarters.

STEFAN MYKYTIUK:

Correct. I guess that's my point, Craig, is I'm saying, given what you're telling me, it sounds to me like Q4 this year should actually be better than it was year ago, and you're saying that it should be about the same on a net-income basis.

CRAIG LAURIE:

Yes.

STEFAN MYKYTIUK:

Just one other question which is you've mentioned, and certainly a lot of your counterparts here in the U.S., that homebuilders have been talking about lot shortages. What are you seeing in some of the markets they've cited, California, Texas, are you thinking about starting to let some of your lots go that you've invested in the past few years, or are you still waiting for prices to improve?

ALAN NORRIS:

We're starting to see some of it Stefan, we've got for instance in the Inland Empire in California, I mean the coastal areas in California have always been tight, have been for the past the 12 to 24 months. In the Inland Empire, we're starting to see some movement, builder interest and some of the lot sales we're planning to close between now and the end of the year. I'm actually in Austin right now, on the call and we're seeing one of our communities in Austin where we only had say two builders last year, we've now actually got five builders working in that community. So there is a perception of a shortage of lots and we are seeing it in a number of different spots. We're seeing a lot of it the same in D.C. as well. So, it is starting to happen. We are seeing some pressure on some of those areas pricing-wise but it will take a little bit of time as we are seeing some other nationals coming to the fore, and wanting to acquire lots in some of the those locations to start to build their backlogs.

STEFAN MYKYTIUK:

Okay. Terrific. Thanks very much.

ALAN NORRIS:

Thank you.

OPERATOR:

There appear to be no further questions at this time. I will turn the call back over to Mr. Alan Norris for closing comments.

ALAN NORRIS:

Thank you once again everyone for taking the time and dialing in. We are feeling very good about our situation as a Company. Hopefully we will hear from you again over the next quarter, and as we close off the end of the year and we do our year-end call. So, again, thanks once again for taking the time.

OPERATOR:

Ladies and gentlemen, this concludes today's conference call. You may now disconnect your lines. Thank you for participating, and have a pleasant day.