Bridgemarq Real Estate Services Inc

2019 Fourth Quarter and Annual Results Conference Call

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CORPORATE PARTICIPANTS

Phil Soper
Bridgemarq Real Estate Services Inc — President and Chief Executive Officer

Glen McMillan
Bridgemarq Real Estate Services Inc — Chief Financial Officer

PRESENTATION

Operator

Good morning. My name is Jason, and I would like to welcome everyone to the Bridgemarq Real Estate Services Incorporated 2019 Fourth Quarter and Annual Results Conference Call. All lines have been placed on mute to prevent any background noise.

After the speakers' remarks, there will be a question-and-answer session. If you would like to ask a question, simply press *, then the number 1 on your telephone keypad. If you would like to withdraw your question, press the # key. Thank you.

I would like to introduce you to Mr. Phil Soper, President and CEO of Bridgemarq Real Estate Services Incorporated. Mr. Soper, you may begin your conference call.

Phil Soper — President and Chief Executive Officer, Bridgemarq Real Estate Services Inc

Thank you, Jason, and good morning, everyone. With me today is our Chief Financial Officer, Glen McMillan. We welcome you to our call.

Following the usual format of our quarterly conference call, I will begin with a brief overview of the quarter and annual results. Afterwards, Glen will discuss our financial results, and I'll conclude by providing some remarks on recent business operational highlights and market developments. Following our remarks, both Glen and I would be happy to take your questions.

I want to remind you that some of the remarks expressed during this call may contain forward-looking statements. You should not place reliance on these forward-looking statements because they involve known and unknown risks and uncertainties that may cause actual results and performance of the Company to differ materially from anticipated future results expressed or implied in such forward-looking statements.

I encourage everyone to review the cautionary language found in our news release and all of our regulatory filings on our website and SEDAR.

Overall, we are pleased with the Company’s financial performance in 2019. Revenue was up 5.5 percent compared to 2018. Revenue in the fourth quarter was up 19.3 percent over Q4 2018. A significant driver of this growth has been the recovery in unit sales in the greater regions of both Toronto and Vancouver as well as the addition of new ancillary revenue streams.

Later in the call, I will go into regional real estate trends. Also, Glen will provide more details on our financials.

2019 was another year of network growth. As of December 31, 2019, the Company had 19,111 realtors in our network, up from 18,725 at the end of ‘18.

On our last call, I spoke about our new digital platform, rlpSPHERE, which was announced in the fourth quarter of 2019. There is growing excitement for this end-to-end real estate brokerage solution, and we plan to complete a phased rollout across the country in 2020, starting in the spring. We are optimistic that rlpSPHERE will be a strong market differentiator that attracts new brokerages and realtors to the Company’s brands. I’ll speak more on this business development later in the call.

During 2019, the Company distributed dividends of 12.8 million to shareholders. Yesterday, the Board of Directors approved a dividend payment on April 30th of $0.1125 per share to shareholders of record on March 31st. This indicates an annualized dividend of $1.35 per share. The Company remains committed to paying out a significant portion of distributable cash flow to shareholders, subject, of course, to working capital requirements and availability of other attractive growth opportunities.

During the quarter, there was a significant shift in unit sales volumes in Greater Toronto and, in the third quarter, Greater Vancouver. We are seeing this trend extend into 2020. We believe that the mortgage stress test introduced in January 2018, which triggered a significant market correction across the country, has finally been absorbed into market, and equally as important, consumers have regained confidence in real estate markets. I will go into this in more detail later in the call and provide an update on recently announced changes to both the mortgage stress test and the recent Bank of Canada interest rate announcement.

Like every organization today, we are concerned about the impact of the coronavirus on our people and the clients and communities we serve. We are taking steps to ensure best practices are followed, guided by directives from the Public Health Agency of Canada and the Health Portfolio Operations Centre, which has been activated to support effective coordination of federal, provincial, and municipal resources. Further, we have business continuity and resilience protocols in place that can be activated in the case of virus-related office closures. We are an agile business with the demonstrated ability for almost all of our staff to work remotely.

And with that, I'd like to turn the call over the Glen for a look at our fourth quarter and full year financial performance in more detail.

Glen McMillan — Chief Financial Officer, Bridgemarq Real Estate Services Inc

Thank you, Phil, and good morning, everyone. As Phil mentioned, revenue in the fourth quarter was up 19.3 percent over last year, rising to $10.7 million. For the full year, revenue rose to $44.3 million from 42 million in 2018, an improvement of 5.5 percent.

In January of 2019, as a result of amendments to the Management Services Agreement between the manager and the Company, the manager transferred certain contracts, giving the Company the right to earn revenues that were previously earned by the manager. These ancillary revenues represented $1.2

million in the quarter and $4.4 million for the year. Partly offsetting these revenue increases was the 2018 expiry of the obligation for certain brokerages in the GTA to pay premium fees.

Net earnings in 2019 were $3.1 million as compared to 17.4 million in 2018. The primary drivers of the reduction, despite higher revenues, are the determination of the fair value on the exchangeable units issued by the Company, an increase in management fees under the terms of the recently amended Management Services Agreement, and higher amortization of intangible assets. Net earnings in the fourth quarter were $1.3 million compared to 8.9 million last year when we recorded a $7.3 million gain on the fair valuation of the exchangeable units.

Distributable cash flow for the full year rose 19.1 percent to $17.2 million, or $1.34 per share, compared to 14.4 million, or $1.13 per share in 2018. For the fourth quarter, distributable cash flow was $4 million compared to 3.1 million last year, an increase of 29 percent.

In the quarter, the Canadian residential real estate market was $57.3 billion, up 24 percent compared to Q4 last year. This increase was driven by a 15 percent increase in unit sales and a 3 percent increase in average selling price. For the full year, the Canadian market was up 9 percent at $244.9 billion, reflecting a 7 percent increase in units and a 3 percent increase in average selling price.

The Greater Toronto real estate market saw a significant year-over-year improvement during the quarter, rising 23 percent to $16.8 billion. The primary driver was an increase of 14 percent in unit sales and an average selling price increase of 4 percent. And as a point of reference, the GTA represents just under 30 percent of the national housing market.

The Greater Vancouver market closed up 52 percent at $7.5 billion compared to 2018 in the quarter, driven by a 58 percent increase in units sold, partly offset by a 6 percent decrease in average selling price.

Market activity in the Greater Vancouver area was largely stalled during 2018 and the first part of 2019 as consumer confidence and previously introduced provincial tax measures weighed on the markets.

During the fourth quarter, the Greater Montreal area closed up 24 percent at $5 billion compared to last year. This reflects a 17 percent increase in units sold and a 6 percent increase in average selling price.

And Phil will now provide additional insights into the markets and an update on our operations.

Phil Soper

Thanks very much, Glen. On Wednesday, the Bank of Canada lowered its overnight rate, the target rate, by 50 basis points to 1.25 percent. This reduction was attributed to domestic signs of economic drag from things such as the rail line blockades and weakness in the global economy as nations grapple with coronavirus-related health concerns.

This is a significant reduction in the cost of borrowing and could bolster home sales activity across Canada as affordability barriers are lowered. This, of course, will be balanced by the unknown economic impact of COVID-19, the disease caused by the coronavirus.

Another policy decision that is supportive of real estate market activity was made on February 18th. The Canadian Government announced a change to the federal mortgage stress test, which was initially implemented back on January 1, 2018. Currently, buyers have to be able to afford payments at an interest rate that is 2 percent higher than the Bank of Canada's five-year rate. Beginning on April 6, 2020, in a few weeks time, the benchmark will be the 5-year fixed insured mortgage rate plus 2 percent. The government is seeking input at this stage as to whether this will impact just insured mortgages, as is the case now, or will include uninsured mortgages.

These changes do reduce the barriers that people have to get into the market, as it makes the hurdle for qualifying to obtain a mortgage lower.

As I've said on previous calls, confidence in the Canadian job market is fundamental to a healthy real estate market. When people are confident about their employment, they are confident about carrying a mortgage. In January, employment grew by 35,000 full-time positions, and the unemployment rate fell 0.1 percent to 5.5 percent. It should be noted that if the drag of the coronavirus on the Canadian economy is significant and sustained, we could see it negatively impacting employment numbers; again, an unknown.

We talked about the surge of sales in Canada's three largest markets. I wanted to drill down into what this means for each respective market.

To start with our largest city, the Greater Toronto area. A spike in sales is a signal that the trend of weak activity, of housing activity, that began in January 2018, when the federal mortgage stress test hurdle was first introduced, it has likely been absorbed, or people have found a way to either acquire more money for a down payment; they've adjusted where they're looking for homes; or potentially the size and cost of the home they're looking at. It's an adjustment we expected, and it took about a year and a half for consumers across the country to adjust.

One thing in particular about the Greater Toronto area is that we just don't have the level of housing inventory, the number of homes available for sale, needed to meet the demand if the growth rate of year-over-year unit sales is maintained. If demand rate remains consistent and inventory remains low, as was the case in the first weeks of 2020 and at the end of 2019, there is a strong possibility that we could see significant price appreciation in the region.

Unlike the Greater Toronto area, inventory in Greater Vancouver has been growing in response to a government policy designed to improve affordability. There has been the inventory to absorb the demand, which has kept a lid on price inflation. However, the market is quickly tightening, and we could see that gap closed and upward pressure on home prices.

The pace of unit sales in Greater Montreal is beginning to exhaust inventory in that region as well. For the full year 2019, active listings were down 19 percent. In January of 2020, active listings were down 28 percent year over year while sales were up 30 percent, obviously shifting what is a balanced market towards a seller’s market.

We are also seeing similar low-inventory, high-demand environment in Ottawa. Sales of residential and condo units were up 6.6 percent in ’19 compared to ’18. January residential sales in the region decreased 4.5 percent, and the Ottawa Real Estate Board is attributing the sales decline to a lack of inventory. They just don’t have the homes to sell at this stage. Of course, this puts upward pressure on price. The January benchmark price for a home in Ottawa climbed 13.7 percent year over year.

Even the Calgary real estate market, which has struggled since the 70 percent drop in the value of oil at the end of 2014, has been showing improvements. We saw a 1 percent increase in sales, largely due to—in 2019, largely due to a stronger second half. The region does continue to have an oversupply in some categories, but it is quickly coming into balance as that supply is absorbed.

This increase in sales will help stabilize the local real estate market, but it would require consistent demand improvement over time before we would expect to see a material increase in prices. For example, even though we saw home prices climb by 11 percent in the month of February 2020, readers would have to look at February 2019, which was one of the weaker months for real estate sales in Calgary in almost 20 years. So year-over-year comparisons, it’s very important to look at what we are comparing things to. All that said though, and coronavirus and other unknown economic variables aside, we are expecting improvement in the Calgary market in 2020.

The Company is committed to putting game-changing technology in the hands of our real estate network. Our technology is sought out by top performance in the industry, and it enhances productivity of both our brokerages and their salespeople across the network. We are proud of our history of introducing new technology in real estate services right from Royal LePage being the first real estate company in Canada to launch an internet website way back in 1995. We were also the first national brand to bring the market things like online school search, home valuations, and lifestyle information.

Our newest venture, rlpSPHERE is our most ambitious yet. This digital ecosystem seamlessly brings together all of the tools and systems that the national company and the local brokerage franchisees and their agents need to more easily operate their business and grow their top lines. We expect the platform to finish rollout in 2020, and things will get underway this spring.

In the first half of the year, our Via Capitale business launched a new marketing tool that promotes listings to over 250 million online visitors in 65 countries. Also, in the second half of 2019, Via Capitale underwent a brand refresh and unveiled a new, more contemporary logo and realtor signage.

Royal LePage Commercial entered a three-year partnership with a leading commercial real estate data provider to provide the brands network access to residential development data, commercial sales data, and leasing availability information. The brand also continued to enhance its offerings to real estate commercial teams through a series of in-person coaching and training programs.

The Company had a strong year in enhancing brand awareness through industry-leading public relations and media awareness programs. During 2019, in addition to publishing its quarterly Royal LePage

House Price Survey and forecast, luxury property releases, and recreational property releases, the Royal LePage brand issued its newcomer release, which was well received by the media and network.

This particular study focused on new Canadians, those who have moved to Canada within the past 10 years, and looked at both demographic trends and real estate buying intentions in this all-important demographic. Key findings included that newcomers represent one in every five real estate sales and will represent over 680,000 purchases over the next five years.

Other new releases and studies in 2019 included a price-per-square-foot piece and a joint release with Genworth Canada on first-time home buyers. Genworth Canada is the largest private mortgage insurer in Canada.

In conclusion, despite considerable market challenges in the first half of 2019, the Company has remained profitable and grown our network. There will be economic drag from the COVID-19 outbreak. We know that. At this stage, it’s not possible to determine if this will directly impact the Canadian real estate market. We are taking steps to protect our people, our clients, and the business overall.

The market has moved through its recovery stage after the correction triggered in January of 2018 by the introduction of the federal mortgage stress test, and it extended into the first half of 2019. We anticipate a return to healthy trajectory. Sales are up in previously lagging Greater Toronto and Vancouver regions, reflecting improved consumer confidence.

Our business produces a reliable revenue stream that supports our goal of paying regular dividends to investors as well as strategic investments supportive of the Company’s leadership position in brokerage services. rlpSPHERE is a good example of our leadership in technology that is expected to grow both our network’s productivity and profitability.

With that, I will turn the call back to Jason, our Operator, and open things up for questions for Glen or I.

Q&A

Operator

Certainly. At this time, I would like to remind everyone, in order to ask a question, please press *, then the number 1 on your telephone keypad if you would like to ask a question. We will pause for just a moment to compile the Q&A roster.

Again, if you would like to ask a question, please press *, then the number 1 on your telephone keypad.

We have no questions over the phone at this time, so I will turn the call back to President and CEO, Phil Soper, for closing comments.

Phil Soper

I wish to thank everyone for participating in today's call and look forward to updating you on the business and industry in more depth at our Annual General Meeting, which will take place on May 12th at 10 a.m. in Toronto. That's May 12th at 10 a.m. in Toronto. The details are available on our website, at the Bridgemarq website.

Thank you all and talk then.

Operator

That concludes today's conference call. You may now disconnect.