Vesta Industrial Real Estate

Second Quarter 2021 Results Conference Call

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PRESENTATION

Operator

Welcome to the Vesta Second Quarter 2021 Results Conference Call.

I would now like to turn the call over to your host for today's call, Ms. Claudia Medina, Vesta's Head of Communications. Please go ahead.

Claudia Medina

Thank you and good morning. Welcome to Vesta's conference call to review our second quarter 2021 results.

On today's call will be Lorenzo Dominic Berho, Chief Executive Officer, and Juan Sottil, Chief Financial Officer.

Our results were released yesterday afternoon and can be found on the Investor Relations section of our website, along with our supplemental package and the appropriate filings with the Mexican Stock Exchange. A replay will be available shortly at the conclusion of the call.

Certain comments we make during today's discussion can be deemed forward-looking statements within the meaning prescribed by the Securities laws, including statements related to the future performance of our portfolio, financial expertise, our pipeline and other investments. All forward-looking statements represent Vesta's judgment as of the date of this conference call and are subject to risks and uncertainties that can cause actual results to differ materially from our current expectations.

Investors are encouraged to further review various disclosures made by the Company, including the risks and other information disclosed in the Company's filings with the Mexican Stock Exchange. In particular, uncertainty remains about the duration and duration and contemplated impact of the COVID-19 pandemic. This means that these results could change at any time, and the impact of COVID-19 on our Company and its results. Our outlook is the best estimate based on the information available as of today's date.

Finally, note that all figures included herein were prepared in accordance with IFRS and are stated in normal U.S. dollars unless otherwise noted.

With that, I will now turn the call over to Mr. Berho.

Lorenzo Dominic Berho

Thank you, Claudia, and good morning, everyone. Thank you for joining us today.

The first quarter of 2021 was a positive but tentative start to the year, and I'm pleased to say we saw continued strengthening during the second quarter. We reached a decisive moment, having passed an inflection point, as the unprecedented effects of the COVID-19 pandemic finally showed significant signs of receding. Demand for industrial and logistic real estate in Mexico is gaining momentum on the back of meaningful U.S. economic recovery.

Mexico's industrial real estate market reached more than 800 million square feet during the second quarter, with 34 million square feet in available gross leasable area. Today, Vesta's tenants have also reached a comfort level where they are starting to make decisions, many who are expanding operations.

Turning to our quarterly results, Vesta's second quarter 2021 revenues increased to $39.8 million, an 8.6% year-on-year increase, while NOI and EBITDA increased 10.2% and 9.8% respectively. Our second quarter performance was supported by the inflow of our $229 million equity follow-on process, with strong Level 3 strategy execution and solid activity due to close client relationships, strong sales and marketing and our country's outstanding reputation as a pre-eminent global industrial manufacturing hub.

We saw demand for industrial space from high-quality tenants and a wide range of international and local companies and sectors during the quarter, including Coppel, The Home Depot and Samsung, among others. We preleased a development building with Eaton Corporation that is currently under construction.

Reviewing our portfolio stats at quarter-end, leasing reached 1.3 million square feet with 92.5% occupancy in the second quarter, up from 90% in the first quarter 2021. It's important to note that today Vesta is at ultra low vacancy numbers in very healthy markets, particularly in Northern Mexico. E-commerce and logistics represented 994,000 square feet during the quarter, 72% of our total leasing. Our success in this regard was led by a continued e-commerce focus as part of our nimble and adaptive Level 3 strategy, with Tijuana and Puebla as two newly-added e-commerce markets for Vesta during the second quarter.

We also saw promising leasing activity from the electronics, electric car component and energy sectors. Further, while construction costs have increased, demand for Vesta's buildings remains strong due to our demonstrated ability to differentiate ourselves through Vesta's unique and compelling product offering that's tailored to our customer's specific needs.

Taking a closer look at regional dynamics, automotive and logistics continue to drive future investments within the Bajío region, with strong performance in data center land purchases, tenant expansions on build-to-suit construction during the second quarter. Demand for industrial space in the Mexico City metropolitan area continued to be led by logistics and e-commerce tenants. We also note occupancy increases with transactions for safety start facilities.

In Northern Mexico, the Monterrey industrial market remains active, with the highest half-year net absorption in the last 10 years. Similarly, demand is outpacing supply in the Tijuana and Juárez markets. Tijuana to Ciudad Juárez comprised 41% of second quarter leasing activity, with Tijuana achieving a 12.6% increase compared with previous tenants in terms of rents.

Inflation had a favorable impact on our Company's uniquely dollar-denominated rent during the quarter, an important competitive advantage related to our peers. Vesta's U.S. dollar-denominated contractual rent increased index to the U.S. CPIs were favorably impacted by inflation during the first half of the year, as the U.S. CPI increased to 5.4% in June from 1.4% in January 2021.

Further, looking back at prior periods of inflation in relation to commercial real estate, property values and rent levels have increased overall. Given that these two items are primary drivers of real estate returns, a natural inflationary hedge is built into real estate investment, providing security in times of economic volatility. This has never been more evident than in the current environment.

We maintain an unwavering focus on ESG excellence, for which we were recognized during the second quarter when Vesta was included in the S&P Bolsa Mexicana de Valores Total Mexico ESG Index, based on the S&P's corporate sustainability assessment for the second consecutive year.

In conclusion, following a strong start to the year, we have hit the ground running in today's reinvigorating market environment. We are as bullish as we have ever been on our outlook for industrial fundamentals and the strength of our markets. We foresee a continued strong trend in the quarters ahead, with robust cash outflows from new projects under development.

Our concentration on the segments which thrive during the pandemic, e-commerce in particular, proved to be a winning strategy. We are focused on expanding our e-commerce footprint into new markets, through strong relationships with high-quality global clients in diversified industry sectors, while capturing the opportunities we're seeing related to U.S. clients' nearshoring trends as well as exciting new Asian clients now reshoring to Mexico.

Properties in our wheelhouse and our markets continue to appreciate in value. It will be hard for them not to, with new supply remaining constrained in our target markets and tenants looking for space to accommodate growth and access to Mexico's uniquely skilled labor centers.

Let me now turn our discussion over to Juan, who will review key financial highlights.

Juan Sottil

Thank you, Lorenzo, and good day, everyone.

Let me start with an update of our financial performance for the second quarter. Beginning with our topline, total revenue increased 8.6% to $38.4 million, mainly due to rental revenue coming from new leases and inflation adjustments to rented properties made during the quarter. This was partially offset by expiring leases that were not renewed in the first quarter 2021, and to a lesser extent by lower rental rates on certain leases that were renewed during the period. In terms of currency mix, of the second quarter revenue, 87.8% was denominated in U.S. dollars, representing a significant increase from the 68.41% recorded in last year's comparable period.

Turning to our costs, total operating costs declined 9.2% to $2.6 million in this quarter. This was mainly due to lower costs from occupied properties resulting from lower allowances for doubtful accounts from improved collections during the first half of the year.

As a result of higher rental revenues and lower costs from occupied properties, net operating income increased 10.2% to $37.2 million with a margin expanding 141 basis points to 94.3%. While administrative expenses were up 24.4%, this was mainly explained by non-cash expenses due to an increase in the Company's long term compensation plan. In turn, EBITDA reached $33.7 million in 2Q21, an almost 10% increase compared to the prior year quarter.

Moving down the P&L, total other income reached $78.6 million compared to $6.1 million in the second quarter of 2020. This increase was mainly due to a $91 million revaluation gain on investment properties, arising from better lease contract term renewals, improved discount rates and capitalization and the successful execution of new leases and building developments in the quarter. In addition, we recorded a gain of $4.3 million from the sale of land in Queretaro. This was partially offset by higher interest expenses.

As a result, we closed the quarter with pretax income of nearly $110 million compared to $36 million in 2Q20 while pretax FFO decreased 16% to $17 million. The decrease in FFO is further explained by the effect of the prepayment of $250 million of the previously contracted debt by the issuance of the new global bonds in May, the prepayment costs and make-whole payment of $3.6 million. Without the make-whole payment, the FFO would have been $20.9 million, representing a growth in FFO of 1.8% without the effect of the prepayment.

Now turning to our Capex and portfolio composition. We invested $22.4 million in the quarter, mainly in the construction of new buildings in the Northern, Bajío and Central regions. At the end of the second quarter, the total value of the portfolio was $2.23 billion, comprised of 189 high-quality industrial assets with a total GLA of 32 million square feet and with 87.8% of total income denominated in U.S. dollars.

Year-over-year, our stabilized portfolio grew 5.6% to 31.3 million square feet with occupancy up 92.7%, down from 93.9% in the second quarter of last year. We ended the second quarter '21 with a land bank of 37.5 million square feet, down 10.1% sequentially, due to the sale of a third plot of land in Queretaro and the construction of the new inventory building.

Moving on to our capital structure, following the successful completion of our equity offering, in the first quarter of this year we closed our inaugural Sustainability-Linked Bond offering, becoming the first Real Estate company to issue a Sustainability-Linked bond out of Latin America. The 10-year $350 million notes that were placed at a 3.625% interest rate allowed us to pay-down debt, extend the company's debt maturity profile, and together with the equity offering, provide us financial flexibility and a strong balance sheet to execute against our Level 3 strategy.

Along these lines, we closed the quarter with total debt of $945 million, and our cash position take stands at $393 million. Net debt to EBITDA was 4.1 times, and our loan to value ratio was 35.1%.

Finally, at the Company's annual general shareholders meeting subsequent to quarter's end, Vesta shareholders agreed to pay $55.78 million dividend in quarterly installments during this year. On July 15 we paid a cash dividend for the second quarter of 2021 equivalent to Ps. 0.40265 per ordinary share.

With that, we conclude our second quarter review. Operator, could you please open the call for questions?

Operator

Thank you.

Our first question comes from Gordon Lee with BTG Pactual. Please proceed with your question.

Gordon Lee

Hi, good morning. Thank you very much for the call.

A couple of questions. First, on the outlook for rents, a competitor of yours mentioned recently that they would expect rents in some markets to grow in dollar terms—this is contractual rents, double-digits year-over-year, which obviously implies not only a boost from inflation, but significant real leasing spreads. Is that an outlook that you would concur with, that you see maybe high single-digit and in some markets low double-digit contractual growth rates in rents?

The second question is on the financial side, so I guess this is for Juan. Your interest expense in the quarter was $16 million and it had been running around $9 million to $10 million quarterly, prior to that. I assume that the $3.6 million in the prepayment expenses are included in that interest expense line? In addition to that, would there be issuance costs related to the debt issuance, or what would explain, even beyond the $3.6 million in prepayment expenses, that jump in quarterly interest expense? Thank you.

Lorenzo Dominic Berho

Thank you, Gordon, for being on the call. I will take first question, and the second one will be for Juan.

Yes, definitely in these times where we are seeing ultra-low vacancy rates in many of the markets, we are starting to see big hikes in terms of rents. As we mentioned, only in Tijuana, we were able to sign leases with rents that are more than 10% above previous rent, and I think that this is very well-reflected not only in our assets, but mainly in most of the market in Tijuana where there's really—the vacancy rate, I believe, could be even less than 1%. That's why it is important to have good land reserves, to start new buildings, and I'm sure that the strategy would be to even prelease the buildings before developing them.

That similar trend, in U.S. dollars, is happening also in Ciudad Juárez where we have also low vacancy rates. But in the Bajío region which we see also that there's several dollar leases, what we are seeing even that the market is probably not as hot as Tijuana and Juárez for the moment, we have seen a very resilient market with pretty low vacancy rates, very disciplined developers approach. I'm sure that that, together with pent-up demand, would trigger into high-growth rents in most of the markets throughout Mexico.

One of the things that we are seeing pretty much overall in all markets nationwide is that developers have a very disciplined approach towards development, on top of many of them that do not have land reserves and do not have the infrastructure in the land reserves such as energy, water, utilities, other utilities. I think Vesta, on that regard, is well-positioned to capture some opportunities as we have been able to anticipate, with good land acquisitions, with good infrastructure in our Vesta parks, and that's really going to be a key advantage looking forward for new projects that might be arising from pent-up demand that we're seeing in many of the markets.

Juan Sottil

Good morning, Gordon, thanks for the question.

Regarding interest, yes, interest expenses was $16.4 million. If you take out $3.6 million in whole payments for the refinancing of the debt portfolio, you will see the effect. In terms of how the interest will increase, please take into account that we increased the debt amount of the Company $100 million by news of the issuance or the long-term bond of $250 million. Net-net, our interest expense, on a normalized basis, will increase around $1 million per quarter, $900,000 per quarter. That's the big effect.

Now, total impact of the new borrowing is very beneficial for the Company. The total interest rate (inaudible) is particularly attractive. If you compare it with our average interest amounts of the existing debt prior to the issuance, it was 4%. All in all, I think (inaudible) debt, it's a very strong signal of the market of the perception and ability of (inaudible).

Now, you also mention the issuance cost of the debt as is customary, issuance cost of the debt, amortized over 10 years of the bond. That's (inaudible) consider on a quarterly basis, on the interest expense.

I don't know if that answers your questions fully.

Gordon Lee

Yes, that's very clear. Thank you both.

Operator

Our next question from Javier (Inaudible) with GBM. Please proceed with your question.

Javier

Oh, hi, guys. Lorenzo and Juan, thank you for taking my questions.

I have a couple. My first question would be related to capital deployment. I just wanted to see what's the company looking at in terms of Capex throughout the year, and what are the main targets for that? With this capital for the Company which I would expect mostly because of the recent equity offering, or is it the returns that you're seeing, is it aligned; what is your Investment Committee looking at, at this time, that there's a bullish sentiment in the market?

My second question is related to Querétaro. Just if you could give us a little bit of a breakdown of what happened on that market in terms of land bank. As you mentioned, you sold some land, but which could imply that you also acquired high market value land. Just a breakdown of what happened would be very helpful. Thank you.

Lorenzo Dominic Berho

Good afternoon, Javier, and thank you very much for being on the call.

Regarding your first question on the capital deployment, definitely, the Investment Committee is very active looking at opportunities right now throughout many of the regions. We believe that the upcoming quarters will be key for some ground-up development starts. Returns are incredibly attractive. Even with some construction costs that have increased, we still see double-digit return on costs for development. That's a particularly important spread when you compare not only with existing cap rates which are in the sub-7% area, but also with interest rates which are currently at close to 3.5%, which is stated in the last bond offering that we did.

Spread investment is still going to be key for us. We're not considering any acquisitions. We believe that for the pricing of acquisitions, which are pretty rich, we are able to develop at a spread which in the end tends to be more accretive for our shareholders, and we're going to keep that same discipline looking forward. We are seeing many of the markets recovering. We closed important transactions with good tenants, as mentioned, with Home Depot, with Coppel, with Samsung and some other logistic companies throughout Mexico. We believe that, for the moment, we're in a great position to start ground-up development as we have done in the past, and it's going to be important to do a combination of build-to-suit projects as well as tech buildings in some of the strongest markets at very attractive returns.

That's something that we're going to be doing in the next upcoming quarters to start new projects. We already own land reserves in Tijuana, for example. We recently acquired land reserves in Monterrey and we have some land reserves in other markets, and for other markets, we are looking at new land parcels. Pipeline is incredibly strong, and we believe it's coming from having very low quarters in the last economic cycle; but looking forward, we think that this is tightening up very quickly with good quality tenants and strong demand in different sectors and different regions.

Talking about Querétaro. What we did in Querétaro is we sold land, and this time we sold it to Microsoft for a data center. This was part of our strategy to sell parts of the Vesta park to final users and particularly final users that are not necessarily in our same business. We decided not to invest in data centers and we have been selling land at very attractive pricing. With that, we think that we are, in Querétaro, the next phase is to keep on developing in the Vesta park that we have already put infrastructure in. There's no necessity to keep on selling land in Querétaro per se, and actually the land that we still own is going to be good to keep on developing build-to-suit and spec buildings for the upcoming years.

That's kind of the strategy in most of the markets where we own land, where we develop Vesta parks to develop build-to-suit and spec buildings for the sectors that we cater. In other markets, we might be selling a little bit of land, particularly where we have larger land reserves, and part of the strategy is to sell the land and to make a good profit on some assets, some land sales too.

Javier

Thank you, Lorenzo, that was very helpful.

Congratulations on the results, and thank you for taking my questions.

Lorenzo Dominic Berho

Thank you very much, Javier, and good talking to you.

Operator

Our next question comes from the line of Pablo (Inaudible). Please proceed with your question.

Pablo

Hi, Vesta team, thanks for taking my question.

I actually have two. The first one is kind of a follow-up from a previous question. We have heard from competitors and other sources that construction costs have increased meaningfully. What's your take on that? Right now we know that you achieved 10% development yields. But what happens if construction costs increase 15% or even more? Can we expect lower yields going forward? That's the first question.

The second question is, again, similar to the previous question. Digging down on Bajío, over the last couple of years, it has been underperforming in the region. Are we close to an inflection point in terms of rents? I don't know, what's your take on that? Thank you.

Lorenzo Dominic Berho

Hola, Pablo, thank you very much for the questions, and I will start with the second one.

Definitely, we're seeing an inflection point clearly coming from good net absorption in some of the market. As it relates particularly with Querétaro and with (Inaudible), we are starting to see better demand. I believe that a portion has to come before rent increases, so now that we have, I believe, healthy vacancy rates throughout the market, because vacancies in Querétaro (inaudible) between 5% and 6%, it's really not a bad number. We believe that, from there on, we're going to start to see more rent increases in many of these markets.

Our focus is very clear. We like to focus on the best companies and have great credit-worthy tenants, and that's the case, so for example, Home Depot where we lease a 175,000 square feet facility in Querétaro, a long-term lease in U.S. dollars, and that's something that we're going to keep on doing to have high-quality tenants in good dollar leases, in long-term leases. I believe that looking forward, rents are going to start picking up.

Also, related to increasing land values, Querétaro is one of the markets with the highest increase in land values, and as I stated earlier, we have three very clear signals, so three land sales close to $100 per square meter. Secondly, we think that the increase in prices, in construction costs, that will also trigger an increase in rent. I believe even that construction costs are increasing, we believe that development deals are still very appealing.

In the past, we were able to do deals at 10% to 11% return on cost, so even with increasing construction costs, I think that returns are going to be incredibly attractive, even if we will have to reduce a bit our yield, let's say 50 basis points. I think that it's worth doing. It's worth developing to a spread, and still, I mean, we can be developing in the Bajío region at $45 a square foot, give or take, $50 a square foot for some built-to-suit projects. That's compared with acquisitions which could be in the $70 to $80 per square foot range. I think it's worth considering development still and attract great companies to great buildings instead of acquiring at low returns.

Pablo

Perfect, thank you very much.

Lorenzo Dominic Berho

Gracias, Pablo.

Operator

Our next question comes from the line of Zoe Tan with Columbia Threadneedle. Please proceed with your question.

Zoe Tan

Hi, this is Zoe.

My question is, I saw headlines with the new Biden Administration. Are you seeing any change in terms of enforcement of the 75% regional content requirements? Are you seeing that affect the auto industry and the signing of new leases on that end?

Lorenzo Dominic Berho

Great, thank you, Zoe, for being in the call, it's good talking to you.

Definitely, there have been several headlines coming from the auto industry, particularly given the large disruption globally that there is in that sector. We believe that the main driver of it still has to be North American competitiveness, and on that regard, we feel very positive with the new Biden Administration that that's exactly what they want to achieve. To get competitiveness in North America, we believe that the integration of supply chains between Mexico and the U.S. has to be closer now, and it's going to be every time, more relevant.

That creates a good opportunity for facilities not only to keep producing in the U.S., but to expand their supply chains in Mexico because this is where they become competitive. I believe that now with the Biden Administration, for the first time in many years, we're starting to see large announcements from American companies in Mexico, and I will use the example of General Motors. They did an announcement of a billion dollar investment roughly a couple months ago; we never heard of those billion dollar investments from American companies in the Trump Administration. I see this as a very positive sign, not only because it shows that companies feel comfortable in Mexico, but also because there's a big disruption now with electronic vehicles, and companies are looking into Mexico for that particular sector.

I think that the USMCA will have its own adjustment. There is a three-year period where companies and auto makers have to adapt to the regional content regulation, but I think it's good timing to adjust, and that will clearly favor Mexico in order to attract more suppliers in a particular industry. The current Secretary of Economy, Tatiana Clouthier, is currently actually in Washington talking about this particular situation in order to get to better agreements. We see this as a favored sector now, not only because of Biden, but also because of the disruption and the pandemic and geopolitical challenges.

Zoe Tan

Right. I was on the call with CBRE Mexico, and they mentioned that it seems like this is causing a delay because companies are trying to structure maybe having a main plant in the U.S. but the supply chain in Mexico. Is that what you're hearing that's causing some delay of signing leases, or has that not been an issue where you're continuing to see companies moving to Mexico despite what is going on in Washington? Is it a wait and see approach, or do you think that companies are already making the decisions right now?

Lorenzo Dominic Berho

No, I think the main delay was the pandemic, but clearly the pandemic brought opportunities, and actually right now we're seeing a very strong pipeline. Remember that these investments are long-term investments in the auto sectors; we've got good high-quality tenants, and that's why sometimes they take a bit longer, because of their approach toward long-term investment.

But actually, we're seeing some of the companies, Tier 1, Tier 2 companies, global companies, in multi-regions expansions throughout Mexico. It's not only one region, but some of them are opening several operations. This is a huge opportunity. But of course, I think that many of these companies, they do large investments in automation, in robotics, in machinery, in equipment, and there have been some delays. But looking forward and thinking long-term, I think Mexico will be well-positioned for them to establish operations over time.

Zoe Tan

Thank you.

Lorenzo Dominic Berho

Thank you.

Operator

Our next question comes from Vanessa Quiroga with Credit Suisse. Please proceed with your question.

Vanessa Quiroga

Hello, good morning, Lorenzo, Juan, and the rest of the team.

I wanted to ask about land bank, the land value. We can see in your supplemental information that the land values for Querétaro per square foot increased by almost 170% quarter-on-quarter, while Tijuana declined about 35%. I wanted to get more color on why—I mean, the reason for these drastic changes in these specific markets.

The other one is some outlook regarding your land purchases. You said that you are looking at different land parcels. So should we expect land acquisitions from Vesta in the coming months?

Finally, maybe just more details about the increase in interest expense funds. Thank you.

Lorenzo Dominic Berho

Great. Hola, Vanessa, thank you for being on the call.

In the Querétaro transaction in land, the increase comes from having a mark-to-market on the land, considering recent market transactions. Secondly, what we did also is, previously we had the land as raw land value and we have an infrastructure component to it. Now, the land that already has the infrastructure, because it has already been improved, reflects that value of having improved land. That's why the increase is a combination of infrastructure as well as market conditions, and that third-party appraiser that does the appraising on the land value, as well as the rest of the properties.

Yes, we're going to be buying more land in other markets. However, as you know, we are very disciplined in trying to hold a certain threshold in terms of land, but clearly, we think that Vesta has the ability of buying land, improving it. The most important thing is anticipating to potential demand, and I think that we are finding great opportunities. We did it recently in Monterrey with a last-mile location where we acquired land, and we develop and we recently closed a deal with Coppel for e-commerce, and the same in Guadalajara. We acquired land, we developed the first anchor project for Mercado Libre. I think that particular anticipation is getting great results, and that's exactly what we're going to keep on doing.

We already had some land—we need to do improvements on some of the land, for example in Tijuana, where we are going to be able to develop more than 1.5 million square feet in one particular project. The good thing is that the land is already ours and we bought at an attractive price, and the same in Monterrey where we also acquired more than 30 hectares. We are going to start putting infrastructure in place this year.

Regarding the interest expense, I believe that what is important from the sense is that this particular quarter, we paid down the debt for a MetLife seven-year loan that we had, and we paid down the debt for the syndicate loan. Both of them, together with the make-whole breakage fees, as well as prepaid (inaudible) interest, that gave us a total expense of approximately $3.4 million. That particular expense on interest is only for the quarter, since this was a quarter when we issued the bond as well as paid down and refinanced—yes, paid down the debt that we had. That's why we had a major expense on interest for this particular quarter which is not going to be happening in the upcoming quarters, clearly.

Vanessa Quiroga

Thank you very much for that. All that information is very helpful.

Just a follow-up, Lorenzo. Every land that you plan to buy, acquire, do you expect to be able to anchor it like you did in Monterrey with Coppel and Guadalajara with Mercado Libre?

Lorenzo Dominic Berho

Regularly, yes, there is an anchor to the projects, so normally the Vesta parks we develop, we do build-to-suit as well as spec buildings. Sometimes we have a new business line, which we call spec-to-suit, which is we start a spec building and while we are in premarketing stage or we start construction. We lease up the building, instead of being only—according to the terms of the client, it's a spec building, which we really like because they are flexible, they last longer in terms of the design; we develop into our needs. I think that that's exactly what we're going to see looking forward. We're going to start spec-ing, but however, in the process of marketing, we're pretty sure that we're going to be able to prelease some of the building.

Yes, many of the (inaudible) where normally would have an important anchor like the one that you mentioned of Mercado Libre.

Vanessa Quiroga

Thank you very much.

Lorenzo Dominic Berho

Thank you.

Operator

Our next question comes from Andre Martinie with Citi. Please proceed with your question.

Andre Martinie

Thanks. Hi, Loren and Juan, thanks for the call, congrats on the results.

The first question would be on the current tax liability. When you look at it both from a quarter-over-quarter—sorry, 2Q ’21 versus 2Q ’20, and also the first six months of ’21 versus first six months of 2020, you will have an important increase, right, in the current tax. Has anything changed, the effective tax rate that you guys have to pay? I remember a while back there was some discussions in Mexico about a property tax; I don’t think that went through. But any structural change for the higher current tax bill that you guys are witnessing this year versus in 2020?

The second question, a broader one on the use of proceeds from the follow-on. Of course, the market is pretty hot. If you guys could remind us again about the timeline for use of proceeds. I think something around 12 to 18 months was something that you guys had in mind at the time of the IPO, but the market has (inaudible) huge investments that you were talking about, the rules of origin and companies having to accommodate more production in North America. Anything changed in the use of proceeds immediately (inaudible)? Your take on that. Thank you so much.

Juan Sottil

I can address the first question.

Regarding the taxes, look, nothing has a structural change, but please bear in mind—I mean, this quarter, we paid roughly, in coverage taxes, $13.5 million. In 2019, we paid a similarly high amount. The normal run rate of… Nothing that structurally has changed, but property taxes are significantly affected by strains in exchange rates. This particular year, the exchange rate was more stable, this particular quarter, and therefore the operational taxes were roughly what they showed. Current tax is quite volatile in Vesta because of exchange rate fluctuations, but that’s about it. I mean, nothing particular changed on our effective tax rates for quarterly operations.

Andre Martinie

That’s clear. Thank you, Juan.

Operator

Our next question comes from Adrian Huerta with JPMorgan. Please proceed with your question.

Adrian Huerta

Hi, thank you. Good morning, Juan and Lorenzo.

My question has to do with—also related to Javier’s question on capital deployment. The pace of new construction so far year-to-date has been, I believe, somewhere around 60,000 square meters of new GLA. Given the strong demand that we’re seeing in many markets, why haven’t we seen yet a faster pace of new construction? Is that related because you’re preparing the land for that, for example in the case of Monterrey? I don’t know if that is the same case for Tijuana.

You did mention that some new price will be approved probably in the coming quarters. Can we see this pace of new construction accelerating significantly already in the second half? You can give more details on this.

Lorenzo Dominic Berho

Sure. Adrian, great having you on the call, thank you.

Yes. The development pipeline that we show, it's only a picture in the quarter, but I think you have to exactly start considering that, yes, in the next quarters, we're going to start new construction. There's a lot that we have been working on our desks, in terms of design, in terms of evaluations, in terms of bidding processes. There's huge work that is being done. But normally, we present it on development pipeline when we really start construction of this. That's an important milestone in the way that we report. Clearly, next quarter—so we are currently under approval stage, but clearly the next quarters, that particular pace will improve. Now that we have raised the capital, now that we have actually increased by an important amount occupancy, now that we see that net absorption is really happening, this is exactly the right timing to start doing more specs and we are already negotiating some build-to-suit.

Definitely, we're going to see a way larger, stronger pace in terms of development in the upcoming quarters, Adrian. That's something that not only we want to start stronger, but also we will monitor very closely according to how we see each of the markets. That's something that we have done in the past: we can accelerate when required and when we need to stop also, we know that this Company can stop when needed. But currently, conditions…

Adrian Huerta

Yes.

Lorenzo Dominic Berho

…look favorably for the Company, with a strong balance sheet, with good land reserves, with well marketing leaders in each of the regions and a strong pipeline. Everything looks favorably for us, and that's something that we're going to be getting more acquired in the upcoming quarters.

Adrian Huerta

Loren, in most of the construction that we could see over the coming quarters, is that highly concentrated in these two markets, Tijuana and Monterrey basically?

Lorenzo Dominic Berho

I think that it will be in pretty much all regions. Also, even some…

Adrian Huerta

Okay.

Lorenzo Dominic Berho

…in the North, some in the Bajío, and there could be more land acquisitions in other markets too. But yes, clearly we see good demand in Tijuana: as I mentioned, we have a 30 hectare plot of land where we can develop to 1.5 million square feet. It doesn't mean that we're going to develop everything at the same time, but we have good land reserves for good timing, the same with Monterrey where we acquired 30 hectares in (inaudible).

Ciudad Juárez, we started a new inventory building, and actually in Juárez, we started a 250,000 square foot facility and, as soon as we hit ground, we signed a long-term lease with Eaton Corporation. Those are exactly the examples that we want to repeat, and I think that we're going to be able to repeat all of those in many of the markets that are favorable at the moment.

Adrian Huerta

I would assume that you're looking for land in Juárez, no? Because you basically run out of land in that market. Is that a market where you're going to be looking to invest in land?

Lorenzo Dominic Berho

Yes, that's a good point, and you got it right. The way we work is we acquire land, and when we finalize developing it, that's when we acquire more, and that's exactly what we're going to be doing. As mentioned, Juárez has been a key market for us. We have been developing at very attractive spreads, developing at attractive costs. I recently read an acquisition which was recently $80 per square foot. Well, I'd rather develop at $50 per square foot than acquire at $80 a square foot. That's why, for us, it's important to keep acquiring land and developing to higher spreads. There's going to be huge value creation for our shareholders, and Juárez is a good example where we can create that particular value.

Adrian Huerta

Great. Thank you, Loren.

Lorenzo Dominic Berho

Gracias.

Operator

Our next question comes from Francisco Suarez with Scotiabank. Please proceed with your question.

Francisco Suarez

Hi, good morning, congrats on the results, and thanks for taking my question.

The question that I have relates to a follow-up made my Zoe on supply chain configuration. To what extent de-carbonization across supply chains in the auto industry is also another huge driver to get more net absorption in your facilities, assuming that your facilities are the right ones to do that? Or to what extent that is actually a risk, given your overall exposure that you have to the auto industry. Thank you.

Lorenzo Dominic Berho

Thank you, Francisco.

If I've got it right, it's regarding carbonization. Do you mean the shift towards electric vehicles, is that…?

Francisco Suarez

Yes, a shift towards electric vehicles, but also to decarbonizing the supply chain, namely, reducing your carbon footprint regardless if you engage in EVs or not.

Lorenzo Dominic Berho

Okay, good. Well, that's an important point. Probably the way I would approach your question is by saying that we recently raised the first public ESG bonds for a real estate company in Mexico, and actually I think it was in Latin America. One of the objectives that we have is that we develop to green standards all of the projects that we have currently under construction. We are going to increase our GLA in terms of green-certified buildings, and that's exactly our approach towards development and towards our ESG exposure, particularly when it comes to sustainability and to green building. That's actually for all of our buildings for all of our sectors. We think that there's, every time, more requirements from companies on these type of activities. We see more value in these type of activities, and that's not only in the auto sector. I think that we're seeing it in different markets, many of the place that we're currently developing like the one in Mercado Libre which is an e-commerce project. It's actually a recertified building.

In that case, I think that looking forward, and you're right, there's not only going to be electric vehicles, looking forward. There's also going to be internal combustion still for many years. But I think that, on that regard, suppliers as well as OEMs are very conscious on their approach. But definitely, the trend is that everybody at some point wants to get to net zero emissions. I think that by doing green-certified building, we will contribute positively to that.

Francisco Suarez

Perfect, thank you.

If I may, a follow-up on that. Considering the unfriendly policies towards renewables, so just think, that might be a risk of OEMs to reconsider further relocation of production to Mexico, or do you think that it's not going to be an issue?

Lorenzo Dominic Berho

Sure. The positive news is that Mexico is part of a global environment, and I think that if you look at political leadership in the U.S. and other countries, it's actually the other way around, so everybody's looking at considering more renewable energies, considering more net zero emissions and sectors and industries. Even in Mexico, in politics, are not necessarily looking that way. I think that we are more part of a global environment, and there's definitely opportunities for Mexico in that regard.

OEMs are having some challenges globally. OEMs are having some challenges in Mexico. It is unfortunate that the current government is not supporting more renewable energies. However, I think that it's going to be a matter of time that they access more renewable energies. They're going to see that there's really no other alternative but to have more cost-efficient energy and cleaner energy, and that, at some point, they will figure out that that's going to be a requirement. But for the moment, I think there's too much political noise on that regard.

Francisco Suarez

Got you. Thank you so much, congrats again.

Lorenzo Dominic Berho

Thank you, Francisco.

Operator

We've reached bottom of the hour. Our last question will be from Armando Rodriguez with Sigmund Research (phon). Please proceed with your question.

Armando Rodriguez

Good morning, everyone, and congratulations on the solid results.

My question is about your inventory buildings that nowadays represents one million square feet in markets, for example in Tijuana, Ciudad Juárez and Guadalajara. My question here is, between your strong net absorption on these markets, so if you feel comfortable with this share of inventory buildings compared to the total portfolio? That's my only question, thank you very much.

Lorenzo Dominic Berho

Sorry, Armando, could you please repeat your question?

Armando Rodriguez

Yes, sure, Loren.

My question is about your inventory buildings that represent more or less one million square feet at the second quarter. My question here is if you feel comfortable with this share of inventory buildings compared to the portfolio?

Lorenzo Dominic Berho

Okay, so inventory buildings, you mean the ones that are currently under development, right, on the development pipeline?

Armando Rodriguez

Yes, that's right, particularly in Tijuana, Ciudad Juárez and Guadalajara.

Lorenzo Dominic Berho

Absolutely, yes. Actually, this is exactly where we believe we can create the most value, by developing at attractive returns, 10%, 11% return on cost. We have three large projects; actually, out of the three of those, one of them has already been leased, the one in Ciudad Juárez, to Eaton Corporation, a long-term lease, U.S. dollars, good quality tenant which matches perfectly to Vesta.

In Tijuana and Guadalajara, we see very favorably, particularly because Tijuana, there's really no building in this size, and actually, even before start, we already had a good lineup of potential tenants for that particular building. We feel very comfortable, and actually if we lease up that building throughout construction, we will soon start the second inventory building, and the same for Guadalajara.

Guadalajara, it's a strong market. We have leased up more than 800,000 square feet with Mercado Libre. We see good demand. There was record demand, record listing activity in the last quarters in Guadalajara. They found that we didn't have a building available, so that's why it was important for us to start construction, and we feel very, very confident that that's going to be leased up at some point. Again, if we are able to lease up part of that in the meantime, we're going to start construction soon of another inventory building and to keep with that virtuous development circle.

Armando Rodriguez

All right. Thank you, Loren, and congratulations again.

Lorenzo Dominic Berho

Thank you very much, Armando.

Operator

There are no further questions. I'd now like to turn the call back over to Mr. Berho for concluding remarks. Please go ahead, sir.

Lorenzo Dominic Berho

Thank you, Operator, and thank you, everyone, for joining our call today.

We are very excited about the second quarter results, and also, we are very excited by the upcoming opportunities that the third quarter and fourth quarter might represent for us. Vesta has passed an important inflection point, which currently resonated in this quarter's key operating and financial metrics. Today, we are in a position of strength and forward momentum and we will leverage our Company's ability to create value based on decades of experience as real estate operators.

I would really like to thank the entire Vesta team for their important contribution for the performance.

Thank you all. We look forward to providing further updates on our third quarter call in October.

Goodbye, everybody.

Operator

This concludes today's conference. You may disconnect your lines at this time, and we thank you for your participation.