Vesta Industrial Real Estate

Third Quarter 2015 Results Conference Call

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PRESENTATION

Operator:

Good morning. My name is Matt Deshura and I will be your conference operator today. At this time I would like to welcome everyone to Vesta's Third Quarter 2015 Earnings Conference Call. Vesta issued its quarterly report on Thursday, October 22, 2015. If you did not receive a copy via email, please do not hesitate to contact the Company at +52 55 5950 0070.

Before we begin the call today, I would like to remind you that forward-looking statements made during today's conference call do not account for future economic circumstances, industry conditions, company performance and financial results. These statements are subject to a number of risks and uncertainties.

All figures included herein were prepared in accordance with IFRS and stated in nominal US Dollars, otherwise noted.

Joining us today from Vesta in Mexico City is Lorenzo Dominique Berho Carranza, the Chief Operating Officer; also Juan Sottil, the CFO; and Iga Wolska, the Investor Relations Officer.

Now I'd like to turn the call over to Mr. Berho. Sir, please begin.

Lorenzo Dominique Berho Carranza:

Thank you very much Matt, and good morning everyone. Thank you for your interest in Vesta and for participating in today's conference call. Our Vesta Vision 20/20 strategic plan has seen us execute two important initiatives this year: our second follow-on offering in January and the approval of our debt program for the next five years in September. This plan is the roadmap for our growth and we look forward to its continued success. In the third quarter, Vesta achieved one of its strongest periods of operational performance since the Company's initial public offering in mid-2012.

We leased just over half a million square feet during the period, demonstrating continued strong demand for quality industrial facilities in Mexico. This drove our vacancy rate down to 11.67% from 14.86% and our same store vacancy rate down to 7.13% from 10.22% previously, while our portfolio grew 2.92% to 18.73 million square feet due to the on-time delivery of two build-to-suit projects. One was in Tlaxcala for Lear Corporation, and the other in Ciudad Juarez for BRP.

Importantly, we were able to price new leases at or above market rates and comfortably exceed our internal hurdle returns, thereby maintaining an industry leading cap rate.

I am also pleased to report that we have now renewed a record 91.0% of leases expiring in 2015 and 15.8% of those set to expire in 2016. These leases were renewed at or above prevailing market rates, illustrating the strength of our client relationships and solid demand.

We grew our strategic land reserves by 57 hectares this quarter with the acquisition of land reserves in Puebla, Tijuana, and Aguascalientes to develop new industrial parks. We also signed a new contract to develop a 120,674-square-foot building built to suit for an existing client, Oxxo, in Veracruz, underlining our ability to repeat business with our existing client base.

Vesta recorded solid financial results for the period with a 14.8% rise in total rental income to $20 million for the quarter. A 16.2% rise in the third quarter gross margin was driven by a 9.2% fall in operating costs. EBIDTA rose 10.9% to $16 million, while net operating income grew 16.4% to $19.3 million. Funds from operations increased 56.0% year-over-year to $10.86 million in the third quarter.

Looking ahead, we are committed to laying the foundation for continued growth as part of the Vesta Vision 20/20 growth plan. Just yesterday, we celebrated the opening of our new corporate headquarters in Mexico City with a facility that encourages collaboration and innovation. This office also aims to meet the WELL Certification established by the International WELL Building Institute, a building standard focused on enhancing employee health and well-being through the built environment. As part of our effort to achieve certification by the first quarter of 2016, Vesta has implemented technologies that positively impact employee health, including air filtration, low and no-volatile organic compounds materials, water purification, circadian lighting, automated shading, ergonomic furniture, and activity incentive programs.

We have also strengthened our organizational structure with the expansion of middle management. In addition, our new Asset Management area is dedicated to improving client satisfaction and ensuring continued high renewal rates.

Our achievements are being recognized. I am proud to announce that during the quarter, Vesta won the 2015 National Logistics Award, in recognition of our Park to Suit concept, the suppliers' park of Nissan in Aguascalientes. This award recognizes innovation in logistics throughout Mexico.

We are grateful for the high regard in which you hold Vesta, reflected in your votes in the Institutional Investors' Latin America Executive Team Rankings and Euromoney´s Best Managed Companies in Latin America 2015.

Thanks to our strong pipeline and the drive of our team, we expect to continue to execute our Vesta Vision 20/20 strategic plan in 2016. Backed by the implementation of structural reforms in Mexico, we will take advantage of growth opportunities and fulfill our expansion goals.

I will now hand the call over to our CFO, Juan Sottil, for a more detailed discussion of our third quarter results.

Juan Sottil:

Thank you, Lorenzo. Good morning everyone, and thank you for joining us today.

For the third quarter, we continued a trend of solid portfolio expansion, grew our strategic land reserves, and achieved double digit growth in key financial metrics.

Our total gross leasable area expanded by more than 532,000 square feet in the quarter to reach 18.7 million square feet overall. This reflects ongoing demand for our facilities, and it is consistent with our intention to double the size of the Company by the year 2020.

During the quarter, Vesta signed new leases for inventory buildings in Toluca, Queretaro, and Aguascalientes consisting of approximately 520,000 square feet. In the Bajio region, we signed leases totaling close to 390,000 square feet with Daewoo, AP Plasman, and Sanoh. In the North region, we signed leases totaling almost 100,000 square feet with OPA and Accel Logistics, while in Central Mexico we renewed a lease with BMW for seven years, increasing the areas. The leases were signed for terms of three to 10 years at or above market rates. Looking ahead, we continue to see strong demand for new leases, which will be reflected in our fourth quarter results.

We renewed leases on more than 1.3 million square feet of our property portfolio in the third quarter. As Lorenzo mentioned, this represents 91% of leases expiring in 2015. We also renewed almost 16% of leases set to expire in 2016.

This high renewal rate, combined with the signing of new lease contracts, saw a fall in our vacancy rate to 11.67% from 14.86%. Our same store vacancy also dropped to 7.13% from 10.22% in the second quarter.

For the three months to September, we made progress on the construction of eight buildings with a total GLA of more than 1.7 million square feet.

Turning to our financial results, we recorded solid growth in revenues, net operating income, EBITDA, and funds from operations. Revenues grew 14.8% to $20 million, reflecting the larger size of our portfolio.

Given more than three quarters of our rental contracts are in US dollars, most of our revenues are protected from the peso's relative decline. However, most of our costs are in pesos which benefits our margins.

On the cost front, our ongoing discipline resulted in a 9.5% fall in total operating costs. Administrative expenses for the quarter rose about 54%. This increase reflects the expansion of our portfolio and a change in the reporting of our stock option policy to minimize volatility in our results from one quarter to the next.

Net operating income rose 16.4% to $19.3 million, while NOI margin increased 130 basis points to 96.8%. This reflects Vesta's ability to lease new buildings during the quarter while keeping operating costs under control.

EBITDA rose 10.9% to $16 million while EBITDA margin fell 280 basis points to 80.2% from the prior corresponding quarter. The fall in EBITDA margin was mainly due to an adjustment to the provision for the stock option plan. As a reminder, the Board of Directors sets robust hurdles for executive management based on total shareholder returns.

The Company recorded a loss before income taxes of $1.35 million compared to a gain of $11.87 million in the same quarter last year. This mainly reflects an exchange rate loss. Third quarter funds from operations rose 56% year-on-year to $10.9 million.

Based on year to date results, we expect full year 2015 revenues to be in line with the low end of our guidance range. Our expectations for full-year operating income margin and EBITDA margin remain unchanged.

Regarding our balance sheet, Vesta's cash and cash equivalents amount to $240 million at the end of the third quarter. Operating activities generated cash flow to $36.50 million during the period. The overall balance of debt as of September 30 was $346.7 million. All of our debt remains denominated in US dollars.

A program to refinance the Company's debt maturing in 2016 and issue additional debt to finance our Vesta 20/20 Vision plan was approved at the General Ordinary Shareholders' Meeting for an amount of $675 million. In addition to the funds needed to refinance our 2016 maturity of debt, this financing program comprises up to $350 million for issuance of new debt.

Once again, Vesta's solid results are evidence of the success of our business model. The Vesta Vision 20/20 plan remains our roadmap for growth while Mexico's appeal as a global manufacturing base is rising. Vesta is exposed to the strongest domestic markets, and will continue to offer industrial facilities of the highest quality to companies across every sector.

Our strong financial position means that we will continue to benefit from the demand for industrial property, while tailoring our offering to our clients' needs. We are faced with many growth opportunities as we approach the year end, and are upbeat as we look to 2016.

I would now like to open the floor for questions. Operator, will you begin taking questions from the audience?

Operator:

Sure. At this time, we'll be conducting a question-and-answer session. If you'd like to ask a question, please press star, one on your telephone keypad. A confirmation tone will indicate your line is in the question queue. You may press star, two if you'd like to remove your question from the queue. For participants using speaker equipment, it may be necessary to pick up your handset before pressing the star key. One moment, please, while we poll for questions.

Operator:

The first question is from Ariel Amar from Itaú BBA. Please proceed with your question.

Ariel Amar:

Good morning. Thank you for the call. I have two questions. The first is regarding the G&A. It shows a small increase up, a relative small growth on the quarter-over-quarter basis. What I'd like to understand here is how big can the company grow? What is the current G&A that's already in place? Basically, without you hiring anyone else, how big in GLA terms do you think that the company can grow? That would be the first question.

My second question is where do you expect, considering your current buy plan, the breakdown of dollars-to-peso rent to converge to? Because it's currently around 80 to 20 in dollars to peso. Do you have any specific goal regarding this breakdown, or is it something which is more of an open metric, and not something that you are monitoring closely? I would just like to get your opinion on both subjects.

Juan Sottil:

Ariel, thank you for the questions. Look, I think that—well, the Vesta Vision 20/20, let me remind, really involves doubling the size of the company. That really implies that we need to have a solid operational base to be able to service our clients, service the buildings, and be in control in the administrative process.

For that reason, we began a hiring program starting early this year. We set up an active management team; we improved our operational staff; we hired people on the ground in each of the regions to be able to go and visit clients and meet client demand. By now, I think that most of the staffing needs of the company are fulfilled. I don't think that we really need to have any more step in growth in people and therefore in operational expenses.

However, please be reminded that a significant portion of our AG&A comes from the bonds, and really your question really goes to the heart of the matter.

Previously we used to market, so to speak, the bonds program on the first quarter and on the second quarter. That's why you saw the change in AG&A from quarter to quarter this year on those two quarters.

Our Board, which guides us in most of the important decisions of the company, said to us, "Look, it doesn't make sense. Why don't you accrue for the bonds on a straight line basis, assuming that management is going to achieve the expected returns, and the fourth quarter reality will set in. You will know what's the total return of Vesta vis-à-vis your peers, and then you will adjust the actual AG&A as per reality." So we are provisioning—this quarter we're provisioning the bonds on a straight line basis. (inaudible) on the previous quarter the bonds' market-to-market was basically nil. It was very small, given the stock market return of the company. This affected this quarter. I think that this quarter—the G&A should be a lot less volatile in the future, and you shouldn't expect it to grow significantly. I still think that over this year we will meet the 82% EBITDA margin as we forecasted. Next year, as the base of the rents grows significantly and we are seeing very strong demand, we will again resume a more generous EBITDA margin because our costs will remain fixed for a number of years.

Lorenzo Dominique Berho Carranza:

And regarding your second question, Ariel—this is Lorenzo—I think that today we're having a strong leasing momentum, and I think we will still see that in the upcoming future. Actually, let me tell you that today we already have binding letters of intent from potential tenants that will turn into signed leases shortly or in the next quarter, and this will give us also a good impact in terms of occupancy looking forward. But what is important on top of occupancy is the type of leases we are signing.

You mention about the 80% having US dollars and 20% pesos. I think that we're going to see the same ratio looking forward. We are still being very disciplined in the type of tenants we are taking into—inside of our buildings. We are very disciplined in terms of the length of the leases. These are—most of them are long-term leases, and of course we focus on still having class-A tenants in our buildings. Today, actually, we have a guest, Steve Williams, who is one of our founders/board members, and he's also part of our investment committee. Our investment committee is still very active. We—nevertheless, I think we have had some impacts in terms of FX. We are still very disciplined in trying to get dollar-denominated leases for most of those companies that are also related to the export industry and we would like to keep so in the upcoming future, Ariel.

Ariel Amar:

Thank you. That was very clear.

Operator:

Our next question, from the line of Ivan Enriquez from HSBC. Please proceed with your question.

Ivan Enriquez:

Hello, Lorenzo, Juan, and Iga. Congratulations on the results, and thank you for the call. Just wanted to ask you—you are saying that you are acquiring land reserves in Puebla to build six buildings. Just wanted to know if these are build-to-suits or speculative buildings, and most importantly, which industries will be represented here. I want to know if it's mostly, because of the location, tenants in the auto industry. That would be the first question, and the second would be in terms of the average leasing rent year over year, how much it increased and which were the areas where you saw the highest increases. Thank you.

Juan Sottil:

Thank you, Ivan. Yes, we did three acquisitions in this quarter. It was land in Veracruz, which was dedicated for the long-term lease-up, also for the build-to-suit. We acquired land in Tijuana very close to the Otai border, which is fantastically well-located, where we will be able to develop over 700,000 square feet, and we also acquired in Puebla good land reserves. The strategy for Puebla is similar to our strategy in the Bajío region, which is pretty much to attract automotive and logistics clients.

As you well know, the Bajío region and Puebla are increasing in productivity in terms of automakers, the production of cars, and we see strong demand particularly from the suppliers of all of the OEMs. So we think that this is a part that will take us some years to develop. We're very happy to have land, to be offering industrial build-to-suits, and to offer also inventory buildings. We are very confident it's going to be a very successful project, particularly since Puebla has very little supply in terms of industrial space, and there's very strong demand, again, from tier 1 and tier 2 automakers.

In terms of rents, I believe that the market fundamentals are still very strong. There is some very important demand, and—they're very good demand, and supply is still scarce, so I believe that rents will probably either keep the same prices where they are at or probably even slightly higher as long as demand is keeping—still being strong. The renewals that we have done recently are a good example that we are able to renew at higher rents than what we were having before. So we're very confident with our development strategy. We're very confident with the leases we are still signing, and looking forward, I think that absorption in those markets is going to be—in the markets where we're at, where we have a leading position—it's still going to be very strong.

Ivan Enriquez:

Okay, that's great. And Lorenzo, very quickly if I may, can you elaborate a little bit more on the adjustment in the provisions for executive compensation that hurt the EBITDA margin? Just—I understood it was a quarterly basis, and now it's going to be paid annually. Can you just please elaborate a little bit more on that? Thank you.

Juan Sottil:

Yes, look, Ivan—let me remind you how the bonus program works. At the end of the day, what Vesta wants to do is we want to compensate management based on the return that the stock gives to the shareholders. So what we do is we calculate total return for Vesta as well as total return for each and every of our peers in the Mexican market. We rank the peers from top to bottom. If you are—if Vesta is in the middle, we will get the expected return. If Vesta is in the bottom, we can get zero compensation, zero long-term compensation. If Vesta is the top performer, we can get 50% more than the standard return. So the volatility of Vesta compensation reflects the volatility of our stock price vis-à-vis the stock price of our peers.

On the last quarter the compensation market-to-market for the executive team was pretty close to nil, therefore last quarter our AG&A was thinner, was smaller. This volatility on results will only confuse you and the rest of the market, so what we wanted to do was to normalize the SG&A during the year. Obviously, on the fourth quarter we will know what is the actual price that Vesta closed (inaudible) and what is the actual stock price of our previous close (inaudible). We calculate total return and then we actually affect the SG&A as per the actual expense of compensation.

Since last quarter the provision was zero for long-term bonds, this quarter the provision is standard for bonds, and that's what affected the EBITDA on this particular quarter. Once we do this, we have to wait until the end of the year to see the actual stock performance of Vesta and the rest of the (inaudible) to see what's going to be the actual compensation of your friends in management in Vesta, and we will reflect that number in the final year-end financial results. Okay?

Ivan Enriquez:

Okay. That's great. Yes, perfect. Thank you, Juan.

Juan Sottil:

You're welcome.

Operator:

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

Vanessa Quiroga:

Thank you. Thank you, Vesta team. Thanks for the call and congrats on the results. My question first is regarding that—I have a question specific about that table where you disclosed the vacancy, same store, and for the portfolio. We saw that square feet that (inaudible) show us inventory actually didn't change. I'm wondering what this refers to, given that on the press release you do mention that several of the inventory buildings have been already occupied. I'm wondering what—if they are related to that table that shows square feet inventory or they are something different.

Juan Sottil:

What we tried to do in that table, Vanessa—good morning, and thank you for being here and your question—what we tried to do in one table, in that table, is to reflect the status of our portfolio. At December 31st we take a picture of that portfolio, and whatever GLA has been delivered as of December 31st, we call that same store. Whichever buildings have increased during the year, we call that growth portfolio, and that's how we can keep track of what was the same stores last year. When we refer to same store occupancy, we compare the occupancy of a given quarter on that particular portfolio to the total square foot as of December 31st.

Now, during the year we deliver buildings, and those buildings that are being delivered, what happens is that as soon as the buildings are delivered to us from the construction company we put them as inventory buildings, and our GLAs expand, which is why our total portfolio grew to 18.73 million square feet. Now—and what we do is we report to you the buildings that are vacant of the delta portfolio, of the growth portfolio.

The inventory number that you refer to didn't change because the deliveries of building that happened on the third quarter were build-to-suits. So area increased, the GLA of the company increased, but the empty space of the spec buildings, so to speak, did not increase because they were build-to-suits. So this is kind of like a double—like a home run, because GLA increases, rental revenue increases, but no vacancy increases, which is why—that's the reason why our total vacancy—our total vacancy—dropped from 14.8, whatever it was last quarter, to 11.66, 11.67 this quarter.

Please take note that the same store vacancy decreased for other reasons. It decreases, but because of the portfolio that was active as of December 31st, we actually lease out empty space to new clients. Let me give you an example. Daewoo, if you recall; on the second quarter we said that Daewoo left the space because they hired a new 3PL and they left a big building, a rather large building in Querétaro. Well, this quarter Daewoo came back because they said that the 3PL—they had problems in absorbing all of the capacity, and they hired back—they leased back basically a third of that building, and we closed that lease for two years. So that dropped the vacancy rate of our same-store portfolio.

That's kind of the way the numbers do. Let me remind you that we're very aggressive in recognizing growth. Every time a construction company delivers to us estate, immediately it's part of our GLA. The policy in the REIT industry in the U.S. and I guess of my peers in Mexico is to not report that increase in GLA until 12 months have passed. We believe that being aggressive in reporting gives us transparency and keeps us on our toes, because if there's an empty space, we're going to be focused on it, trying to lease it as quickly as possible.

Vanessa Quiroga:

Okay, Juan, thanks. Just to be clear, if you have a build-to-suit new building, and it's occupied, it goes to the same store account?

Juan Sottil:

No, no, no, no, no. If I have build-to-suit building growth, it goes to the total GLA, and it doesn't touch same stores. If I lease out any building that was same stores, that was in existence as of December 31st, that building—that GLA that exists on December 31st will remain constant at same stores throughout the 12 months.

Vanessa Quiroga:

Okay, okay. Okay, understood. And a last question just on the general market trends. Have you seen in October that positive trends in terms of occupancy and leasing activity continue?

Juan Sottil:

Vanessa, let me just underline this. On the first half of this year we were incredibly active in looking for new leases. We were receiving a lot of requests for proposals. What we were lacking was the willingness of clients to close the deal. What we have seen in August and September is a very aggressive stance of our clients wanting to close on the available space as quickly as possible. We have a lot of RFPs, but what has changed is the willingness of clients to close on the space, and that, I can tell you, is a substantial difference on the last two months from what happened during the first half of the year.

As Lorenzo said, we have signed—we have already signed binding LOIs. Those are not being reported as they are different from signed leases, but we will convert those binding LOIs into contracts, because the only thing that is lacking is just the financing (inaudible) contracts that my clients have received a couple of weeks ago. We really see a very strong end of the year for Vesta.

Vanessa Quiroga:

Excellent. Thank you. Thanks, Juan.

Operator:

Our next question comes from the line of (inaudible) from BTG. Please proceed with your question.

Alvaro Garcia:

Hey, guys, thanks for the call. It's Alvaro here. Just two quick questions. One, I just wanted to confirm that despite the higher admin expenses this quarter you're confirming your 82% EBITDA margin guidance for the rest of this year, understanding that the first quarter we saw—well, relatively nil admin expenses, at least from the bonus part. My second question is on the NOI margin. I'm trying to get an idea of how much of this NOI margin expansion is due to FX. I was wondering if you could give us just some more color on that. Thank you.

Juan Sottil:

Okay. Let's first tackle the second question, because it's easier. AG&A will—this is what happens. Most of our expenses—80% or 90%—are peso-related. Why? Because salaries of our employees are peso-related. So SG&A is really a peso account. Okay?

Revenues are 80% dollar-denominated and growing, because we tend to sign—Oxxo notwithstanding—more leases based on dollars than leases based on pesos. So you can expect the percentage of dollar leases to continue to increase as the business expands. If that happens, EBITDA will naturally tend to grow. That would be my natural feeling about what you can expect of EBITDA over the next years. Revenues in dollars, costs based in pesos. If the peso keeps depreciating, Vesta is in an extraordinary position. Vesta operationally generates more than $20 million per year on a cash flow basis. That is a great asset. You can expect, if the peso continues to depreciate, EBITDA margins to continue to grow. Okay? That's the expectation that you should have.

Second, very pointed question: will we meet EBITDA margin for the year? Yes, I think we will. The provision would be if we really outperform the market, if we really get total returns for Vesta stock a hell of a lot better than my peers, the first thing that would happen is all of the investors will win a lot, because we, Vesta, as a stock outperformed our peers. Therefore, you will pay me a higher bonus. You're going to have the Vesta team incredibly happy, and EBITDA would suffer a little bit, but let me underline the reason. If EBITDA suffers a little bit, it's because the investors make a killing, and that's why you pay us more.

Now, if we meet—if I value the bonus at a standard as expected, Vesta will meet the guidance of 82%. We will be there, which is fantastic, Alvaro, because the valuation has been 20% this year, and leasing income has not dropped that much. Because our leases are in dollars, the impact of the 20% in pesos is making my meeting of guidance in the lower end, but I'm still needing guidance. Okay?

Alvaro Garcia:

Yes, that makes perfect sense. Thanks very much for the questions. Gracias, Juan.

Operator:

Our next question comes from Froylan Mendez from JP Morgan. Please proceed with your question.

Froylan Mendez:

Hi. Thank you very much for the question, and congrats on the result. My question has to do with the delayed GLA we had from past quarter. Have you changed your strategy on focusing on increasing occupancy rates while still digging further extension, or are you seeing the market being more normalized and you being able to achieve greater GLA without risking occupancy, and also my second question would be if you're seeing any pushback from tenants trying to get any kind of discount or something, given the peso depreciation.

Juan Sottil:

Okay, two great questions as usual from JP Morgan. First of all, pushback from clients. No, we really haven't received any pushback from clients. Let me contrast what happened in 2010 to what is happening today.

In 2010 there was a sharp devolution of the peso. There was a significant—significant—pushback from clients. Why? Because clients weren't selling. They themselves—their own businesses were suffering, and of course when you're suffering in the business you want to (inaudible) every (inaudible). Vesta was one of the biggest (inaudible), so we received a lot of clients, "The peso went from 10 to 13; Vesta, please help me," and we did. We have a close relationship with clients.

This time around, Mexico is really an exporting platform. My clients are sitting on that platform. They are making a lot of business. It is not that they are forgoing cost improvement. It is that we sign a contract in dollars and we see no reason whatsoever and give rental relief when the absorption in the markets that we operate are very strong. So, first of all, we haven't received any calls, and of the few calls that we received, we basically say, "Hey, there's absolutely no reason to give you any respite. If you want to vacate the building, we will (inaudible) with a different client very quickly."

Please take note that on the same stores we increase the occupancy of same stores at the same price of the maturing contract or better. That is very significant, and that again reflects what is happening on this second half of the year. That really underlines our optimism.

Now, on the delay—on the growth (inaudible), let's take the big picture. Vesta will develop three million square feet of new buildings every year. That is the goal. That is the essence of Vesta 20/20. We will do that. Now, at the same time my investment committee—and I cannot lie, because one of the key members of the investment committee's on my right—are very strict, and if we have high vacancy/lower occupancy for whatever reason, they will push the brake immediately.

One of the ways we push the brake is we're doing the park in Toluca, and we have to do infrastructure, and we have to do two new buildings. After the first half of this year, we were not seeing the signing of contracts at the same speed that we were seeing the signing of contracts in other regions. So (inaudible) investment committee said, "Look, be smart. Finalize infrastructure, get the park ready, and play it by the ear." This is what we did with the S-4 and S-5. We're playing it by the ear. Those projects are not being cancelled or anything. They will happen on the first quarter of next year, and it will be business as usual. But the big picture is we will develop three million square feet per year. When total vacancy of the company—not same stores—total vacancy of the company begins to hit 11%, we will begin to aggressively build inventory buildings where we see most of the activity happening. Okay?

Froylan Mendez:

Great. Thanks very much.

Operator:

Our next question comes from Cecilia Jimenez from Santander Bank. Please proceed with your question.

Cecilia Jimenez:

Thanks. Hi. Good morning to everyone. My question is regarding debt and the refinancing portion of the debt with GE. When do you expect to reissue additional debt to refinance that one? I'm not sure if it's going to be this year or next year. That's the first question.

Juan Sottil:

Okay, Cecilia, thank you for the question. I'm happy to hear from you. (inaudible) debt, now owned by Blackstone, matures on September—on August the sixteenth next year, which is why most of the debt is now on the, on the, on the short-term maturity. Well, we're actively seeking alternatives to refinance the debt. The first alternative is Blackstone themselves. We have called them. It is an alternative. It is not the best alternative by far, but it is an alternative. And we're—

Cecilia Jimenez:

What's the rate? Sorry. What's the rate they are offering? Can you disclose that?

Juan Sottil:

High enough for it not to be an attractive alternative,

Cecilia Jimenez:

Okay, perfect.

Juan Sottil:

But in any case—but it is an alternative, you see. But then what we're doing is we're seeking other people. The main reason we established a close relationship with MetLife, and the reason we have close relationships with other MetLife people in Mexico, is because we did a deal with MetLife to open the avenue for debt renegotiation. We have close relationships with people like MetLife in Mexico, and it is an alternative. However, at most large real estate companies the Grail is we would like to issue a market-based debt—a bond—unencumbered, of a long-term maturity. We have and we are preparing the company to do just that.

We think that we're going to be hitting the market sometime in the first quarter of next year. We think we have enough cash reserves, and we will secure whatever is needed from banks in terms of overdraft lines or what-have-you—guaranteed lines—so that we can meet any contingency on the debt maturity.

My expectations are aggressive on rates. I think that we can get rates of around five and a quarter, 5.3 on normal markets. I don't know if right now is a normal market, but I think that when the water reaches its level and we're in a new year and things get a little bit more—less volatile, let's put it that way—I think that we can achieve that type of rescheduling of debt.

Cecilia Jimenez:

Okay, perfect. Very clear. That's the first one, and then the second one. It's regarding development. Today you have 1.7 million square feet under development. That's roughly 10%— a little below 10% of total portfolio. Should we see that level increasing? And according to 20/20 Vision, what's the (inaudible) between inventory and build-to-suit buildings by then, by 2020?

Lorenzo Dominique Berho Carranza:

That's a good question, Cecilia. Let me tell you, I think the strategy of Vesta has always been to have a balance between build-to-suit projects, because I think that's where we have a key—we have a strong advantage compared to our peers, but definitely our inventory building strategy, as you can see, has been also a great opportunity in order to achieve very good returns, and also to attract companies that do not have a lot of time to do a build-to-suit, and in the end, have a good tenant inside of a very flexible building where we can accommodate them and then keep on growing with them.

I believe that Vesta can keep on developing roughly three million square feet per year. Currently we have 1.7 million square feet under construction with the inventory building of Oxxo and other projects that we started at the first semester of the year. Probably closer to the end of the year we will start construction of other projects that we will be announcing soon, including build-to-suits, and including also inventory buildings. So probably a balance still of 50% between build-to-suits and inventory. It's a balance that we believe we can keep on managing in the upcoming future.

I would like to add, Cecilia, that therefore, that's why for us what's key to acquire land reserves in certain markets, and in addition to that, we're still acquiring land reserves in certain markets, because we believe that this has given us also a great advantage in order to keep our leading position in certain markets. This is a way also to keep our competitors away by having good land reserves, good buildings at the time, and therefore we can be able to keep on offering good industrial space in certain dynamic markets.

Cecilia Jimenez:

Right. Thanks, Lorenzo. Just one follow-up there. Are you planning to fund your footprint nationwide or to other markets where you are currently not present?

Lorenzo Dominique Berho Carranza:

Currently we have a very defined strategy that we have worked together with our investment committee members. We want to keep on being a leader in the Bajío region and Central region. Of course, Tijuana has been an important market for us in the border, and also Ciudad Juarez. We are very comfortable in the markets where we are at today. Anyway, as long as we see other dynamic markets, we're always hoping to explore new operations, but keep one thing in mind. We want to really focus in good markets and dynamic markets where we can have a leading position. We don't want to grow nationwide just because.

We expanded recently to Veracruz, for example, and the reason of going to Veracruz was, first of all, because we believe Oxxo is a fantastic tenant. We want to keep on growing together with our tenant base. They needed a space in Veracruz, and Veracruz is a market where we feel comfortable to have a 15-year lease with a good client.

We can keep on growing with the clients like Oxxo, client-driven growth, but in reality we really want to focus in the markets where we can—where we believe we can have a better momentum. Currently, to be honest, I think we're lucky we're in the markets that are the most dynamic markets of Mexico, so there's no necessity to go into other markets—let's say the northeast part of Mexico. We don't see very dynamic markets there.

Cecilia Jimenez:

Very clear. Thanks.

Lorenzo Dominique Berho Carranza:

Thank you.

Operator:

Our next question comes from the line of Pablo Monsivais from Barclays. Please proceed with your question.

Pablo Monsivais:

Hi, guys. Good morning. Thanks for the call. I have two questions, if I may. The first one is what is your same-store (inaudible) growth, quote unquote, year over year? And my second question is are you confident to finish on time the SMA 1, El Florido 2, and J10 projects, given you are expecting to finish those projects by year-end, but as of 3Q15, you have less than 60% progress on these projects? Thanks.

Juan Sottil:

Pablo, thank you for the call. On the NOI, as you know, we don't disclose NOI same-stores and NOI growth portfolio. Perhaps we should. I don't have the statistic for you just like that. I'll take a note of it, and let me consider if we want to disclose that level of detail. Conceptually, I have no problem. I have a little bit more problem disclosing figures on the region by region basis, basically because none of my competitors do it, and (inaudible) reflects—I don't want to signal so closely which markets are better than others. But the NOI same-stores and NOI growth portfolio—it's a good question. Let me consider that, and maybe we should improve our report in that way.

On the other part, I'll let Lorenzo answer.

Lorenzo Dominique Berho Carranza:

Yes, Pablo, regarding the development progress, we are definitely—we're going to hit the development on time. We have progressed greatly. We're very close to finishing the construction of these projects, but on top of that, let me tell you that we are currently already marketing those spaces. This is important for us, because it takes a while to sign leases, so we want to—we are working hard not only to hit—to develop the projects on time, but only to hopefully be able to be closer to closing some tenants also in the—by the time that we finish the building so that we can start collecting rents as soon as possible. So, going straight to your—answering straight, yes, we believe we're going to hit the development on time.

And this will be added to the GLA also for the end of the year. So if you consider the projects that we have for December of this year, you can see that we're going to be close to 20 million square feet for the end of the year.

Juan Sottil:

And Pablo, this is where our policy of transparency bites, isn't it? Because at the end of the year we're going to have rather important roles in our inventory building portfolio, in our growth portfolio Vanessa was talking about, and we're running as fast as we can to sign those leases, because I want to report good vacancies, but this is the price of transparency. Let me tell you, I'm happy that you know, because you will be forcing me to run as fast as I can so that we sign the leases as quickly as we can so I drop vacancy as quickly as possible. I think transparency works great; just be careful when you compare me to the rest of my peers because they don't do it this way.

Operator:

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

Francisco Suarez:

Hi, thank you. Good morning. Congrats on the results. I'm sorry to do a follow-up question on your pipeline. It's interesting, because you have 1.7 million square feet in your pipeline. In absolute terms, that is the lowest level that we have seen over the past five quarters or so also on the (inaudible) basis and GLA. Can you confirm to us if there a certain region which you may be concerned that absorption rates may be changing, and that may or may not have driven already your decision to scale back a bit your overall intention to supply more spec properties to those markets? Because if I remember correctly, you mentioned that you acquired to develop three million square feet. I guess that with 1.7 million you will still be close to reaching your overall objectives.

The second question—perhaps it is a related question—has to do with how—to what extent you will be growing your debt in the years going forward. For sure, refinancing the 2016 maturities for sure, but do you think that we should be expecting an aggressive leverage review of your balance sheet or not? Thank you.

Juan Sottil:

Francisco, thank you for the questions. The second one is easy. I will not issue debt up until my cash balances go pretty close to a hundred million, somewhere around 150, 180. Then I will begin to worry about issuing new debt. So you can expect the debt to total assets of Vesta to remain basically what it is, holding on over the next couple of years. Bear in mind, however, that I cannot prepay the Blackstone debt, so if I issue a bond in March, suddenly I'm going to have a ton of them—I'm going to have a ton of cash. I would try to prepay it, but it depends really if Blackstone wants to receive the money or not. Now—that's the story on that. Pretty straightforward.

The other one is a little bit of cursed if I do and cursed if I don't. Let me tell you why. Last—if you look at the same charts, as of the fourth quarter—as of the first quarter of this year, if you look at that chart, I have three million square feet under development, and that is the Vesta 20/20 plan. Then suddenly, when the buildings got delivered to me, everybody said, "Vesta, you know what? They can (inaudible). What's happening? What's wrong?"

So, to summarize, when management sees occupancy high, we are very aggressive to develop inventory buildings. We always develop build-to-suits if the credit rating of the company's good. On a build-to-suit it's simple. If the client is a good client, we will develop it, and we usually—we're very aggressive on building, and we usually win.

Build-to-suit is—we keep them as they come. Spec building, inventory building—it really depends on the status of my portfolio. Third quarter last year, all of the metrics—total vacancy; same-store vacancy—were very low. Guess what? We started three million square feet of new buildings, because my investment committee was open to hear of opportunities from management, and management is aggressive.

Suddenly in the second quarter buildings came online; we are very transparent. We report the newest spaces available. Suddenly Vesta vacancy is 15% and everybody begins to worry. We said, "Don't you worry! We know what we're doing. Vacancy will calm down." And it does. It did in this quarter. Active, very active signing of leases. Very different first half/second half of this year. Now, it's the (inaudible), and we develop buildings. What we didn't do this year is to increase the pipeline of growth.

We are careful developers. That's why my investment committee has the—they put the brake when they (inaudible), and, well, on the first half the markets were not very—they were not as strong as they are now, so they put a little bit of a brake.

As soon as we sign the leases, as I told you, we have a couple of large-space committed LOIs, binding LOIs from clients. As soon as we hit those contracts, let me tell you, we will go back to my investment committee, and we will continue to aggressively develop, because my concern—the concern of Vesta—is not the three million square feet of 2015 we have accomplished. It's the three million feet of 2016. That is our focus right now, signing the leases so we can continue to grow next year.

Francisco Suarez:

Great answer. Thank you, very clear. Congrats again.

Operator:

Our next question comes from the line of Javier Gayol from GMB—I'm sorry, GBM Capital. Please proceed with your question.

Javier Gayol:

Hi. Thank you for the call, Lorenzo, Juan. I have two quick questions. The first one would be regarding the land bank and the acquisitions that you have guys are plotting going forward, just to get a sense at of what point in time in your land bank would you get the—ready to cover the 20/20 plan? Is that expected? What timeframe are you expecting them to underline that position?

My second quick question will be when looking at your fiscal P&L, given the depreciation of the peso and al the embezzlement, where do you guys foresee that cash access begins to increase rapidly or effectively affecting the cash generation of the company? That'll be all, thank you.

Juan Sottil:

Let me answer the second one, because we have talked often enough about this topic. My managerial accounting standard forces me to report my accounting indoors because 80% of my revenues are indoors. In all of my two series but one my accounting for managerial purposes is dollar-based. Great. It is actually very clear, simple to understand. However, from the point of view of Mexican taxes, the tax reporting rules are peso-based. On the peso-based basis, the Company this year has generated a substantial amount of losses. How substantial? Well, $300 million worth of debt with a 20% depreciation of the peso is $15 million worth of tax losses from a market-to-market (inaudible), roughly speaking. Well, I believe that if the dollar—if the peso-dollar were to remain unchanged—unchanged—it would take us two or three years to eat those $60 million or more, $60 million losses. So on that cash basis I don't expect Vesta to pay a significant number of taxes for the foreseeable future—three years at least.

Javier Gayol:

Yes, that's very helpful. Thank you, Juan.

Lorenzo Dominique Berho Carranza:

And Javier—hola, Javier—regarding your first question on land bank, currently we have a land bank to develop a roughly eight million square feet, which accounts for about $70 million in terms of value. $70 million related to our whole portfolio—we believe we still have some room to increase it. What we don't want to do is we don't want to exceed $100 million in terms of land bank value, so we're going to be doing some acquisitions still for land bank. We have done some very good acquisitions in the last year and this year, and probably next year we are still going to do some important land acquisitions, and with that I believe that we're going to be able to cover a good portion of our 20/20 growth plan.

I think that what we don't want to do is we don't want to either acquire too much land, but nevertheless it is important for us to secure the land in those markets where we still want to keep on growing in the upcoming future. We're very cautious, and I think that 2016 is going to be a very important year to support the land that we need for 20/20 plan.

Javier Gayol:

Thank you, Lorenzo. Thank you. That's very clear. Congratulations on the results.

Lorenzo Dominique Berho Carranza:

Thank you very much, Javier.

Operator:

It appears there are no further questions at this time. Management, would you like to make any closing remarks?

Lorenzo Dominique Berho Carranza:

I think that with this we have—we're very glad to finish the quarter and finish the call. Thank you all for participating in Vesta's third quarter conference. We look forward to speaking with you when we release our fourth quarter and full-year 2015 results. If you have any questions in the meantime, please do not hesitate to contact our Investor Relations department, Iga Wolska. Thank you and have a great day.

Operator:

This concludes today's conference. Thank you for your participation. You may disconnect your lines at this time.