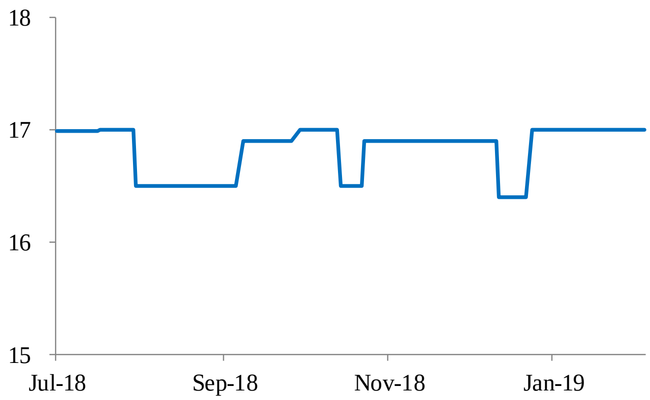
Servicios Corporativos Javer, S.A.B. de C. V.

4Q18: Lower Demand in the Social Interest and Middle-Income Segments Coupled with Non-Recurring Expenses



RECOMMENDATION		HOLD
12M Target Price (MXN$)	$	18.00
Expected Dividend (MXN$)	$	0.26
Current Price (MXN$)	$	17.00
Potential Return		7.4%
Market Cap. (Mn of MXN$)		4,735
EV/EBITDA 2019E		6.0x
P/E 2019E		9.1x
P/BV (Current)		2.6x

Summary and Recommendation

We are downgrading Javer shares to HOLD and reducing our year-end 2019 target price to MXN$18.00 per share (from BUY with a MXN$20.0 target price). The potential return is 7.4%, including an expected 1.5% dividend yield. We believe that the expectation of a slow start of the year and the stock's current valuation fully justify our neutral stance.

4Q18 Results

Javer's sales declined 12.7% YoY in 4Q18, reaching MXN$2.032 billion. The main reason was a substantial 55.4% YoY reduction in social interest revenues and a 10.8% YoY decline in the medium income segment. On the positive side, residential housing sales increased 14.1% YoY. Land sales nearly tripled to MXN$27 million, but accounted for only 1.3% of revenues.

The total number of units sold fell 22.3% YoY to 4,340, which included a 55.5% reduction in social interest and a 13.0% decline in middle income, which was partially mitigated by a 18.2% rise in residential. Infonavit + Cofinavit credits accounted for 92.3% of units sold in 4Q18, compared to 93.8% in 4Q17. However, the company experienced a 56.6% decrease in subsidized units to only 500 due to the new government's policies. This type of units represented 11.5% of total units sold in 4Q18, compared to 20.6% in 4Q17. Vertical units accounted for 23.1% of total units, compared to 19.8% in 4Q17. Meanwhile, Javer's average price improved 11.3% YoY to MXN$462,000 due to a better sales mix.

Gross margin contracted 80 bps to 25.9% in 4Q18 as a result of a lower volume. Sales and administrative expenses rose 11.3% YoY mainly due to severance payments and debt refinancing expenses. This led to a 27.7% YoY EBITDA reduction in the current quarter. However, this indicator increased 11.0% on a cumulative basis in 2018.

Furthermore, the integral cost of financing was up 43.6% YoY to MXN$183.0 million due to a combination of higher interest payments associated with rising interest rates, lower interest gains and higher FX losses. The quarterly net profit was down 87.8% YoY to MXN$17.6 million.

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Javer continued with a manageable net debt to EBITDA ratio of 2.38x at the end of 4Q18, which compared to 1.80x in 3Q18 and 2.04x in 4Q17.

The company generated negative free cash flow of MXN$256 million in 4Q18 due to the acquisition of land reserves amounting to MXN$1.0 billion during the year (+34.2%). As a result, Javer has enough reserves to build 88,455 units of which 67% were acquired directly by the company and the remainder 33% through land trusts.

Javer is currently analyzing several debt refinancing options that will allow it to optimize costs and terms. At the beginning of January, the company decided to hedge 100% of the principal and 100% of the next three coupons of its debt, which has effectively eliminated the FX impact.

The company mentioned that it opened 17 projects in 2018 of which 10 were in the medium segment and 7 in the residential one.

Javer provided its guidance for the current year which includes flat sales which a lower volume, although with an improved mix which should boost the EBITDA by 2.5-5.0%. The free cash flow generation will be positive during the year. The first two quarters will be the most affected ones given the lack of subsidies. The company will also experience higher working capital requirements during the beginning of the year due to the launching of 17 new developments during the first half and 6 more during the second half. However, this effect will likely reverse during the second half of the year due to the titling of units.

The company said that Infonavit is currently studying the implementation of certain measures aimed at increasing the maximum credit amount to 2.8 UMAs (measure and actualization units) in order to offset the elimination of subsidies.

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