Bridgemarq Real Estate Services Inc.

2020 Fourth Quarter and Annual Results Conference Call

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CORPORATE PARTICIPANTS

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

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

PRESENTATION

Operator

Good morning. My name is Casey, and I would like to welcome everyone to the Bridgemarq Real Estate Services Inc. 2020 Fourth Quarter and Annual Results Conference Call. All lines have been placed on mute to prevent any background noise.

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

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

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

Thank you, Casey, and good morning, everyone. With me today is our Chief Financial Officer, Glen McMillan, and we welcome you to our 2020 results call.

Following the usual format of our quarterly conference call, I will begin with a brief overview of the fourth quarter and annual results, and afterwards, Glen and I will discuss financial results as well as remarks on recent business, operational highlights, and market developments. Following our remarks, both Glen and I would be happy to take your questions.

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

I encourage everyone to look at the cautionary language found in our news release and all of our regulatory filings with respect to forward-looking statements. All these documents can be found on our website and on SEDAR.

May you live in interesting times is viewed as an ancient curse; the implication being that steady and boring is preferrable. If my team and I were chasing a dull, predictable life, we would have chosen a different industry.

2020 was a roller coaster of a year. It began on a very positive note, in fact, the most promising start to a year since the middle of the last decade. Then the economic tsunami that was the pandemic-induced recession hit the industry and the economy as a whole. For several weeks in the spring of 2020, sales plummeted in major markets by up to 70 percent, and the Company and industry risked material attrition.

At Bridgemarq, we responded with the Pandemic Fee Relief Plan, temporarily replacing our fixed fees with variable fees and sharing the risk with our frontline agents and our brokerage owners. We released an important forecast at that time, the end of the first quarter; important that it laid out our views as to how the year would unfold.

Simply put, we saw parallels to 2009 in the way to the Great Recession and financial crisis of a dozen years ago. We forecasted prices would soften during the 2020 spring lockdown of the economy, the policymakers would respond with monetary stimulus and financial support for Canadians, and that the lower home prices and lower mortgage rates that would ensue would encourage young buyers into the market. We suggested that the catalyst of young buyers acquiring entry-level homes would trigger a second half recovery and that home prices would end the year up, not down.

2020 did unfold as we expected. The recession and our efforts to safeguard the long-term health of the business with the Pandemic Fee Relief Plan did result in lower revenues for the year, but it produced the desired results. Total agent attrition was held to less than 0.5 percent. Our businesses did not fail, and our franchisees met their commitments to Bridgemarq. A rise in overdue or uncollectable accounts never materialized.

For the full year 2020, revenue was $40.3 million, down $4 million compared to $44.3 million in 2019. And during the fourth quarter, revenue was $7.1 million compared to $10.7 million during the fourth quarter of the previous year, as capping introduced what a temporary fee plan kicked in. Glen will provide a more detailed view shortly.

The year ended strongly, with activity levels that more closely resembled summer months and the start of winter and the traditionally very slow holiday season. With 2021 off to a strong start, we are set up for a very successful campaign this year.

Yesterday, the directors of our board approved a dividend payable on April 30th of $0.1125 per share to shareholders of record on March 31st. This indicates an annualized dividend of $1.35 per share.

In the spring, the Company launched rlpSPHERE, our new digital ecosystem. This highly anticipated, front-of-the-curve technology platform was well received by the network, and early results are very encouraging. I'll speak later on our developments in the products and services area.

I'll also speak in more detail regarding the real estate demand we are seeing from Canadians coast to coast and what factors we are watching closely, the buyer demand that resulted in strong property appreciation, and sales volume increases in key markets that extended into 2021.

And with that, I am going to turn things over to Glen for a look at our fourth quarter and full year financial performance.

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

Thank you, Phil, and good morning, everyone.

Net earnings for the year were $0.8 million compared to $3.1 million in 2019. The primary driver of the reduction, as Phil mentioned, is lower revenue resulting from the implementation of the Pandemic Fee Relief Plan.

In March of 2020, as real estate market sales volumes were poised to drop dramatically below historical levels, the Company introduced the Pandemic Fee Relief Plan as a temporary alternative to its standard fixed-fee plan. The Company suspended franchise fees for approximately 82 percent of its network of realtors and implemented an increased variable fee of 3 to 4.2 percent of gross commission income, subject to a cap.

After a dramatic drop in volumes in April and May, real estate markets rebounded in the last half of the year, with many markets reaching all-time highs. These strong real estate markets in the third and fourth quarters contributed to a large number of realtors reaching their cap, at which point they paid no franchise fees for the rest of the year, negatively impacting Q4 revenues relative to 2019. As of January 1, 2021, Bridgemarq has reverted to its traditional fee plan, which is biased towards fixed franchise fees.

As a company that relies on fixed fees from its network, it was critical that Bridgemarq support its brokerages while lockdown and stay-at-home orders were in effect to reduce the potential for significant attrition. There was an immediate concern that realtors, who were seeing a significant drop in sales volumes and, in some cases, as much as two-thirds of their business, would not be able to meet these fixed-fee commitments and could prematurely leave the real estate services industry.

The Fee Relief Plan not only limited net attrition to approximately 0.3 percent, it has generated significant goodwill from our network, who saw us as true partners when they were in crisis.

In May of 2020, the Company announced an agreement with Brookfield Business Partners and the Manager, which operates the business on behalf of the Company, to defer the payment of a portion of management fees and interest on exchangeable units owned by Brookfield Business Partners. Under this agreement, the Company deferred payments of $6.6 million for a period of up to five years. These deferrals provided financial support for the Company and allowed it to maintain its distributions to shareholders in 2020 at the same level as 2019.

In the fourth quarter, the Company had a net loss of $8 million compared to earnings of $1.3 million last year in the fourth quarter. The change was driven by lower revenues and by a loss on the fair valuation on the Company's exchangeable units of $6.6 million in the quarter. This loss was due to an increase in the price of the Company's restricted voting shares from $12.81 per share at September 30th to $14.80 at the end of the year.

Distributable cash flow for the full year amounted to $13.9 million, $3.3 million lower than the $17.2 million generated in 2019. Similarly, for the fourth quarter, distributable cash flow amounted to $1.9 million compared to $4 million last year. The lower distributable cash flow numbers are as a result of the lower revenues, which I previously mentioned.

As Phil noted in his opening comments, 2020 was a remarkable year in the Canadian real estate industry. For the full year, the Canadian market was up 28 percent at $313 billion, reflecting a 13 percent increase in the number of units sold and a 13 percent increase in the average selling price.

The Greater Toronto Area market, representing 28 percent of the country, was at $88.5 billion, an increase of 23 percent compared to 2019. The Greater Vancouver market was up 33 percent, and the Greater Montreal market was up 25 percent.

Growth in the markets for the quarter was even more dramatic, with the Canadian residential market up 57 percent compared to Q4 of last year. The increase was driven by a 36 percent increase in unit sales and a 21 percent increase in average selling price.

The Toronto market rose 50 percent, driven by a 33 percent increase in unit sales and a 13 percent increase in average selling price. Vancouver was up 47 percent, with 33 percent increase in units and a 10 percent increase in average selling price. And Montreal was up 55 percent, with a 33 percent increase in units and a 23 percent increase in price.

Now I'll turn it over to Phil, who will provide additional insight into the markets and an update on our operations.

Phil Soper

Thank you, Glen. To better understand the Canadian housing market during the pandemic, we need to step back and examine the market prior to March 2020.

In the middle of the last decade, home prices were escalating rapidly as supply failed to keep pace with the demand for housing, with fundamental household formation in this country. Provincial governments responded with legislation to artificially quell demand in the latter part of the decade. And in January of 2018, the Federal Mortgage Stress Test Bill, B-20, was introduced, which required mortgage seekers to show that they could afford to make payments if interest rates were to move to much higher levels.

Particularly in overheated Ontario and BC, markets slowed considerably for about 18 months—longer in British Columbia—while Canadians adjusted to the new rules. In the second half of 2019, we began to see the market improve as prospective homeowners adjusted to the stricter loan approval conditions and saved additional funds for down payments.

The Canadian market entered 2020 on a very positive note, with sales volumes up in double digits on a year-over-year basis. We were positioned for a brisk spring 2020 market. This demand abruptly halted when shelter-at-home orders were introduced by the federal and provincial governments in order to slow the spread of COVID-19.

As market activity paused in April and May, the pent-up demand from the sluggishness in 2018 and ’19, as well as the new demands from a more recent household formation, didn’t evaporate, it didn’t go away. In addition, governments around the world announced significant interest rate reductions to stimulate economic recovery.

We know that few industries react as strongly to interest rate policy as ours. As Canadians adjusted to their working and living reality, we introduced a comprehensive work safe program that showed prospective clients that we were able to serve them safely. This further encouraged people that it was safe to buy and sell property.

As I mentioned at the outset, young buyers entered the market in large numbers, bringing life back into the cycle of the real estate economy. That COVID catalyst resulted in record sales volumes in many areas of the country in the latter half of last year and the beginning of 2021.

As reported last week in a piece of research we released under our Royal LePage business, young buyers were particularly important. In fact, we found that homeownership among 25-to-35-year-olds had climbed to 50 percent, 50 percent of this age cohort now own their homes, and that a full 25 percent of these people have become homeowners in the few months of the pandemic.

Closed borders took away important sources of demand for people who owned rental in this investment property, particularly in our big cities. Temporary residents, foreign students, domestic students who were staying at home, immigrants, all of these sources of demand evaporated. As a result, rental rates for condominiums, particularly in our big cities, and the actual sales prices of those condominiums started to fall.

We then saw a significant shift as these young homeowners purchased homes from investors. There's much more on this and other research we have done, for those who are curious, in royallepage.ca, the Media Room, and you'll be able to read further our analysis of what has occurred in the market, where demand has come from, and where it may come from in the future, and in particular, the unusual forces at work during the pandemic.

Immigration is an important driver within the housing market as it is supportive of real estate markets through economic growth, as well as directly supported through housing demand as newcomers to Canada have a high propensity to own their homes.

In October, the federal government announced its plan to add more than 1.2 million immigrants over the following three years, '21, '22 and '23; a significant jump.

Previously published research by our Royal LePage business into immigrants and housing indicated that these people tend to rent for the first three years in Canada, after which they have a propensity, at the seven-year point, of actually having a higher level of homeownership than people who were born in Canada. An increase in immigration is supportive of both the resale market and the investment demand for rental condominiums.

Earlier, Glen reported double-digit market gains for both the full year and fourth quarter in terms of home sales volumes. A national trend that emerged during the pandemic was the market skewed toward buyers as sellers stepped back. Older sellers tended to be more cautious about transacting during the market, while younger buyers tended to be more focused on improving their work-from-home situation, their living situation during the pandemic. This resulted in a very imbalanced market, which is putting upward pressure on home prices.

We believe that as vaccination rates rise and COVID-19 infection rates fall, that older sellers will be more comfortable with entering the market and should, hopefully, bring more balance to the market, which is so skewed right now in favour of sellers.

The Company is proud of its history and its leadership position in real estate technology, from Royal LePage being the first real estate company to launch on the internet back in the 90s, to being the first national brand to bring automated marketing centres, website enhancements such as school search, home valuations, and lifestyle demographics of neighbourhoods.

2020 was another exceptional year for game-changing technology that we introduced to the network and to the industry. rlpSPHERE, which launched last spring, is our most ambitious investment in technology to date. As mentioned on previous calls, this digital ecosystem seamlessly brings together all the tools and systems our agents and brokerages need to more easily run and grow their businesses.

While designed and built before the onset of the pandemic, its ability to allow users to access the cloud-based AI-driven system anywhere, anytime, from any device, meant that our network had the right technology to work productively and efficiently during the pandemic. It is now available from coast to coast, and early feedback and adoption is overwhelmingly positive. The Company sees rlpSPHERE as a significant competitive differentiator.

Increasing adoption of the system, onboarding, and training is now taking place nationwide, in English and in French. And I’d like to emphasize the training piece of the puzzle. It’s one thing to have a good tool, but if your people don’t know how to use it or aren’t encouraged to use it, it is fundamentally useless. So we believe that it is both critical to build a great tool, to explain to people why it's a great tool, and to train them on how to use it.

To conclude, while the pandemic has created economic challenges, the demand that emerged in the summer of 2020 has extended through and into 2021. If economic fundamentals remain supportive of the Canadian market, pent-up demand is likely to put a continued upward pressure on home prices.

Our network operated with access to the best technology guidance in 2020 as a result of our brand's leadership. The Company is very proud of how its network and staff quickly pivoted to remain highly productive and support each other in this challenging business environment.

With that, I will turn the call back to our Operator and open up the line to questions.

Q&A

Operator

Great. Thank you. Ladies and gentlemen, as a reminder, if you would like to ask a question, simply press *, then the number 1 on your telephone keypad. If you would like to withdraw your question, press the # key. Thank you. Please stand by while we compile the Q&A roster.

And once again, if there are any questions at this time, simply press *, followed by the number 1 on your telephone keypad.

And I'm not showing any questions that are coming in. Mr. Soper, I'll turn the call back over to you for any closing comments.

Phil Soper

Thank you, Casey. And I want to thank everyone—we had a very large crowd on the line for the call today—for participating in today's quarterly and full year results and looking forward to updating you on the business and industry at the Company's Annual General Meeting on May 11th at 10 a.m. Details will be on our website and through our regular communication channels. Thank you.

Operator

And ladies and gentlemen, this concludes today's conference call. Thank you for participating. You may now disconnect.