Company Name: Anadolu Efes
Company Ticker: AEFES TI
Date: 2015-08-14
Event Description: Q2 2015 Earnings Call

Market Cap: 12,493.42
Current PX: 21.10
YTD Change($): -1.60
YTD Change(%): -7.048

Bloomberg Estimates - EPS
Current Quarter: 0.430
Current Year: 0.742
Bloomberg Estimates - Sales
Current Quarter: 3207.000
Current Year: 10952.864

Q2 2015 Earnings Call

Company Participants

- Damian Paul Gammell
- Onur Çevikel

Other Participants

- Edward B. Mundy
- Ksenia Mishankina
- Kenan Cosguner
- Nick J. Ashworth
- Walid Bellaha

MANAGEMENT DISCUSSION SECTION

Operator

Good day, and welcome to the Anadolu Efes' Beer Operation's First Half 2015 Results Presentation. Today's conference is being recorded. At this time, I would like to turn the conference over to Mr. Damian Gammell. Please go ahead, sir.

Damian Paul Gammell

Thank you, and good afternoon and good morning. On behalf of all of my colleagues at Efes, we'd like to thank you for joining our second quarter and first half year results announcement. Onur and I will take you through, as usual, the prepared deck, and I'd just like to draw everybody's attention on slide 2 to our forward-looking statements disclosure.

Before I get into the general overview and operating performance, clearly, as you've seen from our results and as some of you have heard yesterday on our CCI call, the first half of this year has been quite challenging. And today, we'll share our perspectives on that and also share our view on our business going forward.

Despite the challenging environment, we've seen only a marginal contraction on our consolidated EBITDA in the first half versus the same period in 2014. In fact, on the beer side, our EBITDA has actually expanded to 20.7% gave about 120 basis points improvement. As Onur will talk us through later, we've also maintained a fairly healthy free cash flow on a consolidated level, but particularly in our beer business. And as I will share with you across our businesses, but particularly in our beer today, we remain very optimistic and focused on the medium to long term for Anadolu Efes.

In essence, what does that mean? That means we will continue to expand our consumer offering in both soft drinks and beer. And today, I'll be very happy to share with you some of the new consumer products and packing that we brought to market. As you will see, we have stabilized and slightly grown our share [indiscernible] (00:02:06) over a two-year period. And we share expansion in the right segments, mainly premium in Russia.

We have maintained a very strong focus on cost management OpEx, capital deployment and, obviously, free cash flow, which is leading to a much healthier balance sheet for the group, excluding obviously, the non-cash losses on our debt. And as you are aware, we are effectively managing somewhat cyclical issues. And I characterize those as severe currency devaluations, both in Turkey and in Central Asia and now Russia. Macro consumer impacts in both Turkey and, in particular, Russia. And instability in two of our markets, mainly the Ukraine and Iraq. But despite these challenges, as you will hear today, we continue to deliver strong results just if what – somewhat behind our expectations for the first half year. And despite that, we remain optimistic about the medium term opportunities for Anadolu Efes and I'll be very happy at the end of the call to take your question.

So, moving back to the prepared presentation on slide 4, some of the highlights for the first half of 2015. And again, despite some one-off macro factors and also the Ramadan impact we've seen, our revenues remain flat year-on-year, which in this environment, I think, is quite positive. We have had good pricing and we've had good product and packaging mix, which will remain in the business long term as we cycle through these one-off events. We've got better than expected improvement in our margins. Again, good positive free cash flow generation despite the shift of the key period around Ramadan. And we've seen consolidated sales volume momentum improved in the second quarter in the soft drinks business. And in particular, I'm very happy that over the last 24 months, we've seen ongoing improvement in our profitability in our Turkish beer business and in 2015 also, in our Turkish Coke business, which was our priority.

Looking at our consolidated performance, and obviously our sales volume contracting 5%. Thanks to our net revenue holding up at negative 1% and our EBITDA on a consolidated level this time at 3.1%. If we just look at the soft drinks volume development, and again, we've had a number of challenges coming at the same time to our CCI operations. Clearly, our volume performance in Turkey was slower than we would like in the first two quarters, but that has started to improve. And we've seen our profitability improve, so I'm very pleased with that in Turkey.

And we've seen a very intensified competitive environment in Pakistan, which those of you who've been following CC for a long time will come as no surprise as we've taken our share from the mid-20s to just under 40% market share in Pakistan over a very short period of time and ahead of our expectations.

That has resulted in somewhat of a competitive response, and we're dealing with that. But that has slowed down our volume growth in the first half of the year. And then on top of that, which hasn't happened in the sequence before for CCI, we've also had devaluation in Central Asia, which our share was held up, but clearly, that's impacted the consumer. And that's mainly being driven by the situation in Russia, lower oil prices and remittance is slowing into Central Asia. So, not a direct reflection in our performance or on our ability to execute, but more of a macro situation.

So, CCI has been hit by those three events in the first half. We've seen the second quarter improve and as you heard yesterday, we expect to see that improvement continue as we go through 2015 and into 2016.

Our soft drink strategy on slide 7 remains consistent working with the Coca-Cola Company. The good news is on CCI and [indiscernible] (00:06:11) free cash flow, over the last two years, we've successfully implemented the number of capacity expansion projects and they will come to an end in 2015 which will result in a more positive free cash flow going forward to CCI, but critically allows us to meet ongoing demand in the key markets of Kazakhstan and, in particular, in Pakistan.

So moving on to beer volume development. You'll see our performance here over the first quarters and the year-to-date. Our volumes contracted in the second quarter in Turkey, as I mentioned, with slight issue in Ramadan. I will talk about Turkey in a bit more detail. We still remain on a lot of competitive pressure in Turkey, which is good and it's driving market growth. And despite the macro effect in Russia, we have been slightly better than our expectations. And as you can see, volume decline in EBI including Ukraine was down 8.7% year-on-year in the first half, which if you look at Russia alone and the published numbers from our competitors is better than we're seeing across the markets.

As I mentioned in the outset of my introduction, our brands, our execution, our focus on efficiency and our ongoing focus on relationships, particularly with our employees and the regulatory environment remains our group strategy. I'm particularly pleased that with SAB, we continue to make progress on our brand portfolio and our consumer offering and we are improving our execution across all our markets and ongoing cost management and OpEx management is ensuring we continue to drive efficiency at Efes.

On the next slide, you can just see a little bit more color around how we're dealing with our key stakeholders, mainly our consumers, our shoppers, and our customers. And I suppose what's different is if you go back a couple of years, we were certainly under delivering against our consumer proposition. We've improved that and that's now given us the confidence to move forward and expand as you'd expect into focusing even harder against our shoppers and our customers.

Moving to Turkey, clearly, we came under some volume pressure in the first half of the year. Our market share according to Nielsen is sitting at around 69%. If you look at total industry, our market share is somewhere around 71%. What happened in the year-on-year comparison is obviously Ramadan is earlier. Weather has been a challenge, although that has picked up significantly for Efes, we have a very strong presence in the tourism sector, and as I'm sure a lot of you have known, we have seen a slowdown of tourism mainly due to a decline in Russian visitors in Turkey.

We have done well in realizing pricing and clearly, Tuborg and ourselves continue to have a very healthy competitive battle for share in Turkey. Having said that, we're focusing on what we can deliver long-term value and that's around a world class portfolio of brands and you'll see ongoing initiatives, whether it's from our Weißbier Erdinger launching Kozel Dark, Sam Adams and new packaging around Amsterdam, relaunch of our Efes Malt, which is going extremely well, and ongoing reengineering of our Efes [ph] building (00:09:40) portfolio. So those will continue to drive value for the company beyond 2015 and into 2016.

Moving to international beer, and obviously, volume contraction, although we did manage to beat our targets in Russia. And we've seen our performance in Russia continue to improve, particularly in the premium segment, which is where we see long-term value creation. Obviously, we had massive challenges in the Ukraine, as the geopolitical environment there continues to dampen consumer demand and, in fact, make doing business extremely challenging [ph] in Asia and (00:10:16) Ukraine at the moment.

Similar to Turkey, our portfolio expansion in our key markets continued. Clearly, we were in a better position in Russia as we consolidated SABMiller and Efes portfolios. So you'll see more selective expansion in Russia. And in Kazakhstan, we've been trying a number of new initiatives to make sure we have an affordable offering as the currency has devalued, and as I mentioned earlier, consumers come under pressure mainly due to lower income and lower remittance from Russia.

Looking at our market share in Russia, we see the market declining 8.5%. That seems to have accelerated as we have come through the second quarter. The full sanctions and impacts of that continue to hit in Russia. We have maintained our market share, although we've improved the mix of that market share. And you can see our value share is now 100 basis points ahead of our volume share as we continue to focus on margin profitability and long-term value creation.

So in summary, an extremely challenging first half of the year, uniquely for us we've seen on our Coke business a number of one-off issues in Central Asia, competitive response in Pakistan but very good margin growth in Turkey.

On the beer – on our beer business, again, we've seen a better than expected performance coming out of our market in Russia, a good performance in Turkey, although our volumes are slightly behind our expectations and we're clearly going to a deal with that as we move through the second half of the year.

So I'll now turn the call over to Onur, who will take us through a financial overview, and then I'll come back and be very happy to take your questions. Thank you. Onur?

Onur Çevikel

Afternoon, ladies and gentlemen. Thank you very much for being with us today in our first half results call. I will first take you to our first half 2015 financial results, and I will first start with an overall look on Anadolu Efes consolidated numbers.

[ph] Our (00:12:29) total sales volume was 42.8 million hectoliter on a consolidated level, which represents a 5.3% decline compared with the same period of 2014. Our net sales revenue was recorded as TRL 5,075 million in first half of 2015. This represents a very [ph] flat performance (00:12:54) compared with volumes and is only 1% less than the same period last year.

We have registered an EBITDA of TRY 906.2 million, with an EBITDA margin of 17.9%. Despite a challenging first half, decline in EBITDA margin was very limited with 39 basis points with the same – compared with the same period of 2014 as was mentioned by Damian.

Just to briefly talk about segment performances. To start with Turkey, our first half net sales revenue in Turkey grew by 3.3% despite a decline of 4.7% in volumes. Our net sales revenue was registered to be TRL 759.1 million and was positively impacted by price increases, positive mix impact and as well as export revenues. Gross profit margin was 61.8% with 228 basis points decline compared with the same period of last year and our EBITDA BNRI was registered to be TRL 243.4 million. And our EBITDA BNRI margin was 32.1% with 329 basis points decline compared to the same period of last year.

The reason for this decline is most attributable to Ramadan being 10 days earlier and impacting first half results due to volume decline affecting economies of scale and leading to higher per unit cost. Also, FX denominated cost and higher barley cost, partly being compensated by hedging initiated and accelerated sales expenses prior to the season are also two main reasons of this decline.

Now, international beer operations, the volume decline was registered to be 20% with a 7.6 million hectoliter sales. As mentioned earlier, this decline was moderate with 8.7, if we exclude the Ukraine from our volumes. Our revenue was registered to be USD 413.5 million with a decline of 36.2%, mostly due to currency devaluations in the operating region and EBI reporting its results in U.S. dollars.

We don't do that, but if you had applied a constant currency approach, the decline here would have been a lot more moderate. According to our calculations, it would be less than 10%. In our international beer operations, we were able to improve our gross profit margin with 186 basis points to 47.4% and we also adjusted an EBITDA of USD 53.1 million with an EBITDA BNRI margin of 15.2%, with an improvement of 177 basis points compared to last year. This is mostly attributable to leaner operating platform, segmentation and branding initiatives, cost optimization and execution, as well as better procurement and hedging mitigating the FX move.

Finally, in our beer operation, we were able to improve our EBITDA margins with 121 basis points to 20.7% as mentioned by Damian.

Looking at the free cash flow performance, we were able to create free cash flow. First, the free cash flow of excluding minority buyout and other investing activities of TRL 165.1 million on our beer operations. Let me remind you that our free cash flow generation is significantly impacted by Ramadan period starting 10 days earlier and making comparisons harder with first half of 2013, that Ramadan was in July.

We estimate that there aren't an impact being over TRL 125 million – a negative impact on our free cash flow generation compared with last year. We estimate this time [ph] in gas to have been (00:17:13) normalized throughout the rest of the year, and we still target a strong free cash flow generation in our beer operations. As you will all remember, positive free cash flow and the free cash flow generation is one of our major priorities for the last two years, and we continue to beat our targets there.

Talking about our balance sheet, we have our net-debt-to-EBITDA ratio of 2.4 on the FX consolidated level. And we have a net-debt-to-EBITDA of 1.9 times on our beer operations. Net debt-to-EBITDA ratio is negatively impacted majorly by CCI investments being consolidated in the first half of the year as was mentioned by Damian. Increased working capital need before the season including the Ramadan impact that I mentioned earlier, and devaluation impact mainly on TRL. We also expect these impacts to be more smooth and being more [ph] phased out (00:18:11) to the rest of the year.

On the borrowing side, we are happy to have an average maturity of more than five years on beer side and around four years on Anadolu Efes level, which gives us comfort during the volatile times. We are also happy to have a 70% of fixed interest rates in our total debt portfolio, which is in the light of expectations of interest rates going up the limit impact on our finance cost.

On Anadolu Efes consolidated cash flow, we see a negative cash flow of TRL 167 million which is mostly affected by CCI investments in first half of 2015, working capital requirements that I mentioned earlier including the Ramadan impact. We expect these negative impacts to get some more [indiscernible] (00:19:08) towards the end of the year, and as was mentioned by Damien, we expect them to be a lot more smooth in the coming years.

Talking a bit about the finance expenses. As we mentioned earlier, we're negatively affected by the devaluation on TRL, and most of the foreign exchange losses that are incurred due to long term portion of the debts that we have, and mostly non-cash, not having a short term impact on our cash flow.

Anadolu Efes total net financial expense was TRL 503.3 million, and non-cash FX losses due to borrowing was around TRL 534 million.

Just to wrap up, as we had spoken before, our financial priorities are mostly concentrated on being committed to tight balance sheet management and to strong free cash flow generation, continued focus on reduction in cost and expenses, managing proactively the volatility in provident loss due to our FX moves, optimizing CapEx to assess free cash flow generation, and as a result, de-leveraging to a strong free cash flow generation and keeping our commitment to investment-grade ratings.

So we will be concentrating on these financial priorities going further. And this concludes my part of the presentation. Now, I will pass the word back to Damian. Thank you.

Damian Paul Gammell

Thank you, Onur. So, we'd now open the call for any questions, please.

Q&A

Operator

Thank you. [Operator Instructions] We will now take our first question from Edward Mundy of Nomura. Please go ahead.

<Q - Edward B. Mundy>: Good afternoon, gents. Three questions, please. First of all on Turkey EBITDA margins, you're driving for slight decline after the first half down 330 basis points, and clearly part of this is the timing of Ramadan. But could you perhaps talk about some of the other drivers to know the margin dilution for the year.

Secondly, in Ukraine, are you able to comment if there's any light at the end of the tunnel there? And thirdly, Damian, I wish you all the best on the move to, technically, European partners. But could you perhaps provide some color on where we are in the process in appointing your successor and are we looking at an internal or external candidate here?

<A - Damian Paul Gammell>: Thanks, Ed. Let me deal with those in reverse order, if I can. And I'll let Onur talk about the Turkish margin at the end. So firstly, on my move. Clearly, given I'm moving within the kind of Coca-Cola beverage system and, obviously, with SABMiller being a key player and then part of that was – the good news about my move is that, clearly, we could announce that and then take time to ensure a smooth transition and succession planning.

As you can appreciate, I won't comment on where the candidates will come from but you can rest assure that it's a fantastic job. [indiscernible] (00:22:46) for the last four years and it's a great business. So I'm sure a candidate will be announced as we move through this year. Obviously, that doesn't ask me to transition to many roles. So very exciting times for me.

Personally, although I have to say I will miss this great business and the beer business has been a lot of one if not challenging. Speaking of challenges, Ukraine, clearly, we've seen our volume suffer and that cycle will kind of end in 2015 as basically we move out of a period when we're setting in the Ukraine.

Honestly, it's a very volatile and uncertain situation. The good news is we've managed to maintain our brewery there, and we have been able to make sure none of our employees have been impacted or – and we've tried to work with our customers as close as we can in this situation. We're not guiding for any real change in that environment, and certainly not on 2015. And I think also in 2016, we would expect that the situation will remain volatile.

And from [indiscernible] (00:24:02) perspective, clearly, we were building volume momentum which was encouraging, but it was still a very low-margin market. So, while we've lost some volume, it's actually been margin accretive. We still believe in Ukraine for the long term, and it's a big beer market. We've got great brands that can win there, and we're winning. So, certainly, upside for the business at the right time. But, obviously, I can't call when that time will be. But I don't think it'll be in the short term, unfortunately.

And on your first question, sorry. And I will just ask Onur to comment on margins in Turkey. Onur.

<A - Onur Çevikel>: Yeah. Thank you very much for the question, Ed. One, on the margin side, as we have spoken one of the major impacts that takes the major role in the impacts is the Ramadan impact, which makes the numbers not comparable with the first half of 2014 which the numbers were mostly in the second half of the year where the Ramadan had started. So, this plays an important role because this affects the volumes. And being affected by the volumes, the economies of scale is being affected negatively which is creating an issue.

As we mentioned, we also have the FX moves that are going on, and we had a high value prices that had been affecting our margin as well. We also had a partly higher sales expenses prior to season that had been affecting the margins as well in the first half of the year. But as we mentioned last year, we were able to improve our margins around 200 basis points last year in our Turkey beer operations. And our target this year is either to keep this margins or we can get slightly down with this margins. But mid- to long-term target as we have been mentioning is to be above 30s and more we may approach and stay – remain between 30% to 35% [ph] I'm not going to be very happy (00:26:21) with our EBITDA margin.

<Q - Edward B. Mundy>: Great. Thank you. And if I could just follow up on Russia, your guidance is broadly unchanged, but there's this small nuance that it's either going to be in line or a slightly higher margin decline versus prior year, so slightly better. What's giving you confidence? Is it the first half not being as bad as you expected? Or are you seeing anything in the second half into Q3 that's changing your view there on Russia?

<A - Damian Paul Gammell>: Well, certainly, we've seen a slightly better performance than we were expecting in the first half. Again, we'd expect the drivers of that continue. When you look at our business in Russia, Ed, you're seeing the brands where we can make money in the long term and the segments where we can make money in the long term continuing to improve versus for us as we've – through 2014 reshape shape our strategy around value versus volume in Russia, and that's paying off.

Unfortunately, a little bit like my comment on the Ukraine, although certainly not as severe. In the last few weeks, we've seen a lot of currency movement in Russia. And clearly, the impact that may or may not have on the consumer is still what's unknown as we come through August and into the final quarter of the year. So obviously, we'd like to see the ruble strengthen a bit, and obviously, it would help us. But the big impact really is on consumer confidence and spending.

So Russia is still very soft and we'd expect that to continue although we're quite, as I said, and Onur mentioned, we were quite happy that areas that we believe, even in this environment where we can generate value, we are continuing to outperform, and we'd expect some clarity in August on the PET ban, which again, is the kind of final known regulation impact that's been sitting out there for quite a while and has caused a high degree of uncertainty. That should be clarified. And then, I think that's the last major regulatory impact that we're aware of and I think that will also help as we move through the second half of the year.

<Q - Edward B. Mundy>: Great. Thank you.

Operator

[Operator Instructions] We will now take our next question from Ksenia Mishankina of UBS. Please go ahead.

<Q - Ksenia Mishankina>: Hi. Thank you for the presentation. I have several questions. First of all, do you plan to refinance or repay, partially repay your short-term debt? What is your CapEx guidance for this year and next year? And do you plan any price increases this year given ruble depreciation, as well as Turkish lira and Ukraine hryvnia? Thank you.

<A - Damian Paul Gammell>: Onur, I'll let you answer those, if you don't mind.

<A - Onur Çevikel>: Yeah. No problem. Well, on the refinancing side, as we have said, we have been having quite long maturities especially on the beer side, having maturities extending more than five years and on the total Anadolu Efes side extending around four years. So, we don't think that we are going to be having very quick refinancing need in the coming periods. Our CapEx guidance, as we have been talking, we have been very much focused on optimizing and making sure that we do the right CapEx.

So, our CapEx has been around 7%, 8% of net revenue for this year and we are going to be – on the beer side, we are going to be keeping those and as well mentioned by Damian, on the CCI side, our CapEx numbers are going to be more declining in the coming periods due to the investments for capacity issues are going to be getting lower. So, that's more or less what is our guidance for our CapEx.

About the price increases and about the devaluations. We have already made most of our price increases in the operations level. The fact that devaluations have been coming in is affecting the number on dollar terms when we look at our income statements on the local currency basis. We have been seeing improvements especially on the international side about the improvements which are being reflected as well on the EBI side.

So, if you see an opportunity on the prices because price is not just a component that comes to cost, but as well as the market conditions, as well as the competition being imported then. We are going to be reflecting the price increases in the markets that will be needed. But if mainly, made our price increases in our major markets like Turkey, like Russia, so we have already reflected most of the inflationary changes in our prices.

<Q - Ksenia Mishankina>: Thank you very much.

Operator

We will now take our next question from Kenan Co■guner of TEB Investment. Please go ahead.

<Q - Kenan Cosguner>: Good afternoon, gentlemen. Thank you for the presentation. Congratulations on your new challenge. Mr. Damian, I have two questions. First of all, regarding the Turkish beer operations, Turkey – in the Turkish market, you've seen, you lose some market share. Is it like temporarily a situation or you're expecting to win back some market share or market shares? You will – rather than market share you will focus on different measures?

<A - Damian Paul Gammell>: Thank you, Kenan. So, just looking on our Turkish market share, I mean, if you look at it over the last 12 to18 months, if you look at Nielsen or if you take the government figures, which are slightly more representative because they take in the on-trade and not all of the channels are covered by Nielsen. And in our market share is staying somewhere between 69% and 71%. I mean, that's the range we've been in. And some months we've gained, some months we've lost.

Clearly, since I moved over [ph] FX (00:33:27) in Turkey in particular, we have prioritized margin. We have a number of difficult years, particularly 2013, the second half, where margins dropped to a low level. And to be honest, I mean we've talked about this before. In 2014, we saw our margins in Turkey recover faster than we expected and, therefore, our margins in 2015 are more or less in line and that's our guidance given a great year in 2014.

So we're anxious to protect our market share. The good news for us is that our competitive market is growing the market. So we will see that to continue. And we're anxious to protect our free cash flow and the profitability of our Turkish business and that will be our number one priority. But clearly, holding our growing market share and growing profitability are not mutually exclusive and we can do both. And we'd expect, over a longer period of time, our market share to continue to stabilize. And again, similar pattern, it may grow a bit, may come down a bit, but we're not going to sacrifice long term profitability for short term market share. It's not sustainable.

As I've talked about before, our competitor has done a great job in Turkey and it has taken us a while to respond to that and most of those are now in the market and we're seeing some of the benefits. But clearly, on some of our brands, like, [indiscernible] (00:34:59) we're continuing to innovate around that brand to restore its growth.

We've seen that on malt and we've seen that on our other brands. But clearly, Efes still under a bit of pressure and that's something that we're focused on and it will turn. But overall, our market share at around 70 is still a very respectable market share and that, with good margin, I think has got to be the focus with Turkey.

<Q - Kenan Cosguner>: Thank you. I have a question regarding Coca-Cola system. I just wonder is there – there has been a trend in the Coca-Cola system, the merging of the bottling companies. Does it have any implication on Coca-Cola ■çecek, or what does it mean for Coca-Cola ■çecek? Can I have your opinion on that front?

<A - Damian Paul Gammell>: Well, I don't think you've seen too much merging of Coca-Cola bottlers. I think what you've seen in recent weeks is clearly something that I look forward to being involved in going forward is being a merger of the Western European bottlers and excluding Coca-Cola Atlantic.

I mean, I think all of the shareholders involved in that transaction and the management of that, laid out the specific rationale of merging the bottlers in Europe, but I think that clearly makes sense on its own merits. Outside of that, you haven't seen any real Coca-Cola bottler mergers. So, I think what you've seen is in Africa, a consolidation of the bottlers in South Africa which made sense given it was one country.

For Coca-Cola ■çecek, I mean their priorities remain the same. I mean we have a huge consumer franchise on our own, and we've got very underdeveloped markets in terms of per capita, so our growth guidance for CCI remains on an organic footprint. However, as the Coca-Cola bottling system continues to evolve and look for efficiencies. If and when markets become available, clearly CCI, if it's the right market, are going to be at the table for that discussion. But, again, my own opinion is, in terms of ongoing mergers in the Coke system, I think that certainly [indiscernible] (00:37:41) correct in saying has been – will be the biggest one ever. But I don't see much more of that. But, again, that's a personal opinion.

<Q - Kenan Cosguner>: Okay. Thank you. Just a final question. What's your opinion about the Iran market? Is it a good fit for Coca-Cola ■çecek? Thank you.

<A - Damian Paul Gammell>: Well, if the markets that – and, again, it really depends on what happens with the sanctions. But clearly, it's a market that we know. I mean, we've got a business, export business there with FX, so we now the market well. It's a neighboring country. It's got a lot of similarities to other countries in our market in our region. It's on our doorstep. So, clearly, it's a big market with huge potential. But there is a Coca-Cola bottler, so we really need to wait and see what evolves in terms of sanctions and the ease of doing business there. And, obviously, like any market in our geography, we will pay close attention to what happens.

<Q - Kenan Cosguner>: Thank you very much.

Operator

[Operator Instructions] We will take our next question from Nick Ashworth of Morgan Stanley. Please go ahead.

<Q - Nick J. Ashworth>: Hi. Afternoon, everybody. Three questions from me, if I may. Firstly, can you just talk a little bit about Turkey and your volume expectations in the second half of the year, because if I'm right, I think your guidance implies the volume should get a little bit better but it looks like the comp base is not [ph] desperately easing

(00:39:23), there's clearly still a lot of uncertainty around politics and macro. So just a little bit more insight that would be interesting. Can you talk a little bit also around hedging and visibility around COGS and OpEx lines for the rest of this year and into 2016?

And then finally, in Russia, does this proposed retail law amendment, which may or may not go through the [indiscernible] (00:39:50) at some point in the next few months and then part of that is potentially removing that margin and there's been a lot of talk about how this affects the retailers. Can you talk a little bit about how it could potentially affect you? Thank you.

<A - Damian Paul Gammell>: So I will then deal with Russia and Turkey and then I'll let Onur do the hedging. We're not expecting any significant impact on the back margin. I think it's certainly a topic that's got a lot of discussion. We've discussed it with our retailers and, clearly, it may cause somewhat of a restructuring on the retail side but from our side it's not something that we see materially impacting our business going forward.

On Turkey, clearly, there's still on the macros as you point or already mentioned, we've seen a couple of short term negatives on the currency recently driven by primarily what's seen as a little bit more uncertainty in the political system with the lack of certainty around the government. In our view, that's going to be something new to live with until the next election. If that seems to be what it turns out. I suppose the good thing is it's one less uncertainty, if I could turn it into a positive.

So, as the build become clear, we're going to have an election, at least, that gives us some certainty. And then, we'll have to trust the public to come up with a more sustainable solution for Turkey going forward. If we exclude the macros, and I say that given that we are seeing some benefits in terms of the beer category is growing, we have got very good pricing in Turkey, which is in the market.

We have seen very good weather coming out of Ramadan, which we didn't see beforehand. So there are some positives that we see coming through on volume. And obviously, operationally, we've got a number of new initiatives around our Efes brand, our new Malt brand, which is really doing better than expectations, and some smaller brand launches. But on the volume side, they have been less impactful.

So, all of that combined, we see that's somewhat more optimistic. But I would counsel that with the macros, we're going to manage our volume and our inventories in the market very tightly coming through the second half of the year to make sure that we don't build excess inventories in the market and then deliver inferior product quality to our consumers, which is always one of the risks.

So we are optimistic. But obviously, like everybody working in Turkey today, we'd like to see a little bit more certainty around the macros. Some of the recent currency losses will filter down to the consumer. We've got to see how that impacts us in the second half of the year.

So, Onur, maybe you can talk about hedging?

<A - Onur Çevikel>: Yes. Thank you very much for the question, first of all. Well, by the beginning of this year, we had stated that we are going to be taking some actions on the operational side in order to make sure that we mitigate some of the fixed volatility issues that might be coming in. And we have really executed those by the first quarter of 2015. So, what we have done is in Russia, we have hedged most of our [indiscernible] (00:43:29) and most of – more than half of our COGS exposure. So, we feel quite good about doing that. Now, we are looking for some other opportunities whether we might be having or not going further in the operational hedges.

On the Turkey side, we have also done that so we have covered around 40% of our total COGS exposure on the currency basis in the first half – in the first quarter of 2015. And just to remind, we also have – we export revenues on dollar basis that are coming in which is helping us to better mitigate the risk of FX on our Turkey business. So, this is how the hedging side looks for FX operational hedges.

<Q - Nick J. Ashworth>: Does that mean that you don't have anything in place yet for 2016 other than the natural hedges that you have?

<A - Onur Çevikel>: Well, we haven't taken yet some actions for 2016. Yes.

<Q - Nick J. Ashworth>: Okay. All right. Thank you very much.

Operator

There are currently no further questions in the phone queue. [Operator Instructions] We will now take our next question from Walid Bellaha of Barclays. Please go ahead.

<Q - Walid Bellaha>: Hi. Good afternoon, and thank you very much for the presentation. Very quick question actually on my side. You talked that in Turkey in the beer segment, there were some drivers for decline in margins which included lower volumes due to Ramadan and higher sales expenses prior to the season? Would it be possible to quantify this additional sale expenses?

<A - Damian Paul Gammell>: We won't give that level of detail, but what I can say is it's clearly, as Onur mentioned, it is, I think a phasing issue. We quite likely would rather not come in earlier. I think made the right decision to bring forward some of our expenses so we could be, let's say, have the market fully prepped for the key selling season which is coming later because of Ramadan. So it's purely a phasing issue. And on a full year level that will kind of work its way through.

<Q - Walid Bellaha>: Okay. Understood. And I don't know whether it's possible for you to comment on the trends in Turkey beer post Ramadan. Have you seen a pickup in volumes already in the month of mid – from mid-July until now?

<A - Damian Paul Gammell>: Yeah. For sure, I mean, it's pretty much in line with previous years. Obviously, once Ramadan ends, a large number of consumers come right back in to the category during and after the holidays at the end of Ramadan. And then we've seen that again in 2015.

And as I mentioned earlier, we've also seen recently strong weather which is good as well. The only area that we would kind of reference when it's well-known is that tourism in Turkey has been hit and unfortunately, July, August are key tourist months. And so, that's something that we'll work through. But we certainly have seen a similar level of uplift as we've seen every year coming out of Ramadan.

<Q - Walid Bellaha>: Okay. Thank you very much.

Operator

We will now take a follow-up question from Edward Mundy of Nomura. Please go ahead.

<Q - Edward B. Mundy>: Thanks for taking the follow up. Just on Russia, obviously, we have to see what happens with respect to PET ban in August when we the clarification on that. But in the event that there is a ban, I was just wondering what your thoughts were with regards to how the industry or how you expect the industry to behave. I mean do you think the industry will accept, let's say, a 20% volume loss if the [indiscernible] (00:47:44) comes down? Or do you think the industry will reduce prices to protect volumes which has longer term ramifications for the profit pool?

<A - Damian Paul Gammell>: Obviously, each company will make its own decision. I mean, what we're clearly seeing is that all of the producers, Edward, in Russia have taken a significant hit over a number of years for lots of reasons which we don't need to go into. So, I would say margin levels in the Russian beer business would at least make you believe that everybody would focus more on protecting margins with the PET ban rather than destroying it further.

Secondly, what's going to be very interesting and I've consistently said I'm not sure that the PET ban is as negative as some of our competitors see it, and certainly, if you look at the PET segment in Russia, it's extremely low margin. And trying to build brands in 2.5 liter PET, for me it doesn't correlate with a brand. I mean, it's very cheap. And clearly, the quality and product experience is not as good as it is in cans or bottle or draft. So what you are seeing in Russian preparation is from all of the suppliers, a lot of multi-packing on cans. You're seeing a lot more focus on 1.5-liter. And you're seeing a deemphasizing of 2.5-liter. We're leading that, so you're seeing that. You've already seen some downsizing.

So the big question is all of those 2.5 liter beer drinkers, when the ban happens, what do they do? Now, I think it's fair to surmise that if you drink 2.5 liters of beer, you probably like our beer. And therefore, the propensity for those drinkers would be, in our view, to stay in the category and move to the next most affordable package. So there will be some short-term volume impact as we just destock that pack to meet the regulations.

But from an ongoing consumption perspective, either through multi-packs, through an enhanced 1.5-liter or 1-liter offering, we see an opportunity to move people into those packages, which are margin accretive, and to move them into brands that are value accretive. And I think from a regulatory perspective and from a responsibility perspective, it makes sense. So I wouldn't expect, given all of the negative that the Russian beer has gone through, that we would blow such a chance to bring in a little bit more margin and stability to the beer industry. But each company will make its own choice, but ours we've been pretty clear on.

<Q - Edward B. Mundy>: Great. Thanks. And just a follow-up on Turkey. Clearly, you've got – you've done a good job widening your product portfolio the last couple of years. And one the products you brought across is – bought a beer company, Sam Adams. When you look at that company, they've got quite a diversified product offering, Twisted Tea, Hard Cider. And they're now launching some hard root beer as well. I mean do you see fair opportunities to bring over other differentiated products in the near beer occasion.

<A - Damian Paul Gammell>: I think, if I look at the short term, I think we've rapidly expanded our portfolio and we're probably going to use 2015 and 2016 to just reflect and give those products that we brought a chance to bed down. I mean we brought in Kozel, which is a fantastic brand as well. And in a dark market like Turkey is you're going to appreciate, it takes a bit of time, a bit longer than in other middle markets to build trial and to get people to try the beer.

So probably in the short term, no, I mean probably what's more on a radar screen is the SABMiller have made a number of acquisitions in the craft area and then also have some good side of that as well. So probably that will be our first port of call in terms of portfolio expansion and then as I recently looked at the business that they bought into London, which has had some fantastic brand as well.

So, we'll look – but I'd say I haven't got the exact number but we probably had eight new brands to Turkey in a very short period of time. So it's probably good to let them bed down and then we'll take a look at it if there's any more gaps in their consumer offering. And our first port of call will probably be SABMiller to be honest.

<Q - Edward B. Mundy>: Great. Thank you.

Operator

As there are no further questions in the phone queue. At this time, I would now like to hand the call back to the speakers for any additional or closing remarks.

Damian Paul Gammell

So just in conclusion, again, I just want to thank everybody for taking time to join us on the call. I just draw your attention back to my opening comments. I mean, clearly, the first two quarters have been challenging for both CCI and Efes, and that's kind of unique that we've had both companies and in the same period being challenged, normally, we'd have a very good portfolio benefit. However, it's two quarters and if you look back over the last 24 months, and if you look at our guidance going forward, we have continued to focus on the long-term and midterm value generation around our consumer offering. We will continue to focus on free cash flow and a healthy balance sheet, and we clearly see our businesses on the beer side on both Russia and Turkey improving from a consumer perspective and as we've talked earlier, we're happier although it's still difficult in Russia.

On the Coca Cola side, again, not to go over what we've discussed yesterday by Burak and the team we are seeing stronger profitability coming out of Turkey. We have seen a slowdown in international volumes, but again, they seem to be somewhat cyclical and if you look at our share performance in Central Asia and in Pakistan, we see growth returning to all of those markets and in the near term which would bring us back closer to our consistent guidance from the last two or three years.

So, exciting quarter ahead of us and again, I'd like to thank you for taking the time and I look forward to talking to you again. Thank you.

Onur Çevikel

Well, thank you very much for being with us today. Thank you.

Operator

Thank you. That will conclude today's conference call. Thank you for your participation ladies and gent

[Abrupt end]