Anadolu Efes

CONFERENCE CALL TO DISCUSS ANADOLU EFES FINANCIAL AND OPERATIONAL RESULTS FOR THE FOURTH QUARTER OF 2020.

Company: Anadolu Efes

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Participants:

- Can Çaka, Chief Executive Officer
- Orhun Köstem, Chief Financial Officer
- Asli Demirel, Head of Investor Relations

Asli Demirel, Head of Investor Relations
Ladies and gentlemen, welcome to Anadolu Efes Last Quarter Financial Results conference call and webcast. My name is Asli Demirel and I'm the Head of Investor Relations of Anadolu Efes. Our presenters today are Mr. Can Çaka, the CEO; and Mr. Orhun Köstem, the CFO. All participants will be in listen-only mode. Following the first part of this call, there will be a Q&A session and you will be able to write down your questions on the question box on your web screen during the presentation. Just to remind you, this conference is being recorded and the link will be available online. Before we start, I would kindly request you to refer to our notes in our presentation regarding forward-looking statements.

Now I'm leaving the ground to Mr. Can Çaka, Anadolu Efes CEO.

Can Çaka, Chief Executive Officer
Thank you. Asli. Hi, everybody. Good afternoon and as usual good morning to those in the US and again, thank you all for joining our fourth quarter 2020 earnings call. Needless to mention 2020 has been a year, and I'm sure none of us will ever forget this year. We discussed this, we made a very good start to the year and then faced with this unprecedented crisis. However, I'm proud that we responded quite rapidly, ensured health and well-being of our people, crafted our strategy, worked multiple scenarios and started a great execution. Our strong 2020 results are the testimony of our continuous efforts to ensure business continuity from production to the execution.

Despite 2020 being a rocky road we leveraged these challenges and earnings and emerged even stronger.

2020 happened to be a challenging year repeating myself, and obviously there would always be such challenges ahead, bumpy roads, bumps on the roads going forward as well. But looking at the last five years performance, we were able to show an excellent track record in line with our long-term strategy. We were able to grow our EBITDA ahead of our revenues and revenues ahead of our volumes. There has been a superior performance in free cash flow generation where it grew by almost 40% annually through this period. And again, at the same time international beer business has increased its share yielding on more balanced business portfolio. And similarly, our soft drinks, our subsidiary CCI is performing great, increasing its rate within the portfolio, which is good at the end, return on our investments is increasing.

On the next slide, please, let's get back to 2020. Our continuous adoption of new and improved ways of doing business paved the way to report very good set of results in 2020. We were able to expand our revenues by 16% despite a slight decline in our volumes. Revenue growth was a result of our initiatives to drive topline growth. Our EBITDA expanded more than 25%, yielding a margin of 19%, the highest level in the last eight years. And thanks to our commitment to financial discipline and prudent management of cost and OPEX spending, together with our superior working capital management, we recorded an all-time high level of free cash flow, with more than TL 3 billion ending in a very healthy leverage ratio in such a difficult period.

I am also really happy to announce that in line with our commitment to maximize shareholder value, our Board of Directors proposed TL 1.1 billion dividend distribution for 2020 considering the improved operational profitability, substantial amount of free cash flow generation, together with the low leverage ratio. This year is unique from another aspect too. In 2020, we took the initial and most crucial steps to our digital transformation journey, which is going to become the core pillar of our business model across all our processes from production to market execution. So, we are committed that within the next two years, Anadolu Efes will become more digital and mobile company.

Looking at our international beer business, it was another successful year for Russia where the beer industry grew by around 2% according to Rosstat. We outperformed the market in the third consecutive year and sustained our leadership both on volume and value terms. We increased our value share by almost 2 percentage points as seen on the chart at the top right. Yes, it was a difficult year with significant competitive pressures and challenging pricing environment with excise tax hike at the beginning of the year, currency devaluation and commodity price pressures. As we have been emphasizing since the beginning, despite the challenges we're facing, we are committed to our strategy of maintaining of our leadership profitably. In Ukraine, the beer market was down by low single-digits and our performance was in line with the market. However, we were able to post volume growth in the last quarter of the year.

We have observed volume declines across other CIS countries. Despite the fact our volumes were down and obviously throughout the year we have seen two dynamics that are, let's say, to the disadvantage of our businesses, the on-trade closures usually generally in every other market being the market leader, we have higher proportion of our volumes on on-trade, and we have seen also with the macroeconomic challenges economy segments growing and basically we are defocusing in every other market, the economy segments, we are much more stronger, we have much higher market share in the economy on the mainstream segments. So, despite all these trends in every other market, we were able to increase our market share especially in the second half of the year. So, basically our initiatives work very well. And together with that, we were able to improve our profit margins and generate strong free cash flow in the other CIS operations as well.

I want to give some more details on our strategy and drivers of growth as we achieved in Russia and Ukraine over the years. You would remember, we were emphasizing this, we had higher market share on the premium side of the equation and also, we have much more focus on the premium side in order to ensure that we have revenue growth management initiatives. So, in line with this strategy, we were focusing on our premium and super premium brands and we have seen a very strong performance on these segments. For example, Corona Extra in Russia gave a very good indication in that perspective growing more than 50% year-on-year basis through the year. And another area was, we were always mentioning that we had lessened our fair share in the core and lower mainstream. So, throughout the year, especially in Russia our brands in the segments starting from the upper-end Efes, Lowenbrau, Stary Melnik, Bely Medved; and on the lower-end side the Gold Mine Beer we gained market share and we showed the leadership in terms of share growth in this segment with our focus on the core and upper mainstream. We have expanded our portfolio on the non-alcoholic segment, which is growing nicely in Russia. So, we have our global brands Stella, Bud and Hoegaarden in non-alcoholic extensions. Together with that we moved into adjacent categories like kvass as well on that side. So, as a result of our focus on growth of global brands in addition to number of flavour additions, we have also introduced Bud Light on the upper or lower premium side. So, we believe we will gain more presence in the segment going forward.

So, that's overall how we are positioning our portfolio in line with our focus and trust strategy. In Ukraine, we have a similar strategy. We are also eager to expand our non-beer offerings as well. And our best performing brands in Ukraine are Bely Medved, Kozel, Stary Melnik, ESSA. So, we gained market share on the upper end of the core. And together with that our global brands performed well like Stella and Corona and added to the premium segment gains share and improved the revenue growth initiatives. So, that's in a nutshell the winning brand portfolio focus.

Going into Turkey, let's remind globally when we look at the beer industry, beer industry impacted more wherever the on-trade has a higher stake in the total beer market. And within our portfolio Turkey has the highest on-trade share. You would remember it's around a quarter of the total volumes. And if we include also the outside consumption, it is almost one-third even higher than one-third of the beer volumes. So, the impact of the restrictions, closures on the on-trade were mostly felt in Turkey. Therefore, Turkey beer operations finished the year with just under 14% volume decline, where we have been especially observing very tight restrictions since mid-November.

2020 is also a memorable year for us as we made the successful relaunch of Efes family under these difficult circumstances with no on-trade, no social gatherings and with off-trade sales limitations during December. Therefore, we have accelerated market activations and spending related to +1 relaunch to enhance our visibility and consumer touch especially in Q4. The impact on our operating profitability can also be observed in Q4 after a very good run in the first nine months. We started to see certain important stabilization in Efes family performance after the launch that is good. And in Turkey the second half of this year 2021 will be critical as we expect some normalization and opening of the on-trade, more gathering. So, that is in a nutshell what we are doing in Turkey.

Let me say a few words on the Soft Drinks as well. CCI's consolidated sales volume increased by almost 12% in Q4 and thus limiting the full year decline to 1.9%. International sales volume showed us better performance and grew by almost 3% in 2020 as a result of lower exposure to the on-premise channel and a higher share of the strong sparkling category. Pakistan volumes grew by 6.2% driven by the successful market execution bringing the leadership position in the sparkling category. Turkey volumes are undoubtedly the most impacted one similar to the beer due to relatively higher exposure to on-trade, but it has shown a significant recovery in the last quarter of the year as a result of activation of multipacks for at-home consumption and well managed consumer promotions through new digital platforms.

Let's look into the financial results after the volume performance, revenues grew by 16% to TL 26.7 billion as a result of price increases and revenue growth management initiatives. Please note that there was around 10% positive currency translation impact that had positively impacted our top line performance as well. We were able to deliver 26% EBITDA growth with 146 basis points margin expansion. Our EBITDA margin reached to 19%, which is the highest level in the last eight years, and this performance was mainly driven by the saving programs in the OPEX that have been implemented since the beginning of the crisis.

We recorded TL 815 million net income to the year versus over TL 1 billion a year ago although there has been an expansion on the absolute operational profitability. The year-on-year decline on the bottom line was a result of few items like lower contribution from the idle assets sales compared to the last year, and the difference was around 170 million and as well as the non-cash spare parts amortization adjustments and Iraq put option revaluation expense by our subsidiary CCI.

Yet we recorded the highest ever free cash flow of TL 3 billion driven by the superior performance in working capital management as well as prudent spending in our CAPEX programs in addition to the strong EBITDA generation and positive impact of the idle asset sales program. As a result, we finished the year with the consolidated net debt-to-EBITDA ratio of around 0.7x. And Orhun is obviously going to take us to more details.

Orhun Köstem, Chief Financial Officer

Thank you, Can. And good afternoon, and good morning everyone wherever you are. We are very pleased to be with you today reporting on our 2020 full-year results and we are also pleased to report a very good set of results. And to the extent which I believe if one was to look back in the course of the next 5 to 10-year time, it doesn't give a hint that 2020 was an absolutely extraordinary year for all of us.

Now, the reason I believe that is, if I walk you through at first page 12, financials as Can was explaining is good. If you look at Anadolu Efes, we report top line growth despite the fact that our volumes are slightly less and our margin has expanded, our EBITDA margin has expanded, and our free cash flow was a record high. Obviously, Coca-Cola İçecek had a great run in 2020. I'm sure you must have separately followed that. But I'm also sure that you must have noticed that at the end of 9 months in Anadolu Efes, we reported 19.1% margin in comparison to 17.6% a year ago and now we report the same, that's not a typo, it's just that the numbers are the same.

The composition is a little different. CCI was expanding their margins by about 300 basis points then and at the end of this is quite similar, 280 basis points; excellent performance. If you look at international beer or on the beer side, in general, first, we have been able to improve our margin performance quarter-on-quarter throughout 2020. That's until the end of the year. Now, if you look back on Turkey, we only had about 50 basis points margin difference at the end of 9 months, that difference has expanded in Turkey at the end of the year. Turkey is now behind by 150 basis points and obviously that's due to what Can was explaining, we made a massive launch in 2020. And in last quarter of the year as a preparation for 2021, we started investing and spending behind our brands. Nevertheless, if you look at the international part of the business, especially CIS, our operations in Kazakhstan, Moldova, and Georgia, which collectively are at a comparable size to Turkey by all means has reached very high margins and have delivered quite well free cash flow. So, obviously that has balanced the differential. And in our joint venture business in Russia and Ukraine again, we have been improving our margins since the first quarter of the year running through the last quarter basically. So, we ended up the year in international businesses at flat margins versus last year, and even though Turkey was behind, we are reporting only some 20 basis point margin expansion on the beer group.

Strong free cash flow. Again, both on Coca-Cola İçecek but also on the beer group. As Can was explaining, there are differences between these two especially if you look at the last quarter. You will remember that we sold the ex-Istanbul brewery land in the last quarter of 2019. So, that was recorded in Turkey. This year, we sold the ex-Moscow Brewery land and that is recorded in our international businesses. These are some of the differences that you should pay attention in our results. Otherwise Turkey has maintained free cash flow basically in that sense. And the working capital difference on the international is the result of the fact that we have delivered a little less than last year. You remember all of the CIS businesses have done great. In fact, all of our businesses have done great in working capital. I'm going to share with you in a second what I mean. Having said that our JV business delivered negative working capital, so it's accretive to our free cash flow. In 2020, it was less negative than 2019.

So that's the primary difference between two years. But otherwise very good strong performance that we are happy with.

In the next page, if you look at how our EBITDA has developed, I'm sure you will notice that the operating expenses piece that was what Can was referring to, is a positive number and obviously we spent less than in previous year on the beer group. Now and this is great for 2020, but keep in mind that majority of the savings there obviously was coming from our Zero Based Programs and et cetera. But item wise that are mostly coming from sales and marketing and some of the market, since the market volumes are dominant et cetera obviously we haven't incurred the same amount of spending, but we would like to spend in 2021 to foster more consumption in our respective markets. So that's something to keep in mind.

And if you look at this other number, the majority is the conversion. I believe it is TL 190 million that falls into EBITDA is the conversion factor. If you look at the free cash flow there you see a negative change in working capital, as I said, this is a year-on-year difference on the rise. On 2020, we reached a record low working capital in some of our businesses including Turkey, which is primarily driven by receivables management and testament to all teams across all markets. We have managed our receivables at or below previous levels in these relatively difficult times. Our inventory levels, days of inventory have been a little bit higher by design because we wanted to manage 2020 in such a way that if second waves, third waves whatever were to come there won't be any disruptions in our supply chain and production. So, there is opportunity there for next year. And payables basically, we're quite happy with the performance and we're going to continue managing these quite carefully. Hopefully in 2021 especially in the second half of the year we see markets coming closer to whatever normal there could be at that point in time. But in general, as I said good free cash flow performance.

And at the end of the day if you look at, this would be on page 14. Our leverage ratio again, Anadolu Efes, it has gone to 0.7x from 1.1x, and on beer group it was 1x now it is 1.1x; quite let's say flexible balance sheet and healthy ratios for us. As I was saying we recorded very low working capital and in places like Turkey that was lowest ever. We are actively managing risk. At the end of 2020 on the beer group, the Eurobond is the only outstanding FX denominated debt, financial debt that sits on our balance sheet and then we minimize the volatility on our bottom line with net investment hedge that is in place. And separately we manage the commodity and currency exposure in the P&L. In Turkey for example we've hedged against FX price 78% for 2021 across we hedged about 60% of our minimum exposure and about 69% of our malting barley exposure in general. So, hopefully it will allow us to have a good round in 2021 as well.

As I was saying we had an idle asset sales program since the end of 2018. I can say that by the end of 2020 it's almost done. I'm sure you must have followed from our announcements or from our footnotes, the last two items that we reported was on Moscow and then the Lüleburgaz land sales, but that program is for all practical purposes complete. Our Zero Based Spending Program, we made great use of that in 2020. And in 2021, we are increasing the footprint of that program across operations like Moldova and Georgia. We also set it up at the end of 2020 and we'll start executing in 2021.

Our average debt maturity at the end of 2020 is below 2 years, that's primarily owing to the fact that our Eurobond is maturing in November 2022. It's difficult for me to tell you exactly what we are going to do with that, but I can tell you with great clarity that we would be ready to capitalize on any good market opportunity starting from 2021 for that.

With that I revert back to Can. Thank you.

Can Çaka, Chief Executive Officer
Thank you, Orhun. Let me remind you once again about the leverage of our profitable growth and market share expansion. Going forward and especially in 2021, we will continue to invest in the market to drive consumption. I'm happy to say that we will increasingly leverage our digital infrastructure as we expand the footprint of our digital capabilities on the field. Our brands will always be at our core focus. We'll continue to invest in our brands, we'll continue to innovate as we explore new extensions and new categories that are appealing to our consumers.

In terms of profitability, number one priority is to make sure that we have a healthy topline performance. Therefore, we will continue evolving and benefiting our profitable revenue growth management initiatives. As of today, I can say in every other country we had the price increases implemented over the board covering the excise taxes, covering part of the costs and raw material inflation. So, that has been done by within the first 45 days of the year. And we will continue to leverage our Zero Based Spending Program through the year. And in 2021, we started to expand this program across all CIS operations, while also adding new categories within the scope, so, it could be extended in everywhere. We intend to derive consumption and deliver growth profitably as we transition to a new normal hopefully to the year.

However, I would like to emphasize that it is very likely that 2021 is going to be another challenging year, no surprise here. There are still little uncertainties ahead of us. I'm happy to note that we made a good start to the year, but considering the uncertainties lying ahead of us, we remain cautious. Although, we see reason to be more optimistic especially for the second half of the year, we do not expect to get near to normal in the first quarter and probably through the second quarter as well. Under these assumptions, we expect our beer volumes to grow by low single-digits and with Soft Drink volumes growth to be around 4%-6%. As a result of our profitable revenue growth management initiatives and price increases, beer revenues are expected to grow by low teens and that the expectation on the Soft Drink side would be around high teens. We'll continue to invest in our markets and brands to drive consumption in 2021. And therefore, we will step up spending on marketing when there was a significant saving through this year. Thus, following a very prudent 2020, we expect some dilution of our profitability margin in 2021 with topline growth.

We will continue to deliver strong free cash flow generation. However, as we roll a very low working capital base in 2020 and as Orhun said now, that our idle asset sales program is concluded, our absolute free cash flow is expected to be lower than that of 2020.

Thank you again for joining us and thank you for your patience and we can take the questions now.

Asli Demirel, Head of Investor Relations
We already have one from VTB, Alex. Hello, could you please elaborate on your performance in the international markets, Russia and Turkey in the first two months of 2021? What is the growth and how are the on-trade channels performing? Do I get it right that there will be price adjustments in line with tax hikes on inflation and there will be a production change in favour of more premium products?

Can Çaka, Chief Executive Officer
Thank you, Sascha. Actually, partly I answered this. Obviously as I noted in every other operation, we implemented our price increases to cover the excise wherever it is applicable and the cost inflation as much as possible. So, that is done. How the market started? Let’s start from the assumption, we were expecting the first quarter to be more or less with similar restrictions like the fourth quarter of last year and gradual relaxation in terms of limitations through the second quarter and kind of normalization starting from second half onwards.

Having said that, we have seen despite the number of cases are still high everywhere, we have seen certain, let's say, relaxation in Russia and in CIS, Central Asia, in CIS countries, other CIS countries. So, there we had a strong start to the year I would say overall. Turkey, more or less similar, restrictions are very similar, on-trade is closed, weekend lockdowns continue, lockdowns in the evenings during the weekdays continue. So, there is not much difference versus the last quarter.

So, I would say that from the product mix, obviously, overall that is part of the strategy we are driving globally. We see premium segment growing, so that we are investing in that one. That is in every other country we see the premium segment growth and our market share growing in this segment that is balancing the core and mainstream growth as well. So, that's helping us. That's overall where we expect a similar trend like we had this year. I hope this covered the question probably.

Asli Demirel, Head of Investor Relations
If you would like to ask your question, you can write it down on the box. So, let me remind again. There is one from Barclays. Hello, thank you for the presentation. Given leverage is very low do you think you would like to use the headroom you have? Is the priority dividends, expansion CAPEX, acquisitions or do you expect to remain around current leverage levels for the foreseeable future? Thank you.

Orhun Köstem, Chief Financial Officer
Thank you, Daniel. Great question. Leverage is, I have to tell you, if you ask me how we were going to land at the end of 2020 I'd probably have given a different number back in the first quarter of 2020 or second quarter of 2020. So, we are at a good place. Now if you look a few items in terms of our capital allocation that we need to consider. The first priority obviously is to invest in the organic growth of our business, our brands, which I'm sure you must have already seen, as we explained, we are also doing in 2020 and we should continue to do so. Especially in 2021 that could be important given the fact that in many of our markets in Central Asian markets, in Turkey obviously the total consumption, market consumption came down. We would like to make sure that we support consumption growth in 2021. So, basically organic expansion is important for us.

Secondly, yes, from a shareholder value creation, whatever incremental cash is available to us, yes, we do distribute dividends. I'm sure you must have seen through the course of this past two years especially when we have the idle asset sales program. We have turned the proceeds into dividends basically. Going forward, as I was saying, and Can was underwriting, and that program has practical purposes has been finalized. But nevertheless, we will continue to obviously seek to grow our free cash flow.

Finally, a few things for us were quite important in this period of time, over the course of past two years, and I'm happy to say that we have acted on those priorities. One of them, as I'm sure, you must be following us is to ensure that in Russia and Ukraine we would very much like to ensure that the joint venture operates successfully which we have seen for the past two years. In Turkey, we wanted to make sure that we invest behind our mainstream brands, primarily Efes Pilsen family. As I've said in 2020 we have made the relaunch within that family with reasonably early but reasonably good results that we have received.

And finally, going back to answer your questions. Yes, we would very much after making sure that we can achieve these targets, we would look at any expansionary opportunities, but that probably would be practically beyond 2021. And in general, again, as you will remember normally our policy is to maintain our indebtedness somewhere between 1x to 2x net debt-to-EBITDA. As I said we landed at the end of 2020 much better free cash flow than our anticipation, but you should take this again as a general rule, as a general guidance going forward. Thank you.

Asli Demirel, Head of Investor Relations
There are a few more. The next one is from Hanzade, JPMorgan. How is the competitive environment developing in Russia? Have you started to observe price increases by competition?

Can Çaka, Chief Executive Officer
Hi, Hanzade. Very good question. I would say the competitive environment is nicely developing in Russia. It is much more prudent, much more reasonable compared to a

year ago. In that perspective, as you would remember we focus quite a balanced approach here with the profitability and the volume growth together and balancing the value and volume share on our side. And we have seen competition, you're following competition as well, us and competition also had price increases, obviously. In Russia price increases, especially reflection of price increases, especially with the modern trade is about renewing the contracts with the modern trade. So, it's a process. We are renewing our contracts; they are renewing their contracts as well. It takes some time to have the full reflection to the shelves, but it is moving. We have seen in the fourth quarter also the total promotional spending is lower versus the prior period. Overall, I would say the competitive environment is prudent compared to a couple of quarters ago.

Asli Demirel, Head of Investor Relations
The next question is from Metin Esendal. Hi, thanks for the opportunity to ask the question. Do you have any study on the health of Horeca after pandemic? How much of Horeca segment will be under pressure in your view? What's your strategy to support these entities that would be under financial stress?

Can Çaka, Chief Executive Officer
Thank you Metin. Again, another very good point. Obviously Horeca had a reasonably well summer season last year after the openings, after June 1st, July, August, September to some extent, October was okay, but starting from mid-November we have seen again cases increasing, limitations everywhere. So, again this turned out to be very tough period of time for Horeca and it is noted in our presentation, the on-trade proportion is the highest in Turkey. That makes much of an importance in Turkey. And in that perspective, we are very closely working in contact with our partners. Horeca is an important channel, it's part of the ecosystem. I am sure you have followed our various conversations, public announcement and communications. At the end of the day, you are the strongest, the strength of your ecosystem. So, we are supporting our ecosystem in every other manner and dealing with our on-trade partners ensuring that they have nicely return back to the business as the limitations would be lifted. And we expect that to start soon as the government already announced. We will see and follow that very carefully and we will encourage them to open their doors to our consumers once and when the restrictions are lifted.

Asli Demirel, Head of Investor Relations
There is one more from Cemal Demirtaş. In your base case scenario when do you expect some easing in lockdown conditions in restaurants cafes and bars?

Can Çaka, Chief Executive Officer
Thank you again on this question. As I try to explain what we thought of, the first quarter would be strong, second quarter onwards spending on various dynamics, and specifically for Turkey we have the month of Ramadan also starting from April. So, we were expecting our business case scenario was somewhere start of the normalization by early May. And given the current categorization for different cities and so forth, the opportunities where the risk profile is low, the opening and to some extent

normalization can be much earlier in the coming weeks in the low category cities. That is good news. And we'll see how that evolves.

Asli Demirel, Head of Investor Relations
As far as I see there are no more questions. If there are no more questions, we may end the call. Thank you for joining.

Can Çaka, Chief Executive Officer
Thank you all from our side.

Orhun Köstem, Chief Financial Officer
Thank you. Have a great weekend and see you in our next call.