ANADOLU EFES

CONFERENCE CALL TO DISCUSS ANADOLU EFES 1H2023 RESULTS

Company: Anadolu Efes

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Participants:

- Aslı Demirel, Head of Investor Relations
- Can Çaka, Beer Group President & Anadolu Efes Chief Executive Officer
- Mr. Gökçe Yanaşmayan, Chief Financial Officer

Aslı Demirel:
Ladies and gentlemen, welcome to Anadolu Efes' 1H23 Financial Results Conference Call and Webcast. Our presenters today, Mr. Can Çaka; the CEO and Mr. Gökçe Yanaşmayan, the CFO.

All participants will be in a listen-only mode. Following the first part of this call, there will be a Q&A session where you will be able to write-down your questions on the question box of your web screen. For those who would like to ask questions, please write your questions before the Q&A session.

Just to remind you, this conference call is being recorded and the link will be online.

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

Can Çaka:
Thank you Aslı. Hi, Everyone. Welcome. I would like to welcome you all to our second quarter conference call. As you're following, since the start of the year, our performance especially in the beer group has been quite good, quite strong and obviously outpacing our expectations at the beginning of the year. So, we observed an improved momentum versus the first quarter as well especially driven by Türkiye, Kazakhstan and Georgia. Despite last year we had a very high base in terms of high EBITDA margin with the price increases we have taken over the board especially in Russia. We've managed to increase our margins in the quarter as well increasing our record level, obviously that has been supported by the strong topline growth and also the favorable cost environment in the quarter,

especially for the international beer operations supported the margin improvement through the quarter.

So I'm very happy. This marks the sixth consecutive quarter where we were able to expand our margins on the Beer Group side and that's obviously a big pleasure for me. Our strong momentum was not limited with operational profitability. Also we were able to have significant improvement in our balance sheet management and cash flow generation and we have now again pushed new limits on these bonds as well.

So with the very solid results we achieved in the first quarter as we discussed from the very beginning of the year, we had very cautious expectations for guidance for the year as we see the first half performance soon, we are revising our full year expectations on the Beer Group and that has been translated on the Anadolu Efes consolidated results as well.

Going to the volumes obviously, our Beer Group volume performance significantly improved compared to first quarter and we were able to grow our volumes during the quarter more than 5% and again, as I emphasized this was a head of our expectations at the beginning of the year. As I mentioned, the growth is mainly attributable to Türkiye Beer volumes which grew more than 20% in the second quarter. We also see improvement in Russian beer volumes versus the first quarter and especially last quarter of last year. So the decline in the overall beer market is lower in the quarter compared to the previous quarters and similarly reflected to our volumes, and as we have now Ukraine operational with two breweries, that is also supporting the volume growth and overall for the international operations we have recorded a low single-digit growth through the quarter.

Specifically for Russia, Russian beer market as I noted a few minutes ago, showed some recovery versus last year's same quarter, and obviously last year it was a low base for the second quarter as the happenings in the region impacted the quarter very heavily and also we had overall the market had supply chain constraints. Also we are seeing the pricing environment being higher with the pressure from the market players and also the trade members as well. So this is supporting the affordability and supporting the market in that perspective.

Specifically, we see the markets like many global markets, we see both the premium and value segments growing in Russia as well, that is obviously value segment more on the affordable side and obviously the premium segment is a general beer market trend as we see across the board.

And on the other hand, when we look at our volumes, our volumes were down versus last year. And basically, again this is the performance or the decline as a percentage is lower versus the first quarter and the previous quarters of the last quarters of last year and that's partly related to the very high base and we have taken significant market share in the first two quarters, first half of last year. So that was a high base for us, when we look at the second quarter specifically, that's linked to that. But overall despite the high base having a, let's say, limited volume decline is better than our expectations and obviously when we look at the topline and with the pricing carry over with the price increases that we had last year, had a significant carry over impact. For the first two quarters of this year, we are seeing positive impact. Obviously this would partially normalize as we have this carry over effect that is normalizing in the second half, but obviously we have lots of initiatives, lots of execution and better relationship with the trade as well and that was supportive for our volumes through the first half and we believe that's going to be supportive for the remaining of the year and also, when we look at the non-alcoholic beer segment we also see that our performance was ahead of the market overall.

When we look at the other countries in the region, Kazakhstan volume improved versus first quarter grew by low to mid single digit in second quarter, we continue to gain market share in Kazakhstan. That is obviously positive and another strong market for us is Georgia with more than 10% growth registered and that is going strongly on the mainstream and premium side as well.

And when we look at the Moldova that's the market that has the most challenges. I mean, we had the highest inflation in Moldova and that has been impacting the consumers disposable income. And also, we see the total population decline in the country with the macroeconomic challenges. That's why we see the market declining in Moldova, but we are also losing some market share because of the affordability issues. But overall, our CIS volume grew by low single-digits on average during the quarter. So continued our performance in that perspective.

Türkiye obviously deserves a couple of words. We had the strong momentum continuing in the second quarter, obviously the affordable pricing environment in the market is supporting this, but also now higher number of foreign residents in the country. Ramadan coming 10 days earlier, strong tourism and also supporting the market volumes, but again this is a very strong growth we have registered in Turkey and on top of the market growth our volume performance was also very strong over 20% and we have also and that is more importantly the growth was supported or coming from the off-trade channel which is that's obviously consumer offtake and that's very important going forward.

And we believe our divers and affordable offerings also helped our volume performance in the period, that's the continuing trend in the market. Few words on soft drinks as well. I'm sure most of you have followed the conference call our colleagues said, like yesterday obviously just a remark, consolidated sales volumes declined slightly less than 9% in the second quarter with soft volumes in Türkiye and Pakistan. The volumes in Türkiye declined by slightly higher than 9% mainly due to cycling a two quarters of strong growth, high base and we see higher impact of inflationary environment on demand on the soft drink side as the price increases that is supporting the topline and bottom line as well.

In international operations, there was 8.6% decline due to mainly Pakistan and in Pakistan the decline was around high twenties range, and that's mainly driven by the macro headwinds, as well as sudden increase in the excise tax that's returning as higher price increase and Central Asia, Uzbekistan continued to be the fastest growing operation proving the acquisition and geographical expansion as being a very right step for the CCI operations and now CCI registering more than 25% growth in the second quarter.

And couple of numbers before I leave the ground to Gökçe for more details, our revenues grew on a consolidated basis more than 63% in the first half reaching to more than TRY62 billion range. In certain markets, we were able to take pricing and overall we also across the board we enjoyed the carry over impact of the price increases of last year and the growth was also supported by year-on-year higher FX translation impact, which is the international operations translated back into TRY for the reporting purposes.

In Beer Group, it has grew gross profitability performance. And therefore EBITDA performance was delivered with strong support from international brewing, international beer operations and although OpEx to sales ratio was higher, soft drinks gross margin was impacted, as I mentioned, high inflationary environment, but it was mitigated by tight OPEX management on the soft drink side and on top of the strong base, our consolidated net income increased to TRY3.3 billion in first half, mainly due to high profitability EBIT as well as revaluation gain of around slightly less than TRY700 million recorded from Anadolu Etap's consolidation into our accounts. It was another period, where we were able to generate high free cash flow and for our operations when you look at the free cash flow generations, that was supported by both business lines and main source of obviously the support mainly driven by the higher profitability and very strict CAPEX spending to the first half.

That would slightly less in the second impact of the lower CAPEX will be less in the second half as we need to plan for next year and even longer horizon given the extending lead time in terms of machine and equipment, but still with the operational profitability will be able to continue deliver our expectations and as a result, our net debt to EBITDA ratio was parallel to what we had at the end of first quarter, lower than one times that's very healthy on a consolidated basis.

Now I'll leave the ground to Gokce for much more details.

Gökçe Yanaşmayan
Thank you, Can. Good morning, good afternoon, everyone. Welcome to our conference call for first half results. Following another strong quarter, I'm happy to provide you more flavor about the results we're seeing. Beer Group sales revenue was up by 49% to TRY14.6 billion in second quarter, it represents an increase of 29% with FX-neutral basis.

International beer operations sales, revenue grew by 38%, reached TRY10.9 billion and Can also mentioned carry over effect of pricing from last year, still continues to in the second quarter hence revenue per hectoliter increase is still very strong in International beer is around 39%. But again, as Can also noted that this has to get normalize in the second half of the year as the highest price increase, implemented in second quarter last year.

Türkiye beer sales revenue grew by 95% to TRY3.6 billion, again supported by a very strong growth of revenue per hectoliter of 61% and together with volume uplift of 21%. Beer Group gross profit was also up by 68% to TRY7 billion. And similar to first quarter actually, here we have a very solid profit and expansion in gross profit margin by 555bps and thanks to main international beer and driven again by this pricing to get together with the cost escalation being slightly better than our expectations. In the following slide on the left upper side of slide you see net revenue in the second quarter increasing more than the cost of goods sold, which is the expansion of gross profit I just mentioned. And just a reminder, the percentages on the chart represents the FX-neutral growth and you see also here again increase in OPEX is slightly higher than revenue but in last year in second quarter, actually we had a very low base due to low selling and marketing expenses due to frozen expenses in Russia.

Yet, together with positive impacts from conversion, Beer Group EBITDA grew significantly to TRY3.4 billion in second quarter, and with a quite high margin of 23.4% and this came with a high base of last year and represented the expansion of 317 bps in EBITDA margin.

Typically, following a weak first quarter in terms of cash generation, we see a strong second quarter this year as well. And this is very comparable to last year numbers as we see again, free cash flow was supported by higher operational profitability. Here we see negative number in working capital which comes from actually lower conversion impact of working capital in Russia as the ruble also weakened this year.

But all in all, cash generation was reported at TRY5.1 billion in second quarter.

Next slide. And cash and debt management actually here things are more or less in line with our internal policies, at the end of Q2, 46% of cash we hold was hard currency denominated in Beer Group and 53% in Anadolu Efes Consolidated. Net debt to EBITDA ratios are at very healthy zone, 0.8 times for Anadolu Efes Consolidated and 0.4 times for Beer Group.

And then next on risk management briefly, not much has changed here, I can say that from the commodities, we can hedge. We had almost completely hedged our aluminum for 2023 already and we have started to hedge for 2024 exposure and currently we are at around 38% of our coverage and from FX exposure point of view as well, our P&L was for this year well covered, for next year, we will start also hedging Barley. So basically this concludes my presentation. I will give word back to Can. Thank you.

Can Çaka
We've been very cautious at the beginning of the year, with the pricing environment, with the inflationary environment in every other market. We've been discussing at the end of first quarter as well that we will be revisiting our year-end guidance by the end of first half.

So in that perspective, seeing the very strong first half results, we are revising upwards, especially on the Beer Group, our year-end expectations. Still, we are cautious for the rest of the year, but we see various ups and downs and various impacts for the second half of the year. And we expect our performance with respect to the markets in every other market to continue and we have full confidence to revisit and revise our full year guidance.

And accordingly we improve our beer volume to a growth expectation versus an initial decline expectation with the strong momentum we've seen Türkiye beer and less pressure especially in Russia, we see low single-digit growth for the year-end. Therefore, on a consolidated basis, we now expect our volumes to grow by mid single digits. Again this was low to mid single digits at the beginning of the year.

We improve our Beer revenue growth expectation to low twenties on FX-neutral basis as a result of the improved volume. Obviously on a consolidated basis, we expect our revenue to grow by high thirties on FX-neutral basis, again, and this was low thirties at the beginning of the year in terms of Beer Group EBITDA margin outlook, despite we had record level of margin expansion last year, extraordinary strong performance in that line, we have cautious position at the beginning of the year. We were expecting margins to decline and normalize to some extent, but now it's very limited now on the basis decline and be likewise our consolidated EBITDA margin is expected to decline more or less in the same range and I guess this is it for the time being. Thank you for your interest and if there are any questions, we would love to answer your questions.

Questions And Answers

Aslı Kılıç Demirel
Thank you very much Can. We have couple of questions. Let me start with the first one, can you provide an update on your Russian dividends. Can you provide an update on the progress with regards to

Russian JV acquisition? Does news of Russian nationals being prioritized in any acquisition in Russia changed your thinking at all. How have discussions with ratings agencies progressed? Your outlook is negative by S&P and you are still on watch negative by fitch. When can you expect your rating to be normalized?

Gokce Yanasmayan
I can take this.

Can Caka
Thank you Gokce.

Gokce Yanasmayan
With dividend actually we have understood that these processes are overlapping with the deal finalization. So basically, our first focus is to finalize our deal and to be able to apply to that and then we will go forward for dividend payment, so there is a prioritization there and we want to make sure if we finish the deal at first. Well, I think that's to certain extent answered question about the progress of the deal as well. The deal is progressing. We are still in active discussion and trying to finalize the details of our agreements, obviously after the recent developments in Russia, we are being cautious and trying to also understand what's happening and making sure that we took the right steps, but our intention is still to finalize the deal.

And when it comes to the rating agencies. We have basically you know the good news there actually is that our rating was downgraded with reasons out of our company performance and which is a good news and we are obviously committed to take our ratings back, and we have constant touch with S&P and Fitch, reviews meetings with them. Actually I can't obviously tell about timing, that's something that they will know, but our performances are strong and we are willing to take our rating back as soon as distribution allows us.

Aslı Kılıç Demirel
Thank you Gökçe Bey. Can you confirm how much cash you have at EBI Netherlands level and the percent of our currency cash?

Gökçe Yanaşmayan
I can also give an answer to that, around 50% of our Beer Group cash is in Netherlands.

Aslı Kılıç Demirel
And there is a question about ABI deal but you already answered. So I'm not going to repeat it. And a question comes from Erkan Edincik. How is the third quarter performing in both domestic and international markets, are you able to reflect cost increases in selling prices? Is there a possibility of an increase in profit margins in the third quarter? And he continues with a question of, could you provide information about the competitive conditions in Russia, is there any update on the complete acquisition of assets there? The same question. So, Can Bey, maybe you take word.

Can Çaka
Thank you and let me try to respond to this. I mean obviously with respect to updates about Russian JV development Gökçe have already provided the details. When we look at the volume performance like I was trying to pin-point you to presentation. When we look at the international markets, we would be having a lower base effect going forward in the second half volumes mainly driven, mainly we have seen

in the international markets volume decline in the second half of last year driven by Russia, but also at the higher price points and the higher price increases across the board.

So in that perspective, we see second half as a lower comparable in terms of volume, obviously, going forward. Türkiye is different on that perspective in the second half of the year, you would remember, last year we were able to grow volumes with our offerings and making expanding the portfolio with more affordable offerings as well that also helped the market grow in Türkiye. We also, which has been supported by a very strong tourism impact. Therefore Türkiye, we will have a higher comparable in the second half of the year, because of these main drivers. So the two pieces of the equation would be our portfolio, international and Türkiye would have different comparables. But that's again, we reflect all these into our year-end guidance in that perspective. You'll see flattish volume for the time being and we are giving a guidance for the full year as low single-digit volume growth. Therefore, we expect to see volume growth continuing in the second half.

In terms of our cost increases as we discussed at the end of last year as well to 2022 was impacted with very high commodity prices. Current commodity cycle is supportive, but we were seeing a higher inflation carry over impact. High inflation impact moving into 2023, higher energy prices and the higher secondary raw materials in that perspective.

We see in that sense in the first half, we have seen, let's say better than our expectations in the pressure side so that is positive and currently we see that continuing as well. That's also reflected into our margin guidance going forward. So overall, we don't see a major issue in terms of reflecting or covering or how we have already implemented the price increases that are necessary to execute our year-end expectation.

So we properly going forward, we're trying to make sure that we don't lose the, let's say, competitiveness in terms of pricing, see value in segments growing in every other market and our value offerings are usually significantly less than our fair market share across the board. That's why we were cautious to make sure we reflect compete on the response to the competition in that perspective.

And let's link this to Russia in terms of pricing environment we see, again, similar to what I'm trying to describe right now. The pricing environment with lots of promotion from the old players I would say, and let's say, lower than inflation price that is driven by the competition that is driven by the, let's say, trying to make the products more affordable and more driven by the competition. We see the pricing environment tough. Good news is we had significant carry over impact for first half, second half that would be balanced, but again with the volume performance, currently we are in good track for reaching to our year-end targets. I believe that covers all aspects of the question.

Aslı Kılıç Demirel
Thank you, Can Bey. Another question, could you provide cash position in Russia and Ukraine? Could you share the contribution of Russia and Ukraine, the total EBITDA in first half? How it change compared to first half of the last year. Could you provide maturity schedule of loans and Turkish beer operations on how you plan to handle short term maturities?

Gökçe Yanaşmayan
Aslı let me take that. Cash position in Russia is quite strong actually, we are quite cash positive there. And currently, maybe I can again give percentages around 50% of our acquired total cash flow of Beer

Group is in Russia and Ukraine together and that represents more or less one fourth of Anadolu Efes' all Consolidated cash distribution.

Contribution to EBITDA is again Russia and Ukraine together in Beer Group, we can say that it's around 65% and that's very similar to last year's actual numbers and Anadolu Efes, it's again one-fourth of our EBITDA in Russia and Ukraine together. And the Turkish loans, yes, they are of short nature, beyond the average close of six months or so and we accept that there are difficulties in Turkish market is currently about refinancing. Therefore, in the second half of the year, we may choose to pull some of them and refinance some of those depending on the availability and cost of postponed.

Aslı Kılıç Demirel
Thank you. Another question comes from Ece Mandacı. Congratulations on strong results. Could you comment on USD/Ruble performance and its effect on your business overall including price actions. Have you observed a major change in competition in Russia following the change and controlling Carlsberg?

Gökçe Yanaşmayan
Can If you'd like, I can take that.

Can Çaka
Yeah. All right.

Gökçe Yanaşmayan
Obviously, we are working on potential impact of ruble depreciation currently happening in Russia and it is quite volatile, so the number is as we work you know they change I will be able to give a better flavor of the impact of this change once we finalize our budget process towards the end of the year, but there will be some impact that we will probably we need to pass some of them through price actions for next year tough. For 2023, as I told, we are fully hedged actually. So that doesn't have any impact.

Aslı Kılıç Demirel
Thank you. Another question from Parwin Mammadov. We think the volumes in Russia came higher because the overall consumption is higher than expected or you stole market share from the competitors.

Can Çaka
Good question, I mean as I tried to explain, the market performance was better than our expectations, so the market is performing better and I would say, despite a very high base of high market share we had last year, our performance also is better than our initial expectations. I wouldn't say our current market share is higher than what we had last year, but we are very much focusing on value share as we discussed in prior calls as well and in that perspective, we see our value share is reasonably in line with our expectations.

Aslı Kılıç Demirel
Thank you. Can you provide more color on postponed payments in your free cash flow outlook comments for '23?

Gökçe Yanaşmayan

Yeah, maybe I can just tell a detailed that there are certain elements that we have to do on JV level of Russia and Ukraine which were depending on the cash repatriation from Russia. That's why they are being postponed.

Aslı Kılıç Demirel
The last question is actually a similar one. Is my understanding correct that no dividends or other distributions from Russia took place since '22, is it due to difficulties with obtaining permits? Could you please discuss which countries apart from Russia and Ukraine paid dividends in the first half to the holding company beer segment?

Gökçe Yanaşmayan
Yes. We haven't received any dividends, that's the correct understanding. I try to explain the process which overlaps quite a lot with the deal-closing process. Therefore again, we wanted to focus on deal closing before we go forward. And besides Russia and Ukraine, actually all our operations make some sort of dividend or loan repayment.

Aslı Kılıç Demirel
Thank you very much. This concludes all the questions. Maybe we can also conclude the conference call as well. Thank you for joining and listening.

Can Çaka
Thank you all. Thank you Asli.

Gökçe Yanaşmayan
Thank you.