



Tat Gıda Sanayi A.Ş.

Tat Gıda Sanayi A.Ş. Third Quarter 2019 Financial Results Conference Call

Thursday, 31st October 2019 (17:00 TR Time)

Conductors:

Mr. Başak Tekin Özden, CFO

Conference Call Conducted by Chorus Call Hellas



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OPERATOR: Ladies and Gentlemen, thank you for standing by. I am Konstantinos your Chorus Call operator.

Welcome and thank you for joining the Tat Gıda Sanayi A.Ş. conference call to present and discuss the Third Quarter 2019 Financial Results. At this time, I would like to turn the conference over to Ms. Başak Tekin Özden, CFO.

Ms. Özden, you may now proceed.

ÖZDEN B: Thank you, Operator. Hello, everyone, thank you for joining our webcast. I am happy to share that we closed the third quarter with successful results and we maintained our performance. I will walk you now through the details and answer any questions you may have at the end of our presentation.

First of all, I would like to update you on the discontinuation of Pastaville operation, what has happened until now and what we expect to happen going forward. As you may all remember, we agreed with Durum Gida Sanayi AS on the sales of Pastavilla, Kartal and Lunch & Dinner brands on the 2nd of August this year and we had received 8 million Turkish Liras in cash in the same period.

The right of ownership of the brand was transferred with the approval of the Competition Board on 2nd of October, so accordingly the income from the sale of brands will be included in our October financials. In terms of the operation, production at our factory in Izmir stopped on the 2nd of September and activities related with the product sales stopped on 2nd of October with the approval of the Competition Board.

So accordingly, in September, the... for the... because of the termination of employee contracts, the P&L impact of severance and notice payments was 3.3 million TL. The remaining employee agreements will be ending in October and which will have a P&L impact of 1.3 million TL in October again. So in total we will be paying 8.1 million TL in cash for a total of 84 personnel including outsourced employees.

Going forward, there are no obstacles ahead to sell the land and the remaining equipments, so this is now what we will...we are going to focus on now and we will post the relevant income on our books when the sales are realized.

On our Quarter 3 financials, you will see that the Pastavilla business is separated as discontinued operation. And with also 2.1 million TL in 2019.

So coming to our financials, as you see on the chart, we closed the first quarter with a... net sales of 829 million Turkish Lira. This is a growth percent of 4% over last year's same period. I would like to remind you that the reclassification in our sales figures, last year in the same period around 40 million TL of marketing expenses were attributed to action sale of incentive contribution have been re-evaluated as sales discount, so accordingly they have been reclassified under sales. Now with the reclassification, our financial figures are on a comparable basis.

Also I would like to remind you that we have exited the Private Label sales in SEK business last year in the last quarter as the business has started moving away from our profitability targets.

So next, you will see the breakdown of our sales by product group also with a like-for-like comparison. In the second one...in the second graph, we eliminated the private sale...label sales in the SEK business from last year's same period figures. And although you see a 3% contraction in SEK business on the left, you see that there is a 30% growth on the right, 30% all branded sales with our Private Label business.

And we achieved this growth through increase in communications, expanding our distribution network, making listings in discount markets where the growth is, and further pricing actions. We also achieved strong growth in the tomato business. In fact, the growth rate is 12% in the segment. You know that last year tomato output in Turkey was lower than previous year and accordingly the prices were higher. This year, we had a very good tomato season.

Total Turkish industrial production increased by 60% to 2.1 million tons. And accordingly, average tomato prices were lower 13% than last year. So the amount of tomatoes we supplied and the prices are in line with our targets. Our average cost was 0.5 Turkish liras. And we maintain to purchase 340,000 tons in this season. So, we are happy with the results and we are happy that we are in line with our target.

Coming to exports, our export total...revenue totalled 73 million TL. There's the 17% decrease over last year. This is a result of

our decision to increase the capacity we allocate to domestic sales. This is why you see a 12% growth. One of them is our...there are 2 reasons underlying this decision, one of them is our ambition to grow in discount retailers where the market is growing. And the second one is the political and economic volatilities in Middle Eastern markets. We want to grow our branded exports with some business partners that we can build long term relations in the region.

Going over to the profit figures, we generated 175 million TL of gross profits, higher than last year by 25%. And we improved our margins by 3.6 points to 21%. Our operating profit was 77 million TL; this is ahead of the last year same period by 79%. In terms of margins, you will see that the 9.3% of operating profit margins we achieved this year is well above our performance in previous years. In fact, if we exclude the Pasta Villa effect of 3.3 million TL for severance & notice payments, our operating profits would be 80 million TL and our margin would be 9.7%. What is the major reason for this performance?

One of them is high growth in high margin Tat business. The other one is exiting lower margin private label business in Sek and high growth in branded sales, with higher margin, further operational efficiencies in our factories, and also there is a favorable effect with respect to last year same period in terms of exchange differences from commercial activities.

By the end of this quarter, our EBITDA stands at 7 million TL to 8 million TL, higher than last year by 64%. And our margin rose by 3.5 points. Depreciation and amortization expenses increased to 18 million TL from 12.5 million TL. And investment

expenses totalled 17 million TL and this was same for last year same period.

We closed the quarter with 3 million TL of income before tax and our margin rose by 1.9 points...by 1.9 points to 6.3%. This year, financial expenses were higher than last year obviously of course, as with any other company. This year, our financial expenses totalled 25.6 million TL versus the 11.3 million TL last year same period. This is a result of the long term financial loans we have been carrying since last year.

And especially 70 million TL of loans we have obtained last year in September in the tomato season with an interest rate of 33%. This was because of the certain economic downturn, the payments for the tomato season and very high interest rates because of the market condition.

So this September, last month, we closed this loan and we paid the commission of 3.3 million TL for early closure. So, we will bear less financial expenses going forward, the benefits were of course, better than... high in terms of financial expenses despite the commission. So, we will see the beneficial effects of this action going forward. So, if I exclude the Pastavilla termination effect and this additional commission for the credit closures totaling 6.6 million TL, our income before tax would be 60 million TL and the margin...our margin would be 7.2%.

So going over to the financial debt position, you see here that by the end of September, our net financial debt is 165 million TL. This is a result of the tomato season being closed. As you may well know, our tomato business has a seasonal pattern and

we go through this, every year. We make payments to our farmers especially in the month of July, August, and September, so our net financial debts go up.

This year, we had obtained most of the loans not...we don't accumulate all the loans in the tomato season, but we diversified our financial loans with different maturities and interest rates. And we wanted to start the season with improved liquidity and we closed the more costed loans and we rolled part of our credits with lower interest rates.

As the tomatoes were in abundance this season, our supply was higher this year, as I have explained already. And so was our payments to farmers were higher as well. These are the main reasons why you see lower cash and high financial debt now versus the first half of 2019.

Overall, our net financial debt over EBITDA ratio is 2%, which is at a healthy level and we are carrying around 70% of our total financial loans in long-term debt. And let me add that all our financial loans are in TL terms.

Finally, you see here our summary balance sheet. Our assets stand at 1 billion TL, 10% higher than last year. The seasonality effect is also visible here on our balance sheet. But in any case, our financial ratios are at healthy levels and we aim to keep them as such.

Going forward, we will see the positive effects of the discontinuation of the Pastavilla business in our financials and also the positive effects of the favorable tomato season. So this

is all on my part. I'm ready to address all your questions. Thank you.

Q&A

OPERATOR: The first question comes from our audio participant Max Percy with Arisaig Partners. The question is what is the size of the plot of land on which the Izmir Pasta facility sits?

ÖZDEN B: We, the... the parcel of land is 9,272 meters square facing the main street on both sides. And we have a right to build real estate with shops and residences on it. If... for those who are familiar to Izmir, it's a very popular area now with many residential and commercial real estate developments. And you know that our factory was already squeezed between these new real estate projects.

So now that we have completed the sales operations of the brand, we are ready to...we are getting ready to sell the remaining equipment and the land going forward.

OPERATOR: The next question is from our webcast participant, Erkan Edincik with Horizon. The question is, do you have any intention to divest tomato pasta business eventually, like wheat and pasta divisions?

ÖZDEN B: No we don't have such a plan. On the contrary, we want to grow in the tomato business. And if the conditions are favorable and the right opportunities arise, we want to grow... maybe may grow internationally as well. So there is no plan [to divest any of our business segments now. I can take next question.

OPERATOR: The next question is from our webcast participant from Melis Pocar with Oyak Yatırım. And the question is: can you give us some update about the recent consumer sentiment and competitive landscape?

ÖZDEN B: Well, in general terms, if we look at long term trends, we see that the discount markets are growing, but not for the last few months, we see there are... the other channels are also growing. So this is, I think a good sign for the economy.

In the tomato business, we have a dominant position. So we don't have many strong competitors and their business, you know that there are many, many local companies producing... in dairy major competitors are big more corporate, large scale customers, I mean competitors like Pinar, like Sütaş. We are more competitive in the cold chain, let me say the cold chain products like daily milk and we see that our competitors are more...competitors in...like the long term milk segments. So depending on each segment, the competition changes but our strong hold is in the cold chain products.

ÖZDEN B: We can move to the next question.

OPERATOR: The next question comes from our web participant Erdem Hafizoglu with BGC Partners. The question is: what will be the net one off income from the sale of Pasta business to be recorded in the fourth quarter '19? And the second follow-up question is, what is the potential value of Izmir Land?

ÖZDEN B: The income of sale of Pasta business in October will be coming from sale of brand 8 million TL, but we also have again because of the severance and notice payments, the P&L impact will be 1.3 million. So the net off will be 6.7 million TL positive. I wouldn't want to give an indication on the price of land.

We can move to the next question.

OPERATOR: The next question comes from our web participant Max Percy with Arisaig Partners. Euromonitor has private label making strong market share gains in Tomato Pasta. Have you lost share to private label in this or other categories?

ÖZDEN B: No, on the contrary we are gaining share in both private label and in branded products. Maybe, the private label, the euro monitor data maybe including the tomato paste importation that was released this year for the discount market and we had already arranged... we had agreement; private agreement for the 4,000 tons quota of paste import that we did.

Also, we are already making a private label agreements with discounters for our own production, plus we're also making listings with our branded products. So in both terms, private label and branded, we're growing in tomato business, so paste, tomato paste business, there is no market share loss. Please, could we move to the next question?

OPERATOR: The next question comes from our audio participant, Melis Pocar with Oyak Yatırım. The question is, despite the fact that we are aware that you are not a guidance company with exit from

pasta business, is it fair to assume that low double-digit EBITDA margin level is achievable and sustainable?

ÖZDEN B: Yes, we think our performance is sustainable because our performance depends on the mix of high margin sales, growing with branded sales, growing in new channels and discounting with listings as well. And we have also made operational efficiencies in our factories. So going forward, I can say that our performance is sustainable. We can move to the next question.

OPERATOR: The next question comes from our audio participant, Kayahan Demirak with IS investment. The question is, given the decline in raw tomato prices, how much contraction should we expect in shelf price of tomato pasta in 2020? And do you see any significant pickup in demand in next year for tomato pasta given the expected lower prices?

And secondly, regarding that there was a significant rise in the inventory levels in this quarter, so should we see this as you are expecting better demand conditions next year?

ÖZDEN B: Yes, we have of course, because of the higher tomato output, we have higher stocks which were in line with our targets. In the market, there are some...our competitors are... there are some competitors who are trying to make competition with price, but we're maintaining our pricing position, the positioning in the market and we aim to keep our position as it is now.

If the competitors lower their prices with the... I mean, if the gap opens largely, then we may review, but as for today,

because of our brand...equity brand value, we always position ourselves higher than competitors and we dominate the market, so we aim to sustain this.

We can move to the next question?

OPERATOR: The next question comes from our web participant Erkan Edincik with Horizon. The question is, as far as, we know Tat was planning to grow in Dairy business and the cold chain. Do you invest on these lines?

And what is the CAPEX for this year and the going forward, are we going to see some capacity increases?

ÖZDEN B: Yes, as I had mentioned previously, we are stronger in cold chain and we... our strategy is based on growing in the cold chain... also innovating in the cold chain like SEK Quark. We renewed the SEK Quark product. And will also be re-launching our probiotic drinks. We will also have some other new innovations in the cold chain... the cold product line. So we are investing in this line.

This year our investment was almost 3 million TL, where we will keep this level of investment, but not in terms of capacity investments, most of our investments are either modernization, atomization and new product lines...new products.

OPERATOR: The next question comes from our web participant Max Percy with Arisaig Partners. Where are utilization rates for SEK and the tomato business?

ÖZDEN B: For tomato business, you know, it's a seasonal product. So in the season it's like 100% capacity utilization. And in the remaining times the capacity utilization depends on the seasonal products like the... the corns, the other products. But because of the seasonality... in the season we use the capacity 100%. And this is the same for all tomato business.

In the SEK business, our utilization rate depends on the segments or the product. We have... as we have exited the private label business, of course, our volume is lower than last year. But, we had... we arranged our production planning and the capacity accordingly. And this is how we also achieved to make some operational efficiencies. So we are managing our capacity in line with the demand we see in the market now. Other questions?

OPERATOR: Again, our next question comes from our web participant Erkan Edincik with Horizon. The question is, do you have any debt... any net debt to EBITDA target for TAT. Are we going to see deleveraging going forward?

ÖZDEN B: Well, I wouldn't want give any target or guidance, but of course, as we...now we have all the inventory, we have closed the season, now we are going to sell the products. So going forward our aim is to, of course, de-leverage accordingly in accordance with our sales volume.

We will have in the next season... next year, we may again I mean we will evaluate the cash position and take new loans accordingly in the season. So this is next year's question. But, up till the next season, we will be selling our inventory as we aim to deleverage.

OPERATOR: Ladies and Gentlemen, there are no further questions at this time. I will now turn the conference over to Ms. Özden for any closing comments. Thank you.

ÖZDEN B: Again thank you for joining our webcast and your interest. We have to...address any of your questions any time of the year. Thank you.