Anadolu Efes 1H2024 Earnings Call

Company Participants

Onur Altürk - Beer Group President and CEO
Gökçe Yanaşmayan - Chief Financial Officer
Aslı Kılıc Demirel -Group Investor Relations and Risk Management Director

Presentation

Asli Kilic Demirel

Ladies and gentlemen, welcome to Anadolu Efes' First Half 2024 Financial Results Conference Call and Webcast. My name is Asli Demirel, and I am Investor Relations and Risk Management Director of Anadolu Efes. Our presenters today Mr. Onur Alturk, the CEO; and Mr. Gokce Yanasmayan, the CFO. All participants will be in a listen-only mode during the frst part of this call. Following this, there will be a Q&A session where you can submit your questions using the question box on your web screen. If you have questions, we kindly ask you to write them down before the Q&A session begins. This will allow us to review and address them. Unless explicitly stated otherwise, all fnancial information disclosed in this presentation are presented in accordance with infationary accounting. Just to remind you, this conference call 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. Onur Alturk, Anadolu Efes' CEO. Sir?

Onur Alturk

Asli, thank you. Good morning and good afternoon everyone and welcome to Anadolu Efes 2024 frst half operational and fnancial results conference call. We are delighted to announce another quarter of solid volume momentum and robust growth, achieving a high-single-digit increase in our Beer Group. This remarkable growth is further highlighted by a low-single-digit rise in our consolidated volumes. Despite the challenging macroeconomic environment and volatile cost landscape. Yet, we succeeded in delivering a solid expansion in gross proftability margin, which was supported by of course, strong volume performance and revenue growth management initiatives, including pricing, focus on quality mix and premium mix and efective discount management.

On top of our strong top line results, through strict management of operational expenses, we were able to record a fat EBITDA margin. Last but not least, our robust fnancial discipline is clearly refected in our consolidated net debt-to-EBITDA ratio, which stood at an impressive and healthy level of 0.8 times as of June 30, 2024 and comfortably within our targeted leverage ratio range.

And additionally, we have achieved a net cash position in the Beer Group. And when it comes to second quarter in the second quarter of '24, our beer volume surged by 7.1% with strong performances in Turkiye and followed by Russia and Moldova of course driving this growth. And Turkiye beer volume rose by 2.8% while our international beer volume saw an impressive growth of 8.2% and Russia maintained its momentum from frst quarter with volumes rising in the low teens, proving continued strength and CIS countries, however, faced challenges which I will come to details and with volumes declining by mid-single-digits on average. Ukraine, on the other hand, had a successful quarter as well, mainly supported by last year's lower base and recovery in consumer demand.

And when we come to Russia, let me discuss Russia in more detail. The beer industry continued its growth momentum with mid to high-single-digit growth in the frst half. The strong market growth can be attributed to a notable shift from other alcoholic beverages to beers. And of course new product innovations of our company and substantial market investments. We outperformed the industry by registering a low teens growth in second quarter, which enabled us strengthen our position in the premium and core segments while also gaining of course shares in the non-alcoholic beer segment.

Aside from volume growth, we also sustained market leadership on both value and volume basis while gaining share in both metrics. And Stary Melnik, Stella Artois, Essa, and Hoegaarden were successful brands in this quarter, marking strong performances.

When it comes to CIS and Turkiye. Tuning to our CIS operations, Moldova registered mid-teens growth and our volume supported by industrial expansion as a result of increased spending behavior of consumers as well as expanding consumer base. And contrast, unfortunately we observed softer performance in Kazakhstan and Georgia. Our Kazakhstan volumes suffered from weak industrial dynamics and some natural disasters that the country has faced like foods, earthquakes that affected the country during the second quarter and Georgia volumes were adversely affected by production bottlenecks.

But when we look at overall CIS performance, our CIS volume down mid-single-digit in the average. Speaking of Turkiye building on a very high base from last year 2023 as well as a solid performance in first quarter. Turkiye sustained strong volume performance registered at 2.8% growth and truly it's exceeding our expectations. Volume was supported by increased sales in HoReCa, in the hotel channels and the favorable tourism season, despite operating in a high inflationary environment. Additionally, we observed a decrease in consumer purchasing.

When we look at our soft drinks, let's briefly on this one too. In the second quarter of the year, CCI's consolidated volumes increased by 0.7% and thanks to the contribution of Turkiye, Iraq and Azerbaijan. Turkiye volume was up by 1.8%. Effective trade promotions, active consumer marketing including UEFA Euro Cup activations have driven this growth.

International volumes demonstrated a modest recovery, posting a 0.1% increase, which marks an improvement compared to the previous quarter. Iraq and Azerbaijan continued to deliver strong results with 15.1% and 11.5% growth respectively. In Pakistan, while volumes declined by 5.1% year-over-year. This still represents an improvement in volume performance when compared to the previous four quarters.

Kazakhstan experienced a 10.2% decline in volumes, mainly due to the reasons that I mentioned for beer as well, but lower consumer confdence, the return of the foreign consumers to their home countries and high comparison base from the previous year. Now let's move on to our operational results. Actually, we delivered strong results in top line fgures as well as bottom line throughout the quarter despite our eforts for efective pricing strategy, a focus on favorable mix addressing value generation and of course tight discount management.

The adverse impacts on top line primarily came from the implementation of TAS29 because of the mismatch between the infation rates and the devaluation appreciation of reporting currencies in international operations against the Turkish lira. The increase in Anadolu Efes' top line without the impact of TAS29 would be 65% growth. With strong gross proftability and strict control of operating expenses, there was signifcant EBITDA contribution from Turkiye operations in both beer and soft drink businesses. However, the EBITDA margin was pressurized primarily due to the signifcant increase on raw material costs and transportation expenses in Russia.

Our consolidated net income was recorded at the TL3.9 billion increased interest expenses along with a higher share of Turkish borrowing and signifcant FX losses from cash holdings had an adverse efect and led to a decline versus the same quarter of last year. However, these impacts were partially mitigated by deferred tax income resulting from the implementation of TAS29. Free cash fow generation was fattish despite lower operational proftability, which was supported by prudent capital expenditures and strict working capital management with improvement in payables performance.

Consequently, as I mentioned in the beginning, the consolidated net debt-to-EBITDA ratio remained at a healthy level at 0.8 times, highlighting our strong fnancial position. And now our CFO, Gokce will give details on the financial metrics.

Gokce Yanasmayan

Thank you, Onur. Good morning. Good afternoon to everyone participating our conference call today. Onur just summed up the consolidated results of Anadolu Efes, so I would like to go into more detail about the Beer Group results. So, consolidated revenue for the Beer Group in the second quarter of 2024 was TL23.6 billion, down 2.8% from the same period of the previous year. The revenue generated from international beer operations fell by 6.8% during the period, despite solid volume performance. Onur just explained this, but let me repeat because this is important. Simply this is mostly due to the fact that infation in Turkiye outpaced the depreciation of Turkish lira relative to the currencies used in international operations reporting. Under IAS29 last year, financial translated in Turkish lira and are being indexed with inflation rate.

And when depreciation of Turkish lira is less than the inflation, this naturally creates a decline in current year financial compared to the last year, even if local currency financial are same as last year. So in the second quarter, Turkiye's beer operations generated TL6.7 billion in sales revenue, 9.4% rise and in first half of the year, Beer Group's revenue increased by 1.6% to TL41.1 billion. And in the second quarter 2024, Beer Group's gross profit decreased by 3.6% to TL10.9 billion with a 39 bps dilution in the gross profit margin to reach 46.2%. While international beer operations saw a decline in the second quarter, Turkiye's beer operations saw a rise in the margins. This decline in international business was mainly caused by pricing difficulties in Russia despite considerable cost inflation tied to foreign exchange linked raw materials.

So consequently, the Beer Group's first half gross profit was recorded at TL18.1 billion with a fat margin of 43.9%.

In the second quarter 2024, Beer Group's EBITDA dropped by 19.5% to TL4.4 billion with a 384 bps margin contraction from the same quarter the year before. The EBITDA margin of Turkiye beer operation increased, though in the second quarter and continuing the trend from the previous quarter. However, because of increasing transportation costs in Russia, international beer operations faced higher operating expenses. This, along with lower gross profitability resulted in a decrease in the EBITDA margin. As a result, Beer Group's first half 2024 EBITDA was reported at TL5.5 billion with 418 bps declined in margin. And Beer Group's free cash fow grew slightly from TL7.2 billion to TL7.4 billion in the second quarter. Better working capital management and a moderate increase in capital expenditure led to an improvement in cash flow despite decreased operating profitability and increased interest expense. I have to note that as of June 30, 2024, the Beer Group has a net cash position of TL91.8 million due to first half's robust cash generation.

I saw already, I think referred to a disclaimer, but let me repeat. Anadolu Efes' financial statements are prepared in accordance with TAS29 and the Standard. This is the standard for financial reporting in hyperinflation economies. As a result, all information, financial information disclosed on this call and in our earnings release are in full confirmation at TAS29. However, financial information presented on this slide particularly excludes the impact of TAS29 and is presented solely for analysis purposes.

So these figures won't be aligned to Anadolu Efes' financials and have not undergone an independent audit. So, excluding the impact of TAS29, Beer Group revenue was TL41.1 billion with a growth of 74%. Again, excluding the impact of TAS29, EBITDA increased by 45% in the first half to TL6.8 billion and again without the inflation impact, Beer Group net income was reported as TL3.2 billion for the first half.

About cash and debt management. Again, at the end of frst half, we had 57% of our cash in hard currency denominated in Beer Group and 60% in total consolidated Anadolu Efes, which is pretty much in line with our previous experience. And then our net debt EBIT ratio is quite low for Anadolu Efes 0.8 times. And for the Beer Group, as we are in the net cash position, it's below zero.

And the following slide is on the risk management. So just let me provide you key figures here regarding hedges. We have around 89% coverage in aluminum exposure for the year of 2024 and we started to hedge for '25. So the total coverage for the time being is 28%. And for the FX exposure for the year 2024, we are fully covered in Russia and 94% of our exposure in Turkiye. So basically that ends my part of the presentation here. And I'm handing over to Onur. Thank you.

Onur Alturk

Gokce, thank you. So actually, as we have highlighted in our presentation, our first half results have shown resilience across both business lines, particularly in the Beer Group. And reflecting on the performance of the first six months and considering potential future challenges, we have decided to revise our guidance for both the Beer Group and CCI. For the Beer Group, we have made an upward adjustment to our top line figures, although we maintain our cautious stance regarding the downside risk of EBITDA margin.

On the other hand, for CCI we are making some downward revisions due to the lower purchasing power expectations and cautious consumer sentiments. So let me summarize as follows. We improve our beer volume growth slightly expectation to mid-single-digit growth with very good momentum achieved in Russia and Turkiye beer operations. On the other hand, our soft drink operations are revising volumes to flat or to low-single-digit growth due to prolonged sensitivities in Middle East and expected decline in purchasing power.

Therefore, on consolidated basis, we now expect our volumes to grow by low-single-digits which was low to mid-single-digits growth previously. And following this one, we improve our beer revenue growth expectation from low 20s to low 30s on a fx neutral basis as a result of improved volume guidance. Meanwhile, due to softer volume performance and slower pricing executions, we now expect our soft drinks operations revenue to grow by low 30s on a fx neutral basis which was low 40s growth previously. And finally, while our consolidated profitability expectations remain mostly the same, the ongoing operational challenges present a risk our soft drink consolidated EBITDA margin which was previously expected to remain flat, is now anticipated to either slightly decline or remain flat. So this ends our presentation actually. So thank you for interest and patience. We appreciate your attendance. Now, I think we are ready to take questions.

Questions And Answers

A - Asli Kilic Demirel

Yes, Onur Bey. Thank you very much. There are already a couple of questions, so let me start with the first one. It's regarding the process in Russia. Can you give an update on the Russian JV acquisition? What does the rejection of the transaction by Russian authorities mean? There are some more questions about Russia. Maybe I read all of them, and then the answers can be given by you and Gokce Bey, if that's okay.

A - Onur Alturk

Sure, go ahead.

A - Asli Kilic Demirel

Can you disclose what percentage of your Beer Group cash is held in Russia? And can you provide an update when you expect to repatriate dividends from Russia?

A - Onur Alturk

I think there are lots of Russia questions, as far as I understand. Actually, we are unable to provide any further details beyond what has already been disclosed on this matter. And the current structure of the deal, as you already know, did not receive necessary approvals. So what I can say is only now, if there are any new developments on this regard, they will be duly announced to public. I think there are more Russian questions, but in addition, what I can say is in the interim period, the business will continue to operate as usual under the management of Anadolu Efes. And the financial parts, I guess Gokce.

A - Gokce Yanasmayan

I think the question was about EBITDA and cash share of Russia. So in EBITDA, Russia's share is around 60% of Beer Group and slightly less than 20% in our consolidated financials. So this is about the EBITDA. And with the actual cash. We don't want to go into the details of this question, but currently we have around USD820 million cash in Beer Group as of June. And Russia's share is quite similar to last periods that we were giving examples.

A - Onur Alturk

Asli, I think there is question about Russia's performance and the reasons.

A - Onur Alturk

I will take this one. Russia is stated to be holding well dispatch sanctions with respect to consumer consumption. What are your remarks on demand, price challenges, competition, product and channel mix? I think this was a good one. Let's summarize the operation outlook in Russia. We have some reports and we have three actually sources of Russia's beer markets. So we are witnessing an upward trend in the industry and second quarter keeps on like this one. Of course, first quarter was again a solid growth. So the shipments data show increase around 9% market growth. Nielsen data also shows around 6%. The Rosstat data seems a little bit more, almost 10% year-to-date on year-on-year results. So when you look at the average of these three resources, it's around 8% market growth.

And actually we are outperforming the industry and we are gaining market share both in volume and value. And of course the source of the growth, as in the question is mainly supported by increase of consumption, internal consumption and of course the performance of the global and premium brands like Budweiser. Double-digit growth, Stella Artois again double-digit growth Hoegaarden and double-digit growth, Essa double-digit growth, Spaten as well. So also as asking the question that the drivers behind this market growth, beer market growth is mainly due to consumer shifts that we observe from wine, RTD ready to drinks and vodka to beer. And also indulgence categories growth due to unpredictable social environment effects and innovations. Of course, and our teams marketing investment, our rich portfolio in Russian business helps us a lot in this manner.

A - Asli Kilic Demirel

Thank you very much, Onur Bey. There is a question about William Grant & Sons collaboration. My question, it comes from Ertan Bey. My question regarding William Grant & Sons, any progress on operations and impacts on '24 financials? Thanks in advance.

A - Onur Alturk

Thanks for the good question. Actually, William Grant & Sons operation started in Turkiye almost three weeks ago. So we were dealing with supply in the first quarter. So it's too early to say anything to comment on this one. But for the three weeks we are distributing William Grant & Sons, as you may also know as Anadolu Efes Turkiye. We have an agreement between William Grant & Sons, this is one of the biggest scotch distillery around the world to distribute and to marketing their products. And we distributed mainly in the whiskey category. Glenfddich, Monkey Shoulder and Grants, in both key accounts and chains and of course in on trade and off trade channels and also one of the most premium gin brands Hendrick's also we started to distribute but not only these categories. Also we will distribute vodka and tequila as well.

So it's building on and the impacts on '24 financials that was asked. As far as I can see we are expecting low-single-digits in the revenue for this year of course, but we have to think about and this is just going to take six months. But in upcoming years we are seeing a huge potential since the category growth of whiskey and gin, organic growth in Turkiye's CAGR around 30% for the last five years. So we are expecting exponential growth in this category.

A - Asli Kilic Demirel

Thank you very much. Taking into account macro difficulties Turkish consumers are facing and what are your recent consumption trends in Turkiye? Do you see any shifts between alcoholic beverage choices? Can you enlighten us?

A - Onur Alturk

Well, thank you for the question. Actually our category in Turkiye is resilient. I think first quarter and second quarter top line growth, especially the volume growth and that I have to emphasize that volume growth is the most important thing in any financial environment. So we are betting on volume growth and of course effective pricing. But our category seems to be resilient in first half at least. And when we look at our third quarter, I think in our previous conference calls we mentioned that we were expecting a very good tourism support which we gained actually.

So tourism is helping us a lot. On the other hand, although we revised our expectations for the rest for the year to go, still, we are observing some early indicators of purchasing power problems of Turkish consumers, especially in the on trade channel. These are all indicators and after tourism season we can evaluate these indicators better. Yet again, the portfolio of Anadolu Efes seems to be adequate for all kinds of consumer demands. So actually what we observed about the shifts from other alcoholic beverage categories, wine seems to be suffering and also with high prices of absolute prices of spirits. Actually, until now it helped us to grow beer category. So again, I am optimistic for the rest of the year. But I am in a cautious sense. Of course, that's just because of the purchasing power that comes from our pocket money analysis.

Yet again, we are expecting to be solid in the upcoming months of the year.

A - Asli Kilic Demirel

Thank you very much, Onur Bey. Actually, there is one more question about Turkiye, but it's already partly answered, can you speak about expected pricing and profitability for Turkiye business in the second half of the year? Anything if you would like to add, it's more than welcome.

A - Onur Alturk

Well, as we are all familiar, we are increasing our prices in Turkiye at least 2 times a year because of the tax. When we look at Turkiye operation, as I stated before, our volume has exceeded expectations. It almost achieved 3% growth. When we look at the pricing that is asking the question. We started the year with 35% increase. As you can easily remember, in January and in July we have taken another almost 18%

increase following the second excise increase, of course. And recently we also implemented an intermediate increase targeting selected products in the premium segment.

It was around ranging from, let's say, let me give you an interval, it was 5% to 11%. So effective pricing, as I mentioned, is in our agenda and revenue management actions are in plan. And we are also evaluating because of the dynamics of macros and everything, we are getting price increases and our prices mix management in terms of channel and product every month. So but until now, 35% increase in January and 17.7%, almost 18% increase, two months ago.

So that's the Turkish markets. But again, I'm optimistic because of the hotel channel, because of the HoReCa channel, because of the tourism region performances. Yet again, on the other hand, we are carefully observing consumers confidence index purchasing power.

A - Asli Kilic Demirel

Thank you very much, Onur Bey. There are too many repeating questions, therefore, I'm not reading them.

A - Onur Alturk

Are there Russia questions asked? The repeating ones?

A - Asli Kilic Demirel

Yes, there are too many repeating in Russia questions which you already answered, therefore, I'm not reading them once again.

A - Onur Alturk

Maybe there are newcomers, but just let us repeat that again. Actually, now we are unable to provide any further details beyond what has already been disclosed until now, the current structure of the deal did not receive any necessary approvals. If there are any new developments in this regard, they will be duly announced to the public immediately. But for now, that's all I can say.

A - Asli Kilic Demirel

Thank you very much. There seems to be no more questions other than what we have already answered, but if there are any unanswered ones, you can directly reach us by email. So, I think we can end the call right now. Thank you.

A - Gokce Yanasmayan

Thank you.

A - Onur Alturk

Thank you very much.