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Sabancı Holding Q1 2021 Financial Results Conference Call & Webcast

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Speakers:
Barış Oran, CFO
Kerem Tezcan, IR Director

Moderator

Ladies and gentlemen, Welcome to Sabancı Holding 1Q 2021 Consolidated Financial Results Webcast. Thank you very much for standing by. There will be a Q&A session following the presentation, If you'd like to ask a question, please press star five on your telephone keypad and to participate in our written Q&A,just have your question into the ask a question text area and then click the submit button. Before we start the presentation, we would like to inform you that the information that will be shared today is based on the actual results and company judgements. Sabanci Holding does not accept any liability for the information or content discussed with that. I now hand you over to Mr Kerem Tezcan to the investor relations director of Sabanci Holding.

All yours. Mr Kerem

Mr. Kerem Tezcan:

Thank you. Hi everyone. Welcome to our Q1 Webcast.

We had a solid start to the year with our remarkably strong operational performance across the board owing to our resilient and non-cyclical business model despite the market volatility and challenging pandemic conditions. Q1 is yet another quarter when we continue to reap the benefits of having complementary businesses.

We successfully captured the recovering demand both in local and global markets, in which we operate, by even achieving a volume increase well above demand growth.
We sharply improved our operating cash flow via strong increase in EBITDA coupled with solid working capital management during accelerated revenue growth. In general, when growth accelerates, it temporarily increases working capital levels and reduce cash with all the efforts that has been prevented.

Q1 non-bank ROE reached 18.5%, surpassing record high level of 17.1% achieved in 2020.
We kept our balance sheet strong, as our debt to EBITDA improved further and reached 1.4 times with a strong liquidity of 10 bn TL.

Once again we had another upgrade from MSCI in our ESG rating. The two-notch increase driven by successful execution across the board in all aspects of the E, S and G in one of the widely used ESG ratings in less than a year is an early indication of our increasing focus on ESG in the coming years.

As COVID-19 pandemic continues to be a major part of our lives with ongoing lockdowns in our key markets, US, Europe and Turkey, we continue to keep our alert level at the highest degree to preserve the safety and well-being of our employees, their families and our customers. We are carefully following health and economic developments as our investments in digitalization so far enables us to rapidly adopt ourselves to changing conditions both on the ground and abroad.

Our Q1 performance is on track and we are keeping our medium-term guidance unchanged.

Let me share the overall conditions on the ground since March:

As it was the case in Q1, effects of pandemic continued to be marginal in our businesses amid nationwide lockdowns. We are still observing decent demand in the domestic and in the export markets and we are expecting even stronger momentum in the economy by increasing vaccine rollouts and favorable impact of seasonality in the next two quarters.

Local demand is robust and sustaining the momentum, it has gained in second half of last year. Demand in Asia Pacific is rock-solid; Europe & US has been accelerating through 2021.

Let me run you through the details of our Q1 financial performance.

Our combined topline, EBITDA and consolidated net income performances were solid on increasing demand, better sales mix and well managed financing.

Combined revenue growth remained strong at 20% as local and global demand was vibrant and continued to support all of our businesses but specifically, industrials and building materials.

We continue to benefit from our complementary businesses that played a vital role in balancing our financial performance in Q1. The relatively low rainfall in the first three months lowered our hydro generation yet this seasonal abnormality supported the cement demand as solid pace in construction prevailed in the underlying period.

EBITDA performance in the first quarter was strong on solid operational leverage and eliminated the impact of global inflationary pressures driven by demand recovery and ongoing challenges in the supply chain.

Coupled with strong operational performance, we continued to benefit from lower financial expenses in Q1 on favorable cost of funding, which resulted in a massive 48% year on year growth in consolidated net income.

Moving on to next slide,

Despite ongoing challenges related to pandemic, we continued to improve our earnings quality significantly as non-bank operational cash flow increased sharply by 1.6 times year on year with solid working capital management contributing positively.

This strong cash generation allowed us to maintain our solid debt profile. Our net debt to EBITDA improved further to 1.4x at the end of March.

Our total non-bank combined liquidity excluding financial services and tobacco business stands at 10 bn TL, while the total funds at insurance companies is 4 bn TL.

On the next slide, the solid upward trend in our non-bank returns accelerated even further in Q1 and non-bank ROE reached 18.5%, even surpassing our record high level achieved by the end of 2020.

Without an exception, all of our segment have positively contributed to the improvement in ROE. None of the business segments was holding us down.

We have ample liquidity at the Holdco on top of liquidity in our operating entities. FX position remains long.

Let's move on to combined revenue, EBITDA and consolidated net income drivers…
Excluding the bank, combined revenue grew by 22% y/y exceeding headline growth of 20%. Major contributors are industrials, retail and energy segments.

Non-bank comparable combined EBITDA growth was 34% y/y in Q1, exceeding headline EBITDA growth of 30% driven by almost all segments.

Industrials was the largest contributor to the combined non-bank EBITDA growth on increasing demand, better sales mix and higher capacity utilization.

Total comparable consolidated net income surged 48% in Q1, with strong operational performance and well-managed funding cost.

Non-bank comparable net income growth was even stronger at 68% driven by industrials, building materials and energy segments.

To deep dive into the segments, let's start with energy:

In Q1, energy segment performed well despite negative hydrology impact on Generation business.

Enerjisa Enerji recorded strong EBITDA performance with the contribution of both distribution and retail businesses.

The distribution segment's EBITDA increased by 12% y/y in Q1 mainly due to financial income growth together with efficiency and quality contributions. Double digit growth in Regulated Asset Base on a year over year basis, was sustained. The first quarters are seasonally low in terms of investments and the company has revised its supply contracts in that period. Accordingly, the capex that has realized in the first quarter is lower than the average planned CAPEX for the rest of the year, which is in-line with plans. Even though Q1 capex is relatively low, it has more than doubled on a year over year basis with the increase in Capex allowance in the fourth regulatory period. Capex is expected to reach allowed capex levels in 2021.

On the retail side of the business, higher liberalized & regulated gross profit & decline in doubtful provisions fueled EBITDA growth in Q1.

Net income increased by 53% year over year thanks to strong operating performance and declining funding cost compared to the same period last year.

Looking at generation's performance, electricity demand remained strong in Q1 by increasing 4.2% year over year as strong base impact kicked-in by March. In March, electricity demand increased by 12% year over year. And last year's low base was even more visible in April with electricity demand surged further by 27% year over year. We expect this strong momentum to prevail in May and June as well.

Enerjisa Generation's revenue was up 25% y/y driven by higher generated energy volume growth on increasing spark spread in natural gas plants, power-purchasing agreement in lignite plants and higher trading volume. Positive impact of FX-linked renewable sales price partially compensated the effect of low hydro generation.

Despite positive contribution of higher spark spreads and strong volume in natural gas plants, favorable lignite gross profitability and positive impact of weak TL on FX denominated feed in tariff in renewables, Generation's EBITDA dropped by 7% y/y due to negative impact of declining hydro generation on lower inflow in Q1.

Net income declined 15% due to EBITDA weakness and a tad higher financial expense.

It is worth mentioning that, Enerjisa Generation managed to reduce its net debt at the end of March despite its first dividend payment.

Industrial segment's topline grew by %36 thanks to higher volumes and better sales mix in both tire and tire reinforcement businesses despite ongoing sluggish demand in global aviation. Both industrial companies continued to outpace their respective markets in terms of volume growth in Q1.

The segment's EBITDA jumped by 84% year on year with a 6 percentage point improvement in EBITDA margin. Higher volumes, better sales mix and improvement in capacity utilization were the major drivers of EBITDA growth in tire enforcement business.

In tire business, strong EBITDA performance achieved by higher volumes mostly driven by faster pace in exports and effective cost management. Negative impact of higher raw material prices was reduced by future contracts.

In addition to strong operational performance pass-through, lower funding cost further supported segment's tripling bottom-line.

Moving on to the Building Materials, according to Turkish Cement Manufacturers' Association data domestic demand accelerated in the first two months and reached 36% y/y.

Segment's revenue growth jumped 57% compared to same period of last year on strong growth in domestic volumes and the positive contribution of weak TL on exports. Our share in Turkey's export market improved and reached 21.5% in Q1.

In addition to strong topline performance, better energy margin and favorable sales mix led to tripling EBITDA, bringing EBITDA margin improvement to more than 9pp year over year.

Segment's net income significantly improved in Q1 compared to the same period last year thanks to sharp margin expansion and lower funding cost.

On retail, despite slower traffic and closures of shopping malls where we have significant presence of both food super & hypermarkets and technology retail stores, segment's combined

revenues increased by 26% y/y driven by improvement in basket size in food retail and ongoing positive impact of new normal in electronics retail as home office and home schooling fostered discretionary buying.
The major change in customers' behavior towards on-line shopping due to pandemic related lockdowns triggered a significant growth in e-commerce sales. In Q1 e-commerce, sales of our retail companies more than doubled and share of e-commerce sales in their combined revenues increased by more than 3pp and exceeded 8%.
Solid top line growth and relatively limited impact from elevated operating expenses translated into impressive improvement in operating profitability as IFRS-adjusted EBITDA more than tripled compared to last year.
Bottom-line benefitted from effective financing management as both companies' enjoyed lower interest rates and the food retail company positively affected from the capital injection in November 2020.

Financial services segment had another impressive quarter with robust top-line growth, high technical profit and strong ROE.

Non-life premium production increased by 28% y/y driven by motor segment. In life business, 24% premium growth was driven by credit linked and stand-alone life protection.

In life business, technical income has increased by 73% y/y, driven by the growth in life protection volumes and Assets Under Management in the pension business. In the non-life business, sharp increase in motor and non-motor claims stemming from flood in Izmir and some big fire claims adversely affected technical profit, resulting in higher combined ratio of 108% compared to 98% a year ago.

Segment's bottom line improvement was led by life business on the back of strong growth in all major business lines and higher net financial income.

On banking, despite the challenging environment, along with rising funding costs as well as ongoing uncertainties regarding the pandemic, Akbank's positioning enable the bank to leverage its strength while carrying priorities for improving profitability.

Growth, proactive securities positioning, low maturity mismatch as well as robust across the board fee income growth were supportive factors for core operating performance.

Thanks to the proactive and prudent IFRS 9 implementation in previous periods, net cost of credit has been improving since it peaked quarterly in second quarter of last year.

The fortress balance sheet built with robust total capital of 18.5% without forbearances, strong foreign currency liquidity and low leverage of around 8x underline the inherent benefits of the bank's diversified business model and remains a significant source of strength.

I now would like to leave to floor to Barış for further comments and last closing remarks as a Group CFO.

Mr. Barış Oran:

Global business environment & demand is rapidly improving as global economy is rebooting post-Covid. Local economy is not yet in post-COVID phase, but we expect further improvement in Q2 & Q3.

Sabancı Group has maintained remarkably well performance throughout the pandemic. We have a record high non-bank ROE more than doubled in five years from 8.4% to 18.5% improving every year without exception.
Our leverage levels are record low. Literally less than half of what it used to be five years ago, from 3.7 times to 1.4 times net debt to EBITDA at the end of the first quarter.
As I conclude my term here, the group has seller results with record non-bank high ROE and lowest leverage ever with a rock solid balance sheet.

Operator, this concludes our presentation today and we can take questions.

Operator:

Thank you very much for that presentation gentlemen. Right, we will now start our question and answer session. First the audio questions and then the written questions after that if you'd like to ask an audio question, just press Star five on your telephone keypad and you can do that right now. If you want to participate in our written Q&A. Which is coming up later, you can type your question into the ask a question text area and then click the submit button and you can begin doing that now too. But first the audio questions Star five on your telephone keypad to participate and the floor is open. So just remind you ladies and gentlemen, if you would like to ask a question and audio question now is the time Star five and your telephone keypad and then the written Q&A. Which we might do now if there are no audio questions, all you do is just enter your question into the ask a question text area and then click submit. We'll leave a few moments for audio questions and then gentlemen, we probably will start the written questions after that. Yeah. All right gentlemen, it looks like we don't have any audio questions at this stage. So if we can move to the written questions, that would be wonderful. Thank you.

Mr.Kerem Tezcan:

Thank you operator. We have 2 written questions at the moment. The first question comes from Barış İnce from Garanti. Thank you for the presentation. 2 questions: given the recent rights issue in Teknosa is there any other underlying company that needs capital injection? The second question, does the holding consider an IPO or SPO of any assets in the near future?

Mr. Barış Oran:

Let me take that if I may. The right issue in Teknosa is going as planned, and we will continue to monitor the balance sheet of our companies to see if there are any further capital needs. As of today, there has not been any approval of further capital needs of our underlying companies. Having said that you have seen our balance sheet rock solid, we have record low leverage. And as far as the IPO or SPO are concerned, we have limited non listed companies as we have listed or increased the float of our companies during the last five years. As of today, we are looking into further opportunities to list our enterprises but we haven't come to the conclusion yet with our partners to take any further comments regarding this.

Mr.Kerem Tezcan:

Thank you Barış. We have another question from Raimondo Eggink, Congratulations for excellent financial results. I'd like to ask about the retail segments, why it is loss making and what are its prospects for the future?

Mr. Barış Oran:

If we compartmentalize retail into two buckets, food retail and technology retail. Technology retail has had record profitability last year and is profitable at the end of the first quarter. So we can take that aside. Our food retail company is very highly levered, much higher than its competitors and this leverage is creating the loss as of the first quarter. We are looking for operational improvements in food retail to compensate for the financial expenses and to go back into profitability. Furthermore, we are exploring potential asset sales in the real estate side to further strengthen the balance sheet of the food retail company.

Operator:

All right, gentlemen, do we have any more written questions?

Mr.Kerem Tezcan:

No written questions at this point.

Operator:

No. Good. All right. Should we wait a few minutes and just see if anyone wants to submit one and then we will come to you for the conclusion.

Mr.Kerem Tezcan:

Okay, let's wait for a couple minutes. Thank you.

Operator:

Just remind ladies and gentlemen, if you would like to ask a question, now is the time uh pop your question into the ask a question text area and then click the submit button. Thank you so much. All right, speakers, do we have any written questions at the stage? Any coming through to you?

Mr. Kerem Tezcan:

No, we don't have any written questions. We can conclude our presentation.

Operator:

All right, perfect. If you could conclude that would be great.

Mr. Barış Oran:

Thank you. I would like to thank all participants for their interest in Sabancı Holding. We will continue to deliver solid results through the rest of the year. You have seen our performance throughout the last five years, record high nonbank ROE and lowest debt to EBITDA levels reached in the first quarter of 2021. Thanks again. And you have a great day.

Operator:

Thank you, gentlemen, thank you, ladies and gentlemen. And this concludes today's webcast call. Thank you for your participation. You may disconnect now.