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Sabancı Holding
Q3 2023 Financial Results
Webcast

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Speakers:
Orhun Köstem, CFO
Kerem Tezcan, IR Director

Mr.Kerem Tezcan, IR Director: Hi, everyone. We opted to start today's webcast by remembering Atatürk, our great leader and the founder of Turkey on the 85th anniversary of his passing away. We will always remember him with respect. Thanks for joining Sabancı Holding's Q3 earnings webcast. Today, I have our Group CFO, Orhun Köstem with us. Please refer to our disclaimer before we move on with our presentation. Let me give the floor to our CFO, Orhun Bey...

Mr. Orhun Köstem, CFO: Thank you, Kerem. Good morning and good afternoon, everyone.

We're very happy to host you again in this time. Our third quarter, 2023, webcast. First of all, I will have to apologize for my voice, which is far from ideal. I hope to complete this without hurting your eardrums irreversibly. But thank you for your patience, and from now on.

Now, if we can start from page 8, again we're happy to report another quarter of strong profitable growth. If you look at our top-line numbers and we have seen a combined revenue growth of 63% in the first 9 months of 2023, a 43% EBIDTA growth and a 46% consolidated net income growth. And our return on equity has been at 38%. Now, just to put very little in these into perspective, which we're going to go into detail, obviously. In the following pages is that we're quite happy that we still continue generating very significant growth on top of the first 9 months of 2022, which I'm going to say, a little bit, which has been, as you all remember, was a very, very strong and quarter. So we're happy with our results. If you look at our balance sheet again, our net debt/EBIDTA is at

0.4x, and a consolidated long position of 232 million dollars across the group and at the holding only level we hold a cash of about 217 million dollars.

Now and if you look at the NAV growth which is a good problem to have. The NAV growth of our portfolio has increased by about 90% in dollar terms this year, which was great but obviously our discount has widened from the last time we spoke with you to about 41% at the end of the third quarter. But now I think we're back under 40%, anyway. So, this is something we will need to continue monitoring, of course. And I'm sure you will be monitoring as well. The value of our portfolio versus Sabancı Holding’s market capitalization, and our Capex to sales is at 10.3% which is pretty much in line with what we have been committing to invest, based on our capital allocation principles.

And last, but not least, I'm sure you might have followed. We have announced our interim targets for ESG, and we expect to reduce our greenhouse gas emissions by 42% by 2030. That's in line with our net zero target of 2050. And in the interim we expect a reduction of about 15% in our greenhouse gas emissions by 2025, and of course related to that we have committed to invest and to capital and operational spending by about 5 billion dollars for SGD related areas. So, our commitments remain. Our performance remains to be strong vis-à-vis our commitments in this quarter as well.

If you go to the next page of course just a bit on the background of this of this quarter. Now, as you see. If you look at the commodities and energy, this is as measured by Bloomberg. And obviously in the first 9 months you see certain reduction compared to the same period of last few, which was quite excessive, if you may remember that. And again, if you look at our group companies’ performances, this is reflected, for example, on our Building Materials company's performances. I think something to keep in mind.

The CPI on the 9 months is at 62% down from the same period of last year, pretty much in line with what it was at the end of the year, but still high. If you look at the basket movement of the FX, which was at 42% again, roughly, half of what it was last year, but nevertheless quite a big number to manage on top of last year, just to keep in mind. And all the while, of course, the minimum wage increase on a gross level has continued to come up quite significantly. I'm sure you must be hearing this, not from us, but from many of the other Turkish companies as well, which obviously influences the financial performance of businesses in Turkey.

Now, on the next page, just in a little bit of detail, our again Combined Revenues have grown by 63%, EBIDTA 43% and Consolidated Net Income by 46%. If you break this down, you see a strong top-line growth coming from the bank. Of course, as the interest rates continue to increase, that's something that we would expect to see. But in general, I think, for the banking sector, it's fair to say. And that the financial performances are normalizing over and above of last year's conditions. And again, we're quite happy that our performance so far at the end of the 9 months on the bank side meets or exceeds our expectations for the full year so far. If you look at the non-bank business on the other hand, of course, you see, we're quite happy that we have improved back to what we call quality growth. That is evidenced by revenues growing at 46%, EBIDTA at 56%, and net income by 66%. So, we're not only growing our top-line, but adding margins on our growth, and just to take your attention to the fact that on the nonbank side, of course, our performance, compared to the last time we spoke with you for our first half results has gotten better, and compared to the first quarter of 2023, it is much better. So, every quarter actually the performance of our non-bank businesses continue to improve, of course, which makes us quite happy.

This, in turn on the next page results in a good Return on Equity performance. As I said, if you look at the banking sector in general compared to last year, you see reductions everywhere but that's more of a normalization basically. If you look at the non-bank business, you see, we continue with our favourable trend of delivering improved ROE year on year so we moved from 28 to 29 compared to the 9 months of last year, so that our overall actually ROE continue to remain quite strong, and that's assisted by the fact that we have generated a very strong operating cash flow on the non-bank site about 29 billion TL. You know that not only compares quite favourably versus the same period of last year, but also compares favourably, and versus what we've done throughout 2022 as well. So that's a very strong performance. In each case, of course on the non-bank side it's important to underline the fact that our energy business, in addition to our building materials business have been strong contributors to this and very good performance.

If you come to the next page, you see our cash position. We talked about this. About 217 billion dollars, or about 5.9 billion TL. And then, as you remember, our guidance under our capital allocation principles is that we would like to manage across the group and at Net debt/EBIDTA of 2x or less. And we're at 0.4x, even though, as we discuss, we have stepped out our Capex. I think that's still owing to our very strong cash flow generation across our businesses in a relatively dynamic year, or challenging year like 2023.

If we move on to the quarter-by-quarter discussion. First looking from a revenue point of view, of course as we discuss the bank’s performance in the first quarter was a whopping 105% growth, which is great. And of course, the overall growth the combined revenue growth has come to about 70%. Nevertheless, we've seen at the quarter that our rate of growth of the non-bank business revenue have also grown, from 30% in the second quarter to about 48%. So, we continue growing quite strongly on top of last year's numbers.

if you get to EBIDTA, here we see bank’s contribution normalizing, whereas a non-bank business contribution increasing quite significantly, 74% EBIDTA growth in this quarter. And I'm sure you must have seen that on the energy side, even though the revenue performance was somewhat slow. It is improving in EBIDTA, I'm going to show you on the net level. Actually, it is improving even more. And there, you see, between building materials, industrials, financial services, all of our business segments digital have delivered very, very strong EBIDTA growth in this quarter compared to the same quarter of last year.

And finally on the net income side again. Here, especially, the bank's contribution, is large, but it grows 20% within the same quarter of last year. However, on the non-banking side, the growth is over 90%, which is again, as you may see, assisted by all of the business units. That's the industrial growth, however is somewhat slower compared to others. As you remember, we discuss in every quarter that's driven by the global demand and pricing conditions, especially impacting Kordsa’s business in general. For this, obviously, Kerem is going to walk you in detail by business segments in the following pages. But so far, again, I think we can still say we continue to benefit managing a well-diversified portfolio that delivers performance under. And you know, even though there may be volatile market conditions. Now, if you move forward as I said, the NAV of our portfolio has moved from just under 4 billion to 7.6, and which is again about a 90% growth in dollar terms, which is great. But as we discuss, as we reflected on to our discounts, the discount has widened on a quarter of quarter from 29 to 41, as we speak, I think we should be below 40, anyway, but I believe, and that leaves an opportunity.

Talking of which, if you move to the next page, I think it's again important to underline the fact that the pie chart on the left shows you our non-listed businesses valued on book basis, which suggests bank and financial services continue to be the largest contributor of our NAV. But if you look at the pie chart on the right-hand side which actually shows you the same with the independent valuation of the unlisted assets. There, you see, there is a more balanced portfolio. Even today, especially the energy and climate technologies piece growing. That's owing to the evaluation of Enerjisa Üretim in that sense and obviously going forward. I think the way to visualize this is the digital technologies, which is very, very little today. Obviously, that's a very new business unit that's started to grow. Between these four we would expect a more balanced portfolio delivering a more balanced value contribution. But again, you see, our portfolio has grown fast in terms of value this year, compared to last year, end of the same period, but still, I think there is more to reflect on to Sabancı's market cap. If you compare it to the PE multiples and compare it to our historical averages of about 6x basically.

So, with that, while I rest my voice, I will hand it over to Kerem to walk you through the details of the business units, Kerem…

Mr.Kerem Tezcan, IR Director: Thank you, Orhun Bey. Let me start from the banking business.

The bank ended the quarter with a new record high 20 billion net income, resulting in solid quarterly ROA of 5.0% and ROE of 45.5%. This leads to 9M net income to a robust 51 billion, up 35% yoy, with an ROA of 4.9% and ROE of 41.2%, which is well ahead of the Bank’s full year guidance.

Akbank added a solid 1.7 million net active customers year to date. This takes its active customer base to 12.5 million, up by c.50% in less than 2 years.

Strong momentum in customer acquisition along with record high market share gains across the board in consumer loans, broad-based TL deposit base, and TL demand deposits has continued to support core revenue generation.

Akbank's fee income, up by a remarkable 184% year on year. Thanks to this impressive performance, fee income market share among private banks also increased by an eye-catching c. 300bps ytd as of September.

Meanwhile, with the agility in balance sheet management, timely hedges and strong customer related business, the exquisite treasury management – which is one of the strong muscles of Akbank, continued to be supportive for net income evolution.

In addition to these, the bank keeps its leading position in capital with a robust 18.4% capital adequacy ratio, which will continue to provide the bank significant competitive advantage going forward.

Moving on to our energy business, as for the generation business, as a result of lower natural gas volume due to stoppages in natural gas plants from June to mid-September and lower spot prices compared to last year, revenues dropped by 41% compared to last year. Despite low natural gas profitability, EBITDA was up by 41% compared to last year with positive contribution from renewable and lignite assets thanks to higher wind regime and higher dark spreads. Moreover, the asset light contribution on higher trading activities of Enerjisa Commodities continued to remain strong and it was one of the major drivers of generation's EBITDA growth. Net income growth reached 72%, even higher than EBITDA performance, owing to the positive impact of the ongoing tax incentive.

We expect the contribution of natural gas to recover in the last quarter as all natural gas plants are now fully operational.

Enerjisa Energy's operational earnings increased by 53% year-over-year driven predominantly by strong growth from distribution as well as retail and customer solutions businesses.

Distribution business generated 48% growth year-over-year on higher financial income due to higher inflation and investments, as well as the IFRIC methodology change initiated by 1st of July 2022 aimed at more fair presentation of financial income.

Retail business performance was strong, with 41% earnings growth year-over-year, thanks to higher retail service revenues. These are mainly due to increasing doubtful receivables compensation impacted by earthquake and higher mid-year inflation.

The customer solutions segment was also solid, on the back of growth observed in the solar PV and e-mobility businesses.

Investments in distribution and customer solutions reached 9bn TL during the first nine months of the year, corresponding to 268% increase compared to last year and already by far outperforming the overall investments in 2022, which accounted for 4.6 bn TL. Free Cash Flow after interest and tax is driven by these profitable investments and the related interest costs, thus lower compared to last year.

On Building Materials, segment's top-line increased by 60% thanks to strong domestic demand and favorable sales mix.

In addition to a strong top-line, improvement in energy margins and positive contribution from alternative fuel usage led to solid operational profitability and improvement in margins. EBITDA surged almost three times and margin expansion reached roughly 10% points.

The segment's net income more than tripled compared to last year thanks to strong EBITDA performance and higher financial income on increased net cash position.

For the industrials, combined revenue grew by 64% year-over-year in Q3 despite the ongoing weakness in the global tire reinforcement market due to stiffer competition from China. Yet, the weakness in tire reinforcement business offset by higher domestic demand in the tire business driven by both original equipment and replacement markets and higher top-line contribution from composite business.

EBITDA performance in tire business was also strong in the quarter thanks to favorable pricing and sales mix. This resulted in a slight year-on-year improvement in the segment's EBITDA margin in 3Q thanks to effective pricing strategies.

Net income growth remained lower at 29% in the 3. quarter compared to last year due to elevated financial expenses on elevated debt and higher cost of financing.

Financial services segment had another quarter with robust performance as top-line more than doubled and EBITDA growth reached 78% year over year driven by both life and non-life businesses.

In the life business, despite higher general expenses on minimum wage hikes, EBITDA was up by 92% year-on-year thanks to the growth in pension assets under management, higher profitability in Return of premium products driven by TL depreciation and positive impact from credit-linked life premiums. Net income growth reached 53% year-on-year thanks to higher FX gains on weak TL and higher financial income.

In non-life business, despite the company's conservative approach in Motor Third Party Liability, top-line growth reached 120% compared to last year thanks to non-motor segment performance and last year's favorable base. Underwriting Results remained somewhat under pressure as high loss ratios in Motor Third Party Liability prevailed in the third quarter. Yet, higher trading income and weak TL contributed strongly to the EBITDA performance and resulted in tripling net income.

Our newly established digital segment's topline more than doubled with a higher contribution from the electronics retail business driven especially by online sales. In addition to strong growth momentum in online sale of value-added services also positively contributed to the segment's top-line growth. Our digital marketing and cyber security companies had a positive impact on segment's top-line growth as well.

Segment's EBITDA surged 141% compared to last year thanks to strong top-line growth and effective Opex management in electronics retail business despite higher fixed cost to sales ratio due to ongoing integration process in new digital marketing and cyber security companies and adverse impact of minimum wage hike.

Higher FX losses and higher financing costs somehow pressured segment's net income growth.

Finally for the retail segment, top-line increased by 90% thanks to strong like for like sales growth and growth in alternative channels. Despite the negative impact of the minimum wage increase, EBITDA has more than doubled thanks to positive sales mix on gross margin. Solid EBITDA pass-through resulted in a net income in this quarter compared to a loss last year in Q3.

So, this finalizes the details of the segments. I would now like to hand over to Orhun Bey for closing remarks.

Mr. Orhun Köstem, CFO: Thank you, Kerem.

First of all, I will not reiterate the midterm guidance that you see on page 26, that we believe the results that we've seen will assist us, meeting or exceeding our midterm guidance at this quarter. And if you look at the 9 month highlights again, just recap we are still looking at improved earnings quality especially driven by our non-bank businesses. Where the ROE has reached about 29%, about 100 basis point improvement over last year, the energy business contribution and the building materials business's contribution needs to be underlined. And again, with the energy segments and building material segments contribution, the cash flow generation has been very, very strong. That further non-bank net debt to EBIDTA is about 0.4x. Whereas the portfolio's value has grown by 90% in dollar terms compared to last year. Our discount has widened somewhat, which is coming back, but still attractive, maybe an opportunity. And the Capex, as we committed, has continued to improve. Towards also our SGD-related operational spendings and Capex, which we have committed to be 5 billion dollars in order to make sure that we meet our 2050 and our midterm targets, as we have announced as per SBTi.

With this, this concludes our formal presentation, and now we would be more than happy to answer any questions that you may have. Thank you.

Mr.Kerem Tezcan, IR Director: Do you think your holding-only net cash is sufficient to meet future potential equity needs of new economy operations ? How much in total did the parent inject into these businesses in 2022 and 2023 so far?

Mr. Orhun Köstem, CFO: Thank you very much. Obviously, what we hold as liquidity at our balance sheet is not the only source that we invest to grow our new economy initiatives. Last year, for example we invested close to 350 million dollars. And don't quote me. But the numbers should be around this. We had 16 or 17 different transactions across the group, basically. So, obviously going forward, the sources to further our ambitions would be we have not used that balance sheet. You know we've discussed it a number of times. So far this is only what we have undertaken and is the cash that we hold and the dividends that we receive. I think that's an important game changer going forward.

And I'm happy that the Turkish CDS have now come under 400 bps, for the time being. So that is a source going forward that we need to think about that. And of course, there could be other divestment opportunities in our portfolio, just like the Phillip Morris divestment we made at the end of 2021 or start of 2022. So, our spending should be much higher than what you see as cash of our balance sheet.

Mr.Kerem Tezcan, IR Director: Well, the next question. Thank you for the presentation. Can you please provide a brief update on outlook for Kordsa? This company is highly leveraged, and I wonder if there would be a need for capital in case global markets remain competitive. Additionally, I also wonder about your capital allocation for new businesses next year?

Mr. Orhun Köstem, CFO: Thank you. For the tire core manufacturing business. Obviously, this year we've seen a slow market demand driven by the economic turbulence, and that also, on top of that, we've seen significant pricing pressure from, Chinese producers. Now for the last quarter of the year, and I think, for practical purposes in 2024 as well. We don't expect a serious change in the market conditions. And that has been our expectation, for you know, at the start of 2023, anyway. Potentially I'm sure you must have seen how our friends at Kordsa must have given that guidance as well. Maybe towards the back end of 2024 in the second half of the year we may see some normalization that's driven by our historical observations of this industry, which has been quite cyclical in this term. So, this is nothing new that we experience, and you know, probably in a few years' time it may be again. But no, I mean Kordsa wouldn't need to have a capital increase. If you looked at the cash flow generation of the business and the EBIDTA generation of the business that was for us pretty much in line with our expectation.

Basically, our friends did a great job in not only reducing their working capital, but doing in such a way that they will continue benefiting that in the years to come. And so, therefore, I think the the Net debt/EBIDTA should be slightly over 3x. And we should see, you know, when the full year comes further improvement. And going forward we don't see any potential for capital, an increase in Kordsa.

Our capital allocation. I see another question, and let me continue, if I may, about our capital allocation for new businesses next year. It's, as you remember, is, and pretty much similar. What we do on average is we usually spend roughly a quarter of our Capex on our existing businesses, and just about 3 quarters to what we call this new economy businesses. I think our track records show 76%. When I say 3 quarters, you know, it's a touch higher, but they would less. That should be a rule of thumb to expect going forward as well.

Mr.Kerem Tezcan, IR Director: Thank you, Orhun Bey. And we have another follow up question. Can you remind us again the dividend policy of Enerjisa Uretim ? Was it similar to that of Enerjisa Enerji ?

Mr. Orhun Köstem, CFO: Thank you. Well, it is not. Because Enerjisa Enerji has a publicly stated dividend policy which is measured as a percent of their distributable income, of course. For Enerjisa Üretim, I think the company has been distributing about 70 million dollars of dividends to his shareholders, and then doubled it for the past 2 years. I'm sure you must have seen; we're also receiving interim dividends from Enerjisa Üretim. It is more of a fixed number that we set to receive, and, I'm happy to say, given the healthy the financial conditions of the company, and the good performance of the company, even though the company is undertaking a GW of capacity expansion of renewables. As you all know, we don't expect that revenue stream to change. Potentially it may improve, but it's early to say, that depends on our colleague's performance. Yeah, there could be upside potential. But so far, at least, we're happy that company has doubled the dividends that it has been distributing so far.

Mr.Kerem Tezcan, IR Director: Many thanks for the presentation. Should we expect the strength of the trading activity at Enerjisa Uretim to continue over the coming quarters?

Mr. Orhun Köstem, CFO: Thank you for the question. Could be. Look, I mean of course, needless to say, when the volatility is higher than the trading results become bigger. So, therefore, for example, last year, you see a much higher contribution where the energy prices, fluctuation was quite high, and going forward. Especially if you feel any, or if you project any higher volatility in the electricity prices. Yes, we should expect a much higher contribution. And I think the key one of the other potential elements is the capabilities that's been developed under the trading business is not only for trading of electricity or energy, but going forward, we expect to make sure we can start trading carbons, which obviously is going to become an important let's say item, especially across Europe. And that will be an incremental, hopefully and incremental contribution to the performance of our trading activities. Thank you.

Mr.Kerem Tezcan, IR Director: Thank you Orhun Bey. Just wait a couple of minutes if anyone has any further questions. So, if you have any question, please use the Q&A section of the Zoom. Thank you.

It seems we don't have any other questions. Thank you all for joining, hope to see you in the year end financial results. Orhun Bey...

Mr. Orhun Köstem, CFO: Yes, thank you Kerem. Thank you all for your patience and participation. Today we look forward to reporting another quarter of a strong performance hopefully, when we get together and sometime next year bye, for now.