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Sabancı Holding
Q1 2022 Financial Results
Webcast

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Speakers:
Orhun Köstem, CFO
Kerem Tezcan, IR Director

Mr. Kerem Tezcan, IR Director: Good morning, good afternoon everyone, welcome to our Q1' 22 results webcast, first I would like to draw your attention to our disclaimer. Our CFO, Orhun Köstem, will make the introduction today and I'll be reviewing our businesses. Orhun Bey, the floor is yours.

Mr. Orhun Köstem, CFO: Thank you Kerem. Good morning, good afternoon everyone and thank you for making yourself available today. The first quarter of 2022 that's behind us today is also a quite a dynamic day so again thanks for joining and taking the time. I'm happy to report that Sabancı Holding on combined basis has been able to deliver profitable growth in this highly volatile environment.

Obviously, what I'm going to touch base today is how we also proceed towards our strategic goals that we have communicated to yourselves and now starting from two years back. At the same time, reaching for the moments, the highest ever consolidated return on equity for the quarter and maintaining a very healthy balance sheet with ample liquidity that obviously gives us flexibility of maneuvering in this otherwise challenging times. We are also happy to report that our efforts and initiatives in sustainability continues to be recognized by independent bodies. Refinitiv as I'm sure you know, which also is in collaboration with Borsa Istanbul has rated Sabancı Holding , and we have been among the highest, if not the highest of 50+ global investment holding companies. In the quarter, the first quarter, in addition to our good financial results, we have produced the first green hydrogen in Enerji Üretim in our Bandırma power plant. Going forward, we want to continue capitalizing on this capability, so that we can, on one hand, replace our fuel usage for electricity generation by using hydrogen and at the same time, we will try to see how we can further commercialize and create a business potentially out of this.

On the Industrials, I'm sure you may have followed, Arvento was acquired by Brisa and Microtex was acquired by Kordsa which I'm going to touch base very briefly. As we have been telling a few times for most of you who we have been in communication with that we were planning to build a digital business. And the first inroads into that we have taken the steps as we have announced I'm going to briefly touch base on that as well and, finally, on the building materials, Çimsa initiated a Calcium Aluminate Cement capacity construction which is obviously important, because, as you know, Çimsa is one of the global white cement players, this even though is a niche sector is a high and value part of the business of which Çimsa hopefully is going to also participate in the global business of Calcium Aluminate Cement . With that I will move to next page, as I have discussed briefly I'm happy to say that we are continuing our path in terms of delivery on our strategic initiatives. I'm not going to repeat that what has happened until the year and as I'm sure you see on this page and our efforts also have accelerated since the start of the year, in the first quarter of 2022 including than April. We have closed the disposal of Philsa and PMSA shares, as you have followed. As i've touched base, we started producing green hydrogen in Turkey, acquisition of Arvento was completed by Brisa. On the bank side, the transfer of Turk Telekom shares on by LYY to Turkey Wealth Fund was completed. Microtex was acquired by Kordsa, as in the process of completion and the Calcium Aluminate Cement investment has been initiated by Çimsa and we have initiated our digital investments by the acquisition of Radiflow and SEM.

Next, obviously we don't only move towards our strategic goals, but we continue delivering very good financial results and first quarter of 2022 is no exception. I'm happy to report that we have been able to deliver ahead of the very high inflation levels and obviously raw material and supply chain related pricing increases in the quarter and on a combined basis, as you see our revenues have grown, more than doubled year on year. Our EBITDA growth was faster again on a combined basis year on year, close the double and then consolidated net income more than doubled on a year on year basis so that's a very healthy as far as we're concerned delivery of financial performance. Coming from both, our bank, as well as our non-bank businesses, obviously, you know Akbank has announced their results. Very strong set of results. Very good delivery against their RoE guidance, driven by a number of elements including customer acquisition, delivery on their core business revenues and good position in their portfolio on the back of this high inflation environment where the portfolio supports net income generation both for the Bank and for our non-bank business as well on a consolidated basis. On the non-bank side again, the performance is great. The growth is over 100% both in terms of revenue and EBITDA but as we move towards profitability on the non-bank side, of course, we need to consider that the raw material prices, fuel prices, energy prices, I'm sure you know, have been increasing so these results have been delivered on the backdrop of those increases. And, of course, on the fact that the average dollar devaluation was about 88% in the first quarter euro was 75% and the CPI hit over 60% so when we look at the results of course it's important for us to keep those dynamics in mind nevertheless we're quite happy with the net income performance of our group as a whole, driven by our healthy leverage and our favorable cash position. Our long position is just under $400 million which you're going to see at the back end of the presentation on the appendix as well.

So we had a great start to the year,a very strong start. Having said that, we maintain our mid term guidance for the period on the back of a number of volatilities and uncertainties about on the inflationary front, on the raw material front as well as energy prices.

Coming back, on the next page, you see our return on equity has hit its highest levels both on the banking and, obviously, on the non-bank side, so on the consolidated level Sabancı Holding return on equity was just under 25%. If you look our the holding only net cash position, it was 7.7 billion TL at the end of the first quarter and that's, of course, since the end of the year the completion of the PHILSA sale contributed to our cash position, as well as the dividend income. Since the end of March, our net cash still stands about 7 – 7.2 billion TL after the dividends we receive, the dividends we have been paid, and of course the ongoing share buyback program that we pursue. On the next page, you see our operational cash flow. You see the negative stream on our operational cash flow. The main driver as I'm sure you must have followed from our friends in Enerjisa is the cash flow performance of Enerjisa. Basically the distribution business of energy, so does quite well, which is the majority of the business about 85%. On the retail side, the cost of electricity versus tariffs still does not generate enough cash flow. And there is an impact coming from the VAT changes which is temporary, and will be normalized rest of the year. The cash flow impact should be normalized at one point in time although looking from today is difficult to say when. Having said that, again I'm sure you noted that Enerjisa increase their underlying net income guidance for the year and runs a very healthy balance sheet of 1.5 times, so we don't see as a major impediment for our performance in 2022.

Other than that, the cash flow performance over other non-bank businesses are slightly less than last year that's primarily driven by the fact that we're building inventory in most of our businesses with the expectation that the raw material prices, fuel prices are going to increase in the rest of the year so its more like an hedging for the next nine months for us to be able to protect our margins as well as our cash flow. And our balance sheet, you know allows us to do that, we still at 1.2 times net debt to EBITDA still be around a very healthy level of leverage. If we go to the quarter by quarter review again, if you look at the revenues on our non-bank business, the primary driver of the revenues is our, of course, energy, business and we're quite happy that we have a portfolio of generation, as well as distribution. Because we talked about the impact coming from the distribution, whereas our generation business have been performing exceptionally well, which makes us quite happy for the period and adds on to our financial performance. On the industrial side, obviously, as you will remember majority of the business are exports, and of course we have been able to generate a over 24% export growth year on year together with our industrial, as well as building materials businesses with ads on top of our revenue performance. Our retail business has done well in terms of revenue obviously part of that is once mobility comes back and we're getting back to relatively normal and the retail business benefits that both Teknosa's business as well as Carrefoursa's, but also lets keep in mind that, on the back of higher inflation, there is a certain accelerated shopping behavior at this point in time, so, although we still expect to see good results in line with our guidance our year on year growth rates may normalize the rest of the year, if this shopping behavior does not continue. If you look EBITDA again on the non-bank side, one of the important contributors, is our energy business. Regulated asset base growth contributes that greatly from the distribution business, as well as our generation business, which did quite well in terms of EBITDA generation. We would expect, hopefully, you know that's still early to say, but the first signs gives us hope that hydrology could be better than the past two years, which obviously helps us with better margins on our generation business and Kerem is going to you know walk you through the details of these. On the industrial side, of course, again, as you remember Kordsa benefits from the fact that it has a diversified footprint And does not get hampered by the supply chain disruptions globally and that continues to be an advantage for the Kordsa business and on the Brisa side under the industrials Brisa's raw material hedging strategy obviously adds positively on its profit performance. On the building material side you know the top line performance passes through the EBITDA line and, of course, the alternative fuel usage, we continue to increase year on year, which also helps us on the light of increased fuel prices, helps us in terms of managing our margins. One caution though I'm sure you must have seen as well in our elementary insurance, Aksigorta's insurance business, the profitability of Aksigorta both on EBITDA and net profit levels were not well that's the nature of the business. The premium generation does not, at this point in time, match its cost increase driven by the abrupt increases in the inflation levels and this high negative real interest rate environment. Nevertheless, we benefit having a diversified portfolio of businesses, which allows us to double our EBITDA compared to last year well ahead of the inflation as well as the valuation levels. Same is true for the consolidated net income again, you know the profit performance of energy contributes, as well as the industrials contributes positively on our bottomline, I've talked about our cash position, which also helps delivery to our bottom line, and therefore we have been able to grow our bottom line, you know more than two times in the period. Now, very little on what we have disclose to you before the Bayram break that we have been telling you about since last year that we intend to create a digital business going forward. One arm was cyber security and cyber security is an interesting, industry. It's one of the fastest growing business on the digital space in the past three years from 18 to 21, the CAGR growth of the industry was 9. With in, actually what we have been focusing on was the operational technology part basically. The operational technology security, OTS, which has been growing by 14%, faster than the overall cyber security segment and looking forward, unfortunately this operational technology security market is expected to grow even faster, just over 20% CAGR growth and I don't need to tell you the risks associated with cyber security and this operational technology security deals with power generation and distribution, oil and gas distribution utilities and transportation. We have acquired the business called Radiflow. Not a large deal size but the very good growth profile, a very good technology that we expect that would benefit most in this fast growing segment of the cyber security domain, already a global business generating revenue streams globally, operating in Europe and Middle East and APEC markets as well. So we don't have this technology, obviously we bought technology, and we will very much like to continue building on this position to grow. On the other hand, we also acquired SEM. When I say acquired, both of these are subject to completion after customary processes. SEM was a subsidiary of Ströer, globally acclaimed agency. It's specifically is digital marketing and it creates us to leverage the engine that we have generated internally in Sabancı Holding, for marketing intelligence basically with his experience and his customer base, data driven technologies to manage marketing services so both of these businesses, we expect to have great potential going forward. I want to also show you how we structured these businesses I'm sure you must have heard from us our digital arm SabancıDx , we have now accumulating these digital investments initiatives under our Holland based subsidiary our wholly owned subsidiary, Dx Technology Services and Investment BV, so Radiflow and SEM and the commercial businesses and services of SabancıDX will be under Holland subsidiary and, obviously, will create us a platform to enjoy synergies with Sabancı University to grow on the digital front and hopefully create a good business for us. and I will briefly touch base on the acquisitions on the industry side, one of them is Microtex, which was acquired by Kordsa. As you also remember, Kordsa has expanded to composites that was before the pandemic, a great move, not a great timing, unfortunately, what have been able to diversify his business both geographically and product wise. Acquisition of Microtex, which obviously is in Europe, and especially you know it's an important player as a supplier in the automotive in motorsports industry. It accelerates that diversification for Kordsa and will add on top of the existing composite business going forward. Brisa announced the acquisition of Arvento. It's a mobility solutions business fits exceptionally well with Brisa's existing business as Arvento is the leader telematics and IoT solutions company with a high market share in the sub segment. So we are quite happy with these two acquisition initiatives under industry as well. As I said, Microtex also is subject to closing procedures.

And finally, again I'm happy to report that we continue our initiatives in ESG performance. I'm not going to repeat our advances on the MSCI index or the CDP climate ratings which we continually look to increase, but we have been the only Turkish Holding company to be represented in the Bloomberg gender equality index, which was in 2022 and also, as I mentioned we had a very good result under Refinitiv's rating among the 50 plus the investment holdings category globally.

So we are quite happy with our first quarter performance on all fronts, I'm just now going to deliver over to Kerem to walk you through specifics of our segments.

Mr.Kerem Tezcan, IR Director : Let me start with energy. This time it's going to be a little bit long so bear with us. A lot of things happening in the energy sector.

So in Q1 Energy sector's EBITDA more than double thanks to positive contribution from both Enerjisa Enerji and Energy Generation. When we look at the generations' performance, it delivered exceptionally strong results in Q1 thanks to higher electricity prices, weak Turkish Lira, diversified portfolio, higher hydrology, and optimum capacity usage that led to major improvement in both spark and dark spreads.

Electricity demand growth reached approximately 5% y/y in Q1 driven mainly by lower-than-average temperatures despite negative impact of gas supply curtailment. Average spot electricity prices increased 5-fold in Q1 y/y mainly due to increasing commodity prices, gas supply limitation and change in maximum price formula to maintain supply security.

Enerjisa Generation's total generation volume declined by 14% y/y because of lower volume from natural gas plants, which is the optimum level of production to reach highest profitability level as far as spark spreads are concerned.

Despite lower generation volume, revenues increased by almost 4-fold y/y mainly driven by much higher spot electricity prices, higher energy trading volume as well as weaker Turkish Lira.

EBITDA more than tripled in Q1 y/y as natural gas and lignite profitability continued to drive higher spark and dark spreads in generation business driven by higher market prices. On renewables, hydro profitability started to show the signs of recovery as its contribution to EBITDA increased thanks to higher water inflow and weaker Turkish Lira compared to last year. Moreover, we have successfully captured market opportunities by benefitting from higher spot electricity prices and our team's ability on commodity trade. Higher dispatch contribution also supported EBITDA in Q1.

All in all, net income more than quadrupled in generation business compared to last year thanks to robust EBITDA contribution.

To go more in details in distribution and retail business;

In Enerjisa Enerji, distribution segment's EBITDA increased by 48% y/y in Q1 driven by higher financial income on higher short and mid-term inflation assumptions. Regulated asset base growth reached 61% y/y reflecting higher inflation despite lower capex spending due to seasonality.

Retail business EBITDA growth reached 98% y/y in Q1 fueled by increase in gross profit of regulated market segment thanks to higher electricity procurement prices and higher retail service revenues.

Despite the strong operating performance, net income declined by 60% y/y due to higher financial expenses due to higher financial debt and interest rates, and revaluation expenses of bond and customer deposits due to higher inflation. Excluding non-cash deposit revaluation, net income growth was 16%.

The decline in net income in Q1 is not a proxy for the full year due to quarter specific drivers. The peak in inflation took a toll on financing expenses in Q1, while the impact of inflation on costs will be lower in the subsequent quarters. Meanwhile, the positive impact of inflation on revenues will continue to be reflected throughout the year, notably for distribution segment even when the inflation starts to ease.

Like in many countries Turkish authorities also made some changes to the regulation in the energy sector. T

The regulator introduced maximum price limit application for power generators. A maximum settlement price has set for each electricity generation technology. For low-cost generators, the difference between the market price and the resource based maximum settlement price will be allocated to a special fund. This fund will be used to both ensure supply security and to support cash flow of retail companies. The impact of this newly introduced regulation is likely to have limited impact to our generation company but likely to have a positive impact on retail company. Therefore, net-net our businesses is likely to remain at balance even in the changing macro and/or regulatory conditions.

I just wanted stress one again that Q1 has marked as another quarter when we benefitted from having diversified businesses in our energy segment. While cash flow and net profit of Enerjisa Enerji weakened due to extraordinary market conditions, on the other end of the spectrum, Enerjisa Generation business benefitted from the same conditions by delivering an exceptionally strong performance and succeeded in partly offsetting the weakness.

Moving on to industrials segments combined revenue surged by 130% driven by strong demand, pricing flexibility and weaker TL. Our tire reinforcement business volume growth exceeded market thanks to its local agility combined with its strong global footprint.

Segments strong operational profit was driven by top line growth, raw material hedging strategy and channel diversity in tire business and better margins and higher volumes in tire enforcement business.

Segments net profits more than doubled thanks to the strong operational performance and drop in financial expenses.

Moving on to building materials revenue growth was impressive in Q1 reaching %179 year on year on sustained demand and better pricing flexibility. Please note that contribution of Çimsa Sabancı Cement BV segment revenues increased to a meaningful level this quarter, but even without Çimsa Sabancı Cement BV contribution, segments revenue growth still stands at more than hundred percent year on year in Q1.

This despite fuel mix optimization, better energy margin and better opex to sales ratio, escalated fuel, electricity, raw material and transportation costs limit this positive impact of strong topline performance that resulted in the lower EBITDA margin of 11% compared to 18% last year. Yet the EBITDA margin almost doubled compared Q4'21.

Segments bottom line declined 6% on higher financing expenses, driven by increased interest expenses and FX.

I just wanted to highlight finally, our efforts to improve fuel-mix prevails, as our new alternative fuel investment in our Afyon plant became operational in this quarter. As a result segments alternative fuel usage improved even further reached to 21% compared to 14% last year and this is well above Turkey's 8% average.

On retail, segment's combined revenues increased by 70% y/y thanks to strong contribution from electronics retail while food retail presented a top line growth in line with average inflation in Q1 2022. Like for like customer numbers in both businesses have shown double digit improvement.

E-commerce sales growth continued its strong pace with 48% yoy growth in Q1 2022 although e-commerce share in total revenues declined by 1 percentage point due to easing Covid-19 restrictions. As electronics retail company officially launched its own marketplace in February 2022 with the aim of much stronger presence in e-commerce market, the pace of online sales in electronics likely to increase its share in total revenues going forward.

Solid top line growth was able to cover elevated operating expenses and operating profitability has maintained in both businesses. Segment's IFRS-adjusted EBITDA increased by 75% y/y in Q1 2022 and margin improved by 0,1 pp thanks to increased share from more profitable electronics retail.

Despite higher financials expenses, segment's bottom line improved.

In life business, technical income increased by 49% y/y, led by the growth in life protection volumes and pension assets under management. On the other hand, in non-life business, underwriting result was adversely affected by the increase in mobility coupled with negative impact of 50% hike in minimum wage rate and the increase in FX driven claim costs in motor segment. As a result, combined ratio deteriorated to 156% in the quarter compared to 108% one year ago.

Despite higher financial income on increased interest and FX rates, deterioration in non-life business' underwriting result due higher claims resulted in lower profitability of the segment.

Finally on banking, despite the challenging environment, along with higher global inflation as well as the negative impact of ongoing pandemic, Akbank's positioning enables the bank to generate long-term stakeholder value.

Akbank's quarterly net income of above 8 billion TL is almost 4 times of first quarter last year. ROA came at an eye-catching 4% and around 39% ROE- well ahead of the guidance.

Robust TL loan growth, across the board fee income growth as well as strategic securities positioning were supportive factors for solid core operating performance.

The bank further built capital during quarter, reaching a robust figure of 17.7% excluding forbearances - which is the highest among peers.

It's net cost of credit evolution underlines proactive provisioning while improved collateral values and ongoing strong collection performance continue to contribute positively.

For 2022, Akbank's focus will continue to remain on healthy, profitable growth and customer acquisition, while sustainability remains at the heart of the strategy.

This finalize our details on segments. Now I would like to hand over our CFO for closing remarks.

Mr.Orhun Köstem, CFO: Thank you Kerem and again we're quite happy to have a very strong start to in otherwise challenging year. Some of our businesses, obviously, like our bank or our electricity distribution business is very well positioned in this you know high inflationary environment, whereas some of our other businesses are more susceptible. We are aware of the fact that the energy, raw material prices, fuel prices in general will continue to be challenging and will be driven by our ability to price, as well as manage costs and expense basis.Nevertheless, obviously we maintain our guidance for the year after this very strong start and we will be more than happy hopefully to share with you our good progress in the following quarters to come.

So with that we can go to Q&A.

Mr. Kerem Tezcan: Let me remind you that you can write your questions to the Q&A section or either chat section of zoom.

We have the first question.

Question: You mentioned that you are maintaining the guidance. Can you please share a guidance on holding level? on energy business, how should we think about your EBITDA margin consolidating this year?

Mr. Orhun Köstem, CFO : You will remember our mid-term guidance we were guiding for revenues growing 8% better than headline inflation. EBITDA doing 10% better than headline inflation, we were guiding for our net debt/EBITDA to be no more than two times. You will also remember we have discussed that we're going to step up capex in the next five years versus the last five years, which is obviously true, I mean if you take the first quarter and including April our capex to revenue has actually increased from 6% to round about 9% so we pretty much in line with what we have been guiding you and we were maintaining that we would like to increase the share of the FX revenues. And our midterm target is about 30%. Let me see and the other one is the you know, as we transforming our portfolio of investments in the new economy, we expect the share of the new economy to come to some 13% from a base of 6%, which is the average of 2017 to 2021 so that was actually our guidance. On the second question, if you look at the EBITDA performance of our energy businesses together, you know you take the generation as well as the distribution business segment wise and the growth in the first quarter was about just under 130% and, obviously, substantial part of the growth coming from the generation part, as I said although we will see in the second quarter more clearly on the generation side the hydrology could be different from last year. We would expect the energy prices to remain high, you know, given the energy deficit in Turkey, and on the distribution side, as I said, our regulated asset base model actually protects us in terms of EBITDA growth. We don't expect a negative let's say movement, in fact, we could see some margin opportunity, as I said, if the hydrology becomes better compared to the past two years.

Question: After having leveraged the balance sheet, what will be enerjisa generation strategy M&A, greenfield or dividend?

Mr.Orhun Köstem, CFO: On the generation side, it has become a very healthy business. Actually, probably a bit of everything that you have underlined because we would very much like to continue expanding our renewable portfolio and we would want to continue investing on our renewable portfolio. We already have as you will remember we've communicated a 565 megawatts of wind, over 65 megawatts has started to get commissions. We are looking to see if there are reasonable opportunities for acquisition, obviously, the companies in the best position to do that, from an M&A point of view.

And as the shareholders we're quite happy with the dividend streams coming from the generation business. The beauty of generation business it could do everything that you list it without necessarily hampering its balance sheet health. So staying within our midterm guidance for our leverage in group as a whole, generation business could do the green fields or acquire businesses as well as continue distributing healthy dividends.

Mr. Kerem Tezcan, IR Director: These are all questions I guess everything's pretty clear.

Now, I'll hand over to our CFO for closing remarks. Thank you.

Mr.Orhun Köstem, CFO: Thank you all for participating today, obviously, this is the presentation and the discussion and the questions for today.

We don't have to remind you any more questions, please you know follow up with us, we will be more than happy to answer them and we look forward to getting together at the end of the next quarter hopefully sharing a new set of good results with you. Bye for now and stay healthy, thank you.

Mr. Kerem Tezcan: Thank you