Arçelik A.Ş. Full Year 2022 Financial Results Conference Call

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ÇIMEN Ö: Good morning, good afternoon, ladies and gentlemen. First of all, sorry for the delay, we had some technical problem with the public disclosure platform that we have been using. 2022 was the year in which we experienced a lot of headwinds and challenges, so I would like to thank all of our employees for their tireless efforts and commitment to drive growth.

I would like to start with the highlights of the final quarter of 2022. Arçelik recognized TRY 39.2 billion revenue in the Fourth Quarter, posting 74% annual and 14% quarterly growth. On an organic basis, the revenue growth was 67% year-on-year and 11% quarter-on-quarter. In Turkey, both dealer purchases and consumer demand was positive, mainly thanks to pull forward demand. In Europe, consumer demand continued to be weak.

Consolidated EBITDA margin was 9.1% in the Fourth Quarter, delivering 42 basis points quarterly expansion, supported by eased material costs, price increases and further improved OPEX-to-sales ratio. Net Working Capital/ Sales ratio significantly decreased to 21.0% as of yearend compared to 26.3% as of September 2022, mainly thanks to lower inventories and also strong collection.

As a result of substantially improved Net Working Capital/ Sales ratio, we have generated 3.3 billion free cash flow in this quarter. Thus, the leverage as of December 2022 was decreased to 2.26 times, reflecting 0.42 times improvement compared to previous quarter.

On January 17, we have announced the transaction with Whirlpool, we have signed a contribution agreement with

Whirlpool to form a new standalone home appliance business in Europe and in addition to Europe business, we have also agreed to acquire Whirlpool's MENA subsidiaries, and I will explain the details in the coming slides.

Increase in global unit market share, which will be built on Arçelik current strong presence, extended brand portfolio that will serve European customers at various price segments, increased scale to drive operational efficiency and complementary product platforms that will expand product offerings were the main rationales behind the transaction.

European subsidiaries of both companies will be merged under a newly formed company, which is Beko Europe and the new business will be combined of 25 of Arçelik and 38 of Whirlpool's European subsidiaries and 2 of Arçelik and 14 of Whirlpool's production facilities and assets with a total of 24 million production capacity. Arçelik will have the control of Beko Europe, with major share and we will be able to fully consolidate the results.

The size of the combined business will be around €6 billion considering 2021 figures. As a separate transaction to the European business, we have also agreed to acquire Whirlpool's MENA subsidiaries that recorded €182 million revenue as of financial year '21.

And we believe this acquisition will accelerate our growth and strengthen our presence in the region along with our new investment in Egypt. Of course, the closing is subject to regulatory approvals and we expect the transaction to be closed in the Second Half of this year.

I will continue with Slide Four. Arçelik continue to deliver solid revenue growth in the final quarter of 2022. Our consolidated revenue increased by 74% on a yearly basis to 39.2 billion. This robust performance was backed by price increases, higher units sold in Turkey and Turkish lira depreciation. And organic growth revenue was 67%.

On a quarterly basis, we have delivered 14% revenue growth on the back of continued price increases and inorganic growth. On an organic basis, revenue growth was 11%. Our consolidated gross profit margin for the Fourth Quarter was up by 27 basis points on a yearly basis to 29% margin.

And of course, strong price increases on a yearly basis and lower material costs were main drivers of margin expansion. And despite the lower capacity utilization rates due to fall in demand and depreciated Euro/Dollar parity compared to average of the same period in last year.

On a quarterly basis, consolidated gross margin was similarly up by 24 basis points. Our consolidated EBITDA margin for the Fourth Quarter was increased by 42 basis points to 9.1% on a quarterly basis, which was supported by a lower OPEX sales ratio and mainly thanks to lower logistics and marketing expenses.

On a yearly basis, EBITDA margin was down by 21 basis points. If you look at the markets individually starting with Turkey;

Turkish MDA6 market grew by 12% in the last quarter and with this improvement, market ended with an annual contraction of 2% this year.

Arçelik sell-in units grew by 5% in Q4 on a yearly basis. So Arçelik ended the year with an annual contraction of 7%, slightly underperformed the market due to mainly the outperformance in last year. Likewise, sellouts were positive in both October and November, mainly thanks to pull forward of demand and campaigns that are implemented.

Arçelik being the lovemark of the Turkish consumers maintained its strong leadership position by far as of November 2022. Sales in AC market was up by 4% in this quarter on a yearly basis, bringing annual growth to 8%.

We outperformed the market with 10% growth on an annual basis in 2022. Mainly driven by Black Friday and World Cup in the last quarter, market grew significantly in October and November on an annual basis. TV sellouts were up by 2%, while Arçelik units were flattish compared to a year ago in the first 11 months of the year.

Domestic revenue in the Fourth Quarter was 12.5 billion Turkish lira, registering 112% yearly and 24% quarterly growth. The growth was mainly driven by price increases and increase in white goods unit sales. On an annual basis, Turkey revenues were up by 96% delivering the guidance.

The share of domestic market in total business was 30% in 2020, remained flattish compared to last year. In the European market, the share of European region in total revenue was 45%, which is flattish compared to a year ago.

In Western Europe, consumer demand continues to shrink further in October and November by 11% and 8%, respectively, reflecting the ongoing macroeconomic challenges in those markets.

And Great Britain market shrunk the most among all Western European countries with contraction at mid-teens percentage. Despite the contraction of units, market was flattish in value terms in the 11-month figures on a yearly basis due to price increases and higher share of premium segment sales.

However, this trend has been vanished in the months of October and November with almost 2% year-on-year contraction in value terms. Having 26% share in total revenue, Arçelik sales remained flattish in Euro terms.

In Eastern Europe, the markets were down at double digit percentage in Q4 on a yearly basis, which brings the annual contraction to almost 10%. However, in value terms, market grew significantly at mid-teens percentage in 2022 compared to 2021. Having 18% share in total revenue, Arçelik sales were up by 46% on a yearly basis in Euro terms, thanks to price increases and inorganic revenue contribution of our latest acquisition.

On an organic basis, annual revenue growth was 16% in the last quarter. And in total in Europe, lower units were offset by the pricing initiatives and we have been able to post 9% annual revenue growth in Euro terms in 2022. On an organic basis, annual revenue growth of European business was almost 5%.

If we continue with Africa and Middle East region, which accounts for 9% of our consolidated sales in 2022, we see a growth of 27% annually in Euro terms and this strong revenue growth was a result of balanced high performance of both regions.

Defy's domestic unit sales were significantly increased in the last quarter compared to the previous quarter, mainly thanks to the campaigns implemented for Black Friday. And on a yearly basis, units were contracted by a high single digit due to declining market demand and unit sales to the export markets were also contracted by mid to high single digit on a quarterly basis and grew at low-teens year-on-year.

Defy registered around 15% revenue growth in Euro terms in the last quarter which is mainly driven by unit growth and price increases. While posting around 13% growth on a yearly basis in Euro terms with the impact of price increases. As of December, Defy gained significant market share in unit terms and continued a strong leadership position in the market.

Revenue coming from Beko Egypt were up by 29% on a yearly basis in Euro terms, again with the impact of price increases. However, on a quarterly basis, the import regulation imposed by the government in Egypt is negatively impacting the sales and revenue fell by 26% in Euro terms.

Revenues from APAC region having 14% share in total revenue were down by 5% on a yearly basis in the Fourth Quarter in Euro terms. In Pakistan, lower AC sales and deteriorated purchasing power of consumers, the units were down on both quarterly and yearly basis. Accordingly, net sales were contracted by 9% on a quarterly basis in local currency and 11% in Euro terms.

On a yearly basis, driven mainly by price increases, net sales were up by almost 6% in local currency and with the depreciation of PKR against Euro, that resulted in almost 8% contraction in revenue in Euro terms.

Higher TV units and price increases in Bangladesh in the last quarter resulted in 4% annual revenue growth in local currency and in Euro terms, revenues were down by 3% on a yearly basis due to depreciating of Bangladesh currency against Euro.

I will continue with the cost side, focusing on the raw material prices. We have seen the downward trend in the raw material prices, which continued in the Fourth Quarter mainly as a result of eased energy prices and continued contraction in demand. Despite the significant fall of the prices compared to the pre-pandemic prices the costs are still very high.

Going forward, as being primary cost driver of raw material, supply/demand equilibrium and energy costs will play a critical role for the trend of the prices. I want to highlight that through strict, proactive and effective management in a timely manner, we have been able to have lower costs compared to market levels.

In Q4, and moving on to the next slide… a quick slide. In Q4, Turkey sales grew by 111.8% organically on a yearly basis. and international sales increased by 60.6% and out of this growth, 9.7% was organic, 41.9% was coming from the FX impact and 9.1% is coming from our latest acquisition.

On the right-hand side, you can see our regional sales breakdown. We have been benefiting from having enhanced operating geographies and always eyes for further expansion. Turkey's share in total revenue was 32% in the Fourth Quarter of 2022 while the share of Western Europe declined to 26% from 31% compared to a year ago. And Europe as a total, had 45% share in total revenue which remained flattish.

I will continue with the summary, financials. Consolidated net sales grew by 74% on a yearly basis in the Fourth Quarter, despite operating in a declining demand environment. However, we have seen higher white goods sales in Turkey and Turkish lira depreciation and our pricing initiatives were supporting that growth.

On an organic basis, the growth was 67%. And on a quarterly basis Arçelik's consolidated revenues were up by 14%, mainly attributable to price increases and inorganic growth. And on an organic basis, revenue growth was 11%. Our gross margin in the Fourth Quarter was up by 27 basis points on a yearly basis to almost 30%... close to 30%.

EBITDA margin expanded by 42 basis points to 9.1% on a quarterly basis. It is the impact of improved OPEX to sales ratio, where we lowered marketing and logistic costs. And on a yearly basis EBITDA margin was down slightly by 21 basis points. Annual EBITDA margin for 2022 was realized at 9%, which is close to our guidance.

We posted net income of 2.664 billion Turkish lira in the final quarter of 2022. Net margin was expanded by 283 basis points to 6.8%, however, this includes a one-off item where we have recorded an income of negative goodwill which is coming from our recent acquisitions with the amount of almost 1.4 billion Turkish lira.

When we exclude that one-off item, net profit margin was up by 56 basis points to 3.2%. In 2022, we realized 4.7 billion net income, which is reflecting 45% annual growth and 3.5% margin. And again, excluding that one-off item, net income growth was 10% and the margin was 2.4%.

When we look to our debt portfolio, our net debt decreased by 1.2 billion Turkish lira compared to Third Quarter, mainly thanks to the free cash flow that we have generated in this quarter.

Our cash in the balance sheet increased by 4.1 billion Turkish lira, again with the impact of free cash flow and also a collection of receivables. As of 2022 year-end, we have 24.5 billion Turkish lira equivalent cash in our balance sheet. It was well diversification between currencies, so you can see that 39% of our total cash is in dollar-denominated and 24… sorry, 20% in Euro and Turkish lira is 13%.

As a result, our leverage was down by 0.42 times compared to last quarter and as of 2022 year-end, we have 49.1 billion

Turkish lira equivalent debt. And 25% of our debt portfolio is in Turkish lira, while Euro and dollar share was 38% and 21%, respectively. The effective interest rate of Turkish lira was 21.6% as of year-end.

I continue with the next slide. On the upper left corner, you can see the break of our EBITDA margin. As I mentioned, lower OPEX-to-sales ratio and consolidated due to lower OPEX-to-sales ratio, consolidated EBITDA margin was expanded on a yearly basis.

On the lower left corner, you can see our CAPEX-to-sales ratio, which is almost 5.5%. And on the upper right corner, Net Working Capital/ Sales ratio, you can see quarterly. The ratio decreased to 21% as of end of Q4 from 26.3% as of end of Q3.

Finally, on the lower right corner. For the second consecutive quarter, we generated positive Free Cash Flow, this time with 3.3 billion Turkish lira, mainly which is attributable to improved EBITDA and Net Working Capital/Sales ratio improvement.

I will continue with the guidance. In 2022, we have delivered our Turkey, international and consolidated revenue guidance. We have registered 96% Turkey revenue growth, 18% international revenue growth, which is close to our guidance, and 96% consolidated revenue growth in total.

In terms of EBITDA margin, with the impact of higher material costs that we have experienced and Euro-Dollar parity, which impacted our profit margin. We have lowered our EBITDA guidance and we have delivered 9% EBITDA margin, which is slightly lower than our guidance.

Our Net Working Capital/Sales ratio was 21% as of year-end, which is well below our guidance, that is mainly due to a decreased level of inventories as well as the collection performance.

And in terms of capital expenditures, we closed the year with €220 million delivering our guidance. The variance is mainly coming from the shift in CAPEX to the next quarter.

Next year expectations… I mean 2023 expectations. We are expecting our Turkey revenue to be increased by around 45% year-on-year in Turkish lira terms, mainly driven by price increases and slightly increasing in units and also mix improvements.

We expect our international revenue to be increased by around 6% year-on-year in Euro terms which also includes our acquisition impact.

On a consolidated basis, we expect our revenues to be increased by around 45% in Turkish lira terms. In terms of EBITDA margin from today's point of view, we expect better margin in 2023. We are expecting material prices to go down further and a bit the mix improvement, as well as the strategic pricings we will be delivering a higher EBITDA compared to 9% this year. So, our expectation is 10% EBITDA for the 2023.

In terms of Net Working Capital/Sales, we aim to lower our Net Working Capital from the levels of 25% to 23%. So, we think we will be hitting between 23% and 25% in 2023. And our OPEX guidance is around €300 million, which is including our new factories in Bangladesh and Egypt.

So that was the final slide of my presentation. So, we can go to the questions right now.

Q&A

OPERATOR: The first question comes from the line of Demirtas Cemal with Ata Invest. Please go ahead.

DEMIRTAS C: Thank you for the presentation and congratulations for the results. My first question is about the one-off items, we see the impact of Russian operations. Could you further elaborate some details about the profitability of that operations because when we look at your numbers, we see around 169 million Turkish lira contribution to the net income after the acquisition.

And when we look at the impact before the acquisition, it's much more limited. So, could we assume some seasonality in the Russian operations? That's my first question.

And when you look at the net income effects, do we include the tax impact? Did you have any positive tax impact from that side – from the acquisition side or could we attribute better… lower than expected tax expense or let's say higher deferred tax income? Could we attribute that to some acquisitions or asset revaluations?

Çimen Ö: Thank you Cemal bey. That one-off item which has a positive impact in our P&L is mainly coming from the difference of the assets that we acquired and the amount that we will be paying for that acquisition in a deferred terms.

So what I mean is the agreement with that acquisition is, will be paid in deferred payments considering the performance of the company and the expected value to be paid is lower than the assets that we have acquired. So therefore, we have posted a 1.4 billion net income in the P&L.

And there is no tax advantage coming from that acquisition. The positive impact that we see in our P&L as the deferred tax asset is mainly coming from the Turkey operations, where we have higher amounts of incentives that we can utilize that is coming from the investments that we have made so far.

So since we are continuing on that investment, the amount that we are going to utilize is increasing, so that is creating further tax assets, which we have posted in last quarter as a positive tax income item.

DEMIRTAS C: Thank you. And Özkan bey, another follow-up about the trends. I didn't have a chance to look at all the details of financial expenses. But still, I see higher financial expenses compared to my estimate.

Could you give us a little bit color on the financing environment, especially in the working capital need side, how was the picture? Did you record any FX expense in that front? How was the financing environment for you? That's my question.

And the third question is about the outlook. In your growth guidance, could you share any inflation or the TL depreciation assumption? It just coincides with my numbers, but I want to understand if you can give any detail on that side to better understand the picture in the guidance assumptions? And related to that, how do you see so far the First Quarter? Thank you. It has been four questions, sorry for that.

Çimen Ö: Okay. Let me start with the financing part. As you will recall, in the last quarter, our inventory levels have gone up mainly due to the decline in the demand. So, we had higher working capital needs as of last quarter and we have mentioned that we will be focusing on our net working capital to lower that amount, so which we have successfully managed and lowered our inventory levels, as well as decreased our receivables. So that created a 3.3 billion positive impact in this quarter.

And the environment that we see, as you all follow that interest rates have gone up and still continues to increase; mainly most of the countries are targeting to lower inflation rates. So therefore, the central banks act to increase the rates.

And given that we have Turkish lira borrowing in our balance sheet. We are the rate that we have for the renewed Turkish lira loans is higher compared to last year. So, our average Turkish lira loan is around 22% levels, each time we have further additional loan, the rate is increasing.

And on the FX side, we have seen the increased impact in our financials. That additional FX loans is expensive compared to the ones that we carry in our balance sheet. But all-in-all, our net debt position is around €1.3 billion levels that didn't change much in a negative way. But the interest rate is increasing.

And we have posted FX loss in our financials, around 550 million Turkish lira levels in this quarter. And this is mainly coming from the FX position in our balance sheet, net FX position. So, we are hedging our position. So that comes with the cost and that cost is around 25% if you want to hedge your FX position, that means we are also having a negative impact in our P&L to hedge our position.

For the outlook next year. When we look at the markets, we see the inflationary impacts and energy prices have gone up. Nowadays, we see some decline in energy prices. However, that impacts the behavior of the customers and the customers, especially in the Europe region and all the other international regions might be less reluctant to spend on our appliances.

And so that brings some… to have some conservative approach to the market that what we have considered as a growth in unit terms is slightly improvement compared to last year. But mainly our increases of 6% growth in international market is coming from price increases.

In Q1… actually, we haven't seen the results yet for January, however, as a general comment, I can say that for the next year, we are not expecting a unit-wise strong growth even in Turkey and all the international markets.

And all the growth was mainly come from a mix impact, price increases as long as we can do in those markets and also the switch to high-end products also built in the channel. I think, I assume I answered all your questions, but if anything is missing, so I can comment as well.

DEMIRTAS C: Thank you. Its fine, thank you.

OPERATOR: The next question comes from the line of Fedorov Egor with ING Bank. Please go ahead.

FEDOROV E: Hi, thank you for picking up my question. Well, I have three questions. First is regarding your debt activities and the refinancing of maturing used netted loan. How would you prefer to refinance it to extend maybe to come to the market or to use other opportunities? This would be my first question.

And second, I think you partly answered, but just maybe you may also elaborate it a little bit. How do you see demand in Western and in Eastern Europe and in Turkey in terms of number of unit sales volumes? Are you going to sell more or less, well in the international market in Turkey, well like in not well in terms of the revenues but in terms of the number of units?

And third question would be about your guidance. These figures, are they even including the impact of M&A with the group or not?

ÇIMEN Ö: Thank you. We are working on our options of refinancing the Euro bond, which is due by April, so the options on the table are we can have bank loans. We can go for issuance of Euro bonds.

And we can also have a syndication loan, which we will decide in the coming months.

And you asked the demands in Eastern Europe and Western Europe. As I mentioned, we do not expect a major significant unit growth in those markets because of the decline that we have experienced in the last quarter of this year, which we think will continue, but not at that level. So that's why… our growth is mainly coming from the price increases and mix improvements that we are planning.

And similarly in Turkey, in Q1 we expect demand to be high. But due to uncertainties in Turkey that we might face, we do not expect a major unit growth and all the growth that will be mainly coming from price changes and as well as the mix improvements.

In our guidance, since the Whirlpool transaction is just announced and we are in the interim period where we are waiting for this transaction to be closed, so there is no assumption in our financials which is reflecting any revenue associated with the acquisition.

FEDOROV E: Okay. Thank you very much for answers and its fair enough. Thank you.

ÇIMEN Ö: Thank you.

OPERATOR: The next question comes from the line of Kilickiran Hanzade with JPMorgan. Please go ahead.

KILICKIRAN H: Hello, thanks very much for the presentation and I have two questions. The first one is related to acceleration in the receivables collection. What actions have you taken to achieve this reduction in the receivable base? And how sustainable is this? How long will you continue on the actions that you have taken to keep the working capital low?

And second one is, I think this could be pretty obvious, but considering that you are not looking for a major volume pickup being conservative overall in the guidance. How should we think about your profitability on a quarterly basis, I mean, profitability trend? So, you are looking still for year-on-year improvement in the First Half or more in the Second Half? Thanks very much.

ÇIMEN Ö: Thank you. Actually, we have focused on our Turkey operations more closely where we can improve our collection cycle. So, we have some incentives to the dealers which they prefer to pay in advance rather than waiting to due dates. So those incentives and closely monitoring of our receivables help to improve our cash flow.

And also, in the other markets we have looked for the options of factoring of receivables, which actually accelerated our collections in a positive way. And what I can say those costs were compared to financing more favorable. Therefore, we have chosen to use that option.

And how sustainable it is? I think we… it is more realistic to expect a level of 23% rather than 21% which we have experienced in the last quarter. So that I can say, we will continue to lower our net working capital sales ratio, if you consider average of all quarters and 23% or between 23% and 25% is the realistic Net Working Capital levels.

KILICKIRAN H: Thank you very much. Would you please, also comment about the profitability trend on a quarterly basis? Thank you.

ÇIMEN Ö: Yes. Our profit levels is actually depending on how fast will the… raw materials will decrease… continue to decrease and as well as the quantities because of the transformation costs that too is impacting our EBITDA margin.

But in terms of our projection, we haven't… we do not see a distinguishing between factors, between quarters. So, we can say that in average all the quarters will be around 20%... sorry, 10% level.

KILICKIRAN H: Okay. Thanks very much.

OPERATOR: We have a follow-up question from the line of Demirtas Cemal with Ata Invest. Please go ahead.

DEMIRTAS C: Özkan bey, a follow-up question about the effective tax side. Do you recorded some deferred tax income in the Fourth Quarter. Could we expect that to continue in the First Half of the year? And what was the reason behind that was attributed to any asset revaluation? That's my question.

ÇIMEN Ö: Yes. Cemal bey, this was mainly coming from Turkey operations, that positive impact. And the reason of the increase… sorry, the positive impact is mainly attributable to the investments that we are making and the incentives that are associated with all investments. So, the investment levels increased and the amount that we can utilize, credit tax assets in this quarter.

And in the coming year, we do not expect a major increase in the deferred tax asset coming from Turkey operations. But of course, the effective tax rate will change depending on the contribution of each market. But I can say that we are not expecting deferred tax income for the next year.

DEMIRTAS C: And again, related to Russia operations, the acquisition side. Do we see any seasonality in that side? When we look at the numbers, we see that Second Half is stronger, but what could be the contribution in the First Half in a dilutive or supportive in terms of the growth side and the margin. I don't know if you can give any color on that.

ÇIMEN Ö: So, to clarify your question, so the acquisition was recently done. So, I think you're comparing this year last quarter with 2021?

DEMIRTAS C: What I am doing is, when I look at our number for Russia and the regional operations, the contribution since your acquisition is around 1.7 billion. And when we look at the Full Year effect from your footnotes, I see that 2.8 billion for the Full Year, if you start consolidation from the beginning of the year.

So when I look at the number, the portion in the Second Half or the revenue from that operations in the Second Half looks… or after August looks much higher, so that's why I asked this question?

ÇIMEN Ö: Yes, there is some seasonality impact coming from the business, you're right. We have been able to increase our proposition in the markets since many players are not that active compared to previous period. So, the impact is coming from that portion for further growth, meaning.

DEMIRTAS C: And one last question about the IFRS29 side in Turkey, not many companies are implementing that. But I would like to ask your position about this? We know that Turkish regulation, tax regulations didn't apply but they gave a chance to asset revaluation.

But overall, I would like to see… understand your view if… did you have any studies on that as you're a major global company now? I would like to understand your perspective on that IFRS29 for the following years? For this year, can you make any comment to understand the impact of inflation on your operations, just a view?

ÇIMEN Ö: We haven't done… we haven't finished the analysis yet, so we are still in the process of calculating the overall impact, which will come from our two entities in Turkey, which are subject to inflation adjustments.

But I can say that we will not be negatively impacted, but the magnitude we are still working on. And there's no requirement to reflect it to the financial or the TFRS. So, we will do that internal study. And once required, we will publish those figures.

DEMIRTAS C: Thank you, thank you Özkan bey.

OPERATOR: At this moment, there are no further audio questions. We will now move to our written questions. And the first question is from Bozkurt Uğur with Deniz Invest and I quote: Thank you for your presentation. Can we assume EBITDA margin 1Q2023 better than 4Q2022 and 2Q2023, better than 1Q2023?

ÇIMEN Ö: Thank you for the question. We definitely can expect Q1 to be better than Q4 this year. As I said, all the other quarters will be pretty much in the same level of around 10%. We expect value to increase, but as a percentage to be within the same range.

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

ÇIMEN Ö: Ladies and gentlemen, thank you for your participation in our Q4 earnings call. So, we will meet you in the next earnings call.