TAT Gıda Sanayi A.Ş.

TAT Gıda Sanayi A.Ş First Quarter 2023

Financial Results Conference Call

Friday, 28th April 2023 (14:00 TR Time)

***Conductors*:**

Ms. Başak Tekin Özden, Chief Financial Officer

Ms. Banu Çamlıtepe, Investor Relations

Conference Call Conducted by Chorus Call Hellas

CHORUS CALL HELLAS

PROVIDER OF TELECONFERENCING SERVICES

TEL: +30 210 94 27 300

FAX: + 30 210 94 27 330

Web: www.choruscall.com

OPERATOR: Ladies and Gentlemen, thank you for standing by. I am Konstantinos, your Chorus Call operator.

Welcome and thank you for joining the TAT Gıda Sanayi A.Ş. conference call and live webcast, to present and discuss the First Quarter 2023 Financial Results.

At this time, I would like to turn the conference over to Ms. Başak Tekin Özden, CFO & Ms. Banu Çamlıtepe, Investor Relations.

Ms. Camlitepe, you may now proceed.

ÇAMLITEPE B: Thank you very much. Good afternoon, everyone. Thank you for joining our conference call today. I am here with our CFO, Ms. Başak Özden, today. And as usual, we'll take parts in presentation. I will start and then hand over to Ms. Başak Özden, and we will present you Tat Gida's First Quarter Results. Then we'll have time for your questions at the end.

So now if we can move to page 4, just a summary of what we have realized in this first quarter. We have completed first quarter, and overall, we had a similar operational performance like we had in third quarter and fourth quarter since our last harvesting season. First quarter, our net sales doubled to TRY1.1 billion. This time, our domestic sales drive growth registering 178% annual growth. This was led by both higher volume and prices in domestic market.

On the other hand, our exports, which had been on a growing trend in the last couple of years, registered annual growth of 29% this quarter. This is mainly as a result of relatively stable FX rates in second half 2022 versus high inflationary environment. This had a negative impact on our competitiveness in foreign markets and lowered the growth of our export sales.

Production volumes increased by 36% to 12,000 tons. We have seen increases in condiments and ready-to-eat segments. As a reminder, we have seasonality in production, and we produce the highest amount in third quarter. Therefore, other quarters are relatively low in terms of production volume.

As we had mentioned in third quarter 2022, higher harvesting season costs had pressured on our margins. Our COGS increased by 135% in this quarter yearly, and our gross margin came in at similar levels attained in the last two quarters. We concentrated on cost savings in the operating expenses level, and our EBITDA increased by 94% to TRY164 million, higher than TRY138 million attained in fourth quarter of last year. And our EBITDA margin was 14.6% versus 13.5% in fourth quarter and 15.8% in first quarter of 2022.

Higher season costs and higher amount of tomato purchased in 2022 season also led to an increase in our financial debt as of third quarter of last year. And as a result of high financial debt and elevated interest rate, our financial expenses increased this quarter. Net financial expense was TRY128 million in this first quarter, which was TRY11 million in 2022 first quarter. Our net profit came in at TRY98 million, almost the same levels attained in the same term last year; as a result of higher financial expenses as I mentioned. And we continue our investments in innovation, quality, infrastructure, and maintenance, and this quarter our investments totaled TRY30 million, which was TRY8 million around last year in the same term.

On page 5, this doesn't relate to our first quarter results, but just wanted to give you the initial expectation for the new harvesting season globally. In 2022, as you may recall, we have seen 3% decline in overall global tomato processing amount, while Turkey registered 7% growth. Based on current preliminary expectations for 2023 harvesting season, a 12.5% growth is expected globally, while Turkey's initial expectation is at 2.6 million tons, which represents 11% growth year-on-year.

However, we should note that the preliminary figures in 2022 was also higher than the realized figures. For example, last year California's initial expectation was around 11 million tons, but actually results came in at 9.5 million tons. Similar to that, again, Spain's figures last year, the preliminary figures in January was around 2.5 million tons but came in at 2.1 million tons. This may not reflect the actual figures.

On page 6, you can see Turkey's monthly tomato paste exports provided by Turkish Statistical Institute. As we have mentioned in the first page, our exports were lower this quarter compared to the same term last year. This is actually the same picture of the sector. The figures attained in January and February of 2023 is much lower than the figures attained last year, also lower than the figures attained two years ago, 2021 figures. This is showing that Turkish exporters is affected by the fixed rates and higher inflation.

On page 7, you can see breakdown of our production in terms of different categories. Production volumes increased, as I mentioned, by 36% to 12,000 tons. We have seen increase in sauces and ready-to-eat segments. As a reminder, as you can see also here on this graph, the breakdown of total quarterly production figures. Due to seasonality in production, we produced the highest amount in the third quarter, and therefore other quarters are relatively low in terms of volume wise.

And on page 8, These are some market figures for Turkey, excluding the hard discounters. And almost in all categories, we maintain our leading position, and this also continued in first quarter of this year. In tomato products, we had 51% share. We ranked number one. In ketchup and ready-to-eat segments, again, we remain number one. And in ketchup, 25% share. And in ready-to-eat segments, around 26% share. And in tomato paste, we ranked number one with 35%. In pickles, again, we are number one with 20% share.

And as we move to more details about our financials, I will now hand over to Ms. Başak Özden.

ÖZDEN B: Hello, all. Thank you again for joining our call. I'll start with the revenues. Our net sales was TRY1.1 billion in the first quarter, and this was up by 109% year-on-year. On top of a strong first quarter 2022 figures, the total sales volume in the first quarter of 2023 decreased year-on-year to 36K tons due to mainly lower exports. And I will go into the details more in the next page. Domestic sales increased by 178% year-on-year, owing to higher volume and prices. And exports was up by 29% in TL terms. We have mentioned that it has been tough since the second quarter of last year for exporters, as FX rates have been stable versus high inflationary environment. Therefore, our exports upward trend has been slowed down in the first quarter, leading to 29% growth.

When we look at the details, our exports totaled TRY319 million, and this was $17 million, displaying 4% growth in dollar terms. Again, despite soaring input prices, the Turkish lira stability, as you already know, is hurting the exporters' competitiveness, and this is the same scenario picture for us as well. And this is why the exports share in total sales was 28% in the first quarter, whereas it was 37% in the last quarter of 2022, and 46% in the first quarter of 2022. And as you can also see, our trend coincides with the Turkish tomato paste exports trends as well when we look at the first quarter. Of course we are also looking for other ways to grow our exports, which means managing the mix more effectively, securing new clients, and adding new export destinations while strengthening our share in the existing ones.

When we look at the COGS side, we had a surge in costs in the last harvesting season, as you well remember, especially in raw material purchases and energy costs. With this new season costs, our cost of goods sold increased by 135% year-on-year in Q1 and reached TRY832 million. As you can see on the below graph, agricultural input price index increased by 70% year-on-year and by 115% compared to 12 months moving averages in February. The highest annual increase was 83% in seeds and planting stocks and 78% in fertilizer and soil improvers subgroups. Agricultural input price index reached its peak in second and third quarters last year during our harvesting tomato season, impacting negatively our farmer scores. And now we continue to see price increases but at a lower speed.

On page 13, we would like to show you our gross margin trends. Our gross profit in the first quarter increased by 60% versus the same term last year. We have been trying to minimize the impact of high costs with effective sales mix and price management together with productivity improvements and cost-saving initiatives. We see mainly a decrease in export margins as market conditions do not support Turkey's competitiveness in exports markets and the prices. And our gross margin came in at 26% in the first quarter, almost the same level attained in the third quarter and fourth quarter of last year, that is since starting the new season. And this is lower than the first quarter last year, which was 34%, basically because of the new harvesting season costs and the impact of stable FX rates.

Operating expenses was up by 30% year-on-year, and our opex-to-net-sales ratio was 12% in the first quarter versus 14% in the fourth quarter of last year, and 19% in the first quarter of 2022. And our operating profit was up by 92% year-on-year to TRY156 million, thanks to our cost-saving initiatives. And our EBITDA stands at TRY164 million in the first quarter, displaying a year-on-year increase of 94%, while the EBITDA margin was 15% in the first quarter versus 13.5% in the last quarter of 2022, and 16% in the first quarter of 2022.

Moving to page 15, this is a summary of our net-debt position. Our net financial debt increased in the second half of 2022 due to high season costs. It was TRY2.2 billion at the year end, and now it's almost at the same level. As our exports were lower than our expectation, both in terms of volumes and also because of the FX rate stability, this had a negative impact on our working capital needs. And with higher net financial debt and interest rates, of course, this led to an increase in our net financial expenses. Meanwhile, we tried to diversify our funding sources and extend our credit terms. We have issued bonds and also obtained an EBRD loan before and as of March end 2023. Only 6% of our financial debt is in FX, which is the EBRD loan, and the rest is in Turkish liras.

Just to remind you that our investments reached TRY30 million in this quarter, which was TRY8 million in the same quarter last year. And as a result, our net profit came in at TRY98 million in this quarter, which is almost at the same level attained last year, same period. As you can see in the graph below, this is mainly led by higher financial expenses. Our net profit margin is 8.7%, higher than the figures attained in the third quarter and fourth quarter of 2022, which was around 6.6%, but this is lower than the first quarter of 2022. I would also like to mention that we had a tax income of TRY3.6 million in the first quarter. Our effective tax rate is now 10%. The effect of earthquake tax was TRY22 million, but we also had a deferred tax income of TRY64 million due to revaluation of our assets due to higher inflation environment.

Going forward, our margin recovery will depend on the economic and market conditions, of course, and the new season costs. We still have solid top line growth owing to domestic sales performance, while financial expenses limited our bottom-line growth. The last harvest, the harvesting season's elevated costs had pressure on margins and inflation indices now continue to grow, but at a lower pace versus last year.

To summarize again, and domestic sales performance supported top line growth in the first quarter and we anticipate exports to gear up in the coming quarters. We curbed expenses in the first quarter, but we will continue marketing investments in domestic and foreign markets in order to expand growth and product range. Actually, we recently launched an ad campaign for our condiments with new labels in the local market, and we will continue our communication plan accordingly in the domestic and international markets. And finally, the net-debt; we expect the net-debt to come down to manageable levels by the end of the first half, as it is traditionally the case with our seasonality, and also with the growing sales and cash inflow in the coming quarters will have a positive impact on debt levels.

Well, that's all for my presentation, and I will be glad to answer your questions. Thank you.

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

DEMIRTAS C: Thank you for the presentation and congratulations for good results. My first question is about the growth side. I see 18% contraction in total volume, and your exports are down maybe more. What was the contraction in the domestic side? And you mentioned that the cost factors were the reason behind lower exports. Could you make further elaboration about that; what was the reason that cost base was high; in which markets you are competing against, or in which countries are you feeling the pressure? That's my question about the market side.

And regarding the working capital management, as prices increase, we see increase in your net-debt in fourth quarter and first quarter, and it's related to inventory. And you mentioned that these are the rising prices and maybe rising volumes. How will this go forward in the second and third quarter? How do you see the outlook? Do you think you're going to be able to reflect the prices to your products? Because there's the inventory there, there's the financing cost, but the food prices are increasing and maybe you can give us more color about the second and third quarter direction of the profitability. Because in this quarter, despite the cost pressures, I think in such a highly competitive sector, your margins look good at the gross and the opex levels. So I would like to understand how these things develop and what could be the catalyst ahead.

Again, related to that, how did you manage to cut operating costs, your opex-to-net-sales is around 12%, so it's a good number compared to previous quarters. You mentioned that there will be some higher market expenses, but still, what was the driver and what's the sustainable opex level for you? Thank you.

ÖZDEN B: Okay, thank you for your comments and questions. I will try to address all of them. Firstly, volume growth. Actually in the domestic market, we didn't experience a contraction. So both the volumes and the prices are up in the domestic market. Where we see contraction in terms of volume is in exports. And this picture is actually similar with what has been experienced in Turkey. As you have already asked, this is because of the higher seasonal harvesting costs, and the fact that the FX rates have been stable. Turkey lost some competitiveness with respect to other tomato countries, which are Europe, Italy, Spain, Portuguese, also California, as you know, and China, of course.

So in the last harvesting season, the two main drivers, was first the extraordinary rise in our raw material costs due to the inflation in the agricultural sector, and the fact that the

FX rates have been stable. This is where Turkey has lost some competitiveness in the export market, as it is the case also in other industries as well. So this also had, again, as you said, a negative impact on our working capital, because we want to accelerate our exports more than we have now seen, and we expect the coming quarters to be better in this respect.

Of course, going forward, the new season prices, and the macroeconomic environment will determine Turkey's competitiveness. So it's hard to give a very accurate picture now. But because of the fact that although inflation is continuing, but not at the higher rates we had seen last year, and also because we expect more tomato production this season, we can expect that the raw material prices will be more favorable in the new season. And Turkey's competitiveness will, of course, depend on the FX rates, which is hard to say right now for me. But we also see that in other countries, producers are negotiating with the farmers for the new season contracts, and we see that international prices are going up as well in euro terms.

So it will also have a positive impact on Turkey's competitiveness, and of course, our competitiveness. So because of these two drivers, let me say, we expect a more normalized season in 2023 and in the quarters coming up. I hope I addressed all your questions.

DEMIRTAS C: Yes, you did, but about the domestic side, I would like to understand, because last year export and domestic sales volume were almost similar, but this year it's more than 2x exports, domestic versus exports. I'd like to understand the volume growth in the domestic side. Could we assume its double digits? What was the driver behind it? The price increases might be the main reason, but I would like to understand the volume side in the domestic, because that's also a question mark now. Because I assume domestic margins are higher compared to exports. I'd like to understand whether domestic prices were the main reason behind sustaining that level. So I would like to understand the sustainable EBITDA margin for you, maybe for this year. Thank you.

ÖZDEN B: First of all, the volume growth in domestic markets was not only from tomato categories, but also from sauces and ready-to-eat food and vegetables segments. So we can say that the category mix was favorable as well. In terms of margins, the margins in the domestic market are more stable for us, I mean, also compared to last year's first quarter and the last quarters of 2022. So we can say that it has been stable. But, in the market there is an increasing trend for private-label products, and there's a price sensitivity in the market. And this has a positive impact on private-label products or specific campaigns like packages for Ramazan, for example, mixed packages for Ramazan.

So we see that the customer is more price sensitive, and we follow with the trends, of course, and also private-label sales. Therefore, special campaign sales were higher this quarter. But it didn't have a significant negative impact on the margins in the domestic market. So the margins were stable, we can say.

On the export side, last year because of the FX rates and our competitiveness in general, the export margins were higher. That's where we see a decline. Since the export markets are more competitive, we have to adjust our prices accordingly, plus we don't feel the positive impact of the FX rates as we did last year, same period.

DEMIRTAS C: Thank you.

OPERATOR: Ladies and gentlemen, there are no further audio questions at this time. We will now proceed with the written questions from our webcast participants. I will now pass the floor over to management. Thank you.

ÖZDEN B: I see that there's a question regarding the net financial debt over EBITDA. Are you planning to decrease the net financial debt over EBITDA during 2023?

We expect this ratio to decrease in line with our seasonality trends, which is where we see the lowest net financial debt by the end of the first half, just before the new harvesting season starts. So we will see that the ratio will continue to decline. Of course, again, this will be a result of the growing sales and cash flow from our additional sales in the coming quarters.

Of course, in the new season our net financial debt goes up. This year it will be more dependent on the new harvesting season's costs, actually. So we don't expect such higher, extraordinary growth like we did last season. We have shown on the inflation graph, although the prices are still going up, they have been lower than the peak points we had seen last year.

But of course, again, it depends on the new season's dynamics. If Turkey's output, as we have put here, is expected to be 2.6 million, and if the inflation trend stays the same, we can have a more favorable impact in the new harvesting season and going forward.

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

ÖZDEN B: Thank you for joining our call. Of course, you can always reach us by phone or by email. We will be at your disposal for any questions you may have. Thank you.

ÇAMLITEPE B: Thank you very much.