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Presentation

Operator

Ladies and gentlemen welcome to Coca-Cola's First Quarter 2023 Financial Results conference call. I will now hand over to your host, Mrs. Çiçek Özgüneş, Investor Relations, and Treasury Director. Please, ma'am, go ahead.

Çiçek Özgüneş

Thank you. Good morning and good afternoon, ladies and gentlemen. Welcome to our first quarter 2023 results webcast. I'm here with Burak Başarır, our Chief Executive Officer, and Andriy Avramenko, our Chief Financial Officer.

Following Mr. Başarır, and Mr. Avramenko's presentation, we will turn the call over for your questions.

Before we begin, please kindly be advised of our cautionary statement. The conference call may contain forward-looking management comments including projections. These should be considered in conjunction with the cautionary language contained in our earnings release. A copy of our earnings release and financials are available on our website at www.cci.com.tr.

Now, let me turn the call over to Mr. Burak Başarır. Sir.

Burak Başarır

Thanks, Çiçek.

Good morning and good afternoon, everyone.

It's a pleasure to be speaking with you today. Thank you for joining CCI's webcast. Andriy and I will take you through our first-quarter operating highlights, keep prepared remarks brief and then turn straight to your questions.

As you'd remember, we announced our 2023 guidance early in the year, which included certain assumptions and accounted for many risks. However, a lot has changed since then. Türkiye was hit by one of the country's most catastrophic earthquakes in early February that displaced over 5 million people. The macroeconomic situation in Pakistan got more challenging, with the government taking additional fiscal measures, including tax increases, to comply with the IMF program, which is still being negotiated. Access to hard currency remains limited in the country, and inflation hit 50 year high while currency devalued by 25% in the first quarter.

As CCI, rather than using our energy 100% on the existing challenges, with an agile mindset and decades of experience managing volatility, we are well-equipped to respond and adapt our business quickly to the new operating conditions and pursue opportunities. That is what we did in the first quarter, and we modified our plans to sustain our profitable growth under the current environment. Benefiting from the geographic diversification of our business, we are confident that we can deliver in line with our earlier expectations and, therefore, reaffirm our full-year guidance.

We are pleased with our performance for the first quarter, delivering in line with our business plan, given all the additional headwinds we had to face.

Consolidated sales volume grew by 6% year on year. Solid growth in Central Asia and Pakistan offset the softer volumes in Türkiye and the Middle East.

We are happy to see energy drinks gaining scale, a category where we still need to be more indexed and see a lot of growth potential. Despite cycling a very high base, Monster Energy continued its positive momentum with more than 80% growth.

The share of IC in the total mix was 24%, around 1.8% lower than last year. High growth in international operations, where the share of IC is lower in the package mix, resulted in a negative geographical mix impact for the consolidated IC share.

We delivered 80% organic revenue growth in the first quarter, primarily driven by pricing actions across markets and revenue growth management initiatives.

As a result of our focus and discipline to grow our business sustainably, we have achieved organic EBIT growth of 76% and limited the EBIT margin contraction to less than 30 bps despite increased sales and marketing expenses and higher operating costs in the inflationary environment.

Net income grew by 64%, reaching 1 billion Turkish Lira in our smallest quarter.

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We keep increasing our investments in digital capabilities. With our integrated digital supply chain planning platform, we continuously improve forecast accuracy, decrease out-of-stock and increase efficiencies throughout our operations. In this respect, we decreased out-of-stock by 300 bps vs. last year on a consolidated basis. Forecasting accuracy was improved by around 15%.

In Türkiye, online sales through CCI Next, our digital B2B platform, increased by 20% from the previous year.

Building on the growth in comparable EPS last year and our solid liquidity position, our general assembly approved the board's dividend distribution proposal. We will pay 2.90 TL per share from May 22nd.

Finally, On April 26th, we completed the acquisition of Etap Icecek and now own 80% of this juice concentrate business, which will open new possibilities for growing our business to create incremental value.

Next slide, please.

Our core sparkling category grew by 10%, increasing to 82% in the total mix from 80% a year ago.

Stills grew by 6%, having a flat share in the mix.

In line with our value-based strategy, we continue to focus on smaller profitable packs, resulting in water volume to decline by 15%.

The brand Coca-Cola grew by 14% in 1Q23, mainly on the strong double-digit growth recorded in Pakistan, Kazakhstan, and Uzbekistan.

The double-digit performance of iced tea and energy drinks led the growth in the stills category. Monster Energy grew by more than 80%, while the total energy category grew by more than 40% year on year.

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Cycling a solid base and impacted by the devastating earthquake, the sales volume of the Türkiye operation declined by 8% in the first quarter.

Following some stocking at year-end ahead of price increases, January was flattish, as expected. February, however, was severely impacted by the devastating February 6th earthquake.

The earthquake region accounts for roughly 10% of our Türkiye volume, while the highest impacted 3 cities account for 2%. The initial impact was quite severe; the week of the earthquake and the following week, sales volume in the three cities was down almost 100% and nearly 70% in the rest of the 8 cities. Naturally, the disaster impacted the whole country's consumption pattern. We saw a double-digit decline in the rest of the country in these two weeks. In the following weeks, the operating environment started to recover gradually, and we achieved modest growth in March.

The sparkling and still categories declined by 9% in the first quarter. Within stills, energy drinks were the sound volume driver.

The water category was down by 5% despite the strong growth of more profitable IC packs in line with our value generation focus.

Strength at the on-premise channel, which recorded its highest first-quarter performance, created a tailwind. As a result, the share of IC packages in 1Q23 was realized at 35%, up by more than 300 bps year on year.

In the first quarter, we continued to navigate historically high levels of inflation that affected consumers' real disposable income. Nevertheless, we maintained our pricing discipline. As a result of our timely price adjustments, effective discount management, and favorable mix, NSR per uc grew by 109% year on year.

Lower volumes, higher energy prices, and a weaker Turkish Lira created additional headwinds in Türkiye. With the low-cost base of the first quarter of the last year, the EBITDA margin was impacted negatively. We expect to see normalization in the second half of the year due to base effects.

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International operations' volume grew 15% with a solid performance in Pakistan and Central Asia, thanks to increased penetration and strong execution.

The core sparkling category grew by 18% despite cycling a strong base. The Coca-Cola brand led this growth.

The stills category grew 31%, despite cycling 27.0% growth. Energy drink volumes increased threefold.

Having a low base and cycling 31% growth a year ago, the water category contracted by 30% in the first quarter.

Assisted by the solid volume momentum, pricing adjustments in line with inflation, and improving channel mix, NSR grew by 73% year on year.

Price increases, scale efficiencies, and disciplined cost controls resulted in 163 bps EBITDA margin expansion in international operations.

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Our top three international markets all recorded double-digit growth in the first quarter.

Pakistan grew 14% despite a high base, ongoing macroeconomic challenges, and increasing consumer price inflation. The growth comes from new outlet additions, continued distributor warehouse capacity expansion, and regional marketing focus. Coca-Cola grew 24% in Pakistan, the main driver of the sparkling category growth. Coke Studio, a successful initiative by the Coca-Cola Company featuring studio-recorded music performances by established and emerging artists, continued to be highly acclaimed, with the latest season streamed over a billion times. Cycling more than 60% growth a year ago, the stills category expanded further by 2%. The water category declined by 55.0%, while cycling had a 25% growth.

The year started with severe weather conditions in Uzbekistan, and this also caused energy shortages and even production delays for a certain period. Despite this, Uzbekistan continued its healthy growth trend, recording 21% volume growth in the first quarter. This performance was supported by improved distributor structure, focus on execution excellence, and continuing cooler investments to make our brands available, visible and cold. Sparkling grew 18%, while Iced Tea drove the growth of the still by doubling in volumes.

Kazakhstan was the highest-growing country in the first quarter, registering 26% growth, despite cycling 16% a year ago. The demand in the at-home channel was resilient, while the on-premise channel recorded a double-digit performance. Sparkling and stills categories grew strongly, recording 36% and 24%, respectively.

Now I will leave the floor to Andriy for the financial review.

Andriy Avramenko

Thank you Burak.

While navigating a challenging 2023, we concluded the first quarter with sound results in line with our business plan at the consolidated level.

Net sales revenue increased by 80% in the first quarter. Excluding the favorable currency conversion impact, FX neutral net sales revenue increase was also strong at 61%. This was primarily driven by solid volume performance of international operations, pricing actions across markets, proactive revenue growth management initiatives, improving channel mix and higher IC mix in Türkiye.

In the first quarter, we cycled a very low-cost base in Türkiye, thanks to successful sugar pre-buys and hedging initiatives executed last year. Since then, sugar prices more than tripled. Therefore, as we guided before, the first half of the year is more challenging compared to the second half, due to this base effect. Moreover, the soft volume performance following the devastating earthquake created additional headwinds. Therefore, we saw contraction in the gross profit margin of Türkiye. This was more than offset by the higher gross profitability of international operations, which was due to strong volumes, successful hedging, disciplined cost controls, and price adjustments early in the year. On a consolidated basis, our gross margin expanded by 35 bps.

Opex as a percentage of net sales revenue increased by 62 bps, due to weaker operating environment in Türkiye and increasing sales and marketing expenses across the markets. Although overhead savings partly mitigated the impact. As a result, we generated an operating income of 2.3 billion Turkish Lira with an EBIT margin of 15.1%.

We had higher interest expenses incurred mainly from Turkish Lira borrowings. Accordingly, net financial expenses were higher compared to the last year. Despite that, our net income grew by 64% to 1 billion Turkish Lira in this small quarter.

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We closely watch the per unit metrics as a key driver of real value generation.

In the first quarter of 2023, consolidated net sales revenue per unit case increased by 51% on an FX-neutral basis.

Despite being off peak levels, cost inflation continued to be high in our key markets. In this environment we managed to contain COGS per UC increase to 52% with volume momentum in international markets having positive mix effect and marginally improving the economy of scale in these markets. Successful hedging and pre-buying of packaging materials such as aluminum and resin also made positive contribution to managing COGS per UC in the quarter.

Currency neutral EBIT per unit case growth realized at 38% thanks to disciplined opex management despite higher selling and marketing expenses in the first quarter.

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In the first quarter, operating profit followed a healthy trend and was up by 76% compared to the same quarter last year.

The main contribution to EBIT growth came from disciplined and timely pricing across all markets. The robust volume growth of key international markets helped to offset the softer volume performance in Türkiye and supported EBIT generation as well. Although IC mix was favorable in Türkiye, the Future Consumption packages' higher share in international markets neutralized the favorable package mix effect on a consolidated level.

The higher commodity cost pressures fueled mostly by sugar prices in Türkiye and base effect of key raw materials' costs since we were cycling extremely low base of 1Q 2022 created a drag on the margins. However, we managed to navigate these challenges with strong operational performance, timely pricing initiatives and better channel mix.

We also benefited from a favorable currency conversion. As a result, we reported TL 2.3 billion EBIT in 1Q23 with 15.1% margin.

Onto the next slide, please.

As a result of our tight financial policy, our balance sheet health is intact despite the challenging operating conditions.

We have only 423 million dollars of net debt, which is 0.7x of our EBITDA. Our balance sheet is fit to support our growth agenda. Even considering the planned cash outflows related to the acquisition of Anadolu Etap and Pakistan minority buy-out, we expect net leverage to stay below 1.0 times with positive free cash flow generation throughout the year.

Our short FX position before Net Investment Hedge is 400 million dollars, which is only 0.6x of our 12-month rolling international EBITDA. We feel comfortable as long as that short position stays around 1x. The benchmark to international EBITDA is relevant since international operations are constant dividend payers to our Türkiye legal entity that carries the majority of the debt.

If we also take into account the net investment hedges, our short FX position is only 51 million dollars. Therefore, our P&L is quite resilient to the impact of TL devaluations through FX gains and losses.

Thanks to the proactive debt management, the average maturity of our debt was 3.4 years and close to 45% of our current debt is scheduled to be paid between 2026 and 2029. This creates an additional comfort zone to manage debt and liquidity in the globally tight liquidity conditions.

Prudent financial management, protection of healthy balance sheet and strong liquidity position will continue to be our priorities going forward.

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Finally, a brief overview on our commodity hedging initiatives for the current year and 2024. In the context of persistent cost inflation, we mitigate this pressure by dynamic RGM actions and also proactive, timely built physical and financial hedges including pre-buys and long-term procurement contracts.

On the sugar, we cycled an extremely low base in Türkiye operation in the first quarter. Its price more than tripled in the last 12 months in Türkiye. Although we don't expect an uptrend in prices as severe as the last year, we mostly completed our sugar procurement for 2023, for our better visibility and planning purposes. On a consolidated basis, we have almost 90% price visibility for 2023.

In markets where the sugar can be hedged, namely Iraq and Jordan, we also covered 75% for 2024 calendar year.

On the aluminum, 2023 hedges give us 100% visibility and we started looking beyond 2023 to lock-in from favorable pricing levels for 2024. The aluminum hedging level for 2024 is around 15% at the moment.

On the resin, our 2023 hedge coverage is around 65%. We are comfortable with this level for the moment, as resin is closely related to oil prices globally, and we don't expect a major change there. We are also hedged around 10% for 2024 resin exposure.

In total, the relatively flattish pricing trends of packaging materials in USD terms year on year help to cycle low base of sugar cost and to mitigate margin pressures to some extent in Türkiye as well.

Now back to Burak for his closing remarks.

Burak Başarır

Thank you, Andriy. CCI is an emerging and frontier market bottler, and we operate in a volatile geography with tremendous growth potential. While we are keen on delivering successful results today and navigating challenges carefully, we are also focused on achieving our vision to be the best FMCG company across our markets.

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To achieve our vision and serve our purpose of creating value for all our stakeholders by delivering sustainable long-term growth, we leverage our main growth pillars:

- We always put our customers at the center of everything we do. Execution capability is our proven strength. We continuously invest in our commercial capabilities to support our customers and expand our digital reach.

- On the people side, we are the proud and well-recognized employer in 11 diverse countries in our region. Our values of passion, integrity, teamwork, and accountability are shared throughout the organization. We continuously try to improve ourselves to become an even better inclusive, diverse, and inspiring workplace.

- Our diverse brand portfolio includes some of the world's best-known brands. We offer our consumers a wide range of products for every lifestyle and occasion.

- Sustainability is a fundamental and indispensable aspect of our business, and it is embedded in our vision and goals. We integrate sustainability principles into all our operations and activities and are committed to achieving our 2030 Sustainability Targets, which we announced last year.

- Our balance sheet is quite flexible, with sufficient liquidity. We remain focused on driving profitable revenue growth and free cash flow generation while investing ahead of the curve to prepare to capture tomorrow's opportunities.

Now, we can open the floor for the questions; thank you very much.

Q&A

Operator
Our first question comes from Charlie Higgs from Redburn. Please go ahead.

Charlie Higgs
I've got one on Pakistan, please, where I think the volume growth of 13.6% is actually very solid. Can you just comment on what you're seeing in the market in Pakistan from the consumer and the customer standpoint? And did the volume growth benefit at all from the timing of Ramadan this year? Thank you.

Andriy Avramenko
Pakistan volume growth. I think there is a lot of pressure from different sides on the consumer and customer and the economy right now in Pakistan. And the currency level is difficult to understand, whether it's an artificial or real rate, because there is a shortage of FX in the country.

In these conditions, we see that as long as we are able to provide sustainability of our raw materials, there is a demand in the market. So, the market will continue to grow. We really improved our RGM and our reach, and profitability of the entire value chain for customers and distributors, and so on over the last few years. So, we see that our products go to the end sales points through a fairly healthy and robust value chain, despite of the current instability. And the consumer remains fairly strong.

Now, we believe that the further test later this year will be in terms of how much the Rupee will continue to devalue or not and what kind of inflation will be there, and what kind of further price increases we need to take. This may impact demand in the future, deflation of volume and price nobody denies. But so far, the demand was fairly strong, and the pricing levels we maintained. And as I said, the main issue for Pakistan remains securing the sustainability of raw materials, because some of them are imported, rather than having front-end or demand issues.

But again, it may change as we go through the year, as price volume inflation – we monitor very carefully to make sure that we continue to grow.

Charlie Higgs

Thank you and then just a follow-up on the energy drinks opportunity. Where do you think it's the biggest across your markets and is it more angled towards Predator and the more affordable range, and expanding that? Or are you also seeing good growth at the more premium end with Monster? Thank you.

Andriy Avramenko

We see energy drinks as one of our strategic categories for growth. The base is very small. Our presence is minimal still in the market. And we see it as a very long-term growth opportunity. And therefore, we see it as a multi-layered portfolio.

We experienced significant growth at the top end with the Monster brand, particularly in Türkiye. And Predator is a more mass, mainstream brand and we are actively growing in – we started launches both in Türkiye and some of the international markets. And this expansion has proven to be successful.

At this moment, I think one of the large markets where we are not present is Pakistan and these economic conditions need to solve itself for us to decide for the launch or not.

And the second one, I think, Uzbekistan has a very small footprint, because we are focusing on the basics of the business, and primarily sparkling and so on.

But as a long-term, we see growth of energy drinks as a strategic category for us, along with sparkling beverages and iced tea, because of the economics and of its growth potential in terms of the consumption. And we see it as a multilayered portfolio, so we see continued growth on both premium side with Monster, as well as the Predator.

We also maintain a small Burn brand portfolio in Türkiye, which has proven to be quite resilient with a very strong niche following, and very good economics for the business.

Operator

Our next question comes from Hanzade Kilickiran from J.P. Morgan. Please go ahead.

Hanzade Kilickiran

I was also going to ask about Pakistan. And my question is answered, but maybe I can make a follow-up on the margin side. You highlighted that the margin performance is softer than your expectations, actually, currently. And I do think that the current issue in Pakistan may also put some margin pressure, and eventually impact your guidance.

Andriy Avramenko

We actually reiterated the guidance. And if we look forward, we see the second half of the year relatively easier than the first half of the year in terms of the margin performance. Many things may change, but that's our current view.

Now, to put it in perspective, Pakistan has a margin lower than our average. So, overall, even some deterioration there would not have such a significant effect on total portfolio, as long as we continue to perform in Central Asia and Türkiye.

So, I hope this answers your question. But in short, we reiterate the guidance for the year including margins.

Hanzade Kilickiran

And also on Uzbekistan, you have been building up some margins in Uzbekistan after the product mix change. Is Uzbekistan still diluting your margins or it starts to positively affect your margin performance?

Andriy Avramenko

Uzbekistan is still marginally dilutive, not a significant difference of the average. But yes, it's lower than average. Taking into account the growth opportunity, obviously, we are trying to improve, and we will continue to focus on the margin in all our markets. But with the growth opportunities there, we focused first and foremost on the growth.

Uzbekistan grew 20%, 21% year-on-year in the first quarter. This is the quarter where they had a historical freeze. One week at least there was no electricity or any other energy to run the facilities and so on. There was a stoppage. We still managed to grow

21%. So, the growth opportunity is essentially unlimited for the next few years and we are really focused, first and foremost, to build capacity, reach more customers and consumers. And secondary, also focusing on maintaining and improving margins, but the growth is very critical in Uzbekistan. It's a huge opportunity.

Operator

Ladies and gentlemen, there are no further questions. Dear speakers, back to you.

Conclusion

Burak Başarır

Thank you very much. Thank you all for attending our call today and thank you for your interest in our company. We know we're going through some challenging times, and we have, I think, proved again once again that CCI is a very resilient and agile and adaptive company to any kinds of challenges that are ahead of us.

We believe we're going to be able to deliver our commitments to the investors and those who believe in our company.

So, thanks a lot for joining our call today, and hope to see you next time.

Thank you very much.

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