

TOFAŞ TÜRK OTOMOBİL FABRİKASI A.Ş.

TOFAŞ Türk Otomobil Fabrikası A.Ş. 1Q19 Financial Results Conference Call and Live Webcast

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Conductors:

Mr. Cengiz Eroldu, CEO

Mr. Fabrizio Renzi, CFO

Mr. Erman Tütüncüođlu, Investor Relations Manager

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

Q&A SESSION

OPERATOR: The first question is from the line of Bespalov Vladimir with VTB Capital. Please go ahead.

BESPALOV V: Hello, congratulations on the very good results and thank you for taking my question. So my first question will be on your export guidance. How confident you are in the current guidance and what makes you feel that the new models that you are launching will help you to achieve this guidance given that the first quarter was really quite poor in terms of export sales? And do you have any indications from FCA in terms of demand for your new vehicles? Thank you.

RENZI F: Okay, Fabrizio Renzi, speaking. Thank you for the question, Vladimir. Okay, yes, we decided to keep our guidance for exports at the level of 200, 220. We believe that the performance in the first quarter is not the representative one for the entire year 2019.

The European market, and in particular the Italian market, have been affected by specific, temporary and seasonal problem. Erman mentioned the problem again coming from the WLTP Regulation introduced in September and still in the first quarter we are observing a problem coming from this change in the regulation.

Brexit is still playing a role in Europe, as well as, the upcoming political election. On top of that in Italy we believe that also we were penalized by the situation in Italy. The Italian government introduced a new fiscal system for the

vehicles, it's a kind of bonus-malus scheme that at the moment is not working at all and generate a lot of confusion in the customer behavior. Customers are already confused with the new regulation and the mission and this additional fiscal change introduce additional confusion. So we believe that the quarter is not representative.

So we believe that we have a chance to recover in the coming period better position, we believe that also the new version that we... that Fiat launched on the market, so the street, the mirror spot version could bring some better performance in the future. In particular, we are confident that the street version that is the entry level as we mentioned in the previous conference call, we believe that this version could really gain position in the B segment that now is not covered anymore by FCA with the Grande Punto.

So, also, I would like to remind that in our guidance at the beginning of the year, so the guidance that we released in February take already into consideration our contraction of 20% compared to the previous year. So if we... if you consider the lower range 200,000 vehicle, on the full year we are estimating a contraction of 20%. So of course, the second quarter will be crucial to understand if the... our guidance is solid reliable, but in this moment, we believe that we can achieve this target.

BESPALOV V:

Okay, thank you very much. And my second question, could you update us on the status of the development of the new generation of the Doblò model and your talks with FCA. What

is the status right now and when you probably could provide us more information on how this goes?

RENZI F: Okay, we cannot disclose news about the Doblò; we cannot disclose anything different from what we discussed two months ago in the previous conference call. So we can say that we are work at with the FCA representative in order to understand which is the best option, the best option is the best option from economical and technical point of view. So there are more than one options under discussion, but at the moment, we cannot say anything more than this.

If you want, I can add a personal comment also taking into consideration what Cengiz may have mentioned in the previous conference call. I don't know which kind of solution will be adopted for the future Doblò, but I'm pretty sure that will be a Turkish product manufactured by Tofaş. I'm pretty sure of that. So we are a very, very competitive industrial cost. We have a very competitive and excellent R&D center.

So I don't know which will be the final solution but for sure will be a Turkish product.

BESPALOV V: Okay, thank you very much.

OPERATOR: The next question is from the line of Kurbay Berna with BGC Partners. Please go ahead.

KURBAY B: Good afternoon. Thank you for taking questions. I have two, the first one is about exports again, and your guidance you already mentioned that on the passenger car side you expect

some improvements in Italy and your new launch is gaining more traction. I was wondering about light commercial vehicles and exports of Doblò and mini cargo as well.

It seems that those numbers are down significantly year-on-year in the first quarter too. So I was wondering, if you are more optimistic on the light commercial vehicle exports in the remainder of the year as well or whether this actual volume guidance that you are providing on the export slide because it's the remaining below your take-or-pay contracts, anyway isn't as crucial at this point for us and for yourself?

And my second question is about profit before tax margin, it was mentioned during the presentation that you target to achieve around 7%, and in the first quarter you were above that at 8.1% and how much of that is owing to the distortion of the numbers because of the take or pay payments? Thank you.

RENZI F:

Okay. Thank you. Berna let me start from the last question. So we confirm and we repeat that the sustainable profit before tax for us is 7%, but of course quarter-by-quarter we can have some effect that is beneficial for the profit before tax in the first quarter is this the case. So 8%, it's taking advantage and take... and reduce the benefit coming from the take or pay for sure. So Erman before mentioned that the Tipo family, for the Tipo family, we are 15,000 units below the previous year. Basically, this reduction is completely offset and compensated by the take or pay. So, of course, there is an effect coming from this.

On the other side also we cannot forget the extraordinary performance, excellent performance on the local market, so we became the leader of the market, but we became the leader in a market that now has a different structure compared in the past. So is a market that now is dominated by the retail market and because of that the results in effect coming from the mix of the local market.

So now we move to the most profitable part of the local market that is the retail one. So it's a combination of these two main effects. We have not mentioned in the last meetings our cost reduction project, this is now a recurring project, but we continue to push a lot on this direction.

So also in 2019, we have a very challenging target in terms of cost reduction. So we have a target of around €150 per car of reduction. So the combination of 3, these 3 factors motivate the very good profit before tax result that we achieved, but as usual, for the future, we can consider that still 7% is the minimum or if you want the reasonable result achievable.

Yes, coming back to the first question, so the export guidance, okay. My expectation is not to see the Italian or European market to improve a lot, the only thing that I tried to explain before is that I believe that 20% of contraction compared to the previous year on the full-year is something reasonable.

So what I mentioned before is that I don't believe that the results we have seen in the first quarter is representative. So

what I'm saying is that I believe that 20% of contraction is in these moments a reliable estimation for us, but also I mentioned that the second quarter will be crucial for this.

About the contraction in the LCV, more than contraction I believe that on the LCV side, we are let me say more or less in line with the previous year. So we have lost few quantity, and if you exclude the effect of the Opel termination, we are not so far from the previous year.

If you ever look to the evolution of the LCV market in Europe, in total they grew it around 5%. But also, for the LCV, Italy is a little bit below the average because the growth in Italy is only 1%. So also, for the LCV, I believe that in the coming quarter, we could see something better also because of our good evolution of the Italian market.

KURBAY B: Okay. Thank you.

OPERATOR: The next question is from the line of Kılıçkiran Hanzade with JP Morgan. Please go ahead.

KILIÇKIRAN H: Good afternoon and thank you for the presentation. I have 2 questions. The first one is related to the upcoming new Doblò project. I know that you can't disclose much information; you are still in the negotiation process, but I would like to understand if there's any sort of risk on the contract sizes, considering the post weak export volume in the past couple of years, and is there any risk of not continuing under the take-or-pay contract structure or

under... I mean you make the... I mean is there any chance for you to control under a normal export agreement.

And parallel to this with your production volume guidance, it looks like that you are guiding around 60% capacity utilization rate for this year. And I am trying to understand what could be the margin if there won't to be any pay contracts at this level? Thank you.

RENZI F:

Okay. About the Doblò project, we don't know the size of the project, as I mentioned before because we don't know which will be the technical solution adopted finally but the business scene will be the same adopted from this JV from long time. So for long time ago, we are applying two main principle, the cost plus, and the cost plus will remain as our main principle of the Company and the reserved capacity or the volume protection. So these are two pillars of the Company that will be enchanted.

But of course in a contract, in a complex contract like the one that involved Tofaş, there are a lot of economics condition that has to be discussed but these two pillars for me are untouchable for me. But for me means the negotiations that is... this is ongoing. These two principals are never touched and never under discussion.

About the utilization of the production capacity, you are right, so in this moment... and this is the reason why we decided to implement... to shift organization. In this moment, we are using around 60% of our production capacity. So we have a production capacity of more than 400 vehicles on three shift

and due to the contraction of the production that now is below 300,000 make sense to reorganize and to downsize the organization.

But the question was related to the protection of the contract for this kind of contraction of the production, so the protection and the reserved capacity is independent from the utilization of the reserved capacity but is based on number of vehicles.

So there is any kind of risk to see the actual protection of the take-or-pay amended or different because of the change of the organization or because of the reduction of the capacity utilization. If this was your question, I am not sure that I clarified your...

KILIÇKIRAN H: Yes, thank you. Actually I was trying to understand the impact of the pay contract on your margin, I mean what could... I mean I am sure pay contracts are adding extra margin particularly in this quarter after 37% volume decline in exports. And I am trying to understand how we should be thinking about this on our forecast. I know that you are guiding us with the profit before tax, but we need also put some sort of lines on the EBITDA side?

EROLDU C: Yes, but sorry, Cengiz speaking, so this is not the first year that we are benefitting from take-or-pay contracts, now this company since...

KILIÇKIRAN H: Yes, Cengiz Bey, I am not questioning about the take-or-pay contracts structure, I am very happy about this. I am trying

to understand what could be the normal margin for other company who produce at 60% capacity utilization rate without any addition of pay contracts contribution?

EROLDU C: Yes, I understood but...

KILIÇKIRAN H: I mean under your... I mean under a similar structure to yours.

EROLDU C: Yes, I understand but, the deviation on the markups cannot be linked only with the take-or-pay issues, you know, as Fabrizio explained also. Now we are in a very strong position in the local market and we are benefitting the mix issue, because we are not saving only fleet side.

So we are heavily realizing our sales on the retail side. So, all the... and we are very keen on the working capital of the Company. So we are also rightsizing the Company, because now in Turkey also you are also following the environment in Turkey. So the things are changing and we are restructuring the Company accordingly.

So now also, we are also trying to be more efficient under this condition. So a lot of issues helping us to improve our margins and so... but now if you ask me the 0.5% is the impact of the take-or-pay, this we cannot disclose, but nothing more different than the past years.

KILIÇKIRAN H: Okay. Thank you very much.

EROLDU C: You' re welcome.

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

RENZI F: Okay. I would like to thank all the participants to this conference call, and looking forward to speaking to you again in the next quarter. So have a nice day.