

TOFAŞ TÜRK OTOMOBİL FABRİKASI A.Ş.

TOFAŞ Türk Otomobil Fabrikası A.Ş. 20Q3 Financial Results Conference Call and Live Webcast

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Conductors:

Mr. Cengiz Eroldu, CEO

Mr. Fabrizio Renzi, CFO

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Conference Call Conducted by Chorus Call Hellas



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Q&A SESSION

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

BESPALOV V: Hello, thank you for the presentation and thank you for taking my questions. So, my first question will definitely be on the crossover version of the Egea/Tipo family. How much of capacity are you going to allocate to these crossover versions and maybe you could provide some color based on the initial orders, export orders and your analysis of the domestic market? How much of this new version of the model you are going to sell maybe as a percentage of Doblò of sales of the Egea/Tipo? Thank you.

EROLDU C: Vladimir, thank you for your question. This is Cengiz. We are trying to reach a 20% of the capacity with the cross version. But of course, this is the first time that we are entering in this segment, not only in Europe, but also in Turkey. The first reaction for the car... are very positive for this season. We have also possibility to do better. Thank you.

BESPALOV V: Okay, thank you very much. The second question that I have is on your CAPEX. You've spent €75 million so far this year. You have €150 million attached to the same amount for the fourth quarter. Maybe you could comment a little bit on what this investment will go to. Is the Doblò, or maybe some remaining investment in the safety or maybe something else? Thank you.

RENZI F: Fabrizio Renzi speaking, Vladimir. Okay. I understood your question, it makes sense because it seems that we cannot reach €150 million in the last quarter, but please bear in mind that in the guidance usually what we like to put in evidence is the committed amount, so let me say the amount that represent an obligation for us, so it means purchase order, not only invoices registered, so for us this €150 million is the amount that will be committed this year. The major part of this amount is of course people.

On top of that, we have the first spending for the Fiorino prolongation, and we have also other small investments that we continue to carry on for the tractor and delegated investments. Also, we continue to invest in the safety because never we have reduced our spending for the security and safety of the client and our workers. So most probably it's 70... we will have an increase of the registration in the last quarter because in the last quarter it is concentrated a major part of the spending for people.

Most probably the accounting amount will be slightly below this 150 but, but €150 million represent our commitment. So, I don't know if I answered your question.

BESPALOV V: Yes, thank you very much, that's very clear. Thank you again.

OPERATOR: We have a follow-up question from the line of Bespalov Vladimir with VTB Capital. Please go ahead.

BESPALOV V: Thank you again for taking the question. It is basically on the export outlook. You have increased the lower end of your guidance kind of very cautiously, but in general, can you maybe provide some more color what do you see with the October almost over, what do you see in terms of orders for November, December and maybe some color what do you expect from next year given the current trends and the potentially the second wave of the pandemic, how this can affect your exports? Thank you.

EROLDU C: For the... as Mehmet mentioned at the beginning of the meeting, we already started to produce new cars. But as you know, in the automotive industry, there is always a production curve. So, because every day you are also trying to increase the daily speed of the newly produced cars. So now, we started in those days with a very few numbers and day-by-day we will increase.

So, for the season until the year-end, we have the limited capacity for the new version production, so main reason is this. Unfortunately, we have only 2 months and we should manage also this...we have also very sharp production curve. But the main reason is this. So we don't have a technical capacity, let's say for the new car. Thank you.

EROLDU C: But overall, when I comment on the...I can comment both local and export markets; on the local sites the demand is still high. So, we are in a difficult situation in order to find the cars and respond to demand of the customers in Turkey. So, what we see until the year-end this demand will continue although we are seeing increase on the exchange rate side.

But still the demand is very live. For this reason, the local market sites from the Fiat brand point of view is very positive. What can I say? And regarding the export, in September, the sales in the Western European countries is very promising. We are seeing also in our numbers and orders. So also the export for a moment is in a good...say good trend.

BESPALOV V: Okay. Thank you very much.

EROLDU C: Thank you.

BESPALOV V: And can I ask one more question on probably the cost side, given that you are launching a new...the production of the crossover plus the technical version of the Egea/Tipo. Did you have any extra expenses, let's say in the third quarter or maybe in October/November, you are going to have some extra expenses, which are going to put pressure on your margin first on the production side and then maybe some additional marketing costs, was there some impacts on the numbers that you reported or maybe we can see something like this in the fourth quarter? How should we look at this?

EROLDU C: I can say no, because if Fabrizio says also, we are running with the highest technical speed in the plant. So, in this period also one car is important for us. So, for this purpose also we are working in a very proactive environment and we will not face any additional costs due to the ramp-up period. So we did all our plans accordingly, and we will... our main target is to increase the output of the plants, as much as,

possible, because we had the demand from export side and also on the local market as I mentioned before.

Now, actually we are only distributing the cars. So, we are aiming, and we are selling what we are able to produce that situation that we are now.

BESPALOV V: Thank you. Thank you very much. That's very clear.

EROLDU C: Thank you.

BESPALOV V: Thank you.

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

KURBAY B: Good evening. Thank you for the presentation. I have 3 questions. The first one is, just a clarification of what you have already mentioned. Does your fourth quarter guidance on the export side include the new models of Tipo or is it going to be all next year? That's my first question.

RENZI F: Okay. I can answer, Fabrizio speaking, Berna. So the guidance includes also the volumes for the LCA. Of course, these volumes will be sales for Tofas this year, but most probably will be... can sell for FCA next year, because the commercial launch of the vehicle will be in December. But it includes... it includes the last quarter a certain quantity of LCA.

KURBAY B: Okay. Thank you. My second question is about working capital. There has been an improvement in the first quarter compared to the second quarter. And I remembered that you were mentioning that this is going to normalize further. Is Tofaş where it desires, in terms of working capital at the moment or should we expect some further improvement in the fourth quarter?

EROLDU C: Berna, this is Cengiz. So, of course, after the pandemic period, the most important issue for the company has become, a management of the working capital and we are very keen on this. And also, thanks to the high level of demand that we are facing, we are working with, let's say, theoretical stocks. So actually, we don't carry almost none of the CBU cars in our stocks. So, this is also... is bringing advantage for us.

Also, the speed of sales in the network is very high, that's also another advantage that we are carrying. So, for... till the end of this year, we are not facing any increase on the working capital side.

KURBAY B: Okay. Thank you very much for that. And my final question is about the export outlook in general, looking to 2021 and 2022. You have announced that the global contract is extended for another year. And I understand or I assume that it comes with some take-or-pay guarantees continuing into 2022. If you look at it from an annual perspective, would it be fair to assume similar compensation in all 3 years 2020, 2021, and 2022 at this point, or is there going to be fluctuations?

Is this going to be something that we need to pay attention to in terms of forecasting your profit before tax numbers? Thank you.

RENZI F: Okay. About take-or-pay, Berna, 2021 or 2022 will be not so different from 2020. So, if your question is related to the additional year of the Doblò, I can say that the quantity based on what we are going to calculate the take-or-pay will be not so different from 2020. Why I say not so different because you cannot assume that the take-or-pay is flat during the life of the vehicle. So, there is some small variation at the beginning, at the end of the project.

But if you ask, compared to 2020, we will not have any big difference compared to 2021-2022. We will not see any big difference compared to 2020 in term of protection level threshold.

BERNA K: Okay. Thank you very much.

OPERATOR: The next question is from the line of İğnebekçili Murat with HSBC. Please go ahead.

İĞNEBEKÇILI M: Hello. Thank you for the opportunity. I have got several questions. Let me start with the Egea crossovers. Which tax brackets are you targeting for these crossover versions, do you think it is possible to keep this model in the lower tax bracket and benefit from the current price dynamics? This is my first question.

EROLDU C: Of course, our target is still to keep this car in the 50%, bracket because the cars we feel will be at the 80% level of the taxation zone, they are not sellable. I am talking about C segment mainly... C-segment cars, so as today, all our products are below this threshold and this is also the success of two brands, why we have this kind of market share, also thanks to management of the bracket and our competitiveness level in this market, also we are targeting to keep this car in the 50% zone.

İĞNEBEKÇILI M: The reason I am asking is because given the Turkish lira depreciation rate in the last couple of days, I mean it's, I don't know, maybe it is going to stop, you know. But, at some point even the Egea Sedan model due to costly inflation, it will be difficult to keep it in the lowest bracket. Is there a threat like that or you pay the certain...?

EROLDU C: Yes, but this is of course is very linked with the exchange rates. Until certain level, we can keep our position, but of course, if the exchange rate is I don't know, euro will be 15 Turkish lira, then of course, but we will talk with the government then in order to increase the bracket because now you are seeing also there is a big attention from the government side in order to protect the local producers. So, if you take this kind of issues, of course, we will manage it but...

İĞNEBEKÇILI M: Do you think the government will support local producers and increase the bracket?

EROLDU C: But already they are supporting because today, the 50% bracket is supporting local producers. In the month of September, if you see the number of September alone, the local portion of the light vehicle reached to 50% and this is a very high penetration level, and I think it will continue also in this way.

İĞNEBEKÇILI M: Okay. And last question is about this accounting change regarding the amortization period of Doblò. If such a situation did not happen, what would be your quarterly net profit for third quarter? And assuming that, the business is going strong and no such accounting impact will be...will happen in the fourth quarter. We should definitely expect some recovery on a quarter-on-quarter basis, I suppose. Is it fair to think so? Thank you.

RENZI F: Okay. Fabrizio Renzi, speaking. So as you can see from the footnote of the financial statement, the effect on the depreciation is around 80 million Turkish Lira. But this is not the effect that we can see on the bottom line, because as, you know, for the export, we have a cost-plus methodology, so part of this benefit is given and is considering the price list. So, we can say that, that minor part of this related to the local market is in our result. But generally speaking, I could say that no impact on the net revenue and profit before tax.

Of course, you have an effect, at the level of EBITDA where of course, the reduction of the depreciation and the reduction also of the revenue generating effect, but on the bottom line is not a huge effect.

İĞNEBEKÇILI M: Thank you very much.

OPERATOR: Our next question is from our... one of our webcast participants Koort Olavi with Avaron. "What's your take on the domestic market volumes in 2021? Do you expect to see domestic PC and LCV volumes higher than in 2020?"

EROLDU C: But actually, for a moment, our expectation in the local market is the same as this year, is a market size. But of course, the local market conditions are very dynamic in Turkey and you are following closely, but for a moment what I can say, we are forecasting as a flat like 2020 for the local market.

And for the export, of course, with the launch of the new passenger cars, family, our expectation is to have the better numbers than this year, also this year we had a couple of months, the pandemic period, where the important Western European markets were not active. So, for this reason, our expectation for exports for next year is better than this year.

OPERATOR: Our next question is from the line of...from our webcast participant Danis Erol with UNLU & Co. Thank you for the presentation. What is... your initial views on 2021 for the domestic market and the exports? Many thanks?

EROLDU C: Yes, I think we answered this question... in the previous one.

OPERATOR: We have a follow-up question with... from the line of Bespalov Vladimir with VTB Capital. Please go ahead.

BESPALOV V: Thank you again for taking my question. It's a pretty technical one. When do you need to find a new Doblò contract with FCA to be able to launch production let's say at the end of the 2022 or early 2023? How much time is needed between signing the contract and starting production? Thank you.

RENZI F: Hi, Vladimir, it is Fabrizio, speaking. Usually, we need 2 years from the approval of the program to go on the market.

BESPALOV V: So basically, this means that to start production in the end of 2022 you need to sign the contract somewhere at the end of this year or early next year, right?

RENZI F: Or at the most first quarter 2021, let me say, okay? So, usually our best result is 18 months, standard time is 2 years, but let me say first quarter 2021 it could make sense if you want to have the car on the production line end of 2022.

BESPALOV V: Okay. Thank you very much. Let's hope this is going to happen in the first quarter. Thank you.

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

KILIÇKIRAN H: Hello. Thank you for the presentation. And my question is about the progress on the electrification. Do you plan to get any share from electrification program going forward? Thank you.

EROLDU C: As, you know, they already, last week they launched new 500 model and also FCA is following for the Jeep Version of the... the Plug-in Hybrid application also in Turkey, couple of weeks ago, we launched the Compass Plug-in. So, the electrification strategy in... FCA for a moment is mainly to use the mild Hybrids and the Plug-in Hybrids, because what you are seeing also the real demand for the electrification could be started after 2025 from the cost point of view.

For this reason, the FCA strategy has detached this period with the Hybrids and we will see much electrified versions 2023 and onwards.

KILIÇKIRAN H: And Cengiz Bey, when you discuss about the expansion of Doblò short-term you can also discuss about the inclusion of the Hybrid or Electrification process here as well. I mean, do you have the strength here?

EROLDU C: But, for the commercial vehicles more than Hybrid the valid version is the fully electrified version. But, of course, still the electrified cars costs are not very attractive for the customers nowadays and also the light commercial vehicles for example, the FCA also started or they are going to start to sell the Ducato electrified version. But we forecasted that in the coming 1, 2 years the penetration of those cars will be very limited.

As I said everything is linked with the, let's say cost curve of the batteries and the electrical engines. And our expectation is that those cars will be for the mass markets, of course, I am talking not for the niche market. Now, we are all, we are

seeing some niche products also in Turkey, but those are the... they are showing very, very limited numbers.

Also, in Europe the registration of fully electrified cars, is still very low when you compare the total European market, of course, in the next generation of the commercial vehicles, we are going to offer also electrified version.

KILIÇKIRAN H: Okay. Thank you very much Cengiz bey.

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, Operator. We came to the end of this session. I would like to thank you all for the time and for the interest on Tofaş and I wish you all a pleasant day.