Transcription for AGTHIA

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Corporate Participants

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Tariq Al Wahedi
Agthia – Chief Executive Officer

Fatih Yeldan
Agthia – Chief Financial Officer

Presentation

Operator
Ladies and gentlemen, welcome to Agthia Group First Half 2017 Results conference call and a webcast. I will now hand you over to Mr Ozgur Serin, Vice President, Investor Relations, and Corporate Communications. Sir, the floor is yours.

Ozgur Serin
Good afternoon and thank you for being with us today. I'm joined by Tariq Al Wahedi, our Chief Executive Officer, and by Fatih Yeldan, our Chief Financial Officer. Using the opportunity, I am glad to announce Tariq's appointment as the CEO of Agthia Group as of yesterday, after serving as Acting CEO since January this year. Congratulations, Tariq. Before we begin the prepared remarks, let me remind you that you can find this presentation in the Investors section of our company web site at www.agthia.com. Additionally, this conference call may contain forward-looking statements, which should be considered in conjunction with the disclaimer contained in the presentation. Following prepared remarks, we will turn the call over to your questions. With that, it is over to you, Tariq.

Tariq Al Wahedi
Thank you Ozgur, and good afternoon everyone. We've had a lot going on under our belts in the past six months, largely dominated by the operating environment around us. In addition to the ongoing softness in the consumer markets, we also completed one full year in a mostly unsubsidized animal feed market. I am glad to see that we are very close, if not spot on, to our estimations of the impacts of this significant change in both flour and animal feed business models in the UAE. Fatih will talk about this in more detail. Water, on the other hand, continues to be our growth engine, both for revenues and profit. I will substantiate on this point on the next two slides. As

we communicated earlier, we've accelerated our efforts to streamline our processes and organization; given "surprisingly high" utility cost increases, not as buoyant a market as used to be in recent years in not only here at home but in wider GCC, and inevitable losses due to subsidy regime change, we did not have any other chance but optimize our costs in order to protect our profits as much as possible. This mind set has also helped us to a great extent in cutting our losses in all of our bleeding businesses, especially in Turkey, Dairy and Egypt. Lastly, we are showing reasonable progress in our recently completed water acquisition in Saudi, moving faster in particularly marketing integration. Let me now share with you what's been happening in Water.

As you know by now, the Group revenues grew by 2.2 percent in the first six months of the year, and profit declined by around 19 percent in the same period. Water, on the other hand, posted above 30 percent growth rates in both top and bottom lines. Obviously and certainly Saudi has contributed significantly in the revenues but the impact of Saudi on the profit growth is negligible – Fatih will cover this in more detail. What's hauling the lot, the locomotive so to say, however, is indisputably Al Ain Water's performance in the UAE. Let us look at the next slide now.

Al Ain ZERO has been a phenomenal success. You've all seen it all around the country in the last few months of last year following its launch in August, since when it passed 4 percent volume share in the market, bringing MAT share to 2.1 percent. It is also in Oman now. It is a lot, when one considers that it is less than a year and it is one product with a very specific consumer proposition. Albeit the right one, the innovative one, and the differentiating one. That's what leaders do, isn't it?

Propelled by the success of Al Ain ZERO, Al Ain Water market share reached 27 percent, opening the gap versus the runner up to 900 basis points. We are not complacent, nevertheless, as we are aware of the rise of Competitor C, albeit from a low base and still at quite a distance from us. This is not surprising when one observes the level of price cuts our competitors are engaging themselves in, in an effort to snatch share in the market! We have our actions in place, and in the pipeline for the second half of the year.

Our 5-gallon business, or HOD, is also digging in strong with double-digit growth rates over last year. Noteworthy to mention here is the contribution of Al Ain ZERO 5-gallon, despite it was only launched a couple of months ago.

What you see here is a list of our bleeding businesses, and their profit turnaround performance this year. Some remarkable results were achieved in these businesses in the past six months. Egypt and TP businesses are no more bleeding; Turkey is almost at break-even, aiming for full-year profit, and it is worth mentioning that Turkey successfully managed to pay back a few millions of local loans thanks to their positive EBITDA. Yoplait has cut losses by 55 percent. In Bakery, we have plans well in motion to cut the losses significantly. All in all, combined losses reduced from AED 16 million to slightly above AED 7 million. This is an accomplishing performance, and encourages us to do more of everything we did right so far.

I would like to close my part by shedding some light on our priorities for the rest of the year. It is obvious that Water will continue to drive our Group performance hence we will not stop acting like a leader in this category. On Flour and Animal Feed side, both the market and the players have mostly adapted themselves to the new environment, within which we successfully demonstrated our capabilities to weather storms. We are not yet out of the woods, with especially the second phase of flour subsidy changes becoming effective this month, and this will have negative effects on our profitability in the second half. Nonetheless, we have our plans and actions in place to come as unscathed as possible through this wave too. Cost optimization will be an essential pillar during this journey including manufacturing and process efficiencies in especially our new venture in Saudi. Saudi Arabia is the largest market in the GCC, and we strongly aspire to develop and expand our footprint in there not only in the Western region but nationally. Last but not the least we will not pause our efforts to improve the performances of our turnaround businesses.

I am now handing over to Fatih, and will be available for the Q&A session at the end. Fatih, over to you.

Fatih Yeldan
Thank you, Tariq, and good afternoon everyone. Let's start with the revenues. Group revenues reached AED 1.1 billion, posting 2.2 percent growth over last year. The charts above speak for themselves, and you can clearly see what is driving the growth and what is dragging it – while consumer businesses in aggregate increased by 22.5 percent, our Agri business declined by 13.5 percent. Another point I want to highlight on the left hand side of the slide is the share of revenues represented by our consumer businesses. What used to be a mere 17 percent share 10 years ago is now 52 percent, and higher than the contribution of Agri for the first time in Agthia's history. Graphs on the right give a break-down of the growth further into segments in each unit. I will talk about these segments in detail in the next few slides so I am moving on to the next one now.

Let's first look at the consumer businesses. On the top of the slide is the waterfall diagram of 27.9 percent or AED 101 million growth in Water & Beverages, which recorded AED 465 million net revenues in the first half of 2017. Organic growth in the UAE brought in AED 28 million, while Saudi consolidation provided AED 80 million. These were marginally offset by AED

6 million drop in our revenues in Turkey in line with our profit turnaround plans, and less than a million decline in Beverages driven by softer Capri-Sun shipments affected by Ramadan in June. On the bottom of the slide is the performance of our Food segment businesses, which include Dairy, Tomato Paste and Frozen Vegetable, Ambient and Frozen Bakery, as well as other food trading items that we are supplying mainly to Municipalities and other government stores like Sheikh Khalifa Foundation outlets, Fazaa stores, etc. And let me just say a few words on this last one, other food items. Although remaining in shadow, this group of products is one that continues to grow strongly, consistently and profitably. They now represent almost 35 percent of total Food revenues, growing 28 percent over last year. These products and the channels they are available are now receiving more concentrated focus in our business portfolio.

Dairy is back in growth territory after a short and small blip in the first quarter. Frozen Vegetables is driving the decline in our TP/FV business; whereas some of this decline is acceptable as part of our profitability focus, we believe we have room to improve especially from product mix and positioning perspectives, and initiatives are in place for the second half in this respect.

We have talked a lot about subsidy rationalization, and its impact on our Flour and Animal Feed. We came up with our estimates in the early days of the change, and we stuck with them. What we see now is we were not bad at all in those estimates. Let me elaborate for Flour here on this slide, and for Animal feed on the next one. I will not go through the numbers on these slides one by one; they are more there for further transparency so that you can analyze better. What we can say here is that there was not any major deviation from our volume and margin loss expectations in the past 10 months because of partial subsidy withdrawals. We said we would lose around one thousand tons per month in the retail trade due to aggressive price increases we chose to implement, and we are losing only slightly higher than that. The volume loss that we are experiencing in B2B is very small relative to the size of this segment, and it is almost totally driven by very low priced imported flour from Ukraine and Turkey. Time will show whether this will be sustainable. Measures we have taken in order to protect our volumes in affected channels inevitably but expectedly took their toll on our gross profit margin, reducing it from very high forties to very high thirties. The second phase of subsidy removal which started this month will result in further reduction in our gross margin, bringing our full year margin down by an expected 350-400 basis points from where it sits today.

A similar slide is here for Animal Feed. Although overall subsidy story is the same, the characteristics of the changes are different. It is now one full year that animal feed market is mostly unsubsidized. Moreover, it is only the commercial farms that are left with subsidy, and even in this case there are strict rules in place to keep the subsidy in check, like introduction of quotas to individual commercial farms depending on their sizes. It is in this environment that we are losing around 6 – 7 thousand tons a month, slightly lower than what we had anticipated. New products that we launched, including low-cost value range in addition to improved formula products addressing full life cycles of animals, and our relentless efforts to excel in customer service like providing veterinary support to smaller farms, helped us achieve these results so far, and with signs of market stability we believe the worst days are over in this business. One dynamic that needs mentioning here is what we call the CP business – government's annual concentrated pellet tender through which CP is procured from suppliers like us at market prices and then provided to the farmers in heavily subsidized prices directly by the government. It has never been an "immaterial" business for us; either at top or bottom line. Nonetheless, this tender has not been happening this year so far, with no prior warning. Our "commodity" trading volume was able to compensate for the most part of the lost volume in CP but at a fraction of profit margins associated with the CP business. Although we do not know how the government will act in the rest of the year, the silver lining in all of this is that we started to see an increase in volume of our more profitable sheep feed, and feed raw materials like barley, for which CP constitutes a substitute.

Now the P&L. We talked about the revenue, growth and the drivers. Here we can also see the impact of Saudi on our P&L lines. Net profit for the period was AED 118 million, and lower by 19 percent than last year, totally attributable to Flour and Animal Feed on the back of subsidy changes. As you will see on the audited financial statements under segment reporting, profit of our consumer businesses in both Water & Beverages and Food is growing versus last year – actually, in the case of food the losses are decreasing. Combined profit growth in consumer businesses is 54 percent whereas profit in our agri businesses is down by 46 percent. The drop in gross margin is also a direct consequence of above situation. I don't intend to go over each and every line of the P&L here; we can do that later offline once you have a chance to analyze the numbers. On SG&A, though, there is an additional 0.7 percentage points owing to a reclassification from within manufacturing overheads to SG&A, without which ratio to net revenues would have been just above 20 percent – that is excluding Saudi numbers. The increase in overheads apart from this is because of full year impact of new headcount as well as inflationary cost increases. Let me say a few more words on the profit decline on the next and the last slide.

It is very important to put AED 27 million decline in profit in proper perspective. When evaluated in relation to AED 104 million profit that was deprived from our bottom line by withdrawn subsidies and utility cost increases, AED 27 million loss relays a totally different meaning.

Numerically, it means that we recuperated AED 77 million back in only six months. Numbers are easy to reconcile – higher sales, production efficiencies, more profitable products like Al Ain ZERO, Saudi, and cost savings …

But it also means that, at Agthia, we do not give up! No matter what the circumstances, we at Agthia, demonstrate our commitment to deliver the best value to our shareholders. It is not an easy job. It takes a lot of dedication, coherence among multiple layers of the organization, and most importantly passion to deliver on our commitments, both to our consumers and stakeholders.

This concludes our prepared remarks. Thank you for listening to us today. I am now handing over to the operator for the Q&A session.

Question and Answer Session

Operator
We have a question from Jonathan Milan, Waha Capital. Please go ahead.

Jonathan Milan
I have a couple of questions. Any progress on the sale of the non-core divisions and can you please reiterate which ones are the non-core divisions that you want to sell and how are you looking at the sale of these non-core divisions? Will it be all as one entity or will it be separate entities, and are you already talking to interested buyers? The second question has to do with the Saudi business. I mean, what's the capacity of the Saudi water business? What's the utilisation rate and how are you going to move forward to ramp up capacity? What is your expectations for the second half? Thank you.

Tariq Al Wahedi
Okay, for the first part of the question on selling non-core businesses for us, as clearly mentioned, we have focused on managing and turning around the non-core businesses into a stable state, which we've been quite successful doing so far as can be seen on the results that we have achieved there this year. Most of our leading businesses now are in a very good state and we foresee that it will be in a better situation by the end of the year, so this is the plan that we have as of now in terms of stabilising their businesses. I'm sure at a later stage we will be thinking about how… what will be the future steps we need to do on the non-core businesses that we have.

As far as the KSA or the Saudi plant capacities that we have now, we are currently on… I mean, on our [PAT] line we are utilising 60-65% utilisation rate now and on some of the lines, and on some of the lines we are at 80 or 90%, so it's a mixed basket over there and we are trying to maximise the utilisation over there. So prior to thinking about expanding the capacity, we are trying to complete the integration process that we have in place among the team. I mean, a lot of support functions are being integrated as we speak now, and then we will continue expanding in terms of capacity that we are looking forward to.

Jonathan Milan
Okay and do you have an updated outlook for the second half of 2017 and would you revise your EPS estimates?

Fatih Yeldan
For total year for the profits outlook, we are having low double digits. We had before high single digits' decline after the changes happening in the political environment in the region. We are obviously having the same thing what's going on in UAE for UAE companies. Our sales to Qatar, obviously we immediately have to stop, so Qatar business for us is about 2% of our sales and also for our bottom line it's about 4%, so basically instead of having a high single-digit drop on the profit, it will be low double digits decline in the profit, if the situation obviously doesn't change and if something happens in the political environment, something changes positively, it may be impacting our numbers positively but since the beginning of June, obviously we started to have the negative impact of the change in the Qatar business.

Jonathan Milan
If you're going to have more subsidies removed for the flour business in the second half, based on what or what will help you reduce the year-on-year drop in the net income? I mean, so far year-to-date I think it's down mid double digits, 16%, or just in Q2. How will you mitigate the introduction of further cuts to subsidies on the flour business and to reduce that year-on-year drop in net profit?

Fatih Yeldan
Obviously, all other businesses are growing very well and very profitably. As we mentioned, we continue to cut all the losses on the other businesses. Significantly we cut the losses. We turned around Turkey, Egypt. In dairy, lots of cuts also very significantly. Now the next is with the bakery. On the bakery as well we have now plans in the second half which will help us to reduce further the losses. At the same time, we initiated several plans to further optimise our cost. We are looking at the organisation. We already had the first wave and we will see some positive impact on our second half, but mostly

it will impact our 2018, so we are basically proactively taking actions on our cost structure, as we know obviously most of the subsidy change will have an impact on our bottom line. Those are the things basically, you know, it will help us to offset most of the hit coming from the subsidy change. The subsidy changes for the second half, I mean impact-wise we are talking about 18-19 million itself. The gross impact of subsidy change in flour is about AED 18-19 million on the bottom line before any other action.

Tariq Al Wahedi
Just to bear in mind, I mean, we have recovered them in a big gap from the subsidy removal from last year. All these efforts have recaptured a lot of that gap that you guys can see in the results that we've shown you so far.

Fatih Yeldan
Like I was mentioning in my part, we had more than 100 million just coming from subsidies change and utilities as loss, and out of that, about 75% or 77 million is recovered. That's why we have only a 27 million difference versus last year, but actually we started the journey with 104 million losses just coming from subsidy and from the utility change. Mostly it is subsidy; the utility impact is around 12-13 million in that and the rest about 90-91 million it is the subsidy change, so we were very successful to actually offset 75% plus of that. We will keep doing that, so for the second half as well, so we see now mainly for us it is Qatar, so for our outlook, unless something else changes in the coming months, [close to negative].

Operator
Our next question comes from Sandeep Srinivas, FM Partners. Please go ahead.

Sandeep Srinivas
Hi there, thanks for hosting this call. I have two quick questions. One, can you please give us some update on the Kuwaiti plant and your Anderson JV? That's the first one. The second one is we are seeing an increase in accounts receivables for the last couple of quarters. Can you please comment on that?

Tariq Al Wahedi
Okay, I'll have the first part, the Kuwaiti JV, Marabe Agrivita JV that we have. On the Kuwait business, that joint venture is progressing on schedule. There's now as we currently speak machinery being installed in the factory now and we expect the first bottle to be produced by the end of August, but we will

have commissioning until the end of the year, which as per the schedule that we have, so expect there to be commercially by beginning of next year. In terms of the Agrivita joint venture, I mean as you guys have seen in the announcement, we've progressed with that, and since then we've been progressing doing lots of business development and lots of deals have been made in the market. That's progressing quite well and we are at the final stages of doing all the incorporation documents as we speak now.

Fatih Yeldan
On the trade receivables, one obvious thing is the KSA, so Saudi impact is there about 25 million, and in our UAE businesses or in the consumer and agri, in consumer business because of the sales that increased, there is some increase coming from there. There is nothing about any bad debt or something. When it comes to agri business, agri business, with a couple of trading customers, we have deals with them, with [SE] about 60 days, that is one with 90 days, so basically those terms may be increased, otherwise again there… there is nothing like bad debt. Actually in this environment where mainly, I would say, the risk is increasing on the credit, we are doing so far great – actually this year we didn't have any issues with anyone, so stable increase is basically normal business, nothing to do with any increased risk on the credit.

Operator
Our next question comes from Andrew Howell, Citi. Please go ahead.

Andrew Howell
Just a question on the UAE water business and when you look at the 27-30% or so growth in water and beverages in the first half, can you break down that between market share gains and the overall growth of the market? I mean, clearly you're gaining a lot of share, but is the underlying water market also growing? Looking for the full year and then looking into [audio], what is your sense of the underlying growth rate of the water market, so assuming your share stabilises, what could the water business continue to do for you looking into 2018?

Fatih Yeldan
In water business in UAE, obviously one thing is the share gains. We moved from 23 plus percent to 27%, so that's obviously giving most of the growth for us in our business. The other thing is Al Ain Zero impact, because our pricing, average pricing, is about 1.5% better than last year, so in monetary terms we are talking about AED 5 million. It will be about 2% growth on the sales and

on the profits side, Al Ain Zero impact in the mix, so… and for the market itself, we actually don't have the latest-latest data, but just the last reading that we had, it was around 4-5% growth in the market, so we are gaining market share, because we are having higher growth and we have Al Ain Zero obviously positively impacting us. On the other side, we have obviously within UAE sales Alpin as well. Alpin also growing very well versus last year and also we launched our Al Bayan PET, and Al Bayan PET again also doing very well, increasing our overall water business sales.

Tariq Al Wahedi
And also in the HOD side, also we are… we keep the… gained the same growth, the same thing, and we have moved our value added water also to the HOD business as well, so we launched Al Ain Zero as an HOD version now. Added to that also we are focused on the export business as well, which we… I mean, we have gained quite a bit on that as well and we have moved Al Ain Zero to Oman as well recently just to capitalise on our strength and the new innovation that we have.

Fatih Yeldan
Furthermore, I mean, what will happen is we are working on some exciting products, which will be coming to the market in the second half, so that will be also helping us to keep our momentum on the market share and the sales, so there will be some news coming in the next months, which will help on the water business further.

Andrew Howell
How big do you think Al Ain Zero could become for the UAE in terms of market share from the 2.1% where it's now?

Fatih Yeldan
At the moment it's 4%. Ozgur mentioned… we had 2.41 in our script is basically MAT, because we launched only for the last six, seven months, and we had the data, so actually the point is like 4.2% itself.

Ozgur Serin
Strong single digits probably.

Fatih Yeldan
So 4.2%.

Ozgur Serin
Already.

Fatih Yeldan
Already after seven, eight months let's say, so… and still the volumes that we are shipping is actually increasing, so I don't know exactly where it can reach, but…

Tariq Al Wahedi
But the growth is healthy so far and is gaining. I mean, the growth rates that we are seeing are quite healthy. We are maxed out in capacity and we are ramping up capacity as we speak now. We will just have new capacity to be pumped now for production, so we have de-bottlenecked. I mean, so far the capacity was a constraint for us, so hopefully we will see better results for the next one.

Ozgur Serin
It's very difficult to give a number, as you can imagine. It's market share. It's dependent on a lot of things, but as these two gentlemen said, it's growing and we're also beefing up the capacity, so we're expecting to increase. Up to where, where it could stop, I don't think we can say it.

Operator
Our next question comes from Yazeed Al Turki, Ashmore. Please go ahead.

Yazeed Al Turki
Could you please walk us through the economics of the UAE and Saudi water businesses? Where do you source the water? How do you pay for it and are there any subsidies along the supply chain at all?

Tariq Al Wahedi
There are no subsidies in the supply chain of the water. The water that we have is not subsidised and the water that we have our secured sources of water, I mean there are no constraints in terms of water, so our supply chain is fine and we are just like many of the companies in UAE and KSA in terms of how we source our water, and we process it as well.

Yazeed Al Turki
So you source it from natural sources or is it from the utility network, just so I understand [audio] Saudi and the UAE?

Tariq Al Wahedi
We have a mixed basket of different sources, because remember we have many plants around the GCC and in Turkey. Turkey is spring water that we have and Oman also we have wells in there, where in Al Ain we have wells, we have municipal water, and in Saudi we have the same, so it's a mixed basket really. We cannot just pinpoint into a specific sourcing mechanism.

Yazeed Al Turki
But Al Ain has some municipal water in it, is that what you're saying or is municipal water just in Saudi?

Tariq Al Wahedi
Like all the companies in the UAE, municipal water is there, but we also have our own water wells as well.

Yazeed Al Turki
Okay and then the sales price, is the retail price controlled or is that at your discretion?

Tariq Al Wahedi
It's what, sorry?

[All talking]

The retail price is what, sorry?

Yazeed Al Turki
Controlled.

Tariq Al Wahedi
Yes, it is controlled. Yes, there is a control from the ministry of economy, yes, in UAE.

Operator
Our next question comes from Nishit Lakhotia, SICO. Please go ahead.

Nishit Lakhotia
I have got a couple of questions, one on the cost savings that you've achieved in the first half. How do you see the cost savings going forward and will this continue into even next year or the delta would move for the cost savings from 2017 in 2018? That's my first question. Secondly, on the pellet saved, what was the exact number in terms of volumes last year, just to understand the [inaudible] sales this year, what would be the impact on the business? The third question is on the capacity, if you can share on the Al Ain Zero on the HOD and the [audio].

Tariq Al Wahedi
The first one, on the cost saving, cost savings will continue, have to continue, because the thing is that still subsidy removal impact continues to increase, right, because now this half we will have last subsidy second phase change, which will have, as I mentioned, AED 18-19 million of impact, so then next year in July we have one more change in the flour, so that will be one more. So obviously from that perspective, we are working to offset these things, which are coming now and which will come in 2018, so the pace actually will continue, and an increased pace I will say, and according… so that we can offset most of this significant impact, as we did so far. So that's what we are actually doing. We have certain things already we identified. We already actually kicked off some of them [over first] organisation and now obviously most of the impact of that will come in 2018, because this change is happening now, and the full year impact of that will be in 2018, which will help us, the subsidy changes which we'll have in 2018, so that will be covering part of this impact. Again, we are looking for a second wave of it. We are looking under our direct costs, source of the grains, packaging, so you can imagine anything from A to Z, and basically what we have done is the first part of it we are continuing and it should be even an increased pace that we can also cover this next impact, and then 2018 impact.

To your other question about CP, the concentrated pellets, last year six months it was 41,000 tons, which is around in monetary terms almost AED 50 million, so this was what we had last year six months on the CP, which now we don't have, and then you're asking on the capacity. In Al Ain, we have 75 million cases, CapEx before PET, and for HOD we have 36 million including Al Bayan.

Nishit Lakhotia
In Al Ain, the capacity of Al Ain Zero is a part of this, so…

Fatih Yeldan
No, it's together, but so far this capacity is enough for us to take us for a couple of years more and then we have to think about to start doing something late 2018 to do for coming for 2019/20.

Nishit Lakhotia
Okay, thank you, and just one follow-up on the cost savings. If you can give us a number on… like you've done [circa 10] million in the first half, how would it be for the year, do you have any target, and what do you have in mind for 2018 in terms of an absolute number?

Fatih Yeldan
No, I cannot give it now to you, but the thing is what I can say so far, we have done around 25 million and it will need to continue the same or more to offset what will be coming. As I mentioned already, 18-19 million will be hit coming from the subsidy change in the second half, and then we will have for 2018 when it changes, another impact, similar impact, so you can imagine how much we have to save and you total them up.

Operator
Our next question comes from Metehan Mete, Waha Capital. Please go ahead.

Metehan Mete
I wanted to ask you about what are your… what will be your brand positioning in the Saudi water market? Are you planning to embark on a similar market share gaining strategy in Saudi or will you be just like one of the other players there and try to grow with the market? My other question is where are you on your acquisition targets, because when I looked at the presentation or presentations, there is that 1 billion target revenue by 2020 and are we expecting any further acquisitions during 2017 or '18? Are you working on anything?

Tariq Al Wahedi
Okay, the first question on our marketing and branding strategy, of course we always try to become market number one in any market that we get into.

However, of course, there are realities into each market and the competition is different in each market that we head into, so that's why we have to change our strategies in how we penetrate the market and how we look at through to market. We have our strong plans for KSA in terms of distribution and marketing, and this is our focus. We're trying to focus more on our distribution and our reach, and improving our cost to serve into the market, and then focusing more on building the brand equity. Bear in mind, I mean, in KSA we have acquired Al Ain brands over there and that's what we are trying to capitalise on over there, and just to make it a pan-Arab brand. I mean, this is the aim that we have now. That's on the first question.

On the second question, yes, I mean, when we look at acquisitions, acquisition is not really our target. I mean, it's not really the M&A part, but when we talk about the… we are trying to acquire distribution and market share, whether that's as M&A or as market approach etc. There are many ways of gaining, having that particular gain of distribution. This is the main aim, how can we get there as soon as possible, so yes, we are looking at many candidates and we are looking at many strategies to get us that gain that we are… inorganic gain that we are looking at and that we have announced in our strategies.

Fatih Yeldan
Just, Metehan, one thing to add, with our organic growth and with what we already have from the last acquisitions, we are not super far away from our 1 billion target, and in Saudi our business that we have is basically Jeddah related, in the [Mecca] region, and there is good potential for us to expand for the rest of the KSA. As Tariq mentioned, it can be through acquisitions, it can be through a different model, but there is a big potential there to give us the difference to make it a $1 billion business.

Operator
Our next question comes from Mustafa Salih, Blakeney Management. Please go ahead.

Mustafa Salih
I just had a quick question on the profitability of delta of the Saudi water business. Just looking at the numbers it seemed to be generating in the first half a 4% net margin, which I think is much lower than you outlined when you did the acquisition. I'm just wondering, were there any one-offs there, what do you see as a normalised business of that Saudi business as it stands, and maybe your hopes two, three years down the line, how do you get the new line there?

Tariq Al Wahedi
Yes, I mean, what we can say is there… not one-off, but there is one reporting thing there. We have used loans for this acquisition and [inaudible] loans is in the Saudi P&L, okay, versus [out of] corporates, so that's basically loan impact for the business so far. You can take about… it will be impacting the year about 3%, so that's one thing. Then their strong months is basically Hajj, you know, before the Hajj season, so those months are now coming, so now when we will be looking at year-end, also if you correct thing [interestingly] back then you will see around 8-9% net profit margin, but there, I don't know if you recall, we were always mentioning that the net profit margin is not that high, but their EBITDA margin is high because they have very high depreciation. I don't know if you recall. We're always mentioning this, that actually the difference between our business and their business there is the depreciation, and we are looking at the depreciation. We got the ownership of the place three months back and we are trying to put the finance systems and everything there in place, and at the same time we are looking for the depreciation and there is room to also adjust some depreciation there, because their useful lives were too short and that's actually impacting the net profit at the same time, but its opposite EBITDA is good, you know. So by the year-end you will see healthier net profit margins.

Operator
Our next question comes from Fatema Aldoseri, SICO. Please go ahead.

Fatema Aldoseri
I just have a couple of questions. My first one is regarding the flour business, so there has been a lot of competition regarding low price imports, so how is Agthia dealing with that and do you see it impacting your sales especially after the subsidiary removal which happened in July? Second question is now that we're a month into July, how is the [audio] after the subsidiaries were removed and have you seen some shifts in terms of consumer? My third question is regarding the feed business now that's it's going to be a full year after the subsidiary has been removed, are we going to expect similar margins in [28/17]?

Fatih Yeldan
Now, in the flour, this July subsidy change actually doesn't impact the customers. It impacts us because our subsidy that we are getting from the Government becomes half. That's why there is no impact on the customer side yet, so that's why nothing changed so far. When it comes to your first

question, we were mentioning in our presentation, I think you're touching on that.

In flour, when we come after the subsidy change and we said that we were expecting to lose about 1,000 tons a month because of retail business, because we will double our prices in a market where we have 90-plus market share in retail. Obviously all other guys will come and strong competitors with the same or lower price, obviously they will get some share; we are expecting to lose 1,000 tons and what we are losing now, the difference versus that 1,000 tons is basically coming from the fact that what you mentioned is there are cheap imported products mainly from Ukraine, and because of that, around another 700, 800 tons a month we are losing, because we don't want to lower obviously price to that level because then we will lose from the profit. However, in total, when you look at the flour business, we are having a flour business of 22-23,000 tons, so when you compare that versus what we are, let's say, losing, it's quite immaterial in a way, because we are able to keep the bulk of our business, critical business, although most of it is not subsidised.

That was our aim. We would like to maintain our business, our market shares of our business, and take it from there, and in a profitable way. So far, we did quite well. The first half flour margin, if I'm not wrong, is about 39% or something, 39%, and now we are going to change; we'll finish the year around 35-36%. It's still very healthy margins and we keep most of the volume, almost 90 plus volume, so that's what we aimed and we were successfully doing it.

You had one more question on the feed, right?

Fatema Aldoseri
Yes, basically that's a span of one year since the subsidies were removed, so just for [28/17] should expect 13% gross margins, and stable volumes?

Fatih Yeldan
Now, the thing is what the… the feed business, because of trading we have about 13%. If we exclude trading, the feed business, the bulk of our real feed business, is about 15 plus, 15.5, so even better than what we have, because trading is a bouncy business, but you don't make obviously very healthy, very high profit margins. You make 4%, 5%, so depending on the weight of the trading in the results, your margin is actually going down, but apple to apple comparison, in the past before subsidy changes, we were having about 19-20% feed margin. Now, we are around 15 plus and since there is no further subsidy change and actually we are even doing better than what we expected to do in the feed business, so you should expect to have similar margins. It

will only change depending on the trading if trading will be more, it can be 13; if trading will be less, it will be closer to 15, 16, 17, so it is stabilising.

Operator
We have no other questions at the moment. Mr Ozgur Serin, back to you for the conclusion.

Ozgur Serin
Thank you very much to all. Thanks for being together with us here again. As you know, as usual, if you have any further questions, I'm sure you will have, please reach out to me and we will always be ready to answer them, and thanks again. Have a good day.
