Agthia FY ’20 Results Call Transcript

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Corporate Participants

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Hatem Alaa: I'll hand over the call to Sahar Srour, the company's investor relations manager. Sahar please go ahead.

Sahar Srour: Thank you, Hatem. Good afternoon, ladies and gentlemen. Thank you for joining us today in Agthia Group's earnings conference call for the full year ending 2020, hosted by Alan Smith, Group CEO, and Ammar Al Ghoul, Group CFO.

As usual, Alan will first talk about the performance highlights during the period after which Ammar will cover the financial results. We will then continue with a Q&A session. For your reference, the relevant presentation is available in the Investors section of the company's website at www.agthia.com. Please note that this call may contain forward-looking statements, which should be considered in conjunction with the disclaimer included in the presentation. Over to you, Alan.

Alan Smith: Thanks Sahar and Good afternoon everybody.

So, fiscal year of 2020 I think it was an exceptional year from which the company experienced transformational changes across various business aspects. H1 as we came across unprecedent busines environment imposed by the covid-19 pandemic I think we show cased our agility and resilience in response to that by our swift response to ensure productivity and of course the preserving safety of our employees. Q3 we conducted a strategic review of our business including our books, which resulted in significant on time negative impact on our bottom line, with the ultimate aim of improving equality in positioning Agthia group for long-term sustainable growth. In Q4 the focus of the new leadership to delivering on our growth strategy was translated into several successful milestones. We acquired the Al Foah company, the world's largest data processing and packaging company, and that really gives us the opportunity to diversify the product offerings and our competitive access to new markets and allow for cost and revenue synergies from the integration of the combined platform here in the UAE. We also announced the acquisition of Faisal Bakery & Sweets, one of the biggest bakery plays in Kuwait, which obviously allows upscale of our operations in the Kuwaiti market to take advantage of distribution synergies and to optimize costs through back-end integration. We also officially signed a UAE distribution partnership agreement with VOSS of Norway as premium lifestyle water brand, Voss makes our long-term commitment to lead the water category and that gives the opportunity to move into the operate into the premium water segment. In Q1 2021, we also annpounced plans to acquire majority stake in Nabil foods. One of the leading regional producers of frozen and chilled processed protein products. This transactions, subject to shareholders and regulators approval will give us place at the forefront of a fast-growing industry, and it immediately enables us to access to new revenue streams expanding into different product offerings and obviously give us a cost and revenue synergies across the net mark.

So, if we jumped to the financial side, I think the revenues are AED 2.06 billion, 1.1% increase verses prior year despite the headwinds. A top-line growth is largely driven by flour, food and five-gallon water segments which will build on a little bit in the following slides. Groups Net profit came in AED 34.5 billion obviously which was impacted by the unfavorable sales mix. This also include significant one-time impairments and other adjustments booked in the third quarter. If we exclude the aggregate AED 82 million one-offs, normalizing net profit would be AED 117 million.

Resilient operations continue to underpin of robust liquidity position as we continue to focus on working capital overhaul for a strong cashflow generation. In terms of CAPEX spending is lower vs previous year as we had available capacity as we made prudent decisions on were to invest and what to spend on.

If we move on to the next slide, please. So, when it comes to the market shares we continue to retain our leadership in water, in flour, and in animal feed and tomato paste across Al Ain, Grand Mills and Agrivita brands.

On the next slide we will take you through the sales performance, the overall sales performance will provide some insight by product category, geography and sales channels. In terms of category, we saw what should be the home and office distribution business grew with higher volumes from homes of setting the negative impact on office delivery, but we saw good growth in the channel. Food categories are very strong on sustained at-home consumption. Consumers are getting back in touch with the kitchens and cooking. Agri improved on domestic and export demand, and we will come back to it later, but that was helped by the World Food Program order in quarter one, and also a strong performance in retail channel. Low volumes from the bottle water category in UAE and KSA and the beverage segment reflect the impact of cost by the slower than expected performance in the food service channel, and obviously on the beverage side was impacted by excise tax.

From a geographic perspective we faced contrasted results in the UAE wherein increased demand for most of our products portfolio in response to COVID-19 did not offset the shortfall in each of bottled water sales, which really came from the food service channel, the close of restaurants and restrained tourism. In KSA, demand was compromised by the absence of the religious tourism coupled of us taking the cautious line on our credit sales after the challenges we saw with the bad debt coming from sales in 2019. Egypt and Kuwait operations reported good growth in respect of increase percentage of food and I think water business in Kuwait grew around 50%.

By channel, all markets witnessed a significant shift from out-of-home consumption to at-home consumption, so higher sales in retail particular modern trade vs traditional trade, E-commerce and Municipality channels. However, food service and convenience stores were the most impacted from lockdowns in the first half of the year.

Let's now look at the results of our 3 segmental divisions, starting with water and beverage segment, where sales came in at AED 799 million. In the UAE, our 5-gallon water business recorded strong growth in volumes and sales on higher demand particularly from homes which overcompensated headwinds in the corporates channel. On the bottle water sales; on the other hand, we had a decline the volume which was almost totally driven by the loss in the food service channel. We started to see food service improve in the second half of the year, but obviously it was lower than we expected as the covid situation continue to sustain. Kuwaiti operations registered 31.5% year on year growth as we continue to expand our market share. KSA was hit by the movement restrictions particularly in H1 never the less as part of our continual efforts to put KSA operations back on track, we now established promising distribution contracts with key clients, and we saw a change in the overall organization with our recruitment of head of international, head of finance, and head of sales in the market. So, that gives us a good platform as we start to see our business turn around in Q4 and get back to growth. As for beverages, the implementations of excise tax along with the closures had a negative impact on overall sales. We also agree proactively with our friends in Capri Sun to end the license and agreement at the end of December 2020, and taking the business back on January 2021 which we had a smooth exit in that regard.

If we looked at water market shares, Agthia overall has been able to sustain the number one position on volume basis led by the Al Ain band. If we look at the table on the right we see that we will be able to expand that share by 49 bps which is a testament on the overall performance of the business in spite of the category declining by 10.9% in 2020 vs the previous year. Bear in mind the charts capture the retail data which is modern trade and traditional trade and it does not cover all the channels that we operate in.

If we went to the food segments across different segments this falls under the consumer business. We had sales around 327 million increasing by 32% VS the previous year. We saw a remarkable growth driven by both the change of the consumer habit and the consumption in e-commerce business. The food segment continues to shape its portfolio, and its growing contributes in the P&L. Trading items which recorded the revenues 26% year growth, as we capitalized on the response of the covid situation, we immediately opened additional channels, we added SKUs, and we also are very proactive in activating home delivery orders, and we put hundreds of trucks on the road, and we also setup a drive through facility for consumers to be able to collect the goods in a safe environment. In tomato paste and frozen vegetables, revenue from UAE and Egypt grew by 41% vs prior year, as we continue to expand to the catering business, but also we had a good response in terms of market share and distribution, and obviously we benefited from the overall category growth as those consumers bought more. Bakery business tripled as we stepped in to support the increase demand for essential food. On dairy we actually managed dairy business and we faced challenges and we managed to reduce our losses, and despite topline pressure we improved our mix, so the margins improved and that impact reduce the loss on the bottom-line, and we continue to look on how we can improve and move forward. So, in terms of our profitability, food segment margins continue to enhance on higher volumes, and also our improvements in supply chain.

Moving on to the Agri business, I think it is a good year for the agri business overall particularly from a flour perspective. Flour segment shows growth for 11% VS the previous year, driven by higher domestic demand particularly in the retail space and also export sales, specifically by a world food program in the first quarter of 2020. On the other hand, animal food continues to be flat VS the previous year despite the drop in local demand amid further controls to restrict commercial farms from a subsidy perspective. That is really it for my side. Now pass over to Ammar to tell you a bit more of the detail from a financial perspective. Over to you Ammar.

Ammar Al Ghoul: Good afternoon everyone.

Group revenues grew by 1.1% y-o-y reaching AED 2.06 billion in 2020. Net revenue contribution by consumer-businesses reached 55 percent whereas agri-businesses generated the remaining 45 percent.

Consumer-business revenues came in at AED 1.13 billion out of which the Water & Beverage segment posted sales of AED 799 million and Food segment the remaining AED 327 million. The rally in each of the Food segment, Kuwait operations and 5-gallon water business was largely offset by the slip in Bottled Water sales in UAE & Saudi and beverages.

Agri-business revenues recorded AED 935 million and grew by 5% y-o-y on higher Flour sales as elaborated by Alan.

Moving on to the next slide where we show Group gross profit margins.

Current quarter gross margin came in at 32.7% versus 33.0% in Q4 2019. This translates into full year gross margin of 31.1% versus 32.2% last year.

We managed to enhance our gross margins over the course of 2020 closing at 32.7% in Q4 vs. 29.9% in Q1. We highlight that the collaborative team's efforts led to the Water margin improvement by 79bps despite lower sales specifically to the food service channel which was down 34% vs last year, equivalent to AED 48 million lost sales.

All in all, we managed to enhance gross margins of full year 2020 versus same period last year across all categories except beverages on excise tax implementation. Each of the key categories which aggregately constitute more than 95% of total revenues recorded better gross margins. Nevertheless, group margins went down on (i) sales mix tilted towards lower-margin food segment (being at 29% of total consumer sales vs 22% in 2019) and (ii) lower beverage volume.

Next let's talk about Net profits.

Group net profit prevailed at AED 34.5 million for the year 2020. Operationally, profitability was impacted by the consumer-business unfavorable sales mix and the group-level extra manufacturing and logistics costs borne to guarantee business continuity specifically in the first half of the period. Strategically, the management decided to adopt a prudent policy to encourage cost savings initiatives across our value chain and take the lead in recording all foreseeable impairments deemed necessary to improve the long-term quality of earnings.

Excluding the AED 82 million one-offs recorded in Q3, net profit shortfall will be radically reduced. This will be further explained shortly.

On the following slide, we are showing top-line waterfall reconciliation between last year and this year.

AED 39 million related to WFP Flour order have slightly countered the lost revenues against lower volumes of beverages on excise tax and of bottled water in both UAE and KSA on restricted demand from struggling food service segment and tourism amidst COVID-19. Nevertheless, robust growth momentum across our Flour and Food segments, Kuwait operations and 5-gallon water business resulted in the additional "organic" growth, taking our net revenues to AED 2.06 billion.

Moving on to profits. In addition to the resulting impact of the above items on bottom-line, we highlight 3 key variances. We recorded AED 22 million of additional profits from enhanced operations along with the improved efficiencies across our value chain which slightly countered the one-off adjustments which are shown in the next slide.

As explained in Q3 results call, Agthia has taken a strategic decision to improve the long-term quality of earnings and to strengthen our balance sheet. As a result, total impairments booked in 9M'20 amounted to AED 82 million. These include (1) AED 58 million bad debt provisions plus AED 7.2 million net inventory provisions, both following a thorough review of our receivables & inventory outstanding balances, (2) AED 9.5 million impairment of Capri Sun assets and inventories after signing a mutual agreement to end the licensing arrangement and (3) AED 7.7 million one-time accounting adjustment upon changing the payment / collection process of consumer sales in our community support division.

On a like for like basis, net of such one-off adjustments, our normalized net profit would prevail at AED 117 million.

With this we conclude today's prepared remarks. The floor is now open for Q&A. Thank you.

Hatem Alaa: Our first question comes from Nishit Lethotia from SICO. Nishit, please go ahead.

Nishit Lekhotia: Thanks for the call. I have a couple of questions, first on the agri-business given that there is increase in commodity prices how you see that affecting your business currently and if you can give any idea on the competition as well that you are seeing the low competition from Ukraine flour. So how is the market now? any idea on that will be helpful. And on the feed side more on elaborate on the controls on the subsidies that are affecting the feed. What exactly are these and how do you see this is going forward in 2021. My second question is on the Nabil acquisition when are you targeting to finish this acquisition. on the timelines any guidance will be helpful and on the dividends it seems that agthia given close to 100% to dividends in terms of their profit. So going forward do we expect as generous dividend policy as 2020 and if you comment on that will be helpful. Thank you

Ammar Al Ghoul: Thank you for the question.
On Nabil, we are running in a full speed to finalize the legal formalities associated with closing the deal. we reached an advanced stage soon we will announce the EGM date in which the transactions will be presented to the shareholders for a final approval. So reasonable expected closing month will be early May 2021.
When it comes to dividends, this is a very good question. As a matter of facts, for the last 4 years we have been distributing 15% of our share capital as dividends equivalent to 15 Fils per share so from a cash flow perspective available cash as well as borrowing capacity for future expansion in a non-organic basis we did number of mathematical calculations and then the management concluded and presented to the board that we do have the capacity to distribute with the same levels have been distributed at least at the past 4 years. And then a decision was taken to improve the dividends payout ratio from dividend per share perspective by 10%. so we have increased it from 15% per share to 16.5%. This is a clear demonstration of agthia's strong balance sheet, strong management of cash flow and a clear policy to reward the investors and share with them agthia's profit as we generate them rather than waiting one full year to announce them and pay them. Hope that I answered the questions you asked.

Nishit Lekhotia: Thank you so much.

Alan Smith: On your first question, it's been seen that a recent increase in the commodity prices globally and the way we focused on that is what we see by looking at our pricing in the market. And continuing what we did in 2020 to focus on cost. So our incentive is obviously to make sure moving forward to sustain our profitability from that perspective. Accommodating prices and productivity to optimize or maintain a margin from the bottom line for flour business. In terms of the competition at the moment in terms of anything that has link to the market as most of the competitions that we see in the UAE is between local supplies. So at this time no major issue from that side but of course the price increases relatively so we have to see how this applies in the course of 2021. On the feed side, the government is trying to change the policy with the commercial farms in terms of subsidy and having to make sure that they look to the cycles that they ran for each growing cycle for the animals and adjusted the way they are paying out on more usage basis not volume basis. The impact of that was the farmers becoming more efficient and consequently have bought less. This is from the subsidized channel. Hyper market sales for feed on the other hand continued to do well, Agrivita brands are extremely recognized in the market and nutritional profiles of our products are scientifically tested. The fact that we have number one share is a testament of our quality of feed. Our agri-business has a good deal with the head winds and that demonstrates what we did with flour in the recent years as subsidies get phase-out and were able to continue to maintain performance on these categories.

Hatem Alaa: Thank you again. As a fast reminder, to ask a question you can either click on the raise hand button on the right hand side of the screen or you can type in the Q&A. You can either click on the raise hand button or type on the Q&A chat. We have a question from the line of Alok Nawani. Your mic is open.

Alok Nawani: Good evening gents and thanks so much for the call. Just a couple of questions from my side I just wanted to understand when is the consolidation of the incoming assets expected and also what their performance been like during the covid environment in 2020 like for like basis. And also how they are trending as we speak

Ammar Al Ghoul: So we started already the statutory consolidation of Al Foah because the deal was closed very much at the very beginning of January 2021. So we will capture their PNL items line by line from that date. As for Faysal's bakery in Kuwait, statutory consolidation of PNL will start from February-1 more precisely from January 26-2021. For Nabil as we expect to finalize legal formality early May so most probably from May-1-2021. Just to bring to your attention and to the other audience attention that for Al Faysal and Al Foah there will be no dividends distribution so whatever earnings is available on the balance sheet credit side will ultimately end up consolidated with agthia. So even for Al Faisal the month of PNL statutory consolidation that will not come to agthia will ultimately end up in the equity of agthia but will not be routed in the PNL.
As far as the performances concerned, as every food and beverage business they went through some difficult times particularly when it comes to sales to catering services but what we have seen from resilience and ability to compensate the sales into different channels makes us confident as there will be no impact on the valuations because we have to seen covid 19 impact while we were still studying and going through valuations and due diligence at least as for what we have seen so far there was no significant impact on the earnings.

Alok Nawani: Ok fair enough. Would you allow me to comment on how leverage profile looks now after you adopted all the measures

Ammar Al Ghoul: We concluded two transactions and we are about to conclude the third one. AlFoah was acquired for value approximately 450 million dirhams fully paid by issuing shares to the sellers ADQ. There was no really any impact on the balance sheet from leverage perspective to the contrary improved the equity side of the business and the assets side of the business. Particularly that Alfoah came in with a net debt of positive 120 million dirhams which we pulled out immediately to Agthia treasury investments. So it improved the equity and improved the cash with no debt whatsoever. As far as Alfaysal, as part of the deal significant leverage buy out debt was already on the balance sheet that we have paid in full. So again Alfaysal came in with very small amount of debt. The acquisition itself was financed by debt from local bank in UAE at a very accretive long term financing arrangements.

Finally for Nabil, the transaction will end up with agthia owning 80% of Nabil, of which 60% will be paid through issuing shares to the sellers ADQ and 20% to the current shareholders of the company or the minority shareholders with the value of approximately 130 million dirhams which will be financed in debt. So all in all posting the conclusion on the three transactions and on high levels calculations of borrowing capacities I believe we still have a range of 1.2 to 1.4 billion debt capacity up to 1.5 billion as well on a 4 times net debt to EBIDA

Karim Jetha: Hi everyone. Thank you very much for the call. I just wonder if you giving a kind of guidance for this year.

Alan Smith: So I think the way we look on 2021 obviously the strong performance in quarter one in 2020 will not match 2021 quarter 1 as we had good sales in Jan-Feb last year plus some panic buying in March as the lockdown commenced. With the vaccines roll out, we would expect we will be optimistic. I think we will not give any guidance as covid continues to have inflow. We saw some come back in our food service channel in the end of 2020 and in January this year but of course with the restrictions that were announced in the UAE it started to slow down again, in Kuwait we had a reasonable start on the year and then across they announced curfew. Even in Saudi Arabia there were lockdowns and then in a couple of days they are reopening it is a bit volatile at the moment. So I think your question had been answered. It is too unpredictable to say in this point.

Hatem Alaa: We have a question from Nawaf Masri. Can you elaborate on your operation efficiency and cost optimization initiatives?

Alan Smith: Obviously given the unavoidable costs in the first part of the year driven by need to be agile and to protect supplies with interconnected costs in terms of warehousing and the distribution to make sure that we can service the market. We have some Incremental costs in the first part of the year but we continue to focus both organizationally to make an efficient supply chain and how we can make savings. If you have a look over the last 3-4 years savings of around 200 million which demonstrates our ability to continue to drive efficiency in the business. In 2020, I think we achieved around 40 million of savings. so a great effort across the business units and it is just our response you know to the reality we saw in the market with pressure on the water categories. We had to adjust our business in Saudi Arabia to reflect the business to be optimized over our heads to put it in sustainable platform to get back to growth.

This was the key moving forward to focus on being more efficient not cost cutting. So giving at the end we have with the new businesses coming through obviously we were focused on costs but also getting the benefit of the management talent from the new organization that we are bringing in. it was a great effort In the last year and we will benefit from the increased scale of the business

Ammar Al Ghoul: We also clearly distinguished between what is nice to have and what is must have. we really negotiated a lot of service contracts. we reduced significantly some of the costs, we extended the payment terms, manage carefully the cash flow, we managed carefully the available funds we have in our balance sheets so in a tough times in the last year on an average of 600 million in our balance sheet we managed to generate approximately 9 million of interest income. So we left no line in the balance sheet without improvement from the cost avoidance whether from efficiency, accelerate collection so we have seen a drop in receivables aside from the provision on a gross basis and the extension of the payables. So collectively it made quite healthy difference of the PNL in the balance sheet of 2020.

Hatem Alaa: Thank you. No more questions

Alan Smith: Ok thank you everybody. We appreciate the continuous interest and we look forward to talking to you in the next quarter