

TOFAŞ TÜRK OTOMOBİL FABRİKASI A.Ş.

**TOFAŞ Türk Otomobil Fabrikası A.Ş. First Half 2018
Financial Results & Key Performance Indicators**

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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, congratulations on very good numbers, and thank you for taking my questions. So my first question is on the price increase, Erman mentioned that Tofaş was ahead of the market, maybe could give some color, what was the price increase for Tofaş and what was the general increase for the market in the second quarter of this year?

RENZI F: Good afternoon, Fabrizio Renzi, speaking. So as Erman specified before, we decided not to defend our market share on the local markets. So basically we decided not to jeopardize our profitability, so if you have... if you want to have the measure of this, we registered in the first part of the year an inflation close to 15%, and the evaluation of almost 18%, we increased the price in the first six months for a value that is close to 14%. So in this moment, we have a lack of around 4%, 5% compared to the devaluation of the Turkish lira. And so, we decided not to jeopardize our profitability on the local market.

For the remaining part of the year, the expectation is to see the market to recover some position starting from September, and we will consider, let me say our price approach a month-by-month checking carefully which is the trend of the currency and also the trend of the market for the coming months.

BESPALOV V: Thank you very much. My second question is on your margins. Again, you mentioned that there was an FX effect definitely and

cost optimization. If we compare the EBITDA margins, for example, in the first half of this year and in the first half of 2017; how much would you attribute to cost optimization which I believe is sustainable and how much to the Turkish lira depreciation of the margin increase?

RENZI F:

Okay, Fabrizio Renzi, again. We confirm and what we said in the previous conference, so from 11%, 11.5% of EBITDA, EBITDA is something that we consider achievable and our...let me say normal result, so any time you see something above these is due to the extraordinary devaluation of the exchange rate. This happened for example in the second quarter in particular, so the 12.6% that we show in the second quarter is something that is partially due to the sharp increase of the Turkish lira.

Basically, the cost optimization now is inside this 11%, 11.5% that we consider as stable target...as stable achievement. So anytime you see something more than this, is due to strong effect of the Turkish lira. Why I mean that the...the cost reduction project is something that is normal because basically it's a project that started two, three years ago and we continue to carry home this project with the similar target that is this year is similar to the previous year is around...is more than €200 per car.

So obviously this project is not a linear project, so you could have let me say some improvement in one month, and some other improvement higher or lower in another month, but on a yearly basis this 200 euro is more or less what we expect from this project. And this bring us to this 11%, 11.5% that we

consider more or less our achievable target, a sustainable target.

BESPALOV V: Thank you. Thank you very much, but as a follow-up to this, maybe for example, first if we see let's imagine some sharp appreciation of the Turkish lira. Will this negatively affect your margins? And on the cost optimization, I mean, the margins that you mentioned as sustainable, 11%, 11.5% are pretty good, but do you see any scope for further improvements through cost optimization?

RENZI F: No, more than what I explained before, so more than €200 per year is something that is not achievable, so I consider this is maximum that we can achieve in one year. It is a real good, it is real great result believe me.

BESPALOV V: Okay, thank you very much. And the last question, I have on your export in particular the breakdown by country. As I looked at the slides that you presented, there is not that much of diversification in terms of overseas markets, export destinations. Are you working on this, are there any potential markets so you could penetrate, and increase your capacity utilization on exports or the markets are more or less stable where you are present?

RENZI F: Okay, you are talking about the Chart #16, obviously there is no big change in the main markets except for the decline of the UK that is due to the Brexit as Erman specified. We are seeing some good improvement in the North Africa markets, and for the other it's not so visible in the Chart, but we are following carefully the good result of Tipo in South Africa. In particular

the car is performing very well in Morocco, and in Egypt. This is not visible unfortunately in the pie chart, but we are following carefully the interest of this...of this specific market. Also the result in South America is something that we are following carefully also for the future evolution of the Tipo family, for the future years.

BESPALOV V: Okay, thank you very much.

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

KILIÇKIRAN H: Thank you for the presentation. My question is related to your CAPEX, you mentioned that you are going to start the CAPEX cycle in 2019 and we realized that you get some investment incentives actually. Is it possible for you to share more color about your CAPEX plans for 2019, such as, what could be the size of this CAPEX and which products will be considered to be renewed?

RENZI E: Okay, first of all let me clarify the trend of the investment this year that has been mentioned during the presentation, is decreasing a little bit. We are paying particular attention to the cash generation and this is the reason why we start to be more strict in the approval of the new investment. So this is the reason why we have a slight decline of the investment. And also we are particularly following the local market, so this is the reason why we review a little bit the 2018 guidance. Above 2019, we expect to see the investment go up. My expectation is to have an amount that could be around €200 million.

In this moment we cannot speak about the future projects, but more probably end of 2019 this number...so the investment in 2019 could be affected by the new generation or the starting of the study of the new generation of the Doblo. So the expectation is to see in the second part of 2019 this number grow again like in the previous years.

KILIÇKIRAN H: Thank you very much. When you...I mean, when I look at the investment incentives that are approved it seems like that it's an approval for a potential capacity expansion. Is it something like capacity expansion on a product or is it capacity expansion on the plant?

OZDEN D: Hello it is Dogu, so as to the incentive document or the incentive application that started up last month was mostly about structural investments, not the product or specific product development or R&D investments, but to structural side of the plant also structural side of the R&D. So we cannot say it is for a new product.

KILIÇKIRAN H: Okay. Thank you very much.

OPERATOR: The next question is from the line of Kayani Muneeba with Morgan Stanley. Please go ahead.

KAYANI M: Hi, thanks for the call. So going back to your export volume guidance, what risks do you see...from your exports from the slower demand that we are seeing in Italy in recent months?

RENZI E: Okay, first of all let me clarify that despite the decrease compared to the 2017 our numbers about...regarding...about

export are close to our budget...our expectations. So we decided also for the coming period to confirm our guidance. To be honest we are more close in this moment our visibility, bring us close to the lower...the lower range...the lower number of the range indicated in the previous guidance. So in this moment we decided to confirm the guidance

Obviously, we are following the European markets that in this moment is positive, but what we are following is also the trend of the Italian market that is very important for our export, as you have seen before; more than 40% is Italian market.

So our concern is related to the performance of the Italian market in the second semester. For the moment, we are close to the lower part of the guidance, so it really depends from the performance of the Italian market. But in this moment, for the passenger car, it's showing some weakness. But in this moment, we are confident about this guidance.

KAYANI M: Thank you. So as Italy turns out to be much worse than expected, then there would be risk to the guidance that...to the guidance for exports. But for now you are comfortable?

RENZI E: But for now, the number confirms the guidance, as I mentioned, we are maybe closer to the lower part of the guidance. But for the moment, we confirm.

KAYANI M: Thank you. And can I ask little bit on the investment plans. So what are...so the facelift of Doblò is on the pipeline? And then, when would you be looking to do a facelift of the Tipo. And also

if you could give an update on any additional capacity plans, which were being considered outside Turkey?

RENZI E: Starting from the last question, in this moment in term of production capacity, we are not planning anything. So with the production that we have...with the level of production that we showed during the presentation, we are at the 80% of the utilization of our capacity. So in this moment, as we mentioned also in the previous meetings, we are following a possible deal out of Turkey.

But in this moment, it's really difficult because the change of regulation in some countries, in particular in North African countries make this exercise very, very difficult. So start operation in this moment, in this area, that is an area for sure, we are interested on, is very, it's very, very difficult.

About the Tipo MCA, might be, I will leave the stage to Cengiz because the situation of Tipo is...

EROLDU C: Now, but regarding the investments, now as you know, a couple of years ago, we made huge investments for the launch new passenger car family. Our new investment cycle, we have, this will be in 2020, but I can...as also Fabrizio mentioned before, so we will start to spend some amounts in second half of 2019.

For this season, our guidance...possible guidance, the huge portion of the investments, we can forecast for 2020 and 2021. And we will see also some...possibly we will see also some impacts at the end of 2019, if I understood, correctly your question.

KAYANI M: And that will be mainly for the new Doblò or will that also include the facelift of the Tipo?

EROLDU C: Both, but mainly because...let's say Tipo is a facelift, but Doblò will be the brand new.

KAYANI M: Thank you.

EROLDU C: You are welcome.

OPERATOR: The next question is from the line of Dasiran Akif with TEB Investments. Please go ahead.

DASIRAN A: Hi, thank you for the presentation. My question is raised with your consumer finance business. Refereeing to your previous comments, it was you know, used to be seen as a marketing tool and considering the weak market demand in Turkey and increasing financial expense and cost of funding, do you expect any change in your strategy or do you see any risk in the consumer financing business in the second half? Thank you.

EROLDU C: Thank you for your question. So as you said, for us our captive company is a important tool for our activities in the Turkey market for...they are supporting the sales performance of the company. We also... at the past meetings always underlined that, the only risk that we are carrying in this captive company theoretically are the nonperforming loans because we are not borrowing money in hard currency, so we don't have any mismatch both from the currency point of view, also from the timeline point of view. So all our businesses are from this

perspective not carrying risk. So until now we are not seeing and also increase on the nonperforming loans.

We are continuously following the situation, but I can say that we are better shaped compared with the banks in Turkey, and also other captive companies. We don't see also problem on the borrowing side. Of course, we are facing also increases on the cost side, but still in Turkey, the financing campaigns are important drivers for the sales.

So I believe also now this to own a captive company is a much more competitive advantage than the normal conditions, so we will continue to support the Fiat sales in Turkey which are captive.

DASIRAN A: Thank you.

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

KURBAY B: Good afternoon. Thank you for the call. I have got a couple of questions. My first question is about market shares. You mentioned that in the first half of the year you focused on profitability; and market share...overall market share in Turkey is down by about one percentage point to 11.1%. What is a sustainable market share in your opinion going forward, not just for this year, but if you look into 2019. What would be a level that would make you happy? That's my first question.

And I have a couple of questions on the export side. The first one on the export side is that in the first half of the year you

shipped around 9,700 units of Dobló for Opel Vauxhall. Are we going to see a similar amount in the second half of the year or is this contract practically completed now.

My second question is, you also mentioned that you will be at the low...probably closer to the lower end of the exports guidance which is around 270,000 units. Going into 2019, what are your expectations? Are you expecting any improvements in any of the markets that you are operating in at the moment or is it...would it be fair to expect at best flat unit exports next year?

And my final question is about the cost optimization program, if I understood correctly, it was mentioned that this program started two/three years ago, and the goal is to achieve cost savings of around €200 per car every year. So is this an ongoing program and should we expect similar efforts on cost savings going into 2019-2020 as well or is this program kind of at the end for this year and not...and we shouldn't be expecting similar gains going forward in 2019-2020. Thank you.

EROLDU C:

Thank you, Berna. First of all on the local market, first half we saw the increase on the fleet performance in the local market. So why we said that we are lowering profitability, because we are not so aggressive on the fleet side of the passenger car market.

Also my expectation at the second part of the year, we will see the lowering fleet market, because now they are facing, the fleet companies, they are facing with the financing...financial borrowing problems so for this season we reduce also our

expectation for the Turkish market. So for us sort of to stay also next year between 11% and 12% the market share, I think is a fair performance with the product range that we have in our hand.

KURBAY B: And would you expect the majority of the gains in market share going forward on the passenger car side or on the LCV side?

EROLDU C: For next year or this year?

KURBAY B: Next year.

EROLDU C: From market share point of view, I believe passenger car side, because now as you see we are also seeing a down...there is a down trend on the light commercial vehicle business, so also this is a another issue for our total market share because as, you know, we have the high market share on the light commercial vehicle compared with the passenger cars. But when the light commercial vehicle portion of the market is decreasing also this is impacting our overall market share.

So this year, the contraction of 1% market share we are seeing also the impact of this at the first half, because the light commercial vehicle side of the market decrease more than the passenger car side, so it is also mathematics. So for this reason, it's also to continue, with this performance also next year will be a challenge for us if the light commercial vehicle stays in this level or continue to shrink also 2019.

Regarding export, next year, first of all I should underline then the OPEL contract is going to end at the end of this year, also

second part of the year we will continue to produce for OPEL brand. So number also will be more or less similar to the first half of this year.

So regarding the export provision for next year, of course, is linked with several issues or we will see how the main European markets will move in 2019, but, of course will be a year for Tofaş without the OPEL contract. What was your...

KURBAY B: Cost optimization?

RENZI F: For the cost optimization if it is sustainable at this level..

EROLDU C: of course, to continue ever year with the same performance is not the case. So as Fabrizio mentioned also I also believe we did a good job, so we will continue, but not with the same speed, same levels.

RENZI F: Yes, but in terms of...okay, in term of cost reduction, we have basically two main sectors, one is value optimization that focus on the reduction of materials. So the €200 that I mentioned before is related to what we call cost optimization. But, also we are achieving good performance in terms of labor efficiency. Thanks to other project of automation, project that we call low cost automation.

If you have a look to the trend of our workforce also in terms of labor efficiency we are doing a good job, if you have a look to the footnote and it counts, you can rely is that, our production per day remains more or less stable but we are working with the

almost 700 people less compared with the beginning of the year.

So in the basket of the cost reduction project, we have the cost... material cost optimization or value optimization if you want to call, but we have other project...efficiency projects that could, let me say guarantee also for the future are good savings also in 2019.

KURBAY B: Thank you very much.

EROLDU C: Thank you.

OPERATOR: We have a follow up question from the line of Kayani Muneeba with Morgan Stanley. Please go ahead.

KAYANI M: I wanted to ask about, how we should be thinking about take on tax for the new Doblò investment, and are those discussions that you have started with FCA?

EROLDU C: Not yet, but of course as a Tofaş management our priority is to improve our contractual situation, but not started yet.

RENZI F: So, the actual contract...

KAYANI MUNEEBA: Do you expect another contract

EROLDU C: Sorry.

KAYANI M: Do you expect another contract for the Doblò?

EROLDU C: Yes, absolutely, we need to renew, we cannot continue with the existing one.

RENZI F: But the actual contract will terminate 2021. So for sure, we have time to.

EROLDU C: Yes, have also time.

EROLDU C: But, also to avoid any misunderstanding, we don't have yet any agreement with FCA also for the third generation of Doblò. So they,,,we didn't approve also the project yet.

KAYANI M: Is that...can you explain a little bit about how that process works in terms of when the contract negotiations will start, and is it after you decide on the third generation for the Doblò?

EROLDU C: Normally, we are working for the feasibility. Now, we are at the feasibility phase, so the parties will prepare their feasibility in the normal process. So after the preparation of the feasibilities, so we are going to prepare our feasibilities as Tofaş and it is...the FCA also is...and after we will just...we will discuss as we did in the existing...the contracts, is a normal process.

KAYANI M: Thank you.

EROLDU C: You're welcome.

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

BESPALOV V: Thank you for taking my follow-up question. I would like to ask you about the interest rate environment in Turkey, and how it

affects this consumer loan business in general. How do you feel, are the people more reluctant to take loans. ? How do you see the interest rates evolving. As far as, I understand, the full impact of this high interest rates environment is not yet fully reflected in car loans but the interest rates should probably increase further and how this might affect your KFK business? Thank you.

EROLDU C:

Welcome. But actually in Turkey, as other market, there is, let's say, a base interest rates. Now for example, for this week, this month, the base interest rates in the Turkish market is between 1.9 to 2.10, so we can see the bank captive companies and so on. But the transactions mainly are following the campaigns, now, because here the OEMs are supporting the financial, the financing campaigns. And in Turkey until couple of months zero interest rates campaign were very common.

But now due to the high cost because if you are making a financial campaign, I don't know for 50,000 Turkish lira for 30 months, now the cost is not anymore supportable by the OEM. So the battle is going on, so we are not making the zero rate campaigns, but we are making a 0.99% campaign. So customers are not seeing the base interest rate. But of course now in the market, we are not able to see a zero interest rate campaign anymore. So those are very rare, so for this season also for retail customers this means somehow let's say cost increase, which is impacting cost, so the retail demand in Turkey.

So for this is let's say one of the main driver affecting Turkish market volumes, one is the let's say the price increase is due to

the exchange rate increase and second one is of course interest rate increases that customers are seeing.

But as I said also before, so having a captive company under the control is an advantage because nowadays also the captive companies and the banks they are not willing to offer the loans like they did in the past periods, so they are much more selective and so on. Now... but for our customers, we are continuing to be in financing business. So that also I believe will differentiate Fiat brand in the Turkish market.

BESPALOV V: Okay. Thank you very much.

EROLDU C: Welcome.

OPERATOR: The next question comes from Memisoglu Osman, Bank of America Merrill Lynch. Please go ahead.

MEMISOGLU O: Hello, first of all my condolences for Mr. Marchionne's passing to you, the Tofaş family and Fiat and Chrysler family. My question is on the cost plus details. In an environment let's say where the domestic market really weakens, how is that cost plus calculated? In other words does the cost part include... is it for divided to capacity or to just export volumes? I'm not sure if that's clear enough?

EROLDU C: Yes, it is divided to the capacity, not the actual volumes or export volumes.

MEMISOGLU O: Okay, so you are protected from the perspective, if its profit volumes weaken, you will still get the full cost into the cost plus

for the export volumes.... Okay, okay. Thank you very much anyway.

EROLDU C: You are welcome Osman. Thank you.

OPERATOR: We have a follow-up question from Kilickiran Hanzade with JP Morgan. Please go ahead.

KILICKIRAN H: Sorry, actually it was one of the same questions that I was going to ask. So if Italy disappoints for example in the second half, can you please confirm that it's reasonable to assume that that we may not see much changes on Tofaş profitability trends in the second half and....

EROLDU C: I can say that until 2023, it will be difficult to see.

KILICKIRAN H: Yes.

EROLDU C: Changes on the Tofaş financials.

KILICKIRAN H: Okay, perfect. And the second thing is about your dividend policy. We know that you have a tendency to distribute the maximum dividends usually, but you are going to be in the investment cycle starting from 2019. Do you think that this...I mean is there any risk of lower dividends payout ratio in 2019 or you may continue to pay the maximum as much as you can?

EROLDU C: No, no we will continue...we will continue with our existing policy, so I don't see any risk on this.

KILICKIRAN H: Thank you. Perfect.

MANAGEMENT: You are 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, only two...few words to thank you all the participants. Thank you for the contribution. I hope you have appreciated the result and our explanation in the Q&A. So I wish you a nice weekend and I also wish you a pleasant summer period.