

TOFAŞ TÜRK OTOMOBİL F

TOFAŞ Türk Otomobil Fabrikası A.Ş. 20Q2 Financial Results Conference Call and Live Webcast

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Conductors:

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Conference Call Conducted by Chorus Call Hellas



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Q&A SESSION

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

BESPALOV V: So thank you for the excellent performance in the second quarter and for taking my question. I have actually 2 questions. First is on your CAPEX, and you have... reduction on your CAPEX again. And as I look at the breakdown of CAPEX in the first half of the year, the investments in the Doblò were not very significant. So, could you maybe provide some color how the project is going on, what is behind this CAPEX reduction and why the investments were so low in the first half of the year?

And the second question will be in the beginning of the presentation you have something like the expanded PG and Tipo family and some media reports are saying that you are going to expand it by I adding a crossover version, maybe you could provide some color on that as well? Thank you.

EROLDU C: Fabrizio, are you going to answer?

RENZI F: Yes, I can answer if you want. The connection was not perfect, but I believe I have got the 2 questions. I can start Cengiz and then you can complete, if you want. So basically, good afternoon, Vladimir, if you... can you hear me well.

So basically, the question is related to the investments and it's related basically to our new programs. Basically, we are working on 3 products and 3 projects. First of all, these

projects are in a different stage of course, so let me start from the closest one that is Tipo.

As I mentioned before, we are going to produce the first Tipo face lifting in October in the last quarter. For confidentiality reasons, we cannot officialize all the contract of the new car, but what I can say that in October, we are going to add one body type to our offer. In October we are going to offer 3 engines, 2 diesel engines and a new gasoline engine, but the offer will be completed in 2021.

So, let me say coming back to your first question, the size of the investments, the major part of the 150 million that we... includes now in our guidance it related to the spending for Tipo. Part of the spending has been moved to 2021 but the program remain unchanged, so we decide to invest €200 million as you know. But of course, we try to switch as much as possible the spending in 2021.

The second program is Fiorino but there is not too much investments this year, the postponement as a prolongation of Fiorino till 2024 will produce some spending next year. And then of course, the attention is related to Doblò. The situation of Doblò is a bit more complex.

We can say that the outbreak of COVID pandemic didn't contribute to the acceleration of the spending, on the contrary, the spending and the development of the new program is slowed down. This slowdown is due basically to the stoppage of the activity in Italy as a consequence of the long lockdown imposed in Italy, and in particular in the north

of Italy where they have this research and development center FCA is located.

But of course, the slowdown is also related and due to the tentative, to protect the liquidity of FCA for the second and the third quarter.

So having said that, and as a consequence of this, we can say that the possibility to launch the new Doblò at the beginning of 2022, that was an hypothesis that we have discussed in the past, is not anymore realistic, and we can assume that the more likely scenario is to see the new model in 2023.

In this regard, we cannot forget that we are in the middle of the merger between FCA and PSA. So, if during the coming months there will be some optimization, some opportunity I believe that's coming from the integration of a FCA and PSA, I believe that also this is in the interest of Tofaş.

So, coming back to your question in the €150 million, there is a small part that is related to Doblò, but if the program is shifted, it's delayed. And that's all from my side. And I don't know if Cengiz want to add something. I interrupted you Cengiz, very sorry.

EROLDU C: No, no. It's, okay. Thank you, Fabrizio.

BESPALOV V: Thank you very much for answering. Can I clarify one thing? Current Doblò contract expires at the end of 2021. The new... Doblò as you mentioned, right now will be launched sometime in 2023, what can it be in between?

RENZI F: Yes, this is a relevant question, Vladimir. So, the shift of the new generation of Doblò up to 2022 imply that we are investigating the possibility to postpone the life of the actual Doblò in 2022. As you know, the contract basically... expire in 2021.

But I believe it is in the interest of all the parties involved to guarantee the presence of the market of Doblò in 2022. This means that we have to upgrade our engine because in 2022 in the LCV segments, there will be an additional ecological step to the Euro 60 final. So, if this is the case means that in the middle there is an additional investment for the ecological upgrades of the vehicle.

BESPALOV V: Okay, thank you for the clarification. But if you [technical difficulty] it should be other or an extension of the current export contracts, right, for you to undertake the investments?

RENZI F: Sorry, I didn't get very well.... If the question is, if we have to extend the actual contract, yes, but I'm not sure if I got your question exactly, because my connection is not perfect. Please Mehmet.

BESPALOV V: Yes. The question was whether you will be expanding the current take or pay export contract for the Doblò for 2022, if you undertake the investments and keep this into 2022?

EROLDU C: Yes, most probably, yes, but still there is not decision on the subject.

BESPALOV V: Thank you very much. Very clear.

EROLDU C: You're welcome.

OPERATOR: The next question comes from a line of Demirtaş Cemal with ATA Invest. Please go ahead.

DEMIRTAS C: Thank you for the presentation. My first question is related to domestic market. I got the... here some color about fleet sales versus the consumer side, the retail side. How are they developing and how the leasing companies are acting in these times during low interest rate environment? So, could you give us some color on that front in domestic side?

And on international side, do you have any idea about the inventory levels in European markets? And are there any market specific indication that make you offbeat or downbeat for the future?

As far as, I saw you didn't change your guidance, but do see you an upside risk or downside risk to your estimates? Thank you.

EROLDU C: Okay, thank you, Cemal for your questions. So, regarding the domestic market, of course, the split of June and July were extraordinary. So also, we are at the last days of the month of July. So, probably we will see a market around 85,000 units in total. So, of course, we cannot compare with the last year, where the market was only 18,000 but you will remember 2019 July was the first month after incentives... incentive application on the special consumption tax ended in

June. And there were some rumors regarding the extension of the incentives, so for this season also.

Last year, the market was very, very weak, so this year what we are seeing in...particularly in this last 2 months that not only retail, but also fleet customers are very active. But we are seeing mostly daily rental companies and the small entrepreneurs in the market as a fleet site. But still the retail demand is very high.

So of course, this is... this is very promising for the coming part of the year. But last day we are facing the full fluctuation on the exchange rates, this can...if continuing this way, of course, it also can create some uncertainties in the local market also because as you know in Turkey to make the assumption in this period is not easy. So if you think from the positive side, there is a market with high demands, but there is some also question marks.

So regarding the export markets, you saw also from our presentation, our export in the second quarter was very weak. This was mainly, of course, the pandemic period, but also...all the OEMs in Europe, they also tried to reduce the inventories, because the cash management became the most important issue for the OEMs, we saw this example for some importers in Turkey. They dumped thousands of cars also in the month of May and June in Turkey, in order to clear their European stocks in the Turkish market.

So this is an upside potential for the Turkish industry, not only for us, but also for other exporters, because the second

quarter was sure a quarter where the attention was on the cash flow management and the... you are also following, there is some incentive declarations in different countries, in different types in the Western European countries.

Also, this shows an upside potential, but of course, always there is a risk also of the second wave, there is also pandemic. So like Turkey also Europe is...there is a upside potential, but there is also some risks. So that's how we are seeing this situation. Thank you for your questions.

DEMIRTAS C: Thank you.

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

KURBAY B: Good afternoon and thank you for the presentation. I have 2 questions. The first one is about the exports' guidance, which you maintained, and it's a pretty wide range actually. And I was wondering, in light of the scrap incentives in Europe, you're mentioning an upside, but...because this is a pretty wide range, are you thinking of this more in terms of you perhaps pushing the high end of this range?

And before these incentives, you were perhaps thinking that you would be at the low end of the range, because it's a very wide range, as I say. I was wondering if you could comment further on that?

And my second question is actually about the response you gave earlier, about... the question about the renewal of people and the crossover version. My line was bad, and I think I heard you say that you can share at this point that there will be 3 different engines. But is there anything more to that particularly on the... on whether you will be launching this crossover version? If I missed that, I'm sorry. And I would appreciate it if you could repeat that response.

RENZI F:

Okay. About the last question, Tipo, unfortunately, we cannot give you more color, because this is the request of the Fiat brands in Italy. So they have got confidentiality about the content of the new cars. There are a lot of rumors on the media, but I cannot comment more than this for the moment.

So most probably, the next quarter we can dedicate a specific part of the presentation to the new products, including the news that will come later on in 2021, because in October, there will be only the first launch of the new vehicles, but the full range will be completed in 2021. Sorry for that, but next time most probably we can explain something more.

Coming to the first question related to exports. Okay, we keep our guidance in parallel to the one we released in April. But I would like to restart from the beginning, so we started the year with realistic guidance. So, we started the year with 170,000-190,000 vehicles. That imply 10% down compared to 2019, so we started the year with prudent guidance over the exports. In the first 2 months, we achieved a very good and promising results.

In the first 2 years of the month... in the first 2 months of the year, we were 4% up, compared to the 2019. Then as you can imagine the outbreak of the pandemic changed completely the scenario.

Now once again, we want to keep a prudent approach. Of course, we hope, and we believe that the incentives introduced in the major countries in Europe could bring, could generate the revitalization of the market. But for the moment, we prefer to remain very prudent.

For example, in Italy, as you know, in August, we'll start a new incentive scheme. The new incentive scheme will focus on 3 different range of cars: zero emission, and this the maximum incentive that the customer could receive, up to €10,000. There is a second range that is basically the range from 20 to 60 gram per kilometer of emission, Co2 emission. So, the parts related to the hybrid cars in this specific range, together with the scrapping of the old car you can receive €6,000.

Then there is an additional range, that is the traditional power train, up to 120 grams per kilometers. And in this specific range, you can receive €3,500 of incentives. So, the most interesting part for FCA, and for us and for our project is this one. So, there is a...some version of people that is eligible for this kind of incentive. So, of course, we count on these incentives, and we hope to be at the upper part of the guidance, but for the moment, we prefer to keep this prudent approach.

Nevertheless, as you know from financial point of view, there will be any impact on Tofaş, since we are below the reserved capacity, so... but of course, the increased exports could bring some benefits in terms of absorption of the fixed costs. But anyway, there will be no big impact in the economic results of Tofaş.

KURBAY B: Thank you.

OPERATOR: The next question comes from the line of Kılıçkiran Hanzade with J.P. Morgan. Please go ahead.

KILIÇKIRAN H: Hello. Sorry, I was disconnected, so I'm not sure if this question was asked. But my question is related to our margin development and investments of the year. You have very high profit before tax margin in the second part of which was up to like 9.5%, and this is I think out of the normal range.

And so, how should we think the margin evolving in the rest of the year, given that you have a very strong export outlook for second half of the year. And is it possible to share some sort of insight in terms of numbers about your pay contracts impact on the margin this quarter, because I think this is the main part of that we see, the biggest impact on the pay contract. Thank you.

RENZI F: Okay. About the take or pay, as you know, we don't like...we don't give any guidance on the results. We don't like to give details about the take or pay simply because this is

confidential part of the contract and also is a kind of competitiveness issue with our partner, FCA.

But, of course, I can comment because the take or pay had an impact on the second quarter... big impact on the second quarter. As you can imagine, we have exported in the second quarter only 8,000 vehicles. So, you can imagine how big is the effect of the take or pay in the second quarter.

We are speaking about the pay amount, so the pay amount is the amount paid by FCA for the shortage compared to the reserving capacity. What I can comment is that this amount is composed by 3 items.

One item is the fixed cost; fixed industrial cost. So, this is a kind of reimbursement for Tofaş. The second is the cost of the investment financed by Tofaş, so 2 components of the take or pay basically are costs that has been reimbursed to Tofaş. So, without any effect on the marginality.

Then there is an additional component that is marginality and the markup. But of course, I cannot comment the exact detail of the take or pay. I would like to give only an additional explanation. The take or pay is not linear during the life of the vehicle, is not linear during the year, also the components are not linear during the year, so the fixed cost is not the same every month.

So, having said that, I believe that our result is the demonstration that the take or pay is full operative. I remember the last quarter I got the question if under this

unprecedented period take or pay is operative or not, and the second quarter demonstrate that the contract is fully operative. So, this was related to the take or pay. I don't remember the second question.

KILIÇKIRAN H: I just wonder, I mean this 9.5% profit before tax margin. As you said, majority of it is resulting because of a high pay side of the contract. So, but in the second half, you are looking for a strong rebound, in the export and I can see from your guidance. And so, is it normal to assume that this will go back to around 8, 8.5 by the end of the year or we will still see a very high profit before tax margin in Tofaş in 2020?

RENZI F: As you know, our sustainable level is always 7%, 7.5%, so this 9.5% is really a seasonal effect, I believe that never in the future we will experience this kind of quarter, so we keep our...

KILIÇKIRAN H: One off?

RENZI F: Yes, absolutely.

KILIÇKIRAN H: Okay. But since you are still going to have higher domestic market share in the overall revenues and there should be lower exports versus last year. So, you can still exit the normal range on the profit before tax in 2020, I guess. Am I right in terms of thinking?

RENZI F: Yes, for sure, we can expect some upsides, some increase of the normal PBT because of the local markets increase...local market performance, even though this is not...this is not so

easy, because the competitiveness in the local market is very high.

So, let me say the mix is evolving in a favorable way for us. So, the mix is moving to LCV and this means that we can expect a better profitability. But on the other side, we have to remind that the COVID-19 increased and produced extra cost that we have obviously to take into consideration.

So, for example in the second quarter, I calculated that the cost of the car increased by €100 only because of the... the saturation of the fixed costs and because of the extra cost and measures implemented for the COVID. So, of course, there is the expectation to have a good financial performance coming from the local market's, but it will be challenging also.

KILIÇKIRAN H: All right. Thank you very much, Fabrizio.

OPERATOR: Our next question comes from a webcast participant, Maria Kolesnikova with Millennium. The question is and I quote, thank you for the presentation, 2 questions from my side. First question, could you please talk about the pricing environment in the domestic market so far? And your view for the rest of the year 2020 especially given strong rebound in the domestic market? Will you be able to increase prices in Q3 and Q4 2020?

Second question, could you please remind again the timeline of the government incentives for the domestic car purchases last year and this year to better understand the base effects? Many thanks.

AGYUZ M: Hi, Maria. Thank you for the question. Regarding your first question in terms of pricing. In the first half, we were able to fully reflect the cost of equal Lira to our prices and we have done double-digit price increases year-to-date. And we have been quite... actually 2, 3 times we had some price increases. So, we are following any cost increase and reflected to our prices.

And also, given the very strong demand at the moment, we should not have any problems in terms of reflecting any cost increase to our prices in the domestic markets for the rest of the year.

Regarding the government incentives, it started last September. I am assuming you are referring to the state banks incentive for local cars, and it is no longer valid as of this week and most of the major car players are no longer eligible for this program. But, let me add one more color on this one. The penetration of the state bank loans in our loan portfolio is quite low. I would say in single-digit levels.

Of course, that may still have some psychological ramification on the consumer behavior, but overall, so far, the penetration is quite low, it mostly has an impact on consumer behavior in terms of driving showroom traffic at the beginning of the incentives.

On the other hand, considering the very favorable financing rates at the moment, it hasn't had a big impact compared to last September when it was first introduced.

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: Thank you, Operator. So, we came to the end of this session. I would like to thank you all the participants and thank you for their interest in Tofaş. I wish you a good day and a good summer period. Keep in touch for the next session.