Transcrip ion for MAVI GIYIM

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Corporate Participant

Cüneyt Yavuz
Mavi – CEO

Presentation

Operator
Ladies and gentlemen, welcome to Mavi's First Quarter 2019 conference call and webcast.
Sir, please go ahead.

Cüneyt Yavuz
Hello, welcome to our conference call regarding the financial results for the first quarter of 2019. I will be taking you through our operational and financial results for the quarter. During my presentation, I will provide insights on the current trading environment and our expectations for the rest of the year. Also, I have already received some of your questions and I will try to answer them throughout the presentation. Should you have any further questions, I will be happy to answer them at the end of our call.

Before going into the key highlights for the period, I would like to take you through on what we experienced in the first quarter in terms of market and consumer trends specifically in Turkey.

We are seeing three very different dynamics playing out during this quarter. February turned out to be a month in which the retail fashion brands were offering deeper than normal discounts, indicating that they have heavy previous season carry-over inventory. This environment impacted our sales adversely and we closed the month below our budget target. March was the entry to the spring/summer season and we delivered in line with our targets. We had positive traffic growth and like-for-like growth performance was above 25%. April, on the other hand, turned out to be another challenging month where customer traffic and conversion were much weaker than expected. This, we believe, was partly due to weather conditions with one of the coldest April's in history, coupled with the uncertainties of elections. As of May, we are back on track to strong sales performance with month-to-date like-for-like well above 25% trending on positive transaction territory.

Therefore, it is important to note that we do not see the first quarter trends to be fully indicative for the year and we are sticking to our initial guidance for 2019.

Overall, year-to-date performance on our denim category is up in volume terms highlighting the strength and resilience of Mavi as the jeans brand of Turkey. Another encouraging fact is that our spring/summer ’19 woman collection is performing strong with positive sales growth in volume terms.

Now, let’s start with slide two on the key highlights. As you know, we have started applying IFRS 16 reporting standards as of this quarter, however, throughout this presentation; I will be sharing the results without the IFRS 16 impact to provide a more meaningful comparison with the previous year. You may find the full IFRS 16 impacts in detail in the appendix of the presentation.

In the first quarter of 2019, our consolidated revenue grew by 21% to TL 648 million. EBITDA grew by 2.3% to TL 74 million, resulting in 11.4% EBITDA margin, a 210 basis points contraction compared to the same period last year.

In addition to product costs and operating costs, as you are all well aware, financing costs are also significantly higher than the same quarter previous year, hence net profits for the quarter contracted 39% year-on-year to TL 15 million. We continue to be prudent in store opening decisions. We opened three stores and closed three stores, resulting in no net openings this quarter. As of end April, we have 300 own-operated stores in Turkey and in total, 425 monobrand stores globally, including franchisees. Mavi Turkey retail delivered like-for-like revenue growth of 15.5%, and as a loved and trusted brand, we continue to acquire new customers in 2019. We now have 5.4 million Active Loyalty Card Holders that have shopped with us in the last two years.

Moving onto slide three. In the first quarter of 2019, global revenue grew by 21% reaching TL 648 million, out of which 54.8% was in retail, 37.3% in wholesale, and 4.2% in ecommerce. As a result of our efforts and focus on our online business, we are happy to report a solid 114% sales growth in the first quarter coming both from www.mavi.com and Marketplace sales. Sales in Turkey grew by 19% compared to the same period of 2018, with 20% growth in retail, the main driver of our domestic business. We are excited with the achievements of our ecommerce business in Turkey that grew by 100% year-to-date in 2019. International market grew by 32% in Turkish lira terms. As you are aware, we have been closing down retail stores in Europe since last year, where we target future growth to be driven mainly by wholesale and online. In line with this strategy, international ecommerce sales grew by 132%, reaching 10.4% of total international sales in quarter one 2019.

Moving onto slide four, let us focus a little deeper on Turkey retail business. Given the uncertainties and increased cost of capital, we reviewed all of our investments on efficiency basis and guided for net 15 new store openings and 10 expansions for 2019. We are holding onto our guidance. We have closed two inefficient stores plus the Ataturk Airport store this quarter, and opened three new stores, two of which are in the new airport and are relatively smaller in square metres. Additionally, four stores went through expansions. As of end April, we maintain 300 own-operated stores, over 149,000 square metres of selling space in Turkey, with an average store size of 498 square metres. As a result, Turkey retail revenue growth of 20% was mainly driven by like-for-like growth in the first quarter of 2019.

Now, to elaborate further on our like-for-like performance, let's move onto page five. Our like-for-like growth in the first quarter is at 15.5%. Since the second half of last year, given the cost inflation and the need to reflect this to pricing, we have been reiterating the fact that like-for-like growth in 2019 will be driven primarily by basket growth. As per our plans, we delivered a 25% growth in basket size in the first quarter. It is worth noting that this basket increase is in line with the market and we continue to maintain our right-price-positioning in the Turkish apparel market as per our strategy. What was unplanned and we believe will not continue to be the case for the rest of the year is the 7.8% contraction on the number of transactions. Weak consumer confidence along with late season opening due to weather conditions had a negative impact on both traffic and conversion rate. As we continue to offer the right product at the right price and continue to deliver an excellent shopping experience, we will continue to retain our happy shoppers as well as gaining new Mavi customers.

At this point, I would like to repeat that our like-for-like sales performance as of May is back to well above 25% levels, with positive transaction growth.

Now, let's take a closer look at our category-based performance and move to slide six. As I mentioned in the beginning of the call, our denim category continued to achieve positive sales volumes and grew 21% in value in the first quarter of 2019. It is worth noting that women's jeans sales were the strongest among all categories in this period. We witnessed the impact of colder weather and a late start of the season, mainly across the lifestyle categories, especially on shirts and t-shirts. The knit category, which consists of t-shirts and sweaters grew by 20% in quarter one 2019, shorts 12%, jackets 23%, and accessories 18%.

On slide seven, we want to highlight our online growth performance as this channel now has a significant and growing share in our total sales. In addition to our direct to consumer sales covering mavi.com and marketplace, our customers can also buy Mavi products through third-party digital platforms to which we wholesale. Including the wholesale e-com, our online sales grew by 89% and reached TL 54 million globally constituting 8.4% of total revenue. We are putting a great effort to improve our online presence in Turkey, especially over the last two years. We are continuously adding new features and benefits for our shoppers. For example, most recently, we launched click and collect function and introduced our Mavi Store app. We are immediately seeing the returns from such features. The strong growth in online sales this quarter is evidence of more to come. The share of online in Turkey increased from 2.5% in the same quarter last year to 3.9% in quarter one 2019. As of Q1 2019, we are already delivering 27% of our total international sales from online, which grew 94% year-on-year. Our third-party collaborations are very strong and growing in North America and we are focused and continuously investing on improving our digital presence in Europe and Russia.

Let's move on to review our margin performance on slide eight. As you know, we guided for continuous improvements in margins and have been able to deliver beyond our commitments against all the challenging externalities in the previous years. For 2019, we have been guiding for significant increases in the cost of goods resulting from currency devaluation impact on raw materials and high inflation. All of the headwinds related to the macroeconomic environment are now factored into our results of the first quarter. Including the negative impact of the hedged contracts we have for product purchases in September 2018, our gross margin contracted 260 basis points in Q1 2019. We are taking many actions to improve our operational efficiency to offset product cost pressures. Our EBITDA in Q1 2019 realised at TL 74 million, 11.4% EBITDA margin, 210 basis points lower than the same quarter last year. Net profit for the quarter contracted 39% year-over-year to TL 15 million, including the IFRS 16 adjustment, EBITDA increased by TL 59 million to TL 133 million, and net income decreased by TL 5 million.

Now, I would like to move onto page nine to take you through our working capital progress. Our working capital at the end of this quarter stands at 5.9% of revenue, implying a very slight increase compared to last year despite the challenges in the trading environment. Increase in the inventory level is mainly due to, on average, 24% higher unit cost of inventory and projected volume increases. It is important to note that our inventory is fresh and especially starting from March, the consumers are rewarding us for the products we are offering. In Q1 2019, resulting from the increase in working capital requirements, we have generated TL 6.3 million of operating cash flow and our cash conversion is at 8%.

Now, let's move onto the next slide, slide 10. We spent TL 20 million on capital expenditure this quarter resulting with CapEx to sales ratio of 3.1%. Our net debt level has increased to TL 150 million as of end of April 2019, mainly related to working capital financing. This implies a leverage multiple of 0.4 times of last 12 months EBITDA.

Looking into the currency composition of our debt, 23% of total consolidated debt belongs to Mavi U.S., Mavi Canada, Mavi Europe and Mavi Russia, all in local currencies. As of end of April, only 5% of debt is in foreign currency and is covered by receivables from subsidiaries, hence we have no open positions on our balance sheet as of today and we aim to keep zero FX exposure going forward.

Moving onto slide 11, we would like to remind you of our official guidance for the year 2019, which we are keeping. Recall that for the financial year 2019, we are targeting 25% consolidated sales growth. In our Turkey retail business we target 18% like-for-like sales growth along with 15 net new store openings and some expansions of store square metres. We guide for an EBITDA margin of 14.5%, we retain our strategic base target of staying below 1 times net debt to EBITDA ratio multiple and we expect our CapEx funding to be around 4% of total sales.

With this final note, now, I am happy to take any questions you may have. For questions, it is over to you. Thank you for listening and being with us.

Question and Answer Session

Operator
[Operator instructions]

We just received a request from Mr Cemal Demirtas from Ata Invest. Please go ahead.

Cemel Demirtas
My question is related to the trends you mentioned at the beginning of the presentation. Could you please repeat that? What do you think about the other competitors and the shopping mall visits? Do you see your trends are better than the general apparel market trends? How do you see that picture? Thank you.

Cüneyt Yavuz
Just to reiterate, in my presentation, I went into a bit more details in terms of how the quarter on a monthly basis performed, which for us, as you know, starts in February, March and then April. The month of February in terms of our budget growth targets was slightly below, due to mainly, we think, of the heavy discounts that was going on in the marketplace with carry-over trades, so it sort of took away a bit of traffic away from Mavi. The month of March is when the hard-core season starts, the spring/summer collection coming in. We did deliver against and exceeded our budget target, so it was a good start to the season from our perspective with traffic and conversion and volume going well. Then the month of April was a bit of a disappointment from a traffic point of view where the traffic was lower and hence sales really came down. A bit of that, we believe, is part of the elections and a bit, we believe, is part of the weather conditions, which is reflected also in the mix of products we were selling. We were selling less of the t-shirts/shirts and more of the outer wear, sweaters and heavier products, which at that point in time had higher markdowns on them and lower margins for us. The good news is from month May, so it is a bit of a up and down kind of a year going forward, is also exceeding our budget expectations where we delivering like-for-like performance well above 25% with traffic and conversion in the positive territory, which is, again, giving us the confidence to maintain our guidance for the year.

I think the trends in terms of where the apparel industry is going, it is similar in terms of ups and downs. I do hope and I do believe that Mavi is potentially delivering better and continue to gain market share despite the competitive environment, so that would be my takeaway for the general macro view of where we stand within the market.

Cemal Demirtas
Did you mention that in May you see an increase in traffic, you have a positive trend in May so far in this quarter (in the new quarter) and the pricing…

Cüneyt Yavuz
Price is already embedded into our goods, which is roughly 20+ percent depending on the category, but we are observing positive traffic, positive conversion rates, positive basket movements, which is reflecting also in very – coupled with the pricing we have taken, a very positive like-for-like performance. May, potentially, is going to be a very good month for us, and I think this is very encouraging to see.

Operator
Our next question comes from Berna Kurbay from BGC Partners. Please go ahead.

Berna Kurbay
I have two questions. The first one is about gross margin trend in the second quarter and the remainder of the year. You said that high costs from Turkish lira depreciation as well as hedging contracts have already been reflected onto the costs in the first quarter. I was wondering if we are through with that high cost inventory or is it going to carry onto the second quarter as well, especially the portion from the hedging contracts.

My second question is about the operating cost controls, which you seem to have done a very good job in the first quarter. The staff costs don't seem to be reflecting any particular increase from minimum wage adjustments. I was wondering if this is a new quarterly base for Mavi for the remainder of the year or are there going to be some, perhaps, shifts from the first quarter to the other quarters in terms of these operating cost items. Thank you.

Cüneyt Yavuz
Starting with the last part of your question in terms of overheads and management OpEx, I think there are no shifts. I think this trend that you are seeing in terms how we are managing our overheads will continue. The good news is that Mavi has the flexibility of a good portion of its payments on pay-for-performance basis, especially in the field, and you will recall from our journeys on IPO process and ever since the IPO that as Mavi we continue to commit ourselves in improving our SG&A costs every year and also improving our rent costs every year, at least a half a point or a 1 percentage point. This is continuing and it will continue, I think, throughout the year and this is an area where we will work really hard to offset some of the first part of your question, which is the costs related and pricing related piece.

From there, going onto the first part of your question, the larger part of the inventory costs related to hedging and high cost of inventory has been written off in quarter one, almost two-thirds of it, but there is still some leftover for quarter two and quarter three. If I look at the numbers, in quarter one there was TL 9.1 million, in quarter two, 3.6, in quarter three, 1.2, so probably about 60-70% of it is behind us and there is still another 40% in quarter two and quarter three yet to be covered.

What we are also looking at is since our inventory is fresh, we are doing all the operational excellence efforts to make sure that the right product is in the right stores, where we are maximising on shelf availability, maximising sell-through rates by making sure that the customers are meeting with the right products and hence also as committed, doing improvements on our markdowns and markdown management, which is another area which we will work to maintain our healthy EBITDA margins.

Operator
[No further audio questions]

Cüneyt Yavuz
There is one question, which is a written question with regards to CapEx details. Our IR Department will be more than happy to give further detail, but let me suffice it to say that, typically, a good 75-80% of our CapEx goes behind store refurbishments, new store openings and store expansions, while another 25-30% goes behind IT, so this quarter was not any different

than that. For the rest of the year, because as you know, we are at a net zero store openings, we will and we are still guiding for 15 net new stores. If you are modelling on behalf of Mavi, for each following quarter to assume that there will be five new net store openings for the rest of the year would be the right guidance.

Thank you everybody for attending. I appreciate the fact that you are with us and I look forward to meeting all of you in the end of the second quarter with hopefully much better results. All my best. Thank you, bye-bye.
