Transcription for MAVI GIYIM

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Corporate Participants

Cüneyt Yavuz
Mavi - CEO

Tuba Yilmaz
Mavi - CFO

Presentation

Operator
Ladies and gentlemen, welcome to Mavi Full Year 2017 Results conference call and webcast. I now hand over to Cüneyt Yavuz, CEO, and Tuba Yilmaz, CFO. Sir, Madame, please go ahead.

Cüneyt Yavuz
Welcome everybody. As you know, we have successfully completed Mavi's 2017 financial year, as of January 31st. In this call I will be taking you through the operational and financial results for the year end, and we will also be sharing our company guidance for 2018. I have about 10 slides to go through, then I will be happy to take your questions.

Let me start with slide two and take you through the key highlights. In 2017, our consolidated revenue increased by 36% to TL 1.782 billion. At the same time, our EBITDA grew by 48% to TL 252 million, resulting in a healthy 14.1% EBITDA margin.

Coupled with strong top line and EBITDA growth, our net profit grew by 74% and reached TL 90 million, and store rollout continued in line with our plans and we opened 26 new stores in Turkey and six in Russia, to reach a total of 313 own operated stores. As of the end of 2017, Mavi has reached a total of 425 stores globally, including our monobrand franchise stores. Mavi Turkey retail business delivered a very solid like-for-like revenue growth of 22.8% in 2017 and our loyalty card, Kartuş, holders reached 6.5 million customers, and we exceeded our own target of 1 million new customers and gained 1.2 million new customers in 2017.

Moving onto slide three, we experienced another strong quarter thanks to growing traffic and convergence. There was strong revenue growth both in Turkey and in international markets and in every sales channel. 82% of consolidated revenue was derived from Turkey. Global revenue grew by 36% and reached TL 1.782 billion out of which 66% was in retail, 32% was in wholesale and 2% in e-com. Global e-com sales grew by 76% much higher than other channels as targeted, and in the full year 2017, sales in Turkey grew by 30% of which 32% growth came from retail. Wholesale channel grew by 20% and e-com sales growth was at 44%. International growth was also very strong with 76%, including the consolidation effect of U.S. and Canada. On a pro forma basis, international growth was at 32%.

Moving onto slide four, in this last quarter we opened five new stores, which is totalling 26 net new stores in the year 2017, as we guided. We now have 287 own operated stores and 139,000 square metres selling space in Turkey. New stores accounted for more than 16,000 square metres of selling space. In 2017, 19 stores went through expansion, yielding an additional 5,300 square metre of selling space. As we continue to open larger stores, average store size increased from 447 square metres to 484 square metres, as of the yearend 2017.

As a result of this selling space expansion and more importantly with our strong like-for-like growth, Turkey retail sales revenues grew by 32% to reach TL 1billion and 133 million.

Now, to elaborate further on our like-for-like performance, let's move onto page five. We delivered a very strong like-for-like growth of 22.8% in 2017. This like-for-like growth is driven by 14.7% transaction growth and 7.1% basket size growth. Mavi continues to be a key leader in the apparel industry, thanks to its strong brand positioning and top of mind awareness. Mavi is also continuing to attract shoppers, as we continue to witness increases in traffic and conversion, mainly driven by customer loyalty and frequency, new customer acquisition, right product at the right price, and superior service and quality.

Now, let's take a closer look at our category-based performance and move to slide six. We are happy to report robust growth performance on both our denim and lifestyle categories. Volume and newly acquired customers are rewarding Mavi with their shopping across all the range of our product portfolio. Our denim category, including jean shirts, jackets and dresses, grew by 32% in 2017. Likewise, our denim bottoms business is continuing its growth momentum with 27%.

Across the lifestyle categories, we again delivered very strong results. The knits category, which consists of t-shirts and sweaters constitute 21% of sales and grew by 25%. Shirts with 41%, jackets with 50%, and accessories with 30% sales increase are clearly indicating that the appeal and demand for Mavi is on a solid continued growth trajectory.

Let's move onto review our margin performance on slide seven. As you know, we are guiding for improved margins going forward, and that this will be through better product planning and markdown management, better rent/sales ratios and operational leverage arising from economies of scale as we maintain a strong like-for-like growth.

It has been a rewarding year in delivering the abovementioned productivity increases that translated into bottom line margin improvements. Our gross profit grew by 36% while our EBITDA grew by 48%, and our net income grew by 74% in 2017. Our EBITDA margin improved 110 basis points to reach 14.1% in 2017.

Now, I would like to move onto page eight to take you through our cash and working capital management progress. We have seen a solid improvement in our cash management this year. Our cash conversion increased to 111% in 2017 from 84% the previous year. The drivers behind this performance have been a team effort to continue to improve our open to buy supply planning, efficient inventory management, and very strong sell through performance. The impact of all these initiatives reflected positively on our balance sheet, especially on the inventory level, which stands at 37% of COGS (cost of goods sold) versus 43% at the end of last year. And our working capital is now at 4.9% of total sales.

Now, let's move onto the next slide to slide nine. We spent TL 72.8 million on capital expenditure this year, most of which was related to new store openings and store expansions. CapEx to sales ratio stands at 4.1%. A few comments on our debt mix. As you know, majority of our euro credit is based on Exim credit for export financing that have very favourable interest rates. The total euro credit constitutes 10% of our debt. The U.S. dollar debt on our consolidated balance sheet is related to Mavi U.S. and Canada operations, and is totally covered by their own sales in U.S. dollar terms, resulting in zero U.S. dollar currency risk. And finally, 76% of our debt is in Turkish liras.

With strong cash generation, our leverage multiple has declined to 0.4 times as of the end of January 2018, and as you will recall, as a principle, we work as Mavi team towards maintaining a debt ratio below 1.

In this last chart, let me wrap up by sharing with you the 2018 guidance. We are expecting 2018 to be another strong growth year, and we have made our plans and preparations accordingly. For the financial year 2018, we are targeting 25% consolidated sales growth, 16% like-for-like sales growth in Turkey retail operations, along with 25 net new store openings. We target an above 14% EBITDA margin and also our net debt EBITDA multiple will remain at below 1, and we will maintain our CapEx spending at 5% of total sales.

At this point, I would like to end my presentation and leave the floor to you guys to see if you have any questions, and we will be more than happy to take any questions you might have.

Thanks for being with us.

Question and Answer Session

Operator
[Operator instructions]

Our first question comes from Gulsen Ayaz, Deniz Invest. Please go ahead.

Gulsen Ayaz
I have got three questions, if I may. Can you talk a little bit about how you see the COGS increase for 2018 and what is your pricing action so far, and how the consumer is responding to

the new pricing levels? My second question is, can you give us some colour on trading in February, and March, both in Turkey and international markets so far, is it in line with your budget. My last question is, there have been some changes in Government's policy about the Turquality programme. I was wondering what kind of an impact positive or negative in 2018 that will have on your EBITDA.

Cüneyt Yavuz
Roughly speaking in terms of 2018, in terms of cost basis, I just want to remind you that the headline CPI in Turkey goes around 11%, and the apparel and shoes CPI has been around 7-8%. This is the sort of ballpark figure that we are taking into our costing structure. Having said that, with the economies of scale and the currency hedging, capacity booking and growing volumes, we are able to mitigate a good percentage of that cost increase in our planning. Hence, typically, it will be fair to expect that this year in terms of pricing, there will be, depending on the season, between 5-7% price increase on our product categories.

We have already reflected in this ballpark figure numbers into summer season opening, and going back and tying into your question, in terms of customer reaction to this new price – it is not necessarily a price increase, but it is also a category mix and price increase bundled, the initial reaction in February/March in terms of sales, business is in line with our guidance, therefore, our confidence at this point in time for the year 2018 remains very positive.

In terms of Turquality, there is one good news. As we were on the IPO road show, in everything that we presented, the Turquality was taken out of the equation. The Turquality programme had ended for the countries that we were operating, which is mainly Germany and Russia. Hence from a financial perspective, we are not seeing any negative impact.

If any, there is a slight improvement opportunity because U.S. and Canada were not within the Turquality programme, and we will have some trickling impact in terms of some OpEx costing and some marketing costs as they are now included in the Turquality programme. So rather than a negative, actually, we have a slight positive potential that might come through the Turquality programme.

But as a principle, the Turquality income that we will have, we will do our best to sort of keep it separate and I would say isolated from a typical P&L, so that we are not distorting our future like-for-like planning and business growth.

Thank you for the question.

Operator
Our next question comes from Ece Mandaci, Tacirler Investment. Please go ahead.

Ece Mandaci
I also have got two questions, if I may. The first one is about your EBITDA margin. Could you please provide some more information, what do you mean about the EBITDA margin and what do you mean above 14% EBITDA margin, because your medium-term guidance was around 15%, and would that figure be achievable in 2018 given this operating leverage impact and 25% revenue growth, and do you also foresee increment in the gross margin level or will it be just the increment in OpEx over sales ratio? The second question is about your working capital guidance over sales. Of course, we have seen a substantial improvement on that front. Do you project that this level will be maintained in 2018 as well? Thirdly, could you also please provide some information on the potential store openings in Russia or in other regions? I think you also closed a store in the U.S., right? These are my three questions.

Cüneyt Yavuz
First of all on the EBITDA margin, you will recall that I have been guiding the investment community in terms of every year gaining at least half a point of EBITDA margin and in the mid-term delivering a 1% EBITDA margin in our company every second year, as you mentioned thanks to a lot of operational leverage, markdown and rent ratio related cost savings. Last year we had, I would say, over and above a positive year where we delivered 110 basis points of gains, as you know, we ended the year with 14.1%. This year we are guiding that it will above 14%, meaning that we will not reach 15%. It will be budget-wise above the 14.1% and hopefully we will be capturing and working towards gaining another half a point gain, in the ballpark of half a point gain. But because we are not in the 15% ball game, as management, we are refraining from using the 15% guidance. Hopefully if everything goes well, as you know we are doing our planning with a three-year outlook, next year when we are here I will be sharing with you a 15% perspective in terms of where Mavi will be going. So in terms of EBITDA margin and improvement, we will be on track and we will continue to deliver as per as previously shared three-year plan and we will update this through the middle of this year, and give you a further update potentially in mid-year.

In terms of gross margin, we refrain from giving any guidance on gross margin. Having said that, historically our gross margin has been quite stable. We do work a lot in terms of markdowns and sell-through rates, planning and operational efficiencies, and make sure the customer gets the right product mix and we focus a lot in terms of ensuring and capturing the committed 2-3% EBITDA margin improvement in the mid-term.

In terms of working capital, we do believe that the working capital will remain around 6% of sales for this year, so more or less in the same ballpark figure, which means that we will be in a healthy cash conversion position. We do expect that in terms of our cash liquidity and business performance, and return on investments of store openings, we will remain healthy. Now, when it comes to store openings, yes, we are guiding for Turkey and we are repeating our confidence that we will at least open 25 new stores for this year.

In terms of Russia, that's an area, as you may also recall, that I leave certain blank and leave a little bit of management space and decide what to open. Last year we've opened six stores. I want to see all the performance of how these stores are performing. We do expect to open up a few more stores in Russia and I'd like to share how that goes on a quarterly basis, as we progress into the year.

In terms of the closure of the U.S. store, it was part of our plan. The event there was the expiring of that contract and we decided not to renew the store in the U.S. As you know, in the U.S. we are not a retail player; we're a digital and wholesale player, and we will maintain focusing on building our brand both in the wholesale and specialty business partners along with our own dot-com and digital business partners.

Operator
Our next question comes from Görkem Göker, Yapi Kredi Yatirim. Please go ahead.

Görkem Göker
My question is again about your net working capital practices, as because we have limited data to assess your quarterly dynamics and your cash conversion, and IFRS-based calculation might deviate from the actual results, but it seems to be an improvement and could you please provide more information on that front, particularly your relations with suppliers at a time when tariff rates are expected to increase, and should we expect this similar cash conversion performance in 2018? My second question is regarding your store breakdown. In your IPO presentation we had a chance to see the breakdown with respect of years of operation and their contribution to the revenues. Is it possible that you share some information on that front as well for 2017? Thank you very much.

Cüneyt Yavuz
In terms of cash conversion and the working capital management, it would be fair to say that we will have and we look forward to a very healthy 2018. In terms of payables, receivables, and our working relationship, actually you may recall that 80% of our total business is in Turkey and of that, 80-plus percent is in Turkey, so we have a very steady cash flow performance coming from the retail business and we have a very healthy like-for-like growth that is keeping its momentum with new store openings, square metre expansions, and new customer acquisitions. Therefore, again, as was asked previously, looking also at the February/March, the way the year has started, we are very confident that this momentum in terms of sell-throughs will continue.

In terms of our payables, receivables, it's a contractually-based relationship. There are no changes from one year to another, so we do expect a very smooth year in that respect. I'm thinking out loud if I am missing anything, but that should more or less cover it.

In terms of store breakdown in years, in the IPO process we did share the age breakdown because there was a big question around whether the stores that were older like seven years or older etc were slowing down. I'm very happy to share, as we did in the IPO process, I'm very happy to share with you that our like-for-like performance through store clusters, meaning A, B, C clusters, versus new stores or older stores are maintaining their momentum and customer appeal and demand, and traffic is strong both in new and older stores, therefore the mix and the aging mix remains quite steady and was represented to you through the IPO process. Thank you.

Operator
Our next question comes from Asli Tuncay, Goldman Sachs. Please go ahead.

Asli Tuncay
I have two questions. So the first one, your leverage is quite low now, how would you think about potential cash uses? My second question again relates to your guidance on your EBITDA margin. So you talked about some 50 basis points of gain every year. If we were to think about it in a different way, what would make you more optimistic on these gains and what would make you more cautious?

Cüneyt Yavuz
At this point in time, one of the questions that we get, raised and discussed around this at this momentum is: are there further growth opportunities and investment opportunities out there? For the short-term, which is this year, whether this might be a new territory or a new geography, or a new channel, we will stick to our base business plan. This is going to be a very important year for our company following the IPO to sit down with the new board to strategize for the next three years of business plans, and I look really excitedly forward to sharing with you the huge potential that is out there. The team has already started to work on them. As there is nothing crystallised, unfortunately I cannot comment or share some of the ideas we have. But we are all determined to keep the nice profitable, sustainable growth coming in for many, many years to go, and the projects we have and the ideas we have are indicating that there is every reason that as a leader of a company I have confidence that this will maintain.

Now, in terms of guidance, we do, as you will recall, have been sharing with you that every year we would have 50 basis points of improvement and last year we had 110 basis points improvement, which is far more than what we bargained for, so we had a fantastic year, especially coming from as was shared with more traffic and stronger than anticipated, so we are going back to our base plan of not 1.2, but 1 million new customer acquisitions, and building a business and budget based on that. Having said that, we are still looking for this half a point further improvement.

Now, for me to be positive, as you're saying, I would expect the consumer confidence or the new traffic increase to be stronger than what it is right now. Given that we are already a quite aggressive company in terms of aiming for increased traffic, I would like to see a year like the previous year before I can come around and tell you, tell the investment community that we are going to gain not 0.5 but much more than that. So already I think we have a robust and very strong plan, and from that perspective it is to a certain extent up to competition and the consumers. The good news is we are continuing to open up bigger stores. These bigger stores are great enablers, because the traffic coming into these stores is increasing. The second good news – is into these bigger store formats, when customers are there, the conversion rate is increasing. It is also good news, the unit per transaction, the units that those customers are buying and the basket size in these stores, are growing, so not only do we have one, two, but three, four times the multiple of growth coming through our expansion plans. These expansion plans that I shared with you are coupled very much with the category growth, so the customers who are coming in are also buying all the categories whether it's the men's and women's lifestyle, be it also the denim categories, so this is also very encouraging for our business portfolio.

The last thing is, as you know, we grow the base. Last year we expanded 19 stores. Hopefully we will work very hard to find as many, if not more stores, to continue to expand. These are already tested and proven stores, so therefore expanding them from their 300 square-metre basis to 600 base is already a proven formula to add more volume. One of the other key agenda items or points that might make me more optimistic about the future is that rather than finding 19-20 stores, if working with the shopping malls we are able to find 25, 30, 35 new stores to expand, which we have a list to do so and we are not holding anything back, then I can come back to you guys and share with you that there is more upside than what we are doing right now. Thank you.

[No further question]

Cüneyt Yavuz
Thank you all for being with us. We had a fantastic year and the team here is very busy and looking forward to a very successful 2018. Hopefully across the next quarter we will be getting together and sharing good results and good continued momentum. I wish you all the best and all of you a happy, healthy, prosperous new year. Thank you, bye-bye.
