Mavi Financial Results Webcast H1 2022

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DUYGU INCEOZ
Ladies and Gentlemen Welcome to Mavi webcast regarding the financial results for the second quarter of 2022. Our CEO, Cuneyt Yavuz, will be presenting the results followed by a Q&A session. We would like to inform you that this presentation is being recorded and we kindly ask you to keep your microphones muted throughout the presentation. Now, I will leave the floor to Cuneyt Yavuz.

CUNEYT YAVUZ – Mavi CEO
Hello everyone! Welcome to our webcast for the financial results of the second quarter of 2022.
I am very pleased to be announcing another strong quarter with solid results. As you know our first half results reflects the performance of our Spring Summer season. We are very happy that the historic high results we announced yesterday is the reflection of a well-received great collection, our best- in- class communication, all made possible by our committed team.

In the second quarter of 2022, consumer demand continued to be robust amid ongoing high inflation in Turkey. Turkey retail sales grew 119% year over year in the quarter. This positive trading environment allowed for high sell through rates with low markdown spending which continued to help offset significant product cost pressures. Sales growth was driven both by price and volume. Almost all product categories grew in number of pieces in Turkey. In the first half of the year, we sold 6.2 mn denim items globally growing 22% yoy. As always, dynamic and adaptive supply chain management, efficient product planning and inventory management paved the way for our successful results. Our international operations are also performing well in spite of many externalities taking place globally. International sales grew 16% in constant currency in the second quarter. Positive operational cash generation in the second quarter resulted with 47% growth in our net cash position, which now stands at 829 mn TL. As promised, continued investments on brand and customer, focusing on product newness and quality continue to bring market share gains in Turkey.

Now lets look at the key highlights for the period, moving on to Slide 3. Our consolidated sales in the first half of 2022 realized at 4 billion 124 million liras growing 125% versus same period last year. Turkey retail sales grew 148% and Turkey online sales grew 58% on a high base. Our EBITDA, almost tripling year on year, realized 1,109 million TL, resulting in an EBITDA margin of 26.9%. We continue to deliver increasing quarterly earnings. The net income for H1 2022 is 704 mn TL. Our balance sheet net cash position increased to 829 mn TL as of the end of July. The total number of mono-brand stores globally, including franchisees, reached 461.

Lets move to slide 4 to review our channel performance: With the retail channel gaining significant pace this year, our H1 2022 total revenue consists of 65% retail, 24% wholesale and 11% e-commerce sales. 81% of total revenue was generated from Turkey. Traffic to in our stores and the demand for

Mavi products remained very strong in Turkey. The inflationary environment continues to be a driver for the consumers shopping appetite and as Mavi we made sure we have the newness and variety at the right price to respond to this demand and remain consumers' brand of choice. As a result, our sales in Turkey grew 103% in quarter two mainly driven by the retail business which grew 119% on top of a significantly high base last year. Please recall that within the second quarter of last year, Covid restrictions were fully lifted for the first time, driving a very strong pent-up demand. Our e-commerce business in Turkey, which constitutes of mavi.com and marketplace sales, grew only 30% in the quarter, also on top of an extraordinary strong base, especially in the month of May, in which the retail stores were on a full lock-down for 17 days in 2021. We expect to see a normalization of online sales growth going forward with the consumer shopping behavior stabilizing. International operations are back to its normal growth rates, growing 16% in constant currency and 129% in TL terms in the second quarter compared to same period last year.

On slide 5, we start to focus on Turkey retail business: We have been emphasizing throughout the previous years, that retail would continue to be at the heart of our growth strategy. The strong come back of retail performance this year is a testament of how right we were. We continue to open new stores and expand current stores in square meters while constantly taking new actions to make sure that consumers have a great shopping experience. In the first half of the year, we opened 4 new stores, closed 2 stores and expanded 7 stores in Turkey. As of July-end, we have 329 own-operated stores totaling close to 167 thousand sqms of selling space in Turkey with an average store size of 506 sqms.

On slide 6, lets elaborate on the same stores' performance in Q2 2022. Most of the second quarter is more comparable with last year as all restrictions had been lifted as of June in 2021, so we are from now on taking into consideration all days with a proper like for like mindset. In quarter two, traffic in our stores was 40% higher than the same period last year showing the appetite for shopping. Same store sales grew 119% this quarter with number of transactions increasing 23% and basket size growing 78%. Although there are significant price increases due to the inflationary environment, there was still 9% volume growth in the quarter.

Moving on to slide 7 to review category-based developments in Turkey retail: We are happy to report strong growth across our product categories in H1 2022. All categories also delivered significant growth in number of pieces. We are constantly following changing consumer preferences and enriching our product range, offering newness, variety, and innovation in response. Our denim category grew 138% year on year constituting 42% of total retail sales in Turkey as of the first half of this year. The knits business including our growing t-shirt, sweatshirt and jersey categories is now 28% of our total Turkey retail sales and continue to deliver robust performance growing 164%.

Capitalizing on the same trend, our rising category non-denim bottoms grew 163%, now constituting 7% of our total Turkey retail sales. Shirts sales is recovering from the pandemic disruption. Growing 170%, it makes up 12% of our total Turkey retail revenue. Accessories including our well received swim wear collection, grew 167% and contributes significantly to our women's business, especially in the spring summer season. Jackets, seasonally being a fall-winter product grew 123% in the first half of 2022.Overall, our lifestyle categories grew 161% year on year.

On slide 8, lets review our online sales performance: On this slide we review the total online sales of Mavi including the sales to the third-party digital platforms to which we wholesale, in addition to our direct-to-consumer online sales made up of mavi.com and marketplace sales that are reported under e-commerce channel. Recall that our direct-to-consumer e-commerce share is now 11% of total consolidated sales. Including the wholesale e-com, which only exists in our international business, our total online sales grew 69% globally and is now 12.9% of total revenue. In Turkey, with Mavi.com, relaunched with a new upgrade earlier this year, we enhanced the online shopping experience, offering speed and ease to our customers. In the second quarter, online growth in Turkey was softer as expected given a very strong base from last year and the robust retail come-back this year. The 17 days full closure in May of 2021 had accounted for half the sales in the quarter. On the other hand, the aggressive marketing strategy of marketplace platforms in 2021 is now normalized. As a result, online sales in Turkey grew 58% driven by 61% growth of mavi.com and 56% growth of marketplace operations and now constitutes 8.9% of total sales in Turkey. International online business growth is on track with 85% in the first half of 2022. The fact that this growth is largely driven by our direct-to-consumer channels is promising. Our own platform mavi.com grew 114% and marketplace sales grew 149%. 30.1% of total international sales are through online channels as of H1 2022. Mavi's strong digitalization and CRM infrastructure will continue to drive our growth trend in e-commerce and as I noted in previous quarterly updates, the shift towards online will positively impact our margins going forward being a full-price channel across all categories. As retail operations are back in the play as we had anticipated, omni-channel capabilities are becoming more important for future growth and in improving the shopping experience for consumers.

Let's move on to review our margin performance on the next two slides. On slide 9: With rising raw material and energy prices, currency fluctuations and high inflation in Turkey, gross margin continue to be one of our biggest focus areas. Our strong brand strategy, dynamic product-price planning, the newness, and variety we bring in response to high consumer demand resulted with high sell-through rates and lower markdowns in the spring summer season. Meeting high consumer demand with the right product positioning in an inflationary pricing environment supported cost mitigation. Currency impact of international operations has also positively impacted margins. As a result, gross margin improved 330 basis points in the second quarter and 500 basis points in the first half of 2022.

On the other hand, it is important to note that the product cost increases for the second half of the year is much higher. We expect the gross margin levels to gradually trim back as more costly products enter the shelves until the end of the year.

On slide 10 we review our bottom-line performance.The significant opex inflation in the second quarter was mostly leveraged by the strong top line growth. We continued to deliver improvements in our rent ratios and our employee cost to sales ratios in Turkey. Our EBITDA margin excluding IFRS16 adjustments has improved 170 basis points in the second quarter to 20.4%. Here, it is important to note that the IFRS16 impact on EBITDA has become lower compared to previous years because of two developments:
First: the ratio of performance-based rent contracts has increased, leaving the related rent costs on the P&L. Second: the total rent costs as percentage of revenue is decreasing, hence reducing the impact of IFRS16 on EBITDA. In the first half of 2022, we achieved a record high EBITDA of 1 billion 109 million TL including IFRS16 adjustments with a margin of 26.9% improving 490 basis points. The operational performance is mainly reflected to our bottom line. In the second quarter, the 403 mn TL reported net income includes 94.6m one-off tax income due to revaluation of fixed assets on statutory books. Net income margin in the first half of 2022 is 17.1% which is a significantly higher level than last year or any other period pre-covid.

On slide 11, we look into our operational cash flow and working capital performance: The average cost of inventory is 81% higher than that of same time last year and we are taking several initiatives to mitigate product costs pressures such as cash payments, early booking, advance payments for raw materials. As of the end of July 2022, the inventory level in number of pieces in Turkey is only 21% higher compared to end of July 2021, reflecting sales volume growth and comprises of all fresh, mainly FW22 season products. Nevertheless, net working capital is back to our targeted strategic levels of 5% of sales. We generated significant operational cash in the second quarter despite the increasing working capital requirements compared to year-end. Operational cash generation in the six months is 426 mn TL with a cash conversion ratio of 46%.

Let's now move on to the next slide: (slide 12) We spent 118 mn TL in capital expenditures in the first half of the year resulting in a Capex to sales ratio of 2.9%. On the retail side we had store openings, sqm expansions and new store concept transformations taking place. Apart from retail, we have been investing predominantly on IT projects and digital investments. With strong cash generation in the second quarter, our net cash increased 47% compared the end of first quarter to 829 mn TL. All of the foreign currency debt you see on our consolidated reports belong to our subsidiaries, all borrowing in their respective local currencies and hence does not pose a currency risk. We continue our approach of holding no foreign exchange position in our balance sheet. On the other hand, average cost of debt is increasing in Turkey, and we foresee higher rates going forward. We recently applied to the capital markets board for debt instrument issue ceiling to further diversify our liquidity options if need be.

(On Slide 13) We are revising our full year guidance with the six months realizations and the positive market conditions we continue to experience. For the financial year 2022, we are revising our consolidated sales growth target to 120% growth versus 100% previously. We still plan to open net 3 stores but 13 store expansions instead of 11 within the year in total including the ones already completed. We are revising our EBITDA margin expectation excluding IFRS16 to 19% plus minus 0,5% as we see our profitability prospects better than our initial estimations. On the other hand, as previously explained, due to positive developments on the rent cost, the impact of IFRS16 adjustments are lower now compared to previous years. Hence, we are keeping the EBITDA target including IFRS16 at 24% plus minus 0,5%. Our net cash position expectation and capex target are unchanged. As always, I would also like to give you some color on the current trading environment as of date. We had a great start to our fall winter season. We are experiencing a proper strong back to school season, just like the old days with great demand for our products and a positive pricing environment. Turkey retail same store sales increased 153% in August and 135% in the first 15 days of September year on year. Happy to report that, online sales in Turkey is already back to normal with 95% growth in August. With this final note, I am happy to take your questions now.

DUYGU INCEOZ
Ladies and gentlemen, if you wish to ask a question, please click on the raise your hand button, which is the hand icon on your control panel. When I call your name, please open your microphone before you speak. If you prefer to type your questions, you may use the chat screen or email me directly. For those of you who have dialed via audio, we will take your questions last when there are no questions left on the platform. Okay. Cemal has a question, I think. Cemal, go ahead, please.

CEMAL DEMIRTAS
Thank you for the presentation and congratulations for very good results. And I also appreciate your perspective during the pandemic towards your employees and stakeholders. I really appreciate that from the analyst perspective, and I see your numbers are improving further. I would like to understand the impact of the increases in rent and the employee salaries. We see some impact in the second quarter. What kind of a picture could we see in the rest of the year regarding the rent expenses and personnel expenses? How much increase you did in this quarter, and what could be the trends in the following quarters? And could you give us some picture about the trends in 2023? Thank you.

CUNEYT YAVUZ

Thank you very much, Cemal, for the warm words. It's also encouraging to get emotional support from you too. And I think even now, over and above the pandemic, as you know, we are going through economically tough times, and, our priority to maintain a good working relationship with both our top party service providers, as well as taking care of our employees, is still top of mind. And it's one of my top priorities. Therefore, it is critical that you raise the question.

Let me start with rent expenses. The rent expenses, overall, have been coming down as a part of the revenue ratio. And rents are right now down 170 basis points versus where we were the same period last year. Generally speaking, as we continue to price competitively, bring newness, and bring in great products with good pricing, I am quite confident that as a ratio of sales, rents, as you will recall in many of my previous conversations, will always continue to slightly improve from one season to another. And I think this past season, Spring/Summer was a testament of that. And looking into the future, I also expect our rent ratios, as a percentage of sales, to continue to remain same, if not get better in this Fall/Winter season also.

When we come to the salaries bit, employee cost is down overall 200 basis points, and central operating expenses are down roughly 140 basis points. Some of the overall consolidated deterioration or negative trend was due to some of the incentives that were provided in international markets that were lifted. So we did have a base impact of support coming in from Germany, U.S., Canada. These markets, where we were getting government subsidies, which were lifted during COVID. But even regardless of that, overall, our position in terms of Opex-to-Sales and other expense bases are improving and will continue to improve.

I think right now we are growing in real terms. And as we continue to grow in real terms, as Mavi, as a leader of the team, with the support of the board we will be competitively paying our employees. We keep the best talent on board to continue to deliver the stellar results we are seeing. And I'm confident we will do that. But, overall, in terms of direction and the field that we want to get, both on rent ratios and SG&A ratios, I do expect that, as a percentage of revenue, you can assume same or better results moving forward, including for 2023. I hope that gives you a clear picture of where we stand and what my perspective is.

CEMAL DEMIRTAS

Thank you. Thank you very much. Appreciate.

CUNEYT YAVUZ

You're welcome.

DUYGU INCEOZ

Görkem has the next question. Go ahead Görkem.

SPEAKER 4

Thank you, Duygu. Teşekkürler Cüneyt Bey. Firstly, a follow-up question about your rent expenses: You talk about that you switched some of your contracts to turnover-based. Can you give a number on that front? What percentage of your stores' rent costs are turnover-based? And my second question is: You talk about more costly products that will lower your gross margin in the second half of the year; can you still give us a guidance about what percentage we should expect in terms of deterioration? And lastly, you talk about your market share gains. I don't know how accurate it will be to extrapolate your results to the entire sector, but, can you give us some color on the competition environment and quantify your market share gains and overall market? Your views about the overall market? Thanks in advance.

CUNEYT YAVUZ

So overall in terms of rent ratios, as we move down the road, of our total stores, about one-third of them right now are under a contract of rent ratio, of revenue ratio. And the two-thirds are still with month-to-month, fixed income, fixed rent payments, and adjusted on an annual basis. So that's sort of the overall picture. In terms of the margins lowering down, we do expect that we will still close the year, overall, as an annual year, with a margin improvement versus year-on-year.

In the Fall/Winter, as we go into the season, of course we will be following extremely dynamic pricing, and every month, almost, new products are coming in. So we will follow where the competition is and where the pricing is. But for a comparison between Spring/Summer versus Fall/Winter, right now we are thinking there will be two to three percent margin deterioration or pressure in terms of our P&L. Usually, that's the case, by the way. So, let's see, I don't want to be extremely optimistic. There's a lot of headwinds and I also want to protect the consumer and traffic with right pricing. But, at the same time, if and when we see the opportunity in terms of pricing and gaining mix, newness, as well as markdown and campaign management, we might come in with a surprise.

But, generally speaking, right now what we have budgeted is between, roughly speaking, two percent margin erosion versus Spring/Summer. (corrected as year over year in H2 2022 not versus Spring Summer) But total annual yield, still delivering a margin improvement versus last year. So moving in a positive trend.

In terms of the market share position in terms of where we are and what our market share is, we are definitely gaining. I mean, that's our feel. We don't have all that quality data coming in. We are following Ipsos data, which is coming bi-annually. And we are right now number two in men's. And number three in women's, in terms of total overall market share in the apparel market.

The good news I can share with you is, overall, when I talk with my retail business partners, relatively speaking, everybody is happy with how their business is proceeding. But I have a sense that we are doing a bit better than how they are doing. I think the great testament is in the amount of traffic that is increased, that we are seeing. We saw in the Spring/Summer, and also starting with the back-to-school period, more than 40% traffic increase, 40 and above. So that's really encouraging. It means

that we are becoming people's choice to come and shop.
The bigger player, as you know, we have a couple of very big players within the competitive environment. But as Mavi, we can, over the next seasons, continue to solidify our second or third position in the market, depending on how we look at it from a man's or woman's perspective. But definitely moving in the right direction and drawing in absolute volume.
One side impact, also, is our marketing team typically has a target of gaining one million new Kartus card holders that have never bought or used a Kartus card, which is our CRM loyalty card. And we are back on track. So this year, after the pandemic, I think this will be another year where we will have more than one million new customers coming and shopping, which is also a good testament that we are moving in the right direction. I just want to also throw that in as a fact. Thank you.

DUYGU INCEOZ
Görkem, I just want to correct some little point. In terms of the growth margin, we do expect some erosion in the second half compared to last year, year-over-year, not to Spring/Summer, but versus last year.

CUNEYT YAVUZ
Yes, two to three percentage points decline in Fall winter and I said, overall consolidated full year budget would be an improvement versus last year. Yeah. Thank you for the clarification. I didn't mean SS, I meant FW 21. Thank you.

SPEAKER 4
Thank you.

CUNEYT YAVUZ
Thank you. Great.

DUYGU INCEOZ
Ladies and gentlemen, do we have any other questions?

CUNEYT YAVUZ
Okay, it seems like we are done for today. I really appreciate the fact that you have all joined in and tuned in to our quarterly update. I look forward to coming in with good and strong results in the coming quarter and wish you all the best in this competitive and highly interesting times. All my best. Take care. Bye-bye.