Company: GB Auto (EVENT)

Conference Title: GB Auto 3Q16 Results Presentation

Moderator: Dr. Raouf Ghabbour

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Operator: Good morning, good afternoon ladies and gentlemen. Thank you for joining our 3Q16 Results Presentation conference call. From GB Auto we have Dr Raouf Ghabbour, CEO, Mr Mostafa El Mahdi, CFO and Mrs Mena Sadek, CIO presenting 3Q16 results for 2016. Today's conference is being recorded. I will hand the call over to Dr Ghabbour for his presentation, then we will have a Q&A session. Dr Ghabbour, over to you.

Dr Raouf Ghabbour: Thank you Jenny. Good afternoon ladies and gentlemen and thank you for joining our third quarter results call. With me here today is Mostafa El Mahdi, our Chief Financial Office, Mena Fadek, our Chief Investments Officer is dialling into the call this afternoon from Dubai where she's been meeting with investors including, I would imagine, some of you.

I'm going to keep my remarks this afternoon rather brief and to the point. I'm sure you've all had time at this point to dive into our results for the first quarter. I believe they speak for themselves. So I'm going to be brief on that front. Instead, I'll spend a few moments speaking about where we see the business going from here after the events of the last two weeks.

In the first quarter, we see this is another example of results delivered by our long term strategy diversified beyond passenger cars while growing our market share in that core segment. It's also an outgrowth of how our people and systems have proven adaptable to the sweeping changes we have seen in Egypt since 2011. Growing our top line and our market share across the board in a landscape marked by significant inflation and foreign exchange constraints is no small accomplishment. At the end of the day, our success came because we read the market correctly.

That's why we had a liquidity and product line up: we needed to capture demand that our competitors could not serve. It was a bold call but clocking in our market share in challenging macro-economic climate preserved our market leadership. It also ensured we will continue to generate high margin after sale revenues going forward.

Ladies and gentlemen, we have unrivalled market share heading into what we expect will be a challenging quarter as the market adapts to a new economic reality post the float of the Egyptian pound. Our selling prices were up 34% in Egypt and our volumes rose by 13%. As a result, a good share of the devaluation that followed is already priced into our business. At the same time, our after sales business is going north of 40% year on year.

Commercial vehicles and construction equipment are growing double digits. We are referential suppliers for buses, trucks and construction equipment to the private sector and government infrastructure contracts alike. Our tyres business was the star performer of the quarter and our financing business continues to grow at a breakneck pace with excellent credit quality. And we fully expect that our motorcycle and freewheeler business, the traditional star of our portfolio, will whether the coming quarter or two and return to strong growth.

Yes, our performance came at the expense of foreign exchange charges, and yes, we expect we could face a quarter or so of dislocation in the market as consumers adapt to inflation. It's possible that this period we'll see some softness in consumer sentiment. It would be normal for this to have an impact on sales, particularly as the pound overshoots and then cools to what we believe is a more reasonable rate.

That, ladies and gentlemen, is the short term. But looking at the third quarter, we turn in a remarkable top line performance in an incredibly challenging climate. Imagine what we could do in a healthy growing economy with a functioning foreign exchange market . We are increasingly optimistic that that is the direction in which the economy is headed today. The float of the pound, the implementation of the value-added tax and the closing of the IMF facility were critical first steps. The Government and the Central Bank have sent all the right signals in the last two weeks that they will stay the course. To us, this is a signal that it's time to return to the basics. So a time when the performance of our business is measured not by how well we managed multiple years of alternating crisis and headwinds but by how well we capture market share and innovate in a thriving economy.

In the short term, the business will be about managing operations and looking carefully at how we price and reprice our products. But in the long term, the reform process will only fuel demands. This demand is not driven by luxury and replacement records but by a motorisation index that is still significantly below emerging market norms. With higher prices, consumers will look after what are in EGP terms less expensive [inaudible]. That will allow us to drive growth in after-sales where we think consumers will see trusted brand name spare parts and service as a way of protecting their vehicles. Growth will be delivered by our corporate clients, overhauling their fleet after more than five years, in many cases, spent in a wait-and-see posture. It will be delivered by a rising economic tide that delivers sustainable growth to rural and pre-urban regions where our tuk-tuks are stable. It will be delivered by social mobility thanks to rising wages and new opportunities, opportunities that will see new families start out with a motorcycle before upgrading to passenger cars. It will be delivered by the continued roll-out of our high-margin tyre business, including our own brands. It will be delivered by the continued robust growth of our financing business. And perhaps more intriguingly, growth will be delivered by the deepening of our position in the value chain. As you know, we are already producing our own brand of tyres from our own moulds through [inaudible] agreements with existing manufacturers. And we are well down the road on our motorcycle and three-wheelers manufacturing facility.

As we speak today, the House of Representatives is in its third day of hearings on what we call here in Egypt 'the automotive directive'. The directive will give assemblers such as ourselves important protection against unfair imports from the European Union, Turkey and Morocco. It is a package of new incentives that will encourage domestic players to go further up the value chain into manufacturing, and it is pro business, pro employment and pro consumer. There's quite potentially a game changer for us in terms of the long term profitability of our passenger car business. And if law makers get it right, it might open new opportunities for us in export markets across our product portfolio.

With that, ladies and gentlemen, I'd like to thank you all not just for joining us here today but also for believing in our story and our nation's potential these past five years. The journey has been challenging, but as I hoped our stock performance has [inaudible] in the past two weeks. I believe the journey has and will continue to prove very rewarding.

With that, I'll hand over the call – I'll hand the call over to Mostafa. Mostafa, please.

Mostafa El Mahdi: Thank you Dr Raouf. Ladies and gentlemen, good afternoon. GB Auto saw a total sales revenue increase more than 36% year on year. During the third quarter, this was partially due to availability of inventory as well as to the company's effective use of ex-pricing power. Our ability to consistently meet consumer demand, even in such difficult economic environment.

As a testament to our operational strength and our multiple [inaudible] business model. Our top line growth filtered nicely into our gross profit, which rose nearly 39% year on year and allowed us to maintain a gross margin at almost 13% over the nine months. Gross profit was up more than 31% with a margins 1.5% to nearly 14% compared with the same period last year. Operating profit rose almost 66% in the third quarter and it's up just 53% in the year to year. At the same time, operating profit margin was up 1.2 percentage points to 6.8% in fifth quarter and about 1.8 percentage point to 7.7% in the first nine months of the year. Net profits strong, continuing operation, however, came in about 52% lower at EGP 59.4 million with a margin of 0.9% down from 1.8% in the same period last year. The decline is partially due to the company incurring FOREX loss of EGP 80.8 million. During the quarter, circling a [inaudible] related liability.

We continued to use rapidly generative cash to build our inventory under very tough FOREX conditions, resulting in a negative cash flow from operation. This was a strategic move that has seen us position GB Auto as a supplier of choice for consumers, wishing to purchase any type of [inaudible]. The proof is in our market share, which has shot up from about 27.8% in the first quarter of last year to an historic high of 41.5% in the third quarter of this year. That's also what has allowed us to grow volume by more than 15% this quarter, as Dr Raouf said, at the same time as the market shrunk almost by 23%.

The Group's net debt stood at around EGP 6 billion at the end of the third quarter and increased up EGP 183 million compared with the previous quarter. We maintained net debt to [inaudible] issue of about 1.4x as at 30th September. Compared to 1.38x at the end of June. Total debt incudes EGP 2.2 billion of financing business debt, as we continue to expand and grow our financing operations.

It's worth noting that the recent float of the pound will result in a one-time non-cash FOREX loss booked in coming period. We believe that our price adjustment throughout this year has left us well positioned and managed [inaudible] foreign currency risks. And that the float will eventually help resolve most of our cash flow issues in the long term.

Overall, GB Auto is in a very strong position compared to others in the market, as we have continued with our strong push to replenish inventory levels, meet market demands and utilise our pricing [inaudible] successfully.

That concludes my presentation for today. Ladies and gentlemen, I'm going to hand over the call now to Mena Fadek, our CIO, who will wrap up things for us and then open the floor for your questions. Mena.

Mena Fadek: Yes, thank you Mostafa, thank you Dr Raouf for the presentations. I won't take much of your time, ladies and gentlemen, we are anxious to open the floor to your questions and have a good back and forth, whether that's about the third quarter or outlook of fourth quarter and next year. Moreover, I've lost my voice speaking since 06.00 am Cairo time, 08.00 Dubai time today. So yeah, so I'll be very brief. I've probably spoken to most of you and seen some of you, actually some of our shareholders are sitting here with me as well. During the past two weeks, there's been a lot of calls. And I have to say that from our recent meetings and calls, I can only infer one thing, I have not felt this enthusiasm from your side since 2011, probably, you know, since 2007 since we were doing the IPO.

So we have been – GB Auto has been growing its top line and market share since 2011 until today. I will not recite all the events, local or regional, political or economic that have seen our 15% revenue CAGR for the past five years not filter through to similar growth in our profitability, but I will say this: this is about to change. Yes, the environment post-float is challenging in the short term but it was the right thing to do and it was definitely needed before Egypt, our largest market, could open a new era of economic growth.

At this point, everything that we have built at GBO Auto throughout the years, especially this customer centric organisation with a dominant market share, will soon start to pay off. Our goal is to begin reaping the benefits in 2017 and beyond of our sound strategic leadership and truly diversified business model.

Having said that, there are some short-term headwinds that most of you are probably familiar with. We have been transparently reporting our foreign currency exposure, which will lead to the FX book loss that Mostafa referred to on the back of the revaluation of our foreign currencies payable. It's a book entry as most of you told me today. The most important thing for us is to continue to be able to pass on our cost base and consumers, something we've been successfully doing since the foreign currency crisis began. The second headwind is also of a short-term nature, and that's how consumers will react to the inflationary pressures in the economy, a very popular subject we also discussed today. We are not concerned, as we believe in the resilience of our markets in the long term. And as Dr Raouf mentioned, we are now back to the basics.

I look forward to continuing our interesting discussions about the future of our business, especially given that most of our investments are starting to pay off as we look forward to start investing in our exciting two and three-wheeler facility very soon. It has been a pleasure to deal with you in the past few tough years, and I look forward to working with you in the more prosperous days to come.

Now let's got those questions started. Operator, please.

Operator: Certainly. Ladies and gentlemen, if you would like to ask a question at this time, please press *1 on your telephone keypad. Please ensure that the mute function on your telephone is switched off to allow your signal to reach our equipment. If you find that your question has already been answered, you may remove yourself from the queue by pressing *2. We will now take our first question from [inaudible] from Arab African. Please go ahead, your line is open.

Speaker: Hi everyone and thanks for holding the call. I just wanted to ask about if you have a ballpark figure for the FX loss. As per my calculations a bit north of 400 million, if you can – if you can give me you estimate or…

Mostafa El Mahdi: The current estimate we have on exposure of the US dollars of around $81 million, and the final figure of the FOREX loss cannot be accurately – yeah, calculated till the end of the year, till we know at what level the dollar will be stable against the Egyptian pound. But currently the exposure is around US$80 million, as I told you, and there's also almost 400 million loss.

Speaker: Okay, great. I had another question in regards to the Egyptian passenger car segment. I can see in the third quarter prices were only raised by almost 5% quarter on quarter. Are you seeing any slowdown in demand because of the price hikes that took place in the first half.

Dr Raouf Ghabbour: Every time we have a price increase, the same phenomenon happens. For a week to ten days, the market is completely under shock and then they wake up from shock contemplating for the next price increase to happen in a weeks time, so we have one week drop and then one week fantastic sales to compensate for the previous week. So that's the phenomenon. But until now, last month for example, we have delivered a record volume of cars, a record in our history in GB Auto in October. So the market is very resilient until now.

Speaker: And how is demand looking in the first two weeks of November post the floatation?

Dr Raouf Ghabbour: Post the floatation, we did price –we did a price increase in 1st November. We did another price increase on 6th November and we did a third price increase on 15th November. So the market is currently shocked with three hits on their hands. But I expect that the market will pick up within a week time.

Speaker: Okay, can I know the magnitude of these price increase in November?

Dr Raouf Ghabbour: I'm really –I'm not that much into the details but it's healthy. It's big increase. I could assume in the range of the three increases no less than 10-15%.

Speaker: Okay, thank you.

Dr Raouf Ghabbour: Thank you.

Operator: As a reminder ladies and gentlemen, if you would like to ask a question at this time, please press *1 on your telephone keypad. We will now take our next question from [inaudible] from Arab African, your line is open.

Speaker: I have a very quick follow-up question if I may ask about your inventory. What price of the dollar was it purchased at?

Dr Raouf Ghabbour: It's very different, I have parts of inventory at 783 and part at 883 and part at 18. So I have a cocktail of different – it really depends on which business and which product. I didn't really calculate what's average. Do you know where are we…?

Mostafa El Mahdi: No, no. It's totally, yeah I mean, impractical and impossible. It depends on the line of the business and the date of the acquisition and several [inaudible] parts to carry out the 50,000 items.

Dr Raouf Ghabbour: We don't know what's the average but when we price we look at each shipment and we look at the actual payment rates and we calculate our pricing accordingly.

Speaker: Okay, thank you.

Dr Raouf Ghabbour: Thank you.

Operator: As a reminder ladies and gentlemen, if you would like to ask a question at this time, please press *1 on your telephone keypad. There are no further questions in the queue.

Dr Raouf Ghabbour: Yeah. Okay. Okay, I thank you – thanks ladies and gentlemen for joining the call and I wish to be delivering a very successful fourth quarter, hopefully by March. Thank you.

Operator: This will conclude today's conference call. Ladies and gentlemen, thank you for your participation, you may now disconnect.