

# Grupo Rotoplas

## 1Q20 Conference Call

**Carlos Rojas Aboumrad:**

Good morning. Thank you for joining us today. I hope you and your loved ones are safe and healthy. Our societies are facing complex times. The months ahead will be crucial in defining what our daily lives and our economies will look like in the future. However, I am confident that we will pull through, and together we will come out stronger to face new challenges.

As a client-driven water company, Rotoplas has been playing and will continue to play a key role in this crisis, particularly in light of the fact that ensuring the availability and quality of water is a more pressing concern than ever in all the countries we operate. We will continue to bring innovative and effective water solutions to our clients throughout the hemisphere just as we are committed to continue helping our communities. We are in an excellent position to achieve both objectives.

As some of you may remember, for the past two quarters we had been concentrating on strengthening and streamlining key aspects of our business through Flow, our transformational program. Flow is aimed at creating value for our shareholders via optimal capital allocation and increased growth and profitability, while upholding the highest ESG standards and our purpose. Flow remains an ongoing process, of course, but its preliminary results have put us in a strong position to address the challenges brought about by the current pandemic, as we ended the first quarter with a strong balance sheet, an improved debt maturity profile and, most importantly, a resilient client-focused business model and more efficient operations across the continent.

This past February, for instance, we successfully reopened our pioneering sustainable bond, Agua 17-2X, for the second time, netting 1,600 million pesos and extending the maturity to 2027. We also prepaid the outstanding \$600 million pesos from the previous reopening and closed two derivative positions on very favorable terms, bringing an additional \$372 million pesos. Combined with our quarterly growth and our improved efficiencies, including the divestment of underperforming assets which we undertook previously, this gains have greatly strengthened our balance sheet and brought down our debt ratio to 0.4x, all of it peso denominated, giving us significant flexibility in the current environment while fully covering our USD denominated operating expenses for the year. It is important to notice that all our debt is in Mexican pesos.

From an operational standpoint, we successfully implemented our Business Continuity Plan, transitioning the majority of our employees to remote working schemes. We implemented strict hygiene and safety standards and protocols, in accordance to the WHO guidelines, for the remainder who work in the manufacturing facilities.

The health and well-being of our employees is of the utmost priority for us, as is that of our customers and our communities. It is fortunate that, as a multinational company with diverse product lines, we already had a very robust and useful remote working and collaboration set of tools, which have significantly eased the current transition. We will remain attentive to the mitigation measures adopted across the region and, if necessary, will continue to adjust our operations accordingly. And of course, we will keep you updated of any developments as we have

been doing for the past weeks. As Mario will discuss in further detail, we expect that the current reduction in economic activity will have an impact on some of our product lines, but as I also mentioned, we will continue to provide much needed water solutions to help our clients cope with the current situation, particularly through our water-as-a-service platform and our strengthened e-commerce and telemarketing platform in the United States.

Finally, we reactivated the Water for Affected Areas Program or PAZA, which we developed in the aftermath of the 2017 earthquake in Mexico and have redirected it to address the needs of the health system and vulnerable communities in the context of the pandemic. We have already donated in México, Argentina and Perú over 500 storage solutions and over 1,000 hand-washing stations in public spaces as well as purification systems for hospitals, free of maintenance and operation costs for a year in the case of Mexico through the bebbia platform. Moreover, we will continue to work with NGO's and government institutions to identify new opportunities to bring more and better water to those in need.

We have been and remain fully committed to creating value for our shareholders and to the wellbeing of our employees, our clients, and our communities. The current situation demands that each of us do their part, for the sake of all of us. On behalf of our company, I reaffirm our vow to continue doing everything on our power to help our countries overcome this crisis.

Thank you for your time and attention. I will now turn over the call to Mario so that he can go over the quarterly results in more detail. I look forward to your questions.

**Mario Romero Orozco:**

Thank you, Charlie. Good morning everybody. Thank you again for joining us today. I too hope you are all safe and that we will be able to return to our regular schedule soon.

I will now go over some of the key aspects of our first quarter results.

Sales in Mexico grew 10% during the first quarter, due to increased demand for both products and our water-as-a-service platform, which grew by 12%, driven by an increase in sales of water fountains, treatment plants and, most importantly, of Bebbia, our drinking water platform which grew 55% during the quarter and doubled its sales after the adoption of mitigation measures in Mexico in the second half of March—a good example of the need and importance of access to water during the current pandemic.

We successfully executed our pricing strategy for our products ahead of our competitors and our new price-mix helped us offset the reduction in demand that followed the mobility restrictions during the last two weeks of March. Our plants and distributions centers are deemed essential and therefore continue to operate with strict safety protocols and reduced staffing.

Sales in Argentina fell by 19% in Mexican Pesos due to challenging macroeconomic conditions, the continuing depreciation of the Argentinean currency and a reduction in demand which was not compensated by an improved price-mix. Our plants in Argentina operated intermittently since March 20<sup>th</sup>, in line with governmental measures. We are currently prioritizing deliveries to the health system and donated or sold storage solutions under a preferential price to affected municipalities. We expect to participate in the installation of hand-washing public stations.

In Central America sales increased by 19%. This is was due in large measure to the changes we have enacted in our commercial teams and policies, better addressing the specific characteristics of each market and in line with Flow initiatives for the region. Our manufacturing and distribution operations have been affected in varying degrees by the different measures adopted in the second half of march to combat the pandemic.

Peru began a total lockdown after March 16<sup>th</sup>, following positive trends in both January and February. We have reduced our production in Brazil to adjust for the contraction in demand and are currently analyzing the prospects of services project pipeline, which seems to exhibit positive trends.

Finally, the demand for water solutions increased in the United States, as social distancing increased the demand for residential solutions and agro-industrial activities continue, these resulting in a 23% sales growth. Our e-commerce platform saw increased activity, most of our suppliers continue operating and we have secured the availability of delivery services through various logistics companies.

We will be monitoring the situation closely and adjust as necessary in all these countries.

It is important to note, at this point, that government sales as a percentage of total revenue remain well under our 10% target, amounting to 6.7% during the first quarter. An increase compared to last quarter due to programs that provide sanitation systems to areas with no sewage and drinking water fountains contracts for schools.

In terms of our portfolio mix, sales of products during the quarter accounted for 93% of total sales and grew 1.5% compared to the first quarter of 2019. Services, on the other hand, grew 12.2% year-over-year, attesting to the growing strength of our water-as-a-service platform. In particular, Bebbia, our drinking water platform, reached more than 27,500 purification points and 118 municipalities in Mexico by the end of March. In addition to these record sales for Bebbia, we registered a strong performance from our school water fountains business and continue to realize steady income from treatment plants. We added 7 new clients to the portfolio during the quarter.

From the top, quarterly net sales grew 2.2% year-over-year, which shows the resilience of our business model in the context of volatile environments. EBITDA and the EBITDA margin registered a minimum contraction, 0.2% and 40 pbs respectively. Gross margin increased more than 100 bps, as a result of the efficiencies brought about by Flow and reduced raw materials costs.

Net profits from continued operations increased as a result of the strategic divestment of underperforming assets last year and the unwinding of favorable hedging positions as Charlie already mentioned. Specifically, we closed an interest swap related to the outstanding Agua 17x that we prepaid in February and, given the depreciation of the Mexican Peso and our strong position in US dollars, a USD-MXN forward contract. The increase in net profits also caused a hike in our tax burden.

If we take out the gains on the hedging instrument, net profit would have amounted to approximately Ps. 193 million, a 104.9% increase compared to 1Q19.

As Charlie pointed out, the strengthening of the balance sheet through the prepayment and reopening of the sustainable bond program, the optimization of working capital, the discipline in capital allocation and some operative improvements, increased our cash and cash equivalent holdings by 82%, and we brought down our net debt to EBITDA ratio to 0.4x—well below our 2.0x ratio policy and all denominated in Mexican Pesos.

Also, CAPEX remains at a very sustainable rate of 4% of total sales. 34% of total \$77 million investments were allocated for water treatment and recycling plants.

We are continuing to work tirelessly to create value for our shareholders through our transformational effort, Flow. Our strong balance sheet is a result of that process, as are the discipline efficiencies we have brought about in capital allocation and our operations, including the optimization of our working capital. In fact, the preliminary results of Flow, have afforded us a degree of financial flexibility which should help us ensure that we address the challenges associated with the pandemic promptly and efficiently.

To this end, we have established a cashflow “control tower”, which convenes weekly to perform a detailed analysis and follow-up of our liquidity, income and expenses and our terms with both clients and suppliers, amongst other subjects. This not only strengthens the capital allocation discipline we had already established, but greatly increases our ability to address any issues that may arise in the coming weeks and months.

I would also like to point out that we continue to advance towards our goal of having a return on invested capital below our cost of capital by the end of the year. In fact, by increasing our ROIC and decreasing our weighted average cost of capital, during the first quarter we registered the lowest spread between the two in the past 15 quarters. The spread is now of 241 basis points.

Also, as has been pointed out, Flow aims to create value while upholding the highest ESG standards. To that end, this quarter we brought about four key initiatives and processes. The first one was to define our company’s value proposal for each of our stakeholders in the context of climate change dynamics. Through this exercise, we decided to focus in three main aspects: 1) promoting access to water for the “base of the pyramid”, i.e. the most vulnerable populations; 2) reducing waste and resource consumption, what is often referred to as “circular economy”; and 3) potentialize our water-as-a-service platform to increase the access to quality water in all of our communities.

Additionally, we undertook a gender equality diagnostic that will inform our efforts in this regard as well as our diversity efforts down the line. We also updated and disseminated our code of ethics and professional conduct. And, we reactivated our PAZA effort, which is now focused on bringing relief in the context of the pandemic under the name “PAZA C-19”

Finally, we will hold our General Shareholders Meeting on May 12<sup>th</sup>. The main proposals that will be considered can be summarized as follows:

- 1) The approval of a capital reimbursement through capital reduction in the amount of forty cents through exchange of shares of the company and forty cents in cash.
- 2) The ratification of the 15 members of the Board of Directors, including its 8 independent members, the ratification of the current committee composition and the compensation for the members of the Board and its committees; and

- 3) The approval of the total sum allocated to the share repurchase program for the fiscal year 2020 in line with our shareholder value creation strategy, which may amount up to total net profits, including retained earnings, as of the end of 2019.

We expect that the economic downturn associated with the pandemic will have an impact across all of our major markets. However, it must be reiterated that we have a very strong balance sheet and will use the flexibility it affords us to ensure that we are in a position to continue serving our clients and strengthening our water-as-a-service platform through the pandemic and in its aftermath.

In terms of the Guidance for 2020 given the volatility in the different markets where we operate we would rather prefer to remove it an focus more on balance sheet management and cash flow generation.

We believe that, as a water company, our products and services play a key role in the current crisis and we will be closely analyzing its impact on our client-base and our project pipeline. However, we are confident that our business model will continue to prove its resilience, as it has done in the past when faced with complex political and economic environments.

Thank you for your time today. As usual, we will now answer any questions you may have. Operator, could you please open the line for questions?

#### **Operator**

Thank you, sir. If you would like to ask a question, please signal by pressing star, one on your telephone keypad. If you are using a speakerphone, please make sure your mute function is turned off to allow your signal to reach our equipment. Once again, that is star, one if you would like to ask a question. We'll pause for just a moment.

Mr. Rojas, there appear to be no questions from the audience at this time.

#### **Carlos Rojas Aboumrad**

Should we proceed with the questions from the webcast?

#### **Mariana Fernandez**

We have a question from Antonio Rodriguez from ProFuturo. What was the estimated growth in the revenue for 2020 before COVID-19? What is the estimated growth in revenue for 2020 considering such pandemic situation?

#### **Carlos Rojas Aboumrad**

Regarding 2020 sales, I'll allow for Mario to complement, but we do continue to see strong demand for our solutions. While demand continues to be strong because of the need to access water of good quality in some of the cases, it's not possible to access these solutions, as a consequence of what different markets are regulating. For instance, in case of Peru, the country was completely shut down, including all stores, and there were no sales for some of the days of March

In terms of our forecast for 2020, I will allow for Mario to complement the answer.

**Mario Romero Orozco**

Yes. Thank you, Charlie. As I explained during the conference call, we prefer rather to remove the guidance we gave for 2020. Given all the volatility and uncertainty there is week by week a new development we are facing. As explained during the conference, we experienced lockdowns in Peru, Guatemala, Honduras, Nicaragua. It's hard to manage any expectations given all that volatility.

I would tie that up to the question from Antonio from ProFuturo. Before COVID-19 the guidance we gave to the market was sales of about 10%, and EBITDA margin of about 18%, net debt to EBITDA about two times, and ROIC equals about WACC.

I would say that, as mentioned, we're going to be more focused in balance sheet management and cash flow generation rather than P&L. The reason I'm saying P&L is because what we explained before. There's a lot of volatility there. It is not a supply issue that we're having, it's more the demand from the consumers. With mobility restrictions and lockdowns, you know anything can happen.

We are committed to have ROIC equal or above WACC, and we are committed to managing very tightly cash flow generation and the balance sheet.

To give you an idea, Antonio and Liliana, we lost during March about 10% of the quarterly sales from the different lockdowns and interruptions through the different countries where we operate.

**Mariana Fernandez**

We have another question from David Seaman. Can you please provide more details on Bebbia)? For example, are you able to enter households to install and service as normal?

**Carlos Rojas Aboumrad**

As mentioned, we have a top priority making sure that we're safe and our customers are safe, and so we have implemented, in accordance to World Health Organization guidelines, both standards and protocols, and so we have put into place where countries or markets allowed to do as we have been considered an essential industry for this COVID situation. We have been able to access in terms of Bebbia customers' homes and continue to install the water as a service solution in terms of drinking water. We have been very successful. Demand has been very high. There are obviously concerns by customers that we do explain what our protocol in terms of sanitation is. They are confident with our service. They allow us to enter their homes and they're very happy with the alternative of just having us visit them once, as opposed to the alternative of having to access bottled water in a more recurring manner.

Bebbia continues to see a surge in demand, which is very, very interesting.

**Mario Romero Orozco**

Do you want to go to question five, Mariana?

**Mariana Fernandez**

Sure. We have another question from Mauricio Alvarado from Citi Banamex. Thank you for the presentation. Can you please expand on expectations on operating performance during the next month? Any concern?

### **Mario Romero Orozco**

As mentioned, we are going to be fully—well, first of all, thanks for joining the call Mauricio and thanks for the question. As mentioned, we are going to be fully focused on balance sheet and cash flow management. Our concerns are more related—well, first of all, we want to make sure all of our employees are safe and healthy. That's our main concern right now. Second, as explained throughout the call, all the lockdown and mobility restrictions are causing affectations in demand. That would be the concern. On the other hand, and as you know, being the water industry where water is crucial through this COVID-19 crisis, we are seeing constant demand for some of our products and services.

### **Mariana Fernandez**

The next question is from Rodrigo Salazar. What can we see going forward in terms of marketing expenses for the Service segment?

### **Mario Romero Orozco**

Thanks, Rodrigo, for joining us and thanks for the great question. We are seeing a big, big opportunity in Bebbia, which is the drinking water platform and e-commerce. We are really doubling down in our marketing and commercial efforts through this crisis. It might sound interesting, but I think our products or business models are pretty much designed to what is happening right now. We are doubling down our efforts, the water service platform and in the e-commerce platform.

### **Mariana Fernandez**

We have another question from Jose Cebeira. Hello Charlie and Mario. Congrats on the results and the significant improvement in the ROIC. I have just one quick question and is in relationship with the growth strategy. The Company has been able to deliver positive results despite the challenging environment as a result of the COVID-19 restrictions in some countries, but my question is regarding if this growth strategy suggests doing something different in the current situation with COVID-19 against the previous scenario?

### **Carlos Rojas Aboumrad**

Hello Pepe. Thank you very much for joining the call and for the question. I'll answer first and then allow for Mario to complement. It's funny how happen to be for Rotoplas. It's a transformation that really helped us be in such great shape basically in a very, very complex and difficult situation. The reason that we're doing it was because we knew the world was going to change. We didn't know it was going to happen as a consequence of COVID, but we did know that the world needed a different approach to water, and a different approach to doing business. What we see that COVID is really just accelerating these trends that we knew had to happen, which is leveraging the more digital capabilities, strengthening innovation practices and sustainability just becomes more relevant what is in the long term but it's obviously the way to go, being customer centric.

All of the initiatives we have designed were in alignment of what the world is going to need post COVID or in this transformation of the world, because the world will change and the world will change in a more accelerated way but it will change in the direction where it should have changed in the past.

Our purpose of generating well-being for customers, for society and for the environment is in great alignment with the transformation we'll see with COVID. Obviously, in terms of timing,

some initiatives might change due to timing, but in general just having—being passionate about servicing customer needs with the customer at the center of our strategy in a way where they have just a much better experience and where we service them in a much better way end-to-end, it's just super good alignment with the transformation we're seeing with COVID.

Mario, would you like to complement?

**Mario Romero Orozco**

No, I think you have said it all. Just I think I will only add that we started this transformation process more than nine months ago, so the Company is in very good shape to navigate through these challenging times.

**Carlos Rojas Aboumrad**

Mariana, thank you.

**Mariana Fernandez**

Well, thank you very much everybody. We hope you will join us again next quarter. Until then, we'll be sure to keep you updated of any relevant news as they happen.

**Operator**

That does conclude today's conference. We thank you for your participation. You may now disconnect.

**Mario Romero**

Thank you very much everybody. We hope you will join us again next quarter. Until then, we'll be sure to keep you updated of any relevant news as they happen.