Grupo Rotoplas
4Q23 Conference Call

Operator

Good morning and welcome to Grupo Rotoplas' results conference call. Please note that today's call is being recorded and all participants are currently in listen-only mode to prevent background noise. The host will open the floor for questions later.

[DISCLAIMER]

Today's discussion contains forward-looking statements. These statements are based on the environment as we currently see it and as such there may be certain risk and uncertainty associated with such statements. Please refer to our press release for more information on the specific risk factors that could cause actual results to differ materially. The Company disclaims any intention or obligation to update or revise any forward-looking statements, whether as a result of new information, further events or otherwise.

Please allow me to remind you that the company issued its earnings press release yesterday after market close. It can be found in the investor's section of its website. Also, the presentation for the call and the webcast link are in the investor's section.

[PRESENTERS]

Today's call will be hosted by Mr. Carlos Rojas Aboumrad, Chief Executive Officer and Mr. Mario Romero, Chief Financial Officer. I will now turn the call over to Mr. Carlos Rojas.

Carlos Rojas Aboumrad

Good morning, everybody. Thank you for joining us today.

[PERFORMANCE REVIEW]

2023 was a year that challenged us all on many fronts. We faced an adverse macroeconomic and climatic environment, marked by the strength of the Mexican peso and a series of climatic events that tested our resilience and adaptability. However, it was also a year where the strength of our strategy, the solidity of our operations, and our firm commitment to innovation and sustainability became more evident.

[P&L Development & Financial Guidance 2023]

This quarter our net sales saw an increase of 8%, reaching Ps. 3.4 billion. This figure is a record for a fourth quarter and our third -best performance historically, trailing only behind the two quarters of 2022 during the peak of the drought in Mexico. This growth speaks a lot about the resilience of our business model and our capacity in navigating market complexities.

Talking about our financial guidance, during 2023 we focused our efforts on the variables that were within our control which included promoting operational excellence, maintaining brand leadership, and growing our new businesses. Thanks to this approach by yearend sales saw a smaller decline than anticipated, reducing by 5%. This was fueled by a recovery in product sales and sustained growth in our services platform. Our EBITDA increased to a record high, reaching a margin of 17.5%. Our leverage stayed below the 2 times and lastly, though our ROIC was slightly below our revised 2023 guidance, it showcased a healthy increase from the previous year, maintaining a robust position well above the cost of capital.

[ESG Guidance 2023 and Achievements]

Talking about our ESG initiatives and progress, as you can see in this slide during the year, we met most of our ESG targets. We've diligently evaluated our tier 1 suppliers and significantly improved our Global Net Promoter Score to 76. We've made progress in reducing CO2 intensity continuing our commitment to be a net zero company by 2050. We also enhanced water purification, directly impacting the quality of life of many families. Our commitment to diversity continues, with a goal to reach 30% female participation in our workforce by 2025, and though this year we stayed behind our goal we continue to build a more inclusive and diverse workforce.

I'm also very proud to tell you that yesterday we were recognized again as a top ESG performer in the S&P Global Sustainability Yearbook.

[Alliances, Technology, and Programmatic M&A]

Our coming narrative evolves with strategic alliances, technological advancements, and programmatic M&A. Our collaboration with Google Cloud and SAP marks our commitment to a future where operations are driven by intelligence and innovation. This initiative not only improves our internal processes but also raises the quality of the solutions we offer to our clients. Also, the initiation of our Programmatic M&A Strategy with the acquisition of HiTech Irrigation of Mexico exemplifies our strategic approach to growth, enhancing our capabilities and market presence. These fundamental pillars that will support our growth and consolidation in the market.

Now, before I hand over the call to Mario, allow me to introduce my AI-generated voice. It will discuss a matter of great significance and urgency with you.

AI CHARLIE [Water Stress in Mexico and Rotoplas' Role]

Good morning, thank you for the introduction Charlie, I'd like to discuss the current water situation in Mexico. Mexico City, one of Latin America's largest metropolises, is currently facing a severe water crisis, as the capacity of the Cutzamala System has dropped to less than 40% according to CONAGUA. The system's struggles stem from a combination of factors, including years of insufficient rainfall attributed to climate change, rapid and disorganized urban growth, and aging infrastructure. This marks the most stressed state the system has ever experienced in its history, and it's very important that everyone adopts water conservation habits, especially given the approaching dry months and the recent trend of drier seasons.

The crisis has raised concerns about "Day Zero", a moment when water reserves may become insufficient to meet the needs of the population of the region. There are predictions that Day Zero could occur as early as June this year if the reserves of the Cutzamala System do not replenish during the rainy season. With only 8 of the country's 210 main dams at full capacity and the rest averaging 51%, the gravity of the situation is undeniable.

This critical water stress situation demands immediate and strategic responses. Rotoplas has risen to this challenge, offering not just immediate solutions but also demonstrating a long-term vision for sustainable water management.

Our decentralized solutions have proven indispensable, reaffirming our commitment as an ally in tackling this urgent water crisis. In 2023, through the A Fluir initiative, we delivered rainwater harvesting systems, offering benefits to individuals in both rural and urban areas. Additionally, reacting to the destruction caused by Hurricane Otis in Guerrero during October, our PAZA program was reactivated, providing essential support through monetary and in-kind donations. This initiative was instrumental in assisting partners, distributors, and customers by addressing their immediate needs and facilitating home reconstruction efforts, which included complimentary repairs of damaged water tanks. Collectively, these programs made a significant impact, benefiting over 290 thousand individuals and thereby reinforcing our role as a committed partner in addressing the water needs of the population.

Back to you Charlie.

REAL CHARLIE [BYE]

I want to close by expressing my deep gratitude for your continued support. Looking forward to 2024, the year presents itself as one of great opportunities and challenges. We are committed to advancing our fundamental initiatives and to providing solutions that support the population in adapting and mitigating the effects of climate change. We are convinced that, with our strategic vision and capacity for innovation, we will not only overcome current challenges but also lead the way towards a more sustainable and resilient future in water management for the benefit of present and future generations.

Now, I Will turn the call over to Mario to provide you with a more detailed perspective of our financial results.

[Financial Highlights]

Mario Romero Orozco:

Thank you, Charlie. And thank you all being here.

[ACCOMPLISHMENTS]

As Charlie previously highlighted, this quarter marked a return to positive sales growth, with notable increases in services as well as improved market dynamics in our product sales.

The targeted approach to focus our efforts on the three fronts under our control allowed us to achieve a balanced annual outcome. We've encountered our share of challenges but have consistently aimed to create value for our stakeholders in three key areas: profit, people, and planet.

Looking back over the past year, it's clear we've journeyed through a mix of triumphs and challenges.

Kicking off with our significant accomplishments, we not only upheld our brand leadership but also witnessed double-digit growth in our services sector, coupled with a 2-percentage point increase in our EBITDA margin compared to 2022. Alongside this, we achieved record customer satisfaction levels and rolled out our new storage technology in six of our eight Mexican plants. Also, our initiation of Programmatic M&A activities through an asset acquisition aimed at propelling our irrigation solutions forward stands out as a strategic move. Moreover, we enhanced our cash conversion cycle and sustained healthy leverage ratios, underlining our financial prudence.

On the flip side, the journey wasn't without its hurdles. The aftermath of 2022's drought set a high benchmark, complicating year-over-year comparisons. The "Super Peso" phenomenon posed challenges for our consolidated sales in international markets, with exchange rate fluctuations and hedging activities impacting our financial performance and our cash position. We also had to adapt to competitive pricing dynamics as raw material costs fell. Macroeconomic and political developments in Argentina, Peru, and Central America, along with climatic adversities such as the US's wet season and El Niño in Peru, further tested our resilience.

Now, just as Charlie introduced you to his AI generated voice, let me hand the call over to mine to discuss the P&L and country-specific results.

AI MARIO [P&L]

Thank you Mario. Looking into the details of the P&L, starting with the top line, fourth-quarter sales grew by 8%, benefiting from the growth in services and a recovery in product sales, especially in Argentina and Mexico.

The water shortages in the Valley of Mexico, along with our Blue Offers or "Ofertas Azules" campaign, helped us record the best storage sales for a December in the last seven years in Mexico.

Our strategy this last quarter was to balance annual growth with profitability, promoting demand through pricing strategies while safeguarding our EBITDA margin for the year.

Consequently, while annual sales fell by 5%, we managed to achieve a 2-point increase in our margin. As mentioned, net income was impacted by higher operational and financial expenses due to the exchange rate effects.

Let's dive into our regional performance.

AI MARIO [Sales per Country | Mexico, Argentina & US]

Starting with Mexico, we are seeing strong traction in emerging businesses such as bebbia, RSA, and rieggo. Additionally, the product division is beginning to show a recovery in demand. Mexico has recorded a historic high EBITDA margin.

Sales in Argentina have grown in volume, but primarily through pricing. We continue to focus on maintaining profitability, improving plant productivity, and increasing market share.

In the US, the decrease in sales was influenced by several factors:

- The unusual wet season in states like California and Texas, which account for a third of the country's total sales.
- A normalization in the demand for storage solutions following years of pandemic and an agricultural boom in states such as California, Oklahoma, and Michigan.
- Slower than expected development in the septic business due to the wet season and delays in obtaining licenses and permits per county for primary water treatment solutions.

Turning our attention to performance in Central America, Brazil, and Peru: The drop in sales is associated with the following:

In Central America, sales grew by 10% in local currency over the year. However, the impact of the super peso adversely affected the consolidated sales.

In Peru, economic challenges continue, as demonstrated by a decrease in government spending, consumer activity, and private investments. Our sales of water heaters in the region encountered hurdles, mainly due to a milder winter brought on by the El Niño phenomenon.

The wastewater treatment plant business in Brazil is still in development but shows good prospects.

I will hand the microphone back to Mario for him to continue with the call:

[Sales | Products & Services Mix]

Regarding our portfolio mix, product sales accounted for 95% of total sales during the quarter and the full year.

Services displayed 32% growth in the quarter and 43% over the year, largely backed by bebbia and our water treatment plants. Our focus remains on reducing the division's negative EBITDA impact while optimizing our product-service mix.

Now, examining our financial stance:

[Cash Position]

Our financial stability is secured by a robust balance sheet, providing a solid foundation for driving growth and profitability.

We maintained our net debt to EBITDA ratio at 1.6x, comfortably below our established threshold of 2x leverage. To provide further context, this figure includes a short-term USD-denominated loan from the US amounting to 1 million, in addition to the proceeds from our sustainable bond, AGUA 17-2x, which total 4 billion Mexican pesos.

A notable achievement has been the refinement of our cash conversion cycle. Principally through strategic inventory and supplier management, we've successfully shortened this cycle, underscoring our commitment to efficient working capital management. The revaluation of the balance sheet in Argentina also contributed positively in the fourth quarter.

However, it is crucial to acknowledge that our cash reserves have decreased, primarily due to capital expenditures, dividend distributions, and the impacts of our FX hedging strategies.

Now, moving forward to our Discipline in capital allocation:

[Discipline in Capital Allocation]

During the quarter, we increased our CAPEX to close the year at 5% of our sales, representing an 8% decrease compared to the previous year.

The majority of our 2023 CAPEX has been strategically allocated towards enhancing our core product business, with a special focus on Mexico. This deliberate investment not only strengthens our foundational offerings but also positions us well to capitalize on emerging growth opportunities.

During the quarter, significant investments were made in water treatment and recycling plants in Mexico, totaling $122 million, accounting for 2% of our total CAPEX for the year.

[ROIC vs Cost of Capital]

Our Return on Invested Capital (ROIC) increased by 80 basis points to 14.9%, significantly above our cost of capital.

Now, I would like to highlight some noteworthy actions in the framework of our sustainability strategy:

[ESG Initiatives & Progress]

Aa Charlie mentioned, we've achieved five out of our six public goals this year. In addition, we've been honored with five significant awards and recognitions across Mexico, Argentina, and Peru, which I believe is a testament to our team's hard work and dedication.

In the area of environmental sustainability, our efforts have been focused on reducing CO2 equivalent emissions and adopting a circular economy in our processes, notably through the use of recycled resins and the revalorization of waste. These initiatives not only contribute to our planet's health but also drive us towards a more sustainable and cost-efficient operational model.

This Tuesday, we received the results of the CDP questionnaire, and our performance in the climate change dimension has improved from a B to an A-. This advancement elevates us to a leadership level, surpassing the industry average, as well as the averages for North America and globally.

On governance, we maintain our dedication to an ethical culture and anti-corruption. We have enhanced our risk management strategies and reinforced our Sustainability Committee. Moreover, the creation of our Diversity and Inclusion Committee marks a significant step forward in ensuring our governance structures reflect our values and commitment to all stakeholders.

In the social or people dimension, we have actively engaged in volunteering activities, such as cleaning water bodies and building bathrooms, which directly contribute to improving the quality of life in the communities we operate in. Our efforts to create a more inclusive and respectful environment through our gender, LGBTIQ+, and people with disabilities subcommittees have been particularly rewarding, fostering a culture of respect within our organization.

[Guidance + AGUA*]

Now, before discussing our guidance, I would like to emphasize that in yesterday's board meeting, a decision was made to propose to the Shareholders' Meeting a cash capital reimbursement for the company's shareholders. This will be facilitated through a reduction of the capital stock, with a distribution of fifty cents for each outstanding share.

Finally, looking ahead to 2024, and considering the variables we currently have visibility on, we are setting our expectations for:

- Growth of 10% or more
- An EBITDA margin between 18% and 19%
- A net debt/EBITDA ratio below 2.0x
- A spread between ROIC and cost of capital of at least 200 basis points

We deeply value your trust and support as we continue to navigate this environment. I now open the floor for our Q&A session. Thank you for joining us.

[Q&A]

Operator: Thank you. You can submit your questions by pressing the Q&A button. Please include your name and the name of the company you work for. The first questions, because there's two of them, come from Carlos Alcaraz from Apalache Research. And as they might be related, I'm going to read them together. "Good morning, Carlos and Mario. First, congratulations on the record results for the quarter. The first question is about the SG&A expenses. Could you give us more color on the factors that drove this growth?" And the second question is: "related to operating margins during this year, will you continue with a strategy of increasing prices, or will you be looking to increase sales volume for greater cost absorption and maintain the growing trend in the margins?"

Mario Romero (CFO): You're on mute, Charlie.

Carlos Rojas Aboumrad (CEO): Excuse me. Do you want to first talk about SG&A?

Mario Romero (CFO): Sure. Thanks, Carlos, for joining this morning and thanks for your questions. Surrounding SG&A, basically they were driven by commercial and marketing efforts to maintain brand leadership in the product division. Just to share with all the community we increased our market share in all countries and in all segments of products. So that's a great achievement. Obviously, we put a lot of emphasis on the marketing efforts. In addition, as we show in the numbers, the growth in services is gaining a lot of momentum. So additional efforts in marketing, have been put towards it. So that's one part that explains SG&A expenses. The second part is the IT digital strategy that we've been putting in place and we've been sharing with you guys around GCP or Google Cloud Platform with SAP rise. Part of those efforts of digitizing the company account as an increase in SG&A. Obviously the company will benefit from those two increase SG&A and going forward but that's mainly what drives SG&D and for the quarter and the year.

Carlos Rojas Aboumrad (CEO): And then regarding your question about, operating margin going forward, we do not see, what we did saw on the previous year. We don't see raw materials will decrease in the same way that it happened. So we do see more likelihood of an increase in prices and we do see a tremendous opportunity in growing volumes of sales of our products. And so with that, the operating margin is going to be benefited. The driver for the revenues in the product sales is definitely the water scarcity we're experiencing in many of our markets. It's like any other moment we've ever seen at least in the past decade. It's a very critical situation, and I fortunately, we think our solutions will be part of the solution to that situation. And that should be reflected in revenues. Anything else regarding operating margin, Mario?

Mario Romero (CFO): Well, just touching on the prices we expect to increase prices throughout the year relative to the inflation. As you know, we operate in 14 different countries, so prices will be increased differently according to local needs.

Carlos Rojas Aboumrad (CEO): Thank you. Carlos.

Operator: Thank you, guys. Next question it's from Carmen Barroso from Miranda Partners. "Thank you for the presentation and congrats on the results. My question is regarding services growth. How do you anticipate sustaining this trajectory going forward?"

Carlos Rojas Aboumrad (CEO): Well, I think what Mario mentioned in terms of building platforms, building digital and technological capabilities is key here. We've seen that the design of the business model and of our unique value proposition is one that aligns very well with the needs in the market and the needs in the environment. And so we are seeing very positive reaction from our customers in wanting to adopt the solutions, which are novel. It is very important that we have the capability. So we've been working very much in the capabilities that would be able to sustain, accelerated growth rates. And this has been a big investment that we've been making. It continues to grow the investment. And so it explains a little bit of those expenses that we've had in 2023. But it is the pillars that enable us to be able to serve on a much bigger and bigger customer base. When we're growing at these rates, and when we look at the number of customers we have, the new customers we're expecting for the next year is so much larger than the new customers from the previous year. And so it is very important that we focus on these digital capabilities, service capabilities and processes. Mario, anything else that you'd like to compliment.

Mario Romero (CFO): Just probably it can be worth to remember Carmen, which by the way, thanks for being here this morning. That the services business, our markets are ten times larger than the product segment. So, it's a new market, blue ocean opportunities there and the company is building those markets and trying to be the leader in those markets. So I think the market by itself presents an opportunity, and as Charlie was mentioning, I think, is building, the capabilities and skills to access those markets and create value for all the shareholders.

Carlos Rojas Aboumrad (CEO): Thank you Carmen.

Operator: Next question is from Martin Lara, Miranda Global Research. “Good morning, congratulations for the strong results and thank you for the call.” And the question is: “could you please explain the reduction in working capital needs and specifically in inventory levels and accounts receivable in the last quarter, and what can we expect going forward?”

Carlos Rojas Aboumrad (CEO): I'll let Mario take this one. He did a phenomenal job.

Mario Romero (CFO): I think it's a great result, this morning, we were having our town hall meeting with all the company, and we were, congratulating all the teams that make this possible. We're very happy with the result. It's sometimes when you ask people to achieve better, sometimes they said, "results above expectation" and I think this is a case. Going forward, we're being more conservative. I think 14% as a percentage of sales I think it's on that very aggressive side. Historically, the company has been hovering around 18, 19%. So now that that we know that the teams can achieve 14%, I think a good new threshold is going to be somewhere around 16 to 17% of revenues. We're being conservative, obviously, we're seeing some benefits of digitizing more of our processes to achieve this kind of working capital management but please don't be aggressive on your financial model. And let's wait on the 17% as a percentage of sales.

Carlos Rojas Aboumrad (CEO): Just a quick compliment. We saw pressured demand last year, and so we became very disciplined. And like I mentioned, we have a team that executes in a way that makes this company very resilient. So I think it a way of showing how resilient this company can be. But also, as mentioned, the water stress in some of our markets is very high and we expect higher demand. And so obviously we need to also prepare for that, potential demand. And so that will drive those inventory levels to where Mario was stating, thank you, Martin. Thanks for joining.

Operator: Next question is from Regina Carillo, GBM. "Good morning and congratulations on the results. And I have two questions. The first one, could you tell us more about the Ofertas Azules strategy that you implemented this quarter? And the second one, given the current water scarcity situation in Mexico, with further strains in water supply expected for the coming months, what will be your business strategy here and will you be working on any specific programs with the government or institutions to mitigate it?"

Carlos Rojas Aboumrad (CEO): Thank you very much for your question, Regina. The Ofertas Azules promotion happened before there was this shortage. I would say, before the shortage of water that had been happening. But before the operating companies started restraining the supply of water. And we had, um, commitment of growing our market share. We saw a good opportunity to grow market share. And that was nature of the strategy. And like Mario mentioned, we did grow market share in products in all of our markets. And so that generated a very good result. Also, regarding your second question, or would you like to mention anything regarding the as soon as Mario?

Mario Romero (CFO): No, no, I think you just get it right.

Carlos Rojas Aboumrad (CEO): And regarding what we see in Mexico going forward in terms of the situation and the potential demand, we do see, an opportunity particularly in Mexico City, the metropolis, the largest metropolis in the continent, we see it with a very painful situation where water supply will be limited very much. And our solutions are tremendously important for these situations. So we do expect higher demand and the way we'll prepare for this is developing our manufacturing capability and our inventories so that we can serve this opportunity like we've done in the past in other markets, like in 2022, there was a big situation in Monterrey. So Rotoplas is incredibly nimble in these solutions, and we're able to increase capabilities very quickly and to prepare for these situations. We would love to collaborate with the government in promoting a practice of lower consumption of water. It is important that we as a population, as society, we reduce our consumption of water. It's a very key component to navigating the situation. Then there's obviously a very, very important opportunity of capturing rainwater and using that rainwater so that when there's rain, we allow for the system to replenish both on the ground water and the dam system. And also of treating and reusing water. It's already required that big buildings and industrial buildings treat and reuse water. It's important that we make traction with a water treatment model to facilitate this happening. All of these customers usually don't have the expertise to do something as sophisticated in the water industry, such as treating to the level of reuse and then doing the actual reuse. And so this is where Rotoplas is a big opportunity to be a partner for these users and supplying them with the right technology, the right implementation capabilities, and the right operation and maintenance capabilities for this to be sustainable. Mario anything else?

Mario Romero (CFO): Well, let me just compliment on another issue around what are we seeing in Mexico.

Carlos Rojas Aboumrad (CEO): And also irrigation? I forgot about that one.

Mario Romero (CFO): Yes. And from those 20 reforms that the current president of Mexico sent on Monday there's one around water. And more than getting into the debate on the content, I think he highlights what I think is going to be the strategy going forward. And what we capture from that idea is that they're going to be protecting the water consumption for individuals and less water available for industries and the agriculture, so that we believe is going to create a lot of different opportunities for our water treatment and recycling business and as well for rieggo business going forward. So that's what we see in Mexico. In Brazil, as you know three years ago, a new legislation passed on and there are forcing to all industries and private industrial consumption needs to be done by private. We're seeing a lot of that happening also in Brazil. So, all in all, we are seeing a lot of focus from different governments and authorities on how we manage and treat water, and I think that eventually will translate into business for Rotoplas.

Operator: Now we have Felipe Barragán at BTG Pactual with two questions. I'm going to read them separately. So starting with the first one, "what's the status on the programmatic M&A and when can we expect the first acquisition to be made?"

Mario Romero (CFO): Okay. Well, the status of programmatic M&A. First of all, programmatic M&A, it's a process by itself. So it's something that is running every day. In the company we have a small team of people working around, building this capability, sourcing deals, looking for different alternatives of growth on these three strategic venues that we highlighted the last quarter. Just to remember, the focus is on rieggo, on water treatment and recycling in Mexico and Brazil and in bebbia. Regarding the first acquisition was the hi-tech acquisition we announced a couple of months ago. And there are a couple of news coming in the coming weeks. We expect to be announcing more of those small deals to enhance our strategy and growth going forward. And well, sorry Felipe, thanks for joining us this morning. I didn't say hello.

Mario Romero (CFO): You want to compliment anything?

Carlos Rojas Aboumrad (CEO): No, no. Thank you Felipe.

Operator: Thank you. Going to Felipe's second question. Could you touch on the pricing strategy used in Argentina this quarter, specifically, was there anything that changed this quarter vs. the previous quarters and what can we expect for the rest of the year?

Mario Romero (CFO): So basically Argentina, as we all know, inflation last year was 211%. You cannot lose a single day of not increasing prices. So the discipline we have in Argentina is that we increase prices every single month, pretty much in line on what our inflation expectations. So that is what we've done. We did it last quarter and we did it on the third, second or first quarter. So that's the pricing strategy in Argentina. Going into 2024, we're going to be following, the same strategy. We are expecting inflation somewhere around 100%. So the team is increasing anywhere from 8 to 9% their prices on a monthly basis.

Carlos Rojas Aboumrad (CEO): Can I go to the next one? Mariana, please?

Operator: The next one comes from Rodrigo Salazar from AM advisors. Hello, thank you for the call and congratulations on the results. I have several questions, so I'll be reading the first one. The water situation in Mexico is worrying, how much of the growth of 2024 is driven by these dynamics in Mexico.

Carlos Rojas Aboumrad (CEO): There's obviously part of the growth that we've projected as consequence of this situation. Now it's a situation that is not extremely consistent, but the trend is always that we're getting into a more and more critical situation of water stress. And so it has been the case also for the previous years. When we look at volumes. Volumes continued to grow. And the reason they continued to grow over our solutions is because the water stress situation worsens year by year as a trend. How much will it happen this year? It really depends on the policies, the operation practices of the water companies. Which is out of our control, but we do see that there's going to be a higher demand from it. Anything else that you'd like to comment regarding this? And by the way, thank you very much for joining Rodrigo.

Mario Romero (CFO): No

Operator: What drove the improvement in services EBITDA, its seems you are putting a lot of capex to water treatment plants, when we could start to se the benefit of these new investments?

Carlos Rojas Aboumrad (CEO): What would you care to explain, Mario?

Mario Romero (CFO): One of the reasons we're seeing improvement in services in EBITDA is obviously the scale as the business unit gets larger, such as bebbia, rieggo and so on the absorption of fixed costs is much better. So that's an improvement of services. The second one is that we are considering to, we found a way to capitalize on the equipments that we installed in bebbia and that also is improving the EBITDA because now we can account for those, uh, purification units into the balance sheet and we can depreciate in a four-year period. Uh, so those two are the main reasons behind the improvement in services in EBITDA. And the benefit, I think, is as those businesses keep on growing at a higher rate as we showcase. I think you'll see those benefits in the coming years.

Operator: Another question from Rodrigo. It seems margins in products Mexico saw a strong decrease, was this driven by the discounts given or is there some other explanation?

Carlos Rojas Aboumrad (CEO): You're mentioning the decrease in prices, right? There were the discounts, but also there were decrease in prices that happened halfway through the year. So that did impact on margins. Now that we don't see that going forward, as we mentioned and we do see that between growth in volumes and being able to raise prices according to inflation, margins will recuperate in products. Mario, anything else that you'd like to comment?

Mario Romero (CFO): No, it's very, very straightforward. What you mentioned Charlie. And I think you skip question number three, Mariana.

Carlos Rojas Aboumrad (CEO): Can you just mention the question for everyone's benefit, please?

Operator: Yes. What exchange rate in Argentina are you using for your guidance. And did you use average exchange rate in the fourth quarter?

Mario Romero (CFO): We started at 800 and we are doing a monthly devaluation according to what the government in Argentina has announced. So we're starting off at 800 for January and so on all the way throughout December. They say that it's going to be running at 8% per month. So pretty much, that's how we, did our budget for 2024. And then, on the fourth quarter, yes, we use average exchange rate, which is how we compute our numbers according to accounting rules.

Operator: And now, moving to the last question on Rodrigo's side. What could we expect for CapEx investments in 2024 and where will it be allocated?

Mario Romero (CFO): What we're going to be doing in terms of CapEx, you should expect a range from 3 to 4% in CapEx for 2024 as a percentage of sales. We're going to be doing the tale of the Tinaco Plus, as we mentioned in the call. There's still two factories missing out with the new technology. Also, we're going to be, kicking off the technology in Peru, the new technology for water tanks. So I would say that's to protect the core. The other part would be maintenance CapEx to keep the business running. And, and the rest will be on water treatment and recycling plants. So that's more or less where CapEx is going to be allocated in 2024.

Operator: Thank you. Our next question is from Emilio Antor from GBM. With this continuous growth in services for the fifth consecutive quarter, have your expectations of EBITDA break even changed?

Carlos Rojas Aboumrad (CEO): Thank you for your question Emilio. Not necessarily. We're trailing pretty close to our plan and the very accelerated growth in bebbia, has a very big investment in acquiring our customers. And so as we see an opportunity to continue to introduce this novel solution with this novel approach of subscription to our markets, we will continue to invest in that customer acquisition. So, it has to get still much larger and growth rates need to reduce a little bit for EBITDA to see big,

big, big changes. Now, we are seeing that the unit economics of these businesses are generating value. And so we feel very comfortable with investing, um, or having these losses in EBITDA in services, as we have clarity that the unit economics for these customers are profitable. And so just on the investment, which is reflected as expenses that affect EBITDA generating losses, it's something that is of benefit for the growth of the company in a profitable way going forward in a new business model Mario. Anything else that you'd like to comment?

Mario Romero (CFO): Well, yesterday, precisely at the Board meeting, we were discussing around bebbia and the business unit manager confirmed that he expects that by 2026, a break even in bebbia will be achieved. rieggo and water treatment and recycling: rieggo we're expecting to have a positive EBITDA, in 2024 and water treatment and recycling when you put together or combine Brazil and Mexico, that's going to happen in 2025. So they have not changed but I think we are just validating the milestones that we disclose to the market a couple of quarters ago.

Operator: Thank you. Martin Lara from Miranda Global Research is asking, the 2024 ROIC guidance seems conservative compared to the figure that you reported in 2023. Could you please elaborate on this?

Mario Romero (CFO): I think there's a lot of macro elements that can move the cost of capital throughout the year, and that's mainly tied to what the central banks will do with interest rates. So we are being conservative in that spread. And on the ROIC guidance as well, until we don't have more clarity on what are the central banks doing throughout the year. So that's one thing and the other thing is, as you all know, Argentina, with the massive devaluation in December, you know, the market in Argentina is reshaping, by itself. So those two things are the reason why we prefer to be conservative on the spread on the ROIC.

Operator: Thank you. We have one last question. It's from David Seaman from Alpha Cygni Does capitalizing the bebbia units explain all of the increase in D&A? If you are now capitalizing purification units, rather than expensing upfront, does that allow you to reduce the bebbia ASP to drive faster growth?

Carlos Rojas Aboumrad (CEO): Do you want to first talk about the D&A, Mario?

Mario Romero (CFO): Sure. To your question: yes, that is most of the increase of the D&A comes from that capitalization in the services segment.

Carlos Rojas Aboumrad (CEO): Some of it was due to water treatment plants, as you mentioned.

Mario Romero (CFO): And the remainder was on water treatment plants.

Carlos Rojas Aboumrad (CEO): Then regarding, how this impacts the growth model, I do think it impacts it in terms of how we perceive the business slightly. Where we might feel a little bit more aggressive in trying to grow the business. But this is very recent and so I still wouldn't be comfortable in giving you a more detailed impact in the growth model. We do still have a very high customer acquisition cost, as we're still in the early stages of adoption. And so educating the consumers on this model is very expensive. Thank you for your question, David, and thanks for joining. But if you would please also follow up on this later on, a few quarters from now, we can maybe share a little bit more details on the impact it has on our model.

Operator: Thank you. So that was the last question. Mario, would you like to answer something else?

Mario Romero (CFO): No.

Operator: Okay. Perfect. Let us share a poll. If you have one more minute, we will really appreciate if you could answer three questions in a poll about the AI voices and the presentation. Thank you very much.

Mario Romero (CFO): Do we know the results? Or are we going show them next meeting.

Operator: Yeah. Next meeting. So we will just wait ten more seconds and then we can close the webinar.

Mario Romero (CFO): We'll leave those ten seconds. Let me just finish with probably David Seaman question on ASP. I think, just an overall conclusion on this is: capitalizing the cost of purification units rather than expensing them upfront can provide Rotoplas with a more flexibility in its financial reporting and potentially allow for a strategy that includes reducing the bebbia ASP to drive faster growth. However, we should be careful and carefully manage that we align all these new criteria, with the company's overall financial health. And as you know, we're very conservative on that. So, we'll keep the market and investors informed of all the changes. So, as you know, we want to achieve long-term sustainability. And I think that's the uppermost and important objective, for the company and bebbia by itself.

Carlos Rojas Aboumrad (CEO): Thank you, Mario, and thank you everyone for joining.

Operator: Thank you. See you next quarter.

Mario Romero (CFO): Thank you. Have a have a great rest of the week.