

# Grupo Rotoplas

## 3Q19 Conference Call

### **Carlos Rojas Aboumrad:**

Good morning everyone. Thank you for joining us today for our third quarter conference call.

As some of you might recall, in our last call I laid out the four pillars that guide my tenure as CEO: constant evolution, embracing digital technology, permanent product and service innovation and promoting talent development in our team. Through these pillars, we continue to fulfill our company's mission for people to have "more and better water", bringing useful and effective decentralized water solutions to our customers across the Americas, improving their well-being and providing them with a superior experience. And, just as importantly, we continue to do so while upholding and expanding our commitment to sustainability not only in our own operations but in the communities where we do business.

We aim to have a positive social impact and to do so while growing and creating value for our shareholders. And it pleases me to report that we continue to grow in spite of what most people would agree have been challenging economic and political environments in many Latin American countries, including some of our major markets. Our brand and our strategies make us resilient and adaptable, allowing us, for example, to grow and gain market share in the context of adverse macroeconomic conditions in Argentina, where we have managed to outpace inflation and grow 10%, even after accounting for the depreciation of the Argentine Peso. Or as in the case of Mexico where, as anticipated in our last call, our water-as-a-service platform had a very significant positive impact in our results due to the success of our water treatment and recycling solutions and the growth of bebbia, our drinking-water platform. And

Central America, a competitive environment that entails significant logistical challenges and where our increased regional penetration led to double-digit growth.

Throughout four decades, Rotoplas has grown and learnt, constantly facing new challenges and overcoming them, becoming more innovative, diversified and resilient in the process. Nevertheless, it is now time to go further. As I said, Rotoplas is committed to creating value for its shareholders and to do so, it must transform itself, evolve, to ensure that it reaches its full potential as a public company, to grow and increase profitability.

In order to do so, I am excited to share with you that we have started a transformational program for the company, which we have named Flow. Flow has two major components. The first one is the optimization of our production, procurement and billing processes as well as our pricing strategies, while at the same time continuing to promote sales growth across our markets. The second one is to focus on the key innovation drivers for future growth, including enhancing our water-as-a-service platform vision through constant innovation and continued expansion and pursuing an optimal growth strategy.

This is a major effort for our team and our company, but I'm confident that we will achieve the objectives we have set for Flow by the end of next year. We are looking deeply into our operations, building on previous initiatives and introducing new ideas and perspectives with the participation of all areas in our company. Likewise, as we mentioned in the last call, we continue looking for opportunities to streamline our operations and increase our return on invested capital above cost of capital within the period of 18 months.

Such is the case of the sale of our manufacturing assets in the United States, which will fuel the growth of our e-commerce platform and increased our returns.

As we look to the future, I am confident that Rotoplas will reach its full potential and that it will do so while continuing to adhere to the highest ESG standards, helping to preserve water as a future resource and

engaging in collaborative innovation for the benefit of our societies. We will continue to do what we do best: permanently introducing new and better products and services, seeking new avenues for growth and delivering the best experience for our customers.

I will now turn the call to Mario so that he can go over some of the financial highlights of our quarterly report. Thank you for listening and I look forward to your questions.

### **Mario Romero Orozco:**

Thank you, Charlie.

Good morning everybody. Thank you for joining us. I will now go over some of the key financial aspects of the third quarter and the first nine months of the year.

### **ESG – RESULTS**

It is very encouraging that Rotoplas is included in the Dow Jones sustainability indices and the sustainable index created by S&P and the Mexican stock market for the third consecutive year. These indices only include the best performers in ESG principles and best practices as evaluated by expert third parties, and in the case of the S&P/BMV Sustainable IPC, only 30 companies are included. Likewise, it is very encouraging that our ESG score, as measured by Bloomberg, puts us in the top ten of Mexican companies. As such, our inclusion not only signals our commitment to sustainability to the investment community, which as you know is an increasingly important investment criteria for global investors, but it also validates our team's efforts and pushes us to go even further. Now, more than ever, it is imperative to create value in a sustainable way and it has become our way.

## SALES PER COUNTRY

In terms of our geographic breakdown, quarterly sales in Mexico grew 5% year-over-year, in spite of the economic slowdown with a major contribution from storage related products and our water-as-a-service platform. As we anticipated in our last call, water treatment plants whose contracts were won in previous quarters and which began operating in this period once its construction was completed, increased sales by 22%.

Furthermore, bebbia, our drinking-water purification platform reached more than 18 thousand purification points and has doubled its billing speed.

In Argentina, sales in the third quarter continued to exhibit a positive trend, growing 10% and increasing market share across all three business categories that we have in that country which are water storage, flow and heating despite the macroeconomic tension stemming from the primaries elections, the fall of consumer confidence and the depreciation of the Argentinean peso.

Sales increased 38% in the first nine months, driven by the acquisition of IPS. Organic growth in local currency was 71% while the inflation rate was near 50%. It is worth noting that during this period the Argentinean peso depreciated 41%, affecting the Group's growth in Mexican pesos by 11 percentage points for the whole year.

Sales continue to grow at double digits in Central America, driven by enhanced client relations efforts and a strategy of focusing on smaller cities, which lack sufficient water infrastructure, enabling us to increase our market share and reach.

We faced a challenging economic and political environment in Peru, including a reduction in government spending, which resulted in a quarterly decrease in sales in water flow and treatment categories.

Finally, as Charlie already mentioned, we have great expectations for our upgraded e-commerce operation in the United States, where we reached an agreement with the purchaser of our manufacturing assets that ensures:

- a) product sourcing
- b) new product development
- c) nationwide presence

Finally, it is important to mention that government sales hit an all time low as they now only represent 1.4% and 1.6% of sales during the quarter and the first nine months, respectively. This percentage is way lower than the internal guidelines of maintaining our exposure below 10% of Rotoplas revenue.

## SALES – PRODUCTS & SERVICES

Regarding our portfolio mix, sales of products in the quarter accounted for 92% of total sales and grew 4% year-over-year, due to a marketing strategy for mid-range and low-end products coupled with a growing demand for storage products. This related to the scarcity of water resources in the regions where we operate.

Services accounted for 8% of total sales in the 3Q and registered an 8% increase year-over-year related to water treatment plants that entered into operations in this quarter.

## P&L – RESULTS GLOBAL

Starting with the top line, net sales grew 4% year-over-year this quarter and 4% in the first nine months, driven by the factors that Charlie already mentioned and an increased dynamism in the traditional channel and

water-as-a-service in Mexico. Also, commercial and optimization strategies to gain market share and increase sales in Argentina contributed to this result.

The gross margin shows an expansion driven by lower resin costs, improved efficiency in the manufacturing plants, better sales mix and a strict expenditure discipline contributed to the expansion of operating margin by 330 basis points.

As a result, EBITDA grew by double digits, even after adjusting for discontinued operations related to the sale of our manufacturing assets in the United States, which netted \$762 million in cash, strengthening our balance sheet, reducing our leverage from 1.7x to 1.1x Net Debt /EBITDA and increasing our return on invested capital in 140pb compared to the last quarter generating an inflection point.

The adjusted EBITDA for the quarter increased 19% compared to the same period of 2018 and the margin grew 240 basis points to amount to 19.4%. YTD the EBITDA margin stood at 17.2% well above our guidance for 2019.

Net profit for the first nine months decreased due to increased financial expenses and the annual hedge program, with a net interest and derivatives payments amounting to 180 million. Likewise, hyperinflation in Argentina continued to cause monetary position and FX losses amounting to \$148 million.

Discontinued operations were considered at a loss of Ps. 146 million. This was due to the sale of manufacturing assets in the U.S. and the related acknowledgement of differed taxes arising from losses in previous years.

#### CAPEX & FCF

In terms of CAPEX, we will maintain our capital allocation discipline and, through our optimization strategies, we will find new venues for growth and to expand our water-as-a-service platform, as we continue to do with the water treatment plants and the strengthening of our e-commerce platform.

Capital investments made as of September 2019 accounted for 4.0% of sales. Most resources were allocated to Mexico particularly to water treatment and recycling plants which will be translated into future revenue as invoicing takes place.

As for cash flow generation, the company posted a significant increase when compared to last year's quarter.

## BALANCE SHEET & NET DEBT – CASH POSITION

This cash flow generation, give us the confidence that we will keep net debt below 2.0X EBITDA and much in line with our current 1.1X EBITDA leverage which, it should be noted, represents a significant decrease from the 1.5X leverage we had in December 2018.

## ROIC-WACC

As previously pointed out, the objective of Flow is to create value above our cost of capital, and this result will be reported quarterly to the market. It is worth mentioning to explain that the drivers behind the surge on ROIC is mostly explained by a capital reduction in a losing business operation in the USA. Good news is that a positive shift in the trend should follow in the coming quarters.

## GUIDANCE

Finally, as I have mentioned, during the first nine months of the year we continued to face economic headwinds in Mexico and Argentina and the Argentinean Peso depreciation, which is affecting our volumes and top line growth. However, going into the fourth quarter we expect positive effects from:

- Increasing revenue recognition from water treatment and recycling plants.

- Stable raw material costs at a lower price-point than the ones from last year, which have already had a positive effect in this quarter's margins.
- A stronger cash position in our balance sheet which will help us improve further our net debt position.

For the full year, I confirm our last call guidance on revenue with a mid-single-digit sales growth for the year and an increase in EBITDA margin above 17%.

THANK YOU

Thank you for your time today. As usual, we will now answer any questions you may have.

**Mariana Fernández**

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.