

Grupo Rotoplas

4Q18 Conference Call

Corporate Participants:

Carlos Rojas Mota Velasco, Chairman and Chief Executive Officer

Mario Romero Orozco, Chief Financial Officer

Operator:

Good morning and welcome to Grupo Rotoplas Fourth Quarter 2018 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.

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.

Today's call will be hosted by Mr. Carlos Rojas, Rotoplas' Chairman and Chief Executive Officer, and Mr. Mario Romero, Chief Financial Officer.

I will now turn the call over to Mr. Carlos Rojas.

Carlos Rojas Mota Velasco:

Thank you, operator. Thank you all for joining us today.

As you know, yesterday we reported double-digit growth in sales and EBITDA, year-over-year, in both the fourth quarter and 2018 as a whole. All of our country operations grew, except for Brazil, where, as you know, we are reducing government sales and transitioning our focus and product-mix towards the premium segment. And this growth was driven by our acquisitions, increased demand for products such as storage and flow solutions and our water-as-a-service platform: In fact, in 2018 alone, we added over 4,700 purification points and over 1,800 water fountains, exceeding our expectations.

The fact that we grew across the board is very significant for a number of reasons. First of all, as we have discussed in previous calls, some of our Latin American operations experienced significant political, fiscal and economic uncertainty during these past few months, as was, for example, the case in Argentina, where hyper-inflation continued to have a significant impact on our overall results. And yet, not only we did manage to grow in this environment, but we did so while consolidating a more diverse portfolio of products and services, maintaining and expanding our market share.

In this context, it is worth noting that the reopening of our Sustainable Bond Agua 17-2X for 1,000 million pesos was oversubscribed several times, paving the way for greater capital investments in our services platform.

It is significant as well that our recent acquisitions not only contribute to our sales growth, but they also provide us with synergies, technology and institutional knowledge that we can leverage as we move forward and that, eventually, will enable us to fully realize the water market potential in the region.

Finally, it is significant that, as we grow, we also continue to develop a strong ESG culture, pushing forward initiatives in sustainable finance, but also strengthening our corporate governance and promoting access to water through better products and services. We are convinced that this is the only way forward for companies such as our own and thankfully, as we talked about in our previous call, we are being recognized for it: we continue to be included in the Dow Jones Sustainability MILA Pacific Alliance Index, which tracks best-in-class companies that outperform their peers in sustainability. Moreover, we continue to improve in the Corporate Sustainability Assessment conducted by RobecoSAM, the leading sustainability evaluation firm.

We continue to consolidate a robust and diversified portfolio, both organically and inorganically, and we do so with the aim of providing ever more innovative solutions for a market that is growing and evolving constantly and in which we have a deep and well-established leadership position. And we will continue to integrate our acquisitions according to the strategy, grow our business and create value for our all stakeholders and communities.

Thank you for listening. I would now like to turn over the call to Mario, who will guide you through the quarterly and key results. I look forward to your questions.

Mario Romero Orozco:

Thank you, Carlos. Good morning. Thank you for joining us. I will now go over some of the financial highlights of the fourth quarter and the year.

Sales grew 26% year-over-year this quarter and 18% yearly, with a major contribution from IPS in Argentina and the e-commerce platform in the United States. EBITDA grew 57% year-over-year in the fourth quarter and 25% in 2018. Furthermore, we increased profitability margins, obtaining greater efficiencies in our operations by means of a better pricing, lower raw materials costs and a constant expense discipline and cost-control initiatives such as zero-based budgeting.

As for our geographic breakdown, sales in Mexico grew 8% year-over-year in the fourth quarter, accounting for 54% of our total sales. Our operations in Argentina grew 45% in local currency, excluding the recent acquisition of IPS, even though this growth was offset in Mexican Pesos due to the Argentine Peso depreciation, reducing the group's growth by four full percentage points. And the other countries category, which includes our operations in the United States, Brazil, Peru and Central America grew 4% year-over-year.

Regarding our annual results, sales in Mexico grew 6.5% in 2018, boosted by greater sales of water-flow products and purification services, evidencing our leadership position in the market and the success of our diversification strategy. The other countries category grew 29% in 2018, driven by the growth of our operations in the United States and Central America.

Sales in Argentina grew 55%, driven by the successful integration of IPS and an improved price-mix in our organic operations. However, as was the case for the fourth quarter, the inflation rate had a positive effect on our yearly growth, but it was offset by the depreciation of the Argentinean Peso.

The integration of IPS provides a powerful export platform in South America and it also contributes significant growth in volume and sales: in fact, the volume of exports from Argentina grew 42% in 2018. Despite of the adjustment in the purchase price, the acquisition continues to grow in sales and volume and its export platform, market leadership and new product development will accelerate into 2019.

Likewise, the integration of the e-commerce platform in the United States is already boosting the growth of our organic operation in that country.

Regarding our product mix, sales of individual solutions or products in the fourth quarter accounted for 93% of total sales and grew 33% year-over-year in the quarter and 21% for the year, boosted by the integration of IPS and the growth of our operations in the United States.

For their part, integrated solutions or services accounted for 7% of total sales and registered a 24% decrease year-over-year in the fourth quarter, which is mostly attributable to a decrease in sales of self-sustaining solutions that are mainly associated to the government channel. These include rural rainwater harvesting systems; “baño digno”, which is a composting bathroom; and the family orchard agricultural irrigation system.

Sales of services were down 5% for the year, mostly due to the fourth quarter results. Nevertheless, we continue the expansion and strengthening of our water-as-a-service platform. For example, our water-purification platform has now reached 49 cities in Mexico, in line with our projections.

In the water treatment plants business, after undertaking our learning curve during 2017, we observed good traction in 2018 that will continue in 2019: we added new clients during the year and booked 87 new equivalent units, while continuing to grow the pipeline.

It should be noted, however, that our net income was affected by three factors. First, higher interest payments, amounting to \$192 million pesos, due to a positive net debt position. Second, a monetary position loss in Argentina, amounting to \$64 million pesos. And third, higher tax liabilities amounting to \$22 million pesos.

Normalized net income without considering the Argentinian effect from monetary loss and taxes, would have been of \$465 million, equivalent to more than a hundred basis points impact on our net margin.

The fact that our acquisitions contribute significantly to our results, combined with the organic growth of our businesses and the positive outlook of our water-as-a-service platform attest reaffirms our positive long-term outlook and validates our current growth strategy. As Carlos said, we will remain committed to customer-centricity and ESG principles, while maintaining a strong balance sheet and a positive debt outlook.

We are also confident that we will keep net debt below 2.0X EBITDA, in line with our current 1.5X EBITDA leverage. And we'll use the balance to finance capital expenses for our water-as-a-service platform.

Going forward, we are expecting we will achieve for this year sales growth greater than 10% and that the EBITDA margin will stand above 16%.

I would like to have the opportunity to answer any questions you may have. We will begin with the participants in the conference call, followed by our website users.

Operator:

Thank you. Ladies and gentlemen, if you would like to ask a question, please signal by pressing star, one on your telephone keypad. If you're on speakerphone, please make sure your mute function is turned off to allow your signal to reach our equipment. Again, press star, one to ask a question. We'll pause for just a moment to allow everyone an opportunity to signal for questions.

At this time, we will go to a question from José Cebeira of Actinver.

José Cebeira:

Hi Carlos and Mario, congrats on the results. I have a question, but before the question, I just wanted to be sure that the Brazilian still has declined in Brazilian real due to the strategy of focusing on higher profitable products. The question would be, we have seen positive results in the e-commerce platform in the U.S. market. I was wondering when we are going to see this level of implementation, but in Mexico?

Mario Romero Orozco:

Thanks, José, for joining the conference call today. As far as our (inaudible) question, if you remember back in 2017, we had to really shape (phon) some of the rainwater harvesting programs, and we complied with it and we executed. That was not the case for 2018, that we couldn't (phon) in the second half. That is why you see a slowdown in Brazil. If you look at the retail water (inaudible) in Brazil, that is growing, and we're just managing in a small scale.

As for the e-commerce platform, as you explained previously in market, the U.S., which is the most developed market, we are understanding the space; we are understanding what will be their capitalization into the other countries where we operate, and we've been starting to do some final testing in some countries in South America. We believe as e-commerce becomes a greater distribution channel like what's happened in the U.S., being ahead of the curve will help us in doing what's needed in Mexico.

José Cebeira:

Thank you very much.

Operator:

As a reminder, it is star, one if you have a question at this time on the telephone. You may press star, one for questions on the phone. We'll pause another moment.

Mariana Fernández:

We have a question in the webcast, from Liliana De León from GBM. Could you please share with us more details regarding of the growth of water treatment plant during 2018 and going forward?

Mario Romero Orozco:

Thank you again for joining us today. As we present during the webcast, what we're seeing is—as time passes by and we understand better the market, we've been educating, as well, the clients, better traction on the amount of interest and water treatment plants in the marketplace. As you can see, the pipeline in 2017 was—we started the year with, what, 25. We did and execute this deal; in 2018, the pipeline was 124. We did 87, some of them are still in construction and we'll start to reflect on revenue and EBITDA recording throughout 2019. But importantly here is in 2019, we're beginning the year with a pipeline of 417, which is three and a half times last year, and it's like 15 times three years ago.

What you can see, moving from only having six clients in 2017 moving to 60 clients in 2019, we believe that the business that we have shared with you, and the long-term goal of achieving 5,000 water treatment plants, it is feasible. We are confident that this will be achieved.

Mariana Fernández:

We have another question from GBM, Liliana De León. Regarding 2019, you are expecting a growth in all the regions above 10%, or some countries should be above/below the target?

Mario Romero Orozco:

I would say that most of the country will grow above that target rate. At this point, we are not giving those details, but we feel confident that at least that number will be achieved, I'd say, as you hope.

Mariana Fernández:

We have another question, from (inaudible). We see an upward trend for the majority of the main raw materials. I understand that you'll make significant hedges for the raw materials side. Could you please share us with more information about this?

Mario Romero Orozco:

Hello (inaudible), a couple of things. The hedge that the Company does is for the FX exposure in U.S. dollars, and we do hedge our costs but only the FX exposure, not the raw material exposure.

As for the raw materials' future outlook, we are seeing more install capacity in the petrochemical side and more supply than demand. We see a 2019 stable environment regarding raw material costs.

Mariana Fernández:

The last question, from Rodrigo Verduzco, I think it's pretty much the same as the other one about (inaudible) but hello, thank you for the call. Could you give us an update on (inaudible) for 2018 and '19?

Mario Romero Orozco:

I'll give a 2018—today recorded here, 2019, what we're just trying to find out is the amount of island that there is out there, and obviously how many we're going to be looking depends on how good we are on executing there. I think our track record speaks well about our commercial and technology capabilities. We are about 50% (inaudible) ratio in 2017 and 2018, so I think that will help us to make the numbers for 2019.

Mariana Fernández:

Janine could you please open the line again for questions, just to see if we have one on the phone?

Operator:

As a reminder, it is star, one if you have a question on the phone line at this time. That is star, one for questions. We'll pause a moment.

At this point, there are no other questions in the queue.

Carlos Rojas Mota Velasco:

Thank you very much everyone for joining us today. See you soon again, talk to you soon again in next report. Thank you.

Mariana Fernández:

Yes, thank you very much for your time and your interest. We hope you will join us again next quarter. Until then, we'll be sure to provide you with important updates.

Operator:

Again, ladies and gentlemen, that does conclude today's call. We would like to thank everyone for your participation. You may now disconnect.