Company: **GB Auto EVENT**

Conference Title: **GB Auto 1Q/20 Results Presentation**

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Operator: Good morning. Good afternoon, ladies and gentlemen. Thank you for joining our First Quarter 2020 Results Presentation. This call is being recorded. From GB Auto, we have Mr. Nader Ghabbour, Deputy CEO, presenting the first quarter 2020 results.

I will now hand over to Mr. Nader for his presentation. Then we will have a Q&A session. Mr. Nader, please go ahead.

Nader Ghabbour: Thank you, Operator. Good afternoon, ladies and gentlemen, and thank you for joining our results call for the first quarter of 2020. I hope that everyone is staying safe and healthy during these challenging times, and I am confident that we will all emerge from this crisis stronger than ever.

Ladies and gentlemen, GB Auto began the year on a high note. Despite the typically low seasonality of the first quarter, our market was on the path for its recovery, and we were anticipating a second – a strong rebound across all our lines of business. However, like all businesses across the world, the automotive sector is taking the hit from COVID-19. Starting mid-March and in tandem of the government's measures to control the spread, we acted swiftly and rolled out protocols to mitigate the risks and ensure the safety and wellbeing of our people.

We have put in place strict hygiene and sanitation protocols, rolled out occupancy limits and work-from-home policies to maintain adequate social distancing and we are supporting our employees with lenient sick leaves.

Parallel to protecting the safety of our employees and customers, we are implementing business continuity measures across all our lines of businesses to manage the impact. At our Auto & Auto Related segment, our primary focus is maintaining leaner working capital levels. Our target is to ensure inventory levels are aligned with fluctuating demand and to efficiently plan for future orders.

Our balance sheet is strong with net debt having decreased by almost 10% compared to Q4 2019. Meanwhile finance costs for the Auto & Auto Related segments have gone down by 13.4%, surpassing the decrease of net debt.

Additionally, the 300 basis points cut in interest rates by the Central Bank of Egypt in mid-March acted as a vital cushion to support the business. The full effect of the rate cuts will be reflected starting the second quarter of 2020 and will provide for a much needed buffer against anticipated headwinds.

Moreover, we have adjusted our cost structure and investment strategy to accommodate for current market conditions. We began revising our contractual agreements, rationalizing operational and administrative expenses, and most importantly, have put a hold on any new capital expenditure until markets begin to settle.

Moving onto our performance. The Group's Auto & Auto Related segment witnessed a turnaround in the first quarter of 2020 despite the seasonality and the slump towards the end of the quarter. The segment almost broke even following consecutive quarters of losses.

At the Passenger Cars line of business, a recovering market throughout most of the quarter drove our volumes up by 21.7% year-on-year. Revenue of the line of business was also up by 5.5%. However, since the onset of COVID-19, containment measures have taken a toll on demand starting late March and through April, particularly with the closure of the traffic department.

Walk-ins across our showrooms had initially plummeted. However, we are beginning to witness increased traffic as consumers normalize the situation. We are also glad to see the reopening of the traffic department as measures are eased. Our expectation for this line of business is sustained pressure through to the end of the second quarter, after which we are cautiously optimistic to see continuation of the recovery witnessed in the early months of the year.

We will continue to focus on profitability, a strategy that has allowed us to drive up in the passenger cars gross profit during the first quarter. And that is best suited to counter the price advantage enjoyed by vehicles of Moroccan, Turkish and European origins. At the two and three wheelers line of business, the situation is twofold. On the one hand, we have the three wheelers which have been gradually adapting to these restrictions and we are witnessing a sustained quarter-on-quarter increase in volumes, with Q1 figures up by 30.6% quarter-on-quarter.

With respect to COVID-19, these three wheelers vehicles are income-producing to their owners, and thus the impact has been limited. On the other hand, the two wheelers have delivered a strong 52.6% year-on-year increase in Q1 volumes. However, demand has been impacted by COVID-19. We anticipate an overall slower recovery trajectory versus passenger cars owing to the price and economic sensitivity of this division's consumers.

At the commercial vehicle line of business, revenues dropped by 31.4% year-on-year in Q1 2020, primarily due to the shortage of supply of the bus segment and the uncertainty caused by COVID-19. As regards to the supply shortages, those have been resolved in April. We expect the insurance[?] slump in the tourism industry and the general economic uncertainty to lead to austerity at the corporate level across Egypt. This means fleet upgrades and renewal decisions across the commercial vehicle market will most likely be postponed and hence a more prolonged recovery.

The Tires line of business recorded a 17.1% year-on-year decline in revenues in the first quarter of the year. This came as distributors held high inventory levels heading into the New Year following an uptick in supplied volumes in the fourth quarter of 2019. We expect the business to pick as the market clears the excess inventory and we believe we can grow our market share despite the current environment. I also must note that the line of business's profitability has significantly improved with Tires' gross profit increasing 31.4% year-on-year.

On the regional front, revenues declined by 5.7% year-on-year in Q1 2020. Due to the complete lockdown in Iraq, they essentially put a halt to sales activities impacting our passenger car volumes. However, strong demand in the two and three wheeler segment was a key driver in supporting this line of business performance, with volumes up by 30.9% year-on-year.

We are expecting to see a full liquidation of our Hyundai inventory by Q3 2020, particularly with containment measures being eased. We are also looking forward to the rollout of our new MG brand, for which we secured representation, and we expect to hit the market by Q3 2020. We are hopeful that we can position MG as a leading car brand in the medium-term in the Iraqi market.

Moving onto GB Capital. We are very pleased with the performance of the financing business, which recorded a revenue increase of 24.2% year-on-year before Intercompany eliminations in Q1 2020. The performance was driven by solid results from our operating subsidiaries that continued to benefit from Egypt's favorable interest rate environment.

In line with our strategy, we successfully maintained the healthy loan portfolio that grew by almost 17% year-on-year in Q1 2020, with non-performing loans standing at only 1.5%.

Ladies and gentlemen, we are currently facing unprecedented times and we are anticipating a short-term turbulence across our lines of business in the coming months. However, we are hopeful that as restrictions begin to ease, our volumes will begin to recover and we can resume the high note that characterized the beginning of the year. We remain confident that we can navigate though this turbulent environment by leveraging our flexible business model and our ability to adapt to dynamic market changes.

GB Auto will continuously monitor the situation and adjust our operational and administrative controls, the protocols and policies in accordance with developments on the ground. Our top priority is ensuring the safety of our workforce and customers. We will continue pivoting strategically to mitigate the impacts of COVID-19 on the Group's lines of business and we are hopeful that we will resume our rebound momentum as markets slowly reopen and the current crisis subsides.

The second quarter of the year is likely to be the most impacted by the onset of COVID-19. As such, we see the Auto & Auto Related segment achieving revenues of approximately EGP2.8 million with a gross profit margin of around 14%, and savings in SG&A and finance costs of around EGP80 million for the quarter. As for GB Capital, we expect our net profit after tax and minority to remain flat quarter-on-quarter.

With that, ladies and gentlemen, I will conclude my remarks and open the call up to your questions. Operator?

Operator: Thank you, sir. Ladies and gentlemen, if you would like to ask a question, please signal by pressing star one on your telephone keypad. Please note if you are using a speakerphone, to make sure your mute function is turned off to allow your signal to reach our equipment. Once again, please press star one at this time if you wish to ask a question. We'll pause for one brief moment to give everyone an opportunity to signal for questions.

Just as a reminder, ladies and gentlemen, it's star one on your telephone keypad if you wish to ask a question. We'll now take our first question over the phone from Aly Elgamal[?] from Azimut

Egypt. Please go ahead. Your line is open. Please note Mr. Elgamal, we're not receiving any audio.

Aly Elgamal: I'm sorry, can you hear me now?

Operator: Yes, sir. Please go ahead.

Aly Elgamal: Okay. Thank you. Sorry, good afternoon, everyone. Congratulations on the results for the first quarter and thank you for taking the time to listen to our questions. I have three brief questions. The first one, regards to provisions, are there going to – are you expecting any increase in provisions in the Auto or Auto Related or the GB Capital side?

Second one being, how much is the ownership of GB Capital to the mother company?

And the last thing – last night there was a article out that the price competition is going up in the market and we see a lot of – many of car manufacturers that are decreasing their prices and there was [inaudible] Hyundai is also reducing their prices by EGP10,000. So, I just want your thoughts on that. Is there any merit to these articles and how will that hit your margins? Thank you.

Nader Ghabbour: Thank you for the question. Regarding your first question regarding provisions on the Auto & Auto Related front, we do not expect any significant provisions due to the current situation. While on GB Capital, indeed in March, when the crisis hit the Egyptian market, we started taking on some provisions to cater for loans that we expect might have delay in payments.

There is also a good point that I have to mention, in my article I said that the NPL ratio is 1.5% in the first quarter of 2020, regarding GB Capital's portfolio. Out of this 1.5%, there is one big customer with an NPL value of EGP70 million, where we finally took the legal custody of the real estate asset. So, it's going to move from the NPL to – it will move out of the NPL pool, while we have already provisioned 50% on this specific loan but we're going to keep this provision to cover even – we're not going to refund the provision. We're going to keep it on our books just to fund any future delinquencies, if any.

While actually from the middle of March until the end of April, we started seeing the actual behavior, whether on the consumer finance front or the financial leasing front or even the microfinance front. So although in the beginning we thought there might be more delinquencies, the reality of the matter showed in the past 45 days, or at least now 60 days, that collections is much better than expected. So, we will not take on severe provisions at this moment given what we have seen regarding the collections so far.

On the second question, which is, I think, you asked, what is the ownership of GB Auto in GB Capital. If that was the question, then GB Auto owns 100% of GB Capital. So I hope this answers your question.

Regarding the third on the automotive front, what you have seen, yes, Hyundai has reduced prices from EGP8,000 to EGP10,000. These are merely promotional activities and the same happened across different competitors. So, we've seen Opel, for example, reducing on a couple of their model ranges and we've seen a couple of activities here and there, but these are not price adjustments in the passenger car markets. These are no more than promotional activities to increase demand on certain models, where we might have additional inventory in.

I personally expect that going forward prices of passenger cars will increase, actually not decrease, because the only merit that will provide prices reduction is the appreciation of the Egyptian pound, which honestly I do not see on the table at all at this point. And in the opposite I actually think that the Egyptian pound will lose some value over the coming few months, which will result in increase in selling pricing.

Aly Elgamal: Okay. Perfect. Thank you. So, you don't see like – so you don't expect any increases in – or sorry, decreases in margins because of the EGP10,000 – or EGP8,000 to EGP10,000 decrease in prices?

Nader Ghabbour: Of course, gross margin might reduce a little but will be compensated with the additional volume.

Aly Elgamal: Okay. Perfect. Thank you so much.

Nader Ghabbour: Thank you.

Operator: Mr. Ghabbour, there are no further questions queued over the phone at this time. I would like to turn the conference back over to yourself.

Nader Ghabbour: Well, ladies and gentlemen, I would like to really thank you for listening to our Q1 call results. I really and genuinely wish everyone on the call and their families are safe. And that economically, whatever businesses you are involved in, will come out and recover sooner than expected. Thank you all. And I will wish to see you in good health in three months' time. Thank you.

Operator: Mr. Nader, pardon the interruption, we do now have two further questions queued. Would you like to take or end the call?

Nader Ghabbour: Yes, sure. I'll take them.

Operator: Certainly sir. We'll now take our next question Ajal Slem[?] from Jari[?]. Please go ahead. Your line is open.

Ajal Slem: Hi. Thank you for taking my call. Couple of questions. One is –

Nader Ghabbour: Can you please increase your volume or your voice because I can't hear you well.

Ajal Slem: Sorry about that. Is this better?

Nader Ghabbour: Yes.

Ajal Slem: Okay. Just couple of questions. One is on the guidance. Can you just reiterate the guidance that you've given for Q2 for the Auto segment? And the second is, are you seeing any job losses in the business as of now?

Nader Ghabbour: Okay. Regarding the guidance for the Auto & Auto Related segment, we expect revenues in Q2 to be approximately EGP2.8 billion with a gross margin of around 14%, and we expect savings from SG&A as well as finance costs to be around EGP80 million for the quarter. While for GB Capital, we expect that the net profit after tax and minority to be at par with Q1. So, rather than expectations of growth in Q2 in the financing business, we expect the slowdown will yield the same result as Q1.

Regarding the second question, actually what we have done, we do not see any more job losses. What we have done in April, we re-looked at the organization. We have, in the Auto & Auto Related segment, something like 7,500 employees. We have decided to let go of about 140, if I remember correctly, and these are not due to the COVID-19 issue. These were the low performance individuals in the company that they had to go anyways. But other than the 140 people out of those 7,500, going forward, we do not see any more layoffs.

Ajal Slem: Okay. Thanks a lot.

Nader Ghabbour: Thank you.

Operator: We do have one further question which comes from Imran Patel with Tundra Fonder. Please go ahead. Your line is open.

Imran Patel: Hi. Can you hear me?

Nader Ghabbour: Yes, perfectly fine. Thank you.

Imran Patel: Hello. Can you hear me?

Nader Ghabbour: Yeah.

Imran Patel: Thank you very much for your time. I have – yeah, I have couple of questions. My first question is related to three wheeler. During outgoing quarter, the company sold around 4,500 units of three wheeler per month. So, what I recall is that this is the highest monthly sales[?] per month since the restriction was imposed on the issuance of licenses for three wheelers. So, my question is that if there is any change in the new license limit for the company?

And my second question is related to the passenger vehicle segment in Egypt. Recently the company – in recent quarter this segment posted around 11% gross profit margin and there is 55% volume came from CKD and the rest from CBU. So firstly, can you guide us on the estimated gross profit margin earned on the CBU and the CKD in the first quarter? And my second part of the question is that, can you highlight the sectors which resulted in the Q-on-Q improvement in gross profit margin? For example, it could be Egyptian pound appreciation, lower discount to dealer, maybe price increase, change in products mix or better absorption of cost on CKD operation. Thank you very much.

Nader Ghabbour: Okay. Just give me a second. Well, I didn't catch the full details of the first question, but my understanding from the question is if there are further restrictions on the three wheeler licensing? For now there are no. So, before the government restrictions, we used to sell something like anywhere between 7,000-8,000 three wheelers a month and that was up until February or March 2019.

After the government restrictions regarding the licensing, volume significantly reduced until the licensing cycle picked up again. And before the COVID-19 crisis hit us, we were selling anywhere between 4,000-5,000 three wheelers fully licensed a month. And that was more or less the demand because since we were not able to license or to sell more products as demanded in the market during last year, we decided to increase the selling price of the three wheeler to compensate for the lost volume.

Now, currently with the traffic department, we are hovering around the 4,000 to 5,000 units of three wheelers license a month, which is more or less the current demand of three wheelers in the market during these days. So, I hope that answers the first question.

Regarding the passenger car Egyptian market, basically we currently yield higher gross margins on CBUs compared to CKDs basically because we have very few models coming from Europe enjoying the preferential custom advantage, while CKDs of course are at the competitive disadvantage, so they yield lower margins. The combined margin of the passenger car function will be around anywhere between 10-11%.

And the reason behind the improvement in margins is mainly two things. The most important is the appreciation of the Egyptian pound, which we do not pass all these benefit to the customers.

The other was still by towards the end of last year we still had very minimal inventory that was yielding very low margins, which was completely liquidated towards the end of last year. So, basically in 2020, our inventory is more or less fresh. So, we should not be liquidating or yielding negative margins as we saw in the past couple of years.

Imran Patel: Okay, great. Thank you very much.

Nader Ghabbour: Thank you.

Operator: Mr. Ghabbour, the queue on the audio side is now clear once again.

Nader Ghabbour: Okay. Thank you, ladies and gentlemen. Thank you, Operator, and I wish you all the best. Thank you, and have a great day.

Operator: Ladies and gentlemen, this does conclude today’s call. Thank you for your participation. You may now disconnect.