Transcription for ŞOK MARKETLER

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Corporate Participants

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Question and Answer Session

Operator
[Operator instructions]

Our first question comes from Hanzade Kilickiran from J.P. Morgan. Please go ahead.

Hanzade Kilickiran
I have two questions, actually, both related. It is about your revenue performance in the last quarter. With all retailers announcing their numbers, we observed some acceleration in the revenue growth in the fourth quarter, but however, on your side it looks kind of stable. Would you please explain why you have stable revenue growth and we see accelerated inflation in the fourth quarter.

The second question is actually related to this, you have a relatively large like-for-like growth which is around 20% you mentioned. Can you please elaborate why your like-for-like growth is lower than [audio], for example, which is roughly 27%? Thank you.

Uğur Demirel
Actually, the fourth quarter growth was 35% and the like-for-like is almost 20%. One of the reasons is that in September, because of the customer perception, as we already discussed in the third quarter, some of the customers made some [inaudible] because there is coming inflation in the coming months, so they made some [inaudible],so that the number of traffic in the fourth quarter is a bit lower than the expectation.

Coming to the like-for-like basket growth, you need to consider that we have some categories like tobacco, we have zero inflation over there and if you consider without tobacco, the basket size growth would be at least 19-20%. There are some categories that our competitors don't have, which Şok has, which is diluting our basket size growth. These are the reasons that the growth level is not the same compared to others.

Coming to the first quarter, we have seen a strong top line growth, again, and the number of traffic growth is maybe higher than last year in the first quarter. Although the first half of January was a little bit slow. Now, after taking action, we have created a new marketing company, which is Şok Uğur, it has increased the number of customers significantly and it affected in a positive way both like-for-like sales and the top line.

Ziya Kayacan
I would like to also add one more thing to Mr Demirel saying, that tobacco keeps around 13% of our sales, so considering this, our like-for-like [inaudible] sees some increase also in tobacco like others, we will be able to see, as Mr Demirel said, 19-20% basket size increase and if you add it also traffic, so we come up with 23% easily on top. This is also our upside for 2019. As Mr Demirel said also, starting by our company, although in this market condition, we are able to see higher traffic as we planned. This is also, I think, it is different from the general market trend.

Hanzade Kilickiran
Is it reasonable to make a comment that 10% price cuts in order to tackle the inflation didn't have much impact, actually, on the revenue growth slowdown? It is still very high growth, don't misunderstand me, but I am just trying to understand why it didn't improve in the fourth quarter. Tobacco is the main reason I understand.

Ziya Kayacan
Maybe I can also add to what Hanzade said. You are right, of course, private label ratio, as I said, it has increased, also fruits and vegetables discounts, this can also affect slightly our basket size growth, but as I said, even without considering all this, our basket size growth easily can jump to 20% if we see a tobacco increase. That is why our internal inflation – this is also in line with our internal inflation.

Operator
[No further audio questions]

Çağrı Demirel
We have one more question about the like-for-like store number in 4Q 2018 and number of Şok Mini stores in fourth quarter 2018 and full year 2018.

Ziya Kayacan
About the like-for-like [store base] in fourth quarter, I already mentioned in my speech just to find you the number of stores, it is about only 60% of our stores, which correspond 3,766 in my number, which corresponds 62% of our overall store base, so this is like-for-like.

If you come to Şok Mini revenues, I should make comment on the daily sales. Before converting Şok mini stores, it was quite lower, it was around TL 1,700 per day. Now, we are able to – after this conversion, these days we are able to see TL 2,800, which is very close to TL 3,000 per day, which brings almost an EBITDA margin with the original Şok stores, we are quite happy to see this trend.

Operator
We have a follow-up audio question from Hanzade Kilickiran from J.P. Morgan. Please go ahead.

Hanzade Kilickiran
Actually, I have a couple more questions, so probably I can take them now. Is it possible for you to provide some guidance for 2019? I couldn't see your guidance on the top line and EBITDA margin.

The second thing is, I wonder your opinion about the proposed retail law, what types of changes do you expect in the retail sector in 2019. Thank you.

Uğur Demirel
First of all, starting from the government regulation. I think that if there are any changes in the regulation, it will affect positively the consumer trend, so we will be supporting all these initiatives. On the other hand, if the regulation changes, all the sectors will be affected. Right now, we have been affected by some of the initiatives that have been taken already, like fighting with the inflation with 10%, which affected our gross margin in a 0.4%. We have been also affected by some fruits and vegetables initiatives already. It is, again, affecting our gross margin in a negative way. Nevertheless, again, we observed strong top line growth as we anticipated already with our long-term business plan, so there will not be any changes.

In terms of guidance, maybe we can talk about the store opening things. Up to now, we have opened 185 stores in two months. Now, we are still keeping on our pace for the store openings. Nevertheless, we are in a challenging macroeconomic environment. We can revise our target depending on the macroeconomic environment, so that it has to be flexible management. What is important for us to focus on, the payback period, we don't want to increase the number of payback periods for the store openings. If it is affected, again, in terms of FX rate, if it goes up, so we can revise our expectation in terms of number of store openings.

Ziya Kayacan
For the guidance, we don't provide guidance for the moment, but at the time [I am up here], we already guided you about our five years plan, which plays on the store openings, which is in place today and in the future also it will be. In terms of sales revenue, which is the primary goal for us, especially under this market volatility and market environment, of course, some impact on our margins, but our key strategy will be, again, with superior growth, with store openings and like-for-like. This is in place as of today in two months of the year. It is better than our expectation in terms of traffic. Profitability, of course, in short-term because of what Mr Demirel said, because of these results could be affected negatively, but we don't see any reason to deviate from our long-term goal. We already achieved 5% EBITDA. In the long-term, this is much beyond our expectations at the time of IPO. We are not considering so different from our long-term goals. We will look at the market environment and take necessary actions related to our long-term goal.

Hanzade Kilickiran
This EBITDA margin expansion, as you mentioned, was a little bit beyond your expectations. Is it reasonable to assume at least stable EBITDA margin in 2019, despite the fact that there are some obstacles in the retail space in 2019? I am not really sure how we should be looking into your EBITDA margin.

Ziya Kayacan
In fact, there are two elements in EBITDA, one is our operational, the second one is related to our working capital management, so our operational [inaudible] will be in place, which we released, although in quarterly basis it can change, but overall it will not be. When we look at our working capital management, maybe you already point out that our working capital days dropped from 70 days to 60 days level up until the IPO, but this is much more related, again, to market factors especially in private label side, small

to medium companies we are working currently. We will be supporting those firms.

In 2019, without deviating from our working capital management strategy, we will be still managing our cash accordingly.

What I want to say in operational results, we will keep our focus on part of EBITDA, and for the working capital part, also, we don't see deviation.

Operator
Our next question comes from Mete Ozbek from Unlu & Co. Please go ahead.

Mete Ozbek
If I am doing the calculation right, I see a significant increase in your transportation and packaging expenses, although they are not so significant. There is almost 30 million increase compared to the last quarter in these two items. Was there a one-off cost there or are we seeing the impact of the inflation? Is it sustainable in the coming quarters?

Ziya Kayacan
In fact, as you point out, there are three main items which is affected by inflation and FX increases. The first one, as you said, logistic cost [inaudible]. The second one electricity, so we have seen 70% increase year-on-year basis on the electricity and the third one is the packaging expense, which is related to, again, the currency. Rent expenses already increased, but we mentioned that we have control on that.

We are negotiating with landlords, so this is already under control, so it will not be a problem for 2019. Electricity, we have some projects, again, to cover these cost increases, so this will come. Packaging, already 70% decline after the packaging [law] on the consumption and the cost over there dropped from 0.5 to 0.1% level, which is also good. Only personnel expenses, we have to manage it, and we have already taken steps in that direction, in some other cost lines to reduce our cost inflation to the manageable level. We will grow accordingly. Our growth strategy will be accordingly.

Çağrı Demirel
We also have one more question from George.

"Could you provide guidance on Şok Mini rollout in 2019? Also, CapEx per store guidance for both normal and mini format. In 2018, we saw acceleration of CapEx per store due to FX effect. Given the current [inaudible] on Turkish lira, what is the outlook for CapEx per store?"

Ziya Kayacan
In fact, for the mini, we are quite happy with the mini store investment ,so as I already mentioned, our sales per store has increased significantly, but maybe on some occasions, we already mentioned that we are to invest in Şok Mini there is a difference on the payback side, so that is why we give priority to Şok stores. In 2019, also, we will open some amount of Şok Mini stores. This could be not in the hundreds, but it will be less than a hundred, let's say.

In terms of CapEx per store guidance for normal and mini format, I can't speak about what happened in 2018. Our CapEx per store in 2017 was TL 221,000 per store, it increased by 15% to TL 250,000, which is 15% only, although, 50% of our capital expenditure is linked to foreign exchange.

2019, now the exchange rate declined, so we assume slight increase for the moment, at least, from this TL 250,000 maybe to TL 270,000, roughly. It could be average cost per store for 2019.

If you come to Şok Mini, we spent TL 150,000 last year, it can go up to TL 180,000, roughly, maybe up to TL 200,000, it depends on, of course, the square metre, of course less than the normal Şok stores.

Operator

[No further questions]

Ziya Kayacan
For the final remarks, again, we would like to thank all of you that 2018 was – after the IPO especially – it was beyond our expectations what we achieved in terms of revenue growth, also in terms of store openings and EBITDA margin. 2019, as we already outlined, it will be, again, challenging year for everybody, but as Şok we are ready for this challenge and 2019 already started with relatively good level of growth. Also, our store openings is good, what we already budget, we are in line with our plan and of course what we can see some margin, let's say, pressure, especially in the gross margin side, but especially coming from the fruit and vegetable and inflation action. But in the medium and long-term, we assume that we can

handle this cost issue and at the EBITDA level, we don't foresee to dilute in the medium-term for the remaining period of the year, maybe only in the first quarter only could be affected. But our cost plan action, we are already quite effective in cost management, rents are under control, packaging expense is already done, so we also take care of other costs very effectively.

Thank you very much for listening and hope to see you in other occasions.
