EDITED TRANSCRIPT
UNIVERSAL ROBINA CORPORATION (URC) 9M FY14 UNAUDITED RESULTSEARNINGS CALL

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PRESENTATION:

Speaker:

Ladies and gentlemen, thank you for standing by and welcome to URC's Quarterly Investor Briefing. Joining us today from URC are Mr. Lance Gokongwei, President and Chief Executive Officer, Mr. Michael Liwanag, Vice President for Corporate Planning and Investor Relations, and Mr. Nilo Mapa, Executive Vice President and Managing Director. URC will give you a brief company presentation on the results; at the end of the presentation there will be a question and answer session. I must advise you that this conference is being recorded today, Wednesday, 13th August 2014. I now hand you over to Mr Lance Gokongwei. Please go ahead.

Lance Gokongwei:

Good afternoon. Today I will be presenting the unaudited financial results of Universal Robina Corporation as of the nine months of fiscal year 2014. Total URC sustained its top line momentum, as Q3 sales grew by 17% to PHP 23.5 billion. The strong performance came primarily from Branded Foods Philippines, which registered a growth of 26%. After nine months, total URC sales amounted to PHP 69.2 billion, a 14% increase.

The margin expansion trend continued on to the third quarter due to the lower average prices of many major raw materials, good management of operating expenses, and additional economies of scale particularly for our Branded Food business. As a result, third quarter EBIT grew by 28%, which resulted in first nine months EBIT of PHP 10.5 billion, 37% growth versus same period last year, with margins at 15.2% for a 249 basis points expansion.

Core earnings for the nine months was at PHP 10.7 billion, up 22% versus last year, while net income was at PHP 8.6 billion, up 2% versus same period last year. Growth in net income was slower than operating income as we booked lower non-recurring gains versus last year when we disposed of marketable securities. The company registered net finance revenue of PHP 82 million for the first nine months of the year versus PHP 249 million in the prior year as we have liquidated most of our bond and equity holdings last year.

Total Branded Foods revenues remained strong as third quarter was up 19% versus last year, which resulted in first nine months revenues of PHP 57.6 billion, an increase of 20%. Q3 EBIT grew by 46% versus last year, resulting in an PHP 8.2 billion operating income or a 50% increase for the first nine months. Year-to-date margins ended higher by 285 basis points at 14.2%. The strong top line is still driven by the Philippines, which has maintained its momentum at about 20% growth in the third quarter, while we have seen acceleration of sales in International divisions despite the macro challenges in our major markets including Vietnam and Thailand.

Margins are at a record high for total branded foods due to the strong volumes which has given us increased economies of scale, improved margins due to lower average input prices, as well as the implementation of selective price increases, primarily in the Philippines, which started over the summer months.

Sales for Branded Foods Philippines sustained it's momentum as third quarter revenue grew 25% versus last year, which led to a first nine months sales of PHP 38.9 billion, a growth of 26%.

All segments posted double-digit growth led by beverages, as it registered first nine months growth of 43% versus last year, backed by the robust growth of our powdered beverage business – primarily due to 3-in-1. Ready-to-drink beverages, also grew at double digits – with contributions coming from tea, juice and water, all growing at double digits. We continue to gain market shares from competition with latest exit readings as of June 2014 for total coffee at 29% versus 21% in the same period last year. For ready-to-drink tea we have further strengthened our leadership, as we now have 86% market share coming from 82% last year.

Our snackfood business also posted strong growth of 15%, as snacks, bakery and confectionery also all grew by double digits driven by the growth of their core brands. We also continued our efforts in improving our distribution and order fill rates. The new coffee and creamer plant in Vietnam is now operational and started to supply our Philippine coffee requirements.

On to the International business, third quarter sales grew by 10% versus last year, which translated to first nine months year on year growth of 10%. In dollar terms, sales grew by 3% for the first nine months due to the depreciation of the Philippine peso.

Our Thai business grew by 5% US dollar terms, despite the political turbulence and lacklustre economic fundamentals, due to favourable sales posted by key biscuit, and wafer brands and new products that are gaining traction. We also saw the positive impact of our strategy of launching two baht biscuits catering to price constrained consumers.

Vietnam sales continue to post growth at 5% US dollars, even if consumer spending in Vietnam was weak. Our new products C2 Oolong and our Rong Do product in PET registered strong double-digit growth. We were likewise able to successfully defend market share from new product entry, Pepsi Oolong, with our C2 Oolong product offering.

Indonesia sales declined by 18% in US dollar terms versus same period last year as we closed down our C2 beverage business in Indonesia. However, our snackfood business continued to grow in double-digit terms, in Rupiah terms.

Malaysia continues to post positive growth, driven mainly by chocolates, candies, and biscuits, and China continues be on track on the back of cereals and oats growth.

The following chart illustrates the key contributors to our growth. We continued our focus on new products and have launched 25 new products in the last nine months in the Philippines, and they now account for 1% of sales. We have likewise commissioned our Vietnam coffee and creamer facility in April and May respectively. This has augmented our supply for Great Taste, which continues to grow at over 50%. Our market shares for coffee now total 29%, with our 3-in-1 mix at 30%. Our Great Taste White product is currently the single largest SKU in the Philippine coffee mix market. We are also executing better in our distribution and coverage strategy especially in the general trade. A strategy of pervasive coverage has been introduced where we deliberately pointed sources of supply for our trade customers so we guarantee that our products are on the shelves seven days a week.

For our Commodity Foods Group, sales declined by 20% as volume for the Sugar business was effected by lower raw sugar purchases for the first nine months, but total combined sugar production is still higher than last year. We still have inventories allocated for our internal use on our Branded Food business, as well as to fulfill forward contract requirements of our customers. Profitability was also affected by the decline in volumes despite the increase in selling prices. On the other hand, Flour sales increased by 4% due to higher volumes. Absolute EBIT increased, mainly due to lower wheat prices against the same period last year.

On to our Agro-Industrial Group, on the Farm side, sales increased by 12% due to higher volumes, higher average selling prices and growing value added carcass business. For our EBIT, nine-month figures was still significantly up over the same period last year and includes a revaluation gain of PHP 200 million on our biological assets, due primarily to the increased price for hogs. For Feeds, sales increased by 8% but EBIT declined by 23% due to higher production costs.

Turning to our balance sheet, it remains very healthy. We have managed to generate an EBITDA of PHP 13.3 billion for the first nine months of 2014, a 30% increase over the same period last year. We continue to maintain a net cash position of PHP 4.3 billion in the first half, from PHP 8.1 billion at the end of last years' fiscal year. Major cash inflows were PHP 9.9 billion from – cash from operations, whereas major cash outflows were PHP 5.6 billion for capex investments, the majority of which went to our Branded Foods and Sugar businesses, and PHP 6.5 billion in cash dividends paid out. The cash dividends were equivalent to 65% of previous year's reported net income. Gearing ratio continues to remain manageable at the low level of 0.09, as we have zero long-term debt in our balance sheet.

Let me now take you through our outlook and plans. We will finish construction of our factory in central Vietnam and our ethanol plant in the Philippines, and we expect these facilities to be operational by the first quarter of 2015. Our construction of our Myanmar factory is underway, but we expect some slight delays in completion due to logistical issues.

We recently announced our new business, which is a joint venture partnership with Calbee of Japan. Calbee-URC will manufacture snack products in the Philippines. We have ordered the manufacturing lines and these will be installed in our facilities, while the marketing plan is already in process. We expect the first Calbee products to be out in the market by the second quarter of the next fiscal year. Another announcement we did in the last few weeks is our acquisition of the Griffins business in New Zealand, and I will discuss updates on this in the next slide.

We continue to expand our product portfolio through innovation driven in all markets. As mentioned, we have launched 25 new products in the Philippines in the last nine months, while International has launched 36. We plan to launch 26 more products in the Philippines in the current year and 13 more in the International business for the balance of the fiscal year.

We are now in the process of further accelerating the reorganization we announced on Branded Foods, where we are trying to align core functions in procurement, product development, and manufacturing to gain further synergies. We have begun regional sourcing where the aim is to source products based on the least unit cost, with the caveat that shelf life and quality is not compromised and freight and handling costs are not prohibitive. A clear example of this is our sourcing of coffee and creamer in Vietnam for the Philippine market.

We have finalized the options for the financing of the Griffins acquisition. It will be on an all-debt basis; a NZ$700–750 million bridge loan will be taken out by two term loans within one year, half at the Griffins corporate level and the other half at the URC International level with parent guarantees so that we can lower our total interest cost. Pending approval of our application from the New Zealand Overseas Investment Office, we expect to complete this transaction before the end of October. We have also begun internal work to explore quick wins between URC and Griffins for cross-selling and marketing each other's products in the ASEAN and China modern trade, where we believe Griffins premium products will work, while we target and develop URC products for the discount retail branded market, primarily in Australia.

We expect to hit mid-teens top line growth in Branded Foods, which is in line with our intention to growing and doubling our sales every five to six years in the Branded Foods business. We expect our profitability contribution of our Non-Branded Food business to continue to grow, albeit at a slower rate. The good performance of our Farms business this year has been a pleasant surprise for us, with selling prices for hogs remaining quite solid and volumes coming from our value added carcass business being quite strong. With the momentum continuing, we expect to call up our full year guidance for this current year to the high PHP 13 billion to PHP 14 billion for the current fiscal year.

That closes our formal presentation. We are now open to questions and answers.

QUESTION AND ANSWER

Speaker:

Ladies and gentlemen, we will now begin the question and answer session.

(Operator Instructions)

Karim Salamatian, Credit Suisse:

Hi, good afternoon everybody. I've got a number of questions, but let me start – Lance, can you give us a bit more detail on the price increases in the Philippines on the Branded Food side that you talked about were implemented in the summer?

Lance Gokongwei, President and CEO, URC:

Sure. We had a 26% revenue increase; this was on the back of a 20% volume increase. Part of the difference is product mix, as we sold more high value cases of coffee, but we estimate about 3–4% of that is price increases. We expect the effect of price increases to increase towards the latter part of the year as significant price increases were taken primarily at the end of June, most major, notable ones are with our coffee mixes, where we took an average of 12% price increase to reflect the increased cost of Robusta coffee and oils. We've also seen increases in our biscuit and large snack packs, we've also taken price increases in some of the larger ready-to-drink C2 packs, so all in all there's been a preference to raise prices at the modern trade level while keeping most general trade price points fairly stable.

Karim Salamatian, Credit Suisse:

Is this in any way you feeling more confident about the market and the ability to increase prices, or is it really just a function of keeping up with raw material? It sounds like on the coffee it was more raw material-driven, but on ready-to-drink tea maybe you just feel that the market can take it better, is that right?

Lance Gokongwei, President and CEO, URC:

We saw some pricing action from some of the major players on the PET packs so we took the opportunity to follow them, primarily from Coca Cola. I would say for coffee a lot of that is really driven by cost push inflation on the raw material side.

Karim Salamatian, Credit Suisse:

Okay, perfect. On the International business do you have the numbers in front of you if you could – local currency growth rates for Thailand and Vietnam? I know earlier you gave us US dollar, but what are those markets growing at in local currency?

Lance Gokongwei, President and CEO, URC:

We don't have it in local currency, but in peso it's 12% for both Thailand and Vietnam.

Karim Salamatian, Credit Suisse:

Okay. So in Vietnam you're seeing some uptake in growth of your product versus the first quarter, is that fair? In local currency?

Lance Gokongwei, President and CEO, URC:

Yes. I think yes, basically.

Karim Salamatian, Credit Suisse:

Okay. And when we look at that market your gap to the number one player in market share is ten percentage points, so you've been able to nicely close that over time. How does that change the dynamics of the marketplace? Do you get a sense that its becoming more competitive, is the number one player going to – or are they already starting to do things to try and –?

Lance Gokongwei, President and CEO, URC:

Maybe I'll just give a broad question, but Nilo, who's beside me, can give you a more on the ground summation of what's going on. I think we're clearly number two there, but as a brand we now have the number one brand in Vietnam. I think C2 is the single largest tea brand in Vietnam since a few months ago, and we've generally seen that Pepsi Oolong has gained quite a bit of share but more share has been taken from THP than from ourselves. And over the last couple of months since we launched Oolong, our own C2 Oolong, we think our volumes have been recovering nicely. I don't know, Nilo, if you have anything to add?

Nilo Mapa, Executive Vice President and Managing Director, URC:

Well, just to put everything in perspective, I think the entire FMCG market in Vietnam has been relatively soft as of late, and as of the past month and a half or so the weather has also not been that favorable to beverages as a whole, because it has been raining and most of the inclement weather that come through the Philippines actually ended up in Vietnam. Yes, we did see a very strong momentum coming from Suntory Pepsi Oolong, and as Lance has mentioned we got nervous a little bit here and our reply here was to launch our own Oolong variants which also have a certain point of difference when it comes to flavour versus that of Pepsi. And while we were able to defend and even slightly recover some of the shares that we have lost, what we've seen is it has affected THP more than it has affected us.

Karim Salamatian, Credit Suisse:

Do you think margins in Vietnam can hold up here? Or is there some risk of margins coming off?

Nilo Mapa, Executive Vice President and Managing Director, URC:

At this point in time I think we are expecting to hold on to margins, at least in the near-term.

Karim Salamatian, Credit Suisse:

Okay. Just a couple more questions, sorry guys. Sugar – Lance, can you tell us a bit about or kind of frame for us what you think is going to happen with the Sugar business in 2015, with the tariffs coming off in the Philippines? Like, what should we expect – year to date it's about 17–18% of your EBIT; what's this going to look like longer-term?

Lance Gokongwei, President and CEO, URC:

Yeah, I think as a percentage of our EBIT it's running at about 13 – it's about 1.3 out of ten and a half. But we expect to close the year at closer to 1.9 to 2, because we are a little bit back-ended this year in terms of Sugar. We actually expect Sugar to be a strong performer next year, as we think the actual tariff for sugar now is down to 10% in the Philippines and next year it's going to five. This has gone down from a peak of 30 or 40% four years ago and it's been progressively going down by 10%.

I think what's critical for sugar pricing in the Philippines is really a couple of things. One is what the Sugar Regulatory Authority (SRA) does in terms of allocating or allowing imports into the country, and I think the SRA's role is really to keep a balance between the needs of local millers and planters and the price pressures on consumers, so their role is primarily to keep prices fairly flat, to avoid rapid changes or instability in the sugar prices, so even if the tariff is low you cannot import sugar into this market without a license from the SRA.

So overall we expect next year's performance to be quite strong. I mean, the crop seems good, I think the overall demand rate remains good and we expect to begin to see the benefits of some of our investments in value add, as our ethanol plant we expect to be operating by the latter part of this year and our biomass plant sometime early next year. So overall, we still expect a pretty fair increase over our targets for this year.

Karim Salamatian, Credit Suisse:

What kind of contribution do you expect from biomass and ethanol?

Lance Gokongwei, President and CEO, URC:

I would say maybe on a full year production, I think they can make PHP 800 million to 1 billion.

Karim Salamatian, Credit Suisse:

Can you ramp up that fast from the first year or is that –?

Lance Gokongwei, President and CEO, URC:

No, I would say that's a year three number.

Karim Salamatian, Credit Suisse:

800 million to 1 billion year three. Okay, lastly, if I look at your guidance and I use 15% sort of top line growth and your EBIT guidance, it implies margins in the fourth quarter – EBIT margins of about 14.5 I think it comes to. Is there any reason why we should think sequentially EBIT margins will decline in the

fourth quarter, especially after you increase prices? Is there something else going on that would lead to a lower margin?

Lance Gokongwei, President and CEO, URC:

We are seeing some cost pressures on the logistics side, as you might have read about all of these port pressures in Manila. We have about 1,500 containers stuck in the port and we're paying a lot of logistics and storage fees and increased trucking fees which we are budgeting right now to affect us until probably the end of this quarter. So we had to compensate for that with some of the price increases. So that I think is the pressure point on cost, and so I think that it the key pressure.

Karim Salamatian, Credit Suisse:

Okay. Alright, I think I have exhausted more than my time, so thank you very much.

Lance Gokongwei, President and CEO, URC:

Thank you.

Thomas Huang, BPI Securities:

Thank you for the presentation and congratulations on the result. I'd just like to ask if we can expect 4Q effective tax rate to go up or down?

Lance Gokongwei, President and CEO, URC:

I’m sorry, can you repeat?

Thomas Huang, BPI Securities:

Oh, I'm sorry. I'd just like to know if we can expect effective tax rate to go up or down in 4Q for URC, consolidated-wise?

Lance Gokongwei, President and CEO, URC:

Should be about the same, around 20 –

Michael Liwanag, Vice President, Corporate Planning and Investor Relations, URC:

No, no, we are at about 16–17% effective tax rate, Thomas. This is Michael. We're not expecting any change.

Thomas Huang, BPI Securities:

Okay, I’d just like to clarify that. Thank you, thank you so much.

Carlos Jesena, ATR KimEng Asset Management:

Hi, just a question regarding the plan for Griffin. So, what's the distribution platform of Griffin like in New Zealand and what's the plan for Griffin products here in the Philippines? Which specific food items do you guys plan to focus on for the Philippine market with regard to the Griffin brands?

Lance Gokongwei, President and CEO, URC:

Griffin's actually has a very strong distribution system in New Zealand, and very good contacts with major accounts as well in Australia. I think the major opportunities of course for this business are to export the Griffins product into – particularly the modern trade of certain of our countries including Philippines, Singapore, Malaysia, Thailand, China. We're still in the process of developing the product mix and the marketing mix for these countries. As you know, we're not taking over the company until October, but I would say in general we're looking at focusing on wrapped bars, chocolate enrobed products and certain biscuits.

Carlos Jesena, ATR KimEng Asset Management:

Alright, so do you plan to focus on the branded or the retailer-branded side –?

Lance Gokongwei, President and CEO, URC:

No, for URC products going into Australia and New Zealand then you're probably doing a retailer-branded distribution. But for exports of Griffins into Southeast Asia and China, you're talking about a branded business.

Carlos Jesena, ATR KimEng Asset Management:

Alright. With regards to the coffee supply in Vietnam, how affected is URC by price increases of Robusta coffee in Vietnam? And do you see this affecting your margins despite the price increases?

Lance Gokongwei, President and CEO, URC:

I think the price increase we took was sufficient to sustain our margins.

Carlos Jesena, ATR KimEng Asset Management:

Alright, that's it. Thank you.

Koh Sang Lim, NSR Investments:

Hi, I just have a question regarding the Griffins acquisition. Is there a timeline, or an estimated timeline, as to when numbers will be consolidated?

Lance Gokongwei, President and CEO, URC:

We still haven't got into that but I think it shall be from acquisition. So it's either going to be from – sometime in October, upon closing.

Koh Sang Lim, NSR Investments:

Okay, so likely from the beginning of next year – the fiscal year?

Lance Gokongwei, President and CEO, URC:

Yeah, or within a month of the beginning, because the target timeline now is between 15th October to 31st.

Koh Sang Lim:, NSR Investments:

Okay, thank you.

Carissa Mangubat, Deutsche Bank:

Hi, good afternoon. Just one question on the Calbee products that you are planning to introduce next year: what categories do you plan to go into and what would be the price points for these products?

Nilo Mapa, Executive Vice President and Managing Director, URC:

For the Calbee joint venture, what we plan to have is premium potato chips and potato products. We are not at liberty to discuss the price points at this time, but it will definitely be a relatively premium priced snack.

Carissa Mangubat, Deutsche Bank:

Okay, thank you.

Dave Montemayor, UBS:

Hi, thank you for organizing this call. I just have two questions. One, do you mind giving more color on why the effective tax rate in 3Q became 25% compared to 10% last year, in 9M it became 19% compared to 10% last year? That's my first question. Second question is which do you think is the best or maybe the first Griffins product that will be launched in the pan-ASEAN region? That's it.

Michael Liwanag, Vice President, Corporate Planning and Investor Relations, URC:

Dave, I don't know where you got the 25% because our nine months is running at around 17–18%. But if you compare it to the figures last year, you have to remember that we were earning tax-free interest income from the portfolio we had. In the filing and the annual report there's a bridge there from the statutory tax rate to the effective tax rate. So I will just give you the breakdown if you don't have it.

Dave Montemayor, UBS:

Thank you, thank you.

Nilo Mapa, Executive Vice President and Managing Director, URC:

What was your last question?

Dave Montemayor, UBS:

The second question is basically about the Griffins, what do you think is the best or maybe the first product of Griffins that could be launched in pan-ASEAN?

Nilo Mapa, Executive Vice President and Managing Director, URC:

We are undergoing that process right now. We are not at liberty at this point in time to disclose that. It is currently being developed jointly between our country heads and the Griffins people.

Dave Montemayor, UBS:

Okay, thank you.

Speaker:

We appear to have no further questions at this time. I'd like to hand back to today's presenters.

Lance Gokongwei, President and CEO, URC:

On behalf of URC we'd like to thank you for joining in the call. We'll speak to you again next three months. Thank you.

[END OF TRANSCRIPT]