

Brembo S.p.A

"First Half 2019 Financial Results Conference Call"

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MODERATORS: **MATTEO TIRABOSCHI, EXECUTIVE DEPUTY CHAIRMAN**
 DANIELE SCHILLACI, CHIEF EXECUTIVE OFFICER
 LAURA PANSERI, HEAD OF INVESTOR RELATIONS

OPERATOR: Good afternoon. This is the Chorus Call conference operator. Welcome and thank you for joining the Brembo First Half 2019 Financial Results Conference Call. After the presentation, there will be an opportunity to ask questions.

At this time, I would like to turn the conference over to Ms. Laura Panseri, Head of Investor Relations. Please go ahead, madam.

LAURA PANSERI: Yes, good afternoon, ladies and gentlemen. Thank you for joining us today to the Brembo's Group first half 2019 financial results. Today's call will be hosted by Matteo Tiraboschi, Executive Deputy Chairman and by Daniele Schillaci, CEO of Brembo. Detailed slide presentation has been made available on our website in advance so we suggest that we go directly to the Q&A session.

Before we begin, let me remind you that any forward-looking statements that we may make during today's call are subject to risks and uncertainties that can cause actual results to be materially different. I also remind you that this call is being recorded. With that, we can start the Q&A session, please, operator. Thank you.

Q&A

OPERATOR: Thank you. This is the Chorus Call conference operator. We will now begin the question and answer session. The first question is from Renato Gargiulo of Fidentiis. Please go ahead.

RENATO GARGIULO: Yes, good afternoon. Well, my questions are about your updated guidance following your guidance for the full year. First of all, I was wondering about the Chinese market. You were anticipating before a single-digit growth for Brembo this year. You experienced a 4% decrease in the

second quarter. What are your...what is your updated outlook for the full year and also for the second semester?

Second question on North America, even in this case if you can give us an update about your outlook on the second part of the year and an update about your current level of orders for calipers? And third and last question, about your on your guidance, if you can give us any more indication about your underlying assumption for the pricing effect and FOREX? Thank you.

MATTEO TIRABOSCHI: Thank you. I'll try to give you the first and the last question and about the market Daniele will give you an overview about the market where we are and what Brembo is doing. Guidance for the full year: to be honest, it's a very difficult to give you a correct number about the full year. In the last conference call, we said that the top line should be in line with the previous year. Today it is more difficult to maintain the same number, because the market, as you can see, is going down. Sales in the second quarter were declining, impacted by different factors, but should I give you a number today, I would say full-year revenues will be down around 2%-3% compared to last year.

We are now working on maintaining the same percentage of EBITDA, we are very focused on managing in the best way the rump-up of the new plants. Obviously, they are not working at full capacity and this is the point regarding profitability. About investments, we confirm the capex at around €200-220 million, full year basis.

Daniele, if you want to give an overview about the market...

DANIELE SCHILLACI: Thank you, Matteo. Good afternoon, everybody. I am Daniele Schillaci. Regarding the market in China, what we have seen is that sales in China for the first half were down 12.4% versus last year. If you look at the forecast, what we hear around is that the H2 should be a bit better than H1, but the full year forecast might be around -10% versus last year.

In the U.S. the first half of this year is - 2.1% and the full year forecast in terms of sales is maintained at around -2% also. If you want me to give you a kind of a global picture, also including other areas like Europe and other part of the world, we see a global automotive market in the range of around - 4% versus last year. So this is what we see from our side.

RENATO GARGIULO: Okay. So just a couple of follow-ups. On China, is that your focus for the total market or your expectation for your sales because you yourselves further ramped up production I suppose in the second part of the year? And if I may, a second one on your EBITDA Bridge, in your operations line, first of all is it still including some ramp-up costs in the second quarter and if you expect any material impact in the second part of the year? Thank you.

DANIELE SCHILLACI: Of course the numbers that I gave you before, are about the automotive sales. It is what we see in terms of markets.

MATTEO TIRABOSCHI: In terms of forecast for Brembo, as I said before, it regards the overall forecast of the business for the full year.

For the EBITDA bridge, we are talking about operations. In operations we include fix costs for the plants, we have more plants, more people all around the world and so higher costs. There are not start up costs in this moment, our factories, our industrial activities are growing, but of course not as fast as we expected, because the market is not performing well.

RENATO GARGIULO: Okay. Thank you. Thank you, very much.

OPERATOR: The next question is from Andrea Balloni of Mediobanca. Please go ahead.

ANDREA BALLONI: Yes, good morning all. Thanks for taking my question. My first one is about net working capital may be the second quarter has generated an amount of cash far below last year if my math is correct, any comment on that would be helpful? And my second question is about Argentina. Can you give us more detail about the impact on Q1 and Q2 and full year '18 of Argentina in terms of EBITDA that should be a loss if I am not wrong. And my very last question is about the guidance, you have guided about an EBITDA margin which is in line with last year, I would like to know if this EBITDA margin is also including the IFRS 16 impact, as well as, the deconsolidation of Argentina? Thank you.

MATTEO TIRABOSCHI: Net working capital. We know that that we are not performing in the best way about net working capital. We discussed this morning with the board about this point, we have some work to do and we are very focused to push the net working in the next month, for sure.

Argentina is a subsidiary that we needed to close because the business there has completely disappeared, our customers left the country, so we couldn't continue with our operations in Argentina. Therefore we had to reclassify revenue and costs of the Argentinian subsidiary (€ 6 million in the first half); the negative result of the company's ordinary operations in H1 as well as the estimated costs associated with the discontinuation, were reclassified in the item "Result from discontinued operations" (amounting to €6.8 million), at the bottom of our P&L, before net profit.

Regarding EBITDA: probably we can have some help from IFRS 16, in this moment I prefer to be cautious, I would say it's in line with last year including IFRS 16.

ANDREA BALLONI: Okay, thank you. Just a follow-up, about net working capital. You said that this is worse than your expectation, but what's the reason why you have generated less free cash flow from net working capital in the second quarter compared to last year? And about Argentina, sorry for asking

again, but just to understand the real net trend of EBITDA, which was the impact given or taken on EBITDA in the second quarter and which was the impact last year?

MATTEO TIRABOSCHI: In this first half of this the impact was negative for €6.1 million. About the net working capital please remember that the end of June was during a weekend, so when normally customers don't pay.

ANDREA BALLONI: Okay, thank you.

OPERATOR: The next question is from Martino De Ambroggi of Equita. Please go ahead.

MARTINO DE AMBROGGI: Yes, thank you. Good morning, everybody. A just a couple of clarifications on the guidance, sorry, to go back to the issue; but, just to to understand last year, the starting sales were for sure lower because you are deconsolidating Argentina, and EBITDA last year was 19%, but presumably deconsolidating Argentina, it's above 19%. So just to have an idea of what you mean, when we talk about EBITDA similar to last year, I clearly understand it doesn't include any more the 80 bps, 90 bps of additional contribution for the IFRS 16. But is it still 19% at the starting point of EBITDA margin for...to compare with this year?

MATTEO TIRABOSCHI: EBITDA of Argentina last year was close to zero. You have to remember that Argentina is very, very small subsidiary for Brembo, the full year revenue last year was approx. €13 million and it was breakeven... We decided to close because our customers decided to move the platforms away from Argentina. So it's the direct consequence of the decision of our customers. We will continue the business that we had in Argentina from Brazil, so we probably won't lose the business in the future, but in the short-time, yes.

And when we say that we can imagine a direct EBITDA in line in terms of %, we are working in a very difficult season in our sector. There is not a clear visibility for the second part of year. So we prefer to maintain some prudence in our numbers because the scenario is not clear, from all the customers.

MARTINO DE AMBROGGI: Okay. Thank you. And the second question is on the divisional performance because if I look at the second and the first half...the second quarter and the first half revenues, basically all the decline comes from the car business while all the other divisions were up. Is it still the case for the rest of the year? So the other divisions are able to maintain a positive trend or is...they will contribute to the decline?

MATTEO TIRABOSCHI: The passenger car segment was the most affected by the negative performance of the market for sure. There were also the phase-in, phase-out of some new models that was not exactly in line with the initial expectations. We expect that also for the second part of the year, the other businesses will be positive.

MARTINO DE AMBROGGI: Okay. Thank you. And the last clarification on the guidance, when you talk about the plus 2, 3...minus, sorry, minus 2%, minus 3%, it's referring to the volumes or sales?

MATTEO TIRABOSCHI: Thank you to remember to me that is with minus, yes.

MARTINO DE AMBROGGI: No. Sorry. It's referring to volumes or sales?

MATTEO TIRABOSCHI: To revenues.

MARTINO DE AMBROGGI: Okay, perfect. And the last one is on the M&A because you repeated several times in interviews that you are looking for big acquisitions. I don't know if there is any update that you can share with us?

MATTEO TIRABOSCHI: Your question is correct. We spoke several times about it, also on newspapers and magazines. There is nothing on the table today, but we know that is an important way for the future of the Brembo. So we are working seriously on it and that is there is nothing concrete at the moment.

MARTINO DE AMBROGGI: Okay. Thank you.

OPERATOR: The next question is from Monica Bosio of Banca IMI Intesa San Paolo. Please go ahead.

MONICA BOSIO: Yes, good afternoon. Just two follow-ups on the previous questions. The first on the guidance on the revenues, minus 2%, minus 3% at the consolidated level. This is the combination of the car, which I...which is expected to end the year, on a negative ground offset...partially offset by the rest of the business. Can you just give us as an indication of just for the car division for the full-year in term of revenue slowdown? And do you still expect that the commercial vehicle will keep such a high growth rate also in the second part of the year?

And the second question is on the saturation of the plant. If I asked well plants are not fully saturated at this moment, given the difficult situation. Can you give us just a rough indication of the capacity utilization rate of the plants overall? Thank you very much.

MATTEO TIRABOSCHI: I will try... Obviously minus 2%, minus 3% is because passenger cars will be not positive. What we imagine, overall, is a market close to minus 4%-5%, someone sees it at minus 6%, someone at minus 3%, we stay in the middle, and we say minus 4%, minus 5%, something like that overall. Obviously, Brembo is normally more resilient to the market conditions, but we can't do miracles. So when the market grows, we grow better, when the market is going down, we hope to loose less than the market.

Commercial vehicle, they were positive in the first half, probably in the second part of the year, they will still be positive, but not so strong, probably below 10%.

MONICA BOSIO: Okay.

MATTEO TIRABOSCHI: About saturation. We have the new plants that are not yet fully saturated. More in detail we have the Polish plant, a cast iron foundry and nodular cast iron for commercial vehicles calipers: most of it is saturated. We have the Chinese new plant for alloy calipers: there we need one year or maybe something more, to complete the ramp-up of the plant, so in China there is some free capacity available. Then we have the Mexican plant, cast iron foundry and machining shop for discs: there is some free capacity that we can utilize when the market is recovering.

MONICA BOSIO: Okay, I had to imagine that these. Can you give us just a rough number of the capacity utilization rate that you usually run at 98% to 100%? Can we say that the new initiatives Poland, China, Mexico, are running at the 80%, 85%?

MATTEO TIRABOSCHI: It's difficult because they are plants for different business, passenger cars, motorcycle racing and so on, so it really depends on which plant and which country we are talking about. It is very difficult to give you an average number

MONICA BOSIO: Okay. And very last, you mentioned at the very low visibility, I remember that the usually visibility for Brembo is 3 plus one month, is it correct. What is the visibility now?

MATTEO TIRABOSCHI: Visibility, I would say, now is not so good. Some OE customers are talking about some stocks that they have. In September, they will probably re-evaluate the situation and give us some forecast for the rest of the year. Please remember that Q318 was a very, very strong quarter for Brembo, and not only for Brembo, because of the WLTP, so, frankly, the comparison will not be easy in the next quarter.

MONICA BOSIO: Yes. Correct. Thank you very much.

MATTEO TIRABOSCHI: Thank you.

OPERATOR: The next question is from Alexandre Raverdy of Kepler Cheuvreux. Please go ahead.

ALEXANDRE RAVERDY: Thank you very much. I have 2 questions, please. The first one, is on the out performance. What has materially changed for you in Q2 versus Q1 because the environment was already tough in Q1 and you managed too much better, and in Q2 we saw the performance so clearly decelerating? So, I just wanted to understand what has changed for you. And the second question is, I was surprised by the resilience of the business in India, despite the market crash over the over the past month.

So what will explain such a strong performance in a country and should we expect the same trend to continue for the rest of the year? Thank you.

DANIELE SCHILLACI: Yes, I will try to answer your question, we have several factors, you have some also project delays from some players along the years, you have some also calendar years, you know, I would say seasonality that we need to take into account. But one thing is sure is that we are proceeding now more and more, since I would say the beginning of Q2, a slowdown of major markets, like China and also Europe. That was not the case at the beginning of the year. So this is a bit combination of these factors.

ALEXANDRE RAVERDY: Okay. So, just maybe before moving to India finally, do you still use I mean do you use for the top line guidance minus 4% as an assumption or do you use something more let say conservative?

DANIELE SCHILLACI: It's an assumption, yes, if you look at the trend of the 3 big markets that cover the vast majority of the automotive sectors: Europe, US and China, if you look at the trend of the first half and you make some kind of extrapolation, you'll see, as I said before, China in H2 losing some market (H1 I remind you it was minus 12.4%), maybe in H2 China will see a drop of around 6% to 7%, combined is minus 10%; in U.S., we will keep the find of - 2% across the year for H1 and H2.

And Europe; in Europe today we have two speeds: you have the western part of Europe, the big countries like Germany, France and Italy, where the market is not so bad. In Germany in 1H the market is stable, in France slightly down. In the eastern part of Europe we see some drop of two digits. So, combined Europe is -3% in the first half. And we see this minus 2.5%- minus3% to stay also in H2. So, to summarize, when you look at the overall market, we assume that there will a market at -4% -5%.

ALEXANDRE RAVERDY: Okay. Thank you. And on my question on India, please?

LAURA PANSERI: Can you repeat your question, please?

ALEXANDRE RAVERDY: Yes, I was surprised by the strong resilience in India despite...I mean we have seen the market decelerating quite strongly over the past months or how can you explain such a strong outperformance in the country?

MATTEO TIRABOSCHI: Yes, it is correct, the new safety regulation in India is helping us with our products. India is growing, and we are growing fast in this market.

ALEXANDRE RAVERDY: Okay. Thank you very much.

OPERATOR: The next question is from Gianluca Bertuzzo of Intermonte. Please go ahead.

GIANLUCA BERTUZZO: Hi, good morning to everybody and thank you. The first one is on guidance. I am sorry to come back again on this point but I didn't understand. So, let's assume IFRS 16 has never come in force, you still expect profitability in line with last year or you expect 1% decline in terms of profitability. Then, I have another question, if I look at your historical outperformance compared to the market; you outperformed the market by around 5% to 6% over the last few years. Now, considering the guidance you just provided as well as the positive expectation for commercial vehicle and other business, it seems you are guiding the outperformance to reduce compared to the historical level. Are these figures reflecting a cautious approach to guidance or is there something else going on? Thank you very much.

MATTEO TIRABOSCHI: It is difficult to answer, to be honest. Yes, the guidance about the EBITDA includes some help from IFRS compared to last year, probably

we are we are conservative, and too cautious, but when the market it is going down it's very difficult to give numbers seriously,

The market in my opinion will be more negative than some analysts assume, someone says minus 4%, minus 3%; I am a little bit negative, so probably our approach is more conservative. In terms of revenues, Brembo usually performs better than the market, so if we assume a negative market at -6% and we close at minus 2, minus 3, this is still implying a good outperformance compared to the market.

GIANLUCA BERTUZZO: Thank you.

OPERATOR: As a reminder, if you wish to register for a question, please press "*" and "1" on your telephone. Once again, if you wish to ask a question, please press "*" and "1" on your telephone.

The next question is a follow up from Renato Gargiulo of Fidentiis. Please go ahead.

RENATO GARGIULO: Yes, very quick one. On the tax rate, can we assume 22% tax rate for a fully year as a guidance and any update on patent box? Thank you.

MATTEO TIRABOSCHI: 22% is a fair assumption, you know that when we talk about tax rate is very complicated to be predicted, but for the moment something around 22 is reasonable. Patent box, we are working on it and probably by the end of the year we will be able to share some more details.

RENATO GARGIULO: Thank you.

OPERATOR: The next question is from Gabriele Gambarova of Banca Akros. Please go ahead.

GABRIELE GAMBAROVA: Yes, thank you. Very quick question from my side, it is on...at industry level, how do you see the level of stock in the industry. Are they tight or, I mean, how is the situation from your perspective regarding your clients I mean?

DANIELE SCHILLACI: What we guess is that given that indeed market is here, it is tougher and tougher. We assume that the stock level now in the industry is probably above the standards, because everybody is trying to achieve the targets and the targets were fixed last year. Probably some budget assumptions were a bit more optimistic and if you connect the dots, we suppose that the stock level should be at least at standard level, if not above. I would be, honestly speaking, surprised if they were below.

GABRIELE GAMBAROVA: Okay. Thank you.

OPERATOR: The next question is a follow up from Martino De Ambroggi of Equita. Please go ahead.

MARTINO DE AMBROGGI: Yes, thank you. A follow up on the CAPEX, because you mentioned 200-224 for the current year, so you are confirming in any case the CAPEX despite lower volumes, but if in 2020 there is a further decline of the market volumes, what should we expect, significant reduction below the 200 million or you are...okay I know you will answer it is too early to give you a guidance but just to have an idea if...

MATTEO TIRABOSCHI: Yes, It is...to be honest it is too early. We need to better understand the market of next year, before sharing some detail about CAPEX. Obviously, there will be the usual maintenance CAPEX, something around 60 million, 70 million per year, on top of which there will be the new CAPEX, but everything depends on the volume and the strategy of our customers. Now it's a bit too early.

MARTINO DE AMBROGGI: Okay, and any new big platform so you got in the past few months you can share or...

MATTEO TIRABOSCHI: We work every day to win new platform and new business, but you know that we can't share the new platforms and the new projects of our customers.

MARTINO DE AMBROGGI: Okay. Thank you.

OPERATOR: Ms. Panseri, gentlemen, there are no more questions registered at this time.

LAURA PANSERI: Okay, thank you. Thank you everybody for having taking part in our call and have a good afternoon. Thank you, bye-bye.