

Brembo S.p.A.

"Full Year 2018 Financial Results Conference Call"

Monday, March 04, 2019, 14:00 CET

MODERATORS: **MATTEO TIRABOSCHI, EXECUTIVE DEPUTY CHAIRMAN**
 ANDREA ABBATI MARESCOTTI, 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 Full Year 2018 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 IR. Please go ahead, madam.

LAURA PANSERI: Yes, good afternoon to everybody. Thank you for joining us today to discuss Brembo's Group full year 2018 financial results. Today's call will be hosted by Matteo Tiraboschi, Executive Deputy Chairman and by Andrea Abbati Marescotti, CEO of Brembo. A 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, I can open the Q&A session. So please operator go ahead. Thank you.

Q&A

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

RENATO GARGIULO: Yes, good afternoon to everybody. Well, my first question is about your 2019 outlook on volumes. You are stating that you expect flattish

volumes year-on-year. Can you give us any more indication about this indication and in particular referring to China, I was wondering what kind of visibility do you have about this year's volumes also based on our progressive ramp-up of capacity utilization for aluminum calipers? Then my second question is on profitability, you have reported overall around €50 million cost from operations. I don't know if you can give us any more indication about how much of this can be considered as non-recurring? And then my final question is on NAFTA, even on this side if you can give us any more indication or an outlook for 2019? Thank you.

ANDREA ABBATI MARESCOTTI: In January worldwide car sales were down 8.3% - really an unbelievable number - with very bad performance in China -16%, but also in Europe -5% and showing some difficulties also in North America - 2.4%. February preliminary data show a somehow more limited drop in sales, but still a drop. In such a tough scenario we see Brembo maintaining the same level of sales, which means that as of today Brembo is gaining some market shares. Of course, this is a combination of our specific segments – premium cars are performing slightly better than the overall market - plus real market share. So we are confirming in our guidance that in the current very uncertain scenario, Brembo will confirm the same sales. And then going on with the year, we will see if the market scenario changes, currently this is the year...

China: China market in 2018 posted the first decline in their modern history, declining 3.1%; in the same period Brembo grew nearly 15% net of exchange rates (or +12% including forex). Car sales in January and February were really bad, all the same we see again Brembo outpacing the market. It is very difficult to make a full-year forecast on a market such as China, which can really be influenced by change in the legislation, but I can say that we see a growth for Brembo in China this year, I prefer not to give numbers, though. Even in the worst scenario, we see Brembo growing in China also this year.

NAFTA: You asked what we see in NAFTA, well maybe this is even more difficult than China, because already last year, NAFTA did better than the normal consensus was aiming to. Mid-term all the analysts see in three/four years market flat at 70 million vehicles. It is very difficult to say if NAFTA will make plus or minus this year, in my personal opinion total NAFTA market could do something like - 2%. In this market, at least we will be stable with potential for growth, but I don't want to fragment our guidance across the markets; our guidance is based on the current global market scenario and confirms 2018 sales.

OPERATIONS: we already mentioned it in the last two/three calls; in the combination of the ramp-up of the new plants and having to handle at best changes in demand by our customers, which may rapidly change their minds, and vast footprint, there is a tangible portion of those operations 2018, which we do believe is one-time and not recurrent.

But this is already encompassed in our guidance, in a flat market, we are exploiting our best capabilities to offset what a flat market means.

RENATO GARGIULO: Okay, thank you. And if I may just a quick follow-up, can you give us an update about your investments in China, Poland and Mexico? Thank you.

ANDREA ABBATI MARESCOTTI: As of today, with a tough market, our investments are just completion of what we already did. So the Nanjing plant for calipers is adding the last machinery, the Mexico plant is following the very good growth of its main customers - I can mention Tesla which is doing very well, so you will see investments which are basically the completion of what already announced.

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

OPERATOR: The next question is from Monica Bosio with Banca IMI. Please go ahead, madam.

MONICA BOSIO: Good afternoon everyone and thanks for taking my questions. The first one is on the top line, now that is clear that for 2019 the growth will be zero, I can imagine that you are expecting two different trend H1 versus H2. Should we expect in H1 year-on-year below the H1 of 2018? This is my first question, because I believe that the comparison base will be tough in the first part of the year? And my question regards both the top line and the EBITDA margin? And the second question is on more general, if I look at the country level for the full year Brembo increased by 5.3% with Germany...in Germany, while in the last quarter of the year there was a decrease of 5.8%. So I was just wondering if you can give us some more color on your revenues in German. And other two questions, the third one is on CAPEX, the CAPEX was higher than our expectations, and if I am not wrong higher than your initial indications €285 million? And I was wondering what kind of CAPEX are you projecting for the 2019? And can you give us also some clarification regarding the trend of the financial charges, I have seen that they increased a lot partially was due to the FOREX, but it was also due to the financial charges itself? Thank you very much.

ANDREA ABBATI MARESCOTTI: Question one, trying to the split the volumes scenario H1 versus H2, Monica it' is a nightmare. It is impossible for me to say if H1 will be worse than H2. At my current understanding no, but Monica it's very, very difficult, because the customers are taking very short notice on changes. There are so many changes up and down - so it is not that they are going down, they are changing their minds (someone increases the order, someone decreases and so on...). As of today there is no reason to think that H1 will be worse, than if you ask me I would like the opposite, that H2 is better, but I cannot say today.

MONICA BOSIO: Okay.

ANDREA ABBATI MARESCOTTI: Second Germany: what you saw in the data is exactly what is happening here. So the German customers had a question mark in their minds, of which the redistribution of proportion; I mean, what do they do with a very vast capacities of producing diesels, which customers don't buy any longer, causes sharp changes in the orders, specifically the diesel models, they are - I guess - without making names, destocking. So what you saw in the Germany last quarter is simply that they are trying to rationalize what they have in stock, because in average they have issues in selling diesels.

MONICA BOSIO: Okay, do you think these trends will continue, at least for the first part or it could be almost over?

ANDREA ABBATI MARESCOTTI: I would answer out of my stomach, so I prefer not to. I saw the orders in January and February by the German customers were normal.

MONICA BOSIO: Okay.

ANDREA ABBATI MARESCOTTI: Third point CAPEX: I guess we already said in the last call in November that our expectation for CAPEX in 2019 is €250 million - wrong number. Certainly, if the world goes on like this, we could even try and we are trying, to be very wise in the right time for an investment. So if the market goes on being, so sluggish, we will be really careful. But the major portion of those investments are basically the machinery for new platforms and new lines, so sooner or later to serve the customers you have to put it, so plus or minus, that's it.

MATTEO TIRABOSCHI: Financial charges, Monica, are related to taxes. If you look at the comparison with the previous year, you'll see that taxes increased significantly in 2018, by 24%. This is the result of a settlement that was reached in December between Brembo and the Italian Tax Authority regarding an alleged violation of the transfer pricing rules for fiscal years 2012-2013. You may know that the transfer pricing is quite complicated for multinational companies like Brembo, with business, plants and subsidiaries all around the world.

We reached a settlement with the Italian Tax Authority for the period 2012, 2013 and for the following years, and this resulted in a higher taxes and higher financial charges for the interests on the paid amount.

MONICA BOSIO: Okay. Thank you.

OPERATOR: The next question is from Andrea Balloni with Mediobanca. Please go ahead, sir.

ANDREA BALLONI: Hi, good afternoon, everybody. And thanks for taking my question. My first question is about the pricing, is it fair to assume some price increase for your products in order to reflect the raw material cost inflation you should have experienced last year. And my second question is about the order intake, which visibility do you have so far, if I'm not wrong really, your order intake should cover around 3 to 5 months? Do you see any cancellation or delay in terms of order so far? And then my very last question is about the CAPEX. Honestly, I didn't understand the amount of CAPEX, you have guided on 2019, could you say it again, please?

ANDREA ABBATI MARESCOTTI: Pricing is contracted, so changes in pricing due to raw material evolution are contracted. They come depending upon the customers with some delay: best case for us is three months, worst case even one year in some cases in China, normal case is six months; so in a scenario of raw material increase you see price adjustment coming a little later, in a scenario -which sooner or later will come- of raw material

decrease you see the reduction of prices coming 3-6-9 months later, but it is contracted and that's for us is better. So we are not putting any kind of pressure on the customers because it is contracted. And we do like to stay with contracts because that's for us is the guarantee of stability. And so, when it comes, it comes; you know that there are short portion of the empire in which you don't have a strict contractual mechanism, specifically in some portion of China, but I have to say that at the end of last year, we were able to reach a satisfactory agreement also with those customers with which it was not contracted, so it has no real impact on our marginality.

Order intake visibility is the one which leads our guidance of course and whatever we see, it changes with the market. Europe is somewhat more visible, but let me say that on average, except for China, we see nearly five-six months ahead; Chinese customers are different, they give you the orders the month before so it is impossible. We have a clear knowledge of the market, we talk a lot with our customers, but that is different than measuring the real order intake.

Cancellation /delay, no, we don't see any cancellation or delay. What we see – but this is a public information – we see many customers postponing some new platforms. They prefer - as always in this industry - to launch the new models in better general conditions. So the new platforms, which were going to be this year, are one after the other going to 2020, but likely that is not influencing the stability of our volumes. Of course, it may be influencing the growth of our volumes, since we win more business than we lose, of course, new platforms normally means Brembo ramping up. But that is normal when the business of automotive is not going particularly well.

CAPEX, the indication already given in November for 2019 is €250 million, plus or minus.

ANDREA BALLONI: Okay. Thanks a lot. Just a couple of follow-up, about pricing, so is it fair to assume in our model a modest topline growth in order to assume flattish volume and a slight increase in selling prices? And the very last question is about net working capital, to me it looks to be pretty good free cash flow generator, mainly in the last part of year. Should we expect any reversal trend in 2019 about net working capital?

ANDREA ABBATI MARESCOTTI: Okay. First question, pricing, yes, but it is really unmaterial, zero point something.

Net working capital, we were a little worried about the end of the year closing with many holiday dates, we were not so certain about what our customers were doing, so it is fair to say that in the payables maybe we were a little more stingy than usual. As a fact, receivables were very good. So yes, there is some over- performance in the working capital at the end of the year. We did really well on the stocks. That is the balance of receivable and payables. You are right. There is some portion of over-performance.

ANDREA BALLONI: And should you expect any reversal trend in 2019?

MATTEO TIRABOSCHI: It is very difficult to know how our customer will be working during the year.

ANDREA BALLONI: Okay. Thank you.

OPERATOR: The next question is from Martino De Ambroggi with Equita. Please go ahead, sir.

MARTINO DE AMBROGGI: Yes, good afternoon everybody. The first question is always on the guidance for the topline, because you are guiding for volumes flat and sales flat, what about on a standalone basis mix, price and FOREX in your assumption?

MATTEO TIRABOSCHI: We are talking only about volume, not forex, not mix. What we see in this moment is that the market is negative and we keep finger cross to maintain the same volumes of last year. It is not easy but it is without the impact of FOREX or mix.

MARTINO DE AMBROGGI: Okay and I don't even expect in FOREX...at least FOREX slightly better if not for other...for the US dollar we should have. Obviously, we don't know...

MATTEO TIRABOSCHI: Yes, the FOREX can help.

MARTINO DE AMBROGGI: So it is not included in your flattish topline guidance?

MATTEO TIRABOSCHI: My flattish guidance is with exactly the same FOREX of last year.

MARTINO DE AMBROGGI: Okay. And the second is the €250 million CAPEX. Typically when you have such a high level because it is not the all-time high but it is in any case quite high level 9% plus of sales. Typically, when you had such a high level of CAPEX, because you are increasing the capacity, because you used to work at full capacity. So it seems to be a little bit...a mismatch between flattish volumes and CAPEX still strong. I understand you mentioned we need to keep new platforms, so we are obliged to do it, but just wondering if maybe the 250...it is a message of cautious optimism going forward?

ANDREA ABBATI MARESCOTTI: Actually, Martino, if you know us very well, it is a combination of three things. One, there is some carryover of what we consider already invested but it is not yet, because of course the payment on investment has some lead times. It goes with the ramp up of the plant to see that the machinery really works well and so on. So in the 250 million, there is a portion, a round number, €50 million of what you call already the past, but that still is not in our P&L.

MARTINO DE AMBROGGI: Which are...sorry, Andrea, which are the Chinese and Mexican plant you mentioned before?

ANDREA ABBATI MARESCOTTI: Exactly, and the final completion of the third foundry in Poland, because also the foundry in Poland - the one for nodular cast iron - is still being completed. Second, there is the normal business; third there is building up the future, so certainly, if our customers are delaying the new platforms by a year, this means that very likely between 2020 and 2021, there will be a big rush on new platforms and it is the normal behavior of Brembo that we will be ready. You remember very well that when the world was in crisis in 2008/2009, Brembo was building its succes investing. So, you already have the answer.

MATTEO TIRABOSCHI: We invest not for this year, but for the future. This is the point.

MARTINO DE AMBROGGI: Yes. And the other question is on the net financial position, because considering the extra performance in 2018, okay, maybe driven by some recurring impact in net working capital, you are going to basically zero that or almost zero that in 2019? Have you any plan, I don't know acquisitions, we discussed it several times in the past, but any other option for the cash utilization?

MATTEO TIRABOSCHI: No, for the moment, there aren't dossiers on the table for M&A, unfortunately. Obviously for us it's vital for the future to find the correct target and to do a deal with them, but for the moment, nothing concrete to be honest.

MARTINO DE AMBROGGI: And just to finalize the M&A section, let's say the dual voting right, the double voting right for long-term shareholders?

MATTEO TIRABOSCHI: This is in line with what I've just said. For Brembo, a non-organic growth is very, very important. We are ready also for very transformational deal and at the increased voting rights proposal is aimed at maintaining the control of the company also in case of an extraordinary acquisition. Obviously, this is an option that we want to have, we don't know yet, if we are going to use it or not.

MARTINO DE AMBROGGI: Yes, clear. But, would it be open also for a merger or just in case of a rights issue and so on?

MATTEO TIRABOSCHI: What is important is the future of our company. The future is growth in a profitable way around the world, without limits.

MARTINO DE AMBROGGI: Okay, okay. Interesting and very last one, the tax rate, which was unusually high this year. So the guidance going forward is always 22% as it is...it had been last year.

MATTEO TIRABOSCHI: The normal tax rate without any extraordinary effects is something around 24%, 25%; this year there is this extraordinary tax submission, we have positive effects from US, from Poland, and that's it.

MARTINO DE AMBROGGI: So, already for 2019?

MATTEO TIRABOSCHI: Probably less, probably less, for next year probably less. Something around 22-23%, something like that, but it's very difficult to predict.

MARTINO DE AMBROGGI: Okay. Thank you.

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

ALEXANDRE RAVERDY: Good afternoon. Thank you for taking my question. I just have one question left, please. Could you please provide some information on IFRS 16, will there be any material impact for you and if the profitability guidance takes that into account? Thank you.

MATTEO TIRABOSCHI: We are working on it. I can try to give you some general numbers, but we are still working on some fine-tuning. On the debt, we expect an increase of around €150-€170 million; on the profitability, I don't think that there will be a significant impact, just zero point something.

ALEXANDRE RAVERDY: Okay. Thank you very much.

OPERATOR: The next question is from Michele Baldelli with Exane BNP Paribas. Please go ahead, sir.

MICHELE BALDELLI: Hi, good afternoon to everybody. I have a couple of questions, the first one is related to the assumptions behind your assumption about the market. If you say that the sales volumes would be flat this year, it's based on a view of the market that will be down or will be flat, what's your view? Second question is related to the trends of the overall business, because if you see the volumes are stable and there is a structurally good

trends of aluminum calipers, I am just wondering, are you losing share on the discs? Thank you.

ANDREA ABBATI MARESCOTTI: Actually our guidance of flat volumes is not based on the market, it is based on the orders, and this goes back to the question of your colleagues before, about order intake. We have full month of sales solid...3/4 months of nearly solid orders and what we see is comparing to last year, basically same volumes- stop. I don't even try to reconcile this with the real sales of my customers, because that can be so strongly influenced by their stocking or destocking policy. So with the current forecast of the market, which my customers are doing, I see that Brembo is able to maintain the same volumes. Within this, there may be areas that decrease and some areas that increase. Of course the alloy caliper business for us is more linked to premium customers, more than the discs. So certainly, when the global sales go down, it is easier that the alloy calipers don't see it and that discs see it a little more. All the same, I'd say that the disc business, plus or minus, is confirming the volumes of last year because we are entering new portion of segments, which were not ours.

MICHELE BALDELLI: Okay. Thank you very much.

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

The next question is from Gabriele Gambarova with Banca Akros. Please go ahead.

GABRIELE GAMBAROVA: Yes. Good afternoon to everybody. Just one question on the matter of the possible, let's say, tariffs on cars produced in Europe and then exported to the U.S. Is it possible to understand that what might be, let's

say, the volume of your business that would be potentially affected by a similar, let's say, initiative?

ANDREA ABBATI MARESCOTTI: The history of the last 12 months of tariffs is that we saw zero on our accounts and lower volumes. So my real expectation is zero. Basically all the Germans, in case of real tangible tariffs, would have the possibility to switch platforms to other plants, and to grow around the tariffs. So I really don't see any tangible effects. I can produce in two-three months the same part number in any part of the world that may be affected. So I really don't see it.

GABRIELE GAMBAROVA: Okay.

OPERATOR: The next question is a follow-up from Renato Gargiulo with Fidentiiis. Please go ahead.

RENATO GARGIULO: Yes. Hi, just follow-up. My first one is on Tesla. Are you expecting any impact from the plant ramp-up in production in China. And in general, can you give us an update about us on the size? The second question is about the...your minor segments, commercial vehicles and motorbikes. If you can give any more indication about... you know, in this case about your expected outlook for this year? And finally very quick one, on the tax rate. Your guidance is including any impact from patent box, and do you expect anything material? Thank you.

ANDREA ABBATI MARESCOTTI: Tesla, I don't comment anything on the performances of my customers, but you can read the very important sales from Tesla. As a fact that they are in very short-term launching a new plant in China, as they announced the production of Model 3 and then of the coming model 'Y'; it is of course a really good news for us, as you can imagine.

Commercial vehicles: you know that our reference market is Europe, it's going not badly. So the plant is working really well. Volumes are good, the customers are satisfied, we are satisfied, we have some initial promising entrance also in North American market, so commercial vehicle is doing better than the passenger car segment.

MATTEO TIRABOSCHI: For the tax rate, no, we are not considering the patent box in the guidance we gave. We are still working on the patent box; probably in the second part of the year, we'll have some news.

RENATO GARGIULO: Okay. Thank you.

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

LAURA PANSERI: Okay. Thank you for joining us today on this call. Bye-bye.