



Transcription for ŞİŞECAM A.Ş

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Corporate Participant

Görkem Elverici
Şişecam – CFO

Presentation

Operator

Ladies and gentlemen, welcome to the Şişecam 2019 Year-End Financial Results audio and webcast Call. I'll now hand over to Mr. Görkem Elverici, CFO. Please sir, you may begin.

Görkem Elverici

Thank you. Good afternoon ladies and gentlemen. I would like to welcome you to our webcast. We will be talking about 2019 year-end results, and we would like to highlight some of the key developments that have had impact in our operations.

At the end of the presentation, we will be happy to take your questions, and I would like to remind you that our presentation and the Q&A session may be containing some forward-looking statements and our assumptions are based on the current environment and they may be subject to change.

So before moving onto the financial results, I'd like to talk about some major developments that took place in our group in 2019.

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On page two, you can find the major developments that have happened in the first half of 2019, and as we had a chance to go over them during the first half results presentation, I would like to move directly to the page three, where we will be talking about the second half-major development.

So, as you may recall, we started the second half with natural gas tariff hikes of 6.5% and 14% for electricity producers and industrial producers, respectively. Anadolu Cam has expanded its capacity in Mersin plant by 110,000 tons through a cold repair and a new furnace introduction, and the total capacity located in Turkey is now roughly around 1.34 million tons. It also announced the decision to resume production in Pokrov plants, and you may remember that this plant has been inactive since mid-2013.

70,000 tons of capacity will be operational in the second quarter of this year upon completion of a \$15 million CapEx program, and after nine months, cold repairs have been undertaken, Trakya Cam has resumed its production in Bulgaria and in Southern Italy in July and in October, respectively. Trakya Cam also became the full owner of Yenişehir and Polatlı plants through a simplified merger after paying TL 83 million in total for Şişecam for the respective 15% stake in these entities, and Trakya Cam got €200 million syndicated loan to fund its upcoming CapEx and net working capital requirement.

Establishment of Soda Sanayii's wholly-owned US-based subsidiary, Şişecam Chemicals USA and its 50% participation in Pacific Soda LLC have been completed by October. Soda Sanayii covered its initial capital commitment of \$6.75 million in Pacific Soda LLC and started consolidating the company based on liquidity calculated in the last quarter of 2019.

Put option for Pasabahçe shares has been exercised for €152 million, and apart from these, Moody's, and Fitch revised Şişecam's credit rating within the second half, and we have BB- with a stable outlook from Fitch and B1 with a negative outlook from Moody's.

Finally as you might know, we have relocated our headquarters to Tuzla Campus back in 2016 with a long-term lease contract, and last month, we

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purchased the real estate for a total of TRY 310 million plus VAT, which is roughly around TRY 60 million.

Now, we can move on to the financial and operational overview section on slide four.

In this slide, you will see that we posted a solid year-end result with more than TL 18 billion top line, which is up by 16% year-on-year, and a total of roughly around TL 4.3 billion adjusted EBITDA, which is 7% higher compared to what it was by the end of 2018. Adjusted net profit came in at around TL 1.9 billion with 11% margin, and the adjusted net profit margin was 14% the previous year. EPS decreased to TL 0.85 in 2019 from TL 1 last year as return on equity was at 14%.

And moving on to the next slide, the historic evolution of our top line and EBITDA performance can be seen, and 2019 was comparatively a more challenging year, especially for flat glass segment, which has the highest share in the group's revenue composition. It recorded lower margin levels due to mainly acquisition impact and less favorable pricing environment, especially in Europe. Glass packaging exhibited a resilient performance and recorded higher margin levels with strong volume and pricing both in Turkey and Russia. Higher energy costs in Turkey and lower sales volume on the chromium chemicals side and longer TL depreciation coupled with dilutive impact of glass fiber business were the main drivers of declining chemicals margin. Higher sales volume with better pricing and channel mix was supportive for glassware as discretionary downtimes and less favorable local currency depreciation compared to 2018 also had decreasing impact on the margins. Despite 200 bps decline in 2019, EBITDA margin level of Şişecam stayed above the sustainable level of 20%

Moving on to the next slide, the highest contribution to Şişecam top line continued to come from flat glass division. The chemicals business share came down in 2019 due to the reasons I mentioned in the previous slide, and glass packaging's solid performance was confirmed with its higher contribution to Şişecam top line, up from 21% to 24% by the end of 2019.

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On slide seven, glass packaging stood out again by increasing its contribution to EBITDA, while flat glass and other segments' EBITDA contributions decreased compared to previous year.

On slide eight, you can see that we recorded TL 684 million negative free cash flow in 2019, mainly due to the higher CapEx we experienced, and the operating cash flow continued to be strong at TL 3.4 billion.

Moving on to slide nine, CapEx increased to TL 2.9 billion, and the major CapEx items were the two cold repairs and a new furnace investment in Turkey in glass packaging, cold repairs in Bulgaria and South Italy, and new line investments in Turkey in flat glass, glass fiber plant maintenance, equipment renewal and operational efficiency investments in chemicals. Increasing investments still enabled an EBITDA-to-CapEx ratio of 1.7, reflecting our strong and continuous cash generation capability.

On slide 10, you can see the evolution of the production levels in the course of the years. In 2019, glass and soda ash production did not change significantly as capacity additions in glass operations was balanced with the cold repairs undertaken, and higher soda ash production in the second half resulted in, roughly, around 1% rise in total output year-on-year.

Moving on to the next slide, you will see that cash and cash equivalents, including financial investments amounting to \$500 million was up from \$1 billion to \$1.9 billion by the end of 2019. Strong cash generation from business operations and \$700 million Eurobond issuance were the main drivers of this increase, and the gross debt went up from \$1.5 billion in 2018 to \$2.7 billion in 2019 with the Eurobond issuance, a syndicated loan for flat glass operations and the other relevant borrowings.

Put option for Pasabahçe shares have been exercised for €152 million by the end of November, and €52 million of this was paid in cash and the remaining was structured as a financial loan.

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On slide 12, looking at the ratios, net debt-to-EBITDA and net debt-to-equity levels were 0.9 and 0.2 respectively, and still, we have a huge headroom considering the outstanding Eurobonds and the covenants stated in our loan agreement. Our hard currency denominated gross debt is 68% of the total, and 33% of the loans has a maturity of less than a year, which are Şişecam 2020 notes issued back in 2013, and they are maturing by May. The rest is mostly maturing in a one to five-year timeline, and as for the interest rate structure, the portion of fixed rate liabilities is at 78%. We signed a cross-currency swap for \$575 million out of the total \$700 million worth of Eurobonds.

On slide 13, you can see that we continue to have a long FX position of \$590 million at the consolidated level. We are loaning in dollars, while short in EUR in relation with the cross-currency swaps for hedging Şişecam 2026 bond.

Now, I'd like to walk you through each region in the last section of our presentation, and moving on to page 15, starting with the flat glass. Trakya Cam has capped off the year with TL 6.7 billion sales revenues, which is up by 13% year-on-year, and the EBITDA margin came down from 25% to 21%. The major drivers of the top line growth were relatively high average pricing and favorable currency conditions in 2019, as total sales volume was up by 1% year-on-year.

On a regional basis in Turkey, where we generate almost half of our revenues, construction activities was muted especially in the first half resulting in a 20% decrease in domestic sales volume, which was underpinned by the rising exports from Turkey. We have seen an uptake in domestic sales within the second half and ended the year with 13% decrease in domestic sales volume. Interest rate cuts brought some mobility to construction activities and the increase in domestic sales to export dealers was supportive as well.

On the profitability side, positive pricing in Turkey over the costs was maintained with consecutive price adjustments made in May and August until last quarter of 2019. Relatively larger spread between local and export

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prices resulted in higher export dealer rebates. In, and in the meantime, pricing in our export regions has also started to decrease.

We continuously maintain uninterrupted high-quality production as effective capacity utilization rate in Turkey was not affected from the current slowdown. Under these circumstances, we prioritize passing the benefits of the economies of scale on the company by carefully allocating the capacity without compromising utilization.

In Europe, where 37% of our revenues is generated, oversupply conditions created a challenging environment for the pricing, especially in the second half as we have seen a shift in demand from auto glass to architectural product and an increase in imports from surrounding regions, including Turkey. So, the revenues came down by 9% in euro terms year-on-year with sales volume down by 2%.

As you may remember, our plants in Bulgaria and Southern Italy, which were in cold repair for nine months, resumed production starting July and October, respectively. They will enable us to differentiate the sales mix in the region towards creating higher value. For 2020, all players in the region ought to watch the market dynamics closely as cold repairs may be undertaken and ease in the import pressure may reshape the pricing structure.

In Russia, our sales volume decreased by 7% year-on-year, reflecting weak first quarter sales at the end of the year with a 5% decrease in revenues in Rubles terms. Currency was supportive, especially in the second half.

And in India, the competitive pricing continued in the second half due to the new capacity introductions in the region. Dilutive impact of India acquisition, coupled with South Italy cold repair was 100 basis points on EBITDA margin in 2019.

Last but not least, we continue to take cost control measures for our auto glass operations with constantly improving capacity utilization rate. 2019 was a year of higher top line with a slightly lower margin for auto glass, as

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we continue to focus on margin improvement in this business line and to seek for opportunities, especially in the replacement market.

We spent over €160 million in CapEx in relation with the new furnace investments in Turkey and cold repairs in Bulgaria and Southern Italy, and investments in auto glass operations.

On page 16, glassware segment recorded TL 3 billion top line figure, which is up by 22% year-on-year, thanks to better pricing and higher volume, and adjusted EBITDA margin was around 15%.

FX gain on trade receivables and payables, which are included in our EBITDA definition at TL 59 million positive impact compared to TL 97 million sale in the same period last year. Excluding these gains, EBITDA margin was 13%, down by 70 basis points year-on-year, and IFRS 16 implementation had also a 170-basis-point positive impact on the margin.

Share of wholesale channel in total revenues continue to be the highest, while contribution of HORECA channel increased compared to the last year, suggesting further improvement thanks to increased consumer spending on tourism activities in domestic market, and high-quality and reliable service in international markets. Having grown by 19% year-on-year, international revenues uplifted the top line performance with increased contribution of sales through HORECA and retail channels, thanks to higher sales volume and favorable currency conditions. 63% of the revenues were generated from international markets, mostly in Europe, where our market presence strengthened and domestic sales were up by 27% year-on-year, mainly driven by contribution of sales through department stores with higher average pricing.

Our initiatives on working capital requirements reductions continued in the second half. Planned downtimes to manage inventories had a lowering impact on the profitability. These efforts will reflect its positive impact in the mid-term, and we spent €24 million for capital expenditures, which were mostly related to mould, production line improvements and IT investment.

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Moving on to glass packaging on page 17. Anadolu Cam increases its revenues by 31% in the second half of 2019 on a year-on-year basis, and full year top line growth stood at 33%, which was close to three times the local currency depreciation against euro, which is 12%. Per ton price adjustments made in all three operating regions, together with the change in sales mix, added 23% to the consolidated top line, while 8% was a result of local currency depreciation against hard currencies and ruble. Volume sales growth recorded at 2% had a minor positive impact, and in our local market, we experienced weaker demand for glass packaging products throughout the year. Still, we managed to have a significantly better sales performance in the second half and lowered the 15% volume contraction seen in the first half to 6% level at the year-end. In line with our strategy, we continued to expand our footprint in overseas markets through exports, and we ended the year with 59% increase in the volume of exports from Turkey. Meanwhile, sales from Non-Turkey operations went up by 0,4%. Our international sales, having grown by 38% in total, accounted for 57% of the consolidated revenues as of the year-end.

Despite the rise in raw material and energy costs, together with higher packaging, material and depreciation expenses, glass packaging Turkey unit's gross profit margin expanded from 29-32%, and we continuously increase our profitability in our non-Turkey operations, owing mostly to a capacity utilization rate of 99% on average in four active Russian plants. According to the regions, profitability went up from 32-35%, and on a consolidated basis, our gross profit grew by 47% in nominal terms and our margin stood at 33%.

OpEx-to-sales ratio inched up to 19% levels with increased logistic expenses due to the local currency depreciation, the growing inland transportation costs, larger scale of exports, and revision in royalty fee rate.

Our adjusted EBITDA grew by 45%, and we ended the year at 26% margin level, translating into a 220-basis-point expansion on a year-on-year basis.

FX gain on trade receivables and payables, which is included in our EBITDA definition, had a TL 39 million positive impact in the reporting period versus TL 133 million reported in 2018. Excluding these gains, EBITDA margin increased by 540 basis points year-on-year. We spent €140 million in CapEx

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in relation with the new furnace investments and capacity expansions together with cold repair, mold and operational efficiency investments. Through new furnace and development investments, we added 130,000 tons to our operating capacity in the local market, and on the consolidated basis, our total production capacity increased by 5% to 2.65 million tons. In the second half of the year, we announced our decision to bring back online one of the two furnaces located in Pokrov plant, and based on our initial plan, a 70,000-ton furnace will be ignited in the second quarter of this year and will be operational with a high capacity utilization rate.

For our glass packaging operations, we continue exploring the strategic opportunities, focusing on both maintaining our market leader position and expanding our international sales capability.

Moving onto chemicals division on page 18, our flagship company, Soda Sanayii, ended the second half of 2019 with 11% year-on-year growth in its revenues. The full year top line growth of 22% was 1.5 times the local currency depreciation against currency basket, which is 14%.

Although we had a scheduled coal-fired boiler maintenance program in Bosnia plant, thanks to the increased efficiency, we were able to increase our annual production by 1%. Soda ash sales volumes reported as 2.31 million tons were down by 1% year-on-year. We witnessed a decline in sales volumes on the chromium chemicals segment resulting from the alignment of sales mix parallel to the demand. Accordingly, we recorded 13% decline year-on-year in chromium chemicals volume sales.

Per ton soda ash prices increased by 5% in USD on average while prices were in a declining trend on the chromium chemicals except chromic acid.

As previously disclosed, the new glass fiber plants went through a ramp-up period in the first half of 2019, and we ended the year at an annual capacity utilization rate of 65% on average. However, due to a sizeable contraction in glass fiber product demand in the local market, the sales volumes stayed below the planned levels. and we recorded TL 199 million incremental revenues from this segment in 2019.

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In the reporting period, 73% of the revenues were generated from international operations, while the share to group companies increased by 400 basis points to 15%, resulting from higher price levels and volume sales in soda ash. Our cost of goods sold-to-sales ratio also increased by 400 basis points to 66%. Natural gas tariff hikes, we had since the second half of 2018, had also had an inflationary impact on the cost of goods sold. OpEx-to-sales ratio was flat at 16%.

Adjusted EBITDA margin recorded at 27% was 630+ basis points lower than the profitability we had in 2018. The FX gain on trade receivables and payables, which is included in our EBITDA definition, had TRY 40 million positive impact in the reporting period compared to TL 91 million seen last year in the same period. Excluding these gains, EBITDA margin decrease was limited to 420 basis points.

In the reporting period, we had €45 million of CapEx with €35 million of which in relation with the glass fiber business, and the rest mostly being maintenance, equipment, renewable, and operational efficiency investment. In fact, our soda ash production capacity investments in Turkey, and based on our initial plans, the total capacity expansion of 100,000 tons will be operational in 2021.

Coming to the end of presentation, I would like to draw your attention to a few key takeaways and the announcements we made yesterday. We have entered into a heavy CapEx period, although smaller in percentage when compared to the one we had between 2013 and 2018. However, we have the flexibility to slow down or postpone less imminent investments by taking into account the developments in the global and domestic economy. Our focus on operational excellence continues to be a top priority, as well as maintaining above industry average profitability levels compared to our global peers. During first half, free cash flow may be reported in the negative territory, but our strongest position will continue.

Now, moving to slide 20. As you will have seen yesterday, we have announced our intention to simplify the shareholding structure of our businesses, and this involves merging our five listed companies, Şişecam,

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Trakya Cam, Anadolu Cam, Soda Sanayii, and Denizli Cam, as well as Pasabahçe into one single listed entity.

On the following page, you will see what the Şişecam structure looks like, and as we have grown over the years, we have ended up with a business made up of 69 subsidiaries in 18 countries, and those are operating under four business units with five separately listed entity. As you all know, Şişecam has been committed to simplifying the legal and shareholding structure, as well as streamlining key functions and centralizing key decision-making processes, and we have already made significant progress in this. We have consolidated some of the subsidiaries, eliminated cross shareholdings, and acquired the shares of international partners that are appropriate in the last couple of years. However, while significant progress has been made, the business structure we are currently operating under is not optimized enough based on our understanding.

On page 22, the rationale behind this transaction is summarized briefly, and we believe this transaction represents the optimum way of simplifying the structure of the business to fulfill its potential. This will benefit all stakeholders by creating a single stock with increased depth and greater appeal to international investors. This will better position Şişecam to build a strong reputation as the national champion on the global stage. It will positively affect Şişecam's valuation and create long-term sustainable value growth for investors. It will optimize operating costs, unlocking synergies between business units, and centralizing revenue generation, leading to higher operating profit, and the magnitude of the synergy cost improvements are expected to result in a run rate of at least 200 to 300 basis points for EBITDA growth on a very conservative basis in the mid-term.

Now, I will be happy to take your questions.

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Q&A

Operator

We have one first question from Mr. Ali Dhaloomal from Bank of America Merrill Lynch. Sir, please go ahead.

Ali Dhaloomal

I have two questions. I mean, the first one, I was wondering... I mean, your 2019 performance was partly supported by various price hikes taken in late 2018, as well as 2019, and I was wondering what we should expect for 2020? Also, what have you budgeted in terms of natural gas price hikes for this year? My second question is on CapEx. I was wondering what's your guidance for 2020, and where will it be spent in terms of segments?

Görkem Elverici

Thank you for the question. The first thing is, that as we have already announced during the webcast we had for the year-end results of 2019, we were expecting this year to come up with increased input price hikes, and this has happened within this year. So, we based our pricing on the strategy that we will always stay at the north of the input price hike, and we have been able to manage and pass through all the price increases, of which impact even above the budgeted figures for most of the market players. So, our strategy will continue in 2020, and we will continue to set north of the input price increases, and in the markets where it is appropriate, we will do the necessary pricing corrections. Pricing in the business areas like flat glass, where we have seen a decrease especially in the Eastern Europe markets due to the increased capacities, that we believe will be settled with the demand increases, coupled with some of the furnaces that will be undertaking cold repairs this year.

For natural gas price hikes, we have budgeted roughly around 12 to 13% on average for the overall year. For CapEx, we assume that there will be roughly around \$500 million worth of CapEx in the next year, and most of this will be a combination of the cold repairs that we continue to undertake, coupled with maintenance programs and operational excellence program. There has been some limited increase in CapEx that we had planned, like

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we've already mentioned, the one in Pokrov the investments that we are undertaking in the chemicals business, but most of the spending will be made on cold repairs that we' experienced in the upcoming years

Ali Dhaloomal

OK. That's very clear, and if I can, with just a quick follow-up question. Can you comment on the flat glass demand in 2020, and what do you see both in the construction and auto sector in terms of outlook, and also how are competitive dynamics in flat glass at the moment? Where is your capacity utilization at this point of time as well?

Görkem Elverici

So, for the flat glass market, as Turkish market which is the largest one for sure, considering the market reactions especially in the second half of the year and continuous interest rate cuts with government incentives for the construction industry, we believe a the market demand should be higher than what we have experienced in 2019 at least. For the worst conditions, the demand increase that we have experienced in the second half of the year should continue. When you look at the market expectations, the market is still a little optimistic about the growth in the GDP. It might be reflected in the flat glass market. But we believe that together with the extended export arms we have, and the market improvement conditions in the local market, the Turkish operations will not be experiencing issues in making the necessary sales for the required capacity utilization. We have been able to keep the capacity utilizations beyond 80% within 2019, and we believe that we will be in the second half of '18 for the capacity utilization rate within 2020.

So, for the other markets, as I have tried to summarize during the presentation, Russian market is down, which is expected to come back in 2020. Russian market volume decrease has experienced some issues especially in the Balkans and Eastern European markets as some of the Russian producers started to export their goods to those markets, and this has not only impacted the pricing conditions in Russia, but also affected the Eastern European prices. Next year, as there will be a supply and demand

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balance expected for the Eastern European markets, we expect that the pricing conditions for both Russia and Eastern European markets will start to mildly improve.

Operator

We have another question from Mr. Rahul Bhat from JP Morgan. Please go ahead.

Rahul Bhat

I have just two questions. Firstly, probably on the free cash flow generation, one of the line items is the change in working capital, which is TL 700 million. Could you explain what drove that, and what should we expect for 2020? Secondly, on this merger with all the other op-cos, is that going to be like an all-share deal or is there going to be a cash outflow involved, and would it change any of your financing plans at all?

Görkem Elverici

Starting with the last question, it will be a pure share-to-share swap, so the op-cos will be swapping their shares with Şişecam's shares. So, there will not be cash involved apart from the exit price payments that will be made for the investors that are unwilling to take part in the process.

For the working capital increases, in 2019, we have experienced double impacts. The first one was coming from the increased logistic prices, per unit prices, which has been as a result of our extended exports sales, . Ffor 2020, due to the capacity balancing that we made within 2019 as there had been some increased inventory costs, which we believe to be decreasing with the increased sales in 2020, and we have been able to keep the logistic cost prices at par levels for 2020 for the larger amounts. So, we can say that there will not be a real impact coming from the logistic cost increases in 2020, but some small adjustments we may see due to the increased export volumes, especially starting with glass packaging and flat glass business line.

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Operator

We have no other questions, sir. Back to you for the conclusion.

Conclusion

Görkem Elverici

OK. As we have also highlighted during the call for the transaction in the morning, we will keep all our investors informed about all the progress that we are experiencing for the transaction, and we hope to meet you again, apart from the transaction calls, to discuss the half year-end results of 2020. Thanks for everyone for their participation.

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