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FDR.MC - Half Year 2019 Fluidra SA Earnings Call

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CORPORATE PARTICIPANTS

Bruce Walker Brooks *Fluidra, S.A. - CEO & Executive Director*

Cristina del Castillo García *Fluidra, S.A. - Director of Investor and Shareholders Relations*

Eloy Planes Corts *Fluidra, S.A. - Executive Chairman*

Xavier Tintore *Fluidra, S.A. - Corporate General Manager*

PRESENTATION

Cristina del Castillo García - *Fluidra, S.A. - Director of Investor and Shareholders Relations*

[Interpreted] Good morning, and welcome to Fluidra's results presentation for the first half year of 2019. My name is Cristina del Castillo, and I am the Director of Investor Relations and Shareholders at Fluidra. Today's presentation will be made by Mr. Eloy Planes, Executive President; Bruce Brooks, CEO; and Mr. Xavier Tintore, CFO. (Operator Instructions)

All of the documents are available on our web, www.fluidra.com, and it has also been sent this morning to the stock exchange authorities and the multi-conference will available on our website this afternoon. So Mr. Eloy Planes has the floor.

Eloy Planes Corts - *Fluidra, S.A. - Executive Chairman*

[Interpreted] Well, thank you, Cristina. Good morning, and welcome to Fluidra's results presentation for the first half year 2019. I'd like to make a general evaluation before starting the presentation of results after 1 effective year of merger of both companies. Our main goal has been to ensure a quick and efficient integration, focused on acting as a single company in the lowest time possible and focused on implementing the identified cost synergies before the start of the campaign in order to generate the minimum impact in our customers. From that point of view, the company acted with great agility, and the management structure was quickly defined, and we devoted specific teams to the integration and to synergies. This has allowed us to implement more than 85% of our integration plan as of today. And as you shall see in the presentation, we've been able to make significant progress in our synergies implementation plan.

From the point of view of the different markets in which we operate, we have been able to keep, in spite of the very high level of activity devoted to the merger, our commercial focus. We have not doubted during this period to overinvest if we considered it to be necessary in order to make sure the right service and care for the customer were at the highest level, even during the highest risk of the execution. We can say that part of the execution [rates] both in terms of the structure impact and the market impact is behind now. And the fact that we're making significant progress in synergies places -- allows us to look forward to an excellent position in order to reach the goals in our strategic plan.

Now if we want to analyze the results of the first half of the year and to say that after a bad first quarter due to timing factors and weather and negative factors in the American market, the second quarter is -- on a stand-alone basis, shows a solid growth close to 6% under constant perimeter and currency. After the partial of the original (inaudible), temporary factors in North America has eased a good recovery, a growth of 12% in sales on a stand-alone basis for the quarter, in spite of the fact that the weather has been unusually bad until the end of June.

Europe, which accounts for more than 50% of our portfolio of sales, shows solid cumulative growth on a constant perimeter and currency of more than 6%. Now these good performance of Europe and rest of the market offsets the drop in June that we see still in America.

As I told you beforehand, from an operational point of view, we are looking at 2019 as a year for integration and for implementation of cost synergies. You'll be able to see that in terms of the executed synergies, we already show an annual run rate close to EUR 21 million, going over the EUR 19 million synergies that we had planned for 2019 and placing us in an ideal position to reach the EUR 35 million we had foreseen in our strategic plan.



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Now if we analyze the business fundamentals, we see that they are solid. As you have seen, Europe shows sustained growth, and the trend in July assures a very good campaign. And if we analyze the sales in our American distributors, we see that in spite of the bad weather impact, the growth rates they show are at about 3%.

Given that the market fundamentals are consistent and that most of the integration is already part of the past and that the implementation of synergies is growing at a higher pace than foreseen, we expect a very solid second half of the year in terms of sales and results. Thus, we're well positioned to reach the guidance for 2019, and we're still focused on assuring the execution of the strategic plan.

So without any further ado, I'm going to give the floor now to Bruce, Fluidra's CEO, who, together with Xavier, our CFO, will present and -- a more detailed analysis of the first half year.

Bruce Walker Brooks - Fluidra, S.A. - CEO & Executive Director

As always, it's a pleasure to be here today to discuss our results for the first half of 2019. I'll start with comments on our overall performance and trends in the business and then turn it over to Xavier, our CFO, to provide more details on the financial results. The numbers you see on Slide 5 are the pro forma 2018 and 2019 figures for January through June for Fluidra and Zodiac combined. I remind you that the merger was officially completed on July 2, 2018.

For the first half of the year, sales grew 2.4%, 2.8% if adjusted for currency and perimeter compared to the first half of 2018. This marks a solid Q2 despite continued erratic weather in the Northern Hemisphere and some continued timing issues. The strength of our global platform shines through as Europe continues to lead with a good season. Despite the negative leverage associated with the drop in sales caused by weather, change of distribution pattern and the move of our heater factory for the first half in North America, we grew our global EBITDA 4%. We're now beginning to show the operational leverage for our full year guidance.

Margin improved despite material tariff headwind and some merger-related startup in efficiencies. We continue to prudently invest in OpEx, allowing our synergy achievement to begin to read through while still positioning us for long-term sales growth. These mostly onetime challenges will begin to abate or now pose easier comparisons for the remainder of the year.

EBITDA and cash earnings per share grew 2.6% and 4.3%, respectively. The results corroborate our improving returns story, which, as I have mentioned in the past, is a key part of our strategic plan. We will continue to focus on improving product quality, value improvement or product cost reduction, integration synergies and new products to keep us on track with our longer-term goals.

The team has done a nice job managing net working capital, ending the period at EUR 385.5 million, which represents a 1.8% decrease from the same period last year. Net debt stands at EUR 740.2 million. This evolution is basically flat to prior year when adjusted for currency and is in line with our expectations for a full year of strong cash generation.

Moving to Page 6. The integration process is a fundamental part of our plan to solidify Fluidra's position as the global leader in the Pool & Wellness industry. We maintain our relentless focus on balancing integration, synergies and the continued growth of the combined business, concurrently unlocking substantial merger-related synergies and value improvements to drive higher returns and cash flow. The integration process is proceeding ahead of expectations with over 20 teams and 200 of our best people focused on executing a well-thought-out plan. We have identified more than 4,400 actions as part of the plan, and we've already completed 85% of them. By the end of 2019, the vast majority of actions will be complete.

We are excited to share that the gas heater plant in Tijuana is running well. When I woke up this morning, I had a great message from the project leader, confirming another record production month. The team has made great strides to get us back on track. The plant is already manufacturing 22% more than the old plant in San Diego. But I need to remind you that it will still take us most of the third quarter to continue to work through our remaining order backlog.

Pivoting to Europe. Zodiac's European distribution has also been successfully merged into Fluidra's distribution network, although we overspent in the short term to ensure customers were getting what they need for the peak of the season. Our network is now even more potent and efficient.



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We are also pleased to share with you that we have successfully completed the merger of legal, systems and operations in South Africa. This momentum, including the previous announcement of the mergers of Spain, Italy and Portugal, will continue with the Australian integration in August, followed thereafter by that of the U.S.

Our progress on delivering cost synergies in the first half of 2019 was excellent with an additional EUR 4 million of full year run rate synergies generated in Q2 that add to the EUR 16.7 million achieved up until the end of Q1 2019, for now a total of EUR 20.7 million. We're extremely pleased with our progress on the integration and have already surpassed our EUR 19 million guidance of run rate cost synergies by the end of 2019. This progress has naturally caused us more to achieve but has also allowed us to offset some of the typical startup inefficiencies like the distribution center moves that take place during a merge. We expect to keep the trend of acceleration this year, and we are now raising our guidance to EUR 25 million of run rate savings. Clearly, we are well positioned for the EUR 35 million targeted in our strategic plan. After the season, we'll relook at our forecast of cost synergies and expense to achieve those savings related to the overall merge.

Turning now to Page 7. The sales -- you can see the sales evolution by geography. For the first half, global sales grew 2.4% compared to the same period of 2018. The vast majority of geographical areas have positive sales trends despite a less-than-supportive weather environment. After a strong April, we saw a weak May and early June until the Northern Hemisphere finally dried out and warmed up. Southern Europe grew 2.6% with a solid evolution in France and Belgium. Adjusted for perimeter, the growth was an even more impressive 5.9%. The Rest of Europe displayed currency and perimeter adjusted growth of 6.6%, with outstanding performance in Northern Europe driven by double-digit growth in Germany. All together, approximately 57% of our sales came from the European area, again, highlighting our benefit of global diversification.

As mentioned earlier, North America showed a positive recovery from the disappointing start to the season. We experienced a 1.6% growth in the area and a negative 4.8% when adjusted for currency. I'll remind you during -- that during Q1, this currency adjusted number was negative 20.1%. Yet when we see the performance on a quarter-stand-alone basis, growth for the second quarter year-on-year was 16.2%, 12.5% FX and perimeter adjusted as the temporary effects mentioned in Q1 started to wind down, even on the back of persisting headwinds like adverse weather and tariffs. This North America's performance on the quarter goes to show the resiliency of our sector and our belief in the continued strength of our market's fundamentals. As Eloy mentioned, the North American market is growing at approximately 3%.

The Rest of the World showed currency and perimeter adjusted growth of almost 5% driven by solid performance in Latin America and a somewhat weaker evolution in Australia and South Africa. We remain confident to deliver full year sales growth within our guidance. The erratic season will likely have the U.S. at the lower end of the growth range, offset by our global footprint and a particularly strong season in Northern Europe. The recovery we saw in late June continued through this point in July with Europe showing double-digit growth in this critical month. Builder backlog in the U.S. remained strong, which we believe will help extend the season.

Next, on Page 8, we see the evolution by business unit. Residential Pool grew 1.7% driven by pumps, aboveground pool and pool covers. Adjusted for perimeter, the growth was an even more respectable 4%. Commercial Pool grew close to 4%, confirming the positive trend we saw in Q1 and setting us up well for the rest of the year. The Pool Water Treatment business picked up at a good pace after a weaker first quarter, delivering growth of 5.6%. Growth was based on both chemicals and water care equipment. Pool Fluid Handling showed excellent growth of more than 7%.

So in summary, I'm positive with our overall results in the first half of 2019, following a solid Q2 delivery. Our global footprint helped us deliver positive growth in the year-to-date after a challenging Q1 for North America. Despite some persisting headwinds, we delivered solid sales growth on a global basis for the quarter and drove margins through continued improvements in operational efficiency and capital management. Based on trends, we're confident of a strong performance for the rest of the year as well. Most importantly, we are also not only on track with the integration but have exceeded our synergy targets.

With that, I'll turn it over to Xavier to explain the financial results in more detail.

Xavier Tintore - Fluidra, S.A. - Corporate General Manager

[Interpreted] Thank you, Bruce. The results shown on Page 9 have us a goal to ease your understanding of the business evolution comparing equivalent figures. The accounts that have been presented, which are not comparable the merger that took place in July 2018, are to be found in



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the appendices of this presentation, together with the reconciliation between the published accounts and the pro forma presented on this page. You must also remember that this page excludes all nonrecurring expenses associated to the transaction or to the integration of both companies. Additionally, and given the implementation of the IFRS 16 rule, we have excluded its impact on the central column that refer to 2019 in order to be able to compare -- in order to be able to make comments about comparable figures with 2018. We have added an additional column on the right-hand side headed with IFRS 16 with the data adjusted for those concepts.

Having said that, let's now analyze the evolution of the main lines of the P&L account. The sales figure -- or the pro forma sales figure grew 2.4%, and if we exclude foreign exchange, it will be a growth of 0.8%. And if we adjust it for perimeter mainly due to the divestiture in Aquatron, the growth rate would have been of up. 8%.

As Bruce has just mentioned, after a bad first quarter due to the evolution in the U.S.A., the second quarter shows good recovery. The growth on a stand-alone-quarter basis is 5%, and if we adjust it for currency and perimeter, it's 5.8%. The gross margin reached 51.7%, and it is equivalent to the previous year. This quarter, the impact of sale price increases and the merger synergies have been more than offset by the increase in import tariffs to the U.S.A.. S. A. and a reclassification of purchase transport expenses from being OpEx to sales cost.

Operational expenses before provisions (sic) [depreciations] and amortizations reached EUR 246.7 million with a growth rate of 2.1%. This increase, which is net of the synergy savings, reflects: on the one hand, the investments in our key commercial initiatives like the growth in the American aftermarket business or the development of IoT-based products or the commercial teams for sales synergies; and on the other hand, certain inefficiencies or overinvestments in the integration, which Bruce has also mentioned and alluded to. As I've said beforehand, this item excludes nonrecurrent integration expenses, in other words, the expenses needed for the attention of cost synergies.

Bad debt provisions reached EUR 2.3 million, higher than the previous year due mainly to the evolution in Australia and the South of Europe.

EBITDA stands at EUR 142.6 million with an increase of 4%, which is a figure that's very similar when we adjust it for currency and perimeter. The limited operational leverage during this first half of the year is due to the lack of volume in the U.S.A. and the cost factors mentioned previously.

Just like in the case of sales, the second quarter on a stand-alone basis shows a good performance with a very interesting operational leverage growing -- the EBITDA growing adjusted for foreign exchange and perimeter of about 9%. Below the EBITDA, the account shows a significant increase in amortizations associated to the allocation of goodwill to the merger intangibles for purchase accounting.

The financial result reached EUR 23.5 million, which is 7.1% below the aggregation of the financial expense of both companies in 2018. The variation in the financial result is due to the lower cost of debt and the impact of exchange differences. The net result adjusted for nonrecurrent expenses shows a reduction due to the increase in the amortizations of intangibles in the merger. As we have been doing ever since we have had our merger with Zodiac, we have included in the appendices the published accounts of the company and a detailed reconciliation of -- to the pro forma used on this page. Given that the structure of the information is similar with less reconciliation items compared to the previous year, I shall not make any comments about this in -- at this time.

Page #10 shows us the evolution of the group's working capital. The working -- the net working capital reached EUR 385.5 million with a decrease of 1.8%, which is 1.7% if we adjust for currency and perimeter. Inventories grew by 8.3% as a result of the slow start of the campaign in the U.S.A. and they are offset by the increase in accounts payable, which grew by 14.1%.

On Page #11, we show the evolution of the net financial debt and the free cash flow. We have wanted to show the flow based on EBITDA given the existence of nonrecurrent items associated to the transaction, which would distort the comparison between 2018 and 2019. The second quarter is already a cash-generation quarter, given that we have a collection of the early buy sales in the American market. The results in the first half year are very positive with a cash generation of EUR 56.4 million, about EUR 24.2 million or 71 -- 75.1% above the previous year due mainly to the evolution of the working capital. That stands at EUR 740.2 million, which is flat if we compare it with the previous year if we adjust for currency and well aligned with our expectations at the year-end.

And without any further ado, I'll turn it over to our Executive Chairman, Eloy Planes, to conclude the presentation.



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Eloy Planes Corts - Fluidra, S.A. - Executive Chairman

[Interpreted] Thank you, Bruce. Thank you, Xavier. After a bad first quarter due to the impact of the American market, the second quarter on a stand-alone basis shows solid growth, both in terms of sales of about 6% or in terms of results, close to 9%. Europe has maintained good growth rates, and America has started its recovery as the temporary impacts are being reconducted associated to the Mexican plant and the model change in certain distribution channels.

From an operational point of view, we see 2019 as a year for integration and the implementation of cost synergies. And you have seen that the level of cost synergies executed so far show an excellent annual run rate close to EUR 21 million, going over the EUR 19 million synergies, which we had planned for 2019. Given this, we are pleased to increase our run rate savings goal for the year-end up to EUR 25 million. And as Bruce told us, we will have a review of the global goal in terms of synergies for the strategic plan based on the campaign. The information we managed and that we have shared with you, both in the American market and in the European market, point out to the fact that the business fundamentals are still very solid, indeed. In July, Europe accelerates the clear positive trend; and in the U.S.A., in spite of unfavorable weather, the distribution, the sale -- the distribution sales are growing at about 3%.

Given that the market fundamentals are consistent and that most of the integration is already part of the past and that the implementation of synergies is growing at a pace higher than what had been foreseen, we expect a very solid second half of the year both in terms of sales and results. Thus, we are well positioned to reach our forecasts for 2019: sales of between EUR 1.3 billion and EUR 1.4 billion; EBITDA, between EUR 240 million and EUR 260 million; and the net debt-to-EBITDA ratio at below 2.6x.

Listen, both our goals and our plan are clear. We must continue combining our effort in the implementation of integration and synergies in order to keep on improving our margins, whilst we keep our focus on the markets and on our customers to keep on growing at a very high pace. Our estimates for 2019 and the implementation level of integration, position us well to reach as well the goals of our Strategic Plan 2022.

And with this, we end our presentation for today. The only thing I have to tell you is that we thank you for your participation in this multi-conference and to tell you that we will be delighted to answer any questions you may have. Thank you.

Cristina del Castillo García - Fluidra, S.A. - Director of Investor and Shareholders Relations

[Interpreted] Well, thank you, Eloy, Bruce and Xavier for your presentations. And now we will start the Q&A with all of the questions we have received so far. Given that there are many questions and a lot of them are similar, we will try to actually formulate them all at the same time.

QUESTIONS AND ANSWERS**Cristina del Castillo García** - Fluidra, S.A. - Director of Investor and Shareholders Relations

[Interpreted] The first question is related to the guidance for 2019. Given the results for the first half year and the sales figures for the first half year, which would be the growth rate for the second half year in order to reach the guidance at the end of the year? And do we -- are we sure that this sales generation is actually feasible? And we would like you to shed some light on the figures for the month of July. Evolution of the sales figure during the second quarter in order to reach the guidance for 2019 for the whole year and some indications about the sales figures for July.

Bruce Walker Brooks - Fluidra, S.A. - CEO & Executive Director

So Cristina, I think you meant the second half, not the second quarter.



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Cristina del Castillo García - Fluidra, S.A. - Director of Investor and Shareholders Relations

Second half, yes.

Bruce Walker Brooks - Fluidra, S.A. - CEO & Executive Director

Okay. Sorry. That's what was wrong in the translation. Listen, I think we saw some really good trends in Q2 despite the fact that the weather was not particularly great. We saw a really good April. And then May and the first half of June were pretty soft, and then finally, the weather turned on around the -- really, around the Northern Hemisphere. And we've seen really strong sell-through in the month of July. And as I mentioned in the text, the sell -- the sell-out in Europe was north of 10%. So I think a really encouraging trend. And if you think about the Europe, 25% of the back half sales come in the month of July. So yes, they are a stronger number versus the first half but on a relative scale. July is really important, and that gives us a lot of confidence going forward.

As I look to North America, what I would say is, in the first quarter, we talked about EUR 20 million of headwinds that came from the heater facility, the change in distribution patterns and a little bit of the weather situation. We believe we've recovered about 40% of that headwinds that we took on in Q1 and Q2, so that helped the acceleration. But we still see that we have that opportunity, especially when you think about things like the change of distribution pattern and the fact that the heater plant is now running very well to see numbers continue to grow in the back half in the States. Now with that said, I do want to remind everybody, we had a material price increase in Q3 last year. And so therefore, we saw a very strong Q3 in the States. But overall, what I'll say is as long as we -- as the market remains strong, which is what we see, then we're confident that we can deliver the sales in the back half.

Cristina del Castillo García - Fluidra, S.A. - Director of Investor and Shareholders Relations

[Interpreted] The consensus for 2019 in terms of EBITDA is at about EUR 239 million. It looks like some brokers are using data IFRS 16, and others use data post IFRS 16. Could you clarify exactly what the real consensus, please?

Unidentified Company Representative

[Interpreted] Yes. We have seen that that's the case. I mean some financial analysts are using the IFRS 16 pre and post consensus. I mean our guidance is clear, sales between EUR 1.3 billion and EUR 1.4 billion, EBITDA between EUR 240 million and EUR 260 million without the IFRS 16, and that implies about EUR 22 million, EUR 23 million. That should be allocated to that figure, would be divide EUR 262 million to EUR 282 million post IFRS. And the net debt, the guide we had given without IFRS would be below 2.6x. And due to the impact of IFRS we would be -- we would stand at 2.6x. As I'm telling you, it is true that some analysts have used one or the other, but we will work with the consensus and the analysts to clarify and make sure that we have that consensus, that's clean and clarified to ease your work.

Cristina del Castillo García - Fluidra, S.A. - Director of Investor and Shareholders Relations

[Interpreted] What is our strategy in terms of distribution in North America? Are we totally confident and satisfied and comfortable with third parties over there?

Bruce Walker Brooks - Fluidra, S.A. - CEO & Executive Director

So as far as the strategy regarding distribution in the States, one of the things that we've highlighted I think since the beginning of the merge, right, Eloy, is our ability to play football in America, soccer in Europe and rugby in Australia and really position ourselves in a way that we feel like is appropriate for the market. About 70% of the sales in the States go through the distribution channel. We have many, many strong distribution partners. And at this point, we see it is better for us to play as a manufacturer and really don't see the need or the space to enter into the distribution business in the States.



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Cristina del Castillo García - Fluidra, S.A. - Director of Investor and Shareholders Relations

[Interpreted] Could we explain the reason why the sales evolution during the second quarter of 2019 in the South of Europe and in the Rest of Europe and in the Rest of the World? Is this evolution seen in these regions during the second quarter a good point of reference for the whole year?

Bruce Walker Brooks - Fluidra, S.A. - CEO & Executive Director

I think the sales year-to-date is probably a better reference than the -- just the one-off quarter. I mean we saw strong first quarter. We saw a really strong April, as I mentioned before, softer May and let's say, first half of June. But then the back half of June turned on strong, and July has been terrific. So I think to isolate just down to 1 quarter as the trend is a mistake. Clearly, the northern part of Europe is running harder, faster than the southern part of Europe, but both on a year-to-date basis and especially once you start to push July into those numbers, we feel good about the overall run rate of Europe.

Cristina del Castillo García - Fluidra, S.A. - Director of Investor and Shareholders Relations

[Interpreted] Synergies. We have gone over the run rate goals for 2019. Does that mean that we are speeding up the implementation of the plan? Or that we see greater capacity to increase all of the synergies that have been estimated at EUR 35 million for 2022?

Bruce Walker Brooks - Fluidra, S.A. - CEO & Executive Director

I was clairvoyant when we started the whole synergy process. What I would say is I'm really proud of the teams. I think they've done a terrific job on the synergies. Naturally, some of the synergies that we thought would be a little bit bigger or smaller and some of the ones we thought were going to be smaller are bigger, and we have been able to speed up the pace on some of the synergies. So today, I mean, we announced the lift of the guidance, the annual guidance to EUR 25 million. We're in the heat of the season. I think to slow the teams down to look for a longer-term objective just didn't make any sense. I mean this is the time where we have to make hay, as the expression goes. So we'll take a look at the overall synergy target. Clearly, we feel confident on the EUR 35 million. We'll take a look at the cost run rate as well, and then we'll come back to you, guys, after the season with further direction.

Cristina del Castillo García - Fluidra, S.A. - Director of Investor and Shareholders Relations

[Interpreted] So from that point of view, restructuring costs are also evolving with regards to the initial expectation. Could you give us some updating on the total costs expected to reach the synergies?

Unidentified Company Representative

[Interpreted] Well as Bruce has just said, what we're doing right now is an acceleration in the process of capturing these synergies and an acceleration also in nonrecurrent expenses. As Bruce has just said, at the end of the campaign, we will reanalyze the situation, and we will update both the potential guidance for synergies and for the costs necessary to achieve those synergies, which has been the response both from customers and from competitors in the U.S.A. market given the merger of Fluidra and Zodiac.

Bruce Walker Brooks - Fluidra, S.A. - CEO & Executive Director

The response from the customers has been really positive. What the customers in the States are looking for is when the new Fluidra will be able to expand the catalog of products. And as we said, to get to revenue synergies, which we think there will be, it was going to take us a little bit of time to start to convert the product. So what I would tell you, in 2019, is they don't see a dramatic change, but the overall customer base is very enthusiastic about what the potential of the merger brings as far as a broader product catalog for the future.



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Cristina del Castillo García - Fluidra, S.A. - Director of Investor and Shareholders Relations

[Interpreted] So we expect then to reach new market share and both during the second half of 2019 and in 2020, right, we will increase our market share?

Bruce Walker Brooks - Fluidra, S.A. - CEO & Executive Director

Well, it's a bit premature to say what the market share will be at the end of the year. If I think about where the States is year-to-date, we're running behind where the market growth is. I certainly wouldn't expect to lose market share in the States. As Eloy commented and I commented, we believe that the market is growing at about 3% right now. We hope certainly that it's going to continue to accelerate from that. Now that the weather has turned on, we'll continue to catch up from things like that JXI and the -- or the heater plant move and the change in distribution pattern. I don't see the U.S. being a super strong year based on all the things that we've experienced to this point. But I would expect us to be at minimum on the growth rate of the market, hopefully, a little bit ahead. And then again, I'll go back to the benefit that we have of our global footprint and say that Europe looks very, very strong as evidenced, again, in July. So we feel confident on the overall sales number.

Cristina del Castillo García - Fluidra, S.A. - Director of Investor and Shareholders Relations

[Interpreted] What are the effects of the deconsolidation of assets in different geographies?

Unidentified Company Representative

[Interpreted] Okay. Basically, perimeter changes related to assets are related to the divestitures in Aquatron, and basically, they are to be found in Europe. There was a small impact in the U.S.A. and in the Australian market, but most of it is related to the American market -- the European market, sorry.

Cristina del Castillo García - Fluidra, S.A. - Director of Investor and Shareholders Relations

[Interpreted] Could you tell me how the net working capital evolved in the second half of the year and whether the profile with pre-sale -- with the early buys in the -- the early buy season in the States changes this profile in the future?

Unidentified Company Representative

[Interpreted] Yes. The company's profile, once it has merged, changes a little bit compared to the old Fluidra, obviously, because of the impact of the early buy season in the American market. Historically, the lowest point of the working capital in the old Fluidra was the fourth quarter. And right now, the lowest point, the biggest trough of the working capital is at the end of the third quarter because of the fourth quarter -- during the fourth quarter, we start building up inventories, and we start actually with the early buys. So the year-end will be aligned with the previous year at about 24% or 25% of the working capital over sales, which is the company's historical trend. We expect that the fourth quarter, as Bruce has told us, will be a significant sales quarter because of the evolution of the early buy season compared to the previous year, and it's going to be about these figures, what we will have.

Cristina del Castillo García - Fluidra, S.A. - Director of Investor and Shareholders Relations

[Interpreted] The breakdown between price and volume during the second quarter on a stand-alone basis.



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Unidentified Company Representative

[Interpreted] Let's see. Let's say that the price impact per region is different. Europe and the Rest of the World, the price impact during the first half year is about 1%, whereas the impact -- the price impact increase of prices in the American market is significantly above that figure. It is of about -- it is between 3% and 4%.

Cristina del Castillo García - Fluidra, S.A. - Director of Investor and Shareholders Relations

[Interpreted] Could you quantify what has been the impact during the second quarter of the nonrecurrent events occurred during the first quarter that had an impact in the U.S.A.?

Unidentified Company Representative

[Interpreted] Well, in general, the impact that we have noticed in efficiencies are associated to the startup or the merger of the company. There has been some overinvestments that we have referred to for the whole company. They are of about EUR 4 million.

Cristina del Castillo García - Fluidra, S.A. - Director of Investor and Shareholders Relations

[Interpreted] Some of our competitors in the States are talking about an excess inventories in all distribution channels. Could you give us some more color about this?

Bruce Walker Brooks - Fluidra, S.A. - CEO & Executive Director

Yes. Late start to the season, the inventories could be impacted in the channels, but I'll continue to go back to our situation and what we see being a bit different, perhaps it's because of the situation with our heater plant move or the change in the distribution pattern that we had talked about before with Amazon not participating in the prime market and letting that go through third party. So we haven't seen that. I can't really comment to other players' situation, but we believe that inventories are pretty normal at this point of the season.

Cristina del Castillo García - Fluidra, S.A. - Director of Investor and Shareholders Relations

[Interpreted] Some competitors also mentioned that during the second half of 2018, distributors bought additional inventories anticipating the price increase planned for 2019. Shouldn't this, together with a stable dollar, make that the second half had more complicated comparables?

Bruce Walker Brooks - Fluidra, S.A. - CEO & Executive Director

And that's one of the things that I was trying to convey earlier. The comparables will be strange in Q3 and Q4, particularly in North America. For -- again, I can only speak to Zodiac. My belief is that Q3 was very, very strong last year because of the price increase. Zodiac took the price increase on August 1, so it was normal -- earlier than we normally would have taken it, and so Q3 was very strong. And then what I would tell you is that the early buy was just okay, 2 weeks. So we would expect this season or the back half of this year that the States may be a bit behind coming out of Q3, although we do have the benefit of shipping JXIs or the gas heaters to really help offset the tough comparison of the price increase. And then again, we would expect the fourth quarter to be a more normal early buy situation. So in total, we see a very positive second half of the year.

Cristina del Castillo García - Fluidra, S.A. - Director of Investor and Shareholders Relations

[Interpreted] In order to be in the midrange guidance, you need to increase sales at about approximately 7% in the second half, and EBITDA, you need to increase it at about 23%. Which regions do you expect to provide these growth rates and why?

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Unidentified Company Representative

[Interpreted] Well, we have already mentioned the different factors that give us confidence to reach these sales growth during the second half of the year. Basically, the trend we see in the European market and the good development during the month of July, the recovery of volume in the U.S.A. with the supply of gas heaters to recover the backlog we have, all of these are factors that give us confidence for the second half of the year in the sales line. Now with regards to the expansion of results, we have to bear in mind that these inefficiencies we have referred to are already part of the past, and therefore, they should -- they have no impact during the second half of the year. The impact of tariffs -- of American tariffs were implemented during the last part of the previous year. So the comparables from a margins point of view is simpler when we had this first half. And in general, cost synergies will have a greater impact during this second half of the year. Volume, synergies, tariffs, these are affects that will take us to an expansion of these -- of the margins during the second half.

Cristina del Castillo García - Fluidra, S.A. - Director of Investor and Shareholders Relations

[Interpreted] The 22% of growth of gas heaters, is it due to the fact that now you have 22% more demand? Or is it due to the fact that you have to actually update, as you know, the orders that were pending?

Bruce Walker Brooks - Fluidra, S.A. - CEO & Executive Director

The 22% that I spoke to in the text was comparing our production rate in California on a weekly basis to what the production rate is now on a weekly basis in our Tijuana factory. One of the reasons that we made the move to Mexico was obviously costs. But actually, this has been a very successful product for us in the States, and we were not able to have the capacity in California to fulfill our demand. So one of the primary goals of moving to Mexico was to increase the demand. What I will tell you is that 22% is not the end goal. We need to continue to improve our production in Mexico to achieve our longer-term capacity goals. But with that said, the demand for gas heaters at this time of year begins to dissipate. The production level in the second quarter was enough for us to keep the market kind of flowing, although it was difficult. And then now and in late June, we began to really work down on the backlog of orders that we already have in hand, but that again is still part of that EUR 20 million that I talked about. So we still have orders in hand that we need to fulfill in the third quarter.

Cristina del Castillo García - Fluidra, S.A. - Director of Investor and Shareholders Relations

[Interpreted] On Investors Day -- we're referring to Investors Day last year. We calculated that in North America, North America could grow at levels above 8%. Do we still believe this is feasible?

Bruce Walker Brooks - Fluidra, S.A. - CEO & Executive Director

It's feasible in a normal year, but 2019 is not a normal year. And just to reiterate, what we talked about in the Investors Day was North America growing at about a 7% compound annual growth rate. We also talked about the market. Market generally expanding at about 5 -- 4 to 5, and this could be up or down a little bit, depending on things, including weather. So as I look at the North American market this year, I think the North American market in itself was probably going to be at the lower end of the growth rate, and then we will be impacted by that as well. But as I look long term, the fundamental demand for pools is strong. In the markets where weather has been positive, the sales are very strong. And so our expectations is that the fundamentals of the long-term market have not changed at all.

Cristina del Castillo García - Fluidra, S.A. - Director of Investor and Shareholders Relations

[Interpreted] The evolution of our free cash flow is strong with EUR 56 million, but the net debt excluding IFRS 16 is flat. Why is that?



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Unidentified Company Representative

[Interpreted] Well, as we have mentioned, the net financial debt is flat once it is affected by -- adjusted for foreign exchange. And we believe that this positions us perfectly well, well aligned with the guidance goal that we mentioned, i.e., to close the year below 2.6x pre-IFRS 16.

Cristina del Castillo García - Fluidra, S.A. - Director of Investor and Shareholders Relations

[Interpreted] Since when do we have ratings from the agencies? Do you have any forecasts about the issue of new bonds?

Unidentified Company Representative

The agencies ratings for the combined company, i.e. -- I mean, these ratings have been issued by Moody's and Standard & Poor's for 1 year now. During the ratings -- I mean, the ratings were necessary for the financial restructuring of the company due to the merger. And for the time being, there are -- we are not going to issue new bonds or there is -- there are no forecasts about restructuring the debt. Basically, for the merger, we used long-term financing [Term B] and some lines for the working capital, which had some terms between 5 and 7 years, depending on the instrument, and we are very comfortable with that structure. Obviously, we are looking for opportunities that could come up to actually decrease the company's financial costs. But for the time being, we have no need to change that structure.

Cristina del Castillo García - Fluidra, S.A. - Director of Investor and Shareholders Relations

[Interpreted] What's the differential between the interest rate we pay for the loans and the interest rate of the bond?

Unidentified Company Representative

[Interpreted] As I'm telling you, we are looking actively at of the instrument structure, and we feel comfortable with the financial structure we have. We are still very much open to any market changes, and we will see if there are any possibilities during the next few months. We are generating a lot of cash.

Cristina del Castillo García - Fluidra, S.A. - Director of Investor and Shareholders Relations

[Interpreted] If the legislation allows for it and given the seasonability and the impact of weather on stand-alone quarters, are you thinking of showing results on a half year basis and not quarterly basis?

Unidentified Company Representative

[Interpreted] No. We believe that the practice to document the company's evolution every 3 months is a very good practice, and we feel very comfortable if we do it on a quarterly basis.

Cristina del Castillo García - Fluidra, S.A. - Director of Investor and Shareholders Relations

[Interpreted] Any conversations with the main shareholders for a new placement?

Unidentified Company Representative

[Interpreted] Listen, the first market concern we got is when we have told to investors, bankers and analysts the main concern was the shares liquidity, and the placement was done in 3 weeks. And it was basically addressed to solving that concern. I cannot speak on behalf of [Ron] and



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the rest of the families, but what I can tell you is Ron is very much aligned with the strategic plan. And it still keeps its 38%, which has, this year, great value in the company's strategic plan, hence, from that point of view, this placement was an effort to give -- to respond to that concern.

Cristina del Castillo García - Fluidra, S.A. - Director of Investor and Shareholders Relations

[Interpreted] Well, thank you, all. So far, today's presentation, we thank our speakers and to all of you for your participation. And as usual, you know that the Investor Relations department is available to talk about anything you want. Have a very good day. Thank you.

[Portions of this transcript that are marked Interpreted were spoken by an interpreter present on the live call.]

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