Conference Call FY2019 Financial Results

Lorenza Rivabene: Good afternoon and Welcome to our FY2019 call.
Today I am joined by our Group CEO Gianmario Tondato and our Corporate General Manager and Group CFO Camillo Rossotto.
Given the fast evolving situation as a result of the Coronavirus outbreak, we wanted to give you the latest possible information and so you did not receive our usual video, which, as you can imagine, would have been filmed ahead of time.
Before we get started, we want to emphasize that some of the information discussed in this call contain forward-looking statements that involve risk and uncertainty. Actual results may differ materially from those set forth in such statements. For a discussion of these risks and uncertainties, you should review the Disclaimer in the earnings presentation we issued today.
With this I will hand over to Gianmario.

Gianmario Tondato: Good afternoon, 2019 seems a very long time ago. We delivered solid results in 2019, as we balanced the achievement of our short-term targets with the midterm objectives we announced during our Capital Markets Day.
First of all, we met all of our targets, with revenue, underlying EBITDA and reported EPS all in line with the full year guidance we provided in June. And we registered improvements across all key metrics.
We also continued delivering on our three core strategic pillars: growth, profitability and capital allocation.
Starting with growth: in 2019 we generated €5 billion revenue as a result of strong like for like performance at airports, new openings and bolt-on acquisitions.

Secondly, profitability: in Europe, underlying EBITDA margin increased significantly, leading to the improvement in profitability at Group level. Our continued commitment to product innovation and renewed focus on cost efficiencies, especially in Italy, delivered a significant improvement in margin.
And finally, our capital allocation strategy: on one hand we generated significant cash flow with the disposal of our Canadian motorway business. On the other hand we acquired Pacific Gateway Concessions, an airport retail concession company, and we accelerated investments in our US motorway business, namely the New Jersey Turnpike, as we see strong interest in the sector.
In a nutshell, in 2019 we delivered a good set of results.

Camillo Rossotto: Let's look at our numbers in detail, which are all on a constant currency basis and pre-adoption of IFRS 16.
In North America we posted very strong like for like revenue growth, particularly at airports with 4.5% year on year growth. In addition, the top line benefitted from the contribution of bolt-on acquisitions and from a positive calendar effect, as we had one week more in the 2019 financial year.
Underlying EBITDA was up 4.6% and, as expected, underlying EBITDA margin was stable year-over-year, at 11.1%.
Underlying EBIT was 167 million Dollars reflecting an increase in D&A due to the higher investments made over the last years.
Reported EBIT was positively impacted by the capital gain of 134 million Dollars from the disposal of the Canadian motorway business.
In International, we continued to grow our revenue base, whilst focusing on the completion of the startup phase of our latest initiatives, in the context of slowing airport traffic especially in Amsterdam.
As a result, revenue was up 10.3%, and underlying EBITDA margin landed at 9.5%. Thanks to a very disciplined approach on our investments, underlying EBIT margin was stable at 4.2%.
Finally Europe. As expected revenue was stable year-on-year, with a positive like for like performance of 1.6% which together with new openings and acquisitions offset the announced portfolio rationalization.
Underlying EBITDA was up 17% year-over-year, and underlying EBIT was up by 48%. This significant result confirms our commitment to enhancing profitability in the Region.
Reported figures include an 8m Euro capital gain relating to the disposal of our operations in the Czech Republic in 2019, while 2018 was negatively impacted by a 23m Euro one-off cost relating to the Cross Generational deal in Italy.
The Group delivered a solid set of results, with revenue up by 3.5%, underlying EBITDA growing by 7.6% and underlying EBIT up by 6.1%.
As a result, in 2019 the Group posted a 117 million Euro underlying net profit and a 237 million Euro reported net profit.
In 2019, we increased our Free Cash Flow by more than 70%, to 57 million euro, a result in line with our mid-term target of significant structural enhancement in the free cash flow generation, despite the capex ramp up in the US motorways described by Gianmario.

Gianmario Tondato: We delivered a significant amount of renewals and new wins globally, in 2019.
We actively expanded our portfolio, securing close to 3 billion Euros of renewals and new contracts in 16 countries across the world.

We renewed key contracts at airports including in Salt Lake City, Nashville, Indianapolis, Calgary and Zurich. We entered new airports including Langkawi in Malaysia, Mumbai in India and Myrtle Beach in North America. We also won at existing airport locations including Orlando, Dallas, Philadelphia and Seattle.
On top of that, we recently secured a 7-year contract extension at Las Vegas airport, which alone is worth 1.5 billion Dollars.
At the end of 2019, after the disposal of the Canadian motorway business which was worth 3 billion Euros, our portfolio was 35 billion Euros.

Camillo Rossotto: Turning now to 2020 outlook and guidance.
The Coronavirus has developed since the second half of January, leading to a rapid deterioration worldwide in February, affecting air travel as well as broadening to specific countries where the impact has been more acute.
This outbreak is evolving rapidly and the developments are extremely hard to predict.
Let me share with you what we have seen so far.
First of all, as a Group, we have launched measures to safeguard the health and safety of our employees and to counteract the impact of this outbreak, including management of opening hours, store labor optimization and G&A control.
In International, which represents 13% of Group revenue, we saw a sharp decline in traffic since late January in China and Vietnam. During the first week of March, the outbreak resulted in a general weakness of the air traffic. At the end of the first week of March, we estimate a negative impact on revenue of about 5 to 10 million Euro for our International division, mainly in China and Vietnam.
In Italy, which represents 20% of Group revenue, we recorded a very good start of the year until the escalation of Coronavirus starting from the twenty-second of February. There is no doubt that the impact since the outbreak is significant, as we've been forced to close a few points of sale and we continue to be impacted by restrictions on our high-margin bar counter service as well as on the overall network. At the end of the first week of March, we estimate a revenue loss in Italy of about 10 to 15 million Euro.
Given the strong results posted by our Italian operations in 2019, we decided to invest in 2020 60 million Euro capex to revamp our motorway network and to support future growth. This initiative will position us to drive significant long-term value.
In North America, which represents 53% of Group revenue, we have seen a limited impact so far, mostly due to a reduction in international flights. But, in case of additional traffic restrictions, our management is already defining an action plan to deal with the situation and protect profitability.
At the end of the first week of March, we estimate a negative impact on revenue in North America of around 5 million Euro, concentrated mostly in the last two weeks.
In the Rest of Europe, which represents 14% of Group revenue, we have experienced a minor impact so far.
The consolidated negative impact on Group revenue caused by Coronavirus at the end of the first week of March 2020 is estimated to be of approximately 25 to 30 million Euro.
2020 is subject to significant uncertainties, which has lowered visibility on what to expect this year.
For this reason, we plan to release our guidance for FY2020 as soon as the scenario is more stable.
Given the fast evolving scenario the Board of Directors has taken a prudent approach and proposed not to distribute a dividend.

Gianmario Tondato: There is no doubt that the Coronavirus is very serious and as we have seen the outbreak and the measures taken are impacting daily lives more and more, but we think this situation will end sooner or later.
While we remain confident in the medium-term growth opportunities in our business, we continue to execute selectively our capital allocation strategy investing in our core channels, but we are now very focused on managing the current situation.
This is not the first time our Group has faced external factors impacting travel demand. We know that travel is fundamental to people, and we believe the travel industry will rebound again.
We will now take your questions.

Q&A

Lorenza Rivabene: First of all I will be reading the questions we received from Ali Naqvi, from HSBC. He is asking three questions. The first one: Could you let us know how operational gearing impacts results during this period of trading? What costs can be flexed down and to what extent? The second one: Do you expect any relief from any of your landlord partners given the decline in volumes; can you comment on this by region and format(air/rail)? The third one: Can you quantify the mitigation to costs you talked about in your outlook statement? Starting from the first one: Could you let us know how operational gearing impacts results during this period of trading? What costs can be flexed down and to what extent?

Camillo Rossotto: Yeah sure, look, for what we have seen so far, so for the €20-25 million impact, I think it is reasonable to assume a flow through of something like around 20-22% and that would be sort of the first xxx (12:21) in terms of EBITDA impact. I need to realize that 30% of our costs is cost to good sold, so that is terrible by nature, and it is just a question of a short-term adjustment to get that down. Then another 30% approximately is labor and there it is a question of a combination of variable and fixed costs and that is a xxx (12:43) where the team is managing is focusing the most by leveraging existing instruments in the various markets, to be able to reduce costs, allowing the reduction in revenues, and then you have the rank component, that varies by region, and obviously where we have xxx (13:08) and we are seeing coming significant reductions in volumes we have already started entertaining conversations with landlords.

Gianmario Tondato: If I can add, you know, the situation that is for us more advanced is Italy of course, a sizeable situation. So talking about the minimum guarantee, that is stopped the common practice, I would say, in Italy, there are some... Landlords with minimum guarantee but not all of them, we are entertaining conversations. I see, frankly speaking, a lot of understanding, I do not see, frankly speaking, rigid positions. It is worthy to say, I am quite confident, you know, we can all come out with a good result. Talking about labor, you know, there is in Italy one institution that is called Cassa Integrazione, probably the Italian people know it very well. You know, basically the Government pays the salaries, the base salary of the employees, of the people working for the company, for a period, if you keep the job of the people. That is a situation that has been built in Italy, created in Italy for crisis, and that I think is the situation, a temporary crisis, of course, the situation that we are facing now, and the Government has announced yesterday that they are going to provide an important amount of money to support this temporary situation. So I think, you know, xxx (14:41) we are going to have a good relief in our cost of labor. But more importantly, anything else, you know, yesterday there was this Decreto, this Law, you know, passed by the Government. Our locations are going to be open, our motorway locations are going to stay open, because it is a service, you know. And the traffic, I must say, it is probably the only channel in Italy with still some traffic, of course reduced, but with a certain vital traffic, also because of the trucks, because of industries keep still moving. So I think the combination of this three things, you know, and also the resiliency really of the motorway channels looks better than I thought, frankly speaking, at the beginning of the situation, for Italy. For the other countries, you know, it is too early to say, because everybody has his own approach in the US, as we said, you know, it is too early, numbers are still very little and there is not a major reduction yet, so we will see. But of course it is a much more flexible labor market, regarding the United States, and frankly speaking, listening to the landlord we already are entertaining, talking with them, they look flexible as well. As they have been in the past, during September 11th, 2001, of the financial crisis, before, you know, so...

Lorenza Rivabene: The second one is Do you expect any relief from any of your landlord partners... But you have already answered. And the third one was: can you quantify the mitigation to costs you talked about in your outlook statement? So we are ok. So we can go with the questions from Luca Bacoccoli, Banca IMI. The first one was partially answered now: Do you see the risk to hit the minimum annual guarantee in certain locations in Italy or Europe? The second one is: Have you already discussed with landlords to renegotiate the rents or the minimum annual guarantee in Italy? The third one: How can the entry ban in the US for European travellers affect the business in North America?

Gianmario Tondato: Just to give you, I remember, if I do not mistake, there is a number of passengers coming in from Europe is 6% of the total amount of passengers in the US. And just to give you an idea internal traffic is 80% and foreign traffic is 20%. So it is important but...

Lorenza Rivabene: And Nicolò Pessina from Mediobanca is asking Camillo to repeat again the answer on the EBITDA impact, because there was a bad...

Camillo Rossotto: Sorry, I hope it's clear now. What I said was that we are, you should assume for the first numbers that we just quoted, that is 20-25 reduction in revenues, attributable to coronavirus, that the flow through on EBITDA of those numbers, of those xxx (18:19) in revenues will be between 20-25%, we are in a 10% EBITDA margin business, obviously in the short term the impact of the negative flow through is a multiple of the EBITDA margin. On the other hand, when you look at the most impacted region, that is Italy, seasonality is a factor. The concentration of revenues in EBITDA in the strong part of the year, starting from May to September is pretty significant and therefore the heat in also the coming month of March needs to be re-portioned to the low seasonality months that we have in front of us in March and April.
Operator: We will now begin the Question & Answer session. To ask a question you may press * then 1 on your touchtone phone. If at any time your question has been addressed and you would like to withdraw your question, please press * then 2. The first question is from Simon Lechipre with MainFirst. Please go ahead.

Simon LeChipre: Yes, good afternoon, could you please give us more details on the rationale behind this decision and what kind of return you expect on this investment. Secondly, still on CAPEX, could you help us understand how much flexibility do you have regarding your CAPEX budget for 2020 and what do you expect at this stage for this year, excluding of course the investment in Italy. And lastly if you could give us an update on your strategy to sell some very long motorways contract, which you already started to do with Canada. And do you feel the current situation could lead to a delay on the execution of this plan? Thank you.

Camillo Rossotto: I will provide some answers, based on what I understood to be the questions, then correct me if they are not on target. So, on the third one, I think you question was what is the strategy vis-à-vis the long-term, let's say, value extraction from the motorways business in the US. I think, just like Gianmario said, there is an embedded resiliency in the motorways business situations like this. The demand for those kind of assets is still strong, we do not sink even though we have very little now visibility on what might happen in the coming months. The plan is impacted so much so that the last year we also, just let me go back to another point, which has to do with flexibility on CAPEX: we decided managerially, they wanted to fast forward on the refurbishment of the New Jersey Turnpike and we did that with a view to having a more solid base of revenues generation in 2020 in that sector, so when we talk about capital locations, those are the kind of choices that we make on a monthly basis. As far as a guidance for 2020, we are not providing it, so we do not provide EBITDA on cashflow and on any other number. What I can tell you is that a good chunck of the CAPEX of this year is still discretionary and the team is particularly in North America is far as the investments in the airports and the likes are really going through each program. The CAPEX in Italy is part of an example of how having the full capability of a xxx (22:27) in terms of our leverage ratio, when we met in June last year it was asked what would be the leverage ratio at the end of 2019, and we said 1.2 times and that was exactly what it is, because we had a plan for a prudent, you know, cash generation for the year. What this means is that we are entering the situation with lot of elasticity and lot of flexibility as far as our financial position is concerned and we think that the world is not coming to an end and starting with 2021 there is going to be some sort of rebound. And based on that scenario, we have decided to go forward with investing into the new format that up to the month of January this year were giving excellent results on the Italian motorways and that are partly behind the success of the performance of the Italian operations in 2019. So that's the rationale behind it, all of these investments need to meet ex-ante 15% more xxx (23:37) type of threshold, so that, I think it is the color that we can put around this CAPEX.

Simon LeChipre: Ok, thank you very much.

Operator: The next question is from Felix Schlueter with Goldman Sachs, please go ahead.

Felix Schlueter: Yes thank you very much for taking my questions. I had one on your credit facilities. I provided in these slides an overview, but I just wanted to know who provides you with the liquidity from a bank perspective on the ICF. And obviously if you also include the covenants, but what do you think could be the flexibility around covenants, should you really come in a scenario with a xxx (24:22) pressure on... And how often are they tested? Thank you very much.

Camillo Rossotto: From the last one. We do not plan to even get close to touching them. They are major by xxx (24:40) at the end of June, at the end of December, based on the last three months xxx (24:42) EBITDA, as normal, and 3.5 times, like I said, is the ceiling, the interest coverage is a nonsensical number one that we have, it does not even need to be tested. That to EBITDA applies to the facilities that are provided by the largely capitalized European banks, such as Unicredit, Intesa, BNP and Rabobank, so we are talking about very solid liquid providers. The maturity of our debt, which we are working on extending, as we speak, by the way, is in excess of three years, so we have a very comfortable liquidity profile and in terms of the stress test scenario that we run periodically, we are now into the mood of doing that even more frequently and, like I said, we have a very significant headroom, part in terms of availability and in terms of covenants.

Felix Schlueter: And in terms of ruling your debt or renewing, what is the xxx (26:01) back that you are getting from the credit markets.

Camillo Rossotto: We just extended from 2021 to 2024 essentially one of our facilities and that has been part of a normal activity of working on the next year maturities and there has been a very good reception and which has xxx (26:28) with a couple of new counterparts for additional long-term liquidity, I am not talking about short-term uncommitted staff that is obviously very easily available to us. So I think we are very much focused in the coming months, to manage by cash, because that is a kind of situation until when the visibility will be restored, but that is part of the prudency of the house and obviously we are monitoring the situation constantly.

Felix Schlueter: Sure. But I mean, given the kind of fixed undergoing back to your point that you are not looking mostly or that you do not think that covenants will come under pressure, do you think in a scenario where volumes will be down for the year 10-20% and given, you know, the operating leverage that you have, would not that necessarily, or would not that put you at the risk that some of the covenants could be, come under pressure?

Camillo Rossotto: That is kind of the worst case scenario that you are talking about, that would still leave us in excess of one turn of coverage under the major test, that we perform. So that is to give you a sense on an unmitigated basis, then when you pile on also the potential proceed from disposals and, or the mitigated actions on cash, we definitely feel even better about where we are with that current movement.

Felix Schlueter: Ok that is cleat, thank you very much.

Operator: The next question is from Alessandro Cecchini with Equita.

Alessandro Cecchini: Hello everybody and thank you for taking my questions. The first one is about the CAPEX on Italy. I would like to better understand if this 60 million CAPEX were on top of your previous guidance, that you provided during the capital market day. And when do you expect to xxx (28:41) that tangible impact of this renovation of some point in Italy. This is my first question. My second question is about labor cost inflation in North America. I would like, so, the situation is very fluid, but what are you expectations for this first six months, so just to better understand if you still see some inflation in the market for the North America. Thank you.

Lorenza Rivabene: So, Alessandro, ciao. So, first of all, as far as the CAPEX in Italy is concerned, yes, it is on top of the guidance we provided for during the Capital Markets Day, but again now the situation is evolving rapidly, so as Camillo and Gianmario were explaining before, the CAPEX we planned to do during 2020 will be in any case revised, this is the first answer. Then, as far as the payback is concerned, we think that this investment will pay for itself in about three years. You will start seeing some refurbishment, so that the impact of the refurbishment you will start to see them in 2021, but in any case the payback period is three years and of course we also need to have a normalized situation to see the results of this activity. As far as the first half 2020 is concerned, we state again the sector that we are not providing any guidance, because the situation is too volatile and we cannot, we do not want to give information that may be misleading.

Camillo Rossotto: Alessandro, it is sure that we are monitoring it and as soon as things stabilize and the possibility to re-establish some sort of visibility, which is now more crucial in the short-term that in the long-term, paradoxically, because we need to understand what is the shape of the curve that is going to affect us in 2020, we will come out and that is why we haven't put a deadline for our renewal of the guidance on 2020, but just talked about the need for stability, which means understanding at which point this thing flexes and is taking from there.

Alessandro Cecchini: Thank you but the labor cost...

Camillo Rossotto: What was the question on the labor cost, I missed it, sorry, say it again.

Alessandro Cecchini: The question was about the labor cost inflation that you expect in the market in North America, so last year it was, if I am not wrong, +5%, roughly speaking, I would like to better understand if it is still a very tight market and so you are thinking a xxx (31:57) labor cost in North America.

Gianmario Tondato: You can see, you know, due to the crisis, lot of things are changing. Personally... it is like difficult to say, personally I think the pressure on the cost of labor is going to go down in the medium term, because you know there is a slowdown in the economy, potentially, there is a slowdown... Look at the cost of the brand for instance, oil is going down, so a lot of things that in my opinion can help our sector in the medium term. It is too early to say, because we are also in the elections year, so it depends a lot on the decision that they will make to keep up with the pace of economy, but in the medium term it is a political xxx (32:48), you know. I have a got a feeling that xxx (32:50) the pressure on the cost of the, the crisis on the cost of labor is going to ease.

Alessandro Cecchini: Ok, many thanks.

Operator: As a reminder, if you have a question please press * then 1. There is no question at the moment. This concludes our Question & Answer session. I would like to turn the conference back over to Management for any closing remarks.

Gianmario Tondato: Thank you for attending the conference call and bye bye everybody, ciao.

Lorenza Rivabene: Thank you, bye.