Equity / Mid Cap. / Food

Ulker Biskuvi

28/09/2018

BUY

Company Report

Upside Potential 44%

Expanding regional presence with value accretive acquisitions

Following strong 1H18 operational results, particularly in international operations and completed acquisition of United Biscuit's Saudi Arabia operations (IBC and UI MENA) we are revising up our 12M target price for ÜLKER to TL24.5 with a BUY rating. We think that Ülker's operational strength and regional presence in Middle East and North Africa has been got further enhanced by the completed acquisition of United Biscuits' Saudi Arabia operations including Mcvities production and distribution rights and a production company (following the acquisition of Yıldız Holding's confectionary assets in Saudi Arabia, Egypt and Kazakhstan) which will support growth and bring certain synergies to existing Saudi Arabia operations and Ulker's presence in the region as a whole in terms of sales and distribution efficiencies, greater economies of scale, production flexibility and enriched brand portfolio. We believe that the company offers an attractive investment case with increased exposure to Middle East and North Africa, structurally attractive regions with relatively low per capita consumption of confectionary products and favorable demography.

No new acquisition in mid-term agenda, execution will be the key. After the major acquisitions and relatively high capital expenditure in both in Turkey and international operations, Ülker's management medium term focus would be to successfully re-structure international operations to capitalize synergies, expand the brand portfolio of Mcvities brand in the region and improve profitability of combined Saudi Arabia operations. We believe Ülker deserves credit for successfully restructuring its Turkey operations between 2012-2016, and that it can replicate it for int'l operations in the areas of 1) distribution restructuring, 2) effective category mix management, 3) production efficiencies and 4) better opex management.

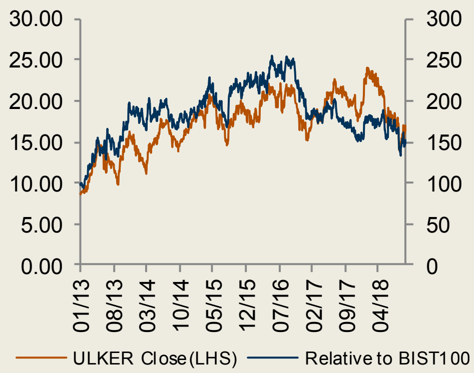
Formation of Pladis umbrella offers long term growth potential and synergies. We continue to see significant upside for Ülker given; the consolidation of Yildiz Holding's confectionary businesses under the Pladis umbrella; increasing volume growth through cross production opportunities with United Biscuits (UB) and Godiva; sharing distribution capabilities with UB; and collective raw material procurement to a limited extent. Ülker currently produces certain SKUs for United Biscuits and Godiva, and has launched some United Biscuit SKUs in Turkey. The company realized TRY156m additional revenues from synergy products in 2017 and expect exponential growth over the next three years with the initiation of production of new brands which already have proven track record and consumer admiration.

Operational cash flow generation set to improve after completion of an investment cycle and expected easing on working capital burden in 2H18. Ülker has completed some major investments over the past two years particularly in Turkey, investing in capacity expansion and modernization of production plans. Relatively high capex requirement and mentioned acquisitions weigh on free cash flow generation and deleveraging. In 2018 we expect capex requirement of company to be normalized at TL120mn and working capital burden to ease with the expected decline in receivables from related parties, Horizon in particular. Accordingly, we foresee that indebtedness level will peak in 2018 with net/debt to EBITDA at 1.7x and will gradually decline to 1.0x in 2020E thanks to declining cap-ex needs and expected solid operational performance.

Ticker		ULKER
Stock Data	**TL**	**US$**
Price at 27 09 2018	17.00	2.79
Target Price	24.52	3.74
Prev.TP	0.00	0.00
Mcap (mn)	5,814	955
Float Mcap (mn)	2,437	400
Avg.Daily Volume (3M, mn)	16.2	2.8
No. of Shares Outstanding (mn)		342
Free Float (%)		41.92
Multiples	**2018E**	**2019E**
P/E	12.8	10.8
P/BV	2.2	1.9
EV/EBITDA	8.5	7.2

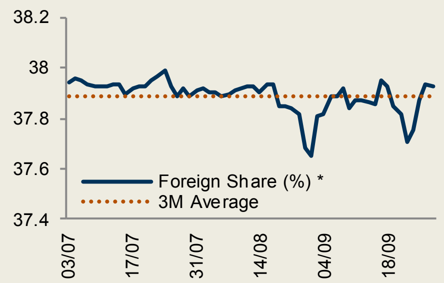
Price Perf. (%)	1 Mn	3 Mn	12 Mn
TL	22	-7	-12
US$	25	-29	-48
Relative to BIST-100	14	-10	-11

Price / Relative Price



52 Week Range (Close TL)	13.76	23.56

Foreign Share (%) *



*Foreign ownership excludes Unlu Shares

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Summary of Financials (TL million)

INCOME STATEMENT	2016A	2017A	2018E	2019E	2020E
Net Sales	4,194	4,811	5,850	6,868	7,761
Gross Profit/Loss	1,074	1,277	1,574	1,854	2,095
Marketing Selling & Distrib. Expenses (-)	-449	-531	-646	-758	-853
General Administrative Expenses (-)	-128	-136	-163	-191	-214
Research & Development Expenses (-)	-9	-14	-16	-19	-22
Operating Profits	488	596	748	886	1,006
Other Income (Expenses)	21	-1	-10	-10	-10
Profit (Loss) from Subsidiaries	0	0	0	0	0
Net Inc.(Exp.) from Inv. Activities	331	583	1,322	460	414
Net Fin. Income (Expenses)	-503	-671	-1,361	-508	-458
Profit Before Tax From Contining Operations	337	506	700	828	953
EBITDA	575	701	880	1,040	1,181
Taxation on Continuing Operations	-52	-75	-149	-176	-202
Net Profit After Tax	284	431	551	652	751
Parent Shares	273	383	455	540	624
Minority Interests	-12	-48	-95	-112	-127
BALANCE SHEET	2016A	2017A	2018E	2019E	2020E
Assets					
Currnet Assets	3,663	4,831	5,537	5,998	6,478
Cash and Cash Equivalents	2,288	3,190	3,254	3,319	3,385
Short-Term Trade Receivables	763	777	1,105	1,297	1,530
Short-Term Other Receivables	27	24	34	40	48
Inventories	406	584	738	865	978
Other Current Assets	177	255	405	475	537
LongTerm Assets	2,503	3,641	4,074	4,256	4,642
Long-Term Trade Receivables	0	0	0	0	0
Other Long-Term Receivables	0	0	0	0	0
Long-Term Financial Assets	929	981	1,079	1,187	1,306
Tangible Fixed Assets	1,119	2,099	2,375	2,392	2,608
Intangible Fixed Assets	168	183	201	221	243
Other Long-Term Assets	288	378	418	455	484
Total Assets	6,166	8,471	9,611	10,254	11,120
Liabilities	4,719	5,908	6,587	6,684	6,926
Short Term Liabilities	3,378	2,211	1,992	2,717	3,492
Short-Term Financial Loans	2,366	891	411	878	1,427
Short-Term Trade Payables	669	945	1,144	1,342	1,515
Other Short-Term Liabilities	342	375	437	497	550
Long Term Liabilities	1,342	3,696	4,595	3,967	3,434
Long-Term Financial Loans	586	3,420	4,300	3,655	3,107
Long-Term Trade Payables	0	0	0	0	0
Other Long-Term Payables	681	194	194	194	194
Other Long-Term Liabilities	74	83	101	118	134
Equity	1,446	2,564	3,024	3,569	4,194
Parent Shareholders Capital	1,247	2,295	2,660	3,093	3,591
Share Capital	342	342	342	342	342
Income Reserves and Others	120	124	124	124	124
Retained Earnings /(Acc. Losses)	385	547	854	1,203	1,616
Current Year Income /(Losses)	275	397	455	540	624
Minority Interests	199	269	364	476	603
Total Liabilites ans Shareholders. Eq.	6,166	8,471	9,611	10,254	11,120

Margins	2016A	2017A	2018E	2019E	2020E
Gross Margin	25.6%	26.5%	26.9%	27.0%	27.0%
EBIT Margin	11.6%	12.4%	12.8%	12.9%	13.0%
EBITDA Margin	13.7%	14.6%	15.0%	15.1%	15.2%
Net Income Margin	6.5%	8.0%	7.8%	7.9%	8.0%
Valuation Multiples	**2016A**	**2017A**	**2018E**	**2019E**	**2020E**
Reported P/E	24.9	17.3	12.8	10.8	9.2
EV/EBITDA	10.7	11.2	8.5	7.2	6.4
EV/Sales	1.5	1.6	1.3	1.1	1.0
Price/Sales	1.6	1.4	1.2	1.0	0.9
Price to Book	5.4	2.9	2.5	2.2	1.9
EPS	0.22	0.17	0.17	0.17	0.17
Dividend Yield	1.7%	1.1%	1.3%	1.6%	1.9%
Returns and Cost of Capital	**2016A**	**2017A**	**2018E**	**2019E**	**2020E**
ROE	-	22%	18%	19%	19%
ROA	-	5%	5%	5%	6%

I. Investment Positives

Expanding footprints in a structurally attractive region

The MENA region is one of the fastest growing confectionery markets in the world, currently valued at USD9 billion. Supported by high demand markets such as Saudi Arabia, UAE, Egypt and South Africa, confectionery sales trends are growing at a steady pace. Acquisition of UI MENA and IBC are the 5th international acquisition of Ülker since the 2016. Ülker acquired some of Yıldız Holding's confectionary operations in Saudi Arabia (FMC) Egypt (Hi-Food and Kazakhstan (Hamle). For now international expansion seems to be completed and management will turn its focus to integration and execution in order to successfully capitalize on the acquisition of production/distribution rights of Mcvities brand, to deliver cost synergies and increase presence of combined operations in Middle-East and Norh Africa. We think that Ülker deserves credit having restructuring its Turkey operations between 2011-2016, and that it can replicate similar performance at int'l operations in areas of 1) distribution restructuring, 2) effective category mix management, 3) production efficiencies and 4) SKU optimization.

After acquiring production / distribution rights of Mcvities in Middle East and North Africa, Ülker plans to expand product portfolio of the brand with new launches to capture greater market share in the region and to support medium term growth. Following the acquisition, Ülker become the market leader in Saudi Arabia biscuit market with 21% market share and have greater access to distribution channels and key accounts in Saudi Arabia with combined operations. Combined distribution will provide greater access to customers for all Ülker brands.

The recent acquisitions will turn Saudi Arabia into a production hub for Ülker with the combined production capabilities of IBC and FMC in having increased flexibility with two production plants while lowering logistics and general administrative expenses as of sales. Additionally, production rights of Mcvities will allow Ülker to produce some of Mcvities imported SKU's locally. Local production will also improve margins of Saudi Arabia operations as profitability of local production is higer compared to importing. Finally, Ülker's Egypt operations will launch Mcvites products and expand the brand's footprints in the country.

Margin expansion story continues

Ülker has managed to improve its EBITDA margin substantially from 4.3% in 2011 to 15.4% in 1H18 as a result of major restructuring efforts which includes optimization of SKU's with elimination of unprofitable brands, simplification and restructuring of distribution channels, production efficiencies trough modernization of production facilities and techniques and major op-ex cuts. We think that margin expansion story is not over as international operations of Ülker has room to post margin improvement with the addition of higher value added products to portfolio, cost savings in procurement and distribution, domestic production opportunity of Mctivities products both in Egypt and Saudi Arabia and possible production optimizations with IBC. As of 1H18, 34% of revenues and 41% of EBITDA of Ülker comes from international operations including exports from Turkey. We expect EBITDA contribution from intl markets to increase gradually over the next two years given the positive FX conversion impact on weak TL and further capitalization of synergies in production, distribution and marketing. We expect EBITDA contribution of international operations to reach %45 in in 2020E from current 41%.

Operational Cash flow generation set to improve after completion of an investment cycle

Ülker has completed some major investments over the past two years particularly in Turkey, investing in capacity expansion and modernization of production plants. Relatively high cap-ex requirement and mentioned acquisitions weighed on free cash flow generation and deleveraging. In 2018, we expect cap-ex requirement of the company to be normalized at TL120mn and working capital burden to ease with the expected decline in receivables from related parties, Horizon in particular. Accordingly, we foresee that indebtedness level will peak in 2018 with net debt/ EBITDA ratio reaching 1.7x and gradually decline to 1.0x in 2020E thanks to declining cap-ex requirement and expected solid operational performance. The management's aim is to keep capex to sales ratio at 2% forward. We assumed capex to sales ratio at 2.5% in the projection period.

Fully hedged short fx position at very favourable terms

Ülker carries TL1526mn net debt position (including derivative holdings) mostly dominated in hard currency as of 1H18. However, the company has fully hedged its short fx position through cross currency swaps at a TL cost at only c. 14% in April 2017, until April 2020. So, this very timely hedging on quite favourable terms creates a positive carry for Ulker. As of 1H18, The company carries only USD38mn short fx positions mainly due to completed acquisition of IBC in May 2018. The management's aim is to hedge the short fx position going forward.

Godiva stake sale might be another catalyst for the stock.

Ülker Biskuvi had acquired 25,2% of Godiva (its share dropped to 19.23% after 6% stake sale to Yıldız Holding), leading premium chocolate producer with significant brand equity globally, for USD240mn back in 2008. The company had used USD240mn bank loan to finance Godiva acquisition, but paid back in June, 2010 in order to take advantage of the early payback option. Ülker values its 19.23% stake at Godiva at TRY821m in 1H18 financials.

According to a news published on Reuters on 26 Septmeber, 2018 Yıldız Holding is looking for opportunities to sell Godiva's Japanese business. The report suggest that the company could fetch around $1.5 billion for the deal.

Possible sales of Godiva's Japanese Arm could benefit Ulker as such cash injection could ease the worries over Yıldız Holding's possible liquidity issues which also reflected on Ulker's stock price. Second of all, such high valuation for Godiva Japan is also positive for Ulker due to its 19.23% stake in the company.

Parent Company, Yıldız Holding shared some details on its syndicated loan facility

Yıldız Holding communicated that it has completed the restructuring of its loans in April 2018 and received the loan in June 2018. Restructured loan amount is TL4.3bn, whose maturity is eight years with a grace period of four years. Yildiz Holding refinanced USD5bn debt in total including a separate facility obtain from Akbank. The terms of syndication loan seems very favourable compared to current market rates at a 4 year fix TL rate of 17.7% and USD rate of 6.8%. 4 year grace period for the group loans, coupled with favourable interest rate terms is also positive for Ulker, in our view as it may relive worries over the stock due to Parent's highly leveraged balance sheet.

Increasing contribution from more value added brands and synergies

As part of growing focus on value added products and SKU profitability , Ülker continues to decrease the level of non-branded private label products and is switching fully to branded products. Its non-branded products share in domestic volume and revenue in 1HM18 decreased by 1ppt which support profitability as the branded product EBITDA margin is significantly higher than private label products. We estimated TRY200m revenue contribution from synergy products for 2018YE but expect exponential growth over the next four years with the initiation of production of new brands as well as the growth coming from existing brands which already have proven track record and consumer admiration.

II. Investment Negatives

Weak TL might put pressure on margins in domestic market

Higher than expected depreciation of TRY in 2019 might put pressure on margins in domestic market and halter volume growth as the company prefers to downsize packages at the time of high cost inflation in order to pass trough some portion of cost increases to consumer without hurting affordability. One of the most important risks of the sector is escalating raw material prices which might create margin pressures on the company. Raw materials, mainly, wheat, sugar, and palm oil, hold the lion's share in company's COGS with 65% share of which 31% are linked to hard currency. As a result, raw material cost inflation stands as the major impediment for profitability and margins. The confectionary market in Turkey had greatest difficulty to pass raw material cost hikes to its prices due to intense competition and high price elasticity. That said, fx portion of COGS represent 25% of sales where as 34% of total sales is fx dominated as of 1H18

Main export markets continue to be problematic

Export markets of Ülker (Iraq, Algeria and Yemen) continues to be challenging, facing serious economic problems and political instability.

Competition challenges strong market presence

Fierce competition in the confectionary market is significantly challenging the strong market presence of Ülker Biskuvi. Aggressive pricing strategy and increasing investments of other players may result in loss in market share of Ülker and pressure margins.

High Exposure to Saudi Arabia market

Current Saudi Arabia operations comprises roughly 20% of the consolidated EBITDA of Ülker, considering UI MENA's exposure to the company in addition to FMC and IBC. Exposure to Saudi Arabia is making Ülker vulnerable to sharp possible decline in oil prices and political challenges in the country. That said, USD peg currency of Saudi Arabia is currently a significant advantage for the company.

III. Valuation

DCF-driven fair equity value for the company is TL mn, which results in a 12-month target price of TL 24.3/per share indicating to a 43% upside potential.

- Our analysis has a 10-year projection period.

Figure Our 12-month target price of TL 24.5/per share indicating to a 44% upside potential
ULKER DCF (TL, mn)

TL mn	2018E	2019E	2020E	2021E	2022E	2023E	2024E	2025E	2026E
Revenues	5850	6868	7761	8692	9735	10806	11995	13314	14779
growth	22%	17%	13%	12%	12%	11%	11%	11%	11%
Gross Profit	1574	1854	2095	2347	2628	2918	3239	3595	3990
Gross Margin	26.9%	27.0%	27.0%	27.0%	27.0%	27.0%	27.0%	27.0%	27.0%
Operating Profit	748	886	1006	1134	1277	1425	1591	1775	1981
Operating Margin	12.8%	12.9%	13.0%	13.0%	13.1%	13.2%	13.3%	13.3%	13.4%
(-) Taxes	-157.2	-186.0	-211.3	-226.7	-255.3	-285.0	-318.1	-355.1	-396.2
Effective tax rate	22%	22%	22%	20%	20%	20%	20%	20%	20%
(+) Amortization	132	155	175	196	219	243	270	300	333
EBITDA	880	1040	1181	1329	1496	1668	1861	2075	2314
EBITDA Margin	15.0%	15.1%	15.2%	15.3%	15.4%	15.4%	15.5%	15.6%	15.7%
(+/-) Change in NWC	-284	-122	-172	-121	-135	-139	-155	-172	-191
(-) Capex	-120	-172	-190	-209	-229	-249	-270	-293	-318
Free Cash Flow	**319**	**560**	**608**	**773**	**876**	**996**	**1118**	**1255**	**1409**
Risk free rate	21.0%	18.0%	17.0%	16.0%	16.0%	15.0%	14.0%	13.0%	12.0%
Equity risk premium	6.0%	6.0%	6.0%	6.0%	6.0%	6.0%	6.0%	6.0%	6.0%
Beta	0.8	0.8	0.8	0.8	0.8	0.8	0.8	0.8	0.8
Cost of Equity	26%	23%	22%	21%	21%	20%	19%	18%	17%
Cost of Debt	24%	21%	20%	19%	19%	18%	17%	16%	15%
After tax cost of debt	19%	17%	16%	15%	15%	14%	14%	13%	12%
Weight of Debt	21%	21%	21%	21%	21%	21%	21%	21%	21%
Weight of Equity	79%	79%	79%	79%	79%	79%	79%	79%	79%
WACC	24%	22%	21%	20%	20%	19%	18%	17%	16%
Sum of PV of FCF	3343								
Terminal Growth	7%								
PV of Terminal Value	4271								
Net Debt 2Q18E	-1526								
Financial Invetments	934								
Minortiy Intrests	-358								
Implied Equity Value	**6665**								
Current Mcap	5814								
12m Target Equity Value	8384								
12m Target Share Price	**24.5**								
Upside Potential	**44%**								

Source: Is Investment Estimates

UI MENA operations

Ulker acquired UI Mena operations at a price of 134k EUR while its Enterprise value was at USD159m, corresponding to an EV/EBITDA multiple of 9.5x at the time of the acquisition.

- UI MENA is the owner of McVitie's distribution / production rights in MENA and Saudi Arabia along with a sales company in Egypt. Main operating markets of the company are Saudi Arabia, UAE, Lebanon, Qatar, Kuwait, Jordan, and Egypt.
- UI MENA has 1H18 revenue of USD19m and EBITDA of USD4m with an EBITDA margin at 26.6%.
- Main motives behind the acquisition for Ulker are to consolidate all MENA operations, to decrease cost to serve in the region through synergies and to increase McVitie's presence in MENA region.

International Biscuits Company (IBC) operations

- Ulker acquired IBC operations at a price of 40mn USD while its Enterprise value was at USD56m USD, corresponding to an EV/EBITDA multiple of 9.5x at the time of the acquisition
- IBC is a producer of confectionary products, mainly biscuits. The company owns a production facility in Riyadh. Main brands of the company are McVitie's & Rana (local brand)
- IBC has 1H18 revenues of USD19m and EBITDA of USD5m with EBITDA margin of 26.6%.
- Following the acquisition, Ulker had a 21% combined market share in Saudi Arabia biscuit market, Mcvites product portfolio contributing 7% to the given market share

Medium terms plans and synergies after acquisitions

Following the acquisition Ülker is planning to expand product portfolio of the McVities further in Saudi Arabia, which will help Ülker to expand its market share further in the region. Currently, almost all 7% of market share of Mcvities comes from digestive biscuits. Ülker is now leader in Saudi Arabia biscuit market with 21% share.

Ülker's Egypt operations (Hi Food) started to produce some Mcvites products and expanded the brand's footprints in the country. Ulker's market share in Egypt increased to 14.7% in 1H18 from 14.1% in 2017 thanks to successful launches of McVitie's products. We think that ability to produce to Mcvities products locally in Egypt will help Ülker to expand the brands market share further and to have a cost advantage.

Since Ülker has an already ongoing operation in Saudi Arabia (FMC), the company saw immediate synergies in procurement, production and distribution in Saudi Arabia. USD2.5 mn saving is expected in procurement, production and distribution synergies in addition to USD1mn savings in G&A.

With this acquisition Ülker is strengthening its position further in the Middle East and North Africa becomes one of the most important player in the region having a global, regional and local brands in its portfolio.

Both acquisitions are margin accretive for Ülker. 1H18 EBITDA margin of Ülker jumped to 15.4% compared to %14.1 in 1H17 (based on not restated figures). In addition to that international operation's EBITDA margin has further room to improve going forward trough synergies in procurement, production and distribution. Increased presence of Mc Vities branded products in the region is also expected to contribute both growth and margins positively going forward.

FIGURE 1: Post acquisitions market share of Ülker in the region

Biscuit market share (1H18)	KSA	Lebanon	Jordan	UAE	Qatar	Kuwait	Egypt
Ulker	#2	#1	#11	#6	#9	#15	#3
	14.2%	12.7%	3.7%	3.4%	3.3%	10.9%	13.8%
McVitie's	6.8%	5.6%	6.1%	8.8%	11.0%	10.9%	0.9%
After acquisition	21.0%	18.3%	9.8%	12.2%	14.3%	21.8%	14.7%
	#1	#1	#2	#4	#2	#2	#3
Main Competitor	13.9%	11.5%	10.0%	19.4%	18.5%	18.4%	18.1%

Source: The Company

Saudi Arabia confectionery market offers promising growth

Low per capita consumption especially in chocolate category with 1.6kg accompanied by increased consumer spending and organized retailing channels is expected to support the growth in Saudi Arabia. The Saudi Arabian confectionery market grew at a CAGR of 4.2% during 2011-2016. Saudi Arabia has a large young population base that have a strong affinity towards confectionery products in which they indulge frequently.

Biscuits segment where Ülker has a strong presence have shown a strong performance with a CAGR of 9.3% since 2012, reaching retail value sales of USD791 million in 2016. Of total biscuit sales, 72.6% came from the sweet biscuits subsector, which includes cookies, sandwich biscuits, wafers, etc.

Saudi Arabia’s biscuit sector is forecasted to continue to grow at a CAGR of 7.6% in retail value sales from 2016-21. Its total bakery market share is expected to decline slightly, from 13.4% in 2016 to 13.1% of the sector in 2021 (Source: Euro monitor International, 2017).

With consolidation and integration of the operations in FMC and IBC. Ülker is going to enjoy from the synergies for procurement production and distribution capabilities, and Ülker believes that cost to serve will decline in Saudi operations in the coming periods.

FMC 1H18 Review

FMC company’s total volume has increased by 14.5% in 1H18. Accordingly, net sales increases by 21% in local currency thanks to effective pricing strategy. EBITDA improved by 50bps on the back of leveraged opex and strong sales performance and favroable sales mix

FIGURE 2: FMC 1H18 Review

FMC Key Financials (SAR)	1H18	1H17	Change(YoY%)
Sales volume (tonnes k)	22.8	19.9	14.5
Net Sales (SAR mn)	314.1	258.5	21.5
EBITDA	45.4	35.5	27.8
EBITDA margin (%)	14.4	13.7	11.0ppt

Source: The Company

IBC 1H18 Review

IBC’s total volume has increased significantly by 40% YoY in 1H18, while revenue growth remained below of volumes due changing volume composition. EBITDA margin of IBC improved by 10.9ppt on strong sales performance and category mix.

FIGURE 3: IBC 1H18 Review

IBC Key Financials (SAR)	1H18	1H17	Change(YoY%)
Sales volume (tonnes, 000)	7312	5217	40.2
Net Sales (SAR mn)	88.4	66.7	32.6
EBITDA	25	11.5	116.7
EBITDA margin (%)	28.3	17.3	11.0ppt

Source: The Company

UI MENA 1H18 Review

UI MENA's total volume has declined by 1% YoY in 1H18 mainly due to shifting import business to the production by the Hi-Food. UI MENA's profitability on the other hand, continued to improve driven by the price positing of Mcvities.

FIGURE 4: IBC 1H18 Review

UI MENA (AED)	1H18	1H17	Change(YoY%)
Sales volume (tonnes k)	5.2	5.2	-0.9
Net Sales (SAR mn)	87.9	86.0	2.3
EBITDA	23.4	19.2	22.1
EBITDA margin (%)	26.6	22.3	4.3ppt

Source: The Company

Egyptian economy shows strong signs of recovery

In March 2016, Üker Bisküvi purchased of 51% ownership of Ul Egypt, which holds 90% ownership in the Hi Food Company operating in Egypt. The cost of the purchase was USD30mn and Ülker Bisküvi Sanayi A.Ş. will thereby own 45.9 percent of the total shares of Hi Food, thus retaining controlling stakes and decision-making power.

Hi-Food 1H18 Review

Hi-food's total volume has increased by 7.4% YoY in 1H18 thanks to local production Mcvities products and new launces. The 1H18 revenues grew ahead of volume in local currency with respect to YoY price hikes and increasing weight of Mcvities products in sales composition. Egypt Economy is in a recovery process currently following the sharp depreciation last year. So stabilizing currency, gradually normalizing inflation and increasing consumer confidence helps high food to recover its EBITDA margin from a very low base.

FIGURE 3: IBC 1H18 Review

Hi Food (EGP)	1H18	1H17	Change(YoY%)
Sales volume (tonnes k)	15.6	14.5	7.4
Net Sales (SAR mn)	570.3	414.8	37.5
EBITDA	89.3	16.7	434.5
EBITDA margin (%)	15.7	4.0	11.6ppt

Source: The Company

ULKER 2Q18 Earnings Review

Ulker posted TL242mn net income in 2Q18, up by 168% YoY, significantly better than our NI estimate of 186mn and Research Turkey's TL 183mn estimate mainly on higher-than-expected FX gains from derivative transactions and slightly better than expected operating profit. 2Q18 consolidated EBITDA grew by 22% YoY to 203mn, slightly above our TL 187mn expectation and RT consensus of TL 191mn. The company's 2Q18 EBITDA margin improved by 1.0ppt to 15.3% in 2Q18 (highest quarterly EBITDA margin). Solid EBITDA growth with margin improvement is attributable to strong performance of international operations. Consolidated revenues grew by 14% YoY in 2Q18 to TL 1.330bn in line with our TL 1.300bn estimate and RT consensus of TL 1.306bn. Please note that Ulker has re-stated 2Q18 financials due to completed acquisition of IBC. The numbers in 2Q18 financial highlights are re-stated figures.

Operating profitability in Turkey remained under pressure on changing revenue composition

Turkey operations 2Q18 revenue grew by 13% YoY to TL882mn on the back of solid 9.2% YoY volume growth in chocolate segment and material c6% to c18% price increase in 3 product categories. Average sales prices in domestic market increased by 12% YoY. Sales volumes in cake and biscuit segment contacted by 15% and 1%, respectively in 2Q18. significant contraction in cake volumes are mostly attributable to upward price adjustments. 2Q18. Gross margin of Turkey operations eroded slightly by 0.8ppt YoY to 21.2%,, reflecting changing revenue composition EBITDA margin contraction was limited with 0.4ppt YoY to 14.1% in 2Q18 on tight opex control. Accordingly, 2Q18 EBITDA of Turkey operations expanded by only 9% to 121mn TL.

Margin enhancement at international operations continues thanks to operational synergies in Saudi Arabia

International revenues in 2Q18 grew by 17% YoY to TL 447mn including other non-confectionary sales which declined by 81% YoY to TL5mn, in line with Ulker's strategy. Confectionary sales volume (excluding other sales) increased by 1.2% in 2Q18 while revenues in TL terms grew by 25% YoY to TL442mn thanks to positive FX conversion impact. 2Q18 gross profit of international operations improved very slightly YoY by 0.1ppt to 35.2% benefiting from elimination relatively less profitable non-confectionary items. EBITDA margin of the international operations, on the other hand, expanded by 3.8ppt YoY to 17.8% YoY thanks to realization of expected synergies in Saudi Arabia and Mcvities impact, leading to lower opex to sales ratio. Accordingly, EBITDA of international operations grew ahead of revenue by 49% YoY to TL 80m.

Cash generation deteriorates on increasing working capital need

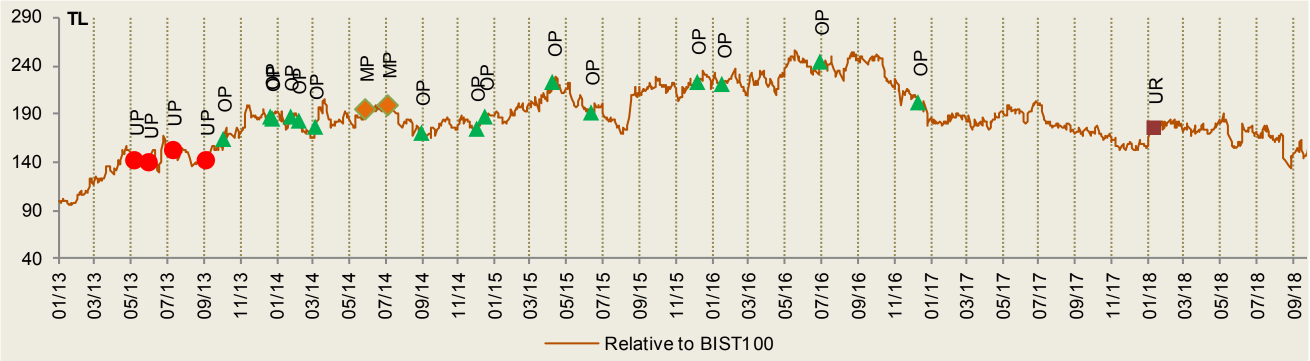
Ulker's net working capital requirement increased by 58% QoQ mainly due to shorter payables and increased receivables days. Company's receivables from related parties, Horizon in particular, continued increase in 2Q18, following the strong jump in 1Q18. Higher working capital need coupled with acquisition cost and consolidation of IBC's debt led Ulker's consolidated net debt to increase by 35% QoQ to 1.526bn in 2Q18.

IV. Peer Analysis

Company	Rec.	Ups.	Close TL	Target	BLP T.P	BLP Ups.	Mcap mn$	P/E			EV/EBITDA		
								2018	2019	2020	2018	2019	2020
ULKER	U.R		17.00		24.18	45%	945	12.8	10.8	9.3	8.5	7.2	6.4
Turkey Avg.								**12.8**	**10.8**	**9.3**	**8.5**	**7.2**	**6.4**
Disc./Prem.								***-45%***	***-53%***	***-52%***	***-49%***	***-51%***	***-50%***
Peer Comp.avg.								**23.4**	**23.1**	**19.3**	**16.9**	**14.7**	**12.7**
Peer.Comp.			Company	Country	BLP T.P	BLP Ups.	Mcap mn$	2018	2019	2020	2018	2019	2020
OLYMPI BD Equity			Olympic Industries Ltd	BANGLADESH	210.00	3%	487	22.8	19.6	16.7	14.5	12.7	11.0
DIAMOND IN Equity			Prataap Snacks Ltd	INDIA	1,631.67	60%	330			29.4	24.5	23.6	15.3
3799 HK Equity			Dali Foods Group Co L	CHINA	7.60	35%	9,853	17.6	15.4	13.5	11.1	9.7	8.5
URC PM Equity			Universal Robina Corp	PHILIPPINES	132.02	-9%	5,888	30.8	27.1	24.5	16.7	15.5	14.1
002557 CH Equity			Qiaqia Food Co Ltd	CHINA	21.50	25%	1,272	23.0	19.3	16.3	14.3	12.1	10.1
TKN TB Equity			Taokaenoi Food & Mar	THAILAND	19.06	10%	742	32.8	25.2	21.2	24.8	19.9	16.9
000716 CH Equity			Nanfang Black Sesam	CHINA			335	6.7					
002582 CH Equity			Haoxiangni Jujube Co I	CHINA	14.25	52%	704	26.9	18.9	13.5	18.8	15.0	
603777 CH Equity			Shanghai Laiyifen Co I	CHINA	14.70	30%	561	26.3	36.5		10.6	9.3	

Source: Is Investment Estimates, Bloomberg

Price / Recommendations



Source : BIST/ Is Investment Estimates