Investor Relations

Monterrey
Ulises Fernández de Lara
ulises.fernandezdelara@arcacontal.com
Tel: 52 (81) 8151-1525

Felipe R. Barquín Goris
felipe.barquin@arcacontal.com
Tel: 52 (81) 8151-1674

New York
Melanie Carpenter
i-advize Corporate Communications
Tel: (212) 406-3692
arcacontal@i-advize.com

Public Affairs and Communications

Guillermo Garza
guillermo.garza@arcacontal.com
Tel: 52 (81) 8151-1441

CONFERENCE CALL

Arca Continental 1Q20 Earnings Conference Call Transcript
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Operator: Good day, everyone, and welcome to the Arca Continental conference. All lines have been placed on mute to prevent any background noise. Please note that this call is being recorded. After the speakers' remarks, there will be a question and answer session, and instructions will be given at that time. For opening remarks and introductions, I would now like to turn the conference over to Melanie Carpenter of I-Advize Corporate Communications. Ma'am, please go ahead.

Melanie Carpenter: Thank you, Katie. Good morning, everyone, we hope you're all well under the current circumstances. Thanks for joining the senior management team of Arca Continental this morning to review the results of the first quarter of 2020. The earnings release went out this morning and it's available on the Company website at arcacontal.com in the Investor Relations section.

It's now my pleasure to introduce our speakers. Joining us from Monterrey is the CEO, Mr. Arturo Gutiérrez, the CFO, Mr. Emilio Marcos and the Chief Commercial and Digital Officer, Mr. José "Pepe" Borda, as well as the Investor Relations team. They're going to be making some forward-looking statements, and we just ask that per usual, you refer to the disclaimer and the conditions surrounding those statements. We imagine that several of you are working from home as are some of our operators, so we just ask for your patience and hopefully we can get through this call as well as can be. And with that, I'm going to turn the call over to the CEO, Mr. Arturo Gutiérrez, to begin the presentation. So please go ahead, Arturo.

Arturo Gutiérrez: Thank you, Melanie, and good morning, everyone. I appreciate you joining us today and I want to express the hopes of all of us at Arca Continental that you and your loved ones are well.

Our company's deepest sympathies go out to all who have been impacted by coronavirus outbreaks throughout the world.

Before reviewing our operating results for the first quarter, I´d like to take a few moments to address the COVID-19 global pandemic and its impact on our business. As many of you have experienced, this unprecedented event is having a significant impact on people's lives, communities and the global economy.

These are challenging times for everyone, which is why we are doing our best to support the needs of our associates, customers, consumers, and communities.

Of course, safety is our highest priority. We have implemented extensive precautionary and hygiene measures to support the wellbeing of our people at all our locations, including strict social distancing, sanitation protocols and travel restrictions. Also, where possible, people are working from home in accordance with guidance from governments and local health authorities.

We are grateful for the extraordinary efforts of all our teams to secure the continuity of our business and to maintain our product supply; we have reinforced all appropriate contingency plans in order to ensure that our production plants, distribution centers and our supply chain safely remain up and running.

As governments implement their strategies to control the spread of the virus, we may still experience some disruption, although the extent and duration is still unknown.

We also recognize that we have an important role to play in our communities. We are actively looking for ways to support those who continue to have their lives impacted by the virus, and those who are tirelessly and selflessly supporting those affected.

We are also stepping up our efforts to support governments and health services, either through financial assistance where appropriate, or product donations and other types of help.

We have committed over 1.5 million liters of bottled water, more than 160 thousand food products from our dairy and snacks division, 100 thousand face masks made from PET and a significant contribution of alcohol from our sugar mills.

It's so gratifying to hear from people throughout our operation, sharing stories about how the community supports our efforts, their pride in Arca Continental and how we are coming together stronger than before despite the distance between us.

We are also working closely with The Coca-Cola system to ensure that we are adopting the best ways to serve our customers and consumers.

It is still early to quantify the full impact that the COVID-19 pandemic will have on our 2020 results.

Nevertheless, and given this challenging situation, we have immediately deployed a thorough plan encompassing several cost-saving measures and reassessed Capex investments in order to prioritize liquidity, profitability and protect our business for the long term.

Now let’s turn to our performance for the first quarter 2020. Overall, results in the first two months of this year were in line with our expectations. And during March, day-to-day operation across our markets was heavily dependent on the severity of restrictions on mobility.

Total consolidated volume grew 0.2% in the quarter, reaching 512 million-unit cases, with total consolidated revenues growing 5.3%, to 38.9 billion pesos.

Consolidated EBITDA for the quarter grew 5.8% reaching $6.6 billion pesos, representing a margin of 17.1%, an expansion of 10 basis points.

Our ability to tailor our portfolio offering and price/pack architecture to the current consumer and macroeconomic environment, a relative favorable raw material price environment, coupled with our tight control of expenses and operating discipline enabled us to sustain margins.

Moving on to our regional operations, our beverage business in Mexico maintained the positive momentum, delivering another solid quarter of volume growth, up 1.9%, driven by personal and jug water segments, up 12.8% and 7.2%, respectively.

Total net sales in Mexico rose 6% in the quarter to reach $15.1 billion pesos, marking the nineteenth consecutive quarter of net revenue growth, despite the challenges in the latter part of the quarter.

Average price per case in Mexico in the quarter - not including jug water - rose 5.2%, reaching $64.20 pesos.

We continue strengthening of our ACT model, leveraging digital technology with "AC Digital", our new e-commerce mobile application. As you know, developing enhanced omnichannel capabilities is a key priority in our Digital Transformation. We are looking to expand the number of touch-points and allow customers to place orders of our full beverage portfolio directly from their smartphones. This is in addition to the pre-seller visits and our contact center.

We accelerated the deployment of this tool across all our operations in Mexico and South America, enrolling more than 3,200 customers per month, and providing them with remote training and coaching sessions through digital platforms.

On the profitability front, EBITDA increased 9.2% to $3.1 billion pesos in the first quarter, representing a margin of 20.5%, for an expansion of 50 basis points, driven mainly by raw material tailwinds and cost optimization initiatives.

In response to the COVID-19 crisis , we are redesigning and optimizing our Service Models in order to serve the market more efficiently, focusing on the execution of our Fundamentals and protecting our core priority portfolio, as we secure product stocking particularly at the Traditional and Modern trade channels.

Notably, our Direct-to-Home channel in Mexico is experiencing a tremendous surge and represents a huge opportunity. We have developed stronger capabilities and further expanded consumer purchase-points by deploying scalable, easy-to-use solutions, while leveraging our remote contact platforms and web-based sales.

Let me close our Mexico operation with a positive note. This quarter, we were honored with the 2020 National Quality Award granted by the Mexican Ministry of the Economy. Our plant "Las Fuentes", which is located in the state of Jalisco and is one of our largest production facilities in

Mexico, was awarded for its best practices and commitment to continuous improvement and excellence.

In South America, our total volume was down 5.5% in the first quarter, as a result of declining volume in Peru and Ecuador, which was partially offset by growth in Argentina.

We doubled down on execution and on our price-pack-channel strategy, as we continue driving affordability by expanding the mix of returnable presentations. The mix of returnables in the region grew 2.2 percentage points.

Total revenues were down 1.8% in the quarter, reaching 9.3 billion pesos, while EBITDA declined 8.7% to 1.9 billion pesos, representing a margin of 20.5%, for a contraction of 150 basis points.

In Peru, volume was down 9.5% in the first quarter, cycling a solid 5.3% growth from last year.

Despite the sharp slowdown in the economy and weakening consumer demand, we were able to maintain value share across NARTD beverages. Our still beverage categories grew 16.2% and posted value share gains, driven by the sports drinks, teas and juice segments.

On March 16th, the Peruvian government declared a nationwide coronavirus lockdown with some of the region's most stringent containment measures. These restrictions cut movement of people as much as 90% in that country and one third of our customers in the traditional channel remain totally or partially closed.

It's important to mention that the national curfew mandate begins at 6pm, so the time window available for the sale and distribution of our products has been reduced considerably. As these restrictions are lifted throughout this quarter, we expect our commercial operations to gradually stabilize.

Nonetheless, a plan to tackle the healthcare and economic emergency was recently unveiled by the government and is expected to deliver resources of 26 billion dollars, equivalent to 12% of GDP. This is by far the largest stimulus package of its type announced by any other Latin American government.

Moving over to Ecuador, volume was down 3.1% in the first quarter. The slump in oil prices amid the outbreak of coronavirus is heavily weighing on the oil-dependent economy, especially exports.

Unfortunately, as you may have heard in the news, Ecuador has the one of the highest per capita number of COVID-19 cases in Latin America.

Our Ecuador beverage business is a great example of our ability to quickly adapt to the new consumer dynamics resulting from the shift in consumption patterns. We are expanding our Direct to Home capabilities, increasing our customer base by replicating key learnings from our operation in Mexico.

Tonicorp, our value-added dairy business is facing the same challenges as our beverage business. Joint initiatives are being implemented in our market and distribution capabilities to cope with the sanitary and financial crisis in Ecuador.

We are confident that despite the contraction of the dairy industry, consumers will accelerate the shift towards product categories that generate wellness, health and nutrition. Tonicorp has strong quality credentials that reinforce consumer confidence in our products and that should enable us to regain growth in the short term.

In Argentina, volume in the first quarter grew 2.7%, cycling a significant decline from the same quarter in 2019.

We continued capitalizing on the two major package innovations made last year to further increase product affordability while reducing our overall production cost: The 2-Liter "Universal Bottle" refillable format for sparkling beverages and the 2-Liter returnable presentation of Aquarius flavored water. As you remember, our operation in Argentina was the first one to deploy returnable packaging in still beverages in the Americas.

Coronavirus officially arrived in Argentina relatively late, with the first confirmed case identified on March 3rd. The government acted very quickly in comparison with other countries, closing its borders and moving on to a national shutdown of all nonessential activity. These measures are being enforced by military and police. The response to the virus outbreak has been strict and swift. The number of cases in our territories is well below the average of Argentina.

We've been through challenging times in Argentina before. I firmly believe we've never been better positioned than we are today and will come out even stronger.

Moving over to our beverage operation in the United States, Coca-Cola Southwest Beverages closed out the first three months of 2020 with a strong operating performance and its twelfth consecutive quarter of revenue growth.

We delivered solid financial results, with 6.2% growth in revenues and 3.9% in volume. EBITDA for the quarter grew 16.6% to $78.9 million dollars, representing a margin of 11.9%, a solid expansion of 110 basis points.

During the quarter, our Northpoint facility in Houston, Texas became fully operational. All five lines began producing product, and we continue to work to achieve their rated efficiencies.

We posted solid volume performance in the quarter across both Sparkling and Still categories coupled with a record 121 new SKUs introduced. Sparkling volume grew a solid 2.6%, driven by the launch of Coke Energy.

Still beverages grew 2.7% for the quarter, as we introduced important brands such as Powerade Ultra, Powerade Water and AHA. This is our new mainstream flavored sparkling water and is the first major new brand launch in a decade.

Volume performance was supported by a solid and disciplined execution of our ACT model. Additionally, in February, the new FSOP service models were implemented in our Oklahoma territory and by this we finished the deployment to our entire operation in the US.

Net price for the quarter grew 2.2% with a true rate increase of 2.5% and a negative impact of mix of 0.3%, due to increase in sales of Dasani water during the final weeks of March.

We also grew sparkling beverage value share, breaking the record high for the second quarter in a row.

Let me now talk about the impact of COVID-19 on our US beverage business. As consumer behavior changes, our volume is shifting channels and our product mix is shifting as well.

During the last weeks of March, our US operation saw the benefit of pantry loading from consumers. However, we expect an impact of the post-pantry loading effect during the second quarter, coupled with a significant impact in consumer traffic due to increased social distancing and shelter in place restrictions throughout our franchised territories.

In the Convenience channel, consumers are making less trips into the stores and we're seeing slower growth in Immediate Consumption packages. Many of our customers, especially universities and colleges, the travel and hospitality industry, and our Food Service/On Premise customers are either closed or have moved to a pick-up/delivery mode of operations. As a result, volume performance in the FSOP and Vending channels was down significantly in the last two weeks of March.

In the Large Store channel, shorter hours of operation have been imposed and the number of consumers who can be in the store at one time is now limited.

We are bracing for fundamental shifts in our business in the coming months. The progress we've made from a strategic standpoint in our US operation in terms of revenue growth management, refined execution and a strong business culture, give me confidence that we are uniquely positioned to capture the growth opportunity after the pandemic subsides.

I will now finish our operation review with our Food and Snacks businesses. Net sales in the quarter rose 4.5% and EBITDA grew 6.4%, mainly driven by Bokados in Mexico and Wise in the US.

Our salty snacks portfolio was impacted in March when the coronavirus outbreak closed TJ Maxx stores and many customers in the Food Service channel. Our small bag segment was impacted the most. Conversely, grocery and club stores sales have stabilized for now and should remain steady with small increases at key times.

We are experiencing a significant increase in e-commerce activity and we are fully prepared for that. There are many consumers who have never ordered online, especially their groceries, and are now doing so.

Our Inalecsa operation in Ecuador has also been severely impacted by the COVID-19 pandemic. From early on, Guayaquil and its surroundings have become the most affected city in the country.

Let me now turn the call over to Emilio to go over our financial results. Please Emilio.

Emilio Marcos: Thank you, Arturo. And thanks everyone for being on the call today to review our financial performance.

In the first quarter, we delivered positive numbers with a strong beginning and mixed results towards the end.

In the first part, we continued with last year's positive momentum, both in pricing and volume performance; and in the last few days of the quarter, we found ourselves amid the Covie-19 outbreak, with a negative impact on volumes and a sharp change in product and channel mix.

Consolidated Revenues grew 5.3%, mainly due to a favorable price/mix trend of 5.1% in Mexico and 2.2% in the U.S. with an overall flat volume performance. This Top-line growth combined with lower PET and aluminum prices, helped us expand the contribution margin by 80 basis points.

We still expect to have tailwinds in some raw material prices throughout the year. We already have lower PET prices in all operations versus previous year, as well as lower aluminum prices from the combination of a lower spot price and our hedges. Thanks to the strict execution of our hedging strategy, we have covered 80% of our US dollar denominated needs in Mexico at an exchange rate similar to 2019.
Non-recurring expenses increased 55.4% this quarter, driven by $79 million pesos for expenses related to COVID-19 measures in all the operations and $174 million pesos related to the new Houston facility.

EBITDA for the quarter grew 5.8%, reaching $6.6 billion pesos. This represents a 10 basis point expansion in EBITDA margin versus the same period in 2019, despite the strong water mix effect in March. This result is explained by the expansion from the contribution margin, which is mainly due to strong pricing, and the raw material benefits previously mentioned.

This was partially offset by an increase in our operating expenses, resulting from the combination of Mexico and U.S. expense increases, impacted by higher depreciation along with exchange rate variations.

Our Net Income increased to $2.7 billion pesos from $1.7 billion pesos in 2019, representing 57.4% growth year over year at a 6.9% margin. This was driven by an improvement in our Comprehensive Cost of Financing from an exchange rate gain of $1.4 billion pesos, generated by our high dollar cash position.

On April 2nd, a dividend of $2.42 pesos per share, totaling $4.3 billion pesos was approved at our Annual Shareholders' Meeting with a payout ratio of 46%, in line with our historic average. The dividend was paid out on April 16th.

At Arca Continental our financial performance has position us well to face the current economic environment; our cash position reached $29 billion pesos, with more than 60% in dollars. We have a strong balance sheet with a leverage ratio of 1.0 time and as you are aware, our credit rating was recently reaffirmed by three agencies.

Additionally, 96% of our debt is aligned to the local operations currency, limiting our exposure to only $100 million dollars from AC Lindley bonds, which already has $49 million dollars in cash to reduce the net exposure.

As Arturo mentioned, we deployed a Crisis Response Team and implemented a series of initiatives within our finance area to focus on implementing a "cash culture". Our priority is to preserve cash and deploy it prudently.

As part of these initiatives we are monitoring discretionary spending in three main areas: operating expenses, marketing and labor. Some of the items that we will be reviewing are overtime, temporary associates, trade promotions, route optimizations, among others.

CAPEX will undergo the same level of analysis. As we continue to change our strategy to respond to our current market needs, we will reevaluate what type of investments are required to maintain the quality of our services and the safety of our associates.

In brief, we are going to take strong action in four pillars: operating expenses, marketing, labor and CAPEX.

In times like these, liquidity becomes essential to keep the business running as we will have top-line timing impacts, which we know are not going to be permanent or long-term.
Nevertheless, we have adequate liquidity to support our working capital and the required investment needs.

Our disciplined cash management, strong balance sheet, and proper hedging policies, combined with our capabilities to implement efficiency plans to adjust OPEX and CAPEX, enable us to be in a good position to overcome the challenging months ahead.

And with that, I'll turn it back to Arturo.

Arturo Gutiérrez: Thank you, Emilio.

We started 2020 with a clear objective of driving shareholder value through long-term, profitable growth. We hit the ground running with a fast start in implementing our plans and maintaining an efficient and optimal capital structure. What a difference a month makes.

Although uncertainty remains, we are confident that the post pandemic future of the business will be strong.

Our company is built for times like these. We have solid leadership and constant renewal is in our DNA. In the 93-plus years of our company history, our business has withstood many global crises.

Nevertheless, given the significant uncertainty in relation to the duration and economic impact of COVID-19 on our markets, we believe that is appropriate to withdraw our guidance for the current year.

We remain committed, as part of the Coca-Cola system, to support our customers and consumers during the coronavirus outbreak. Our leading market share, our strong financial position and our unique portfolio of brands and talented people will allow us to weather this unprecedented crisis.

We strongly believe that the negative impact of the COVID-19 pandemic in our business is temporary. We remain confident on the resilience of our industry. We are optimistic regarding the outlook for Arca Continental, as we start to see gradual improvement in the second half of the year.

Operator, we are ready to open the call for questions. Thanks.

Operator: We will now open the floor for questions. If you would like to ask a question, please press star key, followed by the one key, that is star one, on your touchtone phone. If at any time you would like to remove yourself from the queue, please press star two. Again, please press star one if you would like to ask a question. Our first question will come from Antonio Hernández with Barclays. Antonio, your line is open.

Antonio Hernández: Hi, good morning. Thanks for taking my question. First of all, congrats on your results, and hope that everyone stays safe. My question is around the 79 million pesos that were spent due to health emergency in the virus operations. Is this something that you might expect a little bit of that in the second quarter? That's my first question. And then I have a follow-up.

Arturo Gutiérrez: Antonio, I guess we're not hearing you very well. Can you repeat the question slower, please?

Antonio Hernández: Sure. Can you hear me now?

Arturo Gutiérrez: I think that's better.

Antonio Hernández: Good. Yeah, okay. You mentioned that during the quarter, you faced a 79 million pesos health emergency expense for the virus situation. Is this something that you might expect also for the second quarter and any idea how much might be spent from that line for the second quarter? And then I have a follow-up.

Arturo Gutiérrez: Extraordinary expenses - you mean extraordinary expense arising out of COVID-19, that were incurred in the first quarter, actually in the middle of March, really, and how much of that would continue for the second quarter. That's the question?

Antonio Hernández: Yes, that's correct.

Arturo Gutiérrez: Well, it's not that, I guess, the most significant impact that we will have going forward. Certainly, there are things that we continue to do, and mostly, it is about taking care of the community, I would say, from the beginning of the contingency in every country where we operate, we've been doing additional things to what we normally do in our operations. And that's why they were nonrecurring. And that’s, you know, the basic stuff supporting their health system and helping vulnerable groups in our community. That's, I guess, a significant part of that in the first quarter. We do not anticipate material expenses in terms of layoffs. We're not considering those actions at this point. So, I would not believe that will be as material, as obviously, the impact of the business that we anticipate from the crisis itself.

Antonio Hernández: Perfect. Thanks a lot. And then, my follow-up would be regarding the sales – you named some items of how sales have shifted in the US caused by COVID-19. How can that be relatable to South America and Mexico?

Arturo Gutiérrez: Yeah, in every country we've had obviously an impact during March. January and February were good months in general for all of our markets. And as you know, there are very clear and identifiable stages of the pandemic. And they start with an initial concern, then fear. And then you move into a lockdown and restrictions on mobility phase, which is what we're facing at this point in all of our markets now. It's been more severe in South America. That's where our markets in South America are more impacted, particularly Peru and Ecuador. In the US and Mexico, we are in a better situation now, but we are seeing that shift in volumes that we mentioned, the pantry load phase we experienced in March, lesser growth in modern trade. If you look at March figures in Mexico, supermarkets, convenience stores, they were up 7 percent, and in Southwest, the large store segment and small store, convenience retail, were also growing. And proximity channels have had a slowdown now, and that is also natural. It's expected that they will recover, given that they are channels that serve replacement purchasing during this phase. The ones that are more affected obviously are the food service, on-premise, the at-work channels, where those have declined significantly in all of the markets.

Antonio Hernández: Perfect. That's very helpful. Thanks a lot and stay well.

Arturo Gutiérrez: Thank you, Antonio.

Operator: Thank you. Our next question comes from Sean King with UBS.

Sean King: Hi, thanks for the question. I guess, similar to what the Coca-Cola Company provided earlier this week, can you provide sort of an aggregate number for what you're seeing in the month of April for volume trends across your markets?

Arturo Gutiérrez: Thank you, Sean. You know, what we're seeing, as I was explaining, is the continuation of what we are seeing as an impact in March. And we are at point at which we've identified mostly the factors that are influencing our performance. Mandatory lockdowns are the most relevant factor affecting demand. That is impacting not only our consumers, but also the mobility of our frontline sales force. Many times, they require public transportation to get to our distribution centers and our plants. So that is the current situation and the most severe impact is in Ecuador and Peru. Ecuador and Peru were down 22, 24 percent volume in March. And the trend is worsening in April in those countries. But again, we have identified that factor. And a second, very relevant factor, which then, the closing of points of sale, particularly in those markets. During the lockdown period, we've seen up to 35 percent of small retailers close in Peru, and up to 45 percent also that has closed in Ecuador. And Argentina is better than that. Mexico is much better than that and the US obviously. So, if you consider those factors, you see how the performance and volume moves accordingly. And that's why in Mexico, it's a much better situation in that regard, both in March and the April trend in the US. So, we see, again, a deteriorating trend in South America, Peru and Ecuador basically, but we see at the same time, reopening of stores. For example, in Peru, we had 35,000 stores in operation. The last few days, we've seen 38,000. So, I think that is a good sign. And again, in Mexico and the US, we haven't seen that impact. In Mexico, we have more than 90 percent of stores still open. Traditional trade is a key factor in Latin American markets. So that's why the trend is worsening in all of the markets, but it's still better in our main markets, which are Mexico and the US as compared to South America.

Sean King: Great. That's very helpful color. I'll pass it on. Thank you.

Arturo Gutiérrez: Thanks, Sean.

Operator: Thank you. Our next question comes from Fernando Olvera with Bank of America.

Fernando Olvera: Hi, hello. Can you hear me?

Operator: Yes, sir. Please go ahead.

Fernando Olvera: Great, perfect. Thanks so much for taking my questions. Basically, I have two. I mean, the first one is regarding taxes in Mexico. Given that the government has constraints, and do you see any risk that the government could increase the excise tax on beverages in the short term? And that's the first one. And then, regarding pricing, again, given this new environment and concerning the positive outlook and costs, can you comment what will be your pricing strategy going forward? Thank you.

Arturo Gutiérrez: Thank you, Fernando, and it's always good to talk to you. Let me address the first part of the question regarding taxes in Mexico, and then, I'll hand it over to Pepe so that he can talk about pricing. So yes, I can say there's always the risk in Mexico, these types of initiatives. We've actually seen just one this week about increasing in special taxes to certain products, including our categories. And as you know, we've seen these initiatives before. We know that they are not part of the current sort of government strategy, what the president has expressed. We didn't even hear - just now, just today, one of the leaders in Congress for the party that is in power saying that it's not part of what they want to do, but we continue to see those initiatives. I think that these proposals obviously don't make any sense and even less now. The problem is they impact mainly the poorest segment of the population. So if you think about how we're facing this challenge, which is an unprecedented crisis, and the economic aftermath of what we're seeing, it would be not only highly unpopular, but it would be a very hard hit to small retailers that are working their way out of the crisis. Again, this is a terrible tax, because it affects the poorest consumers and the mom and pop channel. So, it does not seem to be a very prudent measure at this point. But we continue our conversations with government to show them that in addition to what I said, these types of taxes have proven ineffective as a solution to the problems of public health that they're trying to solve. The resources obtained do not have a direct allocation to health programs. And as the company, on the other hand, we try to be a part of the solution. We fulfilled our commitment to be part of that solution by reducing our caloric footprint in recent years, offering a balanced portfolio. So, there is a weaker argument behind those proposals at this point. But I guess what is making them less prudent or less timely now is exactly the situation that vulnerable groups in our population are facing nowadays, and will be facing for the rest of the year. So with that, I'll turn it over to Pepe to talk about pricing strategy.

José Borda: Thank you, Arturo. And thank you, Fernando, for your question. Our strategy remains to increase true rates in line with inflation. But in the second quarter, strategically, we're going to have some impact mainly due to the mixes. As the on-premise channels and entertainment and specifically those channels in which immediate consumption is higher affected, that is going to negatively affect our price mix. And also, as water category grows over some other categories, that also has a negative impact in our pricing. And we expect that to affect us, to have an impact on second quarter, but that is going to gradually be corrected during the third and fourth quarters.

Fernando Olvera: Great. Thank you so much, Pepe and Arturo.

José Borda: Thank you.

Arturo Gutiérrez: Thank you.

Operator: Thank you. Our next question comes from Alvaro Garcia with BTG.

Alvaro Garcia: Hi guys. Thanks for the call, and hope you and your families are well. Good morning. I have two questions. First, I was wondering if you could remind us of your exposure to the on-premise channel in your two largest markets in Mexico and the US. And my second question is on Texas. I mean this is more of a longer-term question. Obviously, oil is a very important economic driver in Texas. And well, there is a potential - we don't know yet, obviously, but of some form of recessionary environment in Texas. So I was wondering if you could sort of provide your preliminary views on sort of the general defensiveness of soft drink consumption in Texas, given what might be softer economic activity there, and then, how to sort of think about affordability, and how you might shift your portfolio in the face of a recession? Thank you.

Arturo Gutiérrez: Thank you, Alvaro, for your questions and your message. Talking about the first part and the on-premise channel. The on-premise channel has - in the case of Mexico, it has a mix of maybe less than 10 percent. Maybe Pepe can give you more detail about that. In the US, what we call on-premise is a little larger. In terms of mix, it's about 15 percent overall, but that is the channel that has basically collapsed in the last few weeks, and that is natural. It's only a takeout service in most of those outlets. So, we're seeing declines there, not down to zero, but they are very, very significant. Obviously, that is going to be temporary, and a certain degree of normality to reestablish, those are going to be recovering. So, we are already working on the comeback plan for that channel, what we're going to do about it. But they are the biggest impact in terms of channel that we're facing. As you see, the mix is not as high as you will find in maybe other markets around the world, because the traditional channel also serves as an away-from-home consumption in our markets, especially in Latin America. And that is the channel that we're most focused in at this point, because it's the key variables for volume performance. So, our efforts in the region in Latin America are focused in maintaining small mom and pop retailers' strength. And that is not only about timely delivery of our products and service, but also communication of sanitary and prudent measures recommended by local governments to keep them in operation, because they work in part as an away-from-home consumption for people who are still - somebody who needs to be out on the street.

So, in the case of Texas, what I would say, and maybe, Pepe, if you would to add to the mix of channels, you can do it in a minute. Just addressing your question about Texas, we've seen the impact of the decline in oil prices in Texas before, especially in our West Texas region. To put this in context, West Texas for us in Southwest is about 10 percent of the total volume. And it's very clear that when prices of oil have come down before, it impacts that market. Significant oil price reductions have resulted, I would say, in the low single digit decline of volume for us. That's what we've observed throughout the years. That Texas region, by the way, is the most critical. We've seen up to in some cases 10 percent decline just in that particular area. But in general, it would be like maybe a low single digit impact what we've seen. I don't think that when oil prices go all the way down to zero, it continues to be a straight line. So, it's harder, actually, to model that. But what we have seen also declining volumes in West Texas even before the COVID crisis. So it's very important for us to take action in terms of affordability with certain packages and our on-premise plans to capture opportunities with the reopening of businesses. Some prospection of new outlets also, to capture some of the volume in our red trucks. Our go-to-market strategy will adjust the frequencies, because we need to adjust also our OPEX to that new reality in that region. So that's a summary of what we're doing.

José Borda: Thank you, Arturo. And I'm just adding some data to what Arturo said. In the US, some on-premise channels represent around 16 percent of our volume. So that's where we have our main impact. In Mexico, it's around 10 percent, as Arturo said. And you know, we have learned from the experience of Peru and Ecuador. When this confinement started, many of our customers closed. And they closed because of fear or really not knowing if they could open and not knowing how to do it. So, in those countries, we are now working with the government and with the customers to help them and to show them that they can open, and they can serve our customers. And you know that our products for these customers weigh around 30 percent of their business, so they are our best partners, and we are also their best partners. So, we're helping them to reopen. But we're using that experience in Mexico. And in Mexico, that has not happened. In Mexico, the traditional trade represents around 60 percent of our mix. And we are on the positive side most of April. I hope that was useful.

Alvaro Garcia: Pepe, that was very useful. And just one quick follow-up, Pepe. I was wondering if you could just comment on the resiliency of the traditional trade. I mean, it's pretty remarkable how strong it's been. Is that case through April? And why do you think that people are still in the streets in Mexico?

Arturo Gutiérrez: Well, the traditional trade has a huge advantage of being the channel of proximity. People that need it stay at home. So, it's natural that they're more resilient. The problem we have with traditional trade, as I mentioned in South America, is that some of the stores have been closing. And it has not happened in Mexico. So, we're anticipating in Mexico this type of situation and support those customers to remain open in a safe way. But there is a very close correlation with the percentage of stores that are closed and our performance and volumes in those markets. And as I said, the trend is improving in Peru and Ecuador. So that is a positive as you see those stores coming back in operation. But they really have the strength. And this is something that's going to continue, I guess, for some time, because you know, habits of our consumers are going to change, maybe definitely, or at least for a longer period of time than this emergency would last. So being close to homes, having that needed access to basic products. I think it's going to be very valuable. So, we're working now, not only on the crisis itself, but what are we going to do when we are reestablishing certain normality. And we're giving special focus to the traditional trade, supporting its recovery and helping them face the new situation. One of the things that we're doing with them is our digital B2B platform. That's an example of important things that we were doing before, but we have now accelerated, because it helps them face this situation. At the same time, it helps to accelerate something that made sense even before the crisis.

Alvaro Garcia: That was very helpful color. Thank you very much.

Arturo Gutiérrez: Thanks, Alvaro.

Operator: Thank you. Again, as a reminder, please press star one if you would like to join the queue. Our next question will come from Luca Cipiccia with Goldman Sachs.

Luca Cipiccia: Hi, good morning, everyone. Thanks for the question. I hope you're well. Just a clarification on the previous discussion. I think I understood you mentioning that South America has been tracking in the mid-20's negative in April or 20 or -24 percent in March? I'm not sure I got - if you made any comment on the overall volume performance in April, or if you could put some range for Mexico and the US. And again, apologies if I missed this already. But I think I got the South America comments and not with regard to Mexico or the US.

Arturo Gutiérrez: No, you got that right. Thank you, Luca. The volume declines in March in South America are around 24, 22 percent, I said, for Peru and Ecuador. So that's the worst performance that we had in the quarter. But the situation in April is worse than that, because we're facing the worst stage of the crisis. So, we have the initial stage, the first cases and initial fear. And then, we're at the lockdown and restriction mobility stage. And that's when the impact is most severe. We're facing that in April. April is going to be our worst month for the overall year. And then, we're going to have a gradual recovery. We anticipate that to be in some markets in mid-May. Maybe June would be really our initial recovery as we return to the new normal. So, we're at the stage where restrictions are at the highest - severe limitations of mobility. So, it's hard to predict. It just depends on how the governments are defining those restrictions. And they are adjusting almost on a day-to-day basis.

What we can say is that Peru and Ecuador are the hardest hit. Mexico and Southwest seem better so far. And naturally, these measures that restrict mobility are of our limited duration. So that recovery should be near. We're already seeing, again, customers coming back into operation even in South America. So, it's hard to present the curves of this performance in volume. It will not be really gradual, not that gradual in the second quarter. Some of the post pandemic effects are still going to be expected. So, what we can say is that April and May again are our most adverse environment. Some recovery in the June, July, August period and a much better trend in the fourth quarter. It really depends on when the markets start to be open. So that's why we have withdrawn our guidance. And as I mentioned, given the great uncertainty of the current environment, we feel that is the prudent thing to do. But we expect to come back to you soon with greater clarity, because many of these variables are not under our control and again, are hard to anticipate. When we are more confident about those estimates, we'll be ready to provide some guidance to you.

Luca Cipiccia: But if I may, and I appreciate you might not want to disclose it fully or in a range, but when you say Mexico and US relatively better, should we assume still declines in the 20's? And I guess my question comes from the fact that Coca-Cola did say that in April, I think global volumes were down 25 percent. I'm just trying to get a handle of whether it's relatively better, but does it mean 10-15 percent, 15-20 percent, and I appreciate that the situation is very fluid. But just not to be too far from what might be realistic.

Arturo Gutiérrez: Yes, it should not be too far from where Coke has estimated but just take into account that theirs is an average of many, many different situations of the stages of the pandemic around the world. I hear that the China market is recovering. Europe is at a different stage. You know, it's hard to compare, but let's say that as a general number, it's going to be pretty much like that and gradually improving as the year goes on.

Luca Cipiccia: Okay, understood. Thank you. Thank you for clarifying. Take care.

Arturo Gutiérrez: Thank you, Luca.

Operator: Thank you. Our next question comes from Ulises Argote with JPMorgan.

Ulises Argote: Thanks so much for the space for questions and for the additional color that you have given us. So, most of my questions have already been answered. So I was just wondering if you could give us any additional color there on the Houston plant? I mean, you said in your prepared remarks that it had already been opened and fully operational, but I was wondering what are you seeing there in terms of logistics like the routes? Are route changes working appropriately, and if there are any incremental costs there that we can expect going forward that could maybe kind of disturb the good margin trends there for the US operations? Thank you.

Arturo Gutiérrez: Thank you, Ulises. Well yes, our Houston plant is now fully operational, and as we've mentioned before, it's a significant part of our synergy projects in the US. So we have five lines that began producing late last year and then throughout the first quarter. So we continue to work to achieve the stabilized and rated efficiencies of the lines. But we are working according to plan. Additionally, there was another part of that project, which is the Vertique system, the semiautomatic picking for the plant. That also started testing during the first quarter. It's very important, that portion of the project, because it brings significant synergies to the overall operation. And it's filling the pallets according to the customer orders and all of that. So, it guarantees a very high degree of picking accuracy. So that's working really well. We're very excited what the future holds for Northpoint as we fine tune the operations. It's a pity that we cannot have our grand opening, which was scheduled for mid-March. But we look forward to have some kind of celebration and having the opportunity of hosting visits by you at the plant. So we expect that CAPEX is in line with what we anticipated, and also synergies that it will bring in addition to what we had as carryovers for 2019 are also in line with the plan. And this comes from lower manufacturing costs, our freight reductions, again, warehousing and picking efficiencies, you know what we said before.

Ulises Argote: Perfect. Thank you very much, Arturo, for the color and stay safe guys.

Arturo Gutiérrez: Thank you, Ulises.

Operator: Thank you. Our next question comes from Emiliano Hernandez with GBM.

Emiliano Hernandez: Hi, good morning. Thanks for taking my question. My question is regarding Bokados. If you could give us a little more color on the double-digit growth in EBITDA in the quarter? And what should we expect in that business for the next couple of months?

Arturo Gutiérrez: Thank you, Emiliano. Well, Bokados has a slightly better situation than the rest of the business units. It did have still a month of March where we grew in revenues, which is a very good sign. I would say in general that the categories of snacks are a bit more resilient sometimes. So, they're still performing with declines, but not as severe as we've seen in some of our beverage markets. We had a positive low single digit sales growth and double-digit EBITDA growth. Our comparisons in profitability are fairly easy. We had also a better raw material environment in the first part of the quarter. And that has been changing mostly because of the peso devaluation. And that's impacting costs a little bit. We're seeing, again, the strength of the traditional trade in Mexico is helping Bokados, so this should obviously that when volumes start to decline, and we're already seeing that in April. And that's natural, although it's not as severe. The lower margins in Bokados resulted in a bigger impact on our profitability. So that's why we started working on our savings plan, even before the sales started to be impacted. So, they're an important part of our optimization plan going forward, to make sure that we maintain a good profitability. The margin for Bokados in the month of March was still at the 9 percent level, so 9-10 percent, which is still good, but it's not the margin, obviously, that we have in beverages, so we need to make sure that we need to protect that. And we have many opportunities in Bokados, as you know, for expanding to other regions. We have been successful in expanding Bokados to the center and south of Mexico. That has, at the moment, obviously been suspended, but I think growth will recover in the second half of the year for Bokados as well.

Emiliano Hernandez: Thank you. That was very clear.

Arturo Gutiérrez: Thank you, Emiliano.

Operator: Thank you. Our next question comes from Leandro Fontanesi with Bradesco BBI.

Leandro Fontanesi: Hi, good morning. Thank you for the opportunity. I have two questions. You mentioned that you have been seeing a decline in volumes in the 20's, right? We understand this is a sizeable decrease in volumes, and at the same time, we understand that consumers still need to drink, right? So just wondering if they're not drinking your products, what are the consumers drinking? And the second question - you mentioned some of the effects in your mix are due to the coronavirus, which is, for example, higher sales of water. But I'm just wondering what changes that you think will be permanent due to the coronavirus? So, thinking beyond the temporary effects that we are seeing right now, such as, for example, permanent changes in product mix or also in your distribution channels? Thank you.

Arturo Gutiérrez: Thank you, Leandro, for your questions. And well yes, we're seeing some things changing in habits of our consumers. Some are temporary due to the emergency. Maybe some will stay for a longer time. Let me address the first part of your question, which is what are the consumers drinking or having? You know, obviously, we are, as in normal times competing with tap water. This is the natural thing that consumers resort to when they are not able to drink our products. We've been mostly stable in our share of value throughout our markets. We're winning slightly in some markets. We're maybe losing them marginally in some others. So, in general, we're stable. The situation is that when people don't go out as much, it's natural that consumption patterns change. Again, we believe that we are in a very resilient industry, considering the current emergency. And there are many reasons that I believe that we're going to be back in the path of growth in the near future. There's going to be an effect in the mix of channels. I would say that the biggest thing I can identify, and maybe Pepe can answer that, is how the e-commerce is going to start to grow. People who were not ordering on-line are going to start ordering on-line. We've seen that in the US, and that might change some of the habits going forward. So, it's very important for us that we have been working on digital initiatives and transformation for a long time, so we can adapt to the new circumstances. In terms of mix of product in itself, probably it's not going to be that relevant going forward. But we're going to be looking into also consumer information to identify any possible trends. So there are two ways in which habits can change. One is the channels, the purchasing habits. And then there's the consumption categories themselves.

Again, we have the reasons to believe that we are in a very strong position going forward. Our categories are in general resilient if you consider the industry. We have strong market presence and leadership in all markets we participate. We have been improving our customer relationships through this crisis through the many things that we're doing. So, we're going to come out of this strengthened in our relationships and the goodwill that we have built in the markets. And we, as I said, we have the digital capabilities that have been developed for some time now, that are so important to have that agility to adapt to new circumstances. I think agility is going to be key as we move into that new phase of normality. And very importantly, something that I've not mentioned before, is the capacity to optimize our OPEX, because some of the go-to-market models are going to change. We have to be more efficient. And I think we've also proven that we are able to adapt in that way as well. So, with that, I'll turn it over to Pepe if he wants to add something to the change in mix that we envision for the future.

José Borda: Yes, thanks, Arturo and thanks, Leandro, for your questions. As you know, we have overcome other crises. I know this one is probably one of the biggest the whole world has gone through. But I think it's too early to talk about important permanent changes. We're studying the consumer, as we always do, but we offer a whole line of beverages to tackle each of the different hydration needs. As Arturo said, I think that the change in channels and the change in mixes can affect the types of beverages people consume. The types of beverages they consume at home can be different than the ones that they consume on premise. And maybe people will start working more from home, and we're going to see more online, more home deliveries. So, at the end, it's going to be a mix between how the channel impacts the different beverages that consumers choose. So, what I can tell is, we are very resilient as Arturo said. And we have a whole line of beverages to offer, and we will adapt to any changes in the situation.

Leandro Fontanesi: Thank you very much.

Arturo Gutiérrez: Thank you, Leandro.

Operator: Thank you. This concludes today's question and answer session. I would now like to turn the call back over to Arturo Gutiérrez for closing remarks.

Arturo Gutiérrez: Thank you. Thank you for participating in our earnings call today and for your continued interest in Arca Continental. As always, our Investor Relations team is available for any additional questions that you may have.

Operator: Thank you. Ladies and gentlemen, this concludes today's teleconference. You may now disconnect.

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