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: 917-797-7600
Mcarpenter@i-advize.com

Public Affairs and Communications

GUILLERMO GARZA
guillermo.garza@arcacontal.com
Tel: 52 (81) 8151-1441

FIDEL SALAZAR
fidel.salazar@arcacontal.com
Tel: 52 (81) 8151-1441

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CONFERENCE CALL

Arca Continental 1Q22 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. Ma'am, please go ahead.

Melanie Carpenter: Thank you, Katie. Good morning, everyone. Thanks for joining the senior management team of Arca Continental this morning to review the results for the first quarter of 2021. 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 Gutierrez; the CFO, Mr. Emilio Marcos; and the Chief Commercial and Digital Officer, Mr. Jose 'Pepe' Borda; as well as the Investor Relations team. They're going to be making some forward-looking statements, and we just ask that you refer to the disclaimer and the conditions surrounding those statements in the earnings release.

And with that, I'm going to go ahead and turn the call over to the CEO, Mr. Arturo Gutierrez, who is going to begin the presentation. So please go ahead, Arturo.

Arturo Gutierrez: Thank you Melanie, and many thanks to everyone for being with us this morning.

Before we review this quarter's results, I would like to take a moment to express our great sadness at the recent passing of our dear friend, former Arca Continental CEO and Board Member, Pancho Garza Egloff.

For 15 years Pancho led the operations of Arca Continental through transformational expansion and sustainable growth. He taught and inspired thousands of our leaders and team members.

On behalf of all of us, I would like to express our most sincere condolences to Pancho's family, and we offer our prayers and our deepest sympathy. We will all strive to always live his legacy in our organization.

Now let's summarize our performance for the first quarter.

I am pleased to report positive momentum for the first quarter of 2022. We initiated the year on a solid note, delivering a strong operating performance and sound financial results.

Total consolidated revenue in the quarter increased 13.8%, to 46.1 billion pesos and total consolidated volume grew 5.4%, reaching 542 million-unit cases.

We delivered another quarter of sequentially improving results, with strong sales and volume acceleration across every one of our five operating groups, as we continued innovating to meet evolving consumer needs.

On the profitability front, consolidated EBITDA for the quarter rose 11% reaching $8.5 billion pesos, representing a margin of 18.5%.

Our revenue management and cost leadership initiatives enabled us to build and sustain strong earnings growth, despite significant cost headwinds.

Let me now expand on our operational performance across geographies, beginning with Mexico, where our flagship market continued to demonstrate the strength of our beverage business.

Total unit case volume grew 2.7%, cycling 1.4% from the same quarter in the prior year.

This marks the fifth consecutive quarter of volume growth in Mexico, confirming sequential improvement throughout the last two years.

Water and still beverages led among categories, up 13.1% and 15.3%, respectively.

Furthermore, Coca-Cola Without Sugar continued delivering outstanding results with double digit growth.

Also, key channels such as on-premise, schools, and entertainment showed a remarkable recovery as consumer mobility continued to normalize, thanks to the reopening and lifting of capacity restrictions.

Single serve mix grew 2.4 percentage points in the quarter, capturing the gradual recovery of immediate consumption in both returnable and one-way presentations, driven by the expansion of our 235-milliliter returnable glass bottle and the launch of the 250-milliliter PET multicategory platform as entry level packages.

Total net sales in Mexico rose 10.4% in the quarter to reach $18.3 billion pesos, marking the twenty-third consecutive quarter of net revenue growth.

Average price per case in Mexico, not including jug water, rose 6.7%, reaching $72.87 pesos, sustained by our strong execution, revenue management capabilities and the launch of the new affordable packages.

EBITDA increased 3.2% to $4 billion pesos, representing a margin of 21.7%. We continue navigating through a challenging commodity environment and we aim to protect profitability by using our tailored pricing strategies, combined with our disciplined focus on cost optimization.

Our universal bottle is a great example of our disciplined focus on efficiencies. We are expanding with new packages such as the 500-milliliter glass bottle in flavored SSDs and still beverages.

In South America, total volume was up 13.9% in the quarter, with a solid performance across our three markets in the region and confirming the positive recovery momentum.

Total revenue rose 18.3%, reaching 10.4 billion pesos, while EBITDA increased 22.1% to 2.2 billion pesos, representing a margin of 21.7%.

We saw sequential positive trend across channels supported primarily by the traditional trade, while on-premise and supermarkets are both showing sustained recovery.

In Peru, our beverage operation delivered sequential volume growth, up 12.5% versus last year and 0.7% above the same quarter in 2019, as we begin to surpass prepandemic levels.

Volume growth was led by sparkling beverages, up 14.8%, on the back of another strong performance in single-serve packages in our core brands Coca-Cola and Inca Kola.

Our commercial initiatives focused on protecting portfolio affordability via an accelerated introduction of multi-serve returnable packages.

The on-premise channel continued accelerating the pace of recovery as Covid mobility restrictions were lifted just last month, and outlets are now operating at full capacity.

This recovery is driving increases in the immediate consumption mix. In fact, single serve in Peru increased 4.1 percentage points in the first quarter.

We doubled down on the deployment of our AC Digital platform, providing customers with the ability to place direct orders using a mobile app.

At the end of the quarter, we reached over 100 thousand active customers, representing 42% of the targeted customer base.

Our beverage operation in Argentina delivered another outstanding quarter of double-digit volume growth, up 27.7% and cycling strong volume growth from the same quarter in 2019.

Volume growth was broad-based across the portfolio and driven by solid performances with sparkling at 25.3% and both stills and water, up 36.7%.

From a channel perspective, modern trade led the recovery driven by our initiatives to promote multi-serve packages and despite price control measures imposed by the government to tackle runaway inflation.

We will continue executing our selective pricing strategy in line with inflation and doubling down on our cost discipline and optimization efforts.

In Ecuador, total volume in the quarter grew 4.4%, as the economy continues to bounce back, in line with higher average oil prices and despite mobility restrictions reinstated last January due to a new wave of Covid-19 cases in the region.

Volume growth was driven by still beverages and water categories, up 24.6% and 9.3%, respectively. Growth in Stills was led primarily by Powerade and Fuze Tea brands, as we leveraged our commercial activities to drive affordability and increase our coverage in the traditional channel.

We have maintained our competitive position in the traditional channel by focusing on evolving our service models to increase customer satisfaction, implementing dynamic routing to adapt to a changing market and building digital capabilities to reach more customers in a more cost-efficient way.

Tonicorp, our value-added dairy business in Ecuador, posted high-single-digit sales growth in the quarter while capturing additional value share.

Growth was driven by yogurt, flavored milk, and ice cream categories, as we capitalized on the recovery of key channels such as schools and entertainment.

Let me now turn to our beverage operations in the United States.
Before I present our quarterly results, I would like to highlight that this month we are celebrating the five-year anniversary of our U.S. business, Coca-Cola Southwest Beverages.

It started on April 1st, 2017, when we completed the acquisition of the territory formerly operated by Coca-Cola Refreshments.

This event marked the start of a new level of partnership with The Coca-Cola Company and we are proud of what we have achieved during our first five years in these territories.

Since then, we have accomplished several important milestones such as expanding into a new territory in Oklahoma, winning the Market Street Challenge and the Candler Cup; delivering all our synergy commitments; opening our Northpoint facility in Houston, the newest production facility in the US in more than a decade; and most importantly, launching our cultural principles, which have continued to drive increased engagement every year since they were introduced.
And now moving to our results in the quarter, Coca-Cola Southwest Beverages delivered steady top and bottom-line growth.

Net revenues for the quarter grew 14.7%, reaching $793.5 million dollars. Net price per case rose 13.6%, with a true rate of 10.4% driven by last year’s off-cycle price increase and a mix rate of 3.2% due to our price-package strategy of shifting volume to higher profit-per-case packages such as Immediate Consumption and Transaction Packages.

Volume for the first quarter grew 0.9%, reaching 101.3 million-unit cases, driven by growth of supermarkets and on-premise channels.

Sparkling soft drinks led the growth for the quarter, up 1.3% and supported by the launch of Coca-Cola Starlight, our newest innovation in the Sparking category.

It’s important to mention that volume shifted substantially from water to the rest of categories due to last year’s pantry loading effect related to the February winter storm.

EBITDA increased 15.6% to $115.1 million dollars in the quarter, representing a margin of 14.5% and marking the fifteenth consecutive quarter of EBITDA growth.

Our beverage business in the U.S. has consistently grown EBITDA every single quarter since 2017 with a compound annual growth rate in U.S. dollars of 11.2% and has improved margins by 270 basis points from 2018 through 2021.

Furthermore, we are making solid progress in our digital agenda with our Trade Promotion Optimization tool. We started expanding to new use cases outside the commercial area, such as Human Resources.

We also consolidated our new eParcel operation covering the Dallas-Fort Worth area. With this capability, we enhanced service to our smallest customers by partnering with third-party delivery companies.

In closing, our Food and Snacks business posted double-digit sales increase in the quarter, driven by solid pricing and volume growth across all our operations, as well as the integration of Carlisnacks in Ecuador.

Sequential recovery was driven by the traditional and modern trade channels in Mexico and Ecuador, coupled with robust performance of the Deep River brand in Food Service and Wise Variety packs in the Supermarket channel in the U.S.

We continued implementing tactical pricing action to offset the increase in key inputs such as edible oil and packaging film.

In addition, we deployed efficiency plans to optimize freight costs, reduce product waste, and streamline administrative processes by leveraging our corporate shared services capabilities.

I will now give you an update on the progress we have made in our ESG initiatives.

As part of our joint efforts with The Coca-Cola Company to create a World Without Waste, and thanks to the close partnership with PetStar, our beverage operation in the U.S. has reached a PET collection rate of almost 40% of the volume we place on the market.

We reinforced our commitment to reduce the use of resin in plastic packaging, becoming the first bottler in North America to lightweight our 12-ounce PET presentation from 22 to 14 grams, by using state-of-the art technology that incorporates an ultra-thin protective layer of glass in the insides of these bottles.

Also, we continued promoting the conservation and replenishment of water sources, the efficient use of water in our facilities, and the reuse and adequate treatment of water discharge.

Aligned with this effort, we signed a collaboration agreement with The Coca-Cola Foundation and The World Wildlife Fund to develop nature-based water treatment systems in Chihuahua, Mexico to reduce water scarcity.

And with that I will turn it over to Emilio. Emilio, please go ahead.

Emilio Marcos: Thank you, Arturo. Good morning everyone and thank you for joining us today.

We have started 2022 with the same momentum we had towards the end of 2021, with solid revenue growth supported by positive volume levels across all our operations. Combined with price-packaging initiatives which we started last year, our flexible commercial strategies have adapted to the current consumer trends. This positive revenue performance along with the financial discipline deeply-rooted in our daily operating culture, allowed us to partially offset the impact from raw material headwinds.

Moving over to the financial results of the quarter.

Consolidated Revenues increased 13.8%, driven mainly by positive volume trends in all operations and a strong price/mix in Mexico, the US, Argentina and Peru. On a currency neutral basis, Net Revenue grew 15% in the quarter.

Gross Profit grew 12%, reaching $20.6 billion pesos as a result of timely pricing initiatives, innovative commercial strategies, and our disciplined hedging program which partially mitigated the continued cost increases of our key inputs. The net effect of cost headwinds and our initiatives represented an 80-basis point reduction in the contribution margin.

Looking ahead, as global events continue to create volatility in all commodities, we still expect our margins to be pressure by higher raw material prices, particularly in PET and aluminum.

Consolidated EBITDA posted an increase of 11% to $8.5 billion pesos, for an EBITDA margin of 18.5%, representing a small dilution of 50 basis-points compared to the 190 basis-points expansion in the first quarter of 2021. This was largely driven by the pressure in contribution margin previously mentioned. On a currency neutral basis, EBITDA grew 12.4% in the quarter.

The SG&A to sales ratio decreased by 120 basis-points, mostly from operating efficiencies, as we continued to capitalize on the learnings from the pandemic. It is important to remark that the market expenses made in the previous quarter paved the way to support positive volume levels at the beginning of the year.

Net Income for the quarter increased 19.7%, mainly due to the positive operating income result. This was partially offset by a foreign exchange loss of $90 million pesos this year versus a gain of $200 million pesos in 2021.

Now, moving onto the balance sheet.

Cash and cash equivalents in the first quarter stood at $35 billion pesos with a total debt of $50 billion pesos, resulting in a leverage ratio of 0.4 times.

On April 1st, a cash dividend of $3.18 pesos per share was approved at our Annual Shareholders' Meeting, totaling $5.6 billion pesos and representing a payout ratio of 46%, in line with our historical average. This dividend was paid on April 19th.

Along with the dividend, the buyback and cancellation of around 20 million shares, representing 1.1% of total shares outstanding was also approved at the Shareholders' Meeting.

This is the first time that Arca Continental executed a cancellation as another capital allocation alternative.

CAPEX for the first quarter was $1.7 billion pesos, an increase of 20% versus the same period last year. As we had previously announced, we expect to invest close to $12 billion pesos, half in Mexico and the rest in the US and South America. These investments are in line with our strategy of strengthening production and sustainability projects, distribution capabilities, market execution, and promoting digitalization across the operations.

As we look ahead, we remain confident that a sustainable top-line growth based on the deployment of innovative and efficient commercial strategies, coupled with our continued commitment to operational discipline, will protect the profitability of our business in 2022 despite the challenging global setting we have experienced so far.

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

Arturo Gutierrez: Thank you, Emilio.

To conclude, we believe we are well positioned to manage through and beyond the near-term issues we are facing and deliver long-term growth and value creation.

We remain focused on efficiency and committed to driving cost savings and productivity in all aspects of our business to mitigate input cost volatility.

Despite the challenging backdrop, we are optimistic and excited about the future of our business.

Over the past ninety-six years, we have developed the right skills, abilities, and experience to navigate volatile environments through effective execution.

The set of actions we took during the pandemic have enabled our organization to stay lean, nimble, and flexible.

And of course, the satisfaction of customers and consumers has been the main driver of our ongoing evolution and progress.

Looking forward, we will continue to invest in our business for the long-term, to be focused on our people, our digital journey, and our sustainability agenda.

We will also step forward toward growth opportunities for regional expansion in the beverage, food, and snacks industries.

With that, we will be happy to take your questions. Katie, please open the floor.

Operator: Thank you, sir. At this time, we will open the floor for questions. If you would like to ask a question, please press the star key, followed by the one key, on your touchtone phone now. As a reminder, due to high interest and time, please limit yourself to one question. We will pause for just a moment to allow everyone the opportunity to signal for questions.

Thank you. Our first question comes from Ben Theurer with Barclays.

Ben Theurer: Thank you very much. Good morning, Arturo, Emilio and congrats on the result. I wanted to ask about the strategy and the alignment with The Coca-Cola Company. And, you know, we've talked about the opportunities you know have being allowed within the system to explore new ventures, partnerships and so on. And you've just said, you're looking obviously into these opportunities. Could you give us an update on where you stand and what you're looking for in terms of possible other distribution agreements or just leveraging your capabilities, be it in Mexico or in South America. But also to a degree in the United States, what could be done on your side to maximize what's being allowed within the new partnership framework with The Coca-Cola Company? Thank you.

Arturo Gutierrez: Sure, Ben and good morning. Thanks for your question.

We have said before, we are in conversations with The Coca-Cola Company to take our business partnership to the next level, over the long-term and we are very close to concluding negotiations in that regard. And this is not the typical discussions that we've had in the past - about how to manage our current business - it's mostly about new product categories, distribution agreements and digital initiatives basically. So, I think precisely here the point is how to align better our mutual interests so that we can capture those opportunities. If you look at what we have been doing in the digital space with Yomp! and some of the things that can complement our business, we know the opportunities are there. Same thing for distribution of products that are different from the KO products. We've been doing that with beer in Argentina and we've started a pilot, as you know, in Ecuador. So, these agreements will come here to align us to better capture those opportunities and they are in all of Latin America, I would say, and they are not only to strengthen our current business, which I think would be still the core and the fundamental purpose. But also the idea is to develop distribution of other beverages and to also expand our digital footprint, particularly the traditional trade in Latin America. So, I will turn it over to Pepe for some additional remarks in that regard.

Jose "Pepe" Borda: Thanks, Arturo, and thanks again for your questions. So as Arturo was saying we continue to work together with Coca-Cola Company, evaluating potential opportunities not only across LatAm but across all our territories. And that distribution pilot we started in Ecuador is part of this. It has been three months since the launch with very positive results, showing important distribution and volume growth and we're evaluating expansion to other regions. And in parallel, we are evaluating alternatives for partnerships in Mexico and Peru, and also beyond, other products distribution opportunities under evaluation we also plan to expand our footprint in flavored alcoholic beverages beyond TopoChico Hard Seltzer. Also in Mexico, Yomp! continued to expand in Monterrey and Guadalajara.

Today we offer more than 1,500, CPUs from 30 different CPGs and we are expanding our value proposition for our customers in the traditional trade with an extended portfolio offering not only products, but also services. And we are also working in CPG alliances to consolidate synergies across our business and portfolios. But, I think the key here is to balance the benefits between a lean agile startup like Yomp! with the synergies with the Coca-Cola system. Yomp! started in different experiments and it's slowly starting to converge into an ecosystem. So, we're scaling Yomp! as a solution for digitizing the whole traditional customer operation, allowing them to offer services to customers, buying groceries from companies that do or do not offer direct distributions. I think the key is that within the Coca-Cola system, the bottlers are testing, implementing and evaluating different alternatives in a continuous learning process.

But as always, we share best practices and learn from each other. So, this increases the breadth of experimentations in areas where there are no proven winning models yet. And further down the road, we will find synergies with other bottlers and work together with Coca-Cola Company to help us materialize those synergies.

Ben Theurer: Perfect. Thank you very much, Arturo and Pepe.

Arturo Gutierrez: Thank you, Ben.

Operator: Our next question will come from Sergio Matsumoto with Citigroup.

Sergio Matsumoto: Yes, hi. Good morning, Arturo, Emilio and Pepe. I wanted to go deeper in this very topic of the multi category. When we look back into the history of ArcaContal, the salty snacks was, you know, the first one that you kind of ventured out outside the beverage territory and I'm just wondering if now if you still see the synergies with the soft drinks portfolio the way Coca-Cola company sees with potential synergies with other non-Coca-Cola categories today. And then the opportunities to deepen these salty snacks or perhaps expand into other categories that you distribute yourself.

Arturo Gutierrez: Thank you, Sergio. With respect to those categories that are beyond the beverage space, we still believe that these are adjacent categories. I think part of the learnings of the last more than 10 years that we've had this business is that, there are some things that can be synergized, but many things should be kept separate and this is how we operated that business over the years and we're still with having the intent to become a more national business in Mexico as we have in Ecuador, as you know, which has a wide footprint. So look at the Ecuadorian model. And I think that makes a lot of sense to us. How we can leverage some of the scale that we have, and also how to leverage technology and digital platforms and making it easier to attain those synergies. I think that how we evolve our go-to-market, especially digital platforms and also the relationship with customers through these platforms present new opportunities.

But the businesses are going to be kept relatively separate. I think that's the best way to operate them in terms of the sales force and the connection with the customers. But we do think that there is still important an adjacency. As many other categories that Pepe mentioned, alcoholic beverages and snacks, and then other things that can be connected as we…At the end, what we're looking at is how to also enhance and strengthen our relationship with the customer and how we become solution providers to the customers specifically in the traditional trade in Latin America.

So, I think that connects very well with the development of snacks and some of these adjacent businesses.

Sergio Matsumoto: Second question, if I may, is on the aluminum cost pressure particularly in the United States. Any color as to how you might face that with may be the mix or maybe pricing architecture?

Arturo Gutierrez: Yes, well, as you know, aluminum has been probably the biggest impact that we've had in raw materials in this first quarter of '22 as compared to last year where we had very important hedges. And that, just in the case of the US, its impact has been above US$17 million directly to us also. So it's significant.

If you look at our pricing, we in a way anticipated that in our off-cycle price increase of last year, which was very important to mitigate and also, the recovery of volumes in the US and the discipline in the OpEx management, if you look at SG&A as a ratio, that's also improving. So at the end, the margins have been sustained, which is I think, truly remarkable considering this very, very challenging environment.

We've had aluminum prices way above historical prices, including the Midwest premium, which has been up more than double. So this environment is going to continue. So we have to anticipate with a combination of prices, better mix, as you mentioned that's been a very important - part of the price increase in the US is around 13% and the improvement in mix is more than 3%. So it's significant. And also how volume recovers particularly in the on-premise channel and, again, a disciplined management of OpEx.

Emilio Marcos: Just to add, Arturo, that on US as I mentioned last quarter, we have 50% hedge--have hedged our needs on aluminum in US and Mexico. And as Arturo mentioned, last year we had great hedges, so that's why the comps are really tough. But we've been able to compensate that with the pricing and mix that Arturo already mentioned.

Serio Matsumoto: Understood. Thanks very much, guys.

Arturo Gutierrez: Thank you.

Operator: Our next question will come from Isabella Simonato with Bank of America.

Isabella Simonato: You mentioned in the fourth quarter result, right? Your expectation of top-line growth for the year about 6-8%, if I'm not mistaken. Is there any change of that expectation, I mean anything that you're seeing in the first quarter, especially, in the US, another region that might bring this potential expectation up eventually? And my second question is on concentrate costs in Mexico. If you could give us an update on, regarding concentrate prices. If you think that there will be an increase or not? Thank you.

Arturo Gutierrez: Thank you. Thank you, Isabella for your question. The first part is--the short answer is there's not a significant change to the guidance that we have provided. What we were seeing this first quarter of this year is a recovery, which we expected not only versus last year. But if we look at our baseline, our pre-pandemic baseline of 2019, we are recovering our volumes around 6% this quarter, which is as we expected.

But I think very important to see is that, that recovery is still with an on-premise channel that is not fully recovered as we compare to that base, maybe except for Argentina, where volumes have been outstanding and maybe Argentina our baseline would be previous years, where we had our record volumes. But in the rest of our markets, if you look at Mexico, on-premise channel it's still 7% below its pre-pandemic level. This is first quarter '22.

The US it's more than 20% so what we're seeing is an opportunity to-- we see that as an upside going forward. But, if you look at our last four quarters, we've seen growth everywhere in every market, we've been growing. So, we expect that trend to continue and the other headline there is that the traditional channel, Latin American continues to be very resilient. We continue to grow the traditional channel regardless of the comparisons that we've had throughout the pandemic.

We've grown at 0.5% volume in the traditional channel this quarter so. For the rest of the year we expect that trend of recovery to continue, which is actually shown in March. If you look at month by month throughout this year, we look at that trend of recovery, specifically about -- again, the on-premise channel, which although it is below 2019 - in for example in Mexico in March, just the month of August, the on-premise channel is above 2019 levels of 2.3%, which I think is a very good sign of recovery and that would be moving forward.

Let me address the second part of your question, which is about concentrate costs in Mexico. And I mentioned before that we are in conversations with The Coca-Cola Company regarding our alignment for the future and previously those negotiations focused mainly on concentrate, basically, and some issues related to our bottling agreements and market investments. Now negotiations are much wider, I would say. So regarding concentrate, we're working with KO to align our business plan and other variables that could affect the market in Mexico or any of the market this year and years to come. So, this is how the business model would work for us now. We would discuss the circumstances that would affect the consumer environment. And then, look at what is best for the market and balance investments that need to be made and challenges that we're facing like, like we are particularly this year with a higher input costs. So then this is again, a much more balanced situation between us.

I think that is sustainable and we maintain that continuous dialogue to define the new opportunities, as in the case of these market investments, new beverage categories, digital space, etc. So, I think we are in a much better position that we were in the past, when I guess the relationship was not as close, was more distant and concentrate prices were basically just announced by The Coca-Cola Company, now it's a continuous conversation.

Isabella Simonato: Got it. Thank you very much.

Arturo Gutierrez: Thank you, Isabella.

Operator: Thank you. Our next question comes from Alan Alanis with Santander.

Alan Alanis: Thank you so much.

Thanks for taking my questions. And first of all, my condolences. I'm really, really sad about Pancho Garza Egloff. I think it's very important to say it here and reiterate it here that he was an exemplary man in both personal and professional aspects of life. So, clearly missed and our prayers go to him.

Now, the question that I have, I'll be a bit more direct in terms of the alliances in Mexico. Coca-Cola Femsa just announced that they have pilot programs already going with Diageo with Kellogg and with Procter and Gamble in Mexico and they are expanding into other places. Do you have any alliances in any of these companies in Mexico right now and with the fact that the Coca-Cola is already having this make it easier for you or more harder for you to have these kinds of alliances in your territories. I would assume that it's easier. But I'd rather hear it here if that's an accurate statement.

Arturo Gutierrez: Thank you, Alan. And thank you about your message regarding Pancho. He certainly will be missed.

And addressing your question. Yes. The system works I guess in a much more integrated and coordinated now. So I think anything that happens around the system in Latin America, especially but even around the world, but mostly Latin America I think will benefit us all and Coca-Cola Company certainly coordinating the effort in many ways. So I think all of that president is going to work in our favor and we have our own pilots and our own experience also taking place and we have sometimes made more progress in digital space, that's something that they can take advantage of the rest of the bottlers will take advantage of and we've been very transparent, very open about what we're doing. And maybe this is different compared to the past many, many years ago and I know you lived that where many people were --many of the bottlers were doing their own efforts on their own.

I think we're much more coordinated, I think that will serve as great learnings to what we need to do and but, also take into account that maybe the markets sometimes are different, maybe the partners that we would have, would not necessarily be the same, depending on the markets where we operate. So, that's something that we're taking a deeper look into, just to make sure that we formalize and work on the right partnerships.

Alan Alanis: That's very clear. Last question regarding capital deployment. You're going to be net cash by the end of this year. Any update in terms of getting closer to M&A or the possibility of increasing or accelerating your share buybacks or your cash back to the shareholders, given the net cash position that you likely be by the next four quarters.

Arturo Gutierrez: Well, our strategy will remain the same as we said, we don't have anything specific to announce at this point. And we're going to continue balancing basically our uses of our resources, aside from CapEx and our dividends and as you know, the shareholders' meeting approved the option of extraordinary dividends to be approved by the board, which is something that gives us flexibility. We continue to look for opportunities in buybacks as we move forward and also considering how the stock price could be a good option for allocating our capital; and M&A, we are still searching for those – well, what we all know is that in this industry and probably different to other industries, there's a lot of value to be captured because most of those integrations, if not all, create value, just because of the geographic structure of the bottling system around the world. If you talk about the Coca-Cola system.

So there's certainly value there. You know that for that to happen many other things need to be aligned not necessarily on the hard business issues, but many things need to be aligned. So we think that we should remain prepared financially and also have the flexibility as a company to adapt to any potential deals that might present in different formats. So, that's where we are at this point.

Emilio Marcos: Yes. Hello, Alan. I just have that on CapEx, we'll increase on the past two years, we've been investing 4% over sales and having a better top line. We will increase our percentage on CapEx, we just announced around MXN12 billion. It's going to be around 5% to 6% over sales. So, that's going to be part of the increase of allocation on CapEx.

Alan Alanis: Very clearly, Emilio. Thank you so much to both.

Arturo Gutierrez: Thank you, Alan.

Operator: Thank you, again if you would like to ask a question (Operator Instructions) Our next question will come from Luis Willard with GBM

Luis Willard: Yes. Hi, good morning. Thanks for taking my question and congrats on the results. So, I mean, you've talked about this in your remarks and also in the questions but I mean, this current circumstances have forced most companies to search for efficiencies inside the organization and as you've mentioned, Arca is not that the exception. So my question is, could you walk us through some of the most relevant sources of savings that you might have already detected. And do you think they are achievable in the short-term and that will be available for the long-term for Arca?

Arturo Gutierrez: Yes, sure. Thank you, Luis for your question.

I think, that's a very important part of our operation. And from our experience through the integration of companies, I think we have developed this culture that is not searching for actual synergies now on a specific deal, which is the methodology that we built over the years. But making it a constant effort of our operation to identify opportunities and there's always a reason to do that.

I mean, there's always a challenge to face and certainly this year, the biggest challenge is certainly the inflation on some of our main raw materials. I would say, basically aluminum and PET. Those are the biggest impacts. So what we're doing in 2022 with the lessons that we learn in the past years is continue to drive efficiencies in cost, OpEx and CapEx deployment.

So, let me mention a few of those. And many of those actually leverage technology including advanced analytics, so initiatives like the trade promotion optimization, it's very important for how to improve our net pricing. We mentioned the rate, then the mix, but this is becoming much more important now. Packing efficiencies are very important - even Universal bottle provides efficiency there; and, aside from that just packaging material in general, there are many things that we've optimized - strategic procurement and indirect and direct procurement…many things also that leverage new technologies and we keep track of that. This is not just something we aspire to, we have project managers for specific initiatives, also in our go-to-market models, our service model so, there's been savings. Not only about how we serve better our customers but also how we do it in a better cost to serve way.

There's a big project in network optimization and also that leverages new technology of bringing new consultants to provide efficiencies, mostly in Mexico, but also in the US. Plant efficiencies as well, better productivity in our plants, yields, waste, etc. So, there's a list of things there and we have a dedicated team and project coordinator, and then specific individuals responsible across the entire organization in every country and they report directly through routines to me and senior management. So, we make sure that this is part of a culture and from there, there are a number of smaller projects that cascade down and add to a number that becomes significant at the end of the day.

Luis Willard: Alright, thank you. That was very clear.

Arturo Gutierrez: Thank you, Luis.

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

Ulises Argote: Hi, guys. Thanks for the space for questions. So, you've already commented a little bit there on the aluminum hedge, but maybe can you provide an update on the rest of the raw materials and where you're progressing and the levels that you're hedging, and kind of on the back of that question, but any expectation for you guys to increase prices further in the short-term across regions? Thank you.

Arturo Gutierrez: Thank you, Ulises. Well, yes, raw materials as I said that impacted us, mostly aluminum and PET had the main impact, if you look at our margins and erosion of consolidated margin, we could say that all of that would be explained by those two basic raw materials. So as I said, we had anticipated some of that and that is the reason for some of those price increases that are off-cycle. Like, in the case in US. So you look at our margins, maybe Mexico is the only one that's impacted, but consider for Mexico that we had record margins as comps so also take that into account. So the trend is that we will - the reality is that we will continue to face high input costs. So it's important to continue to be price leaders, we're looking for windows to more hedging. We've done some of that and I'll let Emilio explain a bit of those details. But from the perspective of pricing, we will continue to work on different perspectives for pricing, rate, of course the opportunity's there based on new tools and analytics. How we improve our mix, and there are many instances where we have improved our pricing through mix with more returnable packs also more profitable packs in the case of US. As the on-premise market recovers, we also try to improve the mix of that market in the US operation. And as I mentioned, the trade promotion optimization, all those are elements that help us mitigate the impact of raw materials on our margins. And so I'll turn it over to Emilio for some color on hedging.

Emilio Marcos: Thank you, Arturo. And thank you for your question, Ulises. Yes. As Arturo mentioned, the situation has not improved, unfortunately with the current global conflict, we expect volatility in raw materials pricing to continue.

So, we have not been able to increase our hedges, as we still have the same as we mentioned last quarter. We have 50% of our aluminum needs for Mexico and US. We have 35% of fructose for US and Mexico. Also, 95% hedges on sugar for Peru and 27% on diesel for US. All of the hedges, of course, are below the current market prices for 2022. And I should add that the beginning of February we hedged 30% of our core needs for fructose for 2023. So, we hit that on very low levels because corn prices have been going up really, really high.

But even though the hedges are helping us to remain under spot prices, the comps as Arturo mentioned are really high. Because last year we did a very good hedges level. So comps are double-digits on cost.

But thanks to the pricing strategy and, you know, the change of mix, we've been able to offset most of the impact of the contribution margin level. And regarding FX hedges, we already hedged 100% of our needs for Mexico at very good levels below 20 pesos, and in Peru also we already hedged 80% of our needs below for soles. So we're comfortable with those. So as Arturo mentioned keep looking for any opportunities to improve that position.

Ulises Argote: Thank you very much. That was really helpful and congratulations again on the results.

Operator: Thank you at this time. I would now like to turn the call back over to management for closing remarks.

Arturo Gutierrez: Thank you, Katie. And to all the participants on this call, we sincerely thank you for your partnership, and your thoughtful questions. Please reach out to our Investor Relations team for meaningful dialogue and follow up questions. Have a great weekend.

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

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