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Arca Continental 2Q22 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 second quarter and first half of 2022. 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 good morning, everyone.

Let me begin by saying that we are pleased with our second-quarter and year-to-date results. At the halfway mark of 2022, we are delivering consistent, topline performance and seeing solid momentum in our underlying businesses, despite an unpredictable global economy.

Our business reported solid results this quarter, growing total volume by 6.7% and reaching 614 million-unit cases. Year-to-date total volume grew 6.1% with all our regions delivering sequential volume expansion.

Total consolidated revenues rose 16.5% in the quarter and 15.2% year-to-date to $53.4 billion pesos and $99.4 billion pesos, respectively.

Consolidated EBITDA grew 11.0% in the quarter, reaching $10.4 billion pesos. Consolidated EBITDA margin for the quarter reached 19.6%.

Notably, this is the highest EBITDA for a quarter in our history as a publicly listed company, and, for the first time, we surpassed the $10 billion-peso mark in earnings for a quarter.
This performance underscores our strong market focus, our ability to successfully navigate through supply chain disruptions and our disciplined expense management initiatives to offset input cost inflation.

Let me now provide you with an overview of our business performance and highlights for our five markets.

Our beverage business in Mexico maintained its positive momentum, delivering another solid quarter of volume growth, up 5.3%.

This was the seventh consecutive quarter of volume growth for Mexico. Water led all categories, up 7%. Brand Coca-Cola was also up a healthy 4.2% in the quarter.

In June, we reached a historic milestone in our Mexico operation, with volume sales of more than 100 million-unit cases for the first time in a single month.

These outstanding results were due to the resilience of the traditional trade, up 2.8%, and the sustained recovery of relevant channels such as supermarkets and convenience stores, which were up 24.8% and 10.1%, respectively.

Total net sales in Mexico rose 15.1% in the quarter to reach $23.9 billion pesos. Remarkably, our beverage business achieved eight consecutive years of net revenue growth.

Average price per case in Mexico - not including jug water - rose 8.1% in the quarter, reaching $74.17 pesos.

EBITDA increased 6.3% to $5.8 billion pesos in the quarter, representing a margin of 24.3%.

Single serve mix sequentially grew 1.1% in the quarter. Growth in immediate consumption packages was driven by the steady recovery of the on-premise and leisure channels. It is important to mention that there is still an upside opportunity to capture additional volume in these channels as they continue to fully normalize to pre-pandemic levels.

Moving now to our beverage business in South America, total volume grew 15.7% in the second quarter, resulting from solid performance across our three markets.

Total revenue was up 26.7% in the quarter, reaching 9.6 billion pesos, while EBITDA increased 36.7% to 1.7 billion pesos, representing a margin of 17.3%.

Despite high inflation and interest rates dampening domestic demand, our most relevant channels continued to recover.

We are making great strides in the rollout of our B2B platform in the traditional trade. Over 120 thousand customers in the region consistently place orders through our mobile app.

In Peru, volume was up 16.6% in the quarter driven by solid growth in the sparkling and water categories, up 17.8% and 16.7% respectively.

All channels posted outstanding results. The traditional trade was up 1.4%, supported by our affordability initiatives. Wholesale, on-premise, and supermarkets delivered double-digit growth on the back of eased mobility restrictions.

Meanwhile, single serve mix in Peru increased by 4.1 percentage points supported by outstanding performances of core brands Coca-Cola and Inca Kola.

Turning to Argentina, our beverage business continued its solid momentum, growing volume 22.6% in the second quarter, cycling double-digit volume growth from the same quarter in 2021.

Volume growth was broad-based once again and driven by sparkling up 22.1%, still beverages 22.6% and water with 27%.

As for Ecuador, President Lasso declared a state of emergency during the last two weeks of June due to civil unrest throughout the country.

Curfews were also implemented as protesters blocked exits, entries, and ports in Quito and Guayaquil.

Our beverage business in Ecuador posted a solid 8.7% volume growth in the quarter, in the face of this challenging backdrop and the resulting impact on our supply chain.

The Sparkling category sustained its strong momentum with Flavors up 15.4%, driven by Fanta and Inca-Kola brands.

From a channel perspective, on-premise, supermarkets, and traditional trade delivered strong growth, as we continued promoting returnable packages and driving immediate consumption in Ecuador. Single serve mix increased 6.4 percentage points, in line with the sequential recovery of the on-premise channel across the region.

Tonicorp, our value-added dairy business, posted double-digit sales growth in the quarter, driven by solid increases in yogurt, flavored milk, and oatmeal categories.

Despite the shortage of milk resulting from the protests affecting the country, we gained value share in our core portfolio, as we capitalized on the recovery of relevant channels such as schools.

Moving to our beverage operation in the United States, Coca-Cola Southwest Beverages closed out the second quarter with positive momentum, delivering a strong operating performance and sound financial results.

Our revenue management initiatives continued to prove very successful, with net sales growing 13.8%, reaching $932 million dollars, marking the second consecutive quarter with double-digit revenue growth.

Net price grew 12% in the quarter, sustained by strong execution and improved management of our promotional spend supported by our advanced analytics tools and capabilities.

Volume for the second quarter grew 1.6%, reaching 118.2 million-unit cases. All our three major channels posted solid volume growth. We saw a recovery of the convenience retail channel as increased transactions drove revenue growth.

Sparkling soft drinks delivered solid sequential gains, up 1.9%, supported by 12-ounce cans and Immediate Consumption packages.

Coke Zero grew double digits, Body Armor brand grew 18.5%, driven by Body Armor MP and Body Armor Edge.

Package mix performance shifted favorably in the quarter, as the FSOP channel continued to grow, up 3.6% in the quarter.

Our E-commerce sales grew by 33% as we expanded our digital commerce footprint with both myCoke and E-Retailer sales. We have made significant progress in digitalizing customer engagement. More than 19 thousand customers have ordered through myCoke year-to-date. Just in June, 74% of FSOP orders were processed through our eB2B platform.

EBITDA increased 7.4% to $148.7 million dollars, representing a margin of 16.0% and marking the sixteenth consecutive quarter of EBITDA growth.

Looking ahead, due to the volatility in commodities, we are working towards implementing an off-cycle price increase during the third quarter that will help us alleviate pressure on our margins.

To wrap-up the review of our operations, our Food and Snacks businesses posted a double-digit sales increase in the quarter, driven by the sustained recovery of the traditional and modern trade channels in Mexico and Ecuador.

The e-Commerce channel in the US continued its strong performance with over 50% growth versus last year by expanding our online connection between consumers and core brands Wise, Deep River and Carolina Country Snacks.

We are accelerating the deployment of our AC Digital mobile platform across our snacks businesses, with a strong focus on segmentation, promotions, and discount management.

I'd like to close with an overview of our ESG initiatives during the quarter.

As part of the World Recycling Day framework, we announced the third phase of expansion of PetStar, the worldwide leader in food-grade PET recycling. This is an investment of $175 million pesos, to strengthen the collection and recycling infrastructure in Mexico.

I am also proud and honored to say that we were ratified for the seventh consecutive year as part of FTSE4Good index, of the London Stock Exchange, which measures the performance of companies demonstrating strong sustainability and anti-corruption practices, human rights initiatives, and strong labor standards.

Moreover, we were also ratified as part of the ESG index of the Mexican Stock Exchange and Standard & Poor's, which recognizes Mexican companies with best practices in environmental, social, and corporate governance matters.

Our determination to be assessed based on the strictest international standards and sustainability indexes is in line with our principles to operate with transparency and ethics, while creating a positive impact on the environment.

And with that, I will turn it over to Emilio. Please, Emilio.

Emilio Marcos: Thank you, Arturo. Good morning, everyone and thank you for joining our conference call.

Supported by positive volume and our successful pricing strategy, we navigated through the complexity of the macroeconomic challenges in our industry, such as: raw material pricing volatility from inflationary pressures and supply chain disruptions. Despite these challenges, we continue with consistent positive results, delivering double-digit revenue increases along with a solid financial performance.

Now moving on to the quarterly results:

During the quarter and for the first six months of the year, Consolidated Revenues rose 16.5% and 15.2%, respectively, driven by our consistent pricing strategy and market execution delivering volume growth. Considering a currency neutral basis, Net Revenue grew 17.3% in the quarter and 16.2% in a cumulative matter.

Gross Profit, increased by 13.6% in the quarter to $23.6 billion pesos. A 120-basis point dilution in the contribution margin was mostly due to the incremental cost of raw materials. For the 6-month period, gross profit grew 12.9% to $44.3 billion pesos while the gross margin was reduced by 100-basis points for the same reason explained before.

As part of our ongoing business relationship with The Coca-Cola Company, we are committed to enhancing the value we create for our customers in Mexico and will jointly align on investments that will strengthen the system. In line with this commitment, we have reached an agreement for an increase in concentrate price for sparkling beverages in Mexico, which came in effect July 1st of this year.

For the quarter, Operating Income was $8.1 billion pesos, increasing 16.5% against the same period of the previous year. Operating margins remained flat year over year, as inflationary pressures were offset by our commercial initiatives and operational efficiencies.

Operating Income for the January to June period was $14.4 billion pesos, up 17.8% and a 30-basis points expansion in margin compared with the previous year, primarily driven by operational efficiencies. Our SG&A organizational discipline continued to capitalize on lessons learned during the pandemic, driving a 100-basis point reduction in its ratio to sales.

Consolidated EBITDA for the quarter reached $10.4 billion pesos, representing an increase of 11% and a margin of 19.6%. For the first six months of the year, EBITDA grew by 11%, yet presented a 70-basis points dilution, led by the above-stated pressures in the contribution margin.

During the quarter, Net Income grew by 34.9%, a 110-basis point expansion in net profit margin. For the accumulated period, Net Income reached $7.3 billion pesos, 28% more versus the same period of the previous year. Both, quarter and year to date increases were beneficiated by our operating income growth.

Continuing with the balance sheet:

At the close of June, cash and equivalents reached $30.2 billion pesos, while total debt was $50.2 billion pesos, leading to a leverage ratio of 0.5 times. Our strong balance sheet allows us the possibility to evaluate further growth opportunities that will generate shareholder value.

We executed $3.5 billion pesos of CAPEX so far this year, a 46% growth when compared to the previous year. This was driven by reinforcing investments in production and commercial capabilities in line with volume growth and the post-pandemic recovery.

Now let me elaborate on our successful bond issuance completed during the quarter.

On June 10th, we completed the issuance of 4.4 billion pesos in *Certificados Bursátiles*, or local notes. This transaction consisted of two tranches, one for 1.2 billion pesos with a 7-year term at a fixed rate and another of 3.2 billion pesos with a 4-year term at a floating rate.

Despite complex macroeconomic conditions and financial volatility due to high inflation throughout the markets, the bond obtained the lowest interest rates for a corporate issuance in recent history for the Mexican debt market.

While we continue to anticipate headwinds for the upcoming quarters regarding the inflationary environment. We continue to look for Windows to reduce raw material volatility through the consistent execution of our hedge strategy.

Our operational efficiencies as well as our organization’s adaptability, have helped us navigate first through the pandemic and now during the global macroeconomic complexities our industry is experiencing. We will maintain our commitment to protect profitability and prioritize cash flow management to preserve and sustain our positive results, in both delivering P&L results and Balance Sheet strength, thru the year.

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

Arturo Gutierrez: Thanks Emilio,

We are pleased with our progress in the first half of the year, and we are grateful for the commitment from the stakeholders across our ecosystem that contributed to our results.

Despite a complex macro-outlook that is pointing to an increasingly challenging backdrop of slow growth, volatile commodities, and inflation, we feel good about the rest of the year.
We are taking the appropriate actions to manage the ongoing volatility, using revenue growth management capabilities and supply chain productivity levers to achieve a healthy balance between volume, pricing, and profitability.

We remain confident that the long-term dynamics of our industry are promising, and we are committed to driving execution and staying at the forefront of evolving consumer needs. And we will do so by ensuring that we always place our highest priority on creating shared value with our customers, and for our shareholders.

We will continue to build on our strong strategic partnership with The Coca-Cola Company. Our two companies continue developing shared goals on a clear and collaborative strategy for sustainable long-term profitable growth in our markets.

We will also continue actively exploring how technology can transform the customer experience, how we can generate new revenue sources, and how we can become more efficient in our processes.

So, to sum up, our growth story remains very robust. The strength of our balance sheet, our strong cash-flow generation, and our dedication to quickly adapt to the ever-shifting needs of our customers and consumers will allow us to continue to generate consistent quality organic growth, and at the same time seeking opportunities for expansion and product diversification.

And with that, I would like to open the call for questions. Operator, we are ready, please.

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 Marcella Recchia with Credit Suisse. Your line is now open.

Marcella Recchia: Hi, Emilio, Arturo, thank you for taking my question. I have two quick questions. The first one is that over the last couple of years, you have delivered continuous gains in efficiency, which had optimized your sales to expenses ratio accordingly and this quarter was not different again. My question is what has been the main drivers of such improvement and how much more room do you still going forward? That is my first question.

The second question is that during the first half you already printed a 15% topline growth and 11% EBITDA growth which are well ahead of the guidance previously provided. So my question is, if we could expect an upward revision to the guidance? Thank you so much.

Arturo Gutierrez: Thank you, Marcella. Let me take your first question and then I'll turn it over to Emilio to address your second point. Well, yes, we have been working as a continuous effort on efficiency in our organization throughout the last few years and there is always justification to make an additional effort to do that. So that's become part of the culture that we have. We have separate metrics, we even have a separate function within the organization to coordinate that as kind of a project management office.

So we also have capitalized on the lessons that we've learned throughout the integration of businesses and then during the pandemic I think some of the learnings there of things that we really could adjust on a definitive basis after the pandemic were also very relevant. Let me give you some examples of what we're doing. It's not only at the SG&A and OpEx level, it's also at the OGS level that we are working on and even pricing, trade promotion optimization is a good example of things that are reflected in the topline, but work as an efficiency project. The digital initiatives also have resulted in many opportunities to optimize manufacturing is a great example of some of the platforms based on analytics that have helped us make our manufacturing more productive. And then once the best practice is identified, we have a methodology to make sure it's shared, it’s implemented across the organization. We have the recognition of people that have come up with the best ideas.

Let me give you a great example of one of those projects that has had a significant impact and still really not rolled out across the organization. We are using a technology that was originally used for submarines many, many years ago. And we have -- there is the adaptation of that technology to improve dilution of carbon dioxide in beverages during the filling process. So what that means is that we can now fill at a much higher temperature and that saves energy. That project was recognized by The Coca-Cola Company globally as one of the great innovation projects. The technology is not ours, but we've been able to adapt that to our processes and that has also the benefit for reducing our carbon footprint. So from like those projects we have a long list that we continue to pursue and it's, I would say, a mindset that it's not really that you reach an optimal level. You find the technologies, you find the processes and you optimize based on your scale as well.

So we believe that is a continuous effort. So we have very precise targets that we want to accomplish as well in terms of opportunities. We've identified opportunities in Mexico, not all with the same degree of certainty and also in the rest of the operations that add up to probably several hundred million pesos in this year. So it become significant once you add up all the projects. So I'll turn it over to Emilio for the second part of your question.

Emilio Marcos: Yeah. Thank you, Arturo, and thank you, Marcella for your question. Well, as you know, we have given a number between 6% to 8%, but thanks to all the initiatives and the pricing and all that we were double-digit, mid double-digit right now. We are not -- we haven't given a number, a specific number because the second half of the year will be with higher comps and volatility is still there, macroeconomic situation, but we could say that we're going to be for sure on the double-digits and maybe between I mean low double-digits on this, but we'll maybe work on that number on the next quarter.

Marcella Recchia: Perfect. Thank you so much, gentlemen.

Arturo Gutierrez: Thank you, Marcella.

Operator: Thank you. Our next question will come from Ben Theurer with Barclays. Your line is now open.

Ben Theurer: Perfect. Thank you very much and good morning, Emilio, good morning, Arturo. Congrats on the results. The question for Arturo and you've mentioned it on the call. The record sales during the month of June. I mean I suspect it had a lot to do with the heat wave that's been impacting the region and obviously there has been a lot of news around scarcity of water and the requests from the Mexican authorities to some of the bottlers to engage and support. Can you share maybe a little bit of context on what you're seeing in the market. How you work together with different authorities and really solve for the needs here given the scarcity of water that we are having in the region. Thank you.

Arturo Gutierrez: Yeah. Thank you, Ben. Well, certainly it's been a great quarter in terms of growth and a great month of June, as I mentioned, because even with the challenges and disruptions to the supply chains we were able to reach a record volume. The volume in Mexico surpassed 100 million unit cases for the first time ever. So we're proud of that.

I would say, first, there are many things that we're doing in the market and sometimes you don't really connect with some of the capabilities that we're deploying in terms of how much of that is resulting in better growth, but now we have a clear picture of how our digital deployment has been impacting growth as well. The AC digital platform for example has grown significantly and there's clear correlation. So there are many things that I think we are seeing the benefits and reaping the benefits of that at this point.

The water scarcity situation is a big crisis in the Northeast of Mexico. Also it's worth mentioning that was the region where we have been growing the most recently. So the market is very solid, but we have been facing this challenge and we have been supporting the government and the community to face the challenge. As you know, in the aggregate industries in the state would consume a small fraction of concession water. It's around 4%. But we know that we need to play a role in solving the crisis. So we are supporting the government and the community. The equivalent of the water of the projects that we've collaborated with, it's more than three times our concession water volume in the state of Nuevo Leon. So that's for us very, very important as we sustain our commitment with the community. We have rehabilitated 15 wells operated by the state. These are not ours, these are state-owned watering wells that supply the municipal drinking water infrastructure and we've also assigned temporarily some of our concession water to supply clean water to public infrastructure. So we have been again very aligned. We have made commitments jointly with the local industry and that will address a good portion of the water deficit in the state currently.

On the other hand we, as you know, have been leading in terms of water-use efficiency. Our efficiency indicator is around 1.5 liters of water per liter, which is, it's something much better than the average of the industry. So in sum, we are convinced that all of these efforts in a coordinated manner between government, the private sector and the community is really the best route to move forward from the crisis and especially avoid other crises in the future, also working on the longer-term solution of this type of crisis.

Ben Theurer: Okay, perfect. Thank you very much.

Arturo Gutierrez: Thank you, Ben.

Operator: Thank you. Our next question will come from Bernardo Malpica with Compass Bank. Please go ahead.

Bernardo Malpica: Hi, Emilio, and Arturo. Thank you for taking my question. Just a quick question related to the last one. So I just want to be clear I mean it was very helpful. But so I mean the President comments regarding a potential fleet of operations to save water in the North are not a worry, that's correct? That would be my first question.

Arturo Guttierez: Yeah, we actually don't see any risk to the continuity of the business. As I said, we've been working very closely with the government in this immediate and long-term solution. So we're comfortable in that regard.

Bernardo Malpica: Perfect. Thank you so much. And I have another question. And we saw an even bigger margin reduction in Mexico than we saw during the last quarter. And also there is zero margin inflation and where are you still seeing the biggest cost pressure and where do you see the biggest cost pressures going forward. And just in addition to this one, will you continue with the pricing strategy for the second half to mitigate this cost pressure environment? Thank you.

Arturo Gutierrez: Yes. Thank you, Bernardo. Yes, let me give you some general comments and maybe Emilio can expand. In Mexico, well, the biggest pressures come from raw materials, as you know, they continue to challenge our margins and the dilution basically comes from increases in PET and sweeteners. We have the positive volume trends, the OpEx discipline and also the hedges that have somehow mitigated that as well. So, but, the most important way to mitigate that is precisely with our revenue management strategy. Our price increase at the end of March helped, then we had a second price increase that has been applied at the beginning of the month of July. That's actually not reflected in the numbers that we reported. And so we're looking forward to continue to protect the margins as much as we can for the second half of the year. So we're going to continue to assess additional price increases and also optimize our discounts in the market.

Bernardo Malpica: Well very helpful. Thank you.

Arturo Guterriez: Thank you, Bernardo.

Operator: Thank you. Our next question will come from Thiago Bortoluci with Goldman Sachs. Your line is now open. Thiago, your line is open. Please make sure your phone is not on mute.

Thiago Bortoluci: Yes, hi. Good morning, everyone. Arturo, Emilio, Arca team thanks for the presentation. Congrats on the results. We also have two questions. During the opening remarks Emilio mentioned an updated agreement with KO regarding concentrate prices. I would just like to explore a little bit more what could be the implications for gross margin and COGS going forward with the update terms.

And the second one is a broader view on the momentum in Argentina right? Performance especially volumes have been solid, but macro has been deteriorated from a very weak base rate. So given persistently high inflation, the effect of depreciation. What are the latest trends we're seeing from a consumption point of view and what could we expect from the region going forward and those are the questions. Thanks.

Arturo Gutierrez: Thank you, Thiago. Well, with respect to the concentrate prices, we did have an additional increase as Emilio mentioned that was implemented effective as of July and well this is aligned with our agreement with The Coca-Cola Company as we've said. This agreement has many other elements aimed at investing together and strengthening our market. So maybe, Emilio can expand on that.

Let me talk about Argentina for a second. Well certainly the environment is challenging, but the consumer environment has been very favorable and we also take into account that we are recovering from a market that has not been performing as we had expected in the last few years. So now we've had very good growth. Again we are capitalizing on many of the things that we have been doing in the market, especially our affordability strategy - I would highlight that through both multi-serve returnable and single-serve packages, managing pricing strategies in line with inflation, which is very important in Argentina and even with that, we continue to grow. We've also accelerated the expansion of digital in Argentina in the traditional channel and that's very important. We have I think about 21,000 active customers that are ordering through our digital platform.

So if you look at the categories, all the categories are growing and all the channels look very healthy - traditional channel has grown 23% versus the previous year and this is a positive trend that has continued over time. Also modern channel is growing more than 20%. So we have mostly double-digit growth in every channel year-to-date, which is quite remarkable. We also have a similar growth in all regions. So growth is very consistent and categories as well. Again we're capitalizing on a better consumer environment, but we are also capitalizing on many of the fundamental things that we have been doing in the market for some time with focus on affordability I would say. So we are looking to probably reach a level in the market -- volume in the market that's close to the highest that we've had in previous year. So we are very satisfied with that. And I'll turn it back to Emilio on your first point.

Emilio Marcos: Thank you, Arturo. I think it's important to mention that part of this agreement, as you said, is that we're going to invest together in Mexico to strengthen and improve the way that we serve to our customers. That's one of the comments. The other one is that the increase is similar to last year's increase and we've been able, as we done in the past to offset that increase through pricing and some other initiatives like promotion optimization. So we don't expect an impact on contribution margin. And the last thing that I would like to mention is that we don't expect any incident adjustments in the near term. So that's also important to consider.

Arturo Gutierrez: Thank you, Thiago.

Operator: Thank you. Our next question will come from Sergio Matsumoto with Citibank. Please go ahead.

Sergio Matsumoto: Yes. Good morning, Arturo, Emilio and Pepe. Just taking it further your comments on the agreement with KO. You also mentioned in your prepared remarks, Emilio you mentioned further growth opportunities. And Arturo, you mentioned expansion and product diversification. Can you connect these comments to the Coke agreement and perhaps anything interesting that you're able to comment at this time with regards to those opportunities? Thanks.

Arturo Gutierrez: Yes, Sergio, and thanks for your question. That's very relevant. There is a clear connection with the agreement with The Coca-Cola Company to pursue these opportunities and evaluate potential growth across Latin America in categories that would complement our portfolio. Other beverage categories in alcoholic beverages. As you know, this new agreement with Coca-Cola will align us in, not only in our core business, in the economic model of the core business and the growth projections and agreement on investment for growth in the current beverage business, but also to pursue other opportunities, leveraging the capabilities that we have in the market. Both the logistical capabilities, the go-to-market infrastructure and the digital capabilities that we're building. This agreement also is an alliance on the digital space and so on. So it kind of covers the whole spectrum of the business and that's why we believe it's really transformational. We have actually agreed on all the aspects. We have a conceptual agreement and everything. We're just working on drafting of documents for that agreement. But we're already working as partners in analyzing these opportunities, particularly beer and other alcoholic beverages. As you know, we have run a pilot in Ecuador for beer distribution and we plan to do similar pilots in the rest of Latin America.

Sergio Matsumoto: Okay, great. And if I may, another question. Could you comment on the state of the reopening in the US and Mexico. In your prepared remarks, you have mentioned FSOP and immediate consumption and single serve several times, and just wondering if what you see today as consumption occasions may have changed through the pandemic and any remaining opportunities with respect to the reopening? Thanks.

Arturo Gutierrez: Yeah, Pepe, maybe can give some details. But in general, I would say that the on-premise channel, even though it's been growing - it's in a very positive trend in all markets including the US and Mexico - still have some upside because it's not fully recovered, just based on a number of outlets and volume as you compare that with the pre-pandemic levels continues to be an opportunity. So I think that would be the summary of where we think it's a -- there is still an upside and some of the occasions have changed, but the trend is very, very positive.

Jose Borda: Yeah I think supporting what Arturo is saying. We've been growing. We've grown 17% in the on-premise channel, but, as Arturo said, it's still below pre-pandemic levels, but we're seeing month over month improvement. So this is a positive tailwind for the next quarters. And obviously this has helped us, among other things, to boost our single serve performance that affects positively the price mix as consumers gain mobility and they are looking for more convenient packaging. We have captured this trend, for example, launching the 250 milliliter PET non-refillable package in all our sparkling and stills portfolio and many other initiatives to capture these trends. So this is improving, but there is still space for improvement. There are still some customers that need to be reopened and we see this as a positive tailwind for the next months.

Sergio Matsumoto: Thank you.

Arturo Gutierrez: Thanks, Sergio.

Operator: Thank you. Our next question will come from Isabella Simonato with Bank of America. Your line is open.

Isabella Simonato: Hi. Good morning Arturo, Emilio. Thank you for the call. Good morning, everyone. Following up on the previous question about the mix and the momentum, right. It's interesting to listen that you guys still see upside on the on-premise channel, but I wonder how that could be impacted or could be delayed, right, by a tough macro and high inflation, right. I understand it's below pre-pandemic. But also we see a tougher consumer environment in general, right. So if you could explore that in the US and Mexico mainly how you guys are expecting a little bit in the mid-term, right, performance of mix of channels and packaging? And also in light of this momentum right for macro, I mean, we saw government in Mexico doing some changes that didn't properly affect you. But any expectation of another measure or something that we should monitor or you think that what it's announced is going to be what's out there? Thank you.

Arturo Gutierrez: Yeah. Thank you, Isabella. With respect to the on-premise and the impact of the macro situation, we really have not seen that. I mean we probably going to see some slowdown in the future and we're going to be expecting maybe that growth that we've seen recently to come to more moderate levels, but we've seen so far and even with the inflation environment that we've seen in the first half of the year, the volume in the on-premise has been growing consistently as Pepe is saying. I think it's probably because the baseline that we have from last year is still fairly low. Again in terms of the number of outlets, if you think about the US were still, were not even at 80% in that metric. There is still an upside we believe. Although certainly growth is going to normalize in the second half of the year, but we haven't seen that impact so far. And with respect to Mexico, we always evaluate the many risks that we have operating in Mexico and in any other country. But we are not anticipating any regulatory measure at this point that we should be specifically concerned about.

Isabella Simonato: That's very clear. Thank you.

Arturo Gutierrez: Thank you, Isabella.

Operator: Thank you. Our next question will come from Alvaro Garcia with BTG. Your line is now open.

Alvaro Garcia: Good morning, gentlemen. Thanks for the space for questions. One clarification and one question I was going to ask about Yomp and sort of the digital space and how it figured into this new concentrate agreement, but you mentioned I think that it's a separate documentation and a separate agreement. I just wanted to confirm that first?

Arturo Gutierrez: You mean that it's a separate agreement?

Alvaro Garcia: Yes.

Arturo Gutierrez: Well it's a – the documents have, you know, segments and sections for the different aspects of our alliance, but at the end it's a comprehensive agreement that we have with The Coca-Cola Company that includes new opportunities in beverages, that includes a digital alliance, that includes also the relationship in terms of the economic model of the core business. So we view that as a single agreement and it's all connected. I mean it can't be separate. It's a unified contractor agreement and the relationship that we have.

Alvaro Garcia: Okay. And just, I wanted to ask about still beverages as well as outlook for still beverages sort of in the context of a potential slowdown. How do you think - maybe it's a better question for Pepe. How do you think about the outlook for still beverages. How defensive they are relative to your sparkling portfolio. The likes of Monster, the likes of BodyArmor, the likes of your different still product relative to colas. Thank you.

Jose Borda: I think Alvaro so we see huge opportunities in still beverages, huge opportunities for growth as Monster as you mentioned, BodyArmor are growing, the value is growing. What we've had in still beverages is some supply chain issues that have affected some global supply chains and we are working fast with The Coca-Cola Company to see potential reformulations, localization of ingredients and capture that volume. But the demand, on the demand side, still beverages are -- have a very healthy demand and we see that continuing for the near future.

Arturo Gutierrez: If you look at Latin America and the mix of still beverages and you compare that with more developed markets, you know our own market in the US. You can clearly see that opportunity and where this is moving.

Alvaro Garcia: Thank you very much.

Arturo Gutierrez: Thank you, Alvaro.

Operator: Thank you. Our next question will come from Luis Willard with GBM. Your line is now open.

Luis Willard: Hi, guys. Good morning. Thanks for taking my question and congrats on the results. So it's just a quick one. In your opening remarks, you mentioned the, I hope I'm not wrong that this -- you had over 20% growth in supermarket volume and 10% in convenience in Mexico. So there is, of course, a component of the weather, but do you see this type of growth as sustainable in the long run and can you share with us a bit more detail on this performance? Thank you.

Jose Borda: Yes. Thank you, Luis. Yes, we've seen, for example in Mexico, we've seen 15% growth in supermarkets and in convenience stores. But if you look at volumes versus pre-pandemic levels the convenience store channel -- the on-premise channel has not recovered yet, but the modern trade is growing very similar to a traditional trade around 10%. Remember that the modern trade, especially convenience stores, were specifically affected during the pandemic, while the traditional trade kept on growing. So convenience stores are going back to -- are going back to pre-pandemic levels, supermarkets are, yes, are growing very healthy in the short-term. But that is also something that is specific from this quarter and we think that the growth will continue, but it will de-accelerate a little bit in the next months becoming more in line with the other channels.

Arturo Gutierrez: There is some catching up certainly that we're seeing.

Luis Willard: Yeah, absolutely, perfect. Second and if I may a quick follow-up on another topic. I mean, how do you feel on the revenue management strategy going forward, especially given the strength that we're seeing in volumes so far?

Arturo Gutierrez: Well, as you know, this is very important, considering also the raw material environment, we've been using pricing as a key topline driver and we're leveraging these capabilities that we're building over time of segmentation, of brand price pack architecture and very importantly of management of discounts. So our strategy continues to be increased prices in line or above inflation. Raw material inflation can be higher at some point. But again we believe that raw materials in the second half of the year will have a more favorable comparison. So we had some carryover and price from last year especially in Mexico and the US So in those two markets, which are main markets, we were growing our price at or above inflation. We plan to continue to do that as a balance from true rate increases - a positive mix - we have a positive change in mix in both countries, as single serve is growing. And then we also have, in the case of the US, a shift in volume to high profit per case packages as a strategy, and we have also the price increases - we have an off-cycle price increase plan in the US for August. And as I mentioned, an additional price increase in Mexico that was implemented this month. So the objective continues to be the same and to grow prices in line with inflation or above.

Luis Willard: Alright, thank you.

Arturo Gutierrez: Thank you, Luis.

Operator: Thank you. Our next question will come from Camilla Azevedo with UBS. Your line is now open.

Camilla Azevedo: Hi, good morning, everyone and congrats on the results. We have a question on your view on sector consolidation. So you have a quite robust balance sheet and sector valuations appear quite low. So just curious if you have been out there looking for something in the US or elsewhere in LatAm?

Arturo Gutierrez: Thank you. Camilla. That's a very important question. We, as you know, we've been open to analyzing attractive opportunities that could arise either from the current situation or in any of the markets where we operate in the Americas.

The premise is that we need to find a way to create value in the transaction. We don't feel to be pressured to rush into any deal and many things have to be aligned, sometimes aside from the economic value creation, we need to know that we need to find way to align ownership of the different companies and franchises to move into a deal. So I think at the end of the day, you know, this economic story prevails, but you got to be patient and disciplined, and that's what we're trying to do. If you look at the value that is, that can be captured or unlocked from the current fragmentation of the franchise system across the Americas, I think that's tremendous. But it's, again, you need to align more than just the economic models many times. So we are working on that as well. But we think that it's just normal trend of the industry into more consolidation just for looking at the number of bottlers that you have in Latin America and in the US as well.

Camilla Azevedo: Thank you.

Arturo Gutierrez: Thank you, Camilla.

Operator: Thank you. Our next question will come from Carlos Laboy with HSBC. Your line is now open.

Carlos Laboy: Yes, good afternoon, everyone. Arturo, different bottlers seem to have different views on what multi-category model is right for them. Are you philosophically inclined to move toward a total beverage model with beer, spirits etcetera? Or are you more inclined to pursue arrangements with a narrow schedule of brand suppliers or go broad I mean petfood, diapers etcetera. Where do you philosophically sit on multi-category efforts and related to that question is, is this an LTRM agreements that you've signed with Atlanta and are you operating under the same or a different profit split and incidence price adjustment arrangement in Mexico and Argentina than KOF now?

Arturo Gutierrez: Thank you Carlos. Let me talk first about the first part. What we believe is that we have an infrastructure in our go-to market that can serve more than just the categories that we are distributing and commercializing at this point. If you think about us as a bottler and not the owner of the core brands - what do we do, we actually connect strong brands with the customers and the consumers in a very effective way. And I see that not as in a logistical way but in an effective way in terms of account development in terms of having the right dollars in the market and actually building brand value as well in those categories. So that's what we are. Historically we have focused on, first on sparkling beverages, then we transitioned to water, still beverages. So I think it's a natural expansion to go into other categories.

But we have not a preconceived idea which of those would make sense and in what combination. We might - we have to analyze this by the building blocks of our go-to market model. So there is an order taking effort, there is an account development effort, there is a logistic effort of delivering, there is an auditing effort in the market. So there are number of things that can be combined in many different ways. So we do believe that there is an opportunity for expansion if you think about those building blocks and how they can be aligned in many, many different ways for different categories. So for some categories order taking might be as far as we can go. In other categories, I think it's going to be very similar to what we do with Coca-Cola.

And this is an experimentation that’s been going on in our system for maybe 15 years since we’ve had Del Valle in the operation. And we're going to continue to do that. And the good thing now is that The Coca-Cola Company has an open mind to explore that as well. We're going to share the profits. But it's an open mind that did not exist years back. So that's where we stand at this point.

The agreement is a precondition to do that. The new LTRM, it's not signed yet by us. But we're pretty much aligned on the concepts. It's just a matter of the drafting of logistics. That agreement is going to be similar to the other bottlers for Latin America. We have obviously a different relationship in the US. And this is also very much aligned to what we had in Mexico and they were agreed in 2016 in terms of the economic model for Mexico. So we're going to expand that to South America with adjustments that I think are positive and good for us as a bottler and we are going to include these other aspects in the agreement that cover other categories and digital as well.

Carlos Laboy: Are you currently operating under different incidence price adjustment arrangements in Mexico and Argentina than Coke FEMSA?

Arturo Gutierrez: Yeah. In Mexico, we have an agreement with The Coca Cola Company, we don't know exactly the terms of agreements with other bottlers. We have an agreement for Mexico and we have a different agreement in South America and they're going to be all in line in the same model going forward.

Carlos Laboy: Thank you.

Arturo Gutierrez: Thank you, Carlos.

Operator: Thank you. Our next question will come from Felipe Ucros with Scotiabank. Your line is now open.

Felipe Ucros: Good morning, Arturo, Emilio, Pepe and team. Thanks for the space for questions and congrats on the results again. I wanted to explore a little bit the question of how do we manage pricing and revenue growth management as well when commodities are coming down and it feels like it's been so many years for quantities going up that eventually it's going to come and we've had a little bit of that over the last month and a half, but still historically high prices. But you know let's assume that over the next two to three years commodities start coming down, start normalizing to the averages we had before the pandemic. How do you think about pricing on the way down and how do you think about revenue growth management specifically price pack architecture where you know within our kind of portfolio that's a lot wider with smaller packages. Do you reverse a little bit of that to have that level back again when commodities are rising or do you intend to keep everything that's gained on those fronts. How do you strategically think about that?

Arturo Gutierrez: Yeah. Thank you, Felipe. First, I would say is that our pricing approach is not really based on commodity price, it's not the pass through of commodities. In fact this year raw materials have increased much more than our prices in most of our markets. So it's a different methodology quite sophisticated based on competitive environment on opportunities, on elasticity, on segmentation as well. So we're going to continue to do that and take advantage of opportunity, certainly a more favorable commodity environment may create a different competitive situation in the market. So that translated into a different approach based on the competitive situation, but not on the raw material pricing in itself.

So the model actually addresses our share of market, our growth expectations, our development of certain categories and also how well we can segment the market and grow the particular channel. So the management of promotions, for example, I think that is completely separate from the raw materials environment - it's an analytical tool of the promotions that we're making and discounts in the open market, how effective they are, what is the return on investment, if you may, on those small promotions that we carryout week by week. So I think that's going to, we're going to continue to refine those capabilities independently from the raw material environment.

Felipe Ucros: So, theoretically, I guess if you'd like to keep a lot of this in place and continue managing things how you have thus far and raw materials were to plunge then we should see a very steep expansion in margins?

Arturo Gutierrez: It depends. Again, go back, it depends on the competitive environment. Yeah, but certainly if you talk about raw material by themselves. I think the pressure certainly going to ease in the second half of the year as Emilio explained and we're going to see a more favorable comparison. But again pricing has to take into consideration some of the factors.

Jose Borda: And Felipe just to your question if the competitive environment is that we need to reduce some prices, we will do it, we won't have any problem with that. Obviously, the easiest way to manage that causing less disturbance in the channel is to increase promotional activity that at the end is what generates that whole price. But, so we would, first, increase promotional activity. And if we have to adjust prices down, we will do it. And as Arturo said, it will depend on a balance equation between market share, between growth, there's some opportunities in volume.

Felipe Ucros: Okay. Now that's very clear on how you think about it on the way down.

And then let me ask you a follow-up on the pilots and that's maybe a little more for you, Pepe. But you've announced a few pilots over the years. I'm just wondering if this is an absolute on a couple of these, specifically interested on the returnables pilot in El Paso?

And then on Yomp, you've been talking a little bit about digital B2B outside of Mexico. And I just wonder how much of that came through sectors with the broader portfolio that we're already piloting in Northern Mexico where I know you already have more than like 24 CPG brands listed on Yomp. Just wondering how much of that is already being kind of experimented on in Latin America or if the digital B2B that you guys mentioned in those countries is mostly focused on Yomp's portfolio at this point?

Jose Borda: Thanks, Felipe. So let's try to do this in parts. Regarding the pilots, multi-category pilot and to Carlos' question before, we are experimenting with many different things. As you know here in Mexico, we are experimenting with a full portfolio, 24 close to 30 companies, a multicategory approach. In some other places, as in Ecuador, we are experimenting with beer in our trucks in our whole system, and the most important thing is that as a system we are learning from what every bottler is doing - they are independent pilots - but we share learnings and we are looking for the best solution that suits every market. If you ask me, I see order taking for multicategory is something that we can definitely do. We are still working on which is the share of wallet that we want to have or that can maximize a relation with the customers and our profit, where are synergies in the warehousing and which products should be in its trucks or not, FEMSA is trying something, we are trying something, Andina is trying other things. So we are all learning of what every other one of us is doing.

Arturo Gutierrez: And with respect to returnables in the US, just to mention Felipe, this is a long-term initiative and we're in the first stages. This is just about 125 customers - some in home market and some of the on-premise market. So the early adoption numbers are very promising for both customers. There are a number of things that we need to figure out if we want to expand this further. But this is an interesting project and interesting learning so far. So we are using this opportunity as an exploration of this possibility for the US market in the future.

Felipe Ucros: Okay, that's very clear. Thanks for the update guys.

Jose Borda: Thank you.

Arturo Gutierrez: Thank you, Felipe.

Operator: Thank you. This does conclude today's Q&A. I would now like to turn the call back over to management for closing remarks.

Arturo Gutierrez: Thank you. I want to thank everyone for your time this morning and your continued interest and trust in our Company. We look forward to speaking with you again soon and have a great weekend – enjoy your weekend, thank you!

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

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