Equity / Large Cap. / Consumer Durables

Arcelik

2/5/2019

Company Update

BUY

Upgraded to BUY on improving margins and WCR

Upside Potential* 28%

We revised up our 12-mth target price for ARCLK as TL24.88/share up from previous PT of TL17.48/share by revising up our EBITDA margin estimates and revising down our WCR assumptions based on company's successful 4Q18 financial results and forward guidance, 0.5ppt downward revision in our € denominated risk free assumptions and carrying forward our DCF valuation for three months. As our revised PT now offers 28% upside potential, we upgrade our recommendation to BUY from HOLD.

The stock trades at 15% discount at 2019E P/E of 11.1x and 31% discount at 2019E EV/EBITDA of 5.7x compared with its international peers' average of 13.1x and 8.3x, respectively. Looking at 5-year historical forward multiples based on Bloomberg, ARCLK trades at 21% average discount based on its both average historic forward EV/EBITDA and P/E with respect to its peers.

Top-line growth driven by international operations We project Arcelik's consolidated revenues to reach to TL33bn in 2019, up by 23% YoY, broadly in-line with company's top-line growth target of 25%. Despite expected 10% contraction in Turkish WG market in 2019, better pricing level on average coming from high base year effect in 4Q18 is expected to result in 15% revenue growth in Arcelik's Turkey operations. The Company projects global WG market to grow by 2% in 2019 over 2018, while targeting to outgrow the market in unit terms. We assume Arcelik's international revenues to grow by 25% in 2019 on mid-single digit volume growth thanks to higher contribution of Romanian operations (new washing machine plant became operational in 2019) and ASEAN operations, m/s gains in operating markets and positive currency impact, where we forecast ca15% depreciation of TL on average against hard currencies in 2019.

EBITDA to increase ahead of top-line growth Arcelik's consolidated gross margin improved to 31.8% in 2018, up by 0.6ppt YoY, thanks to price adjustments in some major markets and support from easing raw material prices. Indeed, metal prices index and plastic prices indexed declined by 6% and 9% YoY in 2018, respectively. We believe downward trend in commodity prices will continue to support Arcelik's margins in 2019, especially for 1Q19 and 2Q19. Indeed, Arcelik management targets ca20bps improvement in its consolidated gross margin in 2019 over 2018. In addition, the Company aims for further 20-30bps decline in its opex/sales in 2019 over 2018 as its tight control on marketing expenses will prevail. We penciled in 10.5% EBITDA margin for 2019 in-line with company's guidance and higher than 10.1% recorded in 2018. We project 27% EBITDA growth in 2019 over 2018 ahead of 23% estimated revenue growth.

Is 2018YE WCR/Sales ratio sustainable? Arcelik's WCR/sales dropped to 28% in 2018YE down from 30.3% in 2017YE thanks to TL appreciation, strong collection performance, inventory depletion in TVs and declining share of Turkey operations in total revenues. Sharp depreciation of TL resulted company's WCR/ sales ratio to hit 35.1% in 9M18-end, as balance sheet items booked in end-of-period rates but income statement items booked in average period rates. The case reversed as TL appreciated 4Q18-end over 3Q18-end. The Company reflected the rapid rise in interest rates to its credit sales to dealers in 4Q18, resulting in shorter collection period for Arcelik. Lower share of Turkey operations on weak domestic demand also supported the decline in WCR in 4Q18-end as Turkey operations are main culprit for high WCR for Arcelik. Arcelik management targets its WCR/sales to be 30% in 2019.

Dividends For the last ten years, Arcelik has an average dividend yield of 3.7% with an average dividend pay-out ratio of 48%. Based on the assumption of 40% dividend pay-out ratio in 2019 lower than 50% in 2018, we project Arcelik to distribute TL340mn dividends in 2019, corresponding to 2.6% dividend yield.

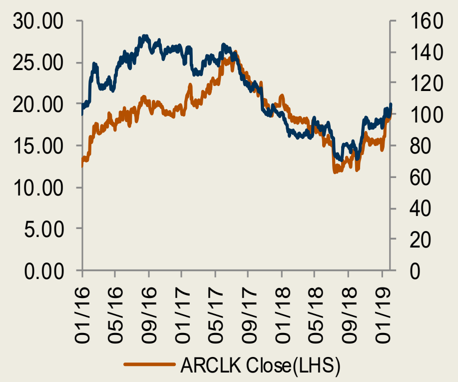
Ticker		ARCLK

Stock Data	TL (₺)	US$
Price	19.46	3.74
Target Price	24.88	4.15
Prev.TP	17.48	3.12
Mcap (mn)	13,150	2,525
Float Mcap (mn)	3,286	631
Avg.Daily Volume (3M, mn)	38.0	7.1
No. of Shares Outstanding (mn)		676
Free Float (%)		25

Multiples	2017A	2018A	2019E
P/E	15.6	15.4	11.1
P/BV	1.9	1.6	1.5
EV/EBITDA	10.3	7.2	5.7

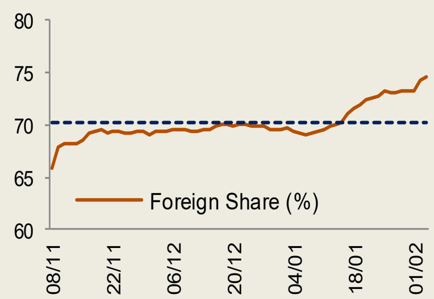
Price Perf. (%)	1 Mn	Ytd	12 Mn
TL (₺)	29.0	23.2	3.9
US$	34.7	25.1	-24.8
Rel.to BIST-100	14.2	9.8	18.5

Price / Relative Price



52 Week Range (Close TL)	3.76	6.89

Foreign Share (%)	Current (%)	75



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Arcelik

Shareholder Structure (%)	
Koç Holding Anonim Şirketi	40.5
Other	36.7
Koç Holding Emekli Ve Yardim Sandiğivakfi	5.1

Company Description

Arcelik is a leading household appliances producer in Turkey with a domestic market share of c.50% as of 2011, ranking as third largest appliances company in Europe. Arcelik offers products and services with 11 different production facilities in four countries (Turkey, Romania, Russia and China), its sales and marketing companies all over the world and its 10 brands (Arçelik, Beko, Grundig, Altus, Blomberg, ElektraBregenz, Arctic, Leisure, Flavel and Arstil).

Income Statement (mn ₺)	2017A	2018A	2019E	2020E	2021E
Net Sales	**20,841**	**26,904**	**32,981**	**41,439**	**49,475**
Gross Profit (Loss)	**6,506**	**8,546**	**10,543**	**13,315**	**16,039**
Operating Expenses	5,134	6,509	7,905	9,899	11,795
Core Operating Profit	**1,372**	**2,037**	**2,638**	**3,416**	**4,244**
Non-operating Income (Exp.)	340	600	181	143	133
Profit (Loss) from Subsidiaries	39	12	14	16	18
Net Financial Income (Exp.)	-931	-1,707	-1,508	-1,707	-2,121
PBT	**821**	**949**	**1,325**	**1,870**	**2,275**
Tax Expense (Income)	-24	94	132	280	410
Minority Interests	2	4	5	5	6
Net Profit	**843**	**852**	**1,188**	**1,584**	**1,860**
NOPAT	1,413	1,836	2,374	2,904	3,480
EBITDA	**1,920**	**2,727**	**3,462**	**4,342**	**5,256**

Growth & Operating Perf.	2017A	2018A	2019E	2020E	2021E
Growth					
Net Sales	29.5%	29.1%	22.6%	25.6%	19.4%
EBIT	14.5%	48.5%	29.5%	29.5%	24.2%
EBITDA	17.3%	42.1%	26.9%	25.4%	21.0%
Net Profit	-35.2%	1.0%	39.4%	33.4%	17.4%
Operating Performance					
Gross Margin	31.2%	31.8%	32.0%	32.1%	32.4%
EBIT Margin	6.6%	7.6%	8.0%	8.2%	8.6%
EBITDA Margin	9.2%	10.1%	10.5%	10.5%	10.6%
Effective Tax Rate	-3.0%	9.9%	10.0%	15.0%	18.0%
Net Profit Margin	4.0%	3.2%	3.6%	3.8%	3.8%
ROE	13.1%	11.3%	13.8%	16.5%	17.2%
ROA	4.5%	3.5%	4.0%	4.6%	4.6%
ROIC	15.4%	14.2%	14.9%	15.2%	15.7%
OCF / Sales	2.8%	6.2%	2.1%	7.1%	1.9%
FCF / Sales	-2.3%	-0.4%	-2.7%	3.4%	-1.1%

Ratio Analysis	2017A	2018A	2019E	2020E	2021E
Adj. P / E (x)	15.6	15.4	11.1	8.3	7.1
EV / EBITDA (x)	10.3	7.2	5.7	4.5	3.8
EV / Sales (x)	0.9	0.7	0.6	0.5	0.4
P / B (x)	1.9	1.6	1.5	1.3	1.1
Cash Flow Yield	n.m	n.m	n.m	10.8%	n.m
EPS (₺)	1.25	1.26	1.76	2.34	2.75
DPS (₺)	0.63	0.64	0.50	0.70	0.70
Dividend Yield	2.0%	2.8%	3.5%	3.6%	3.6%
Net Debt (Cash) (mn ₺)	4,794	6,607	8,987	11,069	12,591
Net Debt / EBITDA (x)	2.5	2.4	2.6	2.5	2.4
Net Debt / Equity (x)	0.7	0.8	1.0	1.1	1.1

Source: Is Investment

Balance Sheet (mn ₺)	2017A	2018A	2019E	2020E	2021E
Current Assets	**13,501**	**19,196**	**20,931**	**26,072**	**30,840**
Cash and Cash Equivalents	2,582	5,342	3,298	3,937	4,453
Short-Term Trade Receivables	6,518	7,756	9,940	12,488	14,910
Inventories	3,780	5,088	6,455	8,090	9,619
Other Current Assets	730	1,011	1,239	1,556	1,858
Long Term Assets	**6,935**	**9,172**	**10,469**	**11,708**	**12,747**
Trade Receivables	12	36	44	55	66
Investments with Equity Method	282	347	390	449	495
Tangible Fixed Assets	3,265	4,534	5,217	5,775	6,247
Intangible Fixed Assets	2,578	3,109	3,414	3,664	3,833
Other Long-Term Assets	798	1,145	1,404	1,764	2,106
Total Assets	**20,436**	**28,368**	**31,400**	**37,779**	**43,587**
Short Term Liabilities	**8,403**	**12,497**	**13,870**	**19,599**	**25,978**
Short-Term Financial Loans	3,262	5,517	5,315	8,878	13,231
Short-Term Trade Payables	3,576	4,734	5,809	7,281	8,657
Other Short-Term Liabilities	1,565	2,246	2,745	3,440	4,090
Long Term Liabilities	**5,118**	**7,652**	**8,462**	**7,998**	**6,036**
Long-Term Financial Loans	4,114	6,432	6,970	6,128	3,813
Other Long-Term Liabilities	1,004	1,221	1,492	1,870	2,223
Equity	**6,915**	**8,219**	**9,069**	**10,182**	**11,573**
Parent Shareholders Capital	6,881	8,183	9,029	10,138	11,522
Share Capital	676	676	676	676	676
Reserves and Other Items	5,362	3,663	7,166	7,879	8,987
Current Year Income (Losses)	843	852	1,188	1,584	1,860
Minority Interests	34	36	40	44	50
Total Liabilites & Equity	**20,436**	**28,368**	**31,400**	**37,779**	**43,587**

Cash Flow (mn ₺)	2017A	2018A	2019E	2020E	2021E
Net Cash from Operations	**590**	**1,681**	**681**	**2,928**	**922**
Earnings Before Adjustments	845	856	1,192	1,589	1,866
Depreciation & Amortisation	548	690	824	926	1,011
Change in Working Capital	-1,786	-1,818	-2,350	-2,537	-2,412
Other Operating Cash Flow	982	1,953	1,015	2,950	457
Cash from Inv. Operations	**-1,070**	**-1,782**	**-1,558**	**-1,503**	**-1,458**
Capital Expenditures	-968	-1,760	-1,531	-1,470	-1,417
Other Inv. Cash Flow	-6	-22	-27	-34	-40
Free Cash Flow	**-480**	**-101**	**-877**	**1,425**	**-536**
Cash from Fin. Operations	**619**	**2,857**	**-1,765**	**-1,316**	**568**
Change in Financial Debt	1,305	3,260	-201	337	2,720
Dividends Paid	-425	-435	-341	-475	-475
Other Financing Cash Flow	-514	-423	-1,222	-1,178	-1,677
Net Change in Cash	**-114**	**2,302**	**-2,641**	**109**	**32**

VALUATION

We revised up our 12-mth target price for ARCLK as TL24.88/share up from previous PT of TL17.48/share by revising up our EBITDA margin estimates and revising down our WCR assumptions based on company's successful 4Q18 financial results and forward guidance, 0.5ppt downward revision in our € denominated risk free assumptions and carrying forward our DCF valuation for three months. As our revised PT now offers 28% upside potential, we upgrade our recommendation to BUY from HOLD. As we believe that DCF incorporates long term growth prospects especially for developing market regions such as Pakistan, ASEAN and India, we have assigned higher 75% weight to DCF and 25% weight to Peer Analysis.

The stock trades at 15% discount at 2019E P/E of 11.1x and 31% discount at 2019E EV/EBITDA of 5.7x compared with its international peers' average of 13.1x and 8.3x, respectively. Looking at 5-year historical forward multiples based on Bloomberg, ARCLK trades at 21% average discount based on its both average historic forward EV/EBITDA and P/E with respect to its peers. Based on stock's 5 year historic discount to its peers, we applied 20% discount on implied value driven from peers analysis which we assigned equal weights to P/E and EV/EBITDA multiples for 2019.

Risks to our call (i) weaker than expected Turkish and European home appliance market ; (ii) higher raw material prices, putting pressure on margins ; (iii) increasing commodity prices on easing US & China trade war iv) weakness in TL and € against US$; (v) worsening in WCR.

Figure 1: Arcelik Valuation

Valuation Methodology	Implied Value	Weight	Weighted Equity Value
DCF	17,467	75%	13,100
International Peers	14,858	25%	3,714
Target Value			**16,815**
Target Price / share			**24.88**
Current Price / share			19.46
Upside			**28%**

Source: Is Investment

DCF ANALYSIS

We discount Arcelik's free cash flows in €uro using an average Cost of Equity of 10.9% in our 10 year forecast horizon. Our risk free rate assumption was revised down by 50pbs, benchmarking Turkey's € denominated 7yrs Eurobond. We assumed 3% terminal € growth rate assumption considering high growth prospective in developing market regions such as Pakistan, ASEAN and India.

Figure 2: DCF

TL mn	2018	2019E	2020E	2021E	2022E	2023E	2024E	2025E	2026E	2027E	2028E	TV
Revenues	**26,904**	**32,981**	**41,439**	**49,475**	**57,994**	**66,922**	**76,953**	**87,984**	**100,191**	**114,122**	**130,244**	
EBITDA	2,727	3,462	4,342	5,256	6,227	7,164	8,237	9,412	10,648	12,045	13,655	
EBITDA Margin	10.1%	10.5%	10.5%	10.6%	10.7%	10.7%	10.7%	10.7%	10.6%	10.6%	10.5%	
EBIT	2,037	2,638	3,416	4,244	5,142	6,023	7,023	8,114	9,248	10,526	12,012	
(-) Tax	-201	-264	-512	-764	-925	-1,205	-1,405	-1,623	-1,850	-2,105	-2,402	
(+) Depreciation	690	824	926	1,011	1,086	1,141	1,214	1,298	1,401	1,519	1,642	
(-) Cap-Ex	-1,797	-1,531	-1,470	-1,417	-1,545	-1,676	-1,814	-1,950	-2,064	-2,186	-2,540	
Cap-ex / sales	*6.7%*	*4.6%*	*3.5%*	*2.9%*	*2.7%*	*2.5%*	*2.4%*	*2.2%*	*2.1%*	*1.9%*	*1.9%*	
(-) Change in WC	-1,233	-2,350	-2,537	-2,412	-2,557	-2,679	-3,010	-3,310	-3,662	-4,180	-4,837	
WCR / Sales	*28%*	*30%*	*30%*	*30%*	*30%*	*30%*	*30%*	*30%*	*30%*	*30%*	*30%*	
FCF (TLmn)	-504	-683	-177	662	1,200	1,604	2,008	2,529	3,072	3,574	3,875	
FCF (€mn)	**-89**	**-107**	**-24**	**82**	**136**	**168**	**194**	**227**	**260**	**286**	**290**	**5,566**
WACC		**7.4%**	**7.3%**	**7.7%**	**7.4%**	**7.5%**	**7.2%**	**7.4%**	**7.6%**	**7.7%**	**7.9%**	**8.4%**
Discounted FCF (€mn)		**-107**	**-22**	**71**	**110**	**126**	**135**	**148**	**158**	**161**	**151**	**2,673**
Terminal Growth	3%											
Sum of Disc. Free Cashflows	929											
PV of Terminal Value	2,673											
Net Debt -2018	-1,093											
Target Value (mn €)	2,509											
Target Value (mn TL)	**17,467**											

Source: Is Investment

Figure 3: International Peers' Comparison

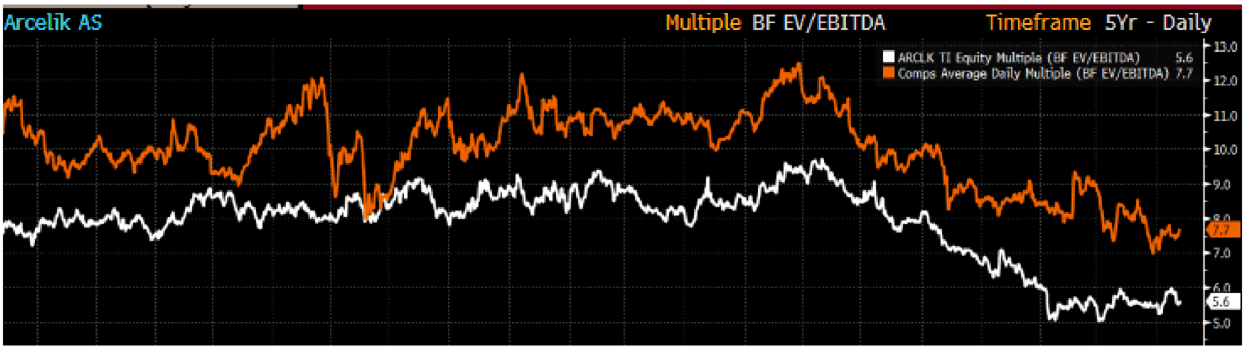
Company	Country	EV/SALES			EV/EBITDA			P/E		
		2018E	2019E	2020E	2018E	2019E	2020E	2018E	2019E	2020E
KING CLEAN ELEC	CHINA	1.1x	1.0x	0.9x	11.7x	8.7x	8.5x	18.0x	14.2x	11.6x
MIDEA GROUP	CHINA	1.1x	1.0x	0.9x	10.9x	9.8x	8.6x	14.2x	12.6x	11.0x
QINGDAO HAIER	CHINA	0.7x	0.6x	0.6x	8.8x	7.8x	6.9x	13.1x	11.9x	10.5x
DE'LONGHI SPA	ITALY	1.6x	1.5x	1.4x	10.1x	9.5x	8.9x	18.3x	16.8x	15.6x
ELECTROLUX AB-B	SWEDEN	0.6x	0.6x	0.5x	7.0x	6.7x	5.9x	14.8x	13.9x	12.1x
WHIRLPOOL CORP	US	0.7x	0.7x	0.7x	7.1x	7.0x	6.8x	9.3x	9.1x	8.2x
Average		**0.9x**	**0.9x**	**0.8x**	**9.3x**	**8.3x**	**7.6x**	**14.6x**	**13.1x**	**11.5x**
ARCELIK		**0.7x**	**0.6x**	**0.5x**	**7.2x**	**5.7x**	**4.5x**	**15.4x**	**11.1x**	**8.3x**
Disc / Prem		**-23%**	**-33%**	**-43%**	**-22%**	**-31%**	**-40%**	**6%**	**-15%**	**-28%**

Source: Bloomberg, Is Investment

Peer Comparison

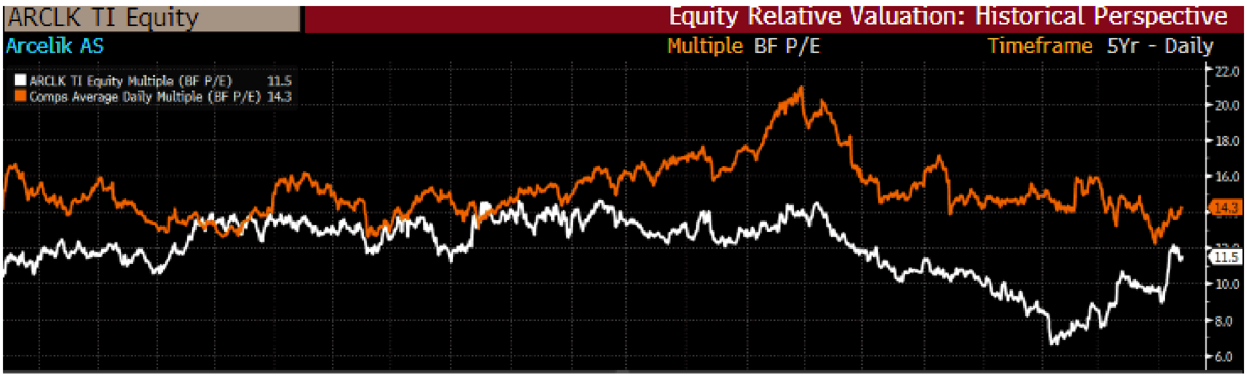
The stock trades at 15% discount at 2019E P/E of 11.1x and 31% discount at 2019E EV/EBITDA of 5.7x compared with its international peers' average of 13.1x and 8.3x, respectively. Looking at 5-year historical forward multiples based on Bloomberg, ARCLK trades at 21% discount based on its both average historic forward EV/EBITDA and P/E with respect to its peers. Based on stock's 5 year historic discount to its peers, we applied 20% discount on implied value driven from peers analysis which we assigned equal weights to P/E and EV/EBITDA multiples for 2019.

Figure 4: Arcelik Historic 12months forward EV/EBITDA (Consensus)



Source: Bloomberg

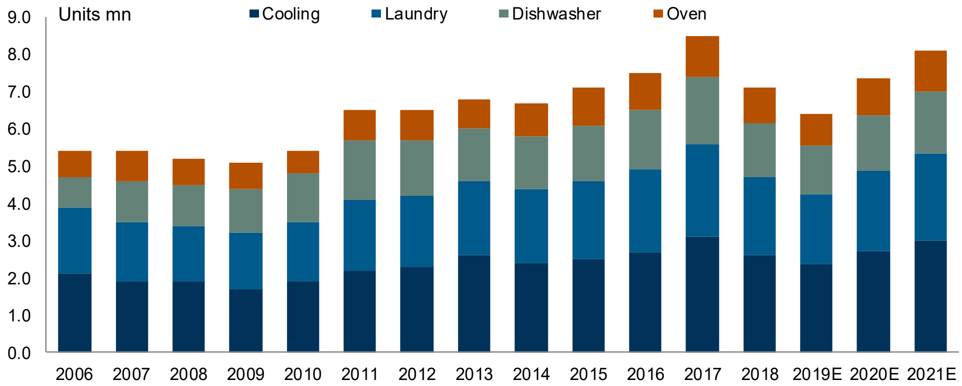
Figure 5: Arcelik Historic 12 months forward P/E (Consensus)



Source: Bloomberg

Contraction in Turkish WG market to continue in 2019 as well Turkish WG market shrank by 17% in 2018 due to decline in consumer confidence, lower affordability, higher product prices and strong base in 2017. Price adjustments to reflect the sharp depreciation of TL since August reached to 50% in 2018 more than offset the volume contraction and resulted in 4% revenue growth in Arcelik's Turkey operations in 2018. We expect headwinds in Turkish WG market to continue in 2019, leading to 10% contraction over 2018. WGs are low ticket items compared to vehicles, therefore are expected to be affected to a lesser degree from distortion in economic conditions. Furthermore, the fact that half of the WG demand in Turkey is driven by marriages/divorces makes the total demand less sensitive to decline in consumer confidence. Better pricing level on average coming from high base year effect in 4Q18 is expected to result 15% revenue growth in Arcelik's Turkey operations in 2019. Arcelik management doesn't expect a major change in competition in domestic WG market following the exit of Whirlpool from Turkish market. Please note that Arcelik has an overwhelming ca 50% m/s in Turkey, whereas as ca40% of market shared by two local manufacturers and remaining ca10% belongs to importers.

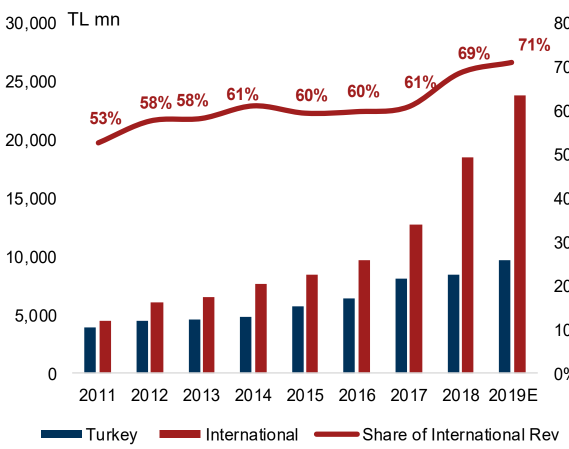
Figure 6: Turkish WG market



Source: BESD

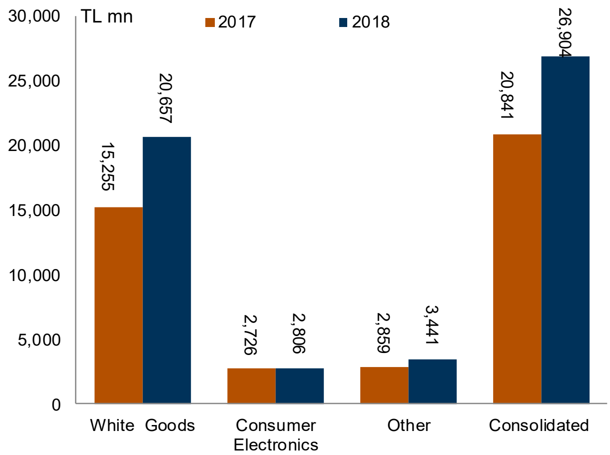
Aiming to outgrow global WG market Arcelik achieved to increase its m/s by 0.7ppt in European WG market which posted 1.6% unit growth in 2018 over 2017. The highest m/s gain at 2.5ppt was achieved in UK, while the Company lost some m/s in Germany, Poland and Ukraine. The Company attained 45% revenue growth in TL terms in Europe in 2018, where 9% coming from organic growth and the rest from TL depreciation against €; increasing its share in consolidated revenues to 69% in 2018 from 61% in 2017. South African market posted 5% growth, helping Arcelik to generate 36% TL based turnover growth in 2018. Pakistan market was weak due to macroeconomic conditions in 2018. Company's revenues in ASEAN market reached to US$135mn in 2018, thanks to 30% product increase in Thailand plant on m/s gains. The Company projects global WG market to grow by 2% in 2019 over 2018, while targeting to outperform the market in unit base. We assume Arcelik's international revenues to grow by 25% in 2019 on mid-single digit volume growth thanks to higher contribution of Romanian operations (new washing machine plant became operational in 2019) and ASEAN operations, m/s gains in operating markets and positive currency impact where we forecast ca15% depreciation of TL against hard currencies in 2019. All in all, we expect 23% top-line growth for Arcelik in-line with company guidance of 25% growth.

Figure 7:Increasing Share of International Revenues



Source: Arcelik

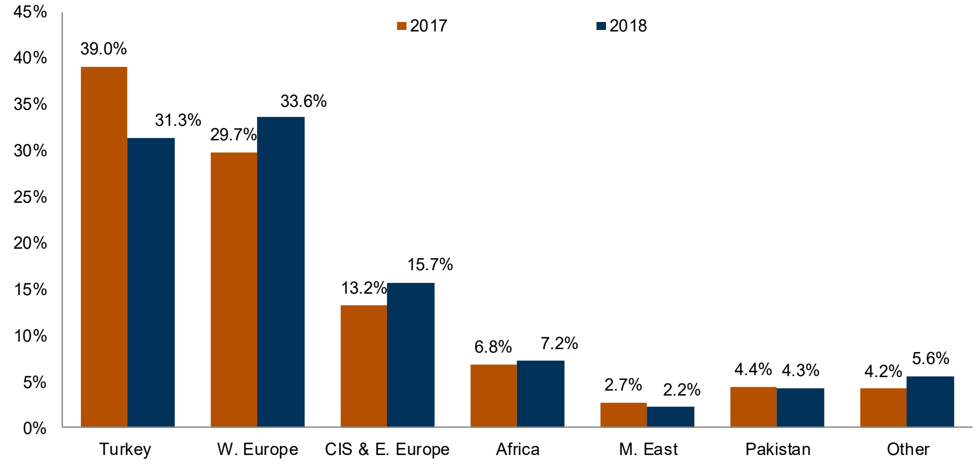
Figure 8: Segmental Revenues



Source: Arcelik

No worries related to Brexit Arcelik is on the safe side related to its export exposure to UK regarding to Brexit in case EU or Turkey can not reach a trade deal with UK. Arcelik's Romania plant manufacturing refrigerator and washing machine which became operational in late 2019 might be a production hub for company's exports to UK.

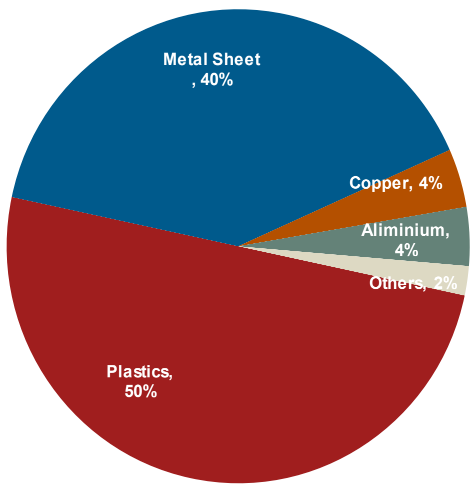
Figure 9: Geographical breakdown of consolidated revenues



Source: Arcelik

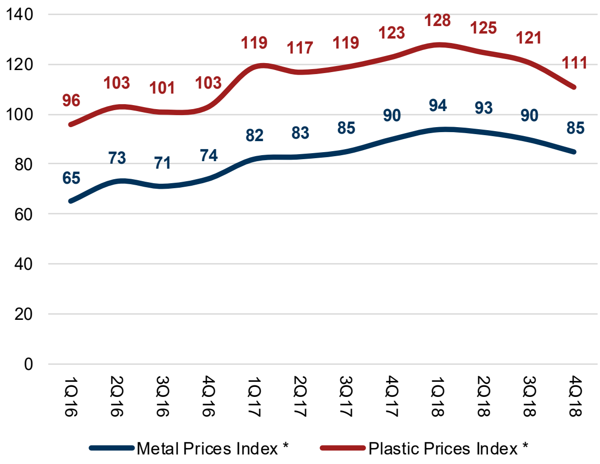
Further margin improvement is on the table Consolidated gross margin improved to 31.8% in 2018, up by 0.6ppt YoY, thanks to price adjustments in some major markets and support from easing raw material prices. Indeed, metal prices index and plastic prices indexed declined by 6% and 9% YoY, respectively. With a deeper analysis on segment breakdown for 2018, we see that gross margin in WG was down 0.3ppt YoY despite higher prices due to lower share of relatively more profitable Turkey operations on weak demand; gross margin in Consumer Electronics was up by 1.9ppt YoY due to the decline in panel prices (despite sharp sales discounts due to Black Friday and X-mas in 4Q18); gross margin in Other (mainly SDA) was up by 1.6ppt YoY on higher prices. Additionally, tight op-ex control (especially marketing expenses) in 4Q18 drag down op-ex / sales ratio by 0.4ppt YoY in 2018, leading to 10.1% EBITDA margin (Company reported -incorporates government grants-:10.4%) in 2018, up by 0.9ppt YoY. We believe downward trend in commodity prices will continue to support Arcelik's margins in 2019, especially for 1Q19 and 2Q19. Indeed, Arcelik management targets ca20bps improvement in its consolidated gross margin in 2019 over 2018. On top of this, the Company aims further 20-30bps decline in its op-ex / sales in 2019 over 2018 as its tight control on marketing expenses will prevail. We penciled in 10.5% EBITDA margin for 2019 in-line with company's guidance. We project 27% EBITDA growth in 2019 over 2018 ahead of 23% revenue growth in 2019.

Figure 10: Raw Material Breakdown



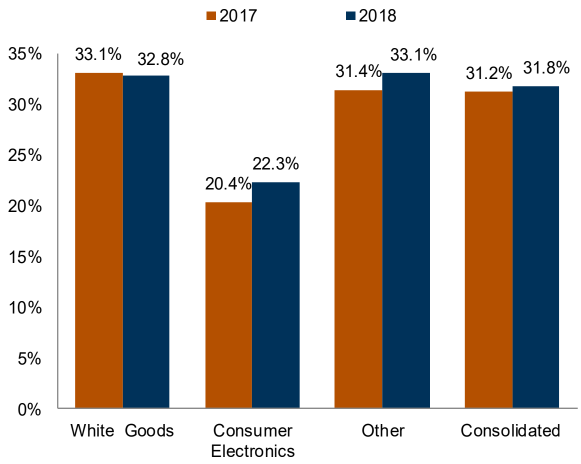
Source: Arcelik

Figure 11: Raw Materials Index



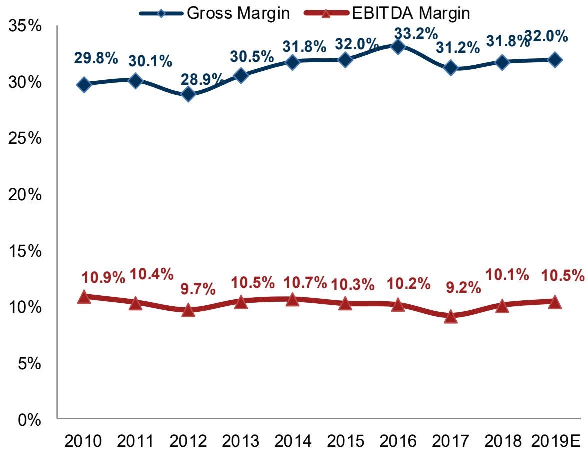
Source: Arcelik
** Quarterly Averages*

Figure 12: Segmental Gross Profitability



Source: Arcelik

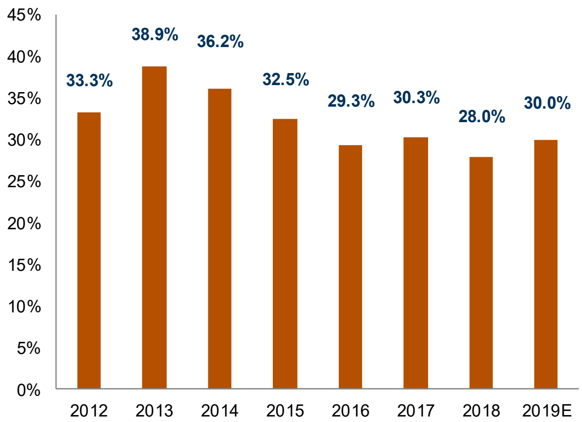
Figure 13: Margin Development



Source: Arcelik

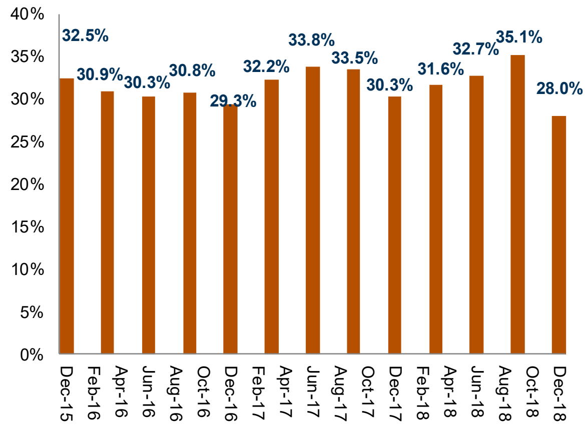
Is 2018YE WCR/Sales ratio sustainable? Arcelik's WCR/sales dropped to 28% in 2018YE down from 30.3% in 2017YE thanks to TL appreciation, strong collection performance, inventory depletion in TVs and declining share of Turkey operations in total revenues. Sharp depreciation of TL resulted in company's WCR/sales ratio to hit 35.1% in 9M18-end, as balance sheet items booked in end-of-period rates but income statement items booked in average period rates. The case reversed as TL appreciated 4Q18 end over 3Q18 end. The Company reflected the rapid rise in interest rates to its credit sales to dealers in 4Q18, resulting in shorter collection period for Arcelik. Lower share of Turkey operations on weak domestic demand also supported the decline in WCR in 4Q18-end as Turkey operations are main culprit for high WCR for Arcelik. Arcelik management targets its WCR/sales to be 30% in 2019.

Figure 14: WCR/Sales - Yearly



Source: Arcelik

Figure 15: WCR/Sales—Quarterly

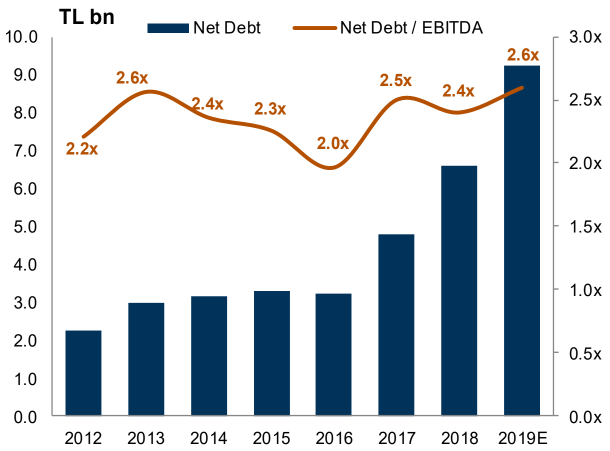


Source: Arcelik

Cap-ex in 2019 will be lower than 2018 Arcelik spent ca€315mn cap-ex in 2018 mainly on its new washing machine plant in Romania, improvement in Pakistan operations, maintenance and new product innovations. The Company budgeted €240mn cap-ex for 2019 to be spent on further improvements in Pakistan, energy efficient upgrading products and maintenance.

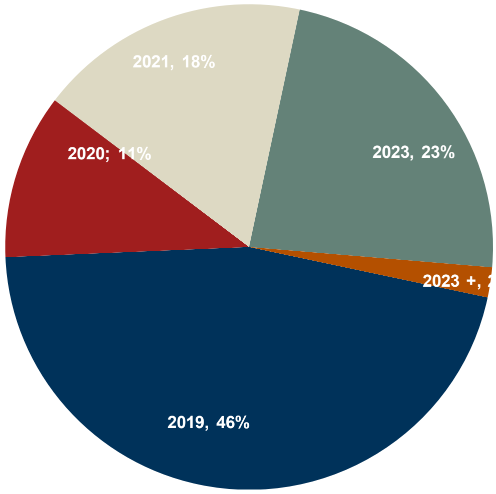
Decline in net debt level Net debt position declined to TL6.6bn as of 4Q18-end from TL7.3bn as of 3Q18-end due to TL appreciation, decline in WCR and strong EBITDA generation. Annual increase in net debt position from TL4.8bn in 4Q17-end was due to 40% annual deprecation in TL, cap-ex of TL1.8bn and higher WCR during 2018. Net debt / EBITDA decreased to 2.36x in 4Q18-end from 3.15x in 3Q18-end and 2.45x in 4Q17-end. Arcelik targets a Net Debt / EBITDA ratio of ca2.5x for 2019. Indeed, company's long term Net Debt/EBITDA ratio target is to be below 3%.

Figure 16: Net Debt



Source: Arcelik

Figure 17: Debt Maturity



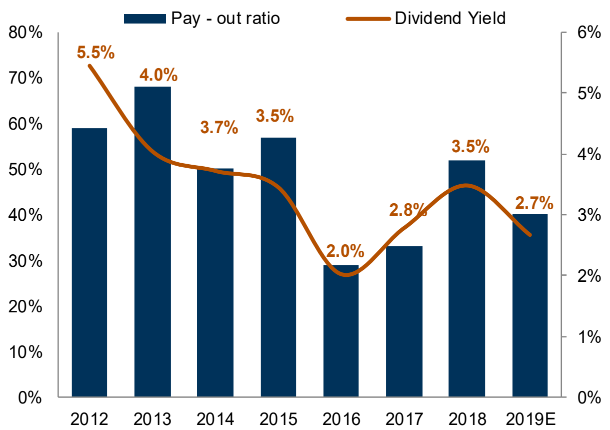
Source: Arcelik

Easing in borrowing rates in 2019 from its peak level in 3Q18 Due to sharp rise in interest rates in Turkey due to economic turmoil in August'18, company's EBITDA/interest coverage dropped to 2.7x in 2018 from 3.3x in 2017. The Company management stated that TL borrowing rates dropped to ca20% in January'19 from its levels of 25% in 4Q18 and 35% in 3Q18. We assume EBITDA/interest coverage ratio to be 2.7x in 2019 similar to 2018. We penciled in average 18% TL borrowing rate for 2019.

Strict hedging policy Despite its strict hedging policy, the company booked TL414mn f-x losses, net (financial income/expense + other income/expense) in 2018. On the flip side, the Company recorded TL279mn net gain on derivative instruments in 2018. Please note that interest portion on derivatives is also booked under f-x losses in financial expenses. It should be noted that it is a KPI for the company management not to have an FX exposure exceeding low single-digit % of equity.

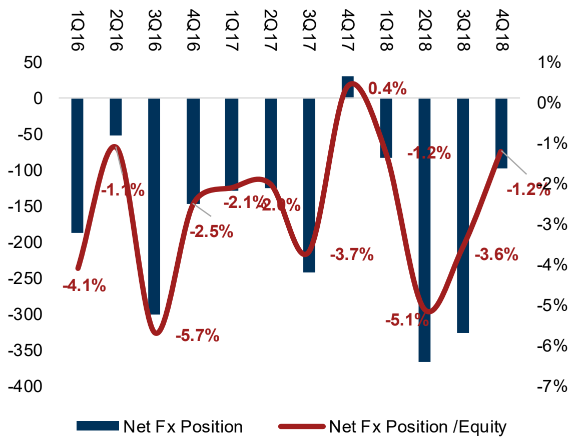
Dividends For the last ten years, Arcelik has an average dividend yield of 3.7% with an average dividend pay-out ratio of 48%. Based on the assumption of 40% dividend pay-out ratio in 2019 lower than 50% in 2018, we project Arcelik to distribute TL340mn dividends in 2019, corresponding to 2.7% dividend yield.

Figure 18: Dividends



Source: Arcelik

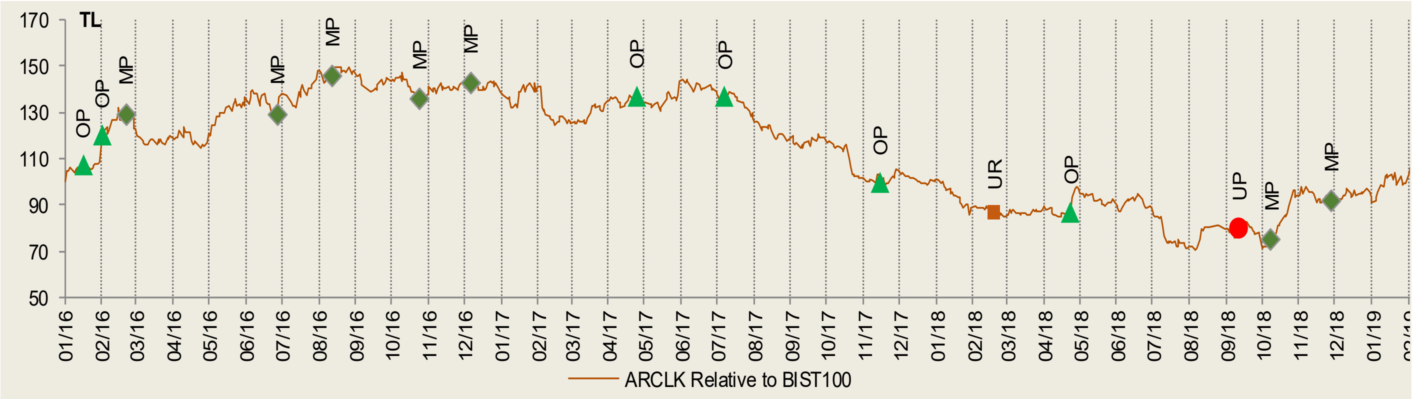
Figure 19: F-x position to Equity



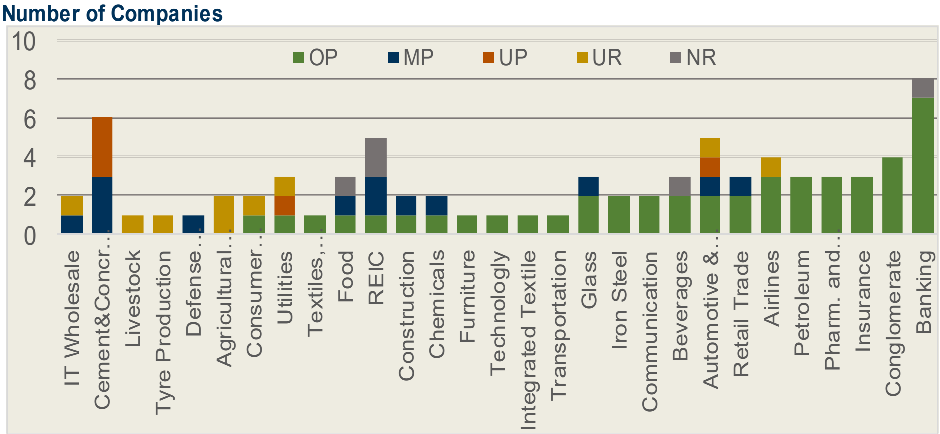
Source: Arcelik

Arcelik

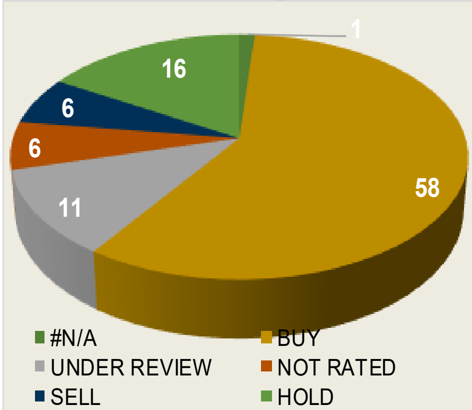
Relative to BIST 100 / Reommendations



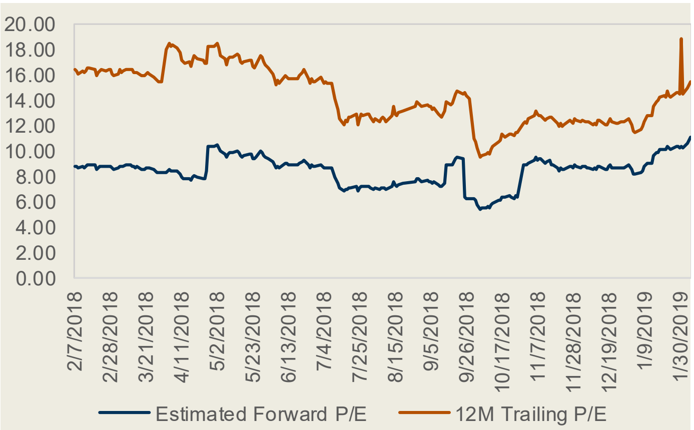
Number of Companies



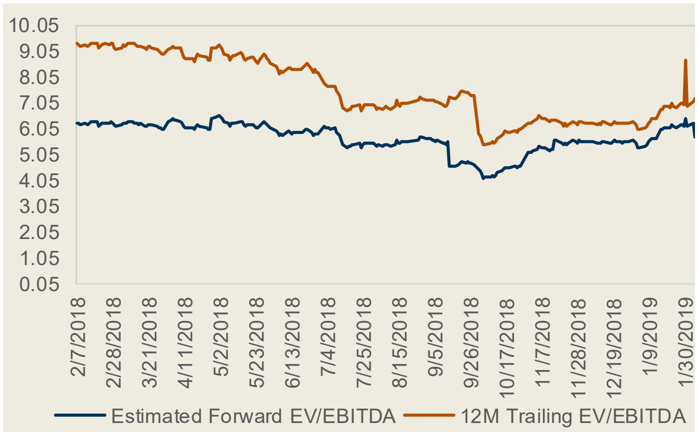
Rec. Breakdown for Coverage



Estimated Forward P/E & 12M Trailing P/E



Estimated Forward EV/EBITDA & 12M Trailing EV/EBITDA



Source: Is Investment