

MEPCO

CONFERENCE CALL TO DISCUSS MEPCO FINANCIAL AND OPERATIONAL RESULTS FOR THE FIRST QUARTER OF 2021.

Company: MEPCO

Date: 10.05.2021

Participants:

- Sami Al Safran, Chief Executive Officer
- Bassem El Shawy, Head of Strategy and Business Development
- Johan van Vuuren, Chief Financial Officer

Operator

Good afternoon everyone and welcome to Middle East Paper Company's first quarter 2021 results conference call. I will now turn the call over to Mr. Bassem El Shawy. Please go ahead.

Bassem El Shawy, Head of Strategy and Business Development

Hello, good afternoon, good morning, everyone. Thank you for joining us today. We'll start with the forward-looking disclaimer as usual. Our management has made every effort to present a fair view of MEPCO's operational and financial performance, it is important to acknowledge the expectations about future results, the common line of prevailing operational, financial, and market conditions may change in the future. Management does not give forward-looking statements for financial investment decision purposes, does not take responsibility to explain differences between the future and actual results stated in the course of this presentation. Thank you very much.

And, again, welcome to today's call. It's a very special call for us, we're happy to have you with us. Today we're introducing a new CFO, we have Mr. Johan van Vuuren with us, he joined the company only last week, so he's been with us for about six days. Johan brings a lot of experience to MEPCO and WASCO, and I will hand over to him

to give you a brief presentation about himself and we look forward to meeting you in person once things go back to normal.

Johan van Vuuren, Chief Financial Officer

Good morning and good afternoon, everyone. I am Johan van Vuuren, South African national. I've been in the region for roughly 6-7 years now in total; academic background, I'm a South African qualified Chartered Accountant, as well as UK Chartered Accountant qualified, extended my qualifications to London Business School, I completed my Master's in Business Administration. Sector background, I've spent first half of my career also in petrochemical and integrated oil and gas, where after I changed into broader ESG-related sectors, predominantly the waste management sector where I was appointed roughly two and a half years ago into the PIF Group as the Chief Investment Officer and Group CFO of a company called SIRC which was established by the Public Investment Fund of Saudi Arabia to develop the waste management, recycling sectors. As Bassem said I joined about a week ago, so fresh off the boat, so to speak, but very happy and proud to be part of MEPCO and joining MEPCO into this very exciting time in the company's history.

Bassem El Shawy, Head of Strategy and Business Development

Welcome on board Johan. And I'm going to give a quick overview about this quarter's results, which are quite pleasant as you see. So, the uptake we saw in the prices in the last quarter of last year continued and this drove our financial performance quite aggressively. In terms of production, we produced 105,000 tons for this quarter, it is quite far off from what we produced last year within the same quarter. The sales, we exceeded SAR 200 million, which is a very good threshold to cross in a single quarter given fairly bright start of the year, and especially recording a healthy margin of 24% in gross profit margin with a value of SAR 48 million. Year-on-year, this is making about 47.5% and close to 55% increase quarter-on-quarter and year-on-year respectively. The EBIT is looking quite healthy, which is defined as the operating profit for MEPCO to SAR 23 million. The overall business environment of this quarter was quite levelled with prices increasing and MEPCO actually increased its prices twice since the last quarter of last year, totaling \$80 per ton. We need to draw your attention that \$80 per ton is not the price passed to consumer, this is the starting negotiation point. And what actually gets recorded on the books as price increases depends on the negotiations with the customer, depending of course on the business relationship and the size of the deals.

This marked the -- if I would call the main highlight of the quarter, which is the price. The second thing is our control of the cost. As prices moved up, there has been also quite an extensive demand on the fiber of the OCC prices, it's a global thing, it's not something related to MEPCO or locally in Saudi Arabia. For those of you are not following quite closely on the paper industry, it's nationally that the prices have been going up and demand on containerboard material has been going up, because a lot of companies now are activating the industrial activity at full throttle. So, they are demanding more and more of the corrugated materials to box the product. So, this excessive demand drove prices up, and of course, it also drove demand of the raw materials, which has been really going up also in Saudi Arabia.

We have WASCO, WASCO is doing a tremendous job for us by securing raw materials and keeping the costs as tight as possible. We also achieved significant savings to offset the increase on raw material which resulted in the blended gross profit margin is 24%. So, when you look at it with an increase in OCC and filling it up with the gross profit margin 24% is actually quite significant result. I think the rest of the quarter is quite self-explanatory in terms of the financial figures. And as we mentioned again, and I would like to stress, our dedication and keenness to tap on the ESG aspects of the business was contracted with a company that I think you might know, which is Sustainability Excellence, to formulate our first ESG report. So, we are catering for the ESG investors that we have seen, we see more and more every day. And we believe we have a fantastic story to tell when it comes to the whole environmental and sustainability aspects. So, we are looking forward to issuing that report by Q3 of this year. We're getting there, and I think it will be a multi-purpose report that will tap on many aspects of the business.

I believe this covers all the important aspects we need to tap on for now. And we'll leave the floor open to you for questions. Operator, please let's go to the Q&A.

Operator

Thank you. [Operator Instructions] We have a question from Anoop Fernandez at SICO. Please go ahead.

Anoop Fernandez, SICO

Good afternoon. Thanks for the call. And congrats on a great set of numbers and also on all these initiatives that you're taking, great going on that. Just two questions. First, on the waste management side, there's clearly a lot happening in Saudi, could you please give us a more color on how things stand at the moment? And what benefits

do you see for your business going forward? I think recently there was some news where you struck a deal with the Jeddah municipality, how do you see that thing shaping up in terms of your availability of raw material, as well as the cost of that? In general, any color on the waste management side? And how do you see that influencing your costs going forward in an environment where OCC prices are rising?

The second question. So, you've taken two price hikes over the last 3-4 months. Now, let's assume a situation where international prices don't rise further. Is there any benefit that you get purely from the fact that container freight rates have gone up so much? That just becomes logistically very challenging to import stuff into the Kingdom through containers. So, does that give you some sort of pricing power? And did you see further opportunity to increase prices through the year as things stand? Or do you think there will be some pushback from your customers at some point? Given where the economy is and so on, that might be a bit challenging, any colour on that as well. That's it from my side.

Sami Al Safran, Chief Executive Officer

Good afternoon, this is Sami. Good to hear from you again. Let me answer you the second part of the question. Regarding the price increase that has been announced, it's in line with the global trend. And it's been backed up by the increase of the demand. So, the whole world is facing actually increase in the demand and the shortage of supply, which is leading to a price increase. So, we do not anticipate seeing that will lead to an increase of imports to Saudi Arabia. However, going forward, again, and there is no certainty, if anything. The second part regarding the further increase, I think what has been done in this quarter is considered to be exceptional. We are usually among the performers of price movements, we usually find such kind of an increase takes a whole year, from the start point until it reaches peak, this cycle is becoming very short that we have seen such massive increase that's happened in the first quarter. Going forward, again, it's my personal thoughts, I do not anticipate further increase that should happen. However, everything is possible to happen. From the other side, we consider seeing a healthy year across the remaining of the year as the demand is not going to be sorted immediately, especially with the economical performances happening across the globe. Does that answer your question?

Anoop Fernandez, SICO

It was on the pricing side. I mean, there's one aspect where you're looking at international prices going up, and then there is the other thing that the cost of

importing anything into the Kingdom itself goes up because the cost of freight has gone up. So, since you are very domestically focused, your raw material is almost entirely domestic, do you get any benefit in terms of this created ability to price your products a little higher than what it would have normally been just because of these factors, extraneous factors? Or do you think the environment is a little challenging for you to pass on these costs to your customers?

Sami Al Safran, Chief Executive Officer

In reality, we are not getting any special privilege or advantage for that one, because keeping in mind that while we are increasing our prices in the local market, the same we do with international. So, we are competing on a similar ground for both. However, definitely, we have to call it the natural logistic advantage of being in Saudi Arabia. But we are competing on a fair ground with both parties. Definitely, the only probably positive thing we are facing is that whenever the market becomes healthy, you do not see any dumping practices happening here.

Anoop Fernandez, SICO

While we're on the prices, the market at the start of 2020 was supposed to be seen extremely oversupplied, there was large amount of supply coming out from the US and from Europe, what has really changed in the containerboard market? I get the demand side, but is there anything that has changed on the supply side as well, that you are no longer seeing those kinds of capacities coming? Because back in the early 2020, I don't think anyone would have thought you would have seen such sort of tightness in this market.

Sami Al Safran, Chief Executive Officer

It's a good question. I will be answering on a global level, which probably will have an answer to support this one. We in Saudi Arabia do not have a specific mass supplies coming from certain countries a lot of that is distributed from across the globe. The majority of that, of course, is United States and Europe. Now, the drivers behind the supply and the demand which impacted the globe is actually China. As you know, that China stopped importing recycled waste materials, which led really to a drop of the Chinese production of a containerboard. Accordingly, they have covered that drop of production by importing finished products. And most of the world including MEPCO had the benefit of that, which we do not see that this is a short-term event, because Chinese will continue not to import wastepaper, and they will replace it with the

finished product. So, that will positively increase the demand of the finished product as a containerboard and above.

We do not see special intentions of changes happened in the local market. Keeping in mind that two years ago, the GCC companies have filed an anti-dumping case and it was really a strong message to people not to miss in the local market. And we are ready to file any cases if it requires or if we notice any dumping comes from any country.

Anoop Fernandez, SICO

Okay, understood. Just the first question on the waste management side.

Sami Al Safran, Chief Executive Officer

Going to the first question, which is the waste management. You must be aware, a couple of times mentioned about Saudi Arabia national strategy to divert the waste from the landfills, by 2035 80% to be recycled and 20% to be converted to energy. And during the past two decades, we used to use WASCO as the vehicle to secure the raw material supply for MEPCO. And from that demand, we have improved the capability of WASCO to do work in different dimensions including the capability of WASCO to operate material recovery facilities and landfill. So, WASCO did enter into different streams of waste management related to the new strategy that is appearing. No doubt, that will give WASCO the power to be one of the local and national waste management companies that already controlling half million ton in the region, distributed in 20 branches, 4 branches of waste material recovery facilities. I see that gives us really the privilege to be the first choice for any party who is interested to deal with the waste management business. And it has been proven from last week signature with Jeddah municipality to develop the recyclable market industries in Jeddah, which we hope that this process will help us to give a good demonstration of local capabilities to be reflected in the local market, we are aiming by doing this one that we would be a role model to be cascaded to the rest of the cities. And this is one of the streams that WASCO is already existing in a strong way. We should be seeing more and more activities in WASCO for future. And that will really pave the road and the stories if we manage to increase, for example, the wastepaper recovery in Saudi Arabia now is limited to a million ton. By improving the recovery capabilities here, we should really increase it which will really give opportunities for further organic growth of MEPCO.

Anoop Fernandez, SICO

Any change in cost that you would like to highlight? And how do you see your costs evolving just on the back of these initiatives? Would it reduce your wastepaper costs going forward, and to what extent?

Sami Al Safran, Chief Executive Officer

It's a good question, thank you for asking. You might notice that the international communities in a globe is increasingly going very high, not the case of the wastepaper, among all other cases, and the same thing we have seen here. WASCO was one of the main sources for us to mitigate that incremental increase of raw material prices to us. Now, going further regulation of the market absolutely will lead to a drop in the cost of the raw material. For example, today, with the efforts we are doing, the cost of our local materials in Saudi Arabia is almost doubled than what is happening in Europe and United States. And that means we are still far away from the normal international benchmark of commodity price. Going further for such kind of an agreement will help to bring the cost of raw materials to the normal international price, which will give us really the privilege and advantage for MEPCO to be more competitive with local and international.

Anoop Fernandez, SICO

Thank you, and all the best.

Operator

Thank you. [Operator Instructions] We have no further questions. I'd like to turn the floor back to Bassem for any closing remarks. Thank you.

Bassem El Shawy, Head of Strategy and Business Development

Thank you very much for joining. And if you have questions later on, please reach out to us, we're always available. Thanks again. And I will see you in the next quarter results of Q2.

Sami Al Safran, Chief Executive Officer

Thank you, gentlemen, for joining us today. It's really delightful to see that the efforts which have been done last year facing the COVID-19, optimizing our operational and performance and maintaining the sustainability of our business. I think for this year,

we are harvesting those efforts and result. And we are biased that the remaining of the year will be healthier for us. We as Management Board are really committed to reflect whatever opportunities available in the market for the favor of the company and our shareholders. Thank you very much.

Operator

Thank you. This concludes today's call. Have a nice day.