

## **6M 2023 – Analyst Conference Call Transcript**

Klára Šípová

Good morning again ladies and gentlemen, welcome to the analyst presentation in connection of a publication of the six months 2023 consolidated financial results of Colt CZ Group and consolidated semiannual financial report. You should have the presentation in front of you. It is also available for download on our website. I would like to welcome today's speakers on the call. It's Mr. Jan Drahotka, the CEO of the company, Hello, Jan.

Good morning.

It is Mr. Jan Zajíc, CEO of Česká zbrojovka Uherský Brod and member of the board of the group.

Good morning.

And Mrs. Jana Matoušková, our Head of Group finance. Hello, Jana.

Good morning.

We will go through the presentation slide by slide. And afterwards, you will have opportunity to ask questions in a q&a session. I would like to ask you to stay muted during the call and also potentially switch off your cameras. Please know that this call is being recorded. And now I would like to hand over to Jan Drahotka to start the presentation.

Jan Drahotka:

Good morning, everybody. Once again. It's a great pleasure to speak to you again after six months of this year. So let's jump into it. First of all, how we feel about the first half of the year. I think that and you saw it in the figures probably already. There was a significant pickup in q2 versus q1. So overall. Overall, if I speak for individual KPIs revenues are at a level of 6.86 billion CZK, which is around 3% below six months of 2022 Adjusted EBITDA at 1,46 billion CZK which is around 18% below last year six months. Adjusted net profit is slightly up to 1.1 almost 1.2 billion CZK which is around 1% increase and EPS I would say flat at 35 CZK per share. If we go to next slide, this is a new slide we have not done it this way yet. Do you see different flags here and we wanted to highlight important things which happened in h1 or q2. Basically, first of all, we did complete an acquisition of swissAA holding. So we have first ammunition producer in the group which is very important milestone for us and we will give you more details about the company today. Second thing is I don't know whether you noticed but Colt Canada signed a, let's say medium term program with Danish army for armament and upgrade of the fleet of Colt rifles with the army. Third thing Sweden, our daughter company in Sweden, Spuhr is continuing supplies to Swedish army were updating some rifles and also we discussed after Q1 results that Colt Canada products were to be used as a donation from Canadian government. And in Q2, quite a bit of this was already done, there is still a part to be filled in, in Q3, but significant part was done in Q2 so that's these are the highlights of the quarter and now let's go for the individual figures. You know, this is this slide has one new element to it that is more focused on the effects but because we had some discussions after last year, last quarter results about what the impact is. So we wanted to show it a bit more

but if you go in the clockwise and start on the top left hand side of the slide you see the geographical split and you see that the US remains the most important market for us, followed by Czech Republic Europe and Canada so and Canada this is important to say there that in Canada it's also quite about the supplies to Ukraine so Canadian Army prioritized its supplies to Ukraine over its own needs. So that's why it's under the umbrella of Canada. And we know that a significant part of the business was going to be an army supply to Ukraine and other markets. I would say less important, especially Asia and Africa are much more driven by larger contracts. We didn't have anything really significant there, even though the sales in Africa went up, not significant an overall mix. Quarterly breakdown of unit sold. When we discussed revenues we said that they went down around 3%. You see the number of units went down more by 13%.

It once again shows the shift towards a more military product. If I had a comment on this one, I would say that US commercial market bottom down so it's I would say that it became kind of stable, but due to comparison is the first quarter of first half of 2022 There is this drop, because definitely, in certain segments, the market was weaker. The segments most affected were polymer frame pistols and also Scorpions on side of CZ. So we saw quite the different performance of two brands Colt very strong on US commercial market, as in the last quarter CZ, in the first half was not as strong as we would hope for and honestly speaking, I'm not happy with the performance, but what we see that the market is changing and what we are involved in we foresee that the sales of CZ branded products will pick up in the second half, especially with some new product introductions. Quarter revenues, you'll see that Q2 2023 was well above Q1 almost 30% but importantly, it was also higher than Q2 2022. So, you see that, when we told you after Q1 results that we believe that the business will pick up we were right. The maybe the slide which needs explanation is the impact of USD CZK rate on our revenues. Do you see that and you saw it on the first slide these KPIs, you saw that net profit is basically stable, whereas EBITDA went down and we already discussed that that there is a significant impact of foreign exchange. CZK appreciated in q1 q2 or q3 q4 last year. So obviously, it does have an impact on the on the EBITDA or revenues and EBITDA, but as we are dominantly hedged of exposure of CZ products, we it's partially offset in the financial result.

So, you see that that compared to the first half of last year, the exchange rate was this year average exchange rate of the q2 2023. Then the revenues will be higher, but we are not trying to we just wanted to show you this explanation because I think that we believe that this is really critical for you to understand better our development of our revenues and EBITDA also, that is important part were around half of our revenues and profitability is derived by COLT or by US Operations US/ Canada and operations and obviously there we are not hedging at all, we are only hedging translation rates but not the risk. So revenues and profits which are derived in dollars are calculated by using the market right so because it's only translation, which we are edging on the balance sheet level. So we are not adding p&l there because it's economic sense on or in this logic. So that's also impacting that. If you go to the next slide here, I think that the two important information are the gray chart. First of all, guidance for both for revenues. We you know that at the beginning of the year we gave you 3 scenarios now having eight months behind us. We are able to narrow the guidance to figures of 16 billion to 16 point 4 billion for revenues, and only adjusted EBITDA 3.2 to 3.4 billion CZK. So, once again the main reasons why we have the guidance in this in this manner is first of all, we see quite significant MLE contracts to be delivered in h2 and we see that the commercial US commercial market will shoot and will pick up in h2. So, these are the main results as far as the main reasons as far as the foreign exchange rate is considered we don't expect CZK to move significantly compared to where we are now. See, go to the next slide please. Can we go to next slide please?

So, what this is what we already discussed that I already touched on that that net profit development outpaces EBITDA the main reason being the effects, so there is a quite significant effects impact on the on the on EBITDA, whereas it's partially offset on the gains on net income, net profit level, because it's in financial results. So that's profit at 1.2 billion, almost 1.19 8 billion CZK so slightly up on adjusted basis, and it the same level kind versus h1 2022.

If you go to next slide, capex, here, we are confirming the what we said already at the beginning of the year and in after q1 results, we expect the capital expenditures to be below 5% of revenues. You also have an indicative split by region, North America versus Czech Republic for h1, we expect still more capex to be done in the Czech Republic, but definitely is getting more closer to be balanced, even though this year, we will be still heavier on it in the Czech Republic. That structure, maybe here it's important if there is one chance one change here you know that in May. So, after results, we did issue seven year bonds. Our net debt that stands out for 4.4 billion CZK or 1.7 times EBITDA, this is after the acquisition of SwissAA. So after payment for acquisition of swissAA. So, this takes into account already. So it was paid before this. Now we are getting to the acquisition, which is the as I say really important news for us. We acquired a Swiss holding company, which has a two key subsidiary two key factories in Switzerland, and then his daughter companies in Austria, Hungary and Italy and Germany, key clients being Swiss Army, German army, Spanish, armed forces Belgium, so it's really Western Europe, Western Europe orientated as two armies orientated, high quality products, high quality producer, as I said, 2 production sites in in Switzerland, and one in Hungary, where Hungary is, I would say, a huge site, but we there's a significant potential because it's quite big and we look at it in a view of potential development. And we look at it that we could maybe beef up our, our ambitions in median calibers like 40, meter, grenades, and stuff like that. You know that here in the Czech Republic we have, we started to develop a project with the army in the Czech Republic, it's now being saved, invested. So we are working on hand grenades there. So this is what we believe that could be one of the use uses of Hungarian site, which is perfectly suitable for it because it's big enough and it can accommodate even primate production and stuff like that. This is a snapshot of the portfolio of Swiss a world class weapons, it's really unique. We can do multi purpose 12.7, which is really high tech and it's a differentiator because it really a different characteristics this density that simple 4.7 then nine millimeter, 0. 338 40 millimeter grenade for gun launchers medium and high velocity 7.62 ammunition and 5.56 ammunition as well non lethal standouts. So you see that the small caliber is done dominantly in Switzerland, the grenades and higher caliber is done in in Hungary.

So that's for the presentation. Once again, how I mean overall to some of the about the h1, I will say that nice pickup in q2, big ambitions for the rest of the year. Or some nice contracts closed or very, very close to being contracted. And we see that that we can grow and especially and you know, if I if I was to say one thing we're which I'm not happy with its performance of CZ on the US commercial market. But I believe that we know what we have to do and what would we have to change in order to make it back. So we already see quite a significant pickup in h2 in h2 orders and an expectation. So that's basically for it. A split maybe last thing split for military law enforcement and versus commercial market for the year. They are still saying that it should be it could approach 5050 We are now at around 4060 Maybe a bit higher, but for the year it might get to 5050 so that's where we are now.

Klára Šípová

Thank you young. Ladies and gentlemen, if you would like to ask questions, please raise your hand in Teams application or speak directly to the phone. The first question is coming from Atinc Ozkan from Wood& company. Please go ahead.

Atinc Ozkan

Good morning, all. And thanks a lot for taking the time for this presentation. I have a couple of questions. But I'll start with US commercial markets. Young running say you expect some recovery in US markets in second half of the year. Okay, please elaborate. Furthermore, what drives that expectation? Because when we look to the FBI, and ICS background checks in July and August, it is still down double digits around 15 - 16%. I know that it's not a perfect indicator of actual gun sales, but it's the only indicator we have. So that's the first question. And the second one. And looking forward for that clip. But we would I think all of us appreciate some color on size of this boutique in Switzerland. How many employees do they have? And if you could give us some ballpoint figures regarding, you know, past performance in terms of revenues or anything similar data to put things in context. Otherwise, I think we will be flying blind to make an assessment regarding impact of acquisition. Thank you.

Jan Drahota:

First of all, you know we did change the organization on the US commercial market on our site. So, we believe that now we have higher reach, you know, we are I would say that we are we are making sure that we have the right representation with the with the different levels of sales, sales and we see it already in the back orders and orders what's happening. Secondly, in the h1 we were we cleaned quite significantly the channels so we are a totally different sales so there's days of supply with service with within the distribution channels. So which again gives us confidence for the h2 and in product so I would say our organization. So we are definitely much more aggressive now in terms of how we are organized in sales. Second thing, clean, clean channels always available for CZ products. So these are the three reasons why we believe and we see it already, we discussed actually quite in detail yesterday, there is a significant pick up in h2 versus h1.

Atinc Ozkan

some color on which segments you expect this recovery or stabilization. Thank you, I

Jan Drahota

wonder if so, especially in the rifles, and I will just have couple of sentences, product means that and it's based on the information you've just provided, we can read now much, much better than the customer and market. So we add quickly a couple of new products, especially the calibers for the rifles. So that's the first one. And these just slightly touch it we introduce a new pistol, the metal frame pistol compact size. So this is the second topic. We also introduced the submachine gun, let me call it Americanized submachine gun is a version of Scorpion level three for us and started the sales. So there's a third and, and last one, which I have not to mention the app, it's a marketing, we also targeted the customers and clients and users and distributors by several marketing channels. So, actually, there are four different topics that we focused on the US market.

Atinc Ozkan

Thank you for that. My second question, please.

Jan Drahota

That was on that it was a second question. So, the company was set up by Andrea Stouffer in 2002. And he was a actually is a specialist for 4.7 MOSFETs. So, so really specialized company and as you said, niche but wisdom, we believe is the best product in terms of f1 Seven, so currently, it will be below 100 People working in the in the business or Around 100 people let's say and, and as far as the revenues are concerned the annual giving savings for new companies, but you can you can you can you can assume that it is around around 30 40 million euro business and so that's around it and this EBITDA, which fulfills our expectations which is which is above which fulfills our expectations and you know that we want to add a valve to numbers and so that's what it takes, we'll look at it the way that we can multiply the business honestly speaking, it has been a very niche producer and we believe that we can really sell the products to too many more clients to more countries.

And we are working on it already. For us now it's about finishing there has been a start they haven't been happy has been started and a complex program in the company. So even before we bought it, so they already install new lines 444476256 So, this is what we are working on and also discussing this with clients. The oppo the 5.7 caliber you know how to how to how to enhance or increase the production and an additional one you know as I told you the hungry one it will take some time to us still to define this the current management of the business would be able to do about it but we are confident that there can be really big things done and wisdom is the business side because it's a significant side it's a really significant side and we can really be we believe that you can really make interesting thing there Yeah. I will also add one sentence on those speaking about revenue generation or value generation if I call it like this we also do see for US Army CZ and Colt cannon also great cooperation with there are more technical guys or ammo r&d team to speed up to increase the height get a higher quality on R&D development or rifles development talking. Seven six to for example 556 and high pressure calibers for example. So it's really beneficial on not only on the revenue side but as well in firehouse production slash sales. Yes, maybe that's I mean homophones up perfectly. When we look at acquisitions and acquisitions which are not in firearms, but are related to firearms. We look at it always in three layers. One is that we should help our platform should help the business to see or more. Secondly, our platform should help the business to serve salt source cheaper, cheap, much achieved more on cheap, more cheaply. And thirdly, r&d. And this is critical for us.

Klára Šípová

Thank you. And the next question is coming from Petr Bartek from ČSAS.

Petr Bartek:

Good morning. Congratulations on great revenues in the second quarter. But I also would like to ask about the margin which, which will some of the weaker than what I expected and declining.

So if you can give us a little bit of light on where the lower margin comes from, and what you expect for the second half and going forward, if it's from the US commercial market, or whether the new contracts from the governmental customers are at lower margins, or how to read words, whether that's simply old inventory being sold, over margin, maybe if you can elaborate a little bit about the development of fourfold cost sight of energy costs and so on.

Jan Drahota

You know, it's a lot of questions, to answer to answer simply, yeah, we did discuss energies. And they were definitely more important on you on season two, besides Season Two besides so that's, that's, that's, that's where it was. But if I, if I come back to the beginning of your question, the margin being lower than in that, then when what you expected for us and we are very clear about it for us will be that minimum business, margin of our business should be 20% EBITDA level. So that's, that's where we are. And then we are, you know, so we look at it the way that, that for us, it's, it's not a satisfactory, it will not be satisfactory, if you are below to 20%. But if it's 21, or 20, or 22, or 21.5. And I know that you don't like it, that's another it's, it's it swings between quarters and videos. So we don't watch it so careful as you do, guys. That's the first thing. So it's not that we don't we don't want to watch it. But it's because it fluctuates. And it's not it cannot be attributed to only worse, or let's say less favorable, or less favorable contracts with government, governments, you know, different commercial markets, it's definitely not like this, it would be a wrong interpretation. I think that the most important interpretation here would be the Forex, if you think about it, you know, I mean, if the Forex rate would be at a different level, where the EBITDA and revenues would be, I would say that whole 100 million of revenues, we hold 100 million in EBIT da if you think about it, right. Because this is this is additional, this is kind of additional, additional revenue with no real input to it, because for access, so I think that this is the most critical one, which does which did have impact or does it impact on us? And then obviously, there can be other things, you know, we were cleaning the channels, so we did have impact on the on the profitability of certain product categories, but the most important from for me would be still doing the forex and you know, and as well, though factor. Yeah, I mean, you know, you know, for us, we were expecting to be more successful in h1 in the US commercial market, you know, and on ceded site, and obviously, it does have impact if you sell, you know, slightly less of volume man.

Petr Bartek:

Maybe one more question regarding the government contracts if you cannot disclose maybe the volume in Denmark or approximately and what's actually the status in the Czech Republic? What's remaining from this midterm contract?

Jan Drahota:

Denmark honestly, speaking, I don't know whether the Danish government released the volume. This is I don't think so. So we don't normally we don't really disclose what governments disclose. Okay, so but it's significant for Canada. That's my comment. I will look whether it whether the Danish government raise the volume I don't think so. I think that they did really the fact that they signed the contract with us but I don't know whether they read the volume. So sorry for that. And, and Czech Republic outside Czech Republic, we run it according to frame agreement, which we have science video his or its addition. So the deliveries continues. There is also one slight figure I would say, on margin probably. And it's not very likely.

Due to customers is related more to the product or product mix, because rifles day, if we sell rifles, they have much more value added than, for example, polymer frame pistols. So we will have significant deliveries to Czech Army in q3 and q4. And this will be this will be continued to q1. So, just to summarize it, we run a check army, according to the three agreements we have signed, we are also working on a couple of more, let's say governmental contracts for 2425 26. And as we already stated a couple of times, we didn't do not disclose the concrete in the particular customers or project. So but we do see huge opportunities in front of us.

So I've also by the way, Peter, I was notified by our guys that the Danish party didn't want us to disclose the volume, they did disclose the disclose the fact that we did sign the contract, but they didn't disclose the volume.

I can tell you this, it's important for us. Colt Canada is a benchmark product in certain countries in Northern Europe, which is really important to us.

Klára Šípová

Ladies and Gentleman, thank you for your questions. The next question is coming from Pavel Ryska from J&T Bank. Please go ahead.

Pavel Ryska:

Good morning. Thank you Klara. I wasn't here the whole time. So I hope that I will not be repeating something that was already explained at the beginning of the presentation. But judging from what was now discussed, the fact that the outlook for the whole year is slightly below the previous middle variant, let's say that you presented in spring, but you also said in your morning report that you signed contracts which are above your initial expectations. So to like to understand this is the major problem was the exchange rates, as Yun mentioned a while ago. So, is your outlook for the whole year based on a specific exchange rate for example, the average exchange rate between the Czech koruna and the American dollar from the first half of the year or is it based on something else? So, because I want to I want to judge if, for example, the current reversal in the exchange rate between the euro and the dollar could help a cult is that achieve a better result than what is in your current outlook for the year? Thank you.

Jan Drahota

As far as the you know, as far as the as the outlook is done, we have done it I think two weeks ago. So this is based on the situation which was, let's say 21 days two weeks ago. So this is this is around eight.

And in respect of forecasts that we have to use the effects right ballot. In the end or the beginning of September, it was about 22 Czech crowns for one even though as we also discuss it or we'll see how to analyze this in Reuters and we see that it is not expected significant increase maximal about 10%. So that's why we decided to be more not to be aggressive in our guidance.

Klára Šípová

ladies and gentlemen, if you would like to ask questions, please raise your hand in teams application. I see additional question coming from Wood& company Atinc Ozkan please go ahead.

Atinc Ozkan

Thank you, Clara. One more from me. Can you clarify whether you have already started shipping through Colt Canada, this 20 21,000 rifles and I guess 4.5 million ammunition for

Ukraine. It was there any contribution in second quarter coming from this contract? Yeah, and it was one of the slide number three that was a significant part of it done and it will, it will continue still in q3 for us, you know, you have to look at in a way that for Canada, it's partially replacing, I mean, it's not fully about partially replacing the current business, right? Because it's basically one customer.

Jan Drahota

Right. So it's kind of a anatomy. So are the Government of Canada. So it's, so is there and it was, it was partially or significant are quite a bit, in q2, q2 and still will be delivered, and they still will deliver in September this year.

So it's going to be completed in September?

Yeah. Yes, it will be completed in q3. Yes. Within two feet should be completed. Crystal clear. Thank you.

Klára Šípová

Ladies and gentlemen, if you would like to ask question, please raise your hand in teams application, or speak directly to the phone. If we don't have any questions from the analyst, maybe we would like to keep space. Oh, additional question from Peter Bartek from CSAS.. Peter, go ahead.

Petr Bartek

Thank you. I have a question. Regarding the US dollar market, if you can be a little bit more specific with what to expect in the second half of this year, maybe in terms of fear on ear development, or in comparison to the first half or whatever.

Jan Drahota:

On the US commercial market overall or for our bands for the market overall. Okay, so expect that only recording of I don't know, 10% Compared to last year, we think that the market has bottomed, you know, kind of, you know, we believe that the market will not decrease by double digit obviously depends on what you use as a as a base, but we believe that the market is, is kind of stabilizing. And we see, we see, you know, some Sunday, Monday in certain markets. So there are categories, and it's, let's say, going out like this in the categories, but we don't expect significant weakness of the market, we believe that the market is, you know, relatively strong, but weaker than 2020 to 120 or 21. And, and we believe that it's kind of bottom up, buttoning up. So I think that we think that we are quite, I would say cautiously optimistic, maybe one more comment here. You know, we were able to significantly outgrow the market on cold side. And it was not the case for CZ. So when I look at it from perspective of how we should look at it, and this is what we always say the answer is and actually, we had a management meeting in Canada, two weeks ago, and I said that the fact that we did not outperform the market on CZ site is a shame on us. And we have to pick up because we believe that we have the CZ and he's a great brand and definitely with great products. So you know, I mean, there was a one off issue that one of the impact of really, quite significant drop of demand for scope will free but we believe that going forward, there are new products which we can capitalize on. So you know, on our ambition has to be and will and will be to outperform the market. And we believe that both brands can do it. And the market

itself can have stable or not going up but definitely not going down. Double digit. That's what our expectation is.

But once again, we expect it I think it is we expect to serve significant more of seated products on US commercial market and we sold in the in the h1 That's that's just how we look at it. That's a multicellular view. And this is what you'd expect to happen.

Klára Šípová

Ladies and gentlemen, if you would like to ask question, please raise your hand in teams application.

If I have no questions from the analyst, I would like to give room for the media to ask questions for Reuters on Royal Bank Bloomberg.

Well, hi, this is Jason Hovett from Reuters. I'll just ask a quick question just on the investment. I saw you were saying capex around 3% of revenue this year earlier this year you were talking around 5%. So if you could just talk about what's So, what's changed in that plan?

Jan Drahota:

Thank you. I didn't say no, no, we still we still keep the guidance below 5%. So, it's only the seasonality, you know, capex is a discipline of its own. So, we still do that we will do capex, more capex, so it will not be 3.5% of our revenues for the whole year. It will be below five but it will be above 3.5 as in the first half.

Okay, okay, it was 4 to 5% of our revenues will be the capex. That's what we expected them but obviously it was complex once again as I said, you know, it's a discipline on its own and we are doing it the way to make sure that that we invest productively to capacities.

Thank you for your questions.

Klára Šípová

Ladies and gentleman, the last chance to place the question. If not, thank you very much for your participation in this conference call. Thank you, Jan and Jana, for your contribution.