Q2 2014 Earnings Call

Company Participants

- João Mauricio Giffoni de Castro Neves
- Nelson José Jamel

Other Participants

- Alexander Robarts
- Armando Perez
- Fernando F. Ferreira
- Jose J. Yordan
- Lauren E. Torres
- Lore Serra
- Luca Cipiccia
- Pedro Leduc
- Robert E. Ottenstein

MANAGEMENT DISCUSSION SECTION

Operator

Good morning, and thank you for waiting. We would like to welcome everyone to Ambev's Second Quarter 2014 Results Conference Call. Today with us, we have Mr. João Castro Neves, CEO for Ambev; and Mr. Nelson Jamel, CFO and Investor Relations Officer. We would like to inform you that this event is being recorded and all participants will be in a listen-only mode during the company's presentation. After Ambev's remarks are completed, there will be a question-and-answer section. At that time, further instructions will be given.

Before proceeding, let me mention that forward-looking statements are being made under the Safe Harbor of the Securities Litigation Reform Act of 1996 (sic) [1995]. Forward-looking statements are based on the beliefs and assumption of Ambev's management and on information currently available to the company. They involve risks, uncertainties and assumptions because they relate to future events, and therefore, depend on circumstances that may or may not occur in the future. Investors should understand that general economic conditions, industry conditions and other operating factors could also affect the future results of Ambev and could cause results to differ materially from those expressed in such forward-looking statements.

I would also like to remind everyone that, as usual, the percentage changes that will be discussed during today's call are both organic and normalized in nature, and unless otherwise stated, percentage changes refer to comparisons with Q2 2013 results. Normalized figures refer to performance measures before special items, which are either income or expenses that do not occur regularly as part of Ambev's normal activities. As normalized figures are non-GAAP measures, the company discloses the consolidated profit, EPS, EBIT and EBITDA on a fully reported basis in the earnings release.

Now, I'll turn the conference over to Mr. Nelson Jamel, CFO and Investor Relations Officer. Mr. Jamel, you may begin your conference.

Nelson José Jamel {BIO 16334129 <GO>}

Okay. Thank you, Chad. Good day to all and thanks for attending our 2014 second quarter earnings conference call. I'll start with the performance highlights for the quarter, and then João will cover the Brazilian operations in more detail. I will then return to go over the results of Hila-Ex, Latin America South and Canadian business units, as well as financial performance before opening up for Q&A. So, let's get started.

On a consolidated basis, our net revenues were up 9.2% in the quarter, mainly driven by the double-digit top line performance in Brazil and Hila-Ex, finishing the first half with a solid 13.1% increase over the same period of 2013. When looking at our second quarter EBITDA performance, our top line growth was partially offset by a one-time gross margin impact in Brazil and a flattish performance in Latin America South and Canada, leading to a 5.4% EBITDA growth. Nevertheless, we finished the first half of the year with a solid double-digit EBITDA growth.

Looking at our divisional performance, for Brazil, net revenues were up 11.3% and EBITDA increased 7.2%. Hila-Ex net revenues rose 19.2%, with EBITDA increasing 18.4%. Latin America South, net revenues were up 6.9%, while EBITDA was down 0.6%. And finally, in Canada, net revenues grew 0.8%, with EBITDA at minus 0.3%.

João, over to you.

João Mauricio Giffoni de Castro Neves

Thank you, Nelson, and good afternoon everyone. It will be impossible not to start talking about the 2014 FIFA World Cup and the big party that took over Brazil during June and July. Since 2011, when we started planning for the event, we embraced the dream of making this the best FIFA World Cup ever. It was a big dream, even more with all the skepticism we saw around the upcoming event. But we like to dream big and we never give up.

The FIFA World Cup is the biggest sporting event in the globe, and we wanted to make it even bigger. And that's what we did, and results were better than expected. During slightly more than 30 days, soccer and non-soccer fans experienced a huge party that took over Brazil, celebrating with their loved beer brands in stadiums, Fan Fests, homes, bars, restaurants and thousands of events organized around the country.

An event so big that on June 11, we had the best selling day of our history, with more than 400,000 hectoliters of beer sold in Brazil. Just to give an idea, this would be similar to selling in one day more than all of the incremental volume estimated from the Confederations Cup last year. According to our estimates, the FIFA World Cup drove approximately 1.4 million hectoliters of incremental beer volume to our business, above our initial forecast of four times the benefit of the Confed Cup.

Along with strong volume growth, we gained 90 basis points of market share sequentially, with the best monthly figure in the last two years in June. Brahma and Budweiser were the official sponsors of the event and had an outstanding performance. Brahma preference was up 10%. And now, from going forward, it will be impossible to think about soccer and not to think about Brahma. Along with market share gains, Budweiser also reached its all-time high preference.

Brahma 0.0 also continued to outperform, leading our non-alcoholic beer segment that more than doubled during this period. Brahma 0.0 has been one of the most successful innovations in the last few years. Another very successful initiative was our stadium cups. Customized for each match, it became a must-have collectible item for anyone that went to the stadiums and even the ones that didn't. They were also so disputed (6:10) that you can still find them online, auctions websites.

Within CSD, another strong performance led by Pepsi and Guaraná Antarctica, the official sponsor of the Brazilian national team. Our promotion with Neymar and other soccer stars was once again a big success, with more than 10 million PIN codes' registrations during the quarter, driving brand loyalty, new consumers and enhancing the equity of our CSD brands. We actually leave the second quarter with the best market share in CSD history, 19.3%.

The FIFA World Cup is just over and results have so far been encouraging, but we're just halfway our plan for the year. We will continue to invest behind our brands and commercial initiatives in the second half, enhancing the equity of our brands, driving volume and market share, and confident we are on the right track for building the momentum in our business we are looking for. With that said, let me walk through our operational performance in Brazil.

We had another quarter of double-digit top line growth in Brazil, with an increase of 11.3% year-over-year, mainly driven by strong volume performance in beer and CSD. Given our strong top line performance in the first half, we now expect to reach the upper end of our guidance in Brazil of net revenue growth of high single to low double-digit. Our EBITDA grew 7.2% in the quarter and 11.4% year-to-date. During the quarter, we experienced an EBITDA margin compression of 170 basis points, fully explained by a one-time packaging mix impact that I will go into detail when we talk about COGS.

Brazil Beer net revenue grew 11.2%, with a volume expansion of 7.2% and a net revenue per hectoliter growth of 3.8%. After a very strong performance in the first quarter, when our volumes were up 10.9%, we continued to grow in April and May and a ever stronger performance in June, driven by the World Cup and a 90 basis point of market share gain quarter-over-quarter, as already highlighted when I talk about the World Cup.

Our premium brands, led by Budweiser, also had a very strong performance along with innovation, (8:16) mainly through Brahma 0.0 and Skol Beats Extreme. Net revenue per hectoliter growth was driven by our revenue management initiative, including the World Cup without Price Increase initiative, as well as specific promotions during the time of the event.

(8:30 – 8:35) at a time when you would expect prices to soar overall, beer prices to consumers are actually growing below general inflation since December of 2013. The campaign is over, but as we move forward, pursuing the optimal balance between volume and price will continue to be key for the success of our strategy in the short and medium-term.

Our CSD and NANC business had an outstanding volume performance, mainly driven by market share gains. Net revenues are up 11.7%, while our volumes expanded 8.8%, driven by a market share gain of 120 basis points on top of an industry that grew 1.1% in the quarter. Both Guaraná Antarctica and Pepsi had a positive performance, growing market share and volumes. Our non-alcoholic, non-carbonated portfolio also showed a good performance, led by the energy drinks. Net revenue per hectoliter were up 2.6% as a result of our revenue management strategy and specific promotions during the World Cup.

Our COGS performance was the negative highlight in Brazil, as COGS per hectoliter grew 12.3%, driving gross and EBITDA margin contraction. Half of this impact was one-time though, driven by a negative mix impact related to the World Cup. Our performance was also impacted by higher currency hedges, partially offset by more favorable commodity hedges, in line with our view for the year. Important to mention, our guidance for COGS per hectoliter remains the same, and we don't expect any significant further impact year-over-year from mix shifts as we head into the second half of 2014.

SG&A was 5.3% higher, driven by increased sales and marketing expenses, as we kept investing in our commercial priorities and behind the initiatives related to the 2014 FIFA World Cup, and higher distribution costs explained by volume growth and increased weight of direct distribution. Moving forward, while continuously investing in our commercial priorities after the World Cup, we remain committed to our full-year guidance.

Before I hand it over to Nelson, I just wanted to go through the quick summary of Brazil. First, we closed the first half with a solid double-digit growth for both top line and EBITDA in Brazil, which grew 15.3% and 11.4% respectively, while gaining 90 basis points of market share on a sequential basis to 68.4%. Second, the 2014 FIFA World Cup was a great success by any measure and a very unique opportunity to leverage our sales and marketing strategy.

Third, we reiterate our full-year guidance, but now expect our net revenues to be at the upper end of our high single to low double-digit growth. And finally, as we move forward, this is the year to once again build the momentum into our business, after three years of softer volumes and in particular a tough 2013, when we faced high food inflation, at a time beer prices were up double-digits to offset the big tax increase into late 2012, weather also didn't help, and disposable income growth, whilst still positive, was weaker.

We decided to take advantage of the positive industry momentum that should happen in 2014 and take the most out of it to fuel our top line growth, pursuing an optimal balance between volume and net sales per hectoliter, and aiming at the price to consumers back to general inflation levels. This is what we mean by building the momentum that will drive our business not only in 2014, but 2015 and beyond.

As we go after that, we have a robust sales and marketing plan that's starting in January and will continue to be executed throughout the year focusing on enhancing the equity of the brands and connecting with our target consumers in different need states and consumer occasions; improving our pack price strategy; expanding the distribution of the 300 ml and the 1 liter returnable glass bottles; leading the growth in the premium segment through our international brands Budweiser and Stella along with the local jewels like Original and the Bohemia family; expanding consumer occasions through packaging and liquid innovation; improving the consumer experience with our brands through investments in point of sales and our franchises; and executing specific plans at target geographies where we see volume and market share opportunities.

As said, the World Cup is over, but we'll continue to invest behind our brands and commercial initiatives, while balancing the volume and price to maximize our top line growth. Nelson, over to you.

Nelson José Jamel {BIO 16334129 <GO>}

Thanks João. Let's take a look at our performance outside Brazil now. Beginning with Hila-Ex, we delivered R$141 million of EBITDA, 18.4% above last year. This performance was led by the Dominican Republic, as our top line was up double-digits, mainly driven by strong volume performance. Our EBITDA also grew double-digits. We come out the quarter (13:12) of margin expansion, as we continued to capture cost opportunities from the integration. In Guatemala, our World Cup execution and the launch of Presidente were important drivers of volume growth and market share gains.

Turning to Latin America South, EBITDA in LAS declined 0.6%, driven by the challenging economic environment in Argentina that significantly impacted the second quarter volume performance. During the second quarter, we faced in Argentina double-digits decline in April, followed by lower mid single-digit decline in both May and June. Important to say, July volumes already showed signs of recovery.

Top line in Latin America South was up 6.9% (sic) [6.8%], with volume decline of 4.4%, offset by net revenue per hectoliter growth of 11.8%, impacted by the later timing of price increase and targeted promotions. COGS per hectoliter in LAS was up 13%, impacted by packaging and labor-related costs, as well as lower [ph] dilution (14:17) from volume decline. SG&A excluding depreciation and amortization was up by 16.2%, driven by a higher sales and marketing expense and distribution expense driven by the World Cup and inflationary pressures in Argentina.

We remain cautious about the overall environment in Argentina. Nevertheless, we have seen volatility in Argentina before and have the know-how to deal with it, leveraging on our strong brands and a very experienced team in place fully committed to keep delivering strong results in the short and medium-term. Looking to the second half of the year, our revenue management initiatives and our focus on tighter cost management in Latin America South to adapt to the industry conditions will be key drivers to protect our profitability.

Finally, Canada, in the second quarter, (15:09) reported volume grew by 7.1%, driven by the inclusion of the Modelo brands in Canada into our portfolio for the first full quarter, as well as some signs of industry resurgency due to improved weather. Despite the continued competitive environment, our brands had a good performance in the second quarter, as Budweiser and Bud Light both retained their momentum from first quarter.

Likewise, our high-end portfolio continued to build equity and was further boosted by strong share performance from Stella Artois to start the summer, as well as successful liquid innovation launch for Shock Top and Rita families. Our net revenue per hectoliter was roughly flat at 0.4%, effected, a little, the impact of our revenue management strategy, while COGS per hectoliter increased by 3.4%, driven by product mix and currency hedges.

SG&A excluding depreciation and amortization expense rose 1.2%, driven by our sales and marketing investments, which are mainly concentrated in the first half of the year, including innovations such as Shock Top extension, the 8 ounce "Quickie" cans and the "3 Below" Coolers. As a result, our normalized EBITDA was almost flat in Canada versus a year ago.

Looking forward, we will continue to focus on the balance between reinvigorating the core of our business, while taking leadership of the segments growing the most in Canada, the high-ends. As we execute our plan, we expect a stronger top line performance through the second half, mainly driven by revenue management strategy, that along with an improved cost management should drive better results as the year progresses.

With that, I would now like to go through the main items between the normalized EBIT of a little over R$2.8 billion and profit of nearly R$2.2 billion in the quarter. Our net finance results were a negative R$298 million, an increase of R$30.7 million versus second quarter last year, due to high interest rates, mainly driven by one-time expense associated with litigations.

The effective tax rate corresponded to 10.4%, benefiting from higher interest on capital and partially offset by lower benefit from amortization on tax books and other tax adjustments. As a result, our normalized profit was R$2.2 billion in the quarter, 16% above last year, and our normalized EPS was up 16.7% to R$0.4 (sic) [R$0.14] in the quarter.

In terms of cash flow, we generated from operating activities almost R$3 billion in the second quarter, which represent an increase of nearly 16% versus the second quarter of 2013 with an improved working capital management. And this strong cash flow generation support the announcement on July 14 of a dividend and interest on capital distribution of R$2.5 billion that will be paid as of August 28. Year-to-date, we have announced close to R$8.5 billion in cash payout, a 6% (sic) [67%] increase over the same period of last year.

Now, Chad, could you please repeat the instructions for Q&A?

Q&A

Operator

Certainly. We will now begin the question-and-answer session. Our first question comes today from Fernando Ferreira with BoA Merrill Lynch. Please go ahead.

Q - Fernando F. Ferreira {BIO 2389113 <GO>}

Thank you. Good morning, João, Jamel. Thanks for taking my questions. My first question, just looking at your guidance, it seems that you're still confident that this margin pressure was mostly a one-off in Brazil and that we should see normalized levels in the second half. Just wanted to get more color on that front, please.

A - Nelson José Jamel {BIO 16334129 <GO>}

Okay. Hi Fernando, this is Nelson. I think the main – as I tried to highlight, the main item that put pressure on all the margins in Brazil, our EBITDA margins – and actually now the gross margins in the second quarter was the COGS per hectoliter performance that was a double-digit increase. And when you look into what drove this increase, I would say that more than half – or around half of it was driven by a unique situation, which was an important change in terms of packaging mix in connection to the World Cup.

So, the special packaging and the increase of cans as a percent of our total mix drove this increase. And we don't expect any material impact as such for the second half. So, that's why we really emphasized this impact as the element that drove the margin compression in Brazil this quarter, if we would say just for the sake of the analysis, right. Just consider or look at the cost performance at the constant mix, our margins would be pretty much flattish in Brazil. And of course, given the strong top line performance, that's what we would have seen.

Q - Fernando F. Ferreira {BIO 2389113 <GO>}

That's pretty clear. Thank you. And then I had a question on Beer Brazil. Given the decoupling we saw from the production data and sales in Q2, I just would like to get a sense, how are inventories in the system and what can this mean for your sell-in volumes during the third quarter?

A - João Mauricio Giffoni de Castro Neves

Hi Fernando, this is João. We never talk really about the specific levels of inventory or the (21:16). I mean, it's there. It's available, and it's production and not sales, right. But what we said is there was no necessary build-up when you put everything together. So, we continue to be optimistic, as I think we said in the speech. We had the idea of really building momentum this year. So we already (21:39) promised a few things to ourselves, which was to take advantage of the World Cup as a good year and give also the tough comps to work on the volume side. We came from three years of, let's say, tough volumes and a good pricing, which overall gave us good results; bad results in 2011 and 2012 and softer on 2013, but still double-digit.

And we thought this is the year to have prices to come in line with the inflation, and there is a cost to that. And the volume so far is more than offsetting it. And in the World Cup, as I said in the beginning, (22:15) working better than expected, one from the volume side, which we said 1.4 million hectoliters against 1.2 million hectoliters, but for sure from the market share and from all the brand health indicators. So when I look forward, not just on 2014, but 2014 and beyond, I get excited. If you look at the volume drivers – not to just talk about the inventories in the short-term, which is definitely not a problem. I look at price to consumers trailing below average inflation, which is in line with the stuff (22:43) I just mentioned, for the year and for building momentum going forward, as we did in other times of our history.

Secondly, real disposable income growth continuing to hold regardless of GDP deceleration, and we know in our industry model, that's what counts, real disposable income and price to consumers. And third, of course, there is the better summer that we had in the first quarter, which is something that we don't control, different from price or real disposable, which we don't control, but it's a micro indicator. But that combination, even without the World Cup, the second quarter underlying volume growth would have been 2.8%, which is maybe one of the best we've seen in the last three years and around 7% for the full semester, of course which is impacted by a better summer. But you can just see how much an impact that can be either on the year or because of the tough comp. But I think that's a pretty healthy and good combination, the 2.8% for the quarter and the 7% for the full semester. So, that gets me excited in a sense that what we've been doing so far has been working. So, we're taking the brands, we're taking the share to new levels. Then, we still have a lot in-store to be done for the year and for the medium-term.

Q - Fernando F. Ferreira {BIO 2389113 <GO>}

That's clear. Thanks João.

A - João Mauricio Giffoni de Castro Neves

Thank you, Fernando.

Operator

Our next question comes from Lauren Torres, HSBC.

Q - Lauren E. Torres {BIO 7323680 <GO>}

Good morning. If I could just follow-up on the EBITDA margin comments and question you had, I understand the issue and the concern obviously in the second quarter and that that shouldn't be as much of a factor in the second half. And I know you don't give quarterly guidance. But with that said, I think you'll be cycling some tough margin comps in the second half. So I don't know if it's fair to say that looking at the first half and what you'll be cycling in the second half that it will be hard for you to actually achieve a margin improvement on the EBITDA line for the full-year. Is that an okay assumption or there's initiatives in place where you think you can improve margins?

A - Nelson José Jamel {BIO 16334129 <GO>}

Hi Lauren, this is Nelson. As you said, we don't provide specific a guidance on EBITDA margins, right. The guidance we provide on the different drivers of the business, we already talked about that, what to expect for net revenue, which is at the upper end of the range we provided in COGS per hectoliter and SG&A. But also, no doubt about it, we're going to have a tougher comp, particularly in Q4. As you know, when I talked about that before, given the one-time gains we had last year and, again, particularly Q4, the one related to the pension costs. So as I said, there is no specific guidance on margins. But at the same time, we stick to our full-year guidance.

And actually, when you look at our EBITDA margin on a quarterly basis, what we think, is not the best approach, as you have different factors such as seasonality, the phasing of commercial investments, which were, for us, concentrated in Q2 and Q1 this year, given the preparation for the World Cup, the one-offs I just mentioned. So, the quarterly margins are something we don't really look at as the best way of looking at the business. I think the bottom line is that we like the margins we have. We don't see ourselves at the margin peak. That actually has been the view of the last five years, 10 years. And at the end of the day, we always were able to increase it over time in the longer run. Of course, there's some quarterly volatility, because of the factors I just said. And always bear in mind that low-hanging fruits are not there anymore.

But still we think we have the levers like from innovation (26:29), liquid innovation, industry growth, a healthier industry, especially with the building momentum of this year, which could drive fixed cost dilution. We know that; the next time volumes are up, we have a natural improvement in margin, given fixed cost dilution; further efficiencies, productivity improvements, to name a few. So, we like to say, we don't say ourselves that the margin peak. But we'll comment (26:54) on a quarterly-by-quarterly basis because of the natural volatility. I think, particularly this year, as was said, we're working to build momentum into our business, and at the same time, results are coming, right. We look at both top line and EBITDA growing double-digit. So, that's what João, I think, already emphasized in terms of the strategy for this year. Now João's going to add something.

A - João Mauricio Giffoni de Castro Neves

Yeah. I would like to say, first, I think, as stressed Nelson, I think there's still a lot to gain, okay, in terms of margin when we look long-term. And from time-to-time, we have to take advantages of the – as we also said before, when you have strong commercial initiatives, when you have a big event as we had in Brazil, how can you best position yourself to do this. And it's good to do that from time-to-time, to either revert trends that you don't like or to actually build trends that you want get to.

So, I think this is one of those special years that we can either revert things that we see that we don't like, but really also fuel and enhance and take advantage of either a big event or things that we have in-store that can combine (28:08). And I mentioned some of them, right. I mentioned enhancing the equity of our brands; guess what happened? Best levels for Brahma ever, best levels for Budweiser ever, one of the best overall that we had in the last few years.

And then I said improving, also, share. Once again, best in a couple of years. And depending on how you look, also best in three or four years. We said we will double the size of the premium segment. Guess what, we pretty much got there for one quarter. We said let's lead that segment with a combination of programs. Once again, guess what, we are there. Let's give consumers new occasions with different programs and franchises. Let's provide events for everybody, so that they did come back to the bar.

Guess what, we're going to do close to 100,000 events this year, a knowledge that we built along the last two and three years that's very hard to copy. That's a knowledge and a know-how that we didn't have three years ago, making a huge difference in order to bring this World Cup for everybody. But also that means people once again going out, enjoying our beers, enjoying an occasion. And so, that's sort of it; a long answer for a short question, but excited with the long-term, and for sure, building the right things in the short-term.

Q - Lauren E. Torres {BIO 7323680 <GO>}

Okay. And if I could just ask a quick follow-up to that, I appreciate those comments on your business, and obviously that's where the focus is, about initiatives you have in place. And yourself and InBev seem rather confident or modestly positive, I guess, on the consumer. But in the next 12 months, are you seeing signs of a recovery? Obviously, you had the bump from the World Cup. But as we think six months to 12 months out, are there indications that the consumer is coming back and you're seeing more glimmers of hope in the whole story?

A - João Mauricio Giffoni de Castro Neves

Again, without giving any volume outlook, you know we're not going to get you to that level of detail. I think there's a couple ways to try to give you some of our views, okay. First, too early to talk about, let's say, 2015. I think we've been saying, for sure, World Cup will be a hard comp. But we continue to see, on the long-term, very important drivers. LDA growth for Brazil, projected to be 1.5% every year until at least 2030. We'll be a young nation, the way the books are written, or the way the theories look until then. Real income growth, which is a big lever for us, continues to be positive, okay; continues to hold despite GDP. So, GDP is not the best metric.

There is incremental benefit from all the things that I told you that are not macro. How do you prepare yourself for a tougher macro? It was the right year to bring prices more in line with inflation, okay. When we look at the underlying 2.8% of the second quarter; again, that's a healthy growth. In July, it's too early to think about it, because you're still impacted by the World Cup. So, we haven't entered August yet. So, if July was a reference, but I don't think it is. So it's not worth going there, because World Cup was here, was until July 13. So, I think those are the good things, short-term positive, long-term positives.

This semester, we'll have to have a few more months. But there'll be ups and downs in volatility, but too early to give a view. I'd rather give a view on the very short-term that we went through or we're looking, and the medium-term is, let's say, 2015 and beyond. Semester is – we're not going to give the details on; there's elections; there's volatility, but again we're very excited with the plans, which make a difference to whatever development to look or the total top line, which is what we gave the guidance for.

Q - Lauren E. Torres {BIO 7323680 <GO>}

Okay, great. Thank you.

A - João Mauricio Giffoni de Castro Neves

Thank you.

Operator

The next question comes from Lore Serra of Morgan Stanley.

Q - Lore Serra {BIO 20729753 <GO>}

Thank you very much. I guess I wanted to ask a couple of questions around the theme of pricing. And I understand the point that you're making that it was the right year to take the pricing down and support volume growth. But the amount of pricing change quarter-on-quarter seemed very strong. And I wondered if you could just comment on where all the change was coming from in terms of the stepped up pricing. Were you leading that? Was the market leading that? And then as you think forward and you think about what's coming toward the end of the year, what's your level of comfort that you still have the pricing lever, if the taxation scenario doesn't get any better? I take the point that the volume growth of 3% ex-World Cup, which is good. But the pricing in the quarter seems to go down more than just what sort of the mix alone would sort of imply. Thanks very much.

A - João Mauricio Giffoni de Castro Neves

Thank you, Lore. Thank you for the question. The sequential pricing impact was all related to all of the commercial initiatives related to the World Cup. When we look at the first half results, the net revenue growth is actually in line with the 12-month inflation. I think that's important, which is consistent with our revenue management strategy. And volumes are up high single-digit when you take the full semester, leading to double-digit top line growth, which is the focus for the year.

So, it's not only looking at volume, it's not only looking at price, but looking at the combination. Totally led by us, giving that if it's led by the World Cup and we're the main sponsors, as a consequence. And the drop is totally related to that. So, it's activation, it's promotions, it's the cans, it's that combination of things that happened during the World Cup, with all the benefits of all the memorable experiences and the volume. So, there is the lasting effect of the brand health, okay; as always, the very positive volume pick-up that we have.

Talking about going forward, the longer we can work with situations like summer without price increase, World Cup without Price Increase, with minimum impact on your net sales per hectoliter, the best. That for sure, of course, will depend on the tax outlook. So, pricing in consumer, I think we are in a good situation today, right. But this will be impacted by the decision of what's going to happen with federal tax, which we don't know. We, of course, continue to work very closely with the sector, with the government. That's why we've been seeing those postponements, which of course were official. The decree was fully reverted, okay, which of course is good news. Dialog is working. What was set out there is that whatever comes should be gradual.

So, the combination of postponing and saying it's going to be gradual, it's a welcome decision, which I think was done because we're doing our part of the work showing that there is a win-win situation in tax collections, jobs and investments, and I think they are seeing that this is a reality. If volumes grew 10%, 12%, whatever in the first quarter or semester – this is tax collections, right, with us maintaining high levels of investments, jobs being created and all that. So, I think it has been a win-win so far. And at the same time, I think we are both looking for a situation where there is less pressure on the pockets of our consumers.

So by coincidence or not, we both want the same thing. So having us coincide on at least three things, which is investment, jobs and pressure on inflation, the only part that we may not totally coincide, of course, are the tax collection. If we can bring that through, through volume growth, then maybe we fully expect the same thing. And we can continue this healthy dialog that has been taking place not just in the last two years, but should be going on as probably in the last six years or so. Whatever happens will impact our decision. We're working to the scenario where we can have the less pressure on our consumers. But what's official is what I just said, gradual and postponed.

Q - Lore Serra {BIO 20729753 <GO>}

Great, thank you very much.

A - João Mauricio Giffoni de Castro Neves

Thank you so much.

Operator

The next question comes from Luca Cipiccia of Goldman Sachs.

Q - Luca Cipiccia {BIO 6914452 <GO>}

Hi, good morning. Thanks for taking my question. Just starting with one point on capital allocation, if possible. Your balance sheet keeps getting stronger even now and somewhat a slight reduction in CapEx guidance for this year and looking ahead arguably, it doesn't seem realistic to expect that that may re-accelerate. So assuming that acquisition opportunities are not necessarily there, if not secondary, but if so, what will happen at the API (37:57) side, what really should we factor in or consider? Is there really a constant increase in dividend and payout? Is there another way we should think about this? Can you maybe discuss a bit that looking forward for – not necessarily for this year, but also for the outer years, for the outer outlook?

A - Nelson José Jamel {BIO 16334129 <GO>}

Okay. Hi, Luca. I think in terms of use of cash and the capital allocation, we have been consistent over time. And as a result – of course, we always try to reinvest in the organic growth of our business. We have, of course, some targeted M&A opportunities, particularly in Central America, and always looking to maintaining the adequate levels of liquidity. But given the strong cash flow generation, and I just talked about that in Q2 cash flow generation from operations was around R$3 billion, and of course, that supported the announcement we did of R$2.5 billion, which adds up, as I talked, to an R$8.5 billion announced payout between dividend and interest on capital year-to-date, which is close to 70% (39:08) higher than what we had last year.

So, I think under this scenario – and of course we're not making any – or give any guidance on what to expect moving forward. But the moving pieces are those that I just talked about, and I think as we always said, we'll continue to maximize interest on cap. That's the most efficient way to return cash to shareholders. But bottom line, I would say these drivers or this rationale around use of cash remains the same, and as the business continued to deliver as we expect, of course, there is a growing trend for the payout to be of course defined over time.

Q - Luca Cipiccia {BIO 6914452 <GO>}

If I can just rephrase my question, do you feel that you're moving to a place where ultimately you're lacking options for capital allocation? I understand the point on the payout. But are you satisfied – is this the type of balance sheet structure that you would like to have, assuming that nothing else comes on the horizon?

A - João Mauricio Giffoni de Castro Neves

Well, I think, Luca, just to reinforce, I think, the point Nelson is making, I think what we're trying to say, and we've been saying this for some time and actually have been consistent with this, is we always look for new opportunities. And I think there's lots of organic opportunities that tie to the things I just said for Brazil. I see that being true for many other countries we operate. And we continue to look for non-organic opportunities as well. We saw two of them in the last two years. We entered Dominican Republic, tripling results and becoming pretty meaningful. We entered Cuba as well.

And we continue to look for bigger things as well, whether they are in Central America or the Caribbean or beyond the Latin America. I think opportunities will arise from time-to-time, and we'll take full opportunity of them. In the meantime, what we don't want stop is continuing to give back to shareholders in different forms the excess cash. Because since 1998, let's say, when we adopted to do this, we continued to do so. So, we'll continue to do both things, returning the excess cash and looking relentlessly for the organic and non-organic opportunities to deploy the cash.

Q - Luca Cipiccia {BIO 6914452 <GO>}

Okay, thank you. Just very quick, I don't want to take too much time, but just as a follow-up. On the SG&A front, on the investments related to the World Cup, you gave an indication of how much the second quarter was for volumes related to the overall. When we think about the costs and the investments, how should we allocate those between the second and the third quarter?

A - Nelson José Jamel {BIO 16334129 <GO>}

Well, of course, there was an important impact of the investments behind the World Cup. And if you run the math, of course, they were always EBITDA positive given the great volume uplift we got. So, I think that's the first message. Regarding allocation of SG&A between semesters, if that was the question, we stick to the full-year guidance. I'm not talking about specific breakdown between quarters. Bear in mind that the same way we invested in the many (42:25) commercial activities we had so far this year, as João said, we continue to support the great brands into the second semester as well. But again, we stick to the full-year guidance.

Q - Luca Cipiccia {BIO 6914452 <GO>}

All right, thank you. Thank you very much.

A - Nelson José Jamel {BIO 16334129 <GO>}

Thank you, Luca.

Operator

Our next question is from Pedro Leduc of JPMorgan.

Q - Pedro Leduc {BIO 16665775 <GO>}

Hi, everyone. Thank you for taking the question. And that will be on Brazilian beer and soft drinks, both of them. Historically, when we see Ambev gaining substantial market share, like we see in this quarter, we usually see a little bit of pricing in the following quarters, exchanging let's say market share for profitability, if you want. So is this something that – is the current market share a comfortable level, something that you guys have goaled for and now it's achieved, so we could see now more in this revenue path that you've increased guidance for actually to the high-end, more pricing-driven to balance as well the EBITDA growth in the coming quarters? Thank you.

A - João Mauricio Giffoni de Castro Neves

Hi Pedro, it's João. A very good question. Whenever we look at the – our long-term pricing strategy has been to have prices going up in line with inflation, right. And there are times when you are more pressured or there are times where you are less pressured, okay, by the market conditions. We saw being more pressure from the market since 2008, much less pressure at the end of 2010, and we have to be smart to take advantage of the things we build, right.

So, I'm not going to answer in the details of our short-term pricing strategy, right, which we never do. But what we'll say is it's always better to look into the pricing strategy when you have a better market position, which as you stated and as I said in the speech and then during the Q&A, we are in a much better place than we were 12 months ago, so it's great. So, whenever the time comes, we are in a better situation than we were before.

Q - Pedro Leduc {BIO 16665775 <GO>}

Great, thank you.

A - João Mauricio Giffoni de Castro Neves

Thank you.

Operator

Our next question is from Jose Yordan of Deutsche Bank.

Q - Jose J. Yordan {BIO 1496398 <GO>}

Hi, good morning, João and Nelson. A quick question – a quick follow-up to the topic you were talking about in Lore's question about taxes. I already noted your reaction to the government's latest announcements, et cetera. But I was just wondering when we might expect some development, some news flow on this. Does it have to wait till after the elections or will there be something – now that the World Cup's over, will there be something within the next couple of weeks or a month or so? And I guess a related question is you talk about higher litigation expenses, et cetera, during the quarter. Does that have to do with any of the longstanding tax cases that you always discuss in your 20-F? If there's any sort of meaningful change in the status of those cases, I'd love to hear about it.

A - João Mauricio Giffoni de Castro Neves

Hi Jose, this is João. On the first part, there's no control over the timeframe. The official announcement was it would be then gradual. It's sort of saying or implying that we should hear back or something could happen in September or October. But there is no specific date being set. Ongoing negotiations always, but that's I think what was said – that's what was said by them; gradual and that we should hear from them between September-October. That's pretty much it.

Q - Jose J. Yordan {BIO 1496398 <GO>}

Great.

A - Nelson José Jamel {BIO 16334129 <GO>}

And Jose, just going to your second question, yes, we talked about actually in our financial results, some one-time interest expense associated with litigations that were – actually those files are provisioned for in 2009. Nothing really to the bigger files we refer to, which of course are also described in our 20-F and there you have the full details. Actually, those files were provisioned for in 2009 in connection with federal amnesty program, and those would be paid over 15 years. What we decided to do this quarter was to settle it upfront with of course a discount on an (47:11) basis there was a gain for us. But then we had to accrue for the interest that incurred to that otherwise will be booked over time, over the remaining 10 years. So, that was the specific one-time expense we had, it was close to R$60 million and pretty much explains the full increase in interest expense booked in this line this quarter.

Q - Jose J. Yordan {BIO 1496398 <GO>}

Very clear, thanks. And if I can just follow-up real quick with another sort of accounting question, are you able to tell us how much excess cash is still trapped in Argentina?

A - Nelson José Jamel {BIO 16334129 <GO>}

So in terms of cash in Argentina, it's a reality that our ability to take the money out remains an issue, given how the volatility in the country, and we have an amount of excess cash in the country, that we to continue to look for investments either to support the business growth or to repatriate them. But it, as I said, remains an issue, given the lack sometime of Central Bank authorization. We are not disclosing specifically the amount we have there. But Argentina, regardless on how we look at the results, they're around 10%. 8%, 12% of every single line of our balance sheet or P&L. So, that's pretty much how we manage that. But we continue to work towards the repatriation of this cash and that describes the struggles we have there.

Q - Jose J. Yordan {BIO 1496398 <GO>}

Great, thanks a lot.

A - Nelson José Jamel {BIO 16334129 <GO>}

Thank you, Jose.

Operator

Our next question comes from Robert Ottenstein of ISI Group.

Q - Robert E. Ottenstein {BIO 1498660 <GO>}

Great, thank you very much. Can you give us an update of where you are in terms of the Budweiser brand and the Corona brand in the region in terms of what countries you have it in and where you may be able to get it in within the end of this year and next year?

A - João Mauricio Giffoni de Castro Neves

Oh, hi Robert, it's João. Thank you. Starting with current situation in Brazil, outstanding result with Budweiser, as I said, both in terms of share and preference and actual volumes, growing significantly with a premium contribution margin. So, enhancing our premium position in every way, shape or form. With Corona, this will be a super premium brand here in Brazil. We will launch now in the second half and increase towards the end of the year, and increasing from there with the goal of mimicking the prestige position that the Modelo Group built along the last few years in many other countries.

Actually, I think what happened is that they attribute a very strong position in most of Latin American countries. I think we did a good job of not giving them much space to grow in Brazil. So right now, the brand's sort of inexistent in Brazil, which is great. So, it can start from a fresh start and we'll do a very job on doing this. And at the same time, it's great that it has very strong position in other places throughout the Americas. Canada, growing 7%; it's a very strong positioning now in our portfolio, giving us 2.6 percentage points, 2.7 percentage points of share growth, 7%-plus of volume growth. So, Canada is done. With Guatemala, it's also done. We'll have a launch of not just Corona, but also the Modelo special brands at different price levels. So, it give us a full portfolio, a very strong portfolio for Guatemala, especially if you look at the neighboring countries.

Also closed a deal for Argentina. Already had closed the deal for other countries, such as Uruguay, Peru. So, a lot to be done; still a few countries to go. We're also doing that for – now we have a strong position in the Caribbean. The Caribbean, I think I mentioned last call; we have a very strong portfolio, as we go to those countries with Presidente. We have three local island brands and you go with Corona and Stella and Budweiser, you are a full shop when you get to countries like this. So, a very strong position, we're getting them in most countries. There's still one or two big countries to be negotiated, but we already have in many of them. In some of them, like Canada and Guatemala, big launches being done this year. And with the closing of the deal in Argentina, big launches also for next year, very exciting with both brands.

Q - Robert E. Ottenstein {BIO 1498660 <GO>}

That's terrific. And as you look at your strong market share sequential increase, obviously, the World Cup was a large part of that, and I'm assuming a lot of those gains were Brahma and it sounds also like Budweiser. Would you expect in the second half of the year, on a sequential basis, for your market share naturally to ease up a little bit? Or do you think you have enough momentum to keep or perhaps even increase where your market share is for Beer Brazil?

A - João Mauricio Giffoni de Castro Neves

Yes, Robert, we don't really give any guidance in terms of market share outlook in specific. Historically, in Brazil, we increase share after certain months of price increase and so forth and so on. We have said as more of a market share guidance long-term to be in the 67% to 69% range. So, that's more of the guidance. So, we always like to be looking for being in the upper range, and this gives us more flexibility.

So, I think the nice thing about where we are right now is that we are building that momentum, building the flexibility, looking for the upper end of this 67% to 69%. And therefore, that will give us options. It's always better to be at the strong commercial momentum position. That's what we're building. I don't think we are there yet. I think there's still momentum to be built, right, and I think that's as much as I can say without then compromising any particular strategy.

Q - Robert E. Ottenstein {BIO 1498660 <GO>}

Understood. Could you perhaps give us any kind of sense about how much market share Brahma 0.0 was able to get?

A - João Mauricio Giffoni de Castro Neves

I think what we can say is what we said in the speech. That we said has grabbing more than half of the market in a very short period of time.

Q - Robert E. Ottenstein {BIO 1498660 <GO>}

Great, thank you very much.

A - João Mauricio Giffoni de Castro Neves

Thank you very much.

Operator

Our next question is from Antonio González of Credit Suisse.

Q - Armando Perez {BIO 18956695 <GO>}

Thanks everyone for the call. This is actually Armando Perez. My question is regarding Argentina. Do you think that, with the increasing salaries in the second quarter, you can increase prices to go for higher labor cost? And how's these salary increases resulted in pricing maybe in July or at least in a qualitative level? So thanks.

A - Nelson José Jamel {BIO 16334129 <GO>}

Okay. Well, I think the key message around the whole situation in terms of salary increase and catch-up with inflation is that, as we said, obviously the macroeconomic environment remains challenging. But we've seen an improvement on a sequential basis since April. April was kind of a double-digit drop and then has improved as salaries started to kick-in. I think that's the most obvious way to see how it can impact our business.

But of course, we go beyond that. We continue to work on our revenue management strategies. And of course, without getting into details for competitive reasons, our goal is always to drive top line growth in line with inflation, and of course, work on the cost side, which is part of the DNA of the company. And I think, as we've always emphasized, we have a strong team, we have a very strong brand, a great portfolio in the country, and we continue to use the full tool kit to manage costs.

We have been there many times and know how to work in this environment. So, we had still volatility in Argentina before. We know how to deal with it. And back to your point, I think once inflation was accelerating since the beginning of the year, consumer real disposable income was, of course, significantly under pressure. But this has been easy as salaries increase, and it started to kick in along the way once labor agreements were reached. So, that's what we see as good news and the main driver for the outlook for the balance of the year.

Q - Armando Perez {BIO 18956695 <GO>}

Okay, thanks a lot.

A - Nelson José Jamel {BIO 16334129 <GO>}

Welcome.

Operator

Our next question is from Alex Robarts of Citi.

Q - Alexander Robarts {BIO 1499637 <GO>}

Thank you. Hi, everybody. Two questions on Brazil, and I wanted to put the first one on the COGS per hectoliter trend. When we think about the quarter's margin contraction in Brazil as well as the margin contraction in the first half, it seems that really the driver is COGS per hectoliter outpacing the revenue per hectoliter. And I appreciate that half of this is structural because of the net effect of your hedges and such. But the other half is – it seems is this packaging mix shift and is connected to the cans. And I'm wondering, as we think about it into the third quarter, you have July that still have the cans related to the World Cup. How should we think about this COGS per hectoliter trend into the third quarter?

What did cans actually get up to, if you could kind of share that with us, in your product mix for Brazil? I'm talking about Brazil Beverage here. And what could be a more normalized level looking out into the second half? And I appreciate you haven't changed your COGS per hectoliter guidance in a constant packaging mix basis. But we can't see that, right? So, maybe you could help us with what was the COGS per hectoliter on a constant mix basis movement in the quarter? So, that's first question, and I have one on soft drinks side. Thanks.

A - Nelson José Jamel {BIO 16334129 <GO>}

Okay. So specifically about the COGS, I think we talked about that. It not only explains half the packaging mix impact, right, will only explain half of the COGS per hectoliter growth, but the full impact of EBITDA margin compression in Brazil. So, I think – and of course we tried to emphasize that it was a unique situation in the sense that, as part of the World Cup, all the special editions, the activation in the (59:06) premise. The promotions drove, of course, lot of our one-way (59:09) mix into our portfolio was sort of similar to what we see normally during Carnival period. But instead of a week of Carnival or two, we had the full month. So, it was expected in a way. And then when you look towards the year, we see a more balanced mix, back to the normal way (59:36), if you will. And so as I said, going forward, we don't expect any further significant packaging mix impact in our COGS or driving negative impacts on our margins. I think that's the first key message you should take.

Q - Alexander Robarts {BIO 1499637 <GO>}

Okay. But as far as a percentage of your packaging mix, can we think about cans being 20 – 25% of your mix on a normalized basis? And with the growth of supermarkets – and I appreciate that 300 ml is there, returnable trying to offset this. But can we – when we think about cans looking out two years or three years, does the percentage of cans in the packaging mix – do you see it increasing over time or is it something that really can be mitigated with the 300 ml returnable glass?

A - João Mauricio Giffoni de Castro Neves

Yeah. Hi Alex, this is João. If we look at the last 25 years, there's been some growth in cans, right. With supermarkets being one of the trends, although the trends of supermarkets today is that the growth of supermarkets are more the one to four checkouts than the hypermarkets. So the one to four checkouts of supermarkets are the one that have more RGBs when you compare with hypermarkets for example.

And therefore, the trend in cans actually from 2011 to 2013 has decelerated when you compare from 2008 to 2010. So the last three years, it was growing less, at a lower pace than what we grew in the three years before, probably from the combination of this growth of supermarkets from one to four checkouts and the introduction of the liter and the 300 ml, right.

In 2014, I think what Nelson was saying is that it's sort of a one-off type of year, because you have three summers in a row. You had the summer and then you had the World Cup, which is the big summer with giving events and giving stadiums and giving cups and giving all this, cans had a higher participation, higher mix, and then you have the summer again. So, this is a one-off year and that's why we said in the gross margin, this is a one-off quarter. And therefore, then it should just be more of the secular trend rather anything different from that.

A - Nelson José Jamel {BIO 16334129 <GO>}

And even when you think of Q3, I think what – we can say that, as we said, that the significant impact of the FIFA World Cup uplift was around 1.4 million hectoliters. But 80% of it, let's say, belongs to the second quarter. So, it would be a marginal impact to Q3. I think (1:02:29) as well.

Q - Alexander Robarts {BIO 1499637 <GO>}

Okay. Okay, that's helpful. So first half COGS per hectoliter in Brazil, right, up 8.3%, what would that have been on your guidance metric, which is the COGS per hectoliter on a constant mix basis? Would have been much lower, right? Is that fair?

A - Nelson José Jamel {BIO 16334129 <GO>}

Yeah. Out of the 12% that we had in Q2, we said half of it was mix-driven. So let's say, take 6% out, you have still 6%. We were around 5% or 4.8% in the first quarter. So, the blend of the first half would have been mid single-digits, consistent with our full-year guidance. And as I said, we don't expect any further relevant impact going forward into the second half. So, we should again be more in line with the guidance for the product mix.

Q - Alexander Robarts {BIO 1499637 <GO>}

Okay, that's helpful. Nelson, (1:03:22) thanks. And then the last one is just on soft drink. Clearly, looking at your volume trends in CSD and NANC in Brazil in the quarter, you had almost 9% of volume growth. Industry was 1%. We understand from the Coke system that they were low single-digit. So, the market share was substantial. And I guess just trying to understand the driver here. You had the CBS (1:03:55) sponsorship around Guaraná. And is that kind of really the main tailwind as we come into the third quarter? Do you see this kind of volume expansion into the third quarter with the sponsorship and Guaraná and pricing there or is just kind of maybe your non-carbs that are doing and getting some new traction? So, I'm just kind of trying to get a sense of this very, very heady volume growth that you've posted here in this soft drink business?

A - João Mauricio Giffoni de Castro Neves

Well, very good question, Alex. We're very excited with the quarter, but really very excited with the whole CSD and NANC business unit. To be quite honest, you're right, it was a hefty – a pretty heavy gain, especially for the World Cup. During the World Cup, as you know, maybe for some people may be somewhat unexpected, given the other sponsor. But we've really been gaining share since the first quarter of 2011 on a rolling 12 months basis. This is the third year in a row that we're gaining share, anyway if we look into the share. And therefore, the initiatives are not just a one thing. There's no silver bullet. It's really a combination of many things starting with pack price. So pack price, I think we're doing a good job, both in the single-serve as well as in the multi-pack.

So, if you think about the single-serve, we have the PET 237 ml. It's been doing great since its launch three years ago. We've been launching this throughout the country. We have it pretty much everywhere. It's growing 20%, 30%, 40% every year since we launched that. In terms of multi-serve, we have launched end 2011, beginning 2012, the Guaraná Antarctica little bottle, once again doing great in every way, shape or form. And then, in the beginning of this year, late last year, we also launched the Pepsi liter, which is far away from where it can get. So that combination of 237, the liter – the liter for Guaraná and the liter for Pepsi, that helps.

We're increasing our execution in the off-trade, a very good job being done by the business unit through different ways. So if you were in Brazil in the past few months, you'd see a really great execution, taking advantage that we had the sponsorship, taking advantage that we had Neymar, taking advantage that we have all the other soccer stars. Building new platforms also for Pepsi, so it's also doing great. That's combined volume growth for both CSD and NANC. So therefore, the share gain that we focus is more towards the CSD.

But again, we launched both Fusion and Monster as energy drinks. And in some channels, we're already the number two player. So in a very short period of time, depending on the channel, already the number two player. We aim for more – for total market, a very profitable industry as well. So, no silver bullets, combination of many things, but brighter future ahead in terms of market share continuing to be very strong.

Q - Alexander Robarts {BIO 1499637 <GO>}

Very helpful. Thank you.

A - João Mauricio Giffoni de Castro Neves

Thank you.

A - Nelson José Jamel {BIO 16334129 <GO>}

Welcome.

Operator

This concludes our question-and-answer session. I'd like to turn the conference back over to Mr. Nelson Jamel for any closing remarks.

A - Nelson José Jamel {BIO 16334129 <GO>}

Okay. Thank you, Chad, and thanks everyone for attending to this call, and I'll speak with you again on October 31. Thank you.

Operator

The conference has now concluded. Thank you for attending today's presentation. You may now disconnect.