Speakers:
- Igor Shekhterman, CEO
- Svetlana Demyashkevich, CFO
- Andrey Vasin, Head of IR
- Natalia Zagvozdina, Head of Corporate Finance and IR.

Participants asking questions:
- Alexey Krivoshapko
- Nikolay Kovalev
- Maxim Nekrasov

Operator:

Good afternoon, ladies and gentlemen. Thank you for standing by. Welcome to today's X5 Q4 and FY 2018 Financial Results.

At this time, all participants are in a listen-only mode. There will be a presentation followed by a question and answer session, at which time if you wish to ask a question you can press "star", "one" on your telephone and wait for your name to be announced.

Also, I must advise you, this conference is being recorded today, 20th of March 2019.

I now hand you over to your first speaker, Natalia Zagvozdina.

Natalia Zagvozdina:

Thank you. Good morning and good afternoon, ladies and gentlemen. Thank you for joining us today on this call where we will discuss X5 financial results for the last quarter and the full year 2018.

Participating in the call today are Igor Shekhterman, X5 CEO; Svetlana Demyashkevich, our CFO; Andrey Vasin, Head of IR; and myself, Natalia Zagvozdina, Head of Corporate Finance and IR.

Before we begin, I would like to remind you that some of the information announced during this call may contain projections and forward-looking statements regarding future events or future financial performance of X5. Please refer to the beginning of the presentation for a full disclaimer with regards to such statements. We disclosed the press release and financial statements this morning via our website, on RNS and through our e-mail distribution list. All documents and the presentation for this call are now available on our website in the Investor Relations section.

I will now pass the floor to Mr. Igor Shekhterman who will take you through the Company's key achievements and strategic priorities.

Igor Shekhterman:

Good morning and good afternoon ladies and gentlemen and thank you for joining our call today.
I would like to begin with our year-to-date results, followed by key achievements in 2018 and an update on where we are with some of our strategic priorities. After that, our Chief Financial Officer, Svetlana Demyashkevich, will take the floor to talk about the external environment and our financial results in more detail. We will then be happy to answer your questions.

- X5’s year-to-date top-line growth stood at 16.5%, our like-for-like sales rose by 5%, with traffic being positive. We are satisfied with how the year 2019 started for the company.

- In 2018, retailers in Russia faced tough market conditions, with low food inflation and continued weak consumer confidence. Despite this, our results, except for the weak first quarter, are encouraging. I am pleased with the turnaround at Pyaterochka, led by the current management team and by the continued strong performance at Perekrestok.

- The financial performance that we reported today is the result of hard work by the entire X5 team and I am grateful to every member of our team for their achievements and contribution to another successful year.

- While we are satisfied with our results, we recognise that competition remains high. We see the Russian food retail merging into a broader food delivery market, where traditional retail players are challenged by ready-to-eat food delivery services and where omni-channel becomes an essential part of the retail CVP. We retained our leadership in traditional food retail, despite the fact that we slowed down new openings and have stricter requirements for new openings in order to maintain margins and returns. Going into 2019, we have an increased focus on our omni-channel offer to customers as well as on the use of innovation and advanced analytics to achieve our longer-term goals.

Let me highlight some of our achievements in 2018.

- We sustained growth in LFL traffic and basket at the group level. LFL traffic growth accelerated in Q4 2018 at both core formats compared to the previous quarter.

- The Company’s gross profit margin in 2018 increased by 27 basis points year-on-year, primarily due to improvement in the commercial margin, resulting from a more balanced approach to promo and the format mix effect from proportionally more sales at Perekrestok. Management initiatives focused on reducing shrinkage levels in H2 2018 had a positive impact on our gross margin. Finally, higher food inflation in Q4 was also a supporting factor.

- Our EBITDA margin was in line with our internal target and remained above 7.0% for the year, despite a challenging macro environment.

- Our online offering saw fast growth in 2018 mostly due to addition of the second dark-store in Moscow. The number of online orders per day reached over 2.6 thousand in December and did not decline in the beginning of 2019. We are also piloting our last mile delivery service through a network of parcel lockers in our stores.
During the last two years we analysed technologies from over 500 start-ups, often in cooperation with specialised funds and accelerators. In total, we launched 68 pilots in our stores, distribution centres and corporate centre. Of these 68 pilots, we have 9 tech innovations in rollout phase in areas such as pricing, process automation, energy efficiency and customer personalisation.

The Company continued to develop its loyalty card programmes. In total, X5’s three retail formats had almost 38 million active loyalty card users as of 31 December 2018. Loyalty cards penetration in traffic in December reached 48% at Pyaterochka, 49% at Perekrestok and 81% at Karusel.

Based on our solid financial results, we continue dividend payments and recommended a dividend for 2018 of 25 billion roubles, or 92.06 roubles per GDR, which represents an 87.3% pay-out ratio.

Now, I would like to discuss some achievements across X5 formats in more detail.

Starting with Pyaterochka format. We were disappointed with Pyaterochka results in the first quarter of 2018, which was affected by negative trends that continued from 2017. I am satisfied with what the current team has delivered in a short period of time: our shrinkage level has been going down since Q3 2018, while staff turnover reduced by over 6 percentage points year-on-year in the second half of 2018. LFL traffic was negative in Q1 2018, but turned positive from Q2 2018 and is positive in the beginning of the current year.

In Q3 we launched a transformation office at Pyaterochka and selected 16 key projects aimed at updating our CVP, store concept, cost optimisation, logistics and other areas to assist with decision-making on pricing and assortment. Sergei Goncharov, the format CEO, is personally involved in implementing these projects.

As you know, in 2018 we slowed down new openings and applied tougher requirements for new store locations. The new Pyaterochka management team became more focused on operating efficiency. Considerable attention is being paid to reducing shrinkage and revising business processes in stores. These initiatives are designed to support margins and return on invested capital.

As we recognise the importance of customer experience and customer journey, we want to make adaptation of our CVP and product mix to the changing needs of our customers a continuous process. In 2018, we finally saw tangible progress on clusterisation for our proximity stores, and optimisation of our assortment to factor in store size, location and regional demographics, which incorporates our loyalty cards data. We are in the pilot stage of the project to automate pricing, which should provide us with a more sophisticated and more transparent pricing system.

Another project we are working on is a new automated assortment management system that will use advanced analytics. These initiatives are expected to generate a positive effect across our Pyaterochka network later this year.
Our fresh products offering is central to the Pyaterochka CVP and we keep improving their quality. We adjusted the fruit and vegetable mix and added new products such as freshly baked bread by piloting bakeries in our stores. In the ultrafresh category, we reduced supply chain delivery times by 39%.

In private labels, we shifted our focus from an entry-price offering to a unique product mix. To improve the quality of private label products, we set up a dedicated team and used feedback from customers when developing new products. We have analysed all product categories and defined the targeted shares of private label in each category.

Pyaterochka’s loyalty programme has demonstrated impressive performance to date and we consider it to be an engine to our future growth. As of December, we had 29 million active card users accounting for 64% of annual sales in proximity format, while penetration rate reached 48%, up from 42% a year before. The most loyal customers, which comprise 10% of the total number, account for 40% of sales and we believe it is critical to increase the share of loyal customers.

Another focus area last year was to improve promo effectiveness. While keeping the share of promo stable, we tried to select the most effective ones. The pilot at Pyaterochka demonstrated that we can decrease the number of promo positions by 10% without any effect on retail sales. Around 1.6 thousand targeted marketing campaigns were launched in 2018, increasing net retail sales of Pyaterochka by 8 billion rubles.

We are continuing to develop targeted promo based on Big Data analytics, in order to enhance efficiency of product selection, timing and pricing of our promo activities.

Now about achievements in Perekrestok.

In 2018, Perekrestok showed outstanding performance, hitting a record with 122 new stores opened and the highest LFL among X5 Retail Group’s formats. Its LFL traffic grew by 6.2%.

We continued the refurbishment programme, with 37 stores upgraded last year. With new openings, this brought the total share of stores operating under the new concept to 86%.

Improving fresh and fruit & vegetable quality is a top priority for Perekrestok. We believe it is key to the format’s success going forward. In response to the consumer trends evolving in Russia, we expanded the product range in fresh, fruits and vegetables and healthy food categories.

We continue adding unique product assortment by developing private labels as well as healthy, ready-to-eat and ready-to-cook products.

Green Line private label was launched to address the rising demand for healthy food among our customers. Around 150 Perekrestok stores now have special health food corners inside. Other examples of our unique private labels are Sarafanovo and Verkhovye which offer high-quality milk and other products. Such exclusive brands are a vital part of our CVP as well as our strategic partnerships with suppliers.
Ready-to-eat is another promising opportunity for X5. We are really excited about the potential to develop the ready-to-eat category for Perekrestok and we think this represents an important new wave of development for the company. In order to upgrade and expand our product offering in this category, our own Kitchen Factory will launch production in the end of March. It will also supply Pyaterochka stores in Moscow and the Moscow region and we plan to start construction of another Kitchen Factory for St Petersburg and the North-west region in late 2019.

Perekrestok is also actively developing targeted marketing. It helps to better manage traffic, boost average ticket, frequency of purchases, as well as number of items in the basket. Targeted marketing and the Perekrestok loyalty programme helped to increase retail sales by RUB 5 bn, or 2% of the format’s net retail sales in 2018.

Our efforts to improve operational efficiency started to deliver results: new regional openings now require less capex and we are testing lower OpEx model for regional supermarkets; logistics costs per box declined by 9.5% y-o-y; our incentive and training system improvements contributed to reduction in personnel turnover by 14% in 2018; we improved the promo planning efficiency, which helps us to better align promo products inventory with demand.

We continued to roll out our Perekrestok Online business. This is a separate business unit within Perekrestok that has its own strategy, its own P&L, infrastructure, logistics and team. I am happy with the results that we have seen so far. In terms of the average monthly ticket, omnichannel customers (offline + online) spend 70% more than pure offline customers. In December, the average number of orders per day exceeded 2.6 thousand and this trend has continued well into early 2019. The average check was 3.1 thousand roubles in Q4. In March 2019, the daily number of orders has reached as high as 4 thousand. NPS reached 83% in December 2018, well above our internal target. Two new dark stores that we opened in Moscow and St Petersburg in 2018 will help us to more than triple our capabilities in processing orders, as well as to double the product range. Traffic to the website increased 2.3 times in 2018 and we saw the conversion rate improve from 1.3% in 2017 to 3.2% in 2018. We have ambitious plans for our online business growth in 2019.

Finally, a few words on our efforts to improve the business at Karusel.

The hypermarket segment is under pressure in Russia and Karusel is no exception. We are not pleased with the performance in 2018, but we are focused on improving the business and implementing a number of new initiatives.

Sales density improvement remains our top focus for existing stores, combined with a conservative approach to new openings.

In 2018, we began to roll out a new concept at Karusel. Product range optimisation was a top priority last year. As product quality and health foods are becoming increasingly important to Russian consumers, we aim to expand our range of healthy products. We are considering options to improve space utilisation and increase traffic by inviting partners to our hypermarkets.
We are also testing the “large supermarket” format. We currently have two Karusel stores being managed by the Perekrestok team and we plan to transfer three more stores over to Perekrestok this year.

As part of our omni-channel approach to CVP, we plan to launch Click & Collect in Karusel hypermarkets in Moscow and Perekrestok supermarkets in Moscow and St Petersburg. If all goes well, the project will be rolled out to other major cities of the country.

Now, let me update you on our strategic priority, which is to create new innovation and omni-channel capabilities.

Our work on innovations has a primary focus on improving the customer journey, which should support our sales. Another big area where we expect to benefit from innovation is in achieving higher efficiency across the business.

The Company has now established procedures to select, pilot and implement innovations for each of the three formats. We are mostly interested in projects focusing on marketing, store operations, logistics and our service centre.

Key projects that we piloted at X5 stores include video monitoring of shelves, smart shelves, facial recognition and Wi-Fi recognition, customer queue video and AI-based monitoring. Based on successful pilots, we have taken the decision to roll out video monitoring of customer queues in all Perekrestok stores.

We operate a lab store under the Pyaterochka brand where innovative technologies and ideas are tested in a real-life environment to help us estimate their potential impact for all of our formats. Perekrestok is set to host our second lab store.

Last year, our Big Data Department rolled out a technology platform to collect, store and process data that X5 accumulates. We are focused on improving how we work with this data and the quality of our analytics. This will enable us to further enhance our data-driven decision-making. With over 100 people in the Big Data team, we are introducing several projects in data analytics for determining promo, pricing and assortment.

In addition to Perekrestok Online, in 2018 we rolled out a network of parcel lockers in our stores to generate additional traffic. Lockers are now installed in over 1.7 thousand stores. If successful, the project will be extended to the entire chain. We are partnering with a number of companies to develop a locker network.

Let me finish my speech with our priorities.

Our shorter-term goal is balanced business growth with stable returns for new openings.

For the longer term, to sustain our market leadership and profitability, we need to focus on customer experience and deploy advanced analytics on different levels of our operations and decision-making.
• First, we need to look at how we can improve the customer journey. To achieve this:
  o We should develop our omni-channel offering as part of the CVP of each format or as a separate line of business, if it does not fit in with the current CVP;
  o We must constantly update our CVP and our product range;
  o We should adopt our assortment with focus on fresh, fruit and vegetables, private label and ready-to-eat to meet our target audience demand;
  o We should better engage store personnel to improve service levels;
  o And we must further develop our loyalty programmes and targeted marketing;
  o These measures will help us to improve customer service and NPS across the formats.

• Second, we need to further develop our expertise in technologies, innovation and big data. It is already clear that retail, as many other consumer sectors, will see an increased use of advanced analytics and we should remain on top of this trend to support our business development.

Now I would like to pass the floor to X5’s Chief Financial Officer Svetlana Demyashkevich, who will comment in more detail on the company’s financial results for the fourth quarter of 2018 and our guidance for 2019. Thank you for your attention.

Svetlana Demyashkevich:

Thank you, Igor.

Good morning and good afternoon ladies and gentlemen. Let me start with the market update, after which I will give an overview of our financials and guidance for this year.

So, first I will say a few words about the external and competitive environment.

• In the fourth quarter of 2018, food inflation accelerated at a fast pace, reaching 4.7% year-on-year in December versus 2.5% in September on the back of the lower harvest in 2018, volatility in global financial markets and other factors.

• Food retail trade grew 1.9% in real terms in Q4 from 1.0% in the previous quarter. Overall, market growth in 2018 was 1.7% in real terms and 4.0% in nominal terms and the market value reached 15 trillion roubles.

• Real disposable income dynamics remained weak, declining by 1.1% year-on-year in Q4. For 2018 as a whole, real incomes fell by 0.3%.

• Consumers remain rational and sensitive to promo. The consumer confidence index remained negative, approaching -17% in Q4 after -14% in Q3 2018.

• The macro environment remains challenging, but food inflation started to pick up. It reached 5.5% year-on-year in January and 5.9% in February. We see this trend continuing in March, which is supportive for all retailers.
We are frequently asked questions by our investors about the changing competitive environment. Competition has increased over the past two years, not only from traditional retailers but also from the ready-food delivery segment. The largest traditional players continued to add selling space, but expansion plans for 2019 have moderated. At the same time, new formats have appeared, which indicates consumers are receptive to new CVPs. We also see new trends in the market while consumer behaviour is changing, as Igor has already mentioned and this puts pressure on retailers, which is especially pronounced in Moscow. All of this had impacted X5 and especially Pyaterochka. This was especially visible at the beginning of 2018, when our proximity format’s traffic in Moscow was negative. However, thanks to the initiatives of the current team at Pyaterochka, including projects aimed at updating CVP, assortment, cost optimisation and shrinkage reduction, we managed to achieve an improvement in like-for-like traffic in Moscow, which is positive year-to-date in Q1 2019. At the same time, traffic in Pyaterochka in the regions remained positive during the year and is positive now.

Before we move to the financial results, I would like to say a few words about ROIC as this question is frequently asked.

Moscow and St Petersburg continue to demonstrate the highest ROIC levels, outperforming our regional operations. You might remember that it involves negative trends in Moscow and St. Pete’s return on investment for almost a year in the second half of 2017 and first half of 2018. But now what we see in our post-investment analysis of the fourth quarter 2018, this trend has stabilised, which gives us optimism for 2019.

At the same time, ROIC and profitability trends in the regions are encouraging. While returns in the regions are lower than in Moscow and St Petersburg, the trend here is the opposite – the rate is growing and exceeding our hurdle rate, which is 19% IRR, implying increased quality of openings in the regions.

Moving on to X5’s financial performance during the quarter, revenue increased by 16.9% year-on-year to 423 billion roubles in Q4.

X5’s LFL sales and traffic growth accelerated to 3.7% and 2.2% year-on-year, respectively, compared with 0.5% and 0.9% in the third quarter of 2018. X5’s LFL basket growth in Q4 reached positive territory on the back of increasing food inflation.

Looking at margins in the fourth quarter, the gross profit margin increased by 30 basis points year-on-year to 24.1% of revenue in Q4 due to the stable share of and more balanced approach to promo and the positive year-on-year impact on the commercial margin from proportionally more sales coming from Perekrestok, which reached 16.0% of net retail sales in Q4. Successful measures to control shrinkage levels also had a positive year-on-year impact on gross profit margin.
The negative year-on-year effect from SG&A reached 91 basis points and was due to increased staff costs, lease expenses and utilities costs. These three cost items had roughly equal impact on our quarterly profitability. All the details of the factors affecting SG&A expenses are disclosed in today’s press release.

The adjusted EBITDA margin totalled 7.2% in the fourth quarter of 2018 and we fully met our internal targets for the year as expected and as communicated at our previous calls, so we were within our prognosis.

In the fourth quarter of 2018, we continued to accrue LTI expenses covering the old and new LTI programmes. The LTI expenses including social taxes accrued for the old programme totalled 386 million roubles and for the new programme – 184 million roubles.

D&A and impairment costs increased as a percentage of revenue by 28 basis points to 3.4%, versus 3.1% for the same period last year. This was due to continued growth in the share of assets with a shorter useful life in PP&E, driven by the growing share of leased space in X5’s total real estate portfolio.

In Q4, net finance costs were 36.0% higher year-on-year. The effect from the increased level of gross debt was partially offset by the decreased weighted average effective interest rate on X5’s total debt from 9.51% for 2017 to 8.39% for Q4 of 2018 as a result of declining interest rates in Russian capital markets and our actions taken to minimise interest expenses. In February 2019, X5 placed a 5 billion rouble bond with a coupon of 8.5% per annum.

The company’s net profit in the fourth quarter totalled 6.4 billion roubles, increasing by 2 basis points year-on-year to 1.5% of revenue.

Turning to our balance sheet, at the end of the year our net debt to EBITDA ratio decreased to 1.70x, the lowest level in the Company’s history. We consider this level of leverage to be comfortable and will seek to maintain a ratio of below 1.8x while paying dividends in line with our policy, going forward.

Turning to the cash flow, the change in working capital in the fourth quarter of 2018 was plus 21.2 billion roubles compared to 4.5 billion roubles in the fourth quarter of 2017. This was primarily due to a higher increase in accounts payable driven by business growth and higher food inflation in Q4, as well as improvements in accounts receivable collection.

Net cash used in investing activities, which generally consists of payments for property, plant and equipment, decreased to 23.8 billion roubles Q4 compared to 27.4 billion roubles for the fourth quarter last year, driven by lower investments in store openings.

Now a few words about capex.

X5’s total capital expenditure amounted to 27.5 billion roubles in Q4 2018, compared to 38.1 billion roubles in Q4 2017. Approximately 55% of the quarterly capex went to expansion of our
store base. The remaining capex includes refurbishments, logistics, IT and other investments. Total capex in 2018 decreased by 15.7% year-on-year reaching 83.2 billion roubles.

Finally, let me confirm our previously-announced plans to open around 2,000 gross stores across all formats in 2019, while maintaining our profitability and returns. Capex is planned at approximately the same level as in 2018.

We also remain committed to continue dividend payments in line with our dividend policy.

That concludes the discussion of our results, thank you for your attention.

Natalia Zagvozdina:

Thank you, Svetlana. Thank you, Igor. Operator, can we please start the Q&A session? Thank you.

Operator:

Thank you ladies and gentlemen. We will now begin the question and answer session. As a reminder, if you wish to ask a question you can press "star", "one" on your telephone and wait for your name to be announced. Please standby while we compile the Q&A queue; this will only take a few moments. If you wish to cancel your request, you can press the "hash" key. Once again, for questions, please press "star", "one."

Again, just a reminder for everyone, if you wish to ask a question you can press "star", "one" on your telephone and wait for your name to be announced.

We have your first question. It's coming from the line of Alexey Krivoshapko. You can go ahead, your line is now open.

Alexey Krivoshapko:

Igor, Svetlana, Natalia, Andrey, thank you for the call. I have 2 questions. There's one on 2019 capex, the RUB 90 bln figure, which you're referring to, does it include VAT? And second, does it include M&A?

Svetlana Demyashkevich:

Hello. As for capex, this RUB 90 bln is including M&A, as always. So, it's an approximate number. This year, capex was actually even slightly lower than our prognosis because some of the M&As were done at the end of 2017 and some of the M&As will be included in capex of 2019. So, there is also some timing difference. VAT is not included. We normally give net of VAT numbers to you.

Alexey Krivoshapko:

OK. Just clarifying. Thank you. And I guess, second question is maybe more serious. You indicated that you had very high losses in 2017 and basically Sergey has come with a strong plan to reduce them and it happened in 2018 already, from Q2. And that was basically one of the reasons why the gross margin has been going up. At the same time, basically we can see that it's
down Q4 versus Q3 by like 50 basis points. And I’m trying to understand a little bit what is behind it, because typically the seasonality for gross margin Q4 versus Q3 is neutral to positive. So, is it so that losses started to go up again? Or did you reduce prices? What happened actually?

Svetlana Demyashkevich:

Yes. Thank you for your question.

So, you’re right that Pyaterochka’s team is very effective starting the third quarter of 2018 with decreasing shrinkages, and we have a steady decrease in trends, which actually continued in the fourth quarter and is still continuing in the first quarter of 2019. If you look at the gross margin of the fourth quarter 2018 comparing with the fourth quarter of 2017, it’s higher, so 24.1 percent comparing to 23.8 percent in the fourth quarter of 2017.

At the same time, yes, you’re right that if we compare gross margin of fourth quarter with the third quarter, the main difference is due to commercial margin. And yes, during the fourth quarter, attracting traffic, which is usually the good thing to do during the high season and that would actually we do every year. We did invest in customer, mostly through regular pricing.

Alexey Krivoshapko:

Yes. And what was the impact of that price reduction? What did you get in return?

Svetlana Demyashkevich:

As you see, traffic is positive in the fourth quarter and again continuing in the first quarter of this year, even with somewhat increased prices, including the change in VAT, we still see a positive traffic even in Moscow and Pyaterochka, which was the primary area of attention for us starting from the beginning of last year.

Alexey Krivoshapko:

Do you think yourself it’s worth financially because, I guess, you see numbers better than we do in the real time because, there is certain trade-off between reducing prices and increasing profits? And I mean, it doesn't seem that we see it financial-wise right now at this point of time. How do you think about it because, there is certain kind of price level in stores, which would not make them economically profitable for new store openings? I mean, what's your line of thinking? What is the normal level of profit in store, or I don't know, operating profit margin, at which you would basically stop as otherwise it will be economically unprofitable to open stores given your current capex levels?

Svetlana Demyashkevich:

So, we’re actually happy with the results for the fourth quarter and overall for the year. If we’re talking about the gross margin performance and overall EBITDA margin performance, we are even slightly above our plans and including return on investments. So, what we see, again, as I commented when I was discussing the factors affecting the fourth quarter, so what we see is the
stabilised trend of returns on Pyaterochka stores in Moscow and increasing trend on returns in the regions. Overall, we think that the changes, which are made in Pyaterochka in the second half of the year regarding category management processes, assortment, pricing and promo are very positive. And we do continue to see these trends in the first quarter of this year, while all these projects are actually continuing. We have 3 major projects in Pyaterochka on assortment, pricing and promo, which are done by our internal team, including our big data team, where we analysed our loyalty card program data and based on that, make our decisions on the profit assortment in particular stores. So, I would say, we are becoming smarter, both in assortment, pricing and promo. And we already see it on our financial results. I think we will see further improvements during 2019.

Alexey Krivoshapko:
So, Svetlana, just a last question. So, is it fair to say that in Q1 you were not happy with Pyaterochka? Q2 was a bit better. So, let's say, second, third, fourth quarter is the kind of level of financial performance of Pyaterochka, which you are happy with and the one which is sustainable. Is it fair to say so?

Svetlana Demyashkevich:
Yes. I think, yes, first half of the year was challenging with the first quarter probably demonstrating the most negative trends and the second half being much more positive. And yes, we see positive developments in the first quarter this year.

Natalia Zagvozdina:
Alexey, we hope you do not mind if you'll let other participants ask their questions...

Alexei Krivoshapko:
...That's all I had.

Operator:
Thank you. We have another question. It's coming from the line of Nikolay Kovalev. Please go ahead, your line is now open.

Nikolay Kovalev:
Yes, hello, thanks for presentation. I have 2 questions. My first question is on the capex. For the guidance of flat RUB 90 bln, can you give us estimates? How much will be allocated for IT initiatives, e-commerce and establishing your omnichannel platform?

Svetlana Demyashkevich:
So overall, around 50-55 percent will be allocated to store openings and refurbishments, around 10 percent logistics, another 10 percent on maintenance and around 25 percent, over 30 percent to IT developments, big data developments and other projects, including innovations.
Nikolay Kovalev:
OK. And, also, I would like to clarify on your LTI booking. Can you share with us your estimate because you have 2 programs going on? How much LTI you're supposed to book in the next couple of years? And what metrics do you imply in your calculation?

Svetlana Demyashkevich:
So, now we still have some part remaining from previous LTI for 2019. The amount is around RUB 0.5 bln. And we also started in 2018 to accrue new LTI program, which started from 1st January 2018. Overall amount, which is now accrued for this new LTI program, is around RUB 2.9 bln over the four years from 2019 to 2022. So, for years 2019 and 2020, overall amounts are around RUB 1 bln per year and further in 2021 and 2022 RUB 0.7 bln and RUB 0.2 bln respectively. And the second question was on the targets included in LTI program, right?

Nikolay Kovalev:
No. I mean, like as a sub-question, it was when you are talking about RUB 1 bln, what kind of triggers you implied in this calculation?

Svetlana Demyashkevich:
So, 2 main targets for this new LTI program are leadership in revenue among Russian food retailers and second target is leadership in EBITDA multiple, among Russian publicly-traded food retailers. So, we do think that the probability of us achieving first target is quite high, that's why we started to accrue this part of LTI program. The probability of us reaching second target on EBITDA is less visible at the moment, but we still have time. So, we didn't accrue it for 2018 and we'll see how it will develop in 2019 and 2020.

Nikolay Kovalev:
OK. It's very clear. Thank you very much.

Svetlana Demyashkevich:
Thank you.

Operator:
And again, everyone, if you wish to ask a question, you can press "star", "one" on your telephone and wait for your name to be announced.

We have another question. It's coming from the line of Maxim Nekrasov. You can go ahead, your line is now open.

Maxim Nekrasov:
Yes, good afternoon. I have a quick question on your finance costs. So, the question is, why your finance costs increased by over 20 percent in the fourth quarter compared to the third quarter,
considering that the leverage has actually gone down and the total debt in absolute terms also went down?

Svetlana Demyashkevich:

So, overall, our debt level increased if we compare beginning of the year and end of the year. At the same time, also within the quarter, there are some fluctuations of debt and it really decreased by the end of the year somewhat. And our expectations of capex, including expectations from M&A were higher than the actual capex in 2018.

Overall, we do see several major items impacting performance of our net profits, while the biggest actually being amortisation, depreciation which increased significantly due to quite sizable capex of last 3 years. And now it'll come down to the amortisation, depreciation line.

In addition to that, there were some smaller changes, including FX, including deferred tax from dividends, some penalties, but all these factors are impacting overall net profit number much less than the difference in depreciation. In addition to that, I think what is important is that we still announced a quite sizable dividend, having increased the total amount compared to 2017, both in ruble terms, in dollar terms and in terms of our pay-out ratio to net profit.

Maxim Nekrasov

OK. Thank you. And final question. What effective interest rate would you expect in 2019 for the full year?

Svetlana Demyashkevich:

So, the last bonds were issued at the rate of 8%. So I would say that's our market level at the moment. We do not expect big movements, both negative and positive during the year. So probably the overall rate will stay in that range. Natalia, do you have something to add?

Natalia Zagvozdina:

Yes. We, last year, compared ourselves with the key policy (really and) how it performed and I think, the good benchmark to keep in mind is that we place the bond with a spread of about 70 basis points. So, if the key rate will be changing, we hope to stay within this spread.

Maxim Nekrasov:

OK. Thank you.

Svetlana Demyashkevich:

Thank you.

Operator:

We have no further questions coming from the phone lines. Please continue.
Natalia Zagvozdina:
Ladies and gentlemen, we would like to thank you for your interest and your questions. We would like to remind you that we will host a separate call on March 25 dedicated to the adoption of IFRS 16 accounting standard. Speak with you then and have a nice day. Thank you. Goodbye.

Svetlana Demyashkevich:
Thank you. Bye.

Igor Shekhterman:
Thank you.

Operator:
Ladies and gentlemen, that does conclude our conference call for today. Thank you for participating. You may all disconnect.