

Second Quarter 2014

Earnings Conference Call

July 23, 2014

Company Participants

Mr. Juan Gallardo, Chairman & CEO

Mr. Carlos Orozco, CFO

Ms. Diana Gonzalez, Investor Relations

Analyst and Investor Participants

Karla Miranda - GBM

Armando Perez – Credit Suisse

Fernando Ferreira - Bank of America Merrill Lynch

Pedro Leduc – JP Morgan

Operator: Good morning and welcome to Cultiba's Second Quarter 2014 Earnings conference call. Today's call is being recorded. At this time, I would like to turn the conference over to Ms. Diana Gonzalez, Investor Relations. Please go ahead.

Diana Gonzalez: Thank you and good morning everyone. Cultiba's second quarter 2014 financial results were released today. A copy of the earnings release can be found on the Company's website at www.cultiba.mx.

As a matter of formality, I need to remind participants that remarks made by management during the course of this call may contain forward-looking statements about the Company's results and plans. Such statements are subject to risks and uncertainties that could cause the actual results and implementation of the Company's plans to vary materially. The words believe, expect, plan, intend, estimate or anticipate, or similar expressions, as well as future or conditional verbs such as should, would and could identify forward-looking statements. In addition, any projections as to the Company's future performance represent management's

Fiscal 2Q14

estimates as of today, July 23, 2014. You should not place undue reliance on these forward-looking statements and we expressly do not undertake any duty to update forward-looking statements, whether as a result of new information, future events or otherwise.

Presenting on the call today will be Cultiba's Chairman and CEO, Mr. Juan Gallardo; and Cultiba's Chief Financial Officer, Carlos Orozco. Mr. Gallardo will begin with some opening remarks, after which Carlos will present a discussion of the Company's second quarter and first half financial results. Finally, Mr. Gallardo will discuss the Company's outlook before opening the call for questions.

Now, it is my pleasure to turn the call over to Mr. Gallardo.

Juan Gallardo: Thank you, Diana. Good morning and thank you all for joining us for our second quarter earnings call. 2014 has been a particularly challenging year for the beverage industry. As you all know, our industry faced a series of headwinds during the first six months of 2014: first, the implementation of the excise tax on sugary beverages in January; second, unusually rainy weather throughout the period, particularly in central Mexico; and third, a slower than expected recovery in the Mexican economy.

More specifically for the second quarter, the quarter got off to a very good start in April, including the Easter holidays; however the May and June time period experienced the worst rainfall in 10 years, and on the macro front, the economy continued to be sluggish.

So, how have we responded to this challenging year? Against a difficult backdrop, we have continued to execute on our original strategy. This has not been an easy task but has allowed us to remain focused on our growth and profitability goals despite the aforementioned hurdles. Since GEPP, our beverage group was created, we have invested more than \$400 million in modernizing our manufacturing and distribution infrastructure so that our processes improve, efficiency, and our products maintain their consumer appeal.

By the end of 2013, when we heard about the implementation of the excise tax on sugared beverage, and given the slow economic recovery, we took strong and decisive measures as mentioned in our first quarter call to prepare for what clearly was going to be a more significantly challenging environment. Some of these measures were both difficult and painful, like the 20% reduction in corporate overhead to streamline administrative processes. Additionally, we are in the process of launching a state-of-the-art shared services office in

Guadalajara in order to centralize overhead requirements, further optimize our back office capabilities, and accelerate our speed of response to the market. This installation should be fully operational by next February.

These transformational initiatives have and will continue to contribute to margin expansion, allowing us to offset some of the effects of weaker volumes and higher marketing efforts required to maintain our competitiveness in the marketplace. We expect this margin expansion to continue step-by-step in upcoming months, allowing us to strive towards our profitability goals.

To bring a little extra color to these comments, I would like to mention one of the very important initiatives that now has been completed. We have over 18,000 unionized employees within GEPP. Over the last few months and through a very, very complex and balanced, I would say, negotiation, we were able to make 80 union contracts uniform. As you can imagine, over the last roughly 80 years, each one of these contracts has reflected local agreements, there were different types of holidays, different treatment for medical situations, et cetera, et cetera, and we had literally a complete mosaic of conditions that made getting all these contracts to be uniform a particular challenge. We were able to complete most of those – there are still two or three remaining, but the kind of effort that meant and obviously the recognition and remuneration to be able to uniform the contracts throughout the Company is now done. This was a major, major step in the last few months.

Additional other measures, such as our price packaging architecture, were designed to maintain our competitiveness in a more challenging environment, balancing customer affordability with Company profitability. We also deployed channel-focused strategies designed to increase our presence in both the traditional and modern trade. Our portfolio was also redesigned to support top-line performance by focusing as we have done on strong brands with national relevance, and we continue consolidating our offerings to bring about profitable volume growth. The most recent example is the introduction of Barrilitos in central Mexico into the markets where Jarritos brands are not present under our distribution. This introduction has been very well received by the market.

Our focused strategy continues bringing favorable results in the beverages division. In response to our price packaging strategy, we saw favorable growth rates in smaller presentations which continue to contribute to profitable top line growth while protecting volumes. Soft drinks and bottled water volume increased 1.1% year-over-year, a significant improvement from the 4.2% year-over-year decrease experienced in the first quarter and evidence that our strategies to

Fiscal 2Q14

navigate the changes brought about by the excise tax and a slower consumer environment are gaining traction.

By contrast, the adverse weather in May and June, particularly in the western and central regions of Mexico, hurt our jug water business by hampering the deliveries in our direct-to-home distribution network as many roads were literally impassable. As a result, water sales and jug water sales were down 3.4% in the quarter.

The good performance in soft drinks was offset by the weaker performance in jug water, and we reported a total volume down 1.2% over the same period of the prior year. Nonetheless, given the challenging environment, we are pleased with this performance.

Our efforts on the efficiency front are also showing the desired results. In the second quarter, the consolidated Adjusted EBITDA margin of 10.5% was essentially flat with the same period of the prior year. Our margin improvement reflects our success in extracting the remaining previously identified synergies from our business combination, totalling approximately Ps 900 million, and we continue to identify additional efficiencies. We have continued to put in place efficiencies that will become more evident in EBITDA margin recovery as volume growth recovers in the second half of this year and forward. All in all, a massive sustained string of efforts and initiatives diligently executed by a great team.

I will now turn the call over to Carlos to take you through our financial results, and will return then and discuss our plans and outlook. Thank you.

Carlos Orozco: Thank you, Mr. Gallardo. Good morning and thank you all for joining us. The quarter began on solid footing, benefiting from Holy Week and improved weather, making April one of the strongest months of the year so far. Weather, however, turned sour in May and June as we experienced the worst rainfall in 10 years, particularly in the western and central regions of the country, with Mexico City included. Our total beverage volume in the second quarter of 2014 was 443 million unit cases, 1.2% below the same period in the prior year primarily focused on weaker jug water sales.

The average revenue per 8-ounce case, excluding the excise tax, was Ps 19.6 in the second quarter of 2014, up 1.8% from Ps 19.3 in the same period last year. Our beverage prices have fully reflected the new excise tax on impacted categories since the beginning of the year, as well as inflation in non-affected categories. We expect further price increases throughout the year to recover inflation, along with industry trends.

Fiscal 2Q14

Going through our P&L, total net sales in the second quarter of 2014 were Ps 10.5 billion, 14% higher than the comparable period of 2013. Excluding the revenue generated from the excise tax, total revenue was Ps 9.5 billion, a 3.7% increase when compared to the same period in 2013, reflecting a slight volume recovery and higher revenue in both the beverage and sugared divisions.

Moving on to costs and expenses, excluding the impact of the excise tax, consolidated cost of goods sold was 6.5% above the same period in the prior year, primarily reflecting higher sales volume in our sugar division for this quarter. As a result, our gross margin in the quarter decreased to 40.2% from 41.8% in the same period of last year.

Our total SG&A expense was Ps 3.7 billion in the second quarter of 2014, up from Ps 3.4 billion in the same period of 2013. SG&A as a percent of revenue increased 80 basis points to 38.3% in the quarter primarily due to higher marketing expenditures to maintain volume recovery in addition to non-recurring expenses up Ps 130 million related to through transformational programs that are being implemented, as Mr. Gallardo mentioned, in the beverages division to achieve cost efficiencies and personal adjustments.

Operating income in the quarter was Ps 184 million compared to Ps 300 million in the same period of the prior year; however, adjusted for one-time expenses, operating income was in fact Ps 315 million, which is a moderate improvement when compared to operating income of last year.

Our consolidated EBITDA was Ps 868 million compared to Ps 978 million in the same period of 2013. The decrease primarily reflects lower volume as well as extraordinary expenses in the beverage division, as previously described. As a result, our consolidated EBITDA margin this quarter was 9.1%, down from 10.6% in the same period last year. On an adjusted basis, EBITDA was up 2% and the margin was basically flat at 10.5%.

We will continue to look for and make additional operational improvements along the way that will improve our cost structure. With the right cost structure in place, our operations and EBITDA margins now have greater upside leverage as costs in the beverage division continue to grow.

Moving down the P&L, as we continue to pay down debt, our financing cost is decreasing when compared to the prior year. For the second quarter of 2014, our interest cash expense was 16% below the same period in 2013. As anticipated, we have completed amortizing the loan the beverages division incurred in December 2013 to make advance payments for raw materials, thus contributing cost efficiency. Both of our business had moderately leveraged up

Fiscal 2Q14

during the quarter for working capital purposes in response to their operational seasonality. We expect deleverage of working capital financing throughout the second half of the year.

Finally, net income in the quarter was Ps 159 million compared to Ps 395 million in the comparable period last year. The decrease is basically due to extraordinary expenses in the beverage division and higher comparable tax provisions.

Let me now briefly focus the discussion on the beverage business results during this quarter.

Net of excise tax, revenue in the quarter was Ps 8.6 million, basically flat with the same period of the prior year, reflecting gradual volume recovery especially in the bottled beverages segment, as well as improved volume mix and better pricing.

On the cost side, our unit costs per case were 1.5% lower than the second quarter of 2013, and we also reported a 6.4% year-over-year increase in gross profit per case. This good performance reflects continued procurement improvement, strong relationships with key suppliers, and favorable raw materials prices partly as a result of the advanced payment we did by the end of 2013.

We continue to make the necessary investments in marketing on our distribution network to increase brand awareness and points of distribution; however, due to lower volume during the quarter, we were not able to further dilute these costs in the quarter. On the positive side, we have achieved many cost efficiencies, including optimized processes and a more streamlined operating structure. As a result, operating income in the beverages division reached Ps 379 million, which is 24% higher than the Ps 306 million of the second quarter from the prior year, after adjusting for the previously mentioned extraordinary expense.

Adjusted EBITDA for the beverages division was Ps 910 million for the second quarter of 2014, 10% above EBITDA in the second quarter of 2013. The Adjusted EBITDA margin was 10.5%, 90 basis points higher than the comparable period in 2013. We expect further improvement as the year progresses as well as additional extraordinary charges strictly associated to further cost and expense optimization initiatives. Results and margins obtained in April, when volume growth was high, have given us confidence that we can deliver improved profitability going forward.

Now, let me discuss accumulated results for the first half of 2014. The first half of this year was characterized by mixed results in the beverages group and a lag in sugar volume when

compared to last year's comparable period as a deliberate strategy to manage sugar inventories and improve yearly average pricing in our sugar division. Soft drinks and bottled water sales were more heavily impacted by the implementation of the excise tax and slower economy in the first quarter, and volume was down while jug water sales were up. By the second quarter, consumers had responded favorably to the changes we made in product packaging and pricing of soft drinks and bottled water and sales increased, while jug water sales were hampered by unfavorable weather, as already discussed. As a result of these effects, our total volume in the first half of 2014 was down a mere 0.8%, reflecting a 1.3% decline in soft drinks and bottled water and a 0.2% decline in jug water sales.

Our sugar business completed the 2013-2014 harvest season with total production of 341,000 tons of sugar. Efficiency indicators were improved and translated into lower transformation costs, and electricity generation was 40% higher than in the previous season. Our domestic sales volume was 21.7% lower in the first semester of the year when compared to 2013; however, we expect second semester sales volume in the domestic market to compensate for this lag and expect higher domestic prices in the second half of the year. Prices in the domestic market were 17.3% below domestic market prices in 2013, and export prices were 11.7% below the same period of 2013.

As previously communicated, our sugar division has been named as a mandatory respondent in an anti-dumping investigation currently in place by the US Department of Commerce. We expect all governments to reach an agreement in the coming months, to guarantee continuity in future relationships between the two countries.

Excluding the beverage excise tax, total Company revenue in the first six months of 2014 increased 0.8% over the same period in the prior year, reflecting lower beverage volumes during the first quarter and a slight recovery in the second quarter. Average revenue per case also improved throughout the period.

We continue to deliver improvements on the beverage cost front. As a result of portfolio mix enhancements and ongoing cost efficiencies, as already discussed, gross profit per case in the first six months of the year was 5.6%, better than the same period of the prior year. We are also making improvements on the SG&A front; however, it is not yet apparent as the expenses we have deployed in both traditional and modern trade channels is not yet diluted by sales growth.

Adjusted for one-time expenses, the beverages division EBITDA increased 3% in the first half of 2014 while the margin expanded by 30 basis points, reaching 8.4% in the period. During the

Fiscal 2Q14

first half of the year, extraordinary expenses associated with personnel reductions and optimization initiatives to further reduce cost and expenses in the beverage division were Ps 177 million. We expect to continue incurring extraordinary expenses during the rest of this year and part of 2015, which we will be describing as incurred.

Slightly lower beverage volume and revenue, coupled with lower compares on domestic market sales in our sugar division, was primarily responsible for holding back consolidated EBITDA margin expansion in the first half of 2014; but nonetheless, we are showing signs of the slight recovery back to 2013 levels, which we expect to continue.

Moving on to the balance sheet and cash flow, a strong balance sheet in both of our divisions continues to be a top priority. Net debt at the end of the period was Ps 4.3 billion compared to Ps 6.3 billion at year-end 2013, primarily reflecting the beverage division's full repayment of short-term debt incurred in December 2013 to finance advance payments for raw materials. Our net debt to EBITDA ratio was 1.7 times on June 30, 2014 compared to 2.2 times on December 31, 2013. Working capital, which by this time of the year not only reflects the deficit due to seasonality both in the beverages and sugar divisions, has improved as a result of collecting IEPS and paying it by the end of the period. This deferred cash flow expense will be offset in comparable terms by next year.

Capital expenditures in the first six months of 2014 totaled Ps 765 million. Funds were utilized for infrastructure and technology modernization programs, as well as supporting additional initiatives to drive top line growth and cost efficiencies. There has been no cap ex at the sugar division during the first half of 2014.

In sum, our financial position remains strong as we are generating strong cash flow at similar levels to 2013 and we are repaying debt. Subject to the general shareholders meeting that will take place early August and respecting our healthy financial position, we also plan to pay a dividend of \$0.24 per share in mid-August and mid-October.

I will now turn the call back to Mr. Gallardo for some further comments before we open the lines for questions.

Fiscal 2Q14

Juan Gallardo: Thank you, Carlos. You have heard both Carlos and me discuss the many actions we have taken to ensure that we are consistently on track to steadily deliver the goals that we outlined and shared with you in our equity offering. Clearly, we all recognize that it has turned out to be a tougher and more complex assignment, but we will continue to deliver our plan and we are literally improving daily all our capabilities and further strengthening the Company.

Lower volumes this year have sidetracked margin expansion, particularly during the first quarter as you have seen; however, excluding one-time items, we did see the expansion in the second quarter. We expect this trend to continue for the remainder of the year and are anticipating full-year adjusted for one-timers 2014 EBITDA to be slightly above the 2013 level.

As Carlos mentioned, we are a financially strong company with an improving balance sheet. We have modernized plant equipment while streamlining processes and optimizing routes. We made investments in IT which in turn has helped us standardize administrative processes, and we have also invested in our go-to-market strategy to drive top line growth. The current year is expected to remain challenging, and we will continue to find additional operating efficiencies to drive this margin expansion. We will also continue to be innovative with product and packaging.

In conclusion, I would like to reiterate that our original strategy continues to be unchanged and executable. We continue investing in our previously discussed engines for growth. At the midpoint of the year, Cultiba emerges as a stronger company, fully integrated, streamlined, and well positioned to succeed under the new industry reality.

This ends our prepared remarks, and we'd be happy to take your questions now.

Operator: Thank you. If you do have a question today, please press star, one on your touchtone telephone. If you are using a speakerphone, please make sure your mute function is turned off to allow your signal to reach our equipment. Once again, press star, one to ask a question, and we'll pause for just a moment.

Our first question is from Karla Miranda from GBM.

Fiscal 2Q14

Karla Miranda: Hi, good morning everyone. Thank you for taking my questions. Juan, Carlos, I've got a couple of questions. First of all, I was wondering if you can give us some color of the jug water performance during July. Have you seen some recovery in the volume trends now that the Easter season has passed and it seems that the rainy season is kind of fading away? In addition, I was wondering if you can give us some color regarding pricing activities in the rest of the portfolio, in the portfolio that was impacted by the excise tax. Thank you very much.

Juan Gallardo: Thank you, Karla. Answering your first question, yes, we've seen a recovery in water jug volumes in July. As you've seen, the weather has changed a bit, in particular in Mexico City. We now see that we are receiving rains at night, so that definitely has helped our routes and volume is recovering to the growth levels we've seen at the beginning of the second quarter.

Now, with respect to pricing activity, we're being as diligent as possible to grab any opportunity there is to pass along inflation, which we have not been able to pass along yet; but obviously as you know, that will be a result of the competitive environment that we see in the second half of the year.

Operator: Moving on, we have a question from Armando Perez from Credit Suisse.

Armando Perez: Good morning everyone. Thanks for the call. I have two questions. The first one will be with the 20% decline in EBITDA you have had in the first half of the year, do you still expect a flat EBITDA by year-end and do you expect to increase prices to do so, and is this including the extraordinary expenses you have mentioned in the past? The other question is regarding the cash flow statement. I see a decline in other receivables and short-term assets and an increase in other liabilities, which have impacted cash flows. What exactly are these accounts? Also, I see that the investment in PP&E is roughly half of what has been—or what was seen last year, and is this a seasonal effect or you have a new cap ex plan for the year? Thanks.

Carlos Orozco: Good morning, Armando. Well first of all, the EBITDA that we mentioned, that obviously is adjusted for these one-time expenses that we have been incurring, it's not fully dependent on price increases. Again, we are not able to pass along those price increases to recover part of the inflation. We expect to be flat with last year's EBITDA.

Now, with respect to cash flow, as I mentioned, you see that our short-term liabilities are going up, and that's helping our working capital; and as I mentioned, it's basically the effect of having been collecting IEPS and paying it the month right after, so that has been helping us on the working capital in this season, which as you can see has been increasing inventories and accounts receivable.

Finally, your observation with respect to PP&E, we have been doing some cap ex, as mentioned – the beverage division has incurred close to Ps 800 million in the first six months of the year, so that's basically what you should be seeing in the financial statements.

Operator: Our next question today is from Fernando Ferreira from Bank of America Merrill Lynch.

Fernando Ferreira: Good morning everyone. Good morning Juan and Carlos. I had a couple of questions. The first one – I just wanted to understand better this accounting change that apparently you guys are now assuming the excise tax as part of the COGS instead of deduction of revenue, so just wanted to confirm that and why did you make this change.

Carlos Orozco: Yes, Fernando. Well basically, that's—we consulted with our auditors both at the beverage division and at the holding company level, and the advice was to register the IEPS as a cost, not as value-added tax. So, that's why you see our revenues and our cost of goods sold being higher – it's basically the effect of reflecting the excise tax in the income statement. You know—as you know, when we invoice soft drinks, we need to include the tax, so that's basically what makes it mandatory to be including this in your income statement.

Fiscal 2Q14

Fernando Ferreira: Sure, but when you're calculating your margins, you're considering revenues net of those taxes, right? Otherwise, your margins would look lower, correct?

Carlos Orozco: Exactly, exactly. That's correct.

Fernando Ferreira: Okay. Then second question – how much have you increased prices to consumers, average price to consumer on the sugar beverage portfolio so far year-to-date? Then the follow-up question to that is why do you think volumes haven't contracted more than what we've seen so far?

Carlos Orozco: Well, answering the first part of your question, since the beginning of the year, as we've mentioned before, we've basically adjusted all the portfolio to reflect the excise tax, which in our case was basically around 16%, so that's the size of the price increase we've taken now. As you know, that's a higher price increase than the rest of the public industry, so that's basically the figure that you can see when you do an analysis of our pricing. Again, we have not yet been able to capture the inflation, and we will try to do that during the second part of the year.

The second part of your question, you got a little bit cut off. Could you repeat that, please?

Fernando Ferreira: Sure. Volumes haven't contracted, right, as much as we would have thought with a 16% price increase, so do you feel good about your volume performance so far, and how do you think about the second half in terms of volumes?

Carlos Orozco: Well, we're obviously satisfied. You've seen results all around and this is what we were expecting, and as you've seen in the past, when we see the economy recovering, we see those growth rates go up again. So yes, we feel comfortable with those not yet growth rates, but we expect them to be growth rates in the second half of the year.

Fiscal 2Q14

Operator: Just a reminder, it is star, one if you have a question today. We'll go next to Pedro Leduc from JP Morgan.

Pedro Leduc: Hi, good morning. Thank you for taking the question. Just a quick one regarding what you call one-off restructuring expenses. How much can we expect by the end of the year? We already mentioned that the slight EBITDA expansion is excluding these, and we've seen some in the first, now in the second quarter. You call them one-off, but how much can we expect to see this further in the second half, and how much do you feel like you're done with your efficiency plans? Thank you.

Carlos Orozco: Thank you, Pedro. Well basically, it's an ongoing effort and as I mentioned, it will be reflected both in 2014 and also part in 2015. For the rest of the year, that figure should be between 100 and Ps 120 million, and that obviously will be explained in the following calls as we incur them.

Operator: It appears there are no further questions today. Mr. Gallardo, I'll turn the conference back to you for additional or closing remarks.

Juan Gallardo: Well, as you can see, as we mentioned, the volume numbers, the cost structure, the marketing efforts, the overall sustained strategy all have been part and parcel of a well-established and committed road map ahead, which we will continue to follow. I would just like to thank you all for your trust and support and look forward to our next conference call. Thank you very much.

Operator: Once again, that does conclude today's conference. We appreciate your participation.

ABOUT CULTIBA

Organización Cultiba, S.A.B. de C.V. is a holding company with a majority interest in one of Mexico's largest bottlers of soft drinks and jug water, and the exclusive bottler of PepsiCo beverage products in Mexico. Carbonated, non-carbonated soft drinks and jug water are marketed under its own brands as well as third party brands. Its beverages division has 44 bottling facilities in Mexico and is the only bottler with nationwide distribution. As a holding company, Cultiba also owns and operates 3 sugar mills and has a 49% interest in a fourth one in the western region of Mexico. The Company is listed on the Bolsa Mexicana de Valores, where it trades under the symbol CULTIBAB. For more information, please visit www.cultiba.mx.

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