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PRESENTATION

Operator

Good evening, ladies and gentlemen. I am Palak, the moderator for this call. Welcome to the Hindustan Unilever Limited September Quarter Earnings Call. For the duration of the presentation, all participant lines will be in the listen-only mode. After the presentation, the question-and-answer session will be conducted for all the participants on this call.

I now hand over the call to Mr. Dinesh Thapar. Thank you and over to you, Mr. Thapar.

Dinesh Thapar - *Hindustan Unilever Limited - General Manager/Head of Treasury, IR & M&A*

Thank you. Good evening and welcome to the conference call of Hindustan Unilever Limited. We will bring this evening results for the quarter and half yearly ending September 30, 2015. On the call from the HUL end as always is Sanjiv Mehta, CEO and Managing Director; and P. B. Balaji, CFO.

As is customary, we will start with the presentation with Balaji sharing aspects of our performance for the quarter and then hand over to Sanjiv for him to share his perspectives on the business performance. We then get into Q&A.

Before we get started with the presentation, I'd like to draw your attention to the Safe Harbor statement included upfront in the presentation for good order's sake. And with that, over to you, Balaji.



P. B. Balaji - *Hindustan Unilever Limited - CFO*

Thanks, Dinesh. Thanks all of you for joining the call. Let me quickly run you through the performance of this quarter and I'm sure there is a lot of questions that you'd be keen to ask, and let me quickly cut to the chase.

As far as the strategy is concerned, good news, no change in strategy at all. So I won't spend too much time on this. You know it much better on this, we've been at it for a while now. Coming to the context, the business environment is challenging. Market growth have led by volumes in a deflationary context as we have signaled earlier as well. And disbursed commodity cost scenario which we saw in June quarter continued into September quarter as well and competitive activity remains high.

Just to give you a flavor of commodity cost, PFAD, the oil that goes into making soaps, you've seen the substantial decrease in cost if you saw that. Exchange rate, marginal depreciation. In fact, compared to what we have seen in other emerging markets rupee has done and been pretty stable and there is a marginal depreciation that we see. But even then on rupee terms, be it crude or in PFAD, both of them actually coming down and something for us, which we have factored in our plan.

In this context, we have sustained another quarter of profitable volume less growth. Domestic consumer business grew by 5% and after adjusting for excise duty benefits on the top line that went away, the underlying numbers are at 6%. Volume growth was 7%, but this does include a stock-up because of the anticipated transport strike which kicked in from October 1 as we had anticipated and therefore towards the last two days, we had to push in a bit of stock to ensure that we don't lose consumer franchise, should the transport strike were to continue for a long time and that's an impact of almost about 50 bps. The negative price growth in the quarter continued and this is fundamentally due to the lower commodity costs, as well as the phase-out of excise duty benefits, very similar to the story as last quarter.

Operating profit at INR1,250 crores, was up 7% and PBIT margins expanded by 40 bps. The impact of phase-out of excise duty benefits on this PBIT line is almost 45 bps, which makes the underlying increase almost 85 bps and in this if you peel the onion further, cost of goods sold on the back of lower input cost and higher savings program was lower by 320 bps. And we had re-deployed these savings that we had received, as I had always been alluding to. And this time we have invested substantially in A&P, almost up by 24%, INR220 crores up, which is almost 230 bps increase in A&P. And if 14.6% of sales is one of the highest A&P quarters in the recent past and this is something I'm sure you would want to cover in our Q&A, we'll cover -- we'll pick it up then.

PAT (bei) at INR970 crores, was up 1% and that's fundamentally because of the impact of additional taxes and lower financial income to a marginal extend and the net profit of INR962 crores was actually down 3% and the growth rate was impacted by the sale of surplus properties of almost INR49 crores in this quarter. And corporate tax rate as we had guided earlier as well at 31.6% in line with our guidance, but of course higher by about 190 bps compared to previous year, same quarter.

So if I then move to the segmental performance, the good news is that, we are seeing healthy volumes across segments and soaps and detergents, the reported sales growth is 2%, but if I adjust for the underlying impact of excise duty, is at 3%. Personal products at 11%, beverages and packaged foods at 13%. Soaps and detergents, there is a robust underlying volume growth, largely offset by price growth and personal products saw a healthy broad-based performance across all the sub-segments there. And packaged foods, as you'll be pleased note, is now the eight successive quarter of double-digit growth.

Moving to the individual category highlights, a strong quarter for innovation where some of the biggest brands that are out there were re-launched and if you see -- and that's one of the reasons you'll see in the A&P lines, for soaps and detergents, you will see that actually coming through. So these are some very big activities be it on Dove soap, be it on Surf Excel Matic, be it on Rin and as well a host of other brands also going through continuous innovations and pretty significant innovations there. And these have also been amplified extensively with a bit on ground activation, and I'm sure a lot of you have seen the kind of work that's happened on Lakme Fashion Week or the Rin Career Academy for instance, which has been a very, very big success so far.

So in this context, over the individual -- given this innovation pipeline the kind of activations, Skin Cleansing saw a robust volume growth come through. Particularly happy to see Dove, Pears, Lifebuoy, Hamam delivering double-digit volume growth, and liquids clocked another quarter of



double-digit growth. For the price deflation in the quarter due to benign commodity cost as I alluded to in the PFAD line, and those are the savings that have been redeployed actually to kick start and turbocharge this volume growth back into this business.

And moving on to home care, the volume growth further accelerated this quarter on the back of the premium segment. Surf, our largest brand, had one of its strongest growth momentum this quarter and Surf and Rin both registered double-digit volume growth. And with the Rin re-launch happening, it started accelerating even further. You'll be happy to note that, the Wheel performance is starting to improve and the Comfort of course continues its strong growth led by market development. Household care led by Vim was driven fundamentally by the tubs and liquids formats and here again we saw further price deflation in the quarter. And given the innovations that we had, it's another area where A&P had been deployed for this particular quarter.

Skin care, happy to see double-digit underlying growth in this business. FAL continues to do well, very good response to the new BB Cream that has launched, and Pond's, Lakme and Vaseline delivered double-digit growth. Pond's is led by premium skin lightening and facial cleansing, while Lakme had the whole CC Cream and Perfect Radiance continuing to do well, and Vaseline particularly happy to see the Healthy White variants actually now coming back into the growth agenda. The facial cleansing portfolio again was a strong performance this quarter with the strong double-digit growth there. And here again, the phase-out of excise duty benefits had impacted the growth and which is why we see strong performance or otherwise.

Hair care, a category that all of you were very keen to understand on the back of some of the competitive challenges that were there. Very, very happy to see sustained growth momentum building further in this business. It was volume led double-digit growth across formats. Dove further accelerated, TRESemme continues to being grown and the pricing on the bottle this quarter was reduced to further drive competitiveness and very strong performance here, despite the phase-out of excise duty benefits and despite the pricing action on bottles.

Oral care, the recovery is underway. Close Up delivered double-digit growth. The very strong activation platform on the First Move Party, it is a very big success. But unfortunately, the Pepsodent performance continues to be subdued, but we are very keenly working on it to ensure that the actions are progressed to strengthen competitiveness here and that's something that we will be seeing in the coming quarters.

Color cosmetics, very consistent innovation led growth across quarters and this double-digit growth momentum of Lakme continued and a whole range of innovations coming through, which I'm sure you have seen in the malls and at the conference.

Beverages had a steady performance this quarter. Tea was -- Red Label continues to lead category performance, with Taaza picking up and in case of Taj Mahal, we had some excellent brand activations done around the Independence Day event. And our star performers be the natural care portfolio as well as the green tea continued to build on their momentum, and coffee growth was lead by Bru Gold.

In packaged foods, this is now the eight successive quarter of double-digit growth. The focus on market development continues to play here. Double-digit growth in Kissan, Knorr and Kwality Walls. While Kissan sustained its activation-led growth momentum, Knorr grew well led by instant soups and of course ice creams had a very good quarter as well.

On Pureit, the leadership was sustained in a pretty challenging market context. The overall performance was subdued in a soft market. While the Modern Trade and Pureit Stores grew well, the rest of the traditional channels did have challenges this quarter, and e-commerce's contribution in this category is starting to become significant. And in this context, we continue to focus on market development and in-store execution and we really are focused on the consumer as the market challenges continue to play out this quarter as well.

So just to summarize the results, net sales up 5%, PBIT up 7%, PBIT margins up 40 bps and PAT (bei) up 1%, net profit down 3% and this factors in, there is an impact of excise duty benefits on this top line of about 100 bps and PBIT of about 45 bps. That's the snapshot of the summary.

Just going from PBIT to net profit, the key ones which I would love to call out is the other income line, where the interest income and dividend income and net gain on sale of non-trade investments -- current investments was shaded lower this quarter compared to what it was previous quarter and same as the dividend income from non-current investments. And in this case, the exceptional items, there is a sale, the base year had a property disposal of about INR49 crores, which is significant compared to what we had this quarter. Therefore to put all the stuff together, we

then realized that the PBIT numbers, by the time it drops into net profit it's actually down 3%. And the effective tax rate for the quarter is in line with what we've guided at 31.6%.

So to summarize, a profitable volume-led growth sustained and the reported domestic consumer growth of 5% underlying at 6%, 7% underlying volume growth with about a 50 bps impact of transport strike in it. PBIT margins in fact expands by about 40 bps, lower COGS of 320 bps offset by competitive investments in A&P of about 230 bps and also compensate for the excise duty drop of about 45 bps.

To move into just a quick snapshot of the first half, strong score card coming through here, underlying volume growth at 6% and A&P up almost 210 bps and despite that we're seeing a PBIT margin expansion of 90 bps coming through. So, and the impact of excise benefits, about 130 bps on the top line and 55 bps on the margin line. Given this performance, the Board has recommended an interim dividend of INR6.5 per share, that's about INR0.50 more than the same time previous year.

Looking ahead in the near term, we expect the growth is likely to be largely volume driven in a continued deflationary environment. Rural growth looks -- our outlook continues to be uncertain and the phasing out of fiscal benefits will continue to have an impact, albeit at a lower level going forward. And the focus on sustaining profitable volume-led growth continues, which mean no change in strategy from our point of view as far as what we're going after. And the mid to long-term outlook, FMCG continues to look positive and our strategy remains unchanged of consistent, competitive, profitable and responsible growth.

With this, let me hand you over to Sanjiv for his views on the performance.

Sanjiv Mehta - *Hindustan Unilever Limited - CEO & MD*

Hello, good evening everyone and thanks, Balaji. Delighted to speak to you all again. And just looking at it from an overall perspective, I think we've delivered a healthy performance given the market's context. In an environment where the commodity costs have continued to deflate and remained soft, price growth has been under pressure for reasons we all understand. So putting the onus of growth largely on the volume that's been our focus. And irrespective whether it is urban or rural, the moot point to recognize is that this is true for markets across, which therefore makes driving volume growth even more important in times like this. It is therefore against this backdrop that I'm pleased about our performance, another quarter of profitable volume-led growth. The broad-based volume growth and sustained improvement in operating margin in many ways reflect the resilience and consistency in our performance. It also indicates that we have been managing the business dynamically and executing a strategy with good deal of rigor and discipline. We also continue to invest competitively behind the brands and capabilities as we focus on strengthening the core of our business, while also investing in developing the future core or market development is what we call out.

Looking at the A&P numbers in the quarter, in fact not just this but even the previous one, it will give you a clear sense of our commitment to invest behind growing the market and growing our competitive position. So on one hand, we are passing on the benefits of lower input cost to the consumers and on the other, we are making significant investment behind the brand, at the same time we are also ensuring that our margins keep improving. All of this [aug us] well for the long-term health of the business and you know very well that we are a business that we are in here for the long term.

Equally, we have been very conscious of our experience some years back when commodities deflated and we were not as agile as we ought to have been in our response in the marketplace. Consequently, we had lost some ground. I am convinced that, this time around, we are doing what is right to sustain the momentum and competitiveness of our business. The benefits of these actions will stand us in good stead, not just now but also into the future.

Alongside, we continue to focus on driving operating efficiencies and cost savings across the business. It is important to keep eyes on this, because today there are benefits that are coming through from commodities, but that cycle as all of you know could change very fast. Therefore, it is very important to be running a lean, agile and efficient operation to stay competitive. We want to be driving all levers of margin improvement and you will see the results reflected in the consistent improvement in operating margin for many quarters now. This is also reflected in the quarter which we are talking about.



Therefore, as you reflect on our results, you'll get a flavor of what our business model is all about and what we have been doing. It starts with profitable volume growth, which provides scale benefit which along with operating efficiency and cost savings provides the fuel for us to invest competitively behind the brand, invest behind market development, which in turn drives more profitable volume growth. More volume growth, more efficiencies, more investment, more profitable volume-led growth, this is what we call as the virtuous cycle of growth.

Having said that, I don't want you to come to a conclusion that price growth is not important, of course it is. No question about it. For us, every source of growth matters. When you look at our own portfolio, soaps and detergents constitute about half of our portfolio, where we had negative price growth, but important is that in the balance part of the portfolio, we had price growth and which kind of negated the negative price growth in soaps and detergents.

While we will keep looking for the opportunities to price up across the portfolio, but given the current context, I'm not overly concerned with this element of price growth, because I know it will come and go. And if recent experiences are anything to go by, gone are the days when it's used to take years for commodity cycles to turn. Haven't we all seen that it takes just a few months for the world and the markets to change?

Therefore, let's recognize the contribution of pricing to growth across time and brand will vary depending on the commodity cycle. We've seen this happen time and again, so while it is something to be conscious of, what's more important from my perspective is to ensure that as a business we're adapting to the changing environment and remaining steadfast on meeting the needs of our consumers.

Same time last year, when we were talking about our results for September quarter of 2014, we were still talking about price increases in soaps and detergents. A year hence, we have seen now several quarters of price weaning off, in fact negative prices. This is where the primacy of volume growth comes in. Delivering on volume growth is an indication that the consumers are with us, that the consumer franchise is well and healthy. We want our brands and products to be preferred by consumers and we want to maintain our leading position in the categories in which we operate in. We are seeing the results of strong brand equities and competitive investment coming through in the healthy volume growth that we have delivered. And I'm very convinced that once there is stability in the market and the cycle turns, we'll reap the benefits of the consumer preference to deliver stepped up levels of growth.

Let me now talk about the segments. Soaps and detergents, as you all know, is the large part of our business. I'm pleased to see that the core of the business has delivered robust volume growth, although it has been largely offset by the price deflation. We are continuing to invest significantly to drive the competitiveness, and it is very heartening to see some of the iconic brands like Dove, Pears, Lifebuoy, Surf, Rin, Vim, all continue to win the hearts and minds of consumers.

Personal products, it's been an excellent performance, it's been broad based, it's been healthy, considering the context in which we are operating. Skin care has again done well across brands; Fair & Lovely, Pond's, Lakme, Vaseline have all added to the growth story.

Coming to hair care, I am particularly pleased with the way this category has been performing for many quarters now. It has and continues to be a fantastic story. Strong consistent broad-based growth right through to this quarter where all formats have sustained momentum. We are now half the market and clearly the investments that we've made over time to strengthen our brand equities and mix in the marketplace is driving preference towards the brands in our portfolio be it Dove, Clinic Plus, Sunsilk, TRESemme all of it doing well.

Oral, yes, we've had a soft quarter, but the important bit is that Close Up, we have got the momentum back and in Pepsodent, we know what is to be fixed, and we are absolutely determined that in another couple of quarters, we should be seeing a turnaround starting to happen on Pepsodent.

And as far as color cosmetics is concerned, Lakme continues its strong run, a great example of how we have built a brand that has gone on to become much more than just a cosmetic brand, I'd say that it is now really a trendsetter itself as a forefront of style and fashion.

Innovation is the need of the hour here and we continue to deliver some very exciting and contemporary premium offerings that have been delighting our consumers. On deos, with Axe Signature range of body perfume now in the market for some time I can say that it has been a very successful launch. As a matter of fact, it has become one of the largest innovations for us last year, and it's now starting to turn the tide for us. And while we have still some ground to make up in this category, I feel reassured that we are headed in the right direction.

So, overall, I'd say our personal products business is in good shape and gives me confidence that we're well poised to leverage opportunity as consumers and markets evolve.

Coming to beverage, beverages have continued to deliver a steady performance for some quarters now. Clearly, the work that we have done in the last couple of years to strengthen the mix, strengthen the brand equities, coupled by some sharp end market execution has started to yield consistent results.

Packaged foods has again been a very pleasing story. I will not belabor the point on commitment to growing our packaged foods business, since you will have seen that reflected in our actions, corroborated by the results for several quarters now. The business has delivered eight successive quarters of double-digit growth with all our key brands, Kissan, Knorr, Kwality Walls, Magnum having performed well. The actions that we're taking on building everyday relevance, driving adoption trials, sharpening our end market execution, are yielding results, and we are now focusing on adding innovation as a lever to growth in this segment, the segment of the future as we would call it.

Therefore, when I look at the totality of our business on balance, I'd say that the state of the business looks healthy, our brands are growing well and we continue to make progress on strengthening our leadership position. Clearly, our strategy is on track, and I believe HUL is well placed to deliver on its goal of consistent, competitive, profitable and responsible growth.

Let me hand the call now back to Dinesh, and of course, I look forward to engaging with you guys over the days ahead.

Dinesh Thapar - Hindustan Unilever Limited - General Manager/Head of Treasury, IR & M&A

Thanks, Sanjiv and Balaji.

With this, we'll now move to the Q&A session. And recognizing we're doing this [in the evening], what we try and do is to bring the call to a close by 7.30, which gives us about 60 minutes for Q&A. Can I request participants who want to ask a question to really keep it tight on the call, so that we can try and accommodate as many during this period of time. In addition to the audio queue, participants also have an option to post the questions through the web option on your screen, and I encourage you to do use that as well. We'll pick those up in the course of the session.

Before we get started with the Q&A, I'd like to remind you that the call and the Q&A session is only for institutional investors and analysts. And therefore, if there's anyone else who is not an investor or an analyst, but would like to ask us a question or seek clarifications on today's results, please feel free to reach out to us at the Investor Relations team.

With that, I'd like to hand the call back to Palak, who will manage the next session for us. Palak, over to you.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Percy Panthaki from Mumbai.

Percy Panthaki - Daiwa Capital Markets India - Analyst

My question is on pricing. Just wanted to understand, I mean, yes, right now we've seen deflation in commodity prices, and therefore a deflation in our own pricing, but going ahead, if I were to have a scenario where the commodity prices stay where they are for several more quarters, how long do you think before you would be able to take pricing up?



Sanjiv Mehta - Hindustan Unilever Limited - CEO & MD

If your question was if the commodity prices remained where they are, yes? If they remain where they are, then once the anniversary of the price growth happens, then at least the negative price growth that we're seeing in S&D will stop happening. Then it would mean that the entire volume growth would start to reflecting in top line. And the price growth, which is there in the rest of the portfolio would obviously help to grow the total top line.

But where we stand as far as the commodities are concerned, very difficult to predict. It is on much your guesses are, but important bit is to understand is, I think our brand equities are strong, our strategy of playing, winning in many Indias has clearly borne fruit to us and once the commodity prices move up, I think we would be in a great position to start hitting the prices up.

Percy Panthaki - Daiwa Capital Markets India - Analyst

So, sir, if I understand your response correctly, supposing if commodities were to remain where they are for the next two years, you don't see pricing coming back in S&D for the next two years?

Sanjiv Mehta - Hindustan Unilever Limited - CEO & MD

Again, we could be looking at selectively, but categories, which have high dependence on commodities, their pricing of course are linked to commodities. The important bit to also understand is that one key part of our strategy is premiumisation, and premiumisation obviously is facilitated when the commodity prices are benign.

P. B. Balaji - Hindustan Unilever Limited - CFO

And just to add to that Sanjiv, there is another angle of pricing coming because of the excise duty benefits.

Sanjiv Mehta - Hindustan Unilever Limited - CEO & MD

That will also [be now].

P. B. Balaji - Hindustan Unilever Limited - CFO

And you saw it at 140 bps in last quarter, 100 bps this quarter, and as I said, we will be seeing that tapering down as the quarters progress and you should expect to see by March quarter more or less everything sorted out. So that's another angle to factor that in.

And as far as -- just keep in mind that when you start premiumizing, there is a mix impact coming through on pricing, which is also start giving you benefit. So these are the various moving parts as far as the pricing is concerned.

Percy Panthaki - Daiwa Capital Markets India - Analyst

My next question is on the ad spends for this quarter. I mean they have been significantly higher at about 225 bps YoY and it wasn't as if the base was low or something of that sort. So just wanted to understand what's happening here, are you increasing share of voice or is the industry moving up, and if so, is this something temporary or likely to continue for a few more quarters?

P. B. Balaji - *Hindustan Unilever Limited - CFO*

Yes. Percy, let me take the piece. Let me also add to the previous question, there is one additional angle for you to keep in mind. When commodities are low but steady that's one kind of a pricing environment. Commodity that is fundamentally deflating or there is a collapse in prices, it's a very different environment. So, we're coming off of collapse in prices, so just seeing some steady numbers coming through. So that needs to be kept in mind as well.

Moving on to your A&P question, as I've always been maintaining, I think there are -- if you look at the business in two parts, there is very clearly a source of funds, which in this case, the source of funds is savings and commodity cost reductions. This deployment opportunities are something that we look at across the table. The A&P segment, there is an A section and a P section, the advertising side and the promotion side. So, therefore those are something that we invest. For example, we did see a step-up in the P side of the picture as well, so not everything that you see is an increase in A&P is all about media. Having said that, it is also about the activation plans and the innovations that we have seen, you would notice some of big innovations have actually landed in soaps and detergents this quarter and that is also stepping up the A&P numbers there.

It where pointed question of are we heating up the market? Not at all. We would never do that. Our job is to ensure that we stay competitive in the market. So it is never a share of voice spike, it's a question of maintaining the right share of voice in the market. But yes, there are other ways to market development, without overheating the market -- without heating up the market, the sampling programs that we run, our [outdoor] promotions that we run. This is a great opportunity to get all those sampled and going and that is how we do market development. And then we do -- this is a great opportunity to do it, so there's a -- when this source of funds dry up, these icons that you are currently putting out there will start growing by that time.

Percy Panthaki - *Daiwa Capital Markets India - Analyst*

And just couple of maintenance questions. One is, have you lost market share in any of your categories? And secondly, on beverages EBIT margin there is a substantial decline, so what is happening on that?

P. B. Balaji - *Hindustan Unilever Limited - CFO*

We don't comment on individual category market shares and therefore wouldn't want to get into that discussion. The way we are looking at it is, very happy with the volume-led growth that we have currently delivered for this quarter, which we believe is a right strategy in a deflating environment. So that's where we are right now.

As far as our beverages segmental margins is concerned, two impacts that you see there. One of course, there is an inflation in tea that we are seeing. We are not yet in a position to call it clean, because the kind of way monsoon has played through and etcetera we're consciously holding back that entire price increases due there, because of the inflation we want to read it a bit more. And second of course is, stepping up the A&P there, because we believe there is a great story going through in the way Red Label is performing or Three Roses is performing or the green tea business is performing. So it's a conscious choice there.

Operator

Jubil Jain from Mumbai.

Jubil Jain - *PhillipCapital - Analyst*

Sir, I have two questions. First one is on Knorr Soupy Noodles. Sir, I personally find Knorr Soupy Noodles better than its competitors, but I always find the stock not available, though it might be -- I mean my observations would be very limited. So I just wanted to understand the strategy we have versus YiPPee and Maggi. I mean, how we can leverage this opportunity to gain a tremendous market share?



And second, I wanted to understand the impact of mix on sales growth and gross margins? How we see the mix impact going forward for the next few quarters?

Sanjiv Mehta - Hindustan Unilever Limited - CEO & MD

As far as the Knorr Soupy Noodles are concerned, you just send me the address where you stay, there is a job for my CD head to ensure that we improve the distribution, no question about that. But I'm very pleased to hear that you love the noodles, yes, and we love our consumers. So thank you for that.

If we look at noodles business, there were some variance on noodle business, which we had withdrawn when the Maggi crisis happened, because they were pending approval. And now we are clearly looking at the whole innovation funnel and drawing up our plans of getting into the markets again, yes as far as the complete the innovation pipeline in the packaged foods business. So watch the space, you will have some exciting offerings on your way.

Jubil Jain - PhillipCapital - Analyst

What about the visibility that A&P, is it -- is the share similar to YiPPees, if you look at the -- I mean, if we compare the sales, and if we take the ratio, is it similar -- is it a bit below, what ITC is doing as of now?

Sanjiv Mehta - Hindustan Unilever Limited - CEO & MD

Jubil, I think the starting point for us is the -- in the entire packaged foods portfolio, this is not a share game, very, very -- first a very small portion of it. And here, it's not a share game or an SOV game here. There is a whole ocean out there to go for. So therefore, we're not looking at it that way. All that we're looking at is get the approvals in place, and then really start developing the market on that and as far -- actually this is a whole thing to play for here.

As far as your point on mix and what are we doing to it, we don't quote numbers on mix, but I think it's a safe assumption to make this personal products the way the growth is coming through, it would be mix accretive from a growth perspective as well as a margin perspective.

Jubil Jain - PhillipCapital - Analyst

But would it be at least more than 50 bps or it would not have a very significant impact in the short term?

Sanjiv Mehta - Hindustan Unilever Limited - CEO & MD

There has been maths on this, so this is not so much a short-term, long-term issue here, but we would -- we do play for mix in everything that we do.

Operator

Amit Sachdeva from Mumbai.

Amit Sachdeva - HSBC Securities & Capital Markets India - Analyst

So just a quick couple of questions. One of them would be obviously look at the volume growth of about 6.5% considering the environment and macro still looks pretty resilient. And if I hear your commentary about most of the categories, even soaps and detergents where most of the brands

have done well, other than one and the commentary on PP is also very, very positive. So I was just wondering, which would be two categories, which if not there would volume growth perhaps could have been 10% rather than 6.5%?

Sanjiv Mehta - *Hindustan Unilever Limited - CEO & MD*

See first is, I would not like to give up any categories, they're all fantastic categories and are stable and it would be wrong to look at the performance of a category from the lens of a quarter. And if you look at the soaps and detergents, clearly our premium brands have done better than a mass market brand. So that's a very clear thing. Part of it is a strategy, very clearly and part of it is that we have to further improve the game on Wheel washing powder.

Other category where the volumes could have been better is very clearly oral care. And in oral care, like I said, Close Up, we are very pleased with the performance, it's gotten to double-digits, there's solid volume growth. Pepsodent is a brand where there is a lot more work to be done, but the good bit is, as a business we now understand what we need to fix. So those would be the headline I would say as far as the categories are concerned.

The other brand where we have just gone in with the fantastic re-launch is the Lux. And Lux, when you are going in with the big launch, there is also a quarter where the pipeline corrections happen. I am very pleased, this is absolutely a great product that's gone into the market, it's a great mix and you will hear more about Lux as we go along.

Amit Sachdeva - *HSBC Securities & Capital Markets India - Analyst*

In terms of Wheel, you obviously commented that it has started responding to the changes you have sort of brought in, in terms of either promotion or even the marketing mix change or whatever it could be. So is it -- can I read it fairly that, now the S&D portfolio, because Wheel is so large, might see some impetus in the next two, three quarters and we should see -- expect that volume trajectory now improve at least on the S&D side, if that is what is responding to what action has been taken?

Sanjiv Mehta - *Hindustan Unilever Limited - CEO & MD*

We refrain from predicting the -- guiding the feature, predicting the future, but look at it from the strength of our brand. First, Rin have been doing extremely well, the brand equities are very strong. And as far as Wheel is concerned, we have done interventions and we are now seeing the volume growth coming back. I'll leave it to your conjecture to estimate what the volumes would be getting into the future.

Amit Sachdeva - *HSBC Securities & Capital Markets India - Analyst*

The reason I'm stuck up, Sanjiv, here is -- stuck up here, sorry, sorry, go ahead.

Sanjiv Mehta - *Hindustan Unilever Limited - CEO & MD*

Full year looks good.

Amit Sachdeva - *HSBC Securities & Capital Markets India - Analyst*

Sure. The reason I was stuck up here is that one of the fears or at least one of the obvious context is, it's deflationary, especially the pricing will continue to be deflationary in the S&D side. And since you are also backing it up with A&P, since there is a question, and is this fair? It looks to me that are we going to see the similar trend of flattened EBITs or it may be right in the short run, because the idea is to maximize volume growth. But are we sort of heading a period where we need to stay with low-single-digit or almost flattish EBIT growth on the S&D?



P. B. Balaji - *Hindustan Unilever Limited - CFO*

I think the starting point for me is that we always look at it, EBIT, at the total HUL level. And that is the power of the portfolio and we will never want to give it up. This is not a conglomeration of four categories that are firing to become HUL. It's one HUL, which has got four categories in it, that's the way we look at it.

While doing so, we do obviously internally focus it as individual category. They have to come to the party and play, but what we give as external commitments always and I think I've -- you guys might have gotten bored of me saying it multiple times. We are committed to modest improvements in operating margins in all scenarios, that is what we're after. And the rest of it, we do decide when there is a source of funds of 320 basis points of cost of goods sold coming down, how to deploy it in the most right manner for the long term, so that we are able to build it.

Let me give you an example. In a scenario when crude prices have come-off, the choice to actually pick up that money and drive Surf Excel exponentially (technical difficulty) ensuring that the biggest brand in the business is growing the fastest, and just look forward into it and say that scenario when you are taking so much consumer franchise in the market, when the commodity prices turn, at least a fraction of them will stay on with you and that's how premiumisation happens. If we let go of this opportunity to deploy with the intensity on our market development initiatives, we'll actually look quite silly two years down the road, saying yes, we declared all the profits and went away and actually we haven't grown the consumer franchise, which will be a sad story. So therefore this is a windfall opportunity and should be treated as such rather than just split it away.

Amit Sachdeva - *HSBC Securities & Capital Markets India - Analyst*

I totally get it, Balaji. So, can I interpret it that A&P spends would need to stay elevated to exploit this situation, let's put it this way?

Sanjiv Mehta - *Hindustan Unilever Limited - CEO & MD*

Let me put it like this. What are the factors which make us spend behind A&P? One is your -- what are the innovations and what are the activations that are happening in the quarter. The second is what is the competitiveness in the category. The third important bit is market development. And we played these different leavers and we play the whole portfolio game, so that our objective of ensuring that we have profitable volume growth, a bit modest improvement in margins, that's continued. You look at our track record of the last few years, three years, four years, what are we talking about is growing -- adding INR10,000 crore to a portfolio and a margin improvement of 350 bps. So that's the direction in which the business we've been leading.

Look at the first half, in a situation which is deflationary, 6% volume growth and a 90 bps improvement in margins. So that is how we have been leading the business and if you listen to Balaji's words very carefully, he underlines modest improvement in margins every time he speaks to you guys.

P. B. Balaji - *Hindustan Unilever Limited - CFO*

One more angle there, I think it is fair for you to be concerned whether, are we spending A&P prudently, are the returns being worth it, are we just wasting money? And that's one thing which we can -- you can rest assured that, returns on marketing investment, ensuring that those investments that are going through are well rewarded is absolutely something that's top of my agenda.

Amit Sachdeva - *HSBC Securities & Capital Markets India - Analyst*

Just last bit Balaji on -- can you give us some amount of -- you may have given it in the past, just want to reassure it, reconfirm it that the taxation trajectory for FY17 would be now -- increase would not be as much and would be very small secular increase or how the --?

P. B. Balaji - Hindustan Unilever Limited - CFO

You're absolutely right. We're now in line about 31.5% is what we are running at and I think that should be the broad range, don't hold me to the last 20 bps, 30 bps simply because it's impossible to know the mix at which we'll sell and therefore that's the only reason. So 31.5% is a fair assumption to go with. And 500 bps that you've gone, that we had last year, the big shift was last year that's already --.

Amit Sachdeva - HSBC Securities & Capital Markets India - Analyst

Already happened, yes.

So just one small bit on beverages, the revenue -- although the commentary seems pretty encouraging, but in terms of numbers it maybe seasonally weaker quarter maybe, but, is it something that -- but doesn't seem like it has done really well, 6% kind of growth on revenues there. I don't know, whether I'm coming back to the same question again, which I think somebody asked on margins, but I think the same investment has not yielded any revenue growth, which actually led to sort of drop in margins there?

P. B. Balaji - Hindustan Unilever Limited - CFO

You're right that the number on beverages is a 6% growth. It's been a steady performer over many quarters and we don't see anything of alarm there. The only thing which we're watching for a little bit, so that we get our actions right is the first part of it, which we will understand it, we will have a very, very much clearer point of view in the next few days. But there is nothing of concern there. And it is just that we normally don't run it quarter by quarter, but it's just that (inaudible) there, nothing to worry there.

Amit Sachdeva - HSBC Securities & Capital Markets India - Analyst

But can you give us a little bit of volume and pricing there, because I think commodities are pretty stable, if I -- it's not really too much down or too much -- almost flattish or minus 10%, I guess or something. But not really an alarming deflation for anything, but are you seeing some competitive activity or something that, because I remember if the A&P spend was increased especially on green tea and other things, as new developments, but if you could give some more color of category that will be helpful?

P. B. Balaji - Hindustan Unilever Limited - CFO

If you look at the brands in that, things like Red Label, really, really stand out performance, doing very well there. We have taken some price corrections in Taj, because we just wanted to take a hard look and the kind of competitiveness that we see. Coffee has been inflating, so this is almost entire bulk of it is price that is coming through there. As far as tea is concerned, it is fair to assume at 50-50 in terms of volume and price and there is clearly a roadmap. If you look at the market development categories with natural care with green tea, continued their really, really strong performance, and with the pipeline corrections in Taj and a bit of internal alignments and executional issue that we are putting together, I am quite comfortable that Tea will get back to its normal ways.

Operator

Prasad Deshmukh from Mumbai.

Prasad Deshmukh - DSP Merrill Lynch - Analyst

Specifically on premiumisation, what kind of readiness are you seeing in customers and say urban as well as rural markets right now?

Sanjiv Mehta - Hindustan Unilever Limited - CEO & MD

India is not one homogeneous entity. Even in an environment where relatively the markets are tough, still there are people who are going in for the premiumisation, getting in for the premium brands. And interestingly, if you would forget the quarter, if you were to look at the last couple of years, even in rural India, the mix of products has started to change, and if you look at the top villages, which is more like [rural] rather than rural, it is very similar to the tier-2, tier-3 cities.

Prasad Deshmukh - DSP Merrill Lynch - Analyst

Just to be a bit more specific there. The premium end that you spoke about just now, that you said that premium end is doing well in soaps and detergent, is that because you guys are offering more promotion or is that there is more willingness from the customer side to try something different?

Sanjiv Mehta - Hindustan Unilever Limited - CEO & MD

See it works both ways. At the end of the day, I believe it's not just about price. It is about price value. When a consumer buys Surf Easy Wash, he knows that at this price he is getting amazing value, so it is worth a while to get in for this brand. And similarly, if you look at Dove again, the people who try out Dove, retention levels are very high. As the prices are soft, the premium brands become more accessible to people. So there would be a general tendency to migrate towards the premium brands, which earlier were a bit far away from the accessibility point of view.

Prasad Deshmukh - DSP Merrill Lynch - Analyst

Second question is on your brand that you had launched about a couple of years back after TRESemme, this is TONI & GUY. So just wanted to understand what is the stage and scale up this brand is at, and what kind of plans do you have for it?

Sanjiv Mehta - Hindustan Unilever Limited - CEO & MD

See, TONI & GUY is a specialist salon brand. And this is at the top end of the game, and this is, we are building the brand and we are very happy with the progress that this brand has made.

Prasad Deshmukh - DSP Merrill Lynch - Analyst

Is there any material contribution right now from this brand?

Sanjiv Mehta - Hindustan Unilever Limited - CEO & MD

Still small, but the target that we had set -- when you look at this salon brand, the more important bit then just the sheer turnover is first is to what extent have they penetrated the salon, and to what extent they have started being used by people who set the trends in the country. And in all those measures, we are very happy with the progress that TONI & GUY has made.

Prasad Deshmukh - DSP Merrill Lynch - Analyst

One last question on same thing again. You have been speaking about reviving Ayush as a brand to target herbal portfolio. So anything that you can share in terms of plans for this?

P. B. Balaji - *Hindustan Unilever Limited - CFO*

Ayush is a brand which we launched at the beginning of this millennium, but I believe that it was a bit ahead of time. Now that there is more clearly there is a trend towards more natural, herbal, ayurvedic kind of products. It was a great time for us to re-direct Ayush and what we have done is initially we are just going to use the e-commerce as a channel, but there is more of innovation lined up and then we are very hopeful.

Prasad Deshmukh - *DSP Merrill Lynch - Analyst*

And this innovation will be mainly in personal care or you are also targeting something in liquid soap or something like that?

Sanjiv Mehta - *Hindustan Unilever Limited - CEO & MD*

We're looking at the whole spectrum and where Ayush can be extended to.

P. B. Balaji - *Hindustan Unilever Limited - CFO*

Actually aware that we are now already launched Ayush on an exclusive tie-up with Amazon for a month and then it goes to other e-com as well. So that process actions are already underway.

Operator

Arnab Mitra from Mumbai.

Arnab Mitra - *Credit Suisse - Analyst*

Firstly on the personal product side, there seems to have been slightly lower growth than last quarter. Also, you did not mention in your commentary that it was volume-led, so I'm presuming that it was more value-led. So while there is a pickup in volumes in S&D probably, is there a slowdown in PP even if it's a small slowdown that you are witnessing or and if you could generally comment on the market situation on personal care?

Sanjiv Mehta - *Hindustan Unilever Limited - CEO & MD*

Just to clarify there, the personal products portfolio, we're very comfortable with the way it is progressing. And if you realize we have called out very clearly healthy volumes across segments. Most segments have actually delivered healthy volume growth and but in the case of personal products there's always a fair play between volume and price. It's one of the things is slightly higher than the other, we're not too fussed about it.

On a broad level, we would want to see a fair mix of price and volume in a category like personal products whether it's not a, yes there are linkage of the commodity to that, but it's not a commodity-led category as intensively like soaps for the laundry.

Arnab Mitra - *Credit Suisse - Analyst*

But in terms of trend, you are not seeing any kind of a slowdown in PP, while S&D clearly lot of brands you've called out as double-digit growth, in PP you're not seeing any slowdown as such?



Sanjiv Mehta - Hindustan Unilever Limited - CEO & MD

We have called out strong -- take hair care category, very strong double-digit growth, take Pond's or a Vaseline or a Lakme, in fact we've been calling out Close Up, a lot of brands have been delivering strong -- have delivered strong double-digit growth this quarter in PP as well.

Arnab Mitra - Credit Suisse - Analyst

One question on S&D, while I understand that you operate as a portfolio and not at a category level, the fact is S&D EBIT in absolute terms has actually declined this quarter, despite the kind of commodity tailwind that's there. So it's been a situation where you have not only passed on part of the benefit, but the entire benefit either in advertising or price. So do you see this as a quarter where there was excessive activity from your side or because it seems this thing that there has actually been an absolute decline in EBIT?

P. B. Balaji - Hindustan Unilever Limited - CFO

As I said earlier, as well, we do not start by looking at EBIT at an individual category level, we start by looking at HUL's EBIT and then of course the individual categories have their own EBITs to deliver. If you have seen, Sanjiv allude to, why we have the A&P investment the way we have this quarter. There is a significant gross margin accretion as far as S&D is concerned, and it is our choice to deploy it to turbocharge growth, as well as step-up market development where it's a great opportunity to step up market development. So that's the background there.

Arnab Mitra - Credit Suisse - Analyst

And given that inputs further declined in SQ as per your own charts. Did you see further price cuts during September quarter where the full impact comes in December?

P. B. Balaji - Hindustan Unilever Limited - CFO

In fact, if we look at the price growth, this quarter in the -- particularly the commodity-led categories is even more negative compared to what it was in June quarter.

Arnab Mitra - Credit Suisse - Analyst

Yes. So my question was because of that, that September quarter further saw decline in inputs, have your pricing further gone down in September quarter from what it was in June and so what I'm meaning is where there further price cuts taken during September quarter?

P. B. Balaji - Hindustan Unilever Limited - CFO

Further price cuts were taken in September quarter was number one. Number two, we do price on replacement basis. So therefore, we do catch the cycle as it comes in, and close about 1% to 2% kind of delta pricing has gone through this quarter sequentially compared to June quarter.

Arnab Mitra - Credit Suisse - Analyst

Sure, just last question on the shampoo price cuts. Now that's been a month and a half that the cuts have happened, do you think there is any elasticity of demand in this category where volume picks up because of pricing going down? And secondly, would you expect a strong upgradation given that there has been such a drop in prices across the board?

Sanjiv Mehta - *Hindustan Unilever Limited - CEO & MD*

First is, it's too early to pick up, whether there is going to be a perceptible permanent change in the mix between sachets and bottles. But having said that, even in a context where there has been a price reduction on bottle, our volume growth has been very strong in shampoos, and we alluded to it. Now, we have the 50% of the hair care market with us. And the good position to be in it that all our brands in hair care are doing pretty well.

Operator

Richard Liu from Mumbai.

Richard Liu - *JM Financial - Analyst*

Sanjiv, you spent a lot of time talking about inflation, deflation, and the pricing growth and pricing decline aspects related to this. Is this deflationary context, one of the key worry spots for FY17, given that all the margin benefits would be in the base by then. And how do you think you will deal with this, if this persists?

P. B. Balaji - *Hindustan Unilever Limited - CFO*

I think the drivers on margin do not change, they are still the same. And we do have mix working in our favor, and that we continue to drive it as we go forward. Let me give you some scenarios. In a scenario where volumes continue to roll, we believe leverages will start kicking in as well, once we're able to also translate a bit of price coming through, it was a significant deflation that we see, even if it goes to up to zero, we'll start seeing the benefits of leverage starting to kick in.

Commodity prices have come off, but our savings programs still continue to be delivering numbers. That's not -- all the 320 bps that you see here is not only commodity price coming off. There's almost 70 odd bps in that which is sitting from savings. So therefore that is something that we will continue to drive and we had a very strong track record of savings delivery in any case. So if I look at mix, if I look at a bit of pricing coming through premiumization, which is translating into mix leverage, savings, I think we do have a very clear roadmap of how to continue to drive margin improvement, which is a reason I keep saying that we are committed to that modest improvement in operating margins.

Richard Liu - *JM Financial - Analyst*

So you don't think that -- if this deflationary context persists in FY17, given that, let's look at like this, if you're doing 7% volume growth and there is no real reason to take up price increase and the inflation does not come back, your top line growth will actually mirror your volume growth and there is no case for margin expansion or compression let's say, given that all the margin benefits are on the base. So (technical difficulty) that volume growth, which is currently in the nature of about 6% to 7%.

P. B. Balaji - *Hindustan Unilever Limited - CFO*

It's a fair question, but if you just reflect on the way of -- today when you see there is no price growth. That's actually -- there are two stories here. The 50% of portfolio, which is a soaps and detergents part of it, there is a price deflation. And the rest of the 50% there is a pricing that is going through be it the personal products portfolio, packaged foods, and I'm sure there'll be some in tea as well. This deflation is what is actually removing this price effect coming through. Even if that goes to zero, I'm starting to see pricing coming through at an overall portfolio level, one. Mix is something -- the reason why we're investing so much in market development, so that we can have sustainable mix that can always keep happening in the business, one. As far as savings program, that continues to deliver, there is no reason why there should be change in that number going through as well. So I am reasonably confident that as far as the commitment to improve operating margins on a modest basis every year we stand by it.

Richard Liu - *JM Financial - Analyst*

Second, I wanted to also elaborate on this segment profit decline in S&D that were spoken about sometime back. So I understand that there is this commodity cost decline, which obviously gives you a lot of flexibility to strategize and so on. So you took price cuts, spent more on A&P etcetera, but why would these choices that you made, if I can call them that, lead to a decline in absolute profit or will you say that this is more quarterly phenomenon that one should ignore?

P. B. Balaji - *Hindustan Unilever Limited - CFO*

Yes, that's always -- we don't look at by quarter because, look at the half year, it's a 90 bps improvement in operating margin. So I would hesitate to, I mean, let's say, too much on a particular quarter of a particular sub-category, when so many moving parts are there.

Richard Liu - *JM Financial - Analyst*

Last one, if I may. Would you be able to give some sense on how much did the shampoo competitive action shave off from the PP revenue and EBIT growth for the quarter?

P. B. Balaji - *Hindustan Unilever Limited - CFO*

Hair did very -- as I went back to my presentation, hair was a strong double-digit growth even after removing significant excise benefit impact on that. So there is a -- it's actually a very strong story there, so I wouldn't -- in fact it's a great growth story there.

Richard Liu - *JM Financial - Analyst*

So therefore the price cut at bottles etcetera, it was basically insignificant if I can call them that?

P. B. Balaji - *Hindustan Unilever Limited - CFO*

They've got compensated by volumes and as I called out, we saw a strong double-digit growth across formats, low cost sachets, premium sachets, bottled and the like.

Operator

Bhavesh Shah from Mumbai.

Vivek Maheshwari - *CLSA - Analyst*

This is Vivek. My first question is a clarification from one of the earlier questions, regarding the price cuts. In soaps and detergents with -- while you called out and obviously the numbers are showing in September quarter, there have been a deflationary -- there has been a deflation impact. Has there been any explicit price cuts in the month of September or October so far?

P. B. Balaji - *Hindustan Unilever Limited - CFO*

Month of September, that's a very precise question, Vivek. I think, definitely in the quarter price cuts were there. I need to check back if there is a very specific number, I don't want to talk -- I don't have the data with me immediately.



Vivek Maheshwari - CLSA - Analyst

I see, okay. Second, again a repetition, but on the A&P side, like you yourself have said, I think it is 19 quarters' highest A&P spend. Do you think that this is somewhere close to the peak of A&P spends now?

P. B. Balaji - Hindustan Unilever Limited - CFO

I think it depends on how the commodity scenario plays out and there is of course an element of how much we can deploy, there is also a question of affordability at some point in time, because we are then start making, we need to start cutting back in case you're not be able to afford that level of A&P, because we need to then deliver the EBIT growth commitment that we have. So therefore we do look at it from that side. Sometimes, when there is a windfall, we are also trying to channelize that into the right places. So, it's not therefore a sustainable level of A&P at this level if the things change.

Vivek Maheshwari - CLSA - Analyst

Third, quick one on operating other income, minus 22% is -- what would it be because of -- operating other income decline on a YoY basis 22% or basically simply put, is the second quarter number representative of how the quarterly run rate should be now?

P. B. Balaji - Hindustan Unilever Limited - CFO

There are two elements in the operating other income that is there -- the other operating income that you see. One of course is what we charge off the Unilever for the cost that we incur within HUL or on their behalf. So we incur the cost, we charge out the cost. That's for me is just as a wash through, there is no strategy or anything from our side on that. Unilever decides what it wants to spend, and we incur it, and then we charge out. So, I wouldn't want to comment on it.

What is the difference is the other, there is a set of -- there are two angles there. One was, we had started a tele-services contract, which we had last year in the base that we are [now one or more there] on some distribution arrangement and we also sold off the Churchgate Head Office where HDFC was earlier being a rent. So those are -- they'll not be there forever going forward. And this year, therefore you see the base impact of this. It's been happening since March quarter this year.

Vivek Maheshwari - CLSA - Analyst

I see. And on the excise duty front, 100 basis points in this quarter, is it possible to quantify while you have indicated it's going to slide down in the next two quarters, but any ballpark number you can indicate?

P. B. Balaji - Hindustan Unilever Limited - CFO

I think I'll need to help you there on this. I think you can assume roughly anywhere between 70 bps to 80 bps for next quarter, and maybe let's say 50% of that, the following quarter and then becoming zero thereafter. Don't hold me to it, it is a broad number that I want you to guide you on for that, you don't get your maths wrong on this.

Operator

Sanjay Singh from Mumbai.



Sanjay Singh - *Standard Chartered Securities - Analyst*

I just wanted to know in the volume growth front where you've called out double-digit volume growth in many of the soap brands and in Rin and Surf Excel, which pretty much covers a large portion of the S&D portfolio. Now in some of these brands the price cuts if I may say, overall consumer value was increased by giving higher grammage. That would also lead to some kind of volume growth, because consumer SKU wouldn't change automatically. So in that sense, is there any way we can remove the higher grammage on a scale basis volumes and get what is the real volume growth per se or can you give some color on this?

P. B. Balaji - *Hindustan Unilever Limited - CFO*

If it is a particular one month or so, I'm completely with you, you could have a scenario where just the guy bought the same one, let's say a Lifebuoy 75 and then you just got delta extra, we call it as volume growth. But over a six months period the person also comes back and buy the Lifebuoy again, so there is an element of usage that is coming through as well. So when we look at volume growth over almost a six month period at a 6%-odd, then I think it is fair to assume that these are all in -- they've been covered off. In one particular month, I'm fully with you. That's exactly a challenge we give to our sales teams saying that it's all about cases that you have sold, but over a period of time it's a different (multiple speakers).

Sanjiv Mehta - *Hindustan Unilever Limited - CEO & MD*

Yes, but we also have to remember that when you increase the size of the bar or you reduce the size of the bar, you change the number of washes. If you were to look at it from a wash perspective, it will go up.

Sanjay Singh - *Standard Chartered Securities - Analyst*

And on rural, you have mentioned there are some challenges, but can you just give some more thoughts on, what's exactly happening, especially the monsoon being bad, so what are you seeing exactly maybe in last quarter, in September quarter or in October as we speak?

Sanjiv Mehta - *Hindustan Unilever Limited - CEO & MD*

First like, we had spoken about in the last call that the rural growth which was running at 1.5 times urban and now really come down to more or less the same level now. As far as the impact of rain is concerned, it is not that across the country the rains have been lower, they have been in batches. And it is too early to say, because the rural demand, one of the factors of course, will be agricultural production. The other factors which impact rural is the minimum support price, the government spending that happens, the subsidy that is given. It is too early for us to pick up a discernible trend impacted by rain as a variable.

Sanjay Singh - *Standard Chartered Securities - Analyst*

And lastly, it's a little broad based, but I understand that you've been pretty satisfied with the volume growth and which is of course in a market environment quite good. But if we take a step back and when we are looking at, at least a printed GDP number of 7% or so and we are doing a 6% volume growth when there is deflation, which ideally should drive some kind of elasticity, then is 6% volume growth while you may be competitive in a way and compared to the market, but if you take the market, if you question the market in itself, is the 6% volume growth for a market when GDP is 7%, when there's a deflationary scenario, there should be some kind of elasticity, would you question that, that 6%, is it a good number in the current market context, I am not even saying economy is improving, but even in the current market context, is it good enough?

Sanjiv Mehta - *Hindustan Unilever Limited - CEO & MD*

It could certainly be better, no question about that. But you have to also understand that the deflation that has taken place, has taken place in categories, which are universally penetrated. These are not categories which are nascent or where the penetration levels are low. These are both

universally penetrated categories and important to understand is what happens when the deflation takes place. When a deflation takes place, there are a lot of new brands which mushroom up and they disappear when the commodity price goes up.

Now, if we were not to respond to the situation of the commodity prices softening, we would have a lot of these mushroom players chipping away at our market share. So our first job is to ensure that the consumers remain within our repertoire of brands. And then of course when the commodity prices soften, it's an opportunity for us also to upgrade that.

So is there a direct correlation between the reduction of price and the volume having gone up to that extent, then the cold reality is in skin cleansing and laundry, the volumes have gone up from the historical rate what we have seen, but because there has been a deflation you don't see it in the top line. We were running in the 4%, 5% level last year in volume growth, which is now stepped up to about 6%. And just pause and reflect on 2008 and 2009. When the commodity prices, we were a bit slow and bit slow in the sense, we were about six months slow in correcting the price. Our volume growth was negative and it took us a long time to recover those consumers and in the process, it also took a toll on our market. So the dynamism of the market is not a straight correlation.

Sanjay Singh - *Standard Chartered Securities - Analyst*

I understand that on the pricing part of it, but if you could and again, I'm not talking about HUL here, I'm talking about the market here, if you want to draw a correlation of let's say, FMCG volume growth versus GDP, do you think 1:1 ratio is something which you're comfortable at or would you think that it can accelerate to much higher levels?

Sanjiv Mehta - *Hindustan Unilever Limited - CEO & MD*

From a long-term perspective, it's certainly 1:1 would be good, because there would be categories which are highly penetrated, where the growth is going to come mainly from up-trading and some increase in consumption rather than penetration. But there would be categories like PP, foods etcetera where the growth rate certainly should be looked at -- it'd be moving at a rate which should be higher than the GDP growth rate of the country.

Operator

Puneet Jain from Mumbai.

Puneet Jain - *Goldman Sachs - Analyst*

Actually, I've got two questions. My first question is again on elasticity. So if you actually look at this quarter, this quarter is actually the slowest of any quarter in the last 10 years. And whenever in the past price deflation actually happened, the volume growth went close to double-digit. So could that be a case that a certain set of customers have become immune to price changes and therefore the elasticity of price changes is not the leading to corresponding response on the volume side?

P. B. Balaji - *Hindustan Unilever Limited - CFO*

Just help me understand that question better, you're comparing it to 2008, 2009 scenario?

Puneet Jain - *Goldman Sachs - Analyst*

Over the last 10 years, this is the lowest revenue growth and if you look at the correlation between volume growth and price growth that seems to have broken slightly over the last two years. So that is possibly resulting in the volume response to price deflation in a much more muted manner.

P. B. Balaji - *Hindustan Unilever Limited - CFO*

If you see the corrections that we have done, if you go back in the 2008, 2009 era when such a price deflation happened and we then took the price corrections almost after six months, seven months. You are coming off of base of volume growth of a very, very low margin. If my memory serves me right, minus 8%, minus 7% kind of volume growth was there in that year. There after you took the price correction. Therefore you have a huge base effect kicking in for you, that is one. Second also keep in mind, all these are also linked into what happens elsewhere in the world as well, because there is a market construct, there is a market that's operating on a particular way. And you can't just wish that away. And therefore, look at the rural tailwinds, the kind of investments that are happening in rural at that time and therefore the kind of tailwinds that came through from rural. And that's basically the very low-penetrated market. And therefore your ability to therefore turbocharge, there is money in the rural market, there is price cut coming in, affordability kicks in and off you go.

So, I think it won't be fair to just compare that situation linearly to the current situation and then conclude that elasticity is not there. There is a reality of the market of rural being under stress, and we all know that rural used to deliver [1.5 times, 1.7 times] kind of growth over urban.

Puneet Jain - *Goldman Sachs - Analyst*

Or possibly the elasticity has come down because as India -- as incomes have increased, maybe certain set of consumers have reached to a certain consumption level, which doesn't change, whenever there is change in pricing, which possibly was not the case may be a few years back?

Sanjiv Mehta - *Hindustan Unilever Limited - CEO & MD*

Again, we won't be able to generalize this comment. If you were to just pick up, that if the categories are highly penetrated, then to that extend the elasticity relatively lower that could be a right hypothesis, but then, you have to isolate variable to understand the whole impact. If the rural consumption, if the money in the hands of rural consumers was much higher, is their propensity to buy would have been much higher when the prices went down. So it is not just a factor of that you've reduced the price, so that the volume should go up at that level. Those were the days when the categories were growing at 18% to 20%. So look at the fact that, in the last 12 months, 18 months the categories have grown at the lowest in the last 10 years.

Puneet Jain - *Goldman Sachs - Analyst*

My second question is actually with respect to, there has been a lot of talk about some stress in the rural distribution channel. And if I look at your numbers also, you have possibly investing a lot more in terms of working capital over the course of last two quarters. So, any thoughts on that thing?

Sanjiv Mehta - *Hindustan Unilever Limited - CEO & MD*

Working capital, in terms of credit into the rural markets is that where your question is leading to?

Puneet Jain - *Goldman Sachs - Analyst*

Because if you look at your capital employed, it has gone up by around INR600 crores-odd this quarter versus last year, and the trend seems to be getting stronger with every passing by quarter. So just that in which direction does it's heading, and so this working capital changes that happening because of which all channels?



Sanjiv Mehta - Hindustan Unilever Limited - CEO & MD

If you look at the days, more than the absolute rupees crores working capitals work on days and therefore days is a better metric, I would suggest. And in that scenario, if you look at mandated days, yes, mandated days has gone up and that's coming off to three factors I would say.

If you look my individual channel growth, so I see you be it -- think like Modern Trades, CSDs, which are fundamentally what I would call as, let's say, a higher credit in that market. So there is an element of mix kicking in, because those are growing faster than, let's say a traditional rural market and therefore there is an element of mix kicking in. And traditionally in CSDs, there is an element of when does collations actually happen and there's an extra question of timing. Whether we are putting more credit into the rural market, my answer is no.

Puneet Jain - Goldman Sachs - Analyst

And looking at segmental, the biggest change seems to be happening in beverages. So will that also get liked to Modern Trades?

P. B. Balaji - Hindustan Unilever Limited - CFO

Sorry, can you just repeat the question please?

Puneet Jain - Goldman Sachs - Analyst

The biggest change in capital employed has happened in beverages?

P. B. Balaji - Hindustan Unilever Limited - CFO

I wouldn't want to comment capital employed into particular category. As a comment, the fact remains that, when it is Modern Trade and CSD as a mix coming through, that is the only thing. The data need to be looked at an overall level rather than an individual category level.

Operator

Ashish Upganlawar from Mumbai.

Ashish Upganlawar - Elara Capital - Analyst

I have a couple of questions. First is picking up from the discussion that we had today is that, 7% kind of volume growth and again a modest improvement in margin seem to be the kind of the targeted numbers, but that essentially is leading to kind of single-digit profit delivery from the -- on the P&L basically. Does it -- despite the fact that there was a description on spending in A&P probably that what I could read from the commentary. So is that the right direction where we are headed or one can expect double-digit EBIT growths to come ahead maybe and that's not a correct way to look at it, what I just said?

P. B. Balaji - Hindustan Unilever Limited - CFO

Let me unpeel this for you. The EBIT growth today, if you look at my top line we've discussed at length, I think we've done a Ph.D. on top line, so let's pass top line for a minute. And we are growing EBIT margins as well, which means EBIT growth greater than top line growth I think is the absolutely the right model in this you want to work, where solid volume growth, a bit of pricing and modest improvement in operating margins means that we should start seeing EBIT growth, which are healthy all linked into the top line delivery that is coming through plus margin improvement, that part of it is very keen.

What you're seeing today, there are two effects that are kicking in thereafter. One is your exceptional income where property sales and those are volatile simply because it depends on market conditions, you're able to put a property out there, and also the inventory of property that is out there. So which we are in a position to dispose off, so that's not something that is part of the plan. We do have a very clear roadmap of what we want to do, but the timing of it is not in our control, that is one.

Second, as far as tax rate is concerned, there has been a big step up in tax rate numbers there. This is probably the last year of the tax rate increase in which case it starts stabilize going forward. So those are the factors that we need to keep in mind as we move from EBIT all the way down to EPS.

Ashish Uppanlawar - *Elara Capital - Analyst*

Keeping aside the tax rate, I'm talking more on the operating line of it. So I think EBITDA growth is 6%-odd now. So, I mean your formula on kind of ensuring that modest improvement in margins and volume growth has to be there. If we take that into account and move ahead for the next maybe three quarters, four quarters, where deflation may be still in the picture. So that suggests that maybe a low double-digit or even a single-digit kind of EBIT growth or the company might be happy with. That's not right is it?

P. B. Balaji - *Hindustan Unilever Limited - CFO*

As I said earlier, I'm not looking at EBIT percent, I mean EBIT growth as a target number or that's not the [goal] that I'm working with. One thing I'm working with is competitive volume growth aided by pricing and modest improvement in operating margins and that depends on how market fares and on that market if it means (inaudible) 10%, 15% market growth, obviously we'll pick up on top of it. So I think it is in the context of what's happening in the market rather than be putting ourselves on a EBIT growth target of any nature, and we've never ever talked about that in our narrative. We've always looked at competitive growths, and then modest improvement in operating margins. That will then be the synergy that we'd really love to do and that is actually the best thing for the business in the long run.

Ashish Uppanlawar - *Elara Capital - Analyst*

Even if that means for some period of time the earnings would might not be that robust. I'm asking because investors would typically look at that metric also apart from the volume growth that generally the company would be targeting?

P. B. Balaji - *Hindustan Unilever Limited - CFO*

I've given you the -- I think we are going around in circles here. I think that's exactly what -- our model is something which is transparent and you've been -- you know it all along. We do not have an EBIT growth as our ambition on which we are operating.

Ashish Uppanlawar - *Elara Capital - Analyst*

Second on the rural side in the first half of the discussion, you mentioned that volume growth and premiumisation both are coming as of now, I mean almost equal to what the company level volume growths are being reported, and the comments after that on the [PBIT] are basically there is an uncertainty and probably you also mentioned that there is some stress. So is it that those stress numbers are still to come into picture and maybe in times to come, things might go on the lower side as far as volume delivery is concerned on rural? Any feedback from your sales channels or why you would put such comments? I just wanted to know reasons for that.

P. B. Balaji - *Hindustan Unilever Limited - CFO*

The comment we have put, if I'm correct is rural outlook is uncertain, is what we've put out the comment there, it's an outlook comment there. As we see it today, if you remember a narrative in July and June that we called out, we do talk about stress in rural. So therefore it is fair to assume

that whatever is there in the rural, lot of it is already in our current performance itself. And therefore going forward, at least our hope is that, we don't have further stress coming through from rural.

And coming to the -- if you look at the rural growth story itself, the fact that it's almost now in line with urban is itself a very, very big story. And therefore and we expect that's probably the way the bottom is and hence, since we're getting multiple views on rural with respect to monsoon or with respect to minimum support prices given global commodity scenario, that's the reason we said rural outlook is uncertain, but our hope is that it's or every one of the bad news from rural is already in our current performance, that's at least our hope.

Operator

Thank you very much, sir. Ladies and gentlemen, due to constraint of time, we are not able to entertain any further questions. This brings us to the end of the audio question-and-answer session. I would now hand over the call proceedings to Mr. Thapar for the web Q&A and final remarks.

Dinesh Thapar - Hindustan Unilever Limited - General Manager/Head of Treasury, IR & M&A

Thanks, Palak. Yes, I'm sure that there are some of you who actually have questions which we've not been able to take up for time, feel free to reach out to us at the Investor Relations team and we'll sure reach our response back to you.

Let's take a couple of questions on the web queue which came in. I'm not going to repeat those which we've already answered in the interest of time.

So we have a question from Lakshminarayana from Catamaran and his question is what is the overall ad spend budget for FY16 and what is the split between digital, TV, print, vernacular print? Do you see a marked change in the mix over the next few years?

P. B. Balaji - Hindustan Unilever Limited - CFO

I think we do not get into details by category there. And if you want us to do by category, by type of advertising, you're almost asking my A&P budget sheet which will be -- I'm sure you understand there's something that we would not be in a position to share. And as far as -- okay, your point was on digital versus non-digital. If you look at our TV spend compared to what used to be almost a 90% in TV kind of spend that we used to have before, that's now down to close to about 70%, and that was a big shift in the way we are spending media money these days. Sorry, I missed that angle there.

Dinesh Thapar - Hindustan Unilever Limited - General Manager/Head of Treasury, IR & M&A

We had a question from Jamshed from Citigroup on the trends in rural versus urban mapping. I think we've answered that, so we will give it a pass. A question from Latika from JP Morgan on mix and the contribution on mix to volume and value and I think we've done that as well. So we'll give that a pass. Percy has got a question from IIFL, on the other expenses line. He says the other expenses have grown by 9.5% this quarter, but before that for two quarters, the growth was 4.5%. What is the reason for the acceleration on this growth?

P. B. Balaji - Hindustan Unilever Limited - CFO

I think one, there is -- do look at other expenses over a longer period of time, because there are costs that do get lumped in at a point in time. So this is a line that we manage for the full year because it's got the [overhead] cost everything sitting in it. There is a bit of lumpiness that does come through here, and it will be a full year number that we would normally work towards.

Dinesh Thapar - Hindustan Unilever Limited - General Manager/Head of Treasury, IR & M&A

Prashant Kutty has a question from Emkay Global. Which categories show a sharp increase in A&P spends and what was the mix between ad and promotions?

P. B. Balaji - Hindustan Unilever Limited - CFO

We did have investments in A&P going through across all our categories, but the soaps and detergents category was the one that saw the lion's share of the spend increase just from an activity planning and what we had in mind for that category. And if I just take that category, the increase was pretty uniform between A and the P line.

Dinesh Thapar - Hindustan Unilever Limited - General Manager/Head of Treasury, IR & M&A

Prashant, we've taken your questions on rural and urban and other expenditures, so won't repeat those. Varun Lohchab, CIMB's question is, is there any one-off in employee costs which is down year-on-year in quarter two in absolute terms?

P. B. Balaji - Hindustan Unilever Limited - CFO

It's not so much this year. There is a -- the base they had a cost true-up that happened, and as far as this one is concerned, there is a one-off of about INR17 crores-odd in the current year coming from some of the pensions true-up [that's gone down]. And here again, do look at these numbers as full year numbers because these are all employee costs or other expense, are all annually budgeted, and there would be an element of lumping that does happen from one quarter to another.

Dinesh Thapar - Hindustan Unilever Limited - General Manager/Head of Treasury, IR & M&A

We have a follow-up question from Percy, IIFL, which is the small and unorganized players have aggregated, have they gained market share in the soaps and detergents market over the past 12 months?

P. B. Balaji - Hindustan Unilever Limited - CFO

We don't comment on shares in this call historically, [no, thanks].

Dinesh Thapar - Hindustan Unilever Limited - General Manager/Head of Treasury, IR & M&A

So I think with that we've come to the end of the Q&A session. Just before we end, let me again remind you that a replay of the event and a transcript will be available on the Investor Relations website. You can always go back and refer to it. And for those of you who were not able to ask the questions, like I did mention, feel free to reach out to us. A copy of the results and presentation that we've just made is loaded on to the site and aware that many of you already have accessed to it, and it can be accessed through the HUL investor app as well.

With that, I'd like now drop this call to a close. Thank you. Thank you, everyone for your participation and have a great night. Thank you.

Operator

Ladies and gentlemen, this concludes the earnings call. You may now disconnect your lines. Thank you for connecting to audio conference service from Airtel.



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