



“Asian Paints Ltd Q2 and H1 FY2019 Earnings Conference Call”

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MANAGEMENT:

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JVs**

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Moderator: Ladies and Gentlemen, good day, and welcome to the Asian Paints Q2 and H1 FY2019 Earnings Conference Call. As a reminder, all participant lines will be in the listen-only mode. And there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing '*' then '0' on your touchtone telephone. Please note that this conference is being recorded. I now hand the conference over to Mr. Arun Nair. Thank you and over to you, sir.

Arun Nair: Good morning and welcome to Asian Paints Investor Call for Q2 FY19 Results. We have Mr. K.B.S. Anand – MD & CEO; we have Mr. Jayesh Merchant, who is the CFO and Company Secretary, and also President of Industrial JV; Mr. R. J. Jeyamurugan – VP, Finance; Mr. Parag Rane – Chief Manager, Finance; and myself Arun Nair from Corporate Communications.

Now I hand over the mike to Mr. KBS Anand to take the call forward.

K.B.S. Anand: Good morning, everyone. Thank you for attending our conference call. I will give a small explanation of our results and then we will take any question and answers.

The domestic economic environment continued to remain challenging with no clear signs of a secular upward trend. The same was reflected in the demand conditions within the coating industry as well. Rising crude oil prices, significant depreciation in the Rupee, tight monetary conditions have only added to this challenging business environment.

The consolidated financials, Revenue from operations increased by 8.5% to Rs. 4,639.05 crores in Q2 and by 11.8% to Rs. 9,037.64 crores in H1. PBDIT decreased by 0.8% to Rs. 847.5 crores in Q2, while it increased by 11.6% to Rs. 1,783.6 crores in H1. PBT decreased by 3% to Rs. 748.7 crores in Q2, while showing an increase of 12% to Rs. 1,596.9 crores in H1. Net Profit from continuing operations decreased by 3.8% to Rs. 506 crores in Q2, while it increased by 11.7% to Rs. 1,077.3 crores in H1.

In the standalone financials, Revenue from operations has increased by 8.7% to Rs. 3,914.2 crores in Q2 and by 12.2% to Rs. 7,620.4 crores in H1. PBDIT increased by 1.9% to Rs. 799 crores in Q2, while it increased by 15.4% to Rs. 1,692.6 crores in H1. PBT increased by 1.1% to Rs. 709.6 crores in Q2, while showing an increase of 16.5% to Rs. 1,519.5 crores in H1. Net Profit increased by 1.7% to Rs. 481.5 crores in Q2, while it increased by Rs. 17.1% to Rs. 1,024.1 crores in H1.

Please note that the figures for the previous year have been suitably adjusted to bring them in line with GST financials. One peculiarity between this year and the previous year is that in the last year, there was an impact of GST implementation in Q1, and as a result Q1 was subdued and Q2 was buoyant. This year, as a result, Q1 appears to be extremely buoyant, although on a cumulative CAGR basis it actually was not so. Similarly, Q2 appears to be subdued in retrospect, both in terms of top-line and profits, largely on account of the buoyant Q2 relatively last year.

However, on profits it was to an extent affected, as I had pointed out in last quarter's telephone discussion that we decided not to pass on the raw material price increases during the quarter because GST had been lowered by 10% on 27th of July, in spite of high inflationary pressures in the period due to the fall in the rupee as well as increase of raw material prices. We have since then taken price increases of approximately 2.35% in the month of October 2018.

BUSINESS REVIEW - DECORATIVE

The decorative business registered a low double-digit volume growth in the current quarter. Volume growth in this quarter has been higher than the value growth, in spite of our 3.4% price increase due to a number of factors. A much higher sale of distempers and putties in this quarter, the reasons for which could be a better Diwali or some change in sales from the unorganized sector to the organized sector; it is probably too early to say this; but the distemper, especially in the smaller markets have increased substantially. And the impact of the stoppage of our Phthalic Anhydride unit in July last year has had a value impact for the standalone business. In addition, there was a significantly higher input cost in this quarter which has affected the top-line. This input cost was given four days prior to July 27th, because we wanted to dispose-off stocks with higher MRP, because it requires massive quantity of re-stickering.

BUSINESS REVIEW - INDUSTRIAL

In the industrial business, the automotive coatings JV, (PPG-AP), witnessed good growth in the General Industrial segment. The Industrial coatings JV, (AP-PPG), continued to grow well, led by good performance in the Protective coating business and in the powder segment. Price increases taken by both the businesses were, however, not enough to counter the pressure on profitability from rising raw material costs.

BUSINESS REVIEW - INTERNATIONAL

In the international portfolio, major units like Egypt, Ethiopia, Bangladesh and Sri Lanka continued to face challenging business conditions. In Ethiopia, difficulty in sourcing forex for imports continues to impact the operations. Incessant rains impacted sales at the unit in Sri Lanka. Reduction in fuel subsidies in Egypt added to the inflationary environment. The greenfield operations in Indonesia continue to progress on the planned trajectory, with focus on expanding the retail network.

BUSINESS REVIEW – HOME IMPROVEMENT

The scale of operations of both the businesses within the home improvement space, i.e. the kitchen business under Sleek and the Bath business under Ess Ess continued to expand with both the segments registering good growth. Both the segments continue to work on further enhancing their market reach and product portfolio.

CAPEX

The first phase of the plant at Mysuru, Karnataka, was commissioned as per planned in the month of September 2018 and we are on schedule to commission the first phase of the plant at Vizag, Andhra Pradesh in the last quarter of the current financial year. The total Capex plan for standalone operations for the current year is about Rs. 1,000 crores, including spends of about Rs. 800 crores of the two new plants.

GOING FORWARD

As mentioned earlier, rising crude prices and the depreciating rupee have added to the challenging business environment. We will need to monitor the impact of demand conditions given the less than forecasted rainfall in the monsoon season, as well as uncertainties arising from a busy election period. At the same time, we expect the raw material prices to rise further in the ongoing quarter.

In the international markets, forex sourcing difficulties in Ethiopia and the overall rising inflationary conditions continue to be a key cause of concern.

Thank you, everyone. We are happy to take any questions you may have.

Moderator:

Thank you very much, sir. Ladies & gentlemen, we will now begin the question-and-answer session. Our first question is from the line of Abneesh Roy from Edelweiss. Please go ahead.

Abneesh Roy:

My first question is on the standalone numbers, so your sales growth is 8.8% and you have mentioned low double-digit volume growth. So, taking assumption of 11% volume growth this works out to around 2% difference, the volume growth is higher. Plus, you would have taken some amount of price hike, so that is around 3%. So, why is there a 5% gap between this, ideally your value growth should have been higher, so you alluded to putty sales and distemper. So, if you could take us through the portfolio.

Management:

So, overall, if we look at the product profile and growth rate, by and large the product profile and growth rates have been fairly consistent over the last couple of years quarter-on-quarter, given, adjusted for the vagaries of GST and things like that. So, definitely there was a much higher growth in emulsions last year in Q2 because of the impact of GST in Q1. That itself gave a higher growth rate as far as emulsions itself is concerned. Distempers have definitely shown a higher volume growth rate in this quarter; so frankly, given all the variables of GST, GST reduction, different Diwali and seasonality, probably taking value and volume growth rates for quarter-to-quarter will lead to anomalies. In addition, if you remember last year, we had shutdown the Phthalic plant around middle of July, that itself, the value growth that came from Phthalic while not significant, would add to an odd percent in terms of difference between value and volume growth. Similarly, I indicated that we took a substantial input hike this year itself when the GST reduction was announced to liquidate stocks, because we had to undertake re-stickering of some 170,000 KL of stock that we were carrying prior to the season, to a lower MRP rate. And it was

not feasible to do it all across stock. So, we eased this process to complete the exercise within a short span of time by giving a fairly substantial rebate to liquidate stock. This reduced top-line automatically; Profits too; but it also affected the top-line.

Abneesh Roy: Sir one follow-up here, you mentioned in opening remarks that because of GST rate cut distempers have done well, so what would be the unorganized share in distemper, and would you expect that to continue, because this is first quarter only?

Management: It is just the first quarter, so let's just wait. At the end of next quarter, I will give you a more specific remark.

Abneesh Roy: But what would be the percentage, unorganized?

Management: The unorganized share in distempers would be substantially higher than the overall share. So, if you take the overall share of the unorganized sector as about say 30% of the paint industry, in the case of distempers it should be at least about 40-45%.

Abneesh Roy: Sir, one more clarification here, in opening remarks you said good putty sales could point towards a better Diwali, could you elaborate on that part?

Management: No, We did not say good putty sales could point to a better Diwali, We said this was a longer Diwali so sales get staggered in a slightly different manner. Last year emulsion sales shifted from Q1 to Q2 because of the GST impact, so it has a difference in value sales.

Abneesh Roy: Sir, second question is on Indonesia, so in Q3 would you see some impact of the earthquake and tsunami? And second, in Q2 could you give some granular detail in terms of the retail outlets, any part of the portfolio which is doing better, which is not doing well and any market share, it is initial days, but any numbers you can put to those remarks?

Management: Market share is so low, I frankly cannot talk about. We are still very small. The tsunami, etc, occurred on relatively low populated island. More than 50% of the market of Indonesia is on Java, and most of our sales focus is around Java at this point of time. So, frankly, our sales is not affected. We have expanded our network; we have about 150 outlets this year and increase the range of emulsions we are selling through the network. So, the response to the products we have launched in the market has been fairly good. But, we have a long, long way to go. It is a heavy investment we are making in that country and we are on track as far as our plans are concerned. But it is like a five-year plan and we will really know how successful we are at the end of five years. But so far things look good.

Abneesh Roy: And sir last one, again on standalone, so your other cost is only slightly higher growth of rate versus sales, I would have expected slightly higher because of the crude oil related impacting your logistics cost. So, if you could comment on that part, how has that behaved? And advertising, is there some cut back because of all these? As a industry has advertising cost come down?

Management: See, this, you are again looking quarter-to-quarter, there is a later Diwali this year so advertising gets postponed automatically.

Abneesh Roy: And logistics costs, sir?

Management: See, we have two freights, the first freight is from the factory to our depots, that cost actually did not increase substantially per ton in this period. Tertiary freight that goes from the depot to the dealer did go up, but the overall impact has thereby automatically reduced. Also there are certain costs which we typically bear like conferences and all those things. So, quarter-to-quarter is not the right comparison, but there are certain additional costs that typically hit us.

Moderator: Thank you. Our next question is from the line of Avi Mehta from India Infoline. Please go ahead.

Avi Mehta: Sir, first, I want to just check on your comment that you made about the demand environment. You said that the coatings environment is challenging with no signs of uptick. Would you argue that, I just wanted to know if you could clarify, are you calling out for weakness or is that a risk that you are seeing, if you could just help us explain that?

Management: All We was saying is that demand has been consistent at that level for the last 1.5 years.

Avi Mehta: So, you are saying, the uptick sign is what you are kind of saying is not yet kind of...

Management: There has been no dramatic change or uptick different from the past.

Avi Mehta: But sir, meaning, despite a delayed festive season, that is the understanding, correct?

Management: Yes.

Avi Mehta: Secondly, on the gross margin bit, we have seen a very sharp QoQ moderation. Now, you have indicated some certain items in your commentary which could be one off, one was liquidation, the other was the higher distemper sales. Would you be able to help us understand how much of the impact would be because of this?

Management: See, inflation was around 5% over Q1, so we have taken a 2.35% price increase in October, which ideally, we should have taken on 1st of August.

Avi Mehta: Okay, so this price increase definitely takes care of inflation as of now, should further inflation happen that is another point?

Management: Not completely, because since then the rupee has depreciated a little further and there is a little more volatility. So, we may have to make further corrective action over a period of time.

Avi Mehta: And essentially you are saying that inflation level till 2Q was taken care, but probably timing is the reason for this?

Management: Yes.

Avi Mehta: But sir, the one-offs that we were indicating, would you be able to help with that?

Management: We were trying to explain because some questions were being posed why the volume growth is higher than the value growth. What we was trying to indicate is the reasons for which we could understand there are differences between value and volume growth in-spite of approximately 3% price increase.

Avi Mehta: Sir, that I understood, that was very clear on your part. What I meant is there is a corresponding impact that will happen on margins because of this, especially the liquidation and the change in mix that you have seen. Would you be able to give us any color on what impact that would have been, just to get some sense?

Management: Percentage margin will not get impacted significantly. Yes, there would be some impact of what input we give, but the change in mix may not make a significant effect in margins.

Avi Mehta: And the liquidation bit, sir?

Management: That will have a little impact.

Avi Mehta: And lastly, if you could share any sense on the input cost trends, while currency I understand, but other than that on the crude based derivatives and titanium dioxide, how has the environment been right now?

Management: Raw material prices are more or less at the same level, it is the rupee variation that is affecting you. Some of the input costs what we are importing, one is rupee depreciation is impacting significantly, and second thing is some of the monomers and things has gone up, even expected to go up in Q3.

Avi Mehta: So, there is a inflation in monomer pricing because of the delay?

Management: See, monomers are derivative of crude, and as a result although they are not directly linked to the crude prices, they are dependent on supply and demand, they tend to have a lag effect over a period of time.

Moderator: Thank you. Our next question is from the line of Vivek Maheshwari from CLSA. Please go ahead.

Vivek Maheshwari: My first question, you mentioned about 2.35% price hike which you took in October, you should have ideally taken in August, right?

Management: Right.

- Vivek Maheshwari:** Sir, does that mean, because September was a period when actually crude actually rose quite a bit and rupee depreciated again quite a bit. So, does that mean that price hike that you have taken does not factor in September inflation?
- Management:** Yes, it does not fully factor in September inflation, you are right.
- Vivek Maheshwari:** And any specific reason, so previous quarter you had rightfully called out that price hike at least for next few months would be difficult, but when you took up prices in October, given from a channel hygiene perspective you cannot keep taking up prices, why did you not go for slightly higher price hike?
- Management:** We were not 100% clear what the authorities are looking at post the GST reduction, whether they are looking at price hike of raw materials from 27th July till the current date or from the beginning of the quarter till the current date. So, we decided to play a safe stand, let a little more time elapse. Anyway, it was a Diwali season so we did not want too much price instability in the market. So, we decided to do step increase in pricing.
- Vivek Maheshwari:** And given that September saw such a large increase and you have taken up prices, the season is just around the corner, which means essentially the next price hike will be at least a few months away, right?
- Management:** Right.
- Vivek Maheshwari:** Second, sorry I have a very basic question, a follow-up to your liquidation part. So, if I understood it correctly, basically whatever you had channel inventory and whatever material would have gone out of the factory on which you would have paid 28%, the rate got changed and it became 18%. The 10 percentage point delta around 27th of July you would have given as rebates to the channel, right, that is what is getting absorbed in a way or is defeating the revenues and margins, right?
- Management:** No. See, we did re-sticker on our own as much stock as we could, but especially the small packs which are packed inside cartons become extremely complex to re-sticker. So, we gave the trader an additional discount in that period, not equal to 10%, significantly lower, to pick-up as much stock as possible, so we would not be that adversely affected in re-stickering all our stocks.
- Vivek Maheshwari:** So, that was essentially the stock which was lying with you or at your warehouses, right?
- Management:** Yes.
- Vivek Maheshwari:** Sir, what about the inventory which was in the channel, whatever it was and on the day of 27th the rates were lower, so ideally there would have been some compensation given to the channel at that point of time. Was there a substantial number or no?
- Management:** No, there was no compensation given, because there was no impact on the dealer network. Our retail selling price to the dealers prior to the tax remains the same, it is the GST component that

has been lower from 28% to 18%. So, whatever we had billed them at 28% they would have got GST credit of 28% in their account. And even if they build that 18% after that to the end customer, they had an extra credit of 10% in their account which they could adjust in future sales. So, they had no monetary impact on them, it was a pure logistics nightmare at our end, we were very clear that we were not allowed to bill any material containing the old MRP from our depots to our customers. So, we either had to clear all stocks before 27th July or re-sticker the material. So, whatever we could not bill till 27th July, we re-stickered at the lower MRP and then sent it out to our dealer network.

Vivek Maheshwari: And one last follow-up on this one, because in my understanding looking at other FMCG companies and all, whatever was the channel inventory it was expected that that will retail at the lower price. So, was that not the case with your dealers on 27th onwards?

Management: Of course, they will sell at lower price because GST is lower.

Vivek Maheshwari: So, there was no impact of this?

Management: See, in the first case there was a total change in taxation policy. In this case there is only a reduction in GST, there is a difference in the two. So, while they got material at a higher GST, they got the credit for that. Our painting contractors, and large customers specially, are fully aware of the scenario and we have directly more than 55,000 stockiest all over the country, more than 1,500 in Bombay. So, in a competitive environment nobody is going to easily buy a higher price. They go from shop to shop to ask prices.

Vivek Maheshwari: Sure, I will probably take it offline separately. And my last question on the economic recovery, your first quarter comment was economic recovery continued to be visible in first quarter, whereas there is quite a bit of a change in second quarter. Can you just elaborate on this bit for me? Thank you very much.

Management: We did indicate that while it appeared to be good, the CAGR over two years was following a consistent pattern. It wasn't really good as it appeared on paper. The CAGR over two years was consistent with our annual growth rates.

Moderator: Thank you. Our next question is from the line of Amit Sachdeva from HSBC. Please go ahead.

Amit Sachdeva: Sir, much of it has been clarified, but just wanted to ask you about the distemper sales getting brought forward in this quarter. So, usually if my understanding is correct, typically Q3 is a very distemper heavy quarter just because of the festival thing as well. Now, that has been sort of brought forward because of Diwali onset and things like that. So, do you expect that mix in Q3 would be different from Q2 and you should expect maybe that Q3 should have little bit more emulsions flowing in which is going into Q4 and further Q1? How do we see mix shaping up, since there is a difference in split festive season last year this time, how is this mix which has impacted somewhat, if not too much revenue line, how the next quarter mix should you expect?

- Management:** See, in general, Q2 has a much higher distemper component than Q3. You are right, Q3 has a much higher emulsion component. But this year Diwali is later than last year, so Q3 would possibly have a higher distemper component this year than last year.
- Amit Sachdeva:** So, as you go into Q3 as well you will see much, much higher distemper component this year, going into Q3 as well?
- Management:** Because it is a later Diwali more distemper is sold in Q3. Now, whether dealers have stocked that much higher distemper, which I doubt, in Q2 from us is a question mark, but in general in distemper is sold largely in the pre-Diwali period in Q2 in every year. Since it is a later Diwali more distemper would be sold at least in the month of October, not in November, December but in the month of October.
- Amit Sachdeva:** Sir, one more thing, when we talk of input prices and look at some data as well, COGS in the standalone has grown by 11% roughly and volumes have also grown by 11%. I see some deteriorating mix which may have impacted margins or something like that. But it does not seem to show that COGS have increased so much as the input prices has swelled so much, or maybe there is some lag of the indirect component which is further due. But how do we sort of resolve this and how do you see that basket growing?
- Management:** So, We tried to explain that there are two, three factors where the top-line has not grown at the same level as volume. One is the mix, which we have to admit, the second is the shutdown of Phthalic vis-à-vis the previous year, the third is higher input this year specifically to get rid of GST cost. So, there are three factors that have led to this deviation.
- Amit Sachdeva:** But sir, the COGS have grown by just 11% in line with volumes.
- Management:** So, material cost in Q2 we did see a 5% inflation over Q1, but we also had the 3% price increase that we have affected from March ending. So, that helped a bit. But yes, the material cost inflation is higher. Going forward the balance we are hoping to bridge with the 2.35% increase in October.
- Moderator:** Thank you. Our next question is from the line of Shruti D. from NVS Brokerage. Please go ahead.
- Shruti D.:** My first question is, can you throw some light on the status of the expansion of plants at Mysore and Visakhapatnam? And as stated in the annual report, this expansion will help in manufacturing of paints at the lowest cost. So, can you provide by how much percentage this cost reduction will be there in the future?
- Management:** We cannot answer the second question, but the first question we had already indicated that the Mysore plant has gone into production from the month of September, went into commercial production on the 20th of September 2018. And the Vizag plant is scheduled to go on production in the last quarter of this financial year.
- Shruti D.:** And my next question, what proportion of sales is between enamel and emulsions and distemper paints? And can you please repeat how much unorganized sector controls in this paints market?

- Management:** The unorganized sector is somewhere around 30% of the paint market. The other questions I cannot answer.
- Moderator:** Thank you. Our next question is from the line of Aditya Soman from Goldman Sachs. Please go ahead.
- Aditya Soman:** A couple of questions, first just on the higher input cost to dispose material. So, there is no increase in promotional intensity in the industry across the channel. And since then things have normalized to the promotional activity which as before in the first quarter or something.
- Management:** Yes, more or less like that. Competitor's intensity is always there, this was not done any reason because of competitive intensity, this was done because it was purely a logistical nightmare to re-sticker 170,000 KL of stock.
- Aditya Soman:** And the second question, is there any difference in geographical demand across the country that you want to call out for, or has it been consistent?
- Management:** For us the East has been consistently growing well, the last few years South did not do well but it is showing signs of recovery this year. Kerala, as you know, has been obviously affected in this quarter, especially in the month of August which was their peak Onam season month; but other than that, it is fairly consistent.
- Moderator:** Thank you. Our next question is from the line of Nillai Shah from Morgan Stanley. Please go ahead.
- Nillai Shah:** First question is on the JV's profitability. I think you have pointed out the fact that the price increases were delayed and not sufficient to cover the input cost. But given that this is usually a B2B transaction why is there a delay in pricing for the JVs?
- Management:** Because there are big boys on the other side, they do not easily agree to increase the prices. We wish B2B was easier than B2C.
- Nillai Shah:** Okay. Has that been corrected more recently or still...?
- Management:** Partially corrected, there is a lag. See, the trouble is you are in a constantly inflationary scenario. And you have to appreciate that this has been a tough quarter even for the automobile sector and some of the industrial sectors because of the demand situation. So, they have not been very open to price increases so to speak. So, it has been constant negotiation and in an inflationary scenario when you increase prices on one day and you cannot easily go back on next day and say I need another price increase.
- Nillai Shah:** And that brings me to the second question, in the past whenever we have lived through very-very sharp inflationary periods we have not really had a big lag, I know now the conditions are different this time, there is GST to content with on one side and plus the demand situation. But in context of where your current margins are in context of where it was historically say three,

four, five years ago, are you comfortable with the comparative scenario that Asian Paints is today in vis-à-vis the past periods?

Management: We have indicated that there is a lag in pricing to an extent essentially on account of GST. But in the case of architectural coatings, the attempt to operate at a certain operating margin which we think with which we are comfortable and can be competitive in the market place, and we are focusing towards doing that; and we do not think that has been in any way adversely affected or otherwise for the medium-term, it may have been affected for a quarter, that is a different scenario. The industrial business, of course the margins are much lower than what we would like in an inflationary scenario and we are working towards improving that.

Nillai Shah: And last question, you mentioned 170,000 KL of stock which needed re-stickering, this if I am not mistaken, works out to about 10% plus of your total output, right? Isn't that too high, I thought your finished goods inventory levels would be just about 10 days or so?

Management: No, it is about 30 days.

Moderator: Thank you. Our next question is from the line of Tejas Shah from Spark Capital. Please go ahead.

Tejas Shah: Just picking up from your demand environment commentary, you mentioned that there was an element of unorganized to organized which also led to lower realization. Sir, usually unorganized to organize happens when the demand environment is robust and that is where the premiumization happens from that segment of demand to more organized segment. So, just wanted to understand how are you reading this trend versus the overall commentary which you made?

Management: We only related this trend to distemper sale because the proportion of the unorganized sector selling distemper is relatively higher in that segment. And because of the implementation of GST, they had a certain price disadvantage compared to how they used to operate in the past. And maybe that has pushed the sale of the organized sector a little higher. But, again, as we said, this is too early to assess, we need to see one or two quarters more before we can make purely definitive statement.

Tejas Shah: And sir was there any unusual share of Project business and decorative business, higher share of Project Sales?

Management: We have been growing consistently in Project Sale business over the last few years, and that growth has continued.

Tejas Shah: But margins in that part of the business would be lower

Management: Yes, you are right.

Tejas Shah: And sir lastly if we look at your gross margins this must be lowest in last many quarters, and you rightly pointed out that there was a lag in terms of price and action that we could have taken. So,

looking at demand environment do you believe that markets can absorb further price hike if need be, without hurting volume growth momentum?

Management: We think so, but we will take that decision on the basis of as we assess the market situation.

Tejas Shah: And that will be post Diwali or before that also you can?

Management: We am sorry, We cannot give this detail. We will be informing our customers first about price revisions.

Moderator: Thank you. Our next question is from the line of Dhiresh Pathak from Goldman Sachs. Please go ahead.

Dhiresh Pathak: Just to better understand the cost push, so what percentage of COGS is TIO2 and what percentage of COGS is other crude downstream monomers?

Management: Around 20-22% would be TIO2 of material cost, and all crude put together would be somewhere around 30% odd.

Dhiresh Pathak: And in terms of better understanding the mix, what percentage of sales is putty and what percentage of domestic...

Management: Sorry, We do not share information on this.

Moderator: Thank you. Our next question is from the line of Arnab Mitra from Credit Suisse. Please go ahead.

Arnab Mitra: After the GST rates were cut there was some expectation that there could be potentially some premiumization within the decorative segment, I am not talking about the distemper upgrade as such, but among the rest of the decorative paint segment. So, have you seen any such trend with this 10% kind of price reduction or anything else you have seen happen after the price has been cut by 10%?

Management: No.

Arnab Mitra: And sir the other question was in terms of the Karnataka facility, are there any tax incentives that you now have now that the facility has commissioned, and will it help in terms of margins in the next couple of quarters?

Management: Yes, there are certain benefits which we are in the process of getting agreed upon. Though, government has agreed we are just documenting it. Once it is done, we will communicate it.

Arnab Mitra: And lastly in terms of, again, the question on the input cost cycle. So, other than this lag effect which is coming out of your conservative stance under anti-profiteering, you do not see any

major challenge in ultimately being able to pass on this inflation over the next two to three quarters, once you have better clarity on GST anti-profiteering?

Management: In architectural coatings, yes, you are right.

Moderator: Thank you. Our next question is from the line of Richard Liu from JM Financials. Please go ahead.

Richard Liu: Sir, I just want to know how do you guys forecast or plan for cost in a year like this when you have two new large plants that is up for commissioning? The reason behind this question is, if I look at the past, whenever you have had a new large Greenfield plant coming up, for example being Rohtak and FY11-12 and Khandala being FY13-14, your other expenses line have typically grown at a significant proportion than what it typically grows at. And given that there are two of them now, I just wanted to ask for some sort of input from you as to how do you see overheads going forward?

Management: So, under Mysore front, we will have the cost impacting us for the next six months, since it is now commissioned. Vizag, we do not think any cost will hit us significantly this year because it gets commissioned only, as per plan, in the last quarter, so maybe next year. But you are right, typically in the first 1.5 – 2 years when the plant is actually running at sub-optimal sort of capacity utilization, you will have the overheads sort of kicking in at a much higher rate. We cannot quantify them for you, but there will be an impact.

Richard Liu: But given that you could be in a position to really project in terms of how capacity utilization could progress over a period in time? Is it possible to match the cost structure with the volume progression in those plants?

Management: Typically, that is not how it pans out, because you will have certain kicks first at the plants which sort of need to incur whether you produce x number or x+y, so those costs typically impact you at the sub-optimized levels.

Richard Liu: And given that these two plans have now come up, let's say four, five years after the last one which was Khandala, and given that technology, etc, has become more efficient over a period of time, let's say renewal energy, etc, etc, has that been an element of cost efficiencies built into these plants such that the additional hit will be lower than what we have seen earlier or the impact would be as drastic as what we have seen in case of Khandala?

Management: We have invested money in terms of upping the automation quotient at these two new plants versus say what we have in Khandala, specifically in terms of material handling cost within the plant. So, there could be some bit of optimization on that front as compared to Khandala.

Moderator: Thank you. Our next question is from the line of Praveen Shetty, an individual investor. Please go ahead.

- Praveen Shetty:** Most of my questions have already been answered. I had two additional questions. First is, it is very much obvious that the market capitalization of your competitor companies are obviously going down since it is a challenging environment for all the parent companies. So, will there be any acquisitions that Asian Paints will be doing?
- Management:** In India, that becomes a difficult task given the kind of market standing we have and market share that we enjoy in India. So, I think that is a pretty difficult task. On the home improvement front and the international front, yes, if there are good opportunities we will scout for it.
- Praveen Shetty:** And my second question is, there is some kind of hyperbola statement that is being made in the markets that crude price can go up to \$100 per barrel, so what will be the margin impact the companies will have? And it is very much obvious that the company will take a hit on that, but...
- Management:** It is too premature to comment on all these hypothesis. But earlier in the past also it has touched above \$100 and we have handled that, we will see.
- Praveen Shetty:** No, I was just calculating the worst case scenario that can happen.
- Management:** Sorry, We cannot comment on that at this stage.
- Moderator:** Thank you. Our next question is from the line of Jigar Shah, an individual investor. Please go ahead.
- Jigar Shah:** Sir, would you be able to elaborate on the wood coating business separately and also give what kind of revenue and margins are there in this business? And some future outlook?
- Management:** Sorry, we do not give you individual breakups of revenue and margins, all we can tell you is we have a steadily growing business, we have a tie-up with an Italian company called Renner, and we manufacture some of their products in India and import others, and we are selling these premium end products through a large number of our stores all over the country and getting steady growth in the polyurethane, polyester and the water based wood finish segments.
- Jigar Shah:** Sir, what is the revenue?
- Management:** Sorry, we cannot comment on that.
- Moderator:** Thank you. Our next question is from the line of Shruti D. from NVS Brokerage. Please go ahead.
- Shruti D.:** With respect to rising oil prices and rupee devaluation, how much percentage of your portfolio or the business is hedged?
- Management:** So, as we said, on the crude side our raw material exposure is close to 30% but there are not too many sort of exchange related products available for hedging. On the dollar front we typically look at short-term hedging, so maybe a month or two months, not more than that. That is where we stand as on date.

Shruti D.: But can you provide a percentage in the case of rupee devaluation, how much is hedged?

Management: We look at covering the short-term payables which is typically month or two months of exposure.

Moderator: Thank you. Our next question is from the line of Abneesh Roy from Edelweiss. Please go ahead.

Abneesh Roy: Sir, in the international markets, some of those you are not the market leader, so where all you have been able to take the price hike and what is the quantum?

Management: So, we have been able to take price hike in almost every market, but the quantum we have been able to take varies. In most of the markets we have taken a quantum very close to what is required to recover the cost, but it is with a lag effect. So, you have to realize it has been towards the end of the quarter, so the impact is higher. Maybe one or two markets this is not true, Dubai and Sri Lanka, but otherwise by and large, we have been able to take prices to recover most of the costs.

Abneesh Roy: Sir, Dubai, what is the issue? Because the market was reviving there, crude is up?

Management: We have a very vigorous competitor after the implementation of VAT of a 5% this calendar year, he lowered prices by 5% to absorb the impact of VAT in an inflationary scenario.

Abneesh Roy: That is the market leader, right?

Management: More or less, yes; the volume market leader.

Abneesh Roy: And sir one clarification, you said the Mysore plant will lead to higher overheads, on the other hand because it will be closer to one of your bigger markets the logistics cost could also come down. Isn't that material enough?

Management: It is material but that will help us next year as volumes pick up, in this year the impact may not be that significant.

Moderator: Thank you. Our next question is from the line of Parthav Jonsa from NVS Brokerage. Please go ahead.

Parthav Jonsa: Sir, I just got one question. Pertaining to the auto sales, the auto sales numbers are really not so impressive off lately, how do you perceive your sector growing pertaining to this auto sector?

Management: So, we have a joint venture with PPG that caters to the auto sector, and some proportion of their businesses is to the four wheeler auto segment. They do not supply largely to the Japanese manufacturers and they supply more to the non-Japanese manufacturers. We have become about 100% supplier to Ford, etc, so actually our business has gone up. But yes, overall growth of the automotive sector is a cause of worry for us.

Parthav Jonsa: So, what would your current market share in India be, like if you can just give me some rough idea on that front?

Management: We have no idea, sorry.

Parthav Jonsa: And my very last one is on the Vizag plant, your Mysore has already started the operations, so when Vizag starts with operation in Q4 or the last quarter, what would be the production which would be coming out from that plant?

Management: Not significant in the first quarter any which ways.

Parthav Jonsa: No, I am not just asking about the first quarter, once it is fully ramped up and all?

Management: Yes, about 3 lakh KL capacity.

Moderator: Thank you. Our next question is from the line of Keyur Pandya from ICICI Prudential. Please go ahead.

Keyur Pandya: Sir, my question is, you mentioned that we have taken price hike of 2.35% from October, which is to take care of inflation till August. So, inflation after August? That is one thing. And second thing, the deteriorating mix of distempers because of the festive season, so looking at these two things, if we do not increase the price then there will be some margin pressure in medium-term or short-term?

Management: So, there is a little margin pressure, we do not deny that. So, there is a probability of a further price increase in the quarter.

Keyur Pandya: But the general story of premiumization in paints, that is the case with most of the products in India. So, this deteriorating in the mix is a short-term aberration or how do you see that?

Management: So, the premiumization continues, We tried to indicate that the growth rate of premiumization remains the same. But there is one chunk of the market that has grown a little faster. So, if you would see the average growth rate over the last so many quarters has not been consistently 11% - 12%, it has been a little lower. This higher growth rate is probably because of the higher growth of distempers and putties.

Keyur Pandya: And that may continue for some time? That is what my point is.

Management: We hope so.

Keyur Pandya: Which would in turn impact our margins, right?

Management: No, nothing to do with the margins. If we sell more on something we make a profit, our profit goes up; We look at absolute margins more than anything else.

Moderator: Thank you. Our next question is from the line of Pratik Poddar from Narnolia Financial Advisors. Please go ahead.

- Pratik Poddar:** Actually, I wanted to ask the rise in short-term debt in the consolidated books is due to the rupee depreciation, right?
- Management:** This is probably happening only at our international holding co level where we are using certain additional borrowings to fund the operations in Indonesia
- Pratik Poddar:** In which region?
- Management:** Indonesia.
- Pratik Poddar:** Another question that I have, if I look at the half yearly balance sheet it appears that you have already invested Rs. 900 crores approximately in the Capex. So, on a full year basis you had given a guidance of Rs. 1,200 crores on a consolidated basis. So, are we going to spend remaining 300 or it would increase going ahead?
- Management:** No, we will be within the stated Capex range.
- Pratik Poddar:** One last question, just to understand the other expenses better here. So, other expenses were a little bit higher due to stickering, logistics or overheads from the new plant, which would be the component which is affecting it the most?
- Management:** It is largely because of the inflation that we have seen in the logistic cost versus Q1, stickering cost, yes, there is a bit of it, but largely it is the logistic cost.
- Moderator:** Thank you. Our next question is from the line of Chinmay Gandre from Future Generali. Please go ahead.
- Chinmay Gandre:** Sir, just a broad estimate in terms of the rebate that we gave to the dealers because of the change in GST rate. Could it be in the range of Rs. 60 crores - Rs. 70 crores for the quarter?
- Management:** No, much lower.
- Moderator:** Thank you. Our next question is from the line of Tejas Shah from Spark Capital. Please go ahead.
- Tejas Shah:** Sir, just one follow-up. Sir, one of the sector peers indicated yesterday that there was some de-stocking pertaining to GST in the month of July. So, did we also experience that kind of de-stocking at dealer level?
- Management:** No, as indicated we had given a rebate; dealers did not want to stop material that had the old MRP because it would complicate their operations. So, we took the counter measure of incentivizing dealers to pickup stock with the old stickering. So, they lifted material. So, we probably saw higher stocking in July.
- Moderator:** Thank you. Our next question is from the line of Jaimin Shah from RWC Partners. Please go ahead.

- Jaimin Shah:** I am just trying to understand on the price increases, when you said that you plan this 2.3% increase in August, which was finally taken in October and then you had kind of rupee depreciation in crude. I am also trying to understand here, what is your margin thought process behind it, because coming from 2016, 2017 and 2018 we had these peak margins when I look at the longer term trend. So, are we thinking about margins in these last three years to kind of maintain around these levels or are we kind of going back to the longer term trend of 19% - 20%?
- Management:** 18% - 20% we are okay. We do not normally change pricing month-to-month and nor do we operate at that level. In a deflationary scenario which we saw two years earlier, margins suddenly increased because raw material prices are falling. And in inflationary scenario, it is the reverse. So, we want to balance the count. I think we are okay at 19% - 20% margin.
- Jaimin Shah:** So, these price hikes kind of keep you in that 19% - 20% range, not necessarily the peak margins that we have seen in last couple of years?
- Management:** Yes.
- Moderator:** Thank you. Ladies & gentlemen, as there are no further questions from the participants, I would now like to hand the conference over to the management for closing comments.
- Management:** Thank you very much, for participating in our conference. See you next quarter.
- Moderator:** Thank you very much, sir. Ladies & gentlemen, on behalf of Asian Paints, that concludes this conference. Thank you for joining us. You may now disconnect your lines.