Investor and Analyst Q1 FY18 Conference Call

July 31, 2017

Operator:

Ladies and gentlemen, good day and welcome to the Godrej Consumer Products Q1 FY18 Earnings Conference Call hosted by Citigroup Global Markets India Private Limited. 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 would now like to hand the conference over to Mr. Aditya Mathur from Citigroup Global Markets. Thank you and over to you, sir.

Aditya Mathur:

Thank you and good evening, everyone. We'd like to welcome you all to this call which we are hosting for Godrej Consumer Products Limited. We have with us the management on the call. I will hand it over to them to take it forward.

Tapan Joshi:

Thank you, Aditya. Good evening everyone and thank you for joining us. We welcome you to the Godrej Consumer Products Limited Conference Call to discuss the performance for Q1 FY18. We have with us, Nisaba Godrej - Executive Chairperson; Vivek Gambhir – Managing Director and CEO; V. Srinivasan – CFO and Company Secretary; and Sameer Shah – Head Finance, India, SAARC & Investor Relations. We will start the presentation with Vivek sharing his thoughts on our performance and then we can open up for Q&A. Over to you, Vivek.

Vivek Gambhir:

Thank you, Tapan. It is a pleasure to be talking to all of you and sharing the highlights of our performance for Q1 FY18. There are three broad messages - first of all, in terms of navigating the GST, as our result would show, we have delivered 6% primary growth in sales and 9% secondary growth. This is a reasonably good performance given the channel volatility in the run-up to the GST implementation. Our teams on the ground have handled the changes very well and the GST transition so far has been smooth. Our growth was relatively well balanced across the category and we continue to sustain and grow share across the category. The thrust in innovation continues. We have now entered the Professional Hair products segment to cater to the needs of salon stylist through a range of innovative products under the new Godrej Professional brand. Generally, consumer demand remains robust. While there has been channel volatility due to the implementation of GST, we expect the market situation to improve and stabilize by the end of Q2FY18.

The second big theme is around investing for growth. This was the quarter where we increased our investments as we feel that the market is poised for recovery. Our advertising spend increased by 15% mainly to support our new products. In spite of some of the sales slowdown in June, we chose to continue to invest for the longer term. This, we believe, will benefit us in the quarters ahead. As a result of this investment and relatively low operating leverage, our profit growth trailed our sales growth. We believe that this profit dip is temporary and that earnings will recover in the quarters ahead.

Thirdly, on the International front, our performance was varied with some bright spots. Africa continues to do very well with 26% constant currency growth, we have maintained this trajectory in Africa for over 8 to 9 quarters now. UK also did well with the 24% constant currency growth. Indonesia had a relatively weak quarter. Some of the macroeconomic challenges continue as this is shown by the results of some of the other companies in Indonesia. We also had 10% less trading days due to the Lebaran holiday which was in July 2016 last year and we also saw some intense sales promotions by competition. The team is taking some corrective actions and we hope the situation will improve in the quarters ahead. Latin America also had a challenging quarter with a 4% constant currency growth rate driven largely by macroeconomic challenges.

Overall, this has been a quarter of mixed performance, clearly lots of positives to take away from the performances in India, Africa and the UK. The good thing is that the teams are putting in a lot of building blocks in place that will enable us to deliver a much stronger performance in the quarters ahead.

I will quickly walk you through the presentation and cover some of the highlights. If you turn to Slide #3, our Q1 constant currency sales increased by 8% y-y, as I mentioned India business sales growth of 6% y-y. Our international business sales grew by 11% y-y on a constant currency basis. Net profit declined by about 9%.

The Board has also announced an interim dividend of 100%, INR Re.1 per share.

The next couple of slides just take you through the exceptional items and also the bridge between operating and reported EBITDA on Slide #5.

On Slide #6, per your request, we have begun listing all the key balance sheet data. So hopefully, you will find it useful. The one caveat to add is that, some of these metrics are best looked at on an annual basis. So while we do provide on quarterly basis metrics such as ROCE, our recommendation would be please do not read too much into it because those numbers tend to be lower in the first quarter and the trajectory will improve as the quarters go ahead. So best to look at them on an annual basis.

If we turn to the India business, as you can see on Slide #8 where the primary sales growth was 6% and secondary growth of 9%. We have made some healthy upfront marketing investments to support our recent new launches, as a result of which we saw bit of an EBITDA dip impacted by upfront marketing investments and some transition related to some of our manufacturing units which led to higher excise duty. That transition is more of a temporary thing. I think you will find us being able to improve our gross margins going forward as well and I think we will continue to work harder on driving EBITDA growth ahead of sales growth.

On Slide #9, you'll see growth rates by category. Generally across the board – Household Insecticides, Soaps and Hair Colors, the category growth rates have been positive. Insecticides had a bit of soft quarter with a primary sales growth of 4%. Generally, April and May did quite well, but we saw fair amount of cautiousness because of the GST in trade in June 2017. Also, in some parts of India, the weather did not fully cooperate like Tamil Nadu and so the result of which we did see the seasonal variation. Good news is that our share positions are looking still strong and our penetration continue to improve and recently launched HIT Gel Stick is scaling up well in the market.

On Hair Colors, the performance was very strong and competitive. There was a little bit of cautiousness we saw in June. Crème continues to do very well with high teens growth and we are now scaling up our BBLUNT launch as well.

On Soaps, we are seeing good recovery with primary sales growth of 7%. The performance was driven by some very effective micro-marketing initiatives, good communication, some selective price increases and withdrawal of consumer offers. Cinthol continues to grow faster than Godrej No.1 and premiumize our portfolio.

In terms of other new launches, I think Cinthol Deostick and Aer Pocket membrane continue to gain more traction.

Switching gears to our International business - if take a look at our performance, we have seen challenges particularly in Indonesia and there have been temporary margin pressures in Indonesia and Latin America in particular.

Turning to Indonesia on Slide #19, as I mentioned earlier, growth was impacted by first of all macroeconomic challenges, consumer spends still seems to be a challenge as is witnessed by the results of the other players as well. Inflation reached an all-time high in June and prices of food and electricity have gone up. So the economy still seems to be a little bit weak. Sales growth was also impacted by 10% less trading days, as I mentioned, and a lot of intensity in state promotions spend by competition.

The team is putting together lot of corrective actions in place. Our expectation is that Q2 will still be a challenge, but you should start seeing an improvement in the business starting from Q3 onwards. The team has planned a lot of new innovations in place and so over the remainder of the year, you will see a fair amount of new launches, etc., that will try and shift the conversation from a largely promotion-led game that the industry is experiencing right now. While the biggest pressure has been in Insecticides, generally Air Fresheners and Baby Tissues are doing quite well, and the response to our Hair Color launch has also been encouraging.

In Africa, we continue to see strong double-digit growth. The SON integration has been going very well. The local manufacturing of Wet Hair Care products has commenced in various parts of Africa. So the benefits of that should start to flow in the remainder quarters ahead.

In Latin America, we saw some temporary challenges. In Argentina, the macroeconomic situation does seem to be a little bit challenging. The country is coming out of a recession in Q1. Some of the austerity measures that the government has imposed did impact consumer confidence and unemployment rates have gone up. What is encouraging is that the IMF last week raised its growth forecast to 2.4% for the country from 2.2% GDP growth. So that augurs well in terms of a slight recovery in the economy.

In Chile, we did see some near-term challenges, a couple of customers ended up merging their backend operations and one of the other customers had scaled down inventory which led to some scale back in Q1. However, the teams are quite optimistic that you will see stronger performance in both Argentina and Chile in the quarters ahead.

In terms of Europe, the results are very strong. One was very good execution by our team, but we have also benefitted from a good season. This was a hot summer in the UK and this benefitted the sun care brand that we distribute. It was the combination of some weather which helped us along with some very good work that has been done by the team.

On Slide #23, we provide a snapshot of our overall performance that we have just covered.

On Slide #24, we have made some management changes. We are very excited that Akhil Chandra has joined GCPL to assume the responsibility for leading our Indonesia business from Naveen. Akhil has worked with top-notch global consumer companies for over two decades. He is been in the leadership role as the Global Category Head for Reckitt based in London. Prior to that, he was Managing Director for Reckitt Benckiser in India. He has also had a very significant stint at GSK Consumer Healthcare, working all across Southeast Asia including Indonesia. Akhil will be based in Jakarta.

After a successful stint managing the Indonesia business, Naveen will now move to Dubai to head the Africa cluster. Over the last seven years, Naveen has done a great job leading our Indonesia business and has been intimately involved in shaping our business there. We hope to see him replicate the same success and scale up our Africa business.

Omar is still very much part of the Godrej Group. He has been instrumental in defining our Africa growth blue print and implementing our M&A agenda. Omar will continue to lead M&A and integration at GCPL.

The other slides are standard slides in terms of some of the recognitions we have received.

So let me just pause there. As I mentioned to you, overall, this has been a quarter of mixed performance. But there are a lot of positives to take away, particularly, given our performance in India, Africa and UK, and our teams are putting in a lot of building blocks in place that will enable us to deliver a much stronger performance in the quarters ahead.

We can now turn to your questions and feedback.

Continue: - Q&A…

Questions and Answers:

Moderator:

Thank you. Ladies and gentlemen, we will now begin with the question and answer session. We take the first question from the line of Manoj Menon from Deustche bank. Please go ahead.

Manoj Menon:

On Indonesia, if you could talk about the competitive environment there, what has actually happened and what is the update as of now?

Vivek Gambhir:

What has been happening there is that the overall economic growth has been a bit of challenge particularly as far as consumer demand is concerned. So over the last three or four months, we have seen a significant ramp up in the promotional intensity by a couple of players. So our first stance was to wait and watch and see what happens as far as the intensity was concerned, but we ended up responding back to some of these promotions. The impact of that is still taking place. So we will probably have to wait and see what happens in this quarter on the impact of some of the promotions and then how we end up continuing to respond. In parallel, along with responding to these promotions, we are also looking at a couple of interesting innovations to be able to change the conversation from just pure promotions to more of an innovation-led agenda as well.

Manoj Menon:

Is it related to Household Insecticides or across categories?

Vivek Gambhir:

This is all Household Insecticides related. In terms of Stella and Mitu, we are continuing to gain share. Hair Colors, the business is too small, but again, it is trending in the right direction. This primarily confines to Household Insecticides, but that is a substantial portion of our business as you know in Indonesia.

Manoj Menon:

On Africa, now that it has been a few quarters of the SON in investments. If you could just talk a little more details in terms of how has been the marketing mix and what has been the initial consumer feedback and how do you see the SON specifically ramping up over the next two to three years?

Vivek Gambhir:

It is still too premature to comment. It has been only a few months since we launched TCB in Kenya and we are now launching Mega Growth in Nigeria. Later on this year, we will look at launching Mega Growth and Dr. Miracles in South Africa. So suffice it to say while the potential is huge, it is too early to give you an indication of how well the launches are doing. What is interesting is that if you look at Africa plus SON together, the non-Dry Hair part of the portfolio is now around 40% of our business. If you look at just Africa excluding SON, the non-Dry Hair part of the portfolio is almost 20% of our business. So strategically, one of the big imperatives we had was to broaden the portfolio that we participated in, so that journey is well under way. With regard to the specific success of the local products that we have launched in Africa, we need about six months more before we start giving more specific data.

Manoj Menon:

For soaps, was there no GST-led trade down stocking?

Sameer Shah:

Relatively, the impact of GST-led destocking in Soap was lower as compared to both Household Insecticides and Hair Colors.

Vivek Gambhir:

We had several months of very lukewarm growth as far as Soap category is concerned. If you recall, a few months ago, there were concerns about a lot of excess stock that consumers had in their pantry. But as the consumers have consumed that stock, we are seeing now the stock levels are quite low across both the channels and consumer homes, which augurs quite well in terms of what the next few quarters could look like as far as Soap growth is concerned.

Manoj Menon:

On the comment about excise increase impacting EBITDA to the tune of 100 bps, is it for Baddi and Soaps?

Sameer Shah:

Yes.

Moderator:

We take the next question from the line of Abneesh Roy from Edelweiss Securities. Please go ahead.

Abneesh Roy:

Is it by design that you want Cinthol to grow faster where your margins will be higher or you expect Godrej No. 1 to come back to at least similar kind of growth versus Cinthol and by when?

Vivek Gambhir:

For us, it is not one versus the other; we are actually seeing a lot of recovery in Godrej No. 1 as well. So clearly with Cinthol, the intent would be to make it a broader range of products, it is not just about Soaps, it is about Deodorants and other grooming products as well. We are seeing a lot of traction in Cinthol. Godrej No. 1 is also showing a lot of recovery. As far as Patanjali is concerned, so far, basis the numbers that we see and there could be certain caveats in terms of their pickup, etc., we are not seeing any impact of Patanjali on Godrej No. 1 per se. But recognize the fact that this data may not be as fully accurate. We have no visibility, for example, into the amount of soaps sales that go through their own store. In terms of some of the data that is reported by research companies, we do not see any impact from Patanjali so far on Godrej No. 1. Godrej No. 1 clearly is seeing good traction as well and we are optimistic that both Cinthol and Godrej No. 1 will do well in the quarters ahead.

Abneesh Roy:

Last quarter you had said that in North India there was some impact of Patanjali. Are you now saying that the impact is now lower in North India?

Vivek Gambhir:

We cannot quantify or assess any specific impact even in North India.

Abneesh Roy:

When do we see predictable growth coming back in Indonesia? Also, launch of the Hair Color has also happened in the last few quarters, so does that get impacted because if your main business is not doing well, you may not have the enough brand support required?

Vivek Gambhir:

I think we are also quite disappointed by the result of the Indonesia business, some of it is not in our control. We had multiple quarters of very extensive rainfall, we have also had a pretty challenging macroeconomic situation and almost every other player in the industry is also experiencing similar kinds of performance pressure. Having said that, the near-term focus will be to get our Insecticides business on track. The team is comfortable that they can get that back on track along with also ensuring focus on Hair Colors as well as Air Fresheners and Baby Tissues. So the team feels confident, they have all the levers in place to be able to get the business on track. But we do expect Q2, while it may be better than Q1, to still have some challenges. As we look forward, I am hoping that you will start seeing better performance from Q3 onwards. So incrementally Q2 hopefully should be better, but it will take at least till Q3 before you can start seeing meaningful improvement in the Indonesia business performance. Given the fact that we have a new leader in place, you also want to give the team an opportunity to try and put the corrective measures in place to ensure the long-term sustainability and success of this business.

Abneesh Roy:

Any impact on new launch in terms of ad budget or aggression?

Vivek Gambhir:

We have not had the challenge of making those trade-offs, but we will revisit that on a quarterly basis. But so far we are putting in adequate investment behind new launches as well.

Abneesh Roy:

What is the specific reason for higher promotions by the competition, any particular player, was it because you have gained market share, so now there is retaliation?

Vivek Gambhir:

I do not want to speculate on the intention or objectives of our competition.

Abneesh Roy:

Is it one player, if you could comment on that?

Vivek Gambhir:

No, there are two players who are high on competitive intensity.

Abneesh Roy:

In Household Insecticides in India, last three quarters because of external factors, growth has been optically low. Personal Repellants clearly is a disruption there. So we are not able to understand how big is it in terms of disruption, in terms of numbers obviously it is getting hidden because of the overall growth being low. So if you could comment on that part?

Vivek Gambhir:

There are two ways to look at it - one this is the category that is seasonal in nature; and second is to see how are we doing as far as brand equity and shares are concerned. The good news is that we have been maintaining and increasing our shares across all formats, and so to that degree, our business is on a good wicket. Personal Repellents, as we have mentioned has a lot of potential but still very early days. It is a new format that will take some time, but we remain very excited about the potential of Personal Repellents as well. But this is one category where once the season starts cooperating, we have seen in the past also that business will improve significantly.

Moderator:

We take the next question from the line of Amit Sinha from Macquarie. Please go ahead.

Amit Sinha:

On Household Insecticides in India, despite a favorable base, this quarter performance was average. What kind of growth potential does the category have over the medium term?

Vivek Gambhir:

If we look at both penetration rates and consumption rates, there is significant headroom for growth both in the core Insecticides category and there is also significant growth potential in adjacent categories like Personal Repellents and other pests. But clearly this category does get impacted a little bit by seasonal factors, and again last quarter as we mentioned, it was soft, April and May did very well, but June suffered quite a bit because of destocking, particularly rural and wholesale. But if I look at the performance in July, it is quite encouraging, but very early days. If I look at our innovation agenda, the kind of distribution we have and some of the fundamentals around the headroom for growth, the category does have a lot of potential, but there will be certain period where you might see some seasonal variation.

Amit Sinha:

So can we say that double-digit kind of a growth for the categories is possible going forward over the medium term?

Vivek Gambhir:

This category has grown somewhere between 9% to 11% over the last five years or so. Certainly, there is no reason why that kind of high single-digit to low double-digit growth cannot be sustained. It will vary year-on-year, but from a pure penetration rate, consumption rate perspective and adjacency potential as I mentioned, there is still significant headroom for growth.

Amit Sinha:

We are already at around 50%- 55% market share in the category, do we see further market share gains going forward?

Vivek Gambhir:

Yes, absolutely, part of it is for us to reimagine and redefine what the category size is because if you start looking at the salience of the Personal Repellents in other parts of the world or the opportunity for other pests for instance, these by itself form a sizeable addressable market with tremendous headroom for growth.

Amit Sinha:

On the Soaps segment, the last two quarters have been very strong. Have we seen market share gains from the unorganized and other organized players?

Vivek Gambhir:

Yes, we have seen incremental market share gains. Our guess is that the category has done well not just for us but for some of the other players as well because we are seeing a recovery in terms of consumer demand after a couple of few tough quarters. So Soap does tend to be somewhat cyclical in that sense. While we are benefitting, other players are probably benefiting as well. So we are seeing some marginal share gains, but this is not the category where you see significant gain. So the entire category uplift is also benefitting us.

Amit Sinha:

How big will be the unorganized in this segment?

Sameer Shah:

This is difficult to quantify what comprises of unorganized segment. If you look at most of the branded players, my sense is that would be 97% of the overall category. If you want to term those local small players as unorganized, that would be 3%-4%.

Moderator:

We take the next question from the line of Percy Panthaki from IIFL. Please go ahead.

Percy Panthaki:

On the India business, what is leading to an accelerating trend in price growth? Secondly, if I look at your gross margins, despite palm oil being flat to negative on a sequential basis, your gross margins have been affected negatively. Can you throw some color on that?

Sameer Shah:

There are two-three drivers resulting in 6% price-led growth. One is compared to Q4 higher price-led growth in Soaps category. Second is a little bit of mix effect. So if you look at the category growth in Q1 and if you further get into Other brands, the growth has been 20% and that lot comprises of categories like Air Fresheners and Toiletries, which are relatively higher realization per unit as compared to few of the other categories. So largely it is driven by mix and driven by accelerated price increases in Soap. In terms of correlation between cost and price increases, one of the reasons for drop in gross margins in this quarter has been the excise. The other reason also has been relatively higher levels of sales promotion spends. Again, if you actually go through Slide #9 and if you see the trade promotion spends, they have moved up by close to around 30% on a sales growth which has been close to around 7%. Because of GST, we had relatively elevated levels of sales promotion and trade promotion spends to our channel partners which we feel is more temporary in nature. Difficult to quantify but my sense is anywhere between 80-100 basis points would have been the drop in gross margins behind higher trade promotion spends.

Percy Panthaki:

Excluding excise duty and sales promotion, the price increase is still 5% on y-y basis. In Q4 FY17, the price increase was 3% on y-y basis and that was sufficient and it has actually accelerated from 3% to 5% and you still have this sort of margin impact. Can you throw some color on that?

Sameer Shah:

Palm oil cost also has gone up in terms of the coverages, from the levels which we had in Q4. That is one of the other reasons why despite having relatively high level of price increases, you are seeing gross margins, even after stripping out some of these one-times or exceptionals, is relatively maintained or marginally going down.

Percy Panthaki:

Over the last three-four quarters on an average, what is the Household Insecticides category growth in Indonesia reported by Nielsen?

Vivek Gambhir:

It has been negative. We are seeing a little bit of it entering the positive territory in the last quarter, but for about four or five quarters now, it has been around mid-single digit negative.

Percy Panthaki:

Is competitive intensity in Indonesia sporadic or there is a definite structural change in the competitive intensity there? Secondly, how do you look at margins over the next say four to six quarters in Indonesia on Household Insecticides specifically?

Vivek Gambhir:

We will have to wait and see. I do not have the perfect answer because it is an evolving situation. In the past as we have indicated, there are periods where competitors do tend to employ promotional levers to try and drive up market share and that is what has been happening. Because of the overall macro environment being slower, players are trying harder to try and see if they can use promotional mechanisms to try and drive up share. We will have to ensure that we are responding adequately. Obviously, we will put in greater science in how we deploy our promotional budgets to be able to respond adequately. The second is trying to change the conversation and try and intensify our plans for innovation. The good news is we began sensing some of this a few months ahead. So we already have innovations that are planned and so we will now figure out how best to bring them into the market. At this stage, the business is sitting on record high profit margins. So if we can sustain it that would be a good outcome for the remainder of the year. However, if we have to lose a little bit of margin to drive, to make sure that our shares are sustained, that will be an important priority going forward. The team is coming up with a plan. We do not know exactly how it will evolve. But the first priority will be to ensure that the overall business gets back on track.

Percy Panthaki:

What would be the non- Household Insecticides portfolio growth or decline this quarter?

Sameer Shah:

Non- Household Insecticides will be in positive, would be close to around 2%.

Percy Panthaki:

Given that Household Insecticides is about 40-50% of your business, is it safe to assume that Household Insecticides decline has been 20-25% this quarter?

Sameer Shah:

Yes, around that number.

Percy Panthaki:

On Africa, 16% organic constant currency growth looks good, but it is in the context of high inflation economy. The reported growth is probably lower on organic basis at around 6%. Is it possible for us to actually drive sales harder because 16% in context of the inflation seems a moderately okay number rather than a good number and on that moderate growth, we have actually lost margin. So can we do one of the two, either defend margins or go for a much higher growth?

Vivek Gambhir:

What is encouraging about Africa is that if we look at the volume growth, it has actually been in the high single digit. There is a conscious choice we are making because if we try and push pricing too hard, then the product gets unaffordable for consumers as well given the inflation that we are seeing. So clearly, the call is to build the business for the medium term and the long term rather than try and optimize too much for just a near term. Our belief is that the opportunity is so huge that let us try and build this for the longer-term but let us not price ourselves out of the market just for short term gains.

Sameer Shah:

16% also includes two months of SON. So when you are reading 16%, that is not just Africa, but that is also two months of SON business, part of which is in US.

Moderator:

Thank you. We take the next question from the line of Kunal Jagda from KR Choksey. Please go ahead.

Kunal Jagda:

In the last two quarters, you have been spending quite a good amount on marketing and promotions especially for new launches and on the other hand there is a GST disruption which we expect to last for at least next two quarters. So how do you foresee the revenue growth and margin stability from here with the situation?

Sameer Shah:

One of the reasons why our primary growth has been 6% or secondary growth has been 9% is because of continuous investments not just last one to two quarters, but over last three- four quarters. If we disaggregate our overall investments, we continue to back our new product launches which continue to be key contributor to the overall sales growth. So we expect the sales growth momentum to continue, in fact, to accelerate from here on, and we would also want to back our new product launches as well as back our core with threshold or at times even above threshold marketing investments.

Vivek Gambhir:

We had very interesting launches over the last few months - one that you are seeing right now is the Godrej Professional range but we had HIT Gel Stick, BBLUNT Hair Color, Cinthol Deostick and Good knight Personal Repellents. So these are critical launches for the longer term as well in terms of the kind of portfolio and the opportunity provided for us. So the belief for us again has been that while we have seen near-term disruption, whether it is demonetization or GST, these augur well for the medium term prospect of the Indian economy. This is as much of a belief that things will start improving and to make sure we capitalize on the benefits we are taking some calls to invest ahead of the market. Having said that, as we said, the intent on an annual basis for us is going to be to try and grow EBITDA ahead of sales growth but there will be certain quarters depending on the timing of launches, where the team will take some conscious calls to be able to invest ahead of the market. So our advice would be so not read too much as far as the quarterly trajectory of some of these spends is concerned, but look at it on an annual basis to ensure that our profit growth remain in line with sales growth.

Kunal Jagada:

How much was the price increase in Soap segment? Do you have any plans to introduce new promotions in this segment?

Sameer Shah:

We did have a meaningful price increase in Soap segment but some of it has also got passed back to consumers behind GST because in GST, there is a benefit in soap as a category and good part of benefit has been actually passed on to end consumers.

Kunal Jagada:

Was there a net increase or decrease in price after the GST benefits were passed on?

Sameer Shah:

There is still net increase on y-y basis because that is not just a factor of GST but also in which direction your input cost has been. I think there will be still some marginal price-led growth in Soap even after GST price.

Kunal Jagada:

On new promotions, any plans as you have withdrawn in this quarter?

Sameer Shah:

Promotions were more at a fag end of quarter behind GST to hand hold our channel partners. Those were temporary nature. So it should come back to normative levels gradually during the course of the quarter.

Kunal Jagada:

When do you expect Indonesia business to see positive growth?

Sameer Shah:

What we are doing right now is we are trying out a few initiatives, we are also tactically participating in this high competitive intensity but alongside that we would also want our medium, long-term growth drivers like new product launches to fire. That is what we are working on. It is difficult to give a number or a time as to when it will be positive or when it will be double-digits or teens or other way round. But definitely, as we heard earlier we expect Q2 to be little soft but starting Q3 we remain quite optimistic at this stage that we should see recovery.

Moderator:

The next question is from the line of Rahul Maheshwari from IDBI Asset Management. Please go ahead.

Rahul Maheshwari:

On the Wet Hair manufacturing into East Africa, can you give what kind of cost savings can be taken because earlier we might have been importing the Wet Hair Care products. How much manufacturing in Dry Hair care, which is the major chunk into the Africa business, taking place and what is the cost savings which we would be getting from two to three years point of view?

Vivek Gambhir:

For competitive reasons, we cannot discuss much information. Suffice it to say the benefits are going to be sizeable. But they will take time to materialize because we are just starting manufacturing and the potential for this market is huge but at this stage we would not be comfortable giving any specific guidance on that.

Rahul Maheshwari:

In Africa, how much is the Wet Hair care and Dry Hair care as a proportion of your revenues?

Sameer Shah:

The quantum of production of Wet Hair care products getting produced within Africa market is very-very low but we are scaling up. So in Q1 we had production in Kenya and in Q2 we will have production in Nigeria. By end of the year, we will scale up South Africa. So this is gradually going to scale up.

Rahul Maheshwari:

In Dry Hair care, is it is completely manufactured or still some portion of it is being imported?

Sameer Shah:

We have end-to-end manufacturing units across pockets in sub-Saharan Africa on Dry Hair. What we import is fiber.

Rahul Maheshwari:

In terms of Household Insecticides, you wanted the conversion between the coil users into LV products. So any rough estimate in terms of margins or cost in terms of the revenue?

Sameer Shah:

Directionally, that is the growth driver which we are working on in terms of upgrading and premiumising all our users to electric. But we would want to shy away from sharing any details on that front.

Moderator:

The next question is from the line of Amit Sachdeva from HSBC. Please go ahead.

Amit Sachdeva:

Do you see a period of sustainably high competitive intensity in Indonesia? Second, a related question to that is if I gather your weighted distribution in Indonesia that has been perhaps one-third of the market leader and then you wanted to grow distribution as well. How can that compensate if at all that happens to find some growth yet being competitive and responding to competition?

Vivek Gambhir:

The way we look at it is one is that this is a seasonal category and had four to five quarters of extremely high intense rainfall. We are at least seeing the season improve, early days but for business some comfort is that the season is improving. With that, while we have to respond adequately on the promotion side, we have to do it smartly. So, a lot of our team focuses on actually figuring out smarter way to play the promotion game. The good news is that we have plenty of experiences in other parts of the world as well which we can bring to Indonesia in terms of smart management of promotions. Again, while we continue to focus on promotions, at the same time we have some interesting innovation lined up. That would change the conversation as far as competition is concerned. Third, as you mentioned, incrementally, there are opportunities to execute better on the distribution side of things, which is why I said if I look at Q2, lot of course correction plans are being put into place but it will take a few months for it to show results. But at this stage, we still seem quite hopeful that in the second half of the year we should see better performance from Indonesia and then the second thing would be obviously to push hard on the other categories as well. So while we will see incremental improvement from Household Insecticides, the hope is that the other categories also start playing greater role to be able to turn the performance around.

Nisaba Godrej:

Also, unlike in our India business, in Indonesia we do not play in Personal Repellants or Coils segment which are quite substantial. Personal Repellants is much bigger than it is in India. We have some very interesting disruptive launches in the pipeline. So for the long-term we are quite confident about our Household Insecticides business and this is not the first time we are seeing competition like this happen. So we would agree that our performance has not been good but we are confident of correcting it and having overall growth in the category.

Amit Sachdeva:

Can you talk about a little bit more rural context in general? There are some signs that rural may pick up, monsoon has been normal, so there is some income effect still playing in rural while GST has been disruptive, but what are you experiencing in the rural market as you approach your channel partners and other stakeholders barring GST, which has been negative from the wholesale point of view?

Sameer Shah:

We feel that rural should return back to normative level, hopefully over a month or so. If we disaggregate our Q1 growth, rural growth was mirroring urban growth, in fact a shade higher for us as compared to urban growth, there are different geographic pockets like for instance in East, we feel that rural recovery could be a longer than pan-India. But that is how GST has impacted. Directionally, again, for the three categories internally, we do believe that the consumer demand generally should remain quite stable to kind of uptrending behind monsoon, even internally a few other initiatives which we are driving.

Moderator:

The next question is from the line of Prasad Deshmukh from Bank of America Merrill Lynch. Please go ahead.

Prasad Deshmukh:

Rural growth was a shade higher than urban and wholesale is still under pressure, so who is filling this gap?

Sameer Shah:

We had strong growth in modern trade and in wholesale channel. We had also incentivized our distributors to have extremely high strong performance in the direct reach which they have. These where the channels which offsetted the gap as a whole which we had otherwise in some of the other channels.

Prasad Deshmukh:

Is it like there is a sharp increase in direct reach in rural?

Sameer Shah:

It is not about just a direct reach, it is about the productivity which we are getting from the outlets where we reach out directly. It is not that we have added like 10% number of outlets we reach, but productivity in those outlets where we reach directly has gone up in last quarter at least.

Prasad Deshmukh:

Leaving aside month of June, what would be the growth in Household Insecticides in April-May?

Vivek Gambhir:

Would be double-digit growth.

Prasad Deshmukh:

In case of Indonesia, if you remove the holidays that you spoke about, what would be the numbers there?

Sameer Shah:

It is difficult to strip it out that way. Mathematically, we lost close to 10% of the number of days but will we get the benefit up to 10% is to anyone's guess to be honest with you. But that is the reason, in fact, even if you look at some of the global CPG companies results and we have been hearing this, that has been one of the many reasons but difficult to quantify.

Prasad Deshmukh:

Indonesia problem seems to be persisting for too long at least in the past five-six quarters, and another one or two quarters will go in weakness in terms of revenue as well as margin, is there any offsetting factors that one can expect say like increased focus on say other SAARC countries or trying to scale up presence there so that some offset can come?

Vivek Gambhir:

It is too big to have any counterbalancing factors. The teams will clearly focus on over-delivering in India and Africa which will make a much bigger difference at the end of the day to be able to compensate for the Indonesia challenges. The teams are feeling quite confident that Latin America, Africa and India are on a much stronger wicket and even the UK seems to be doing quite well. So overall rest of the portfolio will have to contribute more to be able to make up for the Indonesia challenges. SAARC and other ASEAN countries are too small to actually make up for it.

Prasad Deshmukh:

What is the update on your cost control initiatives then given all this is happening?

Sameer Shah:

Last year we did our cost savings project in Indonesia. This year we are very much on track, in fact, if any that will get accelerated but looks like we may not get the scale leverage. Else we were looking at close to 2% of the savings behind the cost saving program, but at least at this stage we may miss the absolute savings target.

Moderator:

The next question is from the line of Vivek Maheshwari from CLSA. Please go ahead.

Vivek Maheshwari:

On the margins front, do you think that for various reasons be it issues in India or Indonesia, this could be one year where actually there can be a margin reset? Do you think this can be the year of a margin headwind on an entire year basis?

Sameer Shah:

We will have to look at it cluster-by-cluster. So India to begin with, what we can share at this stage is we are quite confident and optimistic that we will see margin expansion on a full year basis. Africa (incl. SON) conservatively we can share that we should see margin maintenance on a full year basis. LATAM, we will be more or less maintaining the historic high margins which we saw last year. Indonesia is the only business, which will be more of wait-and-watch mode in terms of what happens practically as well as what happens in terms of medium-term investments and hence there is less visibility in terms of in which direction the margins will shape up. Ex-Indonesia we remain very optimistic in terms of margin maintenance to margin increase on a full year basis.

Vivek Maheshwari:

Given the high base in India, how comfortable you would be to take up product prices if at all through the course of the year?

Sameer Shah:

We remain quite confident, even in India in terms of margin expansion on a full year basis.

Vivek Maheshwari:

On Indonesia, have there been any explicit price cuts by competition or it is just limited to promotions at this moment?

Vivek Gambhir:

It is largely just promotions.

Vivek Maheshwari:

What was the rationale of having higher advertising in this quarter for India?

Vivek Gambhir:

The bulk of the higher advertising is much more for our new launches. So if we disaggregate the composition of the advertising as far as the core is concerned, there is more maintenance in that. So the bulk of the increase for advertising is actually based upon some of the new launches like Good knight Personal Repellants, HIT Gel Stick, etc.

Vivek Maheshwari:

You mentioned about excise duty impact in this quarter of about 100 basis points. Will there be a corresponding impact on the tax rate and if so what will be India tax rate for FY18?

Sameer Shah:

As our Jammu unit was scaling up during the course of the quarter, in the interim, we had to go to some third-party manufacturer especially for Soaps such that we do not miss any kind of volume for the quarter and hence the element of excise was relatively higher in terms of what we had to share with third-party manufacturer compared to what would have been if we would have manufactured it in-house. Hence to that extent, it is one off in its own way, of course, now we have GST. So all of this does not kind of get into Q2. In terms of MAT rate, we continue to remain in MAT for foreseeable future. So the rate will remain at 21% for foreseeable future for us.

Vivek Maheshwari:

From a GST perspective, this may not be accounted for but does that mean this 100 basis points hit gets reversed in the next quarter then as and when you have your own plan?

Sameer Shah:

Some part of it definitely will and if there was no GST for sake of simplicity, then in Q3 it would have been back to the normative level. In Q2 still there would have been some impact of less than 100 basis points.

Vivek Maheshwari:

GST would continue those benefits in any which ways, which means that it may not be visible to us from an accounting perspective, but nonetheless it will be there. Is this correct?

Vivek Gambhir:

Absolutely.

Moderator:

The next question is from the line of Sanjay Singh from Axis Capital. Please go ahead.

Sanjay Singh:

How are things after GST in India specifically in terms of demand in the various channels?

Sameer Shah:

The overall environment is improving with every passing day. We are seeing most of the retailers getting back to business, especially those who are below the threshold turnover limit. Rural except East is also returning to normative levels. Wholesale is the channel which still continues to be subdued. We expect the same to be completely back on track somewhere by end of August. We feel as of today say around two-third of wholesalers are doing business as usual. But we expect the entire wholesale channel for our category to be kind of back to normative levels by end of August. CSD is another channel that did not have any purchases in June as well as in July. We expect hopefully that should also be back to purchases in August. Modern Trade continues to be at kind of very high growth rate including the cash-and-carry channel.

Sanjay Singh:

On Indonesia, have we seen the worst of margins or is it possible that it could get worse in terms of margin before it gets better?

Sameer Shah:

Yes, again, it is difficult to call out, because we just do not know how this competitive intensity will get played out. We have our own understanding of the past as Nisaba was sharing earlier in same category, same market as well as in a few other markets. These are also the players with whom we compete not just in one market but across many markets. So to that extent, we can be ready for different scenarios, but it will be very difficult at this stage to have a strong point of view in terms of whether this is the worst of margins or margin recovery or they go down from here on. Maybe a quarter or so more and then we can be in a much better position to even have a point of view in terms of how the margins will shape up for Indonesia during the course of the year.

Moderator:

The next question is from the line of Abhijeet Kundu from Antique Stock Broking. Please go ahead.

Abhijeet Kundu:

What is the scenario in Soaps in terms of demand, volume growth and what can we expect in terms of pricing there?

Sameer Shah:

In terms of Soaps, most of the players including us have passed on the GST benefits to end consumers. So we will see starting Q2FY18, price reduction for most of our brands and most of the SKUs within those brands. This price drop should help in terms of fast tracking volume growth which has been as you rightly said flattish as well as very subdued generally for most of the players in the category.

Abhijeet Kundu:

In the months of April and May, was there any recovery in volume growth at that point in time which then moderated in June for Soaps, was that the case?

Sameer Shah:

Not for us. We continue to see higher price-led growth in April and May and the same quantum of price-led growth did come down in June just because of this destocking issue. But there was not much change in overall volume growth in April, May versus June.

Abhijeet Kundu:

On Indonesia, on a product basis, what would be the strategy? One is on the increasing promotional spends, but on a product basis has there been any change in the scenario, which you can really put focus on and revive the growth?

Sameer Shah:

Yes, largely it has been in aerosol in Indonesia within the HIT brand. That is where we are seeing very high competitive intensity and we have few new product launches more as medium-term kind of strategy. Yes, it will be a mixed bag of both, gradually coming out of this high competitive intensity and also ensuring that our new product launch generates sufficient traction to see a smart recovery in Household Insecticide category in Indonesia.

Abhijeet Kundu:

New product launches you can benefit from that next year. In FY18, it will be more of how you tackle the promotion?

Sameer Shah:

Correct, in new product launches also during the quarter this year. So I do not think it is only going to be next year kind of phenomena.

Moderator:

Thank you. That was the last question. Ladies and gentlemen on behalf of Citigroup Global Markets India Private Limited that concludes this conference. Thank you for joining us. You may now disconnect your lines.