

Investor and Analyst Q2 FY15 Conference Call

November 1, 2014



Moderator:

Ladies and Gentlemen, Good Day, and Welcome to the Q2FY15 Results Conference Call of Godrej Consumer Products Limited hosted by Emkay Global Financial Services. We have with us today, Mr. Adi Godrej – Chairman; Mr. Vivek Gambhir – Managing Director; Mrs. Nisaba Godrej – Executive Director; Mr. Omar Momin – Executive Vice President, Strategy and Business development; Mr. P Ganesh – Executive Vice President, Finance, Commercial and Company Secretary, and Mr. Sameer Shah – Vice President, Planning and Investor Relations of Godrej Consumer Products Limited. As a reminder, all participants' lines will be in the listen-only mode. There will be an opportunity for you to ask questions at the end of today's presentation. Should you need assistance during this conference call please signal an operator by pressing '*' then '0' on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Prashant Kutty – Research Analyst of Emkay Global. Thank you. And over to Mr. Kutty.

Prashant Kutty :

Good Afternoon, everybody. Thank you for joining us today. We would like to welcome the management of Godrej Consumer Products Limited and thank them for giving us the opportunity to host this call. I would now like to hand over the call to Mr. Godrej for his opening remarks. Over to you Sir.

Adi Godrej:

Thank you Prashant and good afternoon. I welcome you to the Godrej Consumer Products Limited conference call to discuss the performance for the second quarter of fiscal year 2014-15.

Consumer demand has remained subdued in the second quarter of fiscal year 2014-2015, making this one of the slowest years of growth for the Indian FMCG industry in over a decade. On a sequential basis, however, we are beginning to see some improvements in the environment. For the home and personal care sector as a whole, growth in the first quarter of fiscal year 2014-2015 was around 3%. In the second quarter of this year, the growth rate has inched up to around 4.5%. Even in the second quarter, growth in the month of September was significantly better than growth in July and August. While this growth is nowhere close to the sizeable potential of the Indian market, it is encouraging that perhaps the worst is over and that the second half of the year offers better growth prospects than the first half.



In this challenging environment, GCPL has continued to outperform the market. We have continued to grow ahead of category growth and our brands have further strengthened their leadership positions.

Our consolidated sales increased by 9% in constant currency terms, led by strong growth in Indonesia, Africa and Latin America. At 12% constant currency sales growth, our international business performance was encouraging, despite the continuing macro-economic challenges in our international geographies.

Our consolidated constant currency EBITDA growth of 18% was much ahead of sales growth. Our India business EBITDA growth of 12% was again, much ahead of sales growth, led by better cost management and leveraging investments in brand platforms. In our international business too, the constant currency EBITDA growth of 27% was much ahead of sales growth. Our international business EBITDA growth was driven by strong margin improvement in Indonesia and Latin America, which offset weaker margins in Africa and Europe.

I will now recap our six key business imperatives and assess how we have performed on these priorities during the quarter. After this, I will discuss the highlights of our financial performance during the quarter. We will then be happy to answer your questions.

One of our most important imperatives is to sustain leading positions in the three core categories that we participate in, in India - home care, personal wash and hair care. Our focus is on growing ahead of the market, driving consumption and penetration, and strengthening our portfolio. If we look at our India business, we have significantly outperformed reported category growth rates, across categories. Our sales growth too has been more than one and a half times the overall household and personal care category growth. Three of our brands ranked among the 'Economic Times Brand Equity Most Trusted Brands 2014'. Good knight was ranked number 1 in the household care category, while Cinthol and Godrej No. 1 were ranked number 11 and number 15 respectively in the personal care category.

Our household insecticides business had a challenging quarter, growing by 2% on a high base of 25% during the same period last year. This growth was ahead of the category growth, which was impacted by the deficient and delayed monsoon. Excluding Central-Northern India, which had a rainfall deficit of 24%, our household insecticides growth for the rest of the country was 7%. We believe that this slowdown in growth is temporary and a result of the monsoon vagaries this year. We are confident that growth will be better in subsequent quarters.

We continue to gain market share across all formats of electrics, coils and aerosols. In fact, our share in the category is at an all-time high. I am also pleased to share with you that



Good knight Fast Card has become a rupee 100 crore brand in 11 months – in FMCG, this would be among the fastest run ups to get to rupees 100 crore for a new brand. Similarly, our other recent innovations like Good knight Xpress liquid vaporiser and Hit anti-roach gel, continue to perform well. We believe that our continued focus on product innovation and continuous brand investments will help drive further growth and strengthen our brands.

The soaps category continued to be sluggish, reporting another quarter of de-growth. In comparison, our business saw a strong turnaround with a value growth of 13%. Godrej No.1 growth rates clocked an uptick, aided by new media and consumer promotions and focused activation programmes. The launch of Cinthol's new germ protection variant "Confidence+" has also received an encouraging response. With the recent duty reduction on palm oil, we expect the profitability of our soaps business to improve in the second half of this fiscal year.

We continue to be market leaders in the hair colourant category and have strengthened our market share, despite growing competition. We grew by 9% during the quarter, despite a high base of 24% in the same period last year. This growth is far ahead of the category growth. We continue to drive initiatives to increase penetration as well as consumption in the category.

Godrej Expert Rich Crème Hair Colour has become the highest selling crème colour by units within 20 months of its launch. As a recognition of its differentiated proposition, Godrej Expert Rich Crème Hair Colour has been featured in the 'Nielsen Breakthrough Innovation Report 2014'. Nielsen's Breakthrough Innovation report showcases the best in FMCG's new product launches after evaluating over 17,000 launches since 2012.

More recently, we have introduced the BBLUNT range of hair care and styling products. In collaboration with Adhuna Bhabani-Akhtar and her team, we have created the B SYSTEM, which houses world-class products, tools and expertise customised for Indian hair. This introduces, for the first time in India, salon expertise in a simple 3-step approach (Prep, Style and Transform) that you can follow at home.

We continue to make good progress on Godrej aer, our air freshener brand. Our innovation to move to a gel format technology has further enhanced user experience and we have received very good feedback from our consumers on it. The recent 'Economic Times Brand Equity Most Trusted Brand Survey 2014' ranked Godrej aer as number 11 in the household care segment. This is a great achievement for a brand that was launched just a little over two years ago.

Our portfolio of Godrej Protekt hand washes, sanitisers, and anti-mosquito spray – a foray into the health and wellness space - continues to receive a good response in modern



trade. We believe that the hand wash and sanitiser categories have a lot more room to grow, given changing consumer needs and increased awareness of hygiene levels.

The second pillar of our strategy is to drive growth in our international business, guided by our 3 by 3 strategy, of focusing on three core categories of home care, personal wash and hair care in emerging geographies in Asia, Africa and Latin America.

Our biggest international business, Megasari in Indonesia, grew by 15% in constant currency terms. Our growth was much stronger at 21%, if we remove the impact of our foods distribution business. Megasari continues to strengthen its position as the market leader for urban household insecticides and air care in the Indonesian market. We exited September with a historically high market share in the air freshener category. The EBITDA margin of 18%, which is before the payment of a technical and business support fee, was higher by 220 basis points on a year-over-year basis, owing to price hikes, a better product mix and cost efficiencies.

Our African operations, which comprise Rapidol, Kinky, Tura and Darling, delivered another strong quarter with 15% constant currency sales growth. This was mainly led by our Darling business, which grew by 19% in constant currency terms. The organic EBITDA margin of 11% declined by 330 basis points due to upfront marketing and sales infrastructure investments across businesses and the continued sluggishness in the South African market. We are on track with our plan for the consolidation of the new Darling business geographies. During the quarter, we licensed our rights of Darling trademarks for use in Uganda, Tanzania and Angola and acquired 100% stake in Ghana, effective October 2014.

Our Latin American operations, which comprise Argentina and Chile, continued to show improvements during the quarter. Revenues grew by 31% in constant currency terms. The EBITDA margin of 13% saw a sharp improvement of 560 basis points on a year-over-year basis, backed by better business performance and the implementation of Project Iceberg in Argentina. We also continue to further strengthen our market positions in Argentina and Chile.

Our European business had a subdued quarter, with a constant currency de-growth of 9% on a high base from last year. Growth was also impacted by issues related to counterfeits for one of the lead brands that we distribute in the market. EBITDA margins for the business were around 9%, down 80 basis points on a year-over-year basis, due to weaker sales performance.

Our third strategic pillar is to accelerate the pace of innovation and strengthen our brand portfolio. The last few quarters have seen many innovations and new launches across categories and across geographies. We launched new formats in aer air fresheners, new



shades and packs in Godrej Expert Rich Crème Hair Colour, Good knight Fast Card and Good knight Xpress, new Godrej No. 1 and Cinthol soap variants, a new range of Protekt handwashes, sanitisers, and anti-mosquito spray and made a foray into premium hair care with BBLUNT in India. We are also entering the skin-cleansing category with the launch of a Godrej No. 1 face wash, which we believe will be distinctive and will democratize the category. In our international business too, we have introduced several new products for Stella air fresheners, Mitu baby care and Hit household insecticides in Indonesia, Issue hair colour in Argentina and refreshed the Soft & Gentle range in the UK.

We will continue to focus on new launches to drive superior growth. We have been making upfront marketing investments to ensure that we adequately support our new launches. We believe that we will reap the benefits of this upfront spend as the new launches continue to gain scale.

One of our other key imperatives is to create a future ready sales organisation for the India business. We have launched Project Daksh to improve the productivity of our sales force and enhance go-to-market efficiencies in our urban markets. We have also made efforts to expand our distribution reach in rural and urban areas. Our rural growth continues to be ahead of urban growth.

Our fifth pillar is to build a global best-in-class supply chain. We have taken strong steps in this area by establishing centres of excellence in TPM, lean, six sigma and low cost automation. We have set up a strategic sourcing team to leverage scale and reduce our procurement costs. We also recently launched an initiative to improve our supply chain planning and execution capabilities by using an advanced technology solution.

As I had shared with you earlier, we have launched a new cost transformation programme called 'Project Pi' to help implement a future ready cost structure. We have identified several new opportunities as part of this programme and expect to see some positive impact over the next few quarters.

Finally, we continue to execute different initiatives to foster an agile and high performance culture in our organisation. GCPL was ranked the number 1 FMCG company to work for in India by the Great Place to Work Institute. GCPL has featured on the list of best companies to work for, for 11 years in a row. Our overall rank too improved to number 7 from number 11 last year. Earlier, GCPL was recognised among the 17 Best Employers in India in 2013 by Aon Hewitt. GCPL is one of the only two FMCG companies on the list. Our rankings in these people surveys reinforce our commitment to creating an outstanding workplace that attracts and retains talented employees and delivers superior value to our consumers.



I will now cover the highlights of our financial performance for the quarter.

For the quarter ended September 30, 2014, our consolidated constant currency net sales growth was 9%. We did see some decline in gross margins during this quarter, due to an unfavourable category and geography mix. We expect margins to improve sequentially due to a benign commodity cost environment and as the benefits of our cost savings projects kick in.

Organic EBITDA margins of 16.2% expanded by 90 basis points, on account of better margins in our India, Indonesia and Latin America businesses. Our India business recorded an expansion of 100 basis points, driven by better cost management and leveraging brand platforms.

Earnings per share (non-annualised) stood at INR 6.89 for the quarter. The Board of Directors has declared an interim dividend of 100%, which translates to INR 1 per share.

Our sales in India grew by 7% versus the corresponding quarter last year, which was more than one and a half times the India home and personal care category growth. On a sequential basis, growth for the second quarter was 12% versus the first quarter of this year. While there are seasonal differences to bear in mind when looking at sequential growth, the fact that our sequential growth was strong gives us some comfort that the environment growth indicators are trending in the right direction.

Our EBITDA growth of 12%, which was ahead of sales growth, expanded by 100 basis points year over year.

Our international operations, which accounted for little less than half of our consolidated turnover during the quarter, recorded a constant currency growth of 12%. Organic EBITDA margins of around 12%, expanded by 60 basis points year-over-year.

While a potential recovery will take time, we are confident that the second half of this year will be better than the first half. In this uncertain environment, we continue to focus on sustaining and extending leadership in our core categories. We are managing our costs prudently in the near term, while investing for the longer term. We are also continuing our pace of launching exciting new products.

The medium and long-term growth prospects in India and our other emerging markets remain robust. I am confident that with our clear strategic focus, differentiated product portfolio, superior execution and top-notch team, we will continue to deliver industry-leading results.

I now conclude my opening remarks on the quarter's performance and open the floor for questions.



Continue: - Q&A...

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Questions and Answers:

Moderator:

The first question is from the line of Abneesh Roy from Edelweiss.

Abneesh Roy:

We are targeting Premium Hair Care through BBlunt. What is the potential currently, how do you plan to scale up in terms of both technology and brand equity?

Nisaba Godrej:

BBlunt is a very unique brand, it is a salon brand. It is not easily replicable and is a very well-known brand in India which is well connected to Bollywood and the fashion industry. This is a model that is used in foreign markets, similar to John Frieda, Toni&Guy, Bumble and bumble salon-based brands. In terms of technology, I would encourage you to try the products. In all benchmark studies, we have done better than the multinational products and our products are designed for Indian hair, and there is a significant difference between Indian hair and blonde hair. The kind of consumer feedback we have got from people who have used the product has been excellent.

Abneesh Roy:

In the standalone financials, why is the staff cost up 26% Q-o-Q and 17% Y-o-Y? Gross margins are expected to improve in the India business and for the category in the second half, how do you see both advertising and promotions inch up?

Sameer Shah:

On employee cost, the change is on account of variable remuneration which in turn driven by the delta EVA performance metrics which we have in the business. In terms of benign commodity environment and potential gross margin expansion, I think we will see pressure ease, if you see the environment is changing, which is suggested by last month's performance in general, we will also start overinvesting in the categories to reap better returns.

Abneesh Roy:

This quarter's profit is not that high, does the delta EVA capture the future projections because the salary growth is much higher than the gross profit and EBITDA growth?

Sameer Shah:

Our consolidated constant currency EBITDA growth is around 18% on a constant currency net sales growth of 9%. The expansion has been substantial.



Adi Godrej:

Our profit this quarter has been one of the highest ever, and if you look at sequential growth over April-June, and growth over the same quarter of the previous year, our profit growth has been very substantial.

Abneesh Roy:

Will EVA be based on the specific SBU, for example the India profits will mirror the India EVA and India salaries?

Sameer Shah:

This would be on consolidated because the team in India also gets bonus, the consolidated delta EVA performance, and then there are individual clusters, like India, Indonesia, Africa, etc.

Abneesh Roy:

On the sales front in domestic HI, the base is much more favorable in Q3. In that context there is 7 to 8% growth. Are we going to come back to a healthy number because HI post Q2 has been a bit soft, how will the growth be?

Adi Godrej:

We expect strong growth in the second half, the first half growth was affected by various climatic factors; the monsoon was weak and mosquito infestation was poor, but we expect growth to be much stronger in the second half, not just in our Household Insecticides business but across the board, because the base last year in the second half was low whereas in the first half the base was high.

Vivek Gambhir:

We are quite optimistic and hopeful, as we look at the data from the latter half of Q2 even, while July and August were quite weak, September was much better and that gives us enough comfort that at least things are trending in the right direction, and given all the investments we have made in terms of some of our new launches, even in H1 whether it is Fast Card, Good knight Xpress, we now have the portfolio to be able to accelerate our sales trajectory in the second half of the year.

Abneesh Roy:

What is your hypothesis on the sharp improvement in September? Is it because of very good recovery in rainfall? Secondly, Fast Card is a remarkable brand of Rs.100 crore. Is it leading to cannibalization because the overall numbers are muted in the context of the seasonality?



Vivek Gambhir:

September growth rate was high for a couple of reasons, one is as you mentioned, the monsoons were delayed and the monsoon pickup was quite nice since September, which led to a strong performance in HI for us as opposed to June, July, and August. Second is, because September was the season before festivals, there was certainly a little bit of sales momentum, we saw the result of that. Thirdly, we had put in a lot of marketing activation programs particularly in Godrej No. 1 and Cinthol, we had launched Cinthol Confidence+ a month before that. So a combination of launches and marketing gave us a platform to deliver a good in September. On Fast Card, we need to give it a little bit more time. The hypothesis is that over time it will grow the market, but there will also be some cannibalization which frankly is okay, because particularly compared to Coils, Fast Card is a much higher margin product. In some ways it is value creating cannibalization, but our hope is that over time you will start seeing consumers use multiple products and you may have a situation where a consumer might use Fast Card for say 4 hours in the evening, and then switch to an LV format when they sleep at night, that is the intention.

Adi Godrej:

We expect the success of Fast Card, would help expand the overall HI market, it will also help expand our share of the market, despite some of the Fast Card sales coming from cannibalization, most of it will go towards increasing the size of the market.

Vivek Gambhir:

As we know in this category rural penetration is very low, at about 28%, because it is still a few months into the launch, we really have not been able to push Fast Card as much into rural India as much as we would like to. So the next big wave of growth for Fast Card will come from being able to drive a lot of rural penetration and consumption.

Abneesh Roy:

What was the constraint for the rural manufacturing capability?

Vivek Gambhir:

No, it is just getting the sales system and the go-to-market system up, normally any new launch; it takes a few months before products reach the rural market.

Adi Godrej:

Also, it did extremely well in the first few months and we were a little tight supplied.

Abneesh Roy:



In Hair Color, our performance has been remarkable in the last many quarters. Q3 base is extremely high at around 35% to 37%. Competitors have copied your product like a Xerox machine. How are you seeing growth in Q3 and the second half because of similar products and pricing by four to five players? Will Growth be more difficult; is there a new product which you are working on?

Nisaba Godrej:

Although two products have come out, our positioning, product quality and distribution still differentiates us. There is a lot of growth left in Crème, it has really been more of an urban phenomena now. There is a lot of potential for this particular product. At the same time, we have a number of other products in the pipeline for Hair Color which we believe is as strong as Crème or even stronger.

Moderator:

The next question is from Prakash Kapadia from iAlpha Enterprises.

Prakash Kapadia:

What according to you is affecting FMCG demand in India? Is it down trading, lower pack sizes or is it deferment of purchases by consumers?

Adi Godrej:

Generally, the FMCG market in India slowed down in the last 18 months because of the lower GDP growth and the pressure on the wallets of consumers from other items such as education, energy, etc. Now that the GDP growth is picking up and that the consumer sentiment in India has picked up very strongly, we see growth picking up in the FMCG sector. Also, the base effect will make a big difference between second half growth in the FMCG sector relative to the first half. Last year, the first half was strong and the second half was relatively weak. With the second half coming into play, the base effect will lead to better growth in the second half of this year compared to the growth in the first half.

Prakash Kapadia:

On Soaps, is it the low base of last year which has helped us grow 13% or is it the new launches? How confident are we on sustaining this growth in the Soaps business?

Vivek Gambhir:

Generally Soaps does tend to be a bit of a bellwether category, and the fact that soap, the deceleration in volume consumption has come down, we have also been able to see more price-led growth, so which is why we are not completely out of the woods as far as the category is concerned. But, clearly the deceleration in growth has stopped and we are



now beginning to see a certain amount of volume growth in the category and more price-led growth, which puts us in a very interesting position where at least you are now seeing the trends in the right direction. We have launched a lot of good marketing programs, we have launched a new variant under Cinthol, which is our first foray into germ protection, Cinthol Confidence+; Germ Protection is about 25% of the market, we have some more additional plans to launch new variants under No. 1 shortly as well, and we have just also entered the Face Wash category. A combination of innovations, some of our marketing activation programs are working better and consumers are now showing increasing intent to buy Soaps. Our belief is that we are set up quite well to continue the momentum we have shown over the last quarter as far as Soaps is concerned.

Prakash Kapadia:

How large is the Face Wash category because some of the players are already present, is it low penetration?

Vivek Gambhir:

Very low penetration, it is about Rs. 1,500 crore category, growing at 30% Y-o-Y, largely an urban phenomena and even within urban India, it is only 18% penetration. We believe that the opportunity is right for us to be able to enter the category with very distinctive proposition and democratize the Face Wash category like what we did with No. 1 Soap a few years ago.

Prakash Kapadia:

Is it fair to assume given that the second half will be better and gross margins were lower in the first half because of product mix assuming recovery and the second half pans the way as we are expecting, given the sentiment and the change in the consumer buying patterns. Can we expect gross margin improvement as compared to FY14?

Vivek Gambhir:

What we are trying to work towards is to deliver a better gross margin overall this year than the previous year, but obviously competitive intensity in those kinds of things we will have to watch out for, but the intent is to deliver better gross margins this year.

Sameer Shah:

There are also a couple of other drivers – one is we expect a favorable mix in H2, in H1 we did not have best of the category mix, especially from gross margins point of view; and second, we are also in a benign commodity environment, be it on palm oil or be it on crude, both of which should push up the gross margins.

Moderator:



The next question is from Percy Panthaki from IIFL.

Percy Panthaki:

On a consolidated basis, why was the staff cost and other expenses are down on a Y-o-Y basis? And if is any one off exceptional, could you tell me the adjusted Y-o-Y growth?

Sameer Shah:

On the staff cost, you would have just heard the reason for increase in standalone staff cost which is behind the performance linked variable remuneration. When we look at international staff cost, it has come down as we are working on several labor productivity initiatives especially in the Darling business, and we are also moving our high cost production from one Darling geography to another Darling geography which has relatively lower cost production. Project Iceberg in Argentina is also resulting in lower employee cost. Another impact which we need to factor in when we look at the rupee employee cost at consolidated level or at international level is the currency depreciation impact. In our international business, we have had a 10% currency depreciation impact, which also sits in the rupee reported staff cost.

On other expenditure, let us start with standalone first, it is more to do with category mix; we had 2% growth in HI, and a couple of big line items which sits in other expenditure in standalone is contract manufacturing charges for HI, as well as sales promotion, and HI being the category which has relatively higher sales promotion as a percentage of sales compared to other two categories. It is driven by category mix in standalone business, and in consolidated, a good part from standalone is actually flowing in.

Percy Panthaki:

On staff cost, I understand that there is very high increase on the standalone business. While there will be some savings in international because of new sites, labor productivity, etc., are the savings actually so high that they would drive the entire consolidated labor down?

Sameer Shah:

It is a combination of two things; a lot of these initiatives which are actually reducing down our local currency staff cost, and the second is the translation impacts, when you are looking on Y-o-Y basis, 10% of it in rupee terms is just getting completely knocked out because of adverse translation impact, this is also something which you need to keep at the back of your mind.

Percy Panthaki:



On Hair Color, while there is a base effect, do you think that the growth is a little slower on account of the industry growth in Hair Color coming down versus a year or two back, what was the industry growth and what is it today if you can provide me that data?

Adi Godrej:

Certainly, all categories the growth is coming down.

Sameer Shah:

If you look at this quarter and again just one quarter may not be a good period to analyze this, but during this quarter our Hair Color growth has been three times of the category growth. While we have seen a temporarily dip in overall Hair Colors category, but 9% reported growth is nearly 3x of the category which earlier used to be anywhere around 1.5x of the category growth. So our relative market position has strengthened compared to what it used to be a couple of years ago.

Percy Panthaki:

I understand you have been growing ahead of category. Can you give the data for first half. How much is the industry growth for first half of this year versus a year back or two years back?

Vivek Gambhir:

What was typically a growth in the low double-digits for the industry has come down to low single-digit for the industry.

Percy Panthaki:

There has been about 10% decline in the industry growth and that is also probably one of the reasons why your growth has suffered?

Vivek Gambhir:

I would not say 10%, probably be 700 to 800 basis points have come down.

Percy Panthaki:

On Household Insecticides, I wanted to understand your product pipeline. You have done exceedingly well, you have been the innovator in Low Smoke Coils, Good Night Advances, Fast Card, etc., do you think most of your innovations for the next 12 months are through and you would concentrate on the products you have launched or do you think there are more products coming in, in the next 12 months?

Vivek Gambhir:



We have just recently launched Good knight Xpress, which is the fastest LV in the world and Good knight Fast Card. The focus is going to be really to consolidate this current portfolio, but there is certainly some plans to have a couple of more incremental innovations, I do not think we will have anything major over the next 12 months, but I think there will be a couple of things that we are looking at in this category and then depending on again the market environment we will take the call in terms of when to launch those. But, from a product readiness point of view, there are at least two different interesting innovations that we have in the pipeline.

Percy Panthaki:

On Africa margins, these margins in the last several quarters have been pretty volatile. I understand the volatility will happen quarter-to-quarter, but that makes it difficult for me to understand what is the stable full year margin we can expect. Earlier you had guided 16% to 18% margins in this product, so taking a midpoint around 17%. Do you still feel confident that for the full year FY15, 17% margin is something that you will be able to achieve?

Sameer Shah:

You know the answer in terms of outlook for H2 and hence full year margins, but at this stage there is nothing which worries us in terms of achieving a respectable margin for Africa business, something which we have been doing on a full year basis over the last two years. Just for instance, if you look at our last year's margins, they were around 17% with a lot of quarterly choppiness, and you would appreciate that is bound to happen when you have a mix of three to four businesses across four to five geographies.

Percy Panthaki:

Do not think there is anything on the horizon that you can see in terms of margin being a problem for Africa?

Sameer Shah:

Just sluggishness in South African market, that is the only kind of headwind, but otherwise, as of now nothing much.

Moderator:

Next question is from the line of Varun Lohchab from CIMB.

Varun Lohchab:

In Indonesia, your growth has been picking up nicely, could you throw some light on what is the underlying trend in the market, how is the category growth rate shaping up



and how much market share gain would you have done in HI and Air Fresheners out there in the last couple of years. How much you are outperforming the category growth rates?

Vivek Gambhir:

Looking at Indonesia data, clearly at an overall environment there have been a few challenges as far as FMCG growth rate is concerned, and last quarter the growth rate in Indonesia for FMCG as a whole was about 10%, but that number used to be in the mid-to-high teens a couple of quarters ago. There have been some macro challenges in Indonesia. Let us see how the environment shapes up post elections. Our business has continued to do very well and we have gained 100 basis points of share in our two core categories – Air Fresheners and Insecticides.

Sameer Shah:

If you just look at our performance, 21% which is after stripping out the Foods distribution impact, it is nearly 2x of the overall FMCG growth. And a couple of quarters ago, we have been in that range of 1.5x to close to 2x of the overall FMCG growth in Indonesia.

Varun Lohchab:

Broadly outperformance is still pretty much on track?

Sameer Shah:

Yes.

Varun Lohchab:

On margins in Indonesia, they have been slowly inching up. Would they stabilize or is there still some scope for further improving back to 20%?

Vivek Gambhir:

There is definitely scope for improvement, this is one area we do not have a good sense of, because some of it depends on currency depreciation and that is a difficult one to really know what happens to Indonesia. There are some macroeconomic challenges which we will have to remain quite watchful for, that could certainly impact the margins in that category. If those macroeconomic challenges work in our favor, certainly, there is room for margin to improve. But, very difficult to make the call, because we have just had



a new government that has come into place, there is talk of removing fuel subsidies, etc. we just have to watch out over the next two quarters.

Varun Lohchab:

On LatAm, we have seen pretty good pick up this quarter. LatAm performance again has been quite volatile over the quarters in terms of both top line and more so in terms of margins. How should it look over the next 12 months given how the macroeconomic situation is and the competitive intensity is and what is the more sustainable?

Sameer Shah:

In terms of revenue growth, there is a lot of consistency; we have seen on an average mid-20s to late-20s kind of revenue growth in constant currency terms. In terms of margins, as we shared earlier that we have a 'Project Iceberg' running in Argentina, result of which we expect our margins to move up and that is the way we look at our margins over the next 4 to 6 quarters from now.

Varun Lohchab:

Can we still move up from these levels?

Sameer Shah:

It will be difficult to give guidance on this front, but if you look at it on a Y-o-Y basis, averaging out for full year, we expect margins to substantially move up from full year FY14 numbers.

Varun Lohchab:

The Africa license fee that you have mentioned for those geographies, is that going to be recurring every quarter?

Sameer Shah:

Yes.

Varun Lohchab:

What would be the volume growth in Soaps this quarter?

Sameer Shah:

Would be in low single-digit.

Varun Lohchab:

At a category level it is still de-growing?



Sameer Shah:

Yes, at a category level, is mid-single digit degrowth in volume.

Varun Lohchab:

Could you share the rural and urban growth rates for the domestic business?

Sameer Shah:

Urban growth rates have been in mid-to-mid-low single digit and rural growth rates have been in early double-digit.

Varun Lohchab:

You mentioned the rural growth is also because of distribution expansion, but is the underlying trend in rural softening at the margin or will that pick up or are there early signs of pick up that you are seeing in rural as well as urban?

Vivek Gambhir:

The urban markets got hit a lot more. We are seeing slightly better momentum in urban, but we are also now sensing some uptick in rural as well.

Moderator:

The next question is from the line of Harit Kapoor from IDFC Securities.

Harit Kapoor:

Would be the overall volume growth for the India business for the quarter?

Sameer Shah:

Standard business growth is around 7% in India. Half of it would be volume and other half would be price-led growth.

Harit Kapoor:

On the Darling licensing, would the quantum of fee recur every quarter?

Sameer Shah:



Not by the same quantum. As a line item this is something which will recur every quarter. Quantum in turn is depending on many variables and hence to that extent it will not be the same absolute which will recur every quarter.

Harit Kapoor:

On Godrej No.1, you have launched the Face Wash. Where are we placed in the category of Face Washes and what is the thought process? On Godrej No.1, is there a thought to straddle the mass Personal Care portfolio over a 2-3 year perspective across the board?

Vivek Gambhir:

With Godrej No.1 I think thinking in terms of our differentiation is that if you look at most Face Washes in the market today, very few of them have injected the equity of naturals into face wash. So this will be among the early Face Washes that will inject naturals into Face Washes. Second of all, the packaging, when it gets launched, will be quite innovative. The price point is actually also quite a disruptive. The idea is to use these three things to be able to really find a way to democratize the category. We are also launching sachet format that is a multi-use sachet at a price point of Rs.10 along with having a tube format. But overall, the pricing is actually quite a disruptive pricing, the product is also injecting naturals, and it is a unique packaging format. We believe actually this will really help democratize the category.

Harit Kapoor:

Just from a longer-term, can you democratize more Personal Care category?

Nisaba Godrej:

Yes, it is. We are looking at adjacencies in Personal, Wash and Skin Care. And wherever we feel that we can be disruptive both in terms of product, along with that value for money price, will be entering into those.

Moderator:

The next question is from the line of Aditi Murkute from Iden Advisors.

Aditi Murkute:

The EBITDA margins have been volatile in the international market. Could you shed some light on the European market as well?

Sameer Shah:

Our business presence actually is in UK and we had a year-over-year dip in margins behind a soft sales performance. We degrew by 9% in constant currency terms, because



we had counterfeit issues in one of the lead brands which we distribute in that market, the margins have been pretty consistent if you look at the trend of UK business, they hover over high single digit and early double digit levels.

P Ganesh:

And the drop in growth is also on the back of a high base.

Aditi Murkute:

You have mentioned it is (-) 80 basis points?

Sameer Shah:

Yes, that is the margins decline. One of the reasons why the margins have declined is behind sales underperformance which also has declined by 9% during the quarter.

Aditi Murkute:

What is the current core brand which is selling over there?

Vivek Gambhir:

Basically, it is a five-brand play. We have three own brands – Cuticura, Touch of Silver and Soft & Gentle. Those own brands actually doing very well and growing far-far ahead of the industry growth rate. We have two distributed brands – one is P20 which is a Sun Care brand and then we have another brand called Bio Oil, which is a brand for skin treatment. The challenges we have had is in one of our distributed brands, there have been a lot of counterfeit issues and that has led to de-growth for that brand in the quarter. As far as own brands are concerned they have been doing very-very well.

Moderator:

The next question is from the line of Prasad Deshmukh from Bank of America.

Prasad Deshmukh:

The growth differential between rural and urban seems to be very sharp. Is this driven only by HI or is it across the categories? Are you seeing sharp growth in the rural versus that is being witnessed in urban?

Vivek Gambhir:



Historically, if I look at our growth, typically, we have had about 1,000 basis points delta between rural and urban growth. So in some sense, this delta is fairly consistent at least for our business what we have seen over the last 2 or 3 years.

Prasad Deshmukh:

Is this uniform across categories, in Soaps as a category, is rural growing as fast as urban?

Sameer Shah:

Across our three categories, we are seeing more or less similar delta between rural and urban growth. If you are looking at overall HPC, over last two months, what we have seen is sequentially, the growth in rural is higher than what it is in urban, but this is just last two months data and one needs to see a few more months to have belief in it.

Prasad Deshmukh:

Sometime back you were giving a decent push to increase distribution internationally, different models in different geographies. In Africa, you said it was a wholesaler-driven market and you were trying to increase penetration in terms of actually appointing distributor so that you have more control over predicting sales. What is the status now?

Omar Momin:

We have made very good progress on that model which we started in Nigeria in the geographies that we started piloting this direct distribution, now direct distribution accounts for about 30% of our overall sales. We will continue to push this in terms of expanding to other geographies as well as developing it further in the geographies we are piloting this.

Prasad Deshmukh:

How much was it a year ago?

Omar Momin:

Zero.

Moderator:

The next question is from the line of Kaustubh Pawaskar from Sharekhan.

Kaustubh Pawaskar:



On your balance sheet, the long-term borrowing compared with March 31, 2014 has gone up by around Rs. 225 crore. Is it because of the acquisitions you have done the borrowings have gone up?

P Ganesh:

This is largely on account of a refinancing which we have done at a lower cost. If you see from short term it is actually moving in to long term. Because of the refinancing, the installments which were falling due within the first year have now moved into long term and therefore they do not get classified as current liability.

Kaustubh Pawaskar:

Is it expected to further enhance because whatever acquisitions you have done would be largely paid by debt?

P Ganesh:

The strong cash flows which we generate go down to paying down existing debt and that creates more room for fresh debt to be taken for further phases and at that moment we have visibility on the further phases of the Darling acquisition. Net-net, the debt-equity ratio will not move the needle significantly. If you look at where we are versus one year back, the debt-equity ratio has actually improved.

Kaustubh Pawaskar:

On the Soaps category, as we have seen that commodity prices are lowering and it is becoming a favorable scenario for most of the players. In such a case, we will also see mass players or regional players getting aggressive in the market. Considering that would you be looking at enhancing your advertisement spends and sales promotion resulting in higher advertisement spend and other expenditures in the second half?

Sameer Shah:

It is very difficult to ride on this, we will have to play category-by-category, what you have seen in the past is if you take categories like Soaps, especially when the margins expand because of very benign commodity environment, a lot of small local players come back to the market, also a lot of players increase tactical strategies. That pushes up the sales promotion spends, not necessarily the advertisement expenses. But, we will see, answer would differ from category-by-category.

Kaustubh Pawaskar:



Whatever savings you would be having at the gross margins level, would you be looking at investing into your other categories, not specifically in terms of Soaps, but Hair Colors and Household Insecticides?

Sameer Shah:

Yes, it is a portfolio play also, so to that extent we would leverage on gross margin expansion flowing in from one category, supporting and driving growth for other categories, that is quite possible.

Vivek Gambhir:

These portfolio decisions also made with the overriding principle that we would like to keep our profit growth in line with sales growth if not higher than sales growth. Based on that principle, then we make the right calls, based on innovation pipeline and competition etc., how to allocate any incremental growth contribution to the highest potential opportunities.

Moderator:

The next question is from the line of Ritesh Vaidya from Ambit Capital.

Ritesh Vaidya:

On lower advertising spend, can you please elaborate if it is cut for a particular category or has it been cut across all categories?

Vivek Gambhir:

It was more driven by reduced advertising spends in HI, because as Mr. Godrej said, because of delayed monsoon, and we know this from past also is that when monsoons do not come at the right time, mosquito infestation is lower. Strategically, when we saw that happening, we knew that it was better to conserve advertising spend for later quarters. But across both Soaps and Hair Colors, our spends were very much in line with the market requirements, but the spending reduction came more from HI.

Ritesh Vaidya:

On the Soaps portfolio, you have delivered 13% growth which is exceedingly well. Has the outperformance been driven by promotions that you have given and are these reflected in the lower gross margins, what exactly drove the outperformance in Soaps?

Vivek Gambhir:



One reason for the outperformance was clearly Cinthol, which is the more premium play. We have done very strong launches under the Cinthol portfolio; one was Cinthol Cool, which was re-launched, re-advertised a few months ago, and now Cinthol Confidence Plus Germ Protection. Clearly, as we are launching more variants of Cinthol, we are seeing this brand give us very strong growth. We had some executional and tactical challenges as far as No. 1 was concerned. And as we have launched better marketing programs, we have clearly seen No. 1 growth return back. It has been a combination of both – good growth in Cinthol as well as some recovery in No. 1.

Ritesh Vaidya:

Will we see in the coming few quarters, despite some gross margin benefits, these being invested in higher advertising and promotions leading to stable EBITDA margins?

Vivek Gambhir:

We will have to wait and watch, because a lot of it depends on as palm oil prices have come down, clearly, there is more intensified competition that comes into the market from local and regional players which is much more tactical in nature. Having said that if you go historically, No. 1 has done very well during periods when palm oil prices are low. That again gives us some comfort. In terms of margin clearly our hope would be to be able to plough a little bit of the palm oil savings into margins, but some of it will depend on the nature of competition.

Ritesh Vaidya:

We have seen that the acquisitions that you have done in the past especially in the Africa, it has had a few delays especially around integration of bringing into different countries under 100% ownership and some of your acquisitions even in LatAm or UK, they are doing good, but they are still not at the mark. How do you expect inorganic growth going ahead, how central is it to your strategy for the future for the next 4-5 years?

Adi Godrej:

First of all, we have done very well in our inorganic acquisitions. If you look at it, overall it has been very accretive to the Company's earnings. We feel whenever there is a good opportunity we will certainly take advantage, both in Africa and South America we have done well with our acquisitions despite the fact that general economies on both the continents have slowed down. We will continue to look at acquisition opportunity and we will ensure that they are accretive to our earnings.

Moderator:

The next question is from the line of Aashish Urganlawar from Elara.



Aashish Upganlawar:

How much of Darling business are we now controlling in percentage terms?

Sameer Shah:

We have two-three business models, in some business we have 100% stake on like in Nigeria, a few others like Kenya, South Africa, Mozambique, we have more than 50% and in geographies like Uganda, Ghana, Tanzania, we are receiving licensing fees. We control near 80% of the business in terms of the size of Darling geographies.

Aashish Upganlawar:

As mentioned in the presentation; licensed our rights of Darling trademark. Is it only a registration of trademark or is it out licensing?

Sameer Shah:

We have rights to these trademarks and we have licensed out this rights, as a result of which we are receiving this licensing fees which sits in the other operating income in the P&L.

Aashish Upganlawar:

How much is that in the other operating income?

Sameer Shah:

It is around Rs.9 crore for this quarter.

Aashish Upganlawar:

Would this increase?

Sameer Shah:

In terms of quantum, because it is linked to several other variable things, it would be difficult to quantify it, but there is something as a line item which is recurring in nature.

Aashish Upganlawar:

Are there other one-offs in the other income apart, I read a couple of them in the notes to accounts?

Sameer Shah:



There are a couple of them and there is a separate disclosure on it in the performance update, there is insurance claim receipt in India and Indonesia, there is a small restructuring cost in Argentina and the ESOP income in India.

P Ganesh:

There is a separate slide on this.

Moderator:

Thank you. Ladies and Gentlemen, that was the last question. I now hand the conference over to Mr. Prashant Kutty for his closing comments.

Prashant Kutty:

On behalf of Emkay, I once again like to thank you all for joining the call today. I would like to put up to Mr. Godrej for any closing comments.

Adi Godrej:

Thank you, Prashant. And with that I would like to bring this call to a close. Thank you for all of you for being on the conference call and if you have any other details, queries, our people will be very happy to answer them.

Moderator:

Thank you very much members of the management. Ladies and Gentlemen, on behalf of Emkay Global Financial Services, that concludes this conference. Thank you for joining us and you may now disconnect your lines.

Disclaimer - The following transcript has been edited for language and grammar, it however may not be a verbatim representation of the call.

