"United Spirits Limited Q3 FY '18 Results Conference Call"

January 24, 2018

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Moderator: Ladies and Gentlemen, Good Day and Welcome to the United Spirits Limited Q3 FY '18 Results Conference Call. From the management of United Spirits Limited, we have with us today Mr. Anand Kripalu – Chief Executive Officer, and Mr. Sanjeev Churiwala – Chief Financial Officer. 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 '*' followed by '0' on your touchtone phone. Please note that this conference is being recorded. I am now glad to hand the conference over to Mr. Anand Kripalu – Chief Executive Officer, United Spirits Limited. Thank you and over to you, Sir.

Anand Kripalu: Thank you very much and a very Good Afternoon everyone and thank you for joining this results call. As we normally do, I will provide a perspective of our results that we announced last evening and then we will open up the line for Q&A.

Now, as you may have seen in our published results, our net sales in the third quarter was adversely impacted by the expected Route to Market changes in certain states, and to a lesser extent by the residual effect of the highway ban. In fact, over the last six months, there have been RTM changes like Jharkhand, Chhattisgarh, and that is now behind us and it has happened, West Bengal that is just getting completed as we speak, in fact Calcutta Metro is just transitioning, and Haryana and Punjab which had an impact on the quarter and UP that is likely to happen, so if we exclude the RTM states particularly in the last quarter, our underlying sales in the rest of the country remain strong and I am pleased with the sales that we are getting from the other states.

Now, Haryana and Punjab as I said were the ones that were most impacted and most impacted the revenue this quarter. Haryana specifically issued a notification changing the distribution of alcoholic beverages to a corporation model, which is a government corporation model effective April 1, 2018. In light of this expected change, we as a company took the call to make sure we prioritize credit risk over sales risk, which means we put emphasis on making sure that we control our credit and start collecting money from many of these private parties who will not be in business from 1st of April and that is the philosophy that we pursued and we believe that was the only prudent thing to do during this quarter. Now, due to these short-term headwinds, underlying net sales declined 2% and these Route To Market changes also impacted the Prestige and above segment the most where underlying net sales declined about 1% in the quarter.

Now, despite a muted top line performance, I am particularly pleased with our gross margin improvement. Now, this is something that we have been trying to fix for a long time and we believe more than any other indicates the health of our portfolio and business. This has allowed us to significantly increase marketing investment by 27% and thereby invest in the future, so we delivered 373 BPS underlying gross margin improvement during the quarter fuelled by more extensive price increases and more than half the states have given us price increases this fiscal, premiumization and accelerated productivity including the mitigation of GST. Staff costs were lower by 7% benefiting from the savings delivered by the organizational changes that I have spoken about to you on past calls. The underlying EBITDA margin was 13.1%, broadly in line with the previous year and this is after the higher A&P spend and after taking a prudent approach on provision given any future risk on the RTM transition.

We have continued to focus on reducing debt and interest costs were lower by 29%. I am also happy to share that recently USL made its maiden issue of NCD of 750 crores, so as to refinance existing higher cost debt. This will help to further lower interest costs in future period. We are also pleased with the enhancement of our long-term credit rating to AA plus by CRISIL. You may have seen that we have reported 13 crores of exceptional charge during the quarter; this one-off charge relates to manufacturing unit closure and reflects our continued focus on further rationalizing and optimizing our supply footprint. Profit after tax for the quarter was down 9% due to the lower net sales and as a result of the high investments in provisions which we have taken in order to protect the future of this business. As we had outlined earlier, we do not run this business on a quarter-to-quarter basis, we rather manage this on a longer-term basis, but at the minimum, on a full-year basis.

Just to very quickly then summarize our performance in the nine-month of this fiscal, underlying net sales declined 2% with the Prestige and above segment growing 1%, and this was significantly impacted by the highway ban during these nine months and then the expected RTM changes which have happened more recently that I just shared with you. More extensive price increases during the year, continued focus on premiumization, and accelerated productivity has led to 301 BPS gross margin improvement ***(clarification: underlying gross margin improvement),*** which stood at 47% which we believe is really healthy and kind of in the zone that we want to be in. This together with lower staff costs has allowed us to increase marketing investments by 13% in the nine-month and lead to an underlying EBITDA margin improvement of 73 BPS to 13.2%. Interest costs were lower by 29%, this coupled with lower exceptional item has resulted in overall PAT increase of 28% over the nine months. Looking ahead, while the adverse impact of the highway ban is behind us, we do expect to see continued impact of Route To Market changes in certain states as I mentioned earlier in this financial year. Importantly, we now expect that the adverse impact of GST will be more than offset by productivity saving and pricing.

Finally, I do want to say this that while we are not happy, and I know that many of you might have had some concerns with the soft top line. You know, I really do believe that we have never been more confident about the current health and the future of this business. We have overcome some of the biggest headwinds that have the potential to not just derail this company, but to derail this industry and we are past those, and we have come out much stronger for it. We are, therefore, committed to investing in the future and some of the decisions that we have taken this quarter are in line with that perspective, so as to realize our medium-term ambition of double digit growth and mid-to high teen margin. With that, I am going to open up the line for questions which I and our CFO, Sanjeev Churiwala, will jointly address as best we can. Over to you please.

Moderator: Thank you very much. Ladies and Gentlemen, we will now begin the question and answer session. We will take the first question from the line of Manoj Menon from Deutsche Bank. Please go ahead.

Manoj Menon: The one question on the gross margin, what I understand is that the underlying 373 BPS improvement includes the franchisee fees which we collect, which in my understanding again is more like an annuity, so how should I think about the medium-term, I would call it as a one-time impact of this franchise fee which comes in, which kind of comes into the base because after that it grows at, if I remember correctly at mid-single digit number, I am trying to understand the drivers for further gross margin expansion, I understand the top-down premiumization part, but are there any bottom up costs efficiencies also which is feasible be it once this one-off plays out?

Sanjeev Churiwala: Thanks Manoj for this particular question. I think many of you on the call would have similar questions on the shape of the P&L and especially how our gross margins are evolving, so let me tell you upfront collectively as a management team, we have never been so confident in the past as compared to where we are today. We are very, very happy the way our shape of P&L, shape of the profitability and the future health for the P&L is emerging. I would like to just pause here and take you back on the shape of the P&L that we had a year back and how are things looking like now in the nine months' time and this will give you some perspective as to you know what kind of sustainable margins enhancements and profitability we should be looking at. In F '16, if you have the numbers with you, you will see the gross profit stood at 41.5%. In the nine months now, our gross margins are 47.4%, so in the nine months we have seen our gross profit margin enhancing overall by about 600 BPS point, this is on the reported basis, so absolutely there have been some impact because of the movement of the franchisee wherein the top line net sales has gone away and to that extent we see in place the franchisee income coming in and we have very clearly called out that purely on account of the franchise that we see, we have about close to 160 BPS impact because of the franchise and that is the underlying performance that we have been talking about, but when you look at our gross margins evolution, thing is it is perfect.

We have seen a big productivity improvement coming in over the years very clearly. GST impact we said is subdued, it is more than offset by productivity as well as price increases, our franchise business actually going as per our planning overall. If you look at the other shape of the P&L item, our overall staff cost which was about 7% remains almost flattish at 7%. Our A&P spend is as per our aspirations of about close to 10% and our other overheads, it is about 14.5% to 15% odd, so overall as compared to EBITDA margin of 9.4% which we had for F '16, we are standing currently for the nine months at12%, which is about 260 BPS improvement in the EBITDA margin. I do think a year back we were always talking about this, there was always a question about our gross margin enhancement and our EBITDA margin enhancement, so I think we are really delivering on ambitions on pricing, productivity, mix, and overhead improvement. We are now not a million miles away from overall aspirations of mid-to high teen margin aspirations, we have really demonstrated in the last nine months, a very steady improvement in our gross profit margins and EBITDA margins that should, Manoj, answer your questions on the gross profit as well as overall margin mix.

Anand Kripalu: Just to emphasize, our underlying gross margin improvement of 373 BPS is without the franchisee benefit, so that is underlying to the business, and the other thing I just want to add to what Sanjeev just said is if you look at every line item of our P&L, it is moving in the right direction, it is in the direction in which the strategy of the company, we have wanted to drive. There has been a top line impact this quarter, which we recognize, but if you look at every other line of the P&L is moving in the direction which we would like.

Manoj Menon: Secondly, quickly on the input cost, allow me to say that there is a general consensus expectation that input costs corrections, ENA price corrections could potentially lead to margin expansion, of course that is the job of the analyst to figure this out, but just from your perspective, how should I think about, help us in terms of because historically input costs would have been volatile in terms of inflation as well as deflation, is this really an important source of funds for you to say that if input costs indeed get into a deflationary cycle, that does give the liquor industry, the alcohol industry lot of sources of funds to reinvest?

Anand Kripalu: Well, let me just say this first of all, so we have been in a relatively benign commodity environment and when I say relatively benign, it has been less in general inflation and it has been less than the inflation that we forecasted in our P&L for the year and that has helped also drive the gross margins. Now, in this game, it is really hard to say what is going to happen because if we could do that we would all make a lot of money together, but I think our view is that there will be some or could be some hardening of commodity prices as we look into the next fiscal, in fact that is what we are expecting that there will be some hardening and we are trying to work around how to mitigate that to continue our journey of protecting and even building on our gross margin, so that is how we are approaching it.

Moderator: Thank you. We will take the next question from the line of Arnav Mitra from Credit Suisse. Please go ahead.

Arnav Mitra: The first question was on the growth itself, so if you could help us get a sense that if this Route To Market change in states like Haryana, Punjab, West Bengal, excluding this what would be the range of growth that you would have seen in the rest of the country and is it an acceleration over the growth that you saw in the second quarter, why I ask that is this quarter had demonetization as a base, so there should be a low base effect and gradually the highway ban effect should also be going away, so just wanted to get a color on the relative trends also between 2Q and 3Q on a YOY basis?

Anand Kripalu: There are many moving pieces both in the numerator and in the denominator, denominator as you rightly said there was demonetization in the base, and therefore, it was a relatively softer base in terms of purchase and consumption, but equally we pushed very hard during that quarter just to make sure that we get the maximum that we can at a time when there was a lot of instability in the market, and when you look at the numerator this year, obviously there are these RTM changes that we are experiencing. If I look at just underlying performance outside of the RTM states, we have built momentum over Quarter-2 in terms of our growth rates and actually I am quite pleased with the levels of growth. I do not want to give a number there, but I will tell you we are pleased, we have built a momentum and we are pleased with the level of growth, so if is these RTM changes had not happened, I think you would have seen a set of top line numbers that have been far more in line with what you would have expected to see. The gap has been because of this and we always knew that these changes are going to happen and we as a company have played cautious during these RTM changes because recognize there is lot of debt and therefore credit risk with these wholesalers. In this industry, when RTM changes happen, parties disappear and then you can keep fighting them for as long as you want to recover your debt, but then good luck to you with that, so we have taken the call and that is ultimately a management call.

Arnav Mitra: Right, thanks for that. The other thing you had said is that you have made some provisions for the RTM changes, could you just throw some light on what kind of provisions, are they booked somewhere in the P&L?

Sanjeev Churiwala: That provision would appear in the other overhead line, but you could really compare the overhead line as compared to the previous corresponding quarter, you will not see a major difference because we have really been managing our overall overheads far better than the inflation outlook, but yes because of the prudence accounting policy, we did have to provide some provisions which is appearing in other overheads.

Anand Kripalu: We have been prudent, we could have taken the easier way out, but we have played prudent and again that is management philosophy and the management path.

Moderator: Thank you. We will take the next question from the line of Avi Mehta from India Infoline. Please go ahead.

Avi Mehta: Sir, just wanted to clarify this RTM change that you had mentioned about Haryana, Punjab, and West Bengal, as Punjab also you have done a similar exercise A, and B, would it be fair to assume that this impact of this RTM change will moderate from the current levels?

Anand Kripalu: Absolutely, we are going to moderate from the current levels, so Haryana was the most significant impact in this quarter, Punjab was an impact but to a lesser extent. The nature of this beast also is that we are waiting for formal Government policy and on things like this policy also changes sometimes, so there is an impact that is in the quarter, do I expect a big impact on Haryana in the next quarter? I expect a much lower impact of Haryana in the next quarter. We have taken a big impact in this quarter and we have produced sales. Now, Punjab may be a little more in the next quarter, UP could be a bit more, but UP is still a little blurred in terms of what is the government going to do, is the monopoly wholesale system in UP going to change to a Government corporation or a multiple wholesale model, but the reality of RTM changes is, it is a matter of three to four months. Post April, I expect all these markets to stabilize and actually once that happens, we should actually see very strong performance coming back in each of these space, but there is nothing fundamentally wrong with consumer demand or pricing or anything of that kind. There is no fundamental issue. The issue is just a shock that happens because of a structural change in the route to market in terms of how the product loss and as long as consumer demand is intact and as long as we are investing in A&P which we have done, then the demand for our brand should remain strong and the business should bounce back.

Avi Mehta: Perfect sir, this is helpful. Second thing sir on the margins side, could you kind of share how the ENA prices have been behaving now? Have you seen a moderation in ENA prices because Telangana price hike has not yet come, but I just wanted to also understand from the ENA point of view, is that benefit also likely to flow in going forward?

Anand Kripalu: Why do you say the Telangana pricing has not yet come?

Avi Mehta: Sir, I would have thought that it is not flown through to margins completely in this quarter.

Anand Kripalu: Of course not, but it has been announced in the public domain. Guys, you are aware of that. I thought you had some inside information, I got worried. Sanjeev, you want to talk a little bit about commodity and ENA?

Sanjeev Churiwala: Absolutely. So Abhi, I think instead of talking on one particular commodity, let us just focus on the overall input inflation. I think we have very clearly called out that while just like every other industry players, there is an inflation that we have to manage every year which went from depending on how subdued the overall commodity is from 2% to 4% on an average, but we are very pleased about that given the extensive price increases that we had this year in the 9 months, more than 50% of the state have given us price increases. We have never seen this happening in the previous year plus the kind of productivity that we have delivered to the business. Both this put together is more than offsetting the overall inflation that we have and that is clearly reflected in the gross margins improvement that you see.

Anand Kripalu: So just simply, we have mitigated more than 100% of inflation through our internal productivity initiative, right. Now having said that, ENA has been benign, relatively benign and I think is continuing that way. But our team believes that it is going to harden like I said earlier, but that is where it is right now Avi.

Moderator: Thank you. We will take the next question from the line of Jamshed Dadabhoy from Citigroup. Please go ahead.

Jamshed Dadabhoy: Couple of housekeeping questions. One is your tax rate seems little lower this quarter. Is there anything to call out or read in that effective tax rate?

Sanjeev Churiwala: I think tax rate is definitely lower, but I have not looked at it quarter-on-quarter because depending upon the taxes assessment, the tax planning, it will keep on moving from quarter to quarter. What you really see is effective tax rate being 2% lower, I will not really get into completely scrutinizing ETR rates but we are really doing a lot of tax planning and ensuring that our effective tax rates are lower than the statutory tax rates.

Jamshed Dadabhoy: So what is your sense on what your full year tax rate could be?

Sanjeev Churiwala: I think for the purpose of your computation, I think keep it simple just plan on basis of the statutory tax rate and our intention is to ensure that we are lower than that.

Jamshed Dadabhoy: Second question, so if I look at your 9 months of YTD numbers in terms of revenue growth or ASP growth for the Prestige plus segment, it works out to roughly a Rs. 50 increase on a per case basis, about 3.5% increase. Within this 3.5% increase, could you give us some sense in terms of how much is price and how much is mix because I know there is a structural uptrading trend which is happening even within the Prestige plus segment, but I just like to get some more granularity or color in terms of how much has just been the price effect this year because as you said this is more than 50% of the states have given you price hikes and it is something which you have not, it is kind of unprecedented.

Anand Kripalu: So within P&A, I think we could assume that the large part is price or pricing or optimization of other moving pieces in terms of taxes and so on given pre and post GST. I think that would be the lion share. Now what has negated the thing a little bit is the state mix because Haryana and Punjab are high margin states relatively and since those have had an impact, so that has affected mix because mix is not only brands within the P&A portfolio, it is also about state mix and that has had a bit of an adverse effect. So I would say to keep this simple assume that the large part of it is to do with pricing.

Moderator: Thank you. We will take the next question from the line of Amit Sinha from Macquarie. Please go ahead.

Amit Sinha: Sir, would you like to share a particular number on the provisions which you mentioned?

Sanjeev Churiwala: So I think I did mention that provisions is reflected in the other overheads line and when you look at the other overheads line, it shows about 4.8% increase which is more in line with inflation. So while we have provided for certain provisions on a very prudent basis, we would not like to specifically call out the number and you understand why.

Amit Sinha: Okay sir. Secondly sir on the RTM changes specifically in Haryana, Punjab and UP, so you have clearly mentioned that from April onwards you think everything should normalize and sales should come back to normalcy etc. Just wanted to understand how the working capital behave from here on? I understand at this point of time you have credit focus and you are recovering your credit from the private parties, but once it gets to the government or the corporation model, would you assume that the working capital cycle will be similar to what we had in the past from FY19?

Sanjeev Churiwala: If I understand, you have two questions. The first question is we did have RTM changes happening that will continue to impact to us in the current quarter from January to March and of course the answer is very simple. As Anand said, our secondary is really looking good. So barring RTM changes, we are very happy with the way the things are moving. I think our Prestige and above which remains our focus, we will definitely continue to focus in growing that at double digit, there is no question about it and that is our focus area. Coming to the working capital while for December, we do not have to really report on the cash flow on the balance sheet, but we have been extensively working on the working capital. For December, our working capital numbers have vastly improved in the last 9 months and we are very sure going forward as well while we will have pluses and minuses because of the RTM, we will continue to manage our working capital very tightly.

Moderator: Thank you. We will take the next question from the line of Mayur Gadhani from OHM Portfolio. Please go ahead.

Mayur Gadhani: Just one query. I do not know whether you mentioned this or not. The other overheads have gone up from 300 crores to 390 crores quarter-on-quarter. So what has led to this significant increase?

Sanjeev Churiwala: So when we look at overheads, the best way to really look at is the 9 months overheads. Rather than just looking quarter-on-quarter because we will have pluses and minuses between the quarter. For the 9 months, our overall overhead has gone up by **2%** If you look at the absolute overheads, we are at about 1000 odd crores, 1031 crores (to be precise), similar to about 1000 odd crores in the last 9 months, almost flattish.

Mayur Gadhani: That I agree sir, I take that point. Just wanted to say why there is so much of a difference on quarter-on-quarter basis, anyway. On the advertisement side, it is 10% is what you look at on a yearly basis for this year and would you consider the same next year also?

Anand Kripalu: Yes. So our ambition is to spend about 10% on A&SP growth and if you look at our YTD this year for 9 months, it is of that ballpark give and take a bit. So this quarter has been higher, but then this quarter is the most important quarter for our industry, right. Equally in this quarter, we have also introduced a new brand which we did not infuse in this quarter, but this was the main quarter for that brand which is Captain Morgan and I am very pleased that we with our Captain Morgan Dark Rum which has been formulated for India, but how it is doing and how it has done particularly in November-December and how it is going in January and the whole effort here is to premiumize Rum where there has been no real hard intervention to premiumize Rum like has been done in Whiskey and we put A&SP behind that too.

Mayur Gadhani: And coming to the other expense, so the provisions that you have created have been added over here right?

Anand Kripalu: Yes, that is correct.

Mayur Gadhani: And these are provisions that you are just prudently taking because of these RTM changes?

Anand Kripalu: Absolutely.

Mayur Gadhani: And we can see that coming in quarter 4 also because in case with Punjab and UP as well to some extent?

Sanjeev Churiwala: Well, we do not know. As Anand has said that our effort is to really minimize our credit losses in these markets and that is why we ensure that we have pared back our sales in this market. I am really focusing on managing the credit very well and we are really managing it every day and we have to really see how RTM changes behave in the coming months.

Anand Kripalu: And those provisions can move plus and minus. I mean, we might be able to release some of it because of the decisions we have taken on how to manage credit versus sales, but then another state may open up in the next quarter. But this is going to happen and over the next 3 months-4 months-5 months, there will be these pluses and minuses till the new RTM stabilizes.

Moderator: Thank you. We will take the next question from the line of Ankit Panchmotia from ICICI Securities. Please go ahead.

Ankit Panchmotia: Sir this is regarding this RTM change. So we have cautiously tried to focus on credit risk rather sales risk, so just wanted to understand the impact of the same on the market share. How adopting this strategy, we would be maintaining our market share or there would be some sort of market share loss with the strategy going forward for the next quarter as well?

Anand Kripalu: No, so let me clear. Short term during the period of the RTM change, there would have been some market share loss because we took a call of being conservative and how much we want to push versus how much of all the outstanding we are collecting. And we actually sold to many of the syndicates and wholesalers only based on how much they were willing to give old outstanding back to us, okay? So the short term, yes, there will be some market share loss. But what have we done. Our growth drivers in terms of investment behind brands is intact. In fact we stepped it up nationally. So what we are trying to make sure is that the equity for our brands and demand for our brands doesn't scale down or doesn't reduce in anyway but strengthens. So the moment we are done with this, right, I hope that we will be in a stronger position. So we are trying not lose money through credit risk, but also not lose any long term market share. Some short-term shocks in market share, yes, that is part of the strategy that we have adopted which we believe is wise.

Ankit Panchmotia: Right. And sir any update regarding the noncore assets, where have we reached or how are we planning for complete FY18? Any update on the same?

Anand Kripalu: We will continue to maintain our stand that we do have plans for about 2000 odd crores of asset monetization over the next 3 to 4 years' time. Because of the demonetization, we did see temporary blip where we were not able to really improvise on our noncore sale assets, but I think we already now see some traction happening on the ground. For the 9 months ending December, we already see a noncore monetization of about 60 odd crores which has given us a cash of 60 crores and is reflected in terms of profit in other income about 46 odd crores.

Moderator: Thank you. We will take the next question from the line of Latika Chopra from JP Morgan. Please go ahead.

Latika Chopra: Just two questions. Firstly, on this route to market changes, what are you pecking up, have the other players in the industry also behaved in a prudent fashion and you have mentioned some near-term market share losses. Does it mean when the markets move to corporation model, you will move back to your prior market shares?

Anand Kripalu: So as far as the other companies are concerned, Latika, we will ask them, but our observation is that we have been little more cautious than others and so recognize when we talk market share right now, I am not talking tertiary or consumption share because I have the data. What I am talking about is primary sale share and that is based on how much we are selling in, not how much consumers are pulling out and because we are selling on a little less, there is a short-term erosion of primary market share. Now therefore I am not saying for a moment that our consumer market share is actually declining at the same rate or is declining at all. Therefore, when this funny in the middle goes away and we come back to a corporation where we have smooth sales happening and actually I must say one more thing here I actually believe that corporation is not a bad thing at all. Syndicates and management of wholesalers and the margin that they take away, I think is not as good for smooth selling and for ease of doing business as a good corporation is and we have very good corporations which are absolutely painless and clinically clean and compliant to work with. So, I think that the move to corporation in some of these states that have been controlled by a few wholesalers will actually be better. So as we get into smooth selling which a corporation should bring in, I believe we may or may not have lost consumer market share at all. And even if we have lost something in the short run, the investments we are making in equity I will help us to bounce back very quickly.

Latika Chopra: Sure. This is very helpful and lastly, in your core markets like Maharashtra and Karnataka, have you sensed any change in the competitive activity on the ground?

Anand Kripalu: So competitive activity I would say has been quite intense. And it is always pretty intense in this industry because by and large just a couple of players playing in a segment of the market, right? So it tends to be a two horse race, generally speaking in most segments of the market. Not the same two horses in every segment, but typically about two horses in every segment. So it has been fairly aggressive. We know that in terms of advertising spends and I am not talking about ATL, right our brand extension advertising that we do, we have been very competitive. And our share of voice is absolutely intact and competitive over there. On the ground, short term spends in terms of trade and consumer promotions like giving the freebee with the bottle and stuff like that, I think there has been some intensification of short term activity by some of the competitors, right, and these things happen month-to-month. All I can tell you is that, with the A&SP as the way we are planning it, we have the purse to invest aggressively and not just defend but be on the offensive and build shares. And that is exactly what we are doing. So I feel quite confident about the investments we are making, the activities that we have. That we will stay very competitive.

Moderator: Thank you. We will take the next question from the line of Chetan Shah from Jeet Capital. Please go ahead.

Chetan Shah: I have a very specific question about the future strategy if you can just throw some light on that. You spoke about premiumization of Rum versus how it happened in Whisky. So could you just give us some flavor about your thought process, where you want to focus on the next 3 to 5 years without naming any specific brand and all, that will be really helpful for us to understand the big picture situation for the company as a whole?

Anand Kripalu: So first of all, you know the guidance we have given in terms of making sure we get the double-digit growth in the medium term. If you look at our strategic priority, our entire focus, power brands, which is a fraction of the brands that we own, is about investing in those brands, making them stronger and ensuring that the more premium brands grow faster than the ones below. So we expect that each segment of the market if you price segment the market, then each segment will grow faster than the segment below it, right? And that is how premiumization is happening. And we have seen that happen and you can't read that on quarter to quarter basis, we have to read that from a longer-term basis because there are lots of shocks that happened in the short term. So our strategy is absolutely about premiumization and that has been part of our philosophy of also franchising our popular business. So that we can focus on the Prestige and above and focus on the premiumization agenda that we have. Other elements of our strategy include being able to shape how this industry is seen. And how we can create ease of doing business for this industry by making governments and consumers alike celebrate responsibly. I think responsible consumption of alcohol is very high on our agenda and if we are able to land that, I think pricing and regulation will ease and that is to our advantage. We will continue focus on enhancing margins by aggressively driving productivity and savings and the intent is to mitigate a large part of inflation every year. So that pricing and other things can actually help to drive our gross margin which can fund our investments in brands and in stores and finally to have an organization that is fit for purpose, that is not just ready for today, but that is ready for tomorrow and as an organization with a right span, with the right layers and the right culture. All right? So I mean this is about all I can do in a short call like this. But this gives you a picture of really what we are trying to pursue.

Chetan Shah: Thank you for such a brief and broad overview. If I may allow to ask one very specific question, when you talk about sir premiumization and we see the mix of our total revenue both in volume share and also the top in a value share. Do you have any big picture in mind that in five years from today or ten years from today ex amount of volume or ex parentage comes from a premiumization product category versus what it is today? Any road map or something if you can share that will be very-very helpful.

Anand Kripalu: Two years ago the contribution of our Prestige & Above business was 50% in terms of NSV to the total, all right? Today, it is two-thirds almost between 63% and 65% of our business in Prestige & Above. I believe that that if we go into the future Prestige & Above will become 75% to 80% in the fullness of time because Prestige & Above will grow many times faster than popular business. So as we look into the future, the future profit pool of this industry will be in Prestige & Above and the lion share of our business will be in Prestige & Above.

Moderator: Thank you. We will take the next question from the line of Pulkit Singhal from Motilal Oswal Asset Management. Please go ahead.

Pulkit Singhal: I have two questions. One is, while you talk about double-digit growth for lead sales I mean when we look on nine months basis it is actually a decline of 2%. So we as investors are looking at growth at sales as well as at EBITDA but margins can go up without giving much of EBITDA growth. I am just trying to understand for the last two years you have sounded very optimistic, but the numbers are not necessarily reflecting that. So what is it that we are missing? If you could share some anecdotes on the ground that could give us a sense of good consumer demand, that would be helpful?

Anand Kripalu: Yes. So you know it is very hard to answer this question without just doing it a little philosophically. If you look at with this industry and the company therefore has come through, right? I mean have we created an environment for just normal consumer consumption and purchase starting from demonetization to the Highway Ban to the shock of GST that happened, which was complex for us to do and then following up on that other Route-to-Market changes. Now, all I can tell you is this that this has always been a complex regulatory environment and it was actually tougher a couple of years ago when we started our journey in India. But it has started easing. And we think shocks will come and go but I cannot think of how we can have double-digit sales if we are going to have the short-term headwinds and short-term changes happening. Now, all I did say in my opening remarks was, if I leave out states where we have got this RTM changes we are actually delivering strong growth and building momentum versus the previous quarter. Now those are states where there is no shock and where we are able to do business as usual. And if you step back at macro level the fundamentals of industry, the per capita consumption, the progress in GDP per capita and if you then were to use other countries as lead indicators India cannot but deliver strong volume and value growth in the fullness of time. It is just a nature of the consumer opportunity based on people entering legal drinking age and the disposable income and the breakdown of attitudal barriers towards alcohol. So there is a short-term set of shocks and you are not able to see that in nine months and I get it. But there is a long-term opportunity whichever way you look at it you cannot run away from. Now the question really is, are we going to have period of stability in this industry where there will not be short-term shocks. I believe it is there and it is around the corner. But even after the last quarter's results what I told people is that in this industry never-say-never. Things happened and the only way is to change the narrative of how alcohol is seen by regulators and by civil society. There is no other short-term answer to this question. So when I say that we will deliver double-digit growth in the medium-term I absolutely believe it, right. And I am delivering that kind of growth in states where I have stability. I mean that is the way this industry works.

Pulkit Singhal: So I mean this second question and this is particularly relating to popular segment which is 36% of your revenue is currently. One is, what really is your strategy there I mean I understand that you franchise out certain part of the business. But even from the existing business it seems that you are losing competitiveness out there. So is this something you just want to make to zero or I mean then you might as well just sell out the business? Second part to that observation is we are really seeing a lot of these competitors the people you franchise it out to get into that segment and possibly the competition is increasing in that segment and may be four years - five years down the line they start going up starting to premiumize their own things so. How do you look at vacating that segment as it is creating competition out there?

Anand Kripalu: So I will have to say what I have said in the past vacating the segment is your understanding its not my understanding, okay. We are using different business models to be effective and to achieve what is our business strategy in different states in the country. There is no one business model that we are pursuing. If I wanted to vacate, I would have sold the brand. You are right. So why we not sold the brand and why do we have time bound contract on our franchised contracts with different players is because I want to reserve the right to take it back if I believe that there is sudden windfall opportunity that I want to be a part of. Now, the way we are managing states that we have franchised out is we are managing it for profit. But we have an eye on the volume and if we feel that the volume is eroding sharply or something we will then work with that franchise to make sure it does not happen. In states which are strategic for us we are not losing market share just to be very clear, right? In our priority state we are not losing market share in fact we are growing our business, right in our priority states. Now there are set of states in the middle which are states which we wanted to franchise but we have not been able to franchise where we can only franchise it by but when we find the right franchised partner. And that is where there is this little bit of instability. I just want to make it clear that in these strategic states we have created a separate sales force dedicated to sell the popular business that is how important it is for this business, right? I have not just left it there for it to kind of wither away. So I just want to get this notion very-very clearly on mind that we are not vacating. This is alternative business models to achieve our strategic objectives.

Moderator: Thank you. We will take the next question from the line of Mehul Desai from IDFC Securities. Please go ahead.

Harit: This is Harit here from IDFC. Just had a couple of questions. First thing was on the Route-to-Market. You mentioned Punjab and UP so if you can just clarify I mean Punjab especially already the change is happening, or you expect it to happen in 4Q? As well as on the UP part, when do you expect that to start kicking-in?

Anand Kripalu: So let me first make it clear, Haryana actually issued a notification, okay? So Haryana is likely to go. But there are murmurs within the government will it, would not it, will it, would not it, etc. - etc. right? But as of now we are expecting it to go corporation. Punjab will normally follow Haryana. What we do know for a fact in Punjab is that the cabinet of Punjab and following that the Chief Minister made a statement saying there will be a change of Route-to-Market and it is likely to go to corporation route, right? Now that is as hard as we have but you do not have a formal notification from the state of Punjab. As far as UP is concerned all our conversations with the bureaucracy in UP in the excise department and so on and actually senior ministers in UP we have got confirmation that it is going to happen, that there is going to be a change of the existing monopoly model and it is going to most likely move to either a corporation model or it is going to move to a more democratic number of wholesalers compared to the monopoly that is there today. This is what we are hearing. I believe that the probability of a change happening in both Punjab and UP is high but then you have to watch the states as we are watching it too.

Harit: Yes, absolutely. On all these changes in your view could possibly be effective 1st April, right?

Anand Kripalu: That is our understanding because that is the new excise here. Haryana notification is very clear. Run at about 1st April therefore we have taken hard calls on what we are doing to manage credit risk and so on and so forth, right? Punjab there is no hard date yet, so we are just playing cautious and trying to collect any old outstanding we have so that we are not caught on the wrong foot, right? UP for the moment this business is usual. But there is some down stocking that the current monopoly wholesaler is doing also in anticipation of a possible change.

Harit: Okay, understood. And the second question was on the price increases. Now, would it be clear to assume that the only price increase left to flow through in our numbers is one in Telangana? The rest of it would have reflected in 3Q?

Anand Kripalu: So Telangana has to fully reflect into the future. I am not sure, if A. P. was fully reflected in the quarter or not. We will have to just see what will be the effective date and so on and so forth, yes? And most of the others would have reflected in the quarter. Having said that there is new excise cycle starting 1st April and we are aggressively working with state governments to get price increases now in other states as well. So it might not impact this IndAS fiscal, right? But come April, we should be seeing more states beginning to give price increases that will help next fiscal.

Moderator: Thank you. We will take the next question from the line of Himanshu Shah from HDFC Securities. Please go ahead.

Himanshu Shah: Just one question. Are we anticipating any change at the retail level in any of the states?

Anand Kripalu: So in none of these states, no. So West Bengal is same retail, Haryana same retail, Punjab same retail, UP private retail but there may be some changes in terms of who are the people who own the retail. There has been a change in retail in Jharkhand and Chhattisgarh. In my opening comments I talked about six states in RTM change, Jharkhand and Chhattisgarh has been done already. And Jharkhand and Chhattisgarh there has been a change to government retail.

Himanshu Shah: Okay. But outside of these six states we are not foreseeing in any other markets whether government taking over retail or any other changes?

Anand Kripalu: No, we are not anticipating government taking over retail and there aren't many more states left to become corporation now really after this. So hopefully at some point this has to stop.

Moderator: Thank you. We will take the next question from the line of Anuj Bansal from Ambit Capital. Please go ahead.

Anuj Bansal: I just wanted to understand when West Bengal had change in Route-to-Market we possibly did not see too much impact on the numbers, but with Haryana now changing the Route-to-Market there has been a perceptible impact. So has there been any difference in the way the two states have handled the change? And also, going forward what is your anticipation in terms of Punjab, UP is it likely to be more the West Bengal way or more the Haryana way?

Anand Kripalu: West Bengal was unique in the sense that or different because West Bengal has a distributor model which is like the FMCG distributor model and there was zero credit. So we have zero credit risk in West Bengal during the transition, right? That is a very-very important difference. Now having said that, was there no impact of the transition in West Bengal? Not true. There was impact because retailers were getting credit from distributors earlier. Today retail has to buy on cash in advance, make a RTGS transfer to the corporation and then go and pick-up their stock, right? So the whole finances of the retailers they have to bring in more money, they have to go and pick-up the stocks themselves, there were door delivery happening earlier, etc. - etc. So there has been short-term impact during the transition. But then the impact has been phased over a long period of time up-country West Bengal moved into Bevco, The Beverages Corporation over a period of three months, four months, five months and Kolkata (Calcutta) Metro has happened now over the last couple of weeks, okay? So they spread the transition in the states, so you did not see the whole state moving over night. So that is the fundamental difference between Haryana, right where you have a credit risk and therefore you are going slow and these are private parties, right who will run away so that we want to be sure that you are able to collect your money. That is true in Punjab as well. Now in UP it is one party, okay? So you can decide whether the credit risk is lower or higher but it is one party. But we believe that party is big enough and has enough skin in the game for the future as well through retail and other avenue to where actually we will be able to manage the risk a bit more. But the transition of the amount of pipeline that a monopoly wholesaler or wholesaler is carrying when it moves to a different model pipeline tend to shrink and then rebuild back when it goes to the new model and that transition we have to be able to manage in any Route-to-Market change.

Moderator: Thank you. We will take the last question from the line of Chanchal Khandelwal from Birla Mutual Fund. Please go ahead.

Chanchal Khandelwal: Just one thing, if I look at realization per case by that time if I look at nine months realization per case for Prestige it is just up 2.8% whereas Popular is up 8%. So can you explain it to me because if premiumization is happening and the price increase you have got this would have been a better number? And also in Popular, do you account for the franchised fees, that is the reason the realization per case is up 8%?

Anand Kripalu: So why do not we do one thing, we will take away this question and if you can just connect with Richard, we will give you as much clarity as we can, work it through and just explain it back to you, yes. You can just send an e-mail, we will try and get you the response.

Moderator: Thank you. That was the last question. I now hand the conference over to Mr. Anand Kripalu for closing comments.

Anand Kripalu: Well, I just want to thank all of you for the time that you have taken to join this call and also the incisive question. Like I said earlier, we are not happy with our top-line performance this quarter indeed neither of you are. But we are really pleased about the progress of our P&L and the shape of our P&L and we do believe that this business has never been stronger. And once we are done with some of these short-term changes that happen in this industry, I think we are going to have a period of stability and hopefully far stronger consistent performance. So that is what I just wanted to say. Thank you very much for your time.

Sanjeev Churiwala: Yes, thank you very much.

Moderator: Thank you. Ladies and Gentlemen, on behalf of United Spirits Limited, that concludes this conference call for today. Thank you for joining us and you may now disconnect your lines.