"United Spirits Limited Q1 FY20 Results Conference Call"

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Moderator: Ladies and gentlemen, good day and welcome to the United Spirits Limited Q1 FY20 Results Conference Call. As a reminder, all participant line will be in the listen-only mode. And there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing '*' then '0' on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Anand Kripalu – Managing Director and Chief Executive Officer, and Mr. Sanjeev Churiwala – ED and Chief Financial Officer from United Spirits Limited. Thank you and over to you, sir.

Anand Kripalu: Thank you very much. And very good afternoon everyone and a very warm welcome to F20-Q1 Results Call. Before we open up the lines for Q&A as we typically do I just wanted to provide a context of our results that we announced last evening.

As you may have seen in the published results, net sales grew 10% in the first quarter partially benefitting from a one-time sale of our surplus scotch stock in the UK. Excluding that underlying net sales grew 6%. The Prestige & Above segment grew 9% on a solid base of 19% net sales growth in the same quarter of the previous year. The Popular segment grew 3% adjusted for the operating model changes, enabled by a softer March in Karnataka. In addition to the broad slowdown that the entire FMCG sector is grappling with, for us this quarter was also impacted by dry days and restricted store opening hours resulting from the general election.

Moving to the other lines of the P&L COGS inflation as well as adverse price mix significantly impacted gross margins for the quarter which came in at 47.3%. Despite that I am pleased that we have delivered a like-for-like or indeed underlying EBITDA margin of 16% for the quarter which is an improvement of 407 basis points versus the previous year that is after adjusting for the bulk sales and one off restructuring cost in the base. So, the 407 basis points is just pure underlying like-for-like margin improvement. Most of this margin expansion has been made possible through savings in our operating cost as well as the saving benefit of marketing investments for the quarter.

Adjusted for the one-off restructuring cost, staff cost for the quarter were lower by 19% and other overheads were lower by 11% compared to the previous year. While we reiterate the fact that one quarter does not make a trend these numbers give us confidence in our ability to mitigate gross margin pressure through operating efficiencies as we have guided in past calls. While the reported reinvestment rate for the quarter was 7.7% of net sales; after adjusting for the one-time sale of bulk scotch which obviously does not warrant A&P, the reinvestment rate was 8.1%.

Additionally, we trimmed down our marketing investment in light of the ongoing general elections and our marketing investment will kind of normalize over the course of the coming year. During this quarter we also launched McDowell's No. 1 Platinum campaign which featured Vicky Kaushal during the ICC Cricket World Cup both on Television as well as on OTT which is specifically Hotstar.

We continue to stay focused on financing cost efficiencies and interest cost for the quarter were down 11%. As a consequence of this our profit after tax for the quarter was 197 crores up by 143% mainly as a result of improved operating performance and to some extent lower interest cost.

Looking ahead while we continue to monitor the broader economic slowdown and its potential impact in the overall consumption in the near term, we will have to wait and see if there is any specific impact on our category. Having said that, we remained committed to driving consistent and profitable growth of our business and for us really top line and consistent margin improvement are important and therefore I would like to reiterate our medium term ambition to grow the top line by double digit and improve our EBITDA margin to mid to high teens on a consistent basis in the medium term. So, with those opening comments I am going to open up the lines for questions and we will address the questions partly from me and partly by Mr. Sanjeev Churiwala who is seated next to me.

Moderator: Thank you very much. Ladies and gentlemen, we will now begin the question and answer session. The first question is from the line of Avi Mehta from IIFL. Please go ahead.

Avi Mehta: Just on the Prestige sales growth you saw a very healthy 9% growth in Q1, I just wanted to understand A would you have an estimate of what the growth would be like if you had adjusted for general elections impact and B why are you sounding cautious despite such a healthy performance I mean is this linked to the regular performance that is likely to moderate or it is something that you witnessed in June?

Anand Kripalu: And separately you will also have to tell me why the stock price has reacted the way it has today, but answering your question that you asked me. Listen we are pleased with our performance there is no doubt about that. It is speculative for me to tell you or give you any view on how much is the impact the general elections because it is really hard to read that. I think we are not being pessimistic just to be clear I think we are being realistic because as you have seen with CPG results that are coming out there is a general moderation of growth across categories in the CPG industry and we have seen what happened in automobile and in general on consumer spending. So, I think it is sensible to just say that we are going to keep these things in our minds as we determine our outlook; just to be clear it is nothing more than that and nothing deeper and more insightful in that either.

Avi Mehta: Now because 9% is a very good honestly in this kind of circumstances you rightly pointed out and that is why I was surprised to see that comment that is why sir the second question was on the price increase, have you received any price increase in any state and the second part would it be fair to now argue that the gross margins is bottomed out because all those input cost pressures were kind of reflected in this quarter?

Anand Kripalu: As far as the input cost pressure are concerned, I would say that glass is more or less done for the foreseeable future. There is some recent hardening of ENA prices both grain as well as molasses ENA right and we are seeing a bit of an impact on that. I cannot tell you categorically gross margin has bottomed out, but I will be surprised if it erodes any materially from now on. Now as far as pricing is concerned which is the compensation for the increase in COGS. The pricing environment remains I would say reasonably fertile. We have got almost 15 states in the last quarter which you will agree in an industry like us is not bad at all. We still have a few stubborn states and those are some of the bigger ones where we have not got price increase still and partly it is because of the political scenario in those states and you know exactly what I am talking about, but having said that we have also absorbed a bit of price increase because of certain price corrections that we have taken specifically in the state of Maharashtra in terms of absorbing a very significant tax increase that happen in January. Now I believe that was the right decision for us as a business and the numbers are commensurate to what I am saying and therefore we have lost a bit of that pricing benefit by way of excise absorption. Looking ahead I am hoping that we do not have to absorb any more tax increases and that we will be able to retain more of the pricing that we are getting.

Moderator: Thank you. The next question is from the line of Bhavesh from CLSA. Please go ahead.

Bhavesh: Two questions at the time of Analyst meet you mentioned that the low hanging fruit from cost savings are in the bag and it is only the higher hanging fruits that you will be able to capture, so this quarter the other expenses staff cost all these are high hanging fruits or low hanging in your view and how much of this is sustainable as you go ahead?

Sanjeev Churiwala: I think you asked three questions in one question. So, I think in last call absolutely we have said that look the low hanging fruits cannot be already eaten and now looking at the high hanging fruits and that was Anand’s comment largely to the productivity agenda that we have been guiding over the years across all the line items. So, kind of if you look at our cost absolutely lot of productivity what has happened in the past and given the inflation environment that we are in, we will still look for significant productivity happening in that line because this industry normally would have an inflation impact of 4% to 4.5% we cannot allow that entire inflation to come in P&L so significant work would continue happening over there. Besides that as we also spoke about the other lines of the P&L, A&P lines, staff cost and since you have seen over the last three to four years, significant work has happened in staff cost, in spite of inflation of about 10% every year, it has been flattish or lower, a lot of work has happened around there. Going forward also we will see a similar kind of trend where you will see the other overhead including staff cost only growing in moderation. We should be able to absorb a large part of the inflation impact also going forward. So, absolutely whether it is a high hanging fruit or low hanging fruits, fruits are still there, and we will continue to work on them.

Bhavesh: So, first quarter run rate on staff and others is something that we should be working with for rest of the year or for nine months, right?

Sanjeev Churiwala: No so look we do not want to go and give you a guidance basis quarter-on-quarter. We have always told you to look at on a yearly basis. Best is you have to look at the trend over the last couple of years and try and work out the extrapolation this is that rather than just looking we have got a number.

Bhavesh: Second bit on IndAS 116 impact, can you just highlight which all line items or heads is impacting and the quantum?

Sanjeev Churiwala: Sure in our case it is not big. The overall impact on the EBITDA is just about 50 bps around so and basically it is impacting your other overhead line and the interest line, but very insignificant and small amount and of course the depreciation line. The PBT is neutral because of that. And also have that note to accounts which has the complete detail on that.

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

Abneesh Roy: My question is on the bulk scotch so as you mentioned 57 crore PBT or 97 crore sales, so my question is why this kind of an order happened and why it is just a one off and why it is such a high PBT margins so it is good for the company, but wanted to understand the thought process and what is the impact on the gross profit and any other cost you said A&P for obviously this will be zero, but how is the impact on the gross profit and any other cost item is there any impact?

Sanjeev Churiwala: Okay so good question to ask. Let me give you some background and context then we can come back to the number. United Spirits have been maintaining a UK branch for many years I would say going back up to decade wherein because we have a significant IMFL production here. We need mature stocks coming from a UK branch every year in order to deliver ambitions on a blend for our IMFL. So, we recently took a stock of the current matured stocks lying in a UK branch and basis of that evaluation we came with a working that you have certain amount of scotch which are matured bulk scotch which we do not need immediately in India because our blend profile has changed over the years and hence we decided to sell that scotch. We look for various parties and finally we realized it is best to sell it to Diageo because Diageo needs them. So, we did go down into the market and took quotations around that and basis the evaluation and basis arms length transactions we sold this 97 crores worth of bulk scotch to Diageo. So, this was completely planned and this is kind of also cleaning up on the scotches that we do not need and we will never need in future. Now because these are matured stock lying for ages and years right it did not cost much to us. We are very happy that it resulted into a 60% kind of gross profit, no other impact to any other line item. We are happy that we are able to release 100 crores of almost cash into the business, payback our debt, improve our working capital. So, it is a very good thing to happen and we are very happy that we think looking at a current scotch profile that we have we do have some more surplus that we think we should be able to sell during the year, but that is more one off and hence we transparently wanted to call that out.

Abneesh Roy: Sir just one follow up here so this decision had nothing to do with any slower growth in the scotch portfolio in India, it was just because of the mix change which you have done is that correct?

Sanjeev Churiwala: Absolutely it is just because our blend profile the aging profile that we need is very different and the mature stock that we have in the UK branch. It is nothing to do with the slowdown in fact scotch business is growing. Somewhere at the starting of the call Avi said you guys have been fabulous and we will be very happy to beat your own estimates.

Abneesh Roy: Sir my second and last question is on the P&A you have done a good job 9% growth on in a very high base, so is there any down trading you are seeing within this P&A is a very wide portfolio now accounting for almost 70% of your mix, so is there any down trading you are seeing and is that also impacting the gross margins?

Sanjeev Churiwala: So, down trading in what sense if you can be more clear.

Abneesh Roy: Sir from the higher end of the P&A to the lower within P&A?

Sanjeev Churiwala: No absolutely not in fact in our earlier calls also we said our scotch portfolio is really growing, a scotch premium portfolio are definitely growing. So, absolutely we continue to up trade and continue to work on our premiumization journey.

Anand Kripalu: I just want to reiterate the fact that the premiumization strategy is fully intact and just to underscore what Sanjeev said we have each segment growing faster than the segment beneath it. So, luxury is growing faster than premium, premium is growing faster than Prestige and Prestige is growing faster than Popular. So, there is no gross margin impact because of premiumization not happening at all.

Abneesh Roy: And sir one last follow up on the ad spend so adjusted for bulk scotch your ad spent was 8.1% of the sales which is still lower than the 9% to 10% long term which you have been guiding. So, this was in spite of the World Cup impact being almost fully there in Q1 in Q2 there is little impact. So, in spite of that the ad spend is on the lower side, so could this mean that because now you are also expecting slower growth and maybe Pernod also. So, that overall industry could come to lower ad spend in balance part of the year also?

Anand Kripalu: So, I do not think that is the case just to be clear our ad spend is still very competitive at over 8%. The second thing is that there is a global initiative of Diageo which we also shared in the global capital market with their presentation in May called Catalyst where we are deploying certain technologies and tools to improve the way our ad spends are planned and how the return on those ad spends is measured and basically that is a way of driving significant productivity in ad spend. So, for the same spend we expect to get more bang for the buck or indeed we could get the same bang for the buck at a lower spend. Now we had given the guidance of 9% to 10% and that was just a judgment. This quarter I think we spent a little less because we felt there was general elections and other things and we set it up to spend behind our new campaign on McDowell's Platinum for the World Cup. So, where there was something to be spent on in terms of new, we decided to invest behind that. Now looking ahead there will be productivity that we will look at on A&P and we will also spend at what is appropriate both competitively and what optimal in terms of the P&L. So, where exactly this will land I think it is speculative, but it can be somewhere in that range could be a little less or little more, but this as I have always said A&P spends there is no precise signs of what is the right A&P spend it is management judgment and sometimes you open the purse strings spend a bit more and then you feel you do not need to spend that much and then you tweak back a little or you spent less and you say I am spending little let me open up the purse strings and spent more and we will manage this dynamically quarter-to-quarter, but it will remain healthy and competitive because we believe it is fundamental to our competitiveness and fundamental to category growth.

Moderator: The next question is from the line of Nillai Shah from Morgan Stanley. Please go ahead.

Nillai Shah: I just want to dwell a little bit on the Maharashtra impact I understand what you have done and the reasons behind that you articulated that quite well, but how are you thinking about this strategy in light of two or three things. One is the fact that there is gross margin compression on account of input cost moving up. Secondly the mix impact has not been as strong in the last couple of quarters as was the case earlier and obviously the overall tax structure has gone up quite dramatically, so how do you think about this general strategy of withholding prices in a free state like Maharashtra going forward and is the tap on pricing completely shut or would you explore that in the future?

Anand Kripalu: So, I think it is a very good question and it is something that we are thinking about all the time. Now obviously the intent in our industry is not to absorb tax just to put the intent out there. However, you need to be sensible, practical and competitive depending on a situation that you have to face. Now where in segments and I said it before now for instance I will tell you on BIO Scotch there has been almost no change in pricing in Maharashtra. All our BII Scotch brands there necessitated 15% increase in consumer price and we took all of it. And I was in the trade last week in Bombay and scotch is holding up despite us taking the full price increase. Now in Prestige we have partly absorbed depending on the nature of the brand and the nature of the competitiveness in that segment. Now we remained watchful for every opportunity to take price up. Maharashtra by the way is a free pricing market so the day we feel that the environment is ripe for taking a further price increase we can apply, and we can do that. Now while there has been tax absorption which is not ideal, and I must admit that. The tax increase came after 5 years and because it was steep increase, we felt the consumer shock would be too much and also the competitive environment of such that you could not take the full price. So, the way we are going to play this out is and you are right and the COGS is also hardening and therefore obviously this is going to lead to some kind of gross margin pressure. Now having said that, I just want to say that Maharashtra is still margin accretive to our national average margin even after the absorption. So, as long as Maharashtra grows, grows faster than the rest of the nation it is still margin accretive. So, that is the situation and I think we just have to continue to watch this space closely and look for every opportunity to push price further. So, for instance on Royal Challenge we took a price even though the market never moved and we moved up price by about 5% or so and again I was in the market and I was looking at our performance and honestly the decision was right because the momentum on Royal Challenge stays intact compared to what it was before the price increase even though it got more competitively disadvantaged. So, Nillai we are going to watch this space and we are as hungry for every opportunity to take price as anyone else is and we will not miss an opportunity if we see one.

Nillai Shah: Two small questions is there an opportunity to import alcohol given how benign the global prices are at this point in time and the fact that the Indian prices are moving up only because of the blending policy and secondly could you clarify on the IDBI Bank issue and the latest update on that I know there is a detailed explanation of that in the release, but what has happened with the latest course of events and when do you expect court judgments to possibly come through either ways?

Anand Kripalu: So, I will deal with the first part and then I will hand over to Sanjeev to deal with the IDBI issue. So, we are looking at it we have asked our teams to look at the possibility of importing and I do not think there is still any arbitrage post payment of all duties landed in India versus domestic ENA prices, but we are watchful of this and the moment there is an arbitrage opportunity we will see to it. So, we are just checking the feasibility right now it has not been done historically by the way okay. So, we are just checking the feasibility doing this and see whether A we can do it and B whether there is any arbitrage.

Nillai Shah: Just one point what are the chemical manufactures are already importing alcohol given the steep increase in prices that you are seeing domestically?

Anand Kripalu: So, I will take that away and I do not know if alcohol for industrial purposes it is treated in a same way as alcohol portable purposes. So, domestically the alcohol is the same, but if it goes to the chemical industry or it will go into the potable alcohol industry is treated completely differently. So, we will check this out.

Sanjeev Churiwala: Nillai I will try and answer your question on IDBI and I would draw everyone's attention to the note in our notes to account in a specific note number F that you can see there is a very detailed description on the IDBI matter. Now as you are all aware that historically we have been giving a very detailed note in our quarterly statement as well as in annual report and the background is as you all are aware that we had repaid the IDBI loans sometimes back and also on request of IDBI they had also subsequently paid about 46 odd crores which is held in the books of deposit. We have always maintained that this is a very strong case that we have because there is nothing that IDBI can hold against. We have been able to repay the entire interest, principle as well as penalty whatever has been asked for. In June '19 the recent Single Judge Bench dismissed the writ petition purely on the ground of merit the matter has been remanded back to the civil court. Now this order has been disputed by us and the company has filed an appeal already with a divisional bench of Karnataka High Court basis our management estimate supported by external legal opinion from these senior councils. We do believe that it is a very strong case on merits and we will continue to fight that while we speak possibly our matter has been heard in the court today and hopefully in the evening we should have some news on that.

Nillai Shah: By today evening you said.

Sanjeev Churiwala: Yes of course the matter has been heard in the court today as we speak.

Moderator: Thank you. The next question is from the line of Jaimin Shah from RWC Partners. Please go ahead.

Jaimin Shah: Two questions one is on the COGS and raw material given our mix shifting into BIO and BII, how much impact does our raw material have now at overall scheme of things and again on the Prestige versus the kind of the mass side again the pricing power there is fairly high, so just wanted to understand that because while gross margin down year-on-year on a quarter-on-quarter basis it looks like a small blip**.** So, that is one and other question I wanted to understand on the other expenses right this has been fairly volatile line items in last few quarters, but again I can look at on the year-on-year as on trailing 12 months versus 12 months it steadily kind of coming down, how should we think about on an annual basis as well is it kind of flat is it down because trailing 12 month today is down, but is the guidance kind of flat for the full year that is about it?

Sanjeev Churiwala: Yes so maybe I will try and attempt the question on other overheads and I think you are right Mr. Shah if you look at the trend over the last two years our growth on the overhead has been fairly subdued, we have largely been able to beat the inflation. So, we will only expect the other overhead to kind of grow in moderation and more importantly we should be able to keep on getting the operating leverage year-on-year and that is the way we should be computing it. We will still go and guide you not to look at just the quarterly trend and it is volatile you are very right. The industry is per se volatile and many things happens on quarterly basis which is very difficult for us to determine to kind of put a number to that, but I think we are very consistent in terms of our yearly delivery and as it trend over the last two years we have been very consistent across delivery just not on the overhead and other lines as well as on the staff cost line. So, our request is to look at a trend over the last couple of years and may be extrapolate that, that is a better thing to do.

Anand Kripalu: And on your first question, yes GM has more or less held when you look at quarter-to-quarter basis even though there is a drop versus the same quarter of the previous year and that is because most of the COGS inflation has kind of got factored in barring a little bit of ENA movement that we have seen towards the end of the quarter and it is continuing into the current quarter as well. Now as far as the mix are concerned yes, the mix is moving towards scotch without a doubt, but scotch is still a relatively modest part of our total business and therefore the absolute impact of ENA hardening still remain material. Now once scotch becomes more and more and more that impact will shift, but for the moment it is still very much there.

Sanjeev Churiwala: If I can add Anand on the discussion point on the GP margins in the COGS. I think it is important for a moment to just drawback and see holistically as to how the development is happening. If you remember in the yearly call, we have very clearly said that we have seen a very good progression on the GM margin. We had grown our GM margins almost by 750 bps points in the last three years and now very competitive as compared to the industries and in terms of our benchmarking, but yes, we have been hit this year especially by the COGS inflation is largely around ENA and glass. So, our guidance to the market even last time is that you should not be looking at similar kind of growth in the GM margin profile going forward. It will definitely grow, but very moderate and we will continue to work on growing our EBITDA margin year-on-year and to that extent trying to put sufficient operating leverages across all other line items and that is the way we would request you to look at the COGS and the GM margins as well as the overall EBITDA margin aspirations.

Jaimin Shah: If I can just ask simple book keeping question the 97 crores on the 31st March 2019 was sitting in part of inventory for you?

Sanjeev Churiwala: Yes, it was sitting in inventory and as I explained in the last question, we have now released this inventory, we have received the cash and this cash is entirely gone in terms of releasing our debt.

Jaimin Shah: So, on a full year basis I should be using the kind of adjusted number as of March 2019?

Sanjeev Churiwala: Absolutely you should.

Moderator: The next question is from the line of Prashant Poddar from ADIA. Please go ahead.

Prashant Poddar: One quick one on the response that you gave Sanjeev on the previous question when you say that incremental gains will be more on operating efficiencies and not from gross margin. The gross margin decline that we have seen in this quarter because of certain events and which you are likely to gain back over a period of time. So, are you saying that the base quarter of last year from there the gains would be modest or is it are you referring this quarter as the base quarter?

Sanjeev Churiwala: Just again trying and reflect some of you did mention that this quarter's GM margin is perhaps the lowest and yes if you kind of open up the last 8 quarters you would see the GM margin profile and the trend and it has been declining over the last three quarters almost. Even last quarter to your point we delivered 46.5% GP margin and this quarter is again 46.5% kind of yes, GP margin to that extent is holding this quarter in spite of the inflationary impact which is a good sign. When we say we will see a GM margin kind of just growing moderately normally we give a yearly trend we do not kind of go back and just say this quarter or the previous quarter. So, our thinking, philosophy is if we have delivered a certain GM margin profile last year we would kind of want to see a certain moderate improvement in that profile rather than just seeing the quarterly GM margin.

Prashant Poddar: So, despite first half is probably being relatively tougher for the full year you would attempt to improve gross margins from last year?

Sanjeev Churiwala: We would attempt to, but as Anand said we will not exactly be able to pin down or the inflation will go how the ENA and bottling prices could move. I think our focus this year definitely is kind of growing our EBITDA margin as we have reiterated in the past. Without getting into which line item saying will we kind of still deliver a GM margin enhancement or not, the absolute idea is to kind of deliver EBITDA growth as well as EBITDA margin growth and to that extent we will play across all the line items.

Prakash Poddar: Sir the other one is on market shares vis-à-vis Pernod, how would we be doing nationally and are there markets where you are winning or losing? I am sure there would be market you are winning the markets where Pernod is winning, but overall how is it looking in terms of market share?

Anand Kripalu: I do not have this specific information on how we are performing versus the category or specifically versus another competitor. Obviously, any performance will be a mix bag of pluses and minuses, but the bigger opportunity for us is to deliver category growth leading to profitable growth. So, for us managing the top line and increasing our bottom line as you have seen us do this quarter remains paramount because it is at the end of the day that is what is going to deliver shareholder value and that is the way we are looking at this and the big opportunity in this market is the category growth. It does not matter; it is not a winner takes all markets at all and that is our philosophy in terms of how we are approaching our business.

Prashant Poddar: The question is because we saw Pernod being aggressive in price cut or price behavior in the past to defend its turf because they saw course correction since Diageo took over, are you still seeing high competitive action in terms of pricing?

Anand Kripalu: So, there is competitive intensity without a doubt and they are all worthy competitors right at the end of the day and you have to take them seriously. Now, I can tell you this where we have seen aggressive price competition, there are some cases where we have said we will not follow and we will protect margins and the jury will be out in the long-term on what is the right decision to be taken. So, at some time, you might take a call to say I will forsake the short-term to get the long-term and we have taken a few decisions like this and I think this is a question of management philosophy at the end of the day and what is your long-term growth in terms of if is it volume at any cost and that is how the old USL used to be versus profitable growth and driving Premiumization and holding margins and clearly our strategy is the latter.

Moderator: Thank you. The next question is from the line of Harit Kapoor from Investec. Please go ahead.

Harit Kapoor: I just had two questions firstly on the Andhra Pradesh side, just could you give us any update on how the situation is there we understand that the government is going to take over the retail as well so any update would be helpful?

Anand Kripalu: Yes, that is right there is a notification to that effect. So, the good news is that prohibition is not immediately on the horizon. If there is prohibition at all then it is some distance away. Yes, the fact they have notification to take over retail so government will take over retail. Like I said our business I have said this earlier somewhere between 3% to 4% contribution in the state of Andhra Pradesh so it is worth putting that into context. So, I will tell you we have had mixed experiences in dealing with the government retail. There are some states where we have actually done very well dealing with government retail and dealing with them compliantly but yet, building shares and building our business and there are some states where we have got seriously compromised. Now we are hoping that we will use all the lessons of how we have done it right as and when Andhra Pradesh rolls it out. Now the state government what they have also done is that they have also announced the closure of belt shop which are typically unauthorized shops, but they have also announced that they want to increase revenue from excise duty. If you look at this whole picture together, I would say that the opportunities in Andhra Pradesh if you have the right strategy in place to deal with government retail should remain intact.

Harit Kapoor: The second question was to Sanjeev and this was largely about the IDBI issue, just a hypothetical that it does not work in our favor does that mean that we get the 600 odd crores money back that we had given earlier to kind of release these shares I just wanted to understand the technicality?

Sanjeev Churiwala: What we have given is a little lesser than 50-odd crores which is lying in deposit, but again this is hypothetical because we are trying just not to get the 50-odd crores, we are trying to get back all our assets that has been pledged. So, we have a large cause and we think we are in a strong wicket.

Harith Kapoor: Because you had said that your note said that it had deposited a sum of 628 crores initially with the bank?

Sanjeev Churiwala: The note says 459 million so maybe you are confusing million with crores that is 45.9 crores so 46 crores.

Moderator: Thank you. The next question is from the line of Pulkit Singhal from Motilal Oswal AMC. Please go ahead.

Pulkit Singhal: I can understand lot of cost items you have some discretion kind of when it comes to A&P and may be even other expenses, but when it comes to employee expense when I look at the last five quarters I have seen it move from 170, 140, 160, 170 and now again 140. I am just trying to understand what is there in your inherent business model that allows for such variability of employee cost on a quarter-on-quarter basis which we actually do not see in any other company?

Sanjeev Churiwala: Yes so, no other company would also reduce 80 factories to 50. No other companies will have such large severance cost plans for the year. So, what happens is while we have not planned agenda around the organization effectiveness the timing of the payment and the provisioning it only determined as to how we progress during the year. So, as a result you will always see this quarter-on-quarter movements sorry for that hard remarks, but that is how it is, but what is most important for us and what is more satisfying for us is that also among a very few companies to your point that over the last three to four years we have been able to manage a staff cost very significantly well. So, if you see the staff cost efficiency that we have driven over the last three years you can calculate for ourselves we have been able to really achieve significant efficiency around that.

Pulkit Singhal: No, absolutely staff cost have been flat for almost last three years which is incredible, but this year run rate seems to suggest the major decline because even based on this quarter even if I were to see the residual quarterly run rate, it would be way higher at 180 crores which does not seem to be the case, so should we building a staff cost decline over the next one or two years and what would that be driven by as you talked about factories being reduced?

Sanjeev Churiwala: Maybe I will give you a simple answer to solve your issues. Just look at the last couple of years run rate and just try and build that. A whole idea has been to kind of ensuring that we significantly mitigate the inflation around staff and other overhead cost. We will continue to kind of do that so our growth in staff cost and other overheads in the subsequent years and this year also as a full year will only be in moderation and you should not be looking at the quarterly run rate because what happens is in the previous quarter there will be some additional expenses one of severance cost sitting, this quarter it will not be sitting. So, as a result quarter-on-quarter is very difficult to kind of draw a trend line and my request is you look at on the full year basis and draw your projections this is of full year number and not on a quarterly number.

Pulkit Singhal: Do you have enough run rate for this for the next three years or is it because it is already been three years so how much run-rate do we have here?

Sanjeev Churiwala: Well I will not get into specifically telling you how many years in future, but of course if you are looking at the near-term we will definitely try and ensure that we significantly have productivity across all the line items in order to kind of keep it flattish or just grow it in moderation. So, we should still be able to beat inflation largely.

Pulkit Singhal: Sir lastly on the Popular it is heartening to see some growth on the Popular side as well although on the lower digit size 3%-odd, I just wanted to understand the strategy here, have we reached the level of Popular sales that we are comfortable with and we want to grow the business or should we expect that to be flattish again for the next two, three years that has been in the past, how should we look at Popular going ahead?

Anand Kripalu: I mean our best understanding of the growth of Popular is that it is flattish as a segment and this quarter the numbers look better because the previous quarter there was some softness and this is particularly to the state of Karnataka. Every year in Karnataka they normally have an excise increase in the first of April so trade buys up a lot in March this year did not happen. So, they did not buy that in March. So, therefore, April has come back to normal sales all right. So, it is not there is some underlying momentum change to be absolutely transparent about it. So, our guidance on Popular remains what it was in the past, no major shift.

Pulkit Singhal: So, lastly on asset sales and your ability to improve working capital will the pace be faster or slower than what has been in the past on both these aspects?

Sanjeev Churiwala: Well first answer on the asset sale absolutely, we will only sell what we have and we have been selling significant asset in the past three years that you have seen in our books already. Going forward we too have some assets that we want to sell, but most of the assets will largely give us cash rather than the profits that is on the asset side. On the working capital as on the previous call I mentioned that over the last three years we have been able to significantly reduce our average working capital and of course that needs a working capital as well and almost like 1000 bps points reduction over the last three years. I think we are now standing where we are very competitive because we are a very capital-intensive industry when it comes to working capital the cost of Rs. 100 of sales that we need to do almost Rs. 300 of spend has to happen in the managing working capital because the Rs. 1 item there is Rs. 3 of excise payment. So, as a result since we want to continue to grow our top line our average working capital will only now reduce in a moderation. We will still look at efficiency and effectiveness as we move forward, but you will not see the kind of steep reduction that you have seen in the last three years.

Moderator: The next question is from the line of Amit Sinha from Macquarie. Please go ahead.

Amit Sinha: Firstly, I would like to get some commentary from you on the overall competitive intensity and not only from the Pernod but also what we have seen in the last two years is some of the new brands ramping up in that space, but is it a fair assumption that you know in the last few months incrementally the competitive intensity has come off. We understand that the last quarter was because the restrictions on the A&P spend you would not have been able to spend, but how should we look at this kind of A&P spend coming off in kind of cognizance with the fact that the competitive intensity in the market would have come off at the same time?

Anand Kripalu: So, honestly, the A&P spend does not come off because of the competitive intensity coming up. This was just our plan and ability to spend at a time when we believe there was a bit of uncertainty in demand. I just want to make it clear that we are committed to spending competitively in fact more than competitively. As far as A&P is concerned, we will keep looking at opportunities to spend that money as efficiently and as effectively as possible. Now to your earlier points yes there has been an emergence of some local brands in the market and some of them have done well. In some cases, they have done well because the product offers are good and, in some cases, people have invested discontinuous amount behind those mixes to drive it. Now in any category any business if a new person comes and it is willing to really bet the bucks on a brand you will get traction. So, we are seeing some traction there. I think the big question is how many of these will sustain long-term and continue to build shares when that kind of discontinuous spent start tapering off and that I think time will tell, but the good news about the industry is that the opportunity for growth is still limitless almost and the more people invest, the more new products that come in, the faster this category is going to grow and as long as we are able to get a reasonable share of that category growth and do that profitably I think it augers very-very well for our business and that is the way we see it. In fact, there are very few industries where you have as dominant presence of major players as you see in AlcoBev. If you look at most of the categories in CPG there are many more players vying for share of that category and I think there are few more competitors arising on the scene here as well and I am not sure that is always bad news that is all I am saying.

Amit Sinha: Have you already started seeing this disproportionate investment in terms of media spends and promotions coming off incrementally?

Anand Kripalu: Actually, I have not read it that closely to be honest with you. There might have been some softening or coming off as you call it of competitive media spend on some of the launches that have happened, but I have not got the hard data on media spend from the tracking the company yet to really tell you with certainty.

Amit Sinha: Secondly again, you mentioned efficiency in the A&P line, so should we expect a lower overall A&P spend for the full year FY20 I mean I understand that you have not revised your guidance for A&P, but this efficiency should ideally should lead to lower spend on an absolute number?

Anand Kripalu: So, it may it may not honestly so I cannot give you enough clarity as far as that is concerned. I think the important thing is we are always watchful of how much we need to spend to stay comparative segment by segment brand by brand and we are going to do that be competitive and then do that most efficiently. Now Diageo has unlocked through its global tool called catalyst significant A&P productivity around the world and we are hoping to harness a good part of that here too and we have now put that tool into action in the business. So, all our plans for the prospective years are able to go through the rigor of catalyst. Now what exactly it throws up in terms of productivity and so on I think we just have to watch the space, but I do not think you should be alarmed in any major way that we are going to start cutting or be surprised that we are going to spend too much more we are going to be in this zone give or take a bit.

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

Arnab Mitra: I had just one question on the bulk scotch so I think Sanjeev mentioned that you still have some incremental excess bulk scotch if you could help us with some sense of what could be the value there and what is the timeframe in which you would want to kind of sell this off if you have taken a decision on that?

Sanjeev Churiwala: Yes, so we want to sell them off in the next 6 months to a year time, but because it is one-off, we would not like to land up in getting any projections on that. My request to all of you would be not to consider in your future workings and kind of allow us to happen when it happens because your projections should be more business as usual rather than considering one off.

Arnab Mitra: Last question on noncore asset sales so you have had some noncore assets sales last year, but the big ticket residential property is in land and things like that I think those have not gone out, so do you see FY20 being a year when possibly some of this happens or our market conditions still very bad and this could get pushed out into the further years?

Sanjeev Churiwala: Market conditions are definitely bad and most of you have heard of that because the real estate has scant. For us it is important to just to get a good realization across all this asset class and largely industrial and some of the residential property that we have. We do not think any of this asset will give us profit now and we are kind of only eying at cash and we will just sell it at the right time when we are able to get the good price for them.

Moderator: Thank you. Ladies and gentlemen due to paucity of time we will take the last question that is from the line of Chirag Lodaya from Valuequest Investments. Please go ahead.

Chirag Lodaya: Sir you mentioned 15 states gave price increase in last quarter, so what would be the portfolio level increase in pricing?

Anand Kripalu: I am not sure we are getting into that kind of granularity honestly and like I have said in the previous call in the previous quarter that these increases range from very small to kind of medium numbers, but it is tough to say what is the impact on the portfolio total, but I want you to also keep in mind the fact that while we have got this pricing we have also had a bit of pricing reimbursement going back into excise absorption particularly in Maharashtra which is spoken about and the pressure on COGS that is there and continues to some extent, but it is hard for me to give you a number of what is the percentage that we have achieved yet. We will take a look at it specifically and see what is going to be on an annual basis and if we can share it then we will, but I do not think we have shared that kind of number in the past.

Chirag Lodaya: And any big state you are looking I mean expecting any price increase in near-term?

Anand Kripalu: We are expecting in all the balance states, but whether we will get it time will tell. We certainly are trying our best to see what we can do in Karnataka. Now Karnataka everybody knows what the political situation is right now and really is the government functioning and will they take any big decision or not, but that is the real big one and really that we need to try and find a way to unlock honestly.

Chirag Lodaya: Sir you mentioned in Prestige & Above also higher category is growing much faster so we are seeing Premiumization as a trend strengthening further, but when I look at realization per case it is in last two quarter realization per case number is not moving up, so what exactly is happening on that front, price increase is there?

Sanjeev Churiwala: On a like-for-like comparison absolutely the per case moving up and yes we do have these moments and especially the Maharashtra excise policy increase that we had in January and we have been not been to pass on the full price increase to that extent when you compares yes it does undermines some of this effort, but yes absolutely the luxury per case will be definitely higher than premium and premium is higher than Prestige.

Anand Kripalu: So, what I can tell you is that when you take into account Maharashtra as well and despite whatever price increase we have got. When you let all these off there is still negative pricing pressure on the business at this point in time.

Chirag Lodaya: And sir lastly on this gross margin so you mentioned you are focusing on improving overall EBITDA margin I understand that part FY19 your gross margins were around 48.8%, Q1 was 46.5% adjusted and you are still talking of maintaining this kind of operating margin or improving slightly that means H2 you are hoping to have a much better gross margin, is the understanding correct?

Sanjeev Churiwala: We don’t get to a specific number our attempt absolutely would be to keep on improving slightly right. To that extent on a like-for-like basis even the GM margin are slightly better than the previous quarter not the corresponding quarter last year, but yes I think there is this pricing issue and the inflation issue that we are facing right now and we will have to see how it plays that around. We will have to play across the other line items and still deliver our EBITDA and

EBITDA margin aspirations because finally what matter is you know the top line and the bottom-line delivery rest is all the line items have been needed to play around.

Chirag Lodaya: And bookkeeping question depreciation for the quarter was 50 crores, should we take this as a run rate going ahead?

Sanjeev Churiwala: Should be around that because the depreciation kind of almost flattish and growing very marginally. So, I think look at again the yearly trend.

Chirag Lodaya: Historically, we are in the range of 35 to 40 crores and this quarter is 50 so just trying to understand?

Sanjeev Churiwala: Yes, so I think it also impacts us slightly by the IndAS 116 numbers and if you go to the notes like that breakup is there.

Moderator: Sir, would you like to add any closing remarks before we close the call.

Anand Kripalu: No, I just want to thank everybody for their continued confidence in the company and their sharp questions as always and I look forward to staying connected.

Sanjeev Churiwala: Pleasure talking to all of the folks. Thank you very much.

Moderator: Thank you very much, sir. Ladies and gentlemen, on behalf of United Spirits Limited, that concludes this conference. Thank you for all for joining us. And you may now disconnect your lines.