



“United Breweries Q2FY13 Earnings Conference Call”

November 9, 2012



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Moderator

Ladies and gentlemen good day and welcome to the United Breweries Q2 FY13 Results Conference Call hosted by IDFC Securities Ltd. As a remainder for the duration of the conference all participants' lines will be in the listen only mode. And there will be an opportunity for you to ask questions at the end of today's presentation. Should you need assistance during the conference call you may signal for an operator by pressing * and then 0 on your touchtone phone, please note that this conference is being recorded. I would now like to hand the conference over to Mr. Nikhil Vora of IDFC Securities. Thank you, over to you Sir.

Nikhil Vora

Thanks Lavina, welcome you all to this Q2 Earnings Conference Call for United Breweries. It's obviously a very eventful day for the United Breweries Group or UB Group rather. So I will hand it over to Guido, CFO of United Breweries and Poonacha to make the opening remarks and then will start the floor for Q&A, over to you Guido.

Management

Thank you Nikhil for this introduction. To go into the results for a second quarter we achieved a volume of 30 million cases for the quarter against 29.4 million cases in the previous year registering a growth of 2%. If you compare that to the industry growth in this quarter which was about 17% you will see a significant difference, this is on account of two items, one is some destocking in the channel, so if you look at growth on our secondary sales they were around 4%, the remaining difference is coming from Tamil Nadu and Andhra Pradesh. Andhra Pradesh, we are in the last quarter wherein we will feel the impact of the change government policy which was changed a year ago and in Tamil Nadu we continue to feel the impact going forward also, this was indicated in the first quarter after the governments changed this ordering pattern wherein ordering is more on quota based system and not based on brand pull.

So we can now take up those markets where we actually grew in line with the industry, keeping our market share constant at 52.5%, that performance gave us sales for year to date of 75 million cases, amounting it to growth of 9% for the year to date. Moving to brands and markets Kingfisher Lager continued to decline in line with the market down 4.5%, the continued trend of mild beer de-growing and strong beer, growing is unchanged. Strong grew between 11% and 12% in the quarter. If we move to the Northern markets we saw a strong growth of 21% in Q2 largely on the back of the salience shift to the strong beer segment. And the two star performers were Rajasthan and Uttar Pradesh growing respectively with 29% and 16%. It is also good to see that the Delhi market is bouncing back with the growth rate of 15% after being flat for the previous quarters.

Haryana still continues to do decently with high single digit growth in Q2 after reversing the de-growth of 14% in the first quarter. Moving east growth there 16% up in Q2 after bouncing back to growth in Q1 with a 53% growth on the back of easy comparables, on account of changes in duty structure & impact of State elections in the last F/Y.



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West Bengal was largely flat after strong growth in Q1. There was a growth in the state of Bihar, while we are up over 40% after restricting supplies in the previous year the situation has now stabilized. Orissa was slight blemish the market had a slight de-growth mainly on account of competitor activity as well as some delayed approvals for new brands.

So we go to Karnataka and the rest of the markets in the south. Karnataka grew very healthily by over 15% in the second quarter and acceleration over Q1, as in Q1 we had constraints supplies, so the market has been quite buoyant. And Kerala showed small de-growth of 8% after growing strongly in the first quarter. Then we come to Andhra Pradesh, there we were flat which is basically combination of decent market growth and the effect of having higher market share in Q2 of the previous year, before the change in policies. Tamil Nadu we were down by 45% in the quarter, so that's a very material impact and that's purely on account of policy change by TASMACH where they changed the ordering pattern from secondary sale to quota allocation to the various Breweries. So that's impacting us a lot so much so that there is nothing much we can do about it.

In the West, market growth continued at 15% in Q2, largely fueled by growth in Maharashtra and Madhya Pradesh while Goa was flat during the quarter.

In the quarter we expanded the footprint of Heineken across the country by launching the brand in number of additional states and its gaining major traction and taking share from competition.

So we now move to net sale revenues (NSR) you might have seen in the announcement, we showed a growth in NSR for the quarter of about 18%, if you would break that down about 8% of that would be account of consolidation. So 10% is like for like growth out of which 2% is coming from volume growth and 8% is from very healthy increase in realization. I think that's the good news in these quarterly results where we benefited from good state mix with the high value states growing strongly, as well as price increases coming through and some benefits from ongoing mix improvements program. I think that's one of the healthier rates we have seen in the past few years.

Moving to cost of goods sold, a variable cost for the quarter is at around 38.8% of net sales versus 48.6% net sales in the previous period. So that's a result of about 10% which is on account of inter company purchases in the previous years, when one of the mergers was not completed yet. And so that I think is what you need to see through a bit and I will give you some indication on the performance impact of consolidation later on. So if we look at the various items of cost of goods sold we have seen barley prices higher by about 15% during the year which is largely barley from the harvest of 2011 and later in the year will start using the barley from this year's crop which will be bit more expensive so we see some increase in cost in the remainder of the year. But the good news is that the benefits from our UB logo bottles have offset to very large extent inflationary pressures in all the other cost lines and limited our



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cost on goods sold increase on the like for like basis to below 3%. So that's very healthy result and now we have very good flow back from our patented bottles which enables us to limit the new bottle injection that we do. Then moving to fixed cost, in staff costs there was in last year a number of one off costs which were not repeated in Q2 so there you see only a marginal increase, which is on account of consolidations. On like for like basis the personal costs are slightly declining.

So we move to EBITDA, we achieved an EBITDA of 112 crores for the quarter being 53% higher compared to the quarter of last year, very healthy growth for the quarter. Moving onto to interest, interest for the quarter amounted to only 17 crores versus 19 in corresponding quarter of last year, which is largely the result of the capitalization of interest incurred on setting up our Greenfield in Nanjangud as well as re-financing of number of more expensive loans, so that's brought down our interest cost significantly. So profit before tax went up by 74% to Rs. 51 crores of course for the quarter and profit after tax at a similar level up 75% to Rs. 34 crores.

The impact from consolidations on the top lines revenues, net off purchases reported for their first six months of the year is 2073 crores out of which the impact of consolidations is about 500 crores so an organic revenue of 1673 crores against 1436 crores in the previous year. And if you look at EBITDA reported around 316 crores for year to date, Rs. 40 crores is coming from consolidation and Rs. 275 crores would be the organic EBITDA against reported last year of Rs. 226 crores. Similarly reported PBT for this year of 199 out of which inorganic is 19 so organic PBT of 180 versus 136 for the previous year. So even if we strip out consolidations we see a very healthy growth on the back of good price realization and controlled cost for the quarter. So that brings us to the balance sheet, our overall debt stands at 928 crores as of end of September, as against 1041 crores in March 2012. So that was the result of the strong cash flows that helped reduce working capital limits that more than negated the debt raised on significant CAPEX spend.

So that concludes my introduction let's move to any questions if there are.

Moderator

Thank you very much sir, participants we will begin the question and answer session. Our first question from the line of Mr. Krishnan from Fortune Equity Brokers, please go ahead.

Krishnan Sambamurthy

Question on your balance sheet there appears to have been decline in trade payables over March by 56% to 171 crores and 28 % decrease in inventory as well over the same period to 5.1 billion. I guess the periods are not comparable but has there been a significant deterioration in the net working capital, what's your reading on that and what's the expectation going forward?

PA Poonacha

No actually I didn't get the question can you repeat the question?



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- Krishnan Sambamurthy** Yes over March there has been a 56% decline in trade payables and there has also been a 28% increase in inventory levels over the period, March over September, I know this is not directly comparable, but there appears to be an increase in the net working capital, what's your reading on this and how do you see this going forward?
- PA Poonacha** Trade payables, because we are using the discounting route it would not be classified under trade payables. Now if we left the same under trade payables and used our working capital limits then what would happen is our interest cost would have been much higher. Now trade financing through trade bills gives us a clear 100 basis points advantage over working capital borrowing. Net-net actually there is no such thing as trade payables dropping.
- Krishnan Sambamurthy** Okay and on the inventory side?
- PA Poonacha** On the inventory side yes inventory vis-à-vis you are talking about March right?
- Krishnan Sambamurthy** Yes.
- PA Poonacha** March '12 to September '12 we have currently off season and we would have picked up sufficient stocks for next 8-9 months of barley. This would inflate the holding level currently as we move into December-January it would come to more controllable levels.
- Moderator** Thank you. Our next question is from the line of Gaurav Desai from Nomura, please go ahead.
- Gaurav Desai** Just one question given that Heineken now own 100% of Asia Pacific Breweries does that change a relationship with Heineken in any way?
- Guido de Boer** No it does not. We basically have no commercial relations with APB so there is no change in activities now.
- Moderator** Thank you our next question from the line of Mr. Gaurang Kakkad from Religare Capital Markets, please go ahead.
- Gaurang Kakkad** My first question is in the Kerala market you said that we have seen around 8% de-growth after the strong growth in Q1, so any specific reason which is attributable to this?
- Guido de Boer** Not really there was some delays in new brands registration as well as some market disruptions in the route to market but nothing specific to worry much about.
- Gaurang Kakkad** So even the market has de-grown or it is like we have seen some problems?
- Guido de Boer** I think the market was generally weak.
- Gaurang Kakkad** And sir any price hikes that you have taken in Q2 in any of the markets?



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- Guido de Boer** In Q2 we got some price increases in Tamil Nadu where our price increase has come from number of new variants. In Orissa where we had applied for price increases quite a while ago, but now there were actually approved. So a number of quite descent price increases have come in and that has lead to the good improvement in the realization.
- Gaurang Kakkad** Okay right, and sir just one thing on other operating income like the last year it was around 5% of the total sales and like this year this year it is closer to 9-10% of sales, so just wanted to know like what's led to this increase and if you can share the constituents of the same.
- Guido de Boer** So if you look at the other income actually for the quarter it has decreased significantly.
- Gaurang Kakkad** Sir other operating income?
- Guido de Boer** Operating income?
- Gaurang Kakkad** Yes.
- Guido de Boer** That's to a large extent items like spend grain, etc., which are bi-products from beer. So that's has improved in realization wise.
- Gaurang Kakkad** Okay. So larger part of this increase roughly 50% is attributable to this?
- Guido de Boer** There is obviously also consolidation impact, that the consolidation of the MBIL and APB Breweries, etc has resulted in part increase. Apart from consolidation there is an improvement in the realization.
- Swati Nangalia** Just had couple of questions. First is with regards the United Breweries stock which is held by United Spirits. Today the deal between Diageo and United Spirits has been announced, so just want to know your thoughts on any likely transaction on the treasury stock of UB which is held by USL.
- Guido de Boer** I can't comment on what share holders do with their shareholding in UBL.
- Swati Nangalia** Sure, this is more from the perspective that if Heineken has the first right of refusal on that stock, so is there any likely transaction?
- Guido de Boer** What I am saying I cannot comment on what USL will do nor I can comment on what Heineken will do. They are both shareholders I can only comment on what's in UBL's control?
- Swati Nangalia** Sure fair enough. Okay, my second question pertains to our volume growth. We have seen some pressure in the AP market. Could you throw some light on what has changed in this market in the current quarter and what is the outlook for the second half?



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Guido de Boer So in AP basically nothing has changed. Market share is very stable at just below 50% which has been so in the last few quarters. You might recall that there was a government policy in place and at that time we had close to 70% which was then reversed. So this is the last quarter that we will feel the impact of high base. So if you would look at the next quarters we will not have that impact anymore because our market shares are very stable in that market.

Swati Nangalia Alright. Lastly, in the other income component there has been significant decline on a sequential basis, so what is that pertaining to?

Guido de Boer We use to get interest from the advance given to the promoters of Balaji Brewery and that was accounted for over there. Now that it has been materially repaid that's source of income won't be there anymore. But that's to an extent offsets by lower interest cost.

Moderator Our next question from the line of Ashit Desai from B&K Securities, please go ahead.

Ashit Desai Considering that the problems in AP and Tamil Nadu, do you expect to grow inline or higher than market growth rate in second half?

Guido de Boer So Andhra is getting into one year cycles, so the impact should stop and however, the Tamil Nadu impact started on in Q1 and actually there are we don't see much improvement there. The government continues it's stance of favoring breweries not based on the brand pull but they just allocate based on quota to each and every brewery. So until the government changes that stance I don't see much change forthcoming. And given that such a large market where we are severely impact it, I expect that the impact will continue.

Ashit Desai But Tamil Nadu market did see problems last year second half also. I mean has it hit on you now, if you can give some volumes sense on that?

Guido de Boer Yes absolutely, it started a bit last year in Q4, but it has really started to impact Q1 this year and then the majority's impact is being felt now. So we were in volumes down by 45% in the quarter.

Ashit Desai Okay and this is the case even for our nearest competitor?

Guido de Boer I don't know who you mean with nearest competitor.

Ashit Desai Are they procuring lower from SABMiller also?

Guido de Boer Basically SABMiller was not present in Tamil Nadu so they don't feel the impact of that. Its basically local players that exist in the market with unknown brands.

Moderator Thank you. As there are no further questions I would like to hand the conference over to Ms. Swati for closing comments.



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Swati Nangalia

Thanks Lavina. I would like to thank the management team of United Breweries for removing time for this call. Also thanks to all the participants for joining in today. Guido would you like to make any closing comments.

Guido de Boer

No, not apart from thanking you all for joining this call and end of the week and wish you a Happy Diwali in advance.

Moderator

Thank you, on the behalf of IDFC Securities that concludes this conference thank you for joining us. You may not disconnect your lines. Thank you.