



“United Breweries Limited Q2 FY 2015 Earnings Conference Call”

November 13, 2014



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Moderator: Ladies and Gentlemen, good day and Welcome to United Breweries Q2 FY 2015 Earnings conference call, hosted by IDFC Securities Limited. As a reminder, all participant lines will be in the listen-only mode, and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing “*” then “0” on your touchtone telephone. Please note that this conference is being recorded. I now hand the conference over to Mr. Harit Kapoor from IDFC Securities. Thank you and over to you Mr. Kapoor!

Harit Kapoor: Very good afternoon to everybody. On behalf of IDFC Securities, I would like to welcome you all for to the Q2 FY 2015 Conference Call of United Breweries. We have representing the senior management of United Breweries, Mr. Henricus P. Van Zon, CFO as well as Mr. Poonacha. I would like to now handover to the senior management to make their comment, which we will be followed by Q&A. Over to you, Sir!

Henricus P. Van Zon: Thank you very much Mr. Kapoor. Ladies and gentlemen, all very much welcome to this telephone conference regarding the results that we have published this morning.

Let us start with stating that we indeed had a very good quarter the Q2. If you to get the gross and at the kind of improved percentages, one should not forget that the previous year Q2 was a not good quarter for the industry and for the Brewery.

For the industry I want to remind you we have monsoon very heavily this year, this quarter we had basically of course also monsoon, but we had a monsoon that started a couple of weeks later. Last year we had a very sluggish economy. This quarter in particular the Q2 we had seen some improvement in the economy which certainly also benefited from industry. Last year specifically for us as United Breweries we had an issue as you remember probably very well in Maharashtra where we were for six months allowed to only use new bottles and not to use our returnable and returned bottles. So previous year was not a good first half year and certainly not a good Q2.

This year we had seen a good improvement in the first quarter and further very good improvement in the second and this we are also very happy that we have been able to for the total of the first half year report volume growth of 10% which is slightly above the industry growth that we have driven from the volume increases but also as a result of several price increases in different markets, been able to show a revenue increase of 15% that is on the topline and due to the effects that I just mentioned in the beginning, this has resulted in a very healthy increase in the EBITDA of 35% and further kind of increase in the profit after tax.

So that is basically as a start of for the conference. Let us open the floor for questions.

Moderator: Thank you very much. We will now begin the question-and-answer session. The first question is from the line of Sonali Salgaonkar from Axis Bank. Please go ahead.



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- Sonali Salgaonkar:** Good afternoon Sir and many congratulations for a great set of numbers. My first question is now that United Breweries had shown a very good growth in primary volumes. How much has been the industry growth in the same quarter and the breakup of volume and value if you could give it.
- P A Poonacha:** The industry in the second quarter has grown by 18% and we also have the 18% is the secondary growth, so while primary growth is 24%.
- Sonali Salgaonkar:** By secondary and primary sorry what do we mean by that?
- P A Poonacha:** Well we sell beer into the market that is primary growth and that is a primary sales volume. Secondary growth is the sale from the distributor or from the government corporations to the retail, which is the growth we use to track market share.
- Sonali Salgaonkar:** United Breweries has also grown by the same quantum is it.
- P A Poonacha:** Yes, United Breweries has grown in line with the industry.
- Sonali Salgaonkar:** Sir my second question is you have mentioned that some markets saw price increases, so could you please tell which markets have seen price increase and approximately by what quantum.
- P A Poonacha:** Fairly has seen some price increases we have got some price increases in Tamil Nadu and some price increases in West Bengal and in Rajasthan.
- Sonali Salgaonkar:** And if possible could you share the quantum of that approximately.
- P A Poonacha:** No we could not give.
- Sonali Salgaonkar:** Sir my third question is now how much percentage of the recycle bottles do we use as a percentage of the total bottles.
- P A Poonacha:** No, we do not share that because there is an industry common bottle and also our logo bottle that we use so as such we do not give out this information as to what bottles we are using.
- Sonali Salgaonkar:** But just try to assume that it is a significant amount.
- P A Poonacha:** Yes it is.
- Sonali Salgaonkar:** Sir my fourth question is about your Greenfield Breweries in Bihar you are saying it is on track so what is size and what is its capex?
- P A Poonacha:** The Capex would be in the region of 200 Crores with a scalable capacity of 1000000 cases a month, to start the unit with anyway between 500000 to 700000 cases a month and based on



industry volume, there on with very small capex we can scaled it to be to a 100000 cases Brewery.

Sonali Salgaonkar: Sir my last question is with reference to the balance sheet numbers is it fair to assume that will end year FY15 the working capital at almost the similar levels of FY14?

P A Poonacha: No highly unlikely because if you see there is a growth in volumes this year. But since in the last two years the growth in markets with government corporations taking up a largest share of our sale and debtors, it is likely that we will be growing working capital level from this year-end compared to the last year-end.

Sonali Salgaonkar: So sir do we see a sizable amount of increase in the sales.

P A Poonacha: No, while we basically are working towards trying to maintain it but it is highly improbable task.

Sonali Salgaonkar: Okay sir and with the cash coming in with the strong cash position that we are building in because of the revival in the business are we looking at debt repayment or would that be deploy towards capex over the coming years.

P A Poonacha: No, see whatever internal accruals we have we temporarily get the working capital facilities so we get an interest break and as and when capex is needed we has a policy fund from internal accruals 25% we borrow 75% long-term funds which comes at a fairly competitive rate considering now the ECB windows open all told hedged ECB cost are far lesser than working capital rates so we use them so that the overall cost of borrowing is very competitive.

Sonali Salgaonkar: So essentially we could look at a certain amount of debt repayment over the coming year's right.

P A Poonacha: Yes we do plus whatever capex is there we also would take long-term funds to fund 3/4th of that amount also.

Sonali Salgaonkar: Just one last question, but is on the ground are you seeing a revival in the consumer sentiment and do you think the sellar growth that we have witnessed in this quarter could be a ongoing phenomenon in the coming quarters as well.

Henricus P. van Zon: The answer to the first question is yes there is it appears to be an improvement of confidence amongst the consumer now we have to see for the future, for the near future if this will be sustainable, if the economy will indeed also if takers growth which would lead in these kind of an increase spending power with the consumer.

Sonali Salgaonkar: Sir all the best, and thank you so much for taking my questions.

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



- Avnish Roy:** Sir congrats on the very good show. My first question is on the gross margins, there was a very good improvement quarter-on-quarter so if you could explain that and you see the trend being strong in terms of overall gross margins going ahead and raw material where are we in terms of inventory and overall do you see further softening.
- P A Poonacha:** Gross margins better off than last financial year first half by about 2% points, this as we have said in our facility this primarily due to last year input cost being inflated on account of us being forced to use higher percentage of new bottles. However considering that this year the percentage of usage of recycled or usable bottles are higher than last year whereby we have had some containment in input cost against that we have also had some price increases vis-à-vis last year where by the 2% increase in gross profit percentage, however going forward it is very difficult to sustain this increased percentage, because input cost vis-à-vis last year it is difficult to maintain at this low levels.
- Avnish Roy:** And how is the scenario in barley.
- P A Poonacha:** Yes, Barley we have purchased close to 80% of our annual requirement upfront and the rates that which we have purchased is a little higher than what we purchased last year so as the year goes as we start using newer stock and compared to what we have used last year there would be some increase in the input cost with respect to barley and malt.
- Avnish Roy:** No but that will be on an absolute basis my questions is more if we take the price increase in the three, four states and we take percentage increase so as a percentage of sales there should be a saving even on the barley side right.
- P A Poonacha:** Yes there would be, but then you look at the overall scenario but we cannot predict how the mix would be going forward right so we do not know if the markets in which we have taken price increase if that will grow intend with the industry or the other markets grow so we really cannot say how the percentage GP moves as we go forward.
- Avnish Roy:** My next question on what you said at the end price increase in three, four states that seems to be a bit of higher number of states versus the last two three years average now with Lok Sabha elections done and quite a few state elections also done are you expecting price hikes to be much more pronounced and much more frequent versus the last two, three year average.
- P A Poonacha:** No we have to also look at what the competition is doing and also we need to ensure that we are not to overpriced and wherein our market share come under pressure. So all these considerations we need to take before we will think of taking price increases.
- Avnish Roy:** And could you comment on market share where are we currently and how much is the change in the last six months.
- P A Poonacha:** We are close to 51% and 50% plus we are in and it is in line with what we were for about a year.



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- Avnish Roy:** Coming to demand side in the four regions is there any different trends available and in some specifically in Karnataka and Andhra post bifurcation how are you managing the entire taxation and entire sourcing if you could comment on that.
- P A Poonacha:** We have Breweries in both the states of Andhra bifurcated one Brewery in Andhra Pradesh Seemandhra and two Breweries in Telangana so thereby we are the only player which has Brewery in Seemandhra so we have less cross sourcing than compared to competition.
- Avnish Roy:** So that could give us advantage also in terms of pricing and therefore market share.
- P A Poonacha:** Yes both, not pricing at least it will little crossed by not cross sourcing and with respect to faster movement of beer within the state yes it will gives us some advantage.
- Avnish Roy:** How is Heineken launch now quite a few quarters are done if you could comment in terms of some numbers how many key markets have done any sense on market share at least in the top end how much market share this brand has and in terms of margins if you could comment sir in terms of the overall margins versus the Heineken how much is the difference.
- P A Poonacha:** The Heineken operates in the super premium segment there are very few beers which are at that segment we are currently growing at 50% and we have launched in all major metros and all large cities and we have a very positive trend, yes the per case contribution of Heineken is very high, however as a overall business it forms a very small portion of our business as we stick from that.
- Avnish Roy:** Has it become mid single digit in terms of contribution to sales.
- P A Poonacha:** No we would not comment on that as of now.
- Avnish Roy:** When will you start commenting on that?
- P A Poonacha:** When it becomes sizable.
- Avnish Roy:** And sir your initial comments are a bit different from what other companies are saying liquor companies at least you are saying there is an underlying improvement in demand of course Q2 was also held by base and summers but are we also seeing demand continue to be good even in October month because October many other discretionary companies are doing the trends have slowed down. So could you comment on that part?
- P A Poonacha:** No, what others say I cannot comment on but we do not give forward looking statements so let's wait for the December quarter and then we speak about it.
- Avnish Roy:** And sir lastly on distribution if you could comment in the annual reports you do give a comment but if you could say what is the growth we are looking in terms of number of shops etc. that will be very helpful sir.



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- P A Poonacha:** No we do not give all of the statements Avnish.
- Avnish Roy:** Okay sir thanks and I will come back if I have more questions.
- Moderator:** Thank you. The next question is from the line of Ashit Desai from B&K Securities. Please go ahead.
- Ashit Desai:** I have a few questions. Sir if you could give an idea of what is the average excise increase across markets over the last six months.
- P A Poonacha:** Average excise increase.
- Ashit Desai:** Yes excise tax increases that are resulting in your MRP increases in the market.
- P A Poonacha:** That is an humongous job itself Ashit, they have been increases in Maharashtra last year and they have been increases in so many states.
- Ashit Desai:** No last six months I am asking.
- P A Poonacha:** Yes, whatever it is, last six months they have been increase in lot of states and to get an industry average across the country here we do not calculate it, so it is done always states wise.
- Ashit Desai:** Can you give is there any state where you seen a very steep excise increase which is affecting demand.
- P A Poonacha:** No this year we have not see in the last six months.
- Ashit Desai:** And just to confirm you gave some volume number in the beginning 18% secondary growth and 24% primary growth is this for industry or you.
- P A Poonacha:** This is UBL and the secondary growth of the industry also has been 18% so we are grown in line with the industry's respect to market share, because it is a secondary volumes and the secondary sales which is used for market share.
- Ashit Desai:** Okay got it and the Tamil Nadu price increase is also for beer just wanted to confirm that.
- P A Poonacha:** Yes.
- Ashit Desai:** And what is the scenario in Tamil Nadu now in terms of procurement and what...
- P A Poonacha:** No change.
- Ashit Desai:** What would be your market share now in Tamil Nadu?



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- P A Poonacha:** Close to 30%.
- Ashit Desai:** And just one last question on Capex you said you will be spending 200 Crores on Bihar Brewery how much of this is already spent and how much you will be spending this year and next year.
- P A Poonacha:** We will spend the entire amount this year we have already spent 140 Crores 60 more we spend in the next, by the time we close this financial year.
- Ashit Desai:** So the increase within fixed assets that I see in your numbers is because of Bihar or it is because of acquisition of Pacific Spirits.
- P A Poonacha:** Both.
- Ashit Desai:** So part of the 140 Crores was spent last year also.
- P A Poonacha:** Yes.
- Ashit Desai:** And what will be the capex next year.
- P A Poonacha:** In line with what we have this year, with a variation of about 15%, 20% max.
- Ashit Desai:** So what will be your capacity utilization now?
- P A Poonacha:** Currently little less than 80%.
- Ashit Desai:** Because if I look at your numbers that seems like you added some 5, 6 million hectoliter over last three years the volumes have been largely more or less flat so the 80% looks a little bit on the higher side.
- P A Poonacha:** No it depends on how you take capacity because that time when the excise department changes whether we can operate three shift or one shift so we taken now with operate one shift then your capacity as it is comes down right that is how we need to look at it.
- Ashit Desai:** Thanks a lot sir I will come back for more questions.
- Moderator:** Thank you. The next question is from the line of Avi Mehta from IIFL. Please go ahead.
- Avi Mehta:** Hi sir congrats on a good set of numbers. Just wanted to understand two housekeeping bits in the note that you have mentioned could you please explain what do you mean by reversal if the selling and distribution expenses what is this link to.
- P A Poonacha:** Yes because sales and distribution expenses a large portion is freight cost now the freight cost in the brewing industry includes one cost of the transport itself and two the amount charge to the



transporter on account of the truck waiting at the corporations depots to be unloaded. Now that we called demurrages, now when we invoice beer in each invoice there is an approximation made to the extent of freight cost based on past trends of either demurrages or the freight cost. So on a quarterly or half yearly basis we take an analysis of what is the actual spend vis-à-vis provisions and whatever extra provisions are there are reversed and these reversals are not shown as the income separately it is cutoff against the cost head itself thereby the auditors are made a statement that the any distribution expenses are net of reversals.

Avi Mehta: So if I understand these reversals are known as when their truck comes back or is this like a long activity time I am in understanding...

P A Poonacha: No, when do we reverse it is when then we get the actual invoice and the actual invoice vis-à-vis the provision is lesser it is an excess provision we reverse the excess provision that is the reverse on account of freight cost.

Avi Mehta: Sir in that case and two questions then sir as if I were to ex this freight cost in terms of sales promotion expenses are we see some kind of moderation in percentage of sales on as we go forward or we will kind of maintain it or do we increase it any kind of given other sense this is basically kind of gives us the sense that the cooperative intensity.

P A Poonacha: No, sales promotion expenses as a percentage of sales would be online of what we are and do not see a situation where it comes down as a percentage of sales.

Avi Mehta: So it should remain something similarly on annual basis that would be a correct understanding. Sir and the second bit is on the gross margin but if I understand correctly the first quarter we had the issue of the recycling of what is in Maharashtra one of our key markets now that kind of went through that has been reversed so was the full impact seen in this quarter or is there some benefit that would still not visible.

P A Poonacha: No the impact on cost was in the last financial year first half now that impact was not there this year so this half year vis-à-vis last first half year showing a better trend because the impact was there in the last year on cost and this has not there.

Avi Mehta: So this and lastly sir on the employee cost bit would there this be the quarterly run rate going forward and what are our internal one half what would they be sir.

P A Poonacha: No there are one half's so the second quarter payout should be the payouts for the quarter wise.

Avi Mehta: Sorry I did not get that sir.

P A Poonacha: The second quarter payout would be the payout for the next three quarters.

Avi Mehta: So this is the run rate that we should kind of take going forward.



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- P A Poonacha:** Yes.
- Avi Mehta:** Okay sir I will come back in the queue if I have any more questions. Thanks a lot.
- Moderator:** Thank you. The next question is from the line of Arnav Mitra from Credit Suisse. Please go ahead.
- Arnav Mitra:** Just one question on your cost side what are the trend you are seeing on glass prices and with the crude prices coming down is there scope to for glass input cost to come down or are you seeing inflation on that side.
- P A Poonacha:** It will not come down but it may not be as inflationary as it was in the past considering that crude oil prices are stabilizing.
- Arnav Mitra:** And in the last six months have you seen any increase in glass prices or it has been largely stable.
- P A Poonacha:** Largely stable.
- Arnav Mitra:** Okay thanks sir that is it from my side.
- Moderator:** Thank you. The next question is from the line of Harit Kapoor from IDFC Securities. Please go ahead.
- Harit Kapoor:** Sir just one thing, I just wanted to check with you on the competitive intensity you already spoke about it in the last six months close to one year your markets shares have remain more or less in the 50%, 51% range however in the market you also seen activity by MNCs so I just wanted to understand has there been any new entrance which would have gain share versus any of your old competitors and how is the dynamic playing out, we have clearly not loss market share.
- P A Poonacha:** We have not lose market share, we would not want to name brands but some new entrance are gaining and some are loosing so in between them there is a movement.
- Harit Kapoor:** And is there any specific state that you wanted to call out as to where it is largely across the board.
- P A Poonacha:** No there are specific states where new entrance are making a mark especially in Delhi and Mumbai.
- Harit Kapoor:** And lastly on price increases are there any other large states over the next six months the industry is in negotiation with the state controlled organizations for price increases or do we feel that what is happened over the last six months should be more or less it was at least for a while now.



- Henricus P. van Zon:** Basically you can say we are always looking at opportunities for price increases and as Mr. Poonacha said also assessing them in the context of development of the market also and now the positioning of our brands vis-à-vis the completion and all the products for that matter so you could say there is always possible price increases in the pipeline on a quite regular basis.
- Harit Kapoor:** One last thing from my end is that over the last five years you seen operating margins move up from about 10% odd level to about 14% last year it is largely be driven by the work which you have done in terms of cost as well as the reasonably good volume growth and gross margin expansion so I just wanted to understand what could be the next leg which will drive improvement in profitability for united brewery not a six month one year thought process more of three to five year kind of process.
- Henricus P. van Zon:** That is a very tough to respond now, the only thing we can say about that is, that of course we will do our at most to further improve this and the matter will I say the extent in which will be successful will depend on many, many factors.
- Harit Kapoor:** Sure and anything in the last one year or from a excise perspective or a tax perspective that makes you believe that in or any state is there any anecdotal evidence that spirit have taxed at a differential rate versus beer over the last year any state that you could call out.
- Henricus P. van Zon:** You mean that excise changes have been different.
- Harit Kapoor:** Lower for beer versus spirit in the last one year anything that we could call out on.
- Henricus P. van Zon:** No not in very particular.
- Harit Kapoor:** Okay so I will come back in the queue.
- Moderator:** Thank you. The next question is from the line of Ashit Desai from B&K Securities. Please go ahead.
- Ashit Desai:** Hi sir just two more questions. If you can give us split in terms of volumes what are your contracted and owned volumes.
- P A Poonacha:** Approximately 80% is own 20% is contract.
- Ashit Desai:** And with the due two new Breweries in Bihar, Rajasthan how would that change.
- Henricus P. van Zon:** Depends on the demand from the government and it depends on where demand will take place, because not only just a matter of figures it is also mater of change in mix place part of the country which speak about etc.
- Ashit Desai:** And any savings that you see from these two Breweries.



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- P A Poonacha:** Yes we would see savings because then there will be change in freight cost because currently we do not have a Brewery in Bihar, but in Rajasthan yes also because we are moving in some beer from other states of Rajasthan it will be some savings in respect to logistic costs.
- Henricus P. van Zon:** And in for duties.
- Ashit Desai:** Okay, thank you sir.
- :** Thank you. The next question is from the line of Avnish Roy from Edelweiss. Please go ahead.
- Avnish Roy:** Sir on the salary cost you said Q2 will be the run rate by why if there a 17% quarter-on-quarter increases what drives that.
- P A Poonacha:** That is the quarter where we give the annual increase and also it includes the new manpower we have taken onboard with a new Brewery coming on Bihar and in specific...
- Avnish Roy:** And in terms of new Breweries any more planned in the next two, three years which you want to divulge at this stage.
- P A Poonacha:** No.
- Avnish Roy:** Not, because there is no requirement or you do not want to divulge.
- P A Poonacha:** We do not want to divulge.
- Avnish Roy:** And in terms of Kingfisher strong how much is the percentage coming from this is still a very large section coming from this only and any numbers if you can share.
- P A Poonacha:** I can give you approximate that because 82% of the industry is strong and we are 51% of the strong industry and Kingfisher is the largest strong brand we have so you can approximately workout what the size of the Kingfisher strong is...
- Avnish Roy:** And sir Kerala if you see it is going to systematically cut down on liquor consumption so are we also worried on that if you could elaborate on that.
- P A Poonacha:** Yes, it is not that we have not worried but also it is not a major impact on our business also because as revenue and as the profitability it does not form a very large percentage of our revenue and profit.
- Avnish Roy:** Sir market share in Kerala lower than your overall 6%, 7% market share.
- P A Poonacha:** It is higher than our cross the country average it is higher than that in Kerala.



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- Avnish Roy:** But margins in Kerala are on the lower side right.
- P A Poonacha:** Yes.
- Avnish Roy:** Sir one last one you said in Delhi, Bombay new players are doing and taking some market share from other players so and if you could tell what different are they pricing it lower or they are coming at premium and so they are able to create that excitement and doing lot of activation on ground etc. and could that can be long-term risk to you also right because these are the two main markets so can you give more color on why this is happening and why you are not that worried.
- P A Poonacha:** As of now we are maintaining market so we are not really worried about that.
- Avnish Roy:** No, so if you could comment on what is happening, are they getting market share by pricing or it is a new brand so they will get some share.
- P A Poonacha:** I really do not know how they are doing things in the market we have not on to that level but then we do what is needed to protect our market share in our brands.
- Avnish Roy:** And sir if I read our quarterly results which has come out of course there is a seasonality which has benefited you but underlying are you seeing a shift from liquor to beer and you said even overall you also have seeing positive trends emerge even if we knock off the seasonality impact so why are beer companies going faster than liquor in terms of the listed entity at least what is your sense is there a shift happening from liquor to beer or that is too early to call out, because the data has been pointed.
- Henricus P. van Zon:** It would be very early to kind of comment on such a statement in a positive sense it is not really kind of no real clear trend visible.
- Avnish Roy:** And sir all these pickup in sports tournaments' we have always seen that whenever the world cup in cricket etc. happen now what we are seeing is other sports also kind of getting very good viewership are you benefiting already in those specific few cities is there a pickup on those days is that a reasonable growth driver at least on those base in those cities, for example the current football league is there and then kabadi league was there earlier is there some benefit you are getting from that.
- Henricus P. van Zon:** Not yet we have noticed.
- Avnish Roy:** Okay sir that is all from my side thank you.
- Moderator:** Thank you. As there are no further questions I would now like to hand the floor over to Mr. Kapoor for closing comments.



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Harit Kapoor: Thanks. On behalf of IDFC Securities we like to thank the management of United Breweries as well as all the participants' on the call. We now handover to the management for any closing comments!

Henricus P. van Zon: Thank you very much. I want to thank everybody for his and hers participants and the interesting questions being blow out forward. Thank you very much. See you next time.

Moderator: Thank you. On behalf of IDFC Securities, that concludes this conference call. Thank you for joining us. You may now disconnect your lines.