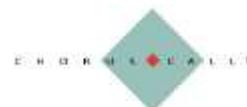




“United Breweries Limited
Q1 FY2021 Earnings Conference Call”

August 17, 2020



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Moderator: Ladies and gentlemen, good day, and welcome to the United Breweries Q1 FY2021 Conference Call hosted by IDFC Securities. 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 phone. Please note that the conference is being recorded. I now hand over the conference over to Mr. Mehul Desai. Thank you, and over to you, sir.

Mehul Desai: Thank you, Aisha. Good evening, everyone. On behalf of IDFC Securities, I would like to invite you all for Q1 FY2021 earnings call of United Breweries Limited. From the management side, we have Mr. Berend Odink, CFO of United Breweries; and Mr. Poonacha from the Investor Relations team. I will hand over the call to Mr. Berend for his opening remarks, and then we can take up the Q&A session. Over to you, sir.

Berend Odink: Thank you, Mehul. Good evening everybody, on the call. Thank you for joining today. I hope everybody is safe, doing well, and today we will discuss the Q1 results, and I will start with providing commentary along with a few slides, and after that, we will open it up for questions.

So, on the results highlights. It is clear that Q1 has been an unprecedented quarter, severely impacted by the pandemic and related lockdown and restrictions. Net sales for the quarter were down 75%, and the company posted an EBITDA loss of 94 Crores, against the context that Q1 is normally the peak season for the beer industry. Interest expenses were down 7% versus prior year.

If we turn to Slide 4, just to recall that there was a full lockdown in place until May 4. Opening up and restrictions in place differed state by state, but common is that on-trade outlets were closed for the full quarter and continue to be closed today.

UBL volume for Q1 was down 77%, moving from 100% down in April to 57% down in June during the quarter.

On the production side, the breweries have put in place all COVID-related measures to ensure all guidelines are strictly adhered to. We continue to observe local restrictions and temporary lockdowns from time to time.

On the taxation side, some state governments imposed COVID-related taxes, which have negatively impacted the industry. Subsequent tax reductions have happened in Delhi and Orissa.

Our volume performance by region is depicted on slide 5. March volumes down 71% with higher



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decline in Delhi due to the severe initial COVID tax, which was subsequently reduced in early June while states of UP and Haryana performed relatively better. In West, also the 79% decline, with broadly similar decline in all the main markets. East was a 90% volume decline due to the imposition of high COVID tax in West Bengal and Orissa. Orissa taxation was reduced early July, while today, no over-the-counter sales in Orissa are happening.

In South, there was a 77% volume decline. Karnataka and Telengana volume trend was ahead of the company average while no sales in Andhra Pradesh due to the low demand and state policy measures. There was a stronger decline in Kerala due to the extended lockdown and introduction of mandatory online preordering mechanism.

The net sales breakdown is shown on slide 6, which, besides the negative volume, there was a positive price mix impact, but the main element being both positive price and state mix in more or less, equal size.

The EBITDA breakdown on the next page shows the main impacts being volume-related and hence reducing the gross profit and gross margin. This was partly offset by a reduction in personnel expenses by 6% and other expenses by 63%, but due to negative operating leverage, resulted in an EBITDA loss of 94 Crore.

Turning to the slide on outlook and summary. The company has and will continue to manage all elements of cost and capital investments in light of the uncertain demand. Active cash management resulted in net debt up by 120 Crore at the end of Q1 versus the prior quarter. The industry outlook is uncertain with negative macroeconomic growth outlook and continued direct and indirect impact from COVID-19 measures.

Overall, UBL is well positioned to navigate the current circumstances with a leading market position, strong brand portfolio and a very robust balance sheet. The company continues to be optimistic about the long-term growth drivers of the industry and is committed to strengthen its market position, while leveraging newly emerging opportunities such as home delivery.

With that, we will be happy to take your questions.

Moderator: Thank you very much. We will now begin the question and answer session. The first question is from the line of Abneesh Roy from Edelweiss. Please go ahead.

Abneesh Roy: My first question is on the home delivery. There are companies like HipBar where some of the liquor



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companies have investment and now e-commerce companies are tying up with these kinds of operators. So, are you present on such service providers like HipBar? And do you also have plans for investing into similar kind of operators?

Berend Odink: The opening up of home delivery for also the beer industry is a very positive development. So, we actively support the new business models. It is early days. I mean, we will not directly invest in the sense of partnership or ownerships or any of those kinds of models, but definitely, on the commercial side, we operate with a number of these companies to make sure this is set up in a viable way and I think the long-term opportunity is there. So that is something we support.

Abneesh Roy: Sir, what is your initial reading on home delivery in Jharkhand, it has been reversed in states where it is still continuing. How would be your performance versus some of the other industry players? I know it is a very volatile period, but in general, qualitative comment?

Berend Odink: In general, you see across the states, different participants, different models. I think over time, this will definitely emerge and evolve. So, the jury is out as to what will be the best model, but I think there is a very active interest from various e-commerce players, but also many industry participants. There are many things going for it to evolve into a long-term opportunity. So again, it is early days, but promising longer term prospects.

Abneesh Roy: Sir, my second question is on the consumption in the pub, bars, etc. So, anything globally you are doing, which you are also doing in India, for example, liquor companies both Pernod and Diageo in India, supporting the pub whenever they open in terms of the very tough time they are facing. So, in whatever way they can support, they are supporting. So, are you also looking to do that? And any other business tactics from other parts of the world, which you are planning to bring to India when this opens up?

Berend Odink: Yes. Obviously, we are very actively in constant touch with other markets across the world. We see very different models emerging, and there is, I would say, a lot of creativity in terms of measures, social distancing, but also supporting pub owners, operators as to make sure there is a conducive environment that is totally safe, but also brings back people together. So those kinds of ideas and best practices, we definitely have onboarded, and yes, we have prepared plans as and when on-trade is allowed to operate again to support this as well.

Abneesh Roy: And sir, 2 follow-ups here. What is a pushback to government here because now everything is almost open, malls are open, most other conventions are open now. So, what is the timeline you are getting from the government, different governments? And what is the pushback?



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And secondly, are you seeing some shift because now consumer is obviously at home. So more of family consumption may happen. So, do you see that as a positive and that as a silver lining from medium, long term, that change in the habit?

Berend Odink:

Yes. So, your first question, I cannot really comment on the rationale for the unlock measures and what will be done at what stage. I mean, we come with proposals, and we think we have viable plans as to how things could operate, but what will be in the next unlock measures, etc., I cannot really judge.

Definitely, there is a point on home consumption. So indeed, I think that is the silver lining that more and more this gains traction, consumer behavior will not kind of change overnight, but again, something we definitely have supported in the past and we continue to do even more so in the sense that this is more and more of an opportunity that, drinking at home a beer, with family, with friends, I think it is socially more and more accepted and on the back of COVID really an additional growth point.

Moderator:

Thank you. The next question is from the line of Pavan Ahluwalia from Laburnum Capital. Please go ahead.

Pavan Ahluwalia:

Just wanted a little more color on the mild versus strong mix. Why is it that strong declined more? So that is one question. My other question is just from a longer-term standpoint, if you look at the evolution of the beer industry around the world, there has been the rise of craft beers and niche beers everywhere. Any thoughts on how you are tackling that in India, where obviously, we have a very strong flagship brand, and we have the ability to introduce products from the global portfolio. How do we plan to address the inevitable emergence of maybe regional brands or niche brands targeted at particular sort of subsegment of the idea that we would try and develop some on our own? Would we look to acquire emerging brands? Any thoughts from that would be appreciated.

P. A. Poonacha:

Yes. I mean, there are 2 parts to your question. The first part is why mild has done better than strong in these tough times. As you see that a large section of this premium and super premium segment that we are currently having brands are in the mild, and most of this superior segment has grown vis-à-vis drop in the other brands, and strong, which is largely your Kingfisher strong, which is about 60% of our volumes has been hit on account of this closure and the lack of opportunities for people to consume this kind of segment has dropped.

Pavan Ahluwalia:

And another way of saying that is you are saying poorer people have been more hit and therefore, this being kind of discretionary consumption for the poor has taken a very big hit?



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P. A. Poonacha: You cannot say poor. I mean, it is like the large majority of Kingfisher strong is consumed in locations, which have been shut. For example, in many retail outlets, they used to allow consumption on the location, even though it is against excise rules, but even with the opening up of this retail outlets, consumption at that location is not being allowed now considering social distancing norms. So, this has affected the opportunity to consume. Not many people in this country can carry alcohol home. So, these retail outlets also allow consumption there. Now, even if we are opening up on outlets, this consumption is not being allowed, I answered the first one.

Regarding the second one, yes, we have this in our portfolio, as you know, that we have launched beers, which is in response to this new emerging craft beer, which is, by and large wheat beers, and we will address this segment as and when it becomes relevant, which we are currently doing.

Pavan Ahluwalia: Thank you.

Moderator: Thank you. The next question is from the line of Himanshu Shah from Dolat Capital. Please go head.

Himanshu Shah: Just a couple of questions. Sir, first, can you provide some outlook on how July and August have been panning out. You called out that June was 57% down year-on-year in terms of volume. So, some color on how it is recovering July and August?

Berend Odink: Yes. I think as things stand on today, it is too uncertain to provide really, outlooks or expectations. From our company side, we look at any kind of scenarios and trigger points as to how to make sure we are competitive and ready to serve the market as the industry demand will develop, but yes, I think we see that it will take time for demand to recover and it is linked to the overall development of the pandemic, lifting of restrictions and the overall consumer sentiment.

Himanshu Shah: Sir would like to qualify out quantitatively some number, like it would be 30%, 40% over versus last year or pre-pandemic level or even...

Berend Odink: No. I mean, we shared the numbers month-by-month for Q1. For Q2, we do that when its the time and the place. I think overall, it is an uncertain market, as we have stated in the release. We have seen restrictions come and go. I mean, Karnataka there is a weeklong lockdown in July in certain parts of the states, and other elements, we have seen a bit of good news that, for example, in Mumbai, over-the-counter sales are now possible. We have seen actually today in Chennai, a lot of trade opening up. So yes, it is, I guess, steps forward, steps back and probably that is all related to how the pandemic will develop in the months to come.



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Himanshu Shah: Okay. Sir, related to this, is it possible to provide some color on volume or value mix and region wise at least? You have provided year-on-year decline in each of the regions, but what will be the contribution of each region, either in terms of volume or value, if you can provide some color? On an annualized basis also it will work?

Berend Odink: We do not provide further details. I mean, we shared, I think, the relevant inputs in terms of the regional volume performance and highlighted some states that were more positive or more negative. Besides, the overall price mix you have seen on the top line. So, I think taking that in totality should give you some insights as to what happened in Q1.

Himanshu Shah: Just, one more question. The gross margin decline has been quite sharp, both year-on-year and quarter-on-quarter. So, is this due to the inflationary pressure on our key raw materials that is glass bottle and barley hop, etc.? Or is it more to do with state mix or combination of what, some color if you can provide on that?

Berend Odink: Yes. Actually, it is more the latter. So, this is really about state mix and the brewery mix as such. In terms of input costs, actually, the bottle, the malt costs were more or less flattish in the quarter. So, it is really about state mix and some component also of low utilization, so you get inefficiencies in the production and in energy, etc. So that has been impacting the gross margin for Q1.

Himanshu Shah: Okay. Sir, just 2 more questions. One is, we have seen sharp decline in other expenses year-on-year, 63%. So, is it purely due to the volume decline in business? Or there are some cost rationalization initiatives also, which will continue in future, basically, which will sustain in future, even as volumes recover gradually?

Berend Odink: It is both. So, some parts are linked to volume, but also some parts are definitely around cost management. So, a lot of the discretionary spends have been brought back, commercial expenses. I mean, if there is a lockdown, obviously, we are not continuing the same level of advertising, etc. So, it is a mix of both.

Himanshu Shah: Okay. Sir, anything you would like to comment on cost management, like what would be potential savings that we may accrue in the future?

Berend Odink: Yes, I am not going to share an absolute number because I hope you appreciate the market and how it evolves is very dynamic. So that is how we also look at our costs and our advertising and our expenses. I mean, when trades open up, we will then definitely support that with appropriate programs to get people back, get their confidence back, but yes, as to how and when that will happen,



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that is very uncertain, but definitely, again, we are looking at all scenarios, make sure we tailor our cost to how the market space is evolving.

Himanshu Shah: Yes Sir, just last question, Capex outlook, if you can provide for the year. Generally, we used to spend 250 Crore to 300 Crore, last 2 years were on a higher side. So, some color if you can provide on Capex for FY2021 and 2022?

Berend Odink: Yes. On the Capex, the last 2 years were around 400 Crore, a little bit of north of that which included quite some capacity expansion as well. Obviously, that part has been suspended. So, for this year, we are closer to a figure of 200 Crore, but within that, there is a fair share of projects that have been initiated before COVID. So, will we be finalizing as circumstances will allow it. It is brought back.

Moderator: Thank you. The next question is from the line of Aditya Soman from Goldman Sachs. Please go ahead.

Aditya Soman: So firstly, in terms of nonalcoholic beer, any update? Have you seen sort of an improvement in mix, given that, that segment has been sort of more open than the alcoholic beer?

Berend Odink: For the nonalcoholic, yes, we posted a 30% revenue growth in the quarter. So that is encouraging despite, of course, a full lockdown, but overall challenges in the marketplace, particularly some good trading on the e-commerce platforms. So that is picking up quite well and we are pleased with that progress.

Aditya Soman: And in terms of, is this now being sold across the country? Or is it in specific states, Sir?

Berend Odink: Sold across the country.

Aditya Soman: And that is both brands, right, so you have got the Radler and Heineken?

Berend Odink: Yes, this includes Heineken Beer 0.0 and SKUs under the Kingfisher Radler umbrella.

Aditya Soman: Excellent, and one more question on sort of production. To what extent is your production capacity normalized, I mean, in terms of, I understand the capacity utilization could be low just because demand is lower, but are all your factories running? And could you run them to full capacity, if needed?

Berend Odink: Yes. So, we have resumed all operations. As you can imagine, from time to time, depending on the local situation, there could be curtailments or restrictions on production, but we do not have any



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unfulfilled demand. So, across the whole network, we are able to supply the market as the demand is there.

Aditya Soman: Understand. So, when demand normalizes over the next few quarters, the supply side would not be an issue?

Berend Odink: No, I do not foresee it. No.

Aditya Soman: Excellent. Alright, yes, these were my two questions. Thanks.

Moderator: Thank you. The next question is from the line of Jatin Chawla from First Voyager. Please go ahead.

Jatin Chawla: One is, if you look at the quarter the spirits companies have done a lot better. So just wanted to understand this beer to spirit shift that we have seen. Are there any kind of longer-term trends to read here? Or this is just kind of factors impacting in the situation that we are in right now?

Berend Odink: Yes. I think, beer has been a bit more impacted versus spirits. First of all, it is more of a bulkier product. So, if you want to take something home, I guess it is less convenient, than maybe a single bottle. Secondly, for beer, you have to consume it cold. Having that kind of slot in your home fridge could be a challenge in some areas. That is why the beer industry has been a bit more impacted and as to what is structural about it? How will it pan out? I think it is very early days. Very little data as yet to say what extent this will last or will it change.

Jatin Chawla: And prior to COVID, what was your on-trade share?

Berend Odink: From our volume base, around 20% was on trade.

P. A. Poonacha: I think I have something here because even if you say on trade, I mean, a lot of our retail shops also allow consumption, which has now stopped. So, the effect has been larger than it has been on paper.

Jatin Chawla: So, if you were to kind of take a guess on, how much of that was around the retail shops, then the number would we what, 30%, 35%? Or even higher than that?

P. A. Poonacha: We cannot because, I mean, these are retail shops which are bending rules, I mean, we cannot really comment on that, but if you look at the market and the way it operates, how many retail shops? what volume? We would not like to call out, but many retail shops did allow consumption on-premise.

Jatin Chawla: Sure. The reason I asked this was because the spirits companies say on trade for them is 25%, and one



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would normally think that beer would have a higher on-trade than spirits, which is the kind of reason to kind of harp a little bit more on this question.

Berend Odink: Yes, I think we have to take into account kind of the license types that I think that Poonacha rightly called out. There is a kind of gray area where people may be outside the off-premise shop and would consume. In some states, it is a very common feature of the business. In other states, it is more traditional within the definition, I guess, of an on-trade premise. So yes, it is difficult to match that one-to-one.

Jatin Chawla: Sure, and I think your press release had a comment on you being encouraged about how some of the states have reversed some of the excess hikes that they have done. So, what are your thoughts on overall kind of state taxation and how it has evolved in the last few months as states have been kind of start for revenues?

Berend Odink: Yes. I think particularly, when the markets opened up, we saw some very quick and steep reactions in terms of excise duties. I think a bit of encouraging news is that in Delhi and more recently in Orissa, this was rolled back to maybe what I call more normal levels of increase. So as of today, it has been West Bengal as to only quite a high duty increase of 30%, Andhra also very high duty, but I guess that is a little bit of a separate situation in the sense of the policy direction the state is pursuing. So, there are some smaller states that have also seen heavy duty increases, but some of the larger ones like maybe Karnataka, like Maharastra, not really duty increases. So, in that sense, it is a mixed picture.

Jatin Chawla: So other than West Bengal, there is no kind of large state where the duty has been like really unreasonable?

Berend Odink: No. What we spoke about last call in Telangana, there some Rs.30 per bottle on the main SKU. So that is also pretty sizable. Rajasthan, some Rs.10. Some states have seen annual increases, more or less, so that will not be too different, but specifically, where it is related to COVID and maybe funding some deficits as the states suffered particularly around COVID, some of that has been brought back and we continue to make representations as to what we see might be a more healthy level of duty for both the industry participants, but also the states themselves.

Jatin Chawla: Right and some of the states have kind of called this out as a COVID cess. So, are you hopeful that in those states, this will reverse once the pandemic is behind us?

Berend Odink: Yes. I think we have seen 2 examples where it was reversed. I think at the end of the day, the demand is so much impacted due to the COVID cess it is a very strong rationale for the state themselves to



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probably reconsider some of those increases. Whether they have labeled is COVID or more general excise term, I guess, is something else, but yes, at the end of the day, the state is also looking at excise revenues in total. So yes, that is a shared interest that we obviously also very much keep looking at going forward.

Jatin Chawla: Just one last point related to this. In your annual report, you also talked about engaging with states on getting taxation more linked to the level of alcohol content. Anything that you would like to share there, where you kind of see making some progress? Or are this still very early days on that?

Berend Odink: Well, this will be a very much continuous effort. So, for example, in Haryana, we have seen a policy that actually distinguishes between alcohol content also of beer. So I think that is encouraging, but in our efforts, yes, we continue to make this representation where we have some strong examples that I think make a lot of sense and that is the message we convey, and whether that leads in the near-term or mid to long-term to follow-up and implementation, I guess that we will have to see later on, but we take very seriously that it is our role to convey those messages and the way the excise model could be implemented.

Jatin Chawla: Sure, thanks. I will come back in the queue.

Moderator: Thank you. The next question is from the line of Krishnan Sambamoorthy from Motilal Oswal Securities. Please go ahead.

Krishnan S: Berend, you mentioned about 120 Crore increase in net debt over March. Has there been any increase in working capital and specifically receivables over this period? And any delay from state governments on this front?

Berend Odink: The working capital is actually very healthy. So, we focused a lot on the cash management on the payables and the collections. So as such, I think the net debt increase was relatively modest, if you would compare to the prior year Q1. Of course, there are a few states where trading is relatively low, so they might be a bit showing more of an overdue, but others, I think we have seen very good collections. So, net-net, I think, on the working capital side, we are in a good shape.

Krishnan S: Okay. The second is, any comments on price increases that you obtained from many of the large states over the last 2 or 3 months?

Berend Odink: Yes. So, as we have seen, I would say, a healthy positive price impact in the quarter. We have seen small price increases, for example, Karnataka, Maharashtra, all in all, I would say, yes, where we



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continue to strive for healthy price increases in the sense of protecting the bottom line and then some of the input costs, I think we are on a good track there.

Krishnan S: Just on a follow-up on that, Berend, the 2 states that you mentioned are prepricing markets. Any states where you were expecting a price increase and you have not obtained it yet and when you are hopeful of getting it maybe in subsequent quarters?

Berend Odink: Difficult to comment on what might happen in the future. I mean, obviously, every state has its own considerations into approving that or not. So, our role again is to strive for healthy balanced price increases, whether those will fall in what quarter or what year that we will report back as and when it happens.

Krishnan S: And then lastly, can you quantify the extent of the price increases you are seeing on an average?

Berend Odink: No, not putting that out, but for example, in Karnataka, it was Rs.5 per bottle. Maharashtra, Rs.10. So, I would say probably very much similar as to the kind of annual increases you have seen in the last couple of years.

Krishnan S: Thanks.

Moderator: Thank you. The next question is from the line of Avi Mehta from IIFL Securities. Please go ahead.

Avi Mehta: Sir, consumer sales have indicated that July has moderated from June given the local knockdowns. Have we seen a similar kind of impact in July as well? Would you be able to share that?

Berend Odink: July has been again, impacted state by state. So, I called out Karnataka, where there was a week lockdown, which obviously is an important state in our total contribution. So other states, some better trading due to reduction of taxes. I think if you would compare it to maybe FMCG, where you might have seen a story of inventory building, which was subsequently, I guess, more depleted and back to more normalized levels. I do not think this is the case for the beer industry where stocking up etc., it is less of a phenomena than maybe in FMCG in some of the states.

Avi Mehta: So, it will be still be an improving trajectory to that extent. I mean, on an aggregate basis, I understand the state level dynamics, but on an aggregate basis, because you do not have the exact proportion of each state so which is why I was just trying to kind of get on an aggregate basis, could it be an improving trajectory or a flattish strategy or declining, whichever way you want?

Berend Odink: Yes, I do not want really specifically call out July and we will come back on the totality of Q2



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obviously, when we talk about Q2 results, but what I said earlier, the industry continues to be impacted a lot by the pandemic and the related restrictions, and currently, of course, within Q1, we have seen a bit of an improvement month-by-month. So, we have to see how that can continue going forward.

Avi Mehta: Okay, and the second bit is could you share if you are seeing any change in terms of either market share, discounting on the ground, or any such sense because of the way that the industry is going through, the beer industry is going through?

Berend Odink: I think our market share is more or less flattish in the quarter. I think we have seen, yes, the usual competitive pressure. I guess there was also quite some discounting on stocks that people wanted to lift out of the market so that maybe was a bit more pronounced than usual, but yes, we continue to be very focused on the market share position and whether demand is low or high, that will be an important parameter for us under any scenario.

Avi Mehta: Okay, and lastly, any update, how is the input cost situation kind of given it is position on the glass and the barley?

Berend Odink: Yes. So, looking on the barley side, with most of the harvest now done a bit softening of prices. So, we have seen around 10% reduction on barley prices versus prior year. Obviously, against a background that we entered the year with a bit more inventory than anticipated due to the drop in demand.

On the glass, new bottle prices also moderated to low inflation kind of levels, and so from that sense, on the input cost side, a much better picture than 1 year ago.

Avi Mehta: No, but on glass, the recycled glass prices, is there any change here because of the lockdown, is that kind of hurting? Or is that a risk that you could see how that been?

Berend Odink: Yes. In Q1, we have seen a similar rate of new versus recollected bottles as usual. How that will move going forward yes, I think that is difficult to forecast. There are a lot of local dynamics in play. Obviously, the market is quite disrupted with on-trade continuing to be closed. So, we will have to see how that impact moves going forward. So that recollection rate, I guess, it is more of a question mark, but the pricing of the new glass is low inflationary.

Avi Mehta: And barley you said inventories, moderately higher, any expectations by when do you expect the new barley to kind of start reflecting?



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- Berend Odink:** It is difficult to call out because, again, that we have to see when the barley process is done, and we have consumed the inventories that we entered to season with, but obviously, that is been taken into account into our buying strategy over the last few months. So, we will come back on that in probably Q2.
- Avi Mehta:** Okay. So, second half or nothing of that sort you could kind of share or no, no comments on that? I am just trying to kind of understand from that point of view. Barley reflecting in, how would you see that you do not want to, sorry, I did not get it. So, you are not able to share or are you reserving your comment...
- Berend Odink:** No, I am not going to speak to specific months or quarters when that will be consumed because obviously that is linked to the demand picture at this point in time versus the coming months. I am just saying that in our buying strategy, when we entered the barley buying more or less in April, we were well aware of the disruption due to the pandemic. So that has been factored into how much we bought in the last months.
- Avi Mehta:** Thank you very much. Thanks.
- Moderator:** Thank you. The next question is from the line of Ashit Anil Desai from Emkay Global. Please go ahead.
- Ashit Desai:** Yes. I had a question, is there any inventory or raw material write-offs during the quarter? We had some situation in Mumbai Breweries, which we had called off earlier?
- Berend Odink:** No, we have not really had write-offs as such. I think it is fair to point out that the whole expiry and usable raw materials, etc., is a topic of attention given the sharp decline in demand, but the quarter is more or less fully impacted by COVID. This is one of the topics that we are focused on, but I think the supply chain team is doing a great job in making sure everything is used in time, etc. So as of now, no definite write-offs beyond the provisions that we have taken in the March quarter end.
- Ashit Desai:** Okay, and on gross margins, I see you called out state mix but actually, you have also called out positive state mix in the presentation. So, what are the drivers for gross margin decline? And how much of those are one-offs that you expect because from a 2-year perspective, if we see your gross margins are down almost 600 bps or 700 bps, last year, 300, 350 and this year also similar decline?
- Berend Odink:** Yes. I would distinguish, let us say, the current impact and maybe last year impact. Last year was driven by a large extent by steep increases in barley and glass, which we were not able to price within



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that year on the revenue side hence the pressure on gross margin. In Q1, we have seen input costs as such, pretty stable. So, it is much more around the state mix and the brewing mix within that, coupled with the other element that I called out, more inefficiencies in the breweries due to the low utilization of the network.

Ashit Desai: Okay, and given the lower input cost, do you think you will be able to get back to last year gross margins going ahead? Or the brewery inefficiencies will continue?

Berend Odink: I think the inefficiencies will be a function very much of the demand development going forward. So yes, that is not something I can call out. What we see or what I shared on the input costs, I think that is looking pretty much better than a year ago, but as to how the demand recovery will move, I do not want to comment.

P. A. Poonacha: Ashit, I mean, coming to gross margin, unless we operate at our regular 80%, 85% capacity, gross margins cannot be compared. It is like comparing apples and oranges. Because there is a lot of costs that we need incur when we are operating only on single shift vis-à-vis 3 shifts sometimes 2 shifts. So, this operating of lower capacity has a big cost burden, which is spread over lower volumes. So, it is really not comparable. So, unless we get back to original levels, you cannot say that we are not getting good prices, or we are not able to procure material at the right price. So, we are doing all that, but it is just that the fact that we are not able to operate at optimum capacity, which is hitting the margins.

Ashit Desai: Got it, and why is your depreciation lower this quarter?

P. A. Poonacha: That is what we are just saying, when we depreciate on a regular basis, on a normal year, it is depreciation of 3-shift basis. 3-shift basis means your depreciation is double of what your normal depreciation is when you operate in one shift. Then if you are operating 2 shifts, it is in between these 2 rates, and in each unit, based on the maximum number of working days and which shift it has worked. For example, if a unit A has worked 20 days with one shift, the depreciation is made on one shift basis. If it has worked on 2 shift maximum number of days, the depreciation on 2 shifts. That is why you are seeing a drop in depreciation.

Ashit Desai: Okay. We followed this historically also? Or this is the only quarter...

P. A. Poonacha: Historically, most of our breweries operated always at 3 shifts.

Ashit Desai: Okay. If I may take one more question. I just wanted your insights on, if you look at other markets



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where the bars and restaurants have opened up, and I mean, if you could call out what is the kind of recovery in the category that you have seen in those markets?

Berend Odink: If you look to maybe take one example, I think in China, for example, it has been, even to some extent, at pre-COVID levels quite quickly, but I would say a lot of it depends on the kind of restrictions that are in place or consumer sentiment around going out and gathering in groups, etc. So, there are differences, given recovery rates at different markets and some have moved up, but maybe also subsequently moved down. So it is difficult to put one figure to it, but there are very promising examples and there are some examples where it has shown to take more time.

Ashit Desai: Thanks, and all the best.

Moderator: Thank you. The next question is from the line of Tejash Shah from Spark Capital. Please go ahead.

Tejash Shah: First question is on any update on Andhra Pradesh this year? And have you seen any revival of order from the government? Or at least how the negotiations have improved?

Berend Odink: If I heard you correctly, the question was on Andhra Pradesh?

Tejash Shah: Yes, on Andhra Pradesh.

Berend Odink: No, there, I think we can safely say that it continues to be very challenging, not least because of taxation increase of some 75% on the consumer price level. The total beer industry, ever since COVID opening up in May has been severely down. So that continues to be a very difficult trading environment.

Tejash Shah: And last quarter, you spoke about CCI report briefly and particularly this quarter. Any update on that to share?

Berend Odink: On the CCI case, no, there is not so much an update. A lot of the process has actually been on hold or suspended due to COVID. So, a couple of these process steps have been pushed back, and hence, we will be submitting our responses to the initial report in the coming 2 months.

Tejash Shah: That is all from my side, thanks.

Moderator: Thank you. The next question is from the line of Vishal Punmiya from Nirmal Bang Institution Equities. Please go ahead.



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- Vishal Punmiya:** So, my first question is regarding the procurement of barley, recently change in regulation. So, you can now basically procure directly from farmers. What benefits can you see from this in terms of procuring directly on the farmers instead of going through the APMC? And the second question is basically, what would be the key focus area for the new CEO who has joined from a medium point of view, while he is not on the call. If you can just highlight his key focus areas, it will be very helpful?
- P. A. Poonacha:** Yes. Just to clarify your first question, what are the benefits UBL gets by procuring directly from farmers by excluding the intermediary, was that your question?
- Vishal Punmiya:** Yes. So, what would be your change in strategy in terms of procurement? And what would be the benefits, if there is a change in strategy?
- P. A. Poonacha:** Yes. I mean, benefits will be cost. Basically, you will have a direct access to the farmer, and when you go through an aggregator, some farmers will be selling at a lower price and the aggregator will be giving it to us at a higher price, right? So, when you are accessing directly, you get that bit of advantage. Of course, there will be fluctuations, which has to be handled carefully, which we are doing. Will have some cost advantage, we will not be able to quantify what it will be, but there will be some cost advantage. With respect to your second question of our new MD. He, I think, would address the investors very soon. So, you can hear from him of how differently he would be handing this company or what his thoughts are. So, I would not be able to comment on that.
- Vishal Punmiya:** Just a follow-up on the first question. Any commissions that go away while procuring directly from the farmer and also the logistics benefit that comes from direct procurement?
- P. A. Poonacha:** Yes. I mean, you will have a little more logistic costs because you will have to source from different locations. That is there, but like you said, the intermediary fees, there are certain things which you will save. So, we are confident that it will have a positive cost advantage on overall basis.
- Vishal Punmiya:** Sir the duration of the logistics would go down?
- P. A. Poonacha:** Sorry?
- Vishal Punmiya:** The duration goes down in terms of traveling from farms to another in terms of the procurement of raw material into the brewery?
- P. A. Poonacha:** That does not matter because between the March and June season, we procured close to 70% to 80% of the barley required for the full year. So, if barley is coming in even 2, 3 weeks later, I mean, we already contracted the size and quantity, the job is done. So, it does not matter.



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- Vishal Punmiya:** No. So, beyond year FY2021, would there be any benefit?
- P. A. Poonacha:** This is a onetime benefit. You cannot keep getting benefit on and on because when you compare these will be the lower base, right?
- Vishal Punmiya:** Okay. Thank you very much.
- P. A. Poonacha:** Yes. It is a one-time benefit.
- Moderator:** Thank you. The next question is from the line of Himanshu Shah from Dolat Capital. Please go ahead.
- Himanshu Shah:** Most of my questions have been answered. Just one question. How do we try and bring back the consumers as the economy starts recovering, like what would be the input factor or key things that you would try to get back the consumers post the pandemic?
- Berend Odink:** Yes. I think again, we have seen practices globally that have worked pretty well. I think on the one hand, it is not only waiting for consumers to come back, but even on current circumstances, driving more of the in-home consumption. So what we are doing digitally is very much focused on that, and yes, as soon as bars and on-trade is allowed to open that, we definitely come with a range of activities to support that, but we have to also see how that deregulation actually will happen, so that we make our efforts accordingly.
- Himanshu Shah:** Okay. Sir, any kind of price cuts or anything that you would envisage or like to take to attract consumers?
- Berend Odink:** Can you repeat the question?
- Himanshu Shah:** Any kind of price cuts or anything in any specific states or any location that we would be envisaging to bring back the consumer?
- Berend Odink:** No, I do not think price cuts is kind of sustainable approach, I mean, you can always have your activations and similar type of programs, but as it is, I think it is more about the long-term sustainable approach that consumers feel confident, feel engaged that yes, coming back socially is safe to do, and I think, many examples around the world show that people like to go out and I think that has not fundamentally changed due to the pandemic, but how and at what point in time that is reasonable, of course, that the different by market, but in essence, people, of course, want to continue to gather with friends and family, and I think that has not fundamentally changed.



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- Himanshu Shah:** Okay, Sir. Just 2 more quick follow-ups. We will be filing the replies within next 2 months, you just called out that. Is that right?
- Berend Odink:** Yes. That is correct.
- Himanshu Shah:** Okay, and Sir, secondly, with respect to Andhra Pradesh state, when you call out the trading environment remains difficult. Just want to confirm, is the state government ordering with us? Or the ordering remains prima facie to private parties only?
- Berend Odink:** So, any orders we get is from the state corporation. What else they order? I do not have visibility on it, if that was your question.
- Himanshu Shah:** Sir, I am asking, I think, so post the open market changes in Andhra Pradesh, a larger portion of ordering was happening with private parties. The same scenario continues as on date for whatever volume that must be happening in this state?
- Berend Odink:** Yes. I commented earlier that I think the total industry is severely down. So, reading in the volumes that are trading there today a lot about market share, I think that is a bit difficult. So, I would just say the market is very severely down and who will get directly what orders I do not have visibility on. I can only see what we have received in orders, which is simply severely down from last year, that is the situation for us in the state of Andhra.
- Moderator:** Thank you. The next question is from the line of Jatin Chawla from First Voyager. Please go ahead.
- Jatin Chawla:** Just a quick follow-up on the gross margin thing. Does the fact that on-trade volumes are down, does that impact gross margins also?
- Berend Odink:** Maybe only a little bit to the extent that the premium part of the portfolio is a bit more skewed to the on-trade so that we will have some bearing, but again, the lower utilization of the network and the state mix has the more pronounced impact in Q1.
- Jatin Chawla:** Thanks.
- Moderator:** Thank you. The next question is from the line of Abneesh Roy from Edelweiss. Please go ahead.
- Abneesh Roy:** Sir, you mentioned in 2 states, the duty has been reversed. So given the current scenario, is there some benefit you are seeing in these 2 states?



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- Berend Odink:** Yes. So, in June in Delhi, earlier in the month of June, Delhi reversed. We have seen progressive improvement in the market since. For Orissa that occurred early July. So, it is a bit too early to read a lot into it, but of course in general, yes, more affordable pricing will be a big plus to have consumers come back to the category.
- Abneesh Roy:** And one follow-up, Sir, in Andhra, you are also suffering, all liquor players are suffering. So now, are you planning some remedial action on the legal front because in some of the other states, we have seen this? And on duty reversal there, is there any visibility? Or all these are steps on the prohibition, which is there, so step wise prohibition which they want to do?
- P. A. Poonacha:** No, when you mean legal action, I did not understand.
- Abneesh Roy:** So in some of the other states, we have seen when route to market, there is a drastic change, and it will start favoring some of the smaller players, regional players, and it is essentially unfair, not level playing field. We have seen in 2, 3 states earlier, there has been some legal action and some states we have actually won, the industry has won. So here, is there anything similar possible, anything similar happened?
- P. A. Poonacha:** You are right. If you are just saying that the size of the industry is remaining as it was prior to these new actions by the state government of Andhra Pradesh and if the ordering was not been given to us, it made sense to try and address the issue, but here, the industry itself has come to a minuscule level, and the state government is of course, not officially, making noises that it is going towards prohibition by the time the current incumbent government comes for reelection. So, when all these things are there, does it make sense to take it legally?
- Abneesh Roy:** Sir, my question is the market share shifting to the unorganized players, operators, is that happening?
- P. A. Poonacha:** You are right, you are right, you are right. The market share is of a large volume. The volume itself is dwindled. The volume of Andhra is dwindled.
- Abneesh Roy:** For the entire, even the illegal player?
- P. A. Poonacha:** It is not illegal. Please do not interpret it. They are not illegal. They are local players who are not national, who are getting orders. SNJ is getting orders, they are not illegal, they have a valid license.
- Abneesh Roy:** No, no local players. My meaning was local players only.
- P. A. Poonacha:** Yes. So, the local players who are getting orders are getting orders, but the entire industry has come to



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probably 1/10 of what it was, does not make sense to take action? It does not.

Abneesh Roy: Got it. Sure, thank you.

Moderator: Thank you. The next question is from the line of Krishnan Sambamoorthy from Motilal Oswal Securities. Please go ahead.

Krishnan S: My question is regarding the logistics of home delivery. Now wherever home delivery is allowed either to the buy shop delivery guy or through the aggregator, how do you get back the old bottles. Does this gets collected on subsequent orders? Or do you say that this is a new avenue of growth, so eventually it will come back to the company at some time and therefore, is there an implication from a lower margin because of higher proportion of new bottles, possibly any time until the on trade segment opens?

P. A. Poonacha: Whether the consumption is home consumption or whether it is on-trade consumption, the used bottles come back to us in a different route. There is no deposit model where it comes back in the route of supply. So, for example, we bill the corporation in Karnataka. The corporation will bill the various retail, or they will bill the various on-trade locations, and all these points of consumption, they do not return it back to the corporation or back to UBL. They are being picked up by bottle aggregators. So, it is a totally different sector itself, which operates. So, whether the consumption at home or whether the consumption is on-trade, it does not make a big difference.

Krishnan S: Yes. So even there, right, if you look at in the current environment, would not there be a delay in pickup by the bottle aggregators and eventually to you?

P. A. Poonacha: There can be, for example, say a consumer has a case of beer at home. Will he keep the bottles for long in his home? No, because it consumes space. So, what will he do at the end of the week, he will find somebody to pick it up. I mean, he will not even want anything for it. He would just want it to be cleared. So, these are the people who pick up these things and it comes back to the bottler aggregators.

Krishnan S: Understood. Thanks. Got it.

Moderator: Thank you. As there are no further questions, I would now like to hand the conference over to the management.

Berend Odink: Thank you everybody for joining the call today. Thank you for your interest and your questions. Please stay safe and look forward to catch up for the next quarter's call. Thank you very much.



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Moderator: Thank you. On behalf of IDFC Securities, that concludes today's conference call. Thank you for joining us, and you may now disconnect your lines.