"United Breweries Limited Q2 FY2020 Earnings Conference Call"

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Moderator: Ladies and gentlemen, good day, and welcome to the United Breweries Q2 FY2020 Earnings Conference Call, hosted by IDFC Securities. As the 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 "*" and "0" on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Mehul Desai from IDFC Securities. Thank you, and over to you, Sir!

Mehul Desai: Thanks Lisa. Good evening, everyone. On behalf of IDFC Securities, I would like to welcome the management team as well as all the investor and analyst community for the Q2 FY2020 earnings call of United Breweries. From the management side, we have Mr. Berend Odink, the CFO; and Mr. Poonacha from the Investor Relations. I will hand over the call to the management for their initial opening remarks, and then we can open the call over to Q&A session. Over to you, Sir!

Berend Odink: Thank you, Mehul. Good afternoon, good morning, everybody, on the call. Thank you for joining the call today. Let me start with providing some context and commentary on our Q2 first half year results. And then after that, we will, of course, open it up for questions.

First of all, the Q2 performance, the volume, UBL's performance was somewhat subdued with domestic volumes in the quarter registering 6.5% growth, and we saw mixed performance across the individual base. Our volume doubled in West Bengal and Jharkhand, growth in West Bengal was triggered by reduced and consumer prices; and growth in Jharkhand was helped by the change in the route to market from government retail to private retail. The markets, including Andhra Pradesh, Delhi, Odisha, Tamil Nadu, Kerala, UBL grew double digits. Other markets like Karnataka, Goa and the markets for the West, excluding Maharashtra, saw a decline in the beer volumes; volumes in Maharashtra remained flat.

If we look at the main regions, in the North, UBL volumes were up low single digits, particularly Delhi was actually up strong double digits whereas Rajasthan, UP and Punjab were low mid-single digits up and Haryana volumes saw a strong decline.

In the South, UBL volumes were up 6%, and the growth in the region is attributed to the growth in Andhra Pradesh, Kerala, Tamil Nadu and Telangana, with an exception of Karnataka which witnessed a decline in volume.

In the East, UBL volumes were up 40%, but volumes in West Bengal and Jharkhand, as I said, doubled; Odisha reported double-digit volume growth.

In the West, UBL volumes declined 8%, with the rest of Maharashtra growing around 6%, with the other markets in the West seeing a decline in volume.

If we look at our gross revenue in total, it was up 8% in the quarter, but gross margin declined by 365 basis points in the quarter. The fall in the margin was due to the high input prices of barley and glass in addition to the subdued revenue growth and unfavorable state mix as earlier referenced.

Shifting to the half-year performance; overall, domestic volumes grew year-over-year 6% and going to the main regions in North, UBL volumes were up 2% with double-digit volume growth in Delhi, Punjab, Rajasthan and UP and Haryana declining, again similar to Q2.

In South, UBL volumes were up 7%. In Andhra Pradesh, Tamil Nadu and Kerala up double-digit, a strong volume performance, but Karnataka and Telangana declined by mid-single digits. In East, UBL grew 28%, again, volumes in West Bengal and Jharkhand growing nearly 100%, 80%, strong volume grow; Odisha volumes being flat. And in the West, kind of a similar trend, volumes declined 6%, Mumbai declined 8%, while the other markets in the West, with the exception west of Maharashtra, declined double digits.

Looking at the growth revenue line for the half year, this was up by 11%, but gross margin declined by 385 basis points compared to the prior year as again, input costs remained high in the half year.

In conclusion, we saw a tough half year impacted by general elections, the severe monsoon in many parts of the country and cost pressures, coupled with lower economic growth. But despite the difficult operating environment perhaps there are certainly some positives in the first half year. UBL expanded market share, based on our own estimates and available public information. Some of our innovations are performing very well, and we have seen premium brands growing ahead of the total portfolio. And we are certainly comparing the results to particularly strong performance first half of the last year.

So at UBL, we remain convinced that the business fundamentals continue to be strong, with the mid and long-term key market growth drivers in place, and we expect the GDP growth, increasing urbanization and growth in population with new entrants into the legal drinking age.

So with that, I would like to conclude the opening comments, and welcome any questions you have.

Moderator: Thank you. Ladies and gentlemen, we will now begin with the question and answer session. The first question is from the line of Krishnan Sambamoorthy from Motilal Oswal Securities. Please go ahead.

Krishnan S: Thanks for taking my questions. Two questions from me. One, you highlighted an overall slowdown in demand during the quarter, and this was witnessed in Q1 as well. Does that mean that your capex plans at least for FY2020 are lower than what they were originally in the past?

Berend Odink: Sorry, lower than? What was the last part of the question?

Krishnan S: Yes, lower that what was initially planned?

Berend Odink: Yes. So, our outlook for full year will be in the area of Rs.400 to Rs.450 Crores and that is indeed lower than we originally anticipated to be spent for the year.

Krishnan S: The second question is regarding working capital. In the press release, you have highlighted that there has been a delay in payments by state governments. Now is this, in your reckoning, something that is happening for the near term? Or is it something that you are worried about on a structural basis?

Berend Odink: So, I think, it has been a year-over-year challenge, let us say, the payments being met on time, but particularly at the end of this quarter, we saw one of the states extending beyond credit terms. So that is why we called it out. Of course, we have, I would say, put in a lot of controls most elements of our working capital. But when we are selling, of course to State Corporations, this is somewhat out of our control in terms of “payments in time”, so this is a situation we faced at the end of Q2.

Krishnan S: Okay. Thanks Sir.

Moderator: Thank you. The next question is from the line of Amarjeet Maurya from Angel Broking. Please go ahead.

Amarjeet Maurya: Just wanted to understand like in a cost rising scenario, like on the raw material front, so what is the strategy to increase your operating margin? And from which state you are getting expected price hike?

Berend Odink: Thank you. On the first part of your question so as you know, the bottles and malt input costs are the key ones on the brewing side, here, we see no further increases to the level that we have been experiencing in Q1 and Q2 and we have put in place additional measures to manage this cost in short and long term, I might say. So that is particularly on the bottles and the malt. The second part of your question was, I will let Poonacha pick that one up.

P.A. Poonacha: I mean, with respect to increasing our margins, well that is what it has always been, even in the past, we are always looking at ways and means to increase our gross margin. But however, as you know that our business is regulated in a manner wherein we have some States are very profitable, while some others are not. And then we have situations like this, States that are highly profitable, there is a decline in volumes. We have confronted this kind of a situation. We are working on ways to take price increases, but however, as you know, already, at the MRP level, beer is a highly priced alcoholic drink. So, we have to be a little cautious that these price increases do not affect our volumes.

Amarjeet Maurya: Sir, what is your current market share in the beer segment? And Sir, what you are saying is like you are losing or you are stable or you are increasing market share? And I believe most of the market share is yours. So what are the strategies to increase in the future?

Berend Odink: We believe we are above the 50% market share and based on our estimates and publicly available information, we believe we are growing around 1% to 2% market share points in the last 5 years so that is definitely good news. To answer the question of the outlook, we are confident that we have a good brand portfolio. We continue innovating. You have seen a couple of examples in the last two years and we are encouraged that this growth has been ahead of the total portfolio, so the strategy is definitely paying off, and we have an ambition to continue to grow a bit ahead of the market, whether that is how every quarter will exactly turn out, remains to be seen, but overtime, we certainly set that up as a target.

Amarjeet Maurya: Thank you Sir.

Moderator: Thank you. The next question is from the line of Ashit Desai from Emkay Global. Please go ahead.

Ashit Desai: Hi Berend and Poonacha Sir. So a couple of questions; one, if you could explain the very sharp increase in staff costs as well as other expenses when the growth has been low? And also, with regards to, on your overall margin outlook, we did almost 18% last year. Is it possible for you to go back to those kinds of margin levels in the medium term? And yes, I will state the second question later.

Berend Odink: Starting with your last question. Usually, we do not put out guidance on the margin front as such, but we are confident on the input costs, particularly malt and glass, we do not see further increases. So that is, I would say, an important element to your question. So, on the margins, yes, let me keep it with that. I think on the cost side, we commented on some of the fixed costs. So obviously, we had a very strong performance last year in the first six months. So, this is something we have as comparable in the current six months. I think, by and large, we did not see any one-offs positive or negative entering our results these six months. So normally, these are the normal salary increases, the normal vacancies, etc., being filled. So there are still, certain extent, some of those elements. But certainly, with the new economic reality that we see on the macro front in India, where looking critically over the cost lines in more detail, as you can imagine. So, also on fixed costs, we continue to take appropriate measures for the lower growth patterns we have experienced the last six to nine months.

Ashit Desai: Sorry, you are saying there are no one-offs in staff costs and other expenses because we have not seen this kind of inflation with other companies?

P.A. Poonacha: In staff costs, we have no one-offs. In the other costs, we have a couple of one-offs, which are basically under the cess and taxes. We have a one-off with respect to an entry tax wherein we took Rs.6 Crores charge. The reason being this matter was litigated, and since the government, after the implementation of GST, came up with the scheme wherein we could pay the principal amount and we get an exemption on interest and penalty; we accepted that offer. In addition to that, we had another Rs.6 Crores, which is on account of brewing license fee name change, which we have been waiting for many years now. So, barring that, the growths in other costs are up largely because of cess and taxes going up. As Berend in his introductory had said that Haryana, the volumes are down, the volumes are down because the bottling fee, which have gone up in Haryana drastically in addition to a something called cow cess in UP. So, all this as increased the cess and taxes. So thereby, you see the growth in the other costs.

Ashit Desai: For staff cost, 20% is the normalized run rate we should look at for second half also?

P.A. Poonacha: You are looking at growth from the first half or only the second quarter and second period quarter?

Ashit Desai: I did not get you.

P.A. Poonacha: You are looking at the growth of staff costs only in the second quarter or the first half growth you are looking at?

Ashit Desai: Yes. Second quarter, it is like 20%; first half, it is somewhere between 16% and 17%, so.

P.A. Poonacha: Yes. So for the next half, you can take it at the half year rate and not at the quarter rate.

Ashit Desai: Okay. And this is driven by capacity increases?

P.A. Poonacha: Yes, we have added capacity in a lot of places, and we had a lot of structural obligation with respect to running a brewery, which needed additional manpower. So there has been some additional manpower, which have been recruited and so these are the reflections.

Ashit Desai: Okay. Just one last question, if I may, on CCI. Since the findings are out and not in public domain, if you can give us some idea as to if there is any material business impact from that? And what are the mitigating things that you have?

Berend Odink: I think there is, at this point in time, not too much more to comment besides what we have put in the notes to the accounts. So, we are really cooperating with the ongoing investigation. The executives have appeared before the DG Office, extensive efforts, complete disclosure has been made by us to counter any presumptions or impacts potentially made against the company. Our understanding is that the DG has filed a report with the CCI. Yes, we will continue to present our case during any hearing by the CCI and submit all mitigating factors for their consideration. I think that is, yes, what we can comment on at this point in time on the CCI case.

Ashit Desai: Okay. Thanks. I will come back in the queue.

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

Harit Kapoor: Good evening. Just had a few questions; firstly, on the weakness in Karnataka as well as Maharashtra the first half, we have seen a fairly weak performance from both the states. I just wanted to get your sense on why do you think performance has been so weak? And now that you have passed the elections and probably some shutdowns, etc., which were a challenge in Q1, and probably the monsoons also passed by in Q2, do you see a normalization of growth in these two states, which are very key to your contribution?

Berend Odink: I think if we look back first, in Karnataka, we see Q1, impacts from production constraints due to the general elections, where the number of shifts you could operate was reduced from what we usually operate. And in Q2, we have seen, particularly in North and Coastal Karnataka, severe impacts of the monsoon which was, let us say, more intense in the year than previously. And again, that all happened against the backdrop of lower GDP growth, which I think the company perhaps will continue to see for some time going forward. Also it is partly, you could call, maybe there were a lot of incidental external impacts. But definitely, I think on the macroeconomic front, this is here for the coming months; that will not change all of a sudden I would say.

Harit Kapoor: And for Maharashtra?

P.A. Poonacha: In Maharashtra, as you know, rest of Maharashtra has grown. So that is the only state in the West. Mumbai had declined, Goa had declined. And the monsoon has been the clear reason for decline in both Goa and in Mumbai. However, we do not expect great growth in Mumbai; it should remain flattish. However, Maharashtra will continue to grow.

Harit Kapoor: Understood. My second question was on the marketing spend side. So if you could just give us a sense how the advertising or marketing spends have kind of trended in the first half versus the first half last year, whether they have grown ahead of sales or you have invested more or how the competitive intensity is in the market? Is it higher than what it was six months back or lower, if you could just give some sense on that?

P.A. Poonacha: Yes. Competitive intensity has been high and particularly high in profitable markets of Karnataka, but however our ad spend as a percentage of topline has remained the same, that we always maintain as a percentage of topline. But we reallocate the spends to where it is most required and as we have confirmed in the introductory note itself that we have gained market share in the first half. This comes with the investment, and we have been prudently investing in the marketing strengths in the markets where they are most required.

Harit Kapoor: Okay, understood. Last thing was on any changes because of certain go-to-market disruptions in AP and Telangana you have seen quite significant growth there in those two states. But do you see that even the growth that you achieved in these two states probably was hampered by the route to market, or there has been no effect for you? Because you seem to have grown double-digit in these two states, while probably some of the other players have got impacted here?

P.A. Poonacha: Sorry, to correct you about before, Berend answers you. The route to market change has been only in Andhra Pradesh not in Telangana.

Harit Kapoor: No, I mean, there was an expectation that it might change in Telangana as well, which did not really happen.

P.A. Poonacha: It has changed in October, but only Andhra Pradesh has changed. So Berend will update you.

Berend Odink: So indeed, in Andhra Pradesh, especially in retail, and that has reduced the outlets roughly by 20%. The impact in September was not that much significant but what we have seen in October, that will possibly certainly take some time to stabilize, and as such, we are closely monitoring the situation. This is definitely a key change in Andhra Pradesh taking place as we speak.

P.A. Poonacha: Just to add one thing here. As a volume salience Andhra is not as big as Telangana, it is a mere 6% of national volume figures.

Harit Kapoor: Very clear. Thanks and all the best.

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

Aditya Soman: Good evening. Sir two questions from my end; firstly, you indicated that, I mean, growth in Mumbai is unlikely to sort of pickup meaningfully; and also in Karnataka, you are seeing sort of slowdown in growth with also, that you also mentioned earlier, that Haryana was affected. Is there something in these cities, I am assuming that there is large chunk of the volume share in Mumbai, Ban and Gurgaon account for lot of these, is there just increased competition from the likes of craft beers that are making you a little more pessimistic on growth? Or why is your guidance not more optimistic in these regions?

Berend Odink: No, I do not think the impact is mainly from Craft. I think it is more about the economics plus the impact of monsoon particularly Mumbai, severe weather, where I think, you are seeing in some of the new articles that there was severe flooding a couple of times, and in general, facing very tough weather conditions. I think Craft is definitely popular in a number of areas you mentioned. Yes, in the total scheme of national markets, I would say it is relatively small, but yes, an important trend in terms of excitement about the beer category.

Aditya Soman: You are attributing majority of the slowdown to the weather. But I was just curious why for Mumbai and you are also then building in sort of flattish volumes even going forward, at least in the near term?

P.A. Poonacha: Mumbai is one market, which has not been growing even when, what do you call, rest of Maharashtra is growing because when we say Mumbai, it is the Octroi limits of Mumbai. And there, if you see, really, consumption is not moving up, because a lot of the people who even work in Mumbai probably stay and consume beer in Thana, which comes under rest of Maharashtra. So this is Mumbai, it is the Octroi limits of Mumbai, where really beer consumption has been flat for some time now.

Aditya Soman: All right. Understand. And the second question is on Kingfisher Radler, any update on how that has been doing, given that we have seen a much wider distribution now?

Berend Odink: Yes, we are happy with the progress of Radler, but at the same time, it is very early days to, again, get to this conclusion. So, we continue further distribution reach also into the second half. So again, we are happy with the early progress, but I would say it is a bit too early to make any definite statements about success of the long-term prospects, but encouraging start for our products, yes.

Aditya Soman: All right. And any numbers you can share on how many distribution points or anything of that sort on Radler?

Berend Odink: We are about over 30,000 outlets at this point in time. I think more than 13 states and the second half, yes we will continue to expand on this. And as you know, it is a completely different route to market from beer, so we are using different distribution partners for that.

Aditya Soman: All right. Thanks a lot for answering the questions.

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

Himanshu Shah: Thanks for the opportunity. Sir, can you just give us some color on the raw material costs what is giving us confidence that we may not see further price increases on the raw material part?

Berend Odink: Yes, we obviously are buying forward to some extent. For the next one to two quarters, we have a reasonable outlook on what we can expect for longer term. Beyond that, we are also dependent on global commodity prices as such. So that becomes more difficult to make any definitive statements. But on the short term, we are reasonably certain. And I think then beyond that, you are more looking at other impacts like mix within the portfolio, managing pack mix costs. Yes, because I have commented earlier on the next one to two quarters, we will not see further increases.

Himanshu Shah: Thanks, that was helpful. Secondly, other than AP and Mumbai, can you help us how the consumer sentiment has been like maybe in the near-term compared to first half? You have already called out for AP and Mumbai, but for other states, the broader markets?

Berend Odink: Sorry, you were adding something to it?

Himanshu Shah: Sir, you can carry on. And then I will just ask the last piece.

Berend Odink: I think for in terms of region going comments, I think it has been a bit of a mixed bag. So we have seen some challenging markets like Western markets and Karnataka, but also some healthy growing states, so partly the reason being economic factors and weather, but also, it is difficult to take out any conclusion that things are particularly on one trend or the other. But I would say the overall economic impacts that the country, of course, is somewhat on a lower growth pattern. I think, as any company in India, we are not immune to that. So this has, to a certain extent, impacted the first half and most likely to continue for some months to come.

Himanshu Shah: Just the last question, what would be the contribution of West Bengal and Jharkhand on the overall volumes? And when were the price cut in West Bengal and the go-to-market changes took place in Jharkhand?

P.A. Poonacha: The route-to-market changes in Jharkhand took place in this financial year. The change in price in West Bengal was in the last financial year, West Bengal and Jharkhand as % volume sales for the country. West Bengal is around 5%, Jharkhand which is at 2%.

Himanshu Shah: So West Bengal, when was the price correction that was taken place? And was it only with respect to reduction in excise duties, or there was also a price cut that was taken by the company?

P.A. Poonacha: See, the reduction in the prices in the MRP was the contribution of the company is being sacrificed. However, the volume has closed to doubled, and it has made up for the cut in price that we have taken.

Himanshu Shah: And when was this last taken, Sir? In which quarter, if it could just help, that would be helpful. That is it from my side.

P.A. Poonacha: I think in the last month of the first quarter, I think it was in March.

Himanshu Shah: March 2019, you are referring to?

P.A. Poonacha: 2019, yes. So the full effect of that is in the current year.

Himanshu Shah: Fair enough Sir. Thank you Sir. That is it from my side.

Moderator: Thank you. The next question is from the line of Manish Poddar from Nippon India AIF. Please go ahead.

Manish Poddar: Could you explain probably this gross margin deterioration, which we have witnessed. How much would be the state mix, and how much would be raw material led?

P.A. Poonacha: Sorry. Your question was actually not very clear?

Manish Poddar: I am trying to understand the gross margin deterioration, which you have witnessed, how much would that be led by, at least the state mix versus the raw material inflation?

Berend Odink: We do not really split out, let us say, impact of sales versus the contacted prices. But I think year-over-year the input costs, of course, are an important element. And then state mix, let me say, is that for the first half it was negative. So, the earlier comment was for example, Karnataka was at a lower volume than the prior year.

Manish Poddar: Would you be able to call up, let us say, what are the sorts of inflation that you witnessed in glass versus barley?

Berend Odink: Well, glass prices have been up in the area of around 25% and on top of that, as the glass industry in India is having some shortages, we also have a portion of our glass is imported from abroad, where prices are again 25%, 30% above the domestic prices. And I think in barley we are looking at around 15% to 20% higher prices versus this last year.

Manish Poddar: 15%?

Berend Odink: 15 % for barley.

Manish Poddar: Either barley is up about 10% odd. So is it primarily because of international or domestic mix or priced asset?

P.A. Poonacha: Yes. This year, we have imported more barley than we did last year. But however, the price of imported barley is only marginally higher than the price of available local barley. But the advantage we have is imported barley can give you a better yield of malt, so primarily the price increase of the commodity barley is affecting the cost.

Manish Poddar: Thank you.

Moderator: Thank you. We will move on to the next question that is from the line of Vishal Biraia from Aviva Life Insurance. Please go ahead.

Vishal Biraia: Sir, in which one states are we expecting price hikes? Which are states, by effect, is taking guidance?

Berend Odink: Yes, we would not comment on the price changes or policies going forward. But in general, of course, we also usually strive for improvement in margin and therefore pursue some other price increases at timely intervals, let me leave it at that.

P.A. Poonacha: The reason being, in most cases, price increases are a result of discussions with the state governments and state-owned corporations, so to tell you that we are, on a regular basis, in touch with various state government corporations. But where we are moving for a price increase we would not be able to share, because only after it comes through we can share.

Vishal Biraia: Fair enough, Sir. Sir, Heineken as a brand, what would be the contribution to our revenue?

Berend Odink: We would not split out, let us say, specific for brands. But as you know, Heineken is an important brand, let us say, in the portfolio. So there, we continue to put our best behind it, let us say even to a higher extent. And this has long-term good prospects for the market and the brand with the premium segment. So there the Heineken brand is an important brand for us to date. We do not provide specific guidance on an individual brand.

Vishal Biraia: Okay. Would you be able to tell me if Heineken has grown higher than the 6% growth that we achieved for the whole portfolio?

Berend Odink: No, we do not split out the brand names or individual brands. But we commented that in general, the premium part of the portfolio has been growing higher than the total, and of course that is very encouraging.

Vishal Biraia: Okay. Fair enough. So the premium part is growing faster than the company average that is right?

Berend Odink: Yes.

Vishal Biraia: Thank you very much.

Moderator: Thank you. The next question is from the line of Sunita Sachdev from UBS Securities. Please go ahead.

Sunita Sachdev: Good afternoon gentlemen. I just have two very small questions. One, I think given the route to market changes, etc., notwithstanding any of the constant push that you guys have with various state governments. Just wanted to understand how is the number of outlets where beer is available changed over the last one to two years? How many outlets do we now have across the country?

P.A. Poonacha: Approximately 83,000 outlets.

Sunita Sachdev: How does this compare with two years ago?

P.A. Poonacha: It could be almost flat, because I mean when the Highway ban came, it slid down, and then on it has gone up. But only after the CCI, we have stopped packing.

Sunita Sachdev: Okay.

P.A. Poonacha: So in that region, plus or minus 5%. Now the retail outlets in Andhra have come down 20%. So there is a lot of things. But by and large, as a country as a whole, should be in that 80,000 region, because it was max 83,000 before the highway ban.

Sunita Sachdev: What is the push across various state governments and availability at maybe malls, supermarkets, etc? What is the visibility for these 80,000 units two to three years?

P.A. Poonacha: Yes. I mean, you have in this 800 or 1000 odd you have some premium outlets and usually, a very small percentage, only less than 10% of the overall places where beer is available at premium outlets.

Sunita Sachdev: That premium outlet growth will be quite robust, my assumption would be right?

P.A. Poonacha: You are talking about growth of volumes in same outlets or are we talking about premium brands?

Sunita Sachdev: Premium outlets itself.

P.A. Poonacha: You cannot say it. It is kind of very different. But I think that a lot of these premium outlets sell premium brands, by and large, you are right. But if you are looking at overall volumes, then it may not be, reason being the premium segment is small when compared to overall volumes.

Sunita Sachdev: All right. Good to know. Second question, now that more and more states seem to be moving towards the corporation model, are there any financial instruments available which you can potentially use to pass on the repayment risk to maybe the intermediaries?

P.A. Poonacha: Yes and no. Yes, I mean in one way, it is a happy situation if we have a corporation, it is a state-backed method to assure of your own collection. It is government debt. The other downside is in the event the state government is facing financial, what we call, crisis or a shortage of cash flow, there are tendencies of the government dipping into the corporation funds, there have been situations where there have been unusual delay in payments. So, it works against us in some places.

Sunita Sachdev: So passing on repayment risk is not an option?

P.A. Poonacha: It costs a lot of money because I mean today, if you have to go to factoring, the cost of factoring would be close to twice the cost of our borrowings. So being financially, I mean, risk wise, what you call, highly rated companies. I mean our short-term rating is AAA+. I mean we can borrow money at fine rates, it makes more sense for us to fund our debtors than factor them and incur costs to further reduce our bottomline.

Sunita Sachdev: Okay. It is very helpful. Thank you so much and all the best to your new CFO.

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

Krishnan S: How large is the super premium segment of the market, premium versus supreme segment market in terms of number of cases now on an annualized basis?

P.A. Poonacha: Sorry, I could not hear your question?

Krishnan S: How large is the premium segment of the market in terms of number of cases annualized?

P.A. Poonacha: If you take the entire industry, I am not talking about UB alone the super premium segment is less than 5%.

Krishnan S: What is the pace of growth? It was growing at 20%, 25%, 30% sales side, has that been maintained?

P.A. Poonacha: Yes.

Krishnan S: Lastly, you had a lower market share in this particular segment compared to your overall market share? Has your market share also increased in that segment?

P.A. Poonacha: Yes, we have.

Krishnan S: Thanks a lot.

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

Ankur Shah: Hi Sir. Sir, can you let us know the premium portfolio mix, the exact premium portfolio?

P.A. Poonacha: We just answered the question, wherein we said that we take the industry as a whole the super premium segment is less than 5% of the total industry.

Ankur Shah: No Sir, specifically for UB?

P.A. Poonacha: We would not share that.

Ankur Shah: So then the second question, on the capital allocation of Radler. Sir like Bihar is quite a nascent market in India and considering the opportunities that we have overall in the segment, considering all the factors which are just there for the time of the deal. So why has not United Breweries taken a decision to invest in non-alcoholic beverage?

Berend Odink: I think twofold. One, we see an opportunity beyond larger beer. So if you look internationally, Radler has been a segment quite successfully in many, many countries. So definitely for India, we think there is a long-term potential in this category. Again, what I said earlier, this is not an investment for six months or one or two quarters. It is a long-term approach. So hence, we decided to step into that opportunity by launching Radler and the second part is also, let us say, an opportunity-driven approach that we produce in Bihar, which as a state, as you know, has existing prohibition. So our production facility over there continues to be used and in that sense, we allocated it completely to Radler, which is then exported across India from Bihar.

Ankur Shah: I got just one last question, do we see any portfolio gaps in the premium or semi-premium segment like, I think we were planning to launch a craft beer to compete with Bira. So there any thought process on that? Because in Mumbai markets, though we have not seen growth, but just like a casual observation whenever I am visiting a bar or wherever I am going, there is a lot of push on the Bira brand. So how are we planning to compete with that?

Berend Odink: Yes. Well, we will not comment directly on competitors. But let us say, if we look at as you are aware, we have earlier shared that we have plans to launch our own craft beer. So in the coming months, we are quite excited to be launching that in many states. And I should say, the wheat beer segment continues to grow healthily. So this is something we will definitely start thinking to come with our own composition. In fact, some of the import brands that we have are already available, which also are, I mean, in this category.

Ankur Shah: Okay. Great Sir. Thanks. All the best.

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

Harit Kapoor: Just one more question. You have mentioned in your press release, regarding the high input cost pressures and overall cost pressure. You said that the company has already initiated measures to mitigate this cost push. So is the context of, let us say, if you were about the forward covers, which you have taken on the input costs? Or is it about relooking at overhead, etc. Just wanted to understand what are those measures that you are talking about?

Berend Odink: Thank you for your question. It is both, actually. So, it is long term. For example, in glass, we are working with suppliers to expand the capacity in India. In that area, there are a couple of those measures where we strategically look at the supply footprint and the strategy around that are longer term. But of course, also short term where, as I stated earlier, we look if the level of the cost increase that has taken place. And just given the new GDP outlook we are seeing today, we are looking with that in mind, again, at our cost structure. And this is a bit more, let us say, short term driven as well.

Harit Kapoor: Got it. That is from me. Thanks.

Moderator: Thank you. The next question is from the line is from Sanjay Sathpathy from Ampersand Capital Partners**.** Please go ahead.

Sanjay Sathpathy: Just my first question is that your company's EBITDA margin is quite volatile in recent past. Is there some kind of a sustainable margin that the company can deliver in cost?

Berend Odink: Well, we do not give out margin guidance, but let me comment that our top line in terms of pricing, in many states is set by corporations and state government. So we are not at, let us say, our own liberty to move prices up and down that such. We have less flexibility as you might have seen in other industries. And hence with the cost moving as we are seeing, which we explained earlier, the margin in our business, yes, might move up and down quite as you pointed out. So that is a direct impact of the top line and cost disadvantage.

Sanjay Sathpathy: And then can you give us a sense of what really is the barley price, let us say now in the international market versus what you have been using in the last six months? And the other thing that I just want to heck with you, that you have made some comment that you had hired some extra people, a certain brewery. I could not really get what really you were talking about in that.

P.A. Poonacha: Regarding the extra people that we have hired, most of them have been on account of compliance and actual needs. I mean, there are certain compliance that arent too easy to meet so most of these have been to meet the new adjusted higher level of compliance needed at our factory units.

Sanjay Sathpathy: Okay. So this is going to be recurring expense, going forward?

P.A. Poonacha: Recurring, I mean, yes. They are permanent employees. They have been already on board.

Sanjay Sathpathy: Okay. And then can I just get a sense of the index of barley prices or glass prices is at now versus in the past and further the outlook there?

P.A. Poonacha: As Berend commented, outlook going forward for the next half of the financials is flat from today. But vis-à-vis last year, both glass and barley prices have been up in the region of 10%, 11%.

Sanjay Sathpathy: Okay.

P.A. Poonacha: As a weighted average.

Sanjay Sathpathy: Okay. So they are going to stay flat, they are not going to decline?

P.A. Poonacha: No. We do not expect it to decline.

Sanjay Sathpathy: Okay. Thanks a lot.

Moderator: Thank you. The next question is from the line of Ashit Desai from Emkay Global. Please go ahead.

Ashit Desai: Yes. Hi. On working capital, this increase across some states, is it a temporary thing or it is a permanent change in the payment methodology?

P.A. Poonacha: It depends on how well the state government financials do. So we really can not comment on the temporary nature.

Ashit Desai: But have they changed the payment terms as such?

P.A. Poonacha: No, it has not changed. But the payments have been delayed.

Ashit Desai: Okay. And you put a note on discontinuation of an export vendor. Can you give some more color on this as to what it is and what the impact is?

Berend Odink: Yes. I mean, well, the impact has pointed out that export volume has been below last year and below what we have seen in the domestic market. So such was an impact. The good news is there is no impact as such from the consumer end. So that would help UBL there, but it is more due to a change in agent that we are undergoing right now. So longer term, this should not be a factor that is recurring.

Ashit Desai: Okay. And for this quarter, what was the impact on topline and EBITDA due to this?

Berend Odink: Well, we do not call out separately the financial impacts of this. But you would see from the volume figures that exports were down. But we are hopeful that once we have a new agreement in place, that this will reestablish itself for 2020.

Ashit Desai: Okay. And when do you expect this new agreement to be in place?

Berend Odink: As we stated in the notes, this is currently what we are undergoing. So this might take a quarter or something to be up and running.

Ashit Desai: Okay, got it. And lastly, from an overall industry perspective, healthy competitive activity, very high, or you see your competitors reducing discounts? And is most of that over or it is still continuing?

Berend Odink: No. I would say, in general, there is healthy competitive pressure in the pending new markets. The major players are present here with all their main brands. So yes, it has been quite a competitive situation. But we are happy that we have seen our market share increase in the first half. And it gives us confidence in the strategy that we are executing for our portfolio, and that is what we will continue to do going forward.

Ashit Desai: But has that increased in the recent ones or it is stable?

Berend Odink: Well, I do not know how we could kind of compare the level of competitiveness. I think in general, I do not think it has declined, given that the industry growth declined somewhat, then you could say that the competitiveness as such continues to be strong. And of course, there are some differences state by state and relative position. But I would say overall it is certainly not declined.

Ashit Desai: Okay. That is it from my side. Thanks.

Moderator: Thank you. The next question is from the line of Jay Doshi from Kotak Securities. Please go ahead.

Jaykumar Doshi: Thanks a lot for the opportunity. So employee cost increase in the first half is about 18%, and on a sequential basis, 1Q and 2Q similar. You indicated some increase in headcount, steady requirement. So all current quarter number is a normalized number, or should we expect further increase.

Berend Odink: You can take this as a base.

Jaykumar Doshi: Second is on other expenses. You indicated cess and taxes have gone up. Is it possible to give us an indication of what rate and taxes as a percentage of revenue was in the first half of current fiscal versus last year? And similarly, any indications you can give on A&P spend as a percentage of revenue in the first half of last year's Q2.

P.A. Poonacha: Cess and taxes, I mean it again depends on mix. Like I said, cess and taxes are not even and it is not across applicable in all states. Haryana cess and taxes have gone up, which has essentially hurt the volumes and the volumes were declined. You have new cess and taxes in Uttar Pradesh something called cow cess and you have some of other taxes in Rajasthan. So it depends on how the volumes in these states do. You cannot take it as a percentage of overall volumes. So the state mix plays a big role on the rate and taxes.

Jaykumar Doshi: I understand. Any claim on advertising and A&P spend? As you indicated flat, as a percentage of revenue it is flat?

P.A. Poonacha: Yes. I mean, we do mention that.

Jaykumar Doshi: I understood. Okay. Thank you so much.

Moderator: Thank you. The next question is from the line of Vishal Biraia from Aviva Life Insurance. Please go ahead.

Vishal Biraia: So these cess and taxes are applicable only for beer or spirits as well?

Berend Odink: Sorry. Could you repeat the question?

Vishal Biraia: Sure. The cess and taxes are not in other states. So was it applicable to only beer or also spirits as well?

P.A. Poonacha: Cess and taxes are for both spirits and for beers.

Vishal Biraia: I mean, if we see the increase in overheads from about Rs.4.07 billion in 2Q of last year to Rs.5.07 billion at least this year. The increase has been substantial and would you say that bulk of the increase would have been contributed by cess and taxes? Because the one-off kind of...

P.A. Poonacha: Of the Rs.80 Crore, as you are insisting on that, I will give you the number. Of the Rs. 80 Crores, Rs.30 Crore is cess and taxes. There are 2 one-offs of Rs.6 Crores each, so Rs.42 Crores is actually there itself.

Vishal Biraia: The balance increase would be because of other admin expenses and A&P increase, would that be fair?

P.A. Poonacha: Yes.

Vishal Biraia: You have grown by 6% of volumes. Of what would have been the industry growth? Any numbers on that?

Berend Odink: Our portfolio grew domestically around 6%, 6.5%. And we think the total industry was around half that that nature.

Vishal Biraia: So this would imply that most of the operators would have been that flat or marginally negative. Is that your fair assessment, just mathematically?

Berend Odink: The mathematics will certainly tell you that.

Vishal Biraia: All right. Thank you very much Sir for a phenomenal quarter on the volume side. Thank you.

Moderator: Thank you. The next question is from the line of Prashant Kothari from Pictet. Please go ahead.

Prashant Kothari: A fixed cost question on the A&P again. The A&P expenses have come down a lot over the years, in terms of percentage revenues. Do you think they have potential to kind of grow a lot more in the future years?

P.A. Poonacha: You are too soft. I can not hear your question.

Prashant Kothari: Sorry, I will just pick up the handset. The question is on the A&P expenses. The expenses have come down a lot over the years in terms of percentage to revenues. Do you think this could climb up again, or this is the more normalized view?

P.A. Poonacha: I will address this. If you look at A&P expense over the last five years, it would have come down. This would be because in the last few years, the discounts that we give or the trade push that we do, in the past it came as part of the A&P expenses due to the change in the accounting standards with respect to those spends on brands and volumes dispatched from our own units, it is reduced from the top line. What you see now is only a small percentage, which is we spend on behalf of those brands which are bottled by our contract brewery operations. But the brand building spends, which we do not show separately, has been maintained as a percentage of the top line.

Prashant Kothari: Okay, got it. And the second question is on this CCI investigation. Have you made any provisions for any contingent liability there?

P.A. Poonacha: No, we have not made any provisions.

Prashant Kothari: I mean, because you already admitted that there is some rounding there. So is it not be prudent to make a provision?

P.A. Poonacha: As an accountant, I would answer it very differently. When you have to make a provision, you need to have a way to estimate it.

Berend Odink: I mean, we have not received any demand order or anything as such. So there is also more particular basics to say if any financial liability if it is forthcoming.

Prashant Kothari: Okay.

P.A. Poonacha: How you estimated? They are yet estimating it?

Prashant Kothari: Yes. But we know that there will be some amount to be paid. I do not know how it estimated, but there is obviously some impact that you need to take.

Berend Odink: No. So as I said earlier, we have not received any such information and no provisions at this point in time are made.

Prashant Kothari: Okay. Sure.

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

Berend Odink: Thanks, everyone, for your attention and interest in the company. Thank you for the questions. We look forward to the next call and wish you a good day. Thank you.

P.A. Poonacha: Thank you everybody.

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