



“United Breweries Q4&FY13 Earnings Conference Call”

May 31, 2013



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LIMITED**



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Moderator

Ladies and gentlemen good day and welcome to the United Breweries Q4 & FY13 Earnings Conference Call hosted by IDFC Securities Limited. As a reminder all participant lines will be in the listen-only mode and there will be an opportunity for you to ask questions at the end of today's presentation. If you should need assistance during this conference call, please signal an operator by pressing "*" followed by "0" on your touch tone phone. Please note that this conference is being recorded. At this time, I would like to hand the conference over to Mr. Harit Kapoor from IDFC Securities. Thank you and over to you, Sir.

Harit Kapoor

On behalf of IDFC Securities we would like to welcome you all to the United Breweries Q4 & FY13 Earnings Call. We have with us Senior Management Team of United Breweries represented by Mr. Hans Van Zon – CFO and Mr. Poonacha, who Heads Investor Relations. I will now put it over to the senior management to make the opening remarks post which we can throw the floor open for Q&A. Over to you, Sir.

Hans Van Zon

Thank you very much. Welcome to this telephone conference on the year end results of United Breweries for the fiscal year that ended at the end of March 2013. If you look at our press release that we handed out yesterday evening and we have clearly stated that we have a profit after tax increase of 36% and EBITDA which was for the full year up by 6%, sales growth in terms of revenues of 10% and volume growth of 5%. We as management looked back together with the Board of Directors at the year that has run very well for us with one exception, which is the change in the ordering policy in Tamil Nadu which we had referred to also in previous telephone conferences, so I will not kind of go into detail on that but with the exception of that we think we had a good year behind us.

If we take for our Indian listeners they might have picked up the telephone or the newspaper this morning and read something different because the newspapers basically have a tendency to report about a fall in our net profit with huge percentage, however, they do refer only to the very last quarter of our fiscal year in which we also clearly stated in the press release and the publication it has become very irrelevant to be compared to the last quarter of the previous fiscal year as we had a full year's results in their of UB Ajanta which we have completely amalgamated into UBL. So a good year behind us.

Let us go a little bit more in detail. If we look at the total volume development over last year I already mention we had (+5%) which was in full driven by the growth in the strong segment which was even above 8% for us and thus our mild volumes as they did in the entire industry decreased. If you compare our achievement with the industry and we see a higher growth in the industry than ours and here the main reason for this is basically Tamil Nadu, when the new ordering policy was introduced in Tamil Nadu we had a high market share in a market which also happens to be a large market, so this kind of had a major influence on our figures for the year.



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In the last quarter the Q4 we have basically had a stable volume if you compare it with Q4 of the previous fiscal year and this compares with an industry growth of our estimate is 2%. This means that there is not only for us the last quarter was a little bit weaker than the rest of the year, it was also kind of a general industry matter. That is basically on the volume side what else can we say?

If we look at the development of pricing as you can already figure out a total year sales increase volume increase of 5% and sales revenue increase of 10% clearly points out that we have also been able in great part of the market to further introduce price increases or to achieve price increases which has been a good development because on the cost side we have been confronted with further kind of increases in raw material costs, in particular malt/barley which have partly been compensated by the further positive effects from the introduction of our patented bottle policy. That is I think the major trends, you have probably seen all our figures, so I would actually rather like repeating them again for what is on paper, give the floor to you for any specific questions.

Moderator Thank you very much sir. Participants we will now begin with the question and answer session. We have the first question from the line of Abneesh Roy from Edelweiss. Please go ahead.

Abneesh Roy My first question is if you could give us the volume growth in the other key states like Karnataka, Andhra, Maharashtra and some of the Eastern and the northern states?

PA Poonacha Of course we want to share the exact growth rate but on the key markets of Karnataka, Andhra and Maharashtra we have grown at high double digits.

Abneesh Roy And you said that the industry has grown at 2% in Q4, right?

PA Poonacha Yes.

Abneesh Roy How do you calculate this data, what is the source of this data?

PA Poonacha Where it is the government corporation, we get data from the corporation of course this data is (+90%) accurate, then we get in another states we get data from the excise records again it is (+90%) accurate hence we say our estimate of industry growth is 2%.

Abneesh Roy In cigarette what you have seen is in one of the state UP where the tax is very high, the tax is reversed because that state was losing a lot of volumes, in liquor I understand that interstate movement is very tough but what I want to know is in the last two years many states have hiked taxes abnormally high versus the last 10 years average, so obviously that is impacting volume which is visible, so any change in the thinking of the government we are seeing that this is counter-productive for them also from a medium to long-term prospective that tax rate growth might come down for them also?



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- PA Poonacha** No, I mean you cannot compare cigarettes to alcohol and beverages because cigarettes are a national subject or a country subject that is Central Excise and beverages like beer and spirits are a state subject and most state government's think differently as it is the second largest revenue earner after sales tax or VAT in each of the states hence depending on the state's requirement for revenue they tend to dip into the excise on spirits and beer.
- Abneesh Roy** So you think they are not likely to reduce their tax increased tendency based on the last two years volume growth data?
- PA Poonacha** No, we have never had a rollback of taxes especially excise duty in recent memory I have been in the business for close to 17 years now. I do not recollect any time wherein the excise duty in any state was first increased and then reduced, but as such what happens is in the year of increase either we have a small degrowth or flat volumes and then in the following year volumes picks up as the customer gets used to the higher price, so that is how history was, the industry bounces back in 15 to 18 months after the price increase.
- Abneesh Roy** My last question is now with a lot of state government's budgets behind us and in the past we have given a guidance of around 15% volume CAGR for the next five years long-term average, so how are you seeing FY14 in that context and what is the market share data specific in Andhra?
- PA Poonacha** We would not want to share specific data, all we will like to say is we are a little ahead of SAB Miller in Andhra and the market shares are neck to neck. What was your other question?
- Hans Van Zon** Your other question was with respect to what do we expect in the next future regarding industry growth?
- Abneesh Roy** FY14 not near term FY14 and 15?
- Hans Van Zon** That is always difficult to kind of comment on a specific year but in general we could say that the growth figures that we have seen in the previous years will be tempered is our expectation a little bit.
- Abneesh Roy** But tax hike has been pretty much on the lower side this time?
- Hans Van Zon** As far as I know in a couple of states already tax increase is announced and there is still some which are open.
- Moderator** We have the next question from the line of Krishnan Sambamoorthy from Fortune Equity Broker. Please go ahead.



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- Krishnan Sambamoorthy** Mr. Ganguly was quoted in Business Standard stating that there has been a realization increase in Andhra Pradesh is there a price increase that has been granted by the state government and if so what is the price increase that has been granted?
- PA Poonacha** No, price increase has been granted in the state of Andhra Pradesh, it is just that we have cut down our spends or discounts in the market.
- Krishnan Sambamoorthy** And the other thing is the Maharashtra Government increased the excise duty on strong beer in the latest state budget. We are two months into the current summer quarter, has there been an impact on the volumes of the same?
- PA Poonacha** Actually if you see whatever growth we are seeing is in the strong segment, we're not seeing any growth in mild beer.
- Krishnan Sambamoorthy** On a YoY basis as a result of this higher excise has there been any impact of volumes?
- PA Poonacha** While I cannot give you specifics here I can only give you a trends here, we're speaking about the quarter ended March.
- Krishnan Sambamoorthy** But we are already two months into the June quarter.
- PA Poonacha** But if I speak about the June quarter before the June quarter results is not what we would like to do.
- Krishnan Sambamoorthy** The final question that I have is regarding the working capital, there has been a 28% increase in inventory, 16% increase in debtors and 35% reduction in trade payables, has there been a deterioration in the working capital, what are the factors which have led to the same and is there likelihood of a sharp improvement going forward?
- PA Poonacha** This if you see the reduction in the trade payables has resulted in lower or more controlled variable costs, when we pay ahead we ensure that we have a cost advantage, so this is purely to a cost advantage if you see we have pulled back our cost of production and that is how we have remained profitable even with lower volume growth, that is on the payables. With respect to debtors going up, yes, our debtors have grown in line with the revenue growth it is nothing more than that. In fact our calculation internally of debtor's days has remained same as compared to 31st March, 2012, so there is no difference.
- Krishnan Sambamoorthy** And the inventory?
- PA Poonacha** Yes, inventory is little high and inventory is high because in the last financial year we were forced to import barley, so that we stem the growth of price in India which was on account of traders hoarding barley, so the minute we start importing, the prices in India have started



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falling and then we started buying it locally so that has resulted in higher stocks of barley which is what is showing in your 31st March numbers.

- Moderator** We have the next question from the line of Jasdeep Walia from Kotak. Please go ahead.
- Jasdeep Walia** If we look at your employ costs for the year it has gone up significantly YoY from around Rs. 188 crores last year to around Rs. 244 crores in this year whereas there has been a marginal increase in number of employees, could you elaborate on why has the employee cost increased so much and what would be the trend going forward?
- PA Poonacha** The increase this year need to be seen by removing a portion of which is towards a provision that we have made in the last quarter. This provision has been made with respect to likely claims that the management expects from agents who provide us contract labor at our various manufacturing units and we have made a one-time provision of Rs. 27 crores in the March quarter financials which towards these claims, so if you want to make a proper comparison it has to be after reducing this Rs. 27 crores.
- Jasdeep Walia** But this would be an ongoing expense, this would not be a one-off?
- PA Poonacha** It is one off, perfectly one-off.
- Jasdeep Walia** Because ultimately it goes towards paying labor only?
- PA Poonacha** No, it is on account of certain dues which the agents are demanding and that is why we were little cautious and made a provision, we expect this demand to come going forward, it is one-time and it will not come up again.
- Jasdeep Walia** Could you elaborate more on the nature of these provisions?
- PA Poonacha** No this is like I said towards manpower agents who provide us contract manpower at various units we have. This is a competitive information. We would not want to divulge further information on the nature of the payout.
- Jasdeep Walia** So after reducing this one off provision from the employee cost the rest of the employee cost, what is your opinion how much will it increase by next year?
- PA Poonacha** It will be in line with whatever we have done in the past there is nothing significantly change.
- Jasdeep Walia** What are they like to like numbers on the sales growth, EBITDA growth etc YoY excluding the merger which happened in fourth-quarter of last year?
- PA Poonacha** We have not done anything specific to this effect while if you see there has been organic growth so in the last quarter while the volumes have remained flat, that is UBL volumes,



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though industry grew at 2% the revenues have grown which in effect means there has been certain price increases and the price increases have moved to the profit line because we have controlled costs. So there have been an organic growth in profits it is just that we are not able to view it one because of this provision of Rs. 27 crores and two, because of the last year numbers have 12 months numbers of an entity which was merged in the last financial year that is financial year '12.

Jasdeep Walia

So you do not have the numbers are excluding the impact of that merger?

PA Poonacha

No, we have not done that.

Moderator

We have the next question from the line of Arun Mehra from AM Capital. Please go ahead.

Arun Mehra

This is regarding the tax within the current quarter if I understand this correctly the tax paid was pretty high during the current quarter around Rs. 27 crores, could you just throw some light on this please?

PA Poonacha

Because like I was explaining we have made a Rs. 27 crores provision in the books in the quarter ended March 2013 and this provision as you know that when you make a provision it is not tax deductible, so if you want to check the exact tax rate please add Rs. 27 crores to the profit and then calculate the tax rate.

Arun Mehra

So do you think that will be a more normalized tax rate if we do that?

PA Poonacha

Yes. Suppose your profit is X you add Rs. 27 crores and then take the quarterly tax and then take the percentage it would be in the region of 33% to 35%.

Moderator

We have the next follow-up question from the line of Abneesh Roy from Edelweiss. Please go ahead.

Abneesh Roy

A few follow up questions one is on the key raw material side like glass, malt barley, etc., how you seen the movement for you in the last three months and if you could compare it with the average price or YoY whichever you can that is the first question?

PA Poonacha

If you see our variable costs as a percentage of top line you can very well see FY13 is far better than what we have achieved in FY12, so that way there has been control in variable cost in FY13 this we have achieved through our patented bottles, the other costs, as all of us know that the financial year FY13 was very inflationary most other key inputs have gone up but however we have managed to control them through efficiencies and of course pulled back the overall increase through this patented bottle initiative.



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- Abneesh Roy** And in the past you have spoken on bigger factories, bigger distilleries is that exercise complete and the margin gain from patented bottle that is now behind us or there is some more room from there?
- PA Poonacha** No, I do not think it will be any other gains from patented bottles we have recorded most of the gains so going forward you will not see as a comparison to the previous year large gains on account of patented bottles. What is the other question?
- Abneesh Roy** From the economies of the scale we had planned to build a larger factories, etc., where is that etc. I understand that takes much more time, so if you can update us on the overall CAPEX planned in FY14 and on the economies of scale strategy where are we?
- PA Poonacha** No I mean wherever we are putting up new units we are ensuring that these units are large with the economies of scale but wherever they have already existing facilities yes, we are making attempts to increase the capacities but as you're aware that to increase capacities we require excise permission which are difficult to get in some cases, so wherever possible we have ensured that units are made of a size which are of a competitive operating level.
- Abneesh Roy** Coming back to Tamil Nadu is the base effect now there, so from Q1 will we see more normal numbers because the base will have that or when does the base effect?
- PA Poonacha** The base effect, September '13 will be very comparable to September '12.
- Abneesh Roy** Recently the main promoter Heineken has hiked the stake in the company?
- Hans Van Zon** No, if I may say something about it, this is a misunderstanding that has been triggered following a publication we legally formally had to do, publication of a transfer of shares that were held before by a company called SNIPL which was already a Heineken subsidiary after Heineken took over S&N and shares were transferred from this subsidiary to another Heineken subsidiary being Heineken UK for further formal reason, it was actually the very last step in the process of the merger or the takeover of the interests of S&N by Heineken, so this has not had any effect on the holdings of both promoters which are still completely in balance.
- Abneesh Roy** Last question if you see most other consumer segments we're seeing a slowdown in the premium product so if you could talk about the Heineken top end which was introduced a few quarters back and so any insight into the consumer behavior in the free market especially I'm not asking on the regulated markets, what are you finding from there in terms of key trends?
- Hans Van Zon** First question we have seen a decrease in premium product I'm not sure what you mean in there?
- Abneesh Roy** Percentage of sales and growth rates have they come down I understand they would still be growing but has the growth rate comes down drastically in terms of premium products?



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- Hans Van Zon** I do not think so because our premium products like to say if you look at our portfolio of Heineken is growing, our KF Ultra is growing very well and is doing very well we have further growth and development in our Kingfisher Blue, we have good growth and reception of our Kingfisher Red so I do not and cannot completely relate to your remark that the premium segment would not be growing any more.
- PA Poonacha** In fact Abneesh it is because of premiumization that we have been able to get the revenue increase higher than volume increase.
- Moderator** We have the next question from the line of Mayur Gathani from OHM Group. Please go ahead.
- Mayur Gathani** Just one simple question the volume growth for FY13 was 5%, is that correct?
- PA Poonacha** Yes.
- Mayur Gathani** And Quarter 4 there was a degrowth or was a flat volume?
- PA Poonacha** Flat.
- Mayur Gathani** We saw top line increase that was because of pricing increase?
- PA Poonacha** Not price increase as I said it is premiumization and price increase in some states.
- Moderator** We have the next question from the line of Hitesh Godani from Span Capitals. Please go ahead.
- Hitesh Godani** My first question is what is the CAPEX you incurred in the last year fiscal 13 and what are your plans for next two years?
- PA Poonacha** In fiscal '13 what has gone into the balance sheet as items capitalized is about Rs. 350 crores and going forward we do not make forward statements, but like I said we will be building capacities to ensure that we grow our business at a CAGR 15%, so whatever it needs we would invest.
- Hitesh Godani** And what is your existing gross debt level?
- PA Poonacha** Our gross debt is Rs. 1326 crores.
- Hitesh Godani** And what is your average cost of debt?
- PA Poonacha** You can calculate that.
- Hitesh Godani** And what that level debt-equity ratio we would be comfortable like now you are at 1:1 debt to equity so you would be comfortable at this or you want to reduce this debt level?



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- PA Poonacha** No such targets that the management has. If there is a business case tomorrow and investment in business is needed, we would do so, so it will be based on each business case.
- Hans Van Zon** In addition to that, what we can say is that we will have an investment planning and investment effort which is comparable to previous years, in the years to come which we will in the first instance attempt to finance out of our own means, out of our own cash flows and perhaps we will have to keep a watch and bridge certain gaps that we would have with some foreign borrowing but we do not expect it to be massive.
- Moderator** We have the next question from the line of Pankaj Chopra from Shanti Asset Management. Please go ahead.
- Pankaj Chopra** Could you tell us what is your capacity is and what is your level of utilization and do we see some kind of scarcity of capacity as of now for next year's growth?
- PA Poonacha** We will not say anything about the capacity available that we would not want to divulge but we currently are at close to 80% capacity utilization and considering the seasonality of the business we are almost there.
- Pankaj Chopra** And in the peak season largely is the summer is it?
- PA Poonacha** It is from March to end July.
- Pankaj Chopra** And the inventory increase will probably tend to stack up in March, is that the nature of your business?
- PA Poonacha** Yes, the inventory would stack up in March and it will remain high till end September and then it starts getting depleted because if we hold large quantities of barley for malting.
- Pankaj Chopra** The second question is could your comment on PAT of what you possibly seeing GST could have on your business, I mean and in which kind of parameters would that affect you?
- Hans Van Zon** May I first come back to what Mr. Poonacha said about capacity he mention in number but still you have to be very careful talking numbers capacity in brewing business and it is difficult in itself already because we have more number of breweries as you know in the breweries the capacity is build up out of different stages in the process of brewing beer as you know brewing beer is a complicated method it is not the same as just making a soft drink or something and the capacities are not always fully aligned of each stage in the process, that is one. Secondly you can sometimes increase a capacity of a brewery may be very simple, depending on where bottleneck is, small steps and some parts of the process can increase Capacity. In addition to that if you speak about some for instance say capacities in the bottling can also depending on what kind of shifts scheduled. You can easily increase capacity by adding an extra shift and in that sense it is extremely difficult to put out a percentage but as Mr. Poonacha has said we



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have no large overcapacities, however, we have flexibility so we are certainly able to produce what this year market will demand.

Pankaj Chopra If I could just squeeze in the same part of the capacity, it would be okay to assume that your debottlenecking could be done very quickly with small CAPEX to meet the?

Hans Van Zon Yeah.

Pankaj Chopra So that the large CAPEX may be a due later, right?

Hans Van Zon That you can do later if you look short-term, if you took long-term of course with the development we expect for the beer market, then you should not of course kind of wait until the last moment.

Pankaj Chopra Could you give us what you think would be the impact of GST on the beer business and what time it is will affect?

Hans Van Zon That is actually impossible to give a kind of relevant or realistic answer to, also in the first instance we do not know yet where the government is going with the GST and as an industry we would like to be fully included in this drive, comparable to all other industries but we do not know where the government stands yet on this, so it is a bit premature to say anything about it.

Pankaj Chopra Would it mean any kind of benefits in terms of logistics for you if it all it is included?

Hans Van Zon I do not think in particular, no I do not expect that. I think it would be a good thing for us if it is being introduced and we can be a part of the whole system let us say we have comparable advantage as anybody else, at least we do not have any disadvantage compared to others.

Pankaj Chopra I'm just taking the leaf of what Abneesh asked earlier about the premiumization, if you are seeing and what I infer from one of your responses was that it is the mix which has changed with the premium products that has helped you have higher revenue vis-à-vis the volume growth, is that the base effect or are you seeing there is premiumization in the market happening, what would be your take on that?

PA Poonacha It is not that the market is getting premiumized, it is just that wherever there is an opportunity to premiumize and meet consumer choices we have done it, so it depends on how consumer trends change.

Pankaj Chopra And do you see any white spaces in this segment that you operate in which is not cater to yet or it is too small to really create products or SKUs in that?

PA Poonacha As we see our belief is we have plugged every level the consumer wants.



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- Moderator** We have the next follow-up question from the line of Jasdeep Walia from Kotak. Please go ahead.
- Jasdeep Walia** Can you give us the volume numbers for the quarter and for the year excluding Tamil Nadu?
- PA Poonacha** I do not have it off hand.
- Jasdeep Walia** Or the growth numbers in terms of percentage?
- PA Poonacha** For the quarter UB has been flat.
- Jasdeep Walia** And excluding Tamil Nadu?
- PA Poonacha** I do not have those numbers.
- Jasdeep Walia** And for the year also you do not have the numbers?
- PA Poonacha** All growth rates including Tamil Nadu I can make an estimation. The overall growth rate is 5% that is inclusive of Tamil Nadu if you exclude Tamil Nadu it will be double-digit.
- Moderator** We have an expression from the line of Aditi Murkute from Iden Advisers. Please go ahead.
- Aditi Murkute** Basically this industry wise growth you said is a 4%, it is basically largely of the beer market or as a liquor industry?
- PA Poonacha** Where do you get 4%, we have not said 4% anywhere?
- Aditi Murkute** The growth of what this total growth was of how much?
- PA Poonacha** 5%, UBL has grown for the financial year ended March '13.
- Aditi Murkute** How much has the industry really grown?
- PA Poonacha** The industry has grown by 12%.
- Hans Van Zon** And it maybe it is good to add to that that if we speak about industry we speak about beer not about liquor.
- Moderator** As there are no further questions from the participants I would like to hand the call back to Mr. Harit Kapoor for closing comments, over to you, sir.
- Harit Kapoor** Thanks Shaima. On behalf of IDFC Securities I would like to thank all the participants on the call as well as the senior management of United Breweries for taking their time out for this call. Sir, would you have any closing remarks.



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Hans Van Zon

I thank you all very much for your attention and your interesting questions and we look forward to be with you again in a quarter from now. Our next board meeting will be in August as you know. Okay thank you.

Moderator

Ladies and gentlemen on behalf of IDFC Securities Ltd that concludes this conference call. Thank you for joining, you may now disconnect your lines. Thank you.