"Parag Milk Foods Q1 FY17 Conference Call"

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Moderator: Ladies and gentlemen good day and welcome to the Parag Milk Foods Q1FY17 Conference Call hosted by PhillipCapital (India) Private Limited. As a reminder all participant lines will be in the listen-only mode and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by entering * with 0 on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Jubil Jain from PhillipCapital. Thank you and over to you sir.

Jubil Jain: Hello. Warm welcome to everyone. On behalf of PhillipCapital I welcome you all to the Q1 FY17 Earnings Conference Call of Parag Milk Foods. On the call we have with us the senior management of Parag Milk Foods represented by Mr. Devendra Shah – Chairman, Mr. Bharat Kedia – CFO and Mr. Shirish Upadhyay – VP (Strategic Planning). We will commence the call with opening remarks from the management post which we will open the call for the Q&A session. Over to you sir.

Shirish Upadhyay: Thank you Jubil. Good evening. We welcome you all to this Conference Call on our Q1 numbers. I would now request our Chairman – Mr. Devendra Shah to give the opening remarks and then we will discuss the results further in detail.

Devendra Shah: Good evening everyone. On behalf of the board of directors and management I would like to extend very warm welcome to all of you present here for the earnings call of Parag Milk Foods Limited to discuss the results for the first quarter of financial year 2016-17. Before we discuss the financial performance of this quarter let me quickly share our business philosophy and provide a brief update on key business developments which took place during the quarter.

Parag Milk Foods sells 100% cow milk products which are healthy and nutritious. We follow an integrated business model which has helped us to pioneer in innovation. Our strong R&D capabilities have enabled us to emerge as a category creator and the category leader in many value added products with a strong emphasis on innovative packaging. We are continuously trying to increase our share of value added products which will help us to improve our operating margins and profitability in coming years. In dairy industry split between the quarters is not equal. Traditionally first quarter remains the smallest quarter for the year in terms of the top line. Similarly margin also remains low. This happened because of commodity market situation during the quarter. Lean season leads to increase in raw milk prices and there is a lag in terms of increased realizations we get from the market. Summers are also traditionally low in demand for all consumer products due to higher temperatures and vacations and related factors. This has therefore some impact on our quarterly performance and you may consider above aspects while analyzing the results.

While our overall top-line growth looks slower that is mainly because of continuous decline in the commodity sales, we have grown well in fresh milk business and continuously focused in new markets. Our growth in milk products is muted because of season as well as overall sluggish sentiments there that were prevailing in the sector. However, with onset of monsoon and good rains across the country we are witnessing bounce back in demand. Further festival season has also started, this supplemented with new innovations shall help us to continue growth momentum.

Coming to the quarter we have launched new products variants like Go Cheese wedges in herbs and spices flavor, Go Badam Milk Instant Mix, Gowardhan 10 Kg curd bucket. We are also planning to launch 3 or 4 new products in the coming quarter. We shall continue to focus on offering wide range variety and innovative products segment to our customers.

We are witnessing a rising expectation of our products in the market. We are focusing our branding efforts through the increase of both traditional marketing and digital marketing by having dedicated websites of the Go brand and the Pride of Cows brand. We continue to widen our distribution reach in the western region by opening a new depot in Jaipur. We are also planning to open three new depots in the northern and southern region in the coming period. During the quarter we have almost doubled our export sales on the global front. Russia and Malaysia are opening up their dairy sector presenting us a wider opportunity for the export of our value added products.

Now I request to Bharat Kedia – our CFO to discuss our financial performance during the first quarter.

Bharat Kedia: Good evening ladies & gentlemen. With the business update holistic presentation by the chairman I would straight away jump into the financials. The overall revenue from operations for the first quarter of financial year 2017 has increased by 2.6% to Rs. 383.5 crores from Rs. 373.8 crores in the same quarter 1 of the financial year 2016. Increase in revenue has come on account of higher volume and better improved mix of products. We also witnessed higher sales of new UHT products and new launches which has a better margin profile for us. During the first quarter of FY17 we saw an increase in the share of fresh milk from 20% to 24% in this quarter vis-à-vis the similar quarter of last year. Also revenue from fresh milk has increased by about 25% year on year from Rs. 75 crores to Rs. 93 crores. It was on the back of a better volume and price realization.

However, the share of the skimmed milk powder has continued to decline year on year and that has been the company’s strategy to focus on the products business which is reflecting in its revenue performance. Skimmed Milk powder business has decreased by 14% year on year compared to the first quarter of last year to this quarter of current year.

Milk products have maintained its share of business at 62% of the total revenue with an increase of 5% year on year compared to the first quarter of last year to the first quarter of this year. All of these in line with the strategy of the company of driving performance of the products and fresh milk business has allowed us to achieve an operating profit margin of Rs.

33 crores in the first quarter of financial year 2017 vis-à-vis Rs. 28.5 crores in the first quarter of financial year 2016. This is a healthy increase of 15.8% in operating profit.

Our operating profit margin has also improved from 7.6% in last year to 8.6% in this year which is a 98 basis points improvement on a year on year basis. The key drivers of improvement in operating margin are improved revenue mix towards value added products, increase in sale of fresh milk and decline in sale of skimmed milk powder. Company's net profit improved substantially to Rs. 10.8 crores in the first quarter of financial year 2017 versus Rs. 7.0 crores in the first quarter of financial year 2016. This represents a year on year growth of 54%, a significant improvement from where we had left last year. PAT margin expanded from 1.9% to 2.8%. This substantial increase is on account of EBITDA improvement that I just talked about plus on account of savings in the finance cost of about 17.5%. This savings in the finance cost has primarily resulted due to repayment of working capital debt from the money that had been generated from IPO. The company's effective tax rate has increased to a 26.5% in the first quarter of this year compared to 19.3% in the corresponding quarter last year. However, the effective tax rate of the company for the first quarter still remains lower than the full year of last year. Company's diluted EPF is Rs. 1.40 vis-à-vis Rs. 1.06 in the prior year. The number for quarter 1 financial year 2016, that is the first quarter of the last year are from unaudited financial results and therefore ladies & gentlemen to be relied upon accordingly.

To summarize the financial performance, the company has grown its revenue by 2.6% year on year, EBITDA by 15.8% year on year and profit by 54% year on year. That reflects the company's strategy of driving profitable growth. Thank you very much. With this we request Jubil to take it further.

Moderator: Thank you. Ladies & gentlemen we will now begin with the question and answer session. We will take the first question from the line of Dhruv Agarwal from Creseta Investment. Please go ahead.

Dhruv Agarwal: My question is I wanted the breakup of the net working capital cycle, the inventory days and debtor cycle, if you could please give it to me.

Bharat Kedia: Certainly, the business in which we are, where we are actually selling milk products, the inventory levels of milk products vis-à-vis a liquid milk is fairly different. We as an organization have about 2/3rd of our business coming from products and therefore our inventory levels are different. Cheese being a major part of our business, cheese carries a large set of inventory and therefore before I reflect the numbers on to the table please be assured that the nature of business this organization is some of these are part and parcel of life. So the inventory days of the company is about 90 days' inventory. Debtors days' ranges from 45 to 50 days and creditors days' range from 35 to 40 days. Net-net a working capital cycle of about 21% to 23% of revenue is something that we look that's the target

Dhruv Agarwal: And sir also if you could give that debt levels, the long term debt and the short term debt.

Bharat Kedia: The company's result before the IPO as we have reflected in our RHP was Rs. 400 crores. The company has started to reduce its debt level post IPO as the funds have reached to the company, company has started repayment. Company has almost repaid about Rs. 100 crores of its debt. Company's new debt level currently sitting is at about Rs. 300 crores. Of the Rs. 300 crores the debt which is in the nature of the working capital is about half of it and the debt in the nature of long term is about half of it.

Dhruv Agarwal: Oh okay, and if I could just squeeze in one question – do you give any volume numbers quarter on quarter or year on year?

Bharat Kedia: See in the business in which we are we have various products which are measured into different units and therefore consolidating one single volume number becomes difficult. However, to give you an overall perspective of the revenue growth that we have achieved in this year which is 2.6% is primarily a reflection of volume growth. The price increases that we have taken we have taken at the very backend of the quarter and the impact of that is only coming up into the quarter 2 and therefore primarily the growth has come through volume.

Moderator: We will take the next question from the line of Prasad Ghadala from Investec Capital. Please go ahead.

Prasad Ghadala: Can you give us a sense about pricing of the skimmed milk powder, what is the trend and pricing over there?

Bharat Kedia: Prices of raw milk have been increasing in the first quarter of this year vis-à-vis the first quarter of last year. However, the selling price of skimmed milk has been lower in the first quarter of this year vis-à-vis the first quarter of last year. This has actually posed a challenge as that you purchase milk at a higher price and you sell commodity at a lower price. However we are lucky as our business strategy has always been to drive products business. We have not suffered from that and in fact that has driven our profit margin ahead of the volume and revenue margin. Having said so, our dependence on the skimmed milk powder has been forced to decline with time and that strategy has fairly worked for us in a time which has been tough right now in terms of the commodity market.

Prasad Ghadala: So can you give an approximate number how much is it lower by?

Bharat Kedia: The price realization of skimmed milk powder in the first quarter of this year is about 6% to 7% lower than price realization under first quarter of last year.

Prasad Ghadala: And compared to Q-o-Q?

Bharat Kedia: Compared to Q-o-Q it is flattish.

Moderator: We will take the next question from the line of Bhaumik Bhatia from Girik Capital. Please go ahead.

Bhaumik Bhatia: My first question pertains to the relative weak revenue growth in the milk products business. Mr. Shah did allude to certain amount of weakness that is visible currently, but if you could throw some more light on which are the segments where within the milk product segment we are seeing weakness and how the future outlook looks like? And my second question would be on the sustainable tax rate going forward.

Shirish Upadhyay: Yes, I will just take you through the first part that is the revenue growth. Revenue growth looks a bit muted in the overall numbers, however as Mr. Shah and Mr. Bharat also explained earlier our commodity business has declined and that is in line with our strategy where we are decreasing our reliance on commodity business and therefore because of that business which anyhow contributes to roughly one-fifth of our revenue has some impact on the overall growth numbers. And as Mr. Shah further explained we have seen quite robust growth in our fresh milk business. That was because of the fact that we had opened few markets earlier and are seeing good growth momentum coming from those markets as well as our existing markets as well. In the milk products business per se as Mr. Shah explained earlier, overall the sentiment in the market were subdued, that was because of the fact that these summers were consecutive third set of summers with drought conditions and there had been compression in terms of demand especially from rural areas. And this has been a trend which has been observed all across the consumer sector and we had also been impacted a bit in terms of demand of few items as a part of our portfolio. So some of the newer products have done quite well but they are still at a lower base but overall we have seen some subdued demand, however post monsoons and rains have been quite good across the country. We are now seeing a solid bounce back in terms of demand and also our major consumption season has started with the festivals kicking in, so now we are looking at quite a good growth coming back and we are looking at covering the overall target in terms of achievement by end of this quarter.

Bhaumik Bhatia: So within the milk product segment would we be able to further dissect in terms of which are the segments where you have seen more pressure and which are the segments which are doing well?

Shirish Upadhyay: Particular segments like ghee have seen pressures because there was a big compression in demand and that also happens because of seasonality and other factors as well. So particularly during summer season consumption of those kind of items gets reduced overall and also this year particularly as I was discussing there have been some compression in demand basically in high value products.

Bhaumik Bhatia: And how is the cheese segment doing for you guys?

Shirish Upadhyay: Cheese segment is doing quite well, so again there is a bit of compression in terms of the overall growth but still it has done quite well during this quarter as well.

Bhaumik Bhatia: If you can answer the second question that I had asked in terms of sustainability of tax rate.

Bharat Kedia: So the effective tax rate for the financial year FY16 was 30%, the effective tax rate for the first quarter here is only about 26.5%. We believe as we finish the full year our effective tax rate will come back to about 30%. And that remains to be a sustainable tax rate as against the 34.61% which is the corporate tax rate due to the benefits of 80 (I)(B) that we enjoy we would be in the range of about 30%.

Moderator: The next question is from the line of Bhavin Cheda from Inam Holdings. Please go ahead.

Bhavin Cheda: What was the milk procurement per day in this quarter and how much it has grown on YoY basis and what was the procurement price? And the second one would be on what was the capacity utilization of cheese and ghee in the current quarter and update on whey protein business?

Shirish Upadhyay: Three things - #1 in terms of milk procurement there has been a volume growth as well. There is more volume growth which has come from the southern facility because that is what has been our focus in terms of growing our portfolio there and ramping up procurement in line with that. So overall our run-rate for this quarter is roughly around 1.05 million liters that is the procurement that we have done for this particular quarter and that is a growth of roughly around 3.3%. In terms of milk price as we discussed on the last call as well there had been an increase in milk price as the lean season has started and on a year-on-year basis we have seen an increase of roughly Rs. 5 per liter on a per liter basis. I forgot your third question.

Bhavin Cheda: The capacity utilization of cheese and ghee and the update on whey protein business.

Shirish Upadhyay: So cheese's is roughly around 80% plus as of now. Ghee being more seasonal in nature we do not look at quarterly utilization because we may manufacture some ahead of the season and stock it up and release in the market later as well. So it is better to look at annual utilization in those kinds of products. And the last one your part on the whey protein business, after getting fresh funds from IPO we have deployed money into that project and project is right now in the commissioning stage, so it may take 2-3 more months in terms of coming on line.

Bhavin Cheda: Just to follow up this Rs. 5 higher milk prices would be now close to Rs. 25 a liter in the quarter procurement price or it is higher than Rs. 25 a liter?

Shirish Upadhyay: A bit less than 25 but near 25.

Moderator: We will take the next question from the line of Nihal Jha from Edelweiss. Please go ahead.

Nihal Jha: Hi sir, good evening. My question is how is the competition in the hotel restaurant segment, the HORECA segment as you say, specially constrained that we have got a lot of capacity coming up especially in cheese from the competition. So just wanted your thoughts on that sir.

Shirish Upadhyay: We have seen some players who are coming up as competitors in that particular segment but we do not see those kind of players making much headway as of now. That is because of the fact that our major HORECA business that we do most of the products that we cater to this particular segment are more customized in nature and it takes time in terms of adapting to taste and preferences of each set of customers and devising specific products for them. And apart from quality of products you also need to create a PAN India distribution network, the service quality levels as well which matches with the kind of network that we have got. So time will tell how competition shapes up, but as of now we do not see much of a problem.

Moderator: We will take the next question from the line of Amnish Agarwal from Prabhudas Liladhar. Please go ahead.

Amnish Agarwal: My question is regarding the margin profile. If we compare our sales mix vis-à-vis some of our competitors, while we are more into value added products but still our margins are in single digits. So first part is that what is the outlook on the margins over the coming 2-3 years? Secondly, looking at the fact that we are going into whey proteins, we are launching more and more new value added products, so what is the outlook on advertising and giving these two balancing factors one is your more value added products and one is your need to spend more on advertising and distribution. So where do you see your profitability going?

Bharat Kedia: Yes, you are absolutely right. So we are also looking at improving margin profile as you are. We are in the right business with the right strategy to drive it. Having said so, as the business is getting stabilized over the last 6-7 years as we have moved into consumer product business, we have put a lot of thrust in driving distribution and branding. So when you compare with the peer industry which is not into as high as distribution and branding and more into the institutional sales which does not require a lot of it. The margin profiles are becoming incomparable. So if you look at a gross margin level of our business, our gross margins levels look very robust and in fact improving with quarter on quarter, year on year. Having said so a lot of that gets redeployed back in as an investment which is an expense into the P&L for driving a long term business of ours which is building distribution and branding. It is important for an organization of ours which is only shaping up for 7-8 years as we mature more and start to have a reasonable size of operations, this starts to pay off even more than it is getting expensed now. Having said so, in the long run, we would like to continue to invest more. We are actually increasing our advertisement expenditure as a percentage of revenue and our distribution cost as a percentage of revenue, because reaching out to Tier-3, Tier-4 cities is becoming more primary and important for us. And therefore as of now I would say in the life-cycle of the company where we are I think it would be little bit difficult and unfair to compare with the peer group who are not completely comparable in a sense they are more institutional than us. But certainly we should be able to drive the answer to your question in 3 to 5 years from now when we look at a significant expansion in the margins.

Amnish Agarwal: Okay, so you are looking at say the increase in advertising and distribution cost to be higher than growth in the sales?

Bharat Kedia: Yes, for a temporary period of 2 to 3 years we would be increasing advertising and distribution cost ahead of the increase in sales.

Amnish Agarwal: So then in that case are you confident of going into say in the next 1 or 2 years into double digits in terms of EBITDA margins or will they continue to hover here? What is the management vision for the next 1-2 years in terms of margins?

Bharat Kedia: So the guidance that we had laid out in our last call about a quarter ago is that the company's belief is that the PAT margin which is 2.9% at the end of FY16 in a longer term horizon of 3 years from then which is FY19 we are looking at a PAT margin exceeding 5%.

Amnish Agarwal: And sir my second and last question is regarding our new capacity additions. We currently have close to 2 million liters of processing capacity per day. And our milk procurement is close to 1 million liters. Now we are already in the process of expanding the capacity as per the RHP which was given to around 3-3.5 million liters. Do we plan to increase the procurement of milk in industry like you? Is it the right benchmark to look at the nameplate processing capacity and the utilization or to say in other words will the utilization level remains at 50% even after that or whatever actually are your plans regarding this?

Shirish Upadhyay: I think we discussed this point at length in our last call. Thing is that the processing capacity of 2 million liters a day is the input processing capacity. And we are more focused in terms of various value added products and it would be better to look at the capacities of value-added products, manufacture and against that the utilization. So the earlier question of Bhavin was much more focused in that regard, major products, their capacities and utilization and that would be the right benchmark to look at. So what we are doing as a part of RHP also we are expanding capacities #1 of those products where we have already reached the optimum capacity utilization. Say for example in case of cheese or further putting up a separate capacity called paneer, so those are the projects that we have lined up. And few of the new product categories that we are entering for example, beverages and others, so that is what we are investing in. And therefore capacity utilization of input milk would not be the right benchmark and also we discussed last time that over last 1.5-2 years we have been focusing in terms of bringing some milk from outside as well in terms of various commodities converting in value-added products and selling into the market. And probably that would not be counted in terms of my capacity utilization of input milk because it straight away goes into manufacturing of various value added products. So best is to look at output of various value added products and what is the growth in that.

Moderator: We will take the next question from the line of Bhaumik Bhatia from Girik Capital. Please go ahead.

Bhaumik Bhatia: Just wanted to delve a bit deeper in this PAT margin that you are saying which will expand from 2.9% to 5%, if I understand correctly you did mention that your A&P as a percentage of sales are going to go up for the next 2 years, right because you would be investing in brand building and so on and so forth. So if you can help us, walk us through the journey from 2.9 to 5 how much of it will be coming from say EBITDA margin expansion and how much probably from say some dated auction or something like that?

Bharat Kedia: So the margin expansion has 5 different factors and reasons for it. First our continuous thrust is on improving product mix which is basically selling more and more of milk products and fresh milk vis-à-vis the commodity. Those impacts margins very significantly as the margin from the products are fairly high compared to that of commodity. #2 our ability to drive price increase in the market vis-à-vis in comparison to the cost increase over and ahead the cost increase has been successfully seen over the last 2 years. We continue to drive our thrust on it and thereby driving margin. #3 we have two operational facilities, one in Maharashtra and the second in Andhra Pradesh. The operational facility of Andhra Pradesh is not fully utilized as of now. Over a period of three years we would be exhausting that facility on the existing platform that we have and thereby sweating those assets to drive economy of scale and thereby driving operating leverages. While our cost has been increasing on advertising and distribution we have been leveraging our cost down in other areas such as administrative staff cost and production cost. So these cost efficiency programs would drive results and last but not the least is that our interest cost burden is coming down as we have repaid partially the borrowing from the funds that we have raised through IPO. So this 5-point program is actually improving our margin from time to time.

Bhaumik Bhatia: Is there any further scope for debt reduction possible?

Bharat Kedia: Certainly so, as the company is generating profit, company is generating free cash flow. It is up to the board at the right point in time to decide how they want to utilize this, accumulated free cash flow that would be generated through organization. They could either go in the form of a reduction in debt or can go in the form of dividend, or can go in the form of further capital deployment. At this stage it would be hard for us to say how the board is going to make that call.

Moderator: The next question is from the line of Shailesh Kumar from Sunidhi Securities. Please go ahead.

Shailesh Kumar: Couple of questions. First thing, what is the composite EBITDA margin in the milk product segment and second thing, when we are harping so much on brand I mean we claim to be one of the top 2, 3 brand in dairy products especially cheese and all these things. And on the other hand we are talking of pushing our products in Tier-3 cities. So I was just wondering I mean consumption capacity of our metros in Tier-1 cities is only couple of thousands crores for cheese and whey product and protein things and all these things?

Bharat Kedia: So let me first take the first question. Unfortunately, the way the dairy FMCG business is structured it is difficult for us to generate and come up with a quantifiable number of EBITDA margin by product or by category. What we are providing is a composite operating profit of the whole organization which is already laid out both in presentation that is loaded plus to the stock exchange. The reason why it is so that the whole organization works on one raw material called milk and that raw material is common to everything of what we produce. The milk gets processed halfway through before it gets allocated to various lines and various production facilities and thereby we lose the ability of ours to clearly distinguish certain cost between those products and in addition to that the production facilities are composite producing various products together, therefore, we have not been able to get out with the EBITDA margin of a product level. Coming to your next and very important question is in terms of distribution reach to Tier-3, Tier-4 cities, the cheese is such a business where in India the market is fairly high on Tier-1 and Tier-2 city coming to your example of cheese. Cheese consumption in Tier-3 and Tier-4 city already very low, having said so this has been increasing. We want to tap that market before anyone else can do. Our expansion facility of distribution goes on route to market that has been redesigned by us to match with the needs, so we believe, specifically when it comes to cheese and obviously other products too that our expansion to Tier-3 and Tier-4 territories are the one where we are going to get most of the volume and value growth.

Shailesh Kumar: Just a question, total traded value of dairy as a commodity in India is, the market size is close to Rs. 5 trillion and cheese hardly couple of thousand crore rupees so don’t you think we have enough potential in our metros and Tier-1 cities first and then we should go into or we believe we have already exhausted that potential in Tier-1 cities and so left with no choice but to go to those markets and there is a push factor means we have high receivables and all these things, so what is the use of brand here I mean just was not able to reconcile so seeking your opinion.

Shirish Upadhyay: Yes you are right Shailesh, the thing is that as a company our focus is into value added products and with the net much higher value added product so our strategy is to move up the value ladder in different categories that we are into and therefore we are focusing into say categories like cheese or UHT, beverages or whey proteins which are going to be the growth drivers for us as a company. You rightly mentioned market is much wide available but we are not into those mass consumption products like say fresh milk or butter. While we are there in that as a category within that also our strategy is to move up within that as well. So we are not going to compete with large established players head-on into those mass market categories, our strategy is to move up market into premiumize kind of offerings and that is how we are moving ahead.

Shailesh Kumar: Okay.

Moderator: The next question is from the line of Varun Puria from Quant Capital. Please go ahead.

Varun Puria: Yes. Sir, we wanted to know in the whey protein segment, how does the entire supply chain work and in this who are the target audience in the whey segment.

Shirish Upadhyay: Okay, supply chain here is quite similar to rest of the FMCG products, so it is a similar distribution retail phenomenon, which happens. As far as target audience is concerned, see basically usage of whey has gone into range of various products but basically we classify mainly into two buckets, the first bucket is what we call functional foods and second bucket is what we call performance foods, so performance foods like sports drinks, muscle building powders and those kind of products which are taken by sportsmen or gym-going people for enhancing performance and then there are functional foods where lot of whey proteins getting added into infant food, into children drinks and into lot of other nutritional supplements so those are the various usages which are there in the market as of now.

Moderator: The next question is from the line of Aman Vij from Astute Investment. Please go ahead.

Aman Vij: I have two questions, one on the distribution, sir could you highlight numbers for this quarter as well as was there any increase in YOY and quarter-on-quarter, both distributor as well as retail reach?

Shirish Upadhyay: Yes, sir we don’t declare those numbers on a quarterly basis but obviously there has been an increase in absolute number of distributors as well as the retail outlets that we cover and as we were discussing earlier since quarter 1 remains a kind of low quarter for us, so obviously whatever groundwork that has been done and we will continue doing so, benefits will accrue in high consumption seasons like quarter 2 and quarter 3 for us.

Aman Bij: Okay sir and second question is regarding export business, sir this quarter we saw a very good growth from 8 odd crores to 15 crores, sir any new markets added this quarter and what was the reason for this good growth.

Shirish Upadhyay: Sir, there are two factors to it, #1. Obviously is the lower base of last year's first quarter and also we have added few markets and also in the existing markets we have expanded our portfolio so while we may be present in a particular market with only say 2 or 3 product lines, we have added few more product lines in those markets which has helped us in terms of growing in those areas.

Aman Bij: Okay sir, any major market added this quarter.

Shirish Upadhyay: This quarter, we added 2 to 3 markets but they are much smaller as of now in terms of our total base, so it may take some time in terms of shaping up.

Moderator: The next question is from the line of Jubil Jain from PhillipCapital. Please go ahead.

Jubil Jain: My first question is on capacity utilization at the AP plant, sir I remember in last quarter you had mentioned that the capacity utilization in the AP plant is actually lower than that in the Maharashtra plant, so currently you know what is going on in the AP plant and what is the strategy to you know improve the utilization levels there.

Bharat Kedia: Sir, as I stated in the early part of the discussion is that Andhra Pradesh plant is underutilized as of now. With the progress of the production that is happening in Andhra plant, we believe between two and a half years to about roughly three years, we should be on optimum capacity utilization in that plant, Shirish bhai also explained that the raw milk purchases that has increased, it has significantly increased in our Andhra plant this quarter on a year-on-year basis, obviously the production in increasing, procurement is increasing. The plant is gearing up for production; however, what has also happened this particular quarter is that our income which is the job work income or the conversion income to utilize this spare capacity has come down, some of the players into the market who has been procuring raw milk and selling commodity, they have seen the stress both sides of the in terms of pricing and therefore has not placed enough order with us for job work so the plant capacity utilization for our own production significantly increased but at the same time job work has come down slightly. This is in the right direction because that is what we want to achieve in a period of about 2 to 3 years, so we are actually moving in a very right direction for our Andhra plant.

Jubil Jain: Okay and second sir, kind of a bookkeeping question but does the gross profit include gains due to the revaluation of inventory because of the increase in cost prices, I mean what would be the contribution to the 450 bps of gross margin expansion because I mean what would be the contribution of revaluation of inventory to this 440 bps gross margin expansion.

Bharat Kedia: First of all the way inventory valuation works is that we are on a FIFO basis and therefore inventory that is purchased towards the end is kept into the balance sheet rather than revaluaing the existing inventory. We just keep exiting the early inventory and keep bringing in onto the balance sheet the newer inventory, so we don’t have a standard cost but we have an actual cost matter so that is one reason and therefore the impact of valuation of inventory cannot be identified as such as a separate number. Having said so it has an impact because as the milk prices have started to go up month-on-month in this quarter, as the later we purchased the last inventory is sitting on our balance sheet.

Jubil Jain: Okay sir, last question, what is the milk procurement target for FY17 and FY18, general ballpark figure?

Bharat Kedia: As we will, actually we as an organization believe in a long-term business rather than putting up a target for a short-term, so over a period of 3 years if we look in order for us to drive A) the volume growth, B) the profit margins, we would continue to drive procurement and we have through the IPO proceeds also committed certain funds to be utilized for improvement for driving the procurement increase of raw milk, having said so we have not been able for competition sensitivity reason able to lay out to the market a year-on-year target for procurement increase of raw milk.

Moderator: The next question is from the line of Sushmit P from Motilal Oswal. Please go ahead.

Sushmit P: Sir, I just wanted to understand until when will this skimmed milk powder rundown impacting the margins, there has to be some base effect which will then start helping us as well. We have already seen about two to three quarters of that impacting the profitability so you think there is only one quarter left, two quarters left of this business, the commodity business, rundown completing.

Shirish Upadhyay: Sushmit it is very difficult to pinpoint exact time in that regard because apart from domestic sectors skimming prices have some impact of global commodity price fluctuations, so globally people are viewing that by end of 2016, there might be some uptake in terms of pricing but it all depends what is the situation at that point of time and by that time what is the situation that happens in India as well, but it is a big difficult question as of now.

Sushmit P: And sir what was the percentage now as a percentage of topline in this quarter of skimmed milk.

Bharat Kedia: Skimmed milk powder is about 13% of total revenue.

Sushmit P: In Q1.

Bharat Kedia: In Q1.

Sushmit P: And what could have it been last year.

Bharat Kedia: 15%.

Moderator: The next question is from the line of Kishore Master from Jeojit Securities. Please go ahead.

Kishore Master: Yes, my question is, do you have any plan to enter the ice cream business.

Shirish Upadhyay: No sir.

Kishore Master: Ice cream business, you are not entering. Okay.

Moderator: The next question is from the line of Shailesh Kumar from Sunidhi Securities. Please go ahead.

Shailesh Kumar: Just checking if it is possible to give breakup of 239 crore of milk product revenue, so how much is ghee, how much is cheese, how much is whey and may be other products, or even in percentage terms that will do.

Bharat Kedia: Shailesh there are certain business information that the management of the company believes, they are very sensitive from a competitive perspective and therefore, we have decided that the information at which we dissect the total revenue would be in the parts of 4 which is the products, fresh milk, commodity called skimmed milk powder and others which is primarily the conversion income. Having said so as you have raised this particular question to satisfy the interest of yours if you can leave with us your e-mail id or number, we would be able to discuss that and get you some hints and briefs which will help you to follow on.

Shailesh Kumar: Yes, I will do it through your IR agency.

Bharat Kedia: Sure.

Moderator: We will take the next question from the line of Ritesh Vaidya from Ambit Capital. Please go ahead.

Ritesh Vaidya: Just a question on the working capital, you said you have inventory of around 90 days, how much of this would be finished goods inventory and how much of this would be work in progress.

Bharat Kedia: The inventory breakdown that of 90 days most of the inventory that we would have would be of finished goods except for cheese, cheese by its own nature requires to be ripened and aged and therefore it is primarily a working capital inventory. Having said so, the raw milk is, the inventory of raw milk is generally not there because the supply chain works on a daily basis and therefore the distinction between the inventory on work in progress and finished goods is not in the way the processing line works but in the way the products are lined up and therefore the inventory level of overall 90-days encompasses both of it.

Ritesh Vaidya: Okay, so I mean I was just trying to understand which milk product because the shelf life of product itself is limited, so I mean high inventory days which product will be ideally be, will it be more powder or something of that sir.

Bharat Kedia: Right, so from that perspective, I would say cheese would be a high level of inventory just because we have to keep it aging and ripening, milk powder would be also a high level of inventory because of seasonality in terms of production and seasonality in terms of sales.

Ritesh Vaidya: Okay, so these would be the two major items in the inventory.

Bharat Kedia: Yes sir.

Ritesh Vaidya: Okay and sir in your export business, wanted to know what are the kinds of products that you are exporting and what is the margin that you realize on these versus the domestic business.

Bharat Kedia: Products that we are focusing in export markets are basically paneer, cheese and ghee and recently we also started focusing on UHT and beverages as well, so these are the standard products which go into exports.

Ritesh Vaidya: Okay, fine and just if I may ask one more question was on the milk products business if you could give us some flavor on how are the beverages business and the UHT business is doing particularly in the milk product business.

Bharat Kedia: Sir, our UHT business which is milk and beverages is growing; in fact, it is one of those fastest growing category that we have. Our markets in Northeast and Uttarakhand and Kerala these kinds of states have really picked up, so the growth phenomena is reasonably high.

Ritesh Vaidya: Right and the fresh milk business which markets have you opened up, because it is a very steep rise of 25%.

Bharat Kedia: Yes, sir that is basically due to the newer markets that we opened up last year like Tamil Nadu, which has given us some growth and also some base effect in existing market.

Moderator: The next question is from the line of Aman Vij from Astut Investment. Please go ahead.

Aman Vij: Sir just one follow up question, the additional cheese capacity which was supposed to come sir is it online as of now or if not then by what time is it supposed to come.

Bharat Kedia: Sir, cheese manufacturing capacity is under expansion as we speak, as of now, we are within the 40 metric ton capacity that we had already laid out. We should be very soon able to increase the cheese manufacturing capacity as the work has really picked up very-very fast on this area.

Aman Bij: For one to two quarters or it could be little more.

Bharat Kedia: One two quarter.

Moderator: The next question is from the line of Manish Poddar from Religare Capital Market. Please go ahead.

Manish Poddar: Just sir one question actually, I don't know if this is addressed in the call earlier. On the cheese side, on the B2B segment, how difficult actually is to enter a vendor, you know from an operative point of view?

Bharat Kedia: Sir, you are looking more from QSR perspective right.

Manish Poddar: Right.

Bharat Kedia: Yes, so I would relatively say how easy it is to get into QSR, you just need to follow certain principles and rules which we follow very religiously in our organization. We need to have the agility in our business processes that means we should be able to produce cheese for the QSR which is differentiated and to his requirement. Number 2, we should be able to not only provide a good quality product, we must be able to provide a good quality service. When I mean service, as this QSR require some of these productions very fast, at short notices, requires changes as and when it is up to their state and number 3 you should know how do you market these products together in partnership with them in order to drive their business along with your business. If we follow these fundamental rules that are defined, I think getting there is easier rather than tougher.

Manish Poddar: Sir, I am just trying to understand that are the other players also trying to foray in the category, sir if that is, is that as easy as you are saying it to be.

Bharat Kedia: Yes, I think the differentiation that we are able to produce to the market vis-à-vis the other categories which we believe is that, the agility in our business, cheese is very large part of our business, in addition to cheese we also have a very big capacity on whey and we are expanding it further making the compliment to the cheese with whey, we are able to actually drive a lot of value addition. Our focus on cheese is very high because it is a very large business of ours. To our competition and that is our perspective to the business is that for them cheese is not a material part of their business and therefore their focus on drive on cheese could not have been as much as ours and therefore, we are able to really focus on drive. We have a dedicated team who works in and out, we have father of Mozzarella who works for us. So we got a team that has been laid up with the experience. We have been in this business for long time. We have the largest plant, second largest market share in this business, so all of that adds because we have been able to do it right at right time.

Moderator: Ladies and gentleman that was the last question. I would now like to hand the conference over to Mr. Jubil Jain for his closing comment.

Jubil Jain: I thank the management for their time and I would also like to thank everyone else for attending the call. Lizann you may close the call now, post-closing remarks from the management, over to you sir.

Devendra Shah: Thank you very much to each one of you, we look forward to see you again in the next quarter with better and sharper results as we all expect together, thank you.

Moderator: Thank you members of the management team. Ladies and gentleman, on behalf of PhillipCapital that concludes this conference, thanks for joining us and you may now disconnect your lines.