



“Parag Milk Foods’ Q1 FY18 Post Results Conference Call”

August 11, 2017



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*Parag Milk Foods Limited
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Moderator: Ladies and gentlemen, good day and welcome to the Parag Milk Foods' Q1 FY18 Post Results Conference Call hosted by Edelweiss Broking. As a reminder, all participant lines will be in the listen-only mode. There will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference, please signal an operator by pressing * then 0 on your touchtone phone. I now hand the conference over to Ms. Sangeeta Tripathi from Edelweiss Broking. Thank you and over to you.

Sangeeta Tripathi: Thank you, operator. Good evening everybody. On behalf of Edelweiss Broking, it gives me a great pleasure to have the management of Parag Milk Foods with us to discuss about the Q1 FY18 performance and the outlook ahead. From the management we have with us, Mr. Devendra Shah – Chairman; Mr. Mahesh Israni – Chief Marketing Officer; Ms. Akshali Shah – Vice President Strategy and Marketing; Ms. Natasha Kedia – Investor Relations; Mr. Deepak Jain – Senior Manager, Finance along with Mr. Shirish Upadhyay –Advisor to the company's management. I would like to hand the call to Ms. Natasha Kedia. Over to you.

Natasha Kedia: Thank you, Sangeeta. We will now begin with insights from the business developments and the financial performance of Q1 FY18. Without any further delay, I will now hand it over to Mr. Devendra Shah, Chairman of our Company. Over to you sir.

Devendra Shah: Good evening everyone. On behalf of the Board of Directors and Management I would like to extend a very warm welcome to all of you present here for the earnings call of Parag Milk Foods Limited to discuss results for the first quarter of FY18.

Let me begin by congratulating all our stake holders from farmers, distributors, retailers, employees, management to you all Shareholders, on the hat trick of awards that your company has received this year.

In the last con-call we spoke about the Most Trusted Brand Award for Gowardhan Ghee for the 2nd consecutive year and moving 132 notches in the overall brand ranking up to 303 from 435 which is a rare phenomenon. Post this, we received the "Consumer Voice Award" again for Gowardhan Ghee in the Cow Ghee Category. To add to this as a hat trick, Parag has been ranked No.1 in the Next 500 companies by Fortune India.

Our Thrust on our Strategic Focus Areas continues with renewed vigor. One of the priority area identified was supply chain strengthening and distribution expansion with Focus on Freshness. Towards this endeavor, our work with Vector Consulting is on the right track.

Implementation of GST is considered to be very welcome move by the business community. We appreciate efforts made by the government to execute such an extensive plan for the country. With implementation of GST, we would now be able to take input tax credits for excise on packaging material, service tax & octroi, etc.

For a company such as ours with multi-state operations, GST will drive operational efficiencies by reducing the complexity of inter-state transportation and uniform law across states. This will also allow us to reconfigure our logistics and rationalizing our depot operations.

In regard to the GST implementation, we witnessed pre-GST destocking in the last two weeks of June, which has impacted our growth during this quarter. But early trends post 1st July, indicate that there was no major loss of consumer sales and the pipeline filling at retail level is getting back. And we were fully prepared with our back end work on the same.

Apart from the GST impact, Maharashtra also saw the farmers strike which impacted our liquid milk dispatches. Post the price increase we took across our products to combat the sharp increase in milk prices in Q3FY17, we haven't taken any further price increases. Also there has been some impact on cheese institutional and exports sales due to price correction. These factors have led to a temporary loss of sales and the same has now been nullified.

On the operations front our new Paneer plant is now operational and the distribution expansion across the country is under progress

Also post the soft launch of Avvatar our 100% absolute whey protein, during the last quarter, we are now into the expansion mode with a plan to cover all major markets with direct distribution and with the e-commerce business. This being a new category for us, the last quarter has gone in learning on fine tuning our route to market strategy. We now have aggressive expansion plans on this product. We also have certification from Informed Sports which certifies Avvatar being free from any abusive substances. The marketing campaigns will focus on key influencers like Gym trainers, nutritionists and dieticians apart from digital plans.

We also test launched our mango drink Slurp during this quarter. The markets chosen were Mumbai, Delhi, Kanpur and Chennai. Now with learnings from this test launch, we have national expansion plans being readied which will be implemented over the next 2 quarters. The USP of this product is it is made from 100% alphonso mango with a dash of milk and that gives us confidence of getting into the large Rs.6000/- crore fruit juice market with this key differentiator. Our marketing campaign revolves around "Yeh Aam, Aam Nahi" and will be exemplified across digital, consumer sampling and point of consumption stores.

I would also like to let you know that we have short-listed candidates for our CFO position and are currently in the process of finalizing a suitable candidate for the position.

Finally, I would like to end by saying that all these initiatives stand testimony to our long term objective of transforming your company into a FMCG dairy company with focus on health & nutrition.

Now, I request Deepak Jain from our Finance team, to discuss our financial performance of Q1FY18.

Deepak Jain:

Good evening, ladies and gentlemen. The revenue from operation for Q1FY18 have grown by 7.7% to Rs. 412.8 crores compared to Rs. 383.5 crores in quarter Q1FY17. Our Q1FY18 revenue year-on-year increase was driven by growth in the consumer product segment and expansion of our distribution network. Consumer product category observed an 8% growth from Rs. 238.9 crores to 257.7 crores in quarter Q1FY18. However due to GST lead destocking in the second half of June, we saw an impact on the overall growth. Fresh milk growth was lower than expected at 5% year-on-year due to farmer strikes in the months of May and June which caused delay in distribution in supply of milk. The share of skimmed milk powder remained stable year-on-year at 12.5% along with an increase in its revenue by 7% year-on-year from Rs. 48.1 crores in Q1FY17 to Rs. 51.4 crores in Q1FY18, which is mainly due to better realization in the market.

The company has seen a marginal increase in gross margin of 40 bps from 28.6% in quarter one FY17 to 29% in Q1FY18. The raw milk prices were higher year-on-year in Q1FY18 which was offset with an increase in price in products. Company's EBITDA declined by 120 bps from Rs. 31.8 crores in the Q1FY17 to Rs. 29.4 crores in the Q1FY18. The impact on EBITDA margin was due to higher expenditure on marketing and distribution. The increase in depreciation from Rs. 9.8 crores in Q1FY17 to Rs. 11.6 crores in Q1FY18 was offset by a decrease in the finance cost from Rs. 9.6 crores in Q1FY 17 to Rs. 7.9 crores in Q1FY18.

Company's net profit has increased by 3% from Rs. 10.2 crores in Q1FY17 to Rs. 10.5 crores in Q1FY18. PAT margin remained stable at 2.5% in Q1FY18 as compared to 2.7% in Q1FY17.

Natasha Kedia:

Thank you team for the insights into the business developments and financial performance of the quarter gone by. We would now like to open the floor for further questions.

Moderator:

Thank you very much sir. We will now begin the question and answer session. We have our first question from the line of Dhaval Mehta from Emkay Global. Please go ahead.

Dhaval Mehta:

Sir my question is pertaining to our consumer product portfolio. So if you see the growth rate on the consumer product portfolio is around 8% which is lower than what we have envisaged earlier. So especially after in the month of January, we have taken a price hike of around 8%. So it means the volumes will be in the negative trajectory. So what are the main factors that we have not been able to deliver on our consumer product portfolio from last few quarters?

Shirish Upadhyay:

Particularly this quarter Q1, we have already informed just now, there were two major issues we get involved. One was obviously implementation of GST led to de-stocking of the entire pipeline particularly into category like ghee where there was a significant change in terms of GST rates and therefore traders wanted to empty their pipeline during the implementation phase. So that was one reason and another reason as we discussed was some effect that we faced in terms of

cheese business, within that particularly export and institutional business where because of hardening of Indian rupee and the increase in terms of pricing in domestic market. We lost business for a temporary period of 2-3 months.

Dhaval Mehta: So you lost business in the cheese category?

Shirish Upadhyay: Institution and export part of this business.

Dhaval Mehta: Okay. So coming to the cheese category, so basically our production has increased by around 50% but still the revenue is not getting reflected. Is the competitive intensity of the category increased in the last few quarters especially after Amul's new capacity being operational, being commissioned?

Mahesh Israni: Let me answer this in two parts. One, as Shirish earlier mentioned saying that in the quarter one numbers you will see a slight dip against the growth expectation that we had, it was primarily because the rupee appreciated against the dollar and we were slightly out-priced in that sense in the exports market which led to a temporary dip and a similar phenomenon was seen in the institutional business but that had nothing to do with Amul. I think it is the overall sentiment of the consumer which was low and hence there was an offtake which was slightly lower in the QSR segment which has led to this decline. I do not think there is Amul in fact which is visible even now. If there is any, we are prepared for it.

Dhaval Mehta: Okay. Sir my second question is on the Ghee category. So how have been the offtakes post July because of the higher GST rate? The prices at the retail level would have increased. So how has been the offtake post the GST era in the ghee category?

Mahesh Israni: Yes. I would look at it from both the pre-GST era and the post-GST era. As a marketer, frankly speaking if there is de-stocking at the trade level and if my consumer offtakes don't go down, I am not worried because it is easier to build back the pipeline at the retail level and our dipstick in the market actually showed us that there was no consumer offtake which declined, there was only a dip in the trade stocking which had happened which has now come back. I mean if I see the early signs in July month, there has been a decent pipeline, re-stocking to use the right word against the destocking which has happened. In terms of the pricing, we have factored in the GST rates as end June and we took a marginal price correction in the month of July on the ghee MRPs.

Dhaval Mehta: Okay. So basically the end product prices have been same at Rs. 540, it has not changed, right?

Mahesh Israni: It has just taken an increase of Rs. 10.

Management: There was a Rs. 10 increase in the MRP.

- Moderator:** Thank you. We have the next question from the line of Kaustubh Gokhale from SKS Capital. Please go ahead.
- Kaustubh Gokhale:** Just wanted to know at 100% capacity utilization, how much sales can you generate from your Avvatar product?
- Mahesh Israni:** See, the Avvatar line which is there for packaging, it has 3 elements into it. The plant has got 3 parts to it. One is the basic product which is WPC and second is when you do a next level of filtration, it comes to a grade which is used as ingredients in basic foods and pharma and the final nano-filtration stage gives us the product which is useable as the direct consumer product which is what Avvatar is.
- Kaustubh Gokhale:** My question only pertains to the direct consumer product.
- Mahesh Israni:** I am coming to that. In any business mix, you cannot have only one product; even if I make only Avvatar there will be a certain element of WPC which will get reduced as the process of filtration, and hence the right mix of the plant for producing all the three were also recognized at the level two of filtration, we have a certain amount of commitment which would have been given in the past for the pharma and baby food industry that also need to be sort of aligned with. The mix of the three is enough to handle the current capacity expansion of cheese which has gone up from 40 MT/day to 60 MT/day.
- Kaustubh Gokhale:** But it still doesn't answer my question. What I am trying to understand is, the product which goes directly to the consumer, am I correct the market size is about 1,000 crores in India, right?
- Mahesh Israni:** If I was to produce only Avvatar and not produce the midlevel intermediate, I would be able to produce 4 tonnes per day.
- Kaustubh Gokhale:** Okay. But what I am trying to understand is how much sales can you actually generate from this if your market size, I mean how much market do you aim to capture in the next 2 to 3 years. Out of the total domestic market share, how much market share is Parag in the product that goes directly to the consumer in the next 2 to 3 years?
- Mahesh Israni:** See, if you look at the way we are going around the product, it was a completely new product category for us which requires a very different route to market strategy. Having done a soft launch in the last quarter, it has taken us 4 months to ensure that we get the strategy right in terms of our learning and moving forward. Having done that now, we are now getting into the expansion mode and we will complete our national expansion in the desired market as per the plan of phase I by the end of the next quarter and at the same time we will go into the e-Commerce business. And hence only after doing a national expansion, doing the right things behind the brand will you come to know how much is the market share of what kind of a product that you want to look at in terms of the volumes and the values. It will be a very difficult...

- Kaustubh Gokhale:** So this year you are saying that whey won't contribute much to your financials, Avvatar?
- Shirish Upadhyay:** See, let me address this in three different parts. So first is that you cannot look at whey as a business in isolation. Whey is a byproduct of cheese manufacture and therefore you cannot hypothetically look at what is the maximum that you can realize out of the whey category because production of whey is not something which is independent, it is linked with cheese production and therefore of demand of cheese that is produced, that is part one. Part two here what Mahesh was trying to mention was that this is a bouquet of different product, it is not just a single product.
- Kaustubh Gokhale:** Yes. So I understand all of this, I don't want to take up much time, but the point I am trying to get to is that if you could give us some direction because you have given guidance on PAT margins, you have said that your target is to reach 5% in the next 3 years, I understand that whey is higher margin than cheese, you can't reach your 5% target without getting some clarity on how much sales your Avvatar product will be able to contribute to your overall financials in the next year because how are you going to reach that 5% margin target is what I am trying to understand without giving some clarity on whey, when yourself don't know how much market share you will be able to gather till at least 6 months.
- Shirish Upadhyay:** Yes. There are two different things and unrelated things I think because Avvatar or its contribution to total margin improvement is not 1:1. There are lot of other products which are also contributing and not just products which is changing product mix itself which is happening, it is cost savings that we are trying to do, so lot of other things which are contributing to the margin expansion. So we have discussed this in detail in our last two con-calls, I don't think we should get into details so there we have discussed how the margin expansion is going to happen at all the 3 levels at the gross margin level, EBITDA level as well as the PAT level and what we can tell you with a confidence is the kind of product mix and the kind of market, we are on track in terms of achieving the medium term guidance.
- Moderator:** Thank you. We have our next question from the line of Mr. Navin Kulkarni from Phillip Capital. Please go ahead.
- Navin Kulkarni:** Sir I have the question on the PAT margins that you have guided for 5% over the next 2-3 year kind of a timeframe. So is this margin inclusive of the GST benefits that you might see on the input tax credit as well as some benefits that you might see on logistics cost. So are they excluded in the margin calculation that you have guided for and also could you quantify the savings that we might see on account of GST coming through in this year or probably the year after this?
- Deepak Jain:** So Navin, this 5% guidance which we have given in our Q4 presentation, we have not considered the GST impact. The benefit which we will get from the GST is the input tax credit on the service tax and the Octroi which we are paying in the Maharashtra. These benefits will be seen in the coming quarters and the coming periods.

- Navin Kulkarni:** So is it possible to provide any kind of number on how much Octroi you have been paying currently and what it would mean in terms of the bump up on the PAT number we could be looking at in the forthcoming quarters?
- Deepak Jain:** Well, it would be very hard at this moment to quantify it in terms of the number. But after 1 or 2 quarters, it will be easy for us to get the real impact from the GST. As of now we are seeing that we will get the multiple benefit from GST and you may refer our annual report where you will get the expense details and derive GST impact.
- Moderator:** Thank you. We have our next question from the line of Shailesh Kumar from Sunidhi Securities. Please go ahead.
- Shailesh Kumar:** I would like to know what kind of average daily procurement we have seen during Q1 FY18, raw milk?
- Deepak Jain:** On an average, we procure around 12 lakhs liters per day. We have an installed milk processing capacity of 20 lakhs liter per day procurement capacity.
- Shailesh Kumar:** During Q1 FY18?
- Deepak Jain:** Q1 FY18 there was little bit blip due to the farmer strikes in the June and the May month. So we have procured around 5% lower than what we have procured in the Q1FY17.
- Shailesh Kumar:** So Q1FY17 was what? 12 lakh litres itself?
- Deepak Jain:** So it was roughly around 10.5 LLPD.
- Shailesh Kumar:** Q1 FY17 was 10.5 LLPD?
- Shirish Upadhyay:** Right.
- Shailesh Kumar:** And we have procured 5% less, YoY basis?
- Shirish Upadhyay:** Yes.
- Shailesh Kumar:** During the initial presentation you have mentioned that our marketing and distribution spend had gone up YoY basis. So it will help if you can quantify what has been our marketing spend in Q1 FY18 vis-à-vis FY17?
- Deepak Jain:** In this quarter, there was major increase in the other expenses. It is primarily due to our new product launches like Avvatar and the Slurp. So these are the new products we have launched in the quarter one. If you see year-on-year, we have also increased our depots, so the new depot

rent and expenses contributed to the other expenses. Apart from that we also appointed Vector Consulting, so their initial expenses also contributed to the other expenses. These are the major items that contributed to the other expenses going up.

Shailesh Kumar: Okay. So if you can't quantify, if you could just tell me what has been YoY growth because of these particular items which you had just mentioned?

Mahesh Israni: I think the numbers are in line with whatever was there in last year and as far as percentage of sales is concerned, and while there might be a little disruption quarter-on-quarter because of lower base of a particular quarter, but on an annualized basis our annual marketing spend was roughly around 2.7%-2.8%, would be in the range this year as well. So we are in range on an annualized basis.

Shailesh Kumar: Have you seen any kind of raw material price increase during this quarter on YoY basis and...?

Deepak Jain: No increase.

Shailesh Kumar: YoY, it was flat?

Deepak Jain: Yes.

Moderator: Thank you. We have our next question from the line of Aniruddha Joshi from ICICI Securities. Please go ahead.

Aniruddha Joshi: Sir, just two questions. One, in this dairy industry as the EBIT margins are somewhere around 6%-7%. So the ad spend remains around 1%-2% of net sales. So we have seen players like Amul or Mother Dairy, they have only one brand and all the products of that Dairy companies or cooperatives are launched under just one brand as Amul or Mother Dairy. Whereas in case of Parag, we have launched multiple products, Gowardhan, Slurp, Avvatar. For every new product, we are in a sense actually a new brand itself. So any particular reason, because probably we may not be able to support so many brands considering the profit margins somewhere around 6%.

Mahesh Israni: Aniruddha, I think it is a very valid question and a right comparison. Let me answer this in two parts. Why do I have multiple brands? I mean the organization strategy as we move on the path of being an FMCG dairy company, you need to have a very defined personality for each of the brands and hence in which categories will the brands play. In that sense, it warranted us to have at least 4 major brands and that is what you will see in terms of whatever support we give around those four brands. The other two brands will be flanking brands in nature and they will continue to be that way throughout. In terms of comparison to a brand like let us say an Amul or a Mother Dairy where they spend a certain amount of the A&P spends on what we spend, apart from the A&P spends that you see in the P&L which is close to about 2.5% to 3% annualized. A large portion of what we do around the brands in terms of BTL initiatives, consumer sampling,

bringing alive the brand at the trade level, so on and so forth have actually knocked off from the revenue itself and that is a pretty high spend of close to about 6%. So net-net if I look at the spends on the brand, it is close to about 8.5% to 9%. As we move forward, once we have a well-established distribution model and strong trade connect, some amount of this BTL initiatives which get knocked off from the revenue might actually get transferred to the A&P spends and you will see A&P spends in the range of 3.5% to 4%. Also, as we grow over the next 3 years, obviously there will be a topline increase which will happen and hence the absolutes, both in terms of the larger topline and as a percentage of 3.5% to 4%, will mean a suitable budget to support at least 3-4 brands. Within those 3-4 brands, obviously the marketing campaigns are strategically well designed there to support a large amount of the money beyond the new brand. So for example if Avvatar is one of the focus brands for the current year, bulk of my spends are going to go behind Avvatar and Go, Gowardhan will have a sustenance kind of a marketing support. Once Avvatar gets established over the next 12-18 months, you might see some other category which comes into focus where I will have a disproportionate spend and the other three will have a sustenance kind of a support. Our internal marketing strategy in a sense is well articulated and eventually as good marketers we need to get bang for your money. And I think we are in the right course in that direction.

Aniruddha Joshi: Okay. Thanks for it. So probably if we launch any new product right now, let us say in one year, two year down the line, will it be under the current 6-7 brands or again it will be new brand that you will be looking at, or in terms of the brand launches we have completed the entire portfolio of brands, right?

Mahesh Israni: Yes. From the next 3-years horizon, we will not be adding any new brand. You will have category expansions happening, but you will not have a new brand. So any of the new category we get in will either be under the Go, Gowardhan or the Avvatar brand.

Devendra Shah: Or sub brand. Sometimes we use a sub brand.

Aniruddha Joshi: Okay. Sir just last question, on the Pride of Cows, we have seen the premium milk market is growing pretty well and the new players have also entered the market such as Sarda, which is from Nashik. Again, 2-3 more products in terms of Dahi is also there or even they have also launched Ghee. So do we have any such plans considering the increase in competitive pressure and also secondly do we have any plans to launch any products from the Pride of Cows portfolio?

Natasha Kedia: I think the business model which has been designed behind Pride of Cows is a by invitation brand. It will continue to focus on the mainstream milk and it will remain at that level of milk. At best if we want to add something, we might add a couple of categories but they will still fall under the by invitation home delivery model. I never intend to go on to the shelf. And if you look at the other product categories, typically they are picked up off the shelf and only milk is the product which gets delivered at home. So the main focus of the brand will continue to be behind just a milk.

- Moderator:** Thank you. We have our next question from the line of Sanidhya Daga from Athena Investments. Please go ahead.
- Sanidhya Daga:** Firstly, could you give me a breakup of the kind of revenue that your different products have given for Q1 for whey, cheese, fresh milk and ghee?
- Natasha Kedia:** Sorry we don't give out that data every quarter. We give it out on an annualized basis.
- Sanidhya Daga:** Okay. So if we come to cheese, our cheese capacity per day in terms of tonnes ramped up from 40 to 60. So that has happened Q1 of 18 or prior to that?
- Natasha Kedia:** It happened in Q1 of 18.
- Sanidhya Daga:** So what is the kind of capacity utilization that we are running at currently?
- Natasha Kedia:** Approximately 60%-65%.
- Sanidhya Daga:** And how we are planning to ramp up that and what is the maximum capacity we can run at?
- Natasha Kedia:** 85% of the installed capacity. So typically any plant in the Dairy industry would run at an 85% installed capacity. So out of the capacity roughly 85% of that would mean 52-53 tonnes per day.
- Sanidhya Daga:** Okay. And that would happen in this FY or the next FY? When would that happen?
- Natasha Kedia:** No. Any kind of plant expansion that you look at, it is not linear in nature. It is done one time and you typically have a 2-3 year time horizon where you put up a plant.
- Sanidhya Daga:** Right. And like typically how many days in a year does the production run, is it 365 or less than that?
- Management:** 365 days in a year.
- Moderator:** Thank you. We have the next question from the line of Jinal Fofalia from AlfAccurate Advisors. Please go ahead.
- Jinal Fofalia:** Sir could you tell us the average procurement price, what was it in Q1 FY18 versus Q1 FY17?
- Natasha Kedia:** Sorry, we actually don't disclose that information, it is competition sensitive for us.
- Jinal Fofalia:** Sir, second thing, hence we are expanding huge by launching new brands, then why aren't we thinking to acquire more brands and go in that direction rather than spending lot on brands. So any highlights on that please?

- Natasha Kedia:** I thought we answered that question in the couple of questions before on why do we have this multi-brand strategy and what is our intent in terms of getting into the relevant product categories.
- Jinal Fofalia:** Okay. Sir, are we looking for any acquisitions going forward?
- Natasha Kedia:** No, not at this stage.
- Moderator:** Thank you. We have a next question from the line of Jasdeep from Infina Finance. Please go ahead.
- Jasdeep:** Sir, how many number of VISI coolers have you put out in the market? How has this number increased YoY?
- Mahesh Israni:** See, I mean it is a planned this thing. We will have to get the details. I mean I would not have the exact numbers right now but it is as per the plan. So basically we plan for example as a part of the IPO spend and we have gone ahead and procured those kind of VISI coolers that are there in the market, yes.
- Jasdeep:** Sir, any kind of percentage number, that you can indicate? Percentage number in terms of increase in the number of VISI coolers deployed in the market?
- Mahesh Israni:** Increase would be multifold, so the increase does not even make sense, I mean if my base x it will be more than 5x today.
- Moderator:** Thank you. We have the next question from the line of Mehul Desai from IDFC Securities. Please go ahead.
- Harith:** This is Harith here. So just couple of things. Firstly, what is the price increase component in your topline growth in milk products because I know you took one in Q4. Any further price increase you took in Q1?
- Shirish Upadhyay:** There was no further price increase in Q1. We had taken price increase in Q3 and subsequent price increase in Q4. Overall for milk products the price increase was in the range of around 12%-13%.
- Harith:** And just to get your sense on the volume demand situation, do you see a significant recovery Q2 onwards because now that the GST part is kind of behind us at least the bulk of it, can you now get back in the balance of the year to a double digit growth trajectory, do you see that given the fact that you are also investing in branding etc.?

- Natasha Kedia:** Early signals are yes because you just look at the July data, we are also entering into the festive season time. So starting from August till end January is a typical season time for the business.
- Harith:** And last thing was on the margin front, so Shirish, do you think this 12%-13% price increase now will suffice to take care of the gross margins as it has in this quarter as well. So we have already seen too much of an impact given the fact that also milk prices quarter-on-quarter haven't done much, in fact it probably would have come off a little bit. So in this environment maintaining our gross margin similar to what you did in Q1 is more likely going forward?
- Shirish Upadhyay:** Yes. So gross margins would remain in a similar band. There is probability of further expansion of 100-200 basis points going down the year because as you rightly mentioned there is good monsoon down the line, we are looking at a little softening of prices going forward in Q3 particularly. So overall we look at a little bit of expansion in terms of margins at a gross level.
- Moderator:** Thank you. We have the next question from the line of Dhaval Mehta from Emkay Global. Please go ahead.
- Dhaval Mehta:** Sir as you told that the milk prices are expected to basically come down in Q3, what you expected after two consecutive years of good monsoon especially in Maharashtra, so did it settle at around 25-26 levels which is ideally a win-win situation for the farmer as well as the company.
- Shirish Upadhyay:** No. So there won't be much decrease that we are looking at. There are two things: the price decrease that is going to happen will only happen post September, so post the Diwali purchases are done and those will last only till end of January or February. And in terms of quantum also, we don't see much decrease in terms of quantum because you have to look at annualized rate of inflation over a longer term of 5-6 years and you have to see that there is a 5%-6% kind of inflation year-on-year. So leaving aside aberrations which happened say in 2016 or 2017, we will see the prices softening a little bit. Say about a rupee or so going down the line.
- Dhaval Mehta:** Okay. That is helpful. Sir my second is a book keeping question. So why our tax rate was so low during this quarter?
- Deepak Jain:** We had a tax benefit of 80IB in the cheese and the whey protein. So we fell under the MAT provision, minimum alternative tax and post that we have Ind-AS adjustment, so it has come down to 10%. But we will be in the range of 20%-25% tax rate.
- Dhaval Mehta:** For FY18 it will be in the range of 20%-25%?
- Deepak Jain:** Yes.
- Moderator:** Thank you. We have our next question from the line of Shailesh Kumar from Sunidhi Securities. Please go ahead.

Shailesh Kumar: Couple of questions. First thing is, is it safe to assume that this 10.5 crores PAT we have done, it would at least be replicated in remaining 3 quarters?

Deepak Jain: So Shailesh, the 10.5 crores that you are predicting for the remaining three quarters, by which I assume you mean a minimum of 10.5 crores for every quarter - but from Q2 and Q3, the festive season begins, so the sales will grow and we will also get the benefit on the GST front.

Shailesh Kumar: So you expect this thing to improve?

Shirish Upadhyay: We normally get the mega project incentive. So in this quarter around roughly 6.5 crores per quarter, this amount is also not contributed in this revenue. So this amount will directly flow into the PAT margin. When we will consider all these benefits which we will get in the coming quarters, you can predict how much the margin will improve.

Shailesh Kumar: Second question revolves around what is the marketing strategy we are going to follow about Avvatar and what kind of marketing budget we are allocating for FY18?

Mahesh Israni: To answer the second question first, in terms of the marketing budget obviously as I said earlier as well that this being a new category, this being a new brand, the spends are going to be disproportionately higher to my otherwise standardized budget over the entire consumer product business. In terms of the strategy, a very clear defined strategy for the next two years is that we will not go on ATL spends behind the brand. This category is such that it has very high involvement of the influencers. Three primary influencers that have been identified are Gym Trainers, Dieticians and Nutritionists and a large proportion of our initiatives in terms of campaigns are going to revolve around this and to bring the brand alive in the consumer's mind we are going to use the social media. Apart from this, I think as in the Chairman's speech we said, we have a certification from informed sports which certify the product being free of any abusive substance. That is a real big play and will be well accepted by the sports associations and the sports authorities at a national level. We have already started initiation of discussions with these authorities and that will be the next level of getting into a direct touch with the sportsman and the consumers of the product.

Moderator: Thank you. We have our next question from the line of Akshay Agarwal from Edelweiss. Please go ahead.

Akshay Agarwal: So I would like to just ask you about the working capital cycle in Q1, since I have seen that creditors in your annual report in FY17 was around 300 crores odd. So is the plan to sort of get down these creditors and who are these creditors exactly?

Deepak Jain: So the creditor days we saw in FY17 was abnormal because for instance, we have a milk supply cycle of 15 days, but in quarter four we received more milk and the milk cycle was extended to two cycles. So majorly around 50% amount contributed to the milk suppliers and rest of the

creditors are related to the materials and packing creditors. So going forward the creditor days will come down. It will be in the range of around 40-45 days.

Akshay Agarwal: Would you sort of roughly share the number in Q1, like roughly? Are they going to come down right now or how is it?

Deepak Jain: It has come down in quarter one itself.

Akshay Agarwal: Just my second question is revolving around the consultant that you hired or Vector Consulting, so what exactly is the scope of work for this consultant and also if you could share what are the expected benefits in the cost related to this consulting?

Natasha Kedia: So the clear mandate when we went into this tie up with Vector Consulting, their expertise is on two parts. One is the backend in terms of the supply chain in logistics and in the frontend in terms of distribution expansion. So if you look at both these things that are conjunction, the primary focus of this entire initiative is behind improving the freshness of the products in the marketplace and ensuring the width of distribution.

Akshay Agarwal: So we are paying them a fixed charge here or is it on basis on the performance of the consultant?

Natasha Kedia: In fact they are one of the rare consultants who actually work on a variable pay, unlike any other consultants who typically comes, evaluate you, charge you a fee and get out. These people are working on a fixed plus variable.

Moderator: Thank you. We have our next question from the line of Mahesh Bendre from Way2Wealth. Please go ahead.

Mahesh Bendre: Sir in presentation we have mentioned that we will achieve 5% PAT margin, does that include GST benefit?

Mahesh Israni: I think it was answered earlier that this forecast was given in the pre-GST era in the quarter four earnings call. Hence obviously does not include the impact of GST in it.

Mahesh Bendre: Sorry sir. I joined a late. But what could be the possible GST benefit we will get it in terms of...?

Mahesh Israni: As we speak, this is the first month which has got over in the month of July. The final impact will be known only in the next two working quarters where you will get a real understanding of what is going to be the impact.

Mahesh Bendre: But sir will it be substantial?

Mahesh Israni: It will be in a neutral to positive range is what I can tell you right now.

- Devendra Shah:** But we will be getting input tax credit, the service tax benefit and Octroi which we are paying currently in Maharashtra. So these benefits will directly flow into the financials.
- Moderator:** Thank you. We have the next question from the line of Sanidhya Daga from Athena Investments. Please go ahead.
- Sanidhya Daga:** Just wanted to know can you give me a number for the kind of revenue or price that you generate from cheese per kg?
- Natasha Kedia:** Sorry, we are not able to share that. It is competition sensitive for us.
- Sanidhya Daga:** Right. Also given that our cheese hasn't really done that well and because of the couple of reasons that you stated, so going forward is there a possibility that we will see some kind of discounting in our rates or was the price of cheese anything to do with the kind of performance?
- Mahesh Israni:** Am I going to discount my products? Certainly no. The entire endeavor and I just mentioned in the earlier question as well, that the entire logic behind Vector Consulting into our hold is to ensure that you have a distribution expansion and one of the mandates on the distribution expansion is how do I ensure that I am more than doubling my HoReCa direct customers. And once I get into a direct HoReCa customers, service becomes more important than the pricing. Pricing is only in that sense confined to large customers who have a direct relationship.
- Sanidhya Daga:** So any kind of price increase that we are going to see in lines with what milk product price you guided, 12%-13%?
- Mahesh Israni:** I think Shirish earlier mentioned that we have no plans of taking any price correction at this stage.
- Moderator:** Thank you. We have our next question from the line of Bhavin Chedda from Enam Holdings. Please go ahead.
- Bhavin Chedda:** Sir, what was the milk procurement number in the quarter?
- Shirish Upadhyay:** Bhavinji, we already spoke, like we have a 5% blip in the last quarter what we have procured.
- Bhavin Chedda:** So this is quarter-on-quarter or Y-o-Y?
- Shirish Upadhyay:** YoY.
- Bhavin Chedda:** So I think last year was 10.5 lakhs liters a day. So should I take a 5% decline there?
- Shirish Upadhyay:** Yes, right.

- Bhavin Chedda:** And on the milk procurement price, what has been the change, either on a quarter-on-quarter or YoY basis?
- Shirish Upadhyay:** YoY, there was a price change but on the quarter-on-quarter there is no price change.
- Bhavin Chedda:** So YoY it was higher?
- Shirish Upadhyay:** Yes higher. On YoY, it is higher.
- Bhavin Chedda:** And the other thing I think the cheese capacity utilization number, you mentioned start of the call it is running at 65% utilization, right?
- Shirish Upadhyay:** After the increase that has happened.
- Bhavin Chedda:** So on a 60 tonne per day, it is running at a 65% utilization?
- Shirish Upadhyay:** As was said earlier, in the Dairy industry maximum capacity utilization over a longer period of time is close to about 85%. Of that 85%, it would be close to about 60% today.
- Devendra Shah:** It leaves the cushion for 10%-20%.
- Bhavin Chedda:** So 50 tonne is running at 65% utilization, roughly? If I take 85% utilization of 60 tonnes...
- Management:** Yes.
- Bhavin Chedda:** And 60 tonnes was started at the start of the quarter or it was in between...
- Mahesh Israni:** It just got commissioned.
- Moderator:** Thank you. We have the next question from the line of Anup Nambiar from Equity Intelligence. Please go ahead.
- Anup Nambiar:** My question was on Slurp, the new mango drink that we have launched and your slide says that this is to drive operational efficiency in the Palamaner plant in South India. So like currently what is the capacity utilization in the plant in South India or any ballpark idea of how Slurp is going to help us improve the capacity there?
- Natasha Kedia:** The utilization of the Palamaner plant with respect to the UHT lines that we have is about 55% to 60% and hence we have enough capacity to expand in that sense. In order to ensure that you have efficiency and optimum utilization of the UHT plant, the endeavor was of getting into newer product lines and one of them was Slurp. We have just test piloted the product in four cities to understand how does the market behave for this new subcategory of milk based fruit drinks. Early indications are it has been accepted well and hence we are looking at into a national

expansion before the next season comes in, that national expansion should get completed in the next couple of quarters.

Anup Nambiar: So any revenue guidance for this Slurp, how much we will be...?

Mahesh Israni: Again as I said in the Avvatar example also I said the same thing. It becomes too premature to decide and have a number for each of the products which are new in the market. It is a 6,500 crores category which is growing at a strong double digit. So we would like to have a decent share of that pie.

Moderator: Thank you. We have the next question from the line of Mehul Desai from IDFC Securities. Please go ahead.

Harith: Harith here. Just one thing ,what is the CAPEX plan for this year?

Natasha Kedia: We have a 3 year CAPEX plan. We have taken 150 crores from the IPO from which 85 crores have already been deployed. We have remaining 60-65 crores remaining and we are estimating around 100 crores from internal accruals. So over the next 3 years, we will have approximately 150-175 crores.

Harith: Yes. But is this more front-ended over the next 12-18 months. How is that going to work?

Natasha Kedia: It will be standard.

Moderator: Thank you. We have the next question from the line of an individual investor, Mr. Sourabh Shah. Please go ahead.

Sourabh Shah: I am both a consumer and an investor of your company. What I failed to understand is why our company has not been able to penetrate the North and East part of our country as compared to the Western and Southern part?

Shirish Upadhyay: Sir I think it is a very nice question. I mean, if you look at the way the companies in the Dairy industry operate, most of the companies in fact I would say are more regional in nature and if you go by that logic, we started our operations in Manchar which is in Maharashtra state and over a period of time, obviously you will first expand into the vicinity around your plant and that is how we have strengthened ourselves in Maharashtra and then we went on to strengthen ourselves in Gujarat and the Western region as a whole. In our endeavor to become a pan India company, obviously we have a distribution which is there across the country not only North and East and you actually left out even South. In the urban centers of the country, we have a distribution, we have our presence felt in most of the markets. In any business that you are in, there always has to be a focus. I mean you can't dilute yourself across the country, India is a vast country. In that sense, we were focused on to West. In the last two years, we have really

expanded well in the North India and in parts of East India. So when you say East is as a whole, in fact in geographies like North East and states like Sikkim, we are pretty much strong over there as well because those were identified pockets where we have said we will get our distribution right. Over the next 18 to 24 months, the endeavor is to cover the balance part of East as you rightly said we might have a presence which is not as per the desire of a national company and also get into South with a focus.

Sourabh Shah: So we have taken any incremental steps to do that? Can you share any numbers of distribution that you are planning to add in say next one to two years?

Mahesh Israni: See, distribution expansion is a never ending game. We can share the number, I would not have the numbers right now with me, but that can be shared separately. We can send you across on e-mail. What I would say is that the way we look at the distribution expansion, we look at the geography, identify the right kind of infrastructure resources that you want to deploy in terms of getting a distribution expansion done. If there is kind of initial support which is required behind it, that is given and then we move on to the next geography and to the next geography.

Sourabh Shah: And sir one more question, Ghee this is one of the most permanent brands in our product segment, what is the present market share in that segment and what are you doing to increase that share?

Mahesh Israni: Let me in fact answer this question in a different note. I think in a category like Ghee, it is such a vast category and it is largely unbranded that it would be very difficult to put a judgment on market shares. Even large research companies do not track Ghee market shares for any of the brands. I would be in fact happy to tell you that we are one of the strongest and the first ones in the Cow ghee category. In a sense we pioneer the cow ghee category with a clear focus on cow's ghee benefits. There are other players which are now thinking about getting into this category seriously. The testimony that we are serious about looking at this cow ghee category and continue to expand the market and grow with the expanded market is a fact that in this year we have been awarded two awards. In the beginning of the year, we were awarded the most trusted brands for Gowardhan Ghee by Brand Trust Report and this was for second consecutive year. So we have the number one ranking in 2016 and again in 2017 and in fact in the overall brand rankings which cover all the categories, we have moved up 132 launches from rank 435 last year to 303 this year. I think that speaks a lot about the brand. And just recently about a couple of months back, we won Consumer Voice Award from Jago Grahak Jago which is government of India initiative on being the number one brand in the cow ghee category. I think these awards are testimony to what we are doing right behind the brand and the category.

Moderator: Thank you. We have our next question from the line of Shailesh Kumar from Sunidhi Securities. Please go ahead.

Shailesh Kumar: There is a small clarification, this mega project incentive that we are expecting, will it be effective from Q2 or Q3?

Management: See, we cannot define time period as of now since this is in the hands of government. But we have already got the in-principle approval and are now at the last stage of compliance.

Shailesh Kumar: Okay, it is safe to take it from Q3. And for how long can we expect to get it?

Devendra Shah: No, it could be from July-August.

Shailesh Kumar: Okay and for how long will we getting it?

Devendra Shah: We will get for 7 years.

Shailesh Kumar: And for full year FY18, what kind of average milk procurement figure we are targeting internally?

Deepak Jain: So we will be targeting around approximately at average 12 – 13 lakhs litres per day.

Moderator: Thank you. We have our next question from the line of Akshay Agarwal from Edelweiss. Please go ahead.

Akshay Agarwal: So I just had a follow up question on the creditors. You have said that Q1 creditors have come down to 45 days which implies the creditors of 200 crores. So there has been a 100 crores reduction of creditor. How has that been funded?

Shirish Upadhyay: I think what we were trying to say earlier was that the creditor period has come down particularly in case of milk creditors. And what he was trying to explain earlier was that we had taken excess milk from farmers when the prices were also quite high because we need to maintain that kind of relationship with these farmers. So while we were benefiting in terms of accepting whatever milk that was given by them, we also negotiated some terms with them which helped us in terms of tiding over the situation, but that was a one-off situation. Now slowly with the milk coming down to normalized level and the prices also stabilizing at the same level, slowly the cycle of creditors is moving out. We will be able to give you an exact number later on, on the separate note. But there is a reduction in terms of the creditor cycle in number of days.

Akshay Agarwal: In FY18 you planned to get these creditors down, right? The question is how do you plan to fund them, fund the payment for the creditors. That is the simple question and by how much?

Deepak Jain: Now, if you see the short term loan advances and the debtors, this is the natural cycle which we will receive from the debtors, and from the advances, so the creditors will be paid off from our working capital cycle. So as such we are not borrowing to repay the creditor.



*Parag Milk Foods Limited
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Moderator: Thank you. As there are no further questions, I now hand the floor back to the management for closing comments.

Natasha Kedia: I would like to sincerely thank Edelweiss for hosting the call and all the participants for taking the time out to join us. Please feel free to get in touch with me with any further questions. My coordinates are provided at the end of the Q1 FY18 investor presentation, uploaded both on the stock exchange and our company website. Finally, I would like to end by saying that we are well poised in our strategic growth journey and are on course to becoming an FMCG Dairy Company with a focus on health and nutrition. With the pan India distribution network, several strong brands, a pipeline of value added innovative product and a unique positioning of 100% cow's milk, we are confident of a sustained mid-term and long-term growth. Continue tracking us and we look forward to presenting a strong performance in the coming quarter. Thank you very much.

Moderator: Thank you. On behalf of Edelweiss that concludes this conference. Thank you for joining us and you may now disconnect your lines.