

Conference Call Transcript

Prabhat Dairy

Q3FY17 Results

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Corporate Participants

Mr. Vivek Nirmal

Joint Managing Director

Mr. Raviraj Vahadane

CFO

Questions and Answers

Moderator: Good day and welcome to Prabhat Dairy Q3 FY2017 earnings conference call hosted by Edelweiss Securities Limited. As a reminder all participant lines will be in the listen-only mode and there will be an opportunity for you to ask the questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing “*” then “0” on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Nihal M. Jham from Edelweiss Securities. Thank you and over to you Sir!

Nihal M. Jham: Thank you Stanford. On behalf of Edelweiss Securities I would like to welcome the management of Prabhat Dairy and all the participants in this Q3 FY2017 post results call of Prabhat Dairy. The management is represented by Mr. Vivek Nirmal – Joint Managing Director and Mr. Raviraj Vahadane, CFO. Without any delay I would like to hand over the call to Mr. Nirmal for his initial comments. Over to you Sir!

Vivek S Nirmal: Good afternoon everyone. It is a great pleasure to greet all of you once again on behalf of all our Board of Directors and the senior management. We begin by thanking all of you for having spared time and joining us here today to discuss our third quarter and nine-month earnings for the financial year 2017.

Before we discuss the financial performance during the quarter, allow me to quickly highlight our business philosophy and our fast transforming business model, which will help us to capitalize on the dairy industry growth and achieve long-term sustainability.

We are a fully integrated milk and dairy products company right from the farmer to the end customer. We are evolving from being an established specialty dairy ingredients company to an emerging consumer focused and brand-driven company with wide range of dairy products under our key brands in Prabhat.

Our strong success is backed by our integrated business model, robust milk procurement system built on intense farmer engagement and trust, state-of-art manufacturing facilities and strict quality control and food safety standards. Today we have solid foundation of B2B business with a very marquee clientele. Just during the last quarter we have developed one of our new products, which is Ricotta cheese, and we are sole suppliers of that to the largest pizza chain in the country today. For mozzarella cheese, again we are amongst the top suppliers to the leading pizza chains for the last quarter. We also have manufacturing agreement for paneer with Britannia, which is our existing clientele. We continue to maintain our strong hold in the SMP business wherein we supply specialty milk powders and we have struck agreements with companies including a lot of new ice cream players in the country, who are our

new clients now. We have also signed an agreement with one of the key players in India for exports for shrikhand and ice cream. Our ghee has pan India presence because the consumer business keeps on growing and we are now in around 25 states and the penetration continues to increase with more than 500 distributors and one lakh retail touch points. Our products like paneer, dahi, lassi and shrikhand continue to gain acceptance under the Prabhat brand name. In terms of our institutional segment, we have recently acquired lot of marquee institutional clients including TajSATS for Eastern India. We are witnessing very rapid scalability in our consumer business, which has grown from being present only in one state to around more than 25 states now. We further aim to scale our B2C business and grow its share from around below 30% to around 50% in terms of revenues by 2020. In terms of our presence in modern trade it has been expanding beyond Mumbai. We have recently started modern trade in Gujarat and by this quarter and the next one, we also plan to expand the modern trade presence across India. Coming to the financial performance for the quarter, our Q3 FY2017 total revenues increased by 34.5% year-on-year to Rs.4081 million. I would like to emphasize that despite adequate monsoons in 2016, raw milk availability continues to be impacted, as the ecosystem has not improved significantly. The lactation cycles of the animals obviously takes more time to adjust and hence the milk shortage continues to be there which has also impacted on higher milk prices; however, our efforts to increase our volume especially since we have our own milk procurement network and our higher realizations across value-added products has helped offset the price rise and our gross margins remain healthy. Our Q3 FY2017 gross profits increased by 26.6% year-on-year to Rs.790 million. Our gross margins have decreased by 122 bps from 20.6% to around 19.4% year-on-year. The share of our value-added products increased from 76% to 86% on year-on-year basis. Driven by specialty ingredients like ghee, cheese etc, our Q3 FY2017 EBITDA increased by 37% year-on-year to Rs.376 million. EBITDA margin increased by 16 bps year-on-year to 9.2%. Although the business promotion expenditure in absolute terms has grown considering our foray into B2C business, it was lower as a percentage of sales compared with previous quarter due to higher proportion of the B2B sales. We saved on transportation cost. This is particularly in terms of incoming milk transportation cost, because in the past few quarters we had to procure milk from the near by states pertaining to drought situations in Maharashtra, but since the milk procurement position has slightly improved, we have saved on the milk inflow transportation cost. Q3 FY2017 PAT increased by 280% year-on-year, PAT margin increased by 534 bps year-on-year to 8.3% in Q3 FY2017; there is a special item in that. We received Rs.256 million this quarter as a part of megaproject income, which actually pertains to FY2015, FY2016 and H1 of FY2017, which boosted profitability significantly. Going forward we shall remain committed on growing our value-added consumer business while maintaining our strong hold on our ingredient business. We are placing strong emphasis on establishing our products under our brands Prabhat and a couple of other brands in both existing as well as new markets across the country. We shall also look to further strengthen our distribution network, delivery systems, and

spread our retail present across India. Our cheese business particularly is ramping up well and our strategy is to grow business by focusing on HORECA clients and institutional customers in India as well as export to key geographies. We have already procured order from major pizza and burger chains in the country. With respect to our B2B business, we shall further leverage our institutional relationship with all the quality clients, which we already have from such institutional customers to further grow our business in India and globally. With this I would like to leave the floor for questions and answer session please.

Moderator: Thank you very much. We will now begin with the question and answer session. We will take the first question from the line of Manish Ostwal from Nirmal Bang Securities. Please go ahead.

Manish Ostwal: Very good set of numbers first of all. First question in the milk procurement side, you talked about increase in the milk prices during the quarter although you have focussed mainly the Maharashtra nearby region only, but overall cost increases on milk procurement side on quarter-to-quarter basis, could you tell that figure?

Vivek S Nirmal: Our milk procurement cost has particularly gone up. It is around Rs.27.20 our average milk procurement price which has remained for the last quarter and the milk procurement obviously is seeing a slight increase, but since last two years obviously the prices I would say were much lower and it is a country wise phenomenon we are seeing that everywhere the milk prices are rising now, which has already started from the last quarter.

Manish Ostwal: How much percentage has increased could you give that number Sir?

Vivek S Nirmal: Our milk procurement price in the range of around 6% to 10% because we procure milk from the print channels and our 65% to 70% of milk is procured from own channel. Around 6% to 10% is our overall milk purchase price rise.

Manish Ostwal: Second in terms of total volume breakup in terms of different products, could you give that liquid milk and value-added product categories?

Vivek S Nirmal: Value-added product categories as I said it is more than 80% now, we do not track it for product wise, but our liquid milk versus or other value-added products. Value-added product is more than 80%.

Manish Ostwal: So value added more than 80% and your total business how much is consumer business right now?

Vivek S Nirmal: Out of our total revenue around 30% of the revenue is from the consumer segment.

Manish Ostwal: Secondly this price of SMP, skimmed milk powder has also increased significantly last couple of months, so one is how it is going to impact our business and secondly what is your outlook on the price on SMP?

Vivek S Nirmal: I believe the prices will remain stronger. We supply a lot of specialty milk powders not the general skimmed milk powders, but the powders, which are customized to the client's requirement. We supply to couple of

corporate clients and lot of even small and mid-size bakery, confectionary and ice cream manufacturers. Prices have gone up and since last two years the prices were low, because there was also lot of inventory in the country. Now we see that inventory has significantly gone down and I expect the prices to remain stronger in the years to come. I believe that it will not impact our business very significantly in the sense we normally have cost plus models in most of the cases wherein whatever milk price rise occurs we pass it onto the clients.

Manish Ostwal: Are we purchasing SMP from the market or we are just manufacturing SMP powder ourselves?

Vivek S Nirmal: We do not purchase a lot of SMP; we sell a lot of powders.

Manish Ostwal: Lastly, have you taken any price hike to arrest the gross margin contraction?

Vivek S Nirmal: Yes, we have taken price rises as I said in terms of cost plus model, the price rise has been passed in terms of our consumer business, there are a couple of products where we have been able to take the rise. There are a couple of products, although in consumer business like liquid milk where we have still not been able to take the price raises which could follow.

Manish Ostwal: Overall outlook on the sales in the margin side, could you give your outlook?

Vivek S Nirmal: We, as a policy do not give any outlook, but obviously the procurement is improving, so we see healthy quarter or a healthy business going forward Manish.

Manish Ostwal: Okay Sir. Thank you very much and all the best.

Moderator: Thank you. We will take the next question from the line of Viral Desai from Equirus Securities. Please go ahead.

Viral Desai: Hi Mr. Nirmal, congratulations for a good set of numbers. Sir my question is again pertaining to the milk procurement rate. So from your presentation when I go through it, it is mentioned that for the current quarter it was at 27.21 vis-à-vis 25.62 a year back. So Sir if you could just explain us the sensitivity of let us say a rupee increase in the procurement, how does it affect your margin and the second question would be about the value-added products that I see is above 80% now, so going ahead do you think that they have reached the peak or this value-added product revenue share would be going up further? Thanks.

Vivek S Nirmal: Yes Viral. In terms of milk procurement pricing it was around Rs.22 for FY2015-FY2016 in Q3 that is around Rs.27 that has risen significantly. In terms of our B2B clients, which happens to be major part of our business, it is mainly a pass through pricing, so whatever milk price go up or go down it is mainly a pass through and in terms of consumer business there might be price rise immediately or there might be a lag effect as well and I think what was your second question?

Viral Desai: My second question was related to the value-added products which you say is around 80%?

Vivek S Nirmal: Value-added product is around 80%, now liquid milk which is 20% I believe it would continue to remain at this level, because our pouch milk business particularly in the consumer are also increasing, is actually more than 85% it is around by 86% right now and I believe it is an optimum level and this mix would continue to be there.

Viral Desai: Okay Sir, if I could just squeeze in one more question, if you could just give us a margin breakup in your B2B and B2C, how would the EBITDA margins breakup be in the business?

Vivek S Nirmal: We do not actually break it up by this kind of segment, but it is at a similar level that in both the businesses.

Viral Desai: Okay, thank you.

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

Ritesh Vaidya: A couple of questions. First of all how much of the milk procurement during the quarter and what was it one year ago and quarter before?

Vivek S Nirmal: Last quarter actually we have procured around 7,50,000 to 8,00,000 litres of milk, this is for Q2 and Q3 we particularly procured about 8,50,000 litres of milk this is on a per day basis and apart from that, we also procured a lot of dairy ingredients because of the milk shortage which includes different ingredients like concentrated milk or cream or butter and all.

Ritesh Vaidya: Is not it quite low compared to the year ago level 8.5?

Vivek S Nirmal: Yes, this year there was particularly the drought situation, so while it was a flush season, there was a lot of milk availability in the last year flush, but due to the continuous drought the milk significantly decreased this year, so in this year, if you see right from the calendar year January, April and June, the milk availability was significantly low. The way we have compensated by purchasing ingredients from different sources to makeup the volumes.

Ritesh Vaidya: But is it fair to assume that the milk procurement prices in Maharashtra particularly have been rising, because there is a strong demand for cow ghee led by Patanjali and that is why a lot of the other smaller players are able to give higher prices to the farmers I mean correct me if I am wrong, I am trying to understand why the sharp raise in milk procurement apart from the drought effect, but is there this Patanjali effect in procurement?

Vivek S Nirmal: Basically what has happened is if you see the prices in over the last two years were unusually low, because the powder inventory and all, other dairy products inventory in India was very high. The export markets were low. Now since last six to eight months, the export markets have been improving significantly and the inventory in the country, the carryover inventory of milk powders and all has gone down. Secondly there is a drought declared in Tamil Nadu, there is a drought declared by Karnataka government. That is why the milk availability, the milk production in these states is down and is expected to go further down. Maharashtra while we had a good monsoon, the milk has

not immediately improved, but it is on an improvement track in the next couple of quarters we are expecting to see a larger volume and the cattle herd in particular what happens is if the prices are very low there is a tendency of farmers to reduce the cattle herd, so the cattle herd has also reduced, now this is again national phenomenon. So obviously as a joint effect of everything the milk production has increased. So if you see the current price rise it is not too much due to the rise in demand, it is mainly due to the production which has gone down and it is now again on a track to pickup. However what you said about the cow ghee not only Patanjali, but overall cow ghee as a category in India is expanding very rapidly given the perception about cow ghee as healthier alternate and that is why the demand for cow fat has been increasing that also has a partial impact on the overall situation.

Ritesh Vaidya: But has that resulted in a differential in your procurement price of cow milk and say that for buffalo milk in Gujarat, has the differential between the two reduced?

Vivek S Nirmal: It has nothing to do with differential actually because cow milk prices are determined by different factors and buffalo milk in Gujarat where main procurement is the cooperative sector, it all depends on what is the consumer price to get for their products.

Ritesh Vaidya: So there is no fear that Amul which basically procures buffalo milk that is having a bit I mean the procurement price increase is not as much as for them versus the cow milk procuring companies like you, I mean is that a concern that price hike for you is higher and for them is lower?

Vivek S Nirmal: If you see first buffalo, the prices are already higher; the cooperative sector operates on a different pricing model especially in Gujarat. In Maharashtra if you see the overall landscape in the past and even today is mainly dominated by the private sector, which handles more milk in the state.

Ritesh Vaidya: Just one question on your product categories. Can you give us the understanding as to - in the value-added dairy products, which are the key products that you are talking about, and in the non-value-added, which is the main product that you talk about?

Vivek S Nirmal: The main products in the value-added would include the specialty dairy powders would include cow ghee, condensed milk, and cheese.

Ritesh Vaidya: And how much is a cheese right now of total sale?

Vivek S Nirmal: We do not track that for product wise as I said earlier Ritesh.

Ritesh Vaidya: And non-value-added which products are the main ones?

Vivek S Nirmal: It is only liquid milk.

Ritesh Vaidya: That you sell under your brand name only or you package it

Vivek S Nirmal: Yes

Ritesh Vaidya: Only your brand name?

Vivek S Nirmal: Yes.

Ritesh Vaidya: Okay, fine. Thank you.

Moderator: Thank you. We will take the next question from the line of Rahul Jha from Bay Capital. Please go ahead.

Nikunj Doshi: This is Nikunj Doshi from Bay Capital. I just wanted to understand this implication of this VAT refund that we have taken into consideration. This 256 million, we have already received or are yet to be received?

Raviraj Vahadane: Ravi here. Total benefit we have accounted for in this quarter is around Rs.29 Crores out of which around Rs.3.17 Crores is for current quarter Q3 and Rs.25.60 Crores is for FY2014-2015, FY2015-2016 and H1 of FY2017. We have received till date Rs.4.50 lakh as a first refund and we are in process of getting another refund of around Rs.12 Crores, which pertains to FY2015-2016.

Nikunj Doshi: But why we have changed this practice earlier, we were to recognize it only on cash basis rather than accrual, so now why we have changed this practice of accounting?

Raviraj Vahadane: We have not changed the practice of accounting. As per accounting standard, you need to accrue the income when you are very sure that you are going to get this income. It is on the basis of certainty. We got the first approval of refund in the Q3 and we got the first refund also in Q3. So from Q3, we have started accruing in this income.

Nikunj Doshi: So this is going to be now every quarter-on-quarter basis will be recognizing.

Raviraj Vahadane: Right.

Nikunj Doshi: And in terms of milk price what you mentioned in the presentation, is 25.6 to 27 is Q2 to Q3 or last year Q3 to this year?

Raviraj Vahadane: It is a sequential.

Nikunj Doshi: It is a sequential increase, okay and last year corresponding period you mentioned it was around Rs.22?

Raviraj Vahadane: It was around Rs.22.

Nikunj Doshi: And in terms of the debt position, where are we right now in terms of the net debt?

Raviraj Vahadane: We have net debt of around Rs.250 Crores, which includes short term also, and long term also.

Nikunj Doshi: Cheese, what is the utilization right now?

Vivek S Nirmal: In the current quarter sitting today, we have around 18% to 20% utilization of the capacity for cheese manufacturing.

Nikunj Doshi: Okay, thank you very much Sir.

Moderator: Thank you. We will take the next question from the line of Anurag Purohit from Anived PMS. Please go ahead.

Anurag Purohit: Good afternoon. My question is regarding the raw milk prices, how is your outlook on that front and till what time you see there is a supply demand being worse to you and second question is regarding how much of our portfolio is on cost plus basis and in the remaining portfolio, what portfolio, we have already taken price increase?

Vivek S Nirmal: Hi Anurag, see in terms of the outlook for milk prices, since there is a shortage all over the country and we do not expect again the summer season is also approaching, so we do not expect the supplies situation to improve immediately in the next couple of quarters and that is why we believe the prices would continue to remain high. There is also possibility they might cool down to some extent with some increase in milk prices, because very lucrative milk prices, there is a tendency of farmers who have cattle field and richer fodder to the animal which results into slightly higher procurement but at overall level we expect it to remain high for a couple of quarters and answering to the second question about particularly for just one minute. What was your second question?

Anurag Purohit: In terms of what percentage of our portfolio is purely cost plus model?

Vivek S Nirmal: In B2B you know what happens is, it is not fixed, there are a lot of clients mostly we work on the cost plus model only, but even for the other clients wherein there is no cost plus model. We normally have certain lag of transferring of the prices or it is a fall pricing on which we work, but the percentage if you see would be around 50% to 60% where we work on the cost plus model.

Anurag Purohit: And the remaining part to what percentage we have already taken price hikes to compensate for raw milk price increase?

Vivek S Nirmal: We do not have the data immediately, but whatever is the cycle, in certain cases we have monthly or quarterly cycle. As per the cycles, we immediately pass on the prices in the cost plus model.

Anurag Purohit: No, I am asking in terms of the other part of the portfolio where we will be required to take price hike and it is not purely cost plus, what percentage of that portfolio we have already taken price increase?

Vivek S Nirmal: We would not be having the data Anurag for that.

Anurag Purohit: Okay and would it be possible to give details in your consumer segment, how much is HORECA as percentage of revenue and how much is your retail?

Vivek S Nirmal: Again in terms of consumer, in particular when we say it is around 30% of the revenue, but in fact 30% we have divisions and everything is common, so we have our common distributors, we have the common outlets and the common teams for that, so we do not have it separately and that is true for most of the dairy companies where in the distribution channel even for larger cooperative or private sector player, it is common and a lot of products actually even from the retail segment moves into the HORECA. So there is no

separate tracking, but the couple of products, which now sell through HORECA particularly, cheese right now whatever we sell is mainly through our channels for the HORECA segment.

Anurag Purohit: Thanks and all the best.

Moderator: Thank you. We will take the next question from the line of Gaurav Jogani from Prabhudas Lilladher. Please go ahead.

Gaurav Jogani: Thank you for the opportunity Sir. First of all, just like to clarify for this Q3 FY2017, the milk procurement is 8.5 lakh litres right?

Vivek S Nirmal: Yes.

Gaurav Jogani: And for Q2 2016 how much it was?

Vivek S Nirmal: It was around 7.5 lakh litres per day.

Gaurav Jogani: Y-o-Y like previous year Q3 2016 what was it?

Vivek S Nirmal: It was around in the range of 11 to 12 lakh litres.

Gaurav Jogani: Now Patanjali I think they have got quite some plant in the Ahmednagar district very recently, so is there any competition for the milk sourcing around this particular area, because in that area you are there. Parag is also sourcing from the same area and now Patanjali would also be there. So do you think any shortage would come in terms of procuring the milk in the same area?

Vivek S Nirmal: We work closely with Patanjali for a couple of products. We have already supplied them sweetened condensed milk for their confectionary and bakery range. We also have supply them with some of the other products, which includes some milk powder. In terms of plant, they have their plant, which is basically for conversion of the raw material into ghee. So they are not into milk procurement really in that region, but obviously in our region there are a couple of players who already operates since last many years wherein large cooperatives are there, large private sector players are also there, because there is abundant milk in that area. Ahmednagar district produces more than 2 million liters of milk per day. So obviously it is a large basin and we expect couple of more players to come in. It all depends on what is the kind of milk procurement network, which remains our larger strength, any company is able to setup over there.

Gaurav Jogani: Like how much do we source it directly and how much do we take it from the middleman or the other people like?

Vivek S Nirmal: Around 65% to 70% of the procurement is what we source directly from our farmers and the rest of it we source from the third party agent.

Gaurav Jogani: One book keeping question like in this Q3 2017 results, the exceptional item that is mentioned is Rs.26 odd Crores, but in the nine month FY2017 it is showing Rs.19 odd Crores, so why is that?

Vivek S Nirmal: In nine months, Rs.18, 95,000 Crores pertains to FY2014-2015, FY2015-2016 which is pertains to the prior product so they have taken it

into exceptional item.

Gaurav Jogani: In the Q3 alone it is showing 25 so, should not it be the entire nine-month number be equal to that number?

Vivek S Nirmal: Right, but for Q3 the item we have taken to revenues around Rs.3,17,000 Crores which pertains to only Q3 not for the nine months. So in nine months, we have taken the full figure of around Rs.9,82,000 Crores which pertains to Q1, Q2 and Q3 so that is the part of revenue and other income exceptional item is for the FY2014-2015 and FY2015-2016.

Gaurav Jogani: What is the policy for this particular subsidy like how much is the amount that we can claim under the subsidy in total?

Vivek S Nirmal: This is the amount that we have claimed.

Gaurav Jogani: Going forward if the plant that we have constructed can we claim for the entire plant amount?

Vivek S Nirmal: Under megaproject status we are eligible to the....

Raviraj Vahadane: This is basically you get it for certain level of investments to do in the rural area where we have been awarded the megaproject status while we can claim much larger, but a lot of our items are not taxable in terms of dairy because like liquid milk and all is not taxable, but overall we have an anticipation that in the couple of years we would be able to get somewhere around Rs.100 Crores plus of tax as a refund depending on what sales and how much amount of sales happens in the states, outside state and all.

Gaurav Jogani: Let me reframe my question. I was trying to ask you is that for example you have spent whatever amount on the cheese plant, so that is the cap that we can claim under this particular subsidy is what I was trying to understand?

Vivek S Nirmal: Cheese plant is one of the plants, there are a couple of other investments, which combine together, have made us eligible for the subsidy Gaurav.

Gaurav Jogani: How much amount would that be total amount?

Vivek S Nirmal: Rs.250 Crores is the cap above, which if you invest you are eligible, so we are already for that and your maximum cap for the refund of VAT is that amount.

Gaurav Jogani: Thank you.

Moderator: Thank you. We will take the next question from the line of Dhawal Mehta from Emkay Global. Please go ahead.

Dhawal Mehta: Good afternoon Sir. Thanks for the opportunity and congrats on a very good set of numbers. One clarification with the VAT refund, which we got, so is this VAT refund taxable because what I am seeing is that our tax rate has increased drastically in this quarter?

Vivek S Nirmal: There are different tax treatments particularly for this income. We are already in discussion with our auditors about the right treatment for this

income level.

Dhawal Mehta: So the Rs.11 Crores tax, which we paid for this quarter, includes a part of exceptional item tax also or it does not include that?

Management: Dhawal, this income claims under the book profit, so we have to make provision as per the Income Tax Act for the MAT.

Dhawal Mehta: Sir second question is on transportation cost so basically we were able to decrease the transportation cost because of the procurement from nearby regions, how much sustainable is it this particular model?

Vivek S. Nirmal: Which model?

Dhawal Mehta: Where we can procure from the nearby regions?

Vivek S. Nirmal: We have been historically procuring from nearby regions only, just as an exceptional situation, last year we had to procure milk from nearby states.

Dhawal Mehta: Okay, so basically last year where we are procuring somewhere around 11 lakh liters, this year the procurement has decreased that is why we are able to basically fulfil it from nearby regions, we did not have to go to different states is that the right assumption?

Vivek S. Nirmal: It depends as I said earlier we are also procuring a lot of ingredients, so we will not be able to judge 11 versus 8, an apple to apple basis, but as I said that pertaining to the question of sustainability of procurement, we have been historically procuring in this region and going forward we have plans to increase our milk procurement from the same region, since it has gone down exceptionally last year due to draught situation, we had to bring milk from nearby states like Karnataka to fill up the volume.

Dhawal Mehta: Sir my last question is on our few categories, which had done exceedingly well in this quarter something like let us say ghee or cheese or specialty milk products, so can you give us the ballpark growth rates of this categories?

Vivek S. Nirmal: These categories particularly if you see growing at whatever the industry data says about the category I say the same would apply to these categories as well. As far as we are concerned, in case of B2B, it depends on lot on growth of our clients about with what percentage they are growing. In terms of consumer business if you ask me obviously it is above industry average because we are also tapping new areas every quarter or maybe every year for our consumer business distribution, which is the next growth frontier for the company, so this products definitely now are growing at a much healthy rate when it comes to quarter-on-quarter growth or year-on-year growth.

Dhawal Mehta: Can you give some figure Sir on it, what was the growth rate for us in this quarter?

Vivek S. Nirmal: There is no consistent pattern on that as such, because there are also a lot of seasonality because for example, last quarter also there was a festival season Deepavali and all, so on Deepavali again the growth rate was

different as compared to summer season wherein relatively the consumption is low. I think when we built up a significant data to support the numbers in terms of our consumer business I am telling especially on the cheese business – the cheese business also is a relatively new that is hardly five- to six-quarter old, I think that would be the meaningful data, which will be able to tell about our growth rates in these categories.

Dhawal Mehta: Thank you Sir. That is it from my side. All the very best.

Moderator: Thank you. We take the next question from the line of Balvindra Singh from Canara HSBC Insurance. Please go ahead.

Balvindra Singh: Hi Sir. Just wanted to understand whether the cost increase on the procurement side that we have seen of 6% to 10%, are we going to see any further increase and the reason why I am asking is because one of your peers reported a year-on-year increase of 20% and quarter-on-quarter increase of 14% in raw milk procurement prices, so is that, we have seen only 6% to 10% this quarter and are we going to see further increase going forward?

Vivek S. Nirmal: Balvindra, we will not be able to comment exactly on that about how it is seeming to be for this quarter, which is Q4, but yes on a overall basis as I said earlier, the milk prices have a rising trend in the entire country and we expect the prices to remain on a tighter side for a couple of quarters as well.

Balvindra Singh: Okay and we have taken price increase commensurate with what increase in procurement prices we have seen, so just wanted to understand the outlook on margins, we will be maintaining margin or we can see pressure on margins?

Vivek S. Nirmal: Again Balvindra, we will not be able to comment exactly on the margins for this quarter, but as I explained earlier our model is to pass on the... a lot of cost plus model to pass on the milk price increase to the clients as well, so we have done in a lot of cases, in whatever cases we have not done also has certain lag effect, also already in the process.

Balvindra Singh: I mean not talking in terms of numbers, but even in terms of direction if you can help whether margins will be maintained or kind of, there will be some pressure because of the cost increase going forward, so in terms of direction also it will be helpful?

Vivek S. Nirmal: Balvindra we will not be able to comment on the outlook really of the Q4.

Balvindra Singh: Okay. Thanks. No problem.

Moderator: Thank you. We will take the next question from the line of Viral Desai from Equirus Securities. Please go ahead.

Viral Desai: Sir my question was regarding this B2B business of yours where you have a special agreement for ricotta cheese, mozzarella and paneer, so Sir if you could just explain us the kind of agreement you are in, is it a yearly thing and how is the billing in these kind of things done?

Vivek S. Nirmal: Billing in the sense?

Viral Desai: How do you all – is it like an annual payment or does it come quarterly, how is it or as and when you are all supplying them?

Vivek S. Nirmal: So Viral normally this agreements are different for different periods, it might range from three months to 12 months agreements, 24 months agreement also in some cases and the invoices actually happen on every delivery, so on every delivery the invoice is – because of the stock transfer is made, the invoice is made on every delivery, which happens a couple of times every month.

Viral Desai: Okay and so Sir, this thing of being a sole supplier would not remain after the contract is done, I mean how good are the chances of the renewal what I mean to ask?

Vivek S. Nirmal: Normally it all depends on the product capability, which a vendor has to manufacture that product. As of now we are the only player manufacturing that product for this particular client. It also depends on the policy of the client about how many vendors would the client like to have for that particular product, if it is a speciality product they would be fine with one vendor, if it is a product, which tomorrow has a larger dependence they would have more than one supplier as well. So it would not be possible for me to comment exactly what the client's policy would be for sourcing this product, but as of now it has not been started and as you talk today we remain the sole supplier of this particular product.

Viral Desai: Thank you very much Sir.

Moderator: Thank you. We take the next question from the line of Manoj Bahety from Edelweiss. Please go ahead.

Manoj Bahety: Hi Vivek. Good evening. First of all let me congratulate you for good set of numbers especially in a challenging environment. I have a couple of questions first one is on cheese, in fact Amul has significantly expanded their cheese capacity and what I understand that they are also aggressively targeting HORECA segment and maybe they may have aggressive pricing as one of their strategy looking because cheese will be just a small percentage of their revenue, so how do you see the competitive scenario changing with so much capacity in cheese coming in the market?

Vivek S. Nirmal: Yes. Manoj. Amul, I think we also have learned that they have increased their capacities and all, actually they have not increased their capacities since last many, many years and obviously so the due capacity expansion as we believe as the market is growing and they are obviously the market leader in that. As far as HORECA is concerned, I think our business continues to grow even after other players have expanded their capacity, we have seen a good increase even in the last quarter, so for a new company like us in cheese we need to see growth every quarter, so every quarter has to be higher than the last quarter, which we are obviously seeing, so I do not think there is some significant price cut or some impact due to the added capacities because in HORECA it also depends a lot about developing a right product and

understanding the requirement of that particular institution. We have spent a lot of time on that since last two years and the segment has accepted our product very well in India as well as the overseas market number one and number two in terms of pricing if you see, all our cheeses made from cow milk. Cow milk is economical against buffalo milk when you compare it on a solid-to-solid basis, so we personally do not think that there would be any impact of the price competitiveness in this segment.

Manoj Bahety: What is the extent of difference in terms of costing for cheese out of buffalo and cheese out of cow?

Vivek S. Nirmal: Again difficult to say because it depends on what kind of cheese is there, even in terms of mozzarella cheese there are different varieties of mozzarella cheese what all these segment use and again cow milk also, the prices right now we share on the rising trend, but on a overall basis I can say you that this is definitely economical than the buffalo milk, so it does not have any impact as such about buffalo milk from one source competing with this especially in the case as you said.

Manoj Bahety: So what I was hearing that Amul has almost tripled their cheese capacity like number which I was getting is like from 60 metric tonne to almost 180 or something almost they have tripled their capacity and with that kind of cheese coming to the market, do you think that the kind of gross margin, which the segment is enjoying right now, maybe under pressure?

Vivek S. Nirmal: I do not think so, because they have already been a couple of months already, their capacity expansion has happened, we have at least not seen any impact on our growth sitting today even we continue, our business is increasing and I do not think they are going to really have a situation of large price cut from a player, which is going to impact the entire sector, I do not see that in the market really.

Manoj Bahety: And have they started catering to the HORECA segment or still they are like, their focus is mainly B2C only?

Vivek S. Nirmal: I do not know much about their strategy, but for the HORECA segment, for Amul particularly, obviously they are pretty large in the consumer segment and their consumer business continues to grow as I see.

Manoj Bahety: My second question is on whey protein, when are you planning to launch whey protein and what would be your strategy on that?

Vivek S. Nirmal: For whey normally definitely it is a very lucrative byproduct, when you manufacture cheese you get a lot of whey and there are a lot of possibilities from whey which includes pharma-grade products, nutrition products and all, it requires a certain skill of operation wherein it is viable to invest and then manufacture these kind of products. Right now we are pretty new into cheese, hardly one and a half year back we have started our cheese manufacturing operation and the volumes are ramping up, maybe in the next one or two years we see a level wherein we will be handling enough quantity of cheese, which would make it sensible for us to invest in the high value-added products of whey.

Manoj Bahety: Okay, so it is still at least two years away right?

Vivek S. Nirmal: Around.

Manoj Bahety: And lastly if you can comment on like earlier you have given guidance of around 50% kind of capacity utilization for cheese next year that number remains same and whether that 50% will be exit rate or it will be average for the next year?

Vivek S. Nirmal: So it is around 40% to 50% we are targeting for the next year, sitting today we are around 20% and we are on track on those numbers.

Manoj Bahety: And 40% to 50% will be average, not exit rate?

Vivek S. Nirmal: It should be our average rate.

Manoj Bahety: Average for the next year.

Vivek S. Nirmal: Yes, if we talk about – so I do not have the numbers exactly in front of me right now Manoj, but we are definitely increasing to, as we are 20%, we are growing quarter-on-quarter, we definitely intend to reach 40%, 50% plus actually by the end of next year.

Manoj Bahety: Thanks Vivek. Thanks for taking my question and wish you all the best.

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

Ritesh Vaidya: Some followup question Sir, you said that you have not been able to increase prices of liquid milk, any reason because normally this is a pass through commodity in product?

Vivek S. Nirmal: It is not a pass through commodity really, it also depends a lot on what other players are doing in the market, so we have not passed it on last turn but in couple of areas depending on the market and depending on strategy about where we would like to grow that is the trigger where we would be taking call about the increase in the milk prices, on the liquid milk.

Ritesh Vaidya: And Sir if you could explain me this, so if I look at your numbers, your procurement as you said that has effectively dropped almost 25%, 26% year-on-year, but somehow there has been a sales increase of 35%, so basically a lot of dairy ingredients sourcing has been done, but still that has not impacted your margins as much, so I mean doing business through dairy ingredients is also equally profitable then through milk procurement, can you just explain me?

Vivek S. Nirmal: It is not the situation always, but it all depends on what is the timing where you have been purchasing this ingredients, we have been purchasing ingredients in last couple of quarters obviously wherein the prices were lower than the current ones and now what we see is again instead of buying ingredients our liquid milk procurement is going up, so we have purchased this kind of ingredients like cream, butter and all and eventually converted it into our other products like condensed milk and whole milk powders and all.

Ritesh Vaidya: So you have a requisite amount of storage capacity, storage freezers are there with so, what is the capacity of storage that you have?

Vivek S. Nirmal: We have capacity, in case we require additional; we hire the capacity on-need basis.

Ritesh Vaidya: Okay and how is the procurement planning going into Q4, has it improved or...?

Vivek S. Nirmal: Procurement is improving; even in the Q4 said it is improving.

Ritesh Vaidya: Lastly you said your cheese utilization is at 18% to 20%, so the utilization is such a lower number because of what reason, is it a low demand or you are scalping up slowly?

Vivek S. Nirmal: We are relatively new to this segment, our plant capacities are larger because in larger plant capacities you can have better technology and better product quality, where you can afford that kind of technologies, so that is the reason why our production capacity utilization is low right now and it is increasing quarter by quarter.

Ritesh Vaidya: And the main product is processed cheese, mozzarella cheese, or ricotta which one is the main cheese?

Vivek S. Nirmal: Mozzarella cheese and processed cheese are the two main products followed by ricotta cheese.

Ritesh Vaidya: Okay Sir. Thank you. That is it from my side.

Moderator: Thank you. We will take the next question from the line of Resham Jain from DSP BlackRock. Please go ahead.

Resham Jain: Just two data points I needed on the inventory and debtor side, what was the number for this quarter end?

Vivek S. Nirmal: Sir inventory for the quarter end stood at around Rs.110 Crores and our debtor number stood around Rs.300 Crores for this quarter.

Resham Jain: And another thing, which I wanted to ask is for cheese plant if you look at the utilization level, will it make a significant difference once we start operating let us say at 30%, 40%, 50% gradually over next, let us say one or two years?

Vivek S. Nirmal: Yes because right now obviously a lot of capital has been invested in setting up the cheese manufacturing facility and as the volume increase definitely that will increase the overall capacity utilization and also our whey manufacturing, which is a byproduct of cheese.

Resham Jain: When can we see this happening, what is the duration in which you are looking this whole process to ramp up as per your internal expectation?

Vivek S. Nirmal: We were saying it to you by end of next quarter we should be at least more than 40%,50% of the overall capacity utilization.

Resham Jain: So does it mean that at 20% currently you might be hardly making money and maybe at 30%, 40% this number will significantly – because

most of the fixed cost might be same and....

Vivek S. Nirmal: That is true.

Resham Jain: Okay. That is it from my side. Thank you.

Moderator: Thank you. We take the next question from the line of Rajesh Kothari from AlfAccurate Advisors. Please go ahead.

Rajesh Kothari: Sir can you tell us, what is your current geographical revenue mix?

Vivek S. Nirmal: Actually we have two strings, consumer business and B2B. For B2B, we supply all over India, even for B2C now we are all over India, but for the consumer business where I do not have it in terms of percentages, but in consumer business most of our business happens in Maharashtra wherein we have two, three channels working together. The milk channel works in Maharashtra, the fresh product channel works in Maharashtra and long shelf life product channel also works in Maharashtra. In terms of our B2B business however, there is no specific geography because our clients have factories everywhere, so all these confectionary, bakery industries, they have factories everywhere, so we supply it almost all the states of India today.

Rajesh Kothari: So B2C is primarily you are saying Maharashtra?

Vivek S. Nirmal: Yes as of now.

Rajesh Kothari: So B2C right now is not pan India am I right?

Vivek S. Nirmal: Consumer business as I said is there in most than 25 states as I mentioned earlier, but that is mainly for long shelf life products, which includes ghee and UHT milk.

Rajesh Kothari: Okay, so can you just explain how difficult in this business to go to pan India because I always thought that there are always regional strong players, whether you look at Southern India, whether you look at Eastern India, whether you look at Northern India, so where every player is trying to become a pan India, how easy or how difficult it is to and what are the challenges when you are expanding from region specific to pan India player?

Vivek S. Nirmal: So Rajesh that is definitely right and you find strong regional players and our strategy also is similar to become a larger or a stronger regional player, but now this if you see about the regional player business profile, it is mainly to liquid milk and fresh products. When it comes to our product profiling we have a good mix of liquid milk and fresh product and also very good long shelf life products like ghee and UHT milk. Now long shelf life products obviously help you to go national because these products have longer shelf life, so three products particularly in our case is what we distribute in 25 states, which is basically are cow ghee and cow ghee has a longer shelf life and there are very limited players in cow ghee. We are getting a good demand for the product, so we are almost in about 25 plus state excluding the southern states. Second is UHT milk, which again has good demand from the milk-deficit states like North East and Jammu Kashmir and all and third is cheese, so again in cheese there are hardly three, four national players, so cheese again mozzarella cheese,

processed cheese has a good demand and that is the reason we are available in these states for these three products.

Rajesh Kothari: My second question is with reference to your B2B versus B2C business, it seems that in B2C business, it is a little bit more difficult to pass on the price increase compared to B2B business where it is more of a cost pressure, contract manufacturing kind of a business, so as – even your B2C business percentage revenue is increasing from I think 11% to now probably more than 30%, 35% how do you see... how you are planning to take this challenge?

Vivek S. Nirmal: In B2B we do not do contract manufacturing, it is only specialty ingredients what we manufacture, we also have some co-manufacturing activity, which forms a small part of our revenue. In that yes it is a pass on model in most of the cases or some cases, but in consumer business you are right, it is not possible for the prices to pass on immediately, given the market situations or given the competitive landscape; however, in a longer term for a company like us who is expanding its milk procurement base, it always is good to have a healthy mix of both these businesses while B2B business in specialty ingredients definitely gives us a good edge, but at the same time in terms of dairy unlike any agricultural commodity you will always see different seasons and different cycles, so having a healthy mix of both these segments we believe will help our company to maintain a stable margin profile going in future and that is the reason of getting into these segments and targeting around 50:50 mix of both these segments going future and longer term.

Rajesh Kothari: So just one last question, in last 10, 15 years since you are in this business from really a very long time I am sure you would have seen many ups and down of the milk procurement prices and because of the scarcity and drought and so on and so forth, so in the past – what kind of price increase has been highest price increase what you have witnessed in any given year and in those kind of years, what were your operating profit margins whether you were making profit or in some quarter it may not be possible to make profit?

Vivek S. Nirmal: So we have really not made losses in past any quarter for company in the history, but if you see in terms of level of pricing we have seen sharp rise in prices in 2013, but even they were not up to the level where the prices are today, so the prices which are there today are the highest prices we have ever seen in the past.

Rajesh Kothari: My last question is what is the brand investment what you are planning at a percentage of a revenue?

Vivek S. Nirmal: Sorry.

Rajesh Kothari: Total brand investment the advertisement spend, the brand investment...

Vivek S. Nirmal: We are working on that, we are right now in process, we have not zeroed in on the number, but we are working on that right now on our advertisement and A&P spends.

Rajesh Kothari: Okay. Thank you very much.

Moderator: Thank you. Ladies and gentlemen we will take the last question. We take the question from the line of Rahul Maheshwari from IDBI Mutual Fund. Please go ahead.

Rahul Maheshwari: Good afternoon. Thank you for the opportunity and very good set of numbers. My three questions, first of all what is the cheese capacity right now and going forward how much capex you would be providing towards the cheese manufacturing facility?

Vivek S. Nirmal: Current cheese capacity is around 30 tonnes per day, going forward we do not envisage any capex in the cheese capacity.

Rahul Maheshwari: And this cheese 30 million tonnes, which you are saying – it is a raw cheese or the processed cheese?

Vivek S. Nirmal: So 30 metric tonnes is the overall cheese, which includes raw and processed cheese manufacturing capacity, which we have right now.

Rahul Maheshwari: How much would be contributing towards the exports part because – towards the...

Vivek S. Nirmal: Very low right now, we have recently started export from the fourth quarter, we have also exported something in the last quarter and in this quarter also we are exporting; however, it is very low right now and we expect that to increase in the next year to come.

Rahul Maheshwari: And this 30 metric tonnes per day would be completely the processed cheese or it might be mix of a raw and processed you mean?

Vivek S. Nirmal: It is a mix of raw and processed cheese.

Rahul Maheshwari: Okay and the second thing as you said that you have got many of the B2B clients in terms of the largest domestic chains and you pass on the prices, so once you pass on the prices, it is the same like peers like Parag as he passed on the prices, so yesterday the commentary was that they might do some volumes for few weeks, so the same thing can be observed under you?

Vivek S. Nirmal: I do not know about the peers really, but as far as we are concerned we have a stable business model wherein the understanding in the cost plus model is the prices are pass on even the prices go down it is still a pass on, even if they go up it is still a pass on.

Rahul Maheshwari: And finally as you do not do contract manufacturing, but you supply the customized powder to Mondelez for the Cadbury and all this once these all clients go for a backward integration or they go for their own production, is that the scenario would be changing completely?

Vivek S. Nirmal: What kind of backward integration?

Rahul Maheshwari: Mondelez Cadbury is one of the big clients for you, so if he goes for... the skimmed milk powder or the customized powder, which is being given by you if he goes for his own production, then the how the scenario would be facing?

Vivek S. Nirmal: I do not think that Cadbury is going to purchase cattle and get into dairy really, rather it is the opposite they initially that has been the history of that company since 40, 50 years where they eventually moved out only to their core area, we do not really see because all these companies to whom which we cater, most of the clients are not dairy client, they are either large in confectionary or in the nutrition business or in the confectionary or in the bakery business, so I do not see them really getting into starting procurement of milk and getting into manufacturing of these products.

Rahul Maheshwari: And to the B2B clients, do you have a long contract kind of thing as means, for example Domino's or Cadbury?

Vivek S. Nirmal: So this ranges from, as I said earlier depending on product, but yes it ranges from around like three to six months contract to even two years, three years contract.

Rahul Maheshwari: Okay and final as the government recently has given a Rs.8,000 Crores to the dairy fund, though it is mostly for the regional players and the co-operative, but going forward as they have also mark that under undeveloped dairy state they would be also tying up with the private dairy company, so how big potential do you think in any form of inorganic opportunities or something because as the consolidation will also take place going forward?

Vivek S. Nirmal: That is definitely very good step government has taken because this segment needs more investments in terms of the dairy production, but the guidelines have not yet clearly come out. Once the guidelines clearly come out, we will be able to understand that how will it directly impact our business.

Rahul Maheshwari: And any inorganic opportunity a regional player, any of small size you are searching, evaluating for?

Vivek S. Nirmal: Right now we have a lot of un-utilized capacities, our major focus is obviously to initially fully utilize our capacities and to grow in the regions where we have already started selling our branded products, so right now we are focusing on that.

Moderator: As there is no response, Ladies and gentlemen since that was the last question, I now hand the conference over to the management of Prabhat Dairy for closing comments.

Vivek S. Nirmal: Thank you very much for all your time and for sparing your valuable time today, so as we continue our endeavor to build our consumer business as I said earlier and let us meet on the next conference call. Thank you very much.

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