"Prabhat Dairy Q2 FY2018 Earnings Conference Call"

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Moderator: Ladies and gentlemen, good day and welcome to Prabhat Dairy Q2 FY2018 Earnings Conference Call hosted by ICICI Securities. As a reminder all participant lines will be in the listen-only mode and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing "*" then "0" on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Aniruddha Joshi from ICICI Securities. Thank you and over to you Sir!

Aniruddha Joshi: Thank you Raymond. On behalf of ICICI Securities, we welcome you all to Q2 FY2018 results conference call of Prabhat Dairy Limited. We have with us Mr. Vivek Nirmal – Joint Managing Director and Mr. Raviraj Vahadane, CFO. Now I hand over the call to Mr. Vivek Nirmal for his comments on the quarterly performance. Thank you Sir and over to you Sir!

Vivek Nirmal: Thank you Aniruddha. Good afternoon everyone. I am glad to welcome you all once again on behalf of 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 second quarter and first half earnings for the FY18.

Before we discuss the quarterly highlights actually let me throw some light on our recently announced Vision 2020. We are an established player in the specialty ingredients business in the country and our aim is to leverage our expertise in milk to build a robust consumer product portfolio. We have revamped our corporate logo in line with our strategy to build our brand presence and expand our reach across general and modern trade. The new logo Prabhat Dairy 'where goodness begins' indicates most customer centric-brand and aspires to keep pace with evolving lifestyle trends of discerning consumers. We have classified products such as milk, dahi, ghee, lassi, chaas, ice cream under specific categories to ensure recover consumer preferences for taste, nutrition and indulgence. Our aim is to achieve Rs.2,000 Crores in terms of revenue by 2020 and we aimed to have a 50:50 mix between the B2B and B2C business.

Now let me emphasize on our milk procurement initiatives as well, which is the foundation of our aspirations. We have recently launched the Sanjeevani Yojana, which is a very innovative model, designed to boost animal management practices amongst farmers with small dairy farmers to improver their profitability. To further increase our milk procurement network, we have also initiated project Mahavistar, which is a continued effort towards increasing our high quality milk and we have increased our presence in existing as well as new regions like Solapur districts in Maharashtra to increase our milk procurement.

Coming to the financial performance of this quarter Q2 FY18, our total revenues increased around 18.7% YOY to around Rs.386 Crores. Pouch milk, cheese and paneer were key drivers of sales growth. Milk prices have remained flat on YOY basis. Gross margins improved from 19.7% to around 21.8% year on year led by higher realizations in the consumer business. Our EBITDA has grown on an absolute level by 13.5% YOY to around Rs.32 Crores. EBITDA margin decreased by 38 bps YOY from 8.7% to around 8.3%, basically manufacturing overheads were higher due to increased capacity utilization of cheese and ghee facilities. There were also some of the one of expenses in the last quarter and that is why manufacturing expenses are bit higher. Our Q2 FY2018 PAT marginally increased by 1.7% YOY from Rs.89.4 million to Rs. 90.9 million.

Going forward, we shall remain committed on growing our value-added consumer business while maintaining a stronghold in the specialty ingredient business. With this everyone I would like to leave the floor open for question and answer session.

Moderator: Thank you very much. We will now begin with the question and answer session. We have the first question from the line of Dhaval Mehta from Yes Securities. Please go ahead

Dhaval Mehta: Good morning Sir. Thanks for the opportunity. One clarification Sir, that Rs. 2,000 Crores revenue guidance, which we have that is for CY-2020 right, not FY2020?

Vivek Nirmal: That is for FY20.

Dhaval Mehta: Okay, so which means that assuming in FY18 in first half we have already grown by around 20%, so for entire FY18 if we grow by 16%, so the CAGR comes to around 12% CAGR from FY2017 to 2020, am I right?

Vivek Nirmal: Yes, around that.

Dhaval Mehta: But Sir our run rate is much higher than that right because we have been consistently going by around 18%-20% from last three to four quarters, so you feel that it is difficult to maintain such run rate and will the growth come down in ensuing quarters?

Vivek Nirmal: See if we go by our historical business model of only increasing the B2B sales, maintaining that growth rate is quite possible but our focus is now on building a consumer brand and we have also wanted to have a margin expansion. For which, we have carefully chosen to keep our B2B business constant as a whole, though it will see a lot of change internally. In B2B, we also service the corporate segment, we service the open market as well and we will continue to grow high quality customers only which give better margins and that is why as a whole B2B segment externally will not look like its growing too much. However, if we look at the consumer business particularly, which is around in a range of around Rs.400-500 Crores right now, we will see doubling from the current levels to around Rs.1000 Crores by 2020 and hence while the growth rate will be pretty high in that segment, our average growth rate will be relatively lower CAGR as you mentioned.

Dhaval Mehta: Okay. So it means that even our other expenditure will be at elevated levels for at least next one or two years because we are building the base to grow the consumer business.

Vivek Nirmal: Yes in terms of marketing, brand and distribution expenses, they will definitely be on higher side than the historical numbers because while our gross margins would expand we will be reinvesting the money in our brand investment.

Dhaval Mehta: Okay, so Sir even employee expenditure was higher this quarter, so any specific reason or this should be the normal around Rs.11 Crores of quarterly run rate, we should take it going forward?

Vivek Nirmal: Yes, as the consumer business increases, obviously the sales force increase is happening, similarly as the consumer business increases, our supply chain is also getting stronger and similarly in terms of milk procurement wherein we source milk directly, we do not source milk from intermediaries hence the employee expenses is on a higher side that is the major reason for employee expenditure to go higher from the current level.

Dhaval Mehta: Okay. That is helpful Sir. Sir I will come back in the queue. Thank you, Sir.

Vivek Nirmal: Thank you.

Moderator: Thank you. The next question is from the line of Prashant Kutty from Sundaram Mutual Fund. Please go ahead.

Prashant Kutty: Thank you for the opportunity Sir. Sir firstly while you said that you are not looking to grow the B2B business much, just wanted to understand over here is that the particular business is in general not growing much or is it a conscious decision from our end not to grow the B2B business?

Vivek Nirmal: Let me tell you we already supply to most of the key clients here in the country, when it comes to our high quality milk powders, cheese and all and these clients will continue to grow, most of the clients are growing, so we will also continue to grow with these clients and that corporate business will definitely see a growth; however, right now apart from those corporate clients we will also do a business, which is an open market business, wherein we sell our goods of milk powder and butter through wholesale channel. From this wholesale channel, the price realization might be good at sometimes, might not be good at sometimes and hence we want to limit that particular channel and hence while that channel will be seeing a reduced share of business, corporate clients will be seeing an increased share of business, but in totality the B2B business will seem to be constant and that is why we say that B2B business would remain constant in the years to come.

Prashant Kutty: Of the B2B, how much would be through our clients, and how much would be through the open market at this point of time?

Vivek Nirmal: So no break up as such particularly.

Prashant Kutty: Okay that keeps fluctuating.

Vivek Nirmal: Yes.

Prashant Kutty: Okay, but in general has that share been reducing for us now for the last year or so?

Vivek Nirmal: Yes. It has been reducing slightly and in the years to come, we will be seeing that reducing fast and the corporate business going up fast as well.

Prashant Kutty: Sir my second question over here is on the while you give a revenue guidance for Rs.2000 Crores with consumer mix also at about 50%, could you speak a little bit on the procurement side in terms of what are the targets you are looking at because you spoke about a couple of programs both with regards to farmer profitability and also with regards to procuring higher milk, if you could just tell in terms of what you really are looking at on the procurement side and how much you are going to be looking at incrementally coming from your end actually?

Vivek Nirmal: See our overall procurement right now is in the range of around 9.5 to 9.7 lakh liters of milk per day to achieve our vision 2020, which is Rs.2,000 Crores we will be needing at least 13.5 lakh liters of milk to 14 lakh liters of milk on a daily basis. So for that obviously the strategy is to go deeper in the villages in which we operate, at the same time we are also expanding our presence in the nearby districts like Solapur which we have already started before a couple of quarters and here we have different channels operating so we are basically setting up bulk milk coolers wherein we directly source from farmers to get a high quality milk which goes for our products like cheese, UHT and all and with the current setup we are quite confident of reaching that level of around 1.4 million liters of milk by 2020. As a part of which we undertake various programs and the Sanjeevani Yojana is also part of that, wherein we need to ensure the farmer profitability also grows, otherwise farmers will always be looking at higher milk prices for profitability, whereas the secret lies in their best farm practices which we impart to them and that is how their profitability also keeps on growing.

Prashant Kutty: Okay, so Sir incrementally when we look at, if I am not wrong, or correct me if I am wrong here, direct sourcing is about 65% and through third parties about 35%, so would that mix change as well over the next five years?

Vivek Nirmal: Yes, our target is ideally to have 80:20 ratio where our 80% would be from direct sourcing and 20% from the third party channel.

Prashant Kutty: Okay and last question from my end Sir you spoke that you will be needing marketing and distribution spends and that is expected to remain high, I am just wondering in terms of gross margins while at one point of time you has always been seeing that procurement costs have been going up, it is only now that it probably starts coming off for us, but obviously the gross margin expansion is to do with your realization improvement in the consumer business, but incrementally do you think that there is enough room as far as gross margin expansion is concerned to fund our marketing expenses and thereafter probably what is the EBITDA margin target we are looking at?

Vivek Nirmal: See as we reached Rs.2,000 Crores of revenues, we also target double-digit margins in terms of EBITDA and yes the strategy is to keep on increasing the gross margins in coming two to two and half years and reinvesting the money in our marketing distribution and sales. So we will continue to do that for next two years, two and a half years to come and ultimately we expect our overall margins to improve.

Prashant Kutty: So what will be an ideal gross margin number for us at Rs.2,000 Crores revenue, I mean assuming a consumer mix at 50%, what is the ideal gross margin mix that we are looking at that particular point of time because double-digit margin technically if you see at this point of time in the dairy industry there is no body who operates at the double digit margin, so I just want to understand what is the kind of gross margins you are targeting at that level?

Vivek Nirmal: See right now we do not have any specific target on the gross margin level, so that is not possible for us to say, but yes directionally the gross margin expansion is the target and which is happening in the past couple of quarters if you see and it is also evident from the last quarter as well and the gross margin are steadily improving, every quarter we increase the gross margin by like half percent, one percent or more than that and the same is being utilized for funding the brand investments.

Prashant Kutty: Okay, there is no target in your mind, but aiming to improve?

Vivek Nirmal: Yes.

Prashant Kutty: What would be the potential mix of the consumer business, when you are looking at Rs.2,000 Crores revenue guidance, any mix of the consumer business in your mind what you are looking at?

Vivek Nirmal: Mix in the sense?

Prashant Kutty: As to what will be the major contributors in the consumer business?

Vivek Nirmal: Yes, so see there are basically three to four categories, which we are focusing on and liquid milk is the largest category, second is cow ghee and third and fourth which are equally important for us is UHT milk and cheese respectively. These are four particular products which we are targeting, and these will be the major contributors in our consumer business.

Prashant Kutty: Thank you Sir. I shall come back.

Vivek Nirmal: Thank you.

Moderator: Thank you. We have the next question from the line of Sameer Gupta from IIFL. Please go ahead.

Percy Panthaki: This is Percy Panthaki here. Sir jut wanted to understand margin dynamics for the B2B business and the B2C business, so my question is at the gross margin level, how much of a difference is there between the B2C margins and the B2B margins currently, in basis points if you can just give the approximate difference?

Vivek Nirmal: That is around 10% difference - in terms of percentage in B2B and B2C.

Percy Panthaki: So that is 10% points or 10% growth?

Vivek Nirmal: 10% points. So if B2B is at 17%-18% gross margin, B2C business is at around 27%-28% gross margin level.

Percy Panthaki: Okay and Sir within B2B also you said there are two types of businesses, one is institutional like Dominos and Pizza Hut and other is the wholesale channel, so again between these is there a difference in the gross margins?

Vivek Nirmal: There is a difference, we do not have a break up for it right now, but yes there is a difference in between both these channels as well.

Percy Panthaki: What I was trying to attempt is just to see I mean once you discontinue this wholesale business and let us say that becomes zero in two or three years, then this 17%-18% margins for the B2B business, how much can that go up to just because of the mix change between the B2B business?

Vivek Nirmal: It will not go down fully, it will reduce definitely, it is not going to become zero for sure but we expect that to remain stable at the current level, maximum gross margin expansion will happen from the consume business side.

Percy Panthaki: But Sir the reason why you are declining this business of wholesale is that – it is very poor margin business right, so if after doing that the margin does not change for the B2B segment then why are you giving up that sales?

Vivek Nirmal: See it is not about poor margins right now, but going forward as you know, the milk situation improves, we believe that it could ultimately result in to lower margin business in the future, so to curb that risk right now we want to decrease our dependent on that particular channel.

Percy Panthaki: Sir my next question is on the operating leverage in the B2C segment, so since the gross margins are about 27%-28%, if you could give me an idea what the EBITDA margins are currently and over three years because of EBITDA just because of the operating leverage even if the gross margin remains constant at that 27%-28%, how much can that EBITDA for the B2C business go up by?

Vivek Nirmal: See for two things right now at EBITDA level, our B2C or B2B is at a similar range of around 8%-9%, not in terms of gross margin we do not expect the gross margin to remain at the same level of B2C, we expect the gross margin actually to improve from the current levels in the B2C business.

Percy Panthaki: Okay and what would be the driver of that?

Vivek Nirmal: It is basically as we invest more into the brand building and all, our realizations we are continuously aiming at pushing up our realizations, second is particularly the mix of value-added products particularly, as it increases that will also push up the overall gross margin level.

Percy Panthaki: Okay, but you do not see any leverage between gross margin and EBITDA margin, so right now your expenses are like around 20 percentage points right, 28 and 8 so the difference is around 20 percentage points, as you become bigger in scale, do you think that 20 percentage points can go down and if so by how much?

Vivek Nirmal: Absolutely, again it is difficult to put a number to that but yes see last two to two and a half years we have been building around distribution, infrastructure in terms of depots, distributors and all and there is a cost to it, it is an operating cost, so obviously as the pipeline carries more and more products, the cost per unit will go down, so we also see some reduction in that as a percentage as well.

Percy Panthaki: Right Sir. That is all from me. Thanks and all the best.

Moderator: Thank you. Next question is from the line of Sanyam Jain from Edelweiss. Please go ahead.

Manoj Baheti: Vivek, this is Manoj here from Edelweiss. My first question is to get your views on recent talks on MSP on the milk prices especially in Maharashtra, one is that though I would say that there may be low probability of that happening, but if that happens, how it will impact, especially the private players in the industry?

Vivek Nirmal: See particularly if you see MSP, it is not possible for the government to have an MSP on milk, no where in India there is MSP on milk first of all, there is no state which follows MSP for milk. There is a similar product 'sugar', in which there is no MSP, but there is FRP, it is the floor price and it is possible in sugar because in the entire country, 100% of sugar business is in organized space, entire sugar is not produced at the household but it is in the sugar mills only and since interstate trade is very high, the FRP has to be implemented in the entire country, not only one state, if a legislation has to happen in milk, number one it is very difficult because 65% of the dairy business is unorganized. There are small farmers who produced milk and sell it directly to the consumers as well. Number two there is a huge interstate trade as well, so if MSP must be implemented; it has to be implemented in the entire country. So I do not think it is a practical thing. Obviously the government wants to secure the farmer prices, there has been multiple agitation and all due to which the state government also is trying to do, something to protect the farmer margins and they have been trying particularly to tell the co-operative dairies because government has an influence only on the cooperative dairies, not on the private sector because the cooperative dairies are governed by certain laws of the state government and hence talks are going on and I do not have any further details on it, but this is about our view based on our experience in the industry.

Manoj Baheti: But Vivek in politics sometimes crazy things do happen, so if that does get implemented, will it impact cooperatives more or even because I believe the cooperatives are having a lower procurement price than the private players?

Vivek Nirmal: See the cooperatives right now have a higher procurement prices than the private players. In Maharashtra particularly if you see 60% of the milk is handled by private sector, 40% of the milk only handled by the cooperative sector and this is also in the organized sector, 65% of the milk which we are still not talking about is completely in the unorganized space, so it is very difficult to have an MSP for that particular milk, and hence it is very impractical thing to have an MSP particularly for this kind of a product. Second issue is about the interstate because if there is MSP here, there is a high possibility of the out of state milk coming in the state again, which has been happening continuously, so with all practical conditions, considering all the practical conditions, all said and done this does not seem to be a practical thing really. I will not be able to comment on whether politics will have an influence over as it is out of my purview, but this is our take on it.

Manoj Baheti: But I mean are you preparing any plan like if it gets implemented how it is going to impact you although I agree that there is a very, very low probability of it is being implemented?

Vivek Nirmal: See first of all if it is implemented, it will have to be implemented in the entire country. There is no MSP in any state right now in the country - number one. If tomorrow by any reason it gets implemented I think it is going to be implemented for the entire industry and hence whatever applies for the industry would apply for us as well. Basic issue if you see is not about the pricing for the farmer. Basic issue is about the profitability of the farmer. And hence if you see Prabhat Dairy is continuously investing and taking a lot of efforts in terms of improving the profitability of the farmer, which we are doing consistently since more than a decade now and hence our farmers continuously do not really focus on the sales price what they get, but the focus is on the farm inputs and how to reduce their cost of production really. They have been successfully doing in the past. I think we will continue our efforts from the front in the future as well.

Manoj Baheti: Okay. Secondly if you can share your views on competition especially in terms of institutional cheese business because I think one of the largest player in the country Amul, mentioned that they will start focusing this segment very aggressively now and also they have scaled up their capacity also significantly, so are you seeing some kind of pricing pressure in this particular segment?

Vivek Nirmal: See, our food service division particularly, there are two divisions, which we operate particularly in cheese, one is the B2B wherein we service the large QSR chains, pizza chains and all and second segment is the food service division. The food service division we already have a large network now throughout the country since we are amongst very few large cheese players in the country through which we sell our mozzarella and processed cheese, so we too depend on the large QSR chains, but we also have our more than 3000 smaller accounts, which buy cheese from range right from 200 kg to 800 kg per month. So growing the food service division wherein the margins are also relatively better is number one priority. Number two if it comes to particularly large players, I think everybody is increasing capacities today because this particular segment 'institutional cheese' is growing at a very healthy pace and whenever capacity expansion has to happen, it cannot happen only considering next one or two years it has to happen considering next five to 10 years, so I definitely see a positive that everybody is adding a capacity. If we talk about the competitive price pressure in that, we particularly operate in very different areas, for example we are a cow player only and that is why we do not operate in buffalo milk cheeses, we operate only in cow milk cheese, cow milk cheeses are much better in terms of functionality and hence we bang on the USP of our products and even today we do not sell our products really at too much of discount, but we get good market share based on the high quality of our products.

Manoj Baheti: Okay, so that means other than the non-institutional HORECA segment, you are not seeing much of the pricing pressure, right?

Vivek Nirmal: No.

Manoj Baheti: And on the institutional side is there some pricing pressure or because of the different segments cow cheese and buffalo cheese and as cow cheese players are less, are you seeing some pressure on that side?

Vivek Nirmal: Not as of now.

Manoj Baheti: Okay. Thanks for taking my question.

Moderator: Thank you. We will take the next question from the line of Aniruddha Joshi from ICICI Securities.

Aniruddha Joshi: Hello Sir. Just two to three key data points, so the GST rate on condensed milk has reduced from 18% to 12%, so what was our revenue coming from condensed milk business and what is the B2B and B2C share, also when we pass on the entire benefit whether there is any possibility of returning some benefits?

Vivek Nirmal: See condensed milk we do not sell in the B2C segment because the B2C segment market is very small particularly for 400 g tins and we have a good business of condensed milk, but again here it is specialty ingredients, which we sell to lot of bakeries and food MNCs and domestic players, our revenue share is not more than 4%-5% of that particular product. It is definitely positive while for us it is passed on, if it is an 18% or 12%, it is passed on to the client because we are operating in the industrial segment but I believe it is a good input I think saving for the client and hence it is good for bakery sector and the confectionery sector and if it is good for that sector, I definitely say it is a positive for us because we are the ingredient supplier.

Aniruddha Joshi: Okay, also now with this relaunch, there must be some extraordinary one-time expense in the other expenditure line in 1H FY2018 results, so is it possible to quantify the cost of relaunch and also by entire relaunch cost is over or there will be some cost which will get incurred in Q3 as well?

Vivek Nirmal: Okay, so actually we have not relaunched our products really so to say what we have done is we have revamped our brand identity only and in our revised brand identity, the entire packaging material and all is now with the new brand identity, the marketing campaigns actually are yet to follow and by next year we will definitely see more aggressive marketing campaigns and all, so it will not be possible really to say that the relaunch is over or there is no extraordinary cost as such for this relaunch right now.

Aniruddha Joshi: Okay, Sir and one data point what was the milk procurement price in Q2 FY2018 versus Q2 FY2017?

Vivek Nirmal: See on YOY basis, it has been very similar in Q2 FY2017 our price was around Rs.25.5 per liter on Q2 FY2017 and Q2 FY2018 it is again on the similar range that is actually around 10-15 paisa cheaper on an average basis, so it has remained constant on YOY basis. Though on a sequential basis, it has reduced from Q1. For on a YOY basis, it is constant.

Aniruddha Joshi: Okay and can you indicate where we will see the milk prices going in next three to four months, do we see any sharp correction or maybe just small correction here?

Vivek Nirmal: Again it is difficult to say, see there are lot of macro factors supporting such as good monsoons consecutively for two years and the milk availability is increasing, so we definitely see that the prices will get softer from the current level, but how much softer it will get will be difficult to say because in hindsight the demand for the cow ghee and fat product is continuing, there has been exports also happening of the cow fat from the country and hence it will be difficult to say exactly how much it will soften, but one thing is sure it will soften from the current level from now.

Aniruddha Joshi: Thank you.

Moderator: Thank you. The next question is from the line of Binoy Jariwala from Sunidhi Securities. Please go ahead.

Binoy Jariwala: Thank you for the opportunity. Could you help me with the geography wise, the region wise breakup of your sales?

Vivek Nirmal: Region in the sense our majority sales, we do not break it up into regions as of now, though we track it region wise, but we have not disclosed region wise sales. On a broad basis, I can definitely help you with the indication. Our majority of the business is in Western part of India because for fresh dairy products which includes our products like milk, dahi, shrikhand, paneer. Since these are all logistics sensitive and short shelf life products, you operate for all these products only in Maharashtra and that is why the share from western part of the country is higher because we have more channels over here. Second is after Western India, our higher share is in North India, particularly we have started north India before around 18-24 months and this is basically because of our products like cow ghee and cheese. Third largest market for sales is northeast right now wherein lot of our UHT milk and dairy whitener gets sold and then the fourth market is east, we are not present in Southern India, we have very recently opened our depots in Hyderabad and Bengaluru and those are particularly for focusing on cheese, we do not intent to launch our consumer products in South India as of now.

Binoy Jariwala: Likewise is the current milk procurement entirely from Maharashtra?

Vivek Nirmal: Yes, our milk procurement is 100% from Maharashtra, we do not procure from outside the state, though we procure some milk in the past from the nearby states and it was a drought situation, but right now 100% of the milk procurement is from Maharashtra only.

Binoy Jariwala: Okay, so now when we have to move from procuring 9.5 lakh liters a day to about 13.5-14 lakh liters, would you have to enter new states for procurement?

Vivek Nirmal: No, we had lot of room to grow here in Maharashtra because of our milk procurement channels are pretty robust and our strategy is to go deeper in the current villages, so at least 15%-20% of the milk will be coming from the current farmers only or the current villages only because there also we are working on productivity of animals and we have seen very good growth in those numbers as well. It is a long journey, but we have been trying since last 10 years, so last two to three years we have been finding very good growth in terms of the productivity of animals and around 20% of the additional requirement will be full filled from the nearby states like Solapur and all where we have started operating from this year onwards.

Binoy Jariwala: So you mean of the incremental 50%, 20% will be taken up by Solapur and nearby areas?

Vivek Nirmal: Yes, so 50:50, if we want 4 lakh liters of additional milk, 2 lakh liters coming from newer regions and 2 lakh liters coming from the existing regions.

Binoy Jariwala: Okay. Within the existing your farmer base, do you have 100% share of their milk?

Vivek Nirmal: Yes whoever formal supply to us are 100% exclusive to us.

Binoy Jariwala: Okay. Thank you so much.

Moderator: Thank you. The next question is from the line of Akshit Gandhi from Kotak Mutual Fund. Please go ahead.

Akshit Gandhi: Just a couple of questions, the first one is we hear that Heritage and all are becoming aggressive in Maharashtra and all, so is there a risk to the procurement prices because I agree Maharashtra procurement prices are quite low versus Hyderabad and all of course, but do we have a risk of increase in procurement prices?

Vivek Nirmal: I do not see there is too much of difference actually from Maharashtra prices and the prices of other states, it always a lag effect and other states automatically follow because now the transportation network is pretty good and in case of a shortage or an excess, the milk is really traded between the two states, through various channels, number one. Number two, I think there is a enough room for growth because Maharashtra and not only Maharashtra we see in all the states right now milk procurement is growing, so particularly for one specific company entering into Maharashtra I do no think that is going to really disturbed the table over here.

Akshit Gandhi: Okay, also on the working capital side, we are seeing that the working capital has improved, inventory days have reduced. So is that a seasonal phenomenon and it can rise back in March or will be continued at these levels?

Vivek Nirmal: See it will continue at this level, though as a larger part of the strategy, we will want to improve our consumer business wherein the receivables are lower, the inventories would be lower, and as a result of which we will be able to free up lot of capital in days to come, but as of now we see it at a constant level for the next couple of quarters.

Akshit Gandhi: Okay and any specific increase reason for increase in payable days?

Vivek Nirmal: No specific increase as such that is a part of our routine milk payment cycles and the other items like packaging material or the consumer bills or the fuel and all. So the credit also maybe increased to certain extent to some of the suppliers, but that is what is reflecting here.

Akshit Gandhi: So let us say when you reach at Rs.2,000 Crores topline, how should we look at our working capital, what would it be?

Vivek Nirmal: See at Rs.2000 Crores level, our working capital will not increase in the proportion of the increase in the revenue growth particularly because the consumer business has relatively lower receivable days as compared to our institutional business right now. So we do not expect the working capital to go up in the similar proportion as the revenues will go.

Akshit Gandhi: One question on the product category side, let us assume that if cheese plants have to run at 80% utilization, what kind of returns to we generated on our invested capital?

Vivek Nirmal: Again we do not track product wise returns reason being lot of things like utilities, storage and all is common, not only for cheese but for other products as well, but definitely cheese has a product category has much higher gross margins than the other products because first of all there are very limited cheese players in the country and second whey in particularly also has supplementary margin to cheese.

Akshit Gandhi: But then the issues that cheese as a higher inventory period also because it takes three days?

Vivek Nirmal: Yes, definitely.

Akshit Gandhi: Yes, so the higher margins in a way is set off because the capital invested is higher, so that was the reason. All right and one last question, how should we look at the tax rates for the full year for this year and next year?

Vivek Nirmal: It is a full tax rate, 34%.

Akshit Gandhi: Okay, if I understand correctly, we had a lower tax rate in this quarter, any specific reasons?

Vivek Nirmal: No specific reason , it will be apportioned over four quarters.

Akshit Gandhi: Okay, so the next half we will see a higher tax rate versus the first half, right?

Vivek Nirmal: Yes, we are at a full tax rate.

Akshit Gandhi: Thank you so much.

Moderator: Thank you. The next question is from the line of Bharath Subramanian from Sundaram Mutual Fund. Please go ahead.

Bharath Subramanian: Good afternoon Sir, just a couple of questions on the retail side distribution, so how are we progressing in terms of our distribution touch points and in the earlier calls also we had touched upon starting distribution to some of the states, outside the western region, so any progress on that Sir?

Vivek Nirmal: See in terms of distribution in the retail, there are two to three channels what we follow particularly on our LSP division, long self life product division, we have recently launched products like UHT through which we are also targeting a couple of A class outlets because we already have a good distribution network built across with more than 12 distributors and 1 lakh retail outlets, but quality of outlet also is a very important matter and the more better quality outlets to have, your sales per outlet increases, so with products like UHT milk and all we are gaining access to better quality outlets in the sense A class outlets as we say. Number two is in terms of modern trade, earlier we operated for the last three to four years only in Maharashtra, but now we have increased our presence in northern towns as well right from Delhi to Lucknow to central towns like Indore, Ahmedabad and even in Kolkata, we have started the modern trade outlets, we are present in chains like Star Bazaar, Big Bazaar, Wal-Mart, Reliance, Easyday, D-Mart and all that is where we have increased our presence and third is food service division, which also serviced through our distributors, retail distributors particularly since they have a very wide range, again in the food service channels, we have tapped lot of small and local chains in those particular towns for our Mozzarella cheese and cheddar cheese, so right now we covered around 100,000 general stores in GT, last year in modern trade we were around 140 stores, right now it is around 289 stores and we are already around 375 distributors now and our presence is right now in 26 states and two Union Territory as well .

Bharath Subramanian: Okay, so currently this year the retail as of the first half would be how much will be the contribution sir in terms of B2C put together and within that retail?

Vivek Nirmal: It is in the range of 30% right now. So while our vision remains to take it to 50%, every quarter the mix really changes, right now it is in the range of 30%.

Bharath Subramanian: Okay and in terms of Volup again when would be we kind of starting a campaign in terms of distribution revamp?

Vivek Nirmal: Volup ice creams we have launched in the month of March. These are all milk based ice cream and we have seen a very good response in terms of offtake of those products. We have done a very limited soft launch that is only in four towns of Aurangabad, Nasik, Ahmednagar and two smaller districts as well. We will continue to remain here itself. We are not planning for immediate large ramping all over the Maharashtra or all over India, because we first of all want to gain a good expertise and understanding of that as a business, it is a frozen business, it is a different distribution chain than our current chilled products, so I believe for the next couple of quarter, we will further observe it, we will further understand what are the customer preference is, where are the products, which give us better margins, where are the products which where we have unique place to play and based on that maybe 2019 onwards, we will expand them largely, so for the next year our focus is going to be remaining mainly on Prabhat milk, Prabhat ghee, UHT milk and cheese.

Bharath Subramanian: Lastly in terms of the dairy farms, we were kind of contemplating the project on dairy farms and a project on the dairy farms and practices over there, so is that something which you can throw light on in terms of what we are targeting in that space?

Vivek Nirmal: Right now if we see around 75% to 80% of the farmers, which supply milk to us are small and marginal farmers and average farmer supply 10 to 12 liters of milk, it was similar situation in other part of the country as well and we are promoting midsized farm from 20 to 40 animals, we have been doing it consistently. Now we have come up with the comprehensive model of a Sanjeevani Dairy Farm, which is the modern dairy farm and which has the best practices, wherein we basically work on four pillars, which is the feeding, breeding, animal management and healthcare and wherein we impart one of the best practices there. We ensure that the profitability of the farm grows, these are implemented in various villages, so once that farm grows, it is a profitable dairy farm and that is then displayed to lot of farmers in that vicinity and for farmers basically seeing and is believing. A demonstration of a successful dairy farm in their region by other farmer is much better than the class room training for them and that is how these are the dairy farms we are building, we have already started these Sanjeevani program. We have 30 farms right now enrolled in this particular scheme and these are successful model dairy farms. We will eventually grow this and enroll more and more farms under this. So the farmers also get the benefit of economies of scale. At the same time these are the mechanized – all these farms follow the best practices in terms of machine milking. So Prabhat also gets the best quality milk, which is untouched by human hands and in the future it will help us to grow to enter into more premium products of farm to home milk and all. So this is the foundation we are building for that through our mild procurement network.

Bharath Subramanian: So we owned the farms over here Sir?

Vivek Nirmal: No we do not own any farm, these are all farmer owned farms, we support them in terms of best practices to come from a level where they are right now to very high profitable level and wherein they implement all the best practices in the industry.

Bharath Subramanian: But the entire procurement from there is captive to us?

Vivek Nirmal: Yes, 100%.

Bharath Subramanian: Great Sir. That is it from mine. Thank you.

Moderator: Thank you. Next question is from the line of Dhaval Mehta from Yes Securities. Please go ahead.

Dhaval Mehta: Thank you Sir. Thanks for the follow up. Sir my question is on the prices, so we are seeing a declining trend in the milk prices, so how are the cow fat prices behaving?

Vivek Nirmal: Cow fat prices are also softer right now. If you see in terms of cow ghee, the prices right now has not been increased in last one quarter as well, though the GST increased from around 5% to 12%, but most of the players continued the MRP at the same level and they observed that VAT increase because the milk prices also have gone down, and fat prices are also relatively soft, but we do not see the fat prices going down from this level because globally there is a fat shortage and there is a lot of fat which has started getting exported from India as well. So these are soft right now, we see it remaining at the current level.

Dhaval Mehta: Okay, so we expect the milk prices to decline further, but the fat prices will be remaining at the current levels?

Vivek Nirmal: Yes.

Dhaval Mehta: Sir at what level of declining milk prices we expect the reduction in our B2C portfolio, so right now we have not taken any reduction in prices, but we might be taking assuming that if the milk prices goes down to around Rs.24 odd level or so and what level of milk price we expect the reduction in the end consumer price?

Vivek Nirmal: There is no threshold as such to that, but it depends on various factors including yes obviously what is the milk price, how much it has down, but also what is the expectation of it to remain down. If it is expected to be temporary dip then the price reduction might not happen. Second it also depends lot on what are the other elements of the industry do, what would the co-operative do and all and as the part of which because in terms of liquid milk we are not a very large player, we have a limited presence, very strong presence in our couple of pockets, so it also depends largely on what other players in the industry do and as a consequence of that the reduction in the MRPs will happen.

Dhaval Mehta: Okay, so till now we are not seeing any reduction by any players?

Vivek Nirmal: No, still now we are not seeing any reduction by any player.

Dhaval Mehta: That is helpful. Thank you Sir and all the very best.

Moderator: Thank you. The next question is from the line of Yogita Desai from Akashganga. Please go ahead.

Yogita Desai: I just wanted to know in ghee and cheese segment what is the share of B2B and B2C business right now?

Vivek Nirmal: We again will not be able to give a breakup of product wise and segment wise things, in terms of cheese, but we particularly see I think it should be in the range of 50:50 because in consumers while we do not have exactly the branded cheese or the consumer packs wherein we have like long and small slices or portion packs and all, our consumer cheese is about food service division and our institutional is about the large pizza or the QSR chains. The display would be roughly 50-50 in terms of cheese.

Yogita Desai: What would it be for ghee segment?

Vivek Nirmal: Ghee is largely consumer only though we do not have a break up right now, but it is largely in the consumer segment only.

Yogita Desai: Thank you very much and all the best.

Moderator: Thank you. Next question is from the line of Bharath Subramanian from Sundaram Mutual Fund. Please go ahead.

Bharath Subramanian: Sir in the initial comments you have mentioned some one-offs in terms of manufacturing over anything that you can quantify over there?

Vivek Nirmal: Again not possible to quantify that but see it is definitely we expect the manufacturing expenses to be lower than the last quarter in the quarters to come.

Bharath Subramanian: Okay and on the bulk coolers that we have kind of embarked in terms of expanding, so how does that work in terms of recording that investment and depreciating and these are investments which we take in our books right?

Vivek Nirmal: Yes, bulk milk coolers are the investments, we own the bulk milk cooler so the entire investment is in our book and that is depreciated over the asset life, I do not, maybe it could be the asset life of what next 8 to 10 years through which it depreciates.

Bharath Subramanian: Currently this year, what is the target in terms of expanding the bulk milk coolers?

Vivek Nirmal: Right now we operate around 150 bulk milk coolers and by end of March we are reaching 200 bulk milk coolers, some of them are in the existing locations wherein the milk is increasing, some of them are in the new locations like Solapur and all.

Bharath Subramanian: Just on this new location in terms of logistics, how different would it be because the crossing center is still at the same place, so in terms of the additional procurement how much expenses or cheap would it be if you were to expand to neighboring regions?

Vivek Nirmal: See additional districts definitely means increase in transportation cost because the farther we go the transportation cost increased, but advantage is that we have two plants in Maharashtra, one is in Mumbai, and one is in Shrirampur. So for example in some places like Solapur we do not bring the milk to Shrirampur because it is equivalent distance from Solapur to Shrirampur as well as Mumbai, so we bring it directly to Mumbai, similar is in case of lot of parts of Pune and all wherein it is again equivalent distance from Shrirampur and Mumbai, hence we directly bring it in our Mumbai plant so to make up that additional transportation cost.

Bharath Subramanian: But broadly it does not – is it too deviant from the average procurement price that we have?

Vivek Nirmal: No, not really. It is not a very large difference in terms of transportation cost from the current ones.

Bharath Subramanian: Thank you Sir.

Moderator: Thank you. Next question is from the line of Sagarika Mukherjee from Elara Securities. Please go ahead.

Sagarika Mukherjee: Thanks for taking my questions. Sir what was the average milk procurement cost for the quarter?

Vivek Nirmal: Average milk procurement cost for quarter was around 25.6.

Sagarika Mukherjee: Sir what is the current run rate, is it closer to 22 or 23?

Vivek Nirmal: No, right now it is around lower by around Rs.1 to Rs.1.5 from the last quarter.

Sagarika Mukherjee: Rs.24 per liter?

Vivek Nirmal: Around 24 to 24.5 right now.

Sagarika Mukherjee: Okay and Sir in this situation where are we expecting prices to let us say fall, I am not holding against it, but let us say does fall, then will you be able to sustain your realizations in your non-pouch milk business anywhere?

Vivek Nirmal: Yes in terms of B2B, most of the businesses are a pass on pricing, so whenever the prices increase we pass them on and whenever prices are decreasing we have a very transparent system, we will pass them on. In terms of consumer business, I think yes definitely it could result in an expansion of margins, it could be for a shorter time if the MRPs go down, it could be for a longer time as well if the MRP do not go down, but as a strategy, we will reinvest all that difference in building a brand because it is a good opportunity for us to build brands as the gross margins expand.

Sagarika Mukherjee: Okay and Sir one more thing if milk presence keeps going down and SMP prices also remains weak globally and in India like it has been till now, then do you think your excess margin in things like ghee, will we be able to cover off the losses in SMP?

Vivek Nirmal: See again in terms of our powder business, we do a lot of whole milk powder business wherein we dry fat and solids together, so there is not too much of a mismatch there and in terms of cow ghee I think we have good enough sales now for the consumers, in the consumer segment of cow ghee, so I think I would not say that we are protected, but I would say we are more balanced on the B2B and B2C side to really manage the impact if the prices go down no more than particular level.

Sagarika Mukherjee: So as a combination ghee and SMP are profitable for you right now?

Vivek Nirmal: **S**ee again we would not do too much of SMP, we do more of the whole milk powder, ghee is definitely profitable.

Sagarika Mukherjee: Thank you Sir. Thanks a lot.

Moderator: Thank you. That was the last question, as there are no further questions, I would like to hand the conference back to the management for their closing comments.

Vivek Nirmal: Thank you everyone for being a part of today's call. Let me assure you that our team, Prabhat is motivated towards achieving our ambitious targets and we are very confident of achieving it as per the expectations of all stakeholders of the company. Thank you very much.

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