"Prabhat Dairy Limited Q4 FY2017 Earnings Conference Call"

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Moderator: Good morning ladies and gentlemen welcome to the Q4 FY2017 results call of Prabhat Diary Limited hosted by Emkay Global Financial Services. We have with us today Mr. Vivek Nirmal – Joint Managing Director and Mr. Raviraj Vahadane, CFO. As a reminder all participant lines will be in the listen-only mode and there will be an opportunity for you to ask questions at the end of today's presentation. Should you need assistance during the conference call, please signal the 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. Dhaval Mehta from Emkay Global. Thank you and over to you Mr. Mehta.

Dhaval Mehta: Thanks Lizaan. Good morning everyone and welcome you all for Q4 FY2017 earnings con call Prabhat Dairy Limited. We would like to thank the management for giving Emkay the opportunity to host this call. From management, we have with us Mr. Vivek Nirmal – Joint MD and Mr. Raviraj Vahadane, CFO. So we will start with opening remark by Mr. Nirmal followed by Q&A. Over to you Sir!

Vivek Nirmal: Thanks Dhaval. Good morning everyone. It is a great pleasure to greet you all 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 fourth quarter and full year earnings for FY2017. Before we discussed the financial performance during the quarter, just allow me quickly to highlight our business philosophy and our fast transforming business model, which will help us to capitalize on our dairy industry growth and achieve long-term sustainability. I am very happy to share that we recently launched ice cream brand Volup in March 2017 in key towns of Maharashtra like Nasik, Ahmednagar, Aurangabad, Jalgaon and Dhule. Our popular range of ice creams are retailing under the Volup brand name and the premium range of ice creams are retailing under the Volup Sinsane brand. Volup is actually an extension to the existing basket of products under the Prabhat brand. While Prabhat brand represents the traditional dairy products, Volup brand will offer products to meet the aspirational needs of the consumers. We are fully integrated milk and dairy product company right from the farmer to the end customers. We are evolving from being established specialty dairy ingredients company to an emerging consumer focussed and brand-driven company with a wide range of dairy products under our brand portfolio. Our strong success is backed by our integrated business model, robust milk procurement system, which is built on intense farmer engagement and trust as well as the state of manufacturing facilities and strict quality control and food safety standards. Sorry to interrupt. Dhaval I think there is some echo, could you please check on.

So now today we have a solid foundation of B2B business with a marquee clientele. During the quarter, we have appointed Mr. Sridhar Viswanath who is ex-Mondelez. He has 16 years of experience in different sectors in the agri business. We have appointed him as a commercial director. We have also entered into MOUs with Nutridor Limited Thailand for being its co-manufacturer for cow ghee and mozzarella cheese. We continue to ramp up our cheese supplies by partnering with companies like Dominos, Britannia, Dabon International to name a few. We are witnessing a very rapid scalability in our consumer business especially which has grown from being only in one state in 2012 to now around 26 states with around 1200 plus distributors and around one lakh retail touch points as on March 2017. We recently appointed Mr. Muthar Basha, an ex-HUL FMCG veteran, as head of consumer business. We further intend to scale up our B2C business and grow in share from 30% revenues in FY2017 to around 50% revenues by 2020. We continue to expand our retail presence in modern trade as we started our retail business more than three years back. Today, we are present only in Maharashtra in 140 modern trade outlets. We have plans to reach 1050 modern trade outlets by March 2018, which would include the expanding our presence in West India, North India and East India.

Coming to our financial performance for the quarter, our Q4 2017 total revenues increased by 23% year-on-year to Rs.3776 million, milk procurement prices increased 5% quarter-on-quarter from an already high level of Rs.27.21 per liter to around Rs.28.57 per liter and the raw milk availability continued to remain impacted. However, better realizations of products like milk, butter, ghee, condensed milk and specialty milk powder have helped us offset the impact of higher milk purchase prices. So Q4 2017 gross profit has increased by 19.9% year-on-year to Rs.712 million. The share of value-added products increased to 88% now of total revenues. It is mainly driven by speciality ingredients and cheese. Our Q4 FY2017 EBITDA has increased by 17.9% year-on-year to Rs.303 million. EBITDA margins decreased by 35 bps; however, year-on-year from 8.4% to 8.0%. We incurred higher business promotion expenses because of greater focus on value-added products and the consumer business. Q4 FY2017 PAT has decreased by around 130% year-on-year because of the higher deferred tax recognition in the quarter.

On a full year basis, our revenues grew 20.7% year-on-year to around Rs.1411 Crores. Our EBITDA increased by 9.7% overall to Rs.128 Crores, our PAT increased by 102%, year-on-year to around Rs.46.9 Crores led by overall growth in the business and recognition of the mega project benefit. So while that is on the business performance, I would also like to update on some of the key events in the last quarter. As informed by the company earlier, there has been search and survey conducted by the income tax department in October 2015. While no additional income was disclosed by the company; however, the department observed some errors in the calculation of depreciation as per the Income Tax Act, hence the company has corrected the same in the last quarter.

Secondly the company has also accrued an income of Rs.33 Crores in the year 2016-2017 which is against the mega project benefit from the state government. Since the income is related to the fixed assets, it has to be reduced from the fixed assets throughout the future life of the assets, which had actually created a deferred tax liability on the company. The entire provisioning of both these events has been accrued in the Q4 of this year and hence the deferred tax liability appeared to be on a very high side particularly for this Q4. This is a one-time event and the future quarters are expected to have normal tax provisioning as per the regular course of the business.

Going forward, I think we shall remain committed on growing our value-added consumer business while maintaining stronghold on our ingredient business. We are placing a strong focus on establishing our products under our key brands in both existing as well as the new markets across the country and overseas as well. We shall also look into the future to strengthen our distribution network, delivery systems and spread our retail presence 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 exports to key geographies. With respect to the B2B business, we shall further leverage our institutional relationships and quality certifications obtained from such institutional customers to further grow our business in India and globally. With this I would like now to leave the floor open for question and answers.

Moderator: Thank you. Ladies and gentlemen, we will now begin the question and answer session. The first question is from the line of Rahul Jha from Bay Capital. Please go ahead.

Rahul Jha: Good morning. Debt levels have gone up significantly in this quarter, what is the reason for that?

Vivek Nirmal: We have short-term debt as on year end is Rs.319 Crores, but on the same hand we have cash in hand balance of around Rs.163 Crores, so the net debt has actually decreased. So net debt with long-term and short-term debt is around Rs.194 Crores at year-end, it has decreased.

Rahul Jha: Also our working capital has increased by around Rs.85 Crores, what is the reason for this?

Vivek Nirmal: This is basically because in the last quarter Rahul particularly, we have increased our stock inventory levels mainly cheese inventory levels have increased, second is our butter inventory levels have gone up. Cow ghee or cow fat is in a great shortage right now in the country because of the higher demand and in order to secure our coming festival season, we have increased our stock levels of butter, cheese and some stock levels of the powders as well. That is the main reason of working capital increasing from the Q3. At the same time, there has also been some increase in the other current assets like our debtors and our advances, which we give to our milk suppliers throughout the year.

Raviraj Vahadane: But Rahul, if you compare the late receivable days, it has come down as compared to earlier it was around 72 days, now it has come down to around 70 days.

Rahul Jha: Okay, thank you.

Moderator: Thank you. The next question is from the line of Manish Jain from SageOne Investment Advisors. Please go ahead.

Manish Jain: I just wanted to understand sales breakup for fiscal 2017 into B2B and B2C and B2C also broken up into milk and value-added products?

Vivek Nirmal: So the B2B business is around 70% of the total sales and 30% is the consumer business. In the overall business if you see around 88% is the value add, which includes our specialty dairy ingredients, cheese and all other stuff and the remaining is liquid milk.

Manish Jain: So 18% of total Rs.1400 Crores is value-added and 12% is milk?

Vivek Nirmal: 88% of the total revenue is value-added and around 12% is milk.

Manish Jain: Okay. Thanks and second is Ravi, on capex for FY2017, what was the capex incurred and what is the plan for FY2018?

Raviraj Vahadane: We have incurred total capex around Rs.50 Crores in FY2017 and for FY2018; we are planning additional capex nearly about Rs.40 Crores.

Manish Jain: Your working capital incrementally over FY2016 has risen by around Rs.90 Crores, on an incremental sales increase of Rs.230 Crores, so Rs.1170 Crores of sales went to Rs.1400 odd Crores and incremental working capital went up by Rs.85 Crores to Rs.90 Crores. So…?

Vivek Nirmal: As explained earlier, our inventory levels particularly last year was very low because the milk availability itself was low and since the prices are on an increasing trend, we have chosen to get higher level of inventories by the end of March, that is the primary reason and if you see overall about the increase in working capital in the business of 230, while business has increased, but inventory levels also has increased substantially, because the milk prices continue to remain higher. We also expect it to remain at the current levels for this quarter and hence we have chosen to have higher inventories.

Manish Jain: Fine. I have some more questions. I will join back the queue.

Moderator: Thank you. The next question is from the line of Saurabh from HDFC Mutual Fund. Please go ahead.

Saurabh Patwa: Thanks for taking my question. Let us know what was the daily average procurement for the quarter and for the year and what trend you are seeing as you said that procurement is becoming difficult because of the high demand, so what is the strategy you would like to follow?

Vivek Nirmal: Our milk procurement has increased last quarter while for average for the year is around 8-lakh litre. The milk procurement in the last quarter is around 9 lakh litre because the milk availability after the good monsoons have started increasing, obviously in the dairy sector, the impact of the monsoon is felt much later after at least 9 to 12 months. We have been seeing that and the handling for the last quarter is around 9 lakh liters.

Saurabh Patwa: This is still lower than what would you have envisaged earlier right?

Vivek Nirmal: Yes, we had actually expected around 10 lakh liters of handling by this quarter; however, the milk increases, but slower than what we have expected. It is catching up now, so that is why it is around 9 lakh litres.

Saurabh Patwa: Is it because of lower production itself or is it because of the competition?

Vivek Nirmal: The production itself is growing at a slower pace plus now the summer. Here the summers are very hot that also has an impact on the milk procurement while competition stays, but we are also rapidly expanding our milk procurement network and last year also we have invested in setting up new bulk milk cooling station, expanded our intensity in the current region as well as also we have started milk procurement in the adjacent districts of Ahmednagar.

Saurabh Patwa: As you mentioned, capex of Rs.50 Crores and Rs.40 Crores next year, can you just give a breakup of?

Vivek Nirmal: Last year obviously, there was some part of the initial cogen plant and everything, which we completed last year. There is also some maintenance capex and the milk procurement capex, primarily it was driven by this two, three things. This year again what we intend to spend is mainly on the maintenance capex, second is extending some of our milk procurement adding up few more bulk milk coolers because we also are parallelly strengthening our direct sourcing and third is we also are adding up few retail packaging lines to our lines which includes cheese packaging lines and all, so that is the overall intent for the expenditure plan this year.

Saurabh Patwa: Okay. Thanks a lot. All the best.

Moderator: Thank you. The next question is from the line of Anurag Purohit from Anived Portfolio Managers. Please go ahead.

Anurag Purohit: I just wanted to understand the rationale between having high current account balances and at the same time high interest expense arising out of short-term borrowing. Is that are we planning some amount of higher working capital or capex-related investment which is why we have high cash balance at the expense of high debt?

Vivek Nirmal: No it is not like that actually it is in the regular course of the business and our recoveries particularly, the debtor recoveries and all by the end of March has been higher obviously because overall the working capital cycle was a bit strained due to demonetisation in the quarter of December. By February, March it all has normalized and hence the cash balances are higher. The capex and all what we have planned for this year is we just explained before sometime is a kind of capex envisage for this year.

Anurag Purohit: So considering that working capital especially on collection front is normalizing, should we expect debt levels to come down in coming quarters?

Vivek Nirmal: We would expect it to remain at current levels or may be slightly going higher but actually if you see the net debt, the net debt we expect to remain. If you see overall on the finance cost…actually finance cost is down by 27% than the last year and we expect it to again remain at the current levels in the coming year as well.

Anurag Purohit: Sure and update on the cheese capacity utilization, how is that progressing and?

Vivek Nirmal: If you see the current run rate, it is around somewhere in the range of 20%, 22% at the current run rate. Obviously it was low at the starting of the last year, it has improved over the last year and by end of this year, we expect it to reach by around 40%.

Anurag Purohit: Thanks a lot.

Moderator: Thank you. The next question is from the line of Punit Arora an Individual Investor. Please go ahead.

Punit Arora: Good morning Sir. The deferred tax liability of Rs.11.5 Crores that you have provided for, is not it only to the search and seizure which was conducted in October 2015 or it also includes the provision for the deferred tax, the provision for the grant?

Vivek Nirmal: What is happened is, there are two kind of things for which deferred tax liability has arrived and if you see the overall number, it includes both the events which is the change in the depreciation calculation as well as the mega project grant, both of them have resulted into this additional one-time deferred tax liability. For all this next quarter, if you see the mega project grant will be adjusted in those quarters, which will be in the regular course of the business.

Punit Arora: How much was the provision for the search and seizure part?

Vivek Nirmal: Sorry.

Punit Arora: For search and seizure how much was the provision for that part?

Vivek Nirmal: The current provision for that is lesser and major of the deferred tax liability would be in addition to the search and seizure including the mega project, but the only thing is that it has come in the last, if you see the mega project liability, it has also occurred in the Q3 as well as Q4. So it includes both the events, search and seizure part as well as the mega project liability.

Punit Arora: Thank you.

Moderator: Thank you. The next question is from the line of Shariq Merchant from Quest Investment. Please go ahead.

Shariq Merchant: Thanks for the opportunity. Can you help me to understand how procurement prices have moved during the quarter both on QoQ as well as YoY basis?

Vivek Nirmal: If you see on the QoQ basis from around Rs.27 it has moved to around rs.28.5 per litre. If you see on a year-on-year from Rs.21, which was the initial last year, it has moved to Rs.27, 28 range, because last year there was a cumulative impact of two years of drought and while the monsoons have been excellent, the impact of that we have started seeing from this quarter. At the same time, in the market the prices of the commodities as well as consumer prices have been up and that is why the impact of that also has been seen in the milk procurement prices.

Shariq Merchant: Would it make a difference as to where you procure from, if you are procuring from Ahmednagar versus other districts, would your procurement price be different or meaningfully different?

Vivek Nirmal: It would be different in terms of transportation cost incurred, but it has not meaningfully different in the sense, the entire state follows a similar kind of pattern in terms of the milk pricing.

Shariq Merchant: If you were in a different states suppose you are procuring in the south versus Maharashtra, then how would you procurement price differ?

Vivek Nirmal: It is definitely different in different states and in parts of North India, there is buffalo milk and states where in there are cooperatives, they have their own pricing pattern. For example in Karnataka, in south states like Tamil Nadu while cooperatives are dominant, they have their own pricing pattern and hence the state-to-state the price varies, so it will not be possible to say that there is a uniform pattern in the price difference, for example it is 10% higher or lower, because that pattern keeps on changing. There has been situations where in Maharashtra milk has been costlier than the southern states and there are also have been situations where Maharashtra milk has been cheaper than the southern states, but yes there is a difference in state-to-state in terms of milk pricing.

Shariq Merchant: As of right now, how would the prices be if Maharashtra is 28.5, how would it be in North India and South India?

Vivek Nirmal: Southern prices would be slightly cheaper and North India obviously the buffalo milk, so you cannot compare it apple to apple, so the buffalo milk prices are obviously costlier than the cow milk.

Shariq Merchant: But you procure it on a fat basis right or milk solid basis, so it should not really matter whether it is cow milk or buffalo milk?

Vivek Nirmal: It would still matter, because the cow milk we procure it per litre, so whenever we talk in terms of pricing, we talk it per litre and buffalo milk if you see per litre again it is higher, so the current prices of buffalo milk will be in the range of Rs.40, Rs.45 a litre in the North India.

Shariq Merchant: When you are buying the milk, you assess it for the milk solids and then you buy it right?

Vivek Nirmal: Yes, we assess in terms of milk solid convert it to the litre and then buy it.

Shariq Merchant: Okay, understood. You also said that cow milk is in short supply, so that gap between cow milk and buffalo milk procurement price would have narrowed substantially?

Vivek Nirmal: Cow fat is in short supply, not cow milk exactly, because overall the consumption of cow ghee in the country has increased and hence the cow fat definitely is in short supplies.

Shariq Merchant: Okay, so what would be inflation for cow fat?

Vivek Nirmal: Cow fat prices have increased significantly over the last two years if we see, the prices have gone up by almost 50%.

Shariq Merchant: Okay. Do you think the ban on cow slaughter has made difference to procurement prices?

Vivek Nirmal: Not yet I would say that is definitely an area where the industries have been discussing and all, but we are not seeing any meaningful difference as of now on this particular aspect.

Shariq Merchant: Going forward, you expect it to make a difference?

Vivek Nirmal: We have not been able to assess it, because there is no corporate dairying. It is all related to the farmers and farmers have the cows and they keep it for a number of lactations, the cows are less yielding, hence we are not able to see any meaningful impact.

Shariq Merchant: What happens generally when cows start lactating, so going forward earlier did a farmer then give it out for cow slaughter or the farmer would still retain the cow?

Vivek Nirmal: There are multiple options farmers retain it, some of them used to give it to cow slaughter, some of them used to give it to gou shalas and all number of gou shalas also have increased, so there are multiple options farmers have.

Shariq Merchant: Okay, alright. That is it from my side. Thank you so much.

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

Resham Jain: I have two questions. One on the inventory side since you have mentioned that we are keeping higher inventory because of shortage of availability which is your expecting over the next let us say one or two quarters and what I understand is that 70% of your business is B2B business, so is it that you are taking a call that you should keep a higher inventory or your customers in turn is asking and will be ready to pay a slightly higher price for the same?

Vivek Nirmal: What we will do is, we normally do not play on speculation, so we do not believe in stocking against some market responses what we anticipate in the future; however, in case we feel that we have confirmed orders, it could be B2B, it could be our increasing branded ghee business which for the next four or five months are the most aggressive selling months because of the festive seasons. So in light of that we take a choice to stock the butter for which we have the confirmed orders in hand for the next couple of months.

Resham Jain: So, does it mean that in terms of let us say any downslide in terms of pricing of this produce then the impact on your inventory will not be there, is it fair to I mean…?

Vivek Nirmal: Yes, since it is a confirmed order at normally confirmed prices where we have a fair amount of surety that is when we stock, because the market elements can play in anyway, so we normally do not believe, we are not a commodity players, so we do not believe in stocking only based on the market sentiments, we do it only based on the confirmed business which we have in our hands.

Moderator: Sorry to interrupt Mr. Jain. May we request that you return to the question queues. There are participants waiting for their turn.

Vivek Nirmal: Okay, no problem.

Moderator: Thank you. The next question is from the line of Rajesh Kothari from Accurate Advisors. Please go ahead.

Rajesh Kothari: Hi. Just two questions from my side. Can you give us the sales mix in terms of how much condensed milk, milk powder, ghee, butter, and cheese is the first question.

Vivek Nirmal: We normally do not give the product wise breakup.

Rajesh Kothari: Second question in terms of how is the industry behavior because the raw material prices kept moving up throughout the last 12 months, so do you think the companies have got the pricing power to pass on this price increase or do you think it needs to be absorbed.

Vivek Nirmal: See there are I would say situations both the situations. Most of all, we have revenue streams mainly coming from the B2B and the branded business. In the B2B and most of the cases, it is a pass on pricing of course for the lag of one to three months. In some cases, it is passed on immediately in the month. In sometimes, it takes at least three months to pass on the prices. So that is where we need not absorb the prices. In the branded business however there are certain products where in we need to absorb the prices and when the market moves up, the prices also move up. So that is the difference in between both the channels.

Rajesh Kothari: So what is the price increase taken by Prabhat on overall basket basis.

Vivek Nirmal: Overall basket basis, we have taken price increases multiple times, so we have taken the first price increase in the month of November. Second price increase we have taken in the month of March. It has not been consistent that these months for these many products, but in the last three to four months, we have seen multiple price increases we have taken in various products including milk, including ghee, including curd, and all.

Rajesh Kothari: Say in terms of percentage on a basket basis if you just index that the RMC cost has gone up by X% compared to the realization on basket basis would have been moved up by how many bps?

Vivek Nirmal: So as I have said earlier, we do not give a product wise breakup, but overall what we have seen is that whatever increase in the milk procurement cost has been there. In the last quarter, we have been able to pass on almost 80% to 90% of the final cost to the market.

Rajesh Kothari: And on full year basis it would be how much.

Moderator: Sorry to interrupt Mr. Kothari.

Rajesh Kothari: This is just continuing on of that question. On full year basis how much it would be?

Vivek Nirmal: We have not calculated on a full year basis Mr. Kothari.

Rajesh Kothari: Okay. Agreed. Thank you Sir.

Moderator: Thank you. The next question is from the line of Pragya Vishwakarma from Edelweiss. Please go ahead.

Pragya Vishwakarma: I just have two questions. One is on your distribution channels, so if you can give a sense on how many retail touch points we are on currently and what is your target for the next two years and the second question is, what is your current capacity utilization in ghee?

Vivek Nirmal: Currently we have around one-lakh retail touch points out of which around 60,000 to 65,000 retail touch points are direct by the company. Around 30,000 to 35,000 retail touch points are indirect because we also have a very strong wholesale network. This is mainly serviced by 1200 distributors and it includes Maharashtra as well as other 25 states. Other states, we have had a presence most probably in the last two years, so we are relatively new to other states, that is number one and I think your second question was mainly on.

Pragya Vishwakarma: I wanted to know what is your capacity utilization in ghee?

Vivek Nirmal: In capacity utilization in terms of ghee, it is around 70% to 75% right now.

Pragya Vishwakarma: So that is for the full year you are saying 70% to 75%.

Vivek Nirmal: Yes.

Pragya Vishwakarma: Okay. Thanks.

Moderator: Thank you. The next question is from the line of Amnish Aggarwal from Prabhudas Lilladher. Please go ahead.

Amnish Aggarwal: Hi Sir just a couple of questions. First being if we look at the balance sheet, which you have given there is a gross debt of Rs.358 Crores, which was around Rs.158 Crores last year and then there is a cash sitting at Rs.165 Crores versus Rs.11.8 Crores last year, so why this anomaly that do we need this much amount of cash in our balance sheet or what is the strategy in having so much of cash in the balance sheet and then having debt on one hand.

Vivek Nirmal: No, it is not debt; it is a normal need of the cash. What we have done is due to demonetization in the December our debtor levels had increased, so we have obviously been very aggressive of collecting all of them particularly by the end of March and that is one particular reason of cash balance being higher. Throughout the year, it is not that normally we need this kind of cash balances on the books, so we might expect this to vary in the coming quarters as well.

Amish Agarwal: But in the normal course of business where do you think I am not looking at the cash side because if you look at our net debt, it is not very different, it is around Rs.200 Crores, but where do you think we will be our normalized level of debt and cash in the coming year or so if you can give us.

Vivek Nirmal: We expect it to remain at similar levels where it is today. We might expect a slight increase in our inventories by going in the next year or some other current expenditure, but more or less we expect it to remain at the same level, the net debt.

Amish Agarwal: Sir my question is on our marketing strategy. I might have missed out. I think you have recruited someone who is an ex-HUL and also some other senior people, so can you throw some light on which are your senior management people are joining and what is the marketing strategy of the company going forward.

Vivek Nirmal: See what we are doing is as the company is moving into branded space and we created have now a fair platform for us. Now the next three years could see aggressive consumer business growth. When you go into this aggressive consumer business growth space, obviously you need to have a strong marketing and sales department. At the same time, you also need to have a very strong supply chain, which is there in FMCG companies, which would include your own sourcing, your entire supply chain network, logistics, and all. So these two senior level recruits are basically one is on the consumer side of the business to spearhead our marketing and sales efforts. We have seen just now we are a completely new brand launched from the basket of Prabhat, which is Volup ice cream. Similarly we will be seeing couple of new brand lunches by this year and next year, which would be mainly in the segment of milk-based beverages, cheese, and all. So the strategy is we are working with the leading marketing agencies and branding agencies. We are also in process of revamping our Prabhat Dairy brand identity as well and the strategy has been to working on the current products to improve the current products packaging and also towards strongly on the brand building side of the product. That is the marketing strategy. At the same time, if you see the second another appointment has been there as a commercial director that is particularly to spear head our B2B business and at the same to build a very robust supply chain to support the branded business growth, which would be in terms of product development, in terms of manufacturing, in terms of logistics, which is very, very critical if you want to grow FMCG business in this aggressive pace. So these are the two key appointments. Mr. Muthar Basha is an industry veteran who joined us from the Levers and a second appointment is of Mr. Sridhar who has been a veteran in the supply chain and the commercial side of the business with organizations like ITC, Mondelez, and all.

Amish Agarwal: Sir thanks a lot.

Moderator: Thank you. The next question is from the line of Manish Jain from SageOne Investment Advisor. Please go ahead.

Manish Jain: Yes actually I was just looking at the total value-added products when you say 30% and I do the calculation of 12% milk and 88% others, has milk volume declined in absolute terms over the last year because last year's figure I had milk of Rs.74 Crores and valued added of Rs.277 Crores.

Vivek Nirmal: I think you are slightly miscalculating. When we say 88% and 12% it is not out of 30%. 88% and 12% is out of the 100% of our revenues including B2B and B2C.

Manish Jain: Yes so Rs.1410 Crores if I look at 30% is Rs.423 Crores and Rs.423 Crores if it take 88%, it comes to Rs.372 Crores.

Vivek Nirmal: That is what I am saying; the breakup of 88% and 12% is not only for the B2C. The breakup of the 88% and 12% is for the entire revenues of the company including B2B and B2C.

Manish Jain: Fine. Thanks.

Moderator: Thank you. The next question is from the line of Pankaj Bobade from Axis Securities. Please go ahead.

Pankaj Bobade: Thanks a lot for taking my question. Sir I have two questions. First is, is the impact of demonetization still lingering and do you attribute the losses made in this quarter to demonetization.

Vivek Nirmal: See demonetization I think, the impact is now completely gone. Second I would like to highlight that there are not losses in this quarter. Our EBITDA has grown. Our EBITDA has grown quarter to quarter. Our EBITDA has grown on year on year. Even there is no cash loss. The only loss what is arriving is of the PAT. There is again no loss in the PBT as well. Only on the PAT, there is a loss and that is particularly due to the deferred tax liability, which has arrived as a one-time event in the Q4, which as I explained earlier is an impact of the change in the depreciation as well as the deferred tax liability arising out of the major project benefit what we have got. So I would just like to emphasize again that there is no loss this year neither in the EBITDA, neither in the PBT.

Pankaj Bobade: Sir the EBITDA margins have declined right.

Vivek Nirmal: The margins have declined from 8.4% to 8%, which is I would say a very slight decline and obviously is attributed to higher milk price and at the same time we are now spending more on the branded side of the business. So I would say that there is a slight impact, which in dairy industry obviously season to season or every quarter to quarter, it is not constant. It changes from quarter to quarter.

Pankaj Bobade: Is this a one-off phenomenon.

Vivek Nirmal: See I have explained the one-off items earlier of the deferred tax liability that is the one-off phenomenon.

Pankaj Bobade: I mean to say the increase in cost of material consumed, one is procurement.

Vivek Nirmal: What you see is unlike any other agri commodity, dairy is also one of them. It has its own cycles as well as its own seasons. So when I say seasons, it is winter or summer where the price fluctuates and when I say cycle it is normally the cycles of drought season or excess rainfall and all. So every two to three years, you see these cycles coming in, so in case of excess rainfall and all you might see the prices doing down. At the same time in the cycles of drought, you might see the prices going up.

Pankaj Bobade: The second question is what is the differential between the prices that you get from retail customer and intuitional customer?

Vivek Nirmal: Actually it depends from product to product because there are a very wide number of products we are into and there is again a lot of difference in between both these. May be to answer your question, I would like to answer it based on the gross margin kind of thing. So gross margin in the customer business would be in the range of 28% to 30% and where as in the gross margins in the B2B business would be in the range of 18% to 20%.

Pankaj Bobade: Almost double.

Vivek Nirmal: Not double exactly. Around 50% would be the difference. 18% to 20% versus around 30%.

Pankaj Bobade: And the cost incurred.

Moderator: Sorry to interrupt Mr. Bobade.

Pankaj Bobade: This is just the continuation and the cost incurred for consumer business. Will that be in similar issue?

Vivek Nirmal: It would be difficult to answer this because in consumer business, we have 80 SKUs right now. So it will be very difficult to answer it on a universal basis.

Pankaj Bobade: Okay. Thank you.

Moderator: Thank you. The next question is from the line of Resham Jain from DSP Blackrock. Please go ahead.

Resham Jain: Sir just one question on GST. What is your overall view and how will Prabhat be impacted on various product lines?

Vivek Nirmal: On basis of GST, we have done our assessment recently because the rates are now out and earlier we were expecting it to be neutral to our company. We are now seeing it, it could be neutral to positive in a lot of cases while there could be some higher blockage of working capital requirement as FMCG Company is going to face, but at the same time, we also have a mega project benefit. So for whatever the tax we pay, we will be getting it refund on taxable product, so our assessment right now that it will be neutral to positive for our side, the GST impact.

Resham Jain: Sir how much working capital requirement incremental will be there?

Vivek Nirmal: We are assessing it Mr. Jain. Right now we do not have any numbers, which we are able to arrive as of now.

Resham Jain: To continue to that on the cheese project, which you have, you have the sales tax reimbursement/

Vivek Nirmal: Yes.

Resham Jain: So on that after GST will there be any impact?

Vivek Nirmal: As I said the impact from GST is neutral to positive. Earlier there was 12% tax on cheese. Now also it is in the similar bracket and hence for cheese as such there would be no change.

Resham Jain: Thank you.

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

Aniruddha Joshi: Hello Sir regarding the one lakh retail touch points that we have, so whether we are selling all the products through all the retail outlets or what will be it for let us say frozen products like ice cream and the fresh products like milk and dahi and then some of the chilled products like may be cheese or butter and then for ghee.

Vivek Nirmal: So I would be able to give you some pointers. I would not be having the entire data right now in front of me. However our fresh dairy products are only in Maharashtra. Hence with all one-lakh outlets obviously we do not sell the entire range of products. For fresh dairy products we are only in Maharashtra where we would be covering around 25,000 outlets, where dairy products include products like milk, dahi, paneer, shrikhand and all. For all other products for long shelf-life products, which are sold through all other outlets, which would include 25,000 plus the rest of the 75,000 outlets because these are mainly which are selling our long shelf-life products like eventually milk and ghee. Now for ice cream and all right now in frozen category, we only have our ice creams recently launched product. Right now we are present in 12,00 outlets already in the last one and a half months of the launch in this particular 8 to 10 cities, where we have launched a product.

Aniruddha Joshi: Okay fine. What is our trade margin for the milk business and for the rest of the business?

Vivek Nirmal: So we again we do not give the breakup of product wise of the sales or of the margins as such.

Aniruddha Joshi: But then what would be our overall trade margins at the company level.

Vivek Nirmal: You are asking about the gross margin at the company levels?

Aniruddha Joshi: No trade margin offered to the distributor, retailer, and that kind of…

Vivek Nirmal: Trade margins obviously are on the branded business. Distributors normally would be having trade margins ranging from 7% to 8% in the range of that and the retailers would be having trade margins in the range of 15% to 20%.

Aniruddha Joshi: Lastly the milk prices have been going up, but what is your outlook for FY2018, so where do you see the margin moving from current level assuming as expected we get a normal monsoon.

Vivek Nirmal: See obviously that this factor is a mix of lot of elements however whatever idea we have of the industry. Last year monsoons have been good. This year they are expected to be average, normal monsoons and however due to summer and festival season, we would expect the prices to remain at the current levels, but with these kind of monsoons and overall good pricing obviously the milk production is on a rise and post this may be the end of Q2, we might see the prices of milk easing.

Aniruddha Joshi: End of Q2 that is September quarter we can see…

Vivek Nirmal: Yes because that is particularly after the festival season it is at its peak. That is the time when we would be seeing the prices easing because by the time the demand for the milk products also is higher. At the same time, due to the summer season and all, the production is also under a slight stress.

Aniruddha Joshi: Sir just last question from my side. We have seen that the profitability is definitely higher in products like dahi, buttermilk, flavoured milk, etc., so we are aggressively entering into segments like cheese and ice cream, so probably the ROC on these segments would be relatively lower, so any particular reason to enter these segments.

Vivek Nirmal: See there are multiple categories now in the market. We have chosen to be in the categories where in there are a few players. For example in cheese there are very few players in the country because it requires I would say high level of technical capability as well as the best quality milk procurement. Since we have both of them, we have entered into cheese as a segment because in the longer term we believe that this segment promises much higher margins through its not only cheese sales, but also the supplementary revenue streams like whey and whey products. Obviously, it is a matter of ramping up. Right now our capacity utilization is lower and hence the ROCEs are also impacted. As we go forward, we expect our capacity utilizations increasing and hence the margins improving from these kinds of streams.

Aniruddha Joshi: And ice cream.

Vivek Nirmal: For ice creams as well I would say. Ice cream is already a high gross margin business. We have been manufacturing ice creams for Mother Dairy since the last three years. We are using the similar infrastructure to manufacture our own ice creams as well.

Aniruddha Joshi: Thank you.

Moderator: Thank you. The next question is from the line of Pragya Vishwakarma from Edelweiss. Please go ahead.

Pragya Vishwakarma: It is a follow up question on your retail touch point. Sir what is the target we have for the next two to three years from this one lakh where do we go from here?

Vivek Nirmal: See there are two things one, is we are now focusing on the weighted distribution while there are one lakh outlets obviously there are limited outlets out of this, who give us higher weighted distribution. So the target this year is on increasing our coverage of the outlets, which give us higher sales. Number two we are also now planning to increase the depth in the current outlets. The outlets, which are stocking our own products they are also now trying to sell more and more lines, which is more and more products in the same outlets to increase the throughput for outlet and obviously since we are geographically expanding, we also target to increase our outlet reach from the current one lakh outlets to two lakh outlets. So obviously we expect a lot of growth coming from doubling the number of outlets as well as the higher depth achieved in sales per outlet.

Pragya Vishwakarma: This two lakhs you say that it is the target when we end financial year 2018.

Vivek Nirmal: It is in next two years.

Pragya Vishwakarma: Next two years and my next question was what is our capacity utilization in pouch milk?

Vivek Nirmal: In pouch milk, the capacity utilization is around 30%.

Pragya Vishwakarma: In FY2017 because I think in FY2016 we were at 45% if I am not wrong.

Vivek Nirmal: See what happens is right now the pouch milk sales are constant and it has been in the same range. It has been in the range of 30% to 40% only. It has not been around 45%, but we also use a lot of capacity for packing milk for clients as well wherein we pack milk for a couple of other brands including Nandini and all. That is how the rest of the capacity is utilized for co-packing.

Pragya Vishwakarma: My last question is on cheese. So what I understand that we are currently doing only through HORECA and we classify HORECA under B2B not under B2C right.

Vivek Nirmal: See what every dairy company does is the entire HORECA is all serviced through the B2C because these are the same distributors who service the retail outlets as well as the small hotels and the restaurants because you cannot have a separate channel for distributing those. For the entire industry, normally this food service channel is through the consumer distributors only and we also do the same thing.

Pragya Vishwakarma: Thanks for clarifying. That is it.

Moderator: Thank you. The next question is from the line of Balwinder Singh from Canara HSBC Insurance. Please go ahead.

Balwinder Singh: Hi Sir thanks for the opportunity. Firstly wanted to understand that on a year on year basis, we have seen almost 30% to 32% increase in our raw milk procurement cost, so you highlighted that we had taken two price increases one in November and one in March, so does that cover on an overall 30% increase or we are still left with some part of the RM cost increase that will pass in subsequent month so just clarify...

Vivek Nirmal: I believe we have a sufficient price increase to cover our input cost price.

Balwinder Singh: So no further cost increase or no margin compression should be seen going forward.

Vivek Nirmal: Correct.

Balwinder Singh: Thanks. I am done.

Moderator: Thank you. The next question is from the line of Alok Agarwal from Striver Capital. Please go ahead.

Alok Agarwal: Hell Sir. This is Alok here. My question pertains to skimmed milk powder. Is there opportunity to import and add to the milk supply locally?

Vivek Nirmal: There is an opportunity to import however the Government of India normally discourages milk powder imports and there is a very high import duty on that, so while the milk powder prices globally are on a lower side, but still there is no import happening in the country. This is basically because the entire milk industry is managed by small and marginal farmers. So in order to protect the interests normally government has very higher import duty on the milk powders.

Alok Agarwal: I agree it is about 40%, but still the blended prices could be cheaper and you can at least add a percentage of your milk sale let us say 10% of the SMP imported can be added to your milk volumes as such, is it possible?

Vivek Nirmal: What happens apart from the import duties, there is also a permit, which the government issues, so the government normally discourages it through the permit.

Alok Agarwal: Got it and the second question is the milk prices what is the cost to you, you have been able to pass on in the last whatever the hike was of the last year. In the current financial year, do you see the raw material prices still inching up, the milk prices of procurement or they have by-and-large peaked?

Vivek Nirmal: As we see they have by-and-large peaked. We would just still expect them to remain at current levels or may be slightly going down from the current levels, but we see them easing only after four to five months.

Alok Agarwal: Sure after the fresh season starts.

Vivek Nirmal: Yes.

Alok Agarwal: Okay great. That is it from my side. Thank you.

Moderator: Thank you. The next question is from the line of Pankaj Bobade from Axis Securities. Please go ahead.

Pankaj Bobade: Sir we have our presence in 26 states across 1200 plus distributors right Sir?

Vivek Nirmal: Yes.

Pankaj Bobade: So how is our milk procurement and processing plant distribute to these states?

Vivek Nirmal: So we have only two factories right now one is mainly Shrirampur, which is near Shirdi. Second factory is in Navi Mumbai. So both the factories service to all the states. We do not have any other factories in these states. So for fresh products, we are only in Maharashtra because for fresh products your factories need to be near the markets. However for long shelf-life products, you need not have the factories near the market. So we distribute our long shelf-life products in other states through these two factories.

Pankaj Bobade: Sir do we have any such plans, so that we can service these all states for this fresh products?

Vivek Nirmal: We have plans, but we do not have them immediately on the cards at least for the next two to three years. The target for the next two to three years is to enhance our own capacity utilization, which is currently at a range of 60%. We intend to take it to around 85% to 90% in the next two to three years, post that we might think of increasing or expanding in the other areas as well.

Pankaj Bobade: And products too?

Vivek Nirmal: Sorry.

Pankaj Bobade: Do you intend to expand new products too other than whatever we are producing now.

Vivek Nirmal: We are already expecting launch of couple of new products by this year and next year.

Pankaj Bobade: Can you name these?

Vivek Nirmal: We are working on them right now. I will not be able to share more details on that, but we are mainly coming into milk beverages category and cheese category.

Pankaj Bobade: Thank you.

Moderator: Thank you. The next question is from the line of Pragya Vishwakarma from Edelweiss. Please go ahead.

Pragya Vishwakarma: I wanted to understand the competitive space in cow ghee and what is our strength vis-à-vis other players in the market. If you can comment on that please?

Vivek Nirmal: So cow ghee now, since the last four to five years, we have expanded in around 25 to 26 states. We are a key player in cow ghee segment. We have our SKUs available right from PET jars to pouches and sachets and cartons. In a lot of states wherever we are present, we are amongst the top three to top four players in those states particularly. Cow ghee as a market obviously is expanding pretty fast and since we have high quality milk, our cow ghee is very well accepted and it is gaining further acceptance in amongst consumers and our maximum distribution increased, which has came in the last two years is particularly through cow ghee.

Pragya Vishwakarma: How are we priced when compared to other players in the industry?

Vivek Nirmal: We are priced at par with the all the key players in the industry. We are not costlier than them. We are not cheaper than them. We are at par with the competitors in terms of the MRPs.

Pragya Vishwakarma: Is it possible for you to give us some sense on what kind of revenue it can generate at may be 80% to 85% utilization.

Vivek Nirmal: So cow ghee obviously we are planning to increase it further. For the next two to three years, cow ghee could see increased sales. If required, we might also need to spend slightly. It would not be a higher amount, but to increase our ghee capacity as well, but we are seeing significant growth in the cow ghee. Now it is not a matter of cow ghee manufacturing capacity really to say. So that we can predict the revenues, but it is more also about how much milk do we handle and how much fat do we generate. That will really determine on our capacity to manufacture ghee. So it will be very difficult to predict it at this point of time Pragya.

Pragya Vishwakarma: Is it possible for you to let us know the capacity, which we have for ghee?

Vivek Nirmal: The capacity for ghee is right now around, so we normally calculate it in terms of fat, so ghee and butter put together, we have a capacity of around 50 tonnes per day.

Pragya Vishwakarma: Okay Thank you so much.

Vivek Nirmal: Thank you.

Moderator: Thank you. The next question is from the line of Shariq Merchant from Quest Investment. Please go ahead.

Shariq Merchant: Hi Sir thank you for the followup. My question is on SMP. Sir after the 5% GST imposed, will that change the dynamics of the industry because even after import duty, will it make it more viable to import SMP in India.

Vivek Nirmal: Earlier also there was a VAT on SMP, which was 5.5% and even now there is GST, so the GST rate has remained unchanged.

Shariq Merchant: So nothing changes.

Vivek Nirmal: Yes.

Shariq Merchant: Okay. Alright. That is it. Thank you.

Moderator: Thank you. The next question is from the line of Punit Arora, an Individual Investor. Please go ahead.

Punit Arora: Sir you have target to achieve 50:50 ratio for B2B versus B2C sales in FY2020. Currently it is at 70:30 for FY2017, and assuming B2B sales remain stable, which is currently at around Rs.980 Crores then B2C sales must increase by at least 32% CAGR till 2020. So I wanted to have your views on that.

Vivek Nirmal: Yes you are right. As I explained before sometime, we are targeting doubling our retail presence. We are also targeting higher depths in the current outlets. We are obviously also targeting launch of new products, which we have started seeing by the launch of categories like ice cream and all, so particularly we will be focusing on our current products. We have already expanded in the geographies like 25 states. However our presence is still not very intense in these states because these are newly launched states. So we would continue to grow our presence in these states by adding up more retail outlets and more number of products. At the same time, our modern trade presence is also very limited. It is only in Maharashtra. So we would also increase our modern trade presence from current 140 outlets to around 1000 outlets plus by the end of this year. So this is overall strategy to increase our geography, to increase our horizontal presence in number of outlets as well as since we have a basket of products to also increase the depth per outlet for achieving our growth target of 30-32% CAGR in the next three years.

Punit Arora: The sales that it will come from cheese plant, most of the cheese will go to the B2B or the B2C segment.

Vivek Nirmal: It is a mix actually because it is a 50:50 I would say because while corporate clients like the large QSR chains and pizza chains are also increasing as a share or our supplies are increasing, but we are also seeing a lot of business coming from the food service sector as well, which also we are seeing an aggressive growth, so I would say both the segments would continue to grow.

Punit Arora: Sir the current cheese utilization you said is around 20% to 22% in FY2017. How much revenue does it contribute combining both B2B and B2C only for the cheese.

Vivek Nirmal: We do not give product wise breakup.

Punit Arora: Thank you so much Sir.

Moderator: Thank you. The next question is from the line of Nitish Sand, an individual investor. Nitish your line unmuted. Please go ahead. The line for the current participant seems to have dropped off. We will move onto the next question that is from the line of Nandita Mehta from JM Financial. Please go ahead.

Nandita Mehta: Hi Sir just wanted to know what is your modern trade presence right now? I missed that number

Vivek Nirmal: It is 140 outlets right now and it is mainly in Mumbai and Pune. Some outlets in Nasik as well, but that is only limited to Maharashtra as of now.

Nandita Mehta: And we are moving up to 1000 plus by…

Vivek Nirmal: By the end of March we are moving to 1000 plus because we already have a distribution now in other states as well, but the distribution is already in general trade. So modern trade is also we are starting by this year in all the states.

Nandita Mehta: Sir a little on Volup. Can you tell us how is that panning out. What kind of customer feedback have we got on that?

Vivek Nirmal: Ice cream market if you see is growing at 25% to 30% plus CAGR and what we have identified is in Maharashtra there are very limited players. There are a lot of players coming from Gujarat and all though. There is a lot of space available not only in tier 1 towns, but in tier 2 and tier 3 towns as well. So we have developed a completely new brand while Prabhat as a brand stands more for trust in purity of milk. We wanted to come up with a brand, which talks about excitement, fun, and indulgence, so that is how Volup has emerged and there are basically two brands Sinsane is a premium category, which has SKUs ranging from Rs.40 to Rs.75 and Volup is a popular category which has SKUs ranging from Rs.5 to Rs.40. For all these, we have identified 10 districts in which we have made a soft launch by the end of March 17, 2017 and by March 18, 2017 we expect this to be distributed across the state. Right now, we are already present in 1200 outlets in 45 days of our launch. The product response have been extremely good because the quality, the USP is mainly only fresh milk and cream. It is not a frozen dessert. It is just a pure milk ice cream and with great branding efforts and marketing efforts, we are seeing a very bright future for this product particularly in Maharashtra initially, but in the next two to three years, we would be expanding out of the state as well.

Nandita Mehta: So really just looking at the neighboring states or be even looking a Pan India presence?

Vivek Nirmal: Initially Maharashtra honestly. For the next two years, it is only Maharashtra. After Maharashtra, we would be looking at neighbouring states because Maharashtra there is a lot of vacuum till today, so we expect a lot of potential in Maharashtra in the next two years.

Nandita Mehta: Thank you.

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

Shraddha: Hello Vivek. This is Shraddha here. Just one question, I wanted to understand as you were saying the procurement improving and also as you said over the next four to five months, we expect even the procurement prices to improve, procurement cost to cool down.

Moderator: Sorry to interrupt Shraddha, can you speak a bit louder, we are not able to hear you.

Shraddha: Hello.

Vivek Nirmal: Yes, Shraddha you can please go ahead. I have heard till now. You can continue.

Shraddha: And also as we are targeting the cheese capacity utilization at higher levels, I wanted to understand if it will be possible to give an outlook on the margins or what is our objective in terms of margins over the next two years.

Vivek Nirmal: So Shraddha as a policy we will not be able to give any guidance as such however yes obviously the increase in capacity utilization and if the milk prices ease, I am sure it will be positive for the company on net-net basis. At the same time, in the next two to three years our overall effort is to improve the gross margin on overall basis and that is why the effort to increase products like cheese and ice cream at the same time an effort to increase the business from the branded side of it.

Nihal Jham: So just working backwards as you said we want to target the B2C at around 50% and also improving the value-added products, will it be possible to give a direction on the gross margin at least roughly what is the kind of trajectory we would be looking at over the next two to three years.

Vivek Nirmal: It will not be possible to comment on the gross margins really Shraddha because we will not be able to comment particularly, but as a strategy and I explained that obviously it is there to improve it from the current levels while we will be continuing to spend on brand building activities, but with the increasing share of business from the consumer side, our overall gross margin is expected to expand from the current levels because the mix from the B2B to B2C would also continue to change.

Shraddha: Sure thank you.

Vivek Nirmal: Thank you Shraddha.

Moderator: Thank you. The next question is from Rahul Jain from Credence Wealth. Please go ahead.

Rahul Jain: Good afternoon Sir. I just heard about ice cream business in terms you mentioned you are talking about growth of 20% to 25%, are we talking about volume growth or how have you seen the ice cream business in the last two to three years because my knowledge says the volume growth has not been that high.

Vivek Nirmal: So if you see the national statistics, the volume growth in this particular industry has been around 25% and that includes all the key players, which are operating at a larger scale as well as the smaller players now present in maybe smaller towns or district levels and all. All put together this category as such is growing at a rate of around 25% plus.

Rahul Jain: Sir what kind of capex and marketing spend you are estimating for the ice cream business.

Vivek Nirmal: Capex is not higher. We are expecting because we already have ice cream manufacturing facilities. We have already been manufacturing for Mother Dairy since last two years. On the marketing spend and all, we are working out. It is a soft launch now. Based on the inputs, we will be planning for the next spend.

Rahul Jain: Sure thanks.

Moderator: Thank you. Ladies and gentleman that is the last question. I now hand the conference over to Mr. Dhaval Mehta for his closing comments.

Dhaval Mehta: Thanks Lizanne. Once again, we would like to thank the management for giving us the opportunity to host this call. Thank you everyone for attending the call. Sir would you like to make any closing comments.

Vivek Nirmal: No it is fine. I would just like to thank everyone for attending the call.

Dhaval Mehta: Thanks everyone.

Vivek Nirmal: Thank you very much.

Moderator: Thank you. Ladies and gentlemen, on behalf of Emkay Global Financial Services that concludes this conference. Thank you for joining us and you may now disconnect your lines.