“United Spirits Limited Q2 FY ‘18 Results Earnings Conference Call”

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Moderator: Ladies and Gentlemen, Good Day and Welcome to United Spirits Limited Q2 FY '18 Results Earnings Conference Call. Today, we have with us on the call, Mr. Anand Kripalu, Chief Executive Officer, and Mr. Sanjeev Churiwala, Chief Financial Officer from United Spirits Limited. As a reminder, all participant lines will be in the listen-only mode and there will be an opportunity for you to ask questions after the presentation concludes. In case you need assistance during the conference call, please signal an operator by pressing '*' and then '0' on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Anand Kripalu, Chief Executive Officer. Thank you and over to you, Sir.

Anand Kripalu: Thank you very much and very Good Afternoon everyone and a very warm welcome to this results' call. As per our normal practice, what I will do is I will give you an overview of our results and then of course we will open the line for Q&A. As you have seen in the published results, our performance has substantially improved in the second quarter and we have delivered strong underlying net sales growth of 4%, which has been enabled by a double digit in fact 12% underlying growth in our Prestige and above portfolio. I must say when you look at what we were dealing with as an industry and as a business which is really the entire onset of GST and both the migration challenge as well as the mitigation challenge in GST and really the quarter was shadowed by the highway ban during that period. I must say I am very pleased with the results that we have just declared. Now, specifically looking a little deeper into our revenue performance, the growth of Prestige and above was fueled by our renovation and premiumization something that we have been doing now for the last couple of years and that continues to deliver value and bear fruit. This quarter, we have seen double digit growth for our key Prestige brand McDowell No. 1 whiskey, Royal Challenge whiskey, and Signature.

Our renovation journey as well as our innovation journey continues and the last brand in our Prestige portfolio which is Antiquity has just gone into renovation. We just started rolling out this new mix and the mix is now available in a part of the country since it does take time to roll out a new mix in our industry, but we are pleased with the market response that we have seen thus far with Antiquity. An important announcement was the recent Supreme Court clarification on the highway ban, and post that particularly in the month of September, we have seen outlets starting to reopen and these have been largely on-trade channels really bars and restaurants and hotels which really benefits our premium and Prestige as well as luxury brand. We expect the highway ban impact to kind of start receding over the next few months, though I must say that some stores are still closed, and some stores may remain permanently closed till they are relocated to a distance beyond 500 meters from a highway.

With our continuous strong performance in Prestige and above as well as our operating model changes, the Prestige and above portfolio now represents two-third of our net sales. Moving onto gross margin, again we are pleased with that in this kind of a quarter; we have delivered significant margin expansion. Our underlying margin are up 395 BPS in the second quarter and by 258 BPS in the first half, and these are underlying excluding one-off and operating model changes. Again, I must say that these numbers are pleasing for us and I know this will be of interest to you particularly because we have always had conversations about margin expansion in this business. Now, importantly this improvement in margin has been fueled by our accelerated productivity initiatives both on the top side as well as on trying to mitigate GST as best as we can as well as price increases that we have received and I must say that price increases while still not in line with inflation have become a bit more consistent and a bit more spread across states than they were in past year, and of course, the premiumization of our portfolio has also continued to fuel gross margin improvement.

As consumption trends have started to improve in the second quarter, we have increased our investments behinds brand, and therefore, you will see that marketing investments improved by 11% in the second quarter and by 3% in the first half, so we really continue to invest behind our brands once the market starts stabilizing. Staff costs were lower by 16% including one-off restructuring costs of 13 crores in the current year and 28 crores in the previous year, and this has been driven by the significant organizational changes that I had shared with you on previous calls, so increased gross margin coupled with organizational efficiencies has led to underlying EBITDA margin improvement of 135 BPS and stood at 13.3% in the first half. Significantly, the EBITDA margin in Q2 was over 16%, so we have continued to focus on reducing debt and interest cost, again something that we have spoken about and our interest costs are down by 29%, so this covered with lower exceptional items have resulted in overall PAT increase of 71% in the first half. As we look forward, we expect the impact of the highway ban to continue to decrease by the end of this calendar year, I think we will be where we can be and therefore the business will start beginning to normalize.

As far as GST is concerned, it is something that was of a huge concern to our business not just this quarter, but over the last two years that we have been working on engaging with the government to reduce or minimize the impact of GST, but through our continued focus and expanded focus of productivity on GST as well, we believe that the overall impact of GST which we had called out as being material in the past, we believe it to be now moderate in this Financial Year. One thing I must tell you is that while this quarter we have seen significant progress, we do run this business not on a quarter-to-quarter basis, but on a full-year basis and I just request you to keep that in mind when you look at the overall context of our results. Net-net we have managed to navigate through the short-term challenges better than we expected and I am really pleased with my team for what we have been able to do as far as this is concerned and our overall results demonstrate, we are continuing to execute our strategy effectively based on the strong fundamentals that we have built in this business over the last three years, so we remain confident about the longer-term consumer opportunity, I do not think that was ever in doubt and really the demand for alcobev and spirit.

We continue to focus on our strategic priorities to capture this opportunity in what we believe is a very, very attractive market in the longer-term and we continue to do that so as to be able to achieve our medium term ambition to grow top line by double digit and improve our margin to mid-to high teens and the fact that this quarter we have delivered 16% EBITDA while it is only one quarter, I must say it gives us confidence that it is indeed possible to get to our medium term margin objective, so with that I am going to open the call up for questions. The responses will be shared by me and my colleague here, Sanjeev Churiwala, CFO, and between the two of us we will do our best to respond to your queries.

Moderator: Thank you very much. Ladies and Gentlemen, we will now begin the question and answer session. The first question is from the line of Vivek Maheshwari from CLSA. Please go ahead.

Vivek Maheshwari: Sir, my first question is on the margins and the overall performance in the last few years had been quite challenging for the industry as well as for you, do you think that now worst is behind and things are going to get better from here on because highway ban is behind, GST is behind, you have started to get price hikes etc., how do you think about and why in the medium-term guidance of mid-to high teens given that you have already done 16% in this quarter?

Anand Kripalu: What I would like to say is, one thing about this industry is never say never, so what we do know in terms of the events that have happened in the past, I do think the worst is behind us as far as those specific events are concerned, but this is a challenging regulatory environment for this industry and you never know what is the next dark cloud that is going to come. All I can say and what you should decode really from what happened is that I think the agility of the company and of the management to deal with these dark clouds, I think you should take away that we have built a little bit of muscle on being able to deal with dark clouds, so that gives confidence that new dark clouds will of course throw new challenges, but I think we have the resilience as a management team to deal with it. As far as the medium-term guidance is concerned, we have always said that our strategy is to improve margins consistently year-on-year, but not have really a dramatic spike in getting to the end game, so it is about continuous improvement and that is really how I want you to see our Quarter-2 results. The only point I made is that when you have done something once, you can take away that we know how to get there, but it is not as easy as delivering it consistently every quarter as we have done in one quarter, so that is what I really like to say.

Sanjeev Churiwala: Vivek, I think this was some of the discussions we had in the previous quarters. I think in the previous quarter there was concerns around what is happening on the GST, what is happening on the highway ban and I think the worst is over, we would continue to reinforce with lot of agility now, lot of confidence that our guidance towards our mid-teen to high-teen margin expansions will remain intact for us and that is what our delivery plan is.

Vivek Maheshwari: Just a follow on this, I appreciate what you mentioned about margins, but given that whatever was to happen has happened, so what is incremental uncertainty or let us say this 16% margin that you have done in this quarter at least that we can take for rest of the year and an expansion from that level the next year, is that a fair way of thinking about margins?

Anand Kripalu: We have said we will consistently improve margins. Our underlying margin, even if I remove one-off operating model changes and so on has improved materially, and therefore, we do believe that they are going to show consistent improvement in underlying margin. Like I told you, you said that, yes, what we do know the worst is behind us and I agree with you, but there is news of route to market changes happening in certain states, we still do not know the full impact of those happening, some of those states have advertised in the newspaper already that they are going to be doing it, so Vivek all I am saying is that I just want you to read fairly into the results, I also do not want to be setting up expectations that are inappropriate and over the top, but yes, I think we are sitting in a much better place today than we thought we would be six months ago that absolutely I can tell you and that is how we feel about it.

Sanjeev Churiwala: Vivek, I think is also the important part to really mention that the way you look at the EBITDA margin expansion, look at the reported EBITDA margin expansion vis-a-vis the underlying margin expansion. If you look at the press release, we have very clearly called it out and maybe I will just try and articulate that very clearly, our reported EBITDA margin for '17, for Quarter-2 was 10% against that FY '18 margin is 16.3, as such the reported margin expansion is 631 BPS point, but within that I think you will have to change and make changes for the franchisee adjustments which for the quarter is about 75 BPS point. Last year, we had certain one-offs sitting in the EBITDA which we had reported, which is about 148 BPS points, so per se the underlying EBITDA expansion is about 408 BPS point. Now in this press release, we have also very specifically called out one-off benefits in terms of structural changes in the commercial terms with some of our customers, which are about 225 BPS points, all this put together the underlying EBITDA margin expansion is about 188 to 185 BPS point and that is the way you should look at it. Now, of course this is for the quarter and as Anand said I do not think we should just extrapolate this and try and figure out the next year expansion earnings. This will move quarter on quarter, but the good part is we have the confidence, we have built up muscles around productivity, we have moved on our premiumization journey, we are getting the price increases, and so there is lot of confidence in terms of delivering our margin expansion plans.

Vivek Maheshwari: This one off is 50 crores, right?

Sanjeev Churiwala: Absolutely.

Moderator: Thank you. We have the next question from the line of Avi Mehta from India Infoline. Please go ahead.

Avi Mehta: Just wanted to these three questions generally, one, if you could explain what are these productivity initiatives, if you could give some examples of them? Second, the fact is that GST impact, could you share any guidance of what is the likely impact now that you have a better understanding, and lastly, if you could give any update on the Maharashtra LBT and Octroi removal and how that has been going?

Anand Kripalu: Productivity in our business is something we have been doing over the last three years and I would like to believe that we have now a method of how to do this and have built a muscle as far as driving productivity is concerned. We attack all aspects of productivity in this business, so every line item of our P&L has a plan against, so it is a comprehensive set of productivity initiative that goes above NSV even and then how we can optimize our trade spend, but all the way down including tax, so productivity is comprehensive and is consistent, so it is not a one-off, there is a one-year, two-year rhythm of how to deal with productivity. Now, as far as Maharashtra is concerned, the fact is that is something that goes up and down in different places and nothing is permanent in this game, so as we have had something here, there is something else going up somewhere else, so the way we deal with tax change is we try and either pass it on in terms of price or balance it off across the country because there are pluses and minuses that have happened in different places at the same time. There are many moving pieces, you win some, and you lose some, that is the nature of these as far as that is concerned. As far as the guidance and GST is concerned, I am going to request Sanjeev to share a bit.

Sanjeev Churiwala: Thank you. I think before we move into the GST impact and this is I think the first quarter, where we are talking in detail about the GST, GST went live from first of July. Company as a whole we were really working towards first migrating to a GST regime and not lose a single hour of operations because of the GST, the day was completely enabled with processes systems and fully compliant with GST launch today. Now, talking about the GST impact somewhere before the beginning of the GST era, we clearly said that we were concerned about the overall impact of the GST, we said that this is resulting into stranded taxation and we had called out in the previous quarter that the impact could be material, I am very happy to report now that with our accelerated productivity initiatives, price increases in selective states, and our continued focus on premiumization, we have now already seen EBITDA as well as gross profit margin enhancement. To that extent all put together, we expect the net adverse impact of the GST to be moderate in this financial year. We are not calling out specifically the numbers yet because GST is still very new, numbers could be moving from various state governments and we are still iterating it, but we are quite confident that we are managing the GST, both migration and the mitigations quite well and as of now our guidance is that impact of GST would only be moderate.

Avi Mehta: Okay Sir, so essentially just on the productivity bit the way I should understand it we are checking each other line items trying to reduce whether it is operations etc. and whatever you gained will continue as we move forward, on a quarterly basis is something that I should kind of use to understand how it is kind of flowing through, would that be a fair understanding?

Anand Kripalu: Over the last, let us say half, our productivity has been higher than inflation to the business, margin accretive as far as we are concerned. Now, the plan is that we will continue productivity, but we will always mitigate all of inflation, well it depends on the commodity cycle you are facing. We have been in a relatively benign commodity environment or to put it more clearly, the commodity inflation has been less than what we anticipated this year so far and may stay that way.

Moderator: Thank you. We have the next question from the line of Kinjal Desai from Reliance Mutual Fund. Please go ahead.

Kinjal Desai: Sir, I just wanted to understand on the price hikes front, one, on the P&A part where we have a 12% net sales growth and in the press release it effectively comes out that 2% volume, so a 10% pricing seems a little on the higher side and also in line with that we called out saying that the price hikes have become a consistent and spread across states, so just more color on that front also?

Sanjeev Churiwala: The way we should look at the press release and I think we have given some breakup over there. When you look at the overall the bar that we talked about price and mix, it is a combination of price and mix, to be very, very specific for that H1 we have received about 86 crores of price increase which for the purpose of gross profit mix has an impact of 120 BPS point. We have improved our premiumization mix, the P&A mix is again called out in the press release, which gives about 20 BPS improvements. If you really look at purely the volume increases, we had called out the impact in terms of P&A and Popular separately in the press release and the underlying increase of 3.5% for the Quarter-2.

Anand Kripalu: Just to add a little bit to this, I have been trying to get all of you to think less volume and more NSV and value because a 1% volume increase in the upper part of Prestige and above is dramatically different from a 1% volume increase in the lower part of Prestige and above. There is a big multiple that happens there, and at the end of the day, what we are doing is we are trying to get share of wallet from consumers, and that is why we are not that we are not volume focused, but we are primarily value focused in this business so that we think that is more important to sell one case of a Super Premium brand than one case of Prestige or a Popular brand. Now, as far as overall pricing is concerned, so I said earlier in my opening comment that the overall pricing environment where for the first two years when I joined this business, we had a drought in pricing and almost no pricing anywhere. Then later we started getting one or two states here and there. As we speak today, we are getting many more states. Have we solved the problem of pricing, no, we have not, there are still some trouble states who have not given pricing for extended periods of time and we are obviously using every compliant lever in the book that we can to impress upon the states that they must give pricing. I think the worst is over on pricing drought, but we still have a journey to do and making sure that pricing is in line with let us say consumer price inflation, which is what it needs to be for an industry, it needs to be in line with CPI and we are not quite there yet.

Moderator: Thank you. We have the next question from the line of Manoj Menon from Deutsche Bank. Please go ahead.

Manoj Menon: Thank you for clarifying the one-offs and the other adjustments needs to be done to come to this underlying margin expansion of 188 BPS, so the question is quite straightforward, you know now that I look at this 188, are there any material tax benefit sitting there, when I say tax benefit, what I mean is whether it is LBT of Maharashtra or any entry taxes in any other states etc. going away; now accounting wise it may not be one off, so you are absolutely correct in not calling as one off, so just for an understanding is there a material benefit because otherwise the sudden jump sequentially appears to be slightly different from the normal trend?

Anand Kripalu: The 180 that we talk about is pure underlying based on the premiumization and productivity and everything else, clean from one-offs, so it is pure underlying.

Manoj Menon: Okay, just to understand basically let us say if 100% index of this entry tax, Octroi and other local levies which was there, which is now not there under GST, any such benefits are not sitting in this 188?

Anand Kripalu: They are not sitting in the 188.

Manoj Menon: Where is this available then, I mean is it there in that structural changes you spoke about, is it their material enough to begin with?

Anand Kripalu: Just say that again Manoj?

Manoj Menon: Are those benefits material enough to call out or is it just miniscule?

Anand Kripalu: They are material, but we have called out one-off benefits in our press statement and we have provided a bridge and if you look at the commentary beneath that bridge, we have called out the fact that there is a benefit of 1% on net sales in the half and that is flows down to the bottom line.

Manoj Menon: Clear, so that is actually my second question, that the structural changes in commercial trade terms which you have called out in the release is essentially including these tax benefits also?

Anand Kripalu: It is not tax benefit, if any tax benefit is included in that, but it is like Sanjeev said earlier, it is about more favorable commercial terms with key customers and that is what it is about.

Manoj Menon: The reason I asked is because there is also one line which you have added in that release which says these are not expected to repeat and it is a one-time benefit, if it is indeed including some tax benefits etc., it cannot be one-off right, unless of course, we cannot assume that it will change in the future?

Anand Kripalu: Let me just say that this is a dynamic environment. Now, the fact is that whether there is tax in that or not is not the debate. Specifically on tax, taxes go up and down. Last year, you are aware that tax was imposed retrospectively, so things go up and down, so what we have done is we have stripped that off. Now also at the end of the day this business is going to spend more on driving business in certain states where we have seen a bit of volume softness, money is also going to be spent to ensure that the revenue engine keeps growing. I think what we have done is we have provided as much clarity as is possible to tell you strip of everything, the genuine underlying business has improved margin by 180 odd BPS, that is something that has come through all management intervention on premiumization, productivity, cost mitigation, inflation etc., and that is what it should be called.

Moderator: Thank you. We have the next question from the line of Arnab Mitra from Credit Suisse. Please go ahead.

Arnab Mitra: My main question is on pricing, so you mentioned that you are now getting a bit more broad-based pricing, one is if you could help us give us some examples of which states have given you price hikes and has actually a price hike come in Andhra Pradesh after the quarter closed? Secondly, is the price hike mechanism still pretty ad hoc that it is kind of goes through a bureaucrat or is that slightly more, are you getting a sense that this could be a more regular feature now going ahead in at least some of the states?

Anand Kripalu: As far as pricing is concerned, yes, Andhra did come in, I am not sure of the impact of the quarter probably not or if anything very marginally, but some price increase has come into Andhra. There are couple of other states that have agreed, Corporation markets that have agreed, so like I said the pricing, Sanjeev has already given you the number of the value of the price increases that we have received as some 80 plus crores. What I want to say is that there is still no natural rhythm to pricing with Corporation, pricing is still given, cannot be taken and there is no guarantee that pricing will come on a rhythmic basis, which means every price increase requires significant management effort, intervention, making cases and justification to get the price increase happening, now that is the Holy Grail. If we make that happen then I am saying, we will be out of the woods as far as this industry is concerned, but that is the Holy Grail for this industry.

All I would ask you to decode is that our persistent management efforts of changing the nature of the conversation with state governments on a more fact-based, White Paper based conversation to convince them rationally about the fact that it is only fair that they give us price increases, that journey is well on its way, have not reached the destination, but it is well on its way and as you have seen now it is better than it was a year or two ago and that is the only thing you should take confidence from that, I think we know how to deal with it, but pricing is a complex issue in this nation and it is highly politicized and you know that. It is not just that simple as the bureaucrat sitting, doing the presentation and saying, “Okay, we will do a price increase.” Finally, the Chief Minister signs the price increase in this industry and when the Chief Minister is signing there are all kinds of compulsion in his mind, when is the next election, what are the other issues involved and so on, and you guys know that. I am speaking to people who know this industry well, so that is all I can really say, but please take away that we feel better about the pricing environment than we had felt before.

Arnab Mitra: Just one clarification, Sanjeev, these 86 crores is at the net sales level, what your price realization increases?

Sanjeev Churiwala: This is the net price increase that we have received through the first half.

Arnab Mitra: One just last question, working capital reduction has been one of the major drivers of free cash flow in the first half and also your CAPEX has been extremely low, so do you see this as a sustainable situation for the rest of the year, and therefore, will we generate good amount of FCF this year under USL?

Sanjeev Churiwala: We have been generating good FCF for the last couple of years, we have seen consistent reduction in the debt and the way we look at the first half is that you have seen already a reduction in debt about roughly 450 crores, which is basically two components, half of that is coming from working capital reduction and the remaining is coming from the operating profit margins. Our guidance is, yes, we will continue to reduce our debt and we are in any case working towards working capital reduction every year now, so that is the consistency. On the CAPEX, the guidance that we have already said that throughout the year we are looking at roughly about 150 to 200 crores of CAPEX. We have started with slow built-in about 40 odd crores of CAPEX in the first half, that basically lapping a very high CAPEX spend that we have in the corresponding period; throughout the year, we are going to take a guidance 150 to 200 odd crores of CAPEX spending.

Moderator: Thank you. We have the next question from the line of Aditya Soman from Goldman Sachs. Please go ahead.

Aditya Soman: My first question is can you throw some light on the Captain Morgan launch and how that has done, and a related question is what you think of other Diageo brands that we launched in a similar fashion across the country?

Anand Kripalu: Captain Morgan first, so we are pleased with the initial response to Captain Morgan. We are now in two thirds of the country or so, but still not a 100% national, but wherever we have gone, I think the response has been good. Building a brand in a media-dark market is not a quick fix by the way so it is a journey and really the main rum season starts now which is winter, so the first winter in Captain Morgan will be in the Indian market in its new avatar of a dark rum named for India, priced for India, the reading will happen over the next two months, three months maybe during the winter months, because rum has significant seasonality, but what we have done is it is a strategic move to premiumize rum in India, so all of rum sits popular in India and just like Prestige, now you have whiskey at popular rate or kind of super luxury rate. There was an opportunity to premiumize 40 to 45 million case market of rum and that is why we have used international brands like Captain Morgan with far better quality liquid, with all the brand credentials of Captain Morgan to start that premiumization journey, so this year is a start and you will have to wait and see, but the initial response is positive. Is there an opportunity for more

Diageo brand, actually most of the strategic Diageo brands that need to be in India are in India today across our portfolio and that happened during the integration of Diageo India into USL because all the Diageo brands came into USL. Now, do we strategically invest in every brands, no, but many of them you play the feeding game, so it is available in luxury hotels, it is available in the on-trade and premium bars, and you feed the market by being present on those shelves and in those bars. When the threshold and timing is right, then we may decide to strategically invest in terms of support, so there are many brands that are there in the Indian market where we do not strategically support, there are premium vodka, premium whiskey and so on and so forth, but I think there is no major gap in our portfolio from what we like it to be.

Aditya Soman: I understand totally, I think the question was more in terms of, for example Diageo is largest brand in terms of volumes would be something like Smirnoff in the non-whiskey category and can you see any of this other brands becoming as large as Smirnoff or even overtaking that over a period of say next three or five years?

Anand Kripalu: I think Captain Morgan can become as big as Smirnoff, we have already launched it just now, so that is our opportunity there and I am not sure there is any other high-volume brand of that kind are bottled in India scotch is by the way which are all Diageo brand like VAT 69 and Black & White, all have big volume potential and we are investing behind them, but I am not sure if you have any other brands in mind, why do not you tell me.

Aditya Soman: Nothing particular in mind, I was just checking if there is any plans on sort of anvil. In terms of you mentioned sort of Black & White and VAT 69, would there be sort of prelaunch of these brands as well similar to?

Anand Kripalu: VAT 69 has just been re-launched, the new package in the market just started going through the market actually, maybe in a few places. Black & White was re-launched actually about three to four years ago and we have just launched, by the way Black & White 12-year-old, so Black & White has been one of the fastest growing bottled-in-India Scotch brand, and we have just introduced Black & White 12-year-old which is again a fantastic liquid, both to contribute to growth of the 12-year segment, but also to strengthen the brand equity of Black & White in terms of its credential, so that is something we have done as well.

Moderator: Thank you. We have the next question from the line of Abneesh Roy from Edelweiss. Please go ahead.

Abneesh Roy: Sir, my question is last few quarters you have been gaining market share in the P&A, so two sub questions to that, one is, how is the trend in your sense currently and in P&A, is there a trend that top end is growing much faster and is it possible to give some data there because it is a very large umbrella, and now it is two-third of the portfolio, we get just one number but to understand performance it will be good if there could be more data on that?

Anand Kripalu: I believe we are delivering competitively superior performance and I leave it for you to decode and compare our numbers. As far as, the top end growing much faster, so I will be honest with you, this has been a very turbulent time, the number of five-star hotels and bars that were shut for few months is not fun, so the short-term trend is tough for me to use to replicate what was the longer term trend that has happened in the past and that we believe will happen in the future, and the longer term trend that we believe that we have seen in the past and that we will believe will happen in the future is that each segment will go faster than the segment beneath it, so bottled-in-origin brand will grow faster than bottled-in-India brand that will go faster than Prestige or IMFL brand and that will go faster than popular brand. I really believe because that replicates kind of India's income distribution and income improvement, so it is rooted in the consumer evolution and that is true actually if you see across industry, that is the trend that we are seeing as a percentage. Now, Prestige will obviously be very big, much bigger than bottled in origin, but I am saying the percentage of growth we should see acceleration as you move up towards the top of the pyramid, and that is all we can read and decode right now, Abneesh.

Abneesh Roy: Sir, that is useful. My second question is on the re-launched brand, this diverse data, two of the brands McDowell and Royal Challenge has seen dramatic recovery quarter on quarter because of the stability of trade channels, on the other hand Signature has slowed down quarter on quarter and last four quarters it is slowing down, any particular issue with Signature in terms of competitive issue?

Anand Kripalu: There is absolutely no issue with Signature and just to be clear, this is the second year only of the Signature re-launch. In the first year, I do not remember the number now, but I think it was about 30% growth or something like that, 30% plus growth is what we had reported, we are still growing strong double digit and just to remind you and the other interesting news by the way is that Signature has two variants, a premium variant which we call Signature Premier and a base variant called Signature Rare. Premier variant is growing even faster than the Signature Rare, so within the brand it is premiumizing sharply and I am pleased about that. Please also remember that this brand was declining for many years before we went into the re-launch, so you have got to look at the recovery and the fact that over a two-year period, the brand would be 50% larger than it was just two years ago, I am actually quite pleased with that performance. Having said that, you need to keep investing in a brand to sustain and extract the full juice of a re-launch, well absolutely we need to. Could we do more than what we are doing today, that will be our effort and our intent.

Abneesh Roy: Sir, one follow-up on P&A, how has Diageo part of the portfolio done in terms of sales, in terms of contribution, how is it and margins also if you could give us some color, normally you do not give, but if you could give some color on the margin front?

Anand Kripalu: Abneesh, normally we do not give means it will be hard to start to give now, so we have stopped doing that. This is one business and I have said this before, it is not important, what is Diageo, what is USL everything is one company, they are all our children and you do not choose between your children and we are not breaking up margins anymore between Diageo and Legacy USL brand.

Abneesh Roy: The sales contribution?

Anand Kripalu: Not helpful to the cause, Abneesh.

Moderator: Thank you. We have the next question from the line of Latika Chopra from JP Morgan. Please go ahead.

Latika Chopra: First question is on the revenue side, when you closed Q1, you had mentioned about 15,000 odd outlets were closed and if you exited the September month, how many outlets remained closed and would you expect a further acceleration growth in Q3 from the underlying 4% that we saw in Q2, and is there any festive-related impact that we should be cognizant of between the quarters?

Anand Kripalu: Thanks Latika, let me try and respond to the two questions. One was about festive-related impact, so yes, Diwali was a little earlier this year, but you know the overall market for Diwali this year across industry has been relatively I would say subdued and so to for alcohol, so it was not explosive or dramatically exciting, so there could be some festive-related selling at the last few days of September ahead of October 19 of Diwali, but I am not sure it is too material, and therefore, I am not sure that something to really worry about or explain our numbers.

As far as the highway ban is concerned, about 15,000 outlets closed in the highway ban post the highway ban coming in, out of the 15,000 about 5000 have reopened which leaves about 10. Out of the 10 that are still closed, half are still in Maharashtra. Successively, we do expect more and more stores to open, it takes time, it is linked to license renewal from the excise department and stuff like that and we might still have a residual 3000, 4000, 5000 stores that remain closed and those will be dependent on those stores relocating because actually they are genuinely on a national highway or a state highway and therefore they are genuinely a risk and I cannot complain if those stores are closed and those stores are forced to relocate. We see a successive reduction in the number of stores that are closed. Now having said that I do believe that is what I said in my opening comment by the end of this calendar year which is over the next couple of months, I do think that whatever consumption has not shifted to stores that are open, consumption will largely shift, and therefore, the materiality of the impact of the Supreme Court ban as we go into Q4 I think will be more and that is what I would like you to take.

Latika Chopra: Second question is actually on other expenses, would it be possible to share which line items would have moved where you would have seen more productivity benefits in that line during the first half and is that level of other expense is something which the company will be able to manage?

Sanjeev Churiwala: For the quarter, if you look other overheads have been consistent and flattish, but of course there are 100 of components within that, so I would suggest you can just drop a mail to us and we can get you the specifics of other overheads, but I think for the overall consumptions, our overhead has been fairly managed well. For the quarter, if you really see other overheads have been more or less flattish against 314 crores that we have in the previous corresponding quarter, we landed in 307 crores.

Latika Chopra: Lastly, what is the update on the sale of your non-core assets, any new update out there?

Sanjeev Churiwala: Absolutely, in the previous calls we have been very consistent to say that we have plans to sell about 2000 crores of non-core assets in the next three to four years. This basically consists of lot of residential apartments, commercial property, and some disputed treasury shares. Our plan is to first attack the residential and the commercial property sale in the next couple of years starting from ‘18 onwards, ‘18 and ‘19 would be more focused on that, and then subsequently we look at some industrial plots and some disputed treasury shares, which is ideally materialized after 2019. We are working on that plan and we are very fairly confident as of now to achieve that.

Moderator: Thank you. We have the next question from the line of Indira Badrinarayan from Morgan Stanley. Please go ahead.

Indira Badrinarayan: Just one quick question, in terms of the franchising, it has only been part of the quarter that the franchising has come through this time around, so would it be fair to assume that as you go through this next few quarters, the benefits on account of lower working capital as well as lower costs will keep accelerating?

Anand Kripalu: I will give you an overall comment and then fill details on this. The franchising journey is not fully complete; we have done what we could do earlier. There are some states that we still want to do, but we are waiting for the right commercial partner in the right commercial terms, so one or two more states may happen over the next few months, so that is going to continue to happen, so we have done a big rump of what we wanted to do earlier and we have successively looking at the space that are left out. Now in terms of contribution of our overall numbers through the operating model change, I think Sanjeev will share a bit more color.

Sanjeev Churiwala: Thanks Anand. If you remember in the previous quarters we had mentioned to you that starting from January 2017 till June 2017 six months, we had progressively franchised across 13 states and Union Territories. Now on an annualized basis, if you really look at the net sales that we have franchised is close to about 650 odd crores in the corresponding EBITDA impact of that was close to about 160 odd crores. Most of the benefits will start flowing in the current year. Since the last chunk of is already franchised starting from January to June, the benefits of the working capital, a big chunk is already accrued to us in the corresponding last two quarters, but however, I think that has had a good impact on the overall our P&L. If you look at very clearly in our press release purely from the perspective of gross profit and EBITDA, our gross profit had impacted positively in Quarter-2 itself about 176 BPS basis points and for H1, we actually had a positive impact on 167 BPS point. In terms of absolute number, in H1 which is also part of the press release, the corresponding net sales that we have franchised is about 259 crores and the corresponding EBITDA for that is about 56 odd crores. Of course, you will see the full benefit coming in as we progress into subsequent quarters.

Indira Badrinarayan: The smaller states like UP etc. came on board only in July and August, right?

Anand Kripalu: June-July, Yeah.

Indira Badrinarayan: If it is a working capital and lower cost to be had as you go on?

Sanjeev Churiwala: Absolutely.

Indira Badrinarayan: Second question is basically, could you quantify on a consolidated basis, what is going to be the impact of the IPL business both in terms of higher EBITDA from what we expect in terms of franchisees and also in terms of lower amortization of the money that we are paying of that?

Sanjeev Churiwala: I think all of you have definitely read in the newspapers the benefits that has come into the IPL and we also quite energized with all those news, but I suppose this quarter is about the standalone USL numbers, maybe when we come back to you towards year end with the consolidated numbers, you can see the benefits going out. I suppose it is a bit early for us to call out those numbers yet.

Anand Kripalu: What you all can do is to cheer for the team to make sure we have a better season next year.

Moderator: Thank you. We have the next question from the line of Himanshu Shah from HDFC Securities. Please go ahead.

Himanshu Shah: Sir is it possible to provide some color on net sales revenue mix state wise top three or four states, it would be very helpful, and what would be their overall contribution to the net revenue?

Anand Kripalu: Actually, I think that is getting into micro-detail Himanshu which we do not normally get into because states go up and down and this is a business where each state is like a country in terms of the way it needs to be run, so we do not really want to get into state wise conversation, but listen, at the end of the day if overall our revenue has performed the way it has and our margins have improved the way it has, let us just decode the fact that the more important state that give the better margins have done well, otherwise, this is theoretically not possible, but I would like to just keep it to that.

Himanshu Shah: Secondly Sir is it possible to provide some color like over the last couple of years say last three or five years like for an SKU or portfolio level what would have been the consumer price inflation for the liquid versus the value realization that the company or the industry gets captured?

Anand Kripalu: Brand level, so I really do not have that kind of information in front of me here today over the last three to five years, but at a brand level I will tell you quite simply for the first two years certainly that when we started this journey there was almost no pricing and for the next year, we started getting some pricing and this year we are seeing something better than we saw in the previous years, and that is really net pricing, so that translates into rupees per case ultimately, but to get into SKU brand level, I think that is again getting in to too much detail at this point in time, but if you have some macro questions, then if you email it again to Richard to whatever extent we are in a position we will certainly try and throw light on it.

Moderator: Thank you. We have the next question from the line of Amit Sinha from Macquarie. Please go ahead.

Amit Sinha: Sir, you highlighted that some of the benefits of local taxes getting subsumed might get passed on to the consumers, so my question to you is, is it possible to bring down the retail price especially in states like Maharashtra?

Anand Kripalu: Everything is possible, I cannot say that it is not possible, the question is whether you want to do something, I want to do something, but listen whatever I had to say about tax and so on, we have already shed light on it to the extent that we can earlier in the call, so I do not have much more to say on that.

Amit Sinha: Another question on again in Maharashtra and this is basically our observation is that some of our popular brands pricing is on the higher side of the band and some of them are very close to some of the P&A brands of competitors, so is it very strategic in nature and you want to keep these brand pricing in that way or does it concern you, I am asking more from the perspective that two years back we had an incidence in terms of Haywards in Karnataka?

Anand Kripalu: You are talking about strategic pricing, so the pricing is what it is and because of the nature of our regulatory and tax environment, very often based on tax changes and excise changes, different segments of the market get impacted differently, so whatever we have strategic pricing, that sometimes gets a little wobbly because of engine of tax is not uniform across segments and slabs. Now we are watching these ourselves and at the end of the day if I feel that the pricing is not working for a particular brand in a particular segment, we will apply to correct it, so we are watching this, but everything is possible is all I would say.

Moderator: Thank you. We have the next question from the line of Pritesh Chheda from Lucky Investment Managers. Please go ahead.

Pritesh Chheda: Sir, I just have one structural question, the industry used to be a double digit growth industry and it has been quite many years that the growth has moved towards single digit, so not even a single digit in fact at time that is so considering Indian structure I see this category or this industry should have double-digit, so your thoughts on when does the overall growth improve to double-digit or what is needed it to increase to double-digit or what are the catalyst for it to improve, so your broader thoughts there, these margins are actually coming at a much softer growth rate so margin trajectory can be really different in the growth rate, some thoughts there?

Anand Kripalu: If you think about why the category slowed down in a category that was growing at double-digit historically, the big change was how we do business after Diageo came in and moved into this industry and took control of this company, we changed how business is done, so that was one big discontinuity in an industry that was already used to operating in a certain way, and then of course you know the regulatory changes, I am not going to bore you and repeat what all has happened over the last year or two for this industry. My view is if we are able to just get a more and I think we are towards the end of the change of the ways of doing business and people understanding that this business and increasingly this industry, which is becoming more and more multinational controlled is going to do business only one way, so if we have stability and a common understanding of how business is done and if we have a more benign regulatory environment and by benign I do not mean low taxation, I just mean no uncertainty or you can have small levels of uncertainty, but you cannot have tectonic changes and shift every few months like we have seen in recent times, and this has slowed down confidence and stability of this industry. Looking ahead, we had conversation before in the call that at least as far as the current things are concerned, lot of things slowly are getting behind us. Now, we can never say never, you will never know everything that is going to happen in the future, but at least the known ones are getting better, so my own view is that if we have a few quarters even of stability I will believe that we will start seeing the industry growth numbers to start inching forward. Now when will it get to double-digit, who knows, but I think it will start moving in that direction for sure.

With that, I just like to thank everyone on the call as always for dialing in and being fully engaged and we thank you very much for your support of our company.

Moderator: Thank you very much. Ladies and Gentlemen, on behalf of United Spirits Limited, that concludes this conference. Thank you for joining us and you may now disconnect your lines.