CONTINENTAL® COFFEE

28th October, 2020

To

The Corporate Relations Department
Bombay Stock Exchange
Phiroze Jeejeebhoy Towers
Dalal Street, Mumbai – 400 001

Dear Sir,

Ref: Regulation 30 of SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015
Sub: Transcript of the conference call held on 20th October, 2020
Scrip Code: 519600

With reference to our intimation dated 16th October, 2020, informing about the conference call with Analysts/Investors to be held on Tuesday, 20th October, 2020, please find enclosed herewith the transcript of the aforesaid conference call.

This is for your information and necessary records.

Regards
For **CCL Products (India) Limited**

Sridevi Dasari
Company Secretary & Compliance Officer

Encl: as above

"CCL Products (India) Limited Results Conference Call"

October 20, 2020

MANAGEMENT: **MR. CHALLA SRISHANT – MANAGING DIRECTOR**
MR. K.V.L.N. SARMA – CHIEF OPERATING OFFICER
MR. PRAVEEN JAIPURIAR – CHIEF EXECUTIVE OFFICER, CONTINENTAL COFFEE PVT LTD
MR. V. LAKSHMI NARAYANA – CHIEF FINANCIAL OFFICER
MR. P.S. RAO – CONSULTANT, COMPANY SECRETARY
MS. SRIDEVI DASARI – COMPANY SECRETARY

MODERATOR: **MR. ABHISHEK NAVALGUND – NIRMAL BANG SECURITIES PVT. LTD.**

Moderator: Ladies and gentlemen, good day, and welcome to the CCL Products (India) Limited Results Conference Call, hosted by Nirmal Bang Institutional Equities. As a reminder, all participant lines will be in the listen-only mode. And there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing '*' then '0' on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Abhishek Navalgund from Nirmal Bang. Thank you and over to you, sir.

Abhishek Navalgund: Thank you, Steve. On behalf of Nirmal Bang Institutional Equities, I welcome all the participants to CCL Products 2Q FY '21 Earnings Call. From the company, we have Mr. Challa Srishant – Managing Director; Mr. K.V.L.N. Sarma – Chief Operating Officer; Mr. Praveen Jaipuriar – CEO of Continental Coffee; Mr. V. Lakshmi Narayana – CFO; Mr. P.S. Rao – Consultant, Company Secretary; and Ms. Sridevi Dasari – Company Secretary on the call.

Without further ado, I would like to hand over the call to Mr. Srishant for his opening comments. And then we will open the floor for Q&A. Thank you, and over to you, sir.

Challa Srishant: Thank you, Abhishek, for the introduction. The group has achieved a turnover of Rs. 322.22 crores for the second quarter of 2020-2021 as compared to Rs. 298.68 crores for the corresponding quarter of the previous year. And the net profit is Rs. 47.46 crores as against Rs. 42.07 crores. The EBITDA is Rs. 77.67 crores and profit before tax is Rs. 61.16 crores.

For the half year ended September 30, 2020, the Group has achieved a turnover of Rs. 611.48 crores as compared to Rs. 572.83 crores for the corresponding half year of the previous year. And the net profit is Rs. 85.94 crores as against Rs. 76.74 crores. The EBITDA is Rs. 140.53 crores, and the profit before tax is Rs. 106.93 crores.

We can open up the floor for questions.

Moderator: Thank you very much. We will now begin the questions-and-answer session. The first question is from the line of Richard D'souza from SBI Mutual Fund. Please go ahead.

Richard D'souza: Srishant, congratulations on better-than-expected numbers. So if I may just ask, your domestic sales were down by about 8%, and your Vietnam sales were up quite a bit. And you had problems in your new FDC unit. But at the same time, your gross margins were up by about 330 bps. So would it be right to assume that most of it is because of higher freeze-dried percentage in your total volume sales or am I going wrong somewhere?

Challa Srishant: Yes. Vietnam, I mean, on the performance, total turnover side, Vietnam performed well as in the last quarter. So almost reached about 100% utilization this quarter also. In respect of India, anyway we are carrying some portion of freeze-dried product from the last quarters, though we have shut down one plant, that's not the SEZ plant, the other plant. The first plant we shut down and the SEZ plant was running to the full capacity. And we are also having carry-forward inventory of freeze-dried, so it's not as though substantial quantity has come down in freeze-dried. We have liquidated the existing stuff, plus as you are aware, the freeze-dried product, particularly from SEZ, has a better margin profile, which we build gross margin levels of about 48% or so.

Richard D'souza: Okay. So it would be right to assume that most of the gross margin increase is attributed to the higher freeze-dried percentage in your total sales volume?

Challa Srishant: Yes. It was there last year also. Second quarter, anyway, it was not there. From third quarter of last year, this gross margin profile was there..

Richard D'souza: Yes. Okay. The second question, sir, is on the performance of your Vietnam unit. I think we have seen some extraordinary growth there. I just wanted to ask whether it is sustainable? Or if not sustainable, then what do you think is the sustainable rate? And the second part to this question is, where exactly is the demand coming from, private label or...?

Challa Srishant: As you are aware, in fact, we have been telling in the last two calls also, that a major order was acquired from U.S. and also there were a few ancillary things, because of which we are hoping that we would do closer to 100% utilization this year. So this will be continued. During this year itself we are going in for that line balancing and expanding the capacity to some 13,500. So surely, if not 10,000 tonnes, we will definitely be doing at least 9,000 tonnes in Vietnam this year, which is a little more than the optimum utilization.

Moderator: Thank you. The next question is from the line of Rupin Shah from InCred Asset Management. Please go ahead.

Rupin Shah: My first question is related to utilization level. Sir, if you can just provide the current utilization in India also, like you mentioned about Vietnam that you plan to achieve 100% utilization because of the large order from U.S. If you can just bifurcate India and Vietnam utilization level, your current position, and then the expected utilization for FY '21 and FY '22, like considering the existing order book position and the order inflow trend. If you can just bifurcate.

K V L N Sarma: Yes. In India's traded capacity, we have utilized to the extent of about 75%. The optimum, as I have always been telling, would be in the range of about 80% to 85%. So Y-o-Y basis, we should be reaching about 80% on the spray dried capacity. In freeze-dried, as you are aware, we have already declared on site also that we had to shut down the plant for two months. So as of now, the composite utilization level between SEZ and our main plant, Duggirala plant is about 65%. From now onwards, we are hoping that we will be utilizing to the full optimum utilization, in which case, on a Y-o-Y basis, we should reach about 70% plus or minus.

Rupin Shah: Okay. Fair enough, sir. And the second question is, if you just give some color on realization and gross margin difference in SD and FD for our company to get a fair idea like how the margin profile will change for the company with the change in product mix going forward?

K V L N Sarma: That will be going into too many specifics. We are a single-product company and on occasions we realize that it is working against us. Broadly, you can take that, the margin profile between spray and freeze would be in the range of 1:2 or 1:2.5.

Moderator: Thank you. The next question is from the line of Akhil Parekh from Elara Capital. Please go ahead.

Akhil Parekh: Congratulations on a good set of number. My first question is on, what we say, the new FDC unit guidance which we had provided last time of reaching around 90%, 95% of utilization level. Do you expect to reach that level end of FY '21?

Challa Srishant: Specific to new FDC unit, normally optimum utilization is about 80% to 85%. On the new FDC facility, we will be reaching that utilization levels. In old facility, we already lost about 2.5 months, plus another one month during lockdown. So to that extent, there will be a reduction in the utilization part.

Akhil Parekh: Okay. So, the SEZ, you were saying around 80%, 85%, and the Duggirala one is...?

Challa Srishant: SEZ facility, which we are sure that we utilize 80% to 85%. In the other one, we already lost, so I could not reach that level.

Akhil Parekh: Sure. Got it. But last time, if I remember correctly, you had mentioned that there has been a postponement of orders, specifically from the Russian client, and we should be able to recover it. So has that changed --

Challa Srishant: Come again

Akhil Parekh: Sir, my question is, in the last quarter con-call you had mentioned that there has been a postponement of orders from the Russian clients. So are those orders going to get executed during the rest half of the year or there is no clarity as of now?

Challa Srishant: No. It will not be in one month or in the third quarter itself, it will spread over the two quarters. So by the year-end, we should be able to execute those orders.

Akhil Parekh: Got it. And one more question if I can squeeze in. In terms of branded business, how we have done for first half of the year?

Challa Srishant: Oh, great, we have done very well. Praveen will tell you.

Praveen Jaipuriar: So for the domestic business, we clocked a turnover of around Rs. 60 crores in the first half, which is almost 70% growth over the corresponding period last year.

Akhil Parekh: Okay. And this includes the institutional part as well or this is pure brand? This includes institutional part, right?

Praveen Jaipuriar: Yes, this includes the institutional part, bulk as well.

Akhil Parekh: Got it. And in terms of profitability, do we expect that minor losses could be there for this FY '21?

Praveen Jaipuriar: See, right now we are expecting a good second half as well, based on what we have done till now. So closer to quarter three we will be able to comment a little better on this. We are trying to see how best we can minimize even though little losses that we had expected at the start of the year.

Moderator: Thank you. The next question is from the line of Kashyap Jhaveri from Emkay Investment Managers. Please go ahead.

Kashyap Jhaveri: I have two questions. One, on the standalone margins front, I understand that we also do advertising on behalf of Continental Coffee and which is later on billed to them. So the standalone margins partially could also be because probably there was no A&P spends in the first half? I understand that even gross margins of about 300 basis points would have helped, but is there anything on A&P spends during the quarter or if we would spend on A& P yet?

Challa Srishant: So 50% of the last year's budget was already spent. So since it is only last year, we have spent the entire amount in the second quarter only. This year, it was only to the extent of 50%, we have spent.

Kashyap Jhaveri: So that was, I think, about Rs. 11 crores last year, right, and which is about...?

Challa Srishant: Correct. This year it is about Rs. 5 crores so far.

Kashyap Jhaveri: Okay. Second question is on the new client in U.S. as well as on the European retail chain side. Any developments on this, if there is anything to apprise of at this point of time? And in terms of supermarket segment in Europe, any new development over there if it is there?

Challa Srishant: There is no new development as such. We have already added this new customer as far as the U.S. is concerned. And we have actually started supplying our first private label small pack business to the U.S. to one of the large retailers. So that was a significant milestone for us, and we have created a very unique product for them. So that is one significant milestone in the U.S. market. As far as Europe is concerned, the existing supermarket business, we got it renewed for next year as well. So that is a positive news again. So next year also we will have supplies to the EU supermarkets.

Kashyap Jhaveri: Okay. Right. And just one last question on the retail side. You mentioned that the first half total on the branded side is about Rs. 60 crores. Did I hear that correctly?

Praveen Jaipuriar: Right. So domestic was Rs. 60 crores, which includes retail plus institutions.

Kashyap Jhaveri: Right. And if I look at FY '20, I mean, the full year sales were about Rs. 60 crores, with EBITDA loss of about Rs. 3.5 crores, and we have spent about Rs. 11 crores last year in terms of ad spends. So let's say, if I were to look at Rs. 120 crores full year sales this year, I mean, are we not expecting still EBITDA breakeven over there?

Praveen jaipuriar: So we are, but as I told you in reply to the last question that let this quarter pass and then we will be able to give a better picture on this, because this year because of COVID and some segments being closed, it's a little wait and watch for us, that how things move. So we will be in a better position. But as you rightly pointed out, and as I was mentioning that we are trying to kind of get as close to breakeven as possible.

Moderator: Thank you. The next question is from the line of Tushar Bohra from MK Ventures. Please go ahead.

Tushar Bohra: Congratulations on a good set of numbers. Just quickly, I want to understand, 70% Y-o-Y growth in the domestic business. Could you give a breakup, I don't want the absolute number, I know it will be sensitive. But if you could just give a breakup, let's say, what would be the growth for branded vis-à-vis for domestic institutional business?

Challa Srishant: So the branded business, we would have doubled the business in branded, so almost 100% growth would be there. Because these two businesses due to the lockdown were pretty muted. So whatever growth has come, the absolute value has come from the branded segment as well.

Tushar Bohra: Yes. So I wanted to check whether it would be fair to assume that branded business would be close to the Rs. 100 crores landmark by end of this year?

Challa Srishant: It should be. We are keeping our fingers crossed but should be.

Tushar Bohra: Okay. If you can also just overall, while it's been discussed in part in the earlier calls as well, if you can just holistically share three or four key products that will drive the upward value movement for you, the new products that you are working on across markets, especially in U.S. and maybe in Europe?

Praveen Jaipuriar: Yes. So value-added products, we are doing several new products, starting from flavored coffees, micro-blend coffees to cold brews, instant cold brews. So these are all extremely high-end products, it's a completely different segment from the standard vanilla type products that we used to offer in the market. So a lot of companies who are getting into specialty coffees are in that. Even existing customers who want to increase their portfolio of products, they have started buying these new niche products from us. So we feel that there is a good growth potential in the future as well because it's a new product consumption pattern that we are trying to create. So it will take some time. So volumes will start slow, but they should pick up going forward.

Tushar Bohra: And how do economics work for these products vis-à-vis the traditional bulk packaging and traditional instant coffee business in terms of either the gross margins or the overall way, how is it different?

Challa Srishant: See, the margins are definitely better, but because the R&D that has gone into this is also quite a bit. What we do normally is we create new products based on our customers' requirements. And once we create the product, we can offer that product to other customers in different territories as well. So that is what we have been doing over the years. A lot of these innovations that we have come up at our end, we have started these things because of our customers. They have put in request saying that this is the inconvenience or the problem factor that they are facing, and they wanted a solution. So cold brew is one such example, cold brew is a product where a customer is costing them about $150 per kilo, which we brought down the cost to something like $30 a kilo for them. So this is a convenient product which is there for us. And the customer also, there is a cost saving, which is why they come to us with $50.

Tushar Bohra: And it would be fair to assume that these products would be significantly higher realization. So in the sense that would this also be a volume game or would this be a much faster scale up for us in value terms, what it's like?

Challa Srishant: See, talking about volumes for these products, right now we are a bit premature. It will take some time to build up those volumes.

Tushar Bohra: Okay. No, what I meant was, Srishant, that whether this will be a volume story or whether the value scale-up will be much faster, and we should look at the value terms in this business?

Challa Srishant: So this business will be value terms only, because there is nobody else who can make some of these products that we are making. We should be able to maintain our value proposition for at least a couple of years.

Tushar Bohra: Great. Thanks. Just one last, very quickly, on the small pack business and on our own labeling and packaging plant. What exactly is the status on that?

Challa Srishant: Well, the plant was actually supposed to be ready by now, but unfortunately because of COVID, all the suppliers, the construction, everything has gotten delayed. We are expecting the plant to be fully operational by next financial year beginning, in Q1 of next financial year.

Tushar Bohra: And that would feed into your existing business itself, right, I mean that would be...?

Challa Srishant: Yes. Actually, we are already operating at peak capacity for small packs. So we are also exploring third-party packing for some of our products, because we are exceeding our existing capacity right now.

Moderator: Thank you. The next question is from the line of Richard D'souza from SBI Mutual Fund. Please go ahead.

Richard D'souza: Sir, on this product innovations which are there, I just wanted to drill further on it. Today, of the turnover, what percentage would it be? Or, let's say, three years or five years down the line, what percentage do you expect these value-added products to be as a percentage of your total turnover?

Challa Srishant: See, right now, this will definitely be less than 5%. And yes, going forward, frankly, it's too early for us to project how much it will grow, but we are hoping that it will increase. Our volumes are also growing, so our volumes are growing for the other generic products much more. So this has to out beat that.

Richard D'souza: Okay. And I believe I had asked this question last time also, but I just wanted to understand your strategy for the single-serve segment. Are we planning to enter that or cater to some of the branded players there or we won't be there? Or it's too early to comment anything on single-serve business?

Challa Srishant: Yes. So single-serve actually is divided into two categories: one is single-serve sachets with instant coffee which we are already present in, and we are already exporting this also to various countries. The other single-serve is the pods, the pods is a segment where you need the machines in order to use the pods. That segment, yes, it is growing, but it's a very regional business today because anyone who has a small roaster can do the packing in pods and sell locally. So it does not make sense for us to actually do the production packing in India, then export it to whichever part of the world, we will lose a lot of time and shelf life also in this process. That's why it's more regional at this point in time. And we have the opportunity of exploring the market in India. But in India, pods market is virtually non-existent. But we can get into the segment very easily if we have to.

Richard D'souza: Okay. But there is no business opportunity in supplying to some of the big guys who are there in the single-serve or the pods?

Challa Srishant: So keeping the shelf life in mind, most of them would want to do it in-house at their end and buy it locally. If you have to supply from here, especially as the transfers and everything, they lose two months out of their six months' shelf life.

Moderator: Thank you. The next question is from the line of Dhiral Shah from PhillipCapital. Please go ahead.

Dhiral Shah: Sir, my question is pertaining to, again, Duggirala facility. Sir, what kind of capacity utilization, at least for freeze-dried which is there in Duggirala, you expect for H2?

Challa Srishant: For the current year?

Dhiral Shah: For the current year, yes.

Challa Srishant: H2, I mean, half yearly we should be doing approximately about 70% or so.

Dhiral Shah: Okay. Sir, I am talking about freeze-dried. So we expect 70% in that?

Challa Srishant: Duggirala plant?

Dhiral Shah: Yes.

Challa Srishant: Yes.

Dhiral Shah: Okay. And sir, when you talked about your Continental brand business, so the total revenue was around Rs. 60 crore and we see 70% growth in there, so how much was the Continental in terms of percentage?

V. Lakshmi Narayana: So Continental brand will be almost 70% of that.

Dhiral Shah: Okay. And sir, with this unlocking of economy, have you seen any growth in institutional business?

Challa Srishant: So institutional business has now started to pick up. The first six months was a complete washout. And now with things opening up, offices opening up and out-of-home consumption increasing a little, we are seeing an uptick, but still it has not come to pre-COVID levels.

Dhiral Shah: Okay. And sir, in our balance sheet we have seen a sharp rise in our short-term borrowing. So what is that for?

Challa Srishant: Yes. To enable them and to operate independently, we have taken working capital limits, both at our Swiss facility and the Vietnam facility also. So on the consolidated figures, the working capital borrowings have increased to the extent that we borrowed for working capital at these two places.

Dhiral Shah: Sir, this is what in cost of funds then?

V. Lakshmi Narayana: 1.5%.

Dhiral Shah: Okay. And sir, in your annual report, sir, we have seen also rise in contingent liabilities.

V. Lakshmi Narayana: Contingent liabilities relating to the income tax assessments. So other than that, there are no other contingencies.

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

Bharat Gupta: Congratulations, sir, for a great set of numbers. Just wanted to get a sense what has been a revenue split between the sales which we got deferred from Q1 FY '21? And sir, can you tell us about the volume growth which has happened during the quarter?

V. Lakshmi Narayana: Volume growth, 7% is the volume growth. And yes, that's all. Your question is that, right?

Bharat Gupta: Yes, that partially answers my question. Sir, I just wanted to get a sense about what has been a spillover sale from Q1?

V. Lakshmi Narayana: So the spillover sales have been to the extent of about Rs. 15 crores to Rs. 16 crores.

Bharat Gupta: Rs. 50 crores to Rs. 60 crores.

V. Lakshmi Narayana: Rs. 15 crores, 1-5. You will see that in the stock adjustment that we have made on the cost side. So I think about Rs. 12 crores also is the stock adjustment. So overall, about Rs. 16 crores to Rs. 17 crores, the existing stocks got impacted.

Bharat Gupta: Sure, sir. Sir, my second question pertains to the current level of pandemic. So we are seeing that there has been some second wave of coronavirus across Europe. So are we seeing some kind of a delay in terms of order purchase by the clients?

Challa Srishant: Yes. It is not totally to the normal levels; we are occasionally seeing these disturbances. But definitely there has been an improvement in off-takes, at least people started taking it as a routine. But not only on the market side, even within the manufacturing also we are seeing a few, one or two of our colleagues also getting infected and then they had to take quarantine and all that. So the effect is there, it's not just on marketing side, it is there on every side. We are trying to overcome, address the challenge as and when it is coming. On the market front, particularly, yes, that slowdown which was there in the Russian market for the past two, three months is slightly improving. We are expecting that whatever backlog orders were there, which, along with the current orders, will be executed in the next two quarters.

Bharat Gupta: Sure, sir. That's really helpful. Just one more question, if I can squeeze in. So if you look at the production volumes, so you have estimated that 9,000 tonnes would be our production from the Vietnam unit. If I look at the freeze-dried unit out here in India, so what can be a suitable amount of production which we can send because two months we have lost in terms of maintenance for our old freeze-dried units. So total, if you look at the cumulative volumes, so in India, what can be the sizable contribution which we can produce for FY '21 as a whole for freeze-dried?

Challa Srishant: See currently, on the freeze-dried front I may not be able to say that there will be a huge growth over last year. We should definitely cross by a minor margin in the current year over the last year. Because last year, first two quarters, the SEZ plant was not fully operational. So there we might be able to maintain the last year's volumes in the freeze-dried. Spray-dried, we are seeing a better traction this year also in the domestic market. So the volume growth could be slightly better in the spray-dried segment. So both in India and in Vietnam, this year, the volume growth wherever is there, it is mainly on the spray-dried.

Moderator: Thank you. The next question is from the line of Lokesh Manik from Vallum Capital. Please go ahead.

Lokesh Manik: Sir, my question is a little on the macro side. We have observed that the Indonesian government has given a big stimulus and some of our export companies in India have been benefited. As I understand, we also export to Indonesia, and we have been performing very well between 2015 to 2019, and there was some dip in 2020. So just to understand from you, are you seeing any positive impact there from that country for exports?

Challa Srishant: So not going very specific into the details, I would say, the exports to Indonesia over the last year has been encouraging.

Lokesh Manik: Okay. And do you see an uptrend from here? And do you see a change in profile mix between spray-dried and freeze-dried what they used to order before and what they are ordering now?

Challa Srishant: Broadly this year, it is only on spray-dried.

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

Tanvi Shetty: Congratulations on a good set of numbers. My question was more on the MEIS benefit. Sir, could you quantify what was the benefits in Q2? And also going forward, since the government has capped the benefits to Rs. 2 crores, what can we expect in Q3 and Q4 and next financial year, sir?

K V L N Sarma: Q3, as you know, it is capped at Rs. 2 crores for that quarter. But as you have already seen from the financials that we have about close to Rs. 300 crores in debtors, so we should be getting at least Rs. 10 crores to Rs. 12 crores eligibility on that, which we should be getting subsequently if it is capped at Rs. 2 crores next quarter. This quarter, we have realized about Rs. 8.5 crore.

Tanvi Shetty: So for the rest of H2, we can expect Rs. 10 crores to Rs. 12 crores. Is that right, sir?

K V L N Sarma: If the government do not impose further cap on the fourth quarter also.

Tanvi Shetty: Okay. Thank you, sir. And also, my second question is relating to the margin. Can we expect FY '21 to close on FY '20 level EBITDA margins, sir?

K V L N Sarma: Yes. Thankfully, you have asked for the same level, so I would say yes.

Tanvi Shetty: Okay. That's good to hear, sir. And sir, also, going forward, once the situation normalizes, can we expect our earlier volume guidance of 15% to 20% to fructify in, say, FY 2022, 2023?

K V L N Sarma: Definitely. With caveat being, as you said, things getting normalized.

Moderator: Thank you. The next question is from the line of Prithvi Raj from Unifi Capital. Please go ahead.

Prithvi Raj: Yes. So the question is, the effective tax rate in your India books seems to be about 40%, 41%. I just wanted to understand, was there a one-off in the tax computation or how should we read this number?

Lakshmi Narayana: No, actually we are on the regular tax, which is at 34.94%, that's what is provided for as against, if you look at the PBT at 54.78%, which assessed at 34.94%, which is equivalent to Rs. 17 crores. Against that, the Rs. 7 crores plus we have provided in the Q1 and Rs. 9 crores plus is provided in Q2.

Prithvi Raj: Okay. Sir, what are the revised time lines now for commissioning the new capacities in Vietnam? I am sorry if I missed this in the opening remarks.

Challa Srishant: It's likely to come into operation by March.

Prithvi Raj: By March. So which means benefits will only be there for Q1 of next year?

Challa Srishant: That's right.

Prithvi Raj: Okay. And once the benefit comes in from Q1 of next year, do we have a lag time before we commercialize this, or can this be commercialized from day one?

Challa Srishant: No, it can be commercialized.

Prithvi Raj: Okay. In terms of the demand that you are seeing, I mean, just to understand, what was your utilization in Vietnam for H2 of last year?

Challa Srishant: H2 of last year, we are at 60%.

Prithvi Raj: Okay. Is it fair to assume that for H2 of this year also Vietnam can see this kind of 85%, 90% kind of utilization?

Challa Srishant: Yes.

Prithvi Raj: Okay. And in terms of the consolidation of our wholly owned subsidiary, I am just curious how will transfer pricing work now? Will we still price it at cost plus margins or will that equation change now?

Challa Srishant: No. We invoice it to subsidiaries on arm's length basis, same way how we invoice to others in terms of the pricing, in terms of the credit period, both we maintain.

Prithvi Raj: Sure. I understand, sir. And an extension from the question of the previous participant. I understand MEIS for H2 could be about Rs. 12 crores, Rs. 13 crores. But then with the MEIS benefit being recalled, what is the outlook on this for the next year, sir, and what will be the negative impact, if any?

Challa Srishant: No, come again? Can you repeat the question again?

Prithvi Raj: See, my question is with the MEIS benefit being recalled by the government in favor of RoDTEP, what would be the impact on our financials for the next year?

K V L N Sarma: So far, if you look at it last two, three years, on an average around Rs. 40 crores is our MEIS contribution. And we do not know the kind of scheme that is going to come in place next year. This MEIS benefit over a period has gone into the pricing with a few of our customers because they knew that we are getting this benefit out of their business and all that. So it is considered and shared among the few of our customers. So with these customers, we are confident that we will be able to retrieve on the pricing to a certain extent. So overall, if you see, I mean, the MEIS scrapped and RoDTEP as it is apparent today, we might be able to cover to the extent of about 60% to 65% in total, both in pricing and the scheme in place. The balance to the extent of about Rs. 10 crores to Rs. 12 crores maybe a risk that we have to derisk ourselves.

Prithvi Raj: Sure. That's helpful. And I have a question for Praveen, if I can. Praveen, there has been an explosion of domestic direct-to-retail kind of coffee brands in India and, obviously, this is at a slightly premium range. How do you see this affecting our brands?

Jaipuriar Praveen: So at an overall category level, what we are seeing is that all these brands, they are very niche in nature. They are still not making a substantial volume impact in the category. So it's good that they are developing the category because after all, all of them help to increase the category size. But as of now, as we are talking to each other, the big section is still coming from the traditional coffee segment, which is instant coffee. So that's not impacting us too much. On the contrary, we are also getting help because we ourselves are doing a lot of innovations. For example, the premix coffees and the flavored coffee. So these have all started to pick up and, in fact, is helping our business.

Moderator: Thank you. The next question is from the line of Jignesh Kamani from GMO. Please go ahead.

Jignesh Kamani: I just want to understand our competitive dynamics versus Brazil, because the real has depreciated a lot in six months, while INR has appreciated. So do you think there will be pressure on the margin when you are bidding, competing against the Brazilian suppliers?

Challa Srishant: Actually, we are not able to understand your question clearly.

Jignesh Kamani: Just a minute. So what I am saying is, if you take about Brazilian real, it has depreciated a lot in the last six months, while INR has appreciated against USD. So Brazil has been a little more competitive in the last five, six months. So is it impacting our future order margin outlook?

Challa Srishant: Well, I think you are already aware that as far as coffee is concerned, throughout the world, the coffee is bought and sold in dollar terms only. So the green coffee is bought in dollars and the finished product is also sold in dollars. So only to the extent of conversion rate, there will be an impact.

Jignesh Kamani: Are you saying that Brazil has been more aggressive because of the favorable currency?

Challa Srishant: No. See, one thing you should understand is, the qualities that come from Brazil are completely different from the qualities that we supply. Brazil grows Arabica coffee, 90% of what they grow is Arabica coffee. And about 95% of our consumption is Robusta coffee. So the kind of output product, the target audience, everything is completely different.

Jignesh Kamani: And if you take that based on current order visibility, what kind of volume growth we are expecting in the second half of this year from India plants?

Challa Srishant: So that's actually a difficult question to answer because at the beginning of the year itself we had actually booked orders for the whole year almost. Unfortunately, with this COVID and all that, with the postponements that we saw, we were in a position where we couldn't take new orders because we had already committed to some customers and we had to execute those orders. So going forward also, at this point in time, we have a completely full order book. But if a customer comes and asks for a postponement, again, it will turn out to be an obligation for us to accept that postponement. So it's very difficult for me to 100% confirm and say that there will be so much volume growth. Our target for this year was around 10% or so. And even now we are hoping that we should be able to achieve that.

Moderator: Thank you. The next question is from the line of Vaibhav Gogate from Ashmore. Please go ahead.

Vaibhav Gogate: Sir, what sort of tax rate can we expect in the stand-alone entity this year?

V. Lakshmi Narayana: It is the regular tax rate, which is at 34.9%.

Vaibhav Gogate: Okay. So why was the tax rate so high in Q2 at around 40%?

Challa Srishant: No, it is 34.94% is the tax that we have provided, if you look at it Q1 and Q2.

Moderator: Thank you. The next question is from the line of Tushar Bohra from MK Ventures. Please go ahead.

Tushar Bohra: Just want to understand how the distribution structure has progressed for the domestic-branded business? I believe we were making a lot of efforts to increase the distribution presence. If you can just share more on that.

Praveen Jaipuriar: So we started distributing our products from south of India to different coffee markets. And last year, year-end, we had a distribution reach of around 55,000 outlets, it currently stands at around 75,000 outlets, and by the end of this year, we are expecting to reach directly to around 1 lakh outlets. Now that we have got a foothold in the southern market, we are expanding our distribution to some of the key towns in rest of India, and this is including 1 lakh outlets. So by this year-end, we would have done a basic distribution or, let's say, product placement in at least 10 lakh plus populated towns across India. So that is the plan for us. And the structure is very similar to any FMCG structure, we have our sales officer in the field who are supervised by area managers and then zonal managers.

Tushar Bohra: So, I missed the last part of that, you said you will intend to reach all 10 lakh plus population towns in the rest of India by the end of this year?

Challa Srishant: Yes.

Tushar Bohra: Okay. Right. Second, I think it was mentioned in one of the earlier calls or maybe I read it somewhere, that the uptick for instant coffee would relatively be much more given the work-from-home culture, and maybe we are seeing some of it. If you can comment on that, you would obviously have an understanding of multiple markets, depending on your client requests, etc. If you can give a global flavor of how the coffee consumption patterns are changing because of COVID?

Challa Srishant: So at a basic level, in the first half, because of the lockdown, what we saw is that the in-home consumption went up. That was a clear trend that emerging on the markets. And out-of-home consumption, which is like cafes and other touch points, they got drastically reduced. So that's a trend which we have seen in the first half. Now it remains to be seen whether a similar trend will continue, because slowly and steadily what we are seeing is that there is now offices are opening, and other out-of-home options are opening. So how much of it gets back to pre-COVID level, how much of in-home consumption continues to be on a higher side, I think we will have to wait for some more time for some clearer trends to emerge. But the first half, clearly, we saw in-house consumption going up.

Tushar Bohra: Did you also see any uptick in, let's say, the higher variants of coffee in terms of quality relative to the base?

Challa Srishant: So, at a very broad level in-home consumption will be better for coffee now. So in that sense, yes, it was. But the clear trend, as I am telling you, it is a very short-term spike that could have come. We will probably need to wait for a longer period of time to see clearer trends.

Tushar Bohra: On the distribution side, let's say, the top 10% of our 55,000 outlets or 75,000 outlets, what would be our market share in, let's say, the top 10% outlets as a percentage of the sales of coffee for our brand?

Challa Srishant: 4% to 5% maybe, 4% is what I would put my finger on.

Tushar Bohra: 4%. And our target would be upwards of 10%. Is it fair to assume?

Challa Srishant: See, that's our wish, I would say. And of course, we are heading towards that. But yes, because it's the branded segment you need to create a lot of brand pool before we reach to 10%. 10% in an FMCG category is a pretty high percentage for a new brand to achieve. So we are all working towards this. And yes, hopefully, we should achieve that.

Tushar Bohra: But are we doing it in any of our stores or an y of the outlets, are we doing 10%?

Challa Srishant: Yes, there are many outlets where we are doing 10%. In fact, there are a lot of e-commerce platforms where we are doing 10%. So that's eminently possible. But as you know, FMCG is not about only handful of outlets, it is about how quickly you can scale up distribution and achieve 10% in all of these outlets. So that's a little distance to go. But what I can say right now is that we are headed in the right direction.

Moderator: Thank you. The next question is from the line of Sameer Deshpande from Fair Deal Investments. Please go ahead.

Sameer Deshpande: This MEIS cap which you mentioned of Rs. 2 crores, is that an annual cap on the export turnover?

Challa Srishant: No. It is for the third quarter, the quarter from October to December, government capped it at Rs. 2 crores per company.

Sameer Deshpande: Per quarter, okay.

K V L N Sarma: Not per quarter, it is only for this quarter.

Sameer Deshpande: So actually, in this quarter you mentioned that you received Rs. 8.5 crores in Q2. So assuming a run rate of about Rs. 7 crores to Rs. 8 crores a quarter, for the next quarter we will have the effect of about Rs. 5 crores, Rs. 7 crores negative?

K V L N Sarma: For the next quarter, it might be capped at Rs. 2 crores, so there will be a negative of Rs. 5 crores for that. But if they allow, subsequently if it is revived, the fourth quarter will see a quantum jump, because already during the quarter we would have accumulated some more eligibility. So it would rather compensate in the fourth quarter, if there is no further restriction.

Sameer Deshpande: And government is actually likely to replace it via certain remission of duties, etc., so will they benefit us, if at all, that is implemented?

K V L N Sarma: No, it will not fully compensate it for us, that's what I answered for the last question. It might compensate to the extent of about 30%, 40%. Some part of it, we are trying to recover through our pricing. We are trying to minimize the damage. If the MEIS goes and the other scheme doesn't compensate it will not fully compensate then.

Moderator: Thank you. The next question is from the line of Manoj Gori from Equirus Securities. Please go ahead.

Manoj Gori: Just missed, I was late to join the call. If you can throw some highlight like what was the potential impact we witnessed during the month of July for the standalone business that resulted in degrowth during the quarter?

Challa Srishant: Can you just repeat it ? There was some disturbance.

Manoj Gori: So potential impact on the standalone business, like we degrew during the quarter, so?

Challa Srishant: Yes, we had to shut down, due to these postponements, etc., we have stopped our freeze-drying plant in our Duggirala facility. So if I have stopped it for two months, it is about 800 tonnes to 900 tonnes reduction in the freeze-drying production capacity.

Manoj Gori: So that would have been roughly around Rs. 50 crores to Rs. 70 crores of impact, sir?

K V L N Sarma: Not Rs. 50 crores, plus or minus Rs. 50 crores. But we were already carrying an inventory, so March end we were carrying substantial inventory, which we have liquidated during the first quarter to a larger extent. And then during the first quarter, we have produced some and towards the end of the first quarter we were carrying some inventory, which we could liquidate during the second quarter. So there will not be a substantial reduction on account of freeze-drying capacity. The capacity was lost, but the sales were almost to the extent of about 60% to 70% in the Duggirala unit also. You would see that on the inventory adjustment there.

Manoj Gori: Inventories have definitely come down, yes. So what we can safely assume, like there wasn't materially loss of sales because of the maintenance that we did for our freeze-dried capacity in Guntur plant?

Challa Srishant: Correct.

Moderator: Thank you. The next question is from the line of Nikhil Upadhyay from Securities Investment Management. Please go ahead.

Nikhil Upadhyay: Congratulations on good set of numbers. I had two questions. One is to Praveen. I think on the branded side we have seen a very strong growth. And if I understand, at the end of March, April, because of a lot of unavailability we were targeting the smaller retail and stockists, and there we were getting good traction. If you can just help me understand in terms of some kind of a same store sales growth trend because the distribution also has grown by 50%. So on the existing stores where we were already present, what kind of a growth are we getting or what is the kind of retention of customer we are getting? Any qualitative aspects if you can share.

Praveen Jaipuriar: So first half, because we were not able to expand too much because of COVID, in fact, all the growth that we have got is largely because we only grew from 55,000 outlets to maybe 70,000, so which is only 15,000 outlets we grew. But the large part of growth came from existing outlets itself. And the good part is that our product has been quite liked by consumers, so we are seeing a lot of stickiness by a lot of new set of consumers. And that is getting reflected by the repeat orders that we are getting from the initial outlets that we have placed the products in. So that's the positive feedback that we are getting for our product.

Nikhil Upadhyay: Okay. And in this, modern trade would not have contributed anything for us?

Praveen Jaipuriar: Yes. Modern trade also, I would say, actually because for a small business and a growing business like us, a lot of green shoots that we had seen last year had started to bear results this year. So also, the good thing is that we have seen growth across channels, so the growth has come from kirana channel, the growth has come from modern trade as well, the growth has come from e-commerce as well. So all the channels have seen a good amount of growth. So I can't say that one has overdone the other.

Nikhil Upadhyay: Got it. Secondly, Srishant, like two, three years back when we were putting the freeze-dried facility, there was a lot of noise about new capacities coming in. Now as those capacities are commissioning or getting operational, is that demand supply good enough or do you think that the pressure on pricing, which we were talking of a year or year and a half back, does that still exist? Or any qualitative aspects if you can share?

Challa Srishant: Well, the pressure is still there. All the capacities have already come online. And everyone is supplying in the market already. And I think last year and this year also we are seeing a slight increase in demand also for freeze-dried coffee. So yes, there is not much of a drastic change in the market dynamics as such.

Nikhil Upadhyay: But contrary, because of the situation which has been impacted because of COVID, won't many of these facilities be facing stress or are they still making good enough money?

Challa Srishant: See, most of the places as far as instant coffee consumption is concerned, even after COVID there is no real reduction in consumption that is there across the world. A couple of places they may ask for a postponement. In Europe, for instance, we have seen an advancement of orders. They anticipated a sharp off-take, so they asked to advance orders. And slowly that gets tapered down for the rest of the year. So like this, we haven't seen any reduction in consumption of instant coffee as such. It's only a temporary postponement what we have seen. So keeping that in mind, as far as FD is concerned also, there is no reduction in demand, but I mean, every year there is a slight increase in demand for freeze-dried, which is there like even this year as well.

Moderator: Thank you. The next question is from the line of Kashyap Jhaveri from Emkay Investment Managers. Please go ahead.

Kashyap Jhaveri: Yes, sir. Just one question on the gross margin. We have this inventory adjustment, which is about Rs. 11 crores sort of adjustment of inventory from the previous quarter carry-forward. If one were to adjust for the costs which are included also in this Rs. 11 crores, would our gross margins be higher by another about 100 basis points, is that a right assumption?

Challa Srishant: Very minimal, because in our cost structure the raw material component itself will be more than plus or minus 70%, if you take the cost itself. So the impact of other costs would be minimal.

Kashyap Jhaveri: Okay. And second question was on the inventory side. You mentioned that we have still carry-forward inventory of freeze-dried coffee...

Challa Srishant: Last quarter. Last quarter end we were having inventory, which during this quarter we could sell. That is how even though the plant was shut down for two months, two and a half months, the sales per se have not come down substantially.

Kashyap Jhaveri: Right. So that I understand, from the first quarter we had highlighted this. But if I heard you clearly, you mentioned that we have still decent carry-forward inventories for the next quarter also? Or have I heard incorrectly actually that portion?

Challa Srishant: No. For the first quarter, we had inventories available because what we were carrying from March, we were able to liquidate during the May, June. But during May, June for some part, after that initial 30, 40 days lockdown, because we are an essential commodity we were able to operate. So that quantity we were having an inventory during the end of the first quarter, which during the second quarter we could liquidate. That is how during the second quarter, though we have shut down the FD plant for more than two months, the sales figure has not come down since we have liquidated all that inventory. Now we are maintaining minimum inventory on finished goods.

Moderator: Thank you. The next question is from the line of Manish Mahawar from Antique Stockbroking. Please go ahead.

Manish Mahawar: Just two specific question. One, in terms of freeze-dried coffee, when you said maybe 2Q when we had liquidated inventory of 1Q. So is it fair to assume because we have taken a production shutdown in our 2Q, so it will be fair to assume that second half our contribution of freeze-dried will be lower as a total company?

Challa Srishant: See, we are able to run the plant to the full extent and we are able to deliver, then obviously we will be able to achieve. We will not have any inventory, or we will minimize the inventory by the end of the second half. Then, we should be able to achieve almost equivalent to last year's sales figures on freeze-dried.

Manish Mahawar: Okay. And second, just again in continuation of this, just wanted to understand. Second half the margin, if we compare with the last year second half, should be lower maybe because contribution of freeze-dried will be lower because Vietnam is doing really fine. And also, your export incentives should be lower, again, in the second half. Is this fair to assume in the second half?

Challa Srishant: The Vietnam improvement in quantity is an additional thing. To a certain extent, MEIS will dampen that additional realizations that we get. But there will not be a total strength on the margins as such. So normally, MEIS is one part, we consider margins without MEIS benefit. So operational margins should be better, the MEIS being what it is, it is changing from quarter-to-quarter for the past three, four quarters. So we take it as a separate. The operational margins definitely should improve.

Manish Mahawar: Okay. Understood. And sir, can you give me export incentive number for the last year same quarter?

Challa Srishant: Last year same quarter, it was about Rs. 10 crores.

Manish Mahawar: Rs. 10 crores. And what was the number for 1H this year and last year, if possible?

Challa Srishant: Pardon me?

Manish Mahawar: This year's first half and second last year first half numbers, sir.

Challa Srishant: It's Rs. 18 crores versus Rs. 15 crores.

Moderator: As there are no further questions, I now hand the conference over to Mr. Abhishek Navalgund for closing comments.

Abhishek Navalgund: Yes. Thank you. Thanks to the management and all the participants, basically. So I will just hand over the call to Srishant sir for his closing comments. Thank you.

Challa Srishant: Yes. Thank you for organizing the call. And thank you to all the participants also for taking part in this. Hope to talk to all of you again next quarter. Thank you.

Moderator: Thank you. Ladies and gentlemen, on behalf of Nirmal Bang Institutional Equities, that concludes this conference. Thank you all for joining us. And you may now disconnect your lines.