"CCL Products India Limited Q1 FY-19 Results Conference Call"

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Moderator: Ladies and gentlemen, good day and welcome to the CCL Products India Limited Q1 FY19 Results Conference Call hosted by Nirmal Bang Equities Private 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. Should you need assistance during the conference call, please signal an operator by pressing '*' then '0' on your touchtone telephone. Please note that this conference is being recorded.

I now hand the conference over to Mr. Abhishek Navalgund from Nirmal Bang Equities. Thank you and over to you, sir.

Abhishek Navalgund: Good morning everyone. On behalf of Nirmal Bang Institutional Equities I welcome you all on 1Q FY19 earnings call of CCL Products India Limited. So, from the management side we have with us Mr. Srishant – the Managing Director; the new CFO of the company – Mr. V. Lakshmi Narayana; Ms. Sridevi – the Company Secretary and Mr. P. S. Rao – the Consultant Company Secretary.

So without wasting time we will start with the opening remarks from the management and then we will open the floor for Q&A. Over to you, sir.

Challa Srishant: Thank you, Abhishek. I wanted to first introduce Mr. Lakshmi Narayana he is the CFO has just taken charge. He has more than 30 years' experience in the finance sector and multiple industries. He has worked in India and abroad as well. So we are welcoming him on board. Thank you.

And coming to the performance of the company, the company has achieved a turnover of Rs. 294.77 crores for the first quarter of 2018-19 as compared to Rs. 249.31 crores for the corresponding quarter of the previous year. And the net profit is Rs. 39.46 crores as against Rs. 27.03 crores.

The EBITDA is Rs. 63.48 crores and the profit before tax is Rs. 54.19 crores. We can go in for the questions now.

Moderator: Thank you. We will now begin the question-and-answer session.

The first question is from the line of Jignesh Kamani from GMO. Please go ahead.

Jignesh Kamani: Sir, in the third quarter where Vietnam continued to report very strong margin. So, is it purely because of product mix or now with the agglomeration capacity on board and the existing client also ramp up in the Vietnam, this kind of margin is reasonable for the full year?

Challa Srishant: No, see it is because particular orders that we had executed in this particular quarter were more profitable. Jignesh, as you already know we work on a yearly basis and not quarterly basis. Our customer mix also, it depends. Once in a while they may place an order in Quarter 2 or Quarter 1 or Quarter 3 or Quarter 4. So in this particular case we had more profitable contracts being executed in Quarter 1.

Jignesh Kamani: So for the full year what kind of margin Vietnam operations can give?

Challa Srishant: It is more or less similar margins as what we got last year. It is only better utilization will be there in this year.

Jignesh Kamani: In Vietnam operations continue I think this is the fifth year we completed Vietnam?

Challa Srishant: Yes, that is correct.

Jignesh Kamani: As per that we can say this treaty I think after five year we come into the 50% tax bracket. So any clarity from when we will start paying tax in the Vietnam?

Challa Srishant: Regarding the tax part there are certain provisions or certain interpretations which have been done by the government that may make us eligible for an extension in tax benefit as well. So we are exploring these options from with the tax department and if that is the case, then this tax exemption will continue for a little longer.

Jignesh Kamani: In Vietnam we mentioned that we are trying to increase our capacity by 2,500 by line balancing. By when it will get commissioned?

Challa Srishant: In Vietnam this will take place in next financial year. We have not placed the order for the equipment or anything yet. We are still in the initial stages. Sometime during next financial year. We have not fixed the date yet.

Moderator: Thank you. The next question is from the line of Karan Sharma from Kredent Capital. Please go ahead.

Karan Sharma: As you had mentioned in the last call that for the domestic business, the person who had taken over they are trying to build the business again from scratch, so you are putting up a new strategy, so any color on the domestic business like for the next three years how much revenues are you targeting and what areas are you looking at exploring?

Challa Srishant: Yes, it is not as if the building everything from scratch. To an extent what they are doing is making a lot of changes from the way that we were operating in the past. In fact last financial year, one of the first things that the team had done is that revise the margin structure. They have increased the MRP of our products, they have also introduced new offers in the market and things like that and with the additional margins they are reinvesting in brand building.

So ATL and BTL advertising has started on a regional level. So their target for this year also is to increase the sales from Rs. 46 crores what we did last year to about Rs. 100 crores that is projected in this year. One of the ways that we are also targeting to achieve this growth is by the introduction of new products and new product categories that we have not done in the past. We have just done a couple of institutional trials and after stabilizing our products and product mix we will be introducing some new products from next month onwards. That includes Remixes, 3 in 1, Roast and Ground Coffees, Chicory Coffee blends all these things will be done in next month.

Karan Sharma: One more thing. The product that we have is very good but if I see that the channels that we have for selling this, mostly are from the ecommerce channel, so are you exploring the traditional modern stores or the normal Kirana shops also for our product?

Challa Srishant: Yes, actually we are present in almost all the stores in South India. Our current focus is only in AP and Telangana. We will be expanding to Karnataka and Tamil Nadu as well during this year. One fact is about 75% to 80% of the coffee sale in India is taking place in these four states. So our target also is to focus on these four states first and in other regions we will make our products present but our focus is not really to do a lot of promotions and activities in other areas right now.

Moderator: Thank you. The next question is from the line of Nitin Gosar from Invesco Mutual Fund. Please go ahead.

Nitin Gosar: Just wanted to understand the nature of this profitable contract which you mentioned. Is it more to do with the higher portion of freeze-dried or is it more to do with the nature of the contract in terms of the time duration, if there are shorter, short duration contracts you will end up doing more profit or is it more to do with the RMHS? How should we see this more profitable contract?

Challa Srishant: No, see this is something which I think I have already explained before. See the range of customers that we have we are usually working with all long-term customers who buy larger volumes. Out of these customers we have, some customers who have maybe 5 or 6 different products in their product mix. They may buy 100 tons of higher margin products, they may buy 500 tons of lower margin products from us. So it is depending on the specialty nature of that particular product that the customer needs, we supply to them.

Whatever production planning and scheduling that we do, we do it again on a year-to-year basis. At the beginning of every financial year we do our estimate for that particular year based on the repeat orders that we have. It is the quarterly execution is something that we do not focus on at all, which is also one of the reasons why you will see that there has been a lot of quarterly fluctuations in the company but yearly targets we are still meeting. Last conference call also there were lot of surprise questions saying that we did not expect Quarter 4 to turn out to be the way it did. But that is something that we had projected from day one.

Nitin Gosar: And sir, we need to hold onto to our guidance of 10% to 20% profit growth for FY19?

Challa Srishant: Yes, as of now 10% to 20%. We might have a revised update after the new plant is commissioned.

Nitin Gosar: Okay sir, in terms of Indian operations the strong top line growth would also mean it is part of the guidance or is it a positive surprise that we should be looking at it?

Challa Srishant: No, it is part of the guidance because we are right now still executing some contracts which were entered into maybe 6 or 7 months ago. So the raw materials that we had procured also was much higher than what it is going to be for the rest of year. There will be a significant decrease in raw material prices from next quarter onwards. Because of the falling green coffee prices when you buy the coffee, by the time it gets delivered it takes maybe even 2 to 3 months. So you would not see the impact immediately in the numbers. Last year's higher numbers are still getting reflected in this quarter as well.

Nitin Gosar: One last question with regard to the order book. Where do we stand? I think around 4th quarter we mentioned that we are at 60% to 65% on order book for FY19?

Challa Srishant: Yes, so I think we are more or less towards around 70% to 75% right now.

Nitin Gosar: I wanted to understand the global scenario in terms of demand supply mismatch, in terms of spray-dried and freeze-dried? I think somewhere in past calls you did mention that there has been excess supply and because of this margins have come under pressure in spray-dried. Has there been any change in that particular scenario as of now?

Challa Srishant: Actually, as far as the global demand and supply is concerned the demand is growing at the same rate of 2.5% to 3% globally. As far as the supply is concerned, to be frank there is more than 50% excess production capacity that is available in the world. You have numerous manufacturers with spray as well as now freeze-dried capabilities, so there is no shortage of potential supply. The reason that we have been able to grow in a systematic and consistent manner is because one we have the right marketing collaborators in different geographies, two we have a wider range of product mix that no one else in the world can offer, three we are keeping our R&D to ourselves.

So whatever is the Research and Development that we are doing we are keeping this as part of our in-house technology and we have now created more than 1,000 blends in our portfolio. So all these factors combined is enabling us to continue to grow year-on-year. This is the same question that we have been asked 5 years ago and it is the same question that we are getting asked now as well and it is fair enough because people find it very hard to believe how come we are the only exception which is there in the market.

That is because one, we have had first mover advantage also and to be frank this is something that I have mentioned before also. We are not expecting this kind of a potential volume growth to continue in perpetuity. We are expecting that over the next 4 to 5 years there is going to be a decline in our B2B business which is also one of the reasons why we are focusing on the branded business more aggressively starting with domestic market.

Moderator: Thank you. The next question is from the line of Gagan Thareja from Kotak Investment Advisor. Please go ahead.

Gagan Thareja: Is it possible to understand the export incentives figure for the quarter?

Challa Srishant: It is about Rs. 8 crores that was booked in this quarter.

Gagan Thareja: Okay, versus 1Q of last year would have been how much?

Challa Srishant: Last year we did not book any incentive.

Gagan Thareja: Okay, and the US Government seems to have dragged the Indian government to WTO for the export incentives that are used by the Indian Government and I do not know what is the status on that matter but what do you foresee as a possible path for the export incentives that are available to you right now?

Challa Srishant: Well, as of now what the government is saying is that at least the official response to the WTO has been that by 2020 they are going to remove the export incentives but considering that the elections are coming up and all this is happening, the government is also focused on increasing exports incentivizing exporters, so we do not see a change happening overnight. Maybe the change might take place over a period of time.

One fact that we have to keep in mind is today the export incentive is built into the price of all the products that have been exported from India. So, any manufacturer who is supplying from India, they are factoring this in and then they are supplying. If there is a removal of incentive, there is accordingly proportionately at least to an extent the price is, the sale price is also likely to get impacted.

Gagan Thareja: But would that not be determined by the fact that there is an excess supply in the global markets and therefore your ability to price all the change in export incentives might be determined by the competitors' scenario in the market?

Challa Srishant: Yes, but India has certain other advantages that other geographies do not have. Though there is excess supply, India's multiple advantage is for example we can import raw material into the country without payment of any additional duties. We can process and re-export. Brazil, which is the largest exporter of instant coffee in the world, they do not have the option of importing any raw material into the country. So we can actually give them a run for their money.

Because as a country we can be much more competitive. Our Per Kg production costs are also lower than what it is for them. So there are multiple advantages that we have which will enable us to remain competitive in the global scale.

Gagan Thareja: Okay, but your margins might sort of be a function of the movement in export incentives to a certain degree?

Challa Srishant: Yes, on a standalone basis for the India operations, yes to an extent, there will be an impact. But fortunately for us by next year we are also getting our SEZ online, that will also enable for the positive contribution to the bottom-line because of the tax incentives.

Gagan Thareja: Okay, if I looks at the Vietnam or for that matter simply the consolidated minus the standalone performance of P&L this year, there seems to be a sharp increase in employee expenditure as well as other expenditure for the subsidiary business. Any specific reasons for that?

Challa Srishant: For the subsidiary business maybe because of the increase in volumes that could be one of the reasons as well. The number of people for packaging and other areas we would have utilized more number of people there.

Gagan Thareja: Okay, so it is all in line with the sales growth in your opinion?

Challa Srishant: Yes.

Gagan Thareja: Okay, is it also possible to get the debt and the CAPEX figures for the year?

Challa Srishant: For this year, the Rs. 300 crores investment that we were talking about will be completed. And there is no other further CAPEX that we are planning for this financial year. I think we have already spent around Rs. 250 crores in the project till date. So the balance Rs. 50 crores also will be spent during this financial year.

Gagan Thareja: Okay, and what is the debt position, gross debt on books as of now?

Challa Srishant: About Rs. 160 crores is the long term debt that we have incurred for this project. Apart from this project the company is debt free. Vietnam is debt free and India operations for existing facility is also debt free.

Gagan Thareja: And what could be the cost of debt for this long-term debt that you have?

Challa Srishant: Our cost of debt is it is around 5%.

Gagan Thareja: Okay, alright and if you could maybe give some insights into the net working capital situation for the company now in terms of receivables and payables? Is the long-term credit credited or is there any change?

Challa Srishant: I will ask our CFO to just answer this.

Lakshmi Narayana: So the receivables and the total current existing liabilities position it remains the same what is there on 31st March. March position continues even June also because the volume of business that we are conducting is in the similar line of the Q4 and Q1 of this year.

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

Akhil Parekh: My question is on the new freeze-dried unit. Any further color on this, should we expect a built in any numbers, volume numbers for this FY19 from the new unit?

Challa Srishant: Akhil, we are not factoring anything in right now because the plant as we had mentioned earlier was supposed to come online by September of this year, so the equipment installation is on track. We are planning and starting our trial production in Quarter 3, and because this is a green field project it will take some time for the production to get stabilized, and after that we have to go in for customer approvals.

So the approvals, when the approvals are going to come is something that is right now unclear for us because it depends on various other factors as well, which is the main reason why we have not given any projections for this year assuming commercial production. Definitely next year we will be in commercial production. Whether we will start this year this financial year or next year we will know a little later down the line.

Akhil Parekh: Got it. So if for example if we do not have any volumes in FY19 and the raw material prices are going down so am I interpreting it correct that the top line for FY19 can stay flat or even decline as compared to FY18?

Challa Srishant: No, it is not likely to decline. Top line also we are seeing maybe approximately a 10% growth between 0% to 10% is what we are seeing on the top line basis.

Akhil Parekh: And that might be because of the product mix?

Challa Srishant: Yes, not only product mix but because of the decline in prices as well. Like Quarter 1, we have seen a 20% increase compared to Quarter 1 of last year but going forward, the lower green coffee prices everything is going to get reflected in the financials.

Akhil Parekh: But will not the realizations drop if the raw material prices go down and the margins will improve but?

Challa Srishant: Yes, it will. Realizations will drop.

Akhil Parekh: Okay. Second question is on the tax guidance. We had 24.4% as against 29% for same quarter last year. For year would we be able to get some tax guidance?

Challa Srishant: This will be more or less along the same lines as last year. There might be a slight improvement because of this Vietnam tax exemption.

Akhil Parekh: Okay and one last question with regards to the discounting rate. Since few quarters you have been mentioning that we are trying to build our product B2C product on par with Nescafe and Bru. But I still see some kind of discounting going on in Amazon like for example 400 grams packet is sold at Rs. 470 of CCL as against Nestle which is sold at 1,000 grams at Rs. 1,800. So ours is Rs. 1,200 per kg and theirs is Rs. 1,800 per kg, so the discounting is still there which we have been mentioning that we will be bringing it on par last few quarters. So any color on that?

Challa Srishant: Yes, one is the MRP has been made on par with the brand leaders. The reason again for the discounting is ours is a new product. We have to incentivize customers to try our products out at least once and this is the reason as an introductory offer we have provided these discounts.

Not only here even in super markets there are certain areas we are giving buy one, get one free but what I do understand in the next couple of months itself that we are going to start reducing the offers from buy one get one they are giving a smaller pack free and eventually over a period of time this will also reduce.

Akhil Parekh: Got it. And if I can just squeeze in one more question, last quarter we had mentioned about one of the US FMCG brand who sells coffee in a big way and we might see some traction coming from that particular company. Any light on that?

Challa Srishant: Not FMCG brand, okay so what has happened in the US is one of the largest conglomerated and packing units in the US is shutting down this year. So there is a transition that people are looking at, looking at alternative suppliers. Most of that business was earlier being done by Brazil, the base product was being manufactured in Brazil and now Brazil is again going to be able to supply the finished product to most of these people.

But a certain percentage of the business is getting transitioned to a Vietnam facility as well. The same company they have approached us, they wanted to have a tie up with us as well so from Vietnam we are going to be supplying to them.

Akhil Parekh: How much would be the quantum?

Challa Srishant: This year I think it is about 400 tons, 500 tons will be there.

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

Jignesh Kamani: Incrementally any color from the US on you can say in terms of adulteration of coffee from Brazil and Mexico. They already you can say form the law, but any implementation, are they going strict?

Challa Srishant: No nothing. The lobby over there is very strong, both the branded segment as well as the unbranded segment both are fighting against the implementation. Officially the law is in force, but there is no laboratory in the US that has the capability of testing for purity of the coffee which is the biggest problem.

Jignesh Kamani: So for next one or two year is there any chance that it will get you can say imposed or it will remain as it is?

Challa Srishant: So to be frank it can happen overnight also because the government itself is such that if they feel that they want to implement something they can and because the law has already been enacted, they can easily implement immediately.

Jignesh Kamani: But on the ground we are not seeing you can say any development as of now?

Challa Srishant: No, nothing.

Moderator: Thank you. The next question is from the line of Sneha Talreja from Edelweiss Financial. Please go ahead.

Sneha Talreja: The green coffee prices have fallen but we have not seen any impact in the revenues. So basically the question was if you are saying that the green coffee prices have fallen or they may further fall so what is the revenue expectation sir, ideally they should fall or what is their expectation, it should remain between 10% to 20%?

Challa Srishant: No, our revenue expectation is between 0% to 10%. One of the reasons why there is a revenue growth in this particular year is because one, our volumes have gone up significantly more than what we have done in Quarter 1 of last year and two, because the green coffee prices are on a downward trend. Some of the more expensive coffees or the contracts are being executed in this particular quarter. That is the reason and this particular quarter we have seen an abnormal increase in turnover.

Sneha Talreja: Sir, how much would be the fall in green coffee prices on a year-on-year basis?

Challa Srishant: Almost about 15% to 20%.

Sneha Talreja: Okay, can you even give the volume increase in the current quarter maybe for Indian?

Challa Srishant: Volume increase is something that we are not given an exact number it is approximately around 30% is what we have increased.

Sneha Talreja: That is combined of both Vietnam and India operations?

Challa Srishant: Yes, both combined.

Rohan: Sir, just to add one question from my side, Rohan here. Just one on a previous question taking it forward, you mentioned that one of the US largest conglomerated coffee player is exiting from the business and as of now Brazil is the sole supplier to them. So how big an opportunity it can be and the customers in the US which are right now procuring from Brazil, are we already connected to them and are we already supplying to them, so we can leverage on this situation?

Challa Srishant: Yes, we are already connected to them, we have been supplying to them small volumes in the past, now because of this transition they are talking to us about buying some more volumes. To be frank they want to continue with Brazil because they have multiple advantages, shorter lead times, and the lack of regulations as well, so all these things are working in their favor. If there is a change in law then automatically we will become the preferred supplier literally overnight.

Rohan: But that is subject to change in law?

Challa Srishant: Yes, that is subject to presentation of the law.

Rohan: Sir, just one more last question from my side, that you mentioned that as in long term like about three to four years the volume growth of the company is likely to slow down on a consistent basis or the structural growth which we have seen in last three to four years that may come down. So what number do you see that what will be long term growth sustainable for the company after three to four years?

Challa Srishant: See for the next three, four years between 10% to 20% is the volume growth that we can sustain, but after that it is likely to slowly start coming down because if you are already at say 45,000 tons or 50,000 tons production capacity, every year growing by 5,000 tons to 6,000 tons is going to be a very big challenge.

Rohan: Because of that it has increased so much?

Challa Srishant: Exactly and because our margins are also more or less on a fixed basis, we will have to our current model is just to keep increasing volumes. We have already gone through the major geographies. If countries like US and all actually pan out, then yes the volume growth is going to be sustainable for a little longer. But bottom line growth if you want to see it is more sustainable way of doing this is through the branded business, which is why for the next couple of years we are planning on focusing on the branded business.

Moderator: Thank you. The next question is from the line of Kishan Gupta from CD Equisearch. Please go ahead.

Kishan Gupta: So basically how does the falling green coffee prices affect your wholesale business, the volumes basically?

Challa Srishant: So the falling green coffee prices first thing is raw material cost contributes to almost 70% of our product cost. So any decline in raw material prices will automatically result in a decline in realization for us. It will not impact the volumes at all, but it will impact the realization.

Kishan Gupta: I want to understand about the industry in general, so how it affects the industry volumes basically?

Challa Srishant: See as far as the industry is concerned, the demand for coffee is growing at the rate of 2.5% to 3% per year. The supply side, there are more than enough manufacturers, there is more than enough manufacturing capability which is there in the market. The reason why we have been able to grow disproportionately is also because of the reasons I mentioned earlier.

We have in-house technology, we have the right collaborators, marketing collaborators in various geographies. There is a lot of R&D that we have focused on. We have created a wider range of product mix. All these things are helping us grow at a disproportionate rate to the industry growth rate.

Kishan Gupta: And what is the effect on your retail prices in India for the effect of fall in green coffee prices?

Challa Srishant: Retail prices today to be frank market leaders, there are two players who are there, one who is leading the pure coffee segment and one who is leading the chicory coffee segment. These are the two players that are determining the coffee prices, the branded products selling price in the market. From our side also, we are not the market leader right now. We are the third player who is there in the market. So we cannot go beyond target prices that they have set. So we have set our prices also based on what they are selling.

They are also manufacturers within India, they also have access to the same raw materials that we have so whatever impact is there on them, will be there on us. The only difference is that we have economies of scale. We have more than double the capacity capability of what they have, which will enable us to be more economically efficient on a per kg basis, so that is our biggest advantage. So our sustainability will be much longer than them even if there is a price war.

Kishan Gupta: Okay, have they reduced prices basically post this fall in green coffee prices?

Challa Srishant: They have actually revised, they have given a lot of offers in the market as well, so in a way they are passing on the benefits to consumers.

Kishan Gupta: Okay, and you talked about value addition, you said, so basically what sort of value addition you do product wise?

Challa Srishant: Product wise, okay. So we have multiple products from products with aroma, with micro ground coffees, functional coffees, flavored coffee. The number of products or the range of products that we have is huge including certified specialties. There are multiple permutations and combinations that we can create as well, and we have the only plant in the world that can actually produce all the various qualities from one single location.

So we have customers who want the most premium products and we supply from the same plant. We have customers who are working with a certain price target and quality parameters. We supply to them as well from the same facilities.

Kishan Gupta: And how much was the R&D spent last year FY18?

Challa Srishant: We are not allocating the R&D as a separate unit until last year. From next year onwards we will be but whatever we have invested is closer to the tune of almost $10 million in the form of equipment we are the first ones to install certain equipments on an experimental basis. We have gone to other countries and tied up with the manufacturers to create new equipments. So this is an ongoing process for us and once we get the equipment we commercialize it. So it is not counted as a separate R&D expenditure for us.

Kishan Gupta: But you talked about doing it in the future so what is the target basically as a percentage of turnovers?

Challa Srishant: It is not exactly on the basis of percentage of turnover, based on the need we thought we will allocate budgets from next year onwards, from next financial year. We have not allocated any budget right now because it is part of the development process.

Kishan Gupta: And how much is the Vietnam capacity now?

Challa Srishant: It is 10,000 tons.

Kishan Gupta: And how much is agglomerated and otherwise?

Challa Srishant: It is about 4,000 tons.

Kishan Gupta: Agglomerated?

Challa Srishant: Out of the 10,000 tons up to 4,000 tons can be further agglomerated.

Kishan Gupta: So 8,000 tons you mean to say?

Challa Srishant: No, it is 10000 tons spray-dried line capacity, for agglomeration one has to convert the spray-dried powder into granules. Agglomeration capacity is 4,000 tons. So for 4,000 tons of the spray-dried products has been converted into granules. For our overall capacity will remain 10,000 tons. It will not be double counted.

Kishan Gupta: So does it affect your realization or your margins with agglomeration?

Challa Srishant: Yes, if we supply agglomerated products to the customers, we are likely to get little higher margins.

Moderator: Thank you. The next question is from the line of Sagar Arya from White Oak Capital. Please go ahead.

Sagar Arya: Just a couple of questions from my side. You have given a guidance of Rs. 1,000 crores for domestic business out of this how much is from our own B2C brand?

Challa Srishant: For 100 crores I think we are targeting around 75 crores from our own brand.

Sagar Arya: And how much are we planned to reinvest into advertising and promotion this year?

Moderator: 100%. We have actually taken our projections that for the next 4 to 5 years this business is not going to contribute positively to the bottom line of the company.

Sagar Arya: So at what scale does it start contributing to the bottom line?

Challa Srishant: Until the point that we make to our growth with the segment we do not need that additional contribution from the domestic team. So the mandate given to them also for the next couple of years we just focus on top line growth because they are going to reinvest everything in building the brand more aggressively.

Sagar Arya: Understood and when you spoke about introducing more product categories and creating a new category in itself, are you talking about, is this for your own Continental brand or is this for other private labels as well?

Challa Srishant: No, it is for a Continental brand. We already have these products for a B2B segment as I mentioned that we are doing 3,000 products to customers across the world, but in India we have only two products that we are selling and chicory coffee blend and one pure coffee blend. If you want to introduce the wider range of products but would be appropriate for the Indian market. So we are also going through product pattern. There is national players they are now in this segments pre-mixes, three in one, institutional sales all these areas of the right products that can help us effectively.

Sagar Arya: Sir, what sort of capacity utilization in Vietnam currently?

Challa Srishant: In Vietnam this year we are projecting 80% utilization as opposed to 80% to 85% as opposed to last year about 70%.

Sagar Arya: When can we expect Brownfield expansion in Vietnam because I remember earlier you mentioned that when we reach 75% utilization in Vietnam then we will go for another expansion there?

Challa Srishant: Yes, for next financial year we are planning and going in for additional expansion. We wanted to do another 4000 tons expansion with a little bit of line balancing and the exact date of the expansion has not been frozen yet once we order the equipment we will have this thing, but it would be at next financial year.

Sagar Arya: And the investment required for this expansion be approximately $8 million. Sir, I understand that there is still over capacity in the industry currently, but have you seen at least a comparative intensity especially in spray dried reducing over the past 1 year. Sir just to repeat my question I wanted to understand the comparative dynamics in spray dried specifically currently even if you can throw some light on how freeze-dried the industry is operating because I believe there is more competition freeze-dried right now as compared to last year, so what are the dynamics there currently?

Challa Srishant: On spray-dried also the competition has eased out a little bit in this year compared to the previous year again because as I mentioned earlier one of the major plans have gone offline and they were in the spray and agglomerated space because their plans shutting down like this for easing our capacity, but there will be new plants that are getting build also on a constant basis. So both spray and freeze there competition as such is definitely going to be there now and in the future as well.

Moderator: The next question is from the line of Nitin Gosar from Invesco Mutual Fund. Please go ahead.

Nitin Gosar: Just wanted clarification you mentioned that in next 3 to 5 years the growth rate can still be at 10% on capacity or on volumes?

Challa Srishant: On volumes.

Nitin Gosar: That would mean we will be hitting our number like say 50,000 ton in four year or five year down the line?

Challa Srishant: Yes, that is correct.

Nitin Gosar: What does it mean in terms of market share today and then?

Challa Srishant: Market share wise today we will be at around maybe 6% or 7% in the market that may further increase to maybe around 9% or 10% by that time.

Nitin Gosar: Keeping in mind that the new capacity do not come up at that pace?

Challa Srishant: Exactly.

Moderator: The next question is from the line of Gagan Thareja from Kotak Investment Advisors. Please go ahead.

Gagan Thareja: On the domestic branded piece initially one would have thought that you are going in only for this valuable coffee, but now you increase basket of offerings to three in once and roast and ground, is it possible for you to give us some idea segment by segment of the market and the significant players in each of these segments and what could be your aspirations be in each of these categories maybe something about you know the business dynamics and procurements as well of the categories?

Challa Srishant: First thing first the instant coffee space is approximately around 1800 to 2000 crores and the three in one segment the premix segment is in the range of approximately 500 to 1000 crores because this is mostly in the institutional segment there is not much data available over here. At the roast and ground segment is also expected to be around another 500 to 1000 crores. This roast and ground segment today is primarily smaller regional players in south India all of them put together will come to this number, but what we are focusing on the existing products we are not restricting ourselves to the 1800 to 2000 crores market. We are focusing on the 3000 to 4000 crore entire coffee markets which is there in India. And in this segment, we will also feel that introducing new products like the three in one which is also soluble coffee by the way will help us reach our targets faster.

Now what are the numbers that we are likely to get we will only be able to tell you this exactly by the end of this year. This whole year it is only about products introduction. One ground reality which most people could already be aware of is that new product launches more than 90% sale when they are introduced in the market that is one of the reasons why we did not want to do things in very aggressive manner. It has taken us three years to systematically grow the market and establish the quality that gets accepted in the market that was our focus till now. When we are introducing new products also, we have done the necessary trial in the institutional segment first and now we want to introduce the same products into B2C segment.

Gagan Thareja: In the roast and ground market you indicated that it is more populated by smaller regional players I presume the likes of Nescafe and CCD put in there when coffee wending machines and supply way the roast and ground coffee I mean this could be an institutional model. I do not know how this sort of breaks up in to an institutional and then B2C, but would it be fair to presume that the brands in this segment are not as entrenched as they are in the instant coffee market and therefore it would be probably faster break for you in this market then in the other market?

Challa Srishant: So the markets that you are referring to the institutional segment where we are placing wending machines and earlier that is a lucrative market, that is the market where we go by volumes, but the margins are going to be very less. We are not counting this as a B2c segment at all. This will be part of institutional segment growth that we have projected. What we are saying is the same products that we are giving to this institution in the form of 1 kilo packs. We want to make it available in the form of single pack sachet so that people can actually have its convenience of getting a café experience at home at a fraction of the cost. So that is the concept which is going to be new in our country. So you can get flavored coffee, you can get a wider range of products available as a fraction of what we are paying in a coffee shop today. So that is the area that we want to focus on and there is no comparable data in the market today for the segment.

Gagan Thareja: For your guidance of 75 crores for the full year from your own brands given how the first quarter at July have panned out, you find yourself well on line to be able to achieve that?

Challa Srishant: Yes, as of now we are on track. So one good thing about having new team on board now is given us a pure guidance for the whole year for quarter one is 100% on track. For quarter two also like we have a review at the beginning and end of every quarter. So quarter two review also it has given us its projections and it is quite confident that the new product introduction we will be on track.

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

Nikhil Upadhyay: Most of the questions have been answered just one question on the new freeze-dried capacity and considering the pricing pressure which we are seeing in the market with new capacities coming up, what kind of utilizations levels we need to reach in order to be EBITDA breakeven in the new capacity, if you can just give some sense on how it works out for us?

Challa Srishant: Around 50% capacity we can reach in EBITDA breakeven with our plant and we are expecting to reach that in the first year itself.

Nikhil Upadhyay: And how would this scenario have changed since the time when we started the ideation of putting the capacity as to now in the last two years because I think the pricing itself has gone down, so probably was it 35 when we started ideation and now it is 50 or how has that scenario changed?

Challa Srishant: Initially when we started with the project that time the demand for freeze-dried also was much higher, but we knew that there were new capacities coming online. So, we had already factored that in. So, our planning from day 1 was 50% utilization in the first year second year closer to around 70%-75% and then gradually increasing from then onwards.

Nikhil Upadhyay: So largely we had already built in with this kind of a scenario before putting the money for the capacity?

Challa Srishant: Yes, because we were already aware of who was building what capacity is in the world. Now we have more clarity with respect to even 2020, the additional volumes that come online in 2020. So we have a projection in place until then.

Nikhil Upadhyay: Lastly when we say for the 75 crores of branded domestic business and you mentioned in the call that we are already present in Andhra Pradesh and Telangana and now we are looking at moving to Tamil Naidu and Karnataka and this 3 x growth in the branded business a large part would it be driven by extension in new markets or how is the market panning out from counters there we are already present over the last one and half year?

Challa Srishant: So the areas that we are already present we are seeing lot of repeat sales and all and the demands has gone up to such an extent that now it is easier for us to go to new supermarket. Last year we had a challenge if you want to go to new supermarket you have to pay a listing fees, you have to negotiate with them, the negotiation process which takes two, three months and then finally we used to place our product. Today because of the advertising and other promotions that we are doing and seeing the faster off take that is there in the market. We are able to now place our products without the listing fee in supermarkets as well in larger chains as well. So that is the major advantage that we have now. By virtue of becoming a little bit more recognized than before. So by placing ourselves in new areas also we are expecting our growth projections to be achieved.

Nikhil Upadhyay: Last sir on Switzerland if I look at last year based on our annual report there was good improvement in the sales which basically brought us to EBITA breakeven, how should we understand the scenario where for this business over the next three to five years do we believe that this kind of improvement can sustain or what is the roadmap for that facility over three to five years?

Challa Srishant: As far as Switzerland is concerned last year we had appointed a new Swiss director over there. He is a local person who we have been associated with for many years. So when he took on his role as managing director in Swiss facility. One of the mandate given was first to breakeven and then to focus on growth year-on-year. Breaking even last year was a very big challenge as you must have seen from our past records and history as well there were numerous issues that we were facing with the Swiss government and getting our product in place was becoming a challenge. What he has done is he had started negotiating with the Swiss government for coming up with the solution for our unit. He has come up with a solution but in the meantime he has also focused on sales, he has added new customers in Switzerland which is enabling us to get this additional profitability through Switzerland. Even for this year he has managed to get some new customers over there.

In the future also in fact he is also going to be introducing some of our brands within Switzerland. This is something that we wanted to do it in a very low-key manner. As we are not intending to advertise or promote or do anything else, but institutional segment Hotels and these areas then currently are restricted to buying all their coffee products from one supplier in Switzerland. We want to become the alterative supplier for everyone which is why we have asked him to take this forward and by having the local person, the local place it became that much easier for us to introduce our products from last year. This year once the new branded or the new rebranded products are introduced for next month. He is going to introduce these new products in Switzerland market as well.

Nikhil Upadhyay: Which means just one clarification the structural issue which we had in Switzerland that is of manufacturing and packaging has to be done in Switzerland and then only we can sell in that area, are we able to look at that structural issue in order to scale up now or do we have a solution to that structural issue with the government?

Challa Srishant: The structural issue the law still remains the same. One of the solutions was it given for ourselves how we have an export-oriented unit in India. Base at our plant they are willing to give us as an export bonded zone, but provided we do a certain minimum volume so this has become a chicken and egg problem we are telling them unless you give us the preferred status we cannot achieve the required volume. So that is the negotiation that he is currently doing. Hopefully in the next couple of months he should finalize that and implement it as well.

Nikhil Upadhyay: So there is a significant progress which is done.

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

Akhil Parekh: You mentioned that we are expecting 100 crores of sales in domestic business of which 75 would be from the branded business? How much we have clocked approximately for this quarter Q1 19?

Challa Srishant: This quarter I think out of 17 crores or so is what we have done in the domestic business out of which approximately 13 crores will be the branded B2C business.

Akhil Parekh: Last time when we had met you had mentioned that we might try and utilize YouTube channel for branding our continental coffee brands and you guys were working on some kind of videos, have you made any progress on it?

Challa Srishant: We have made a couple of videos. I think one video was launched about two weeks ago, but we are still in the process of making the video. We wanted to introduce the video along with the brand launch as such. So next month when we are planning introducing these products so the videos and everything and all would have introduced at the same time.

Akhil Parekh: So during our premix launch you are saying we might see our videos.

Challa Srishant: Not only remix including roast and ground coffee it will be a wider basket of products.

Akhil Parekh: And how much would be the average package size for this new launch we are doing?

Challa Srishant: The premixes will be about 18 grams in a sachet where it will give you one cup of coffee that is the smaller pack size and larger packs were roast and ground we have even 200 to 250 gram packs which are available.

Akhil Parekh: And the pricing you would be able to tell it now how much you are doing broadly?

Challa Srishant: Not right now let us make that part of the official launch.

Akhil Parekh: Just one last question with this agglomeration at Vietnam so we are expecting around 15% of volume growth at Vietnam. So do we expect full utilization of agglo unit at Vietnam like 4000 tons by FY19?

Challa Srishant: Full utilization of agglo is not possible so quickly that we may take a couple of years to come. Agglomeration is just another product that we are another product format that we are giving. It is the primary demand is still there in spray dried coffee only. Agglomeration it may take maybe 4 or 5 years to reach full year utilization.

Akhil Parekh: So maybe like around 50% we can expect you are saying?

Challa Srishant: No, I am saying that over the next couple of years like last year also we have done hardly about maybe 15%, 20%. So that 15%, 20% may go up to 30%, 35% this year. So about 10%, 15% incremental growth is likely to be there at the year and eventually we will reach that full utilization maybe about 4, 5 years down the line.

Moderator: The next question is from the line of Lakshminarayana Ganti from SBICAP Securities. Please go ahead.

Lakshminarayana Ganti: Most of my questions are answered just wanted to prick your brains on one comment you made earlier saying that the long term growth rates could come down to single digit or something, what I wanted to understand is you have a considerable amount of bulk business going and over a period of time the mix changes as and when the product are launched into the markets and they find acceptance that becomes more like a steady business for you, more in terms of annuity sales and better margin product, so that comment on the volume growth would that necessarily imply the same thing for the bottom line or would you be consistently migrating your customers up the value chain and so on just wanted to hear your thoughts on that?

Challla Srishant: One thing is as far as customers are concerned that want what they want. It is not us who can actually convince them to migrate up or down the value chains. Each customer of us has their own branded strategy. I can just give you an example there is one particular customer in Africa that we have. Initially he came to us with proposition saying that he wanted 100% Arabica coffee with plantation. Over the years every years he has consistently reduced his quality. First on Arabica he has converted to Arabica Robusta blend from Arabica to just 100% Robusta then through Chicory coffee blend. And as far as the brand volumes are concerned these volumes are still growing year-on-year their volumes are growing. So they change their strategy based on their market scenarios there will be numerous dynamics that we do not go into. What we do is that we tell the customers this is the range of products that we can provide so you decide what strategy would work for you and go to that particular market that has been our strength till now.

So going forward I am assuming that yes our product mix will just keep increasing year-on-year, but after we reach a 45,000 or 50,000 ton production capacity growing at the rate of 6000 ton per year is going to be a major challenge for us also. Today, if you look at Nestle also we are not growing at the rate of more than a single-digit rate when it comes to Coffee. If you are looking at number two player in the world it is the same story for them as well. Once you reach a certain volume level you cannot sustain the kind of growth on volumes terms year-on-year, but since we want to maintain our bottom-line growth year-on-year, we are focusing on the branded sale now itself. If we have a certain volume base we will place within the next three, four years by the time there is a decline in volume growth in the B2B segment, we are likely to see a positive contribution from the B2C segment in our balance sheet.

Lakshminarayana Ganti: My only thing was you also has this bulk business which is low margin and assuming when you scale to say 50,000 ton per annum, some of them would move from the customer sourcing through the bulk resellers to directly moving to you assuming the volume scale and then the products also would have clicked in the market or whatever it is and then there is a leeway in terms of pricing. So, if there are limitations to the volume through expansion scaling strategy, would that be partly offset by pricing or the mix changing is the question especially given the fact that you are launching freeze-dried which I am told is better margin.

Challa Srishant: One thing that to keep in mind is our product mix is more or less going to remain the same. If you look at our capability also we have 14,000 tons plus 10,000 that is 24,000 tons of spray dried capacity, but we have only 6000 tons of freeze-dried in place right now. So, we are increasing the 6000 to 11,000 with this additional 5,000 tons, the freeze-dried capacity is increasing. Our product mix if you look at it broadly remains the same it has remained the same in the past and it is likely to remain the same in the future as well. Just today we are growing the specialty business and the new product mixes, we will also grow the volume business in the low margin business as well to improve on efficiency. We are not looking at a significant change in product mix anytime in the near future.

Moderator: The next question is from the line of Dhruv Bhatia from AUM Fund Advisors. Please go ahead.

Dhruv Bhatia: Could you just talk about the EBITDA per ton trend in the past as well as going forward, you have talked about for the next four to five years you are looking at 10% CAGR volume growth, will you likely maintain the same type of EBITDA per ton because of the capacity that is there in the system that the pricing pressures will lead to lower profitability?

Challa Srishant: First thing first, EBITDA per ton basis would be an incorrect way of looking at our company because of the product mix that we are currently doing. There are several times customers change the product mix during the year as well. We have seen this happened in the past as well. What we do is we plan our volumes and each customer wise we know what margins we have so it becomes easier for us to predict at least a year in advance based on our business model. What we are doing today is we are taking orders at least a year in advance. We have only about maybe 20% to 30% of the business that we end up taking during the year. We do have customers who come in with maybe couple of months' notice as well, but this is again on an ongoing basis because we have the past record of with us so it becomes easier for us to project and predict the growth in that particular financial year. What we cannot predict, or project is on a quarterly basis. Sometimes customers may ask for certain postponements of premium products dispatches to a different quarter. In such cases, we will not be able to reflect the profitability in that particular quarter. What we can be sure about is that in that particular financial year that particular contract will get executed because just how we entered into contracts with our customers.

Moderator: The next question is from the line of Anand Jain an Individual Investor. Please go ahead.

Anand Jain: One question what has been our advertising and marketing budget for this quarter and what was it for the last quarter I mean Q1 last year and how do we see a changing YOY basis because we are looking for a larger retail footprint how do we see that on a YOY basis?

Challa Srishant: So, on a year-on-year basis this year we are projecting almost about 30% gross margin that is about 30 crores plus 10 crores from the parent company. So, about the 40 crores is the amount that we have allocated for this year in building the brand including team cost, offers and everything else. Next year onwards also the only difference between this year and next year is going to be this year we are expecting the operations to become self-sustaining as in there would not be any additional support that require from the parent company like we have given last year and this year. Next year onwards we will not have to provide any additional support to the domestic team.

Anand Jain: Second question that I have just I am sorry the cost of repetitions in the last concall you had mentioned that because of excess capacity on the freeze-dried we are looking at some kind of margin compression in that sense, so two questions on this a) is that most of our freeze-dried capacity is in terms of very, specialized blends and we own the IP for those. So, they would not be any margin compression there would that be right?

Challa Srishant: Yes, for an existing products we would not have any margin and compression, but for the new products that we will be introducing we will be competing against existing players that were already there in the market.

Anand Jain: So it is not for the current sales that has happened but only for the sales that we are going to look up from here on?

Challa Srishant: But in freeze-dried also we have a certain portion of the business which will be volume business where you have lower margins by default.

Anand Jain: So, on the freeze-dried we have a volume-based business.

Challa Srishant: Of course, yes.

Moderator: The next question is from the line of Dhruv Bhatia from AUM Fund Advisors. Please go ahead.

Dhruv Bhatia: Just continuing the earlier question, from a long-term prospective how do you see this period of times domestic market as you had said to be dependent on the other two competitors, but on the international side do we see any accretion in value-addition or any other way where EBITDA per ton whereby you increase capacity, any other lever you should look at more premium brands, better quality mix, maybe the product mix anything like that at all?

Challa Srishant: Actually, we are because we are increasing our product mix in-house we are offering new products, we are trying to get new customers as well. Usually, it is a bigger brands who want more premium products in their portfolio and we offer these products to them. When we offer a new product it usually starts with lower volumes especially if we are creating a new product category and this year we will actually be the first ones in the world to create new products categories in instant coffee. So, these are things the brands they have to do the marketing depending on the off take that they get the order with us also we will increase. So, we are factoring in all these thing when we are giving our projections. The only area where we can see that there is a potential margin expansion for our international business is if we introduce our branded products outside the country that is happening in a very organic manner right now. Thanks to our Swiss Director is introducing our products currently in Switzerland in UK as well we will be introducing through our marketing collaborator so there are other geographies that we will be introducing a branded products without any significant spend. So, we are focusing on institutions segments and all but a margins are likely to be higher because it is our own brand.

Dhruv Bhatia: And order backlog that you showed in the pipeline does that also reflect a higher level of EBITDA per ton basis you have been doing in the past, do you see a trend whether this is increasing, or you think this is more likely to be in the next three years.

Challa Srishant: It is more or less constant our EBITDA per ton basis on an average basis is more or less constant. Our strategy for the last 20-odd years has been constantly keep the margins as it is. We do not renegotiate margins with our customers. We give that kind of transparency to our customers when it comes to pricing and that also enables us to be very competitive in the market. The drawback of this model is that the only way that you can grow is through volume growth that is why we have always focused on volume growth in the company. The reason why we are growing into the domestic branded business today is because we know that the B2B business is not sustainable beyond a certain point in time. There will be growth, but at the same pace that was there in the past it is not reasonable to expect the same.

Moderator: We have no questions queue. I now hand over to Mr. Abhishek Navalgund for closing comments.

Abhishek Navalgund: Thank you to all the participants and of course management of CCL products for answering all the questions patiently as always. So, I will hand over the call to you sir for your closing remarks.

Challa Srishant: I would like to thank all the participants for taking part in this conference call. Just one point that I was supposed to mention in the opening remarks I thought let me just mention in our closing remarks. Our previous CFO Mr. K. V. L. N. Sarma has been appointed as the COO in the company. So, from next Conference Call onwards he might be joining us as well. Thank you.

Moderator: Thank you. On behalf of Nirmal Bang Equities that concludes this conference. Thank you for joining us and you may now disconnect your lines.