

“Nestlé India - Analyst Conference Call”

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Himanshu Manglik: Good evening, ladies and gentlemen this is Himanshu Manglik. Welcome to the Nestlé India Call. I understand from the system that we have over 60 analysts who are now connected on the call. So as you can see this is joint pin. I hope you have received the press release that we sent out to you earlier in the evening on the quarter two results. We did not want the Analyst Meet which would happen when it does but Shobinder thought he would discuss with you some of the issue that you may have on the press release.

I have here with me Mr. Duggal; Sanjay Khajuria; Kamal Kedia and of course me, and we might have some more joining in our way. The length of this conference call will be about 30 minutes and for the first ten minutes or so Mr. Duggal will discuss issues and then we will be open for question and answers. However, there are just a few ground rules that we will need to follow, while Mr. Duggal is talking everyone else will be on mute mode. So you will not be able to talk to us only listen to what is being said. When I announce that we can take the Q&A and if you have a question, then you will need to press '*', '1' to login your question and to enable you to ask the question I will have to unmute you. If during the call you find that your question has already been answered you can press '*', '2' to remove your question from the log. If you have difficulty on your connection at any time please press '*', '0' and operator will try and reconnect you. And just one last point before we start for governance purposes, this call is being recorded and you need to know that.

Ladies and gentlemen, I now hand over to Shobinder Duggal.

Shobinder Duggal: Thank you, Himanshu. Good evening ladies and gentlemen and very warm welcome to this analyst call from Nestlé India following the results of the quarter ended June 2015 which we have just released about an hour and half ago. I wonder if you got a chance to go through them but I hope you did. The purpose of this call needs to be defined at the outset and the purpose of this call is to give you a better understanding of how the MAGGI Noodles issue has impacted the results for the quarter. This call is not and I repeat not being made to present the complete analysis of the results as it is done in regular Analyst Meets conducted from time to time.

I will start by reading the press release which has just been issued by the Company and I am reading the one which is the non-statutory one which was sent to the journalist which speaks about Nestlé India quarter two 2015 committed to providing safe products will continue to engage with authorities to bring MAGGI Noodles back.

Net sales for the quarter of 1,933.8 crores profit before CSR and exceptional items is 333.6 crores. The exceptional item which is largely on account of rather exclusively on account of the MAGGI Noodles issue is 451.6 crores. Consequently, there is a loss for the quarter for 64.4 crores. The Board of Directors of Nestlé India met today at Nestlé house and approved the results for quarter two 2015. Commenting on the results Mr. Suresh Narayanan, Managing Director (Designate) of Nestlé India said this quarter has been extremely challenging for the Company. Nestlé India would like to reassure consumers that our products are safe. Consumers trust is and will always remain the corner stone of Nestlé.

Nestlé India is making all efforts and will continue to engage with authorities to bring MAGGI Noodles back on the shelves. The Company was faced with a very unusual situation during the quarter and the financial results for the quarter are therefore not comparable to previous year's periods and I would like you to underline this.

The unaudited financial results for the second quarter along with appropriate explanations are enclosed which we are referring here to statutory press release in the SEBI format. Net sales for the quarter has decreased by 20.1% largely due to the impact of the MAGGI Noodles issue. Net domestic sales decrease by 20.6%. The MAGGI issue disrupted business as you all know in addition, to loss of sales from the business disruption net sales worth Rs. 288.4 crores has been reversed during the quarter in relation to MAGGI Noodles stocks already sold and withdrawn from the market. The exceptional item relates to estimates of loss on account of stocks including incidental cost thereto and other cost incurred and are dealt with in line with the appropriate accounting standards.

I will delve on some of these points in a little while. Now, please allow me to read the note number one, to the statutory press release which reads out as follows:

Results for the quarter have been impacted by the MAGGI Noodles issue. The trust of its consumer and the safety and quality of its products is Nestlé's foremost priority. Unfortunately recent developments and growing concerns about the product had led to an environment of confusion for the consumers to such an extent that the Company on 5th June, 2015 decided to take the products temporarily off the shelves despite the product being safe. This was done to reassure the consumers that their trust has always been of utmost importance for the Company and to maintain the continued patronage for Company's products. The Food Safety and Standards Authority of India issued a recall order later on the same day i.e. 5th June, 2015 asking the Company to recall MAGGI Noodles, stop further manufacture and comply with other directions.

In line with the instructions from the authorities and in keeping with the environmental considerations the withdrawn products are being sent for high temperature thermal destruction and the Company has suspended further manufacturing of MAGGI Noodles. The Company has conducted extensive additional testing of 1,676 samples of MAGGI Noodles at its own accredited laboratory in India and affiliate accredited laboratory abroad complemented by 1,100 samples tested at external accredited laboratories in India and abroad. All results confirm lead levels are well below the regulatory limits. Furthermore, several other countries have found MAGGI Noodles safe after testing samples of the product exported out of India.

With a view to resolving the MAGGI Noodles issue the Company approached the Hon'ble Bombay High Court raising issues of interpretation of Food Safety and Standards 2011 while seeking judicial review of the order dated 5th June, 2015 passed by FSSAI and order dated 6th June, 2015 passed by the Commissioner of Food Safety Maharashtra. Proceedings in the Hon'ble Bombay High Court are in progress.

Net sales worth Rs.2,883.8 million have been reversed during the quarter in relation to MAGGI Noodles stock being withdrawn from trade partners and market. The exceptional item relates to estimates of loss on account of stocks withdrawn including incidental cost thereto and other related cost incurred exclusively in the ordinary course of Company's business dealt with in line with accounting standard AS2 on valuation of inventories and accounting standard AS5 net profit or loss for the period prior period items and changes in accounting policies.

Note two, result for the quarter half year 30th June, 2015 are not comparable with the results of the corresponding periods. So you see that the financial results have been impacted in two main areas a) sales and b) exceptional items. I may remind you that lower sales also result in adverse absorption of fixed overheads and I would like you to bear this in mind as this would have an impact generally on the margins of the Company depending on what the sales going forward would be as the fixed cost is carrying on which was there up for the MAGGI Noodles manufacturing business.

We announced the withdrawal of MAGGI Noodles on June 5th, 2015, Sales and production of MAGGI Noodles were stopped thereafter. We started withdrawing stocks from the market and trade partners while minor quantities may still come back from the far flung markets. The sales returns of Rs.2,884 million representing close to 23,000 tonnes accounted for in June quarter and are adequately accounted.. I repeat we may have minor quantities coming from here and there but the Company does believe that this a very fair estimate at this point in time of the returns which are coming through.

Just as a reminder in 2014, we had sold close to 224,000 tons of MAGGI Noodles at a sales value close to 25 billion which represented close to a quarter of the sales of the Company. This is only an information for you because we do not disclose this in our Annual Report and we will not disclose that as we will not change our disclosure policies on the Annual Report but I thought that this was important for you to have a little insight of what is the magnitude of this business and how it could impact the financials for your simulations. The exceptional item relates to three types of cost. One is the cost of MAGGI Noodles stock. Second is the incidental cost in relation to the withdrawal and destruction. And three, there are other costs.

The cost of MAGGI Noodles stock is simply the cost of stocks which were manufactured by the Company and either was sold or were in the warehouses of the Company. This cost was not triggered by any of the events which we have described above but because of order of ban on Maggi Noodles. Normally this is the same cost which we would have incurred and this would be the normal course of business and we would have realized sales out of it. Second part is that the stocks which were withdrawn from the various trade partners and the market and the retailers and so on so forth had to be brought back to our distributors and then from the distributors back to our distribution center and then from the distributors centers to the incineration sites where the stocks are being incinerated.

So this incidental cost in relation to withdrawal is more or less reflecting this reverse transportation as well as the handling and storage cost as well as the destruction charges being

paid to the Company engaged in this exercise. Naturally when this event happened there were a number of contracts which we had with third-parties, including suppliers, vendors etc. which had to be seen in the context of stock obsolescence, in the context of deliveries and so on and so forth. So those costs are also included in this Rs. 4.5 billion which we are talking about Rs. 450 crores around. These costs also include some other cost like the lab testing charges. We have just talked about 1700 samples being tested so all those cost have also been built into this then there were naturally some administrative cost in relation to this MAGGI Noodles issue and so on and so forth. I think it is interesting to note also that there is a certain amount of cost which in the normal course would have been in the cost of materials or what would you say part profit from operations. But because of accounting standard 5 and accounting standard 2 we had to reclassify these cost from the normal items into the exceptional item so to that extent there is an impact on the operating margins of the Company if I may say so that they are a little bit over stated if you see it from a very traditional way but unfortunately or fortunately we have to follow the accounting standards in the reporting and that is why have we have pulled that cost out from those lines and brought them down to the exceptional item.

Some of you have been writing to the Company asking when we will resume the MAGGI Noodles business. Since the court proceedings are in progress it is not appropriate for us to comment on the matter. However, we continue to cooperate and engage with the authorities to bring MAGGI Noodles back to the sales, as soon as we can. I think in the interest of time I am going to stop here and I will give back the floor to Himanshu now to run the Q&A. Thank you very much.

Himanshu Manglik: Thank you, Shobinder. We will start the question and answer now. I am going to open the section. Okay, we have some question coming in and I am going to start unmuting them one by one. Nitin from Societe Generale.

Nitin Mathur: Just on the subject, any further expected losses and what could be the nature of those losses, regarding the MAGGI matter?

Shobinder Duggal: You are referring to the cost which we have reflected in the exceptional item in the press release?

Nitin Mathur: That is right, yes.

Shobinder Duggal: Yes, okay. Thanks, Nitin I think it is a good question because this is what there was a lot of debate on this point in the Audit Committee meeting as well today, frankly speaking Nitin, what we have tried to do is that we have looked at all the touch points and try to access the situation where all could the cost be sitting because as you know these kind of situations are very unusual or they will happen once in a life time of the Company hopefully. So, there is no systematic way of capturing them other than applying your mind and trying to see where are the touch points and then trying to estimate those cost. We believe that we have done a fairly extensive job around that area and the Chairman of the Audit Committee actually mentioned towards the end saying that I am really impressed the way you guys have gone into the details

to figure out where these cost be sitting. So we believe that we have done a fair job but having said that I would not be surprised with some items come a little here or come a little there, there could be a little plus or a little minus. But from materiality standpoint I would say that I feel relatively okay that we got all the big fishes there. So I do not expect a major surprise so to say.

Nitin Mathur: Right, thanks that answers my question. Second, did you see any rub off effect in your other brands?

Shobinder Duggal: Well yes, Nitin I think let's face it. I think you will be able to access it yourself. The MAGGI brand is being hurt with whatever happened and that was one of the reasons why we took the decision to temporarily take it off the shelves so that we do not have a kind of mistrust or a lack of confidence of the MAGGI consumers. So ultimately it has a rub-off effect but it is all intellectual to say how much is it? Can I say all of that is due to this? It is very difficult but I can confirm yes, there has been an impact on the MAGGI brand. So other product sales have been impacted.

Himanshu Manglik: We have Chitrangda Kapur with her question. Go ahead please Chitrangda.

Chitrangda Kapur: One, could you please repeat the tonnage that you had mentioned during your opening remarks to give us an idea about stimulation. How much was that we had sold about same quarter last year? And it was 25 billion I believe was the amount and in tonnage I do not remember sir.

Shobinder Duggal: What I said was that last year for the full year 2014 we sold around 2,24,000 tonnes in the full year. I did not talk about specifically of a quarter. As you know that we do not report these figures by quarters and we do not even report it in our Annual Report but I thought I wanted to give you a perspective of what is the size of the business and the value of Rs. 25 billion which is Rs. 2,500 Crore, right that is the size for 2014. Is that clear to you?

Chitrangda Kapur: Yes.

Shobinder Duggal: Chitrangda, this is only to give you a little thinking through because I know after this you guys will all be mostly sitting on spread sheets and trying to do all sorts of permutations and combinations and I thought this information might be relevant for you but more than that I am not trying to say anything we are going to come back in two weeks' time or we are going to come back in six months or we are going to come back and we will sell this and we will sell that. I just want to make that very very clear. At this point, we are not discussing that chapter at all because the matter is in the court and we cannot discuss that, it is only to give you a little bit feel for the size of the business and I hope that is clear.

Chitrangda Kapur: I appreciate that sir. Actually, I was not asking from that perspective I understand the legalities of the issue. What I am trying to understand here is during this MAGGI fiasco there was also a small news article which came out with regards to your infant food also going under you know there was adulterants which you found there. So now for us it is very difficult to

assess how a situation like this is handled in such a large scale. So what we are trying to understand is not the numbers per se basically what does the Company like Nestlé do during those times to do a reputation damage control? Just a broad idea so that we get to know what exactly is happening because fairly speaking we have only clue to what we are reading in new paper reports etc..

Shobinder Duggal: I am afraid, I have put a caveat in the beginning that this analyst call is basically to discuss the results of this quarter and in particular the MAGGI Noodles issue. We are not taking this call to do a full review of all the points which you or anyone else would like to make, otherwise we will run out of time. As I said, my whole objective is that I articulate some of these things because they are complex for specially those people who may not be Chartered Accountants in the community there and I wanted to bring clarity of the treatment of the costs to everyone, so that there is same level of understanding when you go to do your sensitivity analysis and the purpose is definitely not now to discuss this and that because tomorrow there will be a newspaper item or something else and then day after there will be something else, , we just do not want to get into all that. But yes, when we meet for the Analyst Meet in due course of time at that stage you are more than welcome to ask any such questions and we will address them adequately. But today we want to focus on this and close if you do not mind.

Chitragda Kapur: Okay. One parting shot in that case, MAGGI sales per quarter is it distributed evenly or is it a particular quarter which has a higher MAGGI sale that is it.

Shobinder Duggal: No, I am sorry that's why we have given you the annualized figures and I do not think there are...

Chitragda Kapur: No, I am asking quarter wise. Is there fluctuations which happens per quarter?

Shobinder Duggal: There could be but this is certainly not an ice cream or a soft drink that it will have huge swings but then there will be quarters you will have a little here and a little there and then one quarter you run a consumer promotions so sales go this way and another quarter you do not do something and something else happens like competitors activities are intensified so on and so forth. So I think by and large I just want to make the only point to you is that this is not a seasonal product, per se sales cannot necessarily be exactly the same in every quarter.

Himanshu Manglik: The next person in queue Abneesh Roy from Edelweiss.

Abneesh Roy: Sir, two quick questions. One is staff cost flattish and down quarter-on-quarter so have you managed it because of temporary employees who are related to MAGGI, those are not required. And similarly on other expenditure that is also down 10% Y-o-Y, 18% quarter-on-quarter.

Shobinder Duggal: Yes Abneesh, your question relates to employee benefit expense and other expense?

Abneesh Roy: Yes.

Shobinder Duggal: Okay. Abneesh, this is the reason why I eluded to Accounting Standard 5 and Accounting Standard 2. Please remember one thing that as per Accounting Standard 2 when we value our inventories we have to take the total cost of production which means there is a variable cost which includes material, labour, energy cost, etc. etc. and then there is a cost of overheads of the factory depreciation and so on so forth. So these costs are in the balance sheet reflecting the inventories. When they are taken off and are being incinerated the entire cost moves from there into the exceptional item. So to a certain extent some of these costs which you see here in these lines they were in the cost of the inventories which have moved away from those lines and are fitting in the exceptional item. And going forward depending on when the business comes up , what is the size of the business what is the growth of other business etc. etc. these cost definitely will remain there till the time we take some decisions not to have those cost but today this is a recurring cost. So the people who are in the factory they are still there. So going in the next quarter, this will not be an exceptional cost, this will be treated as a cost above operating profit. And that is what I was trying to mention when I refer to Accounting Standard 5 and Accounting Standard 2.

Abneesh Roy: Sir, you said MAGGI brand impacted other MAGGI products also for example soup, pasta, etc. but were your milk chocolates and beverages also indirectly impacted?

Shobinder Duggal: See Abneesh, let us face it. As I said that I am not going to do a business review here but I can just try to go give you one sense that this whole recall activity has been a mammoth task if not I would say it is actually a herculean task not even mammoth task. There is something like 14 incineration sites which have been used through five cement companies. There are about 800 people who were engaged in this a lot of them were from sales if not most of them. There was something like 11,000 vehicles trips, there were some 34 transporters, there were some 14 additional warehouses, there was some 2 lakh of square feet hired to store Maggi Noodles. So you will appreciate that when you are under an order to withdraw even though you may have announced the withdrawal before the order you have to go through this process and if the sales team is engaged here there will be implications on the sales during that period. How much of it is because of the MAGGI issue etc. I would say it is a little tricky to decompose that. But yes, this was a very unusual situation but I do not want at this stage to reflect on how my business is doing and so on so forth again otherwise we will not give enough opportunity to others to ask the question relating to the cost which is built into this quarter.

Abneesh Roy: Sure, sir. One last one sir, new snacks there were media article. I understand without approval from FSSAI you cannot launch new snacks, right so....

Shobinder Duggal: Sir, no comments because we have not seen that article and I suggest that the best way as I said, that I do not want to go beyond the scope of my discussion of this analyst call but frankly speaking we see a lot of articles and we do not know from where they come etc. So it will become like endless debate, this article and then what is your response?. I think that is media thing and maybe if you wish to know more perhaps you could go back to journalist and try to figure out the source of that. That might be better because this way you will go around circles.

- Abneesh Roy:** Sir one last question on MAGGI Noodles...
- Shobinder Duggal:** Every time you ask question Abneesh you tell me this is the last one. So I hope this is the last one actually.
- Abneesh Roy:** Yes Sir, if you see your numbers 224,000 ton. Sir last year if you see a 100 gram of MAGGI Noodles was around Rs.13-Rs.14. So if I do 224,000 into that 14 it comes to around 3,000 crores versus the 2,500 crores you have mentioned there will be even the higher variant like Atta so, I am not getting into that so, why there is a gap of around 500 crores?
- Shobinder Duggal:** See Abneesh, it is not only Noodles but if you pay for any product in the shopkeeper let's take a bread or whatever you pay Rs.20 to buy a bread or Rs.50 to buy a bread. That Rs.50 is not booked as sales in the bread seller Company. There is a lot of dealer margin, distributor margin and this thing, that thing, taxes etc. etc. so the net sales which gets registered in the Company are always lower than what the evaluation would be based on the printed price on the product.
- Himanshu Manglik:** Thanks, Abneesh. The next person for question is Sunita Sachdev from UBS.
- Sunita Sachdev:** I realize that you mention that you did not want to delve into the other businesses to ensure that this call gets over quickly and it is only because of...
- Shobinder Duggal:** No, I do not want close this call quickly but I want to focus on this issue because this is really important for your community so if we go to the other areas this will go for hours and we have other things to do and you have other things to do because the results are just being announced and people are expecting reports from you.
- Sunita Sachdev:** Thank you so much. No but this is a kind of actually MAGGI question. You have a 340 basis points gross margin expansion. Now, we also know that commodities have been falling now how much is this because of revenue mix improvement because MAGGI is not there and how much it is because of commodity declining now this is apart MAGGI because MAGGI is not there and that is why the gross margin has gone up.
- Shobinder Duggal:** Where are you comparing your margins, can you please tell me that? At which level are you comparing on the press release?
- Sunita Sachdev:** Gross margin.
- Shobinder Duggal:** What do you mean by gross margin?
- Sunita Sachdev:** Just netting out only the raw material.
- Shobinder Duggal:** Okay, Sunita, if I may say so kindly do not apply that methodology just taking the cost of materials out. If you want to do that you rather would take all the variable cost which is not present here. So trying to get to those conclusions from these accounts is not correct. Also for the reasons which I just explained to Abneesh that there is some cost which has moved out

from an accounting standpoint from under the header of other expenses to exceptional item to comply with the Accounting Standard. So, if you try to draw some conclusions by doing margin analysis from there, they may lead you to some absurd results and I would not like that to happen. All I can say is that fairly good level of looking at it is the profit from operations before other income, finance cost, corporate social responsibility expense, and exceptional item. Here, if you see that actually the reported margins have moved from 17.5 is that right? That is the figure 17.5 to 16.7, okay. I would say in the given situation this is a better reflection to go rather than go for the gross margin. Now, I think it is important that this is what I said before that the 16.7 has the benefit of some cost which has moved from operational cost to exceptional item which in the coming quarters will come back above the line and it will all depend on what the growth of the other categories, when do we come back with the Noodles so the absorption of that will depend on the quantum of sales in the following quarter. There is some cost which has moved to exceptional item but I do not think I would let you assume that the margin improvement has happened because more or less Noodles will have about one or two weeks of sales in it effectively after the withdrawal it is not really I would not endorse what you are saying. I would refrain you from getting into that analysis at this particular moment. Maybe when we meet at the Analyst Meet we can go a little bit perhaps more in detail.

Himanshu Manglik: Thank you, Sunita. Next question in queue Anand Shah from Kotak.

Anand Shah: Just a very quick one reversal of sale is completely sitting in the extra ordinary items, right?

Shobinder Duggal: No, reversal of sales are sitting in sales, this is precisely the reason why I am making this call. We were selling Noodles in April, we were selling Noodles in May and we were selling Noodles till 4th of June. The whole episode started 5th onwards and therefore, we have taken the stocks back which we have sold in April and May. For all practical purposes there is very little effective sales of Noodles in this quarter maybe a one or two weeks of sales something like that ball park it could be ten days it could be 15 days something like. So the sales value is in the sales. Whatever I have taken back is netted from sales like any other sales return. The cost of that stock which came back which unfortunately became zero value because of the various directions from authorities etc etc. that is sitting in the exceptional item and I may please remind you this is not an extraordinary item this is an exceptional item and there is a big difference between an exceptional item and an extraordinary item.

Anand Shah: Fair enough. So that is the cost of inventory there?

Shobinder Duggal: Yes, absolutely the inventory cost is in the exceptional item like any other inventory which was at the factory or at the DC, etc.

Himanshu Manglik: Next person Percy Panthaki from India Infoline.

Percy Panthaki: Sir a few weeks back there was a press release or something from your side saying that the loss on account of this ruling by FSSAI is 320 crore. Now you have 450 crores of exceptional so how do I reconcile these two figures?

Shobinder Duggal: I am going to read out the press statement which was given to the stock exchange on 15th of June. Do you have it in front of you?

Percy Panthaki: No, sir I do not.

Shobinder Duggal: Okay, then let's read the statement together and let's analyze it together and then we will ask you this question whether trying to make an attempt of reconciliation of any benefit or not. So I am reading out,. "As already announced we are in the process of withdrawing MAGGI Noodle stock from the market and destroying it. The estimated sales value of the stock in the market including those with our trade partners is around 210 crores, against this 210 crores we have got 288 crores" and this was on 15th of June and we are sitting on 29th of July. "In addition there were MAGGI Noodles and related materials in our factories and distribution centers, when the withdrawal was announced, and the estimated value of these is around 110 crores", this figure of 110 crores now is 165 crores around. Again, we were on 15th of June and we are on 29th of July and it is a dynamic situation. Then we say, please hear this carefully, "these are broad estimates because it is impossible to calculate the final figures while the withdrawal is taking place. There will be additional cost to take into account for example bringing stock from the market, transporting the stock to the destruction points, destruction cost, etc., the final figure will have to be confirmed at a later date. The above and other unforeseen cost associated with this withdrawal will be dealt with in line with the applicable Accounting Standards at the time of announcing the financial results on due dates." So if I may say so with due respect, a lot of people have added up the two figures and put as 320, but unfortunately that was perhaps a misinterpretation of the reading of the figures because one was the sales value and other was the estimate cost of those inventories. So if you want to compare you have to compare is the Rs. 210 Crore with the Rs. 288 Crore and then the Rs. 110 Crore. I have given you the comparative figure of that it's around Rs. 165 Crore but then there were other costs which were not mentioned at that stage because it was too early to compute, to calculate. I think right in the beginning mentioned this point to someone else that these cost are arising at so many different touch points that to assimilate and get all those things at a proper estimate takes a little while.

Percy Panthaki: Understood sir. So that was basically a preliminary estimate and after doing a lot of more work the 450 crores is the final figure that you have arrived at?

Shobinder Duggal: Yes, I hope it remains here.

Percy Panthaki: Right sir. My second question is just to understand basically the effect of MAGGI, if you could just give some guidance or some sort of flavor on if I just remove MAGGI as a brand for this quarter what would your growth have been for the rest of the business?

- Shobinder Duggal:** Sorry, I have given you the information which I could and which I have shared with others, this is not the subject matter for this discussion please, we will take all these questions in the Analyst Meet, let's stay focused on what is important today.
- Himanshu Manglik:** Thank you Percy. Next question Arnab Mitra from Credit-Suisse.
- Arnab Mitra:** Just one clarification, so basically the sales has been reversed and all cost associated with that sales including depreciation or employee cost or any overhead which went into making that sales has also gone out of the P&L?
- Shobinder Duggal:** Yes.
- Arnab Mitra:** Which is why depreciation is also down on a year-on-year basis.
- Shobinder Duggal:** Yes, this is what I mentioned earlier that there is some reclassification of cost from those lines here but they are in the overall cost of the Rs. 450 crores, the overall contribution of all this is not 20% or 30%, but yes that is correct what you are saying.
- Arnab Mitra:** Could you quantify approximately how much of this exceptional item would actually be the operational items had it not been for the accounting code because of which you had to club it there?
- Shobinder Duggal:** No, let's say I have no hesitation to give the basis point impact but unfortunately if I give a basis points impact it will be again misleading you because this basis points will be calculated on the current quarter sales and if you apply that it could give you misleading results. What I can give you another piece of information if that helps you is that if I take this total of Rs. 4.5 billion which is the cost of Rs. 451 crores whatever, virtually two-thirds of this cost is a cost which would have not been here if this issue would not have been arisen and one-third of this cost would have not been incurred had this issue not been arisen. Got the message? I will repeat, Rs. 4.5 billion is the cost out of which two-thirds of the cost I had already incurred, I had already incurred in my normal course of business, I would have sold these stocks, I would have earned revenues, etc., it is only because of this issue that I had to pull that cost down into the exceptional item because I could not sell. But then there is one-third of the cost which I have incurred on this issue which I would have not incurred had this issue not arisen.
- Himanshu Manglik:** Next person Prasad Deshmukh, Bank of America/DSP Merrill Lynch.
- Prasad Deshmukh:** Sir one question about, you mentioned this court case going on with Bombay High Court, so just wanted to know if there are any other cases going on in some other courts as well?
- Shobinder Duggal:** On this issue?
- Prasad Deshmukh:** On this issue yes.

- Shobinder Duggal:** Well, I do not have the head of legal here so it is very difficult for me to comment, but on whatever I know this litigation is going on in Bombay High Court, if there is some one small thing here or there I am not aware but that only Mr. Murli would be aware, I am afraid I do not have that knowledge right now.
- Prasad Deshmukh:** Because why I am asking is because this has been fairly nationwide issue and jurisdiction of Bombay High Court probably remains only in case of Maharashtra and Goa.
- Shobinder Duggal:** No, no, I would only request you to go to the site and see that the central order which was issued by FSSAI and Maharashtra both of them are in Bombay High Court, so do not go simply because it is Bombay High Court therefore it is only a state matter which is listed there and the central matter is somewhere, the central and the state matter are both listed there.
- Himanshu Manglik:** Thank you. Next Jamshed Dadabhoy from Citi.
- Jamshed Dadabhoy:** So just to clarify, you said two-thirds of the Rs. 451 crores is associated with the cost of production, right?
- Shobinder Duggal:** Yes.
- Jamshed Dadabhoy:** Okay. This will also include some fixed cost like depreciation overheads which from the next quarter onwards will go back above EBITDA? Is that the correct interpretation?
- Shobinder Duggal:** Yes, this is in compliance with Accounting Standard-2 and Accounting Standard-5.
- Himanshu Manglik:** Next Gautam Duggad from Motilal Oswal.
- Gautam Duggad:** Hi sir, just one question, what is the tax impact of this Rs. 450 crores, so this Rs. 450 crores is before tax what could have been the normal tax?
- Shobinder Duggal:** Tax deductible.
- Gautam Duggad:** So 33% is what one should take that as?
- Shobinder Duggal:** I will leave you to analyze what our effective tax rates have been and you know what the marginal tax rate is. My only point to you is that this whole cost is incurred in the ordinary course of business and exclusively for the business. So that's the point I think which is more important.
- Himanshu Manglik:** Thank you. Next question Chanchal Khandelwal from Birla Sun Life.
- Chanchal Khandelwal:** Sir on 30th June you have received a notice saying that Bombay High Court allows MAGGI Noodles to be exported, can you elaborate what was this context about and how much of MAGGI Noodles was exported last year and how much can be exported this year?

- Shobinder Duggal:** I do not want to comment on what was the ruling by the court. It is on the website, you can read it there because this matter is sub-judice I do not want to delve into this subject when the hearings are going on very clearly. How much was it last time, I do not have the figures with me here but I can tell you that they are not the most material issues from the perspective of your business valuations and so on so forth, but if you still insist we will try to give you some figures.
- Chanchal Khandelwal:** No, I was just trying to find out the court has allowed export to be done while the selling in India is still on so that was a little surprising from that perspective point of view.
- Shobinder Duggal:** Look as I said Chanchal I do not want to get into it is surprising or not surprising, I just do not want to open a chapter to discuss anything which is going on in the court and I categorically want to turn down any discussion around it. If you want to really have the export figures of last year we will tell you how much of it was this, but we do not normally disclose out of our export sales how much is which category. Having said that, you will be aware that our exports business is not that significant especially the third party as a total contribution to sales, and most of our affiliated sales are not in relation to MAGGI Noodles. So just to give you a sense of that, but please accept my request of not indulging into any discussions on any matter which is in the court proceeding.
- Chanchal Khandelwal:** Okay, just lastly. Assume that this court ruling takes time, can these export component become bigger for you because your fixed cost is already there as you said?
- Shobinder Duggal:** No comments at all because this is again speculation of what will happen? Let's wait. All I am saying is that please take the main message for all your valuation I would not, if I was in your shoes I won't spend too much time trying to simulate what will be the export business and how will that impact value of a firm.
- Himanshu Manglik:** So Nandita's question was not there earlier, but since she is asking there is only one question.
- Nandita Mehta:** Sir just a small clarification. From April 1st to 4th June sales have been booked and from 5th June onwards we have a reversal of sales and the same holds for cost of sales, right?
- Shobinder Duggal:** Yes, we were selling in April, we were selling in May, and we were selling in the first couple of days of June till this episode happened.
- Nandita Mehta:** Yes, so all of those are booked and your cost of sales are even booked so what we are seeing this Rs. 451 crores is primarily from the 5th of June onwards to the 30th of June.
- Shobinder Duggal:** Yes, naturally but do not forget that the sales have also been reversed of the Rs. 288 crores, so it is like not having sold. I sold and I had to get back and we are just trying to tell the size of the sales which was taken back so that you have clarity. The other way to look at it is that they may not have been sold at the first place because they netted from the sales, but what we have withdrawn is around this value Rs. 288 crores.

- Himanshu Manglik:** I think we need to close this call now, we had decided we will take the questions existing at some point in time, more keep coming in and they will never stop. Shobinder if you are able to take more?
- Shobinder Duggal:** Okay, there are two people here, Abneesh Agarwal from Prabhudas and Puneet Jain from Goldman. That's it, Ladies and Gentlemen these are the last two names here and after that please do not embarrass us to take it any longer because after this I have yet one more meeting and I would like to close it after these two questions if you do not mind.
- Abneesh Agarwal:** No, no there is some loss of sales which has happened, loss of profit is there, does Nestle have any sort of a cover of insurance which could provide some relief to the Company in this sort of a scenario?
- Shobinder Duggal:** No, Nestle does not work with business model which assumes that such kind of things will happen and take those kind of exotic covers, we do not believe in that.
- Himanshu Manglik:** Last question Puneet Jain from Goldman Sachs.
- Puneet Jain:** I just wanted to understand this, this Rs 288 crores includes production something which happened in first quarter also or is only for this quarter?
- Shobinder Duggal:** You are talking of the Rs. 288 crores of sales reversal?
- Puneet Jain:** Yes.
- Shobinder Duggal:** Yes, part of it would have been in the inventory at the end of March and part of it would have been produced in the second quarter, I do not know how much but yes, normally speaking yes. But I hope you are not trying to go to numbers which may not be relevant because there is not a very heavy volatility in the raw material cost of these items so the stock valuations or the cost of manufacture is not going to be hugely different between Q1 and Q2, there will be difference naturally but not material.
- Puneet Jain:** So how was it accounted for MAGGI Noodles which were booked in first quarter and then were recalled?
- Shobinder Duggal:** See, you need to just keep this in mind, do you have a little accounting background, can I explain you from an accounting standpoint of view or your qualifications is non-accounting?
- Puneet Jain:** Yes, you can explain to me from accounting view.
- Shobinder Duggal:** Okay. So you see every month we close the books, so we know the stocks are at the end of every month, material valuations, cost of production is determined for every month, so naturally whatever stock was there was there on 31st of May we had some inventory, again on 5th of June we had some inventory in our factories as well as the inventory at the distribution centers and then to this got the inventory which we had taken back from the sales which would have been

made in April and May and then this came into the balance sheet at the total cost and then from there where we have sent it to the exceptional item . They have been written down to zero value and that is what the cost is.

Puneet Jain: Okay. But suppose you book certain amount of MAGGI Noodles in first quarter.

Shobinder Duggal: Book what? We sold MAGGI Noodles in first quarter so there is nothing suppose, actually they were sold in first quarter, they were produced in first quarter, they were produced in second quarter and they were sold in the second quarter and then they were taken back, those are the facts.

Puneet Jain: Yes. So first quarter what you sold, some part of that would also have been in the channel as on June 5th?

Shobinder Duggal: I cannot guarantee, look I cannot guarantee they were there on the 5th of June or not but I can only tell you that in the second quarter we could have had stocks which were produced in the first quarter, that's simply the inventory management principles.

Himanshu Manglik: Thank you Ladies and Gentlemen for joining us on this call at such short notice. Thank you Shobinder for taking up the time because he had a very-very heavy day. We would now close the call and we hope to meet you sometime at next Analyst Meet and we will let you know when that happens.

Shobinder Duggal: Thank you very much Ladies and Gentlemen, we close here. Good night.