TATA CONSUMER PRODUCTS LIMITED

(Formerly known as Tata Global Beverages Limited)

"Tata Consumer Products Limited Q1 FY-21Earnings Conference Call"

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ICICI Securities

CHORUS CALL®

MANAGEMENT:	**MR. SUNIL D'SOUZA – MANAGING DIRECTOR & CEO** **MR. L. KRISHNAKUMAR – EXECUTIVE DIRECTOR & GROUP CFO** **MR. AJIT KRISHNAKUMAR – COO** **MR. RAKESH SONY – GLOBAL HEAD OF STRATEGY AND M&A**
MODERATOR:	**MR. MANOJ MENON – ICICI SECURITIES LIMITED**

Moderator: Ladies and gentlemen good day and welcome to the Tata Consumer Products Limited Q1 FY21 Earnings Conference Call hosted by ICICI Securities 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 phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Manoj Menon from ICICI Securities Limited. Thank you and over to you sir.

Manoj Menon: Hi everyone, good morning, good afternoon, good evening depending on the part of the world you are dialing in from. At I-Sec, it's our absolute pleasure to be host to the 1Q FY21 conference call of Tata Consumer Products Limited today. The company is represented by Mr. Sunil D'Souza – Managing Director and CEO, Mr. L. Krishnakumar – Executive Director and Group CFO, Mr. Ajit Krishnakumar – COO, Mr. Rakesh Sony – Global Head of Strategy and M&A. At I-Sec, we have an ad rating on the stock and an outperformance of process, and we continue to stay believers. Rakesh over to you please.

Rakesh Sony: Thanks, Manoj. And on behalf of the management of Tata Consumer Products, I welcome you all for this conference. I have with me, our MD Sunil, Mr. Krishna Kumar and Ajit. Before we get into a detailed presentation, which Sunil will take us through, a quick recap of Tata Consumer. We are the second largest branded tea player in the world. After the merger of the consumer product business of Tata Chemicals with TATA Consumer, we are now one of the top 10 F&B companies in India. Last year, we did consolidated revenue of close to Rs. 10,000 crores and our current market cap is ~INR 40,000 cr. I will now hand over the presentation to Sunil, who will take it from here. Over to you, Sunil.

Mr. Sunil D'Souza, Mr. Ajit Krishnakumar and Mr. L. Krishna Kumar took the attendees through the key highlights of the investor presentation.

Rakesh Sony: Thank you, Sunil. I will now hand it over to Manoj and we can start taking some questions. First, from the call, and then we will take some questions on the webcast. So over to you, Manoj.

Manoj Menon: So we can open up it for questions, please.

Moderator: Thank you very much. We will now begin the question-answer session. The first question is from the line of Abneesh Roy from Edelweiss.

Abneesh Roy: My first question is on India Foods. So there's a gap of around 11% in terms of volume and value. So is it more because of the mix or is it because of the reduced promotion?

L. Krishnakumar: So it's a combination, as we said, for the difference between volume and value overall, I think there are three main reasons. One is price increase and some of the price increases are not necessarily in the first quarter but spillover of the previous year, where we may have taken a price increase in the later half. The second is the mix. The mix itself has been improving. And if you take our focus has also been on improving the premium variant, and the other thing that is happening in terms of mix overall and this is not specific to food is we also have higher online sales. And thirdly, as you rightly said, there is a reduced level of promotion. So all three are contributing to the gap between value and volume data, and this is not specific to Foods, but across all categories.

Abneesh Roy: My second question is on the India Tea business. You mentioned that market share has improved. So if you could tell us, is it versus the other main players. Second, again and again, you brought the raw material scenario. So normally, we do have a good pricing pass-through to the customer. So is it, you're highlighting the margin because you want to focus on market share and take a bit of more lag pricing, is that the reason?

Sunil D'Souza: I think the critical thing is we did gain market share and we did gain market share from most of our competitors, if I may put it that way. On the pricing itself, I think Abneesh, the critical thing is, there is the commodity cost increase, which normally is passed on to consumers. But we've got to be very mindful and careful of doing it at the right time for two reasons. One is make sure that margins are protected in terms of at least the rupees per kilo margin percentage. Also the second part is to make sure we are neither significantly ahead, nor significantly behind competition when doing that. So we've got to be nimble footed on the piece and that is why the watch-out. Ultimately, the cost creditors will have to pass on to the consumers. The critical thing is when do we press that trigger. I think that is the critical point of watch-out. LK, you want to add?

L. Krishnakumar: We are responsible competitors. So we are not going to be doing something which is just for the sake of share. So we want profitable growth, and we want long-term profitable growth. So that is the orientation.

Abneesh Roy: And historically, you have taken the price increase, or the other competitor has taken in the last 3 years, who has taken it early?

Sunil D'Souza: It happens both ways. Sometimes, it's competition. It depends on inventory levels, what is our inventory position, what is the incoming inventory, etc. So there is no trend of who would exit first. It varies depending on the situation.

Abneesh Roy: And last question, you've seen synergy benefit, distribution, the rest which is expanding. So beyond the current Foods portfolio, are you looking to add more products in the next 2 years or you want to scale this up? And could you look beyond Foods because your name is now Tata Consumer. So is there a thought process that long-term you can look at beyond Foods also?

Sunil D'Souza: So Abneesh, I think we have very clearly said in the near term, the focus is to make sure that we've got two strong businesses both Beverages and Foods, which we need to put together into a common engine and we remain extremely focused on that. And I think Ajit alluded to that, that we're having ambitious targets of finishing this entire integration by December. Once we have a strong engine, which includes a strong front end in terms of sales and distribution, a strong back end in terms of warehousing, logistics, transport, etc., I think after that, plugging and playing with any category is a very easy thing to do. That said, we are immensely focused on the priorities to raise the quotient of new products development and drive innovation in the portfolio, that we operate in. I have also said we will expand our playing field. In the short term, you could probably see us branching out into adjacencies in the categories that we operate in. And in the longer term, obviously, the intention is to become a full-fledged FMCG company, playing across multiple categories. But first, we've got to get our whole own integration proper, build the categories that we operate in, move out into adjacencies where we can leverage the capabilities that we have and then branch out into a full FMCG piece, one step at a time, if I may.

Moderator: The next question is from the line of Percy Panthaki from IIFL Capital.

Percy Panthaki: My first question is on your margins. This quarter, you've seen in the India business, a gross margin tailwind despite the input cost going up, probably because you were consuming old inventory. So going ahead, as you start consuming the new price inventory for the remaining of this fiscal year, do you see any risk that either the gross margins or the EBITDA margin will sort of on a yoy basis be lower than last year, for the remainder of the year.

Sunil D'Souza: So Percy, let me put it this way. Tea prices remain extremely volatile. Right now, they are on a significant uptick. That said, there will be a significant crop expectedly in August and September. We could see movements of pricing out there. I think the critical piece is to make sure that we are balancing volumes as well as pricing. We could make sure that we are protecting margins, but remaining competitive at the same time to continue to drive the volume momentum. However, like I said, the prices are a worrying factor. I wouldn't put our outlook out there on the margins as of now because that is something we've got to play closer to the ground.

Percy Panthaki: Also, just wanted to understand in terms of your outlook on tea prices, I mean it's probably peaked, and you're saying that it might soften a little bit going ahead. But even after the softening, it will be quite high on a YOY basis. So to basically offset this kind of an impact, what is the amount of pricing that you need to take? You have already taken some. How much more pricing in percentage price increases will you need to take to offset the cost inflation in your opinion?

Sunil D'Souza: As I think LK alluded to it, we will not chase volume for the sake of volume. We will chase profitable growth. As our cost of inventory keeps going up, we will make sure that we translate it into the pricing. That said, we've got to make sure that the pricing that we take doesn't stall momentum completely. As I mentioned, it's a tightrope walk. You've got to constantly rebalance the cost and price numbers to make sure that while margins are healthy, you are not stalling volume. So I wouldn't hazard a guess on how much. Like I said, in the last 3 months, we've seen an uptick of about 50% on tea prices. Where it will end, I'm not sure because we keep doing this reforecast. And then again, we see the prices picking up. So it's a sort of weekly forecast on which we are operating today. We will continue to operate that way till we see stability coming back. Again, I said there is significant crop expected in August and September. But that said, we had expected significant crop in July. We did not expect the floods, which spoiled the crop out there. So keeping my fingers crossed that the crop should be normal. And if so, we should see some despite from the nonstop upward trend of the tea prices.

Moderator: The next question is from the line of Arnab Mitra from Crédit Suisse.

Arnab Mitra: My first question was on the distribution expansion as you do this merger of the two businesses. So doubling distribution in a year's time span is obviously very aggressive target. So do you have the outlet snapped out? Is it more rural expansion where the gaps are larger and you mentioned that your front end workforce essentially currently probably does both the businesses separately. And therefore, as they expand, they'll do it together. So does this mean net-

net, there is no significant increase in cost, either for you or your distributors as you double your direct reach in this period?

Sunil D'Souza: So let me answer the last question first. I think, Ajit, during his presentation, said very clearly that we expect 100 basis points reduction in cost to serve at the end of this entire process. That said, right now, we are in the process of putting together the food and beverage system. We had a set of layers both in the sales organization structure as well as the distribution structure per se. We are focused on removing those layers and making sure we are flattening the structure, so that we become more nimble and agile. Work is in progress on putting together the distribution systems, both in urban and rural. That said, the focus is first to put the urban system together and then we will move to the rural pieces. But ultimately, we'll finish the entire process by December. So there are two strong distribution systems coming together. And we do think that we've got the entire data mapped out and the plans laid out to make sure that we are doubling our reach, direct reach initially and then that translating with the wholesale multiplier into the total numeric distribution as we go forward in a period of 3 years. We remain fairly confident. You will see step-by-step implementation of those plans happening over the next 2 to 3 months.

Arnab Mitra: And just one last question on the near term; so Tata Sampann has had very good growth. And this is also a time where consumers are willing to try branded package products in much more easier ways. So in this shorter term, are you being able to ensure, firstly, supply chain in terms of product availability and distribution because this business had relatively low grocery distribution outside modern trade. So in the short term, what are the measures you've taken and can you leap frog this business in this period of next 5 to 6 months?

Sunil D'Souza: So let me put it this way, while you did term that Tata Sampann had a good quarter, I think there is far more potential for this brand, and we remain extremely focused on growing this brand across different channels and across the country. We did have some supply chain hiccups in the early days, especially as plants were not allowed to operate, etc. in lockdown areas. That said, over the months of May and June, I think we've seen progressive easing, and the supply chains are now robust. We are focused on expanding distribution. Like you rightly mentioned, there was a limited reach. In the very-near term, we have expanded our reach and probably our market share in these categories. But one of the critical reasons why we believe that putting an integrated system, doubling our reach, active reach if I may, is critical because that is when we will see the real ticker for the Tata Sampann pulses, spices, the coffee business, etc. which are normally secondary to the tea and salt. So the objective of putting a direct distribution is to reach more outlets actively with the salesman who is selling our entire range. We remain confident that once we get this, we will significantly jump shift the availability of Sampann.

Manoj Menon: We will take 1 question from the webcast now before we go back to the call. The first question here is from Varun Arora. Varun says, could you spend a couple of minutes on changes that we are making in the distribution strategy as we look to increase direct reach and dealing directly with stockist and dealers. What were the issues earlier in distribution and how are we addressing it as we look towards the rest of the stockist and dealers?

Sunil D'Souza: Yes. So let me put it this way, both in Beverages and Foods, as I said, we had layers in the distribution system, a lot of which in the new age are not necessary. So we had the consignee agent system to which the company used to bill, who used to then bill to the stockiest and the stockiest used to bill to the retailer. In the Foods business, we had a distributor whom the company used to bill and the distributor used to bill to the stockiest and the stockiest to the retailer. We have decided to remove this extra layer and will deal directly with the stockiest because we do believe a flatter system is much more effective and much more efficient. And we aim to be much more nimble and quicker out there in the market. Going forward, we will implement the sales-force applications with the front end, connected with DMS and the distributors, link it to our systems. So we have real-time analysis of what is happening out in the market. As a company, both from a marketing/pricing/supply chain or the procurement pieces, we are able to react much more effectively and efficiently to the trends in the market.

Manoj Menon: Thanks, Sunil. One more question from the webcast from Prashant Kutty from Sundaram Mutual Fund. The question that he has is what was the extent of inventory gains that have come in tea business? What is the sustainable margin in the tea business? Question number two, there has been a sharp jump in the profitability of Foods business. Is it to do with any changes in arrangement or sourcing the Tata Chemicals? And what is the level of profitability now in pulses and spices?

L. Krishnakumar: Yes. So there are multiple questions there. I'll just talk about the full business and then come to the Foods business, right? As far as the tea business is concerned, right, you need to remember that, the volatility is there in the Indian tea business than in the international tea business. International tea business has not had that kind of volatility as of now. In India, you should remember what happened during March, April when there was work to be done in terms of plucking, pruning, the right people were not in place because of COVID and other factors. The crop further got impacted by rain, which are unseasonal in some parts of Assam. And 60%-70% of the tea production in India comes from Assam. So there is a problem, which is in this year, which is not a problem forever. It is still, as Sunil mentioned earlier, and some of you are familiar that a lot of the crop comes in, in July and August and going into September, we've had this continuing in July. There's a hope that crop will also improve in August, but notwithstanding a better crop in August, you are looking at a shortfall this year in crop, which could be significant. So you are seeing tea price increases across the board, which are fairly significant. Now the way we will react will depend obviously, we don't want to pass on all the cost increases. There are other efficiencies, and beyond a point, volumes will also be impacted. But the other side of looking at it, just for larger, branded player perspective is we are better equipped because even the smaller players will have to pay more for tea. We will find it difficult to stock large quantum of tea. So there will be some amount of competitive advantage that we will get so I am just trying to explain some of the dynamics which are there and it's going to be an unusual year. So we have taken up prices, will look to take up prices further but also look at rationalization and volume sensitivity. I think the margins will not be what you have seen in the first quarter and our strategy is obviously to built up a little more inventory but then everybody is waiting for the big supply in August. So that's the overall dynamics of the industry. Difficult to give you a specific direction but it's going to be a combination of volume, pricing and efficiency and to some extent we will have some benefit of competitive advantage in volumes which will play out on the results. As far as the Food business are concerned there is no change in any pricing arrangement with the Tata Chemicals but one thing is clear is that we have had good volumes and I think our presentation talks of record volumes in May and June. Full credit to also the team in Mithapur for managing these volumes, we have had record volume month, that's part of the reason for profitability improvement apart from overall better performance of pulses and spices at overall better margins because of selling through some of the channels where we don't necessarily have some other cost that we would otherwise incur so these are combination of reasons.

Moderator: We will take the next question from the line of Gautam Trivedi from Nepean Capital.

Gautam Trivedi: I had two questions. First question was I was at a pharmacy yesterday near my home in South Mumbai when I saw for sale product called Tata Q, ready to eat biryanis, noodles and pastas. What exactly is this, is this part of our company? And I always thought that Chandra's idea was to put all of the consumer business under one roof. So which arm of Tata is this, if it's not part of us?

Sunil D'Souza: Tata Q has been launched by Tata Industries. I would leave it at that and not venture into further speculation, comment on anything beyond that. They are into packaged foods as of now. I believe it's a great product, I have tasted it and Tata Industries normally incubates businesses and takes them to a particular scale. As I said I would leave it at that for now.

Gautam Trivedi: Second question I had was to do with the AGM of Reliance Industries where Mr. Ambani laid out plans before what JioMart wants to do and it appeared again, my interpretation is it appeared that they wanted to also help the Kirana stores, perfect their inventory and so forth. Again this is my interpretation and I wanted to understand how would that impact us in any way or our distribution network?

Sunil D'Souza: So let me put it this way, the distribution system out there is evolving on a consistent basis. 5 years back online did not exist, 5 years back online B2B did not exist, there were certain modern trade formats that did not exist. I would say yes Reliance has flagged off, very strong ambitions in expanding their distribution to Kiranas and making sure that they played a supplier role if I may to the Kirana stores. As they expand their business, I think we have got to make sure that we partner with them and we drive our brand into their system and reach the Kirana store. So, wait and watch because they have started the pilot in Mumbai and now expanding nationally. We are already listed with them and they do carry us. I think the critical piece is to stay focused and make sure that (a) the supply chains are robust to cater to them as they expand their network but more importantly keep a laser focus on the consumer, make sure that your product price, entire proposition appeals to the consumer so the pull-through happens with the Kirana stores/modern trade.

Moderator: The next question is from the line of Satish from JM Financial Mutual Fund.

Satish Ramanathan: I just have a 'bird's eye view' question on how you want to take the company forward because you have so many agro commodities that you are dealing with which have their own cycle; while demand is continuous and constant,.

So, this inventory management across geographies, logistics, warehousing, inventory; all that requires for huge razor-sharp management. When you do your internal benchmark, are we all there already in terms of our inventory management, procurement, cost, control etc.? And what would be your ambition to take this forward I mean in terms of margins etc.?

Sunil D'Souza: Let me answer that in two or three pieces. (a) obviously both the businesses whether it is the Food business or Beverage business has been successful in managing this commodity costs and that is why we built this business to scale and that is why for example we have delivered the last quarter. But that said there is plenty of opportunity to improve from where we are and I would say digitization end-to-end is the key to managing it. I did allude to that, that we are trying to build a direct reach to outlets because if we do that, enable the salesman on the ground to link to the distributor at the back end who links in to our system and our system links in back to the procurement team. I think real-time visibility of what's happening on the front line will make sure that we keep our entire supply chain and inventory positions lean and cost efficient, so the focus is on building that. Apart from that we are looking at different technologies to make sure that we improve our ability to forecast commodities and deal with the commodity movements faster. In Tea for example we have already implemented a system called 'DigiTea' which we are now expanding and taking across different businesses across the globe which for example maps out every single auction piece, does a complete detailed data analysis and feeds back to the buyer so they know what to buy, how to buy, what are the gaps. So, a lot of work in process, just to reiterate, we are good in the space that we operate but we have opportunity to become better and leveraging new technologies and digital into the future is going to be key to enable that.

Satish Ramanathan: Also, in terms of your final debt number because the cash flows have been very strong this quarter. Have we paid down debt significantly during the quarter and the next half year would we see debt numbers at a significantly lower level?

L. Krishnakumar: Overall our net cash position is about 2000 crores and the gross cash is about almost 3000 crores. The debt that we have primarily relates to long-term credit for the Vietnam project and some credit in Eight O'clock which had very low interest rate. So there is no urgency to pay them down so we had a very strong quarter in terms of cash flows because profits were high and we managed working capital well and there is one other point that as we are implementing a uniform sales and distribution system and we bring the advantages and the leverage of scale as we build a larger platform. We are also looking to review some of our credit terms and the like which also will have a bearing on working capital. We started implementing some of these with more to follow. So long story short, it's been a good quarter in terms of cash flow, no hurry to pay down debt. Going forward we expect to have good cash flow with one caveat which is in the short-term the Tea prices are very volatile. Even though we may be holding less stock in terms of per kg, the unit price may be so high that just from a free cash flow perspective which may have an impact. But that's going to be short-term and not from a longer-term perspective.

Moderator: The next question is from the line of Rajesh Kothari from Alfaccurate Advisors.

Rajesh Kothari: My first question is, in the global markets also we have witnessed very good growth during the quarter. So, is there any significant improvement in market share? This is question number one and my second question is with reference to capital allocation. So, in the entire strategy how do you see the return on net worth and return on capital employed because that is very-very muted compared to many other companies in the FMCG sector. And if I can squeeze one more because in your speech you mentioned that your aspiration is also then to become full-fledged FMCG Company. This is over what time period and what do you mean by full-fledged because FMCG is a huge factor. So, if you can get some clarity on that as well?

Sunil D' Souza: Let me take the initial part and then I will ask LK to chip in. So very-very simply put in terms of FMCG. Our ambition is to become a total FMCG company. Like I said we are right now a Food & Beverage Company playing in the big categories of Tea and Salt. We have got the nascent categories of pulses, spices and we have got a Coffee brand too. We will look to scale that up first. Slowly expand into the adjacencies which we operate not far away from the core and once we have built in our number total system of the front end and the back end to get in other categories we will branch out to larger categories. We are right now in the middle of doing a full analysis of different categories out there where we should have the right to win. We will not enter a category for the sake of entering it or adding to the top line. We will enter a category where we can create value for all our stakeholders, make sure that we are delivering healthy bottom lines which add to the business.

L. Krishnakumar: Thanks Sunil. I think the points that you started out with on return on capital employed, right. So, you have to look at it that we are getting a platform for growth with a very strong sales and distribution system at the lead supported by a variety of things. So, on that platform you want to build growth and growth will come from existing categories and we will take Sampann as an example it is an existing product with very-very low distribution, very high potential to grow. So there is a transformation of the existing product range. We can grow on some of the new products in Sampann like snacks and all that which have even lower distribution than pulses and spices. On top of that we will seek to enter other product and categories. So overall as you achieve growth on the platform leaving aside other levers the return on capital employed and hence return on net worth will improve. To that you have to look at margin expansion, tighter control of cost, leveraging sales. So, all this will help us in the medium term to significantly improve return ratios from where they are today. That's the aspiration, that's the journey on which have embarked.

Sunil D' Souza: And if I can just add to what LK said I think the critical thing is to get the platform right. That's why we are immensely focused on getting the integration right and making sure we are building out a system from which we can scale in the future. As we get that system right then you would start seeing the addition of categories and segments and slowly us branching out into a full FMCG company.

Moderator: The next question is from the line of Sanjay Bembalkar from Canara Rebecco Asset Management.

Sanjay Bembalkar: My question is on raw material sourcing in India. So most of our raw material is farm produced and now purchasing from a farm produced is allowed outside purview of FMCG- APMC Act. So, does this have any positive or negative impact on our business going ahead?

Sunil D' Souza: Yes, there have been changes in the whole procurement of farm produce from an India perspective. Right now, we are still in the process of understanding the entire regulation and more importantly understanding how we could take advantage of it. Once we go through the entire details, we will put in systems to make sure we are leveraging this for the full benefit of the company.

L. Krishnakumar: Yes, I think it's a clearly a big opportunity because we have direct access to farm-producer society, and you can have a preferred supply relationships That helps us to ensure reliable quality supply for one, build traceability and overall you can develop a variety of products based on consumer demand. Based on long-term relationships with farmers and the disintermediation, it will lead to a win-win situation in terms of cost for us and return to the farmers, so all these opportunities are there. We are just about to start a few pilot projects in certain crops which we are interested in. So that's where we are but I think more in the medium term.

Moderator: The next question is from the line of Sumant Kumar from Motilal Oswal.

Sumant Kumar: We mentioned in the PPT we have gained a market share in Tea. So is branded player gaining market share due to supply chain issue for our net sales or any other factor for that?

Sunil D' Souza: I think there are two critical things, number one is procurement and number two is distribution. During the lockdown whoever had a better procurement system and whoever had a better distribution system did make inroads. We made it better than most other players. During the lockdown, there were supply of tea, the prices were going up, a lot of the smaller players like LK mentioned were not very sure whether the prices will continue to go up or down. So they did not refill inventories, waited on the sidelines, we continued to supply the market and we came out better off in the bargain.

Sumant Kumar: And the second question is regarding A&P expense, so this quarter it is lower. Can you talk about the next couple of quarters; it will be like that only?

Sunil D' Souza: We are in the space of selling branded products and to sell branded products there are two or three critical elements, number one is sales and distribution, number two is A&P and number three is innovation. We remain focused on all the three. You would see some ups and downs in the short burst but overall we do believe that we have to spend to build our brands. So, it is not that we are cutting out A&P for the medium term or even the shorter term. We would see an increase in A&P spends as we go forward to make sure we are strengthening our brands with the consumers.

L. Krishnakumar: Just one addition on A&P spends. Actually, I think we spent more in the UK and less in India. So overall, it's not that we under spent significantly in A&P. Just want to make that point; if you look at consolidated it will be different from standalone.

Moderator: Thank you. Ladies and gentlemen due to time constraint we will take that as a last question. I would now like to hand the conference over to Mr. Rakesh Sony for closing comments.

Rakesh Sony: Thank you to everyone for joining this conference. We had almost 550 people logging for this call and thanks to the entire team of Tata Consumer who led us to deliver this fantastic growth in Q1. As we all look forward to Q2, we will put our best foot forward to ensure that the performance of the Company continues. With these words we look forward to seeing you again in Q2. Thank you so much.

Moderator: Thank you. On behalf of ICICI Securities Limited that concludes this conference. Thank you for joining us and you may now disconnect your lines.