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SOM Distilleries & Breweries Ltd.

Earnings Conference Call Transcript

Q2 FY2020

Management:

Mr. Deepak Arora - CEO

Mr. Nakul Sethi – Director, Finance & Strategy





Moderator: Good day and welcome to the SOM Distilleries & Breweries Limited H1 FY2020 Earnings Conference Call. 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. Please note that this conference is being recorded. Joining us today on the call are Mr. Deepak Arora – CEO and Mr. Nakul Sethi – Director, Finance & Strategy.

Before we begin, I would like to mention some of the statements made in today's call may be forward-looking in nature and may involve risks and uncertainties. For a list of such considerations, please refer to the 'Earnings Presentation'. I would now like to hand over the call to Mr. Deepak Arora for initial comments and then we will start an interactive question and answer session. Thank you and over to you Sir!

Deepak Arora: Good afternoon everyone. I thank you Raymond for beginning the call. I would like to welcome you all to the SOM Distilleries & Breweries H1 FY2020 earnings call. During today's call, I would like to first discuss the performance highlights, the industry environment in general and the outlook for the company then I will hand over to my colleague Mr. Nakul Sethi, who would have a detailed discussion on the performance post which we will open the call for interactive Q&A.

During H1 FY2020 we recorded a beer volume growth of 26.2% Y-on-Y basis to 51.8 lakh cases and an IMFL volume growth of 91.1% on a Y-on-Y to 6.7 lakh cases. Our revenue for the same period recorded a growth of 37.4% on a Y-on-Y basis to reach Rs. 2,698 million. Our EBITDA for H1 FY2020 stood at Rs. 373 million, a growth of 14.5% on a Y-on-Y basis. EBITDA margin for the period that is Q2 was 13.8% compared to 16.6% in the same period last year.

The declines in the margins can be primarily attributed to input cost inflation coupled with the higher proportion of new glass bottles due to the expansion in the facilities on a pan India basis. PAT for the first half of the year grew by 19% on a Y-on-Y basis to Rs. 171 million with a margin of 6.3% tax for the period included benefits of recent corporate tax. Our annualized utilization levels were at 68% for beer and 40% of IMFL on a consolidated basis.



Existing beer facility at Bhopal operated at peak capacity levels. Karnataka facility operated on an annualized utilization level of 52% and the Odisha facility, which has been started this year operated at around 30% of the annualized utilization level.

The business environment for the beer industry particularly in the second quarter was very difficult. Second quarter was characterized by weak economic sentiment, monsoons particularly in the high growth regions as well as the higher input cost prices on our main raw material.

Q2 is a cyclically weak quarter for us and extended monsoon played further dampener, impacting the demand for beer in most of our key and growing markets. We continue to experience cost pressures on a key raw material particularly glass bottles and barley, which has impacted our gross margins during the second quarter. Third quarter is also a seasonally slow quarter for us and with the prevailing challenges, we expect Q3 to experience similar issues; however, an improvement is expected in the fourth as we start preparing ourselves for the peak season demand and the summer.

We would like to update you that we are in the process of installing a canning line for our beer plant in Odisha and we expect it to be operational by late Q3 FY2020. This will help us in supplying the better SKU mix as well as will enhance gross margins for this facility, which will start reflecting from Q4 FY2020.

Our performance during the first half was as per management's expectation and we further strengthen our view on the performance on the remaining part of the year. We have already made significant investments for the next phase of growth and the focus would be to generate returns on these investments and to capture more market.

With this, I would like to hand over Mr. Nakul, who will run you through the detailed numbers. Thank you and over to you Nakul!

Nakul Sethi: Good afternoon everyone and welcome to our H1 FY2020 earnings call. Moving to a financial performance, our consolidated total income for the first half of FY2020 was Rs. 2,698 million, representing an increase of 37.4% compared to the same period last year. This growth was achieved despite the prolonged monsoon in Q2. Our beer revenue



increased by 31.6%, year-on-year to Rs. 2,264 million. IMFL revenue stood at Rs. 420 million an increase of 79.9% compared to the same period last year.

Our consolidated EBITDA for the period increased by 14.5% year-on-year to Rs. 373 million. The EBITDA margin for the period was 13.8%. We were able to achieve this margin despite the prevailing cost pressure for barley and new glass bottles. Higher employee cost pertaining to new markets also had an impact on the margin for the first half of FY2020. Interest cost for the first half increased by 40.8% to Rs. 75 million. Depreciation expenses increased by 35.3% to Rs.52 million in the first half of FY2020. This increase was primarily attributable to the higher depreciation on the Odisha facility.

Our consolidated PAT was Rs. 171 million, an increase of 19.1% year-on-year basis margin of 6.3%. Our gross margin for Q2 FY2020 declined by approximately 700 basis points primarily on an account of input cost inflation, the sizes of glass bottles had increased to 15% as compared to same period year. Barley and sugar costs have also increased substantially during this period.

Our EBITDA for the quarter was Rs. 82 million, a decline of 19.9% compared to the same period last year. EBITDA margin for the quarter was 10%. Our EBITDA margin declined by 430 basis points compared to the same period last year. We were able to offset some input costs impact on EBITDA by cost rationalization primarily on an account of freight cost savings.

As on September 30th, 2019, total debt stood at Rs. 1,679 million and cash-and-cash equivalent of Rs. 182 million resulting in net debt of Rs. 1,497 million, gross debt to equity ratio was 0.52x and gross debt to EBITDA ratio was 2.93x.

Our main line brand Hunter and Blackfort remained relatively flat in Q2 FY2020 at 6.1 lakhs and 2.6 lakhs cases, respectively compared to the same period last year. The Power Cool brand recorded a growth of 9.5% year-on-year to 4.6 lakhs cases. Overall, beer volumes recorded a growth of 5% year-on-year in Q2 FY2020. Prolonged monsoon season provided us an opportunity to push more IMFL, which is evident from the 80.2% growth year-on-year to 3.2 lakhs cases compared to the same period last year.



With this we would now like to open the floor for Q&A. Thank you so much for your patience.

Moderator: Thank you very much. We will now begin with the question-and-answer session. The first question is from the line of Vijay Ramchandani from Pragma Equities. Please go ahead.

Vijay Ramchandani: Sir, can you share what is the status of our stock moving out from 'T' category?

Nakul Sethi: This is pertaining to our application for listing at the NSE and as soon as that is processed, I think the stock will move from 'T' category to the normal category.

Vijay Ramchandani: If you can share what was the volume growth of Power Cool in Q2?

Nakul Sethi: 9.5%.

Vijay Ramchandani: That would be how many lakh cases?

Nakul Sethi: 4.6 lakhs cases.

Vijay Ramchandani: Also can you share now that first quarters are done, what is the outlook for the next two quarters and how much utilization can we actually achieve for Karnataka and Odisha?

Deepak Arora: With the current utilization levels, I am keeping this forward outlook in mind we set to clock annualized turnover on a consolidated basis around Rs. 480 Crores to Rs. 500 Crores this year.

Vijay Ramchandani: That would be how much utilization for Karnataka and Odisha?

Deepak Arora: The utilization levels would done on an annualized basis, so depending on the Q4, it would be pretty consistent with what we have stated, which is roughly around 68% of the total consolidated basis and 50% around for the Karnataka beer level and Odisha, since it is in the first year of inception, we are at 30% right now on an annualized basis and we look forward to increasing that.



Vijay Ramchandani: Regarding our capex, have we already included all the capex, which we were supposed to do for Odisha and also what is the update on Bhopal expansion, just trying to understand if our debt will increase from current level?

Nakul Sethi: The Bhopal capex would be finished by Q4 as stated in our previous call as well in the previous earnings call and as far as Odisha is concerned, it is as I said in the call, the canning line was a last big capex involved in the expansion and following which there would be a small capex regarding the utilities and other administrative capex such as godowns and etc., so there would not be significant, but you can the majority of the capex is over in both the years.

Vijay Ramchandani: How much capex will be required for Bhopal?

Nakul Sethi: Roughly Rs. 35 Crores for the Bhopal unit.

Vijay Ramchandani: On the margin front, you had said that we should be able to maintain our margins from Q1 onwards, so we are witnessing raw material pricing pressure do we expect that to come down going forward?

Nakul Sethi: I think when we had had this call at the time of Q1, we said that the margins whatever we are experiencing are transitional in nature similarly in Q4 also we had mentioned about it and if you would see the results, which has been announced by my peers also, all the companies margins are under pressure, so we are not the only one. Our margins impact is also compounded by the fact that we are using an extra amount on new bottles for all our facilities, so I think it is a long-term investment, which has been made and puts will come out very soon.

Vijay Ramchandani: Are we still importing glass bottles or now we are able to get it from local?

Nakul Sethi: We are much importing glass bottles.

Vijay Ramchandani: Thank you so much.

Moderator: Thank you. The next question is from the line of Sunil Jain from Nirmal Bang Securities. Please go ahead.



Sunil Jain: Good evening, Sir. Sir, my question relates to the increase in cost, which you are facing, how you are tackling it, is there any scope for increase in prices and all, since our growth has slowed down, the import content of the bottle also may be coming down?

Deepak Arora: There are two aspects to this question, one is growth as per se has not slowed down, it has just been the longevity of monsoon, which has impacted overall the pie, since we are in the growth and expansion phase, our requirement for new bottles will always be more than what we can recover. In the short-term, yes, the cost pressure is there, but these bottles on a longer term 10 to average out, which is nothing to worry in terms of the short-term cost increase. As far as, the barley and malt are concerned these are cyclical costs and should be taken in terms of the weighted average of the previous five years. There are cycles when the cost was down and there are cycles, which the cost goes up, this year we have experienced major cost shift in term of the barley prices, so there is nothing to worry in terms of the long-term impact of these costs and third is we will keep our bottle inventory up as we have suffered before of not having enough bottles in our stock categorically for the Q1. Since we are growth phase our inventory levels for our major raw material, which is glass bottles, which will be always up, but we will see that it being realized at the end of Q1 next year when the inventory will fall down significantly and there would be an inventory build-up in respect of increased peak demand on all our units on consolidated basis.

Sunil Jain: So, this glass bottle prices has further increased in Q1?

Deepak Arora: They are further increased on an account of more stocking of the bottles even by our peers, so it has become a practice, so the cost has gone up and roughly the cost impact has been 15% on y-o-y basis.

Sunil Jain: I was just talking like if you see sequentially, the cost has increased, what you say even from the Q1 also the price now if you want to purchase bottles then that has increased?

Deepak Arora: From the last six months it has gone up by 15% and next six months we see it to be at around the same level.

Sunil Jain: But, you do not see any increase in prices of your products and all?



- Deepak Arora:** No, because these are annualized rates so margins would go up only I think by next year when there is a renewal.
- Sunil Jain:** Overall, for this year, what type of margin we can see, whether we can maintain last year margin or we can see better than last year?
- Deepak Arora:** On a consolidated level, we are looking at maintaining 14%, EBITDA.
- Sunil Jain:** Thank you.
- Moderator:** Thank you. The next question is from the line of Runjhun Jain from Nirmal Bang Securities. Please go ahead.
- Runjhun Jain:** Thank you, Sir. you have given outlook on glass bottles, so whatever the input cost in terms of barley, so how are the prices? Have they peaked out you think when the new crops coming, we can see some decline in the prices and some benefits from Q3 and then further in Q4?
- Deepak Arora:** Yes, compositely if you see Q3 and Q4 in terms of the pie share also goes down, and you cannot accumulate barley and malt as you can accumulate bottles, so henceforth if you check on the overall pie, the cost will remain pretty constant now because, yes, you are right, they have peaked out in terms of the prices for the next two quarters.
- Runjhun Jain:** You are seeing that the volumes are much higher, the percentage of that would come down?
- Deepak Arora:** For the next two quarters with winters kick in so these are generally the lowest industry sales for the beer industry, even if you have new crops, the demand is not there for that so overall the cost impact, which should come does not come, but at the same time these are the highest level of prices, and we hope to see a cyclical shift in the coming quarters to the lower side not to that.
- Runjhun Jain:** Right now, you just said that you are looking maintain 14% margins for the full year, on six months basis we have done around 12%, so where you think that improvement would be coming from, basically from the Q4 with the higher volumes or is there anything, which should look forward?



Deepak Arora: For the H1 FY2020, we recorded an EBITDA margin of 13.8% and we are looking for a bumper Q4 and which will basically bring the cost down.

Runjhun Jain: Thank you.

Moderator: Thank you very much. That was the last question in queue. I would now like to hand the conference back to the management team for closing comments.

Deepak Arora: We would like to thank all our investors for attending this call today. As stated in my previous call as well on the earnings presentation that we are committed to utilizing our new investments across India and you would like to know all our investors that as the capacity utilization levels start going up you would start seeing a much more aggressive returns on the investments made by the management and the company and we are very positive about our growth outlook for this coming year and for the coming years and again, I would like to thank everyone for listening to us patiently. Thank you.

Moderator: Thank you very much. On behalf of SOM Distilleries & Breweries Limited that concludes this conference. Thank you for joining us, ladies and gentlemen. You may now disconnect your lines.

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Note: This transcript has been edited to improve readability

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