June Quarter 2017 Earnings Call of
Hindustan Unilever Limited
18th July 2017

Speakers:

Mr. Sanjiv Mehta, CEO and Managing Director

Mr. P.B. Balaji, CFO and Executive Director, Finance and IT

Mr. Aasif Malbari, Group Finance Controller and Head of Investor Relations

Moderator

Good evening, ladies and gentlemen. I am Mahima, the moderator for this conference. Welcome to the Hindustan Unilever Limited Third Quarter Earnings Call. For the duration of the presentation all participant lines will be in the listen-only mode. After the presentation, the question-and-answer session will be conducted for all the participants on this call. I now hand over the call to Mr. Aasif Malbari. Thank you, and over to you Sir.

Aasif Malbari

Thanks, Mahima. Good evening and welcome to the conference call of Hindustan Unilever Limited. We will be covering this evening results for the quarter ended June 30, 2017. On the call from the HUL end is Mr. Sanjiv Mehta, CEO and Managing Director and Mr. P. B. Balaji, CFO. As is customary, we will start the presentation with Balaji sharing aspects of our performance for the quarter, and then hand over to Sanjiv for him to share his perspective on the business performance. Before we get started with the presentation, I would like to draw your attention to the safe harbor statement included in the presentation for good order sake. With that, over to you Balaji.

P. B. Balaji

Yeah. Thanks, Aasif. Thanks all of you for joining the call. We had a bit of a technical glitch in the Mumbai side, which we've not sorted out I believe. So apologies if any of you had to go through a bit of a pain on this, we're trying to understand what went wrong there, but we are good to roll.

We'll quickly get to the strategy. No change from what we have been communicating earlier, and this continues to remain the same, its serving us well. As far as the market context is concerned in the run-up to GST, we saw a very cautious sentiment in trade despite high promotional intensity. Input costs were stable during the quarter, and rural markets continue to remain challenging. This is a broad market context. And in this context, resilient and performance of profitable growth was delivered in a volatile environment, which we are quite pleased about. Domestic consumer growth was 6% with underlying volume growth flat. Just to draw your attention that bulk of the price growth came from actions in the previous quarter. Additionally, given that we were expecting price drops to happened post the GST transition, we have managed both trade spends and trade stocks were optimized, in order to we're able to ease into the GST transition. EBITDA at INR 1,866 crores was up 14% with margin up 160 bps, and this margin improvement of 160 bps as you would have noticed has come across all lines, the big one being the cost of goods sold being down by 75 bps, aided by a very strong savings program and also competitive A&P spend was maintained while ZBB helped us drive the percentage A&P down by about 20 bps. Overall, the savings program that we have been working on for many years continues to deliver strong results for us and it's across all lines of the P&L. PAT at INR 1,292 crores was up 15% and net profit at INR 1,283 crores was up 9% and we'll talk about – more about this in the coming slides.

This growth of course had a very polarized impact with respect to different segments. Home Care & Refreshment continued their strong growth momentum, while Personal Care & Foods were impacted disproportionately by the thinning of trade pipelines, particularly in the canteen stores, these are army stores canteens, which did not buy for the whole of June and the better part of this month as well.

Just to quickly get to the how the GST transition happen, we've been highlighting that HUL has been preparing well for the GST transition for the past two years and as an entire business project and delighted to see that all come together as the transition happened. It was swift, it was smooth. There's absolutely no disruption in trade servicing, with most of our distributors invoicing on day one itself. And the first GST invoice came out at eight minutes past the midnight on the July 1, and this is from a distributor who was in Jharkhand in Jhumri Telaiya. Internal systems, HUL systems were all working flawlessly from day one, and the transition in the SAP side also went very well. And all our vendors are also now fully normal and inbound supplies are coming through from the first week itself. And the first working day, we started processing record number of payments as well. So, overall the operations of it, I'm delighted to report that have transitioned extremely smoothly.

On the pricing side, as you're well aware that we have called out time and again that HUL is committed to passing on the net benefits at a company level, and just to call out the individual tax changes, output tax rate change went down for four of our categories; detergent bars, skin cleansing, toothpaste and hair oil. And output tax rates went up for detergent powders, hair care, skin cream, colour cosmetics and instant coffee.

Being cognizant of this, what we've done basis what we have committed that we'll pass on net benefit at a company level and the fact that as a company, we've been preparing quite well for this, our pricing started landing with impactful from day one. So we saw dramatic changes in the prices of detergent bars, which are big impacts, hits that we wanted and those have landed with a lot of impact. And also further changes are currently underway, and they will land as per normatively planned. So the full supply chain and grand actions on pricing have all been kicked off, trigged and will be landing in the coming days as well.

Initial days, how has it been, I'm sure is the question that all of you are keen to understand. Unlike demonetization where we saw a significant impact on the consumer side, here the footfalls and off-takes appear normal.
However the trade pipelines are pretty thin, and therefore our focus and the immediate priority, top most priority is to restore trade pipelines, for which we need to work with the trade, and sections of trade, particularly wholesale and small retailers, are still unclear on rules in parts of the country and that is delaying the return to normalcy. So, our plan is to step up the communication to trade and their advisors, because we need to take them along. So that we are able to get them – getting back to business as normal. And they need to make up their minds, how they want to run their business model. So, this is going to be a big piece of work starting now.

And this is a key slide, which we just want to just call out the accounting impact of GST. And there are two distinct sections here. There is a first section which is an optical one, and the second is a real – the second side of it is a real one.

Let me first cover the optical one, which is the reporting of excise. You would recollect that pre-GST, excise was treated as a cost, and therefore, the turnover was gross of excise. And post-GST, there's nothing called excise, it all nets off pre-turnover as GST. Implication of that is reported turnover is likely to be lower by 750 bps, while absolute EBITDA, there's no impact at all, because it's just an entry going from cost line to netting off the turnover line. That's all that is happening. This would imply the EBITDA margins would also be higher by about 150 bps, but of course, EPS has no impact at all. This is in HUL local results. For some of you who are also invested in Unilever, the HUL numbers as consolidated into Unilever, this side of it, there's no impact at all, because HUL turnover under IFRS was always reported as net of excise for many, many years. So therefore, there is no impact of this particular excise side of it on the Unilever results. We are happy to engage with you subsequently, if you need further clarification on the accounting side, but that is an important item there. That was on the excise side.

Come on to the right side of it, which is the impact for input taxes and fiscal. You would recollect that as per Anti-Profiteering Rules – Provisions, it is important that both output and input taxes are passed on as pricing and the benefits are passed on. That's what we are committed to. How does this play out on the accounting side? Pre-GST where input tax credit was availed partially, therefore post-GST you're getting the full input tax credit and therefore that needs to be passed on. That is a driver of this item.

On the post-GST side, there are three impacts. Number one is, since costs are likely to be lower as they are taking the full input tax credit - that is one. Item number two is excise duty post-GST or in the pre-GST world available was not available to us to take a credit, because you're getting a fiscal benefit. However, in the world of GST, we'll get a full credit for the GST paid on input taxes. So that's the second item.

Third item is fiscal refund. Earlier, we were getting full excise benefit. Now, however, going forward, the government is likely to give you only 58% of the CGST on value addition. And we now need to pass on the net impact of items one and two – if you noticed that item one is a credit to the P&L, item two is a credit to the P&L, item three is a debit to the P&L. And the net impact of item one, two and three will now need to be passed on as the net input credit add towards the output tax benefit as well and then you will have the net impact that is felt on your turnover life.

This will impact both local HUL results as well as HUL as consolidated in Unilever the same way, and therefore, reported turnover is likely to be lower and invariably this will play out as price growth. How much exactly it is, is something will be a part of the – it will almost be a guidance for us going forward. So what we will do for you is similar to how we have dealt with when the fiscal benefit went away. Every quarter we'll quantify the impact of this on the intrinsic number, so that you're clear on what is the GST impact on this. But here, again, absolute EBITDA no impact, EPS no impact again. So this is a key slide on this. And as I said earlier, we will – more than happy to walk you through this at a slower pace if required. So that was GST.

So keeping aside GST, as far as the rest of the quarter is concerned, our focus on innovation continued, a strong set of innovations coming through. And moving on to the naturals portfolio that we continue to build, here again, extended the naturals portfolio within the existing portfolio. The Vim bar had a malodor variant, which is pudina based. Then we have specialist brand. We've Citra, which has gone national and that is something that we did - 12 SKUs under Citra in the face care segment has been launched, with very exotic natural ingredients from East Asia, and of course, the master brand, Ayush.

The great is news here is Lever Ayush is now going national. After a successful south launch, we're now delighted with the mix that is there, had a little bit of tweaks that we need to do to the mix, which we have done and we're now going national as we speak. So pretty excited with this innovation now being taken over across the country.

Moving on to the individual categories, Home Care. Home Care saw strong growth across both mass and premium laundry. And Surf continues to sustain its strong robust volume led growth momentum, and the only fly in the ointment was the water business, which witnessed a muted quarter due to challenges in trade, pre-GST. And this being a durable business is something that really got impacted quite significantly in the run-up to GST.

On the Personal Care business, this did get impact substantially because of the thinning of trade pipelines particularly in CSD which I repeated, a big portion of the business comes from there. But however what was exciting was to see the personal wash business delivering broad based growth across brands. And the Fair & Lovely re-launch has been very well received. And color cosmetics delivered yet another robust quarter for this quarter as well.

On the Foods & Refreshment side, refreshment delivered broad-based growth, with the Tea business continuing to deliver strong robust double-digit growth by leveraging the WiMI approach. And in the food side, Soups & Jams continue to drive category growth of Foods, but of course Foods again got impacted by some of the destocking there. So both the discretionary categories did get impacted, Personal Care as well as Foods on the destocking.

A question that keeps getting asked all the time and again stating on how confident are we on the savings agenda and the margin agenda. Just thought we will just pull our thinking together on this. The margin delivery program is a widespread companywide program and that's been running, giving us excellent benefit for the last few years. And here we are thinking and delivering end-to-end savings of 6-odd percent of turnover is the ambition that we work with. And here we work as no functional silos. These are end-to-end business thinking. The whole zero based budgeting comes into this particular piece as well. We push businesses to actually think blue sky as though the business never existed, talk about recreated, how will you do it, have an organization-wide engagement across layers, across functions, so that people are widely engaged in generating ideas, cost savings. And we also look at benchmark ourselves with competition that is out there to understand the essence of business drivers in this. So, it's a pretty elaborate program that we drive, and that is something that is delivering us excellent results.

So, this strong savings program is what gave the margin delivery for the quarter as well, and to just summarize the quarter, we had a sales growth of 5% with an EBITDA margin increasing by about 160 bps, therefore a growth of 14% on the EBITDA side. And the only, the difference that you see, is on the exceptional items side, where on the base included a one-time write back of provision for employee benefits, which we had called out in June quarter 2016, otherwise domestic consumer growth was at 6%. So, that was the quarter in summary.

And looking ahead in the near term, we expect a gradual improvement in rural demand. Trade stocks, we also expect trade stocks to build back to normative levels over the next few months. We expect input costs also to remain stable. And in this scenario, our strategy continues to focus on volume driven growth and improvement in operating margin. And in the broader strategy of 4G, consistent, competitive, profitable, responsible growth does not change.

So with this, let me hand it to Sanjiv for his views on the quarter.

Sanjiv Mehta

Thank you, Balaji. Good evening, everyone. Always a pleasure speaking to you, and thank you so much for joining us on this call. The last few quarters from external variables perspective have been very challenging to say the least. In this scenario, we have been very pleased with the agility displayed and the resilience demonstrated by the business. Tough times, you will all agree are the true test of the strength and character of an organization. Once again, we have navigated turbulence in a very satisfactory fashion. Our planning for GST was granular and detailed and the execution flawless.

Balaji has very succinctly explained the context, the sentiment in the trade was cautious, despite high promotional intensity in many of our categories, the rural markets remain challenging and there was thinning of trade pipeline. With volatile market conditions as a backdrop, we are delighted with the underlying sales growth of 6% delivered by the business.

With justifiable pride in our team, I want to share with all of you the smooth cut over we had of July 1. The excellent planning and execution was reflected in the ability of our stockists that Balaji spoke about to generate GST-compliant billing service, the retailers within minutes of the roll out to ensure that the business continuity was maintained. Our planning was very intense. We had multiple teams working on GST related issues months ahead of transition. In fact, we had set up a GST implementation cell two years in advance. For this was not just about HUL being ready, but we have to influence the bigger ecosystem, the multiple strong pre-engagements that we had with our channel partners, ensured that there is a high degree of clarity on various rules, laws, and requirements. The transactions with our vendors continued smoothly with all supplies moving uninterrupted – in an uninterrupted manner just as we had planned. All in all, the transition of such magnitude was executed in record time and in an absolutely smooth manner. This of course would not have been possible without the passion and dedication of our people and I remain so proud of my team.

In the run up to GST, we saw increased competitive intensity in trade with several competitors making significant trade intervention. However, learning from our experience during demonetization, we focused on the long-term and stayed close to the consumers as well as communicated effectively with the trade to address their concern. Additionally, keeping in mind the planned price drops, we optimized the stock in the pipeline to help land the price stock networks on time. This we believe not only helped us in managing the transition to GST smoothly, but also helped us in improving the profitability in the quarter.

Our initiatives in brining efficiencies and effectiveness across the value-chain like NRM, ZBB together with strengthening the owners' mindset has been paying us the rich dividend. This allows us to invest behind market development, innovations, competitive spending, as well as improve our margins.

Like Balaji mentioned, the pricing action post-GST has already started to land in the market in line with the lead times. We stay committed to passing on the net benefits at the company level and see GST as a win-win for everyone and strongly believe that the consumers will see multiple benefits in the form of cheaper and better products going forward.

As far as turnover growth is concerned, I think it would be only fair to say that with varying degrees, all the categories that we operate in were impacted in the run-up to GST; however, the discretionary categories faced the brunt. Let me call out a few highlights on the category lens.

In Home Care, the premium and mass laundry segment delivered strong growth for the quarter. Our largest brand Surf delivered yet another quarter of robust volume-led growth.

Personal Care and Foods saw relatively higher impact of the trade down stocking. However, happy to inform you that the rebound we saw last quarter in personal wash is continuing to gain momentum, and we are positive about the segment going forward.

Coming to our performance in Refreshment, this category saw robust broad-based growth across all the three segments of Tea, Coffee and Ice Cream & Frozen Desserts.

With a philosophy of long-term focus, we were undeterred with short-time pipeline issues. This was also manifested in our innovations, Balaji spoke about Citra - it's a fabulous brand we are bringing this alive in India with products inspired by two vital ingredients, Japanese Green Tea and Korean Pink Pearl. The other of course is the national roll out of Lever Ayush. We are very pleased with our test marketing in South India and you will very soon see them in your markets as well.

Now, let me reflect on the current state of play. Many parts of the organized trade had disruptions in the first two weeks of July and are now limping back to normalcy. Wholesale remains the most effected, there are many traders who are still sitting on the fence awaiting clarifications and directions from the advisors. We on our part are setting up multiple engagements with the trade to ensure that normalcy restores at the earliest.

With that, let me hand the call back to Aasif.

Aasif Malbari

Thanks, Sanjiv. Thanks, Balaji. With this, we will now move to the Q&A session. So that it doesn't get really late, we will, try restrict it to around 60 minutes to 75 minutes and try to complete by around 07:30. Can I request participants who want to ask a question to keep it really tight, so that we can accommodate as many questions over the next few minutes. In addition to the audio option, as always our participants have an option to post the question through the web option on the screen. We encourage you to do that and we will take all the questions up before we end the call.

Before we get started with the session, I would like to remind you that the call and the Q&A session is only for institutional investors and analysts, and therefore, if there is anybody else who is not an investor or analyst but would like to ask questions to us, please directly reach out to the Investor Relations team here. With that, I would like to hand the call back to Mahima to manage the Q&A session for us.

Operator
Sure. Thank you very much, sir. We will now begin the question-and-answer interactive session. First question comes from Mr. Sameer Gupta from India Infoline, Mumbai.

Percy Panthaki:

Hi, sir. This is Percy Panthaki here. In your presentation on slide 18, you have written at the bottom thinking and delivering end-to-end savings of 6% of turnover, is there a timeframe associated by which you plan to achieve this goal?

Answer:

Hi, Percy. I think the savings program is a very – it's a cultural aspect for us and we intend to run this as an ambition that we charge the teams with. And we have been tracking those levels over the last few years, and we intend to maintain it and step it up as we go forward as well.

So, that's the reason why we have called it out, and we also – we put the slide out at the request of a lot of you were saying that tell us how is that you are confident on your margins. I think the big one that we have is a robust savings pipeline, and adding ZBB to the mix as well gives us the ability to navigate multiple lines in the P&L.

Percy Panthaki:

So, just help me understand here Balaji, this 6%, I mean is it -does it have a starting point from which it will be measured or is it like part of that 6% is already there in the P&L? What perspective, do I look at this number?

Answer:

So it's already there in the way we operate Percy. On a yearly basis, we are keen to drive this level of savings, which we can then use it for deployment into various lines of the P&L, manage inflation, use it to launch new product, use it to drive inefficiencies out of the supply chain. So it is a comprehensive way with which we want to galvanize rank-and-file in the organization to look at savings de novo all the time.

Percy Panthaki:

Okay. So you are saying, this is already there in the result, it's not as if versus today there is an additional 6% of saving which you are targeting, that is not the way to read it, right?

Answer:

No, no, no. This is basically trying to explain how we go about managing margins in the business, and that's an integral part of our way of operating. Like how zero base budgeting, net revenue management, symphony savings are all integral part of the way we operate the company. We just try to put it as one slide, so that we can take imperative.

Percy Panthaki:

Understood. And these initiatives that you're doing in terms of zero base budgeting, etc. You have been sort of talking about and sounding this out to investors and analysts over the last, let's say four to six months. So given that there is a renewed or greater focus on this recently, would I be right in assuming that the savings out of these sort of initiatives will be front-ended and the savings in FY 2018 that you will see will be relatively higher compared to what you will see in let's say FY 2019 or FY 2020 or will it be that you're going to exactly or more or less equally sort of get the benefits over the next three years, four years or will there be some amount of front-ending of that?

Answer:

The ambition is to keep the savings wheel moving year-on-year basis, and it comes from a very simple philosophy, which says that efficiencies are there to be taken out of every set-up, however, efficient they are, number one. Why is it the case, because things keep changing and when things keep changing, you need to go back and look again to figure out what could be a way to make money out of that. And as long as change, we all know is a constant, efficient savings will also be something that we will continue to drive. And hence, this is a way we are galvanizing rank-and-file in the organization. So every year, I'm keen to see a 6% savings come through, which we will deploy at various – I mean it just gives us degrees of freedom to operate the business with.

Percy Panthaki:

Understood. Sorry, to belabour this point, but I mean, see, in this quarter, we have seen a significant acceleration in your margin expansion trajectory, and this is in a quarter where we don't have too much of operating leverage, because our sales growth has been affected by some amount of destocking. So, if I adjust for that, actually I mean your EBITDA margin expansion could be 200 bps or something like that. Now in this context, what I'm trying to say is if this is the kind of margin expansion that we're seeing this year, obviously that pace will not continue going in the future. So it seems that this is getting front ended into FY 2018, if I'm not mistaken?

Answer:

I understand where you are going with this. The key point we are trying to make here is slightly different. We're trying to communicate what the culture we want to drive within the company, yeah, number one. Number two, with respect to the numbers per se on our margins are based – declaration we make, which is about modest improvement in operating margins stays good on all situations, which we are, barring of course if there is an irrational price competition.

Second, we also look at it as a full year, and then operate on a year-on-year basis, because we love to keep degrees of freedom, because objective here is volume driven growth and margin improvement in tandem. And hence, for example, if you're going to step-up the innovation grade, so you're taking Ayush National for instance, we will – we are going to – these savings program gives us degrees of freedom to invest, so that we're giving our innovation a full bank for their buck. And that is how we look at these things. Create the degree of freedom and then deploy it, so that we always treated as a source and use of funds.

Percy Panthaki:
Fair enough.

Answer:

The use of fund depending on what are the returns that we are seeing and what are the competitive situation in the market, multiple variables go into that. But the guys have to generate the money, which is the entire company, not just some three guys or four guys, who are trying to generate money, everybody has got the mandate to generate the money and of course as a business we will decide how to deploy it. We're just trying to – maybe I could have done a better job there, we could have – we're trying to communicate, what is the culture of savings that we want to drive within the company, which is giving us degrees of freedom.

Percy Panthaki:

Understood, sir. And just a quick question on the destocking related to GST. I mean one way to get a sense of, how much is the underlying growth and how much is impact of destocking would be to look at sales in April and May? So any colour you can give me on that?

Answer:

See at a – I knew, this is a key one for you guys and let me help you there. Sections of the remaining trade - GT, MT very difficult to read, because we're still seeing through the fog that is there. But one clear callout is CSD, where we believe the full stoppage of purchases in the month of June impacted by almost 2% at a quarter level on our total growth rate. So we would've seen maybe a 2% more growth, if they just bought what they normally buy in this period. So that is a clear one and we also know that they haven't bought for another 15 days, they're just about starting to buy in the last two days, three days. So almost 45 days – 40 days - 45 days of sales stoppage means that pipelines is CSD are likely to be very, very thin indeed, and we need to quickly get the stocks going in there, so that we don't lose off-take there. So that's a priority for us at this point in time.

Percy Panthaki:

So, at your distributor level, there is absolutely no change in the stockholding, is it?

Answer:

No, none.

Percy Panthaki:

Okay. Okay. And last if I may squeeze in one quick question, we are aware of some of the price cuts you have taken, but that too only the ones which are sort of very heavily advertised. So, if you can give me some idea on what are the SKUs on which the price cut is already there in the market? And also, if you've taken any price increases till now, if you can just give us a few examples of that?

Answer:

I think price cuts, you will see a lot more coming through, I think we have just advertised the ones, because we can't advertise every price cut, but we're advertising the ones that are really big and impactful, we've done that. But at the same time, you'll see a series of network landing from now onwards as the lead times of the network kicks in. Because some of us we were able to take a punt on it and then launch well ahead of GST cut over date, others we had to just wait till July, we must not forget that June 12 was the date on which the official July 1 was confirmed, so there are networks that got triggered on June 13 onwards, but there are others where we've took a call, because we knew it is broadly coming in there, so went in early as - and also the rate. Yeah. So, that's what has happened, and therefore you will start seeing a lot of it happening landing between from now onwards.

Percy Panthaki:

Okay, sir. That's all from me. Thanks, and all the best.

Answer:

Yeah. Thanks, Percy.

Operator

Next question comes from Mr. Amit Sinha from Macquarie Capital Securities, Mumbai.

Amit Sinha:

Yeah. Thanks for the opportunity. The first question is on the gross margin side, and we have seen 80 basis point of margin expansion during the quarter. So, is it coming on account of lower promotional offers in the personal wash segment or this is also some of the benefit coming from the lower material cost during the quarter?

Answer:

Combination of both, Amit. It's also the savings, because material cost inflation also means there are savings opportunities there as well. So, it is a combination of savings, trade spend reduction, as well as material cost at an overall commodity level towards the end of the quarter, but I don't see that impacting too much in this quarter.

Amit Sinha:
Okay. Sure. Secondly, sir, on the Home Care margin front, now this is – I mean this quarter also we have seen significant improvement in the margin, and this is now becoming almost a trend in the last two quarters. And last quarter, you highlighted that, this is in line with your overall company strategy. Now, I just wanted to understand that, is there a dramatic shift in the portfolio mix starting last quarter, because last quarter some of the answers – I mean some of the reasons which you gave was a pretty generic and – but the trend is pretty powerful in the last two quarters, specifically.

Answer: See, I think the Home Care performance has been a story for the last five years, and not just in the last two quarters. So it has been a step-up that has been happening consistently. Premiumization clearly is one of the drivers which you've seen it, we are again reporting strong performance of Surf. But it's also about operating leverage, it's also about savings, ZBB on, for example some of the work on the logistics also a yielding returns. The operating leverage given that is - you're able to drive better volumes in laundry also means operating leverage kicks in as well. So, it's a combination – it's a pretty comprehensive program and in our savings slide that I talked about one of the lead standout categories there has been Home Care.

Amit Sinha:

Sure. So there is no portfolio shift which we need to be aware of? I mean what I mean to say is, has the focus shifted to some brands or we are going little slowly on some of the lower margin brands, something like that? I mean should we be aware of any – on any of those portfolio shifts?

Answer:

Strategy is consistent. We will play – we will straddle the portfolio, and we'll play all parts of the portfolio, and we want to win in every sub segment that is there; that's our going in position. Therefore, if you look at this quarter, Wheel has also grown, mass market has also grown very well for us. So therefore, it is absolutely business as usual when it comes to playing all segments of the portfolio. But what we are definitely disproportionately driving is seeing to push the premiumization agenda, not just through intervention, but also innovation. Take Matic launches – Matic liquid launches that have come through. It is one of the really, really good performing launches for us. And we quite like what we see in the way that particular brand is performing in its various formats, be it the bar format, be it the powder format or the liquid format, and that is something that we really use, we do disproportionately drive, but the focus remains everywhere.

Amit Sinha:

Okay. Thanks. And last question from my side would be on the personal wash segment. Are we gaining market share here in the last two quarters? And is there any impact on the unorganized players, because of the volatile nature of the raw material in that particular segment?

Answer:

Yeah. We have been growing in tandem with the market in personal wash. And as far as the impact is concerned on the unorganized player, I think we'll have to wait and see what happens post implementation of GST, yeah, and that is where, people who have hindered to not being paying taxes, their cost of doing business will go up and that is when we will start seeing the impact of the business. But a couple of quarters back, yeah we were a bit wobbly on personal wash and I'm very pleased to tell you that the last two quarters the rhythm has come back.

Amit Sinha:

Yeah, so has that shift is already started happening in the segment. I understand GST...

Answer:

Its early, give it few months, before you can see it visible in the marketplace.

Amit Sinha:

Thanks a lot. Thank you very much.

Operator

Thank you very much Mr. Sinha. The next question comes from Mr. Abneesh Roy from Edelweiss Mumbai.

Abneesh Roy:

Sir, congrats on good performance. My questions are on your distribution channel. So CSD, what we are hearing in July also the recovery has been slow. So what's your take on when CSD will normalize? And then sir, modern trade, clearly we are seeing the players asking for more margin. So from – specific players, so there, how do you plan to manage that, if you could give some colour?

Answer:

Okay. Let me first take up CSD, you're right, CSD has been slow in recovery, but we have started supplying to few of the depots and we hope that in the next few days this trend will continue and they will get back to the normal buying pattern. It's very important for us, because CSD is one of our real big customer.

As far as the modern trade is concerned, you know we always look at margin in a very fair and equitable manner. That's what our perspective is and we have been able to ensure that all the players, be it GT or MT, wherever they had an extra cost because of GST we have been able to increase the margin to compensate them for the increased cost. And that's the principle we have followed across the channels.

Abneesh Roy:

Sir, my second question is on the Axe Signature grooming range, you have come out with shaving cream and after shave lotion, so in these two segments already entrenched players are there, so what will be your strategy? Do you want to be a niche player here leveraging on the Axe brand or you want to be aggressive player and you'll go after the market share from a longer-term perspective, a leadership position in terms of market share?

Answer:

No. One of the very clear trend which we are observing is increase in the growth rates of male grooming products. And Axe is a great brand and it has a big play in male grooming in many parts of the world. So, we are very clearly looking at how do we improve our play into men grooming and not just in the deodorant segment. So, you will see, getting into the future, more activities in the male grooming segment.

Abneesh Roy:

And, sir, lastly in terms of Ayush National, when do we see mass media aggressive advertisement here? Here, are you going to target share of voice, which is basically Ayush versus the number one herbal player, will you be doing like that in terms of advertisement? And similarly in terms of outlets, what will be the kind of penetration you want to look at Ayush from an outlet perspective, from a longer-term perspective?

Answer: See, Ayush, it has just started, the primary shipments have just started. Yeah and as you know, Abneesh, the first thing we do is primary shipments, then we do the distribution and once it reaches a certain threshold of distribution, then we start the communication. So wait for another two weeks, three weeks and you'll start seeing much more activity happening in the marketplace.

Yeah, we're very clear that it is not about against the number one player or against the number two player, our focus is on consumer. So we will be looking at it, we have a very clear communication strategy and the next time, when we converse, you can really tell me whether our communication appeals to you or not as a consumer. And whole idea would be to get our fair share of voice as far as Ayush is concerned with the consumers, and we keep building the brand. It's a multi-category launch and we're very pleased with the results in South India and now we're very excited in rolling it out nationally. Too early to paint a picture about what the numbers would be, but let's take it quarter-on-quarter, we're determined to make it a success.

Abneesh Roy:

So, why I'm asking this is, Citra which was launched later than Ayush, already we're seeing aggressive advertisement of that, but in Ayush

Answer:

Let me explain. Lever Ayush was launched only in South of India. If you look at the channels in south, you will find pretty good communication happening on Lever Ayush, whereas Citra went nationally, much ahead of

Lever Ayush. Lever Ayush nationally they are just starting the primary shipment and the question of national communication starting hasn't even happened. That will take a few weeks before we start that. So please don't compare, but let me tell you, we are committed to both the brands.

Abneesh Roy:

Okay. Okay, sir, that's all from my side. Thank you.

Answer:

Thank you Abneesh

Operator

Thank you very much Mr. Roy. Next question comes from Mr. Arnab Mitra from Credit Suisse, Mumbai.

Arnab Mitra:

Yeah. Hi, thanks for taking the question. Just wanted to understand what is the problem in GST regarding small retailers, because I thought they would be least impacted given that they can possibly remain under – they need not register. So is it that distributors are finding it difficult to bill to them or – and can there be actually a sales loss here, because these are end-consumer outlets?

Answer:

You are absolutely spot-on, they should be the least concerned about it. But what we are seeing is a lot of misunderstanding. Do I need to be registered, do I need to put HSN number, what do I do with my consumer? I think there is just a lot of confusion in the trade and some of the advisors are not giving the right advice for them. So, our objective is to ensure that we are able to clarify that, we have put together a complete myth versus reality kind of a communication that is going out into the field. And we are hopeful that we will be able to get them on another side of it pretty fast. But most of it is just confusion – needless confusion when it comes to small retailers.

When it comes to wholesalers, slightly different, where there is also concerns on can I bill to an unregistered dealer, do I need to print HSN code on that, what do I do with my – do I need to change my business model for instance. So those are conversations that they are going through with their advisors as well, and that is something that we need to take it towards logical, and they need to make up their mind and move. So, that's the focus on that.

Arnab Mitra:

Well, as far as your distributors are concerned, there is no reluctance to bill to non-GSTN and parties, because I heard there is some confusion even among distributors, also I think the law is pretty clear on that?

Answer:

None at all, we have taken every one of our distributors through extensive training and they know exactly what needs to be done. We're also using them, in fact, that is the only way to convince the trade as well. Because the best relationship is actually maintained by our distributors in the trade. So therefore we are wanting – we are working with them to get into trade and get them to explain to them in their own language, in their own reassuring way, so that it can happen. But all our distributors are 100% registered, and they are billing exactly in line with what the laws allow.

Arnab Mitra:

Sure. And secondly on this question about passing on the net benefits to the consumer. So is there a – I mean, how do you figure out what is supposed to be a normal price hike in FY 2018, because besides everything there's a normal pricing increase which a company can take over and above net benefits. So is there a philosophy on how you're going to work around that?

Answer:

The approach is very simple. We know exactly what are the net benefits that we are getting and that net benefits we've actually put out the entire network for that and we are passing that onto the consumer. So that's an immediate intervention that's happening as we speak and that is what we will implement on the ground. So going forward, in terms of commodity movements etc. those are in the future, but for the immediate intervention, it is the entirety of it.

Arnab Mitra:

So what you're saying basically is that, you pass on the net benefit and from there on depending on what happens to commodity and other things there can be normal pricing in the rest of FY 2018?

Answer:

Yeah, it is reset to a different level, there are traditional playing all lines of the P&L with huge savings program that we have put in place, all that will be brought into bear. But I think we are clearly cutting it as to two cuts. There is in – as we stand on July 1 and look at what our numbers are, exactly what the GST impact is and that has been passed on as pricing.

Arnab Mitra:

Sure. And just last question on the factory in Assam, I – basically I see that the excise duty is down by about 20 bps on a Y-o-Y basis, so any kind of number you can help us with on, how this number might trend for the full year, given that the factory might be ramping-up now? I mean, what kind of reduction can be there?

Answer:

Yeah. So, one of things you did call out if you recollect in the previous quarter was the impact on the ETR line, so that is something which is very difficult for you to quantify.
As far as the excise duty, I mean that factory is just about ramping-up. So, this excise duty reduction is more about productivity across the entire factory network that we see, including Uttaranchal, where you again have the fiscal benefits, the old units of NESA which is again there. So, that's what you see as a number there. And we will of course – at an appropriate time we'll come and share with you, once that factory has ramped-up, it is still ramping-up towards, it's got its first 1,000 tonnes done in the last, what about two weeks, three weeks back. So, it's in a good wicket, ramping-up as in line with plan.

Arnab Mitra:

Sure. Okay, thanks. That's it from my side.

Answer:

Yeah. Thanks, Arnab.

Operator

Thank you very much Mr. Mitra. Next question comes from Bhavesh from CLSA Mumbai

Vivek Maheshwari:

Hello. Hi, good evening. This is Vivek. I have three questions. First on what Percy has asked. Balaji, I mean you have mentioned about 6% saving on turnover. I'm sorry if I'm repeating, but you know I quote Unilever Plc's release on April 6, which clearly mentions that, operating margins are at 16.4% in 2016, target is to take it up to 20% by 2020. The issue with 6% savings when you say, is it the base is, year FY 2014, FY 2015, FY 2016, FY 2017, because there is a modest improvement in margins every year as you have your self also called out. So what is the starting point and by when you target to hit this 600 basis points, I'm still not clear on that. Can you just quantify in the same manner as the parent does it; 16.4% in 2016 to 20% by 2020?

Answer:

Yeah. Hi, Vivek. I think the – okay, the point I'm trying to make here is maybe we could have done a better job with the slide that we put out there. Let me try and start again. The savings program this company has a fundamental DNA of how to drive savings, and therefore what we have tried to do is turbo charge that DNA in terms of looking at an end-to-end approach to savings, different lenses, different people, get the whole organization charged up to deliver savings so that we're able to galvanize them.

Every year, 6% of savings is something that I need to see - that is the source of fund, and this hits all lines of P&L. We look for cost avoidance, we look for cost savings, real cash - everything is put into it, because we want people to get into a mind-set of saving money. Once we get a real money out of it, it's something how we deploy it, because these are the money that go towards, for example, if inflation has happened in crude, and we're not taking pricing, that is something then obviously go hit the margin, but it's something we use for. These savings becomes a DNA with which we deliver. This is something that we know exactly how to do and we've been doing it for many, many years. It is not that, but we've stepping it up year on year on year. It used to be 3.5, we moved it to 4. From 4, we moved to 4.5, 5, 5.2, 5.6, 6. We're now slowly seeing this number inch up because the business is getting into a rhythm of how to make savings, and you then add a net revenue management into the mix.

There's a new dimension as we look at turnover generating the art of pricing, or you look at what is the best way to actually drive zero based budgeting program where we change BMI lens of how to go over looking at it. This then turbochargers the savings delivery. That's an engine that keeps spewing out the source of fund and then we use it for managing pricing. If you recollect something that we keep saying all the time, when our inflation happen, we love to play all lines of the P&L.

This is how we go about playing all lines of the P&L, so that we are able to deliver a good flexibility to the business to take all the decisions that it wants to do and doesn't constraint itself from a source of fund. So that's the fuel for growth that we are generating. And then we then deploy the fuel for growth for delivering various initiatives.

Vivek Maheshwari:

Okay. So basically this 6% you are seeing, as a percentage of revenue, is the gross saving and the effective saving at the operating margins is a function of how many things you do out of the 6%. So if there is a new launch, if you want to expand Ayush, all those things would be funded by this saving. Is that what you're trying to say?

Answer:

Absolutely.

Answer:

Absolutely. So this is not a margin guidance that we're giving. This is the culture that we're trying to share with you as to how we generate the saving, number one. And as far as the improvement in margin is concerned, the modest improvement in operating margin continues. There's no change in that as concerned. It is just that we are then turbocharging this engine of saving, as times get more turbulent and we are able to then need more fuel to navigate.

Vivek Maheshwari:

Okay. You have been for ages mentioning about modest improvement in margins, which has been happening, but have you ever thought of doing something like what parent has done in terms of being definitive about 16.5% to 20% like the parent has done?

Answer:

We don't see the need for it for two reasons. I'll tell you why. Firstly, I think, we are profit accretive to Unilever, which means our first priority for us is to deliver volume-driven growth, because this is a country where opportunities, if you look at per capita consumption, penetration levels is so huge. The way we create value on a long-term sustainable basis is to deliver growth. And therefore that we are committed to, we have put it out there as a 4G growth model. You've seen that we are very consistent in our messaging there. And secondly, the reason why we called out the savings slide this time is also to say to address the request coming from all of you saying that how are you going to generate the money to fuel for growth given that already your margins have peaked, etc. We said, no, this is a culture and not a number on which we operate. And we're keen to then turbocharge that even more as times get more turbulent.

Vivek Maheshwari:

Okay. Sure. Second question on CSD, can you repeat the quantum of impact or hit in the quarter? Did you mention 2% sales impact for the quarter?

Answer:

That's right, 2%.

Vivek Maheshwari:

Wow, okay. Okay. And on the GST bit – but you mentioned a lot of things about trade. So let's say India has 10 million outlets, wholesale has an impact, trade has an impact, sitting on, let's say, 15th, 16th of July or first fortnight of July, where do you think is channel right now or the end retailer right now, given that you are still talking about the wholesale issue? You are still talking about confusion in the trade channel. I appreciate that you're working with the channel, but where exactly or how much time basically it takes to come back to almost virtual normalcy, let's say, in coming time?

Answer: This is very difficult to fathom, because there is a significant and a fundamental shift, which is required of wholesalers, yeah. They would be operating in a very different fashion hitherto and now we are talking about getting into the formal net. So many of the wholesalers have to go back, evaluate how they want to do business, what will be the new business model, and this is where they are seeking clarification. But I think for many of them, this is a big source of livelihood. So we would expect them to come back and start the business again. But there would be some level of channel reset, yeah, which we believe that organized wholesale will become stronger. And just speaking to Walmart the other day, yeah, the number of customers they have enrolled in the last couple of weeks have been much higher than what they have done in the past, so which is a very clear indicator that organized wholesale will go up. But India is such a big nation and the hinterland is so massive that wholesalers will have still a big role to play in the distribution of FMCG products and I think they will come back and we would want them to come back, because they are our important channel partners.

Vivek Maheshwari:

Sure. Just a follow-up. In that context, I mean, if you're saying they will come back and you are hopeful about it, does that mean that business may still see some level of below normalized growth, let's say, for next couple of quarters or maybe even for rest of F 2018?

Answer:
Like difficult to put a prediction on it. But this quarter, right now, we certainly see turbulence. There's no question about that. But I would also expect that as the quarter moves in, moves up, we will find more normalcy coming in.

Vivek Maheshwari:

Okay. Okay. Sure. Thank you very much and wish you all the very best.

Operator
Thank you very much, Bhavesh. Next question comes from Mihir P. Shah from Deutsche Bank Mumbai.

Manoj Menon:

Hi, team. This is Manoj here. Just one question on the zero-based budgeting bit Balaji. If you could walk us through maybe two or three examples of real life situation, because you did quantify for the A&P lines example. While there is some clarity on what you're trying to do on the A part of it, if I go by what Unilever has commented on how they looking at ad spends, so there is I think fair amount of clarity. But generally if you could take two, three line items and give two or three real life examples that would be very helpful.

Answer:

Yeah, we will do that Manoj. Let's take individual line items, yeah. Let's take an item like the P side of the A&P. How do you run promotions, and what are the justification for promotions, particularly third-party gifts. It is something that we are now wanting to take a very, very hard look at to say that is this really adding value in terms of brand equity in the long run. If not, there's no point running it, one way of just clearing out the entire pipeline there.

Taking a very hard look at trade spend, which is TTS side of it, where if you recollect the works that we had done on aligning the trade spends to the channel objectives. And one of the reasons if you look at, let's say the Tea business or the laundry business profitability improving, which you're seeing, we have reduced TTS big time in these categories because we don't see the need for just trade promoting something when your value weighted distributions are pretty high, depth of consumption. You don't need the depth at that point in time, versus running a trade promotion in a category which requires more visibility, in which the way you run the trade spend changes very differently.

Or let's take an item, which is very different, like logistics. Why is that that your secondary logistics costs per tonne per kilometre is significantly higher than primary and what can you do to optimize that? How do you, therefore, get a loadability of trucks for them? How do you design packaging in such a manner that you are able to optimize the volume density ratios of trucks.

Or you take a look at items like overheads line items, flight costs, what are the amount of trips that you travel, how long do you travel, what do you do when you do a hotel booking, how advanced booking that you do on this? So it's a pretty rigorous and robust way in which you look at every line item in that and that is what we are seeing as benefits coming through. Gives you a sense?

Manoj Menon:

Yeah, understood. Now the reason I asked this because any change kind of change in the equilibrium, so I'm just trying to understand that you – actually seems to be from the reported results, you're doing an excellent job because on one side, you're getting the savings and other side, you're getting the revenues, and obviously, I can't quantify the things the softer part of what is happening in the organization. But on the harder side everything seems to be – so I'm just trying to again probably I'll just catch – ask you separately to – ask a little more because any changes. So I was just wondering what has really changed apart from the culture that you mentioned.

Answer:

Spot on. I think you really hit the nail on head in term. So if you try to drive this kind of savings agenda and pressure with this kind of turbulence, what does it do to the morale of the people? Let me give you a very live example of the kind of engagement and the whole thing links to the kind of engagement people have in HUL and the kind of – how they throw themselves at it and there can't be a better example for this company than the way it went about implementing GST. Every function, be it sales, be it marketing, be it supply chain, procurement, finance, IT, threw themselves at it and the kind of fun we have had trying to implement GST has to be seen to be believed. So therefore there is no better way of explaining the fun and the passion that we have for this company and the way we've gone about doing it. So these are all things that we quite enjoyed doing it, pulling it together. I feel Sanjiv has got better perspective than me on this.

Answer:

Yeah, Manoj, good you raised this question, yeah. Very often when you look at cost savings, it is relegated to the back office. You have few guys in the supply chain, a few guys in the finance team helping pull together and kind of driving down cost. But when you instil an owner's mind-set in the company, then it is not a job which is done by a few people. Across the organization people look at how do you create value.

One of the things which you would always ask yourself that HUL has always been a pretty efficient organization. How is it that they would be able to still drive cost efficiency? One is, look at how we have organized ourselves. The whole concept about CCBTs, which we shared with you at the Investor Conference - that has dropped in a huge element of entrepreneurial spirit in the company. They are virtually operating like a mini board of the company, running the category as if they were the owners. And they're looking at newer ways of doing things, harnessing technology which wasn't available yesterday and that is where the mind-set of unlimited juice in the lemon comes in. So this is not something that, because we are very efficient, we can't be bringing in more effectiveness and efficiency.

Look at NRM, NRM is a science of pricing. Yeah, we have brought in newer concepts. Similarly, the whole value chain is up for grabs and we're looking it very closely and seeing, okay where can we bring in technology, where can we bring in more efficiency. Now, ZBB, it's not just about a budget mind-set and reducing expenditure. This is about how do you bring in more science to media for instance. Yeah, and that is where the efficiencies and effectiveness comes in. So, it is a philosophy, and we have been fine tuning it over the last couple of years. We've shared with you how from a 3%, 3.5% savings rate for the last couple of years, we've been running it at 6%, and then bringing in more science through NRM and ZBB; we've been able to sustain savings at this level. So, this in fact is giving energy to the people rather than draining energy.

Manoj Menon:

Understood. Understood, very clear. Just one follow-up on this, is that, are there any changes to the – broad comment would do, on the variable compensation structure for the middle management? Of course for the top management I can actually look up on the annual report, but beyond what you see in annual report?

Answer:

The middle level managers?

Manoj Menon:

Yes.

Answer:

Can you repeat the question, Manoj, we just...

Manoj Menon:

So, what I'm trying to understand is, is there any additional incentives for the guys who are actually executing to actually drive these cost savings, this year versus the years before?

Answer:

First and foremost it's the professional pride, guys. We don't come excitedly to work for HUL just because of the remuneration, yeah. The second important bit is, we have a very clear fair remuneration for our people, which is built on a fixed pay and which is built on the variable pay, variable pay has a cash component and then also you can invest in the shares with matching contribution by Unilever. So that's where the whole package is. And we constantly benchmark our package to ensure that we are competitive. And to our best guys, we of course give them package, which would be at the top of the peer group, so that's the whole philosophy.

Manoj Menon:

Okay. Okay. And then just quickly on the price growth part of it if I see the current quarter, the price growth value you alluded to some of the reasons in your opening remarks, is it the right way to look at it saying that, there are some price increases push through earlier, because when I go back to the Jan, Feb, March, or maybe starting November, December last year, the outlook was that the inflation is – cost inflation is coming back and there was some price increases push through and the inflation has probably kind of reduced, which is also there in your – in the last slide in your presentation. Is it a case of the price increases going through and the input cost kind of fallen after that? Is it a timing mismatch bit?

Answer:

So, if you look at the early part – let's say December quarter as well as the March quarter numbers, the commodity inflation actually started peaking and we've seen the forecast coming through, we've seen the particularly, if you look at vegetable oils, the Lauric part of the portfolio had a significant inflation, which we have signal time and again. It's not that, we've not signalled that. And what we did see through was that, we saw that towards the end of March is when we saw the forecast starting to come off and we could also see the crop coming through et cetera. So, you saw the cost impact of it play out in the early part of June quarter, but thereafter we saw Laurics cool down to a significant extent and then stabilize at that level, at this point in time.

Almost identical when it came to crude run up all the way from $35-odd all the way up to $54, $55, and then back to about $47, $46 kind of a range there. So, it is a clear case of – one of this quarter when you realize July 1 was always the case that was possible but not necessarily confirmed. So, the minute we realized it is likely to happen July 1, we pulled off all pricing from the market because, we had a vested interest not to push stock into trade and also ensure that especially when price drop is coming, which is what categories like soaps and laundries, one of the biggest commodity-linked categories are there that is the reason we then pulled off the pricing completely from there, because it's a very different dynamic post July 1, which is what you see play out in the numbers as well.

Manoj Menon:

Understood. And one last question on the detergents category. Now that you have a lower GST rate for the bars and a slightly rate for powders, but if I look at the long-term, correct me if I'm wrong, the understanding is always that consumers trade up from a bar to a powder – and so, there's two questions here. One, what is the market construct today of bar – powder versus bar. And secondly – what are the – is there an opportunity for you as the market leader to drive bars given that there is a price differential possibility to the consumer?

Answer:

Yeah. You're spot on. The long-term trend is clearly an upgradation from bars into powders, but the bar portfolio is a sizable part of the portfolio, and from a consumer perspective so that you're clear about it, given that bar is a topical application and also is used as almost a stain removal or custom caller kind of a product, as well as something which is given to the maids who actually wash off and given that machine penetration is not all that high, and when you want to have real tight dosage in terms of how much you want to put in, bar still has got a role to play. We just can't just wish that away saying that it is just one needs to find a way migrated into powder. Because dosage control for the consumer is highly value conscious, which is the reason we still continue – we are fully committed to the bar part of the portfolio and we continue to drive it very, very actively. And the best bar product that is out there is the Surf excel bar, and it's a lot of work that goes towards creating that product, as well it has not been copied so far, because it's got a different technology associated with manufacture and we'd love to keep it that way.

So, whether will we continue to invest in bars? Absolutely, yes. Will we continue to drive the upgradation, premiumization? Absolutely, yes, but then we have to leave it to the consumer to then decide when does she want to make the switch. And we cannot force the pace beyond what the consumer would want to do.

Yeah. And just to amplify what Balaji said, first it is not about less use even the powder users they do use bar within that, yeah. And as far as commitment to bars is concerned, recently we have launched Rin bar with the smart foam technology, which reduces the water consumption by half. That is again a very worthwhile innovation and clearly shows our commitment to the bar business in the detergent portfolio.

Manoj Menon:

Understood. And just what is the size of bars; let's say at the percentage of the industry today in detergents?

Answer:

Yeah. It's about 40%.

Manoj Menon:

So, it's not really moved actually, right? I mean, so if I think about what it was five years or seven years back?

Answer:

Yeah. Because, both have grown and within the powders, a lot of shift has happened in terms of upgradation.

Manoj Menon:

Understood. Understood. Thank you so much. All the best guys.

Answer:

Thanks, Manoj.

Operator

Thank you very much Mr. Manoj. Next question comes from Mr. Mihir Popat from Arya Fin-Trade, Ahmedabad.

Mihir Popat:
Yeah. Hi. Thank you for the opportunity. So, my first question is regarding Food business, what led to this significant improvement in this Food business margins?

Answer:

Yeah. Foods business at an overall size level is very small. A small movements here and there in BMI could move the numbers, so don't read too much into it.

Mihir Popat:

Okay. And regarding oral care performance, if you can throw some light there with respect to competition, market share and all that, new launches if any?

Answer:

I think the big one on Oral Care is the Ayush – Lever Ayush launch that is also happening in national. So that's going forward. But in terms of performance for the quarter, I think it continues to remains subdued, but we must keep in mind CSD a big piece of the puzzle when it comes to oral. So, it's difficult to read what of it is offtake and what of it is channel.

Mihir Popat:

Okay. If you can guide something regarding market share, in oral care if possible?

Answer:

We don't comment on market share, but suffice it to say the performance is not necessarily where we would like it to be. Yeah, Oral care is a category where we ourselves have not been very happy with the performance. In terms of intervention, now oral care, we have explained earlier that a large part of the market has shifted through the Natural part of the segment. Where we did not have a play and only now with Lever Ayush, we're getting into the play and we would want to drive Lever Ayush in the oral care pretty high.

Mihir Popat: Okay. Okay, that's it. Thank you.

Operator

Next question comes from Mr. Prasad from Investec, Mumbai.

Prasad Padala:

Hello, sir. Thank you for the opportunity. From the other expenses chart, so I guess there is some part of bonus clause provisions in last quarter, in 1Q FY 2017. So has that come down this quarter, I mean what is the impact due to that?

Answer:

The growth of bonus happens once a year and from that perspective, we continue to true up it where in March quarter, we had the true up happen. And as far as other expenses is concerned this goes more into the employee cost line. And other expenses line is more about productivity and leverage coming through particular supply chain cost that you see there.

Prasad Padala:

Okay. I mean, my question is, sir, if you look at employee expenses and if you exclude this bonus in provision, so what would be the decline or increase in the employee cost?

Answer:

I think as far as employee costs are concerned, suggest we take a full year number on this because, there are moving parts at the time of the true ups that happens there. But on a more conceptual level, I think the productivity drive that we do in every lines of the P&L is equally relevant for the employee cost as well. And this includes both the number of FTE's that we operate with as well as the cost and the various other costs that we incur as we have people in the organization. So, every line is looked at quite spread there. And we would definitely keen to see productivity in that lines as well, as is normal we've always been doing it for many, many years on this one

Prasad Padala:

Okay. Okay. Fine, sir. And sir, you used to give this number on underlying volume growth segment wise. So, I couldn't find it for FY 2017, I mean will you be providing that or any specific reasons that you are discontinuing or anything?

Answer:

We're not discontinuing it, just with the Ind AS transition is something that we have left it without – it will be there, but we will take it offline.

Prasad Padala:

Okay. Okay. Fine, sir. Thank you very much. That's it. That's it from my end.

Operator

Next question comes from Prasad from Bank of America, Mumbai.

Prasad Deshmukh:

Yeah. Question on the efficiency gains in the distribution channel, because of shift to GST. Is there any number that you can put for these kind of gains and how much of this is reflected in your 6% target going ahead?

Answer:

Target 6%, sir, what are you talking about? What target is 6% – fixed, sir? So actual 6% is...

Answer:

Can you repeat the question?

Prasad Deshmukh:

So, as we shift to – as we're now shifted to say GST regime, there was a component of efficiency gain in supply chain and distribution channel that was being discussed about earlier in terms of say, our transportation cost coming down and so up...

Answer:

Yeah.

Prasad Deshmukh: so, is there any component of that?

Answer:

Yeah. So what – see the 6% is the ambition with which we operate the company with. Clearly, for example GST savings will be an integral part of that. In our next year period if we're, going to deliver 6%, one of the things they'll look at is GST-related supply chain efficiencies that they could easily take, because there's a big change because of GST. So, therefore, we'd want them to draw after this and get that component, that's how we drive it. So, clearly, this is rally in price, which is in use for getting people on here.

Yeah. Just to amplify, because this question has come up more than once. So, when we look at 6% of turnover, while we – that's what we aim for the components of savings change every year. In some year, we were driving NRM very hard, sometime we would be doing the ZBB work, next year we would be getting the GST efficiencies in. So, we pull in different levers at different time. So that we keep again moving towards the 6% mark, which gives us huge flexibility to invest in the market development, innovations and also ensure that we keep doing in a very rhythmic manner, the modest improvement in margins.

Prasad Deshmukh:

So, is there any number you can put to these gains for...

Answer:

Early days, we are fleshing it out.

Prasad Deshmukh:

And when will these be visible roughly and safe to say next quarter or it will take like...

Answer:

See the plans are very much in place, we have a clear roadmap and network of how we intend to use out all the efficiency measures that are there. But that's an internal part of the company. And we don't intend to discuss that in the public domain for obvious reason. And we will ensure that on our – there's a clear governance within the company to ensure those benefits are secured in a time bound manner in line with all those changes. Don't underestimate the change needed to get this efficiency. For example, if one has to close the particular DP, it's quite a significant amount of work to be done to ensure the transition managed so you don't have transition losses while you're doing this kind of work. So, it be will risk – ensuring the manner that risk is well managed and delivered. And we've already shown in GST how we do it. So we intend to repeat it as we go forward as well.

Prasad Deshmukh:

Okay. So, whatever efficiency gains are there, those will be over and above the zero-based budgeting that you're doing, otherwise I mean, otherwise on the on the P&L?

Answer:

Yeah, so it's a source of funds. And how we deploy that will be decided by the management committee. And we stay committed to modest improvements in operating margin. So, these three, all go together. So, I would resist the urge to add numbers on top of it because there are also clear calls we will be taking as management to drive volume growth. And our intention is to grow the business by investing be it the market development, be it in capabilities. There is a whole cost of investment opportunities within the company to ensure it is fit for future and we're future ready. So, I would resist the urge to add these numbers linearly.

Prasad Deshmukh:

Got it. Second question is on response to your Ayush toothpaste. Just wanted to get a qualitative sense as to how the response to this particular product has been. And can this actually address the issue in oral care that we have faced so often?

Answer:

Yeah. Let me say that when we launched it in the test market of South India, it met the action standard.

Prasad Deshmukh:

All right. So, okay, fine. Thanks a lot.

Answer:

Thank you.

Operator

Thank you very much, sir. Next question comes from Mr. Naveen Trivedi from HDFC Securities, Mumbai.

Naveen Trivedi:

Yeah. Hi, good evening everyone. Since your GST implementation was very smooth versus others, do you see any such opportunity to gain market share because of this?

Answer:

I think there are two stages in that. I think too early to call it out. It's our intention when we execute a project flawlessly is that it has to benefit the organization, and that's how we have rallied the full organization to do it. But too early to comment on anything, task does not – it is just two weeks into GST and lots of work still to be done. So, let's stay close to – our objective is to put our heads down and get the work going, and how it plays out in the market, let it play itself. We believe we have fired all the right interventions in the right sequence, and let it play it out in the market.

Naveen Trivedi:

Yeah, certainly. Your objective was very clearly mentioned. I'm just trying to understand if any such opportunity which has built up, because the vacuum was there in the retail market, and if we are ahead of the others, we might gain market share at the retail level?

Answer:

I think we wouldn't want to comment on it, till we see it. So, obviously there is something that's an ambition and then there is reality, let the reality play out would be my submission.

Naveen Trivedi:

Certainly. One book-to-bill question, if you can mention the – how has been the rural and urban growth during the quarter?

Answer:

Rural-urban, I think from a point of view of growth has been pretty similar, both rural-urban operating in tandem, rural being slightly lower than urban unfortunately. And that is something in our call out as well we have said that we are expecting to see rural pick up going forward. And it is obviously all our hope to see rural actually do the 1 time, 1.5 times – 1.5 times, 2 times kind of growth rates of urban. For which I think a good monsoon is a good starting pointing. But there's more conditions that had to kick in as well. So, let's see how that plays out. So, we're expecting a gradual improvement in rural. It's not going to be an immediate switch on there and let us see.

Naveen Trivedi:

Yeah. Thanks and all the best to you.

Operator

Thank you very much, Mr. Trivedi. Next question comes from Sameer Gupta from India Infoline, Mumbai.

Percy Panthaki:

Hi, sir. Percy here again. Sir, just one question on the rural demand, weekly, in your presentation, you have said that it would recover gradually but looking at the agri price in the last couple of months, there is a deflation in agri price, which affects farmer incomes very much. So overall, agrarian distress in several parts of the country, so, but do you dismiss a possibility that instead of getting better from here the rural growth can actually get worse from here?

Answer:

I think it's a very good question, Percy. I think we did think through this both the pros and cons of it. And the reason why we have called out a gradual improvement and not a deterioration from here on is from three factors. Number one, the previous challenges coming out of two consecutive years of drought, which had taken down water tables big time and some of the more marginal farmers got seriously affected by that, which I think is expected to turn with the second year of a good monsoon that is point number one.

Point number two, with respect to the last year also had a demonetization impact, which actually affected the realizations. It didn't affect the sowing pattern but it seems to have impacted the realization of – on the farm produced, which hopefully will not be there this year.

Third the government is also equally cognizant of its challenge in rural, therefore there are significant loan waiver programs, I'm expecting significantly infrastructure investment that is coming in there, which will also alleviate some of the pain that is out there.
And particularly post demonization one of the biggest jobs, the employment generators of rural was also rural housing, which got impacted and we are expecting going forward actually the affordable housing will actually go up so, therefore that should also mean job employment opportunities in rural as well.

So, there is on the – you are right, there are both ways to look at it, but I prefer to see this as an optimistic scenario going forward, but of course tempering it with the fact that it is going to be gradual and also be very conscious there's significant population out there and therefore everybody is concerned about that population joining the mainstream economy and therefore that very focus will also ensure that we get the huge 2/3rd of this population back into the growth momentum as well. But it is a very important point that you're raising.

Percy Panthaki:

Understood. Understood. Sir, secondly my question on GST, basically the categories which you have benefit, soaps, detergent, bars and toothpaste, they account for approximately 35% to 40% of your sales and the categories on which there is an increase also account for approximately the same amount of your sales. On the one hand you will get input credit, which is of a higher amount than earlier, on the other hand you will get only 58% refund on some of your tax exempt site. So, overall the entire balance, so I'm a little surprised when you say that the net benefits of GST will be passed through at a company level because it seems that at a company level there isn't really any benefit that you might enjoy?

Answer:

What we are doing is, we are just taking into account the percentage of the business where it is going down and percentage where it is going up. But we are not considering the depth of decrease and the extent of increase, yeah. If you factor this in and the inputs credit then there is a net benefit.

Yeah, just to amplify what Sanjiv is saying, the input credit is available for everybody, for all the categories, therefore treat that as a credit that runs right across. And the category where it's gone down, it has gone down by substantial amount, yeah. And the category that's gone up it is an incremental number there, so that delta was in place itself out, and yes, there is an offset coming on the fiscal benefit, so that is the reason why we are calling out net benefit and it is a net benefit, I can confirm that. But you are almost reading out...

Percy Panthaki:

Would you be able to quantify how much is that net benefit?

Answer:

No. We don't intend to quantify for obvious reasons. What we want to see is you should see it in the market and that's how we would like to move forward and that's why it's equally competitive as much as any other number.

Percy Panthaki:

Okay. And while you have taken some price cuts; I mean, the price increases will they take longer or are they also more or less in the pipeline?

Answer:

In the foreseeable future we don't intend to take a price hikes, because we are seeking it as a net benefit at a company level, therefore we do not intend to take up price rises in the foreseeable future.

Percy Panthaki:

I see. I see. Okay. Thanks. Very helpful.

Answer:

Yeah. Thanks.

Operator

Thank you very much, Mr. Gupta. Next question comes from Mr. Abhijeet Kundu from Antique Stock Broking Limited, Mumbai.

Abhijeet Kundu:

Hi, sir. Thanks for the opportunity. I have two questions. One was the – in view of the price cuts and passing on of the benefits that you would be doing, would there be a moderation in sales growth, if the volumes don't pick up? I mean, yeah, there is even in a quarter where a lot of destocking happened yet you have shown a significant outperformance. But assuming the rural growth takes longer to recover, in that scenario there would be a pressure on overall earnings growth. Yeah, there would be some good amount of savings from efficiency but still the sales growth would it not be impacted, if the volume growth doesn't pick up to that extent?

Answer:

Let me clear the two questions here, two areas there. When it comes to the turnover growth, it is fair to expect that the price growth will moderate and volume growth will increase. And to the extent volume growth does not increase, will it impact turnover growth adversely, the answer is, yes.

However, when I look at the, just purely GST post price cut, if I take that, earnings growth, there is no impact. Because, whatever you lose in your turnover growth, you are also getting it in your cost line and that is what you're going to have. If I look at the accounting slide that I put out there, look at the right hand side of it, if I explicitly called out with respect to EPS, there's no impact because of GST and that's a fundamental sprit behind anti-profiteering.

Abhijeet Kundu:

Question was, we have been talking about it because of price – I mean, the passing on of GST benefits that would be one thing, which will be driving growth or volume growth over a period of time, which is more important. Is the compliance factor more important by the trade, which would mean that the smaller players will get impacted and the bigger players and the more organized players, they will gain market share? So what's your belief? I mean, price I believe will not be the factor, which will drive growth rate, I mean, more compliance will really drive growth.

Answer:

There are two elements to it. You're right. The fact that we're taking it as a company lever and the fact that we're doing a disproportionate investment basis of strategy, to give you an example, the fact that we're now saying premiumization is a key part of our portfolio, that's the reason you'll find that Dove is doing a 33% extra or Pears doing a 33% extra versus a Lifebuoy doing much lower than that. That's an integral part of our strategy. So therefore, one of the reasons we have done that we believe that is a way as a market leader, we need to drive the portfolio, bring our portfolio to effect. That's number one.

Number two, with respect to the compliance factor, I think only time will tell. Our objective is to ensure that we stay compliant. How does it do to the rest of the market, my intention is a lot of them would also want to be compliant and compete well in this market. But for some of them, the cost of this competing may have probably gone up because they're not used to the right ways of working. So we'll have to see how this plays along. We have fired our salvo. Let's wait and see.

Abhijeet Kundu:

Okay, sir. Thanks. That's all. Thanks.

Answer:

Yeah.

Operator

Next question comes from Mr. Mihir P. Shah from Deutsche Bank Mumbai.

Mihir P. Shah:

Yeah. Hi. Sir, just a quick question from my side on the Foods margin again. Sequentially, also there is a big change in the Foods margin and it has increased. Is there any seasonality there, or anything that we should keep in mind?

Answer:

Very small numbers and the savings program also land up there as well. So don't read too much into the Foods part of it, yeah.

Mihir P. Shah:

Got it, sir. Got it. Got it. Thank you so much. That's all from my side.

Operator

At this moment, there are no further questions from participants on the audio...Yes. So now I hand over the call proceeding to Mr. Aasif Malbari for the web question.

Question:

Thanks, for seeing this through. Now, I'll go onto the web question. I'll not repeat the question, which we've answered, but I'll kind of readout the names and we kind of go through all of them.

So the first one is from Chetan from Capital Markets Publishers. The question reads about what are the drivers for growth for the Foods business, EBIT margin growth, are these margin sustainable? This one has been already been successfully answered, so I will skip that. The second question from Chetan is what is the competition level in water business, any pressure on volume and prices?

Answer:

I think if you recollect, water had a very good first quarter, and it is the second quarter where the performance has been muted, particularly because of the GST runoff where trade destocked big time on durables. So we believe that's a temporary phenomenon, and therefore, we should get it back. We are happy with the strategy that we have put in place there. So I'm hoping to see this business come back once the pipeline issues sort themselves out.

Question:

Okay. The next question is from Chanchal from Birla Mutual Fund. What is the margin that Home Care business aspires to reach in the context of the global focus on margin expansion?

Answer:

I think I guess would not want to on the number per share, but the track record of this category has been good and we are very clear that track record needs to be maintained. And at the same time, again, I reiterate they need to grow, they need to grow volumes, they need to premiumize and they have improved their margins altogether. So it is a comprehensive packet they have to deliver for us.

Question:

The next question is from Abneesh from Edelweiss. It's about seeing a lot of Citra ads much higher than that of Ayush and question about how Citra is doing in the initial stage.

Answer:

I think early days, we have covered this point on Citra ads. So you should start seeing Ayush ads coming in, Abneesh, pretty soon. And watch the space. It's a pretty interesting mix. So you're going to enjoy it.

Question:

The next one again is from Chetan from Capital Market Publishers. How long will it take for the wholesalers and small retailers to return back to normal inventory level? Which is the one that you've already kind of spoken about? What is the GST impact on rural market retailers, wholesalers, especially in North India?

Answer:

I think one striking similarity is to demonetization is the speed with which North and Central India is taking to come back to normalcy and that's fundamentally read out of the magnitude of wholesale there and team has to get on to the formal modes of what we saw. This is probably the biggest focus area of us as well.

Question:

Another one from Chetan was on what was sales growth in April and May month compared to F4 FY 2017. We've already answered that. I'll move on.

The next one is from Tejas from Spark Capital. It's been conservative two years of flat growth and employee cost. We are reducing head count or is it just cost rationalisation within the lines itself, and how do we plan to retain and attract new talent with these kind of low variables? Yeah, this we've already answered.

The second part of the question is, we always look upon HUL as a very efficient organization, so how come suddenly we are talking about so much inefficiency and cost savings opportunity in our margin, and how we're trying to monitor this? Again we've spoken on this.

Answer:

Yes. To amplify the point, I would just be careful characterizing this as all of a sudden. We just brought it to the force because there's so much of queries coming in terms of how are we sustaining our margin delivery, and then we said, okay, let's share with you what are the programs that we run internally. So it is not all of a sudden at all. And as I reiterate again and again, this is not going to compromise our competitiveness. The entire reason why we do this is this increases our competitiveness and generates a fuel for growth that we need to deliver. So it is positioned the other way.

Question:

The next one is from Richard from JM Financial. Can you please explain why the growth in excise related to sales growth has been so volatile in recent past, and kind of specifically referred to the growth in June quarter? And what are the factors which are driving the differential?

Answer:

See, one is the mix of products that is there, which also changes it, and also the kind of ramp up of production that happens in the fiscal sites as well. So the productivity drive that we do on fiscal as well a mix of products that we sell, that is the particular aspect there. But what we'll try and do, Richard, is that try to get you a more, let the team reach out to you separately, we'll then clarify for you in a more granular detail what's causing the volatility

Question:

Next one is from Percy, which is talking about agri deflation and agri how this will impact the rural demand, which we've already answered.

The next one is from Tanmay from Edelweiss. In an environment of increased focus on cost saving across many consumer companies, that demand scenario and stable enterprises, does it suggest that it will take more time than expected to go back to double-digit growth rate?

Answer:

I think it's not fair to connect these two, but double-digit growth rate is also a factor of what's the commodity inflation we're running with. And we shouldn't also expect that we are going through some significant external volatility over the last three quarters from demonetization to GST. There's been a significant level of external challenge. It is causing noise in the chain I think once that plays out, the business gets back to business as usual, I think it is the right time to access what are the real volume growth in the business. But if we take a longer term perspective of 4% to 6% volume growth is the kind of track record we have been maintaining and that is something that we also see as something that we should get on to.

Question:

I'll move on to the last question from Amit Kumar from Investec. Couple of parts to the question. The first part of the question is on Personal Care. The price is slower despite Ayush launch. Know only in South India, but that is a big market itself, which would be incremental to the turnover growth

Answer:

Yeah, you're right. It's fair to – that question is a fair question, but the only angle here where Personal Care in particular got disproportionately kicked by CSD, not buying on the last month. So that is a key part there.

Question:

The second part of the question is on the company noted normal offtake at the consumer end, would it possible to share India FMCG growth retail level as reported by Nielsen or as applicable for the company?

Answer:

See, one thing with Nielsen that we observe is that their panel is really taking time to stabilize with respect to growth numbers in particular and that is coming out of this kind of demonetization to GST, channel pipeline. They are struggling to get their numbers in a stable manner. What they report as growth for HUL and what HUL has reported growth for itself, there is an absolute yawning gap between the two. So at this point in time, I think Nielsen growth needs to be taken with a pinch of salt.

Question:

The third question from Amit is on direct reach. Post demonetization, the company had talked about focus on direct distribution. Can you please discuss the progress? What will be the share of wholesale in overall trade pre-GST?

Answer:

Yeah, I think that's something which we've called out absolutely right and very good progress being made on that, and we will continue to drive the direct distribution. And one of the reasons we could arguably say is that our ability to hold the kind of growth rates that we're seeing today is also a factor of the direct reach and the sustainable direct reach that we have been driving as a within the setup, and we see clear benefits coming out of it and we'll continue to keep working on this to keep increasing this further as time go by.

Question:

The last part of the question from Amit is the surprise with a strong net price inflation in an uncertain environment, also since the company talked about compensating trade for any loses on pre-GST stock, will this compensation come through in quarter two?

Answer:

Yeah, I think great question. If you look at the 6% inflation, bulk of the number of 6% came through by price increases that's happened in the previous quarter. As far as cut over related compensations are concerned, you must appreciate that our pipelines are very, very thin. So we keep at a trade that at our distributor level about nine odd days of stock that is all that we maintain there. Therefore when the compensation that we have to pay, we're only paying for a very, very small amount of inventory that is held and that is something we are paranoid about. We don't want to stock up the trade and particularly in a scenario when the price cuts are happening you wouldn't want trade to be carrying the wrong stock. So the impact on this will not be material enough to move the needle on price growth rate.

Question:

One more question coming from Alok Shah from Edelweiss. There has been negligible off take in CSD in June, more proportion of off take in CSD segment would be of lower premium products, which could yield lower gross margin. Would this be one of the reasons for some improvement in gross margin?

Answer:

I think contribution margins for CSD for us, we are quite comfortable. It's quite a healthy margin mix that we run on this. So the portfolio that we run there is a pretty profitable portfolio. So wouldn't subscribe to this assumption.

Aasif Malbari

That's all that we had on the web queue. With that, we'll come to the end of the Q&A session. Before we end, let me again remind you that the replay of the event and the transcript will be available on the Investor Relations website in a short while. And you can go back and refer to it. A copy of the presentation and the results, if not already with you, is available on the website and you can go back and refer to that as well. With that, we will like to draw this call to a close. Thank you everybody for your participation and have a great evening. Thanks.

Operator

Thank you very much, sir. Ladies and gentlemen, this concludes the earnings call. You may now disconnect your lines. Thank you for connecting to audio conference service from Airtel. Have a pleasant evening. Thank You.