# Investor and Analyst Q2 & H1 FY18 Conference Call

## November 01, 2017

**Operator:**

Ladies and gentlemen, good day and welcome to the GCPL's Q2 FY2018 earnings conference call, hosted by Macquarie Capital Securities India Private Limited. As a reminder all participant lines will be in the listen-only mode and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing "*" then "0" on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Amit Sinha from Macquarie Capital Securities. Thank you and over to you sir!

**Amit Sinha:**

Thank you and good evening everyone. We, at Macquarie would like to welcome you all to Godrej Consumer Products Ltd's earnings concall. We have with us the management on the call. I will hand it over to them to take it forward.

**Tapan Joshi:**

Thanks Amit. Good evening everyone and thank you for joining us today on Godrej Consumer Products Limited conference call to discuss the performance of Q2 FY2018. We have with us Nisa Godrej, Executive Chairperson; Vivek Gambhir, Managing Director and CEO; V. Srinivasan, CFO and Company Secretary; and Sameer Shah, Head Finance, India and SAARC & Investor Relations.

Like the previous quarter, we will start the presentation with Vivek sharing his thoughts on our performance and then we can open up for Q&A. Over to you, Vivek!

**Vivek Gambhir:**

Thank you Tapan. Good to be talking to you guys. I will start off by covering a few of the highlights of the quarter and then we will also walk through some of the key slides in the presentation. After which, we would be happy to answer your questions and get your feedback.

At an overall level, we are quite pleased with our performance. After a relatively subdued Q1, we have delivered a resilient performance in the second quarter with robust and strong profitable growth. In our India business, we have delivered a 10% volume growth. It is important to mention that this growth has been delivered on a base of 9% growth in the same quarter last year. On a comparable basis, netting the impact of GST, our sales growth was 11%. And along with this healthy 10% volume growth, our EBITDA in India also grew by 24%, a strong profitable growth. Our teams have been very agile and we have been handling the GST transition well. Post GST, the trade channels are getting back to normal and consumer offtakes have improved, and we remain optimistic of continued pickup in consumer demand in the second half of the fiscal year.

In our International business, our sales grew by 9% on a constant currency basis. Our EBITDA was marginally ahead of sales growth and grew by 10% on a constant currency basis. Within the International portfolio, the Africa and US cluster continues to deliver good performance in spite of political turmoil in Kenya and South Africa. Our Latin American business saw a very strong recovery during the quarter. The UK business continued to deliver a strong sustained performance. In Indonesia, while the sales growth remains relatively weaker due to the challenging environment, the sales performance has improved sequentially versus the previous quarter, and margins have also expanded on the back of already high margins. We are confident of a continued recovery in the quarters ahead.

So what is working well for us is our continued focus on brand building and innovation and relentless execution on the ground. Over the next few quarters, we have exciting plans to launch several new products. And as the environment improves, we remain confident of a much stronger second half performance as well.

I will just quickly walk you through some of the main slides in the presentation. So if you turn to Slide 3, at the consolidated level, net sales grew by 19% on a constant currency comparable basis and EBITDA grew by 19%. For India, the number was 11% sales growth and 24% EDITDA growth. International it was 9% sales growth and a 10% EBITDA growth. On Slide 6, as you will see, the balance sheet continues to remain healthy across all the parameters that we are focused on, whether it is working capital and how we run the business, we have seen improvement quarter-over-quarter. Here again, a better way to look at this is over a longer period, but at least on a quarter-to-quarter basis we are focusing on the right balance sheet metrics and improving them as well.

If you turn to Slide 8, we will start talking about our India business. We have seen strong volume growth that has been led much more by soaps. In Insecticides and Hair Colors, the volume growth was slightly lower, which will be explained in the subsequent slide. But overall, we are quite pleased with how healthy the volume growth has been. Again this is on the back of a very strong volume growth in the base quarter as well.

On Slide 10, we talk a little bit about our Insecticides business. The sales growth of this business was about 4%. So on one hand, this 4% is probably a shade lower than our internal expectations. One thing to remember here is that this is on a very strong base of 18% growth in the base quarter. As you know, this is a seasonal business, since the timing of rain does impact the business. The two-year CAGR is about 11%. To a certain extent, the growth was impacted by weakness in the coils business, which is a little bit more dependent on the wholesale channel. In some parts of the country, particularly the east, the wholesale channel has taken slightly longer to adapt to a post-GST scenario. So, our coil business actually de-grew. This is also bit of a strategic call, where we are focusing far more on the value-added formats, whether it is the liquid vaporizers, aerosols and personal repellents. We have been very pleased with how well the liquid vaporizer business has been growing.

Personal repellents, early days, but we have been very enthused by the initial traction we have gotten in the business. Aerosol business also continues to remain very strong. So as we have been focusing on the more premium parts of the portfolio, we did get impacted by de-growth in the coils business, which ended up bringing the average numbers down. The coil category is almost 30% of insecticides in India; our salience is a lot lower, but it is a very big part of the insecticide category. We believe strategically the right call for us is to continue to drive penetration and consumption in the more value-added, more profitable and more premium formats.

If you turn to the next slide, in Hair Colors, again the performance is a little shade below our expectations. The crème segment is doing very well. Crème is now larger for us than the powders segment. Our powder business de-grew. Again, this was because of the impact of the wholesale channel and East. East is a fairly important market as far as powders is concerned. The powder business got impacted because of the challenges with the wholesale channel adapting to post-GST scenario. Our market shares have consistently been gaining and we are at a highest-level market share as far as crème is concerned. But from a structure point of view and a priority point of view, we feel very confident about the focus and the strategy on the hair segment. As far as the powder segment is concerned, over the next couple of quarters, we are also planning some tactical innovation, which should allow us to at least maintain our position in the powder segment.

On the soap side, it has been a very strong quarter. We have passed on the benefits of lower GST rates to the consumers through price cuts, and that has been a big driver for the category as a whole in terms of the growth that the category has seen. Beyond the category growth in soap, we have also gained share through some very good marketing initiatives on both Godrej No. 1 and Cinthol. Both have grown very well for us. We have been opening up a few new states and so as a result of that we are seeing greater growth in the soap segment. We have also been seeing some early signs of the smaller regional unorganized players facing some challenges in this segment. So there is some indication of growth disproportionately being driven by some of the larger national players.

The other thing to remember on soap is, while the 26% growth looks very good, this was on a weak base of negative 10% in the same quarter last year. So the two-year CAGR actually is around 8% to 9%. We still remain quite confident about continuing strong performance in soaps over the next few quarters.

On Slide 13, as far as the new launches are concerned, we are very pleased with Cinthol deo stick, aer pocket and personal repellents. As I mentioned, the pipeline of new launches over the next few quarters is very exciting and so we will dial up our innovations as well.

On the International portfolio, the performance was somewhat mixed and it did get dragged down a little bit by Indonesia, but we are seeing early signs of recovery in Indonesia. On the margin side, it remains quite intact and we have seen a slight margin expansion.

On Indonesia, we are seeing that the macro environment in Indonesia is still very weak. Consumer expenditure also has been a bit of a challenge. But for us, Indonesia has been a very strong business with a great track record. We have made some management changes and it have gone off very well. The team has done a very detailed diagnostic and we have identified all the key levers that will get the growth back on track. What is also encouraging is that the non-Household Insecticides part of the portfolio is still relatively better. As far as market share positions are concerned, we have regained some of the lost market share in insecticides. Air fresheners and baby tissues' market share remains steady. The team has done a good job and worked very hard to be able to ensure margin and profit protection behind rationalizing some spends and putting a tight control on overheads.

Our Africa business performance has been steady. There were challenges in terms of the macro environment in Kenya and South Africa. In spite of that, the team has delivered a very robust performance. The growth in hair extensions continues to be in the high teens in constant currency terms. The margins have been down slightly. It is a conscious call that we have made to be able to scale up our wet hair business. The wet hair launches are going into the market in various parts in Africa. We are very excited about it and we have taken a conscious call to increase ATL spends and invest adequately to create a much stronger wet hair care business.

On Latin America, on Slide 21, has been a very positive story in terms of both sales growth and profits growth as well. Europe business, on Slide 22, continues to do very well, both in terms of sales and margin growth. The remainder of the slides just captures our summary. We will be happy to pause and take your questions and feedback.

***Continue: - Q&A…***

## Questions and Answers:

**Moderator:**

We have the first question from the line of Manoj Menon from Deutsche Bank.

**Manoj Menon:**

Could you help us understand the India margins, particularly the gross margins. What are the drivers for this?

**Sameer Shah:**

On a comparable sales basis, India's gross margins have moved up by close to around 170 basis points. And why I am saying comparable is because we need to adjust the base, assuming that there was GST, so the gross margin expansion comes close to around 170 basis points. There are two to three reasons to it. One is, we do have good cover on palm oil wherein the cost is much lower than the replacement rate, as well as the increase in prices taken in the past is higher than the increase in input cost. Secondly, the other reason is also relatively lower consumer offers in this period compared to the base period. The third reason is the continuous cost saving program, Project PI, and also there is a little bit of strategic sourcing on some of the key ingredients within household insecticides, which we are procuring at much lower rate than what the cost has been in the base. So, it is a mixed bag of palm oil cover, cost saving programs towards strategic sourcing and lower consumer offers.

**Vivek Gambhir:**

As I mentioned earlier, because coils de-grew and the other parts of the portfolio actually grew much faster, the gross margin difference is actually substantial between the value-added format and the more commodity formats.

**Manoj Menon:**

On palm oil cover, is there still some benefit for the future?

**Sameer Shah:**

We do have covers for next three to four months of production at this stage.

**Manoj Menon:**

On Indonesia, in your release you talk about A&P cuts or rather some rationalization in the short term. Could you give a quick comment on this outlook? Is it fair to say that given that the macros are so bad there that you are dialing down on the innovation pipeline for the time being, because it may not be pragmatic to do that?

**Vivek Gambhir:**

A lot of the promotion spends were not very strategic in some ways. We were spending across a bunch of different channels. So what the team has been doing is first of all getting more surgical about looking at ROI and making sure that we invest in the right kinds of channels. And the other part is, we will dial up our investment to drive sales growth. So the focus is to ensure recovery in shares in a calibrated manner. But this is a call we take on a monthly basis, if the sales are growing more, we will up the investment. But if the sales do not show enough traction over the next one or two quarters, our focus will be to ensure that we protect our margins.

**Manoj Menon:**

On Africa, could you help us understand the breakdown between price, mix and volumes? What we know now is high teens growth in the extensions part. So question is, what is the differential? Is it just explained by the color part of it, or is there anything more to that? Secondly, even within this 13% constant currency, how much would be the volume component?

**Sameer Shah:**

If you strip out the U.S. business, Africa's growth is much higher than 13%. The hair extension, which is largely an Africa play, is growing closer to high teens. As you said, it is difficult to decode volume, value-led growth. But our estimate is that volume versus price is 50-50.

**Manoj Menon:**

So the difference between the high teens extensions growth and the 13% constant currency is essentially the non-Africa piece, which is the U.S. and Caribbean and the SON part of it?

**Sameer Shah:**

Yes.

**Manoj Menon:**

Around 6%- 7% has been a ballpark volume number in the previous quarters also, right?

**Vivek Gambhir:**

Yes. In the previous quarters, Nigeria had slightly higher price-led growth. But that is also moderating as we are focusing far more on driving volume growth as well.

**Sameer Shah:**

To add on this, this quarter was also a little bit tough in terms of Africa, because of the political turmoil in Kenya as well as in South Africa. So to that extent, the performance has been a little lower than our internal expectation on sales growth.

**Vivek Gambhir:**

The optimism in the team is very high for a much better performance in H2, because hopefully by that time Wet Hair will start providing meaningful add-on opportunities as well, because the launches are just going into the market. So in terms of a new growth vector, second half is when we should start seeing a certain amount of acceleration in growth in Africa.

**Moderator:**

Thank you. The next question is from the line of Abneesh Roy from Edelweiss. Please go ahead.

**Abneesh Roy:**

On personal repellents, you have gained a teen market share. So will this be coming largely from the market leader and because your products are innovative and very different from the existing market leader, does it mean you have expanded the category meaningfully?

**Nisaba Godrej:**

Like we said before, the in-home segment is about ₹5,000 crore and out-of-home is approximately ₹150 crore. So our game here is that we will take the market share, but we want to grow the category as well. We have been doing both of that. This launch has been ahead of our expectations and the product has done really well. Media is working very well. So we are very excited. As we have seen in something like aer pocket, where the product is very differentiated and as consumers like it, it gives us huge advantages. So we are very excited about this.

**Abneesh Roy:**

On aer pocket, competition seems to have caught on. So the market leader in that sub-segment seems to have launched a competing product. So does it mean that now growth could come off for aer pocket, or there is enough lead-time?.

**Nisaba Godrej:**

Aer has done very well and we see it continuing to grow. We have seen in many categories, competitors do bring me-too products. With more people investing in the category, it is better for the category growth. Soaps is a 100% penetrated category. But, these categories would be penetrated by 5% to 7% and that too in urban India. So the game here is category growth. The personal repellents category has not grown, because there has been no advertising investment over many years. If we grow the category, it is good for the category, it is good for consumers and the best product will win.

**Abneesh Roy:**

On the India overall 11% growth, the volume growth is 10%, which means pricing was 1%. Now soaps have seen a 26% growth and soaps would have seen a price growth. Does it mean hair color and household insecticides would have seen some price cuts? 1% seems a very low number, could you elaborate why it is that low?

**Sameer Shah:**

The 11% growth is after the incremental sales and trade promotion spends. The growth before sales and trade promotion spends is close to around 12% to 13% and within that if I strip out non-branded and exports, the growth comes to around 13%. So 13% value growth has actually got us 10% volume growth, which means there is actually a price increase of around 3%. Some of it gets offset by this higher trade promotion spends. In terms of category directionally, entire growth in household insecticides and hair colors is volume-led. And good part of growth in soaps is also volume-led growth. So that is how the volume-value equation in each of this category stands.

**Abneesh Roy:**

So this 26% growth in soaps is largely volume-led. So you would have gained from the unorganized players or even from some of the larger players?

**Sameer Shah:**

Yes. It is too early to comment on, but in some pockets we have seen very small local players, presumably behind GST that are not seen at least over the last three-four months. And that is giving opportunity to large players to gain some market share. And also there have been some very serious micro marketing initiatives over last four, five months from our end, especially in Godrej No. 1 brand, which is also reaping some rich dividends.

**Vivek Gambhir:**

It is important to look at a two-year CAGR for us, because the base had a minus 10% growth. So the two -year CAGR is in the high single digits.

**Abneesh Roy:**

GST is supposed to increase market share for large organized players. You pointed out that in soaps you have already seen some initial evidence of that. In any other segment, have you seen the reverse trend happening? So for example, in coils, is there a reverse shift happening?

**Vivek Gambhir:**

Difficult to say that based on two or three months of analysis, because some of it is also driven by us not focusing enough on coils. So part of it is company strategy, but it is a little bit hard to extrapolate that based on the last couple of months. We will have to wait for a quarter or two to be able to find a more generalizable trend.

**Moderator:**

Thank you. The next question is from the line of Aditya Soman from Goldman Sachs. Please go ahead.

**Aditya Soman:**

On both home insecticides and hair colors, you pointed out that some of the traditional products have seen decline in volumes. Would you expect these declines to continue over the next few quarters, or this is just one off because of wholesale de-stocking? And secondly, what would be the steady state growth number that one should assume for these two segments, especially if you can break that down into the new products and older?

**Vivek Gambhir:**

No, we do expect recovery in both coils and powders. In India, particularly in rural and wholesale, these products have a higher salience. We do expect that recovery could happen during the course of Q3 and hopefully by the end of this calendar year. Secondly, we are also intensifying some tactical innovation, some new launches, which should help us gain a stronger foothold. So our belief is that overall environment should improve, but we are taking a few tactical moves to be able to drive higher recovery. It is still in maintenance mode, because ultimately strategically the focus will be on more value-added, more premium format. But in the meantime, in the short term, we will take the right tactical moves to be able to get atleast some of the growth back on track.

**Aditya Soman:**

Would the two-year CAGR that you highlighted, say, 11% for the insecticide segment be a good indicator of where you would expect growth for this segment to be when things are normalized?

**Vivek Gambhir:**

Little bit depends on seasonal variation. But for us, the idea would be to get to growth between 11% to 14%. As personal repellents starts gaining more traction, with the growth vectors that we have, and with our innovation pipeline, it is quite exciting. So the idea would be to actually drive the growth rate higher, because again the penetration rate for this category is only about 50% across India, so there is plenty of headroom for growth.

So we will continue to invest, and we need to try and see if we can drive the growth rates up.

**Aditya Soman:**

You have not talked about Fast Card over the last year or so. Any reason for that because that could be seen as a natural replacement for coil?

**Vivek Gambhir:**

Fast Card has been doing steady for us. As a format for top-up usage, it is doing quite well. Last quarter, Fast Card did see some challenges because of a higher rural, slightly higher wholesale salience, along with coils. The Fast Card performance was not where we would have liked to see it. We do see the value of Fast Card in the portfolio in the top-up format. There are some other follow-on innovations that we are planning to try and drive further growth in Fast Card.

**Moderator:**

Thank you. The next question is from the line of Latika Chopra from JP Morgan. Please go ahead.

**Latika Chopra:**

Could you elaborate more on the status of promotional intensity in the household insecticides category in Indonesia? What is the progress on your hair color launch in the country and what kind of growth did the non-household insecticides portfolios see?

**Vivek Gambhir:**

On promotional intensity, it still remains high, though we have seen, post Lebaran, a little moderation as far as promotional intensity is concerned. As I mentioned, we have gotten far more analytic and systematic about directing our promotional spends on the right kinds of channels. Intensity is still high, but lower than what we had seen before, which is quite encouraging, but still it has been only a couple of months. The non-household insecticides part of the portfolio was close to about flattish, driven by a tough consumer environment. As I look at market shares, they have been holding steady on the non-household insecticides part of the portfolio. Hair colors, we have been very pleased with the launch. It is gaining a lot of traction. The other important part of hair color strategically is if I look at the business there, we have a higher weightage on the modern trade channel and lower in general trade. With hair color, we are now being able to have a more aggressive aspiration to drive up reach in the general trade in the non-Java part of the Indonesia geographic coverage strategy. So over time, we feel very bullish about the potential of the hair color business as well.

**Latika Chopra:**

Have you seen a lower intensity from the competition?

**Vivek Gambhir:**

Before Lebaran, we saw a very unusual level of high competitive intensity, in terms of the level of promotional discounts that were being offered. Over the last couple of months, we have seen a certain amount of moderation there.

**Latika Chopra:**

By the other two-three players?

**Vivek Gambhir:**

Yes.

**Latika Chopra:**

You had introduced a professional hair care range in India few months ago. Any update or anything meaningful to talk yet on this front?

**Vivek Gambhir:**

Very early days. So far the feedback from the channel has been very positive and even the consumers that we have spoken to have loved the range of products. But it will take us about six months more before we get repeat purchases, so we will hold off trying to evaluate.

**Nisaba Godrej:**

We are very positive about this, because from a product front, it has definitely been a hit from the analysis of consumer research and the initial reactions. But it is a new channel for us that we have to build up, but as for what we were expecting in the first few months, it has been very positive, but we need give at least 6 to 8 months to even give a good read of it.

**Latika Chopra:**

On soaps, you mentioned that you are entering new states. Which would these be?

**Vivek Gambhir:**

I do not want to comment on specific states for competitive reasons, but part of our strategy has been to look at contiguous states, every 2 or 3 years, where the soap portfolio has good brand equity.

**Moderator:**

The next question is from the line of Prasad Deshmukh from Bank of America. Please go ahead.

**Prasad Deshmukh:**

In terms of consolidation of the industry, is there any geography-specific prevalence for the consolidation or is it across the market?

**Vivek Gambhir:**

This is very anecdotal right now. We have reasonably good strength in the North, the West and the South. Across the board, we are seeing some initial signs, but quite early to talk about this in a more data-driven manner. We will need about one or two quarters more before we can actually look at this data much more systematically. This is the feedback that we are getting from the trade and from our sales team.

**Prasad Deshmukh:**

You have this program called One Rural. Given there is still pressure continuing in rural markets post demonetization, GST and pressure in wholesale, is there any change to the strategy that there will be a unified approach and you want to grow the share of rural aggressively going ahead?

**Sameer Shah:**

There is absolutely no kind of change in terms of our approach to One Rural. We continue with almost all the initiatives and the related investments. Even for this quarter, our rural growth is a percentage higher as compared to urban, though we think it can be much higher than urban growth, but absolutely no change in our investments and entire One Rural program.

**Nisaba Godrej:**

Both household insecticides penetration and hair color penetration in rural India is very important to us. So a few quarters of slower growth in rural is not going to change our plans. From our innovation pipeline, we have in both these categories, exciting products planned in the coming quarters. One Rural strategy is very key to us and it is very strategic to GCPL, because our rural salience is lower than our peers. So this is a big growth opportunity and we will be very focused on it.

**Prasad Deshmukh:**

Despite challenges, you have managed to grow in Africa. Other than political, are there any other issues in African markets right now?

**Vivek Gambhir:**

Currency is that one challenge and hopefully that should get better over time. The main watch out for us is Kenya, which hopefully should stabilize politically. Internally, in South Africa we had an ERP migration to centralize to a common system and that ended up creating some near-term challenges. But beyond that the team is in place. We are very confident now, particularly with Wet Hair to be able to accelerate on the platform that is being built there. In Africa, if you look at our performance over the last 12 to 15 quarters, consistently the growth has been at least in the high teen across the board. It has not been one or two quarters, it has been almost two to three years of consistent growth in the high teens.

**Moderator:**

Thank you. The next question is from the line of Abhijeet Kundu from Antique Stock Broking. Please go ahead.

**Abhijeet Kundu:**

Where would we be in terms of recovery in the wholesale channel? By when will this be sorted?

**Vivek Gambhir:**

The feedback from our sales teams is that wholesale is probably 80%-85% there and the teams feel quite optimistic that by the end of this calendar year, the wholesale channel should also largely be back on track.

**Abhijeet Kundu:**

In household insecticides, you would be doing some tactical launches and at the same time you would be not focusing much on coils. So would it be into some new formats, or you would push more of the personal household insecticides portfolio?

**Nisaba Godrej:**

Unfortunately, we cannot share what our innovation portfolio would be like. I do not think we are not focusing on coils. In terms of focus and investments, whether it is liquid vapouriser, personal repellents, our new HIT gel stick, will get more of the pie. The coil is still a big volume driver for us and you will see new products or variants there also.

**Abhijeet Kundu:**

In LATAM, we have seen a very strong comeback. Going ahead, will the momentum continue there?

**Vivek Gambhir:**

Q1 was quite weak for the Latin American business. So, as we look forward, looking at the Q1 plus Q2 summation is the right way. The team is doing a great job, our brands are gaining share behind new innovations, but we have to remember that Q1 was very weak for the business. So looking at overall H1 performance and hopefully being better than that in H2, is the way we will be looking at the business.

**Moderator:**

Thank you. The next question is from the line of Vivek Maheshwari from CLSA. Please go ahead.

**Vivek Maheshwari:**

Given that GST provides an opportunity to convert unorganized or unbranded to branded, should not you have focused much more on coils rather than focusing on other formats, because that was the best opportunity for you in this quarter to gain shares from the regional or the local players. Why would you prioritize other formats at this point of time?

**Vivek Gambhir:**

We have to balance near-term versus long-term. Our focus is far more on what will create more value for us in the longer term. Secondly, share gains in coils is quite difficult, because it is such an intense, undifferentiated BTL-led game, so this could be value eroding for us to invest significantly in coils just to gain some share for a particular quarter. The minute you withdraw these promotion offers, the next couple of quarters you lose that share. So in our mind, there is a difference between good share and bad share and our focus is to create growth vectors that will drive value for the future. It is a strategic call that we have taken.

**Nisaba Godrej:**

A lot of our category work is to upgrade coils. So even for an expert crème, the game was to give much more value-added product at the right price. In the same way, whether it is our liquid vapouriser work or other work is to upgrade coils. So when we are looking at advertising investment and the ROI on money spent, it is better spent away from the coil business, although tactically, we still invest behind coils.

**Vivek Gambhir:**

Wholesalers and the east are going through structural challenges adapting to a post-GST world. Just increasing BTL would not necessarily drive and compensate for some of the structural channel challenges that this quarter saw as far as wholesale was concerned.

**Vivek Maheshwari:**

Excluding East, would you have gained shares in coils then?

**Vivek Gambhir:**

I do not have the numbers if front of me, but we will definitely go back and take a look at our coils share ex East.

**Vivek Maheshwari:**

How much of this 10% volume growth be because of restocking versus what will be the intrinsic growth for this quarter?

**Sameer Shah:**

We did around 8% to 9% volume growth without any restocking impact. Only a 1% or maybe 2% would be on account of restocking, after the destocking that happened at the end of Q1. Also do remember that we did not have significant destocking at the end of first quarter. We had 2%-3% higher secondary sales as compared to primary at the end of Q1.

**Vivek Maheshwari:**

On Indonesia, you have recalibrated your A&P investment; do you think the competitors would have done the same?

**Sameer Shah:**

The margin expansion in Indonesia is not just driven by ad-spend rationalization. There is also the cost saving project PI, which actually has got cross-pollinated from India to Indonesia around three or four quarters ago, which is now scaling up. So it is a combination of both, cost saving program as well rationalization in spends. Again, it may not be fair to compare this with other FMCG companies, because of different category play, as well as dynamics in each of those categories. At this stage, though, what is happening in household insecticides is most of the players are very skewed towards sales and trade promotion spends or consumer offers, as compared to the traditional media, which is what even we are doing.

**Moderator:**

Thank you. The next question is from the line of Arnab Mitra from Credit Suisse. Please go ahead.

**Arnab Mitra:**

On Indonesia, in household insecticides, besides the competition was that the market growth itself had become negative last year. What is the trend now, if you could highlight there?

**Vivek Gambhir:**

Insecticides saw 12 months of fairly bad performance from a category perspective. We are seeing improvements in insecticide growth rate, which is a source of comfort for us. At a macro level, things are quite challenging. That continues to be a bit of a worry for us, but one of our big issues was more on insecticides. There we are at least now seeing things returning back to positive growth.

**Arnab Mitra:**

From last quarter to now, do you feel more confident of going into a positive constant currency in second half or one cannot be very confident about that situation looking at the competition intensity?

**Vivek Gambhir:**

The idea for Q3 is to be better than Q2 and then Q4 to be better than Q3. The team has planned a lot of actions and if those actions gain good traction, we should be able to deliver a much stronger H2 versus an H1.

**Arnab Mitra:**

Is it actually possible to drive rural penetration in a situation where you are not focusing on coil? Is it a category where consumers can straight get into an electric repellent or an aerosol, and in that context, would you require some other initiative to drive the rural penetration here?

**Vivek Gambhir:**

It is not as if we are not focusing on coils. We are focusing far more on value-added formats. But from a distribution and rural perspective, coil is a very important part of our portfolio; it will continue to remain so. We will also launch some tactical innovations over the next few months in the coil segment. But relative prioritization certainly is, strategically over time similar to powders versus crème, is to be able to move through innovations and brand building to more profitable formats but coil would still remain an important focus area for us.

**Arnab Mitra:**

Being a market leader, it is also a responsibility to drive penetration. And if the market leader does not invest enough in the penetration segment, does it affect the category growth?

**Nisaba Godrej:**

Yes. The penetration is very important but we feel that at certain price points, even innovation will help with penetration. And you will see a few things from us in the next few quarters itself, which will be penetration drivers.

**Moderator:**

We have the next question from the line of Amit Sinha. Please go ahead.

**Amit Sinha:**

Some of the FMCG peers have commented that they are seeing reverse premiumization and down trading in some of their categories. Would not it be much wiser for you to concentrate on the volume growth of the coil and the powder segment?

**Vivek Gambhir:**

If we can deliver 10% volume growth in spite of coils and powders, I would much rather settle for that because that is far more of a profitable value creating strategy. It is a call again various companies can take. But for us, the focus is on trying to drive profitable growth. We will continue to invest behind coils and powders to the extent possible, but it is harder to differentiate in those categories, and the ROIs of investment may not necessarily be compelling.

**Nisaba Godrej:**

In India, you would actually have to go state by state in terms of what strategy you want to play, it is not as simple as just urban, or rural, or penetration.

**Amit Sinha:**

Is it not something that you would ponder on, being the market leader that cutting prices even at the cost of margin even at some of the products like liquid vapourisers and crème can get you much aggressive volume at this junction, where some of the unorganized is vacating the space?

**Nisaba Godrej:**

In crème, we have very strong volume growth. And in crème, we kept prices stable at ₹30 since we launched. In soaps, price changes quite a bit, it is quite variable. In household insecticides, we are the category leader and it is our responsibility to grow the category.

We want to bring very efficacious value-for-money products, but at a price point suitable to everyone in India. So in household insecticides you will see innovations both at the premium segment and you see also at the mass level.

**Amit Sinha:**

Is it possible to share the volume decline number in the Indonesian insecticide business?

**Sameer Shah:**

For competitive reasons, we would not want to share this number at this stage.

**Moderator:**

The next question is from the line of Kaustubh Pawaskar from Sharekhan Limited. Please go ahead.

**Kaustubh Pawaskar:**

What would be your distribution strategy, especially the direct distribution expansion strategy going ahead?

**Vivek Gambhir:**

This is an ongoing journey. Our direct coverage this year will be higher than 10%, but a lot of it depends on gaining critical mass and the economies of scale to ensure the right ROI, but strategically we believe that both wholesale and direct distributions are very important channels. So we need to have both. But as the economics allow, we will continue to invest much more in direct distribution. But it is an ongoing journey, which should continue to play out over the next few years.

**Kaustubh Pawaskar:**

Post the implementation of GST, it has been assumed that lot of shift is going to happen from unorganized to organized space. In powders, there are a lot of unorganized players, so going ahead, should we see a faster recovery in powders?

**Vivek Gambhir:**

We will have to wait and watch. We should start seeing a greater shift towards the organized segment and we are working towards that.

**Kaustubh Pawaskar:**

Should we see some gain in this particular space going ahead?

**Vivek Gambhir:**

We are hoping for that, yes.

**Moderator:**

The next question is from the line of Chetan Thacker, ASK Investment Managers. Please go ahead.

**Chetan Thacker:**

On the cost-saving initiatives that are ongoing, what is the extent of low hanging fruit still sitting there? What would be the A&P intensity going ahead, given new launches that are planned?

**Sameer Shah:**

The cost saving program, in India is in its fourth year, and year-after-year we have been able to clock bank savings, what we call internally, in line with our initial estimates for the year. There are various components to it, strategic sourcing, productivity, revisiting manufacturing footprint, and the entire distribution. We still feel, there is opportunity, not just for this year, but also next year. Normally what we have seen over last three, four years in terms of revisiting the formulation, the packaging, etc but keeping the product absolutely intact in terms of its quality, look and feel. We remain confident of continuing this program, even cross-pollinating, as we are seeing some very early benefits also coming out from our Indonesia business. So we remain very optimistic on the cost saving program for near future in couple of our big markets.

**Chetan Thacker:**

Are there some low hanging fruit sitting in Indonesia, which can be exploited in H2?

**Sameer Shah:**

Yes, in Indonesia, this is just a full first year, unlike in India in which we are in our fourth year. So definitely there is opportunity in terms of squeezing costs. And you will see the benefits of it continuing in the near future.

**Chetan Thacker:**

On the A&P side, how do we see that intensity increasing in H2?

**Sameer Shah:**

If you look at our A&P spends and assuming your question is more on the domestic business, A&P is driven by new product launches. For us, it is driven by also competitive intensity. Going ahead, we will see this range of 12%, maybe plus, minus 100 basis points in H2. But otherwise we do not see this moving dramatically.

**Chetan Thacker:**

Even in Indonesia this would not increase dramatically given the reduction in competitive intensity there?

**Sameer Shah:**

We would continue to invest as we have done, for instance, not just in Q1, but even in Q2, we will continue to invest on hair color. But household insecticides is close to 35% - 40% of our play over there. This is a category, wherein over last couple of quarters we have seen extremely high competitive intensity and most skewed towards consumer offers, so there is hardly any kind of A&P spend, not just by us, but also by the entire category. So it is difficult to call out, but once we see sales and trade promotion spends scaling down, we definitely will see uptick in ad spends.

**Moderator:**

Thank you. The next question is from the line of Richard Liu from JM Financial. Please go ahead.

**Richard Liu:**

On GST, how sanguine are you on the whole unorganized to organized piece after having experienced the tax regime for about four months now? The tax did scare the unorganized guys a lot in the beginning, but they have incrementally turned a bit more cowboyish again as days passed. How do you think this piece will pan out in the days ahead?

**Sameer Shah:**

I would not call them as "unorganized" but these are local players in few pockets of the country. This is what we have seen from our market visits, as well as updates from channel, as well as our sales team. It also works very well in categories like soap, where your price point is much, much lower as compared few of other categories. For instance, we have not seen much of converts in a way from unorganized to organized in hair colors, as well as to some extent in household insecticides yet. There is going to be more gradual than perhaps what most of us anticipated before getting into GST in terms of this conversion happening.

**Richard Liu:**

What would you attribute that reason to, in terms of expectation of this conversion pre- and post-GST implementation?

**Sameer Shah:**

It looks like that some of the small organized players are either kind of complying or maybe they are continuing the way they were doing business in previous regimes. So there are multiple hypotheses, which are very difficult to validate, but this is what we can think of at this stage.

**Richard:**

On the Africa slide, you mentioned about 13% overall growth and high teens in hair extensions. Depending on what high teens is, does this mean that the SON Wet Hair business growth is just about 4% - 5% or thereabout?

**Sameer Shah:**

Directionally SON business in U.S. is not going to be a high teen business because we are looking more at developed markets and actually emerging markets is where we have the bigger wet hair play. So in a nutshell, the growth, both in Strength of Nature, as well as Africa is very much in line of our expectations. In U.S., in last quarter we did have some impact of Irma Hurricane. So, let us see how the growth rates progress ahead, but otherwise it is quite stable at this stage.

**Richard Liu:**

But the combination of U.S. plus Africa in the SON piece, was the delivery in the range of the figure that I mentioned?

**Sameer Shah:**

13% growth at overall level did have some impact as we shared earlier, whether it be political turmoil in Kenya, South Africa, the ERP integration issues in South Africa. We think this growth rate should be a bit higher than what at least we have clocked in Q2.

**Richard Liu:**

Any update on the Africa household insecticides piece?

**Sameer Shah:**

Right now, we are prioritizing the Wet Hair scale-up plans, as well as the investment over in household insecticides but we will see some action in couple of our key markets over next six to 12 months, in terms of launches.

**Moderator:**

Thank you very much. That was the last question. As there are no further questions, I would like to hand the conference back to the management for any closing comments.

**Vivek Gambhir:**

Thank you for your questions and your feedback. As I mentioned earlier, we look forward to delivering a stronger second half of the year on the back of a good Q2. And if you have any other follow-on questions or feedback, please get in touch with us. Thank you.

**Moderator:**

Thank you very much. On behalf of Macquarie Capital Securities that concludes this conference. Thank you for joining us. And you may now disconnect your lines.

*Disclaimer - The following transcript has been edited for language and grammar, it however may not be a verbatim representation of the call.*