



“CCL Products India Limited 3Q FY18 Results Conference Call”

February 02, 2018



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MODERATOR: **MR. ABHISHEK NAVALGUND – NIRMAL BANG
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Moderator: Ladies and gentlemen, good day and welcome to the CCL Products India Limited Q3 FY18 Results Conference Call hosted by Nirmal Bang Equities 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 the operator by pressing ‘*’ then ‘0’ on the touchtone phone. Please note that this conference is being recorded.

I now hand the conference over to Mr. Abhishek Navalgund from Nirmal Bang Equities. Thank you and over to you, sir.

Abhishek Navalgund: Thanks, Lizann. Good afternoon everyone. On behalf of Nirmal Bang Institutional Equities, I welcome you all on the 3Q FY18 Earnings Call of CCL Products (India) Limited. We have with us from the management Mr. Srishant – Managing Director; Mr. Sarma – CFO of the company; Ms. Sridevi – Company Secretary; and Mr. P S Rao - Consultant Company Secretary. So actually, without wasting much time, I will hand it over to the management for opening remarks and then we can start with the Q&A session. Over to you, sir.

Challa Srishant: Thank you, Abhishek. The company has achieved a turnover of 274.39 crores. The EBITDA is 64.86 crores. Profit before tax is 54.59 crores and the net profit is 40.42 crores for the third quarter. For the 9 months period ended 31st December 2017, the company has achieved a turnover of 820.33 crores. The EBITDA is 170.92 crores. Profit before tax is 139.86 crores and the net profit is 100.88 crores. As most of you already know, the third quarter of FY2016-17 is not a like-to-like comparable quarter to note the performance of this year's quarter 3. Reason being last year there was a plant shutdown in the second quarter and quarter 2 contracts were executed in the first and third quarters making it an exceptional quarter 2016-2017. If you have observed quarter one and two of the current financial year, there is a 23% increase in net profit on a quarter-to-quarter basis and 21% increase when we compare the net profits of Q2 and Q3. This growth will continue in Q4 as well which will enable us to achieve the projected profitability of 10% and turnover of 15% to 20% growth as well in this financial year. Thank you. Any questions?

Moderator: Thank you. Ladies and gentlemen, we will now begin the question and answer session. We will take the first question from the line of Jignesh Kamani from GMO. Please go ahead.

Jignesh Kamani: Srishant, on the Vietnam front, I think our agglomeration plant got commissioned in October. So probably for 2 months, I think we got a benefit of validated product. So in that context, what was the margin we reported looks on the higher side. So this kind of margin is sustainable because still if you take about entire you can say benefit was available only for part of the month.

Challa Srishant: It is not only sustainable, it will further increase for this quarter.



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Jignesh Kamani: So then in the case, what will be your right margin to look in Vietnam considering now agglomeration plant is....

Challa Srishant: Actually, so the range that we are looking at right now is sustainable, but one thing you should understand is again we have to look at it on a year-to-year basis. Looking at a quarter-to-quarter, it is going to be misleading. Sometimes the customer wants delivery in the first quarter, sometimes in the third quarter, sometimes throughout the whole year.

Jignesh Kamani: Have we shifted both our clients from India to Vietnam?

Challa Srishant: Yes, we have.

Jignesh Kamani: So to that extent, India volume has been slightly on the lower side which probably we might fill in the future?

Challa Srishant: Yeah because we intentionally kept it a little lower because in case the customer wants us to execute from India only, we have to keep that auction open. So we intentionally kept it a little lower for that quarter, but now that the transition has completed and this particular quarter, our volume will further increase both in India and Vietnam.

Jignesh Kamani: And now what is the utilization level in the Vietnam?

Challa Srishant: We are almost at peak utilization and this quarter also, we will be at peak utilization.

Jignesh Kamani: Any plan to increase from 10,000 to 20,000 now, first we will focus on the freeze-dried?

Challa Srishant: Not right now. Initially, we want to focus on freeze-dried and we are also focusing on better product mix from Vietnam.

Moderator: Thank you. The next question is from the line of Nitin Gosar from Invesco Mutual Fund. Please go ahead.

Nitin Gosar: Just wanted to understand the volume growth that we have seen for the quarter which must have gone by. Is it more coming from the spray or is it more coming from the freeze-dried?

Challa Srishant: The volume actually is increasing more from spray in this particular quarter. The freeze-dried as we already mentioned earlier were operating at the capacity. So there is no potential possibility of increasing volumes in freeze at this point in time until the new plant comes on line.

Nitin Gosar: And this new plan will be in India that would be in the second half of next year?

Challa Srishant: Yeah, quarter 2 of next financial year.



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Nitin Gosar: And on margin side, Vietnam has now started looking up. So this would be key for you to report 10% profit growth for the FY18 year?

Challa Srishant: Yes, it will be.

Nitin Gosar: And in India, the topline degrowth that we saw, I think you mentioned earlier that the like-to-like quarters are not comparable and point number one, India did not see agglomeration volumes. Did I hear it right?

Challa Srishant: Yes, that is correct. So both the reasons what you said is what we had explained saying that the first reason being last year was exceptional because quarter 2 orders were executed in quarter 1 and quarter 3 of last year and that is one of the reasons why the profitability also was much higher than last year Q3. The second reason being this agglomerations that we have been telling from the beginning of this year itself that as soon as the agglomeration Vietnam is up and running, we will do the transition of the customers from here to there. We will transition them back basically. And during this transition period, we cannot take a risk of not being able to execute the orders if some hiccup comes, so that small quantity we have kept it as spare capacity in India and we have enabled the transition. So once it got completed, we started filling that additional capacity as well.

Moderator: Thank you. The next question is from the line of Sneha Talreja from Edelweiss. Please go ahead.

Sneha Talreja: Actually, it was more or less pertaining to the guidance that we have given. So I think last quarter we were pretty confidence about more than 20% growth on the topline. Is that somewhat downwards or we will still continuously more than 20% kind of topline?

Challa Srishant: So the guidance what we had given 20% was on the assumption of the green coffee prices being more or less stable, but in quarter 3, there was a substantial decline in green coffee prices. So our volume guidance, everything is going to be the same, the same 20% is going to be there. However, the way gets translated is because the green coffee prices have come down of it, it will be maybe between 15%-20% or maybe 15%-17% to 20% or so.

Sneha Talreja: However, that does not impact our volume growth as well as any impact on the margins?

Challa Srishant: Exactly. There is no impact on margins nor is there any impact on the volume growth.

Sneha Talreja: And since we are near to the FY19 also, any guidance from next year as well whether we continue with the similar strategy of focusing on the volumes and margins may or see kind of continuously under pressure?



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Challa Srishant: So first thing first. Normally, we give the guidance for next year only on the completion of quarter 4. We do not give any guidance prior to that, but yes, volume growth will be there, but next year as most of the people already know, we have our freeze-dried unit also which is going to come on line which means that the volume growth and the profitability also should be better than what it is this year. The exact numbers and projections will be giving it only in next quarter.

Moderator: Thank you. We will take the next question from the line of Ritesh Rangwala from Nine Rivers Capital. Please go ahead.

Ritesh Rangwala: Just wanted to know on the Forex volatility that one faces, is there any provisions in your contract with your customer that shields you from the volatility?

Challa Srishant: We actually have back-to-back contracts. So we cover the raw material in dollar terms. Raw material itself constitutes about 70% of the product cost and so there is a back-to-back hedge in foreign exchange volatility.

Moderator: Thank you. The next question is from the line of Manoj Gori from Equirus. Please go ahead.

Manoj Gori: Sir just wanted to know what is currently our booking status because normally we get some idea about the booking for the next year during the month of December and January?

Challa Srishant: Yeah. So the bookings have already started for next financial year. We have already covered about 30%-40% of our capacity for the whole of next financial year. In the next month and a half, I think we will be covering around 60% of our capacity.

Manoj Gori: So this includes your freeze-dried capacity, additional freeze-dried capacity in Chittoor as well?

Challa Srishant: No, the additional freeze-dried capacity, we still have some time. We do not want to start filling that immediately. We are filling the existing freeze-dried capacity in Duggirala.

Manoj Gori: So from FY19 if we look at, so you're freeze-dried coming in and as you highlighted earlier as well, the margins are likely to remain on the higher side. Also with falling green coffee prices, do we hold any inventory at this moment which we should benefit in the coming quarters?

Challa Srishant: Actually no. So what happens is we always look on contract-to-contract basis. We do not take any risk with respect to green coffee fluctuation. So whatever contracts we have in place, we have covered the coffee to that extent. Our speculation is something we do not want to get into because in fact if you look at all the reports and world market data, everyone says there is sufficient raw material available, there is sufficient green coffee available, productivity is up, but at the same time you do have news coming and saying that oh, there is some shortage



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somewhere and funds taking position in coffee. So fluctuations can take place at any given point in time. Lot of people expect that the green coffee prices to come down from actually February onwards, but in reality the correction started taking place in November itself which resulted in the topline and turnovers. So because of this reason, we do not speculate in green coffee at any given point in time. That is the business model of the company.

Manoj Gori: So Brazilian and Vietnam crop have been very good. So that could be the key reason for the drop in green coffee prices?

Challa Srishant: For the drop in prices, yes.

Moderator: Thank you. We will move on to the next question that is from the line of Rahul Maheshwari from IDBI Asset Management. Please go ahead.

Rahul Maheshwari: Just now in commentary, you told that for the capacity which is there excluding the freeze-dried that has been booked about 30% to 40% of capacity and you will book 60%, but in quarter 2 concall you had already told that your 5,000 freeze-dried new capacity which is coming in Chittoor, orders have been filled for FY18 and for FY19, the 30% of the capacity is booked.

Challa Srishant: No, the 5000 tonnes I was referring to the existing plant. For the new plant until the plant is actually commissioned and until we actually submit samples to the customers, we cannot sell the coffee. If we commit to something and if there is any delay for any reason, there will be a lot of penalties and other things imposed on us.

Rahul Maheshwari: So current freeze-dried coffee plant which is there in India, how much does it contribute?

Challa Srishant: Contribute where towards the..

Rahul Maheshwari: Towards the volume, towards the topline, towards the EBITDA, any?

Challa Srishant: Approximately around 300 crores or so comes in on the topline from freeze-dried.

Rahul Maheshwari: And in volume terms, how much it contribute?

Challa Srishant: Volume terms, about 6000 tonnes is capacity that we have here.

Rahul Maheshwari: And with 100% is being utilized?

Challa Srishant: Yes.

Rahul Maheshwari: Can you talk bit on your continental coffee which is a retail segment that you had given a target of 80 crores by FY18 you would be striking. Where is the guideline right now?



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Challa Srishant: So now that we have Praveen on board. He has done a lot of changes in the market, so what he has focused on is revising the current supply chain margins that we are passing on and he has also with respect to the offers, schemes and BTL activities, he has done several revisions. What he has done is he has reduced the volume guidance from the 80 crores to around 70 crores, but he has increased the gross margins from about 5% to 8% that we had earlier to closer to 30% now.

Rahul Maheshwari: So what is the rationale? Can you give more color that what is the strategy that you are taking place that within one quarter what it made you to go less on the volume front, more on the margin side? Going forward it would be more towards keeping it niche, not a volume-based brand or what?

Challa Srishant: Exactly. So that is the right question in fact. So the idea earlier we were just trying to sell our product as a me-too product Nestle and HLL are already there with their products in the market and our products were just another alternative that was available. So we were giving heavy discounts, we were pushing volumes. That is the strategy what he said is not sustainable and the idea is to build a brand. In order to build a brand, you need to create that demand and the pull. For that, you need to change the perception the people have with respect to your product. So that process has been initiated now and the response also has been really good. We have already started ATL activities in December of last year and we are continuing the ATL activities even in this year.

Rahul Maheshwari: So what can be the guidance by FY18, how much you would be targeting if you have reduced from 80 crores to how much?

Challa Srishant: From 80 crores to 70 crores.

Rahul Maheshwari: And but the margins would be 30% from 5% to 8% to 30%?

Challa Srishant: Exactly.

Rahul Maheshwari: But how big is this market which you want to create a brand that in India going for more premiumized coffee kind of thing, generally it has been taken the CCDs and all these outlets which is there, but on a retail front side, at a home consumption, do you think the strategy of consumption of the very premium based brands is working?

Challa Srishant: The current records if you look at, of course the Nielsen's report, see instant coffee market in India, it is 1,800 crore market. I am talking about plain instant coffee sold in retail segment. This excludes data from institutional sales and it also excludes remixes which are currently being sold and it also excludes the roasted ground business. If you combine all the segments together, it works out to be almost 4,000 crore market. In 4,000 crore market, we have right now, though we are present in several states, about 80% of the coffee consumption is coming



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from the South Indian states which is why even we are focusing on the South Indian states at this point in time and without much of advertising or pushing the products, we are seeing an excellent response. So we are hoping that once we start building the brand in a more structured and professional manner, it should grow much faster as well.

Rahul Maheshwari: And what kind of investments would we take in place for this to have?

Challa Srishant: Actually because we have already created a volume base in the last couple of years, there is not much support that is actually required from the Indian company, from our parent company. The exact numbers and guidance will be giving towards the end of this quarter 4 in the next conference call.

Rahul Maheshwari: And third question in last concall, you had told that the number of manufacturers had increased at global level. So can you give a color on how the US is performing? Our capacity is just at 2,000 tonnes right now which we are giving to the US business as compared to 80,000 tonnes which we had mentioned. So can you give color on what is the demand scenario, what is your strategy going on because you used to always say that it is a big trigger for us if one litigation or if the regulation takes place, so on a global level, how the scenario is working on a coffee consumption?

Challa Srishant: So if you look at coffee consumption per se, it is still growing at the same 2.5% year-on-year, but what is interestingly happening across the world is there is a lot of consolidation which is taking place as well. Last year, we have seen one of our major competitors/customers being taken over by a big brand. So all the private label business that they had is now getting spread to other companies and we have taken a large chunk of that business. Now this year, based on the enquiries that we have been receiving, I cannot mention the name, but there is only one manufacturing company which is currently there in the US which might be in the process of shutting down during the year. So all the customers are looking for alternatives immediately.

Rahul Maheshwari: Is that manufacturing facility which is going to shut down. It is a big contributing towards US?

Challa Srishant: It is a major company. So because again because of companies in Asia which have been competing so much with US and other companies, their cost of productions are higher, they are not growing green coffee. So obviously they would not be able to sustain with respect to the others, other competitors. So that is one of the reasons why they seem to be in the process of shutting down. So that is additional capacity that is going to get transferred to the other manufacturers across the world.

Rahul Maheshwari: How big is that capacity? If you do not want to name the company, it is fine, but any out of 80,000 tonnes, any capacity?

Challa Srishant: No, around 10,000 tonnes.



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- Rahul Maheshwari:** How confident you are to get that chunk of 10,000 tonnes?
- Challa Srishant:** It is not possible to get the entire 10,000.
- Rahul Maheshwari:** I agree because that means the capacity itself is not there with the company, but incrementally how much you would be targeting?
- Challa Srishant:** So initially it depends on, there is a huge accrual process and all that which we have to follow. There is no number as such that we can give because there are too many factors which are in place including every single company in the world is after that business. It is not any one customer; it will be say 10, 15 or 20 customers who are currently there with that particular company. Everybody is asking them.
- Rahul Maheshwari:** But is it that from 2010 next year, it can easily be reached to 4000 tonnes doubling the capacity in US?
- Challa Srishant:** What 2000 tonnes?
- Rahul Maheshwari:** The demand which we are catering to...
- Challa Srishant:** Currently, yes for next year from 2000, there is a possibility of going up to 4,000 or more also. But we are not only dependent on that one particular geography. If we do not get the volume from there, we will be able to get it from other places as well.
- Rahul Maheshwari:** Any update on Switzerland plant. After percent being deployed over there, what is the situation and how things are getting recovered over there?
- Challa Srishant:** His primary focus has been to add new customers especially local customers and he has successfully done that. In fact in Europe also, there is a little bit of consolidation taking place. So couple of companies which are reducing operations, in fact manufacturing operations and outsourcing their production to other companies, so they have outsourced to us. So we are getting some new orders in for the Switzerland plant as well.
- Moderator:** Thank you. The next question is from the line of Akhil Parekh from IDBI Capital. Please go ahead.
- Akhil Parekh:** Questions on this freeze-dried plant. When are we expecting, so you had mentioned like we will be starting this freeze-dried plant by second quarter of FY19. Are we on target for this?
- Challa Srishant:** Yes, we are.
- Akhil Parekh:** One thing in terms of this quantitative coffee brand which you just mentioned like we cannot keep on giving discounts and we have to work on the branding side, but just to mention like



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this month on Amazon I was seeing buy two plus two get free on continental coffee brands. So I think it is a kind of dilution of brands. So would you be able to highlight something on that front?

Challa Srishant: Yes, that is exactly what we are doing. So what is currently there, the offers and all are slowly being removed now. So this also being changed. We do not want to drastically change the buy one get one free what is currently there. We do not want to suddenly change that, but we will be gradually facing it out. So whatever margins we are seeing right now, 30% I was talking about is after factoring in this Buy One Get One Free. So once we reduce this, there should be further improvement, but I think we will end up using this additional amount for the brand building purposes.

Akhil Parekh: And when do you expect this phase out to happen?

Challa Srishant: Immediately.

Akhil Parekh: And you mentioned this 80% of the coffee market is based out of South India, but if I remember from our last few con-calls where you had mentioned South India is mainly a filter coffee market and we do not have filter coffee. So I am not able to understand like why we are targeting this market when the market is basically purely a filter coffee market?

Challa Srishant: Yes, it is predominantly a filter coffee market, but the instant coffee sales are also maximum in South India. In North India, if you look at the consumption pattern also, people, the quantity that they consume is 0.7 g for a cup of coffee. But in South India, for one cup of coffee, they use a minimum of 1.5 to 2 grams. So it is just a slight color change which people of North India are expecting. It is full milk with little bit of coffee flavor which they are looking for. So the quantity if you look at value and quantity, North India contributes only to 20% of the entire Indian coffee market and if you want to really aggressively create a presence in North India, you have to spend that much more which did not make sense at this point in time. We wanted to establish ourselves where the current instant coffee sales is maximum and the roasted coffee sales are also high. So we will be introducing new brands including roasted coffee in the South Indian market.

Akhil Parekh: And in terms of sales, you mentioned like 1,800 crores for pure instant coffee in retail market in India and total is 4,000 crores which includes roasted ground plus the institutional sales. So in terms of volume, would you be able to share like some numbers over here like how much is tonnage wise in India instant coffee market?

Challa Srishant: Within India, it will be close to 15,000 tonnes or so.

Akhil Parekh: This is for pure instant coffee right?



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- Challa Srishant:** Yes, instant coffee as sold in the form, let it be in the form of remix or in the form of direct institutional sales through retail B2C as well.
- Akhil Parekh:** And I assume like we do not have much of market shares in this 15,000 tonnes right now?
- Challa Srishant:** Yeah, out of the 15,000 tonnes, I think maybe around 10% market share we have right now.
- Akhil Parekh:** One more thing in terms of guidance like you had iterated last couple of con-calls in terms of bottom-line, we should grow around 10%-15% for FY18 and it does not seem to be possible at this moment given that we are most flattish on consol level for first 9 months. So would it be a fair assessment to say that we will not be able to reach the 10% kind of growth for FY18 at bottom-line level?
- Challa Srishant:** Absolutely not. We will definitely reach our target. See if you look at it, last year as I was mentioning is not comparable, but this year would be a comparable year for the future as well. If you look at quarter one to quarter two, we have seen a 20% increase in the bottom-line. Quarter 2 to quarter 3 also, there is more than 20% increase and quarter 3 to quarter 4 also, there will be a similar increase.
- Akhil Parekh:** So you are saying on QoQ basis, we will see 10% of growth.
- Challa Srishant:** Yeah, quarter-on-quarter, we are seeing 20% growth, but on a year-on-year basis, there will be at least 10% growth.
- Akhil Parekh:** For full year FY18?
- Challa Srishant:** For FY18 compared to last for FY17 to FY18, there will be at least 10% growth in the bottom-line as we have guided at the beginning of the year. We are fully on track for that.
- Akhil Parekh:** So if it would be fair to assume fourth quarter should be very strong quarter then?
- Challa Srishant:** Yes, it will be.
- Akhil Parekh:** And one last question in terms of Vietnam market, what I was reading through is the industry is going through kind of a downcycle. In Vietnam, the growth was around negative 12% to 13%. Can you shed some light in the way how Vietnam market is shaping up?
- Challa Srishant:** Vietnam market, our industry is completely different from others. So it is not exactly a fair comparison to make. We are looking at purely on the coffee side. So coffee side, we have our own strategies in place and there is no change in our strategy. One good thing for us is there is with the new aggro plant and everything coming on line, we will also be able to install some



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maybe small packs and start offering that to customers as well. So our growth potential year-on-year from now onwards from Vietnam will be quite good.

Akhil Parekh: So if I can just squeeze in one more question. For the freeze-dried, you said second quarter 19 we should get started. So how much utilization level do we expect? Can we expect around 40%-50% of utilization level for FY19 from the new plant?

Challa Srishant: Yes, you can.

Moderator: Thank you. The next question is from the line of Sagar Arya from White Oak Capital. Please go ahead.

Sagar Arya: Sir, I was just going through some industry reports and I noticed that instant coffee market, most of the growth is coming from developing countries as compared to developed countries and one of the major reasons for that is in that developed countries you are seeing competition from fresh coffee ports or brewed coffee? What do you make of that? What is your sense of the instant coffee market going forward with such dynamics in place?

Challa Srishant: Actually that is true. There is a lot of competition coming in from roasted coffee and people are willing to pay a premium for per cup basis. If you get a machine coffee like a coffee dispensing machine and then get the coffee, it is costing almost about 80 cents to a dollar to make a cup of coffee. If you are talking about instant coffee, it will be less than 10 cents. So there is a huge gap in pricing. If you want to go up the value chain, yes, that is a good option, but there is also lot of competition in that segment, the roasted coffee segment especially.

Sagar Arya: Right. But sir in sense I mean the fact that the market is declining, it is proof that the consumers are not that price sensitive right? They take care more about...

Challa Srishant: It is not declining. If you look at the global coffee market, it is growing at the rate of 2.5%.

Sagar Arya: Right. But how much of that growth is coming from developed markets?

Challa Srishant: Developed markets wherever there is a population degrowth taking place, the coffee consumption is remaining the same. The actual additional growth is coming like if you want numbers, US is a market that is consuming 85,000 tonnes. Japan is consuming 35,000 tonnes, India which is a growing market is consuming a maximum of about 15,000 tonnes. So even if we grow at space of say 10% year-on-year, it is only about 1,500 tonnes which is getting added. But in an 85,000 tonne market, even if we grow by a fraction of that, you will achieve a similar absolute volume growth. So if the base which is much larger in the developing country which is also wide volume growth, it appears as if there is not too much of a growth over there. India and China especially, these are the two markets where there is a substantial growth in instant coffee consumption. In China also, you are talking about almost 20% growth. That is



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also because Starbucks has come in, they set up shops, they have gone quite aggressive in the market and the trickle-down effect is soluble coffee growth is also there in the same market.

Sagar Arya: So currently majority of your sales are coming from Europe, right?

Challa Srishant: No, not at all. We are supplying to now 9 countries. So it is spread across the world. We will never be dependent on any one geography at any given point in time. So there is a lot of volume that we are supplying to Asia, Russia, CIS, Europe, Africa and North America.

Sagar Arya: Also I just wanted to understand do you sell your produce to the end consumers directly or do you go through distributors?

Challa Srishant: In the domestic market or?

Sagar Arya: In the export market.

Challa Srishant: So our customers are at this point in time are either brand owners or supermarkets. So the brand owners, they take care of the distribution at their end. The supermarkets, we supply directly to them. They just place it in the supermarket. We also supply large volumes to repackers. Repackers are people who buy bulk from manufacturers like us and others. They do blending at their end, packing at their end and they supply to other brands as well.

Sagar Arya: And how much would repackers have gone for total revenues right now?

Challa Srishant: Maybe around 30%-40%.

Sagar Arya: So the major value addition mostly come from getting brand owners and when you are selling directly to supermarkets because that is when you are selling your own blends.

Challa Srishant: No, it is not our own blends. It is usually the customers' blends that we are selling and even if these repackers, you cannot discount because usually what happens is when a brand becomes bigger, they would not buy small quantities from a repacker, they were rather go directly to the manufacturer. So there is a lot of business that has got in transition to us in this manner as well. Initially, they build up smaller volumes from the smaller repackers that we are supplying to. In fact, we recommend that if small enquiries come to us, we recommend that they buy from a repacker that we are supplying to in a particular geography. So that their business volume also gets maintained. Our headache gets minimized. We have lesser number of people to deal with and future when their volumes grow when it justified for them to come to a manufacturer directly, they come to us.

Sagar Arya: Okay. Sir, I was just going through this article dated 2nd June 2015 which said that toxic effluents from CCL Products is impacting the villages around it. Can you please throw some



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more light on this? What exactly was the issue here and what steps have we taken to improve the situation?

Challa Srishant:

Okay. So what has happened is, at that point and in fact this is a question that was asked several times before and we have already answered this, but just to reiterate, our industry is such that our raw material is green coffee and the only other ingredient required to manufacture finished product is water. So water that we use is ground water. In the instant coffee manufacturing process, you cannot use chemicals at any given point in time because it is a food grade product. It is only roasting the seeds and adding hot water extracting the liquid and spray drying it. The effluents that gets generated is simply coffee water, what we do apart from running it through the ETP, what we further do is the solid waste is used in the boiler and the boiler output, the ash that is generated is sold to brick manufacturers. So water that gets generated we actually give it to the neighboring farmers. So we always maintain records for the last 20-odd years, if you visit the factory you will notice, in and around the factory area we have never had a single problem with a single farmer at any given point in time because they specifically request for our water for two reasons. Because of the organic properties which are there, they are getting a better yields than anybody else. The complaints that have come have come from people who try to blackmail us numerous times because they do not have any land or any other business interest, in and around the factory. They come and they said, what benefit are we getting? So you pay us some amount, we will be quiet otherwise we will give a complaint. We said do what you want. So the PCB also has investigated. They are fully aware of all this which is why they are operating normally. We don't have any issues with either the PCB or neighboring farmers. But there will be antisocial elements who will always be there. The fact that they are saying toxic waste is unheard of. Anyone can do any research, it is impossible to use, any sort of chemicals in instant coffee production which anyone in the coffee industry can vouch for.

Moderator:

Thank you. The next question is from the line of Anuj Jain from Valquest. Please go ahead.

Anuj Jain:

Srishant, I have couple of questions. You mentioned in the concall that you have plans to increase roasted coffee in future. So are we planning to get into filter coffee segment in future?

Challa Srishant:

Sir, this is a segment that we didn't want, as in we didn't consider earlier. But Praveen after doing his research was saying that there is an opportunity to grow here as well. So this is largely an unorganized market and we can offer like one of the pain points that are current there in the market is quality consistency. So we have the ability to address that pain point in an efficient manner. So that is one of the reasons why we are seriously going to address this market as well.

Anuj Jain:

And what will be the size of opportunity for this roasted coffee segment?

Challa Srishant:

The roasted coffee is almost a 1,000 crores market.



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Anuj Jain: And also you mentioned that for the domestic business we are targeting 70 crores of sales. So what will be the breakup between institutional and the branded continental coffee.

Challa Srishant: The branded sale will be more than about a 50%-60% and this includes our institutional supply in the branded name. Our private label and bulk sales will be around 40%.

Anuj Jain: Okay. And for both of these segment, the gross margins you mentioned was 30%?

Challa Srishant: For the average blended this thing is 30%, all put together. It is usually the brand which gives you much higher margins than the other bulk business. So the reason why there will be a further improvement in the subsequent years is because the branded sales are growing almost at the rate of 100% year-on-year.

Anuj Jain: And what would be the average realization per kilo for this domestic volumes?

Challa Srishant: It is around Rs. 500 per kg.

Moderator: Thank you. The next question is from the line of Ankur Shah from Quasar Capital. Please go ahead.

Ankur Shah: Sir I just have one question on the volume growth. So when you say that the whole coffee market is growing at 2.5%-3%, how we are so confident of achieving like 9 to 10 times the market growth rate. Like what are the drivers because essentially what I understand, it is a processing business which doesn't require a lot of capital. Maybe a little bit of entry barriers in the mixtures which you all make. So how are we able to achieve that kind of growth and we are so confident.

Challa Srishant: So, the reason again is, it is not only one factor. There are number of factors that play an important role. First is, we have been in the market for a really long period of time. So we have the right partners in each geography. We developed business over the years, business that have started with small volumes, could have started with 5-10 tonnes which has grown to even 2,000-3,000 tonnes. So there is business like this which has taken almost 20 years to grow. There are a lot of steps that we have initiated several years ago which is paying off now and these people will continue to buy from us because we keep the blend confidential. The R&D is 100% ours. We are currently selling almost 1,000 different blends to customers in over 90 countries. Now all these blends are complete property of CCL and if anybody wants to replicate it, maybe about 10%-20% of the blends can be easily replicated by other manufacturers. But the rest of the blends you have to invest substantially in R&D to do it. What we have also done is, we have constantly been upgrading our technology in-house. Whatever latest changes are taking place, we always keep experimenting with technology which also enables us to give products to customers before competitors can. This is also one of the reasons that customers are confident that if they want any innovation, if they want timely



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deliveries, if they want trust and confidence, they would rather come to us. There has been instances in the past where like smaller manufacturers, they have entered in the contract but when the green coffee price moves, they try to renegotiate. Customers don't like that, which is why everything works on the basis of relationships. The coffee industry itself is so small that literally we will know every single manufacturer, brand owner or even competitor directly. In fact, we do have regular meets as well, where competitor meets with each other as well.

Ankur Shah: Okay. So sir, like where does the growth come from? Does it come from the existing customer or the major part of the growth is contributed by new customer acquisition?

Challa Srishant: It is both actually. We do get substantial growth from existing customers also because there is a lot of stickiness which is there in the business. Adding new customers is always a challenge because of the same stickiness that is going to be there with competitors also. We usually give a value proposition or we also give product innovation propositions to enable a customer to shift over to us. If the current supplier is able to give them only 3 or 4 product blends, we will be able to offer them a much wider range, making it more efficient convenient for them to buy from us.

Ankur Shah: Okay. So what is the customer acquisition run rate every year, like on an average how many new customers do we acquire every year?

Challa Srishant: Usually it will be, maybe 1 or 2 major customers and smaller people can be in the range of even 20 or 30.

Ankur Shah: Okay. And sir, the existing customers like just to again think about the market growth, do we get a higher share of the wallet because they are very happy with the products or they themselves are growing at very high rates?

Challa Srishant: It is actually a little bit of both. They are growing as well and what we do is because we are giving a product which is, the quality consistency, all that is there, when the volumes grow the same margins also get maintained and the benefit comes to us. Apart from that, offering new products to an existing customer as well. A new product usually will be lower volumes but higher margins because they will be specialty products.

Moderator: Thank you. We will take the next question from the line of Nikhil Upadhyay from Securities Investment Management. Please go ahead.

Nikhil Upadhyay: Three questions. One is on the freeze-dried capacity, now as we are closer to getting the capacity commissioned and over the next 3 years in terms of pricing and as you said that in earlier comments that the industry is quite small and we know most of the players, so over the next 3 years, do you see any new large capacities coming in other than Tata Coffee? So the



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whole idea is whether the pricing which we are enjoying currently, do you see that to sustain over the next 3-5 years?

Challa Srishant:

Actually the pricing is already under pressure because even Olam has come online with an additional 5,000 tonnes in Vietnam and Tata Coffee I think they are also expecting in the next 3 years to come up with an additional 5,000 tonnes. The market for freeze-dried also is growing. So one good thing is that even though there is this additional capacity, the market is willing to absorb this capacity. That is the positive thing for us but because there is additional capacity coming in this year from two major companies, the pressure has already started for freeze-dried at this point in time. So whatever margins we are currently maintaining should be sustainable, like last year's margins were little bit more on the higher side than what it is from now onwards.

Nikhil Upadhyay:

Okay. Sir and secondly, I think at the start of the year and also when I met you, the idea which we had for going for aggressive volume growth, even if it means some pressure on the pricing which we have to take, the whole idea was that we need to full the capacity, get the customers and then try to move them higher so that some of the customers can graduate towards freeze and all. So, now as the capacity is also coming online and we almost have, as you mentioned in earlier comment that 60%-70% of our other capacity would also be filled in, for next year a major margin trigger would be basically the improvement in the pricing from the existing customers which we give up in this year. Would that be a good understanding?

Challa Srishant:

No, actually this year what we have done, I think I explained this as well, quarter one and quarter two being the lean quarters, we aggressively priced our products to gain new customers. And the guidance that I had given also was that, in the future it is not likely that one year to the next we can suddenly increase margins with the same customer. It is a gradual process which will take some time. But because we have access to these customers now, it will become that much easier for us to fill the capacity of freeze-dried in next financial year. So our strategy that I was mentioning to the previous question as well, what we do the reason for our growth is not something which happens within short period of time. It is a lot towards planning that takes years for it to materialize. So for next year's plan, we have already initiated the steps in the beginning of this financial year. So the actual dividends will start paying out from next year onwards.

Nikhil Upadhyay:

Then effectively as we come to the end of this financial year, we would have a client, sufficiently large client base, which we can increase the wallet share from them over a period of time.

Challa Srishant:

Yes, and will be adding new ones as well. Like whatever we are doing right now is to focus on that volumes for the next year as well.



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Nikhil Upadhyay: And secondly now if I look at over the next 3 years for the company as a whole, now one of the major things which were coming up was the freeze-dried capacity which probably by next year we would have commissioned and we would be also in the process of gaining volume. From here now, does the focus shift for in order to grow the domestic business more aggressively?

Challa Srishant: There is no shift in focus because the domestic team that has been created, I think I have already mentioned this, now we have a professional CEO, they sit in a separate floor altogether. They have their own team. The team also has been built. So from our side, we don't have to do anything different from what we are currently doing. The idea has always been that, see the current rate of growth say a 15%-20% year-on-year growth is sustainable for the parent business for the next couple of years without a problem. That is something which we are quite confident on. Beyond that there will be additional contribution coming in from the domestic market. So we have given them some breathing space as well. We said that for the next 3-4 years you come up with your own strategies to substantially grow volumes within India and maybe in other places as well.

Nikhil Upadhyay: Sir, that was one on the management side, but secondly even if on the capital allocation part, if I look at it, because now we don't have any major large CAPEX as such, so because if we need to increase Vietnam from the current capacity, we have always maintained that it won't be a major capital investment as such. So as you said in terms of the breathing space, the new management team gets that much time, but also in terms of access to more capital income, would that be a proposition which we would be looking at that probably they get more capital in order to grow the business in terms of distribution and more ATL, BTL activity?

Challa Srishant: Actually that was an offer that was made from our side. But the team is quite confident that because the base is already there with them and since they are already earning good gross margin, they do not require too much support from us at this point in time. We want to ensure that we have a more sustainable growth. We are not looking at coming in a very big way, advertising in a crazy manner and then hoping that there will be growth. We want that growth to be more organic which should be a more balanced growth. Which is why we are not telling the team that you have to focus on a say 500% increase in market share within one year or two years. We are telling them you grow on a systematic manner. 100% growth year-on-year is quite good. So that is what we are asking, the branded business especially.

Nikhil Upadhyay: Okay, And lastly, basically then to a large extent, the cash generation which we would be having over the next 2 to 3 years, so how do you see the allotment? So one is we would be looking at reducing our debt, but probably parallelly would there be an improvement in the dividend payout or?



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- Challa Srishant:** Yes, we are considering that as well. Apart from the repayment of debt which is going to start maybe a year-year and a half from now, there will be an improvement in dividend payout as well.
- Nikhil Upadhyay:** And just one book keeping. If we have to expand our Vietnam capacity, if I am not wrong, the number was around 50 crores of CAPEX. Would that be right or...?
- Challa Srishant:** Yes, that is correct.
- Moderator:** Thank you. We will move on to the next question that is from the line of Aayush Bhutada from Aequitas. Please go ahead.
- Aayush Bhutada:** Sir, my question is any update on the US situation, the adulteration law?
- Challa Srishant:** No, there is no change at this point in time.
- Aayush Bhutada:** And any expectations on that?
- Challa Srishant:** No, nothing right now. But I think I have mentioned this last couple of times also, we don't know when it will happen. When it happens we will inform.
- Aayush Bhutada:** But then you were saying that this big manufacturing facility in US is shut down?
- Challa Srishant:** That is completely unconnected with it. That is only market forces that is causing that to happen. The plant itself is quite old. So instead of investing substantially in refurbishing or rebuilding the plant, they find it is efficient to outsource it to other manufacturers.
- Aayush Bhutada:** Okay. That order that might come to us that won't get affected because of the law?
- Challa Srishant:** No, it won't.
- Aayush Bhutada:** Okay. And what would be the current Robusta Coffee crisis?
- Challa Srishant:** The OG bulk prices are in the range of about Rs. 105 to Rs. 110.
- Aayush Bhutada:** Okay. And then any expectations of Robusta production this year? You had mentioned that there would be a bumper crop in Brazil?
- Challa Srishant:** So Brazil grows mainly Arabica. So they grow Rio Minas which is about 90% of the production, Robusta variant is called Conilon and that is less than 10% for them.
- Aayush Bhutada:** So bumper crop group is for Arabica, and what about Robusta then?



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- Challa Srishant:** Robusta also in Vietnam, there is a substantial increase in volumes that is coming in, though the news is that there are some issues here and there. But ground reality is that the crop is quite good for this whole year. The harvest also has just completed. It is in the process of being completed now. So everyone is quite happy with the crop.
- Aayush Bhutada:** So prices would remain around the same range then, Robusta Coffee?
- Challa Srishant:** Yeah. We are not seeing any sharp increase or decrease. Little bit, I think market fluctuations will be there and unless funds take a position and all that, little bit up and down is like to be there.
- Aayush Bhutada:** Right. And any new customers added this quarter?
- Challa Srishant:** Customers always keep getting added. That will be usually smaller people who are there. Major customers usually we are targeting about 1 or 2 customers in a year and that process is a constant ongoing process. It is not like in one particular month or quarter, customer is added, we are suddenly getting a benefit, and it doesn't work that way for us.
- Aayush Bhutada:** So the strategy would still be to you know aggressively add new customers?
- Challa Srishant:** Yes, definitely.
- Aayush Bhutada:** Same strategy, volume guidance, 20% similar?
- Challa Srishant:** Yes. The only thing, bottom line also will be a little more than what we are doing this year.
- Moderator:** Thank you. The next question is from the line Rahul Maheshwari from IDBI Asset Management. Please go ahead.
- Rahul Maheshwari:** Two quick questions. First is that, as you have said you have the blends which are being supplied to many countries. So out of the overall topline, can you give what kind of percentage contribution is taking place through this value added products from you and going forward what is your guidance that where you would be taking this value added so that it can be a margin expansion story kind?
- Challa Srishant:** Okay. So specialty coffees will be around 5% of our entire portfolio, maximum is 5%.
- Rahul Maheshwari:** And what is the margins of this specialty coffee?
- Challa Srishant:** That will be much higher. It could be maybe even 30%-40%.
- Rahul Maheshwari:** So going forward 2 to 3 years down the line what would be the contribution that you would be targeting to?



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- Challa Srishant:** See, going forward we are also going to look at small parts and other products which is currently around 30% of our product portfolio.
- Rahul Maheshwari:** Means, low units packs can....
- Challa Srishant:** Yeah. They are not only bulk packing but also jar, sachets; we are already doing around 30% of our business as that. We want to focus more on the small parts so that we will have better value additions...
- Rahul Maheshwari:** Okay. And but 5% specialty coffee going two years down the line, how much it can grow up to, a percentage of entire sales?
- Challa Srishant:** Not much to be frank because the coffee industry also there is a large portion which is value proposition. Like talking about your pods and all which are all specialty products, organic, rain forest, these kind of coffees, it is growing but it is not growing that drastically.
- Rahul Maheshwari:** I am just continuing the specialty coffee question. In India, the large players like CCD and all the coffee chains which are there, how many such kind of clients are towards your list and how much they contribute?
- Challa Srishant:** These kinds of companies we supply, like for Coffee Day we are giving say Instant Coffee. They do their own branding and there are just selling it. But these companies are all Roast & Ground coffee players and Coffee Day, they have their own plantations. So they do their own roasting and selling in their coffee shops. So their supply chain itself is completely different, but with lower level, there are several customers who do not have plantations and they have coffee shops, they procure from companies like us.
- Rahul Maheshwari:** Okay. And plans you would be coming into vending machines?
- Challa Srishant:** We already have actually. We have already started placing vending machines about 6 months ago?
- Rahul Maheshwari:** And how is the response and what is the target?
- Challa Srishant:** Response is actually really good. We have done something like about 750 machines in the last 6 months and the target is to do around 3000 machines in the next year.
- Rahul Maheshwari:** And what is the profitability kind of thing and how it can be changing. Though it might not be contributing a very large scale, but how it would be contributing meaningfully towards this strategy?



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- Challa Srishant:** So the main reason for the vending machine business is also the branding aspect. The model that is currently there in India is that we have to give machines free of cost. You will recover the cost within 3-6 months. So there is not substantial contribution that will come in because of the machines but there is a good brand presence that gets built up because of the machines.
- Rahul Maheshwari:** Okay. And last question that you told that in the current raw material 70% is the green coffee prices and they declined during this quarter, what was the reason behind the decline? Sorry if it has been answered. But I could not attend.
- Challa Srishant:** The reason for the decline in Coffee market is market forces. Because as you rightly put it in the beginning, your first question was regarding the coffee prices, right?
- Rahul Maheshwari:** Yes.
- Challa Srishant:** The bumper crop and all that because there was an announcement that came up saying that there is a bumper crop in this year. The harvest season starts in November...
- Rahul Maheshwari:** And it lasts to how much period, means if it is starting from November to which period it ends up?
- Challa Srishant:** November to January is when they do the harvest, but you will have a clear idea, before November itself it the crop is likely to be good or not. So based on that, based on speculation and lot of other reasons, there was a sharp decline in coffee prices?
- Rahul Maheshwari:** Has the product been very bumper, what the speculation was being there that due to the bumper crop the prices got decline, so...?
- Challa Srishant:** Yeah, ground reality is also the same. There is a bumper crop. There is lot of availability which is there. And fortunate good part is that for us it doesn't matter. Whether the prices go up or down, it really doesn't matter because the business model is not to work on fluctuating prices. We work on a fixed contract basis. So irrespective of the prices going up or down the only impact might be turnover. Which is why turnover will not be a realistic way of judging the performance, it is usually bottom-lines.
- Rahul Maheshwari:** But sir on domestic front, how much is your contribution to the entire sales and global, no doubt the global will be higher contribution towards your sale. Any just rough breakup kind of thing?
- Challa Srishant:** I think the guidance itself will give you the numbers. We are talking about 1,100 crores to 1,150 crores topline for this financial year and as far domestic is concerned around 70 crores or so is what we are looking at.



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- Rahul Maheshwari:** And the rest is entire global sales?
- Challa Srishant:** Yes, exactly.
- Moderator:** Thank you. The next question is from the line of Nitin Gosar from Invesco Mutual Fund. Please go ahead.
- Nitin Gosar:** Sir, just wanted to understand. You mentioned that there are two new facilities which are coming up globally and the pricing power or the pricing that we used to command on spray and freeze, now freeze has also come under stress because of this two new facility, so does it mean that globally the pricing power conversion that we are commanding has started to come off?
- Challa Srishant:** Not, really. At this point in time, whatever numbers or projections we are giving is on the assumption that these capacities will come on line. We were already prepared for this, well in advance. So whatever guidance that we are giving also, is after factoring in all this.
- Nitin Gosar:** Fair point. But there was also an understanding that the freeze freight realization on the margins that we were seeing that will continue into whole good?
- Challa Srishant:** Yeah.
- Nitin Gosar:** But right now on call, you mentioned that there is a bit of decline or stress on the utilizations and margins that freeze-dried can offer?
- Challa Srishant:** Yeah.
- Nitin Gosar:** There is a bit of change which I am trying to understand.
- Challa Srishant:** There is no change as such. See, we said that the prices will hold good because there is a huge gap which is there between spray and freeze. And freeze, end of the day there will be a couple of percentage points here and there which go up and down, again depending on the number of market situations, so like this capacity is one of those situations. One of the things we did mentioned earlier also was, last year what we have seen in freeze-dried prices was exceptional because of the demand. We won't be able to cater to the demand, which was the main reason for setting up the new unit in the first place.
- Nitin Gosar:** Okay. So in the past you have been in position to do around 20% EBITDA margins on consol basis, is that the number to go by because on 9 month basis you have reported similar kind of number?
- Challa Srishant:** Yes, that will actually further improve a bit.



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- Nitin Gosar:** So, 9-month number that we are seeing right now on percentage margin that can improve...?
- Challa Srishant:** That will improve.
- Nitin Gosar:** So the year to end with, probably the FY18, the numbers that we will be seeing, that is the number to go by or it has potential to improve thereafter all?
- Challa Srishant:** No, it will improve thereafter also because the numbers that you are seeing this year is because we are working with that limited capacity. Next year once we add additional capacity, you will see a better utilization taking place, obviously the numbers will also further improve because of that.
- Nitin Gosar:** Okay. And bit of understanding if you can help and provide on gap between the realization and the margins between spray and freeze, just an indexation to understand?
- Challa Srishant:** To be frank, it will be deterrent for us to get into those details on a conference call.
- Moderator:** Thank you. Ladies and gentlemen, that was the last question. I now hand the conference over to Mr. Abhishek Navalgund for his closing comments.
- Abhishek Navalgund:** Thank you to all the participants and management of CCL Products India Limited for answering all the questions patiently. Over to you sir, in case we have any closing remarks.
- Challa Srishant:** Nothing much. Even I would like to thank all the participants for taking part in this conference call and for asking all the important questions. Thanks again.
- Moderator:** Thank you. Ladies and gentlemen, on behalf of Nirmal Bang Securities that concludes today's conference. Thank you for joining us and you may now disconnect your lines. Thank you.