"Heritage Foods Limited Q3 FY2018 Results Conference Call"

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Moderator: Ladies and gentlemen good day and welcome to the Heritage Foods Q3 FY2018 Earnings Conference Call, hosted by Sunidhi Securities & Finance Limited. As a reminder, all participant lines will be in 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. Shailesh Kumar from Sunidhi Securities & Finance Limited. Thank you and over to you Sir!

Shailesh Kumar: Good Evening, Ladies and Gentlemen. On behalf of Sunidhi Securities, I extend a very warm welcome to all of you for Q3 FY2018 Post Result Conference Call of Heritage Foods Limited. Management side is being represented by Dr. M. Sambasiva Rao – President; Ms. Brahmani – ED; Mr. A. Prabhakara Naidu – CFO; Mr. Samba Murthy –Dairy Division Head; and Mr. Umakanta Barik – Company Secretary.

Presentation giving brief in quarterly performance has already been uploaded on the website I trust you must have an opportunity to go through it.

Without taking much time I now hand over the call to Dr. Rao to give his initial comments and then it will be followed by question-and-answer session. Over to you Dr. Rao!

M Sambasiva Rao: Thank you Mr. Shailesh. We from Heritage welcome you all for this quarter three earnings call and thank you very much for your continued interest in Heritage.

I would now highlight certain financial numbers from the quarter three, which are anyway available on the investor update has been circulated and notified.

Current financial year quarter three standalone Heritage Foods numbers I will be explaining first after that I will give a consolidated numbers for the quarter three. Turnover has reached 571 Crores, which is 27% growth over the previous year same quarter.

EBITDA has reached 37 Crores, which is almost equal to the previous year same quarter which was 37.8 Crores. PBT is 24.4 Crores compared to 29 Crores of the last year same quarter. PAT is 15 Crores versus 21 Crores of the previous year.

Now I explain the consolidated numbers, which includes Heritage Foods, which is subsidiary handling cattle feed and farmer welfare trust. The turnover of quarter three is 579 Crores which is again 27% growth over the previous year. EBITDA is 38 Crores, which is almost equal to the last year same quarter 38.4 Crores. PBT 24.4 Crores, which is lower than the previous year's quarter that is 30.5 Crores. PAT is 16.71 versus 22.87 in the previous year same quarter. PAT I repeat consolidated at company level quarter three current year is 16.71 the previous year is 22.87.

These are the financials, certain operational parameters and details of the quarter three. Milk procurement increased by 29% during this quarter. The last year we collected 10.5 lakh liters per day and this year quarter three average reached 13.6 lakh liters per day. There is a significant growth in the volume in procurement. Sales volume of milk also has grown 22% the previous year it was 8.63 lakh liters per day and this year it is 10.53 lakh liters per day.

Coming to value added products contribution it is 19% to the total revenue. Growth over the last year same quarter is 13%, which is 108 Crores versus 95.75 Crores last year. In the value added products curd contributed to 82% of the branded value added products and the sales growth of curd is 16%.

A few numbers about the acquired business Daily Life from Reliance last year, which was taken over in the month of April 2017, now we have completed nine months and this quarter revenue 45.5 Crores is contributed from that business almost northern states are considered in this.

At EBITDA level this business contributed at 2.5 Crores operational loss, which is substantially lower than the quarter two, which was 7 Crores. At PBT level loss is come to 5 Crores in this quarter which was 9 Crores in the quarter two. As I explained earlier the losses has come down in quarter three on this acquired business from 9 Crores for the quarter two to 5 Crores in the quarter three and quarter four we are looking forward to breakeven.

Volume milk procurement in this acquired business is around 1.5 lakh liters per day out of the total 13.6 lakh liters in terms of sales volume from Dairy Life it is 110000 liters out of total 10.55 lakh liters, this is the contribution from the acquired business.

Capex for the quarter we have spent 23.5 Crores in the Dairy. That is as of now term loan is 136 Crores in Heritage Foods and 83 Crores working capital total 219 Crores is the debt. In Heritage Nutrivet that is Cattle Feed term loan is 5 Crores and working capital is 2 Crores around 7 Crores is the loss there.

Cattle Feed business we have achieved in quarter three 17.3 Crores turnover versus 15.3 in the last year same quarter which is 13% increase. EBITDA level quarter three we have got

87 lakhs versus 45 lakhs in the previous year same quarter. At PBT level the Cattle Feed business got 40 lakhs positive in this quarter versus 44 lakhs positive last year. At PAT level it is higher this year it is 1.41 Crores because of certain deferred tax asset got added and some tax provisions were reversed. Volume metric tonnes Cattle Feed sales in quarter three crossed 11000 tonnes and our new Cattle Feed plant commissioned last year the March 2017 has now achieved 42% of capacity utilization we are going to improve the capacity utilization in this quarter.

These are broadly the important factors we wanted to highlight you for your understanding and appreciation of the business movement in the quarter three. Now I open it for discussion any specific clarifications we can offer. Thank you very much for your patient hearing.

Moderator: Thank you very much Sir. Ladies and gentlemen we will now begin the question and answer session. We have our first question from the line of Dhaval Mehta from YES Securities. Please go ahead.

Dhaval Mehta: Good afternoon. Thanks for the opportunity. Sir my first question is on our value added portfolio. Sir our value added portfolio growth rate has declined vis-à-vis earlier run rate of 18%, 20% plus I understand that the base is now no longer small, but Sir is apart from curd which is the other category which is growing faster in the value added portfolio?

M Sambasiva Rao: In this quarter I am sure you may recall, there were heavy rains in all the markets where we operates Bengaluru, Chennai, Hyderabad, Mumbai, we pass through a massive rainfall days weeks together. So many of the value added product off-takes have come down because of the weather conditions particularly in these cities, otherwise the business as usual but for those days where we have lost the volumes. Apart from curd what we have seen growth is in paneer, flavored milk, buttermilk, these are the products contributing for the growth of the value added products in the branded category.

Dhaval Mehta: Sir how is the ice cream portfolio doing like because we have not heard about the portfolio from long?

M Sambasiva Rao: Ice cream is on a kind of saturated mode and now we are activating with different activities from this season from the month of March we would be putting greater focus on ice cream we are coming out with some premium ice cream with a separate brand a sub-brand also added more and more variants to the range and introducing more freezers in the market and taking up certain marketing activities to promote the ice cream from Heritage.

Dhaval Mehta: Sir my second question is on the Reliance business, when we had acquired our run rate for quarter was around 60, 65 Crores of revenue. So this quarter we have drastically came down to around 45 Crores. So like even being the flush season the overall revenue from Reliance is quite low. So can you throw some light on it?

M Sambasiva Rao: We have scaled down the procurement of milk in that region because the commodity prices were low as you must be watching the prices of milk power, whitener, ghee, butter have come down significantly for the same volume you sell you get lesser realization that one that the reasons for the low revenue second is we are voluntarily scale down or non-consumer products the bulk sales of these commodities we have consciously brought it down because they are prime reason for the losses in that area. So we will be rebuilding our sales through the consumer sales in the months to come and particularly now in a month time season will change in those states then we will see growth of the consumer sales.

Dhaval Mehta: It is like going ahead what should be the run rate for this business still we can expect of order decline in revenue Q-o-Q going ahead or I think this we have to reach from?

M Sambasiva Rao: In-house that moving upwards from this Q4 itself.

Dhaval Mehta: That is helpful. Sir I will come back in the queue sir more further questions. Thank you.

Moderator: Thank you Sir. We have our next question from the line of Aniruddha Doshi from ICICI Securities. Please go ahead.

Aniruddha Doshi: In this quarter our milk procurement rate as well as the milk price realization both have remained almost similar on a September quarter basis, but despite that there is a sharp improvement in the gross margin, now any particular point you would like to highlight I know that in September quarter there were some inventory losses but even after considering that there is a sharp improvement in the gross margin almost 260 BPS expansion is there, so can you highlight that and the second question is on the SMP so milk prices skimmed milk power prices have been coming down so can you indicate any fat losses that you must have incurred in this quarter?

M Sambasiva Rao: Coming to the first point you are right the realizations are same and procurement prices remain same like quarter two. The improvements have come in the commodity side. We have disposed significant volumes in the quarter two particularly coming from the Dairy Life volumes. Those markets are not there in this quarter significant butter, whitener, milk power were all sold in the quarter two that is why the revenue was higher. Now the consumer sales are happening therefore the margins have improved through the consumer sales. Coming to the fat losses we do not have abnormal losses in this quarter or in this nine month compared to the previous periods. Like in this specific quarter our losses due to fat products is around 4 Crores, which is in line with the previous year's similar period.

Aniruddha Doshi: So is it possible to quantify the amount?

M Sambasiva Rao: Amount of PAT losses?

Aniruddha Doshi: Yes.

M Sambasiva Rao: PAT losses for the nine months is around 14 Crores, which was almost equal in the 2016 nine months also first three quarters.

Aniruddha Doshi: Thank you.

Moderator: Thank you Sir. We have our next question from the line of Ashi Anand from Allegro Capital Advisors. Please go ahead.

Ashi Anand: The first question was with relation to milk procurement prices, you know in the last quarterly call you are indicated that you are seeing a fall in procurement prices on the back of decent monsoon and I was expecting that benefit actually come through in this particular quarter could you just kind of indicate where we have a milk procurement prices post last season and what is your outlook for Q4?

M Sambasiva Rao: Milk procurement prices trend if you wish to see December quarter of 2016-2017 cow milk price was at Rs.26.40 it went up to Rs.30 in quarter one, Rs.29 in quarter two and Rs.28 in quarter three, there is a kind of drop from quarter one to quarter three but not very significant in cow milk but coming to buffalo milk quarter three of 2017 financial year 2017 it was Rs.40.77 per liter, it went up to Rs.44 in Q1 of this year Rs.45 in Q2 and now it came down to Rs.41.64 it is Re.1 higher than the December quarter of last year, but significantly lower than the quarter one, quarter two these are price movement and as of now prices are more or less stable and quarter four may have similar price trend till March small exceptions here and there, there may be some movements up or down but broadly the prices remain stable in this quarter.

Ashi Anand: Sir that I just look at the presentation that you give us and on the metrics that seems to suggest to a 34.7 in Q1 this is I am assuming the blended cost 33.8 in Q2 and actually 33.9 in Q3 so on a Q-o-Q basis this is actually flat or marginally up and I was just to understand that?

M Sambasiva Rao: Yes that is why I gave you breakup of cow milk and buffalo milk. If you segregate and see the price movement of cow milk, buffalo milk it will be more clear with a certain markets in several states cow milk prices have not come down in northern states buffalo milk prices have come down our volumes come from different states one is the state wise prices are different, second is the mix of buffalo milk will be greater in the quarter three that also nullifies the gains from the other price drops. So therefore the average price remains same at quarter three and quarter two.

Ashi Anand: That is helpful. Secondly just wanted some kind of an outlook on the EBIT margins on the dairy business in Q4 given the fact that Reliance Dairy kind of losses should continue to come off and any potential increase for the gross margin expansion?

M Sambasiva Rao: Yes, we have to evaluate how the season changes and the price movement happens as of now it looks like stable whether any further movement in the coming weeks will determine the outcome. I would restrain from going beyond this stage.

Ashi Anand: If I could just ask one last question. For the X-AP Telangana Market I am talking of markets which are focus markets was like Maharashtra, Tamil Nadu, Delhi where we are looking at growing what really is a kind of growth outlook on those markets and what is the potential for value added products can we what kind of percentage of sales to be see coming in terms of value added products from those markets?

M Sambasiva Rao: Telangana, Andhra Pradesh our infrastructure has been recently improved. We have added almost 1 lakh liters per day capacity for curd manufacturing in the state, in both the states put together, we have also acquired a new plant near Hyderabad, which has about 1.5 lakh liters to 2 lakh liters capacity, infrastructure has been created and we are also looking at increasing our front-end infrastructure in terms of freezers and chillers in the market and expanding distribution network. We are gearing up for achieving at least 12% of milk growth and 30% of value added products growth in the coming year.

Ashi Anand: Sir this is Telangana, AP right sorry my question was on the X-Telangana, AP, if you are looking at the see Mumbai, Delhi or see in Tamil Nadu kind of markets, so the focus markets were outside Telangana and AP?

M Sambasiva Rao: Excluding these two you are asking?

Ashi Anand: Yes.

M Sambasiva Rao: X-Telangana AP I understood as combined state of AP. Now we call them two states earlier there also we used to see them as one state. X-Telangana Andhra there will give me a different perception. Yes, see these markets also we are looking at growing aggressively. This season was a surplus milk season in Maharashtra particularly. There were a lot of schemes and promotions are in the market once the market comes to normal hence our rate of growth should be much higher than the AP Telangana in this state particularly in terms of milk. Milk we look at the 20% growth but value added products in Maharashtra we do not have much production capacity at the moment during the next financial year we are going to construct our new client and add facilities for value added products. So one more year we have to wait for stepping up our growth in Maharashtra in terms of value added products. Currently we are outsourcing the products from Prabhat Dairy in Mumbai and supplying the market, limited effort we are making through that company, but our own facilities will come to step up the value added products, till then we will focus on the milk at least to achieve 20% rate of growth. In Tamil Nadu, yes we have infrastructure in the clients available there. We went through some bad patch in the last financial year nine quarters of this year due to certain pricing issues and also the local minister's statement saying all private brands are adulterated milk in Tamil Nadu except Aavin Milk. I am sure you must have read that. It went on and on for some time consumer confusion was created then finally High Court intervened and ask the minister not to speak about the private brands without any evidence and they try to create evidence through State Food Laboratory and thereafter National Food Laboratory both food laboratories have given at least it for the private brands which they are talking so we now go at certification that no private brand is assimilated and milk is safe and we are also starting a marketing campaign in Chennai this season to gear up or sales in that market.

Brahmani Nara: Brahmani here just to add to that we are also ramping up our facilities in other areas such as the plant that we have in Haryana, which is processing the Indian milk is being expanded to also make value added products so end of this financial year and sometime around March, April is when we expect that structure also to come up and there is another facility that we are in the process of acquiring in the Punjab market where we will not only be able to manufacture milk but also other value added products.

Ashi Anand: Thanks a lot. That was very helpful. Thanks so much for the detailed answer.

Moderator: Thank you Sir. We have next question from the line of Prashant Kutty from Sundaram Mutual Funds. Please go ahead.

Prashant Kutty: Thank you for the opportunity Sir. Sir one is you are speaking about the Dairy Life which was there, that there were some institutional the non-consumer products which have actually come up which has led to a relatively better margin numbers actually, is it a safe assumption to make that this non-institution which is kind of gone for good now and you will not be focusing that on an anymore or is it just a quarterly phenomenon?

M Sambasiva Rao: Yes as a company our focus was always B2C. Since inception and it will continue to be the same, but when we inherited this business through acquisitions we had certain higher volumes of milk coming and that sales were lower so there was a scenario where you have no choice but convert the milk into milk powder, whitener, butter, ghee etc., and sell. We are trying to rationalize our milk procurement in those areas to match the market requirement. It is still not balanced perfectly. We are trying to balance the demand and supply in those states because certain commitments are made to farmers and they were enlisted their suppliers and chilling capacities are created even now I would say about 20% surplus milk is there in those states, which we are trying to improve the demand and sell more so by coming summer most probably we will be able to balance out our demand supply in those areas once that is done, the post conversion of milk in the commodities will not be there and next financial year, we will come out of it totally and make it only B2C. This phenomenon will continue for another two months, three months, in this year.

Prashant Kutty: That is until this next quarter?

M Sambasiva Rao: No this quarter I think by March we should be out.

Prashant Kutty: Yes that is what this quarter the current quarter January to March quarter.

M Sambasiva Rao: Yes, next financial year, I do not see this kind of forced conversion of milk into commodities and selling but whatever little surplus we get in these markets we make powder and consume for our own internal requirements and butter we get a surplus will be converted into ghee or stable butter, cooking butter and sold in the consumer packs. That is the way forward and direction in which we are working.

Moderator: Thank you very much Sir. Sir we have lost the line of Mr. Kutty. We have our next question from the line of Dhruv Bhatia from AUM Advisors. Please go ahead.

Dhruv Bhatia: Sir could you just give a breakup of the Dairy Life revenue you mentioned 45 Crores was the revenue this quarter is it purely this milk or is it part of milk sold?

M Sambasiva Rao: Could you repeat there was as voice break?

Dhruv Bhatia: The 45 Crores of revenue of Dairy Life quarter what is the breakup of milk and value added products in this like milk and value added?

M Sambasiva Rao: Not much of value added products it may be where the 3, 4 Crores max I do not have exact number but it will be very insignificant it could be 3 or 4 Crores the rest will be milk.

Dhruv Bhatia: When you had acquired this company that kind of the turnover of this company was 500 Crores right.

M Sambasiva Rao: No, that was the year prior to the acquisition, two years prior to the acquisition the 500 Crores was I think 2014-2015 financial year that is what they projected and then next year they themselves have scaled it down to 300 Crores and we further scaled it down because of this bulk business, substantial volumes are coming from the sale of this bulk commodities in that so we approved in all that.

Dhruv Bhatia: How much is now HTFC business or bulk business on this 45 Crores?

M Sambasiva Rao: Bulk business may be about another 3 Crores.

Dhruv Bhatia: 3 Crores is bulk business, which will go away from the next quarter onwards.

M Sambasiva Rao: They may be there for another couple of quarters, 8 Crores is a bulk sale out of this 45 and 3 would be approximately the value added product.

Dhruv Bhatia: Sir how has been the experience because the procurement terms you have reduced the procurement from 2 lakh liters per day to 1.5 lakh liters so going forward also the reason I think the rational of buying Diary Life was also that you are getting procurement and a good brand so what is the thought process going forward?

M Sambasiva Rao: Rebuilding there were couple of issues in this Dairy Life business when we acquired we were aware of that all the infrastructure is outsourced they do not have any assets or like processing packing stations they were all outsourced. We are now trying to merge those volumes into our own existing clients and step up the capacities wherever we do not have adequate capacity we are expanding our plants or acquiring the plants. We will shift the volumes in to our clients first, that is where the growth kicks off. As long as it is done with the third party packing stations we do not have that consistency in quality and satisfaction of the customer so we are trying to meet the customer requirements by rationalizing the operations. Secondly certain chilling centers where the distances were very high they are all being closed by now we have closed 10 out of the 30 chilling centers we have got from then so these 20 centers are being streamlined and certain routes are being closed. In the last nine months the rationalization reorganization of the business has happened it is almost in the final stages. As Brahmani just now explained, we have started expanding our plant in Haryana near Delhi which would be ready by March so once this plant is commissioned, expansion works are completed entire packing operations will be shifted from third party plant to our own plant for Delhi and Haryana markets. We have also finalized the acquisition of Vaman Foods near Chandigarh in Punjab that plant will be available most probably by end of March to us that plant is currently being used by Amul as a third party packing station. Amul will be exiting this plant by end March. We will enter that plant. This will enable us to close another third party plant in Ludhiana, which Reliance was using and we got it, so entire Punjab, Haryana, Delhi market production and the control will shift to our own plants by March and these plants also have capacities to make value added products like paneer, buttermilk, curd so this will help us to ramp up B2C sales. In Rajasthan also we have another third party plant, which Reliance was using and we are continuing now. For the time being we will be using that plant and continuing the production till we acquire or setup a Greenfield plant for Rajasthan market. In Hyderabad also they were using a third party plant for packing. We recently acquired one plant near Hyderabad of Sham Motilal & Company and that plant is now being used for packing reliance brand Dairy Life so the shift is happening into our own packing stations where controls are perfect, so we would expect from April, May onwards the Dairy Life growth to take a better rate of growth.

Dhruv Bhatia: Sir would you say that it is going as per your plan the Dairy Life acquisition, the sales has been on track as we are exit or it is be much lower than what you had thought of is it been more difficult than what you are thought of?

M Sambasiva Rao: It is on track only there is no such issue and we were aware that certain volumes we have to drop like for example they were operating a plant near Nagpur for 4000 liters they are operating a plant in near Agra another Gwalior and Agra another 5000 liters there are a number of decentralized scattered operations for smaller volumes they were expensive so we went up – we know this have to happen and this is happen we have now withdrawn all those operations wherever not feasible we have closed and we have also rebranded certain areas.

Dhruv Bhatia: And you have been able to increase the shelf space on future retail outlets as well as on the Reliance outlets?

M Sambasiva Rao: Sorry can you repeat.

Dhruv Bhatia: Have you been able to increase the shelf space of both your brands on future retail as well as Reliance retail outlets?

M Sambasiva Rao: Both chains have given us access as we said earlier and our sales have really picked up may be at the end of the year next call I will be able to present the comparative picture after we got access to Reliance how much sale we have achieved through their outlets and also Future Group how much it is more than 100%, 200% kind of sales have been reported through these modern retail stores on both these chains in different markets, but a consolidated picture we will give you at the end of the year what kind of gains we got because of this access to these stores.

Dhruv Bhatia: Just one clarity, lastly is that you have mentioned that you will breakeven in Dairy Life are you talking about at EBITDA level or PBT level?

M Sambasiva Rao: EBITDA level.

Dhruv Bhatia: Thank you.

Moderator: Thank you Sir. We have next question from the line of Prashant Kutty from Sundaram Mutual Funds. Please go ahead.

Prashant Kutty: Apologies Sir my phone got disconnected. I am just sorry just on the last point, which you made, is it that what time are we looking for a breakeven of Dairy Life at EBTIDA level?

M Sambasiva Rao: Most probably in this quarter or next quarter at the best the Q1 of next year or Q4 of this year depends on the next couple of months this February, March in our pricing.

Prashant Kutty: So just as an extension to this if you really said that the large part of that commodity business since it is out the consumer business would technically let us say from FY2019 onwards or maybe whenever it exactly that is maybe a couple of quarters down the line that should be a similar margin like the Heritage milk business would that be a right estimate to make the 6% margin which typically make 5.5%, 6% margins you make in milk at EBIT level is that a right assumption to make for Dairy Life as well?

M Sambasiva Rao: It may take some more time, may not reach immediately because we have certain operational overheads, higher overheads and higher material cost, operational cost like for example milk movement cost is higher at the moment so we are further rationalizing and we are yet to start certain operations in our plant so it may take some more time maybe another year or so to achieve the standard margins what company is achieving in other areas.

Prashant Kutty: But it can definitely reach that level right I think the inherent margins can be our Heritage margins, which are there that is possible right, I am not while the time might take one year but it is definitely possible right?

M Sambasiva Rao: Possibly in all the areas but one thing you have to keep in mind even in the existing market in certain states it will go down in some seasons in certain states it will go up it is not that it is uniform across all the states we operate in sometime the local cooperative will increase procurement price and we will also have to increase and that period till they increase the sale price our margins will go down, the lag between the procurement price increase, sale price increase determined how we do that and there is no uniform pattern but our ambition and direction is that we should reach there.

Prashant Kutty: Fair point I agree. I understand the vagaries. I was just asking on a more blended basis typically or rather a more longer period of time I am just trying to kind of figure out that but I understand the quarterly vagaries is there actually. Sir the second question was in the value added part I believe that was one of the first comments which you made that there were some seasonal impact which kind of led to the value add products I mean mix in the value add products business. I just wanted to understand sir everywhere from your commentary we are gearing there is a lot of focus on milk increasing our milk procurement per se and per se there are consumer milk business which is there. Anything which you probably get to do from the value added perspective front probably to be from that particular part of the business it is somehow that while I understand the seasonal part, but somehow that seems to have is that a case there is a bit of a plateau in terms of growth rates or probably the growth rates are kind of come off anything which needs to be done little something out of the ordinary?

M Sambasiva Rao: First thing I am sure you would agree you were in Chennai right.

Prashant Kutty: I am not in Chennai Sir I was in Mumbai, but yes I do understand you speak about the monsoon yes I agree with them.

M Sambasiva Rao: The Chennai, Bengaluru, Hyderabad, Mumbai range of this year or unprecedented and spread over too many days too many weeks so that according to us that was a single factor that period we lost all the volumes, rest of the weeks post that scenario things has come back and this is the best quarter we look forward so let us see this quarter whether we have recover the trend of growth or not, we are looking for better performance in the coming summer.

Prashant Kutty: Do we need to probably go beyond that because somehow for us the curds will forms a large part of that non-value add part. I understand it is a very fast growing market for us but do you think any other couple of let us say product which will be probably target a little more aggressively here so that we are able to probably make it a little more broad base in that sense anything on that front which you are trying to do beyond curd.

M Sambasiva Rao: Maybe we will consult you after this call I have no nothing as of now.

Brahmani Nara: Just to add to that to I would disagree that we have saturated curd as a market because within existing markets of sales facing very good growth when it comes to a new market especially the northern part and the western part curd is still very unexplored by Heritage Foods so I think that is a huge opportunity for us when it comes to growth. Secondly coming to other existing value added products there are several things that we are doing in terms of representing the product to the consumer, be it flavored milk where we are coming up with a wider range, newer packaging type and a more exciting presentation longer shelf life presentation to the consumer or be it ghee where we are coming up with special variants of ghee catering to local markets or be it your value added product such as we are now investing into our first facility for long shelf life milk which has a huge market in certain parts of our existing markets so there is a lot of work going on within existing value added products and we are trying to create products that we are able to sell through the different channels that we have now it is door delivery or through our agents through Heritage parlors to modern retail format stores etc., so there is a lot of work going on when it comes to ice creams again as mentioned before this particular season we are looking at a complete revamp of our range of products so we are coming up with more exciting products and we have completely changed our packaging design, which is more exciting because we realize that we need to be targeting a newer set of consumers more of milliners or the youth as we say so there is a lot of work happening and I think it is also a function of marketing which you are seeing happening at a faster rate this particular year compared to any of the previous year for this distribution.

Prashant Kutty: Sure and are we looking at newer markets in ice creams as well are we just looking at the current we will become in the existing market?

Brahmani Nara: We have a processing facility in Hyderabad and we believe that we will be able to match the capacity. The current market will suffice for this season and once we are able to build our volumes in existing market we will certainly next year or the year after we will definitely look at our newer markets as which we recently entered.

Prashant Kutty: Many thanks and again apologies for the cut.

Moderator: Thank you Sir. We have next question from the line of Akshit Gandhi from Kotak Mutual Funds. Please go ahead.

Akshit Gandhi: Two questions from my side one is what has been our capex in the last nine months?

M Sambasiva Rao: 82.8 Crores close to 83 Crores in dairy and 16 Crores for renewable energy.

Akshit Gandhi: As we end this year we have planned certain acquisition from facilities and everything so what would be the overall capex for FY2018?

M Sambasiva Rao: Maybe another 25 Crores.

Akshit Gandhi: Okay great and any number you would like to mention for next year?

M Sambasiva Rao: Next four years earlier also we discussed every year we need to allocate close to 110, 120 Crores to create infrastructure for accelerating the rate of growth.

Akshit Gandhi: Great and one last thing from my side if I could as on the December end whatever the debtors inventory and creditors?

Umakanta Barik: Good afternoon Sir and so the inventory as on December 31, this inventory days is 18 day trade receivable 2 days the return, trade payables 10 days working capital cycle is 10 days.

Akshit Gandhi: Sir just one question and this is there our working capital has been our biggest strength as we see over several years as we change our mix in favor of value added products where we will have ice creams and other than buttermilk and curd will the working capital change significantly?

Umakanta Barik: No because the contribution from value added products mainly from curd only, curd and buttermilk and all those things so this is similar the working capital cycle for these two value added products are also similar to the milk.

M Sambasiva Rao: Ice cream will not be able to twist to the requirement with them a significantly not a bigger volume therefore it should not impact much.

Akshit Gandhi: Should I understand that this 223 Crores of debt, which we have that would be the peak debt on our books because our capex requirement would be met easily out of our operating cash flows?

M Sambasiva Rao: You are saying total debt level currently is about 220 Crores in short and long-term will it be the peak kind of requirement is the question. Yes it is more or less peak.

Umakanta Barik: This quarter actually we have utilized more working capital for stocking skimmed milk powder is the actually when the prices were low actually we buy for the next year up to September whatever the requirement for captive consumption that is the reason this for otherwise our regular working capital is only 50, 53 Crores.

Brahmani Nara: Yes, and the way I would look at it is probably more an efficiency parameters it is debt equity, which is about 0.16 lower than last year in fact and we plan to manage around that we expect that we will be as attrition.

Akshit Gandhi: Thank you so much for all the answers. Thank you.

Moderator: Thank you Sir. We have a next question from the line of Darshan Parekh from Anand Rathi. Please go ahead.

Darshan Parekh: Sir in last concall you mentioned 40 million revenue contribution for value added products by 522 would you expect the same now?

M Sambasiva Rao: As of now we are around 23%, 24% per annum for the full year. We will be restoring this in the quarter four though as of now it looks little lower for the year so every year 3% to 4% is incremental increase we are looking at so it should be able to reach 40% by that time.

Darshan Parekh: What is the growth rate you mentioned in Dairy and value added?

M Sambasiva Rao: Value added should be around 30%.

Darshan Parekh: And dairy?

M Sambasiva Rao: And.

Darshan Parekh: And dairy, dairy segment?

M Sambasiva Rao: What do you mean by milk?

Darshan Parekh: Milk.

M Sambasiva Rao: You mean milk?

Darshan Parekh: Yes.

M Sambasiva Rao: Milk will be around 15%, 16%.

Darshan Parekh: That is it from my side.

Moderator: Thank you Sir. We have a next question from the line of Ashish Mehta from Motilal and Oswal Securities. Please go ahead. Thank you. We have a next question from the line of Ronak Jain from Vibrant Securities. Please go ahead.

Ronak Jain: Sir my question is basically on the procurement side so you mentioned that the procurement cost of the buffalo milk was around Rs.41 per liter so I was reading an article and it stated that Amul provide the farmer at Rs.49 per liter so as we are moving towards the northern side so do you actually see it as a risk that the cooperatives might be paying more to the farmers and might be taking away our share basically we need to increase our prices and bring it in power with the cooperatives?

M Sambasiva Rao: See in any state for that matter nobody can get milk if you pay less than cooperatives and we have been every private company is paying equal to cooperative in that state. So in Amul market we pay price equal to Amul, in Nandini market we pay equal to Nandini wherever we are otherwise farmer has no reason to give milk to anybody else other than cooperative. The price is almost equal by all companies all over the country within the local market, they benchmark with the local cooperative and pay it. What we offer to farmer to come to heritage is beyond the price. Price is more on the same there are number of other supports and value propositions we offer to farmer like punctual payment, assuring the marketing of their 100% product, fair and transparent way of valuing their milk at the collection center, offering certain inputs extension activities like credit arrangement with the banks, seed supply at good quality at reasonable price or with subsidy, insurance for their animals, insurance for the farmers from the accidents etc., then the welfare activities including veterinary care at doorstep we have a huge veterinary network, artificial insemination facility, disease control facility, supply of veterinary medicines on cost price we have a huge range of input extension activities, which we use to retain the farmers with us but there is no way one can pay less price and still get milk.

Ronak Jain: Basically your price would be decided by whatever the cooperatives are paying so that will be the benchmark?

M Sambasiva Rao: Absolutely. So they are the market leaders in every market and they are there for last seven decades, six decades the people have associations with them and no one can say I will pay less than supply milk to me in this country.

Ronak Jain: So do you by any change feel that in the areas that are like Punjab, Haryana and Delhi so the areas in the north part that you are now concentrating so the cooperatives are little less there. So like because only I suppose the Mother Dairy, and maybe Sara's maybe that is the cooperatives that are present and they do not have?

M Sambasiva Rao: No each state each state has its own brand like Punjab has Verka, Haryana has Vita, Delhi has Mother Amul, Rajasthan has Saras Amul so every state has a cooperative brand and top of it Amul is there from Gujarat occupying other states. So there is no state without a cooperative there.

Ronak Jain: Okay and they are dominant there we need to take the market share from them?

M Sambasiva Rao: No we may not take share from them we may be participating in capturing the incremental increase in the market share.

Ronak Jain: Thanks a lot. That is it from my side.

Moderator: Thank you Sir. We have our next question from the line of Dhruv Bhatia from AUM Advisors. Please go ahead.

Dhruv Bhatia: Could you just on the medium-term would it be fair to say that the EBITDA margins in your dairy business could go back to 8%, 8.5%?

M Sambasiva Rao: It is a function of three, four external factors. One is the monsoon condition whether weather is good, milk production is good and prices are stable. Second is foreign trade policy of Government of India whether they are giving incentive for exports or they are banning exports, they are bringing duty free or with duty milk products in the country. This policy keeps fluctuating and the third is a global prices of milk powder, butter whether Chinese economy has recovered or it is still lagging, whether European production is surplus or deficit, how is the weather in New Zealand these are all decide the global prices though we are not a significant player in the global market those prices have impact on the domestic market so these are all the factors, which will certain years help in building margins certain years do not help. So we just have to wait and see how the year plays by as these factors are beyond anybody's control?

Dhruv Bhatia: But at least so for the next year because of you talking about breaking even in the Dairy Life business here can we see again at lest the 6.5%, 7% EBITDA margin since that will turn positive than your existing business is doing fairly well.

M Sambasiva Rao: Yes that is possible we are working for that but whether you get 8.5%, 9% is a function of several external factors that is what I was trying to explain.

Dhruv Bhatia: Sir and what type of a volume growth or the procurement growth can we see for FY2019?

M Sambasiva Rao: We are yet to finalize FY2019 maybe later the call I can explain.

Dhruv Bhatia: With the procurement from Dairy Life of 1.5 lakh liters per day be the bottom or would you probably see it go further lower than this number?

M Sambasiva Rao: It depends on the demand build up. We are trying to build demand in those markets so if we can absorb and start selling expand our think we will continue to maintain the volume and increase and most probably we will continue to maintain same volume and increase our strategy is not to decrease further. We have to match the sales demand that side.

Dhruv Bhatia: Lastly Sir any update on the facility with the JV partner you are going to put in Maharashtra for yogurts?

M Sambasiva Rao: Yes it is still taking shape on the drawing board only we yet to get onto the ground. Most probably in the first quarter, we will start the works on the ground and complete it let us say seven, eight months' time. We got a bit diverted from this recently with the offer of some client sales for the similar product so we slowed down hoping that product that client will come to us we are yet to finalize that part of it. So we consciously slowed it down by for last couple of months.

Dhruv Bhatia: So you are trying to say that you are going to trying to buyout someone else's machinery or plant rather than buying fresh equipment?

M Sambasiva Rao: It was not our initial plan, initial plan was go for the new plant, recently there was an offer from some company which is interested to partly their client so we try to delay our plant thinking that would come through that is still pending therefore we are not yet firm on commencing our plant work readily. So we are just delaying by a month or so we will be able to conclude by end of February whether we acquire some existing client or we go for a Greenfield as we originally planned. This got a bit delayed because of the new opportunity that came in our way.

Dhruv Bhatia: Thank you.

Moderator: Thank you Sir. We have a next question from the line of Kunal Pawaskar from Indgrowth Capital. Please go ahead.

Kunal Pawaskar: A question on if you can quantify the amount of SMP in tonnes that is produced by the company and how much of that it gets used captively if at all?

M Sambasiva Rao: As of now current year nine months we produce close to 2000 tonnes of SMP with our own milk and our consumption would demand more than that so we will consume 100% internally and we would be buying also from market to meet our internal requirements.

Kunal Pawaskar: Just to add to that in the liquid milk portion and the curds particularly how much percentage within each of them would be using SMP and liquid milks in reconstituted form if at all that happens?

M Sambasiva Rao: This I would be able to answer later I do not have ready numbers with me.

Kunal Pawaskar: That is all from my side. Thank you.

Moderator: Thank you Sir. We have next question from the line of Kuldeep Gangwar from ASK Investments. Please go ahead.

Kuldeep Gangwar: Just couple of things like first medium-term you are saying close to 20% revenue growth is it the right understanding like 15%, 16% in milk and 30% CAGR in the value added product?

M Sambasiva Rao: Yes it will be a bit more than that we have to reach around 25% rate to achieve our created ambition depending on the year-on-year seasonal condition there will be plus or minus but we are targeting around 25%.

Kuldeep Gangwar: For next four, five years is it right.

M Sambasiva Rao: Yes five years.

Kuldeep Gangwar: And margin obviously you said like 6.5%, 7% is doable and beyond that will depend on like you highlighted earlier?

M Sambasiva Rao: Yes I think you got it right.

Kuldeep Gangwar: And the second bit like then your P&L in consolidated there is a fair value gain on FB, TPL, equity shares and then there is an opposite entry on the expenses side so if the future realistic that you are caring so it is being hedged or something like how it is working out.

M Sambasiva Rao: Yes I request CFO to explain this. Can you just repeat the last bit question?

Kuldeep Gangwar: Like consolidated P&L statement if the entry like fair value gain on FB, TPL, equity securities and then corresponding expense entries loss due to the change in the fair value of derivative liabilities. So more or less same number but coming at one place and offsetting entries over there so why it is happening?

A. Prabhakara Naidu: See as per the composite scheme between HSL and HFRL and FRL last year on March 31, we have got actually 17847420 shares from FRL as per the composite scheme of equity share, so Heritage has the second phase of implementing Ind-AS that is IFRS Indian IFRS so in this period actually then till September we have been finalizing actually the way of taken certain options as per the Ind-AS available exemptions and all accounting policies are being finalized because our reporting period for Ind-AS first reporting period is March 31, 2018 till then some accounting policies are being finalized so earlier till September what the preliminary exemption selection of accounting policies as per that whatever the fair value change in this one plus 78 lakh shares in the market quarter-to-quarter we have chosen to route it through OCI, other comprehensive income. Sir now we are finalizing the accounting policy with respect to the investments in future retail share so as per the composite scheme there is an implementation agreement is there whenever we sell the share so there is an obligation to buy 1000 shares to upside sharing to the future retails. So till September actually whatever the paid value gain we have routed through OCI which is an option available to us now after finalizing the accounting policy so whatever obligation to buy those 1000 shares it becomes a derivative liability any change in derivative liability there is no option to route it through OCI it has to be routed through P&L only so equal to that amount actually the paid value change in 1.78 Crores share should also be routed through P&L that is the reason it is offsetting against expenditure versus income so this is the policy, which has been finalized. In the balance sheet side till September we have shown the net effect for financial asset paid value of those financial assets in equity shares of FRL. Now the derivative liability shown on the liability side and gross fair value of the 1.78

Crores shares is to be shown under asset side network does not change with this accounting policy so this is only presentation issue Sir. So now the accounting policy, which gives respect, actually has been finalizing and shown accordingly.

Kuldeep Gangwar: Yes I ask because like if I look September quarters are they were exactly matching numbers over there in December quarter.

A. Prabhakara Naidu: Yes, yes so in the first quarter there is an increase of because of this for out of 1.78 Crores shares is 1.33 Crores shares fair value change is routed through P&L remaining 44 lakh shares paid value change is routed through OCI, with this policy because the as per the accounting standard financial instruments, instrument-by-instrument we can actually take the policy.

Kuldeep Gangwar: And lastly is there any lock in like after which you can sell these shares in the market or something like that three-year lock in?

A. Prabhakara Naidu: Yes three year lock in.

Kuldeep Gangwar: From which date.

A. Prabhakara Naidu: From the date of allotment.

Kuldeep Gangwar: So what for that say 2017 or like.

M Sambasiva Rao: Yes mid 2017, 2020 we get out of lock in by mid 2020.

Kuldeep Gangwar: Okay so after that you can sell in the market you are saying. Okay sure, thanks.

Moderator: Thank you Sir. We have next question from the line of Shailesh Kumar from Sunidhi Securities & Finance Limited. Please go ahead.

Shailesh Kumar: The last housekeeping question after that we will close the call. What has been our EBITDA margin in liquid milk, value added and fact during Q3 and nine months FY2018?

Brahmani Nara: Liquid milk was 6.24% and value added products was 13.4%.

Shailesh Kumar: And for nine months?

M Sambasiva Rao: 7.93 milk and 14.7 for nine months.

A. Prabhakara Naidu: Nine months actually milk is 4.25% anyhow the profitability is low and value add product is 12.86%.

Shailesh Kumar: 12.86% and fat.

A. Prabhakara Naidu: Fat loss for nine months 5.01% and for current quarter 3.43%.

Shailesh Kumar: Great, I think thanks the management team of the Heritage Foods Limited thanks for our valuable time. i believe our investors have really benefited from it I looking forwarded to hear you on the next quarter. Thank you very much gentlemen.

Moderator: Thank you very much Sir. Ladies and gentlemen on behalf of Sunidhi Securities & Finance Limited that concludes this conference call. Thank you for joining us. You may now disconnect your lines.