



“Zydus Wellness Limited Q3 FY18 Post-Results
Conference Call”

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Moderator: Ladies and gentlemen, good day and welcome to the Zydus Wellness Limited Q3 FY18 Post Results Conference Call. As a reminder, all participant lines will be in the listen-only mode and there will be an opportunity for you to ask questions after the presentation concludes. 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 would now like to hand the conference over to Mr. Tarun Arora - COO and Whole-Time Director, Zydus Wellness Limited. Thank you and over to you, sir.

Tarun Arora: Good evening and welcome to the Post Result Teleconference of Zydus Wellness Limited for quarter 3 financial year 2017-2018. We have with us Dr. Sharvil Patel – Chairman, Mr. Ganesh Nayak – Director, Mr. Amit Jain – our outgoing CFO, Mr. Tushar Shroff – Senior Vice President (Corporate Finance), and Mr. Vishal Gor – Vice President (Corporate Finance) with Cadila Healthcare. We welcome our new CFO - Umesh Parikh. He is aged 50 years. He is a qualified Cost and Management Accountant and a Company Secretary. He has also done an Advanced Business Leadership program from IIM, Ahmedabad. He is a qualified Six Sigma Green Belt prior to joining Zydus Wellness Limited. He was working as Vice President Finance in Company Secretary at Zydus Hospira Oncology Private Limited. He carries a rich experience of 29 years in the area of finance. At this juncture I would also like to thank Mr. Amit Jain for his contribution in building the business and wish him well for his future endeavors.

The quarter gone by saw a good improvement in the growth rates led by our Everyuth and Nutralite brands. As a result, we have witnessed a strong performance of the company with the double-digit revenue growth during the third quarter of financial year 2017-2018. Our net sales on GST adjusted basis have increased by 20.4% for the quarter. Reported revenue from operations grew by 18.4% for quarter 3 financial year 2017-2018, which is not comparable with quarter 3 financial year 2016-2017 due to implementation of GST. The government reduced the GST rates of various categories in the month of November 2017 commensurate price reductions were passed on to the consumer with immediate effect. During the quarter gone by, our key brands namely Sugar Free, Everyuth scrub, and Everyuth peel off have maintained leadership positions in their respective categories.

Coming to the consolidated financial performance of quarter 3 financial year 2017-2018, our total income from operations has increased by 22.5% year-on-year to Rs. 1,324 million on a GST adjusted basis. Our reported gross margin as a percentage of net sales and income from operations stood at 67.7% for the quarter. Our earnings before interest, depreciation, and tax has gone up by 49.2% year-on-year to Rs. 332 million as a result EBITDA margin as a percentage of total income from operations increased by 520 basis points and stood at 25.1%. Profit before tax was up by 38% to Rs. 392.6 million. Net profit was up by 43.8% to Rs. 361.6 million.

With that, let me share some of the highlights of operations for the quarter gone by. On the Sugar Free front, during the quarter we continued our focus on strengthening consumer

connect and building awareness through an association with movie Chef in which we brought together renowned actor Saif Ali Khan and Sanjeev Kapoor to create a co-branded TVC supported by print campaign and 3 digital recipes vignettes. To further drive the growth of Sugar Free Green we continued with TV campaign support, outlets expansion program and sampling. Going forward, our focus would remain to expand sugar free franchise through various initiatives like new product launches and investing behind category building. On the Everyuth front, during the quarter, we have witnessed strong growth rates across all segments of Everyuth. We continued to support our Neem Papaya scrub through TV campaign during the quarter. Going forward we would be rolling out our new campaign on Golden Glow Peel Off and we have some exciting new launches plan to expand the Everyuth franchise.

On the Nutralite front, Nutralite has witnessed another strong quarter with a good volume growth across both institutional as well as the retail segment. We have continued to use digital media and retail visibility to build awareness about Nutralite and drive engagement. We are already in the process of rolling out our Mayonnaise in the retail segment and have more launches plan in the next financial year. As per MAT December 2017 report of Nielsen, the sugar substitute category has grown by 13.2%, Sugar Free has maintained its number one position with the market share of 94.4%. The scrub category has grown by 9.9%, Everyuth scrub has maintained its number one position with the market share of 33%, which is an increase of 150 basis points over the same period last year. The peel off mask has grown by 17.9% at a category level. Everyuth peel off mask has maintained its number one position with the market share of 86.5%. Going forward, we would increase the pace of our new product launches and continue to invest behind our brands which will help us to improve our growth rates.

Thank you and we will now start the Q&A session, over to the coordinator for the Q&A.

Moderator: Thank you very much, sir. Ladies and gentlemen, we will now begin with the question and answer session. We take the first question from the line of Tejas Shah from Spark Capital. Please go ahead.

Tejas Shah: First question pertains to Sugar Free, you mentioned that the category grew by 13% and market share was 94.4 just to help us with the number what was this number previous quarter, the market share?

Tarun Arora: 93.8%, last quarter MAT.

Tejas Shah: And sir, visibly very strong set of numbers on revenue line item. So is it right way of understanding that this is a reflection of retail level offtake as well or is this finally the benefit of distribution rejig that we did for a very long period. It is starting to reflect in terms of primary distribution or primary expansion in numbers.

Tarun Arora: So, I do not think it is about just one thing. I think there are several set of activities which we have done over last few quarters are coming together which includes the distribution which

you rightly said but also a lot of work around innovations and brand supports that you have done. So, all coming together has helped us. It also helps that, if you want to give you a sense we are seeing a good movement from last quarter at sequential level also.

Tejas Shah: And sir, what will be the distribution touch point numbers?

Tarun Arora: That would be in the order of some 8.2 or 8.3 lakh outlets at a business level.

Tejas Shah: What proportion this will be OTC and direct to reach?

Tarun Arora: So, we do not share that direct reach numbers but we clearly expanding our base on that direct distribution and it is not about just a numbers but also quality of distribution where we are able to sell through more products within the same stores that we covering. So, quality of distribution also along with the numbers.

Tejas Shah: And sir, just one last on the growth part, would you qualify any factor in this quarter number apart from the base as one-off in terms of because as you rightly pointed out sequentially also we have made a progress, and this is if I recall correctly this is the highest absolute number on quarterly basis ever in history of the company. So, anything would you like to call up as one of this should be taken as sustainable growth momentum in company's trajectory?

Tarun Arora: I think this is an outcome of our sustainable momentum that we see. In the numbers will, I mean the growth will vary because of the basis but we have seen a positive momentum at the brand across all brands.

Tejas Shah: And sir, just one question on margins and I will come back in the queue. What reason you will attribute to Q-o-Q gross margin contractions?

Tarun Arora: Q-o-Q it is mainly because of the increase in the custom duty rates which government did it in the month of November and August on the palm oil.

Tejas Shah: So, there was a duty increase before budget as well is it?

Tarun Arora: Yes, it was two trenches, so on palm oil the duty got increase first in August and then in November.

Tejas Shah: And the one which was done in budget is that an additional one?

Tarun Arora: That is on other type of oil. So, it is on palm kernel oil, soya oil and those type of oil, what I talked about was palm oil.

Tejas Shah: And have we taken price increase to mitigate the same?

Tarun Arora: No, we have not right now.

- Moderator:** Thank you. We take the next question from the line of Kaustubh Pawaskar from Sharekhan. Please go ahead.
- Kaustubh Pawaskar:** Sir my question pertains to Nutralite, for past few quarters we have been seeing that Nutralite performance is encouraging and even in this quarter you mention that the growth has been in double digits. So, what exactly is driving the growth, is it because of the, suddenly what has happened like the product is getting recognition in the market or have you implemented some different strategy so that the product can be tested in the market?
- Tarun Arora:** So, it is a mix of all the things like you said. We have a better enhanced distribution which we have driven as well as new launches like we mentioned on the flavors. So, everything gets coming together that is really helping.
- Kaustubh Pawaskar:** And what could be the margarine category growth as a whole has it, is it improved over the period of time for example for last 4-5 years what was it and now. what would be the growth for margarine?
- Tarun Arora:** There is no quality syndicated data that we could refer to. So, really can't comment in beyond a point we would try to do with Nielsen but not got any substance success on that. So, really cannot say at a category level.
- Kaustubh Pawaskar:** And sir, pharmacist is one of the key distribution channel for you and in the past, you mentioned that it was impacted because of the demon and the GST regime but now how are things at pharmacist level? Last quarter you mentioned that almost 90% of their business is been recovered. So, now we should expect it to be 100% or things or still there are some, it is yet to recover?
- Tarun Arora:** So, we have seen a good improvement at the pharmacy channel. Wholesale is some piece which is done better now, and we hope that it fully recovers the unorganized wholesale and the moving wholesalers. Some of those pieces have got contracted in the structural shifts rest of the pieces are coming largely back to normal.
- Kaustubh Pawaskar:** And sir one last on the advertisement spend this year we have seen substantial increase in the advertisement spends. So, this is something which will continue, or this is the only year where we are saying more of the advertisements spends and going ahead limit yourself to certain budget?
- Tarun Arora:** So, I think you should look at advertising spends more at YTD or year level where we are maintaining a similar kind of percentages. We will back initiatives and launches which are very important to us and bring them to a certain level wherever if the investments has required but I will not see any significant shift at annual levels yet.
- Moderator:** Thank you. We take the next question from the line of Meet Jain from Prithvi Finmart. Please go ahead.

- Meet Jain:** I want to ask that as of product basket is very small like a few brands like Sugar Free, Nutralite are you planning on expanding to some other products as well?
- Tarun Arora:** Yes, we have innovations like I mentioned is important part of our strategy and we will be expanding. It need not be a through a new brand but same brands can carry a much wider portfolio.
- Meet Jain:** Basically, in which particular brand like Everyuth brand as you mentioned above?
- Tarun Arora:** All three have opportunity.
- Meet Jain:** Second question means can you provide us a revenue break up of each brands?
- Tarun Arora:** No, we are not sharing.
- Moderator:** Thank you. We take the next question from the line of Ankit Kanodia from Smart Singh Services. Please go ahead.
- Ankit Kanodia:** I have just couple of questions. First of all in Nutralite can you give us a break up or some idea into how much is the institutional cess and how much is retail?
- Tarun Arora:** So, approximately 70 in favor of institutional cess, 70%.
- Ankit Kanodia:** So, why is the retail contribution is low still low, any idea or any reason specific reason you would like to give it?
- Tarun Arora:** I think details we can discuss it later, but this is being a historical we are focusing a lot more on driving retail business.
- Ankit Kanodia:** And the second question is in the last concall you mentioned about that your international operations are picking up well, but it is still not so significant. So, can you give us a color as in a year from now may be in FY19 what percentage of revenues, ballpark percentage will be our international operations?
- Tarun Arora:** So, we are working towards the 10% organically growing the international business, so in next 3 years to 4 years.
- Moderator:** Thank you. We take the next question from the line of Tejas Shah from Spark Capital. Please go ahead.
- Tejas Shah:** Sir, if I looked at your employee cost line item there has remained healthy double-digit growth for last many quarters and in fact I compare it with 3Q FY16 then it is 40% up. So, is it the existing base is experiencing that kind of inflation or we are adding more headcounts and if we are in which division this addition happening?

- Tarun Arora:** So, it is largely normal. We have not added any significant headcounts over a period of time. The replacement cost in the man power is much higher than what it is, so that is largely what is driving.
- Tejas Shah:** Is that we have to stay this run rate, or you are seeing some?
- Tarun Arora:** No, this is not a sustainable rate. So, if you look at it, I think it is not a very sustainable.
- Management:** We do not see significant expansion in the coming year.
- Tejas Shah:** The second, if you can help us with some qualitative commentary, what proportion of our A&P spend will be going on in commercial activities and how it has moved on Y-o-Y or trend bank basis?
- Tarun Arora:** So, sorry we do not get it between commercial activities as in?
- Tejas Shah:** No, sir I said A&P, advertisement and promotional spend, what proportion of that is going into promotional spend and how it has moved on Y-o-Y basis?
- Tarun Arora:** So our discounting and promotions are very small proportion of our investments. Our more investments go behind brand building and visibility and other kind of engagement activities and which is what we keep talking about. Over a period of time we are not increasing that number as a percentage which usually going down.
- Tejas Shah:** And sir, if you can help us with some quantitative commentary on how is Sugar Free Green going and what is the feedback from at consumer level or dealer level?
- Tarun Arora:** We have seen very good traction on the Sugar Free Green and we are quite optimistic on the prospectus of Sugar Free Green. It will help us build Sugar Free franchise at overall level much faster and that is why we have backing it and even in my speech also mention the same thing.
- Tejas Shah:** Are we recruiting new consumer in the category through Green or as it just the existing users are shifting to Green as a much more organic or herbal platform?
- Tarun Arora:** We are largely seeing new set of consumers coming through.
- Moderator:** Thank you. We take the next question from the line of Meet Jain from Prithvi Finmart. Please go ahead.
- Meet Jain:** One more question, what is our advertising budget for going forward or branding budget if you any allocated anything?
- Tarun Arora:** So, we have maintained a similar level of spends. We do not share those forward-looking specifics.

- Moderator:** Thank you. We take the next question from the line of Monica Joshi from Hornbill Capital. Please go ahead.
- Monica Joshi:** I know you do not share numbers on a segment basis, but it would be great if you could share some volume growth as a ballpark, not as the exact number specially on a sequential basis because I think what more heartening for us to see is the sequential growth in your business. If you could just give some indication on how volumes in each of your categories or if you want to give the whole company has grown on a Q-o-Q basis?
- Tarun Arora:** Largely our growth is volume-led because there is no any specific price increases. I think we have fairly excited about Everyuth doing across all segments doing very well but all brands have done.
- Monica Joshi:** You would like to call out any particular one? So you said Everyuth has definitely done better.
- Tarun Arora:** It is Everyuth which we have more excited about because that small parts have done fairly well and building up clients.
- Monica Joshi:** The second question I have on the raw material side, so you mentioned that there was an increase in import duty in palm oil. What are your key components here, I mean if I look at the 3 or even the 2 basis segments of Sugar Free and Nutralite what are the line items we should look at, when we track raw material cost and any particular item that you would like to call out where you are seeing pricing really change either upwards or downwards?
- Tarun Arora:** Monica can we have the detail chat on this offline?
- Monica Joshi:** Sure, I will do that. Just one question I think it was asked by the previous participant. I understand that you do not give a forward-looking statement on advertising. How do you track it? I mean do you expect to increase your percentage in sales as you go along, maintain it, I mean what should we look for?
- Tarun Arora:** So, we clearly back advertising based on initiatives. So, all the new products we ensure we have substantial backing for it and because we have existing strong brands we are able to manage it at a portfolio levels, so we lead by the flagship initiatives and that is how we are managing as a portfolio. Some percentage may go up for a short period of time but as the response is good I think we will be able to come back to a similar level of percentage over a period of time.
- Participant:** So, a similar level would be about 16% to 17% of sales is that something we should look at?
- Tarun Arora:** Take close to 18% to 20%.
- Participant:** 18% to 20% on an annual level?

- Tarun Arora:** Yes.
- Moderator:** Thank you. We take the next question from the line of Ashwin Reddy from Samatva Investments. Please go ahead.
- Ashwin Reddy:** So, I have a few questions around the Sugar Free brand. So first, between Sugar Free and Sugar Free Green can you talk about the split between the retail and institutional broadly just to give us the picture about where Sugar Free Green is versus Sugar Free and how should we expected to pan out?
- Tarun Arora:** So, there is hardly any institutional business in Sugar Free we do sell HoReCa which is important, and we are driving it more from a visibility and consumption behavior point of view but as a percentage of businesses it is very small. So, we should not be worrying about that. Sugar Free Green is, I mean Nielsen has reported in last couple of quarters close to 1.6%-1.7% market share. So, if that is any indicator for you to look at.
- Ashwin Reddy:** And for the overall market, I mean any point us on what would make the category itself grow faster because all the macro indicators looks good but the market size still looks pretty small compared to the opportunities which is out there. In your opinion what would be the top two-three things that should change or that could change over a long period of time it can be medium or long-term that would help the category itself grow faster?
- Tarun Arora:** So, I think for what we know and understand, I think with we are doing those 2 or 3 things one is bring in products which the consumers will give the reassurance of it is safer and better and that is what Sugar Free Green should help us. We are communicating to consumers on the benefits of Sugar Free being a healthier proposition and we are backing it with our distribution support. So, innovations and brand building and distribution I think simply put that could be the answer for that.
- Ashwin Reddy:** And finally, in your strategic thought process what is being the biggest change in the last couple of years around the Sugar Free category and what is that one big delta which has happen which was kind of a wow moment or something which change for you guys?
- Tarun Arora:** So, we have been building around the things that we talked about and now this work with the better consumer understanding has responded well. If you want a little bit more details, then it may be better to do a separate conversation.
- Moderator:** Thank you. We take the next question from the line of Chirag Lodaya from Value Quest. Please go ahead.
- Chirag Lodaya:** I have couple of question. First on, if you can just tell us what are the new products under pipeline and the timeline?

- Tarun Arora:** So, we can share only what we are launching right now which is Mayonnaise under Nutralite brand now. But forward-looking, I think we will share when we are at that launch stage.
- Chirag Lodaya:** When is this launch expected?
- Tarun Arora:** At least 3 to 4 quarters we have enough products for each of the quarter launches.
- Chirag Lodaya:** This Mayonnaise launch will be in which quarter?
- Tarun Arora:** We are launching at this quarter, current quarter that we are running.
- Chirag Lodaya:** And secondly if you can just throw growth rates across the segment for first 9 months some ballpark growth rate number that would be helpful?
- Tarun Arora:** Do not share those numbers.
- Moderator:** Thank you. Next question is from the line of Aditya Joshi from Anand Rathi. Please go ahead.
- Aditya Joshi:** Sir, my question is pertaining to Sugar Free brand especially the Sugar Free Green brand. Sir, have we reached the total number of outlets what Sugar Free Gold and Sugar Free Natura on account of Sugar Free Green?
- Tarun Arora:** No, we have not reached the same level. It is still some distance away innovations take a much longer time.
- Aditya Joshi:** Sir, I was talking about the distribution, the number of retail outlets that we reach on when it comes to Sugar Free Gold or Natura. Has Sugar Free Green reached same number of outlets?
- Tarun Arora:** No, we have not reached.
- Aditya Joshi:** Sir, how many quarters more will we take to reach the same number of outlet?
- Management:** Will take time, new brands take longer time too, so we do not have those numbers.
- Moderator:** Thank you. Ladies and gentlemen, as there are no further questions from the participants I would now like to hand the conference over to Mr. Tarun Arora for closing comments.
- Tarun Arora:** Thank you everyone and see you next quarter.
- Moderator:** Thank you very much, sir. Ladies and gentlemen, on behalf of Zydus Wellness Limited, that concludes this conference. Thank you for joining us and you may now disconnect your lines.