



“Zydus Wellness Limited Q4 FY-16 Post Results
Conference Call”

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MR. AMIT JAIN – CFO, ZYDUS WELLNESS LIMITED
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Moderator: Ladies and gentlemen good day and welcome to the Zydus Wellness Limited Q4 FY16 post results Conference Call. As a reminder, all participant lines will be in the listen-only mode. There will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference, please signal an operator by pressing ‘*’ and then ‘0’ on your touchtone telephone. Please note that this conference is being recorded. I now hand over the conference to Mr. Tarun Arora – COO and whole time Director of Zydus Wellness Limited. Thank you and over to you Mr. Arora.

Tarun Arora: Good afternoon and welcome to the post results teleconference of Zydus Wellness Limited for financial year 2015-16. We have with us Dr. Sharvil Patel- Chairman, Dr. Ganesh Nayak – Director, Mr. Amit Jain- CFO, Mr. Nitin Parekh – CFO of the Zydus Group and Mr. Vishal Gor – Head of Investor Relations at Cadila Healthcare Limited.

The focus for the year was to revive growth rates on the back of volume led initiatives. As the year progressed, we have an improvement in the growth rates of Sugar Free and turnaround in the peel-off business of Everyuth. We have seen steady improvements in the profit margins as well. We saw stabilization of our revamp distribution in the later part of the year gone by. The attrition in the field has stabilized during the year. We have also strengthened the sales leadership team with additional talents. We rolled out distribution expansion program named as ‘Enrich’ which has resulted in 20% growth in direct coverage.

During the year gone by, our key brands namely Sugar Free, Everyuth scrub, Everyuth peel-off and Nutralite have maintained leadership positions in their respective categories. Coming to the financial highlights, during the year gone by, on a consolidated basis our gross sales were up by 3.2% year on year to Rs. 4570 million, however the growth after excluding the impact of price reduction in Nutralite and discontinued products was 4.5%. Our total income from operations on a like to like basis has gone up by 3.4% year on year to Rs. 4295 million. The income from operations of the previous financial year ended 31st March 2015 included Rs. 155 million related to additional excise duty credit received by Zydus Wellness Sikkim, our partnership firm for the years 2011-12 to 2013-14 pursuant to the order passed by the office of the Commissioner of Customs, Central Excise and Service Tax for the fixation of special rates of the Excise duty. Our gross margin as a percentage of total income from operations on a like to like basis increased by 210 basis points and stood at 71.9%. The increase was mainly due to reduction in prices of key input materials.

Earnings before interest, depreciation and tax on a like to like basis were up by 8% year on year to Rs. 912 million. EBITDA margin as a percentage of total income from operations increased by 90 basis points and stood at 21.2%. Profit before tax on a like to like basis was up by 10.7% to Rs. 1152 million. Net profit on a like to like basis was up by 10.4% to Rs. 1017 million. Our consolidated cash position stood at Rs. 3963 million including investments made in liquid funds. Our consolidated CAPEX for the year was Rs. 45 million, our return on net worth stood at 22.9%. With that, let me share some of the highlights of operations for the year gone by.

We continued our thrust on marketing initiatives to grow the categories and market share of our brands during the year. To narrate a few; on Sugar Free front, we have supplemented the above the line investments with strong on-ground activations and advocacy amongst the influencers.

We focused on growing the culinary business. For this Sugar Free ran all India, Sugar Free dessert challenge with celebrity chef Sanjeev Kapoor being the final judge. We did an on-ground activation linked to festivals like Durga Pooja. We launched influencer program to connect with Diabetics in two cities to begin with which has been further extended to total five major metros by the end of the year.

On the Everyuth front, we launched new campaign for both scrub and peel-off. Scrub campaign focused on innovation of moisturizing with the scrub. We restaged peel off with new packaging and benefits and communication focused on special occasions. This has helped turnaround the performance in Everyuth and overall peel-off category as well where we have significant share.

On the Nutralite front, to further build and strengthen the credentials in health food space, support across different communication medium was provided throughout the year. This included new TV, Press and outdoor campaigns to communicate functional benefits of the brand.

As per MAT March'16, report of Nielsen with a new panel the artificial sweetener category has grown by 6%, Sugar Free has maintained its number 1 position with a market share of 93.7% which is an increase of 120 basis points over last year.

Scrub category has grown by 11.7%, Everyuth scrub has maintained its number 1 position with a market share of 30.7%, the peel-off mask category has grown by 5.7%, Everyuth peel-off mask has gained share by 80 basis points and maintained its number 1 position with a market share of 92.1%.

Coming to the consolidated financial performance of quarter 4 of the year gone by:

Our gross sales were up by 5% year on year to Rs. 1169 million during the quarter. We saw a month on month improvements in the growth rates. Our total income from operations on a like to like basis was up by 5.4% year on year to Rs. 1098 million. The total income from operations for the quarter ended March 31, 2015 included reversal of the additional excise duty credit of Rs. 67 million pertaining to the period of April to December 2014. Our gross margins as a percentage of total income from operations on a like to like basis increased by 330 basis points and now stood at 73.2%, the increase was mainly due to reduction in prices of key input materials. Earnings before interest, depreciation and tax on a like to like basis were up by 15.2% year on year to Rs. 235 million. EBITDA margin as a percentage of total income from operations increased by 180 basis points and stood at 21.4%. Profit before tax on a like to like

basis was up by 9.3% to Rs 290 million. Net profit on a like to like basis was by 9.6% to Rs. 258 million.

Let me share some of the other important developments:

We have re-launched Face Wash range with a fresh new and contemporary looking packaging in March'16. This re-launch will be supported with the new communication in the coming quarter.

To continue our trust on the marketing initiatives to grow Sugar Free category and market share for our brand, we have signed Parineeti Chopra as our new brand ambassador for Sugar Free. The new multimedia campaign is being made and expected to go on air by the end of May'16.

To support growth expansion plans, M/s. Zydus Wellness Sikkim in which the company is 98% partner, has also decided to establish a new manufacturing unit at Sikkim. The new unit is expected to commence its production by the end of current financial year that is 31st March 2017. For this unit the firm is planning to invest approximately Rs. 350 million.

With all the above developments we clearly foresee a gradual improvement in the performance which gives us the confidence to firmly believe that our long term objectives and strategies are intact.

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 the question and answer session. The first question is from the line of Kastubh Pavaskar of Sharekhan Limited, please go ahead.

Kastubh Pavaskar: Sir I have few questions for the quarter. In quarter 3 your revenue grew by 5.4% if we consider the excise benefit which you got in FY 2015 of quarter 4 but what will be the growth if we exclude the price decline in Nutralite?

Amit Jain: This quarter there is no such impact because in the last quarter only that impact was there. We changed the pricing from January 15 so now there is no more impact of that.

Kastubh Pavaskar: In your initial comment you mentioned that your direct coverage has gone up by 20% so can you just elaborate on your distribution system now and what is your target going ahead.

Tarun Arora: We made this point clearly because we believe the revamp of distribution is now stabilizing and we see now streamlined processes back in place in our sales. 20% is more of our direct coverage, as far as Nielsen is concerned they report 8.3 lakhs reach of Zydus Wellness products, specifically Sugar Free is available in about 400,000 outlets and 5 lakhs outlets approximately for Everyuth and we intend to continue building on this distribution expansion,

with our investments on the brand as the task is to grow the category we will continue to expand our distribution. This 20% is just the last year's I think we will continue the same process further.

Kastubh Pavaskar: One book keeping question on your employee cost, this quarter it has gone up substantially so any one off is there in the employee cost?

Amit Jain: Yes, one off is there because the ceiling limit under bonus act has changed, which has impacted growth by around 8%.

Kastubh Pavaskar: So otherwise it could have been 20% increase in employee cost?

Amit Jain: 17%-18%.

Moderator: Thank you. We will take the next question from the line of Sheetal Bhatt of Catamaran, please go ahead.

Sheetal Bhatt: Recently we have been seeing that the Indian consumers are facing a lot of herbal and natural products and we have also seen recent articles about PureCircle investing in India into Stevia production, we have also seen articles about another group investing in Monk Fruit production at a large scale, do you think there are any concerns or threat to the Sugar Free business from any products from companies like these?

Tarun Arora: You have two parts on the question; first of all, the herbal products and I think, clearly I think Stevia and Monk Fruit are two of the ingredients which are talked about. Stevia is something which we have launched and tested, our national scale-up plan we will share when we are ready for it and I think PureCircle is basically investing to grow Stevia, more and we are closely working with PureCircle, even as a supplier so that should not be a problem. Monk Fruit as a potential have been, we are aware of it, it is still not approved by FSSAI even internationally also it is still a product which is being tested and if the opportunity grows Sugar Free would be happy to leverage this new development for the brand.

Sheetal Bhatt: At this point of time you are saying this is still not a threat for any of the Sugar Free lines especially Stevia as well.

Tarun Arora: Not really, not at all. We do not see it as a threat; we only see as an opportunity whenever it comes up.

Moderator: Thank you. Our next question is from the line of Salil Gupta of Enam Holdings, please go ahead.

Salil Gupta: Could you please repeat the market share numbers for Sugar Free and Scrubs that was given by Nielsen?

- Tarun Arora:** Sugar Free market share is at 93.7% which is 120 basis points over last year; this is the MAT March '16. Scrub; it is 30.7% and peel-off is at 92.1%
- Moderator:** Thank you. Our next question is from the line of Aashish Uppanlawar of Elara Capital, please go ahead.
- Aashish Uppanlawar:** Just wanted to have some hang on how you see your top line growing because for some time I mean, this quarter also the gross sales have grown by only 5%, so if you can give some additional knowledge to us on how things are progressing on various brands that you have and how soon you think it will go to double digit growth maybe?
- Tarun Arora:** Just the last quarter gone by, we have seen our numbers go up step by step each of the months, so we expect a double digit growth starting from this current quarter.
- Aashish Uppanlawar:** Okay sir but what gives you the confidence that it will start growing double digit and sustain at that, anything changing in the market place as far as your brands are concerned? Is it more a led driven by distribution because advertising we have already been doing quite a lot?
- Tarun Arora:** So distribution is already in place, it has stabilized and that is very helping plus some of our activation and advertising programs are also getting executed well. So all put together I think the whole piece is coming together and we are seeing that in month on month results we are seeing a ramp up and therefore it should happen and we are expecting a double digit growth in the current quarter.
- Aashish Uppanlawar:** Is it across brands you are seeing that number coming?
- Tarun Arora:** Absolutely, that is correct.
- Aashish Uppanlawar:** So the decline in Everyuth that we had been seeing, now that the market share being very low so that phase is over, now it should expect the buildup overall, is it?
- Tarun Arora:** Absolutely, Everyuth also should see a buildup.
- Moderator:** Thank you. Our next question is from the line of Bhavesh Jain of Envision Capital, please go ahead.
- Bhavesh Jain:** Any update on our export and new product strategy?
- Tarun Arora:** Exports we are focusing first largely on the Middle East and Africa, so that is one markets. SAARC is the second market; we will start exploring the South East Asia as well. So first of all our focus is more of the emerging markets as I explained to you Middle East, Africa, SAARC and then the South East Asia and we already have people in place and we are building on it. It is a slow and steady process; we are taking forward on that. In terms of new product strategy, we are building, we have products in the pipeline and by this year you will see some

new products coming in and we will be sharing in the calls once we have these products in the market place.

Bhavesh Jain: And sir any update on Acti Life because last time we were doing some pilot for that particular product?

Tarun Arora: We are working on it and we will be sharing it once we have it in the market place. So we are still working on it, we see a good opportunity in the nutrition space and therefore we will be taking this forward.

Bhavesh Jain: And any update on our Face Wash?

Tarun Arora: So like I explained in my speech, Face Wash we have re-launched with new contemporary packaging which we will be also communicating, so this quarter will be important for us to get Face Wash back on track for us.

Moderator: Thank you. Our next question is from the line of Kinjal Desai of Reliance Mutual Fund, please go ahead.

Kinjal Desai: I just wanted to understand few things; one could you give us an idea what will be the market size of the 3 categories that we are in right now?

Tarun Arora: Sweeteners is about Rs. 300 crores odd, Facial Cleansing is about Rs. 1800 crores, Rs. 1900 crores and butter substitute category there are different estimates but our understanding is that it should be close to about Rs. 150 crores to Rs. 200 crores. So these are all consumer purchase terms.

Kinjal Desai: And for the distribution expansion that we have undertaken in the last year so could you just give us an idea how has it fructified for us? I mean we have done very good in this one quarter but overall what kind of growth can we be expecting because of this?

Tarun Arora: So distribution is a way to get to the growth so we are working on expanding our distribution but I think we expect our consistent sustainable results because of our strengthened distribution that we are building.

Kinjal Desai: Any new products and/or variants that we would have launched during the past one year?

Tarun Arora: Not really, in last 3-4 quarters we have not launched anything but over next 3-4 quarters we do have products in the pipeline which we will share once they are ready for the market.

Kinjal Desai: Sir when you say new products, it would be like new variant under what we already have?

Tarun Arora: Line extensions, yes.

- Kinjal Desai:** Just one thing to go – our A&P is a little lower as a percentage of sales in this particular quarter, so going ahead do we get at the same time quite a bit for the next one year, so would we see a pick up in the kind of Ad-spends and Ad-investments that we would be doing?
- Tarun Arora:** We remain consistent with our strategy of being annual about 20%, there may be some quarter-on-quarter ups and downs but at our annualized level we stay focused on date to working on 20%.
- Kinjal Desai:** As we going to go forward and we want to do new products and new line extensions, so would we not need higher intensity?
- Tarun Arora:** So once we need it and we have a plan we will look at it but it will be based on initiative by initiative but as a business model I think we will intend to remain consistent on that.
- Moderator:** Thank you. Our next question is from the line of Ajay Thakur of Anand Rathi. Please go ahead.
- Ajay Thakur:** Just wanted some colors on what would be growth across a different segment, if you can just qualitatively give some details on growth rate in Sugar Free versus the non-Sugar Free segment?
- Tarun Arora:** So, giving you a qualitative sense of it like I mentioned even in my speech we have seen good growths in Sugar Free, we have seen good growths in Everyuth, especially on peel-offs and scrubs also has seen good growth. Facewash like we mentioned earlier has been under stress, Nutralite also in between we had a bit of challenging time which is also back on track. Therefore, today if I were to give you sense of overall business, we are looking at a positive growth across categories, Facewash is the only one where we are working on it and is been a bit of laggard for us.
- Ajay Thakur:** And Nutralite you seem to have actually back to our foot as in doing fairly terms.
- Tarun Arora:** Yes, we are back to comfortable growth.
- Ajay Thakur:** And sir you mentioned about the international business foray, so when are we likely to see that actually, as in when will we see the numbers panning up for that?
- Tarun Arora:** So, it is still a very small business, I think in a year's time, we will start sharing some specific details because we are right now, identifying markets, building our distributor network internationally and looking at what products would we need to do for those specific markets, which are the products we can carry as it is and which are the products we may have to adopt for those markets. So, I think a year down the line we will be happy to share some of the numbers and sense of where this business is headed. Our early understanding is sweetener category has a good potential globally and given our understanding of the sweetener category

in India, I think we can leverage it extremely well. For Skin Care we will have to do lot more adaptation as per local markets and other categories we will evaluate as we go along.

Ajay Thakur: And sir lastly given the fact that we have such a strong pricing power, is there any possibility of us taking price increase in any of the segments?

Tarun Arora: Right now, nothing is envisaged, we will take a call when we feel there is a need, right now our focus is clearly getting new consumers and drive business on a volume led growth.

Ajay Thakur: Just one more question, if you look at our product portfolio – we have 3 different categories we cater to and the distribution needs for these 3 categories are also pretty different. So sir any plan to make sure we get more concentrated kind of a distribution structure for all of the 3 categories or is there something colors on that? Possibly, how we are trying to converge all the 3 distribution of all the 3 product actually and trying to drive the growth for whole of the company?

Tarun Arora: So, when we revamp structure, I think we have really looked at it there were clearly opportunities where we worked together across the categories like modern trade. On a general trade there maybe we have to do it by sub channel wise, so I think our model accounts for the differences across and being relevant to each of the category customers, so I think that has been taken into account. We do not see any change in terms of concentration for one and making choices against another. I think we have worked that out fairly well in the whole distribution model.

Moderator: Our next question is from the line of Kastubh Pavaskar of Sharekhan. Please go ahead.

Kastubh Pavaskar: Sir my question is on the Sugar Free delight which is the Sugar Free beverage which you were again planning to relaunch in the market, so any thought on that, when are we planning to launch it?

Tarun Arora: So, we are looking at Sugar Free extensions and relooking at the entire strategy on that and we will share with you once we are ready with that but as of today nothing ready to share.

Kastubh Pavaskar: And your guidance for the tax rate going ahead for '17 & '18?

Amit Jain: It would be in the range of 10-12%.

Moderator: Thank you. Our next question is from the line of Sundar S of Spark Capital. Please go ahead.

Sundar S: Sir my question is regarding this capacity expansion which we have outlined in Sikkim, what is this particular capacity expansion for sir?

- Tarun Arora:** So, this is in line with our growth expectation over next 5-year plan that we are putting in place and some new categories which may also emerge, so with that in mind that we are building this capacity.
- Sundar S:** So, is that going to be a shift completely from that existing Ahmadabad facility into the complete Sikkim or Nutralite is still going to be out of the Ahmadabad facility?
- Tarun Arora:** Nutralite will continue to be in Ahmadabad in the same plant. This is an expansion, so this is another unit in Sikkim itself.
- Sundar S:** So, this also attracts tax benefits?
- Amit Jain:** Yes
- Sundar S:** Another question regarding your gross margin is that, what is the outlook on that front; because we were about 72% is where we have closed the year with end and 73% for 4th quarter seems to be one of the highest, so any outlook on that particular path?
- Tarun Arora:** So, we expect that it will continue.
- Sundar S:** Any number that you would like to throw?
- Tarun Arora:** No, very hard to say, given the way commodity prices are moving, very hard to say but we are reasonably optimistic at the overall level.
- Sundar S:** Pardon my ignorance but what would be our major commodity in our raw material basket sir?
- Tarun Arora:** Palm oil, lactose, Sucralose, and SMP.
- Sundar S:** And what is your outlook on palm oil sir because we have been hearing in the market that palm oil prices are going up at a rapid pace, so any comments on that?
- Tarun Arora:** Very hard to estimate, there are enough experts talking, so it is very hard for us to give you any suggestion on that, given the way it is.
- Moderator:** Thank you. Our next question is a follow up from the line of Bhavesh Jain of Envision Capital. Please go ahead.
- Bhavesh Jain:** Are we actively looking for any acquisition target, considering the cash which is sitting on our balance sheet of around Rs. 400 crores?
- Tarun Arora:** Yes, we are looking for it both India as well as international.
- Bhavesh Jain:** Okay, can we get the perspective on Zydus Wellness from Mr. Sharvil Patel?

- Sharvil Patel:** What perspective would you like to hear about?
- Bhavesh Jain:** About the business, where they want to take this business over the next 3-5 years. Their perspective about Zydus Wellness.
- Sharvil Patel:** So, I think we have had this whole distribution revamp that has happened which has taken us a little longer time than we expected in terms of being able to put that in order and now we are seeing signs that there is stability in the team and we are seeing what we had planned earlier which is distribution expansion that is happening for us. The other aspect is that we have not been present in the international market for some of our products and we see a lot of opportunity in the markets that Tarun spoke about which is the Middle East, the markets nearer to India. We already have initial opportunities to talk to with lot of distributors, so we will see a good expansion happening over next 5 years on the international business, which is near to India. And the final point is that as you said we have lot of cash, we are looking at opportunities in acquisition in both in India and internationally and we are evaluating multiple opportunities, so hopefully we will be able to do some acquisition in the coming year. So, this all put together we should see a good opportunity for Zydus Wellness at the same time we are looking at the brands that we have not seen, how we can expand those brands in other categories and that is some work that is going on which will be more clearer by next year.
- Moderator:** Thank you. Ladies and gentlemen that was the last question. I now hand the floor back to Mr. Tarun Arora for closing comments. Over to you sir.
- Tarun Arora:** Thank you gentlemen and ladies. See you next quarter.
- Moderator:** Thank you members of the management. Ladies and gentlemen on behalf of Zydus Wellness Ltd. that concludes this conference. Thank you for joining us and you may now disconnect your lines.