"United Spirits Limited
Q2 FY '23 Earnings Conference Call"
October 25, 2022

MANAGEMENT: **MS. HINA NAGARAJAN – MANAGING DIRECTOR & CHIEF EXECUTIVE OFFICER – UNITED SPIRITS LIMITED**
MR. PRADEEP JAIN – CHIEF FINANCIAL OFFICER - UNITED SPIRITS LIMITED

Moderator: Welcome to United Spirits Limited Diageo India's Second Quarter Earnings Conference Call. Hosting the call today from USL Limited are Ms. Hina Nagarajan, Managing Director and Chief Executive Officer; and Pradeep Jain, Chief Financial Officer. As a reminder, all participant lines will be in a 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 star then zero on your touchtone phone. Please note that this conference is being recorded.

I now hand the conference over to Ms. Hina Nagarajan, Thank you, and over to you, ma'am.

Hina Nagarajan: Thanks so much. Hi. Good evening, ladies and gentlemen. Thank you for joining us on the second quarter earnings call of United Spirits Limited. At the outset, I would like to take the opportunity of wishing all of you and your family is a very joyous and safe Diwali. I hope you had a lovely unconstrained celebration this year after a couple of years of very quiet Diwali during COVID. As always, it's a delight to interact with all of you and I'm joined today by Richa our Investor relations head and Pradeep, our CFO. I intend covering the following today in the opening comments:

- A little bit on the consumer context in the current environment as we are seeing it.
- A short update on the key pillars of our strategy communicated last year, especially the portfolio re-shape and the Society 2030 goals.
- Some contexts on the results that we announced last Friday and
- Then we can open it up for Q and A.

On the consumer context,
While inflation has been a bugbear in the recent past, the larger consumption story anchored in premiumization continues strongly for our consumers.
Premium & Luxury consumers are driving growth ahead of middle-India Prestige consumers and the latter are also coming back to the pre-Covid growth trajectory as well.
Affluent consumers repertoire behavior too continues with non-whisky categories like Gin & other white spirits gaining further traction. This is also indicative of consumers increasingly wanting to drink better not more.
Among the middle-India consumers, while we are witnessing downgrading in the larger FMCG space, I would say the Prestige consumers in our category are managing their wallet-share by moving to smaller sized sku’s but not downgrading to lower priced brands. This is reflective of the brand affinity in our category.
On the strategic side on our strategy pillar, Our Portfolio Reshape strategy is accelerating; we have covered a lot of ground and are relentlessly at it.
We had announced earlier in the quarter that an investment of INR 45 crores was made by the company for its state-of-the-art craft and innovation hub in Ponda, Goa. This investment is in line with the company's strategy to accelerate transformational innovation and strengthen our craft and premium portfolio. Our recent innovations renovations position are better to meet changing consumer tastes and preferences and will propel growth.

Godawan, our Indian single malt is now available in five states. Rajasthan Delhi, Goa, Karnataka and Haryana and launched in the international markets of UAE. It will soon be available in the UK and in the United States of America.
Black Dog renovation that was rolled out last year continues to be well accepted by consumers, leading to continued momentum on the brand. We continue to scale up the campaign with global icon Kiera Knightley across digital platforms as well as out of home.
Royal Challenge American Pride has now become available in eight states during the quarter. We are launching the brand in October in three more states Maharashtra, Rajasthan, Punjab.
On Signature the momentum from the renovation last year continued on the back of significant improvement in consumer equity, with consumers really appreciating the creamy blend and differentiated packaging and crafted from nature proposition.
With focused energies on Royal Challenge, we have been able to lead the growth in that segment in this quarter. It grew on the back of both competitive pricing as well as renovation, especially in the state of Maharashtra, Telangana, Delhi, and we are now in the process of extending the renovated Royal Challenge to other states in the country.
On McDowell's No.1, our intellectual property of Yaari Jam with a tribute to the singer KK has driven huge engagement with over two billion views and the first of its kind consumer engagement in the relevant key states. Despite segment headwinds, this is one segment where we do see some impact of the inflation, but despite those headwinds McDowell's No.1 has delivered really good performance.
Last but not the least, the critical components of our portfolio reshape strategy, we have successfully completed the sale of the entire business undertaking associated with 32 brands in the popular segments to Inbrew Beverages Private Limited and have given effect to the franchise of 11 other brands in that segment for a period of five years. The completion of this transaction enables us to unequivocally focus on prestige and above and capitalize on the rapidly changing consumer and category trends. Five manufacturing facilities have been transferred, four of these third party and one of our own manufacturing to Inbrew. We have also provided continuity of jobs and benefits to employees working on this portfolio who have now moved from Diageo USL to be part of the Inbrew team.

On the digital side, in.thebar.com is the hub for our brand to enable hosting landing pages of different brand campaigns. The biggest initiative has been linked to Ecommerce in West Bengal, building the direct-to-consumer linkage of the bar with third party aggregators like Swiggy, Boozy, Bigbasket for consumers visiting the bar from that market. The social content calendar which comprises of cocktails knowledge, drinks, bar, bartender, brands, and celebrations also went live with now regular content available to consumers. We will continue to scale this up with more content, better user experience and engagement for the community.

On our Society 2030 goals, we continue to make progress towards our Society 2030 goals.

Aligning proactively with the SEBI disclosure requirement on Business Responsibility & Sustainability Report (BRSR) for next year, we have published on our website an independent Environmental, Social and Governance (ESG) report for FY 2021-22. It has been prepared in accordance with GRI (Global Reporting Initiative) standards. The disclosures are mapped with UNGC (United Nations Global Compact) principles and SASB (Sustainability accounting standards board) sector specific standards. This is further aligned with Diageo PLC's ESG Reporting Index 2022. We request you to go through the above ESG (both quantitative/ qualitative) disclosures for a comprehensive understanding of our objective and progress in this space.

Now, a little bit on our financial performance, we have delivered strong top line growth and resilient EBITDA performance. Like-for-like, our business is bigger and stronger versus pre-pandemic levels of 2019. We have delivered a growth of almost 18% in the second quarter. P&A growth stands at 23%, growing on a strong base and the highest underlying growth in the last 24 quarters.

The price mix during the quarter was at 9.4%, reflecting the higher growth in more premium segments as we move up the consumer price later. More importantly, we have seen sequential gains driven by the recent innovation and brand renovations in both mid-prestige and upper prestige. Double-digit inflation and ongoing scotch pricing discussions led supply constraints adversely impacted our gross margin. Our marketing reinvestment rate during the quarter was 5.5% of net sales. We continue to drive customer-centric activation, strengthen our brand equity and premiumize the portfolio. We have also leveraged media opportunities on the back of marquee Cricket Associations like that on Asia Cup and the India-England series. And of course, you must be delighted with Virat's performance in the match that happened just a couple of days ago or yesterday or day before.

EBITDA was INR 446 crores and EBITDA margin was 15.5%. Underlying EBITDA, excluding one-off in previous year was up 11%. Exceptional items primarily include a net one-time profit arising from the slump sale of the business undertaking associated with 32 brands in the popular segment. Profit after tax after incorporating the tax-adjusted exceptional gain was at INR 563 crores in the quarter, up 105.9%.

Our outlook on inflation and pricing, we do expect double-digit inflationary pressures to continue to impact in the near term, driven by the sequential surge in prices of input going into glass manufacturing and ENA. We are cautiously awaiting the ethanol blending policy that we will stand announced in this coming quarter.

On the flip side, we are also seeing some green shoots in paper price and crude-linked commodities. Pricing realized in some of the states will now start ramping up in the quarters to follow. Revenue growth management and delivering on our productivity initiatives across the value chain will also help us to partially combat the inflationary headwinds.

In conclusion, all I want to say is that we are confident in the resilience of our business, our strategy and our ability to navigate headwinds as our team has demonstrated over the last couple of years. We remain focused on our strategy of reshaping the portfolio, driving commercial excellence, in-store and on-premise, revenue growth management and everyday efficiency and productivity extraction. This gives us the confidence to deliver sustainable growth and create long-term value for all our stakeholders.

With this, we can now open the line for Q&A.

Moderator: Thank you very much. We will now begin the question-and-answer session. Anyone who wishes to ask a question may press star and one on the touchtone telephone. If you wish to remove yourself from the question queue you may press star and two. Participants are requested to use handsets while asking a question. Ladies and gentlemen, we will wait for a moment while the question queue assembles.

The first question is from the line of Abneesh Roy from Edelweiss Securities. Please go ahead.

Abneesh Roy: My first question is on demand side. So you made two remarks, one was premium and luxury growing faster than the overall P&A. And second is the customer is not downtrading, he is consuming smaller SKUs, just like in FMCG. So is it possible to give some insight, some numbers on both of these? And the related question on overall P&A was when I compared to pre-COVID in terms of the specific channels say pub, bars, larger event consumption, for example, say, large weddings or say, off-sites in hotels, is it now back to the pre-COVID whatever data you have, if you can share on that?

Hina Nagarajan: Hi, Abneesh, I'll answer the second question first, which is that our events, marriages back to pre-COVID level. Actually, yes, they are. And marriages are back and how? I mean, we are seeing larger and larger marriages. So that's pretty good for our demand forecast. Luxury premium, we continue to see the double-digit growth that we have been seeing for a while. That has not changed really over the last few years. So the premiumization trend is continuing there. I would say even on the Prestige side, we have seen pretty healthy growth.

I would only caution that, look, it's just a few quarters after the opening up of the market. So I don't feel that the demand in this segment has fully settled. I would say, basically mid and upper-Prestige. But there is some level of premiumization that's continuing in these segments. We've seen a little bit of slowdown on lower Prestige which is primarily attributed to, I would say, uptrade from the popular and the country liquor. This is a bit slower than what we've seen over the last few years. But having said that, I think our brands are performing very competitively in each of these segments. And overall, we feel very confident about the demand scenario in the industry.

Abneesh Roy: Sure. My second question is on the specific statements you made on two of your brands. So on Royal Challenge, you mentioned competitive pricing and in McDowells, you mentioned some inflation impact. Now inflation is across the board as a portfolio itself. So what do you mean when you said that McDowells is facing the inflationary impact?

Hina Nagarajan: No, my comment on McDowell was largely to explain that we see some slowdown in the lower Prestige category on account of inflation hitting that category of consumer, and therefore, some slowdown in uptrade from, say, popular or country liquor to this segment. So that's the clarification on inflationary impact on the category rather than McDowell. So on Royal Challenge, we were not fully competitively priced in a couple of states, and we have corrected that pricing, to be competitive in those states. And the brand is actually showing very good growth momentum, not only in those states, but across the market.

Pradeep Jain: Yes. And maybe an additional build Abneesh from my side is that, look, Hina and I have consistently maintained over the last two, three quarters that when we renovated McDowell's and RC, we were not really delighted with how RC had performed. And therefore, over the last three - four quarters, we were working on reengineering the blend to make it grow further. And now what we have done with the Delhi RTM change and this competitive pricing reaction in Maharashtra and Telangana, we are pretty happy with the way they've responded.

Abneesh Roy: Sure. One follow-up on that, your corrective action in Royal Challenge, has it led to any retaliation by the other players? And on Delhi market, if you could elaborate what is the current situation?

Pradeep Jain: So, like we said, we were over-priced in a few of the critical markets. We've just become competitive on pricing. So that addresses your first question, Abneesh. And on Delhi market, maybe I'll hand over to Hina to talk about the renovation that we did.

Hina Nagarajan: Look, so I can't put a retaliation. I think all competitions are following their strategy and continue to follow their strategy. And for us clearly, we had said that we will reshape the value proposition in mid-Prestige through the renovation of Royal Challenge. And I think we are feeling very confident that we have managed to now reshape the value proposition, and we are seeing good results for Royal Challenge whiskey. And therefore, we are rolling out this renovation to many more states sequentially. So I think our strategy is now falling in place as we had expected it to. And competitors continue to follow their own strategy.

Moderator: Thank you. The next question is from the line of Harit from Investec. Please go ahead.

Harit Kapoor: So just my two questions. Firstly on the quarter, so you mentioned that in your release that you've successfully concluded discussions in a few states for scotch prices. So would we assume now that most of these is now done with and the supplies are normally resumed? Or should you give us an update on that and on those discussions as well as what's been the impact of that in quarter 2 to you?

Hina Nagarajan: So in some of the space, we have concluded discussions and supplies will be normalized in this quarter. Even in the couple that are pending, we expect closure on that during the current quarter. So you can assume supplies will start getting normalized during the quarter.

Harit Kapoor: And are you calling out what is the impact on quarter 2 on account of this and any basis point impact that you would have had a net supply in the state?

Pradeep Jain: Harit, in quarter 2, the quarter that has just passed?

Harit Kapoor: Yes.

Pradeep Jain: Okay. So, and maybe I'll just start and then Hina can build. Look, it's not just one isolated factor of the BIO supplies. There are a couple of balancing factors, I would say. In terms of the benefits that we have got, I think it's two things. One is Puja in West Bengal was a little ahead compared to last year. So therefore, the loading that happened into the trade happened a month earlier. Last year, it was October, this year, large part of it was September. And it's so large that it does impact national numbers.

And also, we were lapping a soft base of last year in two states, which is again Delhi and Bengal because both were gearing for an RTM change last year in October/ November. So therefore, the July August, September numbers were a little soft. And conversely, these two benefits that we had in July, August, September this year are balanced by the BIO of supplies due to the pricing discussion. Now net-net, yes, the two are squaring off each other, maybe some amount of moderation will happen to the 23% P&A growth that we have said but we'll have to wait and watch over the next 2 months, 3 months, how much is that. Does that answer, Harit?

Harit Kapoor: Yes. Got it. The second question is on, if you look at the first half, you've done about close to 14.5% margin, 13.8% if you just for the one-off in quarter 1 and 15.5% in this quarter. This is in spite of your gross margin being close to 500 bps plus down versus normalized levels if I recall them. Does that give you more confidence on the medium-term guidance of mid-to-high teens? Or rather, is there a possibility that given your cost structure currently, you would look at maybe a revised guidance, given the fact that you're already almost hitting a mid-teen number with such high inflationary pressures?

Pradeep Jain: So look, Harit again, let me start and I request Hina to build on that. So first of all, yes, absolutely, we are committed to our mid-to-high teen guidance. And obviously, it's a desire to try and stay true to that. Now having said that, let me start with what we are happy about. We are happy with the growth momentum, which continues to give us an operating leverage on our fixed costs. So that is something that we are happy about.

We are also happy about the fact to exactly what you mentioned that if you take the inflation impact, our gross margin is probably off by about 720 bps to 730 bps, but we are offsetting a good 1/3rd of that through a combination of headline pricing, mix management, and management productivity, so that again reassures us. Now having said that, if you also then, we are also maintaining a good cost discipline on our overall fixed overheads. So that allows us to get a further operating leverage on our P&L. Now what Hina and I would ideally want to do a little more is the 5.5% on A&P, we would want to ideally inch that back to about 8% to 9% A&P level. And in this kind of environment, when the inflation is so steep, etc., you end up making some tough choices and calibrating that a little bit. So that's the way I'll pass it, in case Hina has any additional build on that.

Hina Nagarajan: Yes, I would say the year will continue to be challenging. Look, Harit, our inflationary pressures, we are not seeing them come down like other FMCG companies primarily because of the raw materials we use, which are glass and ENA, so I would say there will be pluses and minuses. Some pricing will flow through better in the coming quarters, a little bit of mixed advantage we will have. On the other side, we do want to go up on A&P as Pradeep said. So I would say that, we will try and, of course, pay through to our mid-to-high teens, but I see our margins pretty much in this range for the next few quarters.

Pradeep Jain: Yes. In the lower end of the mid-to-high teens.

Moderator: Thank you. The next question is from the line of Palak Shah from Infina Finance.

Palak Shah: First question was I want to check with you after the deal conclusion, what quantifiable working capital release that we've seen?

Hina Nagarajan: Working capital release.

Pradeep Jain: Okay. Yes. Did I get the question right? You're saying that post the deal closure, how much of working capital has got released?

Palak Shah: Yes.

Pradeep Jain: Okay. So the number is roughly about, it will come in two phases. The number is roughly about INR 420 crores, INR 280 crores to INR 285 crores is part of the slump sale and then the balance 11 brands that we franchise that leads to a further relief of about INR 140 crores. So those are the broad ballpark numbers.

Palak Shah: Got it. Secondly, just on the gross margin front. So as Hina mentioned that there has been a lot of optimization that has happened this quarter, plus if you look at the excise, that’s reflecting in the excise component coming down instead of a 68% to 65% this quarter on a Y-o-Y basis, despite a better gross margin actually contracted to 39.5%, is that indicative of a high inflation and unless you get a price hike from the larger states like Maharashtra and Karnataka, you would actually be able to go back to that 44%, 45% gross margin?

Pradeep Jain: Yes. So Palak, like I said, we've always maintained that the inflation that is impacting us is roughly in the double-digit range, double-digit to low teens and then it's pure math. On a 40% gross margin, roughly that whatever low double-digit inflation will knock off roughly about 750 bps of a gross margin, simple math. And then what it has actually diluted by is roughly about 480 bps. So therefore, the way you will have to see it is that what we are being able to recoup despite the commodity inflation. What I do acknowledge is there is still not too much of pricing flowing through in our P&L.

To the point that last year, some of the BIO reversals happen, we had to participate as forced in by the government, and then a couple of competitive pricing actions that we had to get back to parity, etc. So therefore, there's not too much of pricing going through. Having said that, the inflation is also likely to continue. For example, you've seen the natural gas pricing announced by the government. That's a 40% increase already on top of an 80% to 90% increase that was made in April. So that sequential inflation will continue, but we are confident, having seen the approvals come through, etc., pricing will also ramp up in the coming quarters.

So that's broadly what it is. Our gross margin will remain under pressure for right now. And we will have to just play with the other lines of the P&L and the other value drivers to maintain our EBITDA margins.

Palak Shah: Got it. Just a follow-up on this, which states have actually got price hike during Q2?

Pradeep Jain: So we have got in the last three months to six months over six states, I'm just looking at, so you've got pricing in Haryana, Punjab, UP, West Bengal, some pricing in Maharashtra and some pricing in Karnataka. So we have that pricing in all these states. Rajasthan, we had got pricing in the April-June quarter. Assam, we had got hefty pricing in the January-March quarter.

Moderator: Thank you. The next question is from the line of Latika Chopra from JPMorgan. Please go ahead.

Latika Chopra: I just further just digging a little bit more into the pricing part. Would it be possible to tell us with 8% price mix growth for P&A portfolio, how much of this could be pure pricing because you did take some competitive pricing action and you did get incremental price hikes from two states as well. So just wanted to understand where does net price effect settles down. What is the mix effect out of this 8%?

Pradeep Jain: Yes, it's largely mix, Latika. It's largely mix. 90% of this is largely mix in this quarter. Like I said, net pricing flow-through is minimal because of the negatives and the positives, but we expect that to ramp up, as the negative fallout and we've got fresh pricing from the state that, in fact, will ramp up significantly in the coming quarters.

Latika Chopra: Pradeep, is it fair to assume that gross margins bottomed out because of scotch pricing discussions, which were concluded and some more might come in will flow through fully in Q3 and that also happens to be seasonally a strong quarter for you?

Pradeep Jain: Latika, I would one would, Hina and I would want to believe, yes. Now unfortunately, the commodity environment remains a little volatile. I would have been in a far more confident position to agree with you but come 1st October, natural gas pricing has happened, 40%. As a result of which, we are having to give the price increase to our glass suppliers. And then the big impact of the Delhi RTM. That's a reversal. That's a big blow all said and done. Delhi was adding about in the last 4 quarters, Delhi was adding about almost 3[#] points to 4[#] points of national growth and as the Delhi RTM has reverted back to its original pre-RTM change contract, we will have to figure out a way to recoup that loss through the rest of the country. How much of that we will be able to recoup that is yet to be established.

[#] *Corrected from 4-5 points to 3-4 points*

Latika Chopra: So, as it stands, Pradeep, does it imply that Delhi is a no go? What's really happening there? The sell-throughs are lesser, significantly lower?

Pradeep Jain: Okay, sell-through. No, so we are waiting for things to stabilize Latika. The new RTM has come into effect. The rolled back RTM has come into effect towards September end, first week of October. Our sense is that things will stabilize over the next 60 days to 90 days and then we will be in a better position to call out what's the longer-term impact of Delhi. It's too volatile right now to talk what's the long-term implication of Delhi.

Latika Chopra: All right. And then the last bit that I wanted to check was on your efforts towards non-whisky portfolio. I think I mentioned that in our opening comments as well. What growth are you seeing in this portfolio? What are the brands that excite you? Is that something which could pick up a meaningful part of your growth contribution over the next couple of years?

Hina Nagarajan: Sure. I would say that both gin and vodka, are the categories that are really growing well. Largely because I think consume the highly mixable drinks, and they make perfect, fantastic cocktails. Cocktails have really taken off, especially post-pandemic. During the pandemic and post and in the cocktail culture, especially driven by millennials.

So, I'm very excited by both the category. We have really activated Tanqueray and Gordon's gin brands. And in the Tanqueray in the brunch occasion, Gordon's in the Sundowner occasion, and both brands are seeing very strong double-digit growth, I would say. Smirnoff, we introduced the pocket format of Smirnoff a quarter ago, quarter or two ago, and it rolled out given the thing and we've done activation on-premise with Smirnoff, with our vodka going along with a range of other drinks. And Smirnoff is also growing at a very healthy double-digit growth rate. So, I'm quite excited by the white's category per se, I think this category will continue to grow with millennials and the whole repertoire drinking that I was talking about in my opening narrative, which especially at the premium and luxury end seems to be a phenomenon to state. So we are continuing to invest behind these brands and grow them.

Moderator: Thank you. The next question is from the line of Prakash Kapadia from Anived Portfolio Managers. Please go ahead.

Prakash Kapadia: Two questions from my end. How large is Delhi contribution to our annual sales, if you could give some percentage?

Pradeep Jain: Delhi will be broadly, and we have some broad ballpark numbers. It will be about 4%[#] to 5%[#] of our national P&A business. This was on the revised ramped-up volumes, Prakash. Now as I said to Latika earlier, we'll have to wait for what the volumes to settle down.

[#] *Corrected from 6-7 % to 4-5% of Net P&A sales value*

Prakash Kapadia: Understood. And in the first half, we've seen broadly a 50% impact on sales due to volume and 50% impact due to price and mix as we progress more towards P&L that contribution increases post the divestment, that should be 2/3rd, 1/3rd going forward? Is that the right understanding?

Hina Nagarajan: You mean volume to mix?

Prakash Kapadia: Yes.

Pradeep Jain: Yes, probably, like we have said earlier, when we are selling the full portfolio, our price mix should stabilize around the 7% to 8% range. Once we have the full scotch availability and we are supplying across the country, in the full portfolio, our price mix should be about 7%-8%. And then yes, our aspiration would be that volume can also so probably it will remain in the 50-50 range.

Hina Nagarajan: Yes, I expect this to remain in pretty much the same way because we are ramping up our volume growth in the Prestige categories and so I wouldn't expect that change dramatically.

Pradeep Jain: It should be in the 50-50 range.

Prakash Kapadia: And lastly, as this, again, contribution of the premium segment increases, there have been carton cost reductions, there have been declines due to some of the mix changes. Could you call out a number or an annual impact, which could happen once on a full-year basis or next year once this entire sale has gone through?

Pradeep Jain: Sorry, Prakash. So I missed the question. Can you repeat that? So I know it's to do with the divestiture. So once the divesture...

Prakash Kapadia: Once the divesture is done yes, on an annual basis, if you could help us understand, carton costs will decline as we premiumize and we don't put outer cartons on the premium brands. So is there a number which you can…?

Pradeep Jain: I think it has to do with the divesture cost Yes, it's got nothing to do with the divesture.

Prakash Kapadia: Mix will also change, so as the mix changes, the gross margin obviously will trend upwards and this as a percentage of costs could reduce. I was trying to assess the annual reduction due to this change, irrespective of the divesture if you can call out, it would be helpful?

Pradeep Jain: I mean, we haven't really called that out so far, but yes, we are consciously going to phase that out, starting from another couple of quarters down the line. We haven't publicly called that number and we won't want to call out that.

Prakash Kapadia: Once the year-end comes out and then we'll have more clarity on that. We'll have actual structure.

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

Chetan Shah: Just one quick and maybe a little broader question. I'm just taking the liberty to Hina ma'am is around. Then if you see our mix of volume and revenue in a three different category, if one wants to fast forward and look at the business profile, three years from today or five years from today, what is the most optimal mix, which you would want to see beyond which you may not want to tinker around with the mix of both volume and the value, value-mix? Just to get a sense from a team's point of view that looking at India as a market, which is a customer in all the three segments? So how do you see that get shaping up?

Hina Nagarajan: Yes, I think we did cover it briefly in the previous question. We've been delivering 8%, 9%, 10% mix as we transition in the portfolio. My expectation is that over a steady state, maybe in a couple of years or whatever, we expect the mix to settle at about, I would say, 6% to 7%. The broader reshape of the portfolio, we have completed now with the divestiture and the franchising of our popular. The big action that we wanted to take on our portfolio reshape is done and as we grow P&A now and focus more on that, I would imagine that a steady state 6% to 7% mix impact would probably be something that we will use a measure of success.

Chetan Shah: Great. Now in a couple of questions before, you alluded about the opportunity into gin and other category. If I may take a liberty to understand from a Diageo's global product portfolio, you spoke about this a couple of quarters back also. But just to get a sense, how do you see this -- I know from a competitive point of view, we're not want to talk about it. But just as a category, if you can give us some sense, which can become a future growth driver maybe from next year, five years horizon, apart from the whiskey as a category from a volume point of view, if you can share that will be very-very helpful?

Hina Nagarajan: Sure. From a global point of view, we saw gin really explode. I would say, particularly during the pandemic. And basically, it had a lot of momentum, the last three to five years, I would say. And in India, we saw the movement on gin pass really maybe a couple of years ago and vodka also has in our country, it is growing quite well. So I would say that vodka around the globe is not as fast-growing as gin, but vodka is growing very fast in India. So like I said, I'm quite excited about the growth potentials in the white category, both gin and vodka. Even the craft gin segment is quite exciting. And as you know, we've invested in now brand, which is Hapusa and Greater Than gin, which are the craft side of gin. So we're quite excited about this category.

I do have to say though that we want to be more value-focused than volume, and we will play choicefully in the premium segments, in the right segments in Prestige and above in both these categories. And this is reflective of our overall philosophy of supporting consumers to drink better, not more. So the value strategy really ties in with drinking better, not more, and we are quite committed to moderate consumption, but help people drink much better products.

Chetan Shah: Just one small last question from my side. In terms of the pre-mix drink, which is another fad, which goes and comes, goes and comes, do you have any thought process around that specific segment because we spoke about white spirit just to get your view on that? And wish you and team all the best and happy and prosperous New Year.

Hina Nagarajan: Yes, thank you. And I think you are talking about ready-to-drink category, if I'm not mistaken, right?

Chetan Shah: Yes, ma'am.

Hina Nagarajan: It's a category that we have said, look, we saw traction in ready-to-drink, say, in markets like USA and in the UK during COVID. In India, the category is it's been pretty volatile actually. For a while, it has not really grown. There are some smaller players who have come in now, and we are seeing some selective growth. It's a category that we are watching. It is a category that we are watching more from a future back lens and if we see the trend really accelerate and the consumer acceptance of pre-mix drinks go up substantively, then we have a very rich portfolio of drinks in our global portfolio that we could potentially bring to India or we could explore making the ready-to-drink in India itself. So it's a category that we are watching, and we will look at participation if we feel the time is right and the traction is high.

Moderator: Thank you. Next question is from the line of Mehul Desai from JM. Please go ahead.

Mehul Desai: So I have just two questions. One was, obviously, you have seen higher inflation in some of your raw materials specially in P&A. In that context, how do you see backward integration? What is your thought on backward integration? Do you see that as a possibility in the coming years or which as you would like to look at? And that's the first question. And second question on the packaging side, I think there were a lot of articles where in that have been mentioned about removal of monocarton. Do you see that as a material benefit coming to you guys also, especially on the lower end of P&A segment, maybe not starting in FY '23, but let's say in FY '24?

Pradeep Jain: Yes. let me take your first question, which is the backward integration. Look, nothing is off the table. Absolutely, nothing is off the table. However, I do want to share that our own experience is that you can get the same level of efficiency and benefit through aligned partnerships. But like I said earlier, nothing is off the table. In case we feel there is a great opportunity of backward integration, whether in partnership with someone, or on our own backing, etc., we won't shy away from exploring it and taking it further. So that will be the response to the first question.

Your second question, just remind me, Mehul, what was your second question?

Mehul Desai: On the removal of monocarton?

Pradeep Jain: On the removal, and just to close out the first question, I mean, the one classic example that we gave is that we have an asset-light model. So we have always preferred to get additional growth capacity through aligned bottling partners. Similarly, our entire Extra Neutral Alcohol footprint of co-location, etcetera, is always to third-party partners and aligned bottling partners.

Now on the removal of carton, we addressed that a couple of minutes ago. Yes, we have communicated that we shall be doing that over the next couple of quarters in a phased manner, starting with some brands and then gradually expanding to the rest of the portfolio. We will be in a better position to share more detail as we start taking those actions, starting let's say, in the January-March quarter.

Hina Nagarajan: But just to add, I would say that the removal of carton is driven partially by productivity and cost consideration, but to a very large extent, by a sustainability objectives. So, this is one big way of removing or reducing our carbon footprint and our Society 2030 goals, which you know are very aggressive. This is one of the big initiatives. And we are taking many more such initiatives to reduce the carbon footprint. So, I would say that this thought of removing the cartons has come even before this unprecedented inflation, and it is driven by that larger objective of sustainability.

Pradeep Jain: That's the primary objective. And obviously, in the secondary objective is that we will get some productivity, which in the current environment, we will not complain about.

Moderator: Thank you. The next question is from the line of Manish Poddar from Motilal Oswal AMC. Please go ahead.

Manish Poddar: Yes. So just want some clarity. If you could help me understand the ad spend, which you've done this quarter, how much of that would be for BII and BIO?

Pradeep Jain: We normally don't share a breakup of that. We can just say that, look, because BIO, some of the pricing discussions were on and our salience was a little low, we had consciously calibrated the A&P spending also in that segment, but normally, we don't share that level of detail. All we can say is leave the portfolio to us, we are committed to deliver the mid-to-high teen margin guidance on sustained basis.

Hina Nagarajan: And I would say that the A&P spend is really in service of brand equity of building the brand equity of all the brands that are focused brand for us. So when we renovated and innovated Royal Challenge American Pride, Royal Challenge with the Signature. So we are putting the A&P spend behind all the key brands that we are focusing on, Black Dog, which was renovated. And we drive a huge amount of effectiveness and efficiency out of the spend to ramp up our brand equity. And like Pradeep said, we have calibrated on BIO because BIO supplies pricing discussions were on. So quarter-on-quarter, I think we take those calls on which brands have the activations, which brands have some needs and keep it quite dynamic of allocation of A&P spend.

Manish Poddar: So here the two points to clarify. First is this 10% margin, this distribution margin, which we get is post allocation of ads spend, right?

Pradeep Jain: That's right. It's post allocation of ads spend and overheads also.

Manish Poddar: And overhead also. And let's say, with size and scale, I think this agreement was done somewhere around 2014-15 if I'm not wrong. So this means about seven, eight years now. So with size and scale, can we revoke this number? Or this is -- I understand this is a global business transfer agreement, which you've been alluding earlier. But with -- do you get operating leverage on this business that is what I'm trying to understand?

Pradeep Jain: So two responses. One is it's got nothing to do with the agreement signed earlier. Like I said, this is an independent global transfer pricing. So, there is an independent third-party benchmarking study that if an independent third-party distributor was to import these brands and sell in India, what kind of a margin will they need. So that's the rationale of why we get to 10%. Now coming to your second point, do we get operating leverage, we get significant operating leverage. Like we said, the 10% is after full A&P spending and after full overhead loading. And because these are very, very high premium price brands, they do absorb a fair amount of overhead. We've got dedicated sales team. We've got dedicated demand generation teams, etc. It's a fairly high-overhead structure model. So we get to absorb all that and then land the 10%, which we have said that on an EBITDA rupees per case as well as on a return on invested capital, which is highly accretive to our portfolio.

Manish Poddar: Sorry, what I'm trying to understand. Thanks for your explanation, what I'm trying to understand is let's say if you're doing x rupees in absolute number today, and let's say that x rupees becomes two x and that's the next two or three years, whatever the rate of growth and stuff is. I'm just trying to understand is if you make -- do you look at absolute margin or you look at EBITDA per case internally when you're looking at this math?

Pradeep Jain: So, in terms of what we are allowed to make? Right.

Manish Poddar: What are you allowed to make, let's say?

Pradeep Jain: Which is 10%. That's a variable number. It's a percentage margin number.

Manish Poddar: It's a percentage margin. That's right. Okay. And so even, let's say -- sorry, just to harp on it. So let's say, even if you double in size, you would still make a 10% margin only.

Pradeep Jain: It would make a 10%, yes. Absolutely. That's how -- Benchmark change and that warrants a change in the market.

Manish Poddar: Because your ad spend in all will get calibrated with size and scale. So I'm just trying to understand, does this margin number move up or that is static.

Pradeep Jain: Similarly, on overheads also we will get operating leverage.

Moderator: Thank you. Our next question is from the line of Gaurav from Goldfish Capital. Please go ahead.

Gaurav Mehta: Just want to understand your pricing negotiation that you have set on spots.

Pradeep Jain: There's a lot of background noise. We're not being able to tap the question.

Gaurav Mehta: So yes, so my question was on this price negotiation on spots that you're having with various states. Hypothetically, let's assume that in the next one year, the prices were to go up. So do we need to go back to the states where the price negotiation have already taken place? Or have you negotiated a mechanism wherein any inflation can be a pass through?

Hina Nagarajan: Well, to answer that, I wish... the second part was true. Unfortunately not. So the short answer is we do have to go back annually and negotiate the price increase again. We have not yet found a way to get the government to sort of set a mechanism where inflation link or whatever that you're alluding to. So yes, we will have to go back and negotiate every year till such time that we can find a reasonable mechanism with the government.

Pradeep Jain: What you have mentioned will be our desired end state.

Gaurav Mehta: But have you been signed for this?

Pradeep Jain: And we'll continue to advocate for that.

Gaurav Mehta: That's what I wanted to check and secondly, now that the sale of the category has been completed, and we'll be generating a lot of cash. Any thought process on what you want to do in terms of payout? Because you mentioned you need to recoup some of the losses. We are almost near that space. So you want to comment on how the payout would pan out in the next few years?

Pradeep Jain: Yes. So we are in discussions on how and like I said in the last call also, we would officially release our dividend distribution policy over the next three to four months as we are working through it. But just to give a broad dimension of numbers, when we exited March 22, we had accumulated losses of about INR 1,050 crores on our balance sheet.

Now in the six months, after incorporating the one-time profit from the sale of the divestiture, we have recouped about INR 750 crores of that, INR 750 crores to INR 760 crores. So that leaves about INR 300 crores, which, over the next couple of quarters, if everything remains as is, we should be able to recoup and therefore, we should be in a position to get back to dividend distribution by the end of this financial year.

Moderator: Thank you. This was the final question for today. If your question has not been answered, please feel free to contact Richa Periwal, Head Investor Relations. I will now turn the floor back over to Ms. Hina Nagarajan for closing remarks.

Hina Nagarajan: Thank you very much, and thanks to all of you for participating today and for all your questions. To wrap up, I would really like to say that I can best describe this time as a celebration of our culture. And a great example of how diverse experiences and perspectives drive growth and create value within our organization. We continue to be very focused on building on our current top-line momentum. We will continue to invest in and accelerate what's already worthy and explore future growth opportunities to further unlock value from our ecosystem.

Finally, I would like to express my gratitude to all for their continued resilience, passion, and ownership within our organization. And a big thank you to all of you for your time today and your ongoing partnership in support of our business. I wish you a really lovely festive season ahead. Thank you so much.

Moderator: Thank you very much. Ladies and gentlemen, on behalf of United Spirits Limited, that concludes this conference. Thank you all for joining us and you may now disconnect your lines. Thank you.