Acquisition of Paras's Personal Care business from Reckitt Benckiser

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Presentation Session

Moderator: Good evening ladies and gentlemen. I am Dennis, moderator for this conference. Welcome to the conference call of Marico hosted by Motilal Oswal Securities. At this moment, all participants are in listen only mode. Later, we will conduct a question and answer session. At that time, if you have a question, please press * and 1 on your telephone key pad. Please note this conference is recorded. I would now like to hand over the floor to Mr. Amnish Aggarwal.

Amnish Aggarwal: Good evening dear friends. I welcome you all to Marico concall to discuss the acquisition of erstwhile Paras Personal Care Business from Reckitt Benckiser. Today we have with us the top management of Marico, headed by Mr. Milind Sarwate, who is the Group CFO and CHRO, Mr. Saugata Gupta, who is the CEO of the Consumer Products Business and they are also accompanied by Mr. Chaitanya Deshpande : EVP and Head Investor Relations and M&A and Mr. Vivek Karve : EVP and Head Corporate Finance. I would now hand over the floor to the management to take the proceedings further.

Milind Sarwate: Good evening everybody. This is Milind Sarwate. I am pleased to be with you to have a call about the acquisition, documents of which we executed today. You must have gone through the media release that we issued. Just to capture the highlights, the brands that we have agreed to acquire include Set Wet, Livon and Zatak. You may be aware that these brands belonged to Paras Pharma earlier. And sometime last year, Reckitt Benckiser had a deal under which they had bought a larger basket of brands, out of which these few personal care brands are now being bought by us. The transaction involves certain structured steps towards Marico finally owning 100% of the company, which owns these brands. There are some statutory formalities to be completed, which will take anywhere between two and three months. So, our actual operation with these brands will commence in the first quarter of FY13. We have given some indication of the size of the business; it is at around Rs 150 crores for FY12. We have not been able to give precise idea of the consideration that we have paid for this, because the documentation does not allow us to disclose that. But, we are quite open to discussing the strategic implication of this deal and the value that we see it adding to ourselves. I would now hand over to my colleague, Saugata Gupta, who handles the consumer product business to say a few words on the brands.

Saugata Gupta: Yeah, good evening everybody. The current categories in which these brands operate are deos, gels and leave-on conditioners, All these categories are categories of the future. They have low penetration and they are currently at the bottom of the S-curve in the adoption cycle. And the penetration in India is low. In terms of the compounded annual growth rates over the past two-three years, the deo category is growing at around 40%, the styling gels around 20%-25% and leave-on conditioners at 22%. These brands essentially plug the gap in our portfolio in terms of having a portfolio addressed to youth. It fast forwards our journey into creating a portfolio of the future, by participating in more tailwind categories. It is expected to bring about capability synergies between our international business and the Indian business since we participate in each of these categories either in India or in some of the international businesses like Vietnam or the Middle East. We can thus leverage our bouquet of products and product offerings across the category as well as capabilities in terms of consumer insights, technology and other such capabilities. . So, we are reasonably excited about this acquisition. And we believe that these will essentially be some of our growth drivers in the future.

Milind Sarwate: Amnish, we can have the Q&A session now.

Question and Answer Session

Moderator: Thank you sir. Ladies and gentlemen, we will now begin the question and answer session. If you have a question, please press * and 1 on your telephone keypad and wait for your turn to ask the question. If you would like to withdraw your request, you may do so by pressing * and 1 again.

The first question comes from, Mr. Percy Pantakhi from Daiwa Capital.

Percy Pantakhi: Hi sir, congrats on the acquisition. Can you give us some idea on what has been the growth rate of these particular brands in the last two or three years and also in the last one year, that is the period after which Reckitt has taken them over and also some idea on the EBIT margins of these brands?

Saugata Gupta: Those brands have been growing in the last two years at around 20% and I am talking about the time including the transition time between Paras and Reckitt as well as currently in the hands of the Reckitt. .

Percy Pantakhi: Okay. So, the growth trajectory has not altered significantly after Reckitt has taken them over?

Saugata Gupta: Not really.

Percy Pantakhi: Okay. And this 20%, most of the brands are clustered around this figure or there has been a variation and 20% is the average?

Saugata Gupta: Obviously, there is a little bit of variation, but all the brands are reasonably on the growth track. In the last one or one and a half years, there have been few new offerings, other than Livon Hair Gain, which was launched during the last year, when the brand was with Paras. So, essentially the growth is organic.

Percy Pantakhi: Right. And on margins?

Saugata Gupta: Being in the personal care categories these offer attractive margins of 50% plus in terms of gross margins. The blended gross margins of the acquired portfolio is much higher than our current portfolio.

Percy Pantakhi: Saugata, my reference was more relating to the EBIT margins, rather than gross margins.

Saugata Gupta: We would not like to comment on the EBIT margins right now.

Percy Pantakhi: Okay. And it's been only about a year since Reckitt took this over, so would you be able to throw any insight as to why they are now selling off the brands to us?

Saugata Gupta: I think Reckitt, as far as what we know, feel that the OTC portfolio has a far more strategic fit. So, if you really look at the Reckitt portfolio globally, they essentially don't participate in these kinds of category. So, I think they are much more keen on the OTC part of the portfolio.

Chaitanya Deshpande: Percy, also as I understand it, when the first sale was done, from Paras to Reckitt, at that point in time they did not encourage joint bids, where somebody took one part of the portfolio and somebody took another. The condition under which it was sold at that time was, you have to pick up the entire package. And so when Reckitt went in with this, they had already decided that they would buy the entire business, but then hive this part off. They never intended to continue with this part of the business.

Milind Sarwate: Percy, in other words, there is no event which happened in last one year, which caused them to divest.

Percy Pantakhi: Understood. And sir, lastly I know you will not comment on valuation, but just one concern is that when Reckitt had bought this over, it was supposed, I mean it was talked about as one of the very expensive acquisitions on the street at that point of time. So, you mean that they would not have sold it off at a value substantially lesser than what they acquired? Do you have the same kind of concern that the purchase price probably could be one of the issues which would not leave too much on the table in terms of value accretiveness of the deal?

Milind Sarwate: Percy, may I ask you a counter question?

Percy Pantakhi: Yes sir.

Milind Sarwate: Do you believe that Marico will pay any amount for any acquisition?

Percy Pantakhi: Sir, absolutely not sir, that was not my inference. I am just trying to gain some perspective as to, if this is what meets the eye, I am sure there is something that I would be missing also. So, if you could just point out that something that I am missing?

Milind Sarwate: See, since the documentation precludes us from getting into details, let me tell you the philosophy. As I mentioned we are not the kind of macho company, which will pay any amount just to record an acquisition. That's the basic philosophy. Second, we have our own way of examining an acquisition in detail. And the amount of detailing we have done for this deal is huge. We believe that the price at which we have acquired is reasonable and it provides us enough elbow room to derive the maximum possibility, evident from this acquisition. Now, there are several ways in which you can look at the consideration. You can look at it as multiple of XYZ or you can look at it whether we paid a discount or a premium over what Reckitt might have paid. But, we have not got into that. We believe that the price that we have paid is a fair price, it leaves us enough room for creating value for our shareholders.

Percy Pantakhi: Right sir. And my last question, how will you finance this acquisition?

Milind Sarwate: See, there are two ways of looking at the financing. One is that, in the immediate run, the long term options are not readily available to any acquirer. So, in the short run we will have short term debt, which will be used to complete the acquisition process. Thereafter we would use a mix of equity and debt. We are yet to freeze the proportions. But, we have to also keep in mind that we also have our internal accruals in the form of war chest with us. We have liquidity. We have a certain internal mandate to maintain a certain level of liquidity, we will maintain that and the balance will be used to fund a part of the acquisition. So, net-net this would be a mix of internal accruals represented in a war chest, equity and debt. We have to keep in mind that not all times are good for equity and not all times are good for debt. So, we will have to work out a proper strategy, wherein we don't cause any destruction of value, because of the means of financing.

Percy Pantakhi: Sure sir, that's all from me. All the best and thank you.

Milind Sarwate: Thanks Percy.

Moderator: Thank you sir. The next question comes from Mr. Nikung Doshi from Bay Capital.

Nikung Doshi: This is Nikung Doshi here. Milind, I appreciate your point about you being conservative in valuation of brands and perhaps acquisition and rational of acquiring this brand. But, as an investor how one can decide whether it is a good acquisition or not, without knowing even EBIT margin or knowing what is the value? Because, everything is good at value, so I don't understand logic of not disclosing value.

Milind Sarwate: Nikung, I agree with your concern, but you have to realize that there are limitations to what details we can disclose. There are several issues, starting with the documentation part, also going into competitive confidential information. What I would also say is that, we are a very transparent company and through our periodic communications, we disclose a lot of details. When we close the accounts for this year, obviously a lot of details will be visible to an analyst. So, you will need to wait until then. Meanwhile, you could trust us that we have applied the right yardstick and as we are running an otherwise efficient business. I am not able to share specific data. For that matter, you would not find us sharing the EBITDA margins of all our brands. And in fact I doubt, which company shares the EBITDA margins brand wise?

Nikung Doshi: Okay, thanks.

Milind Sarwate: Thanks Nikung.

Moderator: Thank you sir. The next question comes from Mr. Nillai Shah from Morgan Stanley.

Nillai Shah: Sir, one question on this strategic part of this acquisition, post wash hair care, you do have a very strong brand in Parachute. You have the technology in terms of availability from your other businesses globally. Why not use that technology under Parachute brand to enter this business line? Why do we need to acquire something out here?

Saugata Gupta: Okay. There are two kinds of post wash hair care. One is in the area of nourishment and one is the area of styling. Parachute Advansed through its equity can definitely play in the area of nourishment, but perhaps not in the area of styling.

Nillai Shah: Okay. And the follow on question out there would be that if you are going to use debt to finance this acquisition in the near term, this obviously has to be domestic debt, right?

Milind Sarwate: Yes.

Nillai Shah: So, in that case will you still be, by using domestic debt, will this still be an earnings accretive acquisition as per your calculations?

Milind Sarwate: At this moment I would not comment on that.

Nillai Shah: Okay. And could you just talk about the yardsticks which you have applied internally, just a measure which you applied, is it a payback period you are looking at, is it ROCE that you are targeting to get to the valuation that you are talking about?

Chaitanya Deshpande: Typically what we apply as the first yardstick is discounted cash flows to arrive at the valuation and then we take a call on that number. Obviously, we will look at some of the other yardsticks as well. Coming to ROCE, having paid a price for an acquisition, it is very unlikely that you can match the ROCE of the rest of the business in the short term. However we do look at the likely ROCE, with the acquisition price in the denominator, going five or six years forward.

Nillai Shah: And that beats your cost of capital obviously.

Chaitanya Deshpande: Yeah, obviously. But in the first, maybe period of three or four years, it can't match of the ROCE of the average business for Marico. It will take longer.

Nillai Shah: In the next three or four years, will the ROCE match or beat the cost of capital that Marico has currently?

Chaitanya Deshpande: It can't. No, it will not match the ROCE in the next four years.

Nillai Shah: Alright, perfect. Thanks so much guys.

Moderator: Thank you sir. The next question comes from Mr. Aditya Soman from Goldman Sachs.

Aditya Soman: Yeah, quick couple of questions actually. Can you just share the market share for the key brands that you have acquired?

Saugata Gupta: Okay. The deo market share is around 6%. In the case of gel/cream, the market share of Paras brands is 24% And in the case of Livon conditioner it is around 68%. In addition to that there is a product called Livon Hair Gain now that obviously is a new product which is growing.

Aditya Soman: Yeah. And what would the market share in the styling gels be with addition of your products, your existing products?

Saugata Gupta: If you look at entire styling gels and creams, it will add another 11%, so it will be around 35%.

Aditya Soman: Okay, that's all. Thank you.

Saugata Gupta: Thank you sir.

Moderator: The next question comes from Mr. Abneesh Roy from Edelweiss.

Milind Sarwate: Yes, Abneesh.

Abneesh Roy: Sir, my first question is on the thought process, if you see deodorants 6% market share, if you see historically your strategic intent has been to be in categories in which MNCs are not there and you have a niche and a right to win. Could you explain in deodorant what is the right to win, because all the MNCs are there and what do you intend to do with deodorant, will it be a key focus area for you?

Saugata Gupta: If you look at global play, there is only one single MNC which is present in deodorants. We would not perhaps enter categories dominated by three-four MNCs where we don't have a right to win. . So, this is different. So, as I said, in a growing category and we have seen whether we have entered body care or we have entered the breakfast market, in a growing category you can participate in growth and be in the top three-four players. So, I think there are enough opportunities in the deodorant category to participate in this category. And Set Wet is a strong brand and Set Wet straddles across deodorant, gels and other male grooming categories. That allows efficiencies in of A&P spends. In addition to that, as I said, we do have a readymade portfolio of products and variants from our international business. This provides us a significant innovations pipeline which is ready to be transplanted into the Indian market.

Abneesh Roy: Sure sir, thanks, that's useful. Second question is, in deodorants you said that single MNC, could you tell us what is the market share in Recova? Recova definitely will have almost all the MNCs being present there. So, what is the philosophy on Recova?

Saugata Gupta: Recova is too marginal. So, as things stand now I think we do believe that almost 99% of the turnover comes from these three brands, which is Set Wet, Zatak and Livon.

Abneesh Roy: So, will it be fair to say that this will be a non-focus and maybe you would like to dispose it off over a longer timeframe?

Saugata Gupta: I think it is too early to comment on that. But, as I said that I think there is enough opportunity to grow in these three brands, which currently contribute to 99% of the sales.

Abneesh Roy: Sure. Sir, my next question is on the distribution side. Would we need to scale up in terms of say, salon distribution, currently how are we placed there and what would we need to do to fill up that gap, distribution gap?

Saugata Gupta: Essentially the channels that drive the category are cosmetic and cosmetic wholesale, chemists and modern trade. There is no separate salon channel, but salons buy from a wholesale. We have a presence in certain channels. There is about 80% overlap between the erstwhile Paras reach and that of Marico. So, I don't think there is too much incremental distribution to be had. For some of the channels the Paras hair fall product together with our body care product will provide critical mass and traction.

Abneesh Roy: Sir, my next question is on the margin side and the advertising side. Paras was creating all this business for selling it, so obviously the ad spend would have been much higher as a percentage of sales. So, now when this is part of your portfolio, we would also now need to step up. So, as a percentage of advertising, how does this compare with the existing line of business? So, some clarity on that if you can share.

Saugata Gupta: See, today first thing you must appreciate that these are growth categories. Number two, the gross margins of these categories are significantly higher than the weighted average gross margin of our existing portfolio. They do carry a certain A&P, but there are two things that are going to happen. In our hands where we already have a certain significant amount of A&P, with this incremental A&P, we will have significant efficiencies of scale in our A&P spends. Number two, our ability to straddle across various categories, so there will be a halo effect. For example, Set Wet participates in gels, creams and deos so there is a halo effect which is there versus participating in a single category. So, I think in our hands it will be perhaps far more efficiently spend and given the gross contribution and also mind you, what will also happen is we have a certain play in these categories with brands like Silk-n-Shine and Parachute After Shower, it will have even synergy in our cost structure for example. So, I think there are multiple synergistic benefits which will neutralize any demands for incremental A&P.

Abneesh Roy: And sir, two small questions, interest you said near term would be essentially domestic debt. But, over a medium-long term, are we looking at overseas debt also?

Milind Sarwate: For this particular acquisition we can not borrow from overseas. Over a medium term we will have to look at a judicious mix of local debt, equity and internal accruals.

Abneesh Roy: Sure. And sir, last question in terms of Kaya or maybe even Derma Rx, do we have a long term plan of using their technology and then rerouting through these brands, is that a possibility?

Saugata Gupta: I think the overlap between the offerings of Kaya and Derma Rx and this acquisition, is not significant.

Abneesh Roy: In the skin creams?

Saugata Gupta: No, not really. Between Set Wet, Zatak and Livon, I don't think there is any. The synergies are more with Vietnam business and the other portfolio here.

Abneesh Roy: And sir, what happens if the team who runs it, you retain the team, does some rationalization happen here? Are you able to cut cost on the distributor margins?

Saugata Gupta: Yeah. A few members of the erstwhile Paras team who are operating in Reckitt Benckiser will also work in our team. And I think it will be extremely helpful, because at the end of the day they have nurtured these brands and have grown these brands at high growth rate. It will add tremendous value to us.

Abneesh Roy: But, who heads it?

Saugata Gupta: It will be integrated into our consumer business.

Abneesh Roy: And any saving from distributor margins, any leeway to cut there?

Saugata Gupta: So, obviously there would be certain synergies where it gets integrated into the system, so I think there will be synergies right across.

Abneesh Roy: Okay, sure sir. Thanks and all the best.

Chaitanya Deshpande: Abneesh, just to provide a little more detail on what is envisaged in the transaction, once this takes place around three months from now, we have discussed a transition services arrangement with Reckitt,. So, immediately after the transaction gets fructified, , they would provide us distribution transition services over a three months period and then it gets fully integrated into Marico's distribution.

Abneesh Roy: Okay. So, no problems would be there in terms of distribution?

Chaitanya Deshpande: We don't anticipate any.

Abneesh Roy: Okay sir, thanks and all the best.

Chaitanya Deshpande: Thank you.

Moderator: Thank you sir. Participants are kindly requested to restrict with three questions.

The next question comes from Mr. Hemant Patel from Enam Securities.

Hemant Patel: Yeah hi, I have three questions actually. First one being, you said that the numeric distribution reach is quite high, so there is probably not much of gain which can be got from distribution extension. But, just was wondering whether the total number of outlets itself where these products are present, with this post wash hair, even the gels, are these likely to go up significantly?

Saugata Gupta: Yes, they will. Because, I think these categories are growth categories. And as with premiumisation across metros and the next set of towns and even in rural, these outlets will grow. So, what is also going to happen you must realize is that in certain set of outlets like cosmetic and chemists, our portfolio will attain a far bigger critical mass , enabling us to leverage our existing brands through these channels.

Hemant Patel: Okay. And if you were to put a number to the extension of the distribution outlets where they are indirect, could you let me know how much that is?

Saugata Gupta: As I said, I think there is already a significant overlap. So, it will be marginal in that way. But, what it will do is, it will increase saliency in these set of outlets.

Hemant Patel: Okay. Just one question in terms of the growth you mentioned that the category itself or the portfolio itself has been growing at 20% per annum. Do you envisage post bringing this portfolio under your fold and with the kind of new variants that have been launched in the last couple of, last year in fact, can it grow faster under your fold?

Saugata Gupta: I think our endeavor will be to ensure that it grows in line with the category growth rates definitely in the first few years. And as I said the category growth rates, deo has been around 35%-40%. In gel, it has been around 25% and in leave on conditioner it has been around 20%.

Hemant Patel: Okay. So, this wouldn't involve higher degree of brand investments post it is carved into your fold, right?

Saugata Gupta: As I mentioned some time earlier it will have lot of synergistic advantages, because we are straddling one brand across multiple categories. And even if you look at our A&P today, we already operate at 10% A&P with our turnover. It gets added to our A&P, so it gives provides significant efficiency. Yes, there will be certain immediate A&P of these categories, but as I said that the gross margin of these categories are extremely attractive it facilitates a higher A&P.

Hemant Patel: Okay. And one final question, was this a competitive bidding and to what level of comfort do we have in terms of the debt to equity level?

Milind Sarwate: Yes, this was a competitive bidding process and involved few rounds of bidding. On debt equity portion, I think we have a fair degree of comfort, because as I mentioned earlier, we did have a war chest in hand built out of internal accruals. So, we don't have to fund the entire acquisition through debt or for that matter even through equity. And as I mentioned, we will keep looking for the best option to, rather we would look at this requirement of funds along with our other funds and we will redraw our entire financing pattern, so that could involve some equity, some debt from India and some debt from overseas.

Hemant Patel: Okay. And would it involve even probably even dividend reduction as well?

Milind Sarwate: I think we are already operating at a very frugal level of dividend. I don't think we will tinker with that, because our payout is already quite low. In anticipation of acquisitions like this that we had moderated the dividend pay out. I don't think we would do anything significant with that.

Hemant Patel: Fair enough. Thanks a lot.

Moderator: Next question comes from Mr. Jamshed from Citi Bank.

Jamshed: Yeah hi, thank you for taking my questions. My first question is, could you just run through the market shares again? My second question is, when you look at these brands and the brand positioning vis-à-vis what you all have with Parachute Advansed and the body lotion, will these be flanking brands, because you seem to have indicated a couple of times that you are looking for critical mass. So, could you give us some sense in terms of or could you elaborate on that critical mass a bit?

Saugata Gupta: Just to repeat the market shares in deos it is around 6%, in styling gels it is around 29% and in leave on conditioners, Livon has a market share of 68%. When I talked about critical mass, I spoke about getting critical mass in certain channels where these categories are present and they have a higher weighted distribution, because of the throughputs will happen in channels where our existing portfolio also goes through. So, these are not flanker brands. If you really look at it, it is a market leader in both the segments of gels and Leave-on conditioners. And both these categories are growing at 20% plus. In the case of deo, it is a little more competitive, but as I said the category is growing at a far higher rate and it has already got critical mass with a market share of 6%. I also would like to mention, I think that Livon is also present in the Middle East and therefore we get opportunities for growth, both Livon and Livon Hair Gain in such markets.

Jamshed: Is it fair to say that in this Rs 150 crores top line, deo's will be roughly 50%, given that 6% market share on roughly 1000 crores category?

Milind Sarwate: Yeah, Jamshed, your estimate is correct.

Jamshed: Okay, alright. Thank you.

Moderator: Thank you sir. Next question comes from Mr. Vivek Maheshwari from CLFA.

Vivek Maheshwari: Hi, thanks for taking my question. My first question is, the 80% overlap that you mentioned between Paras and Marico looks very high. You reach roughly around 3.3 million outlets, right?

Chaitanya Deshpande: Vivek, just to clarify that; if Paras reaches 100 outlets, Marico reaches 80 of those outlets. We expect to get leverage from 20 of those outlets that Paras reaches today and Marico doesn't.

Saugata Gupta: So, therefore there are opportunities for example, if you look at the history of Paras, they have been traditionally strong in North and West, not so strong in South and East. That offers opportunities of growth in certain channels like modern trade also. .

Vivek Maheshwari: I see, okay. And the reverse would also be true, right?

Saugata Gupta: Yes total reach of Paras versus Marico would be significantly

Vivek Maheshwari: And would it be possible to get that number, against your 3.3 million outlets, how many outlets they would be reaching?

Saugata Gupta: Paras is around 0.7 million.

Vivek Maheshwari: I see, okay. So, they are just 0.7 million you are saying, right? And is there a huge urban bias for these kinds of categories which essentially means that these will be primarily urban centric?

Saugata Gupta: They are currently urban centric, but as you realize that with increasing rural prosperity and disposable income and convergence of aspirations, we believe that there is tremendous potential for the growth in the next set of towns and in rural markets.

Vivek Maheshwari: No, but still 0.7 million versus 3½ million clearly signifies that if you want, obviously if the market can absorb that, then you can actually see significant penetration in these, with Paras brands. So, 0.7 million can easily go up to 2X, 3X, 4X, depending on how much the market can absorb. Is that a fair thought process?

Saugata Gupta: I will give you some pointers. Suppose if Paras brands today reach 2.7 lakh outlets in gel, the gel category has a total reach of around 6.2. Therefore there would be headroom for distribution extension, given our distribution strength.

Vivek Maheshwari: Understood, okay. And how big is hair gel and hair cream as a market separately?

Saugata Gupta: In terms of market size?

Vivek Maheshwari: Yeah.

Saugata Gupta: Deo is around Rs 1100 to Rs 1200 crores; styling gels and creams, around Rs 190 to Rs 200 crores and leave-onconditioners around Rs 80-85 crores.

Vivek Maheshwari: Okay, Rs 80-85 crores. And how is Paras structured in terms of production? Do they have their own facilities or they have contractors who do the stuff for them?

Saugata Gupta: It's a mixture of both. And as I said, since we also participate in most of the categories, we also currently have manufacturing capabilities on most of them, within own manufacturing and third party.

Chaitanya Deshpande: Just to be a little more specific on that, the deo production is outsourced by them, which we will continue to do. And the rest of the major production is hair creams and gels, where again they have offered to provide support to us over about a four months period, which we will avail of and then transit production to our own factory.

Vivek Maheshwari: I see, okay. And just one last, may not be a question, but an observation, see it's a key, there are three key brands in, it's not a single brand company right? So, I still don't understand what is the rationale for not giving EBITDA margins. I understand about the purchase consideration, but at least from the EBITDA margin perspective, considering that it is a portfolio of many brands, of which three are very important.

Milind Sarwate: I appreciate that this data would have helped draw up a complete horoscope of these brands. But, look at it this way that from our side we have disclosed that the gross margins are significantly high. They are higher than even our average portfolio. Now, it depends upon how we are going to farm these brands in the future that will drive the ASP that will drive the variable expenditure that we will make on these brands. So, the EBITDA margin would also vary in the years to come. From a strategic perspective, I feel that it is critical to look at how the gross margins behave and have those sustainable in the long term, we are convinced on that. And hence we don't want to give more details, because we have to realize that it's a competitive world and we don't want to provide far too many details on this call or a similar forum.

Vivek Maheshwari: I see, I understand. Thank you very much and all the best.

Moderator: Thank you sir. The next question comes from Mr. Ashit Desai from B&K Securities.

Ashit Desai: Yeah, hi sir. Congrats on this acquisition. Just two questions. One is, you mentioned about some synergistic benefits between India and your international business, if you could highlight these and also what is the current presence of these products in the international markets?

Saugata Gupta: Okay. Paras brands, particularly Livon are available in the Middle East and Bangladesh through the exports / distributor route. Both Livon and Livon Hair Gain have potential in some of the international markets we operate in. It terms of synergies, we do have an innovation pipeline under Code 10 in Malaysia that can be leveraged.

Ashit Desai: Sir, could you share what is the percentage of revenues that come from these markets, if it is sizable?

Saugata Gupta: Which one, the international market?

Ashit Desai: Yeah.

Saugata Gupta: Right now very negligible, since Paras had only started to seed the market.

Ashit Desai: Okay. Sir lastly, looking at your portfolio mix, 50% of your revenues come from deos, which is a highly competitive market. Going forward which of these brands you feel have a very strong opportunity and a positive one and whether this mix will change over the years?

Saugata Gupta: Growth rate of deo is around 35%- 40%.Zatak plays in the mass end, while Set Wet operates in the premium end This provides us leverage to participate at both ends of the market. And while I agree deo is competitive, it's a very high growth category and we do have significant capability, specially with existing Paras brands and also through our X-Men portfolio in Vietnam in terms of innovation. Therefore we are confident of being able to grow in line with the category and also start gaining market share.

Ashit Desai: Okay. Could you give an idea how the deo, your deo's market share has moved over the last three-four years?

Saugata Gupta: It's has been at the same level in the last year.

Ashit Desai: Okay. Sir, just one last clarification I wanted, Paras personal care also included Borosoft, your acquisition doesn't include that?

Saugata Gupta: We have the trademarks, but the brand is currently not active.

Ashit Desai: Okay, thanks a lot sir.

Moderator: Thank you sir. Next question comes from Mr. Sirish Pardeshi from Anand Rathi.

Sirish Pardeshi: Hi Chaitanya and Saugata, Milind, congratulations for this acquisition.

Milind Sarwate: Thanks Sirish.

Sirish Pardeshi: Just couple of questions and a clarification, you mentioned this Rs 150 crores is FY12 revenue, I would assume that this deal is happening post March, or is there any part of sales will be booked by you guys in this financial year?

Chaitanya Deshpande: This is the estimated sales up to the year ending March 2012. This is only an agreement to buy. We have not made the acquisition as yet. There is a demerger process in Paras that is on. Once this business gets demerged into a separate company, that is when Marico will actually step in. So, like Milind was saying, this is estimated to happen about three months from now. So we would have actually acquired the company, around May or June 2012. We cannot be precise at this point in time as we have to depend on progress on the court process for the demerger.

Sirish Pardeshi: Okay. You also mentioned that this will fit in, in the international portfolio. So, in this Rs 150 Cr, how much is the export part or international business for Paras?

Saugata Gupta: As I said it is negligible, it is less than 1%. Two years ago, they had sold worth Rs 10 crores. Obviously when the merger happened, Reckitt Benckiser concentrated on integrating the Indian business. So, right now the international business is negligible. We feel that there are opportunities which can be tapped.

Sirish Pardeshi: Okay. The other question I have is that, now if you look at the Marico strategy last one and a half, two years, you have been saying that personal care, post wash, these are the segments. Do you think now getting into the deo space, which is quite competitive and the original promoters of Paras is also been aggressive in that space with the brand differentiation, which is not gas and actually deo, do you think that this brand investment would be significantly higher or probably it would be like, you would be getting vanished, because you are just 6% of the market share?

Saugata Gupta: See, at 6% we are number three actually. It is a fragmented market. There is a lot of grey market today. But, the market tends to consolidate when main line players start participating in the market and specially the fact they participate at both ends of the market by straddling different price points. In the long term there is consolidation and this is seen in any personal care category across the globe.

Sirish Pardeshi: Okay, just last one question I am pushing, assuming that you have a 30% EBITDA margin and would be EBITDA of say, 50 crores, would this acquisition would be higher of 20 multiple or would be less than that?

Chaitanya Deshpande: It doesn't have a 30% EBITDA margin; it will be lower than that.

Sirish Pardeshi: Alright, thanks. Congrats and best of luck.

Chaitanya Deshpande: Thank you.

Moderator: Thank you sir. The next question comes from Mr. Pankaj Trewal from Kotak Mutual Funds.

Pankaj Trewal: Good evening. Couple of things, before we discuss this acquisition, as a share holder it will be worthwhile to gain more confidence on the execution ability on the inorganic side of the company, if you take us exactly in January-February of 2006, when we acquired Nihar. At that time it was a much talked acquisition where we paid Rs 240 crores around for Rs 120 crores turnover company. And if my memory serves me right, lot of value was expected to be created in the medium to slightly long term. But from my rough calculation and I may be wrong, suggest that we haven't broken even in that acquisition still, though we may argue on the synergy benefits may come in. So just to get some more confidence on your this acquisition per se as a shareholder, can you help us understand how the value has been created for the shareholder in your past acquisition and can we expect a good breakeven say, five years, six years down the line? That's first. And second, I am sure there must be a lot of intangible that will be created. Earlier your company policy was to not maintain intangible in your books of account and depreciate it fast and as a result, you got a tax shield last time when you did an acquisition of such a high amount. That was in 2006. Could the same policy be followed this time around in this acquisition as well? Thank you.

Milind Sarwate: This is Milind here. I will say a few things on acquisition policy. Firstly, I don't think acquisition decisions are taken in excel sheets. They will have to be taken at strategic level. And if we have to achieve sustainable profitable growth over the long term, then accounting statements for any particular period will not be relevant, because those may not bring out the strategic value of whatever we acquire. So, as far as this deal is concerned, as Chaitanya explained sometime ago, we have adopted a set of evaluation parameters, all of which suggest that there is a very strong strategic fit of the portfolio to our current portfolio. It is a high margin portfolio. It is in an emerging segment, where we had a gap. So, it fits into our portfolio very well. It is not too far away from our current business configuration, so integrating is not going to be difficult. So, we hope that with all these factors we would be able to create significant value for the long term shareholders.

Pankaj Trewal: I have been shareholder for last six years and I am happy with the performance of the company. I am not complaining, but I am just saying I am trying to understand in more detail that your past acquisition was the most talked about acquisition.

Milind Sarwate: The Nihar acquisition has created immense value for us, not only in the brand Nihar itself, but by completing the portfolio in our perfumed coconut oil segment as also the pure coconut oil segment and giving us a strong foothold in East India, especially Bihar. So, there is huge value created. And we can always separately meet and we can take you through the details. Now, coming to this acquisition, I think it will take a while for the market and all shareholders to appreciate the strategic relevance of this acquisition. As of now, we are happy that we have gone into details, both at the strategic level as also the operational level. So, we are quite confident this strategic fit and confidence that we have as regards to our right to win in these categories. I think these are good enough at this stage. As you go along, you will get more details. We will come out with our annual report, in that you will have lot of details and then we can get into specifics.

Your second question was about intangibles and how will we depreciate them. I think that leeway that companies had earlier of offsetting intangibles against accumulated reserves, may not be available anymore. And we also may want to treat things differently. So, anyway these things will come out in the accounting policies when we publish our annual accounts, which is not too far away now, it's just about 45 days from now.

Pankaj Trewal: Sir, if I understand correctly, the tax shield component has gone into the calculation of the acquisition price. I am sure that intangible on the depreciation will provide to tax shield as well, so that has gone into that component on calculation of the acquisition.

Milind Sarwate: We are acquiring shares of a company which holds these brands. Therefore we cannot claim depreciation.

Pankaj Trewal: No, in the intangibles which will be created in the books of accounts.

Vivek Karve: Just one clarification. The acquisition will create goodwill, which will be on consolidation.

Pankaj Trewal: That's what I am saying.

Vivek Karve: Yeah, goodwill does not give any tax shield.

Pankaj Trewal: Okay, fair enough. Thank you, thank you so much.

Moderator: Thank you sir. The next question comes from Mr. Rohit Gajare from UTI Asset Management.

Rohit Gajare: Hello sir, some book keeping questions. How much will be the debt on the balance sheet as on December?

Vivek Karve: About Rs 800 crores.

marico
be more. every day.

Rohit Gajare: And how much is the cash?

Vivek Karve: It is about Rs 400 crores.

Rohit Gajare: And is it right to assume that the acquisition takes another three, maybe three months from now that any capital (not sure) from debt or otherwise, would be at that time only, right now it is too early to debt that for that, right?

Vivek Karve: In The immediate plan would be to raise the debt and we also have some war chest in terms of liquidity. We will take a call on raising equity at a slightly later stage. Yeah, just one clarification, you asked us about the gross debt and gross cash. So, the gross debt as on 31st of December is about Rs 800 crores, while the cash is about Rs 400 crores as a result the net debt is about Rs 400 crores.

Rohit Gajare: Thank you very much. Thank you very much.

Moderator: Thank you sir. The next question comes from Mr. Yogesh Bhatia from ICICI Prudential.

Yogesh Bhatia: Hi team, Chaitanya. Yogesh here. Good evening. Just one question. What we understand is this Paras acquisition by Reckitt was done in April 2011. And we have been hearing in the market place, the other bidders also who were willing to buy these portion of the business. So, according to you the Rs 150 crores expected FY12 revenue, would it be little bit on the subdued side, in the sense that the concentration of the company to focus on these brands which anyway they are going to sell, would be little lower than the normal, the other OTC business which they have bought?

Milind Sarwate: It may be in some way, because normally when brands get transited from one company to another, there are some transition hiccups. But, I think whether it was Paras to Reckitt or now it would be Marico, I think the focus on these brands has been fairly strong. So, while what you say is right in parts, there may have been some loss of value, but it is not significant to impact the long term potential of these brands.

Saugata Gupta: Just to add, basically what Milind is trying to say is that, there could be certain integration issues which does happen, because there were two systems. But if you really look at it, now it is fairly integrated at the Reckitt's system. And Reckitt system and Marico system are similar in terms of the distribution. So, the handover will be far smoother.

Yogesh Bhatia: Okay. And another last question. This 6% market which you just mentioned and we have been hearing you guys that unless you become number one, number two and then, so that strong position which you normally look at, so is this the same path which here also we would be looking for say, next three to four years time or do you see more of the MNC's still coming here and playing their game? As you mentioned that there are only one MNC right now present in the category.

Saugata Gupta: Interestingly, across global markets in the deo category only one MNC has a dominant presence. There are other MNC's which don't play in the mass, they might be playing in the very niche top end of the deo market. Again in deos, we are playing essentially in the male deo market. Now, in a growth market, I think there is enough space for at least three to four players to grow. As the market matures, there are only three to four players that consolidate the market share between them. So, right now for example, the market leader has a market share of around 17%, Paras with 6% share is a very close number three. The number 2 brand has a 7% share. So, it's a very extremely fragmented market. So, I think with focused inputs and focused presence, there is potential to gain market share.

Yogesh Bhatia: Okay, thanks. Thanks and all the best sir.

Moderator: Thank you sir. The next question comes from Mr. Prakash Kapadiya from I Alpha Enterprises.

Prakash Kapadiya: Thanks for taking my question. Sir, what kind of seasonality would there be in deodorants as a category? I guess this will be a fairly summer product. And if you could share your some mix in terms of the category between men and women in India for the deo market?

Saugata Gupta: It's around 60-40 in favor of men in deos, but both segments are growing at around 35% to 40%. Yes, there is a seasonality, but it is not very pronounced as compared to some of the other categories like cooling oil or a body lotion. And as the category matures what happens is that, you need to be all round. In fact in lot of developed markets and temperate climates, there is an opposite seasonality with an increase is deo usage in winter.

Prakash Kapadiya: And sir, in terms of positioning this obviously would be a mass market for Paras, so the price point would be what, Rs.100 or would it be more?

Saugata Gupta: There are two price points, one where Zatak operates, these are the mass point. And there is Set Wet, which operates as a semi premium and which is more in line with some of the other players in the category.

Prakash Kapadiya: And sir, if you could give some sense on the hair serums, is that a professional salon driven market and what is the typical pricing difference in terms of hair oil or hair conditioner and a serum?

Saugata Gupta: This is a home use post wash segment. And it is priced at least around 3X to 3.5X times of conditioners or 4½X times hair oil. So, to give you a perspective, Livon is priced around 180 bucks to 200 bucks for 100 ml. And Silk-n-Shine which is our offering is priced at 160 for 100 ml. Hair oils are around Rs.45 to Rs.50 for 100 ml.

Prakash Kapadiya: Okay sir. Thank you. All the best.

Moderator: Thank you sir. Next question comes from Mr. Richard Liu from JM Financials.

Richard Liu: Hi, thanks for taking my question. Firstly, on the margin front I understand that you won't be sharing data on that, but just to get a perspective, would it be fair to assume that once you have synergized the acquisitions sufficiently, you would be able to eliminate large part of the other expenditure, the fixed cost of the business, such that a higher portion of the gross margin flow through to your bottom line ultimately, given that large part of distribution and other fixed cost could be common, is it a fair assumption over the next, once you have done the synergies?

Saugata Gupta: I think we will be gradually gaining some synergies as we integrate over the next couple of years.

Richard Liu: No, considering that your products are pretty similar in distribution profile to your existing ones and I guess, at one point in time, it might even be possible for you to eliminate almost the whole fixed cost, which is currently sitting in this entity, which you won't have to incur when it becomes part of Marico. Is that one of the options, apart from A&P maybe, where you will obviously need to spend?

Chaitanya Deshpande: Yeah, Richard that's right actually. So, in the entity itself there isn't much activity right now . So upon assets such as trademarks and some molds etc. for the packaging material will come to the entity that Marico will acquire. We are not acquiring any factory, or large number of personnel. Just a few key people are moving. And once we integrate it into our system, most of this will flow through our distribution system and field force. The incremental cost that we may incur in terms of adding numbers in distribution for instance, I agree with you, will be marginal.

Richard Liu: So, would it be fair to assume that, what we call gross margins less the A&P spends, a very marginal fixed cost, would therefore be the EBITDA margin of this business or of this set of business?

Chaitanya Deshpande: Yes, that is correct.

Richard Liu: And that is what your acquisition assumption is based upon?

Chaitanya Deshpande: Yes.

Richard Liu: Okay sure, that's helpful. And number two, in terms of the number of categories that you are working with right now, I think would it be fair to assume that or would it be fair to question that you are probably spreading yourselves a bit too thin and how the organization is gearing up itself to deal with all these, because the number of categories would I guess suddenly expand?

Saugata Gupta: See, we already are present in the leave on conditioner category, we have a brand called Silk-n-Shine, which is an extension of our brand Hair and Care, where we have already got a 23% market share. In terms of styling gels and creams, through After Shower we are already present in that category and we have a 11% market share. So, both the categories we are present in, so we are not adding any this one. Deodorant is a new category. We are not creating any new brand, but Set Wet straddles across that. So, actually the only new category obviously will be deo. As I mentioned earlier we have the advantage of an innovation pipeline through our presence in some of these categories in our international markets. We had also reckoned some of the new categories in which to enter in the domestic market over the next three years or so. This opportunity has fast forwarded some of those plans.

Richard Liu: Okay. And I don't, one more question if I may, I don't expect a straight answer from you. Does this make your scouts for acquisition a little slower or you are still hungry for more?

Milind Sarwate: I think we have always been an acquisitive company. This will not change significantly. See, let's look at it this way, we believe that if we have good acquisition opportunity, we will always be able to fund it appropriately through equity or debt. We have rarely gone out and spoken about a number available for acquisition. We don't really have a budget for acquisition. If we have a good acquisition, I think it will create the budget for itself.

Richard Liu: Okay sure. Thanks for taking my question. All the best.

Milind Sarwate: Thank you.

Moderator: Thank you sir. Next question comes from Mr. Sai Das from Pari Washington.

Sai Das: The number that you gave for the MNC, they command 70% to 80% of the deo market?

Saugata Gupta: No. It is 17%-18%

Sai Das: Alright. So, he is 17% to 18%, the second player is 7% and the third player is 6%.

Saugata Gupta: That's right.

Sai Das: And the rest is unorganized?

Saugata Gupta: Yeah, or mostly as I said, there are lot of gray market players.

Sai Das: Okay, lot of gray market, by that you mean sir?

Saugata Gupta: I think there are two kinds of deo's sold in India. One is, the ones which are manufactured in India by organized players and the other one could be unorganized or sporadic players. There could also be market for imported deo's, which is what is popularly called as the gray market. But, I think the key factor about this market is that there is a long tail. If you add up 17, 7 and 6, you get 30, so the balance 70% is made up of several small players, none of whom is significant to be reckoned with , beyond 1% or 2%.

Sai Das: And you can attack them, okay, great. Great, thank you. Thank you sir, thank you very much.

Moderator: Thank you sir. The next question comes from Mr. Ashish Upgalawar from Spark Capital.

Ashish Upgalawar: Yeah, similar question again relating to the deo space. It's a difficult space and if you compare to your brand with Parachute, it is very, very strong and it's a very, very different play in deos. How do you think it will be possible to maintain brand sale in this category, given this gray market and pricing differentials and many other term that we have here? And would you game plan this something different from the owner's, Paras had nurtured…?

Saugata Gupta: I would say two things. In the evolution of these kinds of categories across global personal care market, it always starts like that. and There are lot of local players and when an MNC and one or two large FMCG players start participating in the category, invest behind A&P, the market share consolidates. You would have seen it even in India in processed food categories like oats for example And secondly, I think I have been repeating this; we do have a pipeline of potential innovation. We use an open innovation model in our international market. So, we don't have to actually conceptualize and execute an innovation, unlike other categories. We are almost placed like MNCs where a battery of products and product portfolio already available in international market which we can be transferred.

Ashish Upgalawar: Okay. So, can we say that this product portfolio will be expanded under the brands Zatak and Set Wet by bringing Xmen maybe innovation from there to India?

Saugata Gupta: Yes since these brands have been invested in and they have high degree of saliency and equity today, especially Set Wet. It is one of the fastest growing brands in this segment.

Ashish Upgalawar: Okay. And sir, when you said that the acquisition will be funded by equity, internal accruals as well as debt, so equity does not mean dilution, it is rather internal accruals, right?

Milind Sarwate: No, it could be a mix of both.

Ashish Upgalawar: Okay. So, some dilution may also be there?

Milind Sarwate: We have some internal accruals readily available in the form of war chest, we might use that and debt and equity. So, the mix we will decide as we go along. But, it will not be a lopsided mix of these three.

Ashish Upgalawar: Okay. Sir, finally wanted to understand your views, since we are expanding into personal care and the body care lotion plus now deo's, so where does Marico lay its outlines in terms of expanding into personal care and which are the target areas probably that we can understand from here?

Saugata Gupta: See, I think we have a framework where we talk about market attractiveness and a right to win. And we will look at categories which are essentially low penetration, at the bottom of the S-curve and about to hit an inflection point. And where there is, in terms of competitive intensity, would perhaps avoid categories where there are three or four dominant MNCs. So, one single MNC is okay. I think that is where we would like to operate.

Ashish Upgalawar: Okay. Any other international synergies that you would be seeing for these brands, you spoke about Vietnam?

Saugata Gupta: Besides the X-Men portfolio in Vietnam, we also have a portfolio of male grooming products under Code 10 in Malaysia.

Ashish Upgalawar: Okay. So, these would be used rather for innovations, rather than bringing those brands here?

Saugata Gupta: See, finally the brand is what you attach to the underlying product. The product actually serves the consumer needs. What we available are product formulations and product packaging formats and so on.

Ashish Upgalawar: Okay, got the point. Thank you so much sir, thanks.

Milind Sarwate: Thank you.

Moderator: Thank you sir. The next question comes from Mr. Naveen Trivedi from Pinc Research.

Naveen Trivedi: Hi sir. If you can share the volume growth number of these brands for the last one year?

Saugata Gupta: The portfolio grew by around 20% in the last two years, there was very little inflation in the portfolio. So, majority of it is mostly volumes

Naveen Trivedi: Okay. My next question is, is there any addition of the depreciable assets?

Milind Sarwate: No, there won't be any.

Naveen Trivedi: Okay. Another question is that, is there any significant difference between the personal care margins as well as compared to all the Paras Pharma EBITDA margins?

Milind Sarwate: We don't have that data.

Naveen Trivedi: But, just to compare the personal care business as well as the healthcare margins, if you can just share or indicate some kind of…

Milind Sarwate: I don't think we are concerned with what margin Reckitt was making or what Paras was making, we are concerned with the margins available on these products..

Naveen Trivedi: Sure, sure. The last question is, if I want to understand the rationale of this acquisition, then the acquisition was because of the sales of potential or scope of margins format or tax valuation, the key things if you can share?

Milind Sarwate: We went for this acquisition because it has a very good strategic fit. We find that it addresses the gaps that we had in our portfolio. And we believe that this will enable us to strengthen our offering of sustainable profitable growth. So, fundamentally it is a strategic acquisition. It's effect on margins is going to be positive, because strategic placement gives it a strength to contribute to our margins.

Naveen Trivedi: Okay, yeah, thank you so much sir.

Milind Sarwate: Thank you.

Moderator: Thank you sir. There are no further questions. Now I hand over the floor to Mr. Amnish Aggarwal for closing comments.

Amnish Aggarwal: Yeah, I would like to thank the management team of Marico for sharing with us the details of the acquisition and how they perceive the future to be for the new business. I would like Milind to give some final comments and after that we will close this call.

Milind Sarwate: Amnish, thanks for anchoring this call. We had a very engaging set of questions and answers. I hope we have been able to within the limitations that we have put by the documentation, reach out and give as much information as we could. We hope this was useful and we will stay in touch with those who want to meet us or talk to us offline. So, thanks a lot and have a good time ahead. Good night.

Moderator: Thank you sir. Ladies and gentlemen, this concludes your conference call. Thank you for your participation and for using Door Sabha's conference call service. You may disconnect your lines now. Thank you and have a pleasant day.