



November 29, 2016

To  
The Manager  
The Department of Corporate Services  
BSE Limited  
Floor 25, P. J. Towers,  
Dalal Street, Mumbai – 400 001

To  
The Manager  
The Listing Department  
National Stock Exchange of India Limited  
Exchange Plaza, Bandra Kurla Complex,  
Bandra (East), Mumbai – 400 051

**Scrip Code: 539450**

**Scrip Symbol: SHK**

Dear Sir/ Madam,

**Sub: Submission of transcript of conference call under Regulation 30 of Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements) Regulations, 2015**

Pursuant to Regulation 30 of SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015, we hereby submit transcript of Q2 FY17 Earnings conference call for investors and analysts organized by the Company on Wednesday, November 16, 2016 at 11.00 AM IST.

You are requested to take note of the same.

Thanking you,

Yours faithfully,  
For **S H Kelkar and Company Limited**

  
**Deepti Chandratre**  
Company Secretary & Compliance Officer



*Enclosed: As above*



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## **S H Kelkar and Company Limited**

### **Q2 & H1 FY17 Earnings Conference Call Transcript**

#### **November 16, 2016**

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**Moderator** Ladies and gentlemen, good way and welcome S H Kelkar and Company Limited Earnings Conference Call. As a reminder, all participant lines will be in the listen-only mode, and there will be an opportunity for you to ask questions after the presentation concludes. In case you need assistance during this conference call, please signal an operator by pressing '\*' then '0' on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Anoop Poojari from CDR India. Thank you and over to you, Mr. Pujari.

**Anoop Poojari** Thank you. Good morning, everyone. And thank you for joining us on S H Kelkar and Company Limited Q2 & H1 FY2017 Earnings Conference Call. We have with us Mr. Kedar Vaze – Whole Time Director and CEO of the Company, Mr. B. Ramkrishnan – Head (Strategy) and Mr. Tapas Majumdar – CFO of the Company.

We will initiate the call with opening remarks from the management, following which we will have the forum open for a question-and-answer session.

Before we begin, I would like to point out that some statements made in today's call may be forward-looking in nature and a disclaimer to this effect has been included in the Earnings Presentation shared with you earlier. I would now like to invite Mr. Kedar Vaze to make his opening remarks.

**Kedar Vaze** Good morning, everyone, and thank you for joining us for our second quarter and first half financial year 2017 earnings call. I will begin by taking you through the operational and financial highlight for the quarter and then look forward to taking your questions and suggestions.

I am pleased to share with you that we have reported strong results on the back of healthy contribution from both Fragrances and Flavors business. In the first half 2017 our total income increased by 17% to Rs. 501 crore and growth on constant currency basis was 16%. The EBITDA improved by 36% to Rs. 95 crore. PBT doubled to Rs. 82 crore and PAT grew by 95% to Rs. 52 crore. We have reported this strong growth on the back of solid performance in the domestic market. Revenues in India grew by 26%, which were primarily assisted by robust demand and better realizations Our performance in the overseas market was subdued with just 1% growth in this period.

The Fragrance division reported 9% growth in the first half, while our domestic revenues were up 19%, overseas revenues were lower by 8%. Overseas business reported subdued

performance owing to slower demand in key markets and reported lower realizations due to depreciating foreign currencies, particularly in the MENA region, Africa, Middle East region. However, the division registered a notable 41% growth in profitability and margins improved 400 bps to 16% in first half compared to 12% in first half 2016. This was in line with our strategy to focus on margin growth rather than only top-line growth in some of these markets where we perceived higher credit risks.

In the first half 2017, the Flavor division registered a robust 144% increase year-on-year to Rs. 57 crore, both domestic and export registering a good growth, 178% and 109% respectively.

Our recently concluded acquisition of HTT along with significant off-take in the domestic and overseas market enabled us to report such healthy performance in the flavor segment. The business registered healthy growth in profitability at Rs. 14 crore, up 190% with margin improving to 24% compared to 20% in first half last year. In addition to HTT, we also recently announced the acquisition of Gujarat Flavors Private Limited where we have executed the business transfer agreement and expect the complete process of integration over the next few months. GFPL is a Vadodara based 34-year-old company in flavors with a top-line of Rs. 10.5 crore reported for last year FY16. These acquisitions are in line with our plan to pursue strategic tuck-in acquisitions to increase market share and consolidate our operations of these businesses to organically penetrate the domestic flavor market.

Overall, we continue to believe there is huge potential for growth in the Indian food industry which is yet to surface. Over the past few years the food sector has emerged as a high growth and high profit sector due to the immense potential for value addition, particularly within the food processing industry. With the Food Safety and Standards Authority (FSSAI), becoming very active in recent times and plans to further strengthen its testing infrastructure in the country, we believe it will be a bonus and a good environment for organized players like us to operate. This will provide organized larger players opportunities to either acquire smaller competitors and/or simply expand our presence in the local market in a better regulated environment.

Coming to our operating profit, EBITDA during first half 2017 improved by 36% to Rs. 95 crore and margin expanded to 19% as compared to 16% in the corresponding period last year. Margin improvement was primarily due to higher realizations and better raw material buying efficiencies. Increase in volumes has also helped us improve our margin performance, given the operating leverage in our business. The PBT was up by 100% to Rs. 82 crore. Notable savings in interest cost, lower depreciation charge and change in policy for accounting R&D expenses helped improve PBT ahead of the EBITDA. Net PAT also grew by 95% to Rs. 52 crore versus same period last year.

To conclude, SH Kelkar and Company is an R&D driven company and our investments here will continue to drive innovation and growth going forward. We are confident of our business model's ability to leverage on the growth and deliver above industry growth rates. We will continue our focus on increasing our market share in India as well as other emerging markets. We believe our leadership position in a very niche fragrance and flavors industry will enable us to create sustainable value for all stakeholders.

I look forward to your questions and suggestions.

**Moderator**

Thank you very much. Ladies and Gentlemen, we will now begin with the question-and-answer session. Our first question is from the line of Kunal Jagda from Keynote Capital. Please go ahead.

- Kunal Jagda** Sir, my first question is related to the fragrance business. Sir, considering that GCPL has introduced quite a few new products in its HI segment, how do you look the demand going forward and how it will impact your revenue growth and how much realization do you expect in this line?
- Kedar Vaze** So when you say GCPL, Godrej Consumer Product household insecticides?
- Kunal Jagda** Yes sir.
- Kedar Vaze** So like GCPL most of the FMCG companies who are our customers have been continuing to innovate and introduce new products in the market. We do not speculate or guide on a specific product-by-product or company-by-company discussion, only to say that we have more than our fair share of new products being introduced in the market which will allow us to continue to grow our business in the future.
- Kunal Jagda** So how it will drive your revenue growth and what is the expected realization that you expect in this line?
- Kedar Vaze** In household insecticides specifically?
- Kunal Jagda** No, means overall FMCG sector.
- Kedar Vaze** So our overall organic growth this year this period has been 14% over last year, taking out the like-for-like. And we will continue to be able to sustain that kind of growth level going forward.
- Kunal Jagda** And if you can just share what would be the realizations or how much you are currently, what is your realization at current stage?
- Kedar Vaze** I am not really sure I am understanding the question, realization in terms of gross margin, in terms of our wallet share or...?
- Kunal Jagda** Wallet share.
- Kedar Vaze** So without commenting on the specific customer we have approximately a 30% wallet share of the Indian FMCG sector. So we continue to keep that wallet share and in fact enhance that wallet share as we have been doing in the last many years.
- Kunal Jagda** And sir the second question is on the international market. Can you just give some overview what was the reason behind the subdued demand and when do you think that it will get revived?
- Kedar Vaze** In fact, from second half of last year we have been keeping a strategy to observe the market, particularly exports to the Middle East and African markets which were linked to oil and expected large devaluation of currencies which were happening in the region. In this situation we have actually not competed beyond a point on customers or countries where there was a high credit risk and focused on the profitable customers in the countries where demand was growing and economic situation was continuing to hold normal. So in that sense businesses which were eventually exporting to countries like South Africa, Nigeria, some of these countries where there was a steep devaluation, we have discontinued or lost that business to other products in the market. And we have taken a conscious call to continue to focus on the premium area of the business which we

can support and which continues to build long-term brand value for our consumers and customers.

- Kunal Jagda** Sir, is the US political condition going to impact the revenue, international business?
- Kedar Vaze** Not significantly, I think the US policy will not affect our markets directly, to the extent it has effect on the oil price, there may be some effect in the Middle East and Indonesia, if there is a large impact of pricing on oil. But I do not expect to see that happening. The only part which will affect our consumption in these international markets that we are operating is if there is a huge change in the environment regarding oil or energy sector.
- Kunal Jagda** And sir my last question is, what is the new depreciation policy that we are going to follow now?
- Kedar Vaze** So we have now adopted SLM policy, straight line method policy, which some of our overseas subsidiaries were already following. So as a company group we have adopted the SLM method of depreciation.
- Kunal Jagda** So this is now across all subsidiaries and parent company?
- Kedar Vaze** Across all subsidiaries. And if you look at the accounting policies of all our peers globally in fragrance and flavors, they are all following SLM depreciation method. So we have also changed to follow that consistent method of accounting vis-à-vis peers on a global basis.
- Moderator** Thank you. We have the next question from the line of Vicky Punjabi from JM Financials. Please go ahead.
- Vicky Punjabi** I just wanted to know on the domestic fragrance side the growth looks quite strong during the quarter, around 20% plus. Could you help me understand what has driven this growth because the overall consumption demand seems to be going down?
- Kedar Vaze** So, like I mentioned earlier the revenue growth has two components, one is the underlying growth of demand and as we have already indicated in the last couple of quarters we have started additional service business where we give combination fragrances to our customers instead of them doing additional work. So that is a top-line growth which is not like-for-like, apple-to-apple, it was not there as an activity last year first half. We have roughly about Rs. 27 crore to Rs. 28 crore of revenue in the first half of the year as a service business. If you take that out, we have about 15% growth on organic like-for-like business.
- Vicky Punjabi** But sir this appears to be a strong escalation versus the previous quarter because I think the service business was present in the previous quarter as well. So what was the reason for this kind of a move?
- Kedar Vaze** So there is no specific acceleration vis-à-vis previous quarter, we are in line with our growth. Typically fragrances continue to grow quarter-on-quarter, it is a more stable business across multiple segments and there is growth. So vis-à-vis the first quarter you will always see some difference between first quarter and second quarter based on the calendar and a little bit of seasonality based on festival season demand. So it can move from the first quarter to the second quarter. Previous year the demand was in the first quarter, this year it was more evenly spread in both the quarters.

- Vicky Punjabi** And sir the first half growth is what you believe is more representative of the trends going forward?
- Kedar Vaze** Yes. I think we would look at year-on-year or first half to half as a good indication of performance of the business.
- Vicky Punjabi** And second thing was on the flavor margin, despite a very strong top-line growth the margin was quite depressed. What could be the reason for the same?
- Kedar Vaze** The margin depression is on account of two investments which we have made for the growth of the business. We have set up almost 14-15 people in marketing and sales offices across the country to reach out to more customers. We have also setup our export factory for the flavors for which effective rent and operating cost has come in for the first time. Combining these two, these are costs which have come in for the first time and these are costs that we have decided to put in place and incur based on the acquisition of HTT, giving us the additional products that we can now market in this area. So it is a very conscious call to invest this surplus in future growth to sustain upwards of 20% CAGR in the flavor division.
- Vicky Punjabi** And sir, all these costs are sustainable right, I mean they would be recurring cost, they are no one-offs in this?
- Kedar Vaze** Yes. So these are all recurring cost. If you compare this first quarter to second quarter you will see a steep decline in the margins, because in the first quarter also there was additional business from HTT in the transfer in the first couple of months which was higher than the average. So that business because of the transition transfer was higher in the first quarter. And I think on the total picture, we will see the EBITDA margins not at 17% and not at 12%, it should be somewhere in the middle. Because the first quarter was exceptionally better in terms of revenue line of the seasonality of HTT, second quarter in the seasonality aspect is a lower quarter. So you see the cost impact being much higher. For the full year, our guidance would be neither of the two quarters are representative of the full year. So if we take the first half as a indication of the performance of the business, that is more in line with a longer term expectation.
- Vicky Punjabi** Sir just one question, what would be the HTT turnover for the quarter?
- Kedar Vaze** So the HTT turnover for the quarter is Rs. 8.21 crore.
- Moderator** Thank you. We have the next question from the line of Yashesh Bhatt from LKP Securities. Please go ahead.
- Yashesh Bhatt** I wanted to ask as to what is the process that actually goes through from the point of placing an order to delivery? The question why I am asking is, there might be some short-term disruptions on the FMCG sector in general because of whatever has transpired over the past couple of weeks. So if you could give us an idea as to the entire process from ordering till delivering it to your customer that will be great.
- Kedar Vaze** Our lead times are typically seven to 10 days, and it is a direct delivery to the customer, so there is very little warehousing distribution involved, it is a very much direct-to-customer model. We have a capability to react within five to seven days of any change in demand. However, our customers reach the end consumers through warehousing, distribution and retail stores and they will see the effect of demonetization policy, if any, de-growth or slackness in demand. And we will only come to know in our system with a lag of 30 to 45 days of time. So we will have a much clearer picture towards the end of December as to

what is the effect on the business in the short-term. Having said that, in the long-term this is a great shot in the arm for companies like ourselves who are organized and have a national presence, because there in combination with the events of the previous demonetization with the expected GST rollout, I think a lot of the unorganized or regional or very small SME kind of companies may find it difficult to compete. They will need to change and adopt these systems in a significant way. For us, the ease of doing business is actually a big benefit and we see that the growth will actually move towards the center, so the mid-sized companies will benefit from these actions.

**Yashesh Bhatt** Sir but what kind of an effect are you expecting, will this hamper your long-term guidance like for this year of around 16% to 17% top-line growth?

**Kedar Vaze** I do not think we are looking at any de-growth or slowdown for this year at all. We may actually end up with beneficial longer term effect towards the next two, three years. We do not know how to estimate it, we will get some feelers in the next 50 - 60 days and thereafter we will closely monitor if there are any changes in demand. But structurally I think we are well-positioned, we are the leading player in the fragrance and flavors business with presence across India. And with GST and the steps that the government has taken, we are well positioned to continue our growth.

**Yashesh Bhatt** In terms of your exports, it has been a laggard owing to the demand situation and to the political instability that were prevailing over the nations over the past three, four quarters since we have conference calls. So I was wondering, how much more do you think that this trend is going to continue?

**Kedar Vaze** So, our overseas business has broadly two components, one is a global demand of fragrance and flavors globally because some of the ingredients and inputs go to other F&F houses across the world. If you look at the global growth rates which were typically average of 4% estimated year-on-year in the last 12 months has been kind of 2%, 3% at best. So it has been half of the expected growth on a global basis. In addition, the competitive environment because of the slow growth has been more acute, so we see the combination of declining prices and almost flat or small nominal growth vis-à-vis previous year, this year has been very flat for that segment. And for the other business, we already talked about the formulations business where we have taken a conscious call to move towards the premium sector and not work in the large volume low margin areas with higher credit risk.

**Yashesh Bhatt** And my last question for now is, how are you seeing your raw material costs panning out, are they more or less stable or do you expect any fall or rise in the same?

**Kedar Vaze** So the raw material cost, as most commodities and much of the raw material has come down in the previous 12 months. And depending on each commodity somewhere in the last quarter of the previous financial year they too would have bottomed and now they are stable or slightly moving upwards. I think very recent in the last seven, eight days we have had a currency devaluation vis-à-vis the US dollar that might have a small impact on our overall buying market. But as we have mentioned earlier on the call, in the previous quarter as well that with the working capital we have already built up sizable inventory in this period on lower cost, we will benefit in that period going forward.

**Moderator** Thank you. We have the next question from the line of Avinash Nahata from Aditya Birla Money. Please go ahead.

**Avinash Nahata** Sir, my question pertains to the demand pattern you were seeing of natural extracts, natural colors, flavors versus synthetic, both in domestic market as well as international

market. How is the user industry moving, how is the user industry shaping and what we are doing?

**Kedar Vaze** So it is a proper observation in terms of the trend, there is more natural and nature identical flavors which are in demand vis-à-vis synthetic flavors, most consumers or most regions around the world or countries around the world consumers are preferring natural over synthetic, particularly in the food processing and health and wellness. We see the same trend. In view of that, we have actually had a development project last year where we created 29 to 30 unique natural flavors including ethnic flavors for the domestic flavor market. So we have a product range developed for this market and we continue to invest in natural product or natural flavors on an ongoing basis.

**Avinash Nahata** So what would be ballpark difference between what is our international portfolio and how much is the demand on the domestic side for natural?

**Kedar Vaze** So, as a market, if you look at the global market the demand in the developed countries for natural is probably 60% of the entire flavors. Again, different countries define natural and nature identical, combining that it would be a 60:40 ratio. And in India it is probably still 20% natural, nature identical and 80% artificial or synthetic in usage. But the new business is almost 60% or 70% natural and 30% synthetic.

**Avinash Nahata** So incremental new business you are saying in India as well is 60% -- 70% natural?

**Kedar Vaze** Yes. The actual final flavors which are sold, a large part of that is synthetic today, they are all moving towards natural or nature identical.

**Avinash Nahata** You said that combination fragrance you sold during the quarter was worth something like Rs. 27 crore - Rs. 28 crore, is it?

**Kedar Vaze** Yes, that is the additional service revenue.

**Avinash Nahata** So do you do this thing in flavors also, like combination fragrance, combination flavors also?

**Kedar Vaze** No.

**Avinash Nahata** So it is restricted to fragrance?

**Kedar Vaze** Yes, this is restricted to fragrance and specific customers.

**Avinash Nahata** I am not aware in detail about the company, do we do natural colors also, sir?

**Kedar Vaze** Not at this moment.

**Avinash Nahata** And you do not foresee yourself getting into that business?

**Kedar Vaze** Natural colors and particularly natural food colors and natural flavors are very close adjacency. So we will evaluate in the future on any opportunity and work on that. At the moment we have no business in natural colors, we are only on the flavor part of the business.

**Moderator** Thank you. We have the next question from the line of Chintan Modi from Motilal Oswal. Please go ahead.



- Chintan Modi** Sir, just referring to your fragrance business, we had 9% growth in 1H FY17, so can you help with breaking it up into what was the like-to-like growth, I mean what was the growth in the same business which we had also done in the base 1HFY16 and how much would have been the growth from the new businesses?
- Kedar Vaze** So, what I have, I am getting you the numbers which are not exactly your question but we have divided our growth rate which is 20, so total of 9% is divided as overseas which was lower by 8% and domestic which was higher by 19%. Within the domestic is 19%, 15% was the organic growth of fragrances and the 4% was contributed by the service business which was not present in the first half of last year.
- Chintan Modi** And within that 15% of growth would have been there, some businesses which would not have been present in the base year?
- Kedar Vaze** Roughly 1.5% of our business is coming from new products, so it depends. If you take a full year basis it will be roughly 2%, the growth comes from new products.
- Chintan Modi** Secondly sir, you mentioned that in FY16 first quarter was much better in terms of demand compared to the quarter two. So is it the right way to look at, like we already had a low base in Q2 FY16 and on that we have done a growth of 13% in the fragrance business?
- Kedar Vaze** No, I think the business migrates because of the calendar as some of the demand is linked to the festival season. So we have seen that last year the festival season was almost a month earlier and therefore the demand was largely in the first quarter or more in the first quarter than in the second quarter. But the combined H1 was the correct representative sales. And so H1 versus H1 growth is actual organic growth of demand and our products growth in the market. If you look at quarter one versus quarter one, our quarter one last year was very good, quarter two was also good. But if you compare quarter two versus quarter two then the difference is very, very large. So if you look at first half to first half, that is the right representation of what is the actual growth.
- Chintan Modi** So just to clarify one thing, like going ahead we will continue with this service business income or is there some lumpiness related to it?
- Kedar Vaze** No, so there is no lumpiness related to the service income, it is a regular running business service to the customer. I think there might be some business model change at the customer's end, if GST makes it easier for them to operate in one location and not have it centrally produced at our location. So unless there is a business model change at the customer's end, it is a continuing business.
- Chintan Modi** So, do you think that second half we can do a much better growth rate in fragrance business compared to 9% which we have done? Considering there would be some impact of demonetization which your customers are going to face.
- Kedar Vaze** I think the impact of demonetization on our business will be very small.
- Chintan Modi** No, what I am referring is your customers are going to face some impact, we had also done some channel checks like most of the consumers companies are going to face some impact on its supply chain. So there would definitely be a short-term impact on those companies which can in-turn have an impact on your business is what I am trying to understand.

- Kedar Vaze** Yes, I am trying to explain to you that there are two opposing forces or opposing benefits. So the bigger companies will face some of the demand erosion. In our business we also see that, the smaller competition will find more de-growth and therefore some of that business will migrate to us. So there will be, as I said earlier, the business will come to the middle, the mid-sized retail companies will continue to grow, very small ones will have a very difficult environment, the big ones will see some decline in their product offering because of the liquidity being affected.
- Chintan Modi** Are you guiding for any growth rate, particularly in the fragrance business for the full year?
- Kedar Vaze** So, not for the full year, we maintain that we will not have a policy to give a short-term guidance. We are committed to our growth rate expected over a longer period, three to five year horizon of 15% CAGR. And we have been achieving that in the last year and we continue to maintain that growth rate in the future.
- Moderator** Thank you. We have the next question from the line of Naushad Chaudhary from Systematix. Please go ahead.
- Naushad Chaudhary** I am sorry I joined late, so really sorry if I ask some repetitive question. Can you share the revenue breakup in terms of your customers like from institutional and B2C business?
- Kedar Vaze** Almost 93% of our business is institutional and 6% to 7% of our business is kind of B2C facing, it is not directly to consumer but it is facing to consumers more closely.
- Naushad Chaudhary** And how this number was in H1 FY16?
- Kedar Vaze** Very similar. Actually it was higher in H1 last year because the flavor growth has been largely institutional. So on the fragrance side the business has continued in the same manner, when you aggregate the two businesses together the flavor business is largely institutional.
- Naushad Chaudhary** And can you share the number of clients in both fragrance and flavors right now?
- Kedar Vaze** So we have more than 2,000 clients on the fragrances and we have I think more than 300 customers on the flavor side.
- Naushad Chaudhary** And all 2,000 in fragrance business are our active clients, right?
- Kedar Vaze** Yes.
- Naushad Chaudhary** And what would be the contribution of top five customers to the top-line?
- Kedar Vaze** I do not have the exact number with me, but our largest customer is less than 5% of the revenue, so the business is well diversified.
- Naushad Chaudhary** This is for fragrance business, right?
- Kedar Vaze** Total business.
- Moderator** Thank you. We have the next question from the line of Anand Shah from Kotak Securities. Please go ahead.

- Anand Shah** The first one is on domestic, this service business income, so that was about what, Rs. 27 crore - Rs. 28 crore in 1H?
- Kedar Vaze** Yes.
- Anand Shah** And this has moved up from a quarterly run rate from about Rs. 10 crore?
- Kedar Vaze** Yes, so last quarter last year was about Rs. 12 crore.
- Anand Shah** So 1Q was Rs. 10 crore - Rs. 12 crore and this probably Rs. 15 crore - Rs. 16 crore in 2Q?
- Kedar Vaze** I just want to highlight that it is linked to the underlying fragrance growth of 15% anyway, because then this is in addition with the growth of the fragrance. So if the fragrance has grown, then the additional service will grow on top of that.
- Anand Shah** That is fine, I am just comparing the base, so 1H still does not have right, because this you started from 4Q?
- Kedar Vaze** Yes, 1H does not have.
- Anand Shah** But then you would be doing Rs. 50 crore - Rs. 55 crore kind of a service business income this year?
- Kedar Vaze** I think the indications on normal basis would be the same. I am being little bit more conservative to give any guidance based on the policy changes that have happened recently and with expected GST. So if the business model continues as it is then we would expect around Rs. 45 crore to Rs. 50 crore of service income year-on-year. We need to take a note of what is the effect of economic policy changes and tax changes on the business model of our customer.
- Anand Shah** And within the fragrances of overseas and export business where you face 8% decline, can you give just qualitative comments on these parts of those business, as in the PFW, exports and ingredients?
- Kedar Vaze** So there are three broad parts of the business, one is the ingredient or the fragrances going to other global fragrance companies input. There is the business within, we call the formulations business to our FMCG companies. So also we look at broadly three kind of segments, the below \$10 segment which is functional product or much more functional utility product like laundry, soap, floor cleaner, detergent, soap and so on so forth. So they have much higher volumes but lower margin profile. The mid sector beauty products and the premium fine fragrance or attar related products. If I divide broadly, we have continued to grow in the premium segment, we have continued to maintain our market share in the mid-segment, a sizable part of the revenue loss has been in the ingredient business or the input business and the low value formulations business which is actually it is not automatic, it is a tactical call which we have taken to focus on the premium side of the business.
- Anand Shah** So this would be a one-off kind of a hit because you are partly exiting that kind of a business?
- Kedar Vaze** Yes.
- Anand Shah** And so next year this growth should stabilize?

- Kedar Vaze** Yes.
- Anand Shah** And PFW continues to remain sluggish?
- Kedar Vaze** So the global demand on fragrance and flavors, as I mentioned earlier, is indicated to be around 2% compared to a normal year of 4% in the previous many years. So if that demand remains low we would see a sluggish demand for our operations in Europe. And based on that we will evaluate the new economic realities with the advent of the new president in the US, if there is any fallout. In accordance, we need to reevaluate our strategy on our assumptions for global growth over the next five years.
- Anand Shah** And within the flavors exports part, I mean we have seen a QonQ drop from 1Q, 2Q, so why is this volatility there?
- Kedar Vaze** Actually it is linked to the third quarter and fourth quarter of previous year where we had supply chain disruption particularly in the Middle East region due to geopolitical situation where road lines were cut off and factories could not access the markets where they were selling. So many of these businesses relocated their factories in the second half of last year. So we had some pent-up volume demand from the previous quarter also coming in the first quarter of this year.
- Anand Shah** So then can we assume that the 2Q run-rate is actually the one which is more sustainable?
- Kedar Vaze** Yes, I think second quarter run-rate is sustainable, definitely. I see that business while on the fragrance we have looked at exiting some of the low value segments. On the flavor we are only at the premium, high end flavors in our export markets. So we will continue to sustain that growth.
- Anand Shah** And broadly just on the gross margin side, I mean, would you have any guidance to share on the gross margin front? I mean, you still have not gone back to your historical gross margin that you had before that fall happening in FY15. So when do you see gross margins recovering back to those levels?
- Kedar Vaze** To the extent the gross margin without the service income, I think we have already come very close to the margins of previous periods. Except for our export fragrances where we see currency translation effects and overall lower margin profile in some of the products in the exports. But domestic margins have stabilized to long-term basis where we see it sustainable and it is continuing to hold there.
- Anand Shah** So if I was to exclude the service income part, then on a like-to-like business basis gross margins in standalone domestic would have gone up to 43% - 44%?
- Kedar Vaze** Yes.
- Moderator** Thank you. We have the next question from the line of Suvarna Joshi from SMC Global Securities. Please go ahead.
- Suvarna Joshi** Just wanted some understanding from you on one of the business segment that we are present in, that is the branded small pack business. So what is the activity on that front, because I understand that we had mentioned in the previous concalls that we will be looking to focus on this particular business as well as it helps us improve our margin profile overall. So your thoughts on that should be helpful.

- Kedar Vaze** So, also on that segment we are organizing additional marketing and sales to focus on that business with the distribution, marketing and sales. In addition, we are evaluating the effect of GST which I believe would help us to streamline the branded small pack business in a much better way. So I think with the advent of GST we can focus on further enhancing and growing this business in the years to come.
- Suvarna Joshi** Sir, just a follow-up on that. With the GST coming in, will we see any impact on our tax rates as such?
- Kedar Vaze** In terms of tax rate because of the input credit which we are availing, I do not think we have any net differential, we will probably have a very small difference between the cost input and output as compared to today. So there is no net real effect of GST in our cost structure.
- Suvarna Joshi** And what would be the utilization level that we would have clocked in quarter two and 1H FY17?
- Kedar Vaze** Utilization of capacity?
- Suvarna Joshi** Yes.
- Kedar Vaze** So in terms of capacity utilization we have continued to be around 40% - 45% for our fragrance plant in India, about 80% plus for our capacity in the Netherlands. And the Vapi facility where we have new investments, that continues to be around- which was much lower is now 65% capacity utilization.
- Suvarna Joshi** So what are we doing to improve the level of utilization levels in the fragrance plant? Because if I see the past four - five quarters, we have been stuck in this range of 40% - 45%. And therefore we are not seeing a very meaningful improvement in our return ratios to that extent.
- Kedar Vaze** I think the operating cost part of it has actually significantly improved. When we look at the capacity we are also seeing the net productivity improvement and addition to the capacity. So the capacity actually has gone up as well with the investments that we have been making. As far as improvement in the volume that we are producing, so the 40% - 45% while it remains the same on capacity utilization, our actually output capacity has almost been 1.5 times compared to one year ago in our Vashivali factory, that is happening in the second quarter this year. We have shortened the throughput time in our factory, so we have additional 50% capacity.
- Moderator** Thank you. Ladies and Gentlemen, that was the last question. I would now like to hand the conference over to the management for their closing remarks. Thank you and over to you.
- Kedar Vaze** Thank you, everyone, for joining the call. I hope we have been able to answer your question satisfactorily and some of the suggestions were very well appreciated by the management. Should you need any further clarifications or would like to know more about the company, please feel free to contact our team or CDR India. Thank you once again for taking the time to join us on this call. At the end, before closing, I would also want to thank the investors who have invested through the IPO process, we have completed four quarters post the listing of the Company and I am proud to face the investors again with the trailing PAT of Rs. 100 crore having delivered in the last four quarters. So I am happy with the faith that the investors have shown on us and I am taking this responsibility to ensure continued performance in the future. Thank you.



**Moderator**

Thank you very much. Ladies and Gentlemen, on behalf of SH Kelkar and Company Limited, that concludes this conference. Thank you for joining us. And you may now disconnect your lines.

- ENDS -

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