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July 25, 2016

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Scrip Code : 532424

The National Stock Exchange of India Ltd
Exchange Plaza, 4th Floor, Bandra-Kurla Complex,
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Dear Sir,

Sub: Transcript of the Concall on 13th July, 2016

We enclose herewith for your information, a transcript of the concall held on July 13, 2016 to discuss transition to Indian Accounting Standards (Ind AS) for the Company.

For Godrej Consumer Products Limited

Ramesh Iyer
Dy. Company Secretary

Analyst Conference Call to discuss transition to Ind AS

July 13, 2016

Moderator:

Good Day, Ladies and Gentlemen, and welcome to the Godrej Consumer Products Conference Call. As a reminder, all participant lines will be in the listen only mode. And there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing '*' and then '0' on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Sameer Shah. Thank you and over to you, sir.

Sameer Shah:

Good afternoon and thanks for taking the time out for the call. The purpose of this call is to communicate the impact on reported profits of GCPL under the new accounting standards known as Ind AS and clarify any doubts that you may have in this regard. Joining me today in the call are Jamil Khatri, Partner & Head of Audit, KPMG, Koosai Lehery, Partner KPMG, V Srinivasan, CFO & Company Secretary and Ramesh Iyer, Associate Vice President - Finance. We will start the update with Ind AS roadmap led by Jamil, followed by impact analysis led by V Srinivasan and finally with Q&A session. The presentation has been shared with stock exchanges and is also available on investors section on our website www.godrejcp.com. Over to you Jamil.

Jamil Khatri:

Thank you, Sameer and good evening to everyone. I would like to start by sharing how GCPL will be covered by the Ind AS roadmap. Just to set the context, the Ministry of Corporate Affairs has provided that Ind AS will mandatorily apply to all companies whether listed or un-listed with a net worth more than Rs. 500 crores as of 31st March, 2014; and the first year of transitioning and reporting under Ind AS is financial year 2016-2017. The Ind AS would apply to the company which meets the criteria as well as all subsidiaries, associates and holding company of this company.

As GCPL had a net worth of more than Rs. 500 crores as of 31st March, 2014; it is covered by Ind AS and will start reporting Ind AS for the financial 1st April, 2016 to 31st March, 2017. Accordingly, the numbers that will be reported for Q1 in June 2016 will be reported in accordance with Ind AS.

The Securities and Exchange Board of India has provided that when the company reports Ind AS for the first time for June 2016 the comparative numbers for June 2015 would also be reported using the same principle for consistency and comparability and a disclosure be made of the reconciliation between the profit previously reported and the profit as per the new Ind AS framework. Recently, the SEBI has made some concessions on some of these requirement but largely what you will see is comparative numbers under Ind AS with a profit reconciliation.

One of the important things to appreciate is that Ind AS changes many accounting policies, practices and presentation and disclosure but does not of course change anything fundamental relating to the business. So for example, cash flows remain the same, some of the other business metrics remain the same. But because you are changing the accounting policies and practices and the disclosures, some of the performance metric that have been disclosed by companies in the past may undergo a change as you make changes to your policies and practices.

I would now like to spend a few minutes on talking about what we are seeing as the key impact areas from Ind AS generically for corporate India. The first key impact is on revenue recognition. Previously, a lot of items which were reported as a cost line item whether it is cash discounts, whether it is incentive that are provided to customers will now be required to be reported as a reduction from the sales line item. Secondly, items like excise duty which are currently netted off from sales for presentation and disclosure will be shown as a cost line item; this will come into play for the full year because SEBI has permitted companies to continue with reporting sales on a net basis in the quarter but eventually you will see the excise duty is not being reported as a net number but as a cost line item.

The second big area of impact is on acquisition. Today, there is very little guidance available under Indian GAAP on acquisition accounting a lot of which is driven by the form of the transaction and also driven by court schemes under which the acquisition is reported if it is a merger. Going forward the Ind AS principle would require all acquisitions to be accounted by the fair value method. Under this method, the consideration paid is recorded as fair value whether paid in cash or paid in stock and all the assets and liabilities of the acquired company are also reported at fair value including any intangible asset that may exist in the business that is being acquired but which are not been reported by the acquired company. What this means in practice is you will have a higher depreciation charge, higher amortization for intangible assets going forward. The other important part of acquisition accounting is today transaction cost which are incurred are capitalized while going forward on Ind AS all transaction cost be it the legal cost, the due diligence cost will be expensed through the profit and loss account.

Lastly, Ind AS brings in some additional concepts around contingent consideration or earn out transactions. So, if there is an acquisition where there is a future earn out, today the practice is that when the earn out gets determined it is capitalized as an additional acquisition cost. Going forward these earn out would need to be recorded upfront based on the fair valuation and any changes in the fair value, the earnout would bring in profit and loss volatility because it will be charged through the P&L.

Another element of acquisition accounting is if there is a minority interest involved in the acquisition. So, if a company acquires a majority but there is still a minority left and you have any special arrangement with the minority shareholder in the form of either an agreement to buy that interest in the future or an agreement whereby the minority shareholder can sell it to you in the future then that obligation has to be reported upfront in the balance sheet. How that changes and that value of that balance sheet item are reported depends on the specific nature of the arrangements. In some arrangement it will result in movement in the fair value being reported through the P&L while in some other arrangements it will not impact the P&L. So acquisition accounting is a big area of impact. The third area of impact is on employee benefit program. Stock options which have previously not been accounted for in the P&L as long as option is given at the market price will now be reported in the P&L because all options will be recorded at fair value. The second impact is on employee benefit like gratuity scheme. Under current Indian GAAP movement in assumptions which affects the value of the gratuity benefit are reported through the profit and loss accounts. Going forward these benefits will be accounted through the reserves.

Another area of impact is on financial instruments. Ind AS requires that all financial instruments be recorded at fair value and generally all moments in fair value are recorded through the profit and loss account. So for example, if a company has investments in mutual fund unit they would be recorded at each period end and at fair value with the changes being recorded through the P&L. Similarly, if a company has any derivative transaction whether it is forward contracts or commodity contracts or any other form of derivative generally these derivatives will be recorded through the P&L, recorded in the balance sheet and that will also have an impact on the P&L.

The other area of impact on financial instruments is on the type of financing instruments. In the past if you raised money through instruments like bonds and debentures and the return to the investor was through redemption premium, under Indian GAAP you could charge that premium to the reserve and all cost did not necessarily go through the P&L. Going forward under Ind AS all costs of issuing a financial instrument whether it is in the form of coupon, whether it is in the form of redemption premium will all be recorded over the life of the instrument through the P&L account.

Of course life does not end without taxes, so all of this would have an impact from a taxation perspective. Two specific area of differences under Ind AS. One is Ind AS records deferred taxes based on what is called the balance sheet approach as opposed to Indian GAAP which is based on what is called the profit and loss approach. Very simply put there are certain items whereby a company may acquire a tax shield because of certain tax benefits that are available. For example, on long-term capital assets company gets benefits of indexation under the Income Tax Act. Under Indian GAAP the benefit of that indexation is not recorded because this does not come into the current profit calculation or it does not come into the current P&L as prepared under the Companies Act. But under Ind AS because this is a tax shield that the company is acquiring this would need to be recorded period on period and would therefore have an impact on the deferred taxes that are recorded.

Similarly, if there is an inter-company transaction whereby one company in the group sells goods to another company in the group, today under Indian GAAP that transaction and the profit on that transaction is eliminated in the consolidated financial statements but any taxes that have been paid on that transaction are not eliminated. Ind AS is based on the matching principle year. So if the basic transaction is eliminated the taxes paid are also deferred in that case resulting in matching of the tax expenses with profits that are recorded and that also is an area of difference that we are seeing coming up in practice.

So those are the big areas that are coming up in practice and I will now hand it over to Srinivasan to talk about the GCPL specific areas.

V Srinivasan:

Thanks, Jamil. Good afternoon everyone. Now we will go over the specific impact that these differences in Accounting Standards will have on GCPL's reported numbers line by line. I will take you through each slide in detail.

We go to Slide #7 on revenue. Trade promotion spends as Jamil said are required now to be reduced from revenue while excise duty is now part of the expenditure line item and not netted off from revenue. With these changes the standalone revenue increases by Rs. 76 crores and the consolidated revenue of GCPL reduces by Rs. 210 crores for FY2016.

Coming to Slide #8, consumer promotion spends also are now required to be reported under cost of raw material and with this change, the cost of raw material goes up by Rs. 15 crores in standalone and by Rs. 23 crores in consolidated numbers for FY2016.

Now we come to employee expenses on Slide #9. The long-term compensation incentives are to be recognizes as liability at their present value. The unwinding of discount will be reported as a finance expense in the profit and loss account. Also the actuarial gains and losses on defined benefit plans are to be recognized in other comprehensive income instead of profit and loss account. This reduces the employee expenses in standalone by Rs. 6 crores and consolidated by Rs. 13 crores for GCPL for the financial year FY2016.

In the next two slides – Slide #10 and Slide #11, we have given the details of adjustments to advertisement and publicity and other expenses. The trade and consumer promotion spends earlier part of A&P and other expenses now get reclassified between revenue (as a reduction), cost of raw materials and other expenses. Overall A&P reduces by Rs. 17 crores in standalone and Rs. 301 crores in consolidated and other expenses reduces by Rs. 230 crores in standalone and Rs. 238 crores in consolidated numbers for FY2016.

Now we go to Slide #12, impact on finance cost. Under Ind AS all finance cost including redemption premium on debentures are accounted as interest cost in the profit and loss account. Hitherto these were adjusted with securities premium account. As these debentures have now been redeemed in FY2016 there are no such cost going forward for GCPL. Going forward the finance cost will go up to the extent of interest unwinding on long-term liabilities such as earn out mainly Strength of Nature and Canon acquisition and long-term employee incentives which have been discounted to the presented value.

Now moving to Slide #13, under Ind AS minority shareholding what is called as non-controlling interest or NCI where there is a put option is acquired to be presented as financial liability. The agreement with JV partners for Darling & Chile businesses provided for call and put option for the balance stake. The change in their fair value of this option is included under exceptional items for FY2016. Consequent to the stake increase, the agreement with Darling JV partners have been amended with a result that future changes it any in the fair value of options for the residual stake will have no impact in the P&L going forward. As per the requirement of first time adoption of Ind AS, GCPL has chosen to grandfather the accounting for business acquisitions of the past. The Ind AS requirements will apply for the new acquisition done subsequent to Ind AS transition date for example, our Strength of Nature acquisition, etc. The NCI or non-controlling interest relating to the past acquisition has been reclassified to liability and the liability is periodically restated at its fair value. Further under Ind AS cost incurred in connection with undertaking the business combination is charged off to P&L account. So these are the impacts on exceptional items that we have shown.

Now on Slide #14 on taxes. Most of the Ind AS adjustments will have a corresponding impact on deferred taxes accounted by the company. In case an intangible asset is determined to have indefinite life as we have done for the brand HIT and Good knight, there will be a difference between the book base and the tax base of such intangible assets. The tax base will be lower than book base resulting in recognition of deferred tax liability. Under Ind AS deferred tax is also required to be recognized on consolidation adjustments such as profit margin pertaining to unsold inventory. Under Indian GAAP though intercompany transactions are eliminated deferred tax adjustments are not required to be recognized in consolidated financial statements on these adjustments. As a result of the above the deferred tax amount increases by Rs. 21 crores in the consolidated financials for FY2016.

We move to Slide #15 on minority interest. Given that most of the non-controlling interest is reclassified as a financial liability such entities are consolidated based on full stake in the company including the NCI stake and corresponding share in profit is also appropriately accounted in the income statement. Hence, no significant minority interest is expected going forward. As earlier mentioned by Jamil, the business fundamental continue to remain unchanged, the change is only in reported financial numbers due to application of Ind AS principle. The underlying business cash flows too remain unaffected. Due to the restatement of numbers, some of the balance sheet ratios would also undergo changes. We have provided the impact on key ratios in the next slide. If you see the net debt equity ratio is going up from 0.39x to 0.56x. The net worth is adjusted for put option liability, deferred tax liability on brand, etc which is offset in part by reversal of interim dividend charge and brand amortization. The closing return on capital employed as well as return on equity for FY2016 excluding the exceptional items are increasing as the base i.e. capital employed and equity have reduced on account of the aforesaid adjustments.

We have provided the re-casted consolidated and standalone P&L statements by quarter for FY2016 as also a summary of the adjustments to P&L statements which we discuss in detail line by line.

To conclude, at an overall level, while the revenues for FY2016 have come down by about Rs. 210 crores and the operational EBITDA marginally moves up by about Rs. 12 crores. So, on overall basis, the operational performance is largely unchanged.

That concludes what we wanted to share on the impact of the new Accounting Standards on our reported financials. We now open the floor for any questions that you may have.

Continue: - Q&A…

Questions and Answers:

Moderator:

Thank you very much, sir. Ladies and Gentlemen, we will now begin the question-and-answer session. We will take the first question from the line of Kunal Jagda from Karvy Stock Broking. Please go ahead.

Kunal Jagda:

Is the goodwill that is in the balance sheet at this moment which got created because of the acquisition i.e. the goodwill on consolidation; is there is any change in the treatment of the same under the new accounting standards?

V Srinivasan:

Yes, as we mentioned basically there are adjustments both on the equity front as well as on the goodwill front to the extent that we need to adjust them for the fair value. So essentially all the adjustments have been captured in the financials as we have presented now. In terms of acquisition, when we split them into pre-Ind AS acquisition and post-Ind AS; pre-Ind AS acquisition only 10% of the Darling business acquisition remains to be accounted for. Rest of it is already been considered, so we do not expect going forward any major changes to the assets or liabilities.

Ramesh Iyer:

Just to add-on to that, goodwill under the new standards are determined at the date of acquiring control and going forward goodwill amount does not change after increasing the stake as per the new Ind AS regulation.

Kunal Jagda:

What is the process of determining this fair value?

Sameer Shah:

I think there will be different ways of revisiting the fair value. One, which comes immediately at the back of my mind is the way the business performance has been. It also depends in turn on what is the formula for the balance stake payout which more often than not could be last 12 months, last 24 months of corporate performance at some locked in multiple and to determine that you would more often than not look at the recent past performance and revisit that.

Jamil Khatri:
Just to add-on to that as Ramesh said, as far as the books of accounts are concerned initially and when assets and liability are recorded at fair value that is done at that particular time on the date of acquisition; and as Sameer said there are different ways of measuring fair valuation. Most companies in our experience have their internal models which are linked to the rationale for the acquisition to determine this fair value. In some cases, where it is a very complex external valuer may also be involved. So it is a combination of internal and external but always linked to the business rational for that acquisition.

Kunal Jagda:
What is the process of amortization? Will goodwill that amount remain the same through the future years?

Ramesh Iyer:
Goodwill it is not amortized under the new Ind AS calculation; it will only be reviewed from an impairment perspective on an annual basis.

Kunal Jagda:
So that will be tested by the Board of Directors.

Ramesh Iyer:
Yes.

Moderator:
Thank you. The next question is from the line of Manoj Menon from Deutsche Bank. Please go ahead.

Manoj Menon:
Only one question on the items which are netted off from revenue. Basically, the advertisement and promotions if you could just give a few examples on each of the scenarios for example, let us say straight price offs in my understanding actually gets netted off anyway but what about the quantity linked discounts given to the trade partner or if you are giving one of your products you get another product free what happens to that? Any changes to that? And secondly if it's a bought out item does it change anything or suffice to say that advertisement spends what gets reported now will only be media spends and most of the other things gets netted off?

Sameer Shah:
So I think largely you know any spends which is with channel partners will be in nature of sales promotions, trade offer spends, which to a greater extent will be netted off from

revenues. Any spends which is for the consumers say media, will remain in advertisements. Spends for consumers like consumer offers will be added to cost of goods sold and hence to that extent will get reflected in gross margins.

Manoj Menon:
Okay. So the third item which you mentioned is basically - buy brand A, you get brand B free so the cost of the brand B goes into the COGS?

Sameer Shah:
Absolutely.

Manoj Menon:
Will it be then correct to say that the advertisement spends line will be purely media spends and there is no promotion expenses in that?

Sameer Shah:
So for GCPL, yes, this will broadly media spends, for industry it will be difficult to call out because we honestly do not know as to what all goes into the advertisement and publicity. In fact some even call this line as advertisement and promotion so, it is difficult to kind of disaggregate as to what goes at least from quarterly reporting basis.

Manoj Menon:
Understood. In your case for example, where does let us say merchandizing cost go?

Ramesh Iyer:
So the way the Ind AS regulation requires us to account for consumer promotion is that all kinds of discounts which you have given to customers which are linked to sales those are the ones which are netted off from revenue. There would still be some kind of promotion which would continue to be reported and accounted as part of cost. So those would continue to be in sales promotion line and advertisement spends and media related spends will continue to be there in advertisement line.

Moderator:
Thank you. The next question is from the line of Arnab Mitra from Credit Suisse. Please go ahead.

Arnab Mitra:
My first question is on the Slide #12, could you just tell us what kind of impact does SON earn out impact will have going ahead? Is there a way to build in what kind of impact can be there like assuming if Rs. 1,000 crores was the total acquisition and one-third was to be paid three years later, what kind of impact it can have on the interest cost line?

V Srinivasan:
Essentially, we discount all the pay outs that are to be done in the future at the borrowing cost. So depending on the geography and the borrowing cost in that geography, this amount will be determined. So that gets expensed out as finance cost in the years prior to the actual amount being paid.

Arnab Mitra:
Okay. So any way we could estimate this number because would this be a material number going ahead in terms of FY2017 - FY2018 impact?

Sameer Shah:
I think there are too many moving parts in this but I think just in terms of estimation we can bake in anywhere around Rs. 12 crores to Rs. 15 crores of new impact on this front going ahead.

Arnab Mitra:
So basically would there be no need to book minority interest now and would it entirely go into the liability line?

V Srinivasan:
It depends on the agreement with the minority shareholders. In terms of our agreements with our joint venture partners, since we have full controlling interest in the business and the liability for their payment has already been created, no minority interest of any significant nature will get created.

Arnab Mitra:
And dividends paid to minority investors will get booked as a cost?

Sameer Shah:
That's true. But just to add, we expect that amount going ahead to be materially lower than what we have seen in FY2016 as minority stake has gone down in Darling and in Chile, we converted from 60% to 100% last year.

Arnab Mitra:
On deferred tax on Good Knight and HIT being infinite life, so were you earlier using amortization on these brands as a tax shield?

Ramesh Iyer:
Earlier we used to amortize it for tax purposes but in Indian GAAP it was recorded as a permanent difference. So, deferred tax was not required to be recognized on permanent

differences. Under Ind AS all kinds of differences on balance sheet have to be accounted for and therefore this deferred tax liability is coming up now.

V Srinivasan:
So, as the tax base keeps going down, this impact on P&L also, for deferred tax will keep going down.

Sameer Shah:
Which means on delta basis the quantum of Rs. 27 crores will keep on coming down.

Moderator:
Thank you. The next question is from the line of Sameer Gupta from India Infoline. Please go ahead.

Sameer Gupta:
Since exceptional items are being created for each period could you just guide on the kind of tax shield that these exceptional items would incur so that we could calculate the pre-exceptional PAT in a little more accurate way?

Sameer Shah:
There are two things, one is there is no tax shield on any of these exceptional line items and broadly we also expect the quantum of exceptional line items going ahead to be minimal starting FY2017. So operationally, I do not see any impact as such on the P&L going ahead.

Sameer Gupta:
So I can just take the normal tax rate to calculate the pre-exceptional PAT, is it?

Sameer Shah:
Yes, so you will have to just adjust it now for this deferred tax impact which we have taken on our brand. Otherwise there is no impact as such. So, just to help you out, I think the weighted average tax rate may move up by 150-200 basis points from whatever the earlier tax rates you would have in your model.

Moderator:
Thank you. The next question is from the line of Richard Liu from JM Financial. Please go ahead.

Richard Liu:
I am referring to Slide #13 this Rs. 181 crores of agreement with JV partners for Darling &

Chile business, etc., can you give us an idea of how do you compute these? What are the factors on which this is going to be based?

V Srinivasan:
Basically, you can split the acquisitions that we have done into two parts - one is a pre-Ind AS acquisition and one is post. Now for pre-Ind AS acquisition all the required adjustments have been already captured in the financials and most of the non-controlling interest has already been acquired and only a small portion of Darling stakes remains to be acquired and that consideration payable also has been captured. Since we have acquired a majority stake, the agreements also have been amended suitably so we do not expect any future P&L impact on account of remaining stake acquisition. Now in the case of new acquisitions for you to estimate what kind of hits could come possibly, entire liability for un-acquired stake or earnouts will be recognized up front based on the agreement that you have with the joint venture partner and corresponding assets will be recognized like in the case of Strength of Nature. So basically all the assets, brands, etc., will be stated at fair value. Hence, we may not have any significant impact that will come quarter-on-quarter through the P&L.

Richard Liu:
In case you get into a future acquisition where you have a similar kind of call / put option like Darling acquisition again, then how do you estimate this Rs. 181 crores? I know it is not going to hit the P&L based on the situation as of today but in case you were to make something like that how do you determine this kind of a charge, what is the factor on which it is based?

Sameer Shah:
So there is couple of things, one is going ahead technically we will take care of this in the way we structure some of our M&As and our agreements that is one. Secondly, as of now we do not expect any material amount on this line item going ahead so, I think in forecasting may be you assume as good as zero amount. The only one thing I think which we should keep at the back of our mind is we will also be fair valuing the earn-out in case of Strength of Nature on a periodic basis. But again as of now, we do not expect any material P&L impact on that front at least in this fiscal year.

Jamil Khatri:
At a conceptual level though, the way this liability is measured whether it is for earn out or put option is going back to the same principle aligned to the business rationale for the acquisition. So most of these will either have a formula or have something which says that this is the way fair value would be determine and what you then do is based on that set up a liability at a point in time. As Sameer said it may not have a P&L impact going

forward but the way the liability is determined is to say if you had to pay that out what would that amount be and that is the basis for the calculation.

Richard Liu:
Referring to Slide #10 which is the advertisement and publicity slide, what is the nature of this Rs. 172 crores what will now get reduced from sales and also what is this Rs. 111 crores that I is moving from advertisement to sales promotion to other expenses?

Sameer Shah:
What we are doing in Ind AS is revisiting the line by line grouping by nature of spends and bucketing it in the way as defined in Ind AS. So just to clarify Rs. 172 crores which is in consolidated and more so driven by international business is getting netted off from sales is actually a nature of sales promotion as defined in Ind AS. Rs. 111 crores is also actually going back to other expenses, which again, as per Ind AS definition is to be classified as one part of promotion which does not get netted off from sales. So the point over here is that driven by the nature of spends and read with the Ind AS definition some part of it is getting netted off from sales and some part of it is remaining in other expenses and this is more so an international business than anything else.

Richard Liu:
What is the nature of Rs. 172 crores and what is the nature of Rs. 111 crores?

Sameer Shah:
Let us start with Rs. 111 crores, I will just give you may be top two-three spends – the first one is again in Indonesia. To be very specific, our distribution model is very unique where we have around 1,400 – 1,500 sales promotion girls (SPGs) who are deployed in modern retail channel. So these SPG related expenses, read with Ind AS way of classifying, remains in other expenses. Also, a lot of modern trade listing fees and related charges and which is true for most of our international business because ex-Darling most of our international business has a very high salience of modern trade so modern trade listing fees and related expenses also fit in that Rs. 111 crores. So these are the large spends which sit in the Rs. 111 crores basket.

Richard Liu:
And some expenses of Rs. 172 crores?

Ramesh Iyer:
So the items under Rs. 172 crores are all kinds of discounts paid to customers and linked to sales gets netted off from revenue.

Richard Liu:
Does Ind AS accounting have any impact on the way you calculate profit for the purpose of determining taxes or that remains the way they were?

Ramesh Iyer:
We have a recent circular from the Government on the way MAT has to be calculated from Ind AS principles' point of view. In our context, it is not materially different from the way we use to calculate taxes as per the old GAAP.

Jamil Khatri:
To deal with this issue on what is impact of Ind AS on taxation, the government has come up with the set of standards call the income computation and disclosure standard. These standards will become applicable parallel with Ind AS from 2016-2017 and what this will ensure is that irrespective of how you report your books whether Ind AS or Indian GAAP because many companies will continue to be in Indian GAAP going forward, the tax liability will be calculated on a different basis in accordance with income computation and disclosure standards.

Moderator:
Thank you. The next question is from the line of Sandeep Gupta from Motilal Oswal. Please go ahead.

Sandeep Gupta:
The two brands, in our books, which are currently being amortized as per the court order through the reserves are no longer required to be amortized. So would the Ind AS standing be basically taken forward ahead of the court orders?

Jamil Khatri:
In this case, as far as the court order is concerned and as well as Ind AS is concerned, you are achieving the same outcome, which is you are not debiting the profit and loss account but for slightly different reason. In the case of Ind AS, given the nature of these brands these are indefinite life and therefore do not need to be amortized while the court prescribed the same treatment of not debiting the P&L. Therefore the conflict does not arise.

Sandeep Gupta:
Sir, maybe there is no P&L impact in both these cases but if the asset value is retained at the same level may be the return ratios might get impacted?

Jamil Khatri:
Yes, so I think that is a fair point. But as I said the way to look at it going forward is you

have independently applied the principles of Ind AS. Think of a brand like a Coke or a Pepsi and which is what this is being equated to and it is not necessary that over time the value of this brand comes down and that is reflected in the fact that you are not showing an amortization in the P&L or the balance sheet.

Sandeep Gupta:
So to conclude basically the Ind AS would prevail over the court orders is that is the right way to read that?

Jamil Khatri:
In this instance as I said we do not perceive there to be conflict between the court order and Ind AS. Generically and not for GCPL, if there is a conflict between the court order and Ind AS this question is still open and the regulators are looking into this.

Sandeep Gupta:
In the finance cost line item there is one portion which comes because of the discounting charges. So would there be some change with respect to how the debt would get booked or probably the discounting would also lead to the debtors now coming into the book or something of that order?

V Srinivasan:
No, there is no change in the way in which the discounting transactions are accounted in Ind AS. What we have mentioned in case of finance cost are a couple of things which are changing like in zero coupon debentures, premium on redemption, etc. The premium cost being in the nature of finance cost, effectively as the return to the investors, will come as finance cost and secondly there are certain long-term liabilities which are being recorded at present value. So whatever discount rate you use to convert the liability into a present value liability that discount rate is used for interest unwinding and that amount is charged off as finance cost.

Sameer Shah:
We expect this interest cost which will come in the P&L to be in range of Rs. 12 crores to Rs. 15 crores so that is the maximum impact if any it will have also in the balance sheet. So the point is that there will not be any material impact behind this in the balance sheet.

Sandeep Gupta:
These discounting charges would be partly because of the receivable discounting?

Sameer Shah:
No, as what is mentioned even in the presentation on Slide #12, we have identified what are the two or three line items. So one is long-term liabilities and we have given few

examples like earn-outs in case of Strength of Nature and Canon acquisitions and our long-term employee incentives which more so in GCPL's case happens to be the performance linked variable remuneration. So largely it's only behind the two line items that we have interest unwinding and hence, to that extent the finance cost and interest cost goes up.

Sandeep Gupta:
So these discounting charges are not pertaining to any receivable discounting?

Sameer Shah:
No.

Moderator:
Thank you. The next question is from the line of Amit Sachdeva from HSBC. Please go ahead.

Amit Sachdeva:
If you look at the Slide #19, the excise duty say in the Q2 is Rs. 78 crores for example and in COGS the adjustment is say Rs. 88 crores. So the balance Rs. 10 crores is because of the consumer promotion in COGS?

V Srinivasan:
Yes, you are right.

Amit Sachdeva:
That is the only difference, right there is no other thing.

V Srinivasan:
Yes.

Amit Sachdeva:
Can you help me understand this earn-out a bit more clearly how we should sort of understand this because I am not yet fully clear. What I understand is if there is an earn out due in say three years from now we present value using some method and bring it to other current value using the discount rate which is like a debt borrowing rate?

Sameer Shah:
So just to again simplify this, there would be two potential impact because of the earn out which we have in Strength of Nature which as of now falls due at the end of third year. The first impact is the discounting which anyways we have shared earlier on this liability.

Second is basically the fair value of the liability which we have. So we estimate 'X' liability and 'X' could be 'y' plus or 'z' minus at a particular point in time. So that plus or minus is something which will be routed through P&L and that is the impact which could come in future. But again as mentioned at this stage, at least for FY-2017 we do not expect any meaningful material impact on account of fair valuation of the financial liability towards Strength of Nature earn-out.

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

Harit Kapoor:
Just on this Rs. 12 crores to Rs. 15 crores increase in the financial cost so, this would be over a four quarter period, right, it would not just come in Q1?

Sameer Shah:
Yes, this is spread out across four quarters.

Harit Kapoor:
Okay. And the fair value change again, if any, would be part of an exceptional item at the end of the year?

Sameer Shah:
Yes.

Harit Kapoor:
And third thing I wanted to check was, you mentioned that there will be a 150 bps to 200 bps increase in the overall tax rate on a consolidated basis for next year, right for FY2017?

Sameer Shah:
Yes.

Moderator:
Thank you. The next question is from the line of Ritesh Vaidya from Ambit Capital. Please go ahead.

Ritesh Vaidya:
On the return on the equity pre-exceptional,. what is the change in equity and what has brought this change because ROE has gone up with mostly no change in PAT?

V Srinivasan:
Yes, so in case of equity, it gets adjusted for the put option liability and deferred tax liability on brands and it is to some extent offset in parts by reversal of the interim dividend because unless the dividend is actually approved by the approving authorities it is not charged off to the P&L and, brand amortization, which is now not required. So that is the kind of adjustment because of which the equity goes down. So largely it is put option liability and deferred tax liability on the brands of the past.

Ritesh Vaidya:
Okay. And the total impact on the equity is around 15%-20%?

V Srinivasan:
Yes, it is around Rs. 700 crores to Rs. 800 crores.

Moderator:
Thank you. The next question is from the line of Vivek Maheshwari from CLSA. Please go ahead.

Vivek Maheshwari:
On the EVA based staff payments that you have anything to highlight which will be different under Ind AS?

Sameer Shah:
So just to again lay down a little bit context. So the way it works is we have performance linked variable remuneration which is based on delta EVA. However, the payouts are capped. So this entire impact is coming on the performance linked variable remuneration which is over and above the capped payout. The way it happens is the performance linked variable remuneration in absolute terms has a particular cap in terms of payout for the year and then there is subsequent period of payout in year one and year two. So this entire interest unwinding is coming on that liability which falls due in year one and year two to be paid out to employees. So that is the only change which comes in this.

Vivek Maheshwari:
So this is only to the extent of interest and not basically the principle payout?

Sameer Shah:
No, absolutely no correlation. So theoretically if the total performance linked variable remuneration was 100 of which 80 is paid out immediately and 20 is not paid out, the interest discounting will be on the 20 pay out assuming it falls in year one. In our case, the 20 is say 10 in year one and 10 in year two and hence, the interest discounting will be on 10 and 10 in year one and year two accordingly.

Vivek Maheshwari:
And would it be fair to assume that this will be only in the fourth quarter because by then you know whether the company has hit the target that it had set out beginning of the year. Is that a fair way of thinking about it?

Sameer Shah:
So Vivek this will start accruing as and when we breach the cap limit. So yes directionally, but it is highly unlikely it will come in quarter one and quarter two. If any, it would start coming in quarter three, yes that is right.

Vivek Maheshwari:
Second on the actuarial gains or losses, whatever it may be so, if there is a gratuity contribution that you make as long as actuary does not change base assumption of may be life expectancy or interest assumption, the incremental contribution will be routed through P&L it is only when the assumption change the differential will go to OCI is that correct?

V Srinivasan:
Correct, it is right.

Vivek Maheshwari:
Revenues are being grossed up for excise duty and not VAT. Also, will GST tilt towards excise or tilt towards VAT in terms of accounting?

Jamil Khatri:
I think the fundamental and conceptual reason is excise duty is a tax on manufacture and not on sale and that's how the principles flow because theoretically even if you had manufactured but you did not kind of sell it, the tax would be incurred. Therefore the rules require it to be treated as a cost line item and the recovery from the customer to be treated as the sales line item. As compared to sales tax and other sales linked taxes where it is a pass through to the government because generally what you collect or what you bill is what you pay out and that is really the rationale. Just one point of reference is we should not go by the name whether it is excise or sales tax. Globally as well, the right way to do it is to evaluate the nature of the tax. Look at whether it is linked to sales or manufacture and then take a call whether it is gross or net.

Vivek Maheshwari:
Okay. And would you have a view on GST, what is GST?

Jamil Khatri:
So the short answer is no, the accounting profession has not taken a view on whether it will be gross or net.

Vivek Maheshwari:
The A&P spends move down from Rs. 971 crores to Rs. 670 crores so, basically 70% of what the spend you had reported in FY2016 at consolidated level. When you look at from an MIS perspective, how would you think about these expenses for your MIS perspective? Would the management thought process and therefore analysis and all these things change based on the new Accounting Standards?

Sameer Shah:
I think internally the way of monitoring some of the spends will be all in the bucket of advertisements and sales promotions. Which again in the business parlance is ATL, above the line spends and BTL, below the line spends agnostic of whether it is getting netted off from revenues or whatever be the mode. So internally I mean we would continue to look at all of this as our advertisement and sales promotions spends which roughly hover in range of around 20% - 21% as a percentage of revenues for us.

Vivek Maheshwari:
On exceptional items on Slide #17, I presume bulk of these exceptional are because of the changeover? Other than that in FY2017, other things being equal, should be pretty much negligible number from an exceptional items perspective. Is that fair?

V Srinivasan:
Yes, absolutely correct.

Vivek Maheshwari:
Okay. So if that is the case at the time of change over did not have you an option of directly adjusting it to reserves or whatever in the opening balance sheet?

Sameer Shah:
No, Vivek.

Jamil Khatri:
Not in relation to these items. These items are items for the period and therefore kind of have to be reported as exceptional for the period.

Vivek Maheshwari:
Sorry, when you say for the period as in for the period of FY2016?

Jamil Khatri:
That is correct.

Vivek Maheshwari:
So in that case, why is that you believe that these items cannot get accounted as exceptional in FY17.

Sameer Shah:
Okay. So I think let me just again reword what Jamil said. I think the point which he was trying to bring out is because we had this stake change conversion happening in FY2016 for Darling from 51% to 90%, we had to recognize this in P&L. Whatever has happened say before 31st of March 2015, we had a flexibility of putting it in reserves. Now going ahead, why we are very sure that we would not expect any material impact; again this on two counts – one in FY2016 this is originated predominantly because of Chile moving from 60% to 100% which is now done with and Darling moving from 51% to 90% or 100%. Now if you look at Darling right now, in only couple of geographies we have remaining 10% stake buyout. As also mentioned earlier we have kind of reworked, revisited the agreement to take care that it does not route through P&L. The only impact, if any, would be behind the earn out revaluation in case of Strength of Nature which, at this stage, we are very confident that there will not be any P&L impact in exceptional line item in FY2017.

Moderator:
Thank you. As there are no further questions from the participants, I now hand the conference call over to Mr. Sameer Shah for closing comments.

Sameer Shah:
Thanks and thank you all for being on the call. In case if there are any incremental or follow on questions, we will be more than happy to walk you through. Thanks again.

Moderator:
Thank you very much. Ladies and Gentlemen, on behalf of Godrej Consumer Products Limited that concludes this conference call. Thank you for joining us and you may now disconnect your lines.