**Ref: SECT: STOC: 18-23**

25th January, 2023

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| To<br>The Secretary<br>**BSE Limited**<br>Phiroze Jeejeebhoy Towers,<br>Dalal Street,<br>Mumbai - 400 001 | To<br>The Manager,<br>Listing Department,<br>**National Stock Exchange of India Limited**<br>Exchange Plaza, C-1, G Block, Bandra-Kurla<br>Complex, Bandra (East), Mumbai – 400 051 |
| **Scrip Code: 519552** | **Scrip Code: HERITGFOOD** |

**Sub: Transcript of Conference Call with the Investors/Analyst**

Dear Sir / Madam,

In Continuation of our letter dated January 13, 2023 the Company had organized a conference call with the Investors/Analysts on Monday, January 23, 2023 at 16.00 PM (IST). A copy of Transcript of conference call held with the Investors/Analysts is enclosed herewith and the same has also been available on the Company's Website at www.heritagefoods.in.

Kindly take the same on record and display the same on the website of your exchange.

Thanks & Regards

For **HERITAGE FOODS LIMITED**

UMAKANTA BARIK Digitally signed by UMAKANTA BARIK Date: 2023.01.25 16:32:25 +05'30'

**UMAKANTA BARIK**
Company Secretary & Compliance Officer
M. No: FCS-6317

Encl: a/a

**About the Company:**
Heritage Foods founded in the year 1992 is one of the fastest growing Private Sector Enterprises in India, with two business divisions' viz., Dairy and Renewable Energy under its flagship company Heritage Foods Limited and Cattle feed business through its subsidiary, Heritage Nutrivet Limited (HNL). Presently Heritage's milk and milk products have market presence in Andhra Pradesh, Telangana, Karnataka, Kerala, Tamil Nadu, Maharashtra, Odisha, NCR Delhi, Haryana, Uttar Pradesh and Uttarakhand. It has total renewable energy generation capacity of 10.50 MW from both Solar and Wind for captive consumption of its dairy factories.

# HERITAGE FOODS LIMITED

# Q3 FY2023 Earnings Conference Call

# January 23, 2023

**MANAGEMENT:**

**MRS. N BRAHMANI** – EXECUTIVE DIRECTOR – HERITAGE FOODS LIMITED

**DR. M SAMBASIVA RAO** – PRESIDENT, HERITAGE FOODS LIMITED

**MR. A PRABHAKAR NAIDU** – CHIEF FINANCIAL OFFICER, HERITAGE FOODS LIMITED

**MR. SRIDEEP N KESAVAN** – CHIEF EXECUTIVE OFFICER, HERITAGE FOODS LIMITED

**MR. J SAMBA MURTHY** – CHIEF OPERATING OFFICER, HERITAGE FOODS LIMITED

**MR. UPENDRA PANDEY** – CHIEF EXECUTIVE OFFICER, HERITAGE NUTRIVET LIMITED

**MR. UMAKANTA BARIK** – COMPANY SECRETARY & COMPLIANCE OFFICER, HERITAGE FOODS LIMITED

**MODERATOR:**

**MR. ANUJ SONPAL – VALOREM ADVISORS**

**Moderator:** Ladies and gentlemen, good day, and welcome to the Heritage Foods Q3 FY '23 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. Should you need assistance during the conference call, please signal an operator by pressing star then zero on your touchtone phone. Please note that this conference is being recorded. I would now like to hand the conference over to Mr. Anuj Sonpal. Thank you, and over to you, sir.

**Anuj Sonpal:** Thank you. Good evening, everyone, and a very warm welcome to you all. My name is Anuj Sonpal from Valorem Advisors. We represent the Investor Relations of Heritage Foods Limited. On behalf of the company, I'd like to thank you all for participating in the company's earnings call for the third quarter and 9 months ended financial year 2023.

Before we begin, let me mention a short cautionary statement. Some of the statements made in today's earnings call may be forward-looking in nature. Such forward-looking statements are subject to risks and uncertainties, which could cause actual results to differ from those anticipated. Such statements are based on management's beliefs as well as assumptions made by and information currently available to management. Audiences are cautioned not to place any undue reliance on these forward-looking statements in making any investment decisions. The purpose of today's earnings call is purely to educate and bring awareness about the company's fundamental business and financial quarter under review.

Now let me introduce you to the management participating with us in today's earnings call and hand it over to them for opening remarks. We firstly have with us Mrs. N. Brahmani, Executive Director, Dr. M. Sambasiva Rao, President, Mr. S.N. Kesavan, Chief Executive Officer, Mr. A. Prabhakara Naidu, Chief Financial Officer, Mr. J. Samba Murthy, Chief Operating Officer, Mr. Upendra Pandey, CEO of Heritage Nutrivet, and Mr. Umakanta Barik, Company Secretary and Compliance Officer.

Without any further delay, I request Mr. Rao to now start with his opening remarks. Thank you, and over to you, sir.

**M. Sambasiva Rao:** Good evening to everyone joining us today on this call. We are pleased to welcome you all to this earnings call for the third quarter and 9 months ended for the current financial year '23. Financial results and earnings presentations have been uploaded on the exchanges and I do hope you must have got a chance to look at them.

Now let me take you through the financial performance of the quarter under review. Consolidated revenue for quarter 3 grew by 17.8% year-on-year to INR 786 crores despite inflationary pressures in our important markets. EBITDA during quarter 3 stood at INR 33 crores as compared to INR 41 crores during the previous year same quarter. The EBITDA margin stood at 4.15% in quarter 3 for current year. The decline in EBITDA was mainly on account of sustained increase of raw material costs, which were higher than the increases in the sale prices of products undertaken by us. During the current quarter, net profit stood at INR 14 crores.

Now I take up the 9 months performance. Consolidated revenue grew by 22% year-on-year at INR 2,423 crores. EBITDA is INR 96 crores and EBITDA margin stood at 3.97%. Net profit for the period was INR 40 crores.

Now moving on to the operational performance for the quarter. The average milk procurement during the quarter under review was 1.43 million liters per day as compared to 1.19 million liters during quarter 3 of last year. With regards to the sales of our products, we have had a healthy year-on-year growth across product categories. Average milk sales during the quarter 3 stood at 1.07 million liters per day compared to 1.04 million liters per day in the same period of the previous year.

The sale of curd during quarter 3 was at 294 metric tons per day compared to 271 tons per day. During this quarter, the value-added products revenue surged by approximately 21% year-on-year to INR 199 crores, and its contribution to the overall revenue increased 25.55%, while for 9 months ended, the contribution of value-added products was around 29%. We continued on our path to add innovative and unique value-added products. During the quarter, the company launched new products like Mawa Kulfi ice cream in bars, Matka Kulfi ice cream in matkas, and Chocolate Doodhpeda.

With this, we now open the floor for question-and-answer session. Thank you.

**Moderator:** The first question is from the line of Resha Mehta from GreenEdge Wealth Services.

**Resha Mehta:** So the first question is that if you could just comment on the milk price inflation that we are seeing right now. So has that moderated in Q4? And directionally, if you could just give some sense on the procurement prices, considering that the flush season has been weak. That's the first one.

Second, despite seeing healthy topline growth, we are not seeing the benefits of operating leverage kicking in. And here are two sub-questions. So first is on the employee cost. So historically, it's been in the sub-6% range, but now it's moved to that 7% of net sales range. So I understand that on the people front, we've added a lot of people across different functions. But where do we see this employee cost number settling? And the other sub-question is that are there any one-offs in the operating cost for Q3?

And thirdly, on the demand front, so because of the price hikes that we have been taking, are we seeing any sluggishness in the demand in the markets that we are operating? And the context for this is that if I look at the curd volumes, sequentially, curd volumes have dropped 10%, which is much sharper drop than the previous years.

And lastly, on the distribution. So we had outlined an aggressive plan to increase the number of Heritage distribution centers to around 1,000 in two or three years. But I see that since the last 9 months, the number has been constant at around 122. So has there been any change in the target? Or are we reevaluating the expansion plan? So yes, these are the questions.

**Samba Murthy:** Regarding this, procurement prices have gone up by 14% compared to the previous year same quarter. And the sales prices also have gone up by 17.5%, the same compared to the previous year quarter. And even compared to last year also, there is an increase of 2.35% in the sale price increase. And regarding this curd volumes, because of the seasonality, generally, Q3, the volumes will come down compared to Q1 and Q2. So that is that, whereas growth is there actually. In Q3, almost 17% growth is there compared to the last year same quarter.

**Srideep Kesavan:** Yes. Thank you, Murthy. This is Srideep. Resha, so if I could just add a few points to what Mr. Samba Murthy said. First is procurement prices, like he mentioned, sequentially, we have seen increases. And even at this point in time, we feel that the situation has not stabilized and we might continue to see some more inflationary trends going into the next few months. So that's something that we are preparing ourselves for. And as we speak right now also, we are seeing the trend continue.

Secondly, yes, you're right that the topline growth is something that we have delivered consistently and the bottom line is something that has been under strain for some time. And primarily, for us, this has been only due to raw milk price increases and not because of the other cost pressures. And I'd just like to -- you mentioned, for example, the employee cost increase. The employee cost increase for us is well within control. For example, in this particular financial year, we are within the financial budgets that we had created at the beginning of the year.

As far as direct employees are concerned, we are still a -- direct as well as indirect employees are concerned, we are still below 6% of revenue as far as the employee cost is concerned. So we do not see -- while there are definitely opportunities for improving the productivity of people, it's something that we are working on constantly, and with revenues growing, that will naturally happen as well. But at this point in time, we are not alarmed or we do not have anything to worry about as far as the employee cost is concerned.

And same goes with other operating costs as well. So you mentioned about other operating costs in our business. We have actually held our transport cost, which is the second biggest cost after employee cost. It is almost stagnant despite increases in the fuel prices and all of that because we have been able to improve the transportation or logistics productivity across our operations. In fact, in quarter 3, we have been able to deliver on many other operational cost improvement parameters, which we can discuss later. And those have also contributed to sustaining our profitability despite a significant increase of raw milk prices.

Curd contribution is something that the COO already addressed. I'm very happy to say that actually, even in this quarter, our curd revenues have grown at 18%. So curd has actually shown robust growth for us. In fact, the level at which we are operating curd at this point in time is giving us a lot of hope that we are entering the new summer season on a very strong footing.

The last question that you had raised is regarding distribution. We have a multi-model, multi-pronged distribution approach. You may recall that we had discussed that in the beginning. So we are not dependent on one channel alone for distribution. One of the strategic initiatives that we have taken up this year was the Heritage distribution center, which you're right, at this point in time, it stands at 122 distribution centers. In this running quarter, we have made some structural changes, in the sense we had closed on some of those underperforming distribution centers and opened 20-odd new centers.

So there has been a churn, which is why that number looks stagnant. The strategy remains one of the top priorities for us. We're not changing from that. The numbers might not show that, but we are progressing well on that initiative as well.

**Resha Mehta:** So just two follow-ups here. So see, my question was more on that now that we are seeing a healthy sales growth, we should see some improvement on the operating margin side. See, because if I look at your Q3 margins, your gross margins, in fact, have improved by 60 bps sequentially, while EBITDA margins have declined by almost 70 bps sequentially. So why aren't we seeing that operating leverage kicking in, if the topline growth is healthy?

**Srideep Kesavan:** There are a couple of reasons to this. The first is the market mix that we have. And we are pretty diversified as far as our market mix is concerned, and that is one aspect that we should remember at this point in time. So while some of our marginal non-core markets are seeing significant growth, so our growth, for example, if I could just break down our growth of 20%, 23% year-to-date, the marginal markets or non-core markets are growing anywhere between 50% to 100% rates. Now those markets will take some more time before the level of operational efficiencies or operational leverage that you spoke about, for the operational leverage to kick in.

So while our core markets have actually suffered due to increase of raw material prices, so it's purely a function of mix, which is actually causing or making it seem like the revenue growth is not or the operational leverage is not going in line with the revenue growth.

**Resha Mehta:** But I would imagine your core markets would be contributing a lion's share of your revenue. So it would be to the tune of 70%, 80%, 80%-plus kind of a number, if I'm not wrong?

**Srideep Kesavan:** That is right. So core markets contribute a significant contribution. At this point in time, it's around 70%. You're right about that. But the core markets are also dependent on milk that comes from outside. For example, Hyderabad has dependency on other markets, other milk-producing regions for its milk. And it's purely a function of how we are structured. And Hyderabad is our strongest, or Telangana is our strongest market, AP is also our strong market. And these are markets where we have had significant inflationary impact as far as the raw milk is concerned. And those marginal or fringe markets, where we have significantly improved, does not have sufficient contribution to move the needle when the core markets get impacted with raw material price increase.

So it's purely a function of the present mix that we have at this point in time. But what I should encourage you to look at, Resha, is that the fundamental on the business is actually improving quarter-on-quarter. So if I can just talk about, for example, the revenue growth itself, this is almost the sixth quarter that we are growing in teens or high teens or 20s, which means that we are consistently delivering on revenue growth quarter-on-quarter, year-on-year.

Secondly, we are improving our value-added product contribution even in the worst of times. In this quarter, we have grown our value-added product contributions unlike most of the competition. So these are all encouraging things that help us believe that we are just about to turn a corner as far as the margin profile and potential is concerned.

**Moderator:** Next question is from the line of Bhargav Buddhadev from Kotak Mutual Funds.

**Bhargav Buddhadev:** My first question is on advertising costs. Is there any increase in the advertising spend as a percentage of revenue? Because other expenditure, the number has gone up almost 25% Y-o-Y?

**Srideep Kesavan:** The advertising cost as a line item has not increased. The cost increase is marginal for this quarter, it's 0.6% compared to previous quarter -- previously, the same quarter, it's about 0.5%. So it's very marginal increase.

**Bhargav Buddhadev:** So is there any emphasis on boosting this number up? Because we are trying to pursue stronger growth on the value-added side.

**Srideep Kesavan:** So see, we have been able to deliver significant growth in value-added products and not just one quarter, but sequentially quarter-on-quarter for the last almost two years, we've been growing value-added products every quarter. So we have been able to do this without significant investment in marketing, advertising spends so far. We are coming to a stage where a certain number of our markets are having critical volume and scale of distribution as well as volumes that we are contemplating increasing our advertising spends in the coming season.

But that said, we will be doing that judiciously and cautiously, keeping our margin profile and margin potential, margin requirement in mind. So our strategy at this point in time is to continue to grow distribution, which still will be the biggest driver as far as value-added product contribution is concerned. And wherever required, wherever the distribution has reached a particular critical mass or critical number, we will be making strategic investments in advertising to increase the demand. So far, we are seeing robust demand as far as the consumers are concerned, and we are meeting that demand by delivering the products to the consumer.

**Bhargav Buddhadev:** And in terms of milk inflation pass-through, how much price hike is yet to be done to fully pass on the inflation in milk procurement prices?

**Samba Murthy:** So this 14%, we've passed on to the market at about 11.5%. So at abou, that is a 2%, 2.5% net.

**Bhargav Buddhadev:** And assuming a scenario where milk procurement prices soften maybe in the next three to six months, is there a case where dairy companies may also cut prices to pass on that softness? Or that will not happen given that the profitability has been significantly hit in the last 15, 18 months?

**Srideep Kesavan:** Not because of the historic profitability or the current financial situation, but we haven't seen prices coming down. I don't think that -- at least, if you look at -- if you take history as a lesson, it's a one-way street. Prices just go up.

**Moderator:** The next question is from the line of Aniruddha Joshi from ICICI Securities.

**Aniruddha Joshi:** Sir, this year we have not yet seen any meaningful flush season. So how do you see the milk prices remaining?

**Moderator:** Sir, there is some disturbance. May I request you to use the handset, please?

**Aniruddha Joshi:** I am on handset only. Sir, basically we have not yet seen the proper flush season. So how do you see the input prices? And also, how do you see the cattle feed prices moving up and their impact on the milk prices? Secondly, what was the sale of SMP in this quarter -- or rather SMP sales in this quarter versus last year same quarter? And the third question is the growth in B2B sales in this year, because probably it seems that with the opening of the economy, there is a higher sales in B2B market that is institutions, or hotel, restaurant, catering, HoReCa, as well as out-of-home consumption. So if you can indicate the growth in B2B sales?

**Samba Murthy:** Yes. Just regarding this procurement prices, procurement prices already gone up by 14%. Going forward, generally, when the season sets in, then procurement prices also will go up.

**Moderator:** Sir, sorry to interrupt. May I request you to please come a little more closer to the mic?

**Samba Murthy:** So regarding this procurement prices, so already the procurement prices have gone up or increased by 14%. And now we are entering into the season, that is summer season. So once the summer season sets in, prices also will go up. So that is the indication about the procurement prices.

Regarding the second point on the demand of HoReCa, our HoReCa contribution is negligible actually. So we won't focus on the HoReCa segment. So that is where there is not much impact on the HoReCa sales. So third is on?

**Upendra Pandey:** Cattle feed.

**Samba Murthy:** Cattle feed, yes. Probably, yes...

**Nara Brahmani:** As CEO of Nutrivet division, Mr. Upendra can take the question.

**Upendra Pandey:** So thank you, Mr. Joshi for asking this question. Regarding the cattle feed price, for next one month or so, we expect the same price will continue. After that, maybe there will be a 4 to 5% drop in the price of cattle feed.

**Aniruddha Joshi:** And last question on sale of SMP during this quarter versus last year same quarter?

**Srideep Kesavan:** So the question is about SMP. So Mr. Aniruddha Joshi, if I -- would you like to answer?

**Samba Murthy:** Generally, we will not sell SMP, only the consumer pack sale, which is very marginal actually. And it is not -- yes, we generally are not into the bulk sales of SMP. So generally, whatever we produce, generally that will be for our internal consumption only. And rather we will be short of SMP, then we'll be just buying and consuming it internally.

**Srideep Kesavan:** So in principle, there is something that I'd like to add. This is Srideep here. On the question of B2B sale, SMP sale, etcetera. See, we are highly focused on direct consumer sales. And all our business is built on selling to consumer and building our brand, Heritage. We believe, and this has been proven time and again, that B2B business is a business which is a commoditized business. Commoditized business has its ups and downs and has its risks. It's not something that we engage in much. In terms of, for example, there's a commodity, so there could be situations where commodity prices are good and people might make money, but it could go south as well. Our business is steady. We believe in selling every single day to the consumer. Consumers buy our brands in smaller packs, and that is what gives us the long-term earning potential.

**Moderator:** The next question is from the line of Ankur Kumar from Alpha Capital.

**Ankur Kumar:** I have two questions. One is on this raw material inflation. Is it a global phenomenon? Or is it India-specific? Because I was looking at SMP prices globally, they seem to be falling down.

**Srideep Kesavan:** Yes, you're right. Global SMP prices have come down in the last three to six months' time. And primarily, it is driven by sluggish demand in China. But unfortunately, India has a tariff barrier as far as importing of SMP is concerned, because India, as you know, is a self-sufficient country as far as milk and milk produced products are concerned. And because of that tariff barrier, India is very well insulated from the global market. So global markets for SMP prices do not impact much unless situation becomes that dire or drastic. The Indian situation is quite unique to India.

**Ankur Kumar:** Sure, sir. And sir, second question is on margins. So do you think current margins are the bottom that we have hit? Or do you think current -- as in this tough situation will continue for a couple of more quarters? Because as you are saying, RM prices will continue to go up. So can we take on enough price hike to improve our margins? Or how do you think the margin will move in the upcoming quarters?

**Nara Brahmani:** Yes. This is Brahmani here. We do see that we are entering the season not just for generally increased procurement prices, but also significant increase in sale of our value-added products. The highest contribution on sale of our value-added products starts off in Q4 and continues into Q1 of the financial year. So typically, as we've said earlier, and as you probably know, the EBITDA margins of these products are 2x that of regular liquid milk.

And we've been showing a consistent increase in not just the contribution, but also in terms of growth of value-added products and product sales. As my colleague Srideep had mentioned, we've seen, in the low season of Q3, an 18%-plus growth in terms of revenues. So having said that, what we feel is margins should strengthen going forward on the back of growth of value-added dairy products in the coming months and quarters to come.

**Ankur Kumar:** And ma'am, our long-term guidance is supposed to be 8% to 10% of EBITDA margin. So how soon do you think we can reach on those numbers?

**Nara Brahmani:** So I think today, about 75%, 80% of our realization goes to paying the farmer for the raw material. However, having said that, like we said, we've seen tremendous growth in value-added dairy products. We are also investing into growing those products going forward. We are targeting a contribution of packed products towards our revenues of close to 45% to 50% in the next couple of years, which will require some investments at the same time. So going forward, the season, when it comes to raw material volume increases, at the right times of flush, etcetera, sort of stabilizes going forward, we should be expecting these margins in the next couple of quarters to come. But this is heavily dependent on how the prices of raw material behave. But internally, we are taking a lot of actions to ensure that we optimize our operations. It's a continuous process. And I would request Srideep to allude upon that.

**Srideep Kesavan:** Sure. So one thing that we spoke about earlier is the gap of about 2.5% between the increase in raw material prices and the market net realization improvement. So if we can capture that gap, then our EBITDA profile improves and gets closer to the 8-percentage mark that you spoke about. But then at the same time, we are also aware that the raw milk prices may not have peaked yet, and it might go up further. So there might be at least few more months or quarters of catching up until such time as the animal population or the milch animal population increases and the milk availability improves to a certain level that it comes down. Usually, it takes about 12 to 18 months for such structural correction to happen.

So we might still have a few months ahead of us until the stability happens, because of which, to expand our margin, we have taken several initiatives at our end. One is to improve or reduce the cost of milk delivered to our factories. We have taken several initiatives to improve the efficiency of our raw milk procurement operations. For example, there was something that we spoke about in the last quarterly call also, we are significantly increasing the density of clustered procurement, which means actually the productivity of the procurement unit is increasing significantly. And we have made tremendous improvement on this in this quarter. For example, the milk procurement per unit has actually gone up by about 12%. This all means that the productivity at a unit operating level is improving.

Second is we have improved significantly the inward logistics of bringing the milk into the factories. We are also looking at many other ways of reducing that cost by rightsizing the vehicle. We are leveraging technology in terms of routing using geo coordinates and all of that, which is actually helping us reduce the number of vehicles drastically and reduce their kilometers run also. So there's a lot of efficiencies that we are working on in terms of raw milk procurement.

Second, in terms of operating efficiencies, we believe that we can reduce our operating cost by 10%, which is the cost of converting the raw milk to milk as well as the value-added products. 10% is the target that we have set internally for bringing in those operating efficiencies, and we are well underway. Many of those efficiency measures have been taken already.

The third is, of course, driving the net revenue, which is a direct outcome of improving sales of our value-added products because value-added products have got higher net realization. So all three put together should be able to help us expand the margin profile potential in addition to, of course, catching up, getting the net revenue increase closer to the raw milk increase, which I think is still a catching up game. Six to nine months is the time we'll probably need, not just Heritage, but I think the industry will also need for that flatten out.

**Moderator:** The next question is from the line of Sameer Gupta from India Infoline.

**Sameer Gupta:** First question from me, just a book-keeping one. Milk procurement prices and liquid milk prices for the quarter, usually you give that number.

**Samba Murthy:** So milk price actually, so it is about INR 52.29 per liter. And the procurement price is INR 43.70 per liter.

**Sameer Gupta:** Second question from me, sir, you've already taken 11%, 11.5% price hike this quarter, and previous quarters also we have taken price hikes. When I look at the liquid milk sales, they are up only 3%. And going forward, if milk prices are going to inflate further, is there room to take more price hikes? Are you not worried that you'll start losing consumers at some point? And if this assumption is correct, then until the next flush season, apart from the strategic levers that we are building on, which probably will be back-ended returns, our margins should remain subpar at least in the near term, is that a fair assumption?

**Samba Murthy:** Yes. Prices are -- actually, liquid prices are going up now, even value-added products price is also being corrected now in the market. So it's happening actually, even so far, quarters to come, December also we have taken up certain prices. That impact will come in this quarter. So prices are going up, sales prices also are going up.

**Srideep Kesavan:** Yes. If I could just add a couple of points. You're right that it's not like, at the end of the day, somebody has to pay for this. So we can't -- it's not possible for us to keep on increasing prices without end, which is the reason why there is a gap between raw milk prices of -- the money that's getting paid to the farmer has gone up much more than the money we have been able to collect from the consumer. So the reason why we are going cautiously as far as the consumer price is concerned is precisely because of the point that you raised because eventually, it's coming out of the pocket of the consumer.

But that said, so far, we have been able to increase prices without losing volumes. Yes, milk volume growth is slightly lower, but that is not only a function of the price increases. It is also a function of our focus on value-added products. So we are trying to convert as much of milk into value-added products, and we are letting go of some of the not so profitable milk volumes. So for example, some of the large packs where our realization is much lower, we have actually defocused on that. That is why the net growth in milk is slightly lower.

On your second question in terms of should you expect a softer margin profile going forward? I think the Executive Director had previously, already addressed that question. I hope that answers. If there is anything very specific, Sameer, you may please...

**Sameer Gupta:** Yes. I get what Brahmani had said. I also stated that in my question that apart from the strategic levers, which probably will give back-ended returns. I mean, value-added products will take its time to improve and the mix and the margins, they show up over a period of time. But that -- this is my question.

My last question is that our milk procurement, when I look at volumes, last four quarters, there has been a higher growth in that versus the liquid milk sales. So probably we have some buffer of lower cost milk. Should there be a breakaway inflation, I think we should be in a better position to protect margins. Again, is that a fair assumption or no?

**Samba Murthy:** Yes. I think we'll meet the sale requirement, whatever the sales growth plan is there. Definitely, if there is a price advantage, it will help us.

**Srideep Kesavan:** So our strategy is also that. See, we are working towards -- we feel that the shortage in milk doesn't stay that way for longer than nine to 12 months, because eventually, when the prices are attractive enough, the farmer will start producing milk. They might have missed, or small percentage of farmers might have missed an insemination cycle, but eventually the milch animal population should come back and production should restore or catch up with demand. This is there in any business. Supply and demand will eventually catch up. And when that happens, we'll be in a very strong position.

**Moderator:** The next question is from the line of Hitesh Sharma from White Sky. Since there is no response from the current participant, we will move to our next question that is from the line of Rohit Suresh from Samatva Investments.

**Rohit Suresh:** I had a question on the lumpy skin disease. So in the previous call, you had mentioned that in South India, there is no major issue on the lumpy skin part. But in your press release, you have mentioned that the flush season in South India has been impacted by the lumpy skin disease. So just wanted some clarity on that.

My second question will be on the non-core markets. So as you mentioned earlier in the call that the non-core markets are growing at 50% to 60%. So what is your strategy going forward for those markets? And lastly, on the curd, what are your peak volumes that you can achieve on an annual or a quarterly basis? If you could give me those numbers.

**Samba Murthy:** So yes, this is Samba Murthy here. So lumpy skin disease, actually as of now, the disease has subsided. There is not much impact in the field actually. So even entire country also, there are not much of lumpy skin disease cases actually. It has subsided.

**Srideep Kesavan:** Yes. With reference to -- and if your point is, like we are -- most of our procurement is in South India. It's not just South India, I think that Maharashtra and south of Maharashtra is where we procure. But then if there is impact elsewhere in the country, because of which certain companies migrate to Maharashtra to procure milk from Maharashtra and to compensate for losses elsewhere, that all adds up to inflationary cost, inflationary trends in Maharashtra. You can imagine. As in procurement, companies have moved into Maharashtra this year, more and more companies have moved into Maharashtra this year to procure the milk they might have lost because of lumpy skin disease. Maybe that, it's a reference to that. As far as South India is concerned, there were a few isolated cases here and there, but we are not seeing anything.

Yes. The other questions you have asked, I'll just try to quickly address that. One, yes, our non-core markets, which is markets outside of Telangana and Andhra Pradesh are growing much faster. As far as our strategy is concerned in these markets, it's very clear, we are working in a very capsulated fashion rather than spreading it too thin. We are focusing on certain suburbs of Mumbai and Pune. We are focusing on certain suburbs in Delhi NCR region and Haryana. So in Haryana, you will find us in certain cities. And in those cities, we are actually growing into a strong brand. So we are focused on Bangalore, we are focused on Chennai. So we are focused on urban markets. We are focused in a concentrated fashion. That's something that we are working on.

Secondly, we are working on building value-added products in these markets ahead of milk. So while in our core markets we are still milk dominated, many of these frontier markets, we are actually VAP-led, Value-Added Product led. So that's our strategy for growth. The third, as far as curd is concerned, may I clarify, is your question, what is our capacity, or is it how much can we do? Is that what you've asked?

**Rohit Suresh:** How much the peak that we can achieve on an annual basis, the peak that we can do?

**Srideep Kesavan:** Yes. So see, I think that will be speculative. I think at this point in time, we have capacities to do upwards of 800 tons, but then I don't want to give a number. All I can say is that we are growing in very high teens, 18%, 19% as far as curd is concerned. And we have not seen this growth slowdown at all for us. So we'll continue to grow. Quarter 1 for us looking, quarter 4 and quarter 1 is also looking very positive.

**Moderator:** The next question is from the line of Rajat Setiya from IthoughtPMS.

**Rajat Setiya:** So we have mentioned our aspirations to reach INR 6,000 crores in the near future. I wanted to understand what kind of capital expenditure do we need to do to be able to achieve those sales levels?

**Nara Brahmani:** This is Brahmani here. As mentioned earlier, capex expenditure is of different types. We need to keep investing into procurement, like my colleague had mentioned. High density of procurement is very important for us, and we've been a company that's been directly procuring from the farmers. So we take this very seriously. So that's one aspect of it. The other is on the plant operations side, which basically is focused on expansions as well as replacement capex of older machines for efficiency, etcetera.

And thirdly, in the market in the form of chillers, freezers, especially for our value-added dairy products, as well as investing into our newer channels for growth, where we have a more direct connect with our consumers. We expect this generally to be around INR 120 crores per year on an average going forward. However, depending on the years, it might be a little variable in the next three to five years. However, the average could be around INR 120 crores per year.

**Rajat Setiya:** The other question, once again, what kind of -- so this is related to the milk procurement that we do. So to achieve those sales targets, what kind of farmer reach do we need to achieve? I think currently, we are at 3 lakh farmers in eight states. So if you can help us understand about that?

**Srideep Kesavan:** So even this year actually, we have added quite a number of farmers. Close to 30,000-odd farmers have joined our ranks. But these 3 lakh farmers may not all of them will be active at all the time. It depends on the milch animals in their household at that particular point in time. So we are progressively adding farmers to cater to the growth. At this point in time, the growth in volumes that we are seeing is a mix of milk per farmer as well as the number of farmers joining. So if we say that we are growing in double digits as far as many procurement is concerned, it's a combination of both.

**Moderator:** Next question is from the line of Resha Mehta from GreenEdge Wealth Services.

**Resha Mehta:** Srideep, you made a very interesting comment on improving your milk procurement density. That per center, this has increased by around 12%. I believe that was the comment that I heard. So in this context, if you could just explain that -- for us, I think broadly, we've been at 3 lakh farmers, around 13 lakh liters per day procurement, so that's roughly 4 liters. And we've been thereabouts for quite some time.

So 4 liters per farmer, if I were to calculate it that way. So what steps have we taken to kind of increase this? And we've seen this 12% increase in milk procurement per center, over a period of time, or is it just in the last six months? And what steps specifically we've taken? Because I believe we were, in any case, deeply engaged with the farmers in terms of helping with their ancillary vet support, increasing milk productivity, etcetera. So what is it that we have specifically done that has improved the procurement per center?

And also, if you could talk a little bit about that typically, when we are present in a village, how many other dairy companies are present there? What would be our market share in terms of procurement from the farmers there? What would be the typical farmer attrition rate? And if you could break up your answer into how does it look like in your core markets of AP and Telangana? And in your new markets, if you could just comment on Maharashtra?

**Srideep Kesavan:** Yes. You asked a very detailed strategic question, Resha. A lot of things are a bit confidential in the way we operate. But if I can give you a sense of it and if that satisfies you, I'll be glad. First of all, you've divided the volume that we procured by 3 lakh farmers. As I mentioned, it's not like all 3 lakh farmers have an animal giving milk all the time, as the animals also go through a dry period.

And then they have to be inseminated, pregnancy, lactation comes back again. You can imagine. So even though we have 3 lakh-plus farmers, actually, we added 30,000 farmers this year, but not all of them are active at any point in time. Yes, as far as the milk production per farmer is concerned, we will roughly be in the range of 5 to 6 liters per farmer if I go by the ratios that you mentioned.

In terms of how we get more density, it's a choice we have. See, when we need milk, we can either go further-and-further into newer places and look for milk, or we can look for recruiting more-and-more farmers in the same village where we operate. So we actually choose to do the latter because it gives us more milk flow into the units that we have already existing. So it's a very high-level answer, I know, but I hope it satisfies you. I think we have got two options. One is we can go looking for new villages or rather we can look for new farmers in the same village. So we go for the latter, and that's what is helping us get more milk in an economical fashion.

Secondly, also in terms of -- I spoke to you about, we look at routing, which are the routes where we have poorer vehicle utilization. So if we can increase milk in that area, it probably helps us reduce the cost in that particular area. That kind of approach is what we are having. And we're still a long way as far as improving those metrics are concerned. But it is an area that we are focusing on and which will hold us in good stead in the years to come. That's all I meant.

**Nara Brahmani:** Resha, I just also wanted to emphasize on something that you briefly mentioned, but it's really core to the company's procurement growth strategy, which is the basket of welfare activities that we offer to the farmers directly. Over the period, we've mastered it and we've improved it. We are using technology to be able to more efficiently service the farmers, not just in terms of being very fair to them in terms of paying them in time and measuring the quality and quantity of milk, but also when it comes to facilitating third-party lending within a couple of hours for them.

It's a huge benefit that they see in terms of purchasing or procuring more cattle, newer cattle, and, hence improving their business. At this time, it's very attractive for them. As we've mentioned, procurement prices are high and it's very favorable for the farmers. So we've seen a significant increase in interest through this activity. We're also seeing a lot of interest in buying subsidized cattle feed that Heritage Foods itself manufactures and delivers at the doorstep of the farmer. We have two processing facilities and manufacturing facilities for our own cattle feed. And that's a huge attraction. That's a huge benefit for them.

And thirdly, I think on the technology part, our newly launched Heritage VET+ app has been a huge hit among our farmers. Today, as I speak, we have 17,000-plus subscribers on our YouTube page for this particular app. Farmers are seeing significant benefit of better animal care activities, feeding activities, how to deal with the diseases such as lumpy skin disease, etcetera. In fact, there are several functionalities such as the option of indenting cattle feed through the app itself. So technology has been exceptionally empowering. And I think a mixture of all these basket of welfare and input activities is benefiting and will continue to benefit us going forward and give us a competitive edge.

**Resha Mehta:** And my second question is on the supply chain. So do we own the temperature-controlled vehicle fleet? I think we have some 2,000-odd distribution vehicles. So do we own them or are they outsourced? Or it's a combination? And what is the standard industry norm? And how do we think about this?

**Srideep Kesavan:** No, we don't own any vehicles. We hire them from the market.

**Resha Mehta:** But does that lead to higher wastage in terms of raw milk spoilage or something of that sort, or?

**Srideep Kesavan:** No. These are vehicles which are standard. So we have a very -- see, we've been doing this for the last three decades. So method of shortlisting vendors based on their capabilities, there's a very strong quality process in place, which ensures that the vehicles are of certain quality which we inducted. There's a strong negotiation process that we have, which keeps us at the lowest end of the market price. So we feel that's working fine for us.

**Nara Brahmani:** Yes. And Resha, I'd like you to keep in mind the fact that milk is extremely fresh. So the turnaround time is very quick from the time of procurement of milk from the farmer to making the milk or milk products available to the consumer within, anywhere between 24 to 36 hours mostly. So I think the wastage in the process is none, as a result of that because milk moves around very quickly. It's very fresh. We have to move it around quickly to make it available to our consumer, to our channel on a daily basis. So we don't see any such challenges in our value chain.

**Resha Mehta:** Sure. That helps. And I have some more strategic questions around your procurement, but I think I'll take them offline.

**Srideep Kesavan:** Thank you, Resha.

**Moderator:** Thank you. Ladies and gentlemen, that would be our last question for today. I now hand the conference over to Dr. Rao for closing comments. Thank you, and over to you.

**M. Sambasiva Rao:** Thank you very much for your continued interest in Heritage, and we'll be getting back to you soon for the next quarter. And meanwhile, I have a positive news to share. Our company's credit rating has been upgraded from A to A+ recently. Happy to share with you. Thank you very much.

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

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