THE TRANSCRIPT

Sep - Dec, 2022

#INVESTFORGOOD

DSP
MUTUAL FUND

This is a compilation of observations & comments from AGMs/ Concalls/ Interviews/ Presentations.
The compilation should not be used for investment decisions. Read our disclaimer below and at the end.

SEGMENTS

1. **Unorganized:** Periphery Strikes Back?
2. **Tobacco:** Stuck In Groundhog Day
3. **Cement:** Capacity Conundrums
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QUOTE OF THE QUARTER

***When you get market development right - it trumps macroeconomics*.**

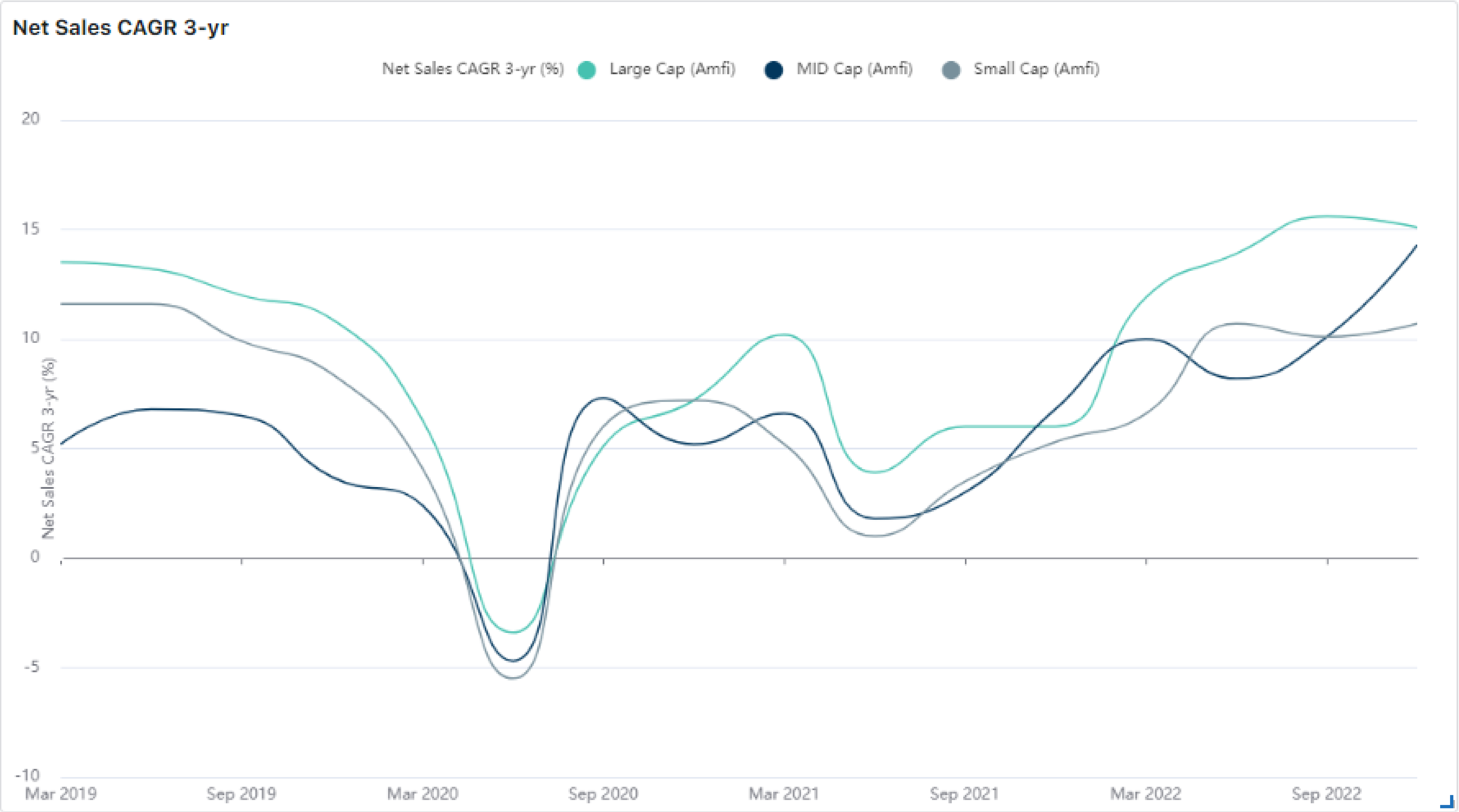
Sudhir Sitapati | CONSUMER PRODUCTS

Unorganised: Periphery Strikes Back?

DSP

Multiple companies indicated increased competition from unorganized sector in this quarter. One possible reason for this resurgence could be the sharp decline in commodity prices which may be providing a fresh lease of life for the unorganized players.

There has been significant downtrading in certain segments as well. In the organized space the Large Cap companies continue to grow faster than Small Caps. What is termed as “unorganized” could also just be private labels & direct to consumer E-Commerce. Can you guess the GMV for Meesho?



Source: Internal, Company Reports

Unorganised: Periphery Strikes Back?

DSP

We see a lot of times, people come up with this notion that there is going to be a radical change in the business because of lockdown or because of other factors and the unorganized sector will die out. I think once bitten twice shy. So what we have seen after demonetization, after GST, after the rollout of E-Way Bill and now after lockdown is the ingenuity of the Indian entrepreneurs cannot be challenged. So the unorganized sector has revived. I think, yes, we have taken some market share away because of the innovation that we have done, but the destruction in the unorganized sector has not been substantial in any which way.

Q3 FY21

Demand (in laminates) is relatively weak and the competition from the unorganized has increased.

CENTURYPLY®

Unorganised: Periphery Strikes Back?

DSP

As far as rural is concerned, there people are cutting back on their expenses and down-trading on products and actually choosing among the consideration set, it's not necessarily a brand. So, a lot of smaller brands have made their way into the rural market just because they are actually cheaper. So that is one sense, which is there is down-trading.

Dabur

(The nature of competition in pumps) A lot of it is attritional. A lot of it is local.

Crompton

(Competition) has become more intense, because during COVID, lot of players were not able to really supply. Now everybody has come back, everybody has ample supplies

PAGE INDUSTRIES LIMITED

Unorganised: Periphery Strikes Back?

DSP

So gross margin, if you look at it has been in the similar range even with a better standard ratio and even with a better non-South revenue, okay. That is basically because of the pressure from the unorganized segment in the gold pricing itself. The gold rate itself has a pressure and there's high competition with regard to that, especially from the unorganized segment.

KALYAN JEWELLERS

The two large branded players (in beverages), both of them have lost share to the loose end locals. That in my mind is a temporary phenomenon, which should get corrected as we go forward.

TATA CONSUMER PRODUCTS

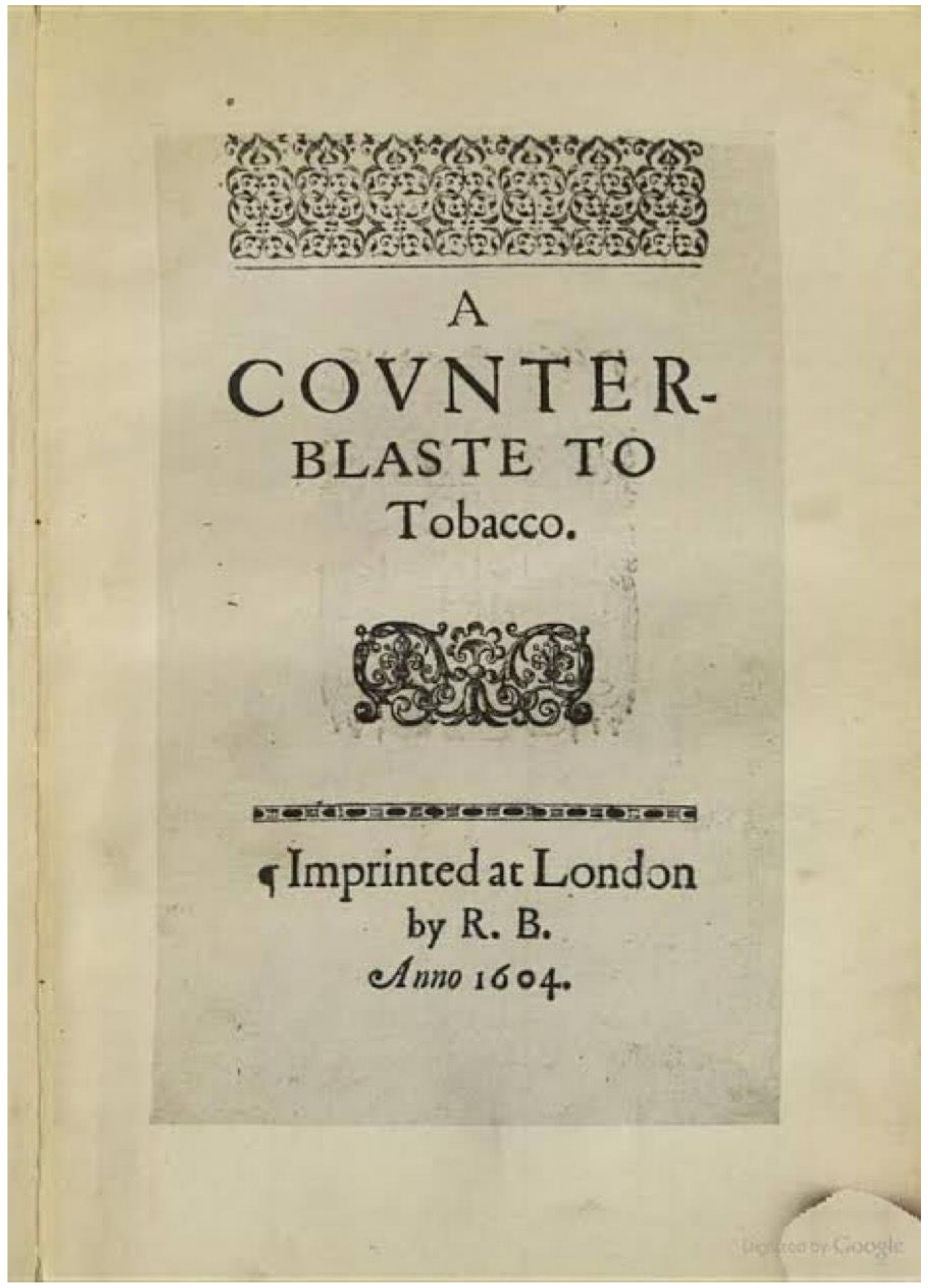
The cables and wire, I think, has been competitive right from the beginning and it will continue to remain so. And as you just mentioned, some brands are coming on the B2Cside. In fact, the more they come, in fact it gets easier and it becomes better to actually reorganize the unorganized sector to these -- towards the organized sector. So that is all beneficial. I think our focus has always been at how do we grow faster than what the market and gain market share..

HAVELLS

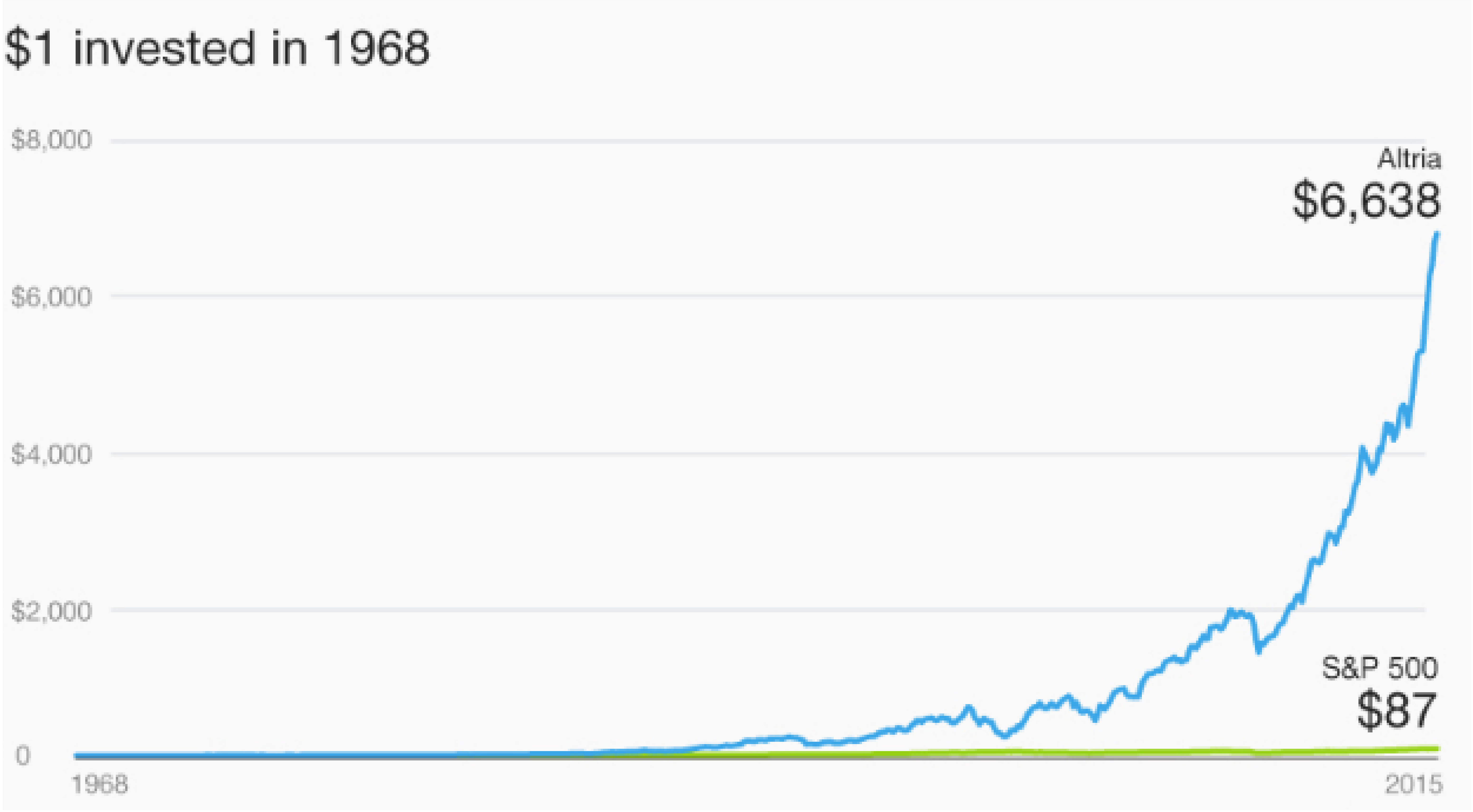
Tobacco: Stuck In Groundhog Day

In 1604 King James of England, instituted an excise tax on Tobacco. In his treatise, Counter Blasts To Tobacco, he (rightly) called the product, "loathsome to the eye, hateful to the nose, harmful to the brain, dangerous to the lungs".

Throughout history, tobacco and cigarettes have been subject to high taxes and have raised concerns about their harmful health effects. This has often limited competition. Companies like Phillip Morris/Altria & ITC have generated significant wealth for shareholders over the years. A lot of these companies have been trying to diversify away from their core.



Source: New York Public Library



Source: CNN Business

Tobacco: Stuck In Groundhog Day

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The cigarette industry contributes nearly 90% of Government revenue from tobacco, even though it accounts for less than 20% of tobacco consumption in India. Hence, any growth in the share of cigarettes within the tobacco basket, helps to expand the tax base. The small size cigarettes (of length less than 60 mm) helped the cigarette industry to achieve a record volume in 1996/97, thereby enabling a larger number of tobacco users to upgrade to the most modern form of tobacco consumption. Simultaneously, this helped to expand the tax base for the exchequer by bringing a larger number of tobacco users in the tax net. Unfortunately, the excise increase of 20% announced in the recent Union Budget, may reverse this trend, as smokers in the lowest price slabs are forced to convert to other forms of tobacco, which yield marginal revenue. This is likely to impede revenue accretion, and thereby sub-optimise the revenue potential of this sector.

ITC Annual Report 1997

Over the years a large grey market of international brands of cigarettes has developed in the country. This market is growing rapidly at nearly 25% per annum and currently represents an unaccounted drain of foreign exchange of over Rs. 300 crores and an estimated revenue loss to the exchequer of around Rs. 200 crores. This apart, there is a loss of corresponding economic activity within the shores of the country.

ITC Annual Report 1998

Tobacco: Stuck In Groundhog Day

DSP

Indeed, India would probably be the only country in the world where 85% of tobacco users are virtually outside the tax net.

ITC Annual Report 1999

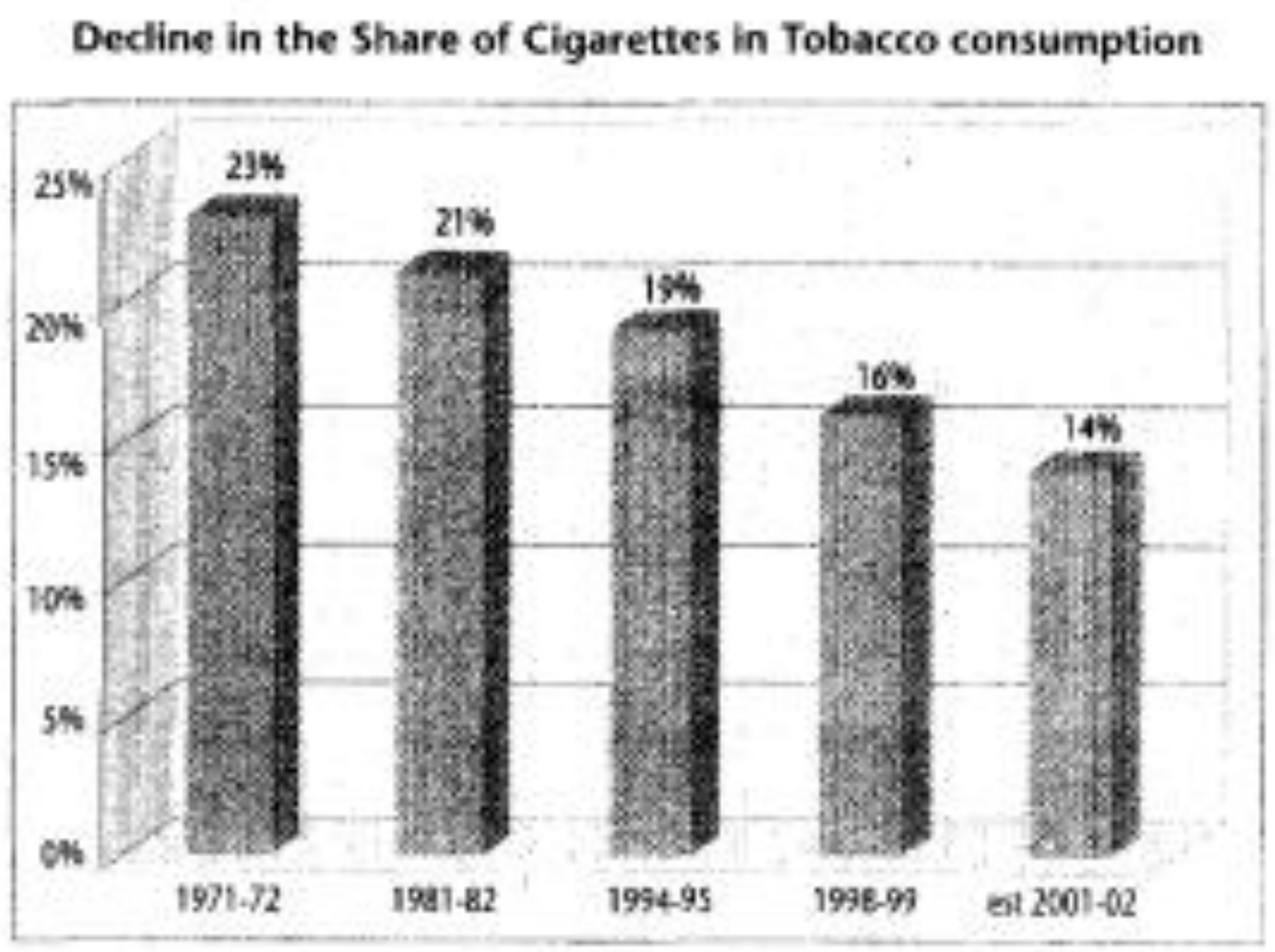
High rates of taxation, particularly at the upper end, have also spawned a flourishing trade in smuggled cigarettes. Recent conservative estimates indicate that smuggling in cigarettes is causing an unaccounted outflow of foreign exchange of anywhere between Rs. 500 Crores and Rs. 1000 Crores, and the related loss of revenue to the Exchequer that would otherwise accrue on equivalent domestic manufacture. This contraband trade is estimated to be growing at an alarmingly high rate upwards of 20% per annum.

ITC Annual Report 2000

The menace of contraband cigarettes is well recognized the world over. According to one estimate, one third of the total world trade in cigarettes is contraband in nature. Since tax is avoided in the exporting country and evaded in the consuming country, smuggling of cigarettes has become lucrative and appears to be highly organized. The regulatory framework in respect of tobacco products needs to be pragmatic and equitable, such that the regulation of tobacco consumption is orderly and progressive, securing maximization of economic contribution even in a shrinking basket of tobacco consumption.

ITC Annual Report 2001

Tobacco: Stuck In Groundhog Day

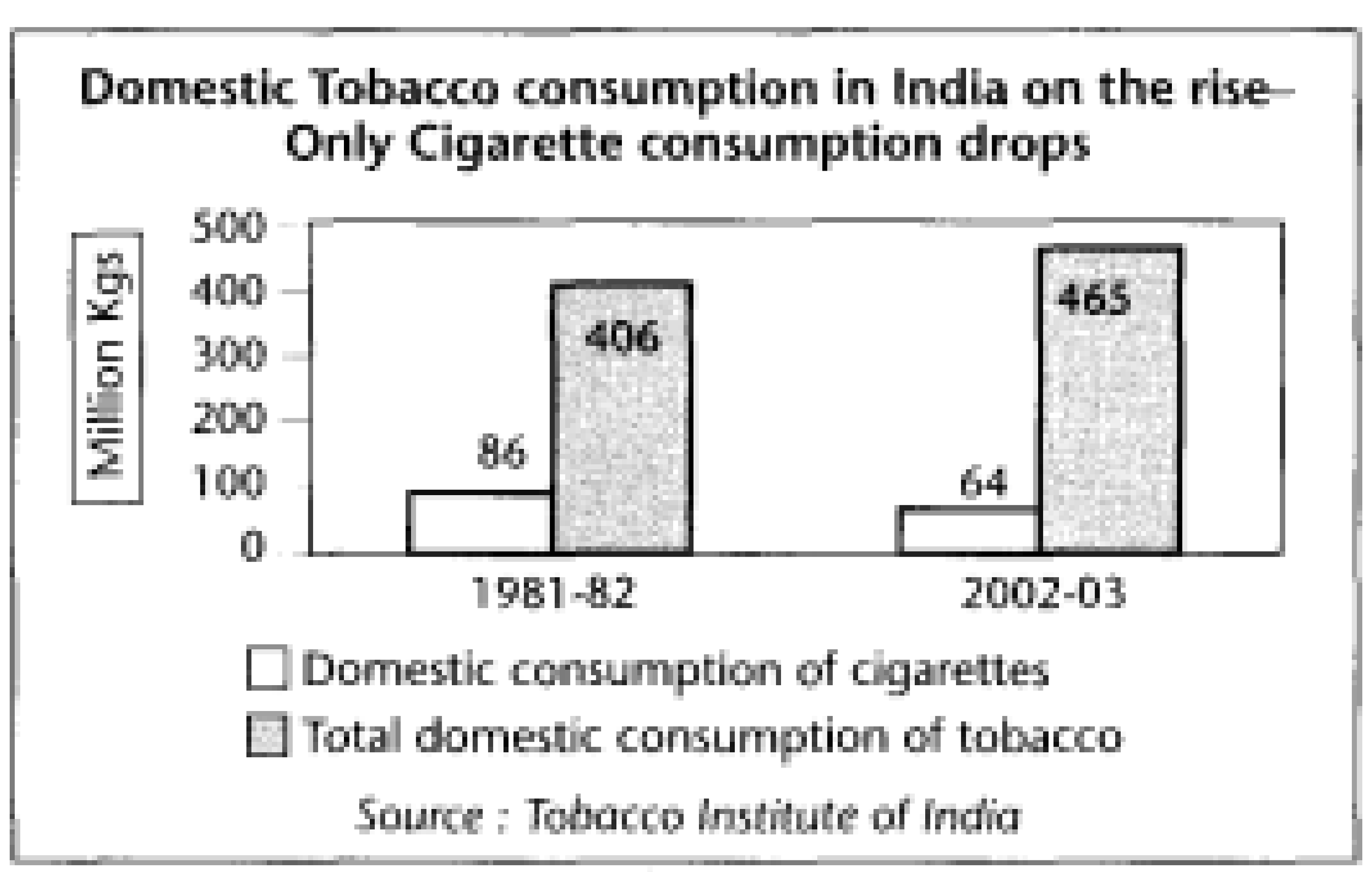


ITC Annual Report 2002

Country	Per Capita Adult Cigarette consumption per annum
India	**119**
Bangladesh	232
Pakistan	562
Nepal	628
China	1,315
UK	1,833
USA	2,372
Japan	2,855
World Average	**1,267**

Source: Tobacco Institute of India

ITC Annual Report 2003



ITC Annual Report 2004

The need of the hour, therefore, is to reduce the difference in effective tax rates across classes of tobacco products in manner that maximizes contribution to the Exchequer from tobacco sector even in shrinking basked of overall tobacco consumption.

ITC Annual Report 2005

Tobacco: Stuck In Groundhog Day

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Despite comprising such a low share of tobacco consumption, cigarettes contribute 90% (approx. Rs. 8000 crores) of the total Central and State tax revenues generate from tobacco sector. This is on account of the fact that on a per kg of tobacco basis, cigarettes are taxed 34 times higher than other tobacco products.

ITC Annual Report 2006

Excise Duty Collected from Tobacco Products in India

(Rs. Crore)

Product	2001/02	2002/03	2003/04	2004/05	2005/06	Cumulative Growth (%)
Cigarettes	5342	5427	5662	6185	7242	36%
Growth	-0.8%	2%	4%	9%	17%	
Other Tobacco Products	1384	1284	1152	1134	1134	-18%
Growth	NA	-7%	-10%	-2%	—	

Source : Answer to Rajya Sabha unstarred question no. 4242 dated May 3, 2005 and Tobacco Institute of India.

ITC Annual Report 2007

The combined impact of the increase in the rate of excise duty by more than 6% and imposition of VAT @ 12.5% ad-valorem – without a corresponding reduction of excise duties collected in lieu of State level sales tax – resulted in a total increase in tax incidence of about 30%.

ITC Annual Report 2008

Unlike international markets, it is a serious misconception to equate tobacco consumption with cigarettes in India. On an average, cigarettes account for about 90% of tobacco consumption globally, with an even higher share of almost 100% in large markets like China. In sharp contrast, in India consumption of tobacco in cigarette form has steadily declined from 23% of total tobacco consumption in 1971/72 to less than 15% currently.

ITC Annual Report 2009

Tobacco: Stuck In Groundhog Day

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Tobacco Consumption (Million kg)			
Year	Cigarettes	Non-Cigarette Forms	Total
1981/82	86	320	406
2008/09e	74	421	495
Difference	(–) 14%	(+) 32%	(+) 22%

Source : USDA; Tobacco Institute of India

ITC Annual Report 2010

Disproportionate taxation coupled with a growing incidence of smuggling and illegal manufacture, continue to be the biggest challenge for the Indian cigarette industry. India now ranks 6th globally in illicit cigarette trade with one of the highest growth rates - 58% over the period 2004 – 2009. It is estimated that the illegal cigarette trade costs the Exchequer more than ` 3000 crores per annum in lost revenues apart from offering products of dubious and inferior quality to consumers.

ITC Annual Report 2011

The domestic legal cigarette industry is faced with the growing menace of illegal cigarettes. Independent research indicates that, in India, whilst there is a fall in volumes of 'duty paid' cigarettes by 4.4% during the period 2005 to 2010, the 'duty-not-paid' volumes grew by 49.3% during the same period. India has now been recognized as one of the leading destinations for illegal cigarettes.

ITC Annual Report 2012

Tobacco: Stuck In Groundhog Day

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India has a miniscule share of only 1.8% of global cigarette consumption but accounts for about 90% of the global consumption of smokeless tobacco. According to the Global Adult Tobacco Survey, 2010 conducted by Ministry of Health and Family Welfare, Government of India, while 34.6% of all adults in India use tobacco in some form, only 5.7% of the adult population consume cigarettes.

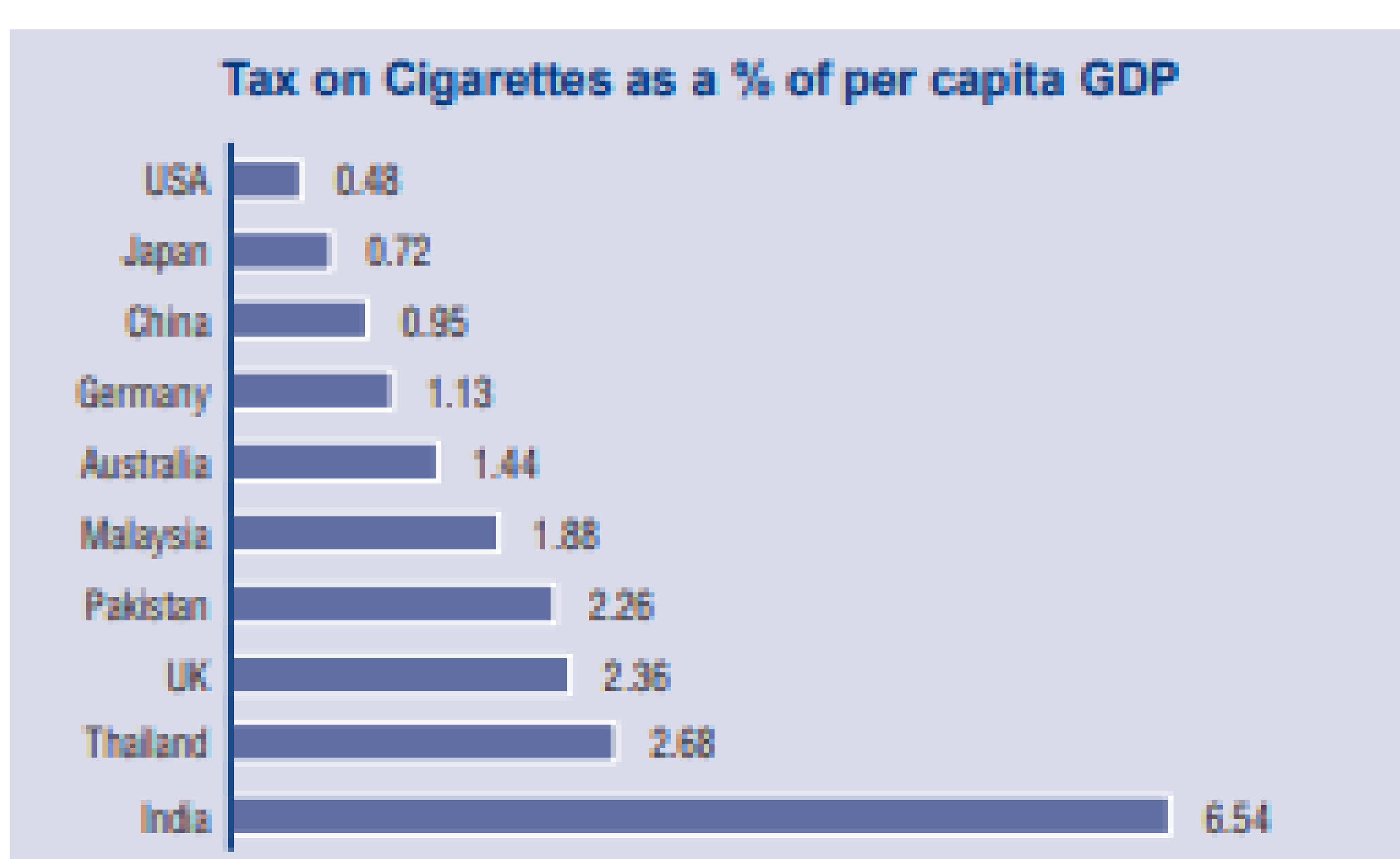
ITC Annual Report 2013

Uttar Pradesh and Punjab, which had increased VAT rates to punitive levels of 50% and 55% respectively, witnessed a huge decline in legal cigarette volumes even as illegal and duty-evaded cigarettes gained significant traction leading to loss of potential tax revenues. The recent pragmatic decisions of the State Government of Uttar Pradesh and Punjab to rationalise VAT on cigarettes is a step in the right direction and is already showing positive results in terms of revenue buoyancy and arresting the growth of illegal trade.

ITC Annual Report 2014

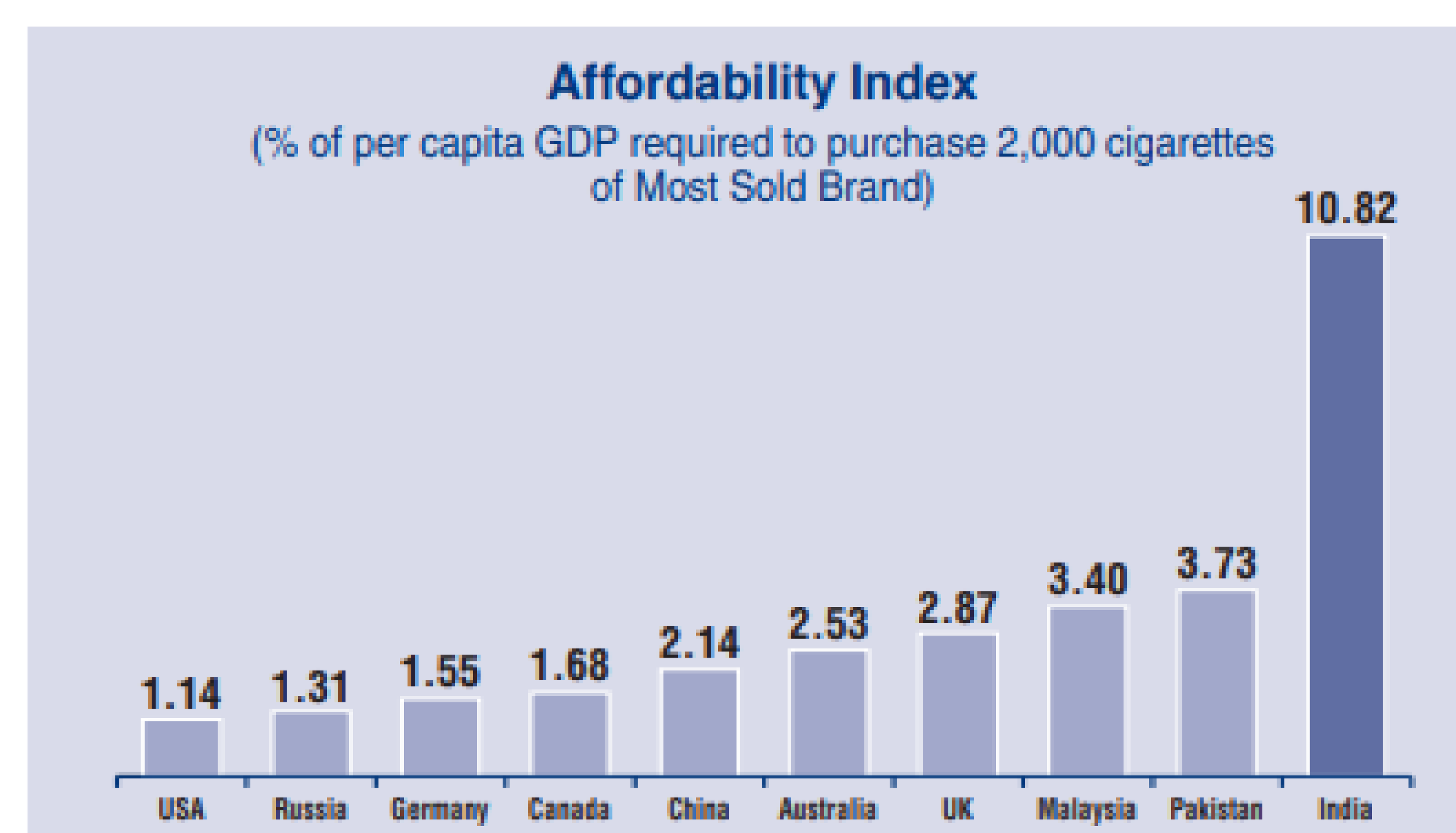
According to an independent study conducted by Euromonitor International - a renowned global research organization - India is now the 5th largest market for illegal cigarettes in the world. In fact, illegal trade comprising smuggled foreign and domestically manufactured tax-evaded cigarettes is estimated to constitute one-fifth of the overall cigarette industry in India resulting in a huge revenue loss of over ` 7000 crores per annum to the national exchequer.

ITC Annual Report 2015



Source: WHO Report on Global Tobacco Taxation, 2015

ITC Annual Report 2016



Source: WHO Report on the Global Tobacco Epidemic, 2015 - Raising Taxes on Tobacco

ITC Annual Report 2017

Tobacco: Stuck In Groundhog Day

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The Indian tobacco control laws have, had the inadvertent and unforeseen effect of causing losses to the Indian farmer with corresponding gains to tobacco farmers in the countries that have opted for moderate and equitable tobacco control laws.

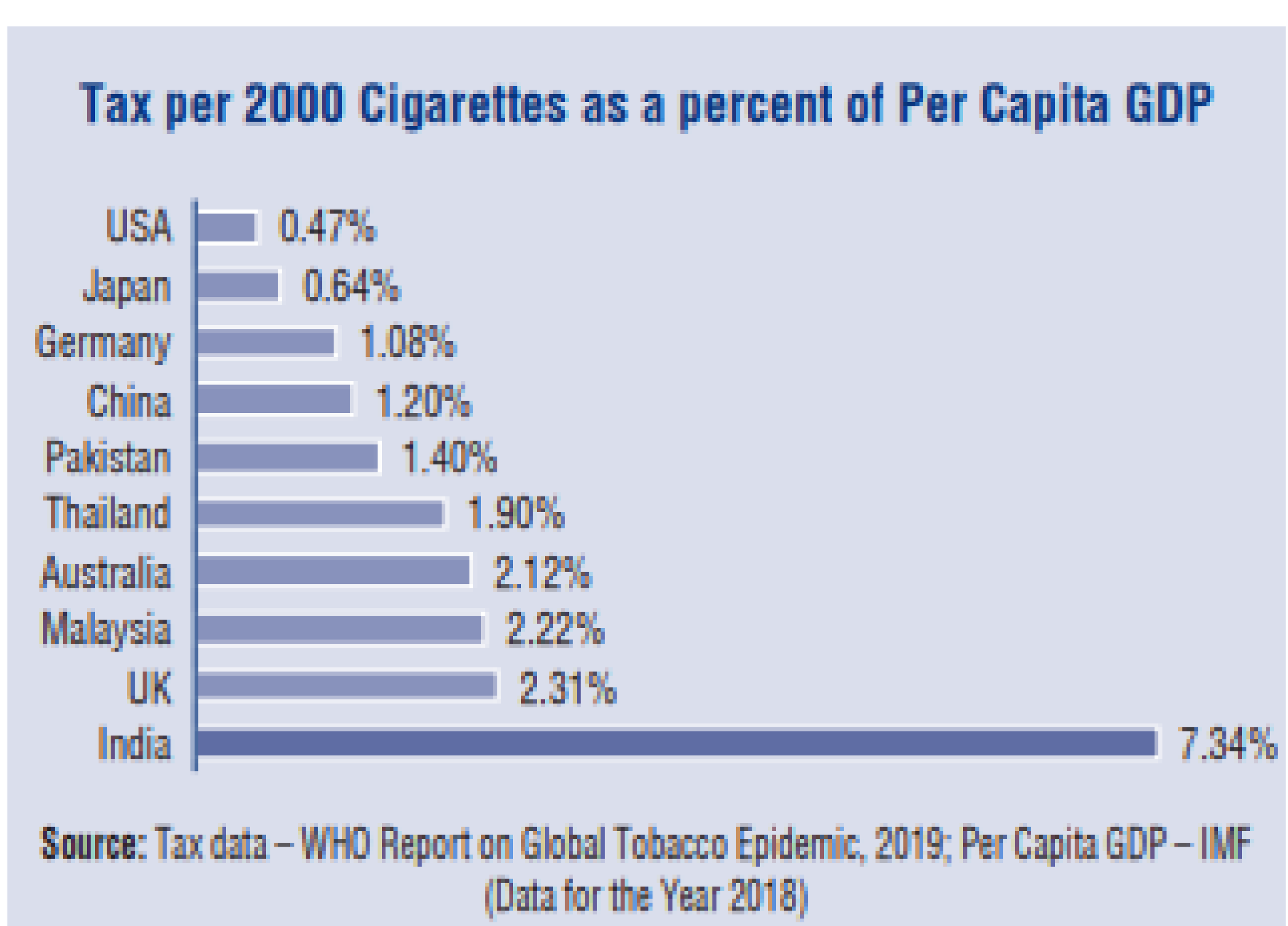
ITC Annual Report 2018

The legal cigarette industry, already reeling under the cumulative impact of steep increase in taxation over the previous five years in the pre-GST regime and intense regulatory pressures, was further impacted by a sharp increase of 13% in tax incidence on cigarettes (19% increase for the king-size filter segment) under the GST regime. Coupled with the increase in Excise Duty rates announced in the Union Budget 2017, this resulted in an incremental tax incidence of over 20% on cigarettes, post implementation of GST.

ITC Annual Report 2019

A punitive and discriminatory taxation and regulatory regime along with a sharp increase in illegal trade in recent years, especially at the premium end, continue to pose significant challenges to the legal cigarette industry in the country.

ITC Annual Report 2020



ITC Annual Report 2021

Taxes on cigarettes in India are multiple times higher than in developed countries viz. 17x of USA, 10x of Japan, 7x of Germany and so on. Further, the same is also substantially higher than that in neighboring countries. It is pertinent to note that India's per capita cigarette consumption is amongst the lowest in the world and is significantly lower compared to that of China, Japan, USA, UK and even neighboring countries such as Bangladesh and Pakistan.

ITC Annual Report 2022

Cement: Capacity Conundrums

DSP

"Replacement Cost" is often used as a Valuation metric for cement companies. **How much peak cement capacity would India need?** As urbanization peaks cement demand also plateaus and then comes down. US consumes about 110 MT of cement compared to approximately 380 MT for India. Current capacity is about 580 MT - capacity utilization is about 65%.

When compared internationally, if India's per capita cement consumption was to peak/plateau at that of world average of ~550 Kg/person, India would need installed capacity of ~1150 MTPA at 70% utilization. In a more bearish case, if cement demand plateaued at world-average (ex China and India) at 60% utilization India would need 770 MTPA capacity. Hence, the recent announcements of cement capacity addition aspirations in India, which could take our cement capacity to over 850 MTPA by 2030, leave limited room for capacity addition beyond that.

- Bernstein Research

	2019	2020	2021	2022	2023E	2024E	2025E	2026E
All-India								
Closing installed capacity (mtpa)	486	507	533	552	579	599	648	710
Incremental installed capacity (mtpa)	16	21	26	19	27	20	49	63
Effective capacity (mtpa)	486	507	533	552	579	599	648	710
Incremental effective capacity (mtpa)	16	21	26	19	27	20	49	63
Capacity growth (%)	3.5	4.4	5.0	3.6	4.8	3.5	8.1	9.7
Cement consumption (mn tons)	333	330	330	354	383	418	439	466
Incremental consumption (mn tons)	39	(3)	1	24	29	35	21	27
Consumption growth (%)	13.4	(0.8)	0	7.1	8.1	9.1	5.1	6.1
Cement production (mn tons)	337	334	335	359	387	422	443	470
Incremental production (mn tons)	39	(3)	1	24	29	35	21	27
Growth (%)	13.3	(0.8)	0	7.0	8.0	9.0	5.0	6.0
Capacity utilization (%)	69	66	63	65	67	71	68	66

Source: CMA, Kotak Institutional Equities estimates

Cement: Capacity Conundrums

The way things are going, we have already commissioned 6.8 million tons during the first nine months and we'll commission close to10 million tons in the next few months. Further, work has already commenced in full swing on the Phase 2 expansion of 22.6 million tons. Long-lead item orders have already been placed and civil work has already started at most of the sites. We should be able to deliver this capacity expansion on time by '25 - '26.

We would like to grow at our own pace. Just because others are doing fast, does not mean that we also start running faster. So we believe we have given you guidance, 80 million ton in 2030 and we would like to stick to it. Just because the industry is adding up fast, we will not, we will maintain our own pace.

We remain committed on doubling the capacity goal which is a five year goal, we had set in September – on the day of the takeover.

Cement: Capacity Conundrums

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We remain committed to our interim capacity milestone of 75 million tons by financial year '27 and long-term goal of 110 million to 130 million tons by 2031.

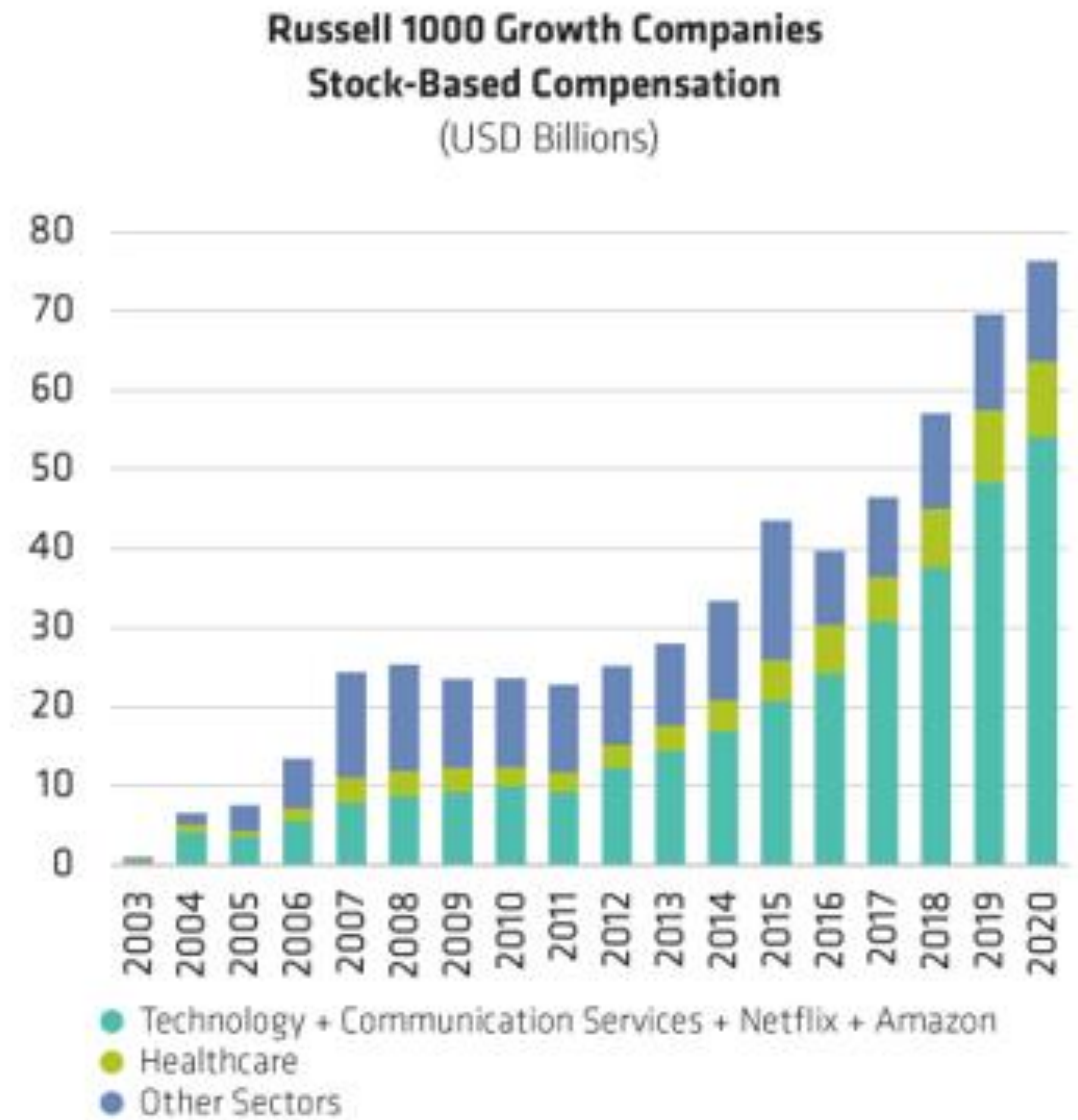
Dalmia Bharat Cement

Cement (clients), we've got new capacity coming in. So previously we were going through a wave of brownfield replacements for waste heat recovery. Going forward, we will be seeing new capacity coming in and then the tail end of the waste heat recovery cycle

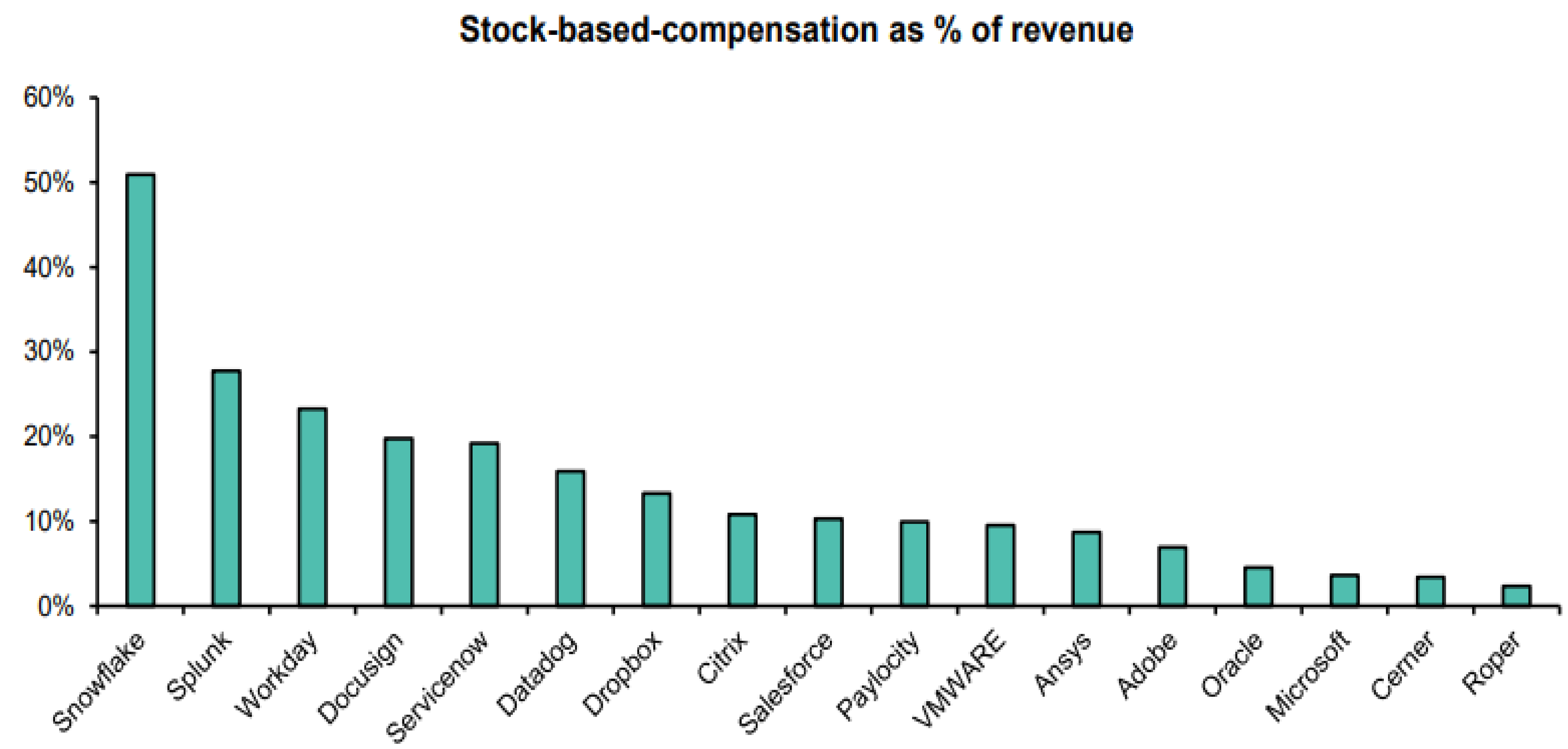
THERMAX

Stock Based Compensation: Real Cost

Stock based compensation, where employees get shares of the company became popular in 1980s. It was a convenient way for cash starved companies to attract and retain talent. It is believed that this also aligns the interest of the employees with those of other stakeholders. Since 2013 stock based grants have picked up significantly in US particularly in the technology sector.



Past performance and current analysis do not guarantee future results.
As of December 31, 2020
Source: FactSet, FTSE Russell and AllianceBernstein (AB)



Source: Company reports, Bernstein analysis
Figures represent numbers for FY21

Stock Based Compensation: Real Cost

DSP

Name	Total TTM SBC Cost	SBC As A Percentage Of TTM Revenue
Matterport, Inc. (MTTR)	$183.5 Million	151.7%
C3.ai (AI)	$179.6 Million	66.5%
Robinhood Markets (HOOD)	$811.4 Million	60.5%
Snowflake, Inc. (SNOW)	$756.5 Million	40.6%
SentinelOne, Inc. (S)	$144 Million	39.8%
The Trade Desk (TTD)	$576.5 Million	38.8%
Okta, Inc. (OKTA)	$669.6 Million	38.6%
Unity Software (U)	$474 Million	37.7%
Asana, Inc (ASAN)	$178.1 Million	35%
Zscaler, Inc. (ZS)	$424.8 Million	34.9%
UiPath, Inc. (PATH)	$347.8 Million	33.4%
Palantir Technologies (PLTR)	$602 Million	32.8%
Bill.com (BILL)	$231.9 Million	30.7%
MongoDB (MDB)	$353.1 Million	29.6%
Alteryx, Inc. (AYX)	$202.9 Million	27.8%

Source: https://seekingalpha.com/article/4563868-stock-based-compensation-list-of-worst-offenders-and-few-best
Dec, 2022

If you get stock options at $200 and you exercise it when the stock is higher– then you incur tax on the differential. People also borrow at times the $200 per share to exercise their options. Imagine before you have paid the taxes the stock crashes to $100.

Such stories were common during the dot com bubble. Following is an excerpt from a LA Times article from 2001.

Former Cisco engineer Jeffrey Chou, 32, owes $2.5 million in taxes on company stock he purchased last year that has since withered in value. Chou figures that if he were to sell everything he owns, including the three-bedroom townhouse that he shares with his wife and 8-month-old daughter, the family still could not pay the bill.

“I’ve lost sleep. I can’t eat. I cannot pay and we’re ruined,” Chou said.

Source: https://www.ft.com/content/9998720e-bc80-44e6-950c-d47469a1862a

Employee stocks options costs are as real as any other cost. Owners of the business need to consider if these costs are productive like any other business expense.

Stock Based Compensation: Real Cost

DSP

Overall, if you are wondering if our expense is going to shrink, the answer is no, because as a growing company, we have to continue to expand our talent and our reach. So I don't see the ESOP costs going down. It's not like Google or Amazon, where they have already invested in all the employees so far ahead of time that now they can't afford to keep it at whatever, a few basis points of their P&L. A very good case in point, if you look at HDFC, in the first 10 years of their P&L, look at their ESOP cost, it's always increasing. So that's how growth companies operate because you need that premium to get talent onto the team.

AngelOne™

Look longer term, we expect the ESOP charges and I say longer term, I mean beyond the five years, beyond the first five years, we expect ESOP charges to be roughly about INR100 crores a year. That's my guess, right. And even now, if you take the founders out of it. It will probably something in that range, it maybe INR150 crores because, yes, there was an IPO and you would have a little additional all of it has not been rewarded actually.

pb Fintech

Stock Based Compensation: Real Cost

DSP

So regarding stock-based comp. So we are looking at all parts of our cost structure, including employee compensation. We recognize, and there is a fair amount of noise particularly on the West Coast regarding stock-based compensation. What I would say is that we expect our employment levels to be, our headcount will be relatively stable this year. We will continue to focus on performance management across all of our businesses. And you saw that we took some action in our Freight business in January and now specific to the Freight in the marketplace. And there'll be some other pockets of that, that will happen during the course of the year. I think you won't see any demonstrable change in stock-based comp because it takes a long time for that.

Uber

We're going to have about $1 billion of stock-based compensation. We'll least be offsetting that through share repurchases, and -- but I don't have anything more to say beyond that at this time, but we will continue to evaluate what the appropriate amount of cash is to keep and how much we should continue to return to shareholders. But remember, we are still heavily in growth mode. We want to be able to invest in the long-term growth of this business

airbnb

Stock Based Compensation: Real Cost

DSP

We do stock repurchases as a tool to manage our share count and protect the long-term returns of our shareholders. In the near term, with stock-based compensation expected to be the primary driver of any share count growth, we prefer to see dilution not exceed 3% year-over-year over any extended period of time.

Snap Inc.

Projected ESOP costs

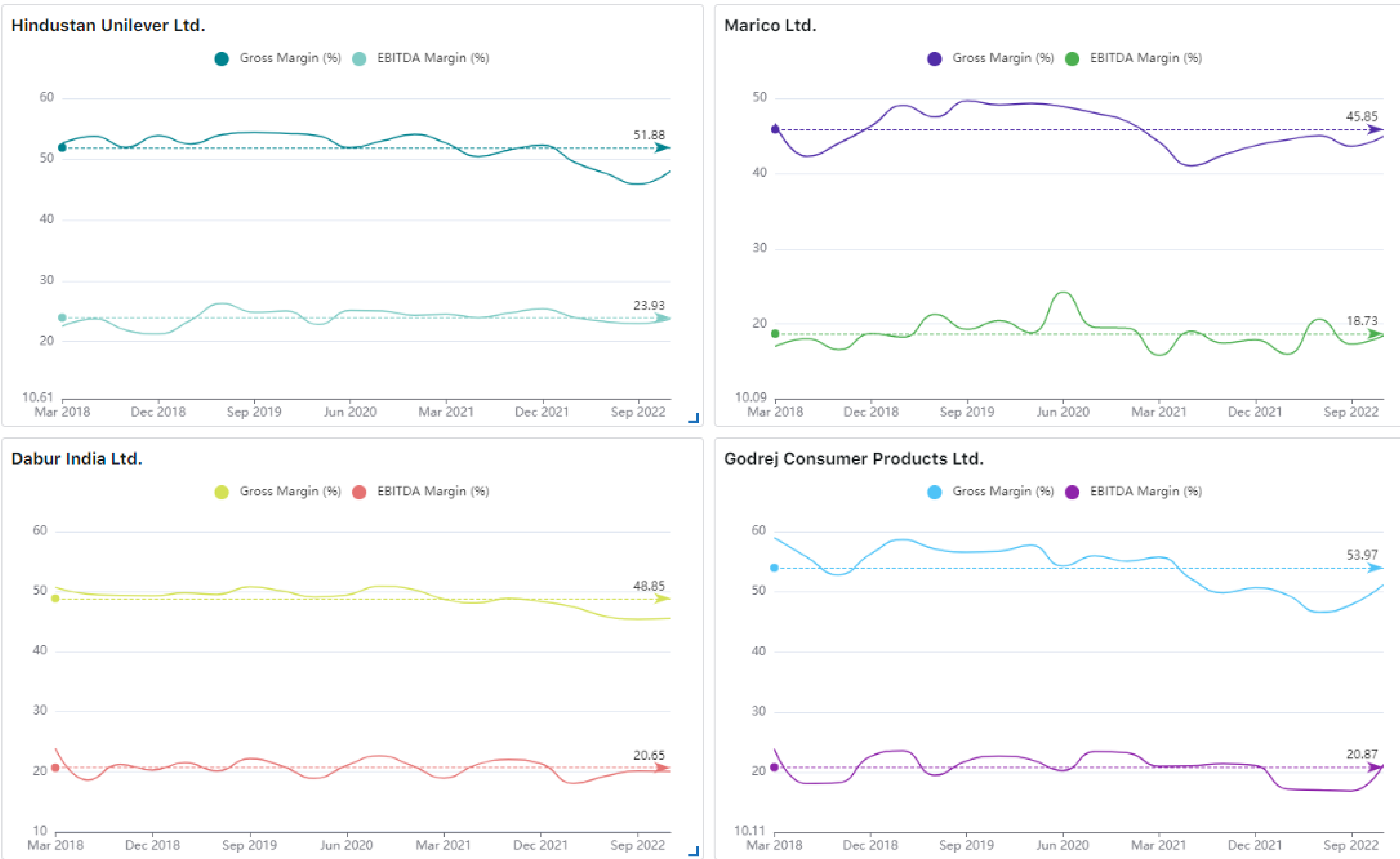
Estimated P&L charge (non-cash) for ESOPs already granted		
₹ Cr	Cost of time-based options(1)	Cost of performance-based options(2)
FY23	238	57
FY24	143	94
FY25	71	40
FY26	23	12
FY27	2	2
Total	**477**	**204**

DELHIVERY

Advertising: Still, Below The Line

DSP

As gross margins took a hit post Covid due to rising commodity prices, a lot of companies reduced their advertising and promotional spends to mitigate the impact on Ebitda. The compression on gross margin was higher than compression in Ebitda margin. As gross margins recover, due to receding commodity inflation – the advertising spends should come back.



Source: Internal, Company Reports

Advertising: Still, Below The Line

DSP

Our plans for next year as well is to try and increase ATL (above the line), BTL (below the line) spends in the market. Obviously, there is the legislation around advertising can be quite restricted in some areas.

UNITED BREWERIES LIMITED

Instead of advertising too much in ATL, we advertise more in BTL and consumer promotions and trade promotions. So that our market shares don't get impacted, because of which, what has happened is our LUP (Low unit packs) percentages have gone up quite a bit, our low unit price points have been scaling which is a little margin dilutive to us. So that is a little change of course that we want to do going forward.

We want us to chart again going back to reducing our trade spends and increasing our advertising spend, so intent will be to increase our advertising spends going forward, rationalize the trade spends and consumer promotions and go back to building demand on our power brands also.

Dabur

Advertising: Still, Below The Line

DSP

HPC (Home & Personal Care) typically I mean the categories in which we are in or alike, maybe the threshold is any where between 10 percentage to 12 percentage. So, we are not too far off , either. I mean, last quarter we were at like 9.5 percentage to 10 percentage. There seems to be some opportunity in terms of scaling up the working media investments incrementally, but I think that will more than get funded from a controllable cost savings in gross margins expansion.

Godrej | CONSUMER PRODUCTS

We have normalized our advertising spend this quarter. So we have gone back to the pre-COVID levels.

BRITANNIA

Starting from an operating environment perspective, we continued to see curtailed ad spending by FMCG brands during the quarter. While October did see a very brief pick up due to festive season, subsequently spent has been -- spends have continued to taper off . We believe this is a cyclical slow down and as demand recovers, we will see pick up in TV advertising.

ZEE TV

NOBODY KNOWS...

Current level of world oil production will never be exceeded.

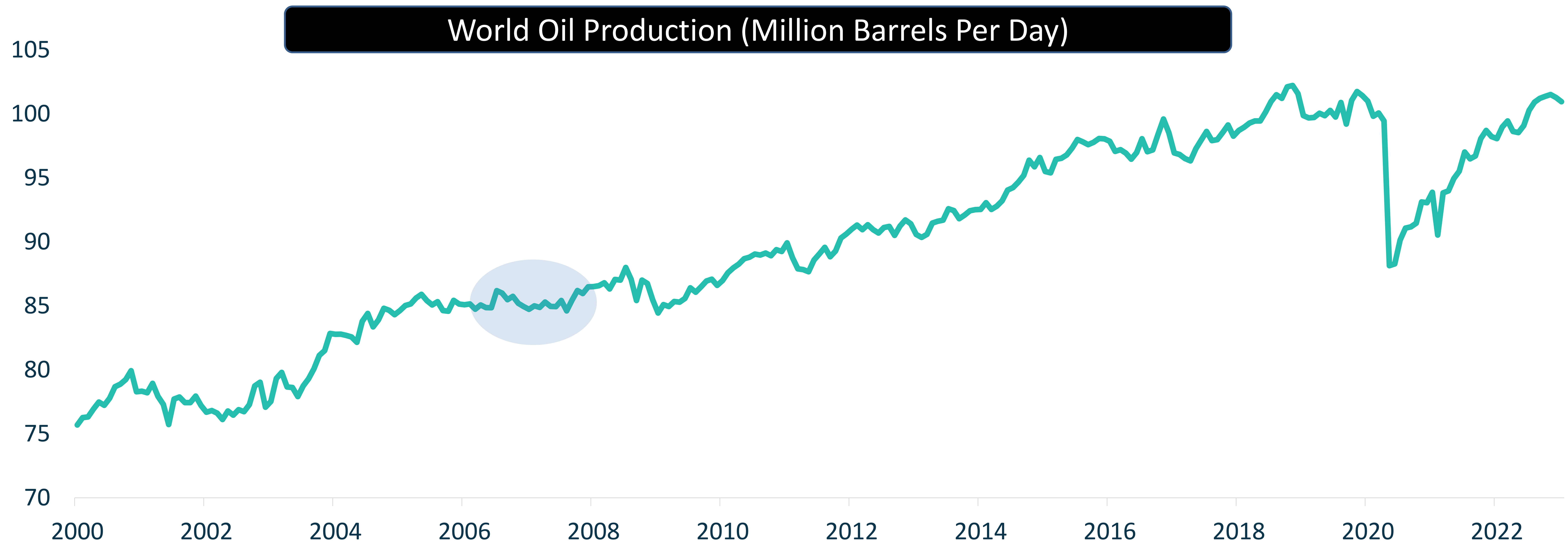
Sadad Al-Husseini, 2007

Ex- Head of Saudi Arabian Exploration & Production

World oil production peaked in 2006.

T. Boone Pickens, 2007

Founder, BP Energy Fund



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