Management Discussion

Jorn Elimar Kersten - Director and Chief Financial Officer, United Breweries Ltd
Thank you, thank you. Good afternoon, everyone, and thanks for joining us today. It's been a very interesting quarter. We'll take a bit of time to do an introduction. I'll make a few comments before I hand over to Vivek, and of course afterwards we'll very happily address all of your questions. But before we dive into the questions, I think this last quarter we can characterize by two very different realities. On the one hand, the beer category continues to accelerate. So industry growth at approximately 13%, very positively supported by both premiumization as well as increasingly supportive regulatory development, which we see across several states, which Vivek will also comment a bit more on, which makes us believe that this is really the start of a new era for beer in India, where we think the reforms increasingly recognize beer as a differentiating category, which will create a more favorable environment for long-term growth.

Now that's one side of the story. On the other hand, in the quarter we operated through one of the most significant cost shocks that the industry has experienced over the past couple of years, referring, of course, to the Middle East conflict that created substantial pressure across the entire value chain on packaging materials, logistics, foreign exchange rates, our export business overall, on the overall supply chain.

Despite the headwinds, we're very proud that we delivered solid growth that we very intentionally improved cash generation and that we continue to strengthen the underlying business. And I'll talk a little bit more about that, but first on the top line, as you would have seen, our sell-in volumes increased by around 9% while our sell-out volumes increased in line with the industry at 13%. The gap between the sell-in and the sell-out is driven by a very deliberate choice to reduce our in-market inventory, which went down by approximately 20% versus the same period last year.

This we did to strengthen our free operating cash flow given the external headwinds, and which also grew our working capital by 38% versus the same quarter last year. That combination of strong top line growth while being able to really protect the margins, and I'll talk a bit more about this, as well as deliver cash flow gives us a lot of confidence that the fundamentals of the business continue to strengthen. Now, stepping back a little bit from the quarter, we believe that the broader industry context is becoming increasingly attractive.

If we look at Karnataka and the ABV-based tax reform, that represents an important milestone for the industry and for the beer category specifically. While we see also other states like Maharashtra, Jharkhand and Andhra continue to demonstrate strong category momentum as well. We think it's very important to mention that this is no longer a story of isolated growth pockets. It is something where we see sustained category expansion across regions and across segments. And UBL as a market leader, we remain very committed to playing our part as a category maker with strong brands w ith innovations but also through responsible advocacy as well as disciplined execution, a lot of which we have seen proof of during this quarter.

I'll talk a little bit about margins as well. At the headline, we see that the gross margin of 41% was down by approximately 155 basis points versus last year. EBITDA delivered 10.9% while EBIT margin was 8%. Clearly, these are not the margins that fully reflect the underlying performance of the business because the Middle East conflict created an estimated impact on our GP margins of around 300 basis points during the quarter alone.

And we, of course, spoke about this after the previous quarter as well as on a recovery program

which includes pricing actions, a lot of fulfillment activities, as well as productivity measures, and that helped us to recover approximately half of the impact that we've seen, mitigating the impact to roughly the 155 basis points that we see on the reported financials. During the quarter, we delivered over INR50 crores through that recovery program, both on the top line with accelerated pricing across a large set of markets, as well as revenue management initiatives including trade spend optimization.

Again, some very deliberate choices which Vivek will also elaborate on. And secondly, on the cost base through productivity, both in our variable and in our fixed, a cross-functional effort where procurement as well as supply chain drove many initiatives to deliver savings as well as quite a bit of cost avoidance. On the EBITDA margin, I'm happy that we improved materially versus the previous quarter from 6.5% to 10.9% in this quarter, despite this external cost pressure. And while we expect that the inflationary pressure continues to be elevated, especially on the near term, we remain extremely focused on the disciplined pricing, the cost management, as well as productivity improvements to protect the profitability for the short term as well as the long term.

One thing that I really want to highlight, which also plays into the margin story, is the continued evolution of the premium portfolio, one of the structural growth opportunities for us as well as for the category. And during Q1 of this fiscal year, we reached an important milestone which we didn't want to leave unaddressed because we've spoken about this many times. And following multiple years of localizing production, optimizing our network, and improving the execution, we can now proudly mention that premium margins have become accretive for the first time in the past quarter.

And we believe this is structural and the premium portfolio will continue the upward trajectory to become a meaningful contributor to profitability for UBL in the future. The premium volumes increased approximately 17% if we exclude the intentional interventions that we made in some markets where we reduced the investments to mitigate the pressure on cost and to also really protect profitability. Where premium is led by Kingfisher Ultra, which continues the strong momentum, but also very good to see Heineken Silver growing approximately 28% in the quarter and really driving the growth on the international premium segment.

To conclude, we really believe that this quarter demonstrates the resilience of the category and specifically our business. Industry continues to grow double digits. We are very happy in how we're navigating external factors while we really improve and strengthen the underlying business. Premium margins, I can't stress enough, became accretive for the first time. We're very happy with the cash flow delivery where we also think it's really strengthening the muscle of generating profitable growth. And while we do think that the near-term volatility will remain, the confidence in the long-term opportunity for beer in India has never been stronger than it is today.

With that, I'll happily hand over to Vivek before we address your questions.

Vivek Gupta - Managing Director and Chief Executive Officer, United Breweries Ltd
Thanks, John. I think you have captured most of it. I would just say that as you started, that this was a quarter with two key milestones and two key wins. I think first, big milestone for us that we made structural improvements. The work we have been doing for last couple of years to get premium business in structurally right shape, I think we achieved it. We actually achieved ahead of our glide path, and now we can say that our premium portfolio is accretive to the business and which gives us even more courage and conviction to drive the investment.

The second big milestone is we talked about making structural improvement in business through our

network design. We... Despite having very tough context on the board, as an organization, we stick to our long-term priorities and the structural intervention. In this quarter, we achieved a lot. We did our network optimization work in northwest . We closed our Punjab brewery, which was not an easy decision but the right call from a business and profitability and long-term health of the business.

And we transitioned to a partnership with ABB in Punjab. We had a choice to delay this transition because there's a lot happening, but as an organization, we stick to the plan. Because it was important to take some short-term hits to get the right. And I'm proud that our transition is complete and we are back on full force from this quarter. The second milestone related to network design is our can line in Telangana is commissioned. It is one of the record times in which UBL has commissioned a new can line facility.

And I'm happy to report that last week's first can was consumed by the consumer from the line. And the third important part, as part of the network milestone is that our other projects where we were doing localization of premium in some of the states, we were improving better production excellence related features, they have also been completed. So on one side, good milestones. At the same time, I think it's a revolutionary moment for the category. I can actually say that I think the beer category, after all the efforts of differentiating versus rest of the alcohol, is paying off.

The Karnataka move is a revolutionary move, and we have been seeing that category is now growing higher of 30%, 35% in Karnataka, and in some months... the recent month is actually up more than 50%. We saw the similar intervention in Maharashtra last year and category continues to grow upward of 20% in Maharashtra. We saw privatization of retail happen in Jharkhand, and we have seen the category size has significantly increased. So it gives us a lot of confidence that it is not an isolated event.

The more governments are looking at beer as a separate go-to category, and this is going to be revolution for us. So most important for us during this turmoil phase, where the costs have really gone up, I think we have delivered a plan. We had three priorities as a company. Number 1, we wanted to make sure that we are increasing our brand power. So I am happy to report that based on the recent data post peak summer quarter of April, May, June, our brand power as a company has improved.

On brands like Kingfisher, it has improved. On Ultra, it has improved. Heineken has improved. So we have emerged stronger from the brand power. Second, we continue to drive focus on premiumization and pricing. O ur sell-through volumes increased 13%, and we took the the right call to ensure that we reduce inventory so that we can offer fresh beer to consumers, especially getting into monsoon. This was a learning from last year. But also at the same time we create working capital because cash is king in this scenario.

And third area, which is extremely critical, we made choices and tough choices to get the structure right in the market. We reduced trade discounts where it was needed. We made sure that we are not unnecessarily taking big losses to serve a market versus working a structural solution. F rom the long-term health of the business, we improved productivity in the organization. We created a lot of cost initiatives, and despite having a 300 bps o f impact on the... behind the war, I think the team was able to mitigate a large part of it.

We actually... T he most important thing is we actually took pricing intervention in 22 states, and that have been all implemented. A nd when we take the pricing implementation, it takes time, it takes transition, but by end of this month, we are now live in 22 states with the pricing implementation, which again tells us that we were not chasing business at any cost. We did the right thing and we

are also able to create a large level of network with the stakeholders so that they can understand how the category is going through a bad phase a nd leveraging BI, we were able to do a lot of things.

The outlook for the category is looking positive. I expect we are hearing positive news coming out of some of the other states where they are looking at Karnataka model, where they also discussing with us on what needs to be done. So let's hope since nothing is firmed up, that we think this momentum can actually further build up. The other thing is a lot of people ask that this volume result is based on good summers.

I think definitely based on good summers. But when we go deeper into it, there are big states where the category is still down despite having very good summers. And the states which are actually accelerating are having good summers but mostly took strategic reforms which are leading to the multiplication effect. And some of those reforms hopefully will stay for the rest of the year and this category momentum should continue. So with this, I hand over back to you for any questions.

Questions & Answers

Operator
Thank you very much. [Operator Instructions] The first question is from Ashutosh Jain from Barclays . Please go ahead.

Ashutosh Jain - Analyst, Barclays
Hello, everyone. Thank you for taking my questions. I have two questions. First would be we have seen contract brewing weighing on the price mix. So could you just highlight some more color was the contract growing more than the 20% to 25% range which was highlighted previously? And is there... A nd also on the other side, do you also see any impact in Maharashtra from MML, that is Maharashtra Made Liquor? Because I'm talking about more towards the mainstream portfolio.

And do you... A nd are you seeing any substitution from beer category into the lower-end spirits category? And my second question would be, could you just please remind us like what is your fiscal year '27 ambition? Is it still double-digit top-line growth led by high single-digit volumes? Thank you.

Vivek Gupta - Managing Director and Chief Executive Officer, United Breweries Ltd
Yeah, I think let me answer the Maharashtra and the other question. I think it's very difficult to see the data on how much is the MML impacting beer. B ased on the recent data we haven't seen much of the impact. But one thing we are definitely seeing in Maharashtra there is strong growth happening at economy segment. So there is definitely affordability is becoming extremely critical for the consumers, and we continuously see at the economy end, there is significant growth happening in Maharashtra, which is more linked to affordability.

Whether there is a direct impact of beer to MML, I think is yet to be seen. On our '27 ambition, I think we absolutely believe that it is critical that the category continues to grow at high single digits, and our goal is to, of course, grow ahead of the category in the profitable balanced manner. And we do expect our ambition is still to have double-digit revenue growth with the share growth and the strong momentum on premium which we have done in the last few years.

But at the same time, we are also ensuring that we continue to improve our brand power and strengthen the portfolio so that we can continue to build this category.

Ashutosh Jain - Analyst, Barclays
And on contract...

Jorn Elimar Kersten - Director and Chief Financial Officer, United Breweries Ltd
Maybe to address the... Sorry, to address the first question on contract brewers. So yes, the volume through our contract partnerships is growing ahead of the overall volume which is in line with the plan because we also expanded our footprint with... through our partnerships in locations where we saw growth. So I think also coming out of the summer, we were happy to be able to deliver those volumes for which these partnerships were contracted. On the accounting side, it has a dampening effect on the revenue growth because actually we report this as one line in our accounting, and so hence also inflationary pressure there dampens the revenue growth.

So that combination of those two factors is what you see in the reported revenue number versus last year. Underlying, we're very happy with the 9% volume and the approximate 4% price mix that are there.

Ashutosh Jain - Analyst, Barclays
Thank you so much.

Operator
Thank you. The next question is from Harit Kapoor from Investec. Please go ahead.

Harit Kapoor - Analyst, Investec
Yeah. I agree. So just a quick follow-up from the earlier question. How much was the impact on the source mix for this quarter? Just wanted to understand how to look at this going forward. And secondly, given that these states are delivering exceptionally high growth where we are contracted, is there a plan to kind of look at own manufacturing in these states? Are those states conducive for that? That's my first question.

Vivek Gupta - Managing Director and Chief Executive Officer, United Breweries Ltd
I think let me answer the second question. I think the first question was on the source mix again, right?

Harit Kapoor - Analyst, Investec
Yeah.

Vivek Gupta - Managing Director and Chief Executive Officer, United Breweries Ltd
Sorry. Because your voice was breaking. You were asking what is the source mix? Sorry, Harit , your voice was not clear in the first.

Harit Kapoor - Analyst, Investec
Yeah, can you hear me? Can you hear me now? Is this better?

Vivek Gupta - Managing Director and Chief Executive Officer, United Breweries Ltd
Yes.

Harit Kapoor - Analyst, Investec
Yes. Yeah, my question was on how much was the source mix for the quarter so we can realize the real revenue... get a sense of the real revenue growth. And the question was given that these states where we have contracted breweries, those states are showing very strong growth, just wanted to

get your sense of whether there is a thought process here of having own breweries, etc., in them as well.

Vivek Gupta - Managing Director and Chief Executive Officer, United Breweries Ltd
Yeah, I think let me answer the second question coming with the data on this one. I think the... Look, I think what we are seeing is our own breweries are also getting full. Like Karnataka is a good example where we have two breweries, and Karnataka policy started happening only in the second half of the quarter. Maharashtra, we have our own breweries, but we already have a plan to have a greenfield in UP where today we are in contract brewery. We also expand... done the brownfield expansion with two can lines , one in Maharashtra where some of that requirement was served through the contract breweries, and also now in Telangana as well.

So yes, we have been investing in our own breweries either in expansion, but I think the main thing is we look at the potential of a state, how much is the growth potential today, the stability of the policy our portfolio gap, and then we make the call. And we believe that it's a good mix of having our own breweries and the contract breweries because it's a highly capital-intensive business. So we need to also make sure the return on capital invested is also into account. So it is going to be a good mix.

We consistently invest in our breweries. The two can lines are in our own breweries. The greenfield is our own brewery. But at the same time, we also invest in the contact breweries wherever is needed. So we consistently are looking at our network.

Jorn Elimar Kersten - Director and Chief Financial Officer, United Breweries Ltd
No, and indeed. I think that like Vivek mentioned, the capital intensity also means that when the CBUs give us flexibility, so if we see sustained growth of category across state, that for us triggers the thinking around where do we think it's feasible. And that's what happened, for instance, in UP, where we see that the opportunity is long-term and will stay. And then we'll move also to investments. And to your earlier question on the CBU, it's approximately 4% impact in the quarter.

Harit Kapoor - Analyst, Investec
Got it. The second question was if you look at premium now, as you said, is accretive to the margins. Just wanted to understand that the earlier thought process was that you would require a higher share than it is currently to make that accretive. So is it that your accelerated localization efforts have driven a sooner than expected milestone here?

And would premium be in the low double digits or 11%, 12% type of your total mix right now? So that was my second question.

Jorn Elimar Kersten - Director and Chief Financial Officer, United Breweries Ltd
Yeah, so I think there's... there's two things on the premium and the being accretive. Yes, you are absolutely right. It's about tipping the scale on the size of the business where the localization helps, being closer to the market also helps the collection of bottles, which is the underlying factor which really helps to drive the profitability. The other thing is what I think we did well and where we accelerated is the interventions that we did through the revenue margin team and really looking at trade discounts also for the premium portfolio, that has helped and has probably also accelerated a bit the delivery on margins where we structurally looked into the business and how can we optimize, where we have been more deliberate in choices, and that helps to drive the profitability.

Harit Kapoor - Analyst, Investec
Fantastic. And third question was, you mentioned about price increases. So what is the extent on a weighted average basis of these price increases that you would have got in these 22 states? Just wanted to understand how to model price increase component over this year.

Jorn Elimar Kersten - Director and Chief Financial Officer, United Breweries Ltd
I think it's always a very mixed bag, and also looking at how do we serve the consumer best and how does it work across the value chain. We would say that it's between 2.5% and 3%, but accelerated through other initiatives around price lettering and trade spends.

Harit Kapoor - Analyst, Investec
Great. I'll come back if need be. For now, wish you all the best. Thank you.

Jorn Elimar Kersten - Director and Chief Financial Officer, United Breweries Ltd
Thank you.

Operator
Thank you. The next question is from Abneesh Roy from Nuvama . Please go ahead.

Abneesh Roy - Analyst, Nuvama
Yeah, thank you. My first question is on the trade spend. You said that wherever needed from the long-term health of the company, you have reduced the trade spend, and you also did mention that you don't want to do business at any cost. I wanted to understand, there is an IPO for a large multinational company, and generally the valuation is linked to the exit quarter sales, etc. So we are picking up that there is some level of increase in aggression by that player. So are you responding to that?

Because it seems you're not responding. And is that impacting you in any way, either in terms of share or in terms of, say, placement, etc.?

Vivek Gupta - Managing Director and Chief Executive Officer, United Breweries Ltd
I think the first... T hanks, Abneesh, for asking the question. I think one of the key focus areas for us is to really build very strong brand power and pull for our brands. And as I said, in holistic package which includes investment in sponsorship, trade spend, distribution, all of this put together, I think I'm very proud that we are able to grow brand power, which is, consumer-centric data on this.

And we continue to increase the brand power. We have seen the increased investment in the category, which on one side is good for the category because there's more interest in the category. But at the same time, I think it is extremely important that we do the business responsibly . And I think the state where we don't make enough money and pricing and margins are very thin spending more money to push the products with the trade discounts doesn't make sense. At the same time, we work with the retailers to create value creation initiatives..

We are working with retailers to actually create initiatives which actually help them to create categories. We have placed 50,000 coolers now. We did not put a break on our cooler program, which is also seen in that appreciation numbers, because that is the right thing to do when the category is growing. In states like Karnataka, Maharashtra, we go to market executions where we are now able to hear the retailer's name within 20 days which used to take six months. We are using technology to better predict the out of stock and giving them the service.

We have reduced 20% less inventory and bringing better ROI for the retailers. So we are actually

moving our capabilities from being just push-driven to actually building category and building business for the retailers. So in most of the cases, we have got very strong conversations and very good alignment with the retailers. At the same time, we have been brutally honest and transparent. The impact on the margins and the cost because of the war impact and the data is absolutely clear that the states where EBPs are very low, we actually don't make money, and it's very difficult for us to invest the money in pushing the product.

So it is always a balance. W e are not playing in isolation, but having said that, we are making the choices. We are also challenging our own cost structure to really see that where we can actually reduce the inefficiency so that we can invest behind customers, consumers, and our products. So short answer is yes, we have seen impact. For example, Haryana is one state where we saw a significant drop because we significantly reduced the case spend, but it is also one state where the product is not sold on MRP.

Consumers is actually paying much more than the product, the beer should be. So I think there's no point in feeding those margins when it's not going to the consumer. So I think we have made those choices.

Abneesh Roy - Analyst, Nuvama
Understood. Second question is on the price hike and the cost inflation. So you had given out very upfront that number of the cost inflation due to war. Now we have a bit more understanding of war, plus you have got now price hike in most of the states, which is also reasonable price hike.

Now how do you see Q2, Q3 impact of the war?

Jorn Elimar Kersten - Director and Chief Financial Officer, United Breweries Ltd
Yeah. Look, I think no one has a good understanding of the war and it will remain volatile. So we remain a bit cautious. That being said, and also seeing that our recovery program really kicks in, we do revise our full-year impact downward. Where we said INR400 crores to INR500 crores, we now think it's more on the lower side of that range, between INR350 crores to INR400 crores impact. So in that sense, we're slightly more positive. Overall, we see the volatility is high. We've seen the crude oil today and how it moves. And so every day is a new dawn, but we keep being very vigilant on how we treat it from a recovery point of view.

Abneesh Roy - Analyst, Nuvama
Sure. Last quick question on the demand side. So some of the large states are doing very well for you. So Maharashtra, 20% volume growth, Karnataka, 20% to 40% or maybe even higher. But what are the laggard states? If you could discuss how is your performance in those laggard states, say, versus competition, and what will be the outlook in such states now? P eak season is behind, but anyway, we'll see the YoY numbers, if you could discuss the laggard states pulling down the number.

Vivek Gupta - Managing Director and Chief Executive Officer, United Breweries Ltd
See, we do have a... S ee, we have a national business. Of course, there are states where we have made choices. I gave an example of Haryana, where we had to reduce the paid discount because the business was not viable, and that had an impact on us. We also had an impact in states like West Bengal because we import... used to import a lot of products from other states, and it did not make sense at an inflated cost to pay higher taxes and other things to do that. But we do have structural plan in next few months where we will see more capacity in that state.

So which will mean that instead of relying on these short-term volumes, we will actually have volumes to serve the market to really do that. We're also working a very good plan in Haryana with the retailers to actually work a joint business plan to show them the value of what we can bring in the markets. So it is state by state. As I said we are seeing more positives where they are reformed. But we also have states where we still are in negotiation with the government on pricing and the viability of the business.

And it is difficult for us to invest more commercially till our margin structure makes the business sustainable. So I think it's a matter of doing the right thing for the business, but that's also the right thing for the category. But in a whole, as Jorn said, we feel the outlook is positive. We have got more positive response from the state government and corporations at 22 states, is a huge number when we are saying that we are implemented a revenue and pricing plan which is now in market from this month of July.

So we feel that we'll be able to grow shares in the coming quarter.

Abneesh Roy - Analyst, Nuvama
Sure, 22 states is a large number. One question on Haryana I had. I'll end there. If it is unviable for you in Haryana in the short term, is it also unviable for the players or their scenario can be a bit different?

Vivek Gupta - Managing Director and Chief Executive Officer, United Breweries Ltd
I think everyone's scenario is very different because the portfolio is different, ability to have local manufacturing of different formats is very different. So I think it's all about making choices, right? And it's also about the network part of it.

Abneesh Roy - Analyst, Nuvama
Yeah, thank you. That's all for me. Thank you.

Operator
Thank you. The next question is from Latika Chopra from J.P. Morgan. Please go ahead.

Latika Chopra - Analyst, J.P. Morgan
Yeah. Hi. Thank you for the opportunity. A couple of clarifications. The first one was on your differential in sell-in and sell-out volume growth. Was this specific to the quarter, or you do you anticipate that the inventory rationalization piece is kind of behind us and both these growth rates will now be more aligned in the quarters ahead?

Vivek Gupta - Managing Director and Chief Executive Officer, United Breweries Ltd
Yes, I think this was primarily for the quarter because usually we build these stocks and we say that when you come out of the season, you need to maintain a certain level of inventory. Based on our last two years learning and getting more smarter analytically, we were able to do more deliberate attempt to really do that. We still are working on stock norms in many of the depots, both for us as well as for the... for our partners. So I would say that mostly you will see our sell-through and sell-in in line, but we will not hesitate to take corrections because the fresher the beer, the better it is.

So because many of the inventory points are actually government depots, and we still are working with the new tools to really understand what is the right replenishment model so we get the freshest beers and the high rotation and given that we also focus on premiumization and in many cases economies, that is a large number of SKUs are added now. So we are working through it but we

expect this to be more in line. But as I mentioned to you, if we find opportunities, we will continue to correct it.

Jorn Elimar Kersten - Director and Chief Financial Officer, United Breweries Ltd
Yeah, if I can add one thing is, in this quarter I think we were specifically both to make sure that we protect the cash flow from any shocks that we couldn't anticipate up front. So I think that's where maybe we were a bit bolder than we otherwise would have been. Another element that we cannot underestimate is the reliability of our supply chain. Given the high seasonality of the business and the fact that it's capital intensive, as I've mentioned before, there's a lot of reliability around stocking up to be able to source the season.

I think the increased reliability of our supply chain on delivery also led us to lower stock levels throughout the season because we knew that production would be able to cover the demand. Now for the full year, we don't expect that inventory levels will be lower exiting December 2026 versus the previous year because we still build stock for the peak season ahead of peak season really happening, and that starts at the end of the year. So as an exit for the calendar year, I don't expect material changes in inventories because that's required in order to deliver the peak season.

Latika Chopra - Analyst, J.P. Morgan
Sure. No, this is a very useful color. The second bit I heard your optimism on volume growth and the traction that you're seeing on account of policy reforms. When you look at Q2 and Q3 and maybe even Q4, even the volume number, that is a low base, right, from a volume perspective for you. So is it fair to assume that we are getting into a double-digit volume growth trajectory for the rest of the year, or at least close to it?

Vivek Gupta - Managing Director and Chief Executive Officer, United Breweries Ltd
See, we are hoping that. That is how we are building the plan. I think you are right. There is a base there. B ecause of the seasonality, we are in a better position on our inventories sell-in versus sell-through, and we continue to see the momentum on the category. So definitely in the coming month, coming couple of quarters, we should be seeing a double-digit growth unless there are big roadblocks in the policy or something else comes which we are not predicting. But definitely that is the data is pointing to that.

Latika Chopra - Analyst, J.P. Morgan
Understood. And the last one on margins, do you think 41% gross margins that you delivered in Q1, it's kind of the bottom because you have taken pricing interventions in 22 states which will get fully reflected in coming quarters. There has to be an operating leverage benefit, plus the fact that your cost impact is now at the lower end of the earlier guided range. So should we... I s it right to assume that gross margins kind of bottomed out in Q1? And they can progressively stay here or possibly improve depending on how raw material inflation plays out?

Jorn Elimar Kersten - Director and Chief Financial Officer, United Breweries Ltd
Yes. So as you mentioned, a lot of dependencies here. I think important to note here that we don't necessarily take this as a quarter-by-quarter guidance or deliverable. Over time, we look to expand our margins whilst making the right choices. And whether that has to do with the supply chain network, investing behind the brands, whether it's the right choices on portfolio or inventory, that will be our guidance. So over the longer term, we're still looking to expand margins, absolutely. Is it the absolute bottom?

I'm not going to commit to it. But of course we do look to expand margins quarter- over- quarter.

Latika Chopra - Analyst, J.P. Morgan
All right. And just for a better understanding, you called out the source mix impact of 4%. Your reported price mix growth was negative too. I just wanted to understand directionally, how these two numbers will change or behave in the coming quarters given your growth agenda and capacity plans.

Jorn Elimar Kersten - Director and Chief Financial Officer, United Breweries Ltd
That will continue to be there. We have a hybrid network between contract brewers and our own assets. So that will continue to be there and will continue to also be part of the reported financials.

Vivek Gupta - Managing Director and Chief Executive Officer, United Breweries Ltd
Our underlying price mix is plus 4%, right?

Jorn Elimar Kersten - Director and Chief Financial Officer, United Breweries Ltd
Yeah.

Latika Chopra - Analyst, J.P. Morgan
Sorry. Co uld you repeat, Vivek? Sorry.

Vivek Gupta - Managing Director and Chief Executive Officer, United Breweries Ltd
I'm saying our underlying price mix is actually plus 4%. And I think the role of contract manufacturers will remain and will continue to accelerate business in our own brewery, but we expect the business to grow in their breweries as well. So the ratios will still remain.

Latika Chopra - Analyst, J.P. Morgan
Okay. It's all according. All right. Thank you, gentlemen. Thank you so much for answering these questions.

Jorn Elimar Kersten - Director and Chief Financial Officer, United Breweries Ltd
Thank you.

Vivek Gupta - Managing Director and Chief Executive Officer, United Breweries Ltd
Thank you.

Operator
Thank you. The next question is from Krishnan Sambamoorthy from Ashika Institutional Equities. Please go ahead.

Krishnan Sambamoorthy - Analyst, Ashika Institutional Equities
Yeah. Hi, Vivek. Three questions on a structural basis. One, while you had a very good summer season, it is also true that the seven year CAGR in terms of the summer season has been about 6% top line growth, right? There are... I understand there are many factors which is outside the control of the industry and the participants, whether it is war, whether it is seasonal patterns, but do you see this changing? And therefore, are you... if not, then are you still dependent on the vagaries of the weather?

Vivek Gupta - Managing Director and Chief Executive Officer, United Breweries Ltd
Yeah, I think you said that seven-year CAGR is 6%. I think this quarter has been 13%. It's almost

double the category growth. And therefore I'm mentioning it's not only the summer season, because summer has been there in many states. And I think it is summer season plus significant reforms which are now translating into category growth. And I talked about if the beer revolution happened in few states like Karnataka or Maharashtra last year, or the change of these reforms, which is showing that if they... if it is in the right direction, the category growth and the potential is much higher.

Krishnan Sambamoorthy - Analyst, Ashika Institutional Equities
Okay, sorry to harp on this, but still the seasonality does remain a factor, right, for the industry? And will you see that changing?

Vivek Gupta - Managing Director and Chief Executive Officer, United Breweries Ltd
It has to be. You drink beer when it is hot. And but last year also, in the season, the volume growth was more than 8%. So there is a seasonality factor. But there is also seasonality plus reform which is accelerating it even higher.

Krishnan Sambamoorthy - Analyst, Ashika Institutional Equities
Okay, the other two questions hark back to the analyst meet that you had a couple of years ago. Vivek, you had pointed out that 75% of Indian customers start out with beer and then subsequently the share of throat, so to speak, is only about 20%, right? So one of the longer-term targets that you had was to to ensure that you retain a decent chunk of these customers?

I know still early days, two years is still early from a strategy perspective, but could you highlight the efforts and the success that you've seen on this front?

Vivek Gupta - Managing Director and Chief Executive Officer, United Breweries Ltd
No, I think it's a great question. I absolutely I think we are consistently working our innovation pipeline and our brand plans to address that. A few things which is already working. We launched our Kingfisher Strong Smooth innovation which is actually growing share. E very month the share is better than the previous month. And we are getting very strong repeats because consumer trend is towards smoother beers.

We are also... O ur Heineken Silver business is up 28%. Heineken Silver beer is again, which is about one of the beers which is only off from barley, hops, and water. I t's actually... W e also having the right premiumization there. So we are actually expanding the portfolio mix on Heineken Silver in many states. We are launching Heineken Silver in states like Kerala. We are launching Heineken... W e launched Heineken Silver in Haryana. So we are... O ur innovation program is working.

Third is we also looking at draft beer in many states because that also improves the consumption and more consumption occasions. And we also have a strong innovation pipeline which I don't want to talk much, which addresses some of the share of occasion things which you are talking about. But this is absolutely on top of the mind, and that's why I started off saying the good part is the brand power is improving, which means some of these actions what we are taking is actually being recognized by the consumers. A nd we are seeing, that is only going to accelerate.

Krishnan Sambamoorthy - Analyst, Ashika Institutional Equities
That's very encouraging to hear. A nother thing, Vivek, that you highlighted in the analyst meet a couple of years ago was that, beer penetration consumption drops off significantly out of the large cities, right? And your visi-cooler expansion plan was to ensure that it does... this doesn't happen.

While you have highlighted the extent of the visi-cooler expansion, can you just also highlight as to whether these the outside of the larger cities, the demand is picking up?

Vivek Gupta - Managing Director and Chief Executive Officer, United Breweries Ltd
Absolutely. In fact, we are actually ensuring there are disproportionate allocation in the smaller cities. A nd in fact, our activation in the smaller cities has significantly improved.

It is also showing in our share data. In some of these states, we got the data by city. And it's showing that we have much higher shares and category growth in some of the tier 2, tier 3 towns behind these efforts. But it is... it is a start because the number of stores are still a limiting factor. As you know, there are only 100,000 stores which are selling beer, and we are using some of this data with the stakeholders also that why is it required to have some more stores in tier 2, tier 3 towns, a nd how the whole infrastructure is critical to drive tier category growth. We also actually partnering... we also partnered with BCCI to actually activate Fan Park in some of these tier 2, tier 3 cities where we actually brought the IPL experience to these consumers. And wherever we piloted it, we saw a massive response. So yes, there's a lot of work happening in tier 2, tier 3 cities.

Krishnan Sambamoorthy - Analyst, Ashika Institutional Equities
Very useful. Thanks, Vivek.

Operator
Thank you. [Operator Instructions] The next question is from Ajay Thakur from Anand Rathi Securities. Please go ahead.

Ajay Thakur - Analyst, Anand Rathi Securities
Hi, thanks for taking my question. So I wanted to understand a bit more on the premium beer side of it. What kind of a level of premium beer can help us to offset this input cost inflation? Because I believe that input cost inflation will be a pertinent kind of a or it will be persistent kind of a feature going forward as well. But if we grow the premium beer to a certain extent, then obviously that could be offset. But what level of that premium beer can offset this kind of input cost inflation on an ongoing basis, i s the question.

Vivek Gupta - Managing Director and Chief Executive Officer, United Breweries Ltd
Unfortunately, this... I think, it's a very less leverage on the scale there because the beer is a very low margin business. I think we need to just have the right pricing and right revenue structure by SKU and by brand to make it happen. And if you make it too expensive, you just say we can price it premium, because premium, the consumer is only willing to pay a certain price on premium as well, right? So affordability across the tiers is important for consumer to do that. I think localization has helped, but we need to just get our revenue structure and the cost structure right.

And most important thing is, with the inflation, we need to price it right, w e have to have the ability to recover the price, w e have to balance our trade spend to make sure it's there, and we need to make sure the design of the product is right. So that we are not adding inefficiencies on the product or in the network.

Ajay Thakur - Analyst, Anand Rathi Securities
Understood. But any sense on the volume and value share of the revenue pie that the premium beer is sitting right now?

Vivek Gupta - Managing Director and Chief Executive Officer, United Breweries Ltd
The premium is almost 10% to 11% of our revenue, and we only expect this to increase... the failures of premium to increase. As I mentioned in previous calls, we have aspiration that premium will become almost 20% of the revenue, and we will... we are on track on that.

Ajay Thakur - Analyst, Anand Rathi Securities
Understood. Also, if you can share some bit of insights into the cost efficiency measures and the cost efficiency programs that we had, what is the status and the timelines on the same?

Jorn Elimar Kersten - Director and Chief Financial Officer, United Breweries Ltd
Yeah, so to start with the last part, the timeline is continuous. So we are delivering, and we're also very aware that this is a continuous effort to Vivek's previous answer, in a market where it will, at least for the short and medium term, always be difficult to translate cost hikes into pricing, we very much rely on cost efficiencies throughout any period. If I can elaborate a little bit more on ongoing initiatives that help to deliver on the productivity, we can talk for instance with the procurement team to really look into what are the longer-term partnerships, what can we do in forward buying to make sure that we lock in price.

We talk about recipe flexibility where we see how can we optimize both utilization of our supply chain as well as be flexible in terms of the recipe where we look how can that contribute to a better cost base. We look very closely at investing in the organization so to really make sure and we've done a lot of investment in the organization in the past. But now we really look where can we add value and where can we accelerate the growth through investments. And just remain very strict on overall budgets to make sure that, let's call it, the cost consciousness and the cost-saving muscle within the organization is a constant development so we can leverage it not just to navigate current headwinds, but for us is really the foundation of building strong business f or the future.

Ajay Thakur - Analyst, Anand Rathi Securities
Understood. Quite helpful. Thanks.

Operator
Thank you. [Operator Instructions] Well, that was the last question. I would now like to hand the conference over to the management team for closing comments.

Vivek Gupta - Managing Director and Chief Executive Officer, United Breweries Ltd
Yeah. Thank you everyone for asking the question. As I said this quarter has been a tipping point for the category with some of the policy changes which has happened, some of the discipline what we have brought in the organization. We still are not out of the woods because of the war, but having said that, as a company, we are much better prepared. We were the first one to declare the impact so that we could plan. We took strong action. We believe the category growth momentum will continue, and our choices are working.

And yeah, we look forward to seeing you next time. Do you want I hand over to you?

Jorn Elimar Kersten - Director and Chief Financial Officer, United Breweries Ltd
Yeah, I can quickly do the announcement before we end it here. But it's a quick intro to what's coming to your way, is that we're planning a Capital Markets Day early September to basically give a bit more glance about the industry in total. So like we mentioned before, we feel like we're at an inflection point, really at a revolution of time in the beer industry at the moment. And we feel we can

give a bit more total glance of what's currently happening and our position in the total market on that. So more information to come, but just make sure to keep an eye on the email and we'll share it shortly with all of you.

Vivek Gupta - Managing Director and Chief Executive Officer, United Breweries Ltd
Thanks, Jorn. And we really look forward to hosting you for this day because I think it will be good for you to see what plans we have in store, but also to get your thoughts as well. Jorn, anything?

Jorn Elimar Kersten - Director and Chief Financial Officer, United Breweries Ltd
Thanks, everyone. Thank you.

Operator
[Operator Closing Remarks]