"Somany Home Innovation Limited
Q3 FY2021 Earnings Conference Call"

February 12, 2021

ANALYST:	**MR. MANISH MAHAWAR – ANTIQUE STOCK BROKING**
MANAGEMENT:	**MR. RAKESH KAUL – WHOLE-TIME DIRECTOR & CEO – SHIL** **MR. RAJESH PAJNOO – PRESIDENT – PIPES BUSINESS, BRILLOCA LIMITED** **MR. SUDHNASHU POKHRIYAL – COO BATH FITTING, BRILLOCA LIMITED** **MR. SANDEEP SIKKA – GROUP CFO** **MR. NAVEEN MALIK – CFO, SHIL**

Moderator: Ladies and gentlemen, good day and welcome to the Q3 FY2021 Earnings Conference Call of Somany Home Innovation Limited (SHIL) hosted by Antique Stock Broking. 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 "*" then "0" on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Manish Mahawar from Antique Stock Broking. Thank you and over to you, Sir!

Manish Mahawar: Thank you Rutuja. On behalf of Antique Stock Broking, I would like to welcome all participants on the call of Somany Home Innovation Limited. Without further ado, I would like to hand over the call to Mr. Gavin Desa from CDR India. Over to you, Gavin.

Gavin Desa: Thank you, Manish. Good day everyone and a warm welcome to all of you who are participating in Somany Home innovation Limited Q3 and 9M FY2021 Earnings call. We have with us today from the management, Mr. Rakesh Kaul – Whole-time Director and CEO, SHIL, Mr. Sudhanshu Pokhriyal – COO Bath fitting, Brilloca Limited, Mr. Rajesh Pajnoo - President - Pipes Business, Brilloca Limited, Mr. Sandeep Sikka –Group CFO and Mr. Naveen Malik – CFO, SHIL. Before we begin, I would like to mention that some statements made in today's discussion may be forward looking in nature. The actual results may vary as they are dependent on several external factors as well. A statement to this effect has been included in the result presentation sent to you earlier. We will start the call with the opening remarks for the management following which we will have an interactive Q&A Session. I would now request Mr. Naveen Malik to open the call. Over to you Naveen!

Naveen Malik: Thank you, Gavin. Good afternoon everyone and welcome to Somany Home Innovation Limited earnings call. I would like to take this opportunity to share a brief background of SHIL before we take you through the company's Q3 financial performance.

Pursuant to the composite scheme of arrangement approved by the Honorable National Company Law Tribunal, Kolkata Bench vide court order dated June 26, 2019, the marketing and distribution of consumer products and retail divisions of HSIL Limited (HSIL) were demerged from HSIL and vested into Somany Home Innovation Limited. Further, the marketing and distribution of building products of HSIL comprising of sanitaryware, bath fitting and faucet, plastic pipes and fittings segments were vested into Brilloca Limited, a wholly owned subsidiary of SHIL. The company's equity shares were listed on National Stock Exchange and Bombay Stock Exchange on December 26, 2019.

SHIL is home to the iconic brand, Hindware, which as you all know has a rich legacy of enriching the lives of millions of households in India. Our versatile brand Hindware has demonstrated its versatility by its successful presence across our varied product line, across businesses ranging from kitchens to bathrooms and living room. We are relentlessly focusing on expanding it further. Our robust infrastructure includes 3 distinct distribution channels namely, consumer appliances, sanitaryware and faucet, and hardware for plastic pipes and fittings. Our operations are supported by an expansive distribution reach with omni channel presence extended across 35,000+ touch points, 3100+ distribution partners and 700+ modern retail outlets. Our business model and investments made during the last few years are now yielding results both in terms of topline as well as the bottom line. We have achieved a sharp recovery in the just concluded quarter of this financial year and we expect the growth and momentum to continue.

I will spend the next few minutes to take you through our last quarter's figures. The nine months' data is not comparable due to impact of lockdown and COVID during Q1 and Q2 of current financial year. The respective business heads will share in-depth details of their businesses as we move forward on this call.

The consolidated revenue from operations for the quarter amounted to Rs.551 crore approximately, registering a growth of 24.1% year-on-year. As compared to Q2 FY21, the revenue growth was 29.7%. EBITDA came in at Rs.60 crore having grown by 73.6% as compared to Q3 FY20 and 30.7% from Q2 FY21. EBITDA margins expanded by 309 bps from Q3 FY20 to 10.8% for the quarter under review. The profit after tax for the quarter came in at Rs.38 crore growing by 305.8% year-on-year and 93.5% quarter-on-quarter. Non annualized EPS for Q3 FY21 stood at Rs.5.21 per share, up by 307% year-on-year compared to the same quarter last year and 93.7% sequentially.

Moving on to the segmental financial figures, the Consumer Appliances segment revenue came in at Rs.156 crore, it registered a growth of 39.1% year-on-year and 37.4% quarter-on-quarter. EBIT for the segment came in at Rs.16 crore having grown by 375.3% year-on-year and 51.9% quarter-on-quarter.

Now coming to Building Products. The revenue for the building product segments stood at Rs.377 crore, growth recorded was 22.8% year-on-year and 29.4% quarter-on-quarter. EBIT for building products stood at Rs.34 crore and has grown by 51.7% year-on-year and 26.3% quarter-on-quarter.

Now coming to the Retail business. Just to update, we have closed 8 physical stores of retail business by September 30, 2020 and shifted focus to online sales and franchise-based sales model with an aim to move the retail business to cash earn model**.** Revenue for the retail segments was Rs.18 crore and is negative 28.3% year-on-year and negative 10% sequentially due to the reasons stated above. EBIT for the retail segment stood at Rs.1 crore as compared to Rs.3.2 crore EBIT loss in Q3 FY20 and Rs.2.8 crore EBIT loss in Q2 FY21.

We have laid the foundation for sustainable and profitable growth and are well positioned to continue our success story with support from all stakeholders including dealers and distribution partners, bankers, suppliers, vendors, shareholders, and teams who are working extensively to achieve growth and profitability. We are excited by the abundance of opportunities and scope for the growth in these businesses.

I would now like to hand over the call to Mr. Rakesh Kaul to take you all through the consumer appliances and retail business. Thank you and over to you.

Rakesh Kaul: Thank you, Mr. Malik. Good afternoon and a warm welcome to everyone. I will be sharing the overview of the Consumer appliances and the Retail business. I joined the company in 2015 to build the consumer appliances business from the ground up. We started with an extremely small base with just Rs.15 crore in 2015 with the kitchen appliances vertical under this business. The teams have worked exceptionally hard to deliver the planned growth as we see today. The business has always been a separate vertical even in the erstwhile HSIL pre-demerger as the business dynamics and retail touch points are distinct from that of building products business which is now part of Brilloca. To become the fastest growing appliances company in India for the past couple of years, we made strategic investments in the distribution channel, we launched highly differentiated and innovative products, expanded our presence across offline and online networks, digitized the supply chain, after sale service, marketing and most critical of all, research and development. Our investment in our research and development has yielded us considerable results as they have consistently helped us to launch innovative products which in turn have helped us to win new customers and retain old customers as well and also at the same time to achieve the sales growth we set out at the inception of the business. We have applied for 26 patents so far in just a short span of time which underline the recognition of our approach towards innovation. The consumer appliances portfolio as of now consist of brands such as Hindware Kitchen Ensemble, which houses kitchen chimneys, popular name for kitchen hood, built-in hobs, cooktops, built-in ovens, built-in dishwasher, sinks, food waste disposals basically all the large kitchen appliances which constitute category of large kitchen appliances.

The next one is Hindware Atlantic, which includes water heaters and electrical heating. Moonbow by Hindware consists of purification products and Hindware Snowcrest, which includes the air coolers and ceilings fans, tower fans, and pedestal fans as well. We also recently entered in a strategic partnership with Formenti and Giovenzana, a highly reputable Italian company to distribute a wide variety of high-quality modern furniture and modular kitchen fittings under the brand "FGV powered by Hindware". We also have a technical collaboration with Group Atlantic, a very prominent European company for our radiant water heater and electrical heating. Today we are amongst the top 2 players in the kitchen chimney segment with around 18% market share in the kitchen chimney segment. However, in the e-commerce and digital space where we focus and grown significantly. Hindware Kitchen Appliances leads, with an overall market share of around 40%. We are also amongst the top 5 players in the category of evaporative air cooling and amongst the top 6 players in the category of water heating segments, while on e-commerce platforms for both these above categories we are amongst the top 2 in the desert air cooler segment and amongst the top 3 in the water heater segment. We have also the largest range of internet of things or IoT products in the consumer appliances business in India. We have launched 6 products so far and are in the midst of launching some more. Faster digital adoption, increased penetration of internet in day-to-day life and availability of smart and affordable devices is giving rise to the applicability of internet of things where everything is connected or will be connected in India. We believe that the future is to have massification of technology from our consumer appliances business to launch more innovative products as we go ahead. We believe that the consumer should be empowered in order to build up a bigger consumer base and our decision to give power in the hands of the consumer has yielded significant results. We believe consumers to be our trusted advisors, it means letting go of a lot of things which we held close to learn and we want our consumers to be our trusted advisors which become a basis of bringing in new and innovative products into the market. Our last 2-3 years, CAGR has been 32% and based on the current market sentiments, we aim to achieve a CAGR of around 20-30% in the medium to long run.

Moving onto the Retail segment. SHIL launched Evok, an e-commerce chain offering a host of furniture and home furnishing products to meet the demand for furniture and home décor in India. Currently, Evok has 2 company owned and 20 franchised stores across the country. We realized our fixed cost like store rentals, etc were hampering our growth and in the last financial year, we took a strategic decision to shut 8 out of the 10 retail owned storerooms and we wanted to be leaner in our go-to-market approach through the franchisee route and the e-commerce route. This has helped us become EBIT positive in Q3 as compared to the Q3 of FY2019-20 where we were losing money. However, our strong online footprints through our e-commerce website which is our own i.e Evok.in and our presence on major third-party platforms like Amazon, Flipkart and Tata Cliq arehelping us to grow and enhance our visibility and customer connect. Our journey has just started now, and we are very excited to see the future unfold.

At this stage, I would now like to hand the call over to Mr. Sudhanshu Pokhriyal to give you an overview and take you through the performance of our sanitary-ware and faucet business. Over to you Sudhanshu!

Sudhanshu Pokhriyal: Thank you Mr. Kaul. Good afternoon, ladies, and gentlemen. I will give you a brief overview of SHIL's sanitaryware and faucet business. I will take you through the Q3 highlights for the same. I understand you will have many questions relating to our sanitaryware and faucet business which we can address after Mr. Pajnoo's brief.

Today, Brilloca is one of the leading players in sanitaryware and faucet segment in India with five brands spread across a wide pricing spectrum from luxury and super premium to mass segment**.** Our brands in the space are Queo, Alchymi, Hindware Italian Collection, Hindware and Benelave. I would also like to briefly talk about the segment evolution for the past 3-4 years. Sanitaryware and faucet business has seen extreme competitive pressure with entry of new players. In addition to this, the impact of COVID on our segment has actually been greater because of the end user our business caters to. Most renovation and construction activity was kept on hold during this time. On the back of the improving environment, in the last few months, we have seen an uptick in the growth in Q3 and as the situation normalizes, we expect the recovery to be fast. We are in the process of transforming the business to gain market share and track double digit growths.

Further in line with our focus on profitable growth, we have rationalized our product portfolio and made it market facing with greater emphasis on increasing our direct connect to customers. Currently, we have more than 2,000 direct retailers selling sanitaryware and faucet products and we want to expand distribution reach ever further. Towards achieving the same, we have identified regions and cities in the country where we are relatively weak as compared to competition and we have in place aggressive plans to increase our distribution and dealer base in these locations. We have further increased our emphasis on customer service focusing on satisfaction of distributors and dealers. Over the years, we have lost ground among some of our channel partners and now we have reestablished our presence in many of them.

We are also focusing on creating customer demand and our latest ad campaign "Thoughtful is Beautiful", identifies the white space of this segment and communicates how innovative performance led product solution that offers convenience to the consumers is where true beauty lies. The ad campaign and our recent innovative design led products such as sensor faucets, touch free and tankless sanitaryware which are addressing certain customer needs that we identify based on customer insight and market research which we have undertaken. We have also increased our focus on internal digitization through which we want to bring this transformation alive. This includes the introduction of distribution management system, dealer management portals, warehouse management and sales force automation amongst others. So, this an exciting phase for us as we are gearing the organization for market leading roles.

I would now like to invite Mr. Rajesh Pajnoo to take you through the plastic pipe and fitting business.

Rajesh Pajnoo: Thank you Sudhanshu. Good afternoon everyone. Thank you for joining us today. We are very enthusiastic about the prospect of plastic pipes and fittings business.

I joined the HSIL in 2015 to start the business from the conceptional stage and it has been an exciting journey. We commenced commercial production in that Company in August 2018 and in the span of first 8 months, we achieved a revenue of Rs.130 crore. While the manufacturing of CPVC, UPVC, PVC and SWR continues to be done by HSIL, we at SHIL bring it to the market and sell these products under the brand Truflo by Hindware. In the first complete cycle and first commercial year, that is last year FY2019-20 we have achieved a sale of Rs.250 crore till lockdown and in the current year so far, sale has been achieved in the first three quarters to the tune up to Rs.250 crore till December 31.

Our products are extremely well accepted in the market owing to their quality and strong brand recall and our strong relationship with influencer community. Our entire range of CPVC products that is for hot and cold-water application, this entire range received NSF certification from US which is prominent certification for potable water application in the world. Backed by a strong demand for our product and feedback we garnered from our channel partners, we successfully launched two new products this year also, that is, column pipes for borewell applications which is under patent and overhead water storage tank. These tanks are of premium quality and are durable and safety oriented. Both our new products have been well received by the market.

We actively engage with influencer community to build a strong network of channel partners who share our vision. We have initiated numerous marketing activities including participation in exhibitions, trade partner engagements, plumber needs and several outdoor campaigns which have helped us to amplify our visibility and maximize impacted exposure. Last year, we had a plumber connector of one lakh plumbers. We believe the addressable market size will keep expanding. Understanding needs and leveraging technology to develop products to deliver on our customer needs is how we will continue to grow.

With that, I would like to conclude the opening remarks and request the moderator to open the floor for questions-and-answers. Thank you.

Moderator: Thank you very much. We will now begin the question-and-answer session. The first question is from the line of Pritesh Chheda from Lucky Investment Managers. Please go ahead.

Pritesh Chheda: Sir, I was looking at your P&L and it seems to suggest that we tend to operate at about 35% gross margin and then there is another 11%-12% which is a direct cost head. So the contribution margin of the business is about let us say about 22%-23%. Employee head is another larger head where the operating leverage can flow in, so just wanted to understand that in your initial commentary when you are indicating the appliances business to grow at 20%-30% and the build ware products also to grow at a faster rate, this employee expense line should behave in what way, when you scale up from, let us say a Rs.1,600 crore revenue last year to a higher revenue over the next couple of years?

Sandeep Sikka: This is very important question and rightful question. First, I will just take you back one step and just try to communicate here that our company, which is SHIL along with the subsidiaries, is a very unique company in India today, wherein we operate three go-to-market channels separately and these are separate verticals internally. One vertical deals with the consumer appliances, second is building materials or building products, and third is a new channel which again has been developed over last 2 years which is the hardware channel. When we do this verticalization, all these business are built separately and on this call today we have CEO/COOs of all the respective teams. Definitely, it adds value and also cost to the bottom line in terms of the employee cost, but that is our strategy that each of these verticals should be built independently. Over a period of time we have gained success story over last 3-4 years and we have been reiterating over calls that we have done over 3-4 years even on pre-demerger times about this. This verticalization has an impact on overall growth of the company and the major part of that growth comes from the employees themselves.

Now answering your question, we feel that as the businesses grow, the employee cost in medium to long run should come down by around 10%-15% on an overall basis, based on the existing cost structure because employee cost is always the semi fixed cost or semi variable cost and the in each business as we are growing we feel that employee cost may be in the next 2 years we should be able to bring down by around 10%-20%.

Pritesh Chheda: For the current quarter, which is at about 10%, if you scale up your revenue to about Rs. 2,000 crore – 2,100 crore, is that the EBITDA margin number that we should be looking forward considering the operating leverage and will all your incremental business come at 35% gross margin?

Sandeep Sikka: Basically, all our businesses are not at 35% gross margins. These are different businesses. All our businesses have different gross margin structures like consumer product, the gross margins are different from what we do in sanitaryware and faucet and in pipes business, but you have taken a consolidated figure of an overall 35%. Definitely when the overall business grows, a part of the gross margin expansion should also happen. We are working on a contract manufacturing model and as the volumes build up definitely some part of the synergy is there with increased volumes; it gets built into the overall cost impact. So we feel that in next 2-3 years as the volumes expand with the type of growth which we are envisaging, we should be able to unlock an additional 2%-3% incremental gross margin.

Pritesh Chheda: My second question is one on the depreciation and one on the debt side, so we being larger distributor, I could not understand why we have such a large depreciation number of Rs.45 crore last year and let us say about Rs.30 crore in the first nine months and second, incrementally and as of now, how do you see the debt movement happening in the companies, what it is today and how do you see the debt figures panning out?

Sandeep Sikka: Answering your question on depreciation first, definitely the depreciation cost is there, so when we do consumer facing businesses, especially on the consumer side and also on our sanitaryware and faucet side which is a building material, the focus is on the premiumization of the product and when you do a premiumization of the product, we do lot of investments at our dealer end on building up their shops and creating our own branded display areas. As a matter of policy, we do an accelerated depreciation for this which is spread over 3-5 years, depending on what type of model we do and also there are various elements of investments, which we do in terms of creation of molds like when we go for a contract manufacturing, especially on the consumer side. Most of the tooling which we do, that we own, so that overall the aesthetic impact or design impact is not shared by the contract manufacturer with anybody else, so that leads to a depreciation charge. Like most of the retail shop which we do, they get these depreciated over 3-5 years and that also we will plough back money from the dealer if the dealer is not able to perform. Also one element of depreciation that this year is high is that we are having retail stores and as a part of the Hindware, the rental expenses now get divided between depreciation and interest, so, in Q1 and Q2 by the time the stores were closed, the depreciation is charged on account of expenses and since 8 stores have already been closed this financial year, so next year you may see slight decrease in depreciation on account of the store rental. On the debt side, on a consolidated basis in the first nine months on a year-on-year, basis we have been able to pull down the overall debt on consolidated basis by around Rs.135 crore to Rs.140 crore. The overall debt level today is at Rs.189 crore on an overall debt basis, consolidated and primarily it is working capital debt and very less quantum of long term debt that primarily goes towards the mold expenses.

Pritesh Chheda: You have three distinct businesses with three distinct distribution line needed for that business, how is the organization structure shaped up and it is fairly unique to have three businesses house or three distribution set up house under one company, so if you could just give a short knowledge on this?

Sandeep Sikka: This is a very good question in fact many guys have asked this question in past. Today we have whole management team here with each of CEO/COOs of the businesses who take their own decisions including in terms of the overall control mechanism as regard the organization which they focus on. We have these verticals and the whole synergy which we have built. Hindware brand, if you see 10 years back were servicing may be around Rs.4,000 crore market. We have built it up, we included faucets, which is another Rs.9,000 crore, then we built up pipes and addressable market size today is Rs.11,000 crore and another Rs.15,000 crore to 20,000 crore is an addressable market size on the consumer business. So, from Rs.4,000 crore market brand, which were addressing, today it is almost servicing Rs.40,000 crore plus market size. And it is not only just a small market share, we have communicated historically also that the consumer business which was a small business 5 years ago is now number two player in kitchen chimney, hood, and hob in the market.

Pipes is another very aggressive business which we are doing. We have disclosed what sort of turnover we are doing, we did in this quarter itself Rs.117 crore of sale itself, so, the potential or what we call as the real unleashing of a brand value, we are demonstrating in market today. Historically, many people have discussed with us whether we need to be investing in these verticals but today we are demonstrating the success of our consumer business. In 4 years of investments which we did, I think on an overall business, we invested around maximum of Rs.60 crore of EBITDA in last 3-4 years, and now we have a business which we feel in next 5 years may be doing Rs.1,500 crore plus business on an overall basis on a consumer side. and similarly, in next 5 years we see pipes doing more than our similar size Rs.1,200 crore to Rs. 1,400 crore on the pipe side also. So we have created a substantial value. Not only that, the Hindware brand, 10 years back which was primarily a bathroom brand has not only moved out from bathroom, it has gone to kitchen, it has gone to the drawing rooms, it now has its presence across the houses and it is not only present across the houses, it is taken as a premium trusted brand with the consumers and they are ready to pay a price and a premium for that.

Moderator: Thank you. The next question is from the line of Pranav Mehta from Equirus Securities. Please go ahead.

Pranav Mehta: I just wanted to understand on your bath ware segments, so how did sanitaryware and faucet, both the segments perform during nine months and if you can share some number for FY20 as well separately because you have shared it for pipes but just wanted to understand on the sanitary and faucet ware segments?

Sandeep Sikka: I think Mr. Sudhanshu briefly spoke about this on the performance of our sanitary-ware and faucet business. Over last 2 years, market has become crowded and we had few processes, which we were trying to build in last 2 years. Last quarter, we did around Rs.252 crore of sale for building products other than pipes. Nine months figures are not comparable over the previous figures but on nine-month basis we did around Rs.538 crore on the sanitary-ware and faucet vertical other than pipes. As far as pipe is concerned, we had done Rs.117 crore sales on the pipes for the quarter and around Rs.250 crore for the first nine months.

Pranav Mehta: Sure, Sir and have you taken any price hike in either of the sanitaryware or faucets product portfolio?

Sudhanshu Pokhriyal: We have seen unprecedented input price increase in the faucet specially and we have… actually in the Q3 period we have actually taken a 1% price hike in the sanitaryware business. However, we have planned 5%-10% price hike in the faucet business in Q4, so by the end of February in the last week of February, these prices would be effective in the market and this is to take care of unprecedented increase in especially brass prices and also in so these benefits will accrue to us starting from March.

Pranav Mehta: Sir and on your tiles segment Neom tiles, anything on that side? Are you gaining traction or are you mostly focusing on exports, how are things moving in that direction?

Sandeep Sikka: The primary focus of our tiles business is on the premiumization of the tiles. Mostly it is GVT tiles and we are doing an addressable market size of around Rs.10,000 crore. We do not want to focus on the mass side of the tiles, our whole strategy is built around adding value to the product, so we work along very closely with the European guys in terms of the design and design is ours and based on that design, we go for a contract manufacturing. So, initial responses have been very good. We started this business somewhere in December-January last year but immediately got hit by the COVID, but we have seen good traction recently. We are not disclosing financials separately right now as part of this conversation because the figure is not that big right now. But as you move ahead, I think once it attains a critical mass, we will definitely disclose the figures.

Pranav Mehta: Sir and one last question from my side, any new product segment you are looking to move into this consumer product division?

Rakesh Kaul: We being the fastest in the industry to have launched seven categories within just span of 4 years, so any category, which we add on in future, the basis of adding any category is an extensive consumer research where we see the long term demand plan and long term demand of that category and also as a brand and as business what is the differentiation approach we could bring into that category and the other objective is very clear that if we have to enter into a category, we have to be sure that we become the top three players in that category within 5 years of its launch and another factor which governs our approach to being in a new category to attain an ROCE of between 15%-22% which is a basis of that category. So we take these decisions based on all this extensive research which we conduct and from time to time, we will take an appropriate decision on the same and keep our investors informed.

Pranav Mehta: Sure Sir, and one question regarding pipes, so how many dealer distributors do you have currently for the pipe segment?

Rajesh Pajnoo: When we started, we started with 110 distributors, this is a distributor model business and currently we have more than 260 distributors across the country.

Moderator: Thank you. The next question is from the line of Rahul Garg from Shikha Family Office. Please go ahead.

Rahul Garg: My question is more on demand side, is it like pent up demand or we can sustain for medium-term like 2-3 years period and geographical wise if you can give the numbers like more on rural sides, we are looking at the demand?

Sandeep Sikka: We feel that the demand which is coming up initially, we thought in Q2 was pent up demand but, now we feel a full recovery happening in India and it is not only our sector, it is across various sectors when we try to monitor. Pent up demand can happen actually in fast moving consumer products, like when people tend to store some material and then the consumption increases. Our product is more linked to the end use. As a part of the overall growth scenario, which has happened in the COVID period is that people have been more exposed to various consumer products and they have understood the benefits of the consumer products. And based on the value added consumer products, which are available in the market people are seeing that how they can make their life easy. But, we feel that the scope inside the kitchen and inside the home space is very extensive. One thing COVID has left with everybody is work from home. Each and every organization has considered or is considering as a part of the processes, how much percentage of their staff should work from home so that they can optimize their cost and be more cost efficient. We feel that the demand structure is further going increase, this is an initial trend which we are feeling here and especially as the real estate sectors in certain pockets are also building up, we feel the demand from those sectors is going to increase. In pipes, we feel that lot of replacement is happening on the GI pipe side. So each of the segment we feel that there is a substantial leeway for further growth, both for the industry as well as for ourselves. Our internal plan and our internal targets based on the current market condition is that each of the businesses should outperform the industry by 1.5 to 2 times the industry growth.

Rahul Garg: Got it. So, how does it work for us like for example, if growth kicks in and demand goes in hyper mode, how we are going to serve it, is that like from the outsourcing perspective if you could put some color like the product mix or how we give the heads up to the outsourced vendors, how do we manage that demand scenario from the market to the outsourcer?

Sandeep Sikka: If you see over last many years, we have excelled ourselves in terms of developing outsourcing and contracting model. Based on the visible market scenarios over next 2-3 years, we work very closely with our vendors. We understand what their capacities are, what are their capacity utilizations, what sort of product design innovation we are working on, also there is a pipeline of new inventories which is there. So, we feel that we can service this growth on a medium-term range with the contract manufacturing. And now contract manufacturing is also a very viable structure in India and this also brings benefit that the guy who is actually doing a contract manufacturing, is primarily focused on bringing a quality product at a right price at the right cost and that has helped us in terms of building up our business. But definitely over a period of time, after reaching a critical mass in respective businesses, the company may evaluate in terms of looking at inhouse manufacturing but the whole logic of doing this is building an efficient capital model, wherein our focus would be that if we put up manufacturing, our return ratios should further enhance over a period of time, although in a short run they can put some pressure on capital employed in terms of building of the assets, but they should unleash the value in terms of higher ROCE with inhouse manufacturing.

Rahul Garg: Got it and we work with co-design like we also design, or we get the help from vendor for example, in the frame it is showing that capability to design and showcase its product to the clients. How does designing works?

Rakesh Kaul: We design our products ourselves. We have an inhouse design set up in our organization at SHIL and we work closely with our design agencies, some of them inhouse and some of them outsourced. And once we get to the stage and again design is all inspired by the consumer needs actually. So, when once we are into an extensive research, see the needs and gaps and then we create a renovation around the need and gap through our innovative design, then we work closely with our tooling guy to get the molds for that. These are all done under very standard NDA agreements where there is no disclosure of the design as such with third parties and then once the mold is ready, we parallelly work with our contract manufacturer to work on the product and manufacture exclusively for us, so that is how go about it. So, most of the times if you see in the consumer appliances business, we are working on our own models or own designs as such.

Rahul Garg: Got it and how do we measure innovation in our organization? For example, IKEA does this outsourcing from the design perspective. Have we taken such initiative in the organization?

Rakesh Kaul: Yes, we from time to time do a lot of consumer research, an extensive research on the basis of what will be the future needs of consumers and in my opening remark, as I said we have registered around 26 patents in a matter of just 3.5 years, this points to the significance of innovation in our organization. Simple example I can give you is the example we have a water purifier that treats microbes, which has an auto fill function which means you can just keep the jug there and it will fill it to a level and you do not have to wait there for minutes for the jug to get filled and you can take out the jug and put it into the refrigerator. So, we have seen these smaller needs of the consumers and we have amplified them to our use of technology to make the consumer buy simpler. So, at various stages of our development and thought process we take this fact into consideration that how do we make the lives of our consumers simpler and easier through the means of technology. I hope that answers your question.

Moderator: Thank you. The next question is from the line of Uttkarsh Sogani from Moneybee. Please go ahead.

Uttkarsh Sogani: Sir, my first question is on our revenue target going ahead. So, I see the revenue contribution of the building product segment coming down and the consumer segment going up. So, what is the long-term target for this?

Sandeep Sikka: We do not give guidance on a quarter-to-quarter basis but, on a medium-term to long-term range if we see on a consumer side for last 2 years, our CAGR is around 32% and guidance to market is that we should be able to build up 20%-25% growth on a medium-term to long-term basis. As far as the building products business is there where we have sanitaryware and faucets, industry is growing at around 7%-9% and again we have said that on a medium-term to long-term basis based on the current market conditions we should be able to beat the market by 1.5 times to 2 times the industry growth. As far as pipes is concerned it is a new business, we are just completing second full year of business and the target is in next 5 years we plan to build more than a Rs.1,000 crore business of pipe itself.

Uttkarsh Sogani: Okay, and when you get production outsourced, are they exclusive to us or they manufacture for someone else as well?

Sandeep Sikka: As far as the sourcing of our building products is concerned that is primarily exclusively from HSIL, but we also do lot of traded products in terms of the procurement of faucets and sanitary-ware from third parties, both imported and outsourced. But as far as the consumer business is concerned, we do not have a dedicated vendor there, most of the vendors are focused contract manufacturers and they are manufacturing for various brands, but the design element in consumer business primarily we own so that we have exclusivity in the market.

Uttkarsh Sogani: And Sir, how much of that would come from China, the imports?

Sandeep Sikka: Our overall imports from China as far as the consumer product was less than 20% but as we move ahead, we see that we are building up the vendor resources within India to even shift those to the Indian base.

Uttkarsh Sogani: Okay, Sir and just last question on the advertisement expenses what is the target advertisement expense and whether we share anything with HSIL for our branding purposes?

Sandeep Sikka: No, you have to understand here now that the entire Hindware brand is a part of the SHIL, which is Somany Home Innovation Limited. HSIL from the perspective of building products is pure play focused manufacturer on an OEM basis.

So, on a broader side again, we have started various campaigns in the market both on the consumer side as well as the building material side, and lot of BTL happening on the pipe side also. But on a medium range again we feel that we will keep investing around 4%-4.5% of our businesses sales into communicating newer products to our consumers and maintain the growth in the business.

Moderator: Thank you. The next question is from the line of Deepak Poddar from Sapphire Capital. Please go ahead.

Deepak Poddar: Sir, regarding margin you spoke about in next 2-3 years incremental gross margin of about 2%-3% is likely and plus the kind of growth that we are seeing. So, we are sure we are going to get the operating leverage advantage as well. So, just wanted to understand something on the EBITDA margins trajectory or the EBITDA margin outlook that we might be having over next may be 2-3 years that would be quite helpful.

Sandeep Sikka: This has to go business by business. Like consumer products, there is huge potential which we feel and that it is a very nascent business which we started 5 years back. 2-3 years was an investment phase and around 2 years back we became EBITDA positive and now we are PBT positive with a good number on the customer side. So, we feel that consumer business, in 2-3 years' time, we should be able to build up a model wherein our EBITDA margins are ranging between 14%-17% and in terms of building materials also in a similar range this is based on our contract outsourcing model. But as we build synergies into the business model, we feel there is a great upside as far as the margin expansion is concerned from here.

Deepak Poddar: So 14%-17% is the kind of potential that you highlighted in two of the major businesses that we currently have, and the new businesses can have much higher potential, right? Is that understanding right?

Sandeep Sikka: I am giving an overall guidance because the various businesses are at various stages of their growth. So, basically on sanitaryware faucet we were around 16% on post de-merger basis, so that can expand by another 2%-3%. But on the margin expansion on the consumer and pipes business will be substantial.

Moderator: Thank you. The next question is from the line of Bharat Sheth from Quest Investment. Please go ahead.

Bharat Sheth: Hi! Sir, thanks for the opportunity. I wanted to get some sense that Hindware, where building material once upon a time we were No.1, and what has really happened that we lost the market share and now we are talking of growing again at 1.5 times than the market. So, where we went wrong and what are we exactly are doing to gain market share?

Sandeep Sikka: Markets are very dynamic today like anything which has high margin game. Sanitary-ware used to fetch the highest margins in terms of the building products if you see as from previous quarters. Definitely many of the other players who were not there in sanitaryware, they thought of on an outsourcing model they started selling which definitely put the pressure on the overall markets. So, we run a strategy that we do not discount our products in terms of the pricing to the market because being a leader if you start doing that then you can have a higher growth and higher market share but, then the bottom-line growth will be hampered. So, we tried to create a balance over last 3-4 years and we had done some course correction both in terms of rationalization of the product mix. Ultimately our focus is that we should create a value in the eyes of the consumer they should feel delighted by buying our products. They should feel enlightened in terms of the brand which they have bought. So, we have over last 12 months or so, we are focusing on introduction of newer products, newer designs, better aesthetics. Also, we started a lot of rationalization of various interactions which we used to do with our dealers, distributors and we have done to large extent of course correction there. We have also worked around improving how we can improve our ROI as well as the dealers' ROIs at the same time. I cannot disclose that as it is the part of the strategy we have. But definitely, we feel the impact of that has started coming in last three– four months and we are bullish in terms that it will definitely help us in bringing the growth on the sanitaryware and faucets side.

Bharat Sheth: Sir, and second thing in how much business out of that building material is coming project side?

Sandeep Sikka: We have a ratio of 70% coming from retail and 30% from which is the institutional sale we call it. As a part of strategy, we now focus to build both the models, the focus is both on the retail and also build up again institutional sales.

Bharat Sheth: On these consumer kitchen appliances where we are except one or two segments, we are either number 4 or number 5 players, so what exactly make sense to again have a large product portfolio which can dilute our marketing focus or building really a good brand. So, what exactly is our strategy?

Sandeep Sikka: If you see, we spoke about our strategy that whenever we look at any category introduction, we should be able to bring lot of value in terms of our positioning in the market and we have fairly demonstrated like kitchen chimneys, hoods, and hops so we are number 2 player in the market in less than 4 years.

Rakesh Kaul: I think it is a valid question in terms of that why have we extended into the largest kitchen appliances space in terms of all the categories. Yes, we have significantly improved our position in terms of being the number-2 player outright in kitchen chimneys and among the top 4 brands in the hobs which are copper top hobs as well as the built-in hobs. At the same time, there is a lot of interest in the consumers as far as the built-in product is concerned and one is that we have to be in those segments present like countertop ovens or built-in dish washers, built in ovens predominantly to complete the range because when a consumer shops in a modular kitchen he probably looks at all these products. So, as a brand, it does not make sense to be present in just one or two parts of the larger kitchen appliances. Having said that, our focus is significantly increased on the kitchen appliance other than the kitchen chimneys and hoods segment in this quarter on dish washers. There is a lot of interest in the consumers in the dishwashers and built-in ovens as well and we see a significant proportion of business also coming in the next 2-3 years from that category. So, we continue to spend on that as well and while from a marketing perspective, kitchen hoods and hops continue to be the lead categories in terms of the overall market size contribution in larger kitchen appliances.

Bharat Sheth: I appreciate that on kitchen appliance, but I am talking on the consumer electric side also where like a fan and then the water purification and air purification, which is again a different category than kitchen. Within these electronics also why several verticals that we would like to have?

Rakesh Kaul: I think predominantly if you see Hindware being an iconic brand in the bathroom space, we had a base of more than 60 million consumers covering 300 million Indians so, we needed to leverage that consumer base by not only being in the bathroom as a leader, but also coming out of the bathroom and getting into the spaces of living rooms, drawing rooms and bedrooms and for each of these categories we have entered by creating a significant innovation into this category to make a meaningful appearance for ourselves, it is not that we have leveraged our distribution strength by getting into those categories, we have entered into each of these categories with certain thought process and certain inbuilt product features or innovation which are differentiated from the competitors. So, hence if you see our presence in water heaters where we have attained a 7% market share, in evaporative air cooler segment again a 6% share in just a span of 3.5 years of launch is a testimony to the fact that we have done pretty well.

Sandeep Sikka: And these are the markets which are fragmented markets.

Rakesh Kaul: Very highly fragmented where the leader itself is not more… for example, in water heating segment, the leader itself is not more than 16% to 17% and in air coolers the top player is at 28% - 29% and the second player is at 12% to 13%. Highly fragmented market yet we have attained shares which have upheld us to the top-5, top-6 within three and half year goes to the testimony to the fact that we brought in innovative products, right product which actually filled the needs and gaps of the consumers. So, from that perspective to being in a larger home space, I feel Hindware to be a perfect brand set.

Bharat Sheth: And on retail business what is our strategy? Does it really fit in our strategy or we would like to discontinue over a period of time, any thought on that because apart from cash burn not being the only thing, but management bandwidth also it diverts?

Sandeep Sikka: Basically, what you have to see here is that how each product is performing in terms creating a value at the bottom line. There are various product baskets, which are very essential to buy out the counters in the electrical or any space which you have. So, we keep focusing, we keep evaluating these products. Any product which is not able to have a demonstrable impact in terms of volumes which we can sell and generate over a period of time, we may consider that we may get out of that industry. So, like air purification, it is very new segment in India. Air purifiers historically were not there but today it is still a seasonal business, but we feel that now every home which is getting built up now is buying one or two air purifiers. The same trend was there if you walk back 25 years, how many houses had air conditioners, hardly anything. But then the trend came in each and every house has air conditioner, it is an essential necessity today. We feel that the way our air pollution is in India, in various pocket segments over a period time each house will need to have an air purification and a water purification similarly on the water side into their houses. We feel there is a good potential market upside which is there, and businesses are still at a nascent stage and will build up over a period of time.

Bharat Sheth: And last on this retail business. So, what is our strategy, because when we want to compete against several particular people with deep pockets and also retail so, does it really make a business sense to have physical retail also?

Sandeep Sikka: Basically, there is lot of transformation. I do not know whether you cover the company on a day-to-day basis. We had around, if you see 18 months back, 14 owned stores. So we have shut down 12 stores now we have just 2 stores which we are there to showcase our products and our brand store concept to various franchisees, the franchisees which were hardly anything. So, we have built up almost 20 franchise stores so that it is a better model for us, and we are focusing on e-commerce sale through our own website evok.in and also through Amazon. But the concept here is not a cash burn model. If you see our retail segment business which will disclose as a part of the segment, we are EBIT positive on that so which we are not losing money we have started building profitability there.

Moderator: Thank you. The next question is from the line of Sachin Kasera from Swan Investments. Please go ahead.

Sachin Kasera: Sir, first question is you mentioned that you look at categories where you think that you can be one of the very strong players that is only when you enter and there was just a previous question from one of the participants regarding the participation in so many categories. So, when we say that we want to be a strong player it is across mainly the 3 key products or 4 key products or when you are saying we have presence across 10 products to 12 products, each product in the next 3-4 years we see ourselves as one of the very strong players?

Rakesh Kaul: A good question, so at the outset also in my earlier remark also I have said the basis of being us in the consumer appliances category or any of the category is that, within launch of that category within 5-6 years of the launch of that category we need to be among the top three players. So, it is not that we are seeing each of these categories that we just need to be dominant in one category or two categories. We need to be dominant and a profitable player in each of these categories. We need to be in the top three, and towards this, we have successfully completed our course in kitchen appliances within a span of 5 years. In kitchen chimney's, we have entered into the top 3 and in the evaporative air coolers and water heaters segment we have already been closer to the top-5. So, it is not that we would look at each of these categories to be dominant because each of these categories have different market sizes and different market dynamics. But in order to be a sustainable and a profitable player in each of these categories we are very clear that we intend to be among the top-3 within the 6 years of launch actually and we are definitely there.

Sachin Kasera: So, basically each and every product that we are launching is being done after a very thorough understanding of the market and the potential and the competition and after only we are very strongly convinced that we can win the top 3 in the five year – 6 years are we launching any product?

Rakesh Kaul: Rightly, you are very right on that.

Sachin Kasera: Sure. Second question on the building products side, if you could just tell us what exactly is the type of… because there is pricing transfer involved between us as well as our group company. So, how does that exactly work, that is point number one. And secondly, in terms of are we only going to restrict ourselves to Hindware brand here or we could look in terms of getting some even higher end or may be imported brand from some of the other European countries thereby expand the overall range. What is the thought process there?

Sandeep Sikka: First the question which is there on the transfer pricing, when we source some material from HSIL, this is done in a very transparent manner. As a part of the board mandate, we hired one of the big four accounting firms and on an annual basis they give us a benchmarks and that's how transfer pricing mechanism will work and the concept here is whatever is the cost of production plus markup basis. If you see the results of HSIL, very transparently you can see how much margin is there on the building product side in HSIL and that is what we feel that is a trend based on the current market condition. So, it is transparent mechanism, it is done with the approval of the shareholders and it is done with the backing of transfer pricing reports of the big four. Second question in terms of your brand, so in terms of our own ladder if you see, we have the mass market brands and we also have a premium brand the focus is not to bring a third brand from outside and sell because we have premium brands like Queo, we have Alchymi, we have Hindware Italian then we have medium market brands which is Pure Hindware and then bottom-line brand we have Benelave. So, we already have a full basket of brands within our organization and we feel that once these brands start performing on a full basis, we have a substantial head way in terms of achieving our growth on each of the brands which we right now have within ourselves.

Sachin Kasera: Sure, and just a follow up on, in the building product segment, right now we are majorly into sanitaryware and faucets, but the adjacent categories of further hardware like for example taps and some of the other products which are used in the bathrooms, are we looking at some adjacent categories also to get into that? For example, Jaguar has had a successful transition from taps and some other products into your sanitaryware and faucet, are we also looking at something like that?

Sandeep Sikka: If you see, we started our faucet business around 7-8 years back and today we have a market share of around 10% on the faucet side. Earlier, the company was pure sanitaryware manufacturer way back till 2014 and we started faucets in a real manner. So, we have also extended our brand horizon in terms of capturing the more counter share but at the same time competition is also trying to do the same. But now as we told, we have three distinct go to market channel and our initiative is to bring best of the products and introduce into those channels so that we can earn better margins, better gross margins and we are able to absorb the fixed cost over a higher spread of gross margins.

Moderator: Thank you. The next question is from the line of Pritesh Chheda from Lucky Investment Managers. Please go ahead.

Pritesh Chheda: I am just asking that all the brand rights stay in our company, right Somany Home Innovation Limited? There is no brand which stays in HSIL and there is no payout on account of royalty or any other expenditure that needs to be paid to HSIL, am I correct on that?

Sandeep Sikka: I will just make everything clear. HSIL has packaging business which has nothing to do with SHIL. So, all the brands relating to packaging business like AGI Glasspack, are part of HSIL as a part of the de-merger. Hindware brand and all other brands which are consumer facing brand let it be for the consumer business, let it be for sanitaryware and faucet business or the pipes business or even the furniture retail business, as a part of the scheme of the de-merger, they are part of SHIL.

Pritesh Chheda: SHIL okay.

Sandeep Sikka: There is no question of any royalty payment outside.

Pritesh Chheda: So our transaction with HSIL will only be to the extent of procuring as a contract manufacturer?

Sandeep Sikka: Yes, as a third-party vendor.

Pritesh Chheda: As a third-party vendor.

Sandeep Sikka: And this is done in the most transparent manner as I just communicated.

Pritesh Chheda: So it is basically a distribution business for us. What would be the net working capital cycle that you would operate at sum total for all the business lines or channels together?

Sandeep Sikka: If you call us as a distributor, it may not be the right terminology. So basically, we service consumers right from beginning, from door-to-door basis other than manufacturing today. Because it is not only distribution it goes even in creation of products, building that product, building a story around the product, selling it to the dealer, selling it to the consumer, servicing, doing after sales service and building a trust in the consumer. So, that entire thing is being done by this vertical other than the manufacturing. So, the benefit of this is when we are looking at manufacturing. The core manufacturing is looking at its own efficiencies over a period of time which will come through to us and we are building our efficiencies on each one of the marketing we do, the distribution we do, the supply chain we do, which has been our focus, and this is what we have communicated also over last few years.

Pritesh Chheda: The net working capital cycle?

Sandeep Sikka: Net working capital cycles this year, have changed to large extent but the real measure of working days you have to see the Q3 sales because if you take nine-month sales then it is a misnomer. So, we have been trying to bring down, on an overall basis, to around 20 days of working capital when we try to compare ourselves on a March basis to the December basis. Various businesses have their different market dynamics. So, for each business on an average, net working capital on an average basis if you see it is around 100 days of net working capital.

Pritesh Chheda: But until last year when I see, let us say I must have seen your balance sheet. I see on a consolidated basis net current asset of about Rs.180 crore on our Rs.1,500 crore top line?

Sandeep Sikka: The definitions you use and the definition we use, may have misnomer, so we can do on a sideline and communicate to you how can fill it.

Pritesh Chheda: Okay, otherwise in your opinion it is about 100 day of net working capital, right?

Sandeep Sikka: Yes.

Pritesh Chheda: And that would stay the way it is?

Sandeep Sikka: It should because I cannot fix it like that because this is again, we were operating in the market and market dynamics change a lot. But our guidance is that we should be in a range of 10% up or down.

Moderator: Thank you. Ladies and gentlemen, due to time constraint that was the last question for today. I would now like to have the conference over to Mr. Manish Mahawar for closing comments.

Manish Mahawar: Thanks, Rutuja. On behalf of Antiques Stock Broking, I would like to thank the team of Somany Home Innovation Limited for providing us an opportunity to host the call. Sir, would you like to make a closing comment Sir.

Sandeep Sikka: Thanks everybody, I would like to thank all the participants who reverted with the good set of questions and it is our endeavor to answer all. We had time limits on the arrangements, we already exceeded that. So, this company is under transformation. I think we have been communicating our story over last 4-5 years you can go through our Conference Calls transcript on a pre-demerger basis on the website of hsilgroup.com and post demerger on our website shilgroup.com. But our story remains the same as we invested in terms of expansion of the brand horizons and we have now started demonstrating the success of the same, both on the top line and the bottom line. And this is backed by the very hard work which each of our stakeholders let it be our vendors, dealers, distributors, employees and even our shareholders who have been long-term with us and have been very patient. They have been supporting us, but I think now the time has come to unlock the value and really build the growth in the business. I thank everybody who joined us today on the call. Thank you very much.

Moderator: Thank you. On behalf of Antique Stock Broking, that concludes this conference. Thank you for joining with us and you may now disconnect your lines.

Notes:
1. This transcript has been edited for readability and does not purport to be a verbatim record of the proceedings.
2. Figures have been rounded off for convenience and ease of reference.