"KDDL Limited
Q3 FY2020 Earnings Conference Call"

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Moderator: Ladies and gentlemen, good day and welcome to the KDDL Limited Q3 FY2020 Earnings Conference Call. This conference call may contain forward looking statements about the company, which are based on the beliefs, opinions and expectations of the company as on date of this call. These statements are not guarantees of future performance and involve risks and uncertainties that are difficult to predict. 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. Yashovardhan Saboo, CEO for his opening remarks. Thank you and over to you!

Yashovardhan Saboo: Thank you and good afternoon and welcome everybody for our Q3 and nine months FY2020 earnings conference call. I am joined by Mr. Sanjeev Masown, CFO of KDDL and SGA, our Investor Relations Advisors. Mr. Raja Sekhar, CFO of ETHOS is away on a study program but he will be joining us over the phone. I hope everyone had gone through our updated investor presentation meanwhile.

Let me start with the consolidated numbers. Consolidated revenue for Q3 FY2020 rose by 18.7% year-on-year to Rs.203.7 Crores, for the nine months period it grew by 8.5% to 515 Crores. Consolidated gross profit for both Q3 and the nine months period FY2020 was up by 9.8% to 79 Crores and Rs. 215.5 Crores respectively. Consolidated EBITDA for Q3 FY2020 was up by 6.7% to Rs.26 Crores and for nine months it was by 21.9% to 62 Crores. Please remember that the growth in EBITDA is significantly impacted due to changes in accounting standards with the applicability of IND-AS 116 standards. These new norms impacted the accounting for other expenses, depreciation and finance cost for the company. As the result, the consolidated adjusted EBITDA on like-to-like basis for nine months FY2020 has degrown by 28% to Rs.36.5 Crores. This is mainly on account of higher other expenses due to new store openings in our retail business. Consolidated PBT for Q3 FY2020 and nine months FY2020 stood at 8.1 Crores and Rs. 10.1 Crores respectively.

I will now discuss the business wise updates. Our manufacturing business performance was lower compared to the previous quarter. There was decline in revenue and operating expenses was relatively higher. The change in revenue mix was also weighing down the profitability of the business for the quarter. We have seen a continuous decline in Swiss Watch business globally especially in the segments of the watches priced below Swiss Franc or US $3000. Swiss Watch exports for the year, year 2019 as a whole in value terms grew by only 2.6% as compared to 6.2% in 2018. So there has been a marked slowdown in the growth.

More important in the segment below 3000 Swiss Francs there has been a marked decline. The lower price segment consists mainly of Quartz Watches which degrew by 6.2% while the segment of mechanical watches, which is mainly concentrated above the 3000 Swiss Franc price points, it grew by 4.5%.

The challenges in the Hong Kong market and slowdown in the Middle East are some of the important reasons besides the impact of the smart watch owing to which the watches in the lower priced segments have degrown. The decline of Swiss Watches in the lower priced segment trend has been witnessed for many quarters and is expected to continue for a bit longer. We have been conscious of these markets developments and have accordingly moved up the value chain reducing our dependence on lower price point watches.

The encouraging part for us was that domestic market continues to witness traction and is growing. We are strengthening our position there. In the last few weeks, the Coronavirus threat has been impacting this business. This will have a significant impact on the Swiss exports in the immediate future as the markets of China and the Far East are very important for Swiss Watches. Also Chinese and Far East Asian travelers buy watches when they travel abroad, therefore this segment is likely be impacted in the immediate future. However, it will also provide us additional opportunities to make important inroads into other customers who will want to derisk supplies from China.

We believe this is going to be a very important opportunity for us after the immediate impact of the Coronavirus wears out. Our manufacturing revenue for the quarter was recorded at Rs.42 Crores similar to the levels recorded in corresponding quarter of last year and for the nine month period it grew by 6.6% year-on-year to Rs.140 Crores. EBITDA for Q3FY20 stood at 6.4 Crores down by 7% year-on-year and EBITDA for nine months stood at 23.7 Crores up by 2% year-on-year. EBITDA margins came in at 15.1% for Q3 as compared to 16.1% in Q3 of previous year. While EBITDA margins for the nine months period was 17% in the current year versus 17.7% in the same period of last year. The marginal reduction in EBITDA is due to change in the revenue mix of different business segments.

Profit after tax for Q3 of the current year stood at Rs.1.6 Crores and for nine months was at Rs. 8.6 Crores. The watch component business witnesses a decline of 15% in Q3 over the revenue of the previous quarter. The nine month period; however, the watch component business registered a growth of 5% over the previous year. This segment registered revenue of Rs.30 Crores in Q3 and Rs.100 Crores for the nine months period of the current year.

Precision Engineering business, the revenue in Q3 FY2020 was Rs.10.6 Crores higher by 17% compared to Q3 of last year; however, a decline by 12% if compared with Q2FY20, the decline in revenue for the quarter was mainly due to economic slowdown in the domestic market across various segments including automotive segment and electrical and electronics. We are continuously realigning the capabilities in line with the market expectations and developments. We are confident that our initiatives for improving operational efficiencies, realigning the product mix and strengthening of the teams will help in healthy growth and sustainable profits for the company.

At Estima AG, the company that is acquired in Switzerland, we are witnessing a good response from the new customers and we expect to capture an additional market share in the European market for the mid and high priced segment, which would otherwise prove impossible to capture working out of India. We continue to believe that the Swiss Origin Regulation will help us in growing our watch component business through Estima and our presence in Switzerland will be a major stepping stone for capturing additional market share.

I will now discuss our retailing business, ETHOS. The domestic watch business picked up well in the third quarter on the back of festive season buoyancy. Our strategy of offering the widest variety of watches to the Indian consumers at the best possible price is playing out well with stable gross profit margins and a steady growth in revenue. We believe the best consumer experiences backed by strong digital marketing approach, trust and authenticity of our retail stores, our pan India presence will continue to help us to outperform the competition and gain market share as indeed we have done in the current year too.

It is heartening to see the response of brands to associate more readily with ETHOS the case in point being taking over of existing boutiques of Omega and Rado in Jaipur and also opening the first and only Hublot brand exclusive boutique on joint venture basis at Mumbai.

We continue to build complimentary verticals for our watch retailing business, the latest being the launch of a dedicated independent website for the sale of certified preowned watches, which is fully supported by our state-of-the-art service center. Our goal is to make ETHOS the customer’s first and only choice for luxury watches.

Exclusive brands or house brands are an important part of our strategy and we are happy to report that our partnerships continue to gain immense traction. We have 15 brands on exclusive basis across varying price points that help us crop for a differentiated buying experience to the end consumer with significantly higher margins for us. Over the last few years, we have focused mainly on the price segments between Rs.50,000 and Rs.500,000 for the exclusive brands. Recently, however we have extended this strategy for higher priced watches, this extension allows us to add newer brands to our portfolio and to cater to super luxury segment which is the fastest growing price segment globally and also in India.

On the new stores front, with the addition of the Rado and Omega exclusive boutiques in Jaipur our total store count is now 55. Both the new stores are approximately 500 square feet each.

Let me give you some financial highlights for ETHOS. Our billings for Q3 FY2020 grew by 20.7% year-on-year to Rs. 179 Crores while for the nine months period it grew by 6.6% to Rs. 420 Crores. Billings of exclusive brands grew faster at 48% year-on-year to almost Rs.40 Crores in Q3. For the nine month period, the growth was nearly 51% year-on-year to nearly Rs.95 Crores.

Same store growth for Q3 of FY2020 stood around 7%. Exclusive brands contributed 22.1% to the Q3 topline and 22.6% to the nine months period topline. Consolidated ETHOS revenue for Q3 posted a strong growth of 23% year-on-year to Rs. 160 Crores while for the nine months period it was up 7.9% year-on-year to about 369 Crores.

Consolidated gross profit grew by 17.2% in Q3 and 11.5% in nine month period year-on-year. Gross profit margins for Q3 stood at 28.5% as compared to 29.9% last year same quarter on account of slight increase in discounting which happened due to an additional but very successful sales in Q3. For the nine months period, it stood at 29.5% an increase over 27.6% during the same period last year.

Reported EBITDA for Q3 rose by 25% year-on-year and for the nine months period by 58.6% year-on-year. As also mentioned previously, the EBITDA gain reflect changes in accounting standards. Adjusted for Ind-AS 116 consolidated EBITDA for nine months degrew by 19.3% year-on-year to Rs.25.2 Crores due to higher other expenses on account the new flagship store openings.

In this connection, I would like to stress on this little bit more as most of you are already informed during the last six months, we have opened some very important flagship stores which are the cornerstones of our new strategy. This includes the Kolkata store, the large flagship store in Hyderabad, the ultra luxury collectors store at Chanakya Mall in Delhi as well as the luxury store in Chanakya and in Pune, so collectively these 5-6 flagship stores which opened during the period June to around October, they have added a lot to the other expenses by way of rents, salaries, manpower cost and launch expenses; however, the full impact of the revenue is not being felt.

I am happy to report that in all these stores we are a seeing a huge traction and the entry of ETHOS into price segments that we were not before, we are selling more in the luxury segment and we are establishing in each of these cities, ETHOS as the number 1 retailer of premium and luxury watches.

The adjusted EBITDA margins for the nine month period stood at 6.8% compared to 9.1% in the previous year. Consolidated profit after tax in Q3 came in at 4.7 Crores while for the nine month it stood at 1.9 Crores versus 12.2 Crores in the same period last year. Stock carrying at the end of December 31, 2019 is about 8.2 months, this is also higher than the previous year mainly again on account of the fast paced store roll out as you understand the stock in the new store shows up in the overall stocking while the sales is still only a few months and not the full year. We are very confident that over the next year we will see the stock in terms of number of months go down to the original projected levels as the sales from these store starts to kick which it already has.

At ETHOS we remain buoyant on our strategy and expect to grow faster as the economy turns around and we expect a more solid growth for the economy as a whole. I now welcome your questions and participation.

Moderator: Thank you. Ladies and gentleman we will now begin the question and answer session. Ladies and gentlemen, we will wait for a moment while the question queue assembles. The first question is from the line of Priyanka Singh from Atidhan Securities. Please go ahead.

Priyanka Singh: Very good afternoon Sir. I have a couple of questions. How many stores are expected to launch in the next quarter and subsequently in the next financial year? and what is your capex plan for the next year for manufacturing as well as for the retail business and has the supply situation of Rolex watches improved?

Yashovardhan Saboo: Let me answer all the three questions. I will start with the shortest answer which is the third one - the supply situation for Rolex. In the Q3, I can tell you that supply situation with Rolex did improve and that is one of the reasons why we achieved the fair same store growth despite obviously overall macroeconomic situation and consumer sentiments for the sale. So we are hoping that the improvement in the supply situation in Rolex will continue. I must tell you; however, that worldwide Rolex demand has gone through the roof and we cannot really take anything for granted. Given the fact that the markets in China will probably remain challenged for the next couple of months on account of coronavirus, I do believe that supply of Rolex watches to India should be actually much better than previous year. That is on the Rolex situation. For the next year, in terms of new stores we have basically planned three new stores one of them flagship store which is at Mumbai, at the new mall coming up in BKC that is expected to launch in the first quarter of next year. Two other new stores one in Bengaluru and one in Delhi, Bengaluru in the area of Whitefield where we have not been present. There is now a flagship store, it is an ETHOS store and similarly a new geography in Delhi where we are not present, it is a new mall, Vegas Mall these are the two stores. They will also be launched in the first quarter of next fiscal. We have not planned any other store launch other than that there is a mono-brand boutique of Omega, which we will launch at Palladium in Mumbai probably in Q3, this is going to be the first and only boutique for Omega in Mumbai and we are really looking forward to doing this. It is going to be very, very important for us. These are four stores that we have planned in the next year; however, we have also planned about four closures of store in fact there maybe five closures of stores mainly smaller stores where we do not see enough traction. As you know our strategy is to go in for larger stores instead of smaller stores and stores which do not fit in our approach we plan to close them, so overall the store count is not going to go up. Your last question was capex for ETHOS and for manufacturing. In manufacturing, overall across all the manufacturing businesses we are looking at a capex of between Rs. 10 Crores and Rs. 11 Crores. Much of it is for some machines and some tools, but there is also upgradation at our dials factory in Parwanoo which is in need of upgradation of some section other than that is mainly routine capex and in ETHOS we are expecting a capex of about Rs. 6 Crores to Rs. 7 Crores most of it being in the 3 stores and a couple of renovations.

Priyanka Singh: That was very helpful. Thank you, Sir.

Moderator: Thank you. The next question is from the line of Shalini Gupta from Quantum Securities. Please go ahead.

Shalini Gupta: Good afternoon Sir. Just wanted to check if you could talk about the SSG for ETHOS during the quarter?

Yashovardhan Saboo: Yes. So SSG during the quarter, if I am not mistaken, SSG stood at about 7.7% which in the previous year was actually -5% so we have seen an uptick in the same store growth during Q3. You will remember actually that in first two quarters same store growth was actually negative and I am not sure Shalini if you were on earlier earnings calls but this was significantly due to the sharp reduction in supply of some key brands such as Rolex and as I mentioned as an answer to the last question from Priyanka, the Rolex supply situation has improved but not only that, I think we saw lot traction coming from the additional sales that the end of year sales that was launched in December, which was successful for us and December was a good month. Of course, it was at the cost of slightly higher discounting, but the same store growth did perk up. Does that answer your questions, Shalini?

Shalini Gupta: We should be seeing a substantial jump in ETHOS EBITDA next year given the new stores will start delivering more. Is that correct?

Yashovardhan Saboo: That is absolutely right. We expect to see a sharp jump in EBITDA due to full operations of these new stores and as I mentioned, they are already seeing a fabulous traction in most of these stores. I would not say all because in one or two stores we are looking at some challenges and we are addressing to them through a very focused marketing and digital marketing campaign but the main store such as Kolkata, Hyderabad even Chennai and the Chanakya in Delhi they are turning over a fabulous performance and traction.

Shalini Gupta: Sir if you could just give some kind of understanding as to how much the EBITDA margin on an adjusted basis we should see in ETHOS?

Yashovardhan Saboo: We had said two years ago that our target is that by 2021-2022 when we had outlined the plan, we should hit an EBITDA margin of 9% to 10%. I believe this current year is a bit of gap in that mainly because of the depressed consumer sentiment and coinciding with the new traction; however, we remain inline to hit this 9%-10% EBITDA margin for the year as a whole by 2021-2022 and to hit this we would probably be just somewhere between where we are today and this 9-10% in the next year that is FY2021 and hit the 9% and 10% by FY2022. That is our goal.

Shalini Gupta: Thank you and Sir just one last question on the borrowing do you see borrowings going up or what is outlook on borrowings?

Yashovardhan Saboo: We do not expect borrowings to go up significantly at all. Most of our stores are now generating cash, so if at all borrowings may go up by a few Crores. I do not expect any significant increase in borrowings. What is happening is and I am glad to report that I sort of did not mention that in my speech we are signing on some exclusive brands in some of the high-priced segments. One of the brands which is called Girard-Perregaux, GP it is one of the most well known and most historic brands in the high-priced segments. We have signed it on exclusive basis and other brands like this are also in the pipeline or have been signed, so we will need a perhaps a bit of extra borrowing to finance the rapid growth of this but as I mentioned I do not believe the borrowings will be significant and our internal generation is quite capable of taking care of the growth in the watch segment.

Shalini Gupta: Thank you Sir.

Moderator: Thank you. The next question is from the line of Vikram Suryavanshi from PhillipCapital. Please go ahead.

Vikram Suryavanshi: Sir just wanted to know about the Estima AG, what is the revenue in this quarter and nine months or it would be possible or was it consolidated in our consolidated KDDL revenue. I just wanted clarity on that front and how was the profitability for this quarter or nine months if you can share?

Yashovardhan Saboo: Vikram the revenues are included in the results. The revenue at Estima for the year is about 1.5 million Swiss Franc, it is significantly lower than what we had budgeted mainly as I had explained in the last time that we had to go in for a substantial renovation of the factory and much of this revenue actually started to come up after the renovation was over.

Vikram Suryavanshi: Yes and how was the profitability?

Yashovardhan Saboo: We have a loss of about 1.3 million Swiss Francs which include depreciation loss which in previous period was not being provided by Estima. In their previous years, Estima was not providing any depreciation which was apparently allowed under Swiss Law; however, now we have started to provide the full depreciation including some backlogs of the past.

Vikram Suryavanshi: By when we can see it turnaround, any plan for that?

Yashovardhan Saboo: Vikram I am very hopeful that in the second half of the next fiscal we would start to see a turnaround in terms of a profit and generally a cash break even in this year. We still need to make some more investments in Estima and the reason is the following. It is actually linked to what I said in my speech. Estima was mainly focussed on the mid priced segment in Switzerland which is a price segment between $500 and $3000 watches. As I mentioned, this segment is actually declining steadily whereas the growth is happening in the segment above $3000. Our strategy has been actually to focus on the segment above $3000 and Estima is going to help us to focus there, but this requires a significant increase and improvement in the quality and offering of the product from Estima, part of the investments was done last year and some investments are planned in this year which are already in process and I expect that in the second half of the next fiscal we will start to see a sharp turnaround in Estima. I can say this because we have extremely interesting leads from customers which we have no chance to get in India. I am talking about brands in the price segment of and I am not mentioning these as specific brands only as price segments but in the price segments of Omega, Cartier and similar brands, which will never buy from India, they will never buy from Asia and we have a very enthusiastic response from them to buy from Estima, so we are hopeful that within the next six months or so we will start to see a very handful turnaround.

Vikram Suryavanshi: Second Sir this is Precision Engineering how was the revenue for this quarter or nine month and how is the outlook given the challenge in economy?

Yashovardhan Saboo: Sanjeev has the figures. I will let Sanjeev answer this one and I will get back to you on how we see the prospect for this business.

Sanjeev Masown: Vikram**,** during the current year, the revenue for nine months has grown by almost 12%-13% as compared to same period of last year. During last year nine months. the revenue was around Rs. 30 Crores where as during the current year we have reported revenue of around Rs. 34 Crores. Quarter on quarter there is a growth of 17% but from previous quarter there is a decline of about 12%.

Vikram Suryavanshi: How are you seeing this export? Are there any interesting export orders and how is that outlook?

Sanjeev Masown: Regarding Export order position, basically our focus is on the aerospace segments where it takes longer time for the product approvals, but once product approvals come then there is some kind of lock-in and it continues for very long period, so during the current year we have been successful in making inroads and door opening with some of the big accounts which we are hopeful that from the coming years, it will help in major growth of revenue..

Yashovardhan Saboo: Vikram you asked a question about future prospects, we have been reviewing this business very closely, because frankly it has not grown as we had expected it to over the last 12 months. Part of it is of course due to the slowdown in the economy, the electrical and electronics segments as well as the order component segments, these two segments we all know have slowed down and as a result the demand or interest in new products offered by us or new products required that is slow and also existing orders are being postponed so that is one of the impacts but that is not the only thing. We need to reassess which are the most profitable segments, some of the growth that has happened over the last 3-4 quarters has actually been in low contribution segment and we are addressing that very actively. We are now focussing on three or four segments that actually bring us high contribution and of course one of them is the aerospace segment. It has a longer lead time, but we are stepping up our efforts to actually focus very intensively on this besides of course continuing with the auto components and the electrical and electrical segment. We expect that in the next fiscal even in the first half, we will see a growth in the topline but more importantly there will be an improvement in the EBITDA and the profitability. From the second half of next fiscal, I think the real growth in topline will also kick in based on some of the new leads and customers that we are getting, so it is still going to be steady growth, there is not going to be a very sharp growth expected in the next 3-6 months but from September of this year, we should start to see a growth not only in the bottomline but also in the topline

Vikram Suryavanshi: Do you have any meaningful exposure to auto segment from this division?

Yashovardhan Saboo: The auto segment. Yes, we do. That has been obviously slow. We are supplying a lot to the auto electricals. The electrical business of the automobile industry, the connectors and so on, so that has been a significant part and obviously there has been a marked slowdown over there. We are not seeing a very specific turnaround there. There seems to be a turnaround in the electronics and electrical segment, slow turnaround and the aerospace segment again I do not think the Make in India part is taking off soon, but there we are focussing much more on direct exports.

Vikram Suryavanshi: Last question Sir about this watch component. If you can give comment in terms of quarter or nine months revenue and how is the outlook for hands and dial?

Yashovardhan Saboo: On the hands and dials as i mentioned, a lot of hands and dials business in the past has been focussed on brands in the segment below the $3000. We have gained market share significantly in this segment, but the fact is that this segment is declining. I mentioned we have gained market share in the Indian producers which have grown, so Titan has grown, Timex has grown, Fossil Group has grown and we have gained market share in that but the profitability and margins in the supply to the Indian segment are lower than export to Switzerland and therefore that is one reason why even though topline has grown, so margins have declined a bit that is because of the change in the product mix. Going forward our strategy is to reduce our dependence in the price points below $3000 and increase our business price points of watches above $3000. This is already happening as I am speaking and the inclusion of Estima is further actually enabling us to go more into this segment. We believe that both the watch component business dials and hands, they will continue to see a growth in the topline and the profitability which has declined slightly in the last quarter will be revived. I do want to add that we are anticipating an impact of this Coronavirus. In the short run it may hurt because a lot of brands depend on Chinese vendors for some components, they also depend on sales in China into Chinese people so if the sales falls or the component supply, their supply chain is disturbed the production and sale of Swiss Watches in this segment will fall, and we are starting to see some impact in terms of delays, postponement on delivery and so on. I believe this will last for a couple of months. We are all hopeful that in the next six to eight weeks, this Coronavirus spread will be halted. The long-term impact of this Coronavirus scare is going to be extremely beneficial for us. Let me explain how. For the last 3-4 years we have been hearing about brands wanting to derisk from China, they have too much exposure to sourcing in China and they want to spread their risks by starting to buy in other countries. We are standing by and waiting for this opportunity to come to us. Unfortunately, it has not happened fully, it has happened a bit but not fully, because brands hesitate to change from the supply chain that has already established in China. China logistics is better. They have their purchasing offices in China. They have to travel to China more frequently, because it is a larger market. India is seen as a little bit more complicated, logistics is not that easy, and shipments out of India take a little bit more time due to custom procedures and so on. So they have not really made the full effort to derisk from China. Now with the impact of this Coronavirus, I think at the top management levels in all the brands, we are hearing of this tremor, it is almost like a tsunami and they are saying that we cannot be so dependant on China that both our market and supply chain can be jeopardized at the same time, so we believe that whether it is Swiss brands, whether it is Japanese brands like Citizen, Seiko, Casio or whether it is American fashion brands like Timex and Fossil, all of which are active in India, they will look much more actively in sourcing out of India. We believe that the positive impact of this will start to be felt in the next fiscal year from Q2 onwards.

Vikram Suryavanshi: That was really helpful. Just for housekeeping if you can just tell how was the absolute number for this quarter and nine months from overall watch component excluding Precision Engineering?

Yashovardhan Saboo: The watch component in this year-to-date it has grown by 5% just the watch component business and in this quarter, it has declined by 5% compared to Q3 of last year. So in this quarter there is a decline of 5% and for the year as a whole there is an increase of 5%.

Vikram Suryavanshi: What was the absolute revenue in this quarter?

Yashovardhan Saboo: The absolute revenue in watch component in this quarter was about Rs. 30 Crores, Rs. 29.95 Crores.

Vikram Suryavanshi: That was helpful. Thank you very much Sir and all the best.

Moderator: Thank you. The next question is from the line of Govind Sabu from IndiaNivesh PMS. Please go ahead.

Govind Sabu: Good afternoon Sir. Sir just an update on the corporate holding structure of ETHOS. Any development on that front?

Yashovardhan Saboo: In what sense Govind. There has not been are you taking in terms of the demerger?

Govind Sabu: Yes demerger, merger there are lot of options which are being talked about in the past?

Yashovardhan Saboo: There is not much of a change from a previous quarter. We have looked at all the options; have been presented to us by the advisors that we have appointed for it. Obviously, the most preferred option is the direct demerger and direct listing of ETHOS. That cannot be achieved with SAIF partners remaining as a shareholder in KDDL because they will not be allowed to hold shares in ETHOS being a multibrand retail company. We are in discussion with Saif to find a solution either if they can shift the shareholding to a compliant body or they might be interested to take an exit, we are in discussion and we are waiting for them to come back with options. The other options which we have presented which was to list through another holding company to separate from the manufacturing company but to create a holding company for retail and to list under that is not seen a very beneficial because in the end it will not achieve what we want to. The value discovery will not happen if what you do is just list with another holding company, so basically, we are in discussion with Saif Partners and we are hopeful that in the next quarter we will have a clear line of action on how to go about it. We are very aware that this demerger and value discovery for shareholder is extremely important. It is also important for the business because we have a vision to grow this business not only in the watch business as I mentioned our goal was to grow to a number of a Rs. 1000 Crores in topline but actually also pursue opportunities outside the watch business and we believe that the value discovery and the recognition of the potential of our business is extremely important and the direct listing of the company is important for that.

Govind Sabu: Great Sir. Great for an update, just a small question regarding the capital plan for ETHOS, so I believe that since most of the expansion is now done with and the future expansion as you told over the call earlier it is limited to 3-4 stores in the next year, is it fair to assume that there will be no more dilution in ETHOS or there will no more capital raise in ETHOS?

Yashovardhan Saboo: Yes, we have no intention of diluting for starting new stores for any of this.

Govind Sabu: Thank you Sir. That was helpful.

Moderator: Thank you. The next question is from the line of Arush Sheth from VDV Securities. Please go ahead.

Arush Sheth: I have set of question, so the first one is that the other expense has been rising sharply, when do you expect this store throughput to increase? So first one was this one and the second one is I would like to know the gross debt figures for KDDL standalone and ETHOS business as on December 31, 2019 The third one is that how has been the traction of after sales service segment and the second hand watch business?

Yashovardhan Saboo: Let me start by answering the last one first which actually is an extremely exiting story. There has been a lot of effort which has gone into the after sales service and connected to that the preowned business. On the February 1, 2020 we launched an independent website for the preowned business. It is called Second Time Zone and I would invite you to go and visit it. It is Second Time Zone powered by ETHOS. We are seeing a great traction in the preowned watch business and this was only possible because of the support of the service center. I am just going get back to you on the service and pre-owned business. In terms of your question on gross debt Sanjeev will give that you.

Sanjeev Masown: In the KDDL our debt is Rs. 50 Crores, this is including the deposits which we take from the members and in addition to that the working capital borrowing is around Rs. 20 Crores. This is actual figures on December end and for the ETHOS the gross debt which is mainly the working capital is around Rs. 72 Crores.

Yashovardhan Saboo: The first question, so other expenses yes, it is true other expenses have gone up. This is due to three main reasons, the first of course is the rent and running expenses of the fixed flagship stores and the revenue from these stores are still building up so this is the first impact. Second is a lot of the growth in the existing stores has happened in the duty free stores, Delhi and a bit in Bengaluru and these are stores with a quite a heavy revenue share so obviously it has led to a good profit but overall expenses of rent go up quite substantially because of the growth in the duty free stores and third the entire vertical of preowned watches and service center in fact we having to expand our service center to cater to the needs of the preowned segment there also expenses have gone up and the revenue are to still to come through, you asked a question as to when the revenues will start to kick in, you will start to see the margins being impacted very positively already from this quarter and revenues to start kicking in from the next quarter. Why is there a difference? Let me explain in this quarter we have taken a position of actually focusing on gross margins by a very strong control on overall discounts. You will notice that in Q3 last year although the topline went up a lot, but the margin did not go up because the overall consumer discount went up due to the sales that we had done. We are now tracking down on that and we are bringing discounts down which is also supported heavily by the brands, they want to see lower discounts and this is already happening, so we will actually see a jump in the gross margin during this quarter and a sharp rise in the topline starting from next quarter as the sales of the new stores start to pickup. On the after sales service, I am not able to get the figures readily. Shekar is not here unfortunately, but if you do not mind I will get back to you by tomorrow or someone will get back to you on the figures of after sales service and preowned watches.

Arush Sheth: No problems Sir. Thank you so much and all the best for the future.

Moderator: Thank you. The next question is from the line of Lala Ram Singh from Vibrant Securities. Please go ahead.

Lala Ram Singh: Sir first question is on ETHOS we have not seen proportionate increase in the employee expense, it is Rs. 8.1 Crores in this quarter and in the previous quarter it was Rs. 8.7 Crores so it has actually gone down, so may I understand what is happening there? Second question in the light of current macroenvironment I was surprised to see such a strong growth, so may I know at what rate would the industry would have grown in this quarter to get a sense of how much market share we have gained? Third question I wanted to understand in the preowned watch business how does the mechanics work in the sense that the customers would be scattered across the country so do we have to ship their watches to the service center or we collect from their home or whichever location they want to and then we ship them in the center and then we give a code so to understand the exact mechanics or is that we also put those watches on sale in stores across pan India level, how does that stocking of those watches happen if you explain the process that will be helpful?

Yashovardhan Saboo: Regarding employee expenses, there are two reasons for that. One is of course we have been very cognizant on employee expenses having gone up and so there has been a control on that. Second there were some provisions made in Q2 for variable pay based on overall profit and since the overall performance for the year is now likely to be less than the budget that is we are provided with so there has been a reversal of that, so these are two reasons for variable pay and the provisions for variable pay and overall a reduction as well. So that is one. Second on the market share, so what is interesting is that for the year, the Swiss Watch export to India has reduced, it is a decline of about 2.5% if I am not mistaken It is about 2.5% whereas ETHOS overall YTD growth is about 8% higher. So 8% higher growth in ETHOS versus a 2.5% reduction in Swiss Watch exports and we are basically concerned with Swiss Watches and we are not really talking about watches of fashion brands which are not Swiss that is anywhere a small portion of what we are dealing so overall we have gained market share, now we can work back and see what is gain in market share but the fact that we have grown 8% while the overall market seems to have declined a bit marginally by 1-2% or 3% shows that we have gained traction. Now I am coming to the point about the preowned watches and let me explain how it works. So first of all right now obviously the main attention is in Delhi where we have the service center and Mumbai. Delhi and Mumbai are the two main areas where we find people interested in selling their watches. These watches first of all the discussion happens over phone, with our preowned watch consultants. We have got three senior consultants. If the watch appears to be interesting and genuine then the collection is arranged through our local supports which ever is closest to the customers and brought to the service center. The service center examines them to check a) whether they are genuine, b) whether they have the requisite documentation, and c) whether as to their saleability and that is when so if everything looks okay, then we take it on and put on the website. As of now we are not planning to sell or display any of these watches at any of our existing stores. They are mainly featured only on the website and the sale will happen through the website. Delivery could be organized through our existing stores, but as of now there is no plan to display these preowned watches at any of the stores. There is a potential conflict that might arise by displaying these watches at the current stores, so for the moment we are not planning to do that. There is a plan perhaps to create a dedicated physical store in Delhi and eventually in Mumbai for preowned watches which will not be connected to the stores for the new watches.

Lala Ram Singh: Understood and these will be branded as Second Time Zone or we have not thought about that aspect?

Yashovardhan Saboo: Well the website is Second Time Zone powered by ETHOS and that is somehow in line with trends across the board where in the preowned watch segment and in fact preowned other luxury products as well there are other websites that have been purchased by large brands, so I think the distinction between the identity for new products and for preowned products is in line with global trends also.

Lala Ram Singh: Got it. One more question, was around in terms of the sales for ETHOS what percentage would be based on EMIs?

Yashovardhan Saboo: I will have to get back to you on that Lala Ram, but I have to tell you that it is not very significant. We have been wanting to focus a bit on this, but right now even with the problems with NBFCs and the imperative has really been to grow the ultra luxury segment with flagship store so I think that has taken a bit of a backseat but we do believe that it is an important direction in the future and the revival of the NBFC I think will also help for that.

Lala Ram Singh: But is it a common phenomenon globally wherein people use finance borrowings to buy watches.

Yashovardhan Saboo: It depends, it varies. For example, in the US it is reasonably common, outside the US it is not very popular.

Lala Ram Singh: With the current footprint which is around 72 thousand square feet, if I am not wrong what is the kind of sales which we think we should do to justify this current retail footprint?

Yashovardhan Saboo: I believe that there is not going to be a great increase in the store count in the future. If I consider Rs. 1000 Crores as a kind of benchmark that we have sort of aimed at and I believe it is possible to reach this figure over the next I would say 2-3 years I do not believe that we need to increase the store count from the current level of 55 store maybe it will go to about 60-62, but earlier we used to talk about 80 and 85 stores, I do not think that it is necessary. What will happen is that some smaller stores will close down and we will rather go towards larger stores but fewer stores, so in terms of square footage, I think it will go up probably by another 10,000 square feet or so we know that in Mumbai there is going to be a large flagship store coming up maybe in Delhi there is going to be another flagship store other than that there will be a few smaller stores, but I do not expect that the square footage is going to go up by more than 10%-12%-15% over the next 3-4 years or let us say 2-3 years, whereas I believe that we should be able to step up billings to between Rs. 900-Rs. 1,000 Crores within this period.

Lala Ram Singh: Effectively you are saying that around 80,000 square feet would be enough to support the billings of 900-1,000 Crores?

Yashovardhan Saboo: Correct.

Lala Ram Singh: So that implies that we will be increasing our revenue per square feet beyond 1 lakh which is the kind of peak which we have seen in the last 3-4 years, so we will be moving beyond that?

Yashovardhan Saboo: Definitely. This will be impacted not only because of better throughput but also because the average price point of what we are dealing is also starting to go up and we are seeing that stores in which we deal with higher price points, actually deliver a much greater throughout per square foot and also greater profitability.

Lala Ram Singh: May I know the average ticket size in this quarter?

Yashovardhan Saboo: Lala Ram, let me get back to you on the exact per unit billing.

Lala Ram Singh: No issues. There were a couple of numbers which I wanted to confirm, which I missed. The gross profit share for exclusive brands which you mentioned, can you please repeat that for me?

Yashovardhan Saboo: Exclusive brands contributed 22.1% for the topline and 32.8% was the gross margin for the quarter

Lala Ram Singh: Understood and for the Estima you had mentioned the losses were 1.3 million CHF is it?

Yashovardhan Saboo: Correct.

Lala Ram Singh: That was for 9 months period or for this quarter**?**

Yashovardhan Saboo: This is 12 month period.

Lala Ram Singh: 12 month ending December.

Yashovardhan Saboo: Ending December correct.

Lala Ram Singh: One final question is in light of the slowdown in the entire economy and consumption and in other sectors, are we seeing any good prices for rental locking to lock prices for our new stores?

Yashovardhan Saboo: The three new stores that we are going to do those who are negotiated and agreed already 12-15 months ago. We are not really signing up any new stores for the moment. I am not really very sure whether we are going to able to do that. If there are things coming up, I think what is going to happen is that there are some stores which are coming up for renewal of lease typically at the renewal of lease there is a 20%-25% increase that happen,we are probably going to able to negotiate that down a bit. The thing is that for top locations there is always availability of brands who wanted to take up the top location.

Lala Ram Singh: Yes so, they are unaffected by the general macro.

Yashovardhan Saboo: B class location we are not even interested to renew them, so we are actually walking out of some of them.

Lala Ram Singh: The five stores, which you plan to close how much would they contribute in terms of revenues around Rs. 10 Crores around that figure or less significantly more than that?

Yashovardhan Saboo: I think it would be around Rs. 10 Crores maybe a little bit more. So these are typically stores that are not yielding profit, they are not throwing out cash and they do not really have much impact, they do not have much of strategic impact either. If they are locking a lot of cash or lot of working capital which we can be better utilized, in terms of stocks, in other stores and also, they are not providing any sort of great strategic value, then we are planning to close them.

Lala Ram Singh: In the larger stores how is the inventory turnover which you feel is possible because you had mentioned that the rental and other expenses as a percentage of sales would definitely be lower because of higher throughput but the inventory days do you see that there is significantly better on a steady state basis?

Yashovardhan Saboo: What happens is that initially the stock turn at these stores is little bit low and the reason is the part of the whole flagship offering is that not only it is a large store with a lot of brands but it also offers a large variety within each brand that is why it becomes destination for shoppers. But what happens is that overtime, these stores continue to grow strongly whereas smaller stores starts to pitter off. A good case in point was the first 12, 13 years of our store in Chandigarh the first store that we had opened which we have now closed down, because it was replaced by the new store at Elante Mall but this store being a 2500 square feet store, much larger than normal stores for its time for 12-13 years, it continue to show same store growth of 10%-12%. So in the later period these flagship stores actually become destinations and they turn out a lot more profit without an increase in turnover so the operating leverage really kicks in. So in the initial period stock turn is low, but overtime it improves and overall throughput is much better.

Lala Ram Singh: That is very helpful. Thanks a lot Sir and all the best.

Moderator: Thank you. Ladies and gentlemen that was the last question, I now hand the conference over to management for the closing comments.

Yashovardhan Saboo: With this we come to an end of today's conference call and I wish to thank all participants for being here with us and sharing you comments and questions. Thank you very much.

Moderator: Thank you. Ladies and gentlemen, on behalf of KDDL Limited that concludes this conference. Thank you for joining us and you may now disconnect your lines.