"Khadim India Limited Q4 FY2018 Earnings Conference Call"

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ANALYST: **MR. HARIT KAPOOR - IDFC SECURITIES**

MANAGEMENT: **MS. ISHANI RAY – CHIEF EXECUTIVE OFFICER – KHADIM INDIA LIMITED**
MR. INDRAJIT CHAUDHURI – CHIEF FINANCIAL OFFICER – KHADIM INDIA LIMITED

Moderator: Ladies and gentlemen good day and welcome to the Khadim India Limited Q4 FY2018 Earnings Conference Call hosted by IDFC Securities. 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. Harit Kapoor from IDFC Securities. Thank you and over to you Sir!

Harit Kapoor: Thank you Stanford. On behalf of IDFC Securities we would like to welcome the management of Khadim India as well as all the participants on the call. From the Khadim India Management we have Ishani Ray, CEO and Indrajit Chaudhuri, CFO representing the company. I would like to now hand over to the management for the opening remarks following which we will take it for Q&A. Over to you!

Ishani Ray: Good evening everyone, this is Ishani here. On behalf of the Board of Directors and the Management of the Company we extend a very warm welcome to all of you to discuss the Q4 and full year FY2018 Earning Call of Khadim India Limited. We have completed more than six months being a listed entity and we are enjoying every bit of interaction we are having with the capital market participants. I would like to give a small brief about the Company before we touch upon the quarterly results.

Khadim India Limited is one of the leading footwear brands in India with an existence of more than three decades. We are the second largest footwear retailer in India in terms of number of retail stores with the largest presence in East India and one of the top three players in South India. We also have the largest footwear retail franchisee network in India signifying the strength of Khadim's brand. Khadim's brand is positioned as an affordable fashion brand for the entire family for every occasion. We have adopted a two-prong market strategy of retail and distribution businesses each with its own customer base, sales channels and product range. Our retail business operates through 753 exclusive retail stores and our distribution business operates through a nationwide network of 445 distributors. We are also engaged in the business of institutional sales and export of footwear.

Today we are present across India in 23 states and one union territory. We have adopted an asset-light model for our growth and scalability. Around 76% of our retail stores are operated on franchisee model leading to faster expansion with low capital requirement. Our retail business is backed by outsourced manufacturing and more than 89% of our product requirement is made from outsourced vendors. For our distribution business we rely on in-house manufacturing capacity and contract manufacturing. Faster growth through franchisee model and optimized manufacturing process helps us to drive positive operating leverage and improve profitability.

Now let me take you through financial performance for the quarter. Q4 FY2018 net revenues increased by 31% from Rs.1498 million to Rs.1963 million. Retail business grew by 19% while distribution business has grown by 44%. In addition to our usual sales there was an institutional sale of Rs.296 million to UP Government in Q3 FY2018, which was not there in Q3 FY2017. We have also received institutional order of Rs.219 million this quarter compared to Rs.75 million during the previous quarter. Gross margin has reduced to 33.7% from 35.9% in the corresponding period previous year as we had higher institutional sales during the quarter. Despite lower margin it helps us to boost cash generation and return ratio hence we were opportunistic and have undertaken this institutional order.

Q4 FY2018 EBITDA increased by 20.2% from Rs.148 million to Rs.178 million in line with the higher revenue. Other expenses increased primarily due to higher rent expense on account of new stores, new office space and periodic increase at existing stores, higher advertising and sales promotion expenses, higher freight charges and transport cost and increase in job worker charges.

EBITDA margins were lower as we were front loading the expense while venturing into newer market and expanding store and distribution network. So in a sense we are setting expense to achieve growth in coming years. Interest cost during the quarter were lower by 42% as we have reduced our debt level. The total debt stands at Rs.685 million as on March 31, 2018 with a debt equity ratio of 0.3x. PAT has been flat on year-on-year comparison due to reversal of tax provision of Q4 FY2017. Our PBT for the quarter has increased by 49% over Q4 FY2017.

With that I would now like to open the call for question and answer session. I would be happy to listen to any feedback or suggestions that you may have. Thank you.

Moderator: Thank you very much. Ladies and gentlemen we will now begin the question and answer session. The first question is from the line of Ravi Naredi from Naredi Investments. Please go ahead.

Ravi Naredi: You told your model is asset-light model when Company invested 25 Crores in stock this year and 53 Crores in debtors total 78 Crores while our cash profit was 39 Crores only so what is the reason to be heavily invested in stock and debtors?

Ishani Ray: When we are talking about asset-light model we are talking of capital expenditure. Asset light in the terms of we are opening new stores and our expansion is more through our franchisee model, which does not require capital expenditure. When we are talking about asset-light we are pocketing the effect of capex. If we are talking about investment in stock and debtors we being a retail company, investment of the stock obviously would be there, but we have a stock days of about 60 days.

Indrajit Chaudhary: The overall working capital days has come down from 67 days to 57 days, which as per the retail business if we see is more than sufficient.

Ishani Ray: In a retail business the two component of our retail business being stock and debtors so we are having net working capital days of 57 days.

Ravi Naredi: So you mean to say your days has come down by 10 days?

Indrajit Chaudhuri: Yes.

Ravi Naredi: What is the reason so much heavy debtors in this quarter any specific reason?

Ishani Ray: One of the reason is that as I have mentioned we have undertaken institutional sales and the debtor days for institutional sales because these are government tender based orders, are slightly longer.

Ravi Naredi: So usually in government tenders in how many months we receive the payment?

Indrajit Chaudhuri: Within six months.

Ravi Naredi: Six months?

Indrajit Chaudhuri: Yes.

Ravi Naredi: Thank you.

Moderator: Thank you. The next question is from the line of Ankush Mahajan from JM Financial. Please go ahead.

Ankush Mahajan: So madam if I divide this business basically in two parts retail and distribution, so I am taking year-on-year the growth in the retail business is 12%, similar way the distribution growth is 38%. so I see on retail business side we have opened 80 new stores, I am trying to understand what is the SSG growth in the retail business and what are our target to open new stores in this year and how do you see the growth basically in both the business, Can you give me some breakup for SSG growth and throw some light on that?

Indrajit Chaudhuri: The retail business if you see we have grown by 12% if you see that there are two components in retail business one is CO and one is the franchisee, so the CO has grown at a rate of 14% and the franchisee has grown at a rate of 11% combining the total growth is 12%, but this year if we compare the net sales with the gross sales, because of the GST the net sales previously the effective tax rate was around 7% and now the effective tax rate is 10%. So if you compare gross sales we are grown at 15%, but in the next year it is coming down to 12%. We continue to open this year also 75 stores out of that 20 would be COCO and balance would be franchisee. Our growth rate in the retail business would be in the line of 14% to 15%, which is as far as our industry growth and in distribution we have grown at 37%, but we intend to grow for the next two years at a rate of 28% to 30%.

Ankush Mahajan: What is the SSG growth in the retail business?

Indrajit Chaudhuri: SSG growth in our own stores is around 7% and balance comes from the newly opened.

Ankush Mahajan: In COCO 7% growth?

Ishani Ray: 7%.

Ankush Mahajan: And in franchisee basically?

Indrajit Chaudhuri: Basically franchisee also growth is at the same rate maybe 6% their secondary sales.

Ankush Mahajan: So how do we see this SSG growth for this year 2019?

Ishani Ray: SSG growth we expect to continue at a similar rate of around 6%- 7% that is what we have seen over the years, so going forward we expect the SSG growth to continue at the level of 6% -7% and the balance would come from the new stores.

Ankush Mahajan: So madam this SSG growth is basically we are taking a market share from others, you are seeing some shifting from unorganized to organized what are the reasons that we see in this SSG growth basically?

Indrajit Chaudhuri: SSG growth comes from two factors one is the volume and ASP growth. We see there is a volume growth of around 2% and there is ASP growth of 5%, it is a combination of both from unbranded to branded and also taking share of some competitors.

Ishani Ray: Another thing also what we have seen that in our product portfolio we have some premium sub-brands and we have the Mother Brand Khadim so there is also shift from the mother brand Khadim to the premium sub-brands, so that is also leading to an ASP growth.

Ankush Mahajan: So can I say madam this FY2018 the ASP growth is also 5%?

Indrajit Chaudhuri: FY2018 ASP growth on a new product it is more than 5%, but also we offer discounts so net is that the ASP growth would be around 3% to 4%.

Ankush Mahajan: But that is not reflected in the gross margins actually. because the gross margins are same year-on-year basis on retail side.

Ishani Ray: The proportion of discount sales, offering products on discount is not so much involved with your liquidating your stock, but more to attract footfalls. What we have seen over the period of discount sales and the proportion of discount sales was higher than that of the year before, so that is why you see the reflection is not there in the gross margin, but if we bought up the discounts the gross margin is much higher.

Ankush Mahajan: Agreed and madam second part is from the distribution business side now we are saying that we will grow at 28% of growth in the distribution business what are the reasons behind it, how do we get this?

Ishani Ray: We have given guidance that distribution business we would be growing anywhere between 28% to 30% and actually that was more on a conservative basis we have actually outperformed our guidance in a way. Reason being distribution we are concentrating on the eastern part of the country and whereas in east we are number one player in retail and distribution and still have a long way to go we are the fourth or fifth player, so as it is in the East there is plenty of opportunity to take the market share and over and above that , in rest of the country we have got the full basket of products, we have also introduced a new products like sports shoe and flipflop in our distribution ticket, so we are quite optimistic and aggressive on the distribution growth.

Ankush Mahajan: Any target to increase the distributors this year madam FY2019 incremental?

Ishani Ray: On an average we do add around 40 to 50 distributors.

Indrajit Chaudhuri: This year FY2018 we have added around 80 distributors.

Ishani Ray: Yes so, on an average we do add around 40 to 50 distributors so we will keep on with that for three years and it can be even more also depending on which regions we set out foot on.

Ankush Mahajan: And madam are we seeing ASP increases in the distribution businesses?

Ishani Ray: ASP in distribution business is relatively flat because it is a very price sensitive segment and the distribution business we can only increase if we introduce higher price product. So this year we are introducing products like sports shoe and phylon, so there can be a marginal improvement in these products. Typically it is a volume driven mark-to-market business we have to flow on volumes over there.

Ankush Mahajan: Last one from my side is our advertising expenses & the marketing strategy that we will follow now?

Ishani Ray: See on the market strategy till now we do not have any big plans on hiring brand ambassadors and things like that we would rather do a focused sort of marketing. We have done few tie-ups like we had a tie-up with KKR, we have done a tie-up with CSK because we are strong in southern region, so we try to get maximum mileage that we can get out of these two tie-ups, barring that we would do region based specific marketing activity through our outdoors and printers.

Ankush Mahajan: Thank you madam. That is it from my side.

Moderator: Thank you. The next question is from the line of Arpit Kapoor from IDFC Mutual Fund. Please go ahead.

Arpit Kapoor: Thanks madam and congrats for great set of numbers. Just continuing on the distribution side of the business. so we added almost 100 odd distributors last year so what would be the run rate going forward for the next two three years?

Ishani Ray: See usually we add anywhere between 50 to 60 so we would continue, some year it will be 40, some year will be 30, on an average we should be adding anywhere between 50, 60.

Arpit Kapoor: And on a consolidated basis is there any target that we are looking at that this as a percentage of sales distribution as part of your overall revenue should be 35, 40 and you limited that or it can go as high as 50%, 55%?

Ishani Ray: We do not have any intention to limit it because if the business is doing good and we see there is scope we would definitely allow the business to grow because retail business it is a different channel, we have dedicated two teams to take care of the business, we know that the retail business would be growing at anywhere between 14% to 15%. Distribution business on the next two three years we expect it to grow at anywhere between 28% to 30%, but after that it would mellow down. Today the growth that we are seeing of 35%, 38% that is because the base is small and as it starts expanding, definitely the growth rate would taper down. So in next two, three years yes the distribution and retail mix can change to a level of maybe 60%, 40%.

Arpit Kapoor: But then to that extent given the fact that we understand distribution business the EBITDA margins are slightly on the lower end as compared to the retail. which we saw in the current year number as well so on a full year basis our EBITDA margins actually declined by a 40, 50 BPS so what kind of EBITDA margin target do you have in mind for the next two years given if distribution business continues to grow higher than the retail business?

Ishani Ray: One thing is for sure that if a distribution business grows, we expect to improve the EBITDA margin in the distribution business because as I told in my opening remarks there are expenses, which are being incurred to create the infrastructure to cater to that entire distribution network and the business. There would be leveraging of the cost that we are incurring today so naturally we expect that the margin in distribution business itself would improve. We are also introducing products, which were not there in our product portfolio before in the distribution segment. The introduction of these products would help us to earn higher margin in the business. So the small dip that we have seen in the margin was not only due to distribution business but also because we had the institutional sales, which has pulled down the margin the general mix of the sales has changed, brought down the margin, but on overall basis we expect the margin to improve as I said before also by about 50 basis points on year-on-year basis.

Indrajit Chaudhuri: Because if you see that the retail business the proportion of retail business has come down to 66% and the growth of retail business is around 12% and the retail channel growth at 14% we are higher than what we have done.

Ishani Ray: We are higher than what we have done on the period last year.

Arpit Kapoor: And last one more question on the same so distribution everything we do is in-house manufactured if I am not wrong so what would be our current capacity utilization and given that if we are assuming 40 to 60 distribution to retail would there be any capex requirement 12 months, 18 months down the line?

Ishani Ray: See as we have said that in-house manufacturing and contract manufacturing so going forward we would be investing on machines and moulds because it scale up your capacity and beyond that we do not intent to invest in new factory immediately in the near one or two years, but yes to ramp up the product backing we would probably go and provide machineries and moulds to the contract manufacturers and they take their facilities on a tolling basis to ramp up the production process. We do not see we would be incurring capex for machineries and moulds, which would be around 25 to 28 Crores in a year.

Arpit Kapoor: Yes so that would can easily be addressed by whatever EBITDA or internal accruals?

Indrajit Chaudhuri: Yes.

Arpit Kapoor: And we should still be able to face some of this. so what would be the current debt that we would have in our books?

Indrajit Chaudhuri: As on March 31, 2018 we have a debt of around 68.4 Crores.

Arpit Kapoor: So given the fact that we would not be going to do a lot of capex in next year or in the next two years the debt level should go down to what extent?

Ishani Ray: Remain at the same level because if you see this entire 67 or 68 Crores of debt that is primarily our working capital debt, it will not have any term loan for capital expenditure. So working capital in our type of business we have cycle, there can be spike during the festive season and it will come down. The debt level on an year end would remain at a level of anywhere between 65 to 70 Crores not beyond.

Arpit Kapoor: So the interest cost that we paid for this quarter should be the one we should look in for modeling for the next year?

Indrajit Chaudhuri: No, the interest cost for the fourth quarter would not be the model because in this first and second quarter the working capital remains.

Ishani Ray: Utilization would be higher so whatever is the full interest cost for the year…

Indrajit Chaudhuri: Obviously that will come down.

Ishani Ray: That would come down there may be value of 4.5 that is what we should take when you extrapolating the numbers for our margin.

Arpit Kapoor: Thanks. I will come back if I have more questions.

Moderator: Thank you. The next question is from the line of Manasvi Shah from ICICI Prudential. Please go ahead.

Manasvi Shah: Thank you for taking my questions. Madam you mentioned that the discounting has gone up for the year can you please tell me what is the percentage of discounts to the overall sales?

Indrajit Chaudhuri: Last year it was around 15% of the overall sales, now this year it came to 21%.

Manasvi Shah: And going forward how do you see this moving?

Indrajit Chaudhuri: Because in FY2018 we have given discount for around six months so I think that will not increase it will reduce a bit.

Ishani Ray: At the most it can stay stagnant, but definitely it will not go up.

Manasvi Shah: And what is discount primarily because open stores in newer geographies and you wanted to like you mentioned get more footfall?

Ishani Ray: Yes it was one of the reasons of course was that because it is more like you offer something to the consumer and you then end to the store. Apart from that it is a general syndrome that happens in the retail segment that people are constantly consumers are looking for that discounting period when they do come to do their buy.

Manasvi Shah: And I missed your comment on the store openings that you are looking at for the next year can you please repeat that?

Ishani Ray: We would be opening around anywhere between 70- 75 stores of which around 20-22 stores would be your COCO and the rest would be your franchisee. Franchisee typically would open in areas where the brand has a reasonable visibility.It can be south, it can be parts of Gujarat where we have been operating for a reasonable number of years and newer geographies like Maharashtra or Mumbai or parts of Rajasthan we would try possibly COCO.

Manasvi Shah: Fair enough and in your opening remarks you mentioned that the reason for taking the government orders, which basically are looking at the cash flows and to improve the ROC can you just explain that point?

Ishani Ray: Yes so what is happening for taking these government orders - though the debtors days are higher and also the margin is lower, but for that we do not have any additional cost whatever is your gross margin contribution that clearly comes down to your EBITDA. so in a way it helps to improve our EBITDA on the absolute terms, which in result improve your ROC and also the cash flow.

Indrajit Chaudhuri: And the debtors that we carry in institutional business are also our creditors.

Ishani Ray: So on a net-net basis the net working capital for institutional business has been stable.

Manasvi Shah: So what sort of ROCE would you be making on institutional orders?

Indrajit Chaudhuri: Around 12% to 13% ROCE at present.

Manasvi Shah: Pretax?

Indrajit Chaudhuri: Yes pretax.

Manasvi Shah: That is still below the company average?

Ishani Ray: Yes it is below the company average, but this is something which it is more of like opportunity that comes.

Ishani Ray: We were at liberty of not entertaining this particular channel, but then we would have missed out on the absolute PROFIT contribution that is there.

Manasvi Shah: That is it from my side. Thank you.

Moderator: Thank you. The next question is from the line of Kunal Bhatia from Dalal & Broacha. Please go ahead.

Kunal Bhatia: Thank you for the opportunity. Some of my questions have been answered. I just missed out on the point in terms of your division of retail sales into COCO and franchisee just wanted to know the growth numbers in the same?

Indrajit Chaudhuri: COCO is around 14% and franchisee is around 11% overall is 12%, but this is on the net sales. This year we have undergone the implementation of GST so in GST what has happened is, the net output tax from the erstwhile rate has increased because the average rate was 7% so it is sale of MRP is 100 then the mid sales book is 93 but now the average rate has come down to 90, net sales is booked. So if we configure the gross sales to gross sales, our retail growth rate is around 14% to 15% while on the base of net sales it has come down to 12%.

Kunal Bhatia: This we are talking about the COCO part?

Indrajit Chaudhuri: It is COCO and franchisee, if you separate COCO , then COCO based on the net sales of 12% COCO has gone at 14% and franchisee has grown at 11%.

Kunal Bhatia: And sir in terms of the other expense you did explain there was some new opening of the store or wherein there was some filling of the pipeline so how much of the other expenses was impacted because of this element?

Indrajit Chaudhuri: Opening of new stores?

Kunal Bhatia: Yes mean there was some inventory, which was put into the new stores that impacted the other expenses, so you are explaining something that the other expenses went up this quarter?

Ishani Ray: No, other expenses goes up because other expenses comprise of rent, rent is a major component.

Indrajit Chaudhuri: See there was opening of 21 outlets where the rent increased by 14.71 million. There was a incremental expense full year rent there was increment from FY2017 of existing gain of 12.22 millions, then there was increase in corporate office of 10.45 million ,and on new ware house, which was part operating in FY2017, which we can fully operating it that expense increased by 10.54 million. The overall increase in rate is 60.63 millions considering new opening, existing enhancement, new corporate office and full year operation of the ware house. This is on the part of rent then there was an increase in advertising and sales promotion by 31.32 million then trade transport increased by 58.41 million, job work by 40.08 million, commission and discount by 14.96 million, and power and fuel by 18.84 million due to higher production and opening of 21 new outlets. These comprise of the total increase in other expenses.

Kunal Bhatia: Got it sir. Thank you so much.

Moderator: Thank you. The next question is from the line of Vismaya Agarwal from Axis Capital. Please go ahead.

Vismaya Agarwal: Thank you for the opportunity. My main question is regarding the distribution business. I understand the crude price is going up should have an impact and some input price pressure on this business and as you also mentioned earlier this given that we are more in the value segment there is limited price hike that we can take over that the product is a price sensitive so how do you sort of plan to pass that on or does that really impact our margins going ahead?

Indrajit Chaudhuri: We are see in some of the price sensitive markets, suppose there is increase in crude oil so the prices of the product will also increase depending on how much the competitor also increases.

Ishani Ray: See in distribution to take any pricing decision we have to keep a watch on the competitor, so long the competitors are absorbing the price we need to absorb the price also, but what we usually do we actually do a forward contract of our raw material so as to cover up the increase in the price fluctuation, but if there is a point where we feel that the forward contract is insufficient and we are unable to absorb the price anymore then we would pass on the price to the consumers. We see every competitor as they would be also having a capability of absorbing the price and beyond that they would pass on to the consumers.

Vismaya Agarwal: And one more thing so also you have mentioned you will be introducing some new products in the distribution segment so any sense that you could give us?

Ishani Ray: See we have been introducing new products like year before we only had PVC and RI . Then we introduced PU to some small extent. Now we have a full range of the PU product, which is very popular both in South and West and also there was a demand from the distribution channel of introducing sports shoe and phylon product so that is also something we have developed and we will push it across the channel. so these products again they have a capability of raising out gross margin.

Vismaya Agarwal: And the introduction would definitely help our ASP in this?

Ishani Ray: Yes absolutely.

Vismaya Agarwal: Thank you so much.

Moderator: Thank you. The next question is from the line of Rakesh Jain from Asit C Mehta. Please go ahead.

Rakesh Jain: Thanks all my questions have been answered. Thank you so much.

Moderator: Thank you. The next question is from the line of Rajesh Majumdar from Stewart & Mackertich. Please go ahead.

Rajesh Majumdar: Good afternoon Ishani madam, Indrajit sir and congratulations on a good set of numbers. I just had a couple of questions - one is that we have your overall numbers in terms of growth for COCO and franchisee, is it possible to break it down in to price and volume data as well in terms of what is the percentage growth in prices and the percentage growth in volumes for these two areas?

Ishani Ray: I can give you a gross sense of it if you need further details you are free to write to us we will give you all the details you can write to our ad partner we provide you with the details. Actually we have seen that on a same store basis we have an SSG growth of anywhere between 6% to 7% and of that 6% maybe 2% comes from your volume growth and other 4% to 5% comes from your value growth in retail business. that is what I can tell you, but if you want further detail breakup on an absolute basis that what is the incremental volume that we have done and the price maybe you can give me some time.

Rajesh Majumdar: This should be alright. My second question was more related to you have given us the data for the distributors and the retail stores region wise what is the percentage of sales that we still have in eastern region specifically for the FY2018 numbers?

Indrajit Chaudhuri: Retail around 65%.

Ishani Ray: 65%, 66% is sale from east and distribution I think is around 75%, 76% is from east.

Indrajit Chaudhuri: That can be found in the presentation.

Rajesh Majumdar: So basically what I was coming to is - you have mentioned earlier that you will not be going for any major increase in ad spend in terms of celebrities and that it will be an asset-light model going forward. My basic question is that from predominantly an eastern region company you have now plans to become an all India brand. So what is the thinking process behind that and where exactly do we see the company investing to reach that level say to become a player where eastern region will be less than 50% in three or four or five years?

Ishani Ray: See first of all we would not be doing something what we have achieved in east in one year we cannot go and achieve that in rest of the country, so as I said our growth the focus area is that we would be opening more stores in south and west so this dependence on east or the sales of 66% that we still have in east going forward it will come down to 50 and 40, whereas on the distribution side we still have lot of scope of growing in east itself, so distribution the growth happen will still continue the way it is.

Rajesh Majumdar: The 50% and 40% you mentioned for the retail sales, which are the years this will come down to 65% now?

Ishani Ray: I cannot exactly give you the year, but since 70 or 75 stores are opening in areas outside east so naturally there would be a down in the share that is what I am saying.

Rajesh Majumdar: The distribution will be around the same level in terms of this in the yield contribution?

Ishani Ray: I think it would be around the same level.

Indrajit Chaudhuri: The exact share of east in retail is 62.88%.

Rajesh Majumdar: And this you envisage to come down because you are increasing the number of stores in the south and west?

Ishani Ray: In the other parts of the country.

Rajesh Majumdar: Thank you.

Moderator: Thank you. The next question is from the line of Agastya Dave from CAO Capital. Please go ahead.

Agastya Dave: Thank you for the opportunity madam. I am not very familiar with your company so some very basic questions here. Can you describe the terms of trade that you have on either sides, what are your key deliverables and agreements with franchisees, is there agreement on volumes that X amount of volume will happen, what happens if sales is happened for a particular consignment. On the other side on the manufacturing side again how much volumes are committed, what happens with their returns, how do you settle all those effects and in terms of sharing of profits what are your agreements with the people who are doing the manufacturing for you and currently then settling returns on their investments if they undertake any capacity expansion do you probably part fund them or you have any other kind of agreements with them? second question is can you also describe the same management of the working capital side what are the arrangements there and primarily what is your average ASP and what is your average MRP?

Ishani Ray: So first to speak on the arrangements that we have with our franchisee partner. There is no question of sharing any profits with them because we sell our stocks to them. Our arrangement with the franchisee partner is that the entire capital expenditure for setting up the store is borne by him. The opex cost is borne by him. We sell our products to our franchisee by offering them a channel margin from MRP, so if my MRP is 100 I would give him a 35% discount and sell the product to him at 65 and within that the franchisee in turn would sell the product to the ultimate consumer at 100 MRP, so within Rs.35 he has to manage is entire operational cost.

Agastya Dave: These are exclusive arrangements?

Ishani Ray: These are exclusive franchisee they have to stock 100% of our product, the look and feel of the stores are similar to us, we give them this particular design layout of the store, we have a dedicated vendor who would actually go and build the store for them. We have agreement with the franchisee, usually the agreement is for five years with renewable clause and there are certain conditions that they have to follow - some certain do's and don'ts and we also have a typical debtor period with them depending on franchisee it varies anywhere between 45 to 60 days by which they have to if we are giving them credit then they have to pay that debt.

Indrajit Chaudhuri: The average ASP is 450 and the average MRP is 550.

Agastya Dave: And on the manufacturing side?

Moderator: Excuse me this is the operator Mr. Dave may we request you to come back in the queue for a follow up please?

Agastya Dave: Sir my questions were not answered completely they are not finished. Madam on the manufacturing side what are your arrangements?

Ishani Ray: Yes so on the manufacturing side we have a dedicated vendor base at about 100 to 110 vendors to whom we supply our designs and specifications based on which the manufacture and they sell the product to us, so there is an arrangement with them that if there is a manufacturing defect we will return the stock.

Agastya Dave: Thank you madam.

Moderator: Thank you. The next question is from the line of Kartik Mehta from IDFC Mutual Fund. Please go ahead.

Kartik Mehta: Just wanted to check one thing that if we were to remove the institutional revenue in FY2018 numbers what could have been the margin?

Indrajit Chaudhuri: Gross margin?

Kartik Mehta: Whatever EBITDA margin which was 10.1 on the reported basis if we were to remove the institutional business because this is one off business like next year whatever margin guidance you are giving of 50 BPS improvement, you are not assuming any of the institutional business coming to you right?

Ishani Ray: We have assumed institutional business coming to us.

Kartik Mehta: You have assumed that next year?

Ishani Ray: Yes we have some sort of an idea of what are the tender flows that expected to happen to maintain that we have set a figure for ourselves.

Kartik Mehta: So whatever 9% contribution of this business in the topline how it would move like going ahead?

Indrajit Chaudhuri: That will be the percentage of institutional business on the total sales would remain at same percentage because the sale will increase.

Ishani Ray: That percentage of institutional sales will continue to be around 8% to 9%.

Kartik Mehta: But it would grow so eventually you would be sitting on some order book right that is why you are giving this number?

Indrajit Chaudhuri: Yes.

Ishani Ray: More or less yes.

Kartik Mehta: So can you just spell out the number?

Indrajit Chaudhuri: Institutional sales?

Ishani Ray: I cannot spell out the order book number or what we have taken as a book please excuse me for that.

Kartik Mehta: So just coming back to the first point if you were to remove the instructional pie your margin would have gone up right, so have we done that back testing exercise that how much margin improvement it would have been?

Indrajit Chaudhuri: The margin would have remained what we have done in FY2017 because the gross margin for retail business and the distribution business are at the same level what we have done in the last year. because retail EBITDA is more or less same as the EBITDA margin so overall the margin have remained at what we have done 10.6%

Kartik Mehta: Thanks a lot.

Moderator: Thank you. The next question is from the line of Ravi Naredi from Naredi Investments. Please go ahead.

Ravi Naredi: Sir can you tell us what is the COCO store cost to the company?

Indrajit Chaudhuri: COCO store cost as a percentage of sale it is around 22% to 23%.

Ravi Naredi: the capital expenditure of company in COCO store?

Indrajit Chaudhuri: The capex is 25 lakhs and the working capital is around 15 to 20 lakhs.

Ravi Naredi: 35 to 40 lakhs we have to invest for one COCO store?

Indrajit Chaudhuri: Yes on an average.

Ravi Naredi: And second what is growth w are expecting current year and what margin is in your mind sir?

Indrajit Chaudhuri: In COCO?

Ravi Naredi: No in overall as a company.

Indrajit Chaudhuri: Overall we should increase our margin by 0.5% to 1% in the years to come.

Ishani Ray: We expect a topline growth of around 20% to 22%.

Ravi Naredi: Thank you very much.

Moderator: Thank you. The next question is from the line of Ankush Mahajan from JM Financial. Please go ahead.

Ankush Mahajan: Madam my question is just a followup to previous question we are saying the improvement of margin of 0.5% to 1% . how do you see margin improvement on the retail side that could be driven from increase in ASP?

Ishani Ray: Yes retail side margin improvement would come from increase in ASP, which would be a combination of your mix or shift from a mother brand to the sub-brand that is one and another margin improvement would also from is that we do not expect that so long discounting period this year we are taking NIM where we would cut down on the discounting period because in any case this year we have some incremental budget for our ad spend so effectively the discounting period would come down and that would help in getting the full value sales, which would automatically improve the margin.

Indrajit Chaudhuri: The discounted sale, which is around 21% of the total COCO sales we tend to cut down that to around 16% to 17%, which overall will improve our margin by 0.5% to 1%, if you see gross of discount our margin has grown from 55% to 57%, but if we take the discount factor then it has come down by 0.50 basis points.

Ishani Ray: And on the distribution side since we have introduced premium products like sports shoe and phylon so there is a small dip in margin that we have seen we expect to clock that and improve on the margins.

Ankush Mahajan: In the previous discussion madam you said that it could be flat ASP in distribution more over a volume growth?

Ishani Ray: Generally flat there can be small improvisation. What we have seen if you see the distribution margin is come down what I am saying is that this fall in the distribution margin we will clock and we will keep it at that level or might be small few BPS improvement.

Ankush Mahajan: So any operating leverage that can help to drive margin in distribution business?

Ishani Ray: Yes, that definitely but for that we have to wait for another year or so because this business is in a growing mode. today we are mostly in east if I pan out to south or west there might be requirement of setting up warehouses, but going forward yes the business is growing at 30%, 35% we will be saying operating leverage in next two years to come.

Ankush Mahajan: So madam if I am saying this proportion of sub-brands it is almost same that 52% in last two years so how do you see that proportion in upcoming year? these are the major portions that are driving our ASP?

Ishani Ray: So proportion of sub-brand has been improving we will see the improvement to be more one of the reason is the mother brand is primarily if we look at our entire franchisee component we have two formats, we call them the exclusive brand outlets, which is more for the tier one and tier two and we have the brand outlets that which is the Tier III. So all these years we were opening brand outlets in the Tier III also where the consumption is for your mother brand again. Now from last year onwards what we have decided we are not opening brand outlets in Tier III because we can go and opening Tier II only when the popularity of the brand is that much, demand if you have your outlets in the Tier III. Now since our focus is on the newer geographies we have to first cover the metros, mini metros and the Tier I and Tier II with the growth in the Tier III. that is brand outlets it would be restricted and as a result the consumption of product under the Khadim brand would be relatively lower than that of the sub-brands because the consumption of sub-brands is much more in the metro, mini metro and the Tier I. So going forward we would see a higher proportion of sub-brand sales as compared to your mother brand Khadim sales.

Ankush Mahajan: Madam last one- how do you see the competition basically from the organized players?

Ishani Ray: See if we are talking about competition yes distribution we do have competition, but one thing is that distribution market is also very large and we are much smaller than all our competitors so even if we take a small bit of share from them or if not from your organized competitors but if you take the share from the conversion that is happening from the unorganized to the organized and we have a great scope of growth. In retail the competition comes from Bata. Though Bata is way ahead of us, but again the price point that which we operate and our target consumer that is the huge Indian middle class I do not think there is any others who actually target the segment - organized retail chain. There can be localized competition on a region where they exist, but at a national basis organized retail there is no major competition. Bata which was actually operating in this segment also,is shifting towards the premium segment.

Ankush Mahajan: Shall I say madam in distribution business we are competing with Relaxo, Relaxo is also on the same business?

Ishani Ray: Yes Relaxo is on the same business there are two other south players that is Paragon and VKC they are also in the same business. We have a regional competition from a brand called Ajanta. You have the people like Aqualite from north so there is competition in distribution, but still saying the market is so huge and there is a constant conversion from unorganized to organized with GST coming in and now that it has stabilized we also expect that the unorganized player would really get rated out so there ramp up scope for all.

Ankush Mahajan: The Relaxo has a strong path?

Ishani Ray: Because we have to appreciate that Relaxo is a company, which focuses only on distribution. We are the only player who have both distribution and retail so we have to keep a very strict demarcation amount of product. whereas for Relaxo they do not have any bar in because they are not focused on the retail business so they can put any product into the distribution channel, but since we have an exclusive retail business we cannot offer the leather product which is a much high margin product or a high value product in our distribution channel because that would actually cannibalize my retail business.

Ankush Mahajan: Thank you madam. That is it from my side.

Moderator: Thank you. The next question is from the line of Jignesh Makwana from Asian Market Securities. Please go ahead.

Jignesh Makwana: This is on the gross marginal level madam we have been undertaking the judicious premiumization both our segment retail and distribution despite that our gross margin in these two channels are declined. is it the higher number of discounting the sole reason for this?

Ishani Ray: In retail discounting is a sole reason because that Indrajit just now said if we remove the discounting effect the gross margin, which was previously I think 65% that has gone up to 67% so as far as the distribution is concerned in the last quarter we have seen there was a sudden change in the distribution ordering pattern like there was a more requirement for the basic product and the premium product so that is the reason why in the last quarter there was a dip in the gross margin, but we have to wait and watch in this quarter to see whether that was the general trend, which continue or it was one off impact in the first quarter.

Jignesh Makwana: And as you mentioned we will have a less discounting sales in the coming years so can we expect gross margin in the retail business can see a material improvement in FY2019?

Ishani Ray: We do expect that because if I can restrict my discounting period season to whatever it was in FY2017 then I say we should see an improvement of around 0.75% to 1%.

Jignesh Makwana: Yes madam what I am saying we are planning to introduce more sports footwear in the distribution business, so can we expect so current ASP is around somewhere around Rs.90 in distribution business so can you tell what kind of number we are expecting in distribution?

Ishani Ray: Frankly speaking I will not be able to comment it immediately because we have just introduced it sports shoe and the phylon into the distribution business I would need a quarter to see how it picks up and in next quarter I can come back.

Indrajit Chaudhuri: As a percentage of total distribution it was very miniscule.

Ishani Ray: So we have to really see how it takes off and then come back on this.

Jignesh Pakwana: And lastly madam what kind of margin we are getting in institutional business?

Ishani Ray: Distribution business gross margin is around 13% to 15%.

Jignesh Pakwana: That is all from my side. Thank you.

Moderator: Thank you. The next question is from the line of Rohit Harlikar from HDFC Securities. Please go ahead.

Rohit Harlikar: Can you provide the breakup of revenue in terms of the current distribution sales for the quarter and for the year?

Ishani Ray: Breakup of retail and distribution sales.

Indrajit Chaudhuri: The retail sales is around 510 Crores.

Indrajit Chaudhuri: Distribution 185 Crores for the full year. for the quarter retail is 126 Crores, and distribution is 50 Crores.

Rohit Harlikar: Madam if I look at the debtor days it has gone up significantly from FY2017 to FY2018 from 46 to 75 days any reason about that?

Ishani Ray: Yes we have institutional debtors if we remove the institutional debtors that debtors it would be around 50 days.

Rohit Harlikar: So it is solely because of the institutional sales?

Indrajit Chaudhuri: We have done institutional business with our government.

Ishani Ray: That money is to come in and institutional debtors period is usually about six months.

Rohit Harlikar: And what was the institutional sales for the year?

Indrajit Chaudhuri: Around 62 Crores.

Rohit Harlikar: And madam can you provide the capex plan for FY2019?

Indrajit Chaudhuri: Capex would be around 25 to 28 Crores for FY2019 out of which 10 to 12 Crores is for the factory capex of machinery and moulds, 6 Crores for opening of new outlets, 6 Crores for refurbishing of the existing outlets and balance 3 to 4 Crores for general corporate purpose and warehouse.

Rohit Harlikar: And what was the capex utilization for the year?

Indrajit Chaudhuri: Overall around 75% whereas in Hawai sector it is around 85% and PVC around 64% to 65%.

Rohit Harlikar: Thank you. That is it from me.

Moderator: Thank you. Ladies and gentlemen due to lack of time that was the last question. I now hand the conference over the Mr. Harit Kapoor for closing comments.

Harit Kapoor: On behalf of IDFC I would like to thank the management and the participants on the call for their time. I would now like to hand over to the management for closing remarks.

Ishani Ray: Thank you for being with us and in any case if I have not been able to answer anyone’s questions you can please come back to our IR partner Dickenson Seagull and he would be happy to answer the unanswered questions. Thank you.

Moderator: Thank you very much sir. Ladies and gentlemen on behalf of IDFC Securities that concludes this conference. Thank you for joining us. You may now disconnect your lines.