S.P.APPARELS LTD.

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Sub: Transcript of the Conference call held on 12th November 2020	

Dear Sir/Madam,

With reference to our letter dated 09th November 2020, intimating you about the conference call with Analyst/ Investor to be held on 12th November 2020, please find attached the transcript of the aforesaid conference call.

This is for your information and record.

Thanking You.

Yours faithfully,

For S.P.Apparels Limited

K.Vinodhini
Company Secretary and Compliance Officer

Encl: As above

"S P Apparels Q2 FY21 Earnings Conference Call Hosted By Systematix Institutional Equities"

November 12, 2020

MANAGEMENT: **MR. P. SUNDARARAJAN – CHAIRMAN & MANAGING DIRECTOR**
MRS. S. LATHA – EXECUTIVE DIRECTOR
MR. S. CHENDURAN – DIRECTOR, OPERATIONS
MRS. PV JEEVA – CHIEF EXECUTIVE OFFICER
MR. V. BALAJI – CHIEF FINANCIAL OFFICER, S.P. APPARELS

MODERATOR: **MR. ANKIT M. GOR – SYSTEMATIX INSTITUTIONAL EQUITIES**

Moderator: Ladies and gentlemen, good day and welcome to the Q2 FY'21 Earnings Conference Call of S.P. Apparels hosted by Systematix Institutional Equities. 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 a touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Ankit Gor from Systematix Institutional Equities. Thank you and over to you, sir.

Ankit M Gor: Good evening everyone. On behalf of Systematix, I would like to welcome all to 2Q FY'21 and 1H FY'21 Earnings Call of S.P. Apparel. From the management side, we are joined by Mr. P. Sundararajan who is Chairman and Managing Director; Mrs. S. Latha, who is the Executive Director, Mr. S. Chenduran, who is Director of Operations and Mrs. PV Jeeva, Chief Executive Officer and also Mr. V. Balaji, Chief Financial Officer.

Without much ado, I would like to hand over the call to Mr. Sundararajan for the opening remarks. Thank you. And over to you, sir.

P. Sundararajan: Thank you, Ankit. Good afternoon, everyone. A very warm welcome to all of you who are present on the call to discuss our financial results for Q2 and H1 FY'21. At the outset, I hope all of you and your loved ones are healthy and safe. After subdued Q1 performance led by unprecedented coronavirus pandemic, the company is witnessing significant recovery in Q2 FY'21 in terms of an order book, workforce, and supply chain. Post the liftingof lockdown restriction, we swiftlygeared ourselves towards normalcy without facing any major disruption in the supply chain and workforce. As a result, we witness all-round performance across all our businesses during Q2 FY'21.

Let us talk about the "Garment Division." Discussing on our segment-wise performance, the garment division witnessed healthy traction in Q2 FY'21. As the shipments to customers increased once the lockdown was lifted there, our customers are witnessing recovery in demand, especially for the online retailing business. Moreover, they have also started consolidating their supply base further, and we continue to remain one of the preferred suppliers. We are also getting multiple enquiries across brands and retailers as they are looking to diverse their supply base beyond China to some extent. We are exploring possible business opportunities with these brands.

We have added one customer from the U.K. in Q1 FY'21, and already delivery started to reach the customer. And further one more from Europe in Q2 FY'21 and deliveries are expected to start from Q4 '21 onwards.

Our current order book stands at Rs.226 crores which gives good revenue visibility for H2 FY'21.

Our garment division revenue for the quarter stood at Rs.148 crores, an increase of 202% QoQ, a decline of 33% year-on-year.

As mentioned in the previous call, we have consolidated small rented factories with a bigger one in order to reduce the rent, workmen transportation cost and other operating overheads. This also contributed to our EBITDA margins for the garment division to improve to 20.8% for the quarter.

In addition, as we have mentioned in the last concall, we have efficiently worked on the consumption wastage control and control on personnel costs, which contributed to margin improvement.

We are confident that the EBITDA margins will sustain at this level going forward.

Our sewing machines installed capacity as of September 2020 stood at 5,100 machines. Our capacity utilization as of today stands at around 3,000 machines, and we expect the utilization to reach more than 4,000 levels by March '21.

As of today, all the factories are operating at around 70% capacity. We are still expecting more migrants to come post-Diwali.

While our order inflows, customer base, supply chain, installed capacity are very much intact, our only challenge was to increase the skilled labour to optimize utilization of capacity. Now, we have strategically planned to ensure a regular inflow of workmen for scaling up of our capacity.

With regard to the spinning, after the expansion project completed, the unit has started contributing reasonably to the margins of the Garment division.

Also, cotton prices have stabilized, and we expect the prices to be around this range.

"Processing Division." The biological treatment plant project is completed and is up and running. This has improved the efficiency of the plant, and now our capacity has increased by another three times per day. This is also contributing to the margins of the Garment division.

With regard to S.P. Apparels U.K. Limited, the revenue stood at Rs.25 crores for this quarter, and EBITDA margin stood at 8.7% compared to Rs.8.6 crores of revenue and (-2.6%) QoQ on EBITDA margins. S.P. U.K. witnessed good traction due to an increase of online business, especially of kids products. We believe that S.P. U.K. will maintain a similar trajectory, going forward. Our current order book for S.P. U.K. is at GBP 5.06 million.

Let us talk about "Retail Division." As the economic conditions gradually improved post the lifting of the lockdown, our retail segment saw a decent uptick in Q2 FY'21. Revenue for the Retail division stood at Rs.14.2 crores compared to Rs.2.2 crores in Q1 FY'21. We are expecting Retail division to do further better in Q3 due to festive season and the gradual pickup in the customers demand. We have taken serious efforts to cut costs by personnel and other overheads which will result in improving the margins in the Retail Division. The revenue of the Retail Division will be gradually growing quarter-on-quarter in a sustainable manner.

We have recalibrated well to the new reality by moving towards a leaner cost structure. We rationalize our employee cost and the other operating overheads. The cost reduction initiatives helped us to improve the adjusted EBITDA margins and saved around 2% to 3% overall across all divisions, which has offset the loss of MEIS incentive.

Our leverage and liquidity profile continues to remain comfortable. We have cleared all the interest and debt instalment obligation that were due during the H1 FY'21.

Our strategy, as we advance a robust, comprehensive business continuity plan, as a response to disruption due to COVID-19, is focused on customer engagement, continuous cost reduction, calibrated expansion plan, business strategy realignment, employee productivity and efficient utilization of IT-enabled systems. Hence, looking beyond the near-term challenges, we are excited with opportunities that the future holds.

S.P. Apparels as a company remains fully geared up both in terms of the technology and infrastructure to capitalize on the opportunities going ahead.

Now, I will request the CFO to give an overview of the Financials. Thank you.

V. Balaji: Thank you, sir. Good afternoon, everybody. I will run you through the quarter-wise performance of the company. This quarter we have made Rs.187 crores of revenue as against Rs.255 crores last year. It has decreased by 26.6% year-on-year. Our EBITDA stood at Rs.23 crores as against Rs.38 crores last year. Our PBT stood at Rs.23 crores for the current year as against Rs.23 crores of last year. Our PAT stood at Rs.18.78 crores as against Rs.34.89 crores of last year. Last year, we recognized DTL reversal because of the effective income tax rate changes.

For the first half, we have done a revenue of Rs. 247 crores and then EBITDA of Rs.40.39 crores with the PBT of Rs.17.33 crores and a PAT of Rs.12.96 crores.

For the current year, our gross debt is Rs.198 crores, and our net debt is at Rs.180 crores. Rest is available in the presentation which is uploaded in the exchanges.

Now, we will get into the question-and-answer session.

Moderator: Thank you very much. We will now begin the question-and-answer session. The first question is from the line of Manoj Dua, an individual investor. Please go ahead.

Manoj Dua: Can you throw some light on the new clients which we have added?

P. Sundararajan: Already we explained to you last time, one customer we added in the U.K. who does their in-house designing and supply of Disney characters, a licensed company, which already started shipping the goods. So they are in this business for the two generations and very strong, and they cater to most of the retailers in the U.K. So that is a very promising continuous business. And the second customer is in France. The shipments will start from say March, April 2021.

Manoj Dua: Last quarter because of the lockdown supply side was disrupted. So, how much per cent you can think the supply side has been normalized?

P. Sundararajan: Supply chain 70% to 80% is back on track we are, and there are some overseas imports and some of the special processes, special raw materials, a slight delay, otherwise we have recovered about 80%-plus.

Manoj Dua: What is the commentary of buyers for the future coming quarters?

P. Sundararajan: As I told you that they are consolidating the supply base and there are a lot of businesses from other countries, including China, are coming to us. So they are insisting us to increase the capacity to accommodate their orders. That is the current scenario.

Manoj Dua: How is our relationship increasing with the clients which we added last year because we might not have been communicating much more because of the supply-side problem, so how this new client which we added which have a good potential to increase, how is the relationship going on, what is the commentary from their side?

P. Sundararajan: One American customer started increasing the volume, they started sending more enquiries, and for the European customer, yes, we are going to get the new orders placed during the period of Q4, we will start getting the orders because we want to stabilize and then allow them to place more orders. So from Q4 onwards, we will be chasing them to place more orders.

Moderator: Thank you. Next question is from the line of Nirmal Shah from Seraphic Management. Please go ahead.

Nirmal Shah: I just wanted to check, yesterday there was an announcement about the PLI Scheme from the government for the man-made fibre and technical textiles. So since our entire product basket is made up of cotton, how do you plan to capture the benefit of the new scheme, can you throw some highlight?

P. Sundararajan: See we are the babies and kids product-based, so which are in a more of 100% cotton. And this PLI is something which is a very good thing for those 10 industries, where textiles and apparel are also one of the beneficiaries. But it is too early for us to explore anything at the moment, we are waiting for more clarity about the policies and the schemes, then probably will be able to give some inputs during the next concall.

Nirmal Shah: And sir, my second question was in Q4, considering that you already have an existing set of customers in addition to that, you have added a couple of more customers, how do you see the ramp-up, capacity utilization and the revenue and what will be the peak revenue you can achieve once the new customer starts contributing to the incremental order inflows?

P. Sundararajan: As we mentioned before that we have still more than a thousand machines to be fully utilized. So we will plan in such a way that there is good flexibility for maximum utilization of all the machines where we can accommodate these two new customers. And within the existing factories, we can add more machines also. And once we stabilize our workforce inflow, we will start working on those things.

Nirmal Shah: What I wanted to understand was that… correct me if I am wrong, you already have 5,000 sewing machines, and at one point of time, you are going to utilize those machines based on your existing customers, which were there prior to this year, right. Now, you have to accommodate new customers based on the same setup. So, does it mean that the product mix will go for a change, you will go for better margin orders and the existing customers you will probably fulfil the orders to a lesser extent, can you just throw some strategy how do you plan to this entire thing because you are not increasing the capacity, on the other side your customers are being added now.

V. Balaji: So, in terms of the capacity, I guess, today, we are at 70% utilization. So, there is still another 30% possibility for us to increase our capacity. The other thing is that if you recollect the chairman's speech, he says that we have strategized in terms of bringing in more workmen where that by my March-end, we are looking at 4,000 sewing machines utilization. Our bottleneck is on the utilization of the capacity. By March, I guess, once we reach 4,000, then we reassess ourselves going forward. So our aim is to reach 4,000 utilization level by March.

Nirmal Shah: And at 4,000 machines, what will be your revenue potential?

V. Balaji: We can easily reach 18 lakhs per machine, so it should be close to around 740-760.

P. Sundararajan: Per month will be about 60 to 65 crores.

Moderator: Thank you. The next question is from the line Sachin Shetty, an individual investor. Please go ahead.

Sachin Shetty: Just now in the earlier query, you cleared the China discussion. So, my question is how China distribution relationship to India? How is the China apparel market share in the USA? I mean, how much if the distribution happens and how much India will get?

P. Sundararajan: See, China's business, as I always mentioned, even 1% of the Chinese production is diverted to India, then India will be flooded with a lot of orders, that is the kind of the match. So, it is like this. Even anti-China sentiment will bring more orders into India, and the customers will insist that they want to increase their capacity to take more orders. So, this is definitely not going to affect China's production manufacturing thing, but India will be taking the advantage of a situation.

Sachin Shetty: So, last month, I read one article that Carter, one of the bigger USA retailers, I think S.P. is looking opportunities for the Carter's. So have you got an order from Carter's, or you are just…?

P. Sundararajan: Article was in Times of India where there was a question are you geared up for the Chinese fabric which is not the conventional fabrics of India, for which I answered, yes, Carter is one of the customers have asked us to develop these fabrics because they want to place more of such kind of products in India. So it is not that Carter is coming as a new customer; they are already our existing customer.

Sachin Shetty: Sir, now the second lockdown is announced in the U.K. So, how it will impact our business again?

V. Balaji: So far, I guess we have not received any feedback from the customers in terms of how effective the lockdown is going to be and what will be the impact on the retailers on the lockdown. But I think the lockdown is only for three weeks, and it should not impact much because the Christmas season is near, so this should not impact any retailer going forward.

P. Sundararajan: In fact, the customers have sent us a message saying that "Not to get panicked due to the second lockdown, we will not be cancelling any orders." So that is the message we got from the customers.

Management: And moreover, they are not holding any shipment, they continue to take the shipment, and they are not allowing any extension also. So what they are planning is they are taking the goods, and they are holding the goods there. And once the lockdown is released, I think they will be supplying in full because Christmas is very close and their sales will be good they are expecting.

Sachin Shetty: In this holiday season or a Christmas season, how is our current order book?

V. Balaji: So, I think M.D. has explained of Rs.226 crores.

Sachin Shetty: This is for the quarter or six months?

P. Sundararajan: In the next two to three months time.

Sachin Shetty: That means Q3 is fully flooded with an order of Rs.226 crores?

P. Sundararajan: You should not take it like that. In the current order book, some maybe shipment in January, some in February, some in March, some in April. The total order is on hand.

Management: As you said, Q3 is fully booked as of now.

Sachin Shetty: We are doing all continuous 24-hours three shifts or only one shift working?

P. Sundararajan: Only one shift for the garment team. But we have plans to increase it. Once this workforce strategy has been in place, then slowly, we will start two shifts in the factories in a phased manner.

Sachin Shetty: My final question is on EBITDA. Going forward it will improve, or it will be same for Q3 and Q4?

V. Balaji: So in terms of our EBITDA, we have guided for 18%, and CMD in his opening speech has said that we are expecting this EBITDA margins to sustain.

Sachin Shetty: With this 4,500 sewing machines operational out of 5,000 during Q4 time, then what would be the revenue for this 4,500 machines?

V. Balaji: 4,500 number I do not know how you have got from. CMD spoke about 5,100 machines which are operational.

Sachin Shetty: So, in terms of revenue, how much we can expect or forecast for this if the 5,000 machines fully operational?

V. Balaji: If all the machines are at 100% utilization, I think we will reach Rs.840 crores of revenue.

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

Deepak Poddar: My first question was around your garment division. You did mention that you are looking EBITDA margin to sustain at the current level of 20%, 21%. So I was just wanting to understand as your capacity utilization increases from this current 70%, is there any upside to that 20%, 21% that we are talking about? And my second query is on your overall EBITDA margin of 18%. Now, as your utilization level in garment increases, your higher-margin business share will increase overall. So overall, your EBITDA margin ideally should increase. So any comment on that also would be helpful?

V. Balaji: Mr. Deepak, when you look at the matrix, the guidance of 18% of EBITDA margin versus what we have achieved in terms of 20.8%, see, this moves up and down based on the currency also. So like, whenever there is a better currency rate, it can even go up to 23%. So, that is why we guide only for 18%, and if there is going to be better utilization going forward, you will have new people coming in. So the training cost is going to cost also. So like you will have the training cost which will be at months time, which will bring down the margin again. So, that is why the guidance is only on 18%, and 1% or 2% up and down here and there it can go.

Deepak Poddar: So this 18% you are talking overall, right, including all the three business together?

V. Balaji: No-no, garment division 18% is what we have been guiding for.

Deepak Poddar: But we did about 21% because of the reasons you mentioned. But do you think that 20%, 21% is sustainable?

V. Balaji: On the opening remarks of Mr. Sundararajan sir, he said that there are certain steps which we have taken, we have consolidated in terms of the number of clients, we have brought down the transportation costs, we have improved in terms of EBITDA margins from the spinning division, we have improved our EBITDA margins from the processing also by investing into the biological treatment. So, many reasons are there which are part of an improvement in the EBITDA margin this quarter.

Deepak Poddar: And coming to the last question like, at 5,000 machines, I thought we could do about Rs.1,000 crores of revenue in your Garment division?

V. Balaji: Mr. Deepak, we can do Rs.1,000 crores of revenue when I do 100% utilization and 100% efficiency also.

P. Sundararajan: Practically all 5,000 machines cannot always be in the running because always depends on the site we need to balance the machines, 10% will be from the balancing we have to keep them. So maybe 4,500 to 4,600 machines will be running next year by now.

Moderator: Thank you. The next question is from the line of Mr. Resham Jain from DSP Investment Managers. Please go ahead.

Resham Jain: Just on the margin side further, what we have seen is that last year there is a MEIS included in the margin, this year actually without MEIS you have done almost 18% margin which looks quite good. So, my question is, what are the factors which have led to this improvement in the overall margin?

P. Sundararajan: As I mentioned, we are fully backward integrated. So, there are certain savings from the spinning mill side and certain saving from the processing division, and we are efficiently working on the consumption of the materials and control over the wastages. So, all these things put together, this is what we promised during the roadshow also that by the investment in spinning and the processing division will fetch about another 1%, which has started yielding now. This is going to be the real saving. And in addition to that, as we scale up our operations, our fixed costs will come down naturally. And we have very cautiously worked on the utilization of the manpower. So, these things have helped us in improving the margins and consolidation. This is another major factor where we have consolidated some of the small factories and merged with the biggest factory, so, our overheads have come down.

Resham Jain: My second question is on shift thing which you mentioned. So, this 80% utilization which you can do on 5,100 machines, but this is based on one shift, are all your factory able to do this two shifts or are there specific factories which can do these two shifts, how easy or difficult is to operate factories in two shifts, because we have generally not seen that happening in India per se. So, just your thoughts on the same?

P. Sundararajan: Generally, two shifts are not really in practice in this industry, especially in India, you are right. But since we have three, four, hostel factories, so it is easy for us to manage for converting into two shift factories. So, we are yet to experiment it, but we do not see any challenge in this one. So, on a phased manner probably from April onwards, we will try to experiment, one factory first gradually for a few months to optimize both the shifts in full utilization, then we will see the difficulties or challenges we set it right, so gradually we will increase other hostel factories also. So, we are hoping that it should not be a problem. So, it will take about six to eight months from now to convert this single shift to factories to double shift factories.

Resham Jain: So, is it fair to say that let us say at 4,000 machines you can do let us say 1,000 crores or 900 crores with this capacity, can one assume that by making it two shifts, this revenue can double also?

P. Sundararajan: It can. We are not going to convert all the factories to double shifts. As I said that only about four factories where we have the hostel facilities, we will be gradually in a phased manner convert it. So it will take the next one full year to convert these four factories to double shift.

Resham Jain: So, the equivalent of 5,000 will become how much sir in terms of capacity if you add these four factories?

P. Sundararajan: If we convert everything into a double shift, so there will be an addition of 1,500 machines in the same factory.

Resham Jain: And 80% of that, that means from 3,000 currently, you can go up to 4,800 machines is how one can look at it, is that right way to look at it, sir?

P. Sundararajan: Yes, can go up to 4,000 plus with the existing 3,000 machines.

Resham Jain: Sir, just one last question related to this. So we already have sufficient capacity now. So for the next one, one and a half years, our overall CAPEX requirement will be relatively lower, right?

P. Sundararajan: Yes, relatively not much excepting maybe a little bit for the hostel, we may need to invest.

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

Bharat Sheth: I was looking at this cost of material which was 42% in last year, September quarter which has come down to 31%. So, how much is because of efficiently use of raw material and how much is due to backward integration?

P. Sundararajan: See, what we have done is there is a change in our product mix, when there are certain products during last time literally we wanted to feed the machines during the last time. So, as I mentioned before that we have taken most of the orders in the bigger volumes with a lesser margin. So, that is the reason why last year the cost of material has slightly gone up. But now, once we have stabilized the products sense, and now we have restructured the product to make sense and made it in such a way currently, the cost of material is the one, is the real one.

Bharat Sheth: It is a more premium product or…?

P. Sundararajan: Suddenly, when we increase the capacity just to feed these capacities, definitely, we would like to go for some products where the margin is very less, and subsequently we will gradually move to the better products. That is how things go always.

Bharat Sheth: Second thing, see, if we say that 100% capacity utilization say 5,000 with whatever marginal, 10%, 15%, we are targeting around Rs.840 crores kind of a sale, so, which roughly works out Rs.210 crores per quarter, whereas, with this 3,000 machines we have already achieved Rs.165 crores sale quarterly, so, I am just confused that where is a gap, I mean?

P. Sundararajan: There is installed capacity of 5,000, but we will be utilizing only about 80% to 90% because always 10% machines are needed for line balancing, we cannot fully run all the machines like spinning mills.

Bharat Sheth: Correct. Still, with say at the utilization of 3,000 machines and which is also in September last month, so, the average may be lower, we have achieved sales of Rs.165 crores standalone garment division whereas say even 4,500 utilization we are talking of Rs.210 crores per quarter, so, where is a gap, I just do not understand?

V. Balaji: Rs.150 crores is the revenue of garment division, out of which Rs.130 crores is the exports alone. We are looking at Rs.130 crores export versus Rs.840 crores, that is what we are trying to say.

Bharat Sheth: Balance Rs.35 crores is what?

V. Balaji: Not Rs.35 crores, it is Rs.20 crores where you have the duty drawback, ROSL benefit, part of that and also the other revenue which comes from third-party dyeing from the dye, and a better bit of lawn which we sell outside which is excess production. So, that is all put together, are Rs.150 crores.

Management: Finally, you need to compare with Rs.130 crores to Rs.200 crores. We are talking about Rs.200 crores only for the garment export division.

Bharat Sheth: These RoSCTL, this duty drawback and MEIS benefit have been withdrawn, so what sense are we getting from the government, when do we expect I mean?

V. Balaji: RoSCTL has been extended until March, which is currently at 4.7% and 2.1% from duty drawback. That is what we are getting. And MEIS has been withdrawn. That is the current status.

Bharat Sheth: But MEIS percentage how much was it?

V. Balaji: It was at 4%.

Bharat Sheth: So, that will affect us from which quarter?

V. Balaji: So, like in the second quarter, we had MEIS of 4%, but they retrospectively reversed in the Q3, So, from March onwards, they reversed it. That is the status.

Bharat Sheth: So, in this Q2, it is not there, correct?

V. Balaji: Yes, now it is not there.

P. Sundararajan: In financial Q1 '20 and Q2 '20 MEIS was there, but subsequently in Q3 '20 it was withdrawn retrospectively including Q1 and Q2 of 2020. That is continuing. There is no MEIS.

Bharat Sheth: Are we looking any kind of benefit because we are, I mean, employment generation industry. So, any sense are we getting from the Ministry some kind of benefit?

V. Balaji: We have been requesting the local association to talk to the Ministry to get better benefits so that we can support the export. We are expecting finance minister to come up tomorrow and come up with a fresh stimulus package for the textile apparel.

P. Sundararajan: But there is a strong love about FTA with the U.K.

Bharat Sheth: So, how that will benefit us?

P. Sundararajan: Because it is more or less like a duty-free, so, we will get better margins, and the more orders will be coming to India.

Bharat Sheth: You said in this quarter we must have some benefit because of rupee depreciation vis-à-vis euro. Because of this currency benefit, how much is there in this quarter?

P. Sundararajan: The customers always take that into account when they negotiate it. I do not think we have great benefits, maybe 0.25% or 0.50% we can play, that is all.

Bharat Sheth: Because sometimes we earn processing also, so one has to look once we reach these Rs.840 crores kind of garment division revenue, so, what will be the company's revenue and EBITDA margin?

P. Sundararajan: First of all, we are not giving any guidance of Rs.840 crores. One gentleman asked about this. If we want, we can go up to Rs.840 crores, but we are not committing Rs.840 crores.

Bharat Sheth: No, no, I agree, sir. Totally whenever we reach something if things open up more, so, what kind of revenue one can really look and the kind of clients that we are adding say next year subject there is no lockdown and things normalized from say here on, so FY'22 what kind of a sense are we getting?

Management: So, in terms of demand, we are getting good traction from all the retailers, the demand is very good because we are in a very niche category and it all bottle downs to the capacity increase that we are going to do over a period of time. So, that is the real matrix which we are working today. That will be our main strategy going forward also.

Bharat Sheth: Sir, of course, this quarter because for whatever reason, working capital has gone up. So, is there any room to bring down the working capital cycle?

V. Balaji: So you are looking at the working capital cycle versus March 31st. If you look at our overall working capital utilization, we have been utilizing at 160 170 right from day one. But during the month of March, what happened is that we have not paid creditors for the last two weeks because of the lockdown. So the utilization level came down. Now, we are looking at the fresh limits which are as on 30th September where there are no pending which are payable to the creditors. So, we are at normal utilization level. But in terms of working capital, inventory, if you look at, we are at par with March 18 numbers where we were at 240, now we are at 240 of inventory. What we can do in terms of decreasing the working capital cycle is that, if we are able to take orders from the customer with a short production cycle, then that could be possible.

Bharat Sheth: Mr. Balaji, my question was on the receivable side, so which was Rs.85 crores as of March whereas it has gone up to Rs.105 crores in September end. So is there any room to bring down that?

V. Balaji: Even that is also contributing. Because we received funds from the customers until March 31. But we have not paid. That is what I am trying to say. And no export happening for 15-days or so. So there is no accumulation of receivables.

Bharat Sheth: And now currently, how is the split between U.K., Europe and American clients?

V. Balaji: Americans now are at 13%, the U.K. should be 55%, a balance should be Europe.

Bharat Sheth: Margin differential is there between all these different geographies?

P. Sundararajan: Margins would be the same because it all depends on the product. We are catering the same products to across all the countries. So there is no big difference in the margins.

V. Balaji: There should not be any big differences.

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

Vikas Jain: My first question is with regards to the average realization per piece that we clocked this quarter, that is Rs.123. Can you just briefly explain the first thing, what was the mix of our product is, what is the share of basic and fashion into this?

V. Balaji: For this quarter, the realization of 120 itself shows that we have done a lot of niche products for the current quarter and that is why find the material costs on the lower side and our labour cost on the higher side.

Management: Product mix; basic is only 30% to 35% and the balance 65% to 70% is on the fashion for this quarter.

Vikas Jain: When we say that our Q3 and Q4 look robust, do you expect that this mix to largely stay at current levels or it should even out at around 50:50 for the next two quarters depending on your order book that you have currently?

P. Sundararajan: You are talking about realization? That depends product-to-product and customer-to-customer.

P. Sundararajan: It will range from 100 to 110.

Vikas Jain: That is what I am asking, sir. The realization that we clocked this quarter, are we expected to normalize in H2, right?

V. Balaji: You cannot extrapolate the same realization rate for H2; it could differ; it all depends on the customer maximum and the product mix. So, you cannot go by that.

Vikas Jain: One more question on the garment margin. If we could quantify what are all the reasons that led to this higher margin, product mix contributed, any quantification that you can give?

P. Sundararajan: I mentioned to you before, 2% to 3% from spinning and the processing division where we have done a production of spinning and in **processing** division, biological treatment plant project. So, these have all enabled us to increase the buying capacity and in the productivity also. In addition to that, we have done a lot of control over the personnel cost reduction and transport cost of the people, people mobilization costs and consumption and wastage control, so a lot of things that we mentioned during the last concall, which we already started with working on a plan, we are straightaway able to feel the difference of it, and this will continue.

Vikas Jain: Sir, as you said, the spinning and processing investment that we have made started yielding results. The second thing is you said about the cost control that you have exercised in H1. So my question is, while clubbing of the factories and savings on a logistic cost would continue. But what part of it would probably return back to its normal levels if you could in percentage terms quantify how much of the cost-saving will be sustainable, and as normalization occurs further, how much of it would return to earlier level?

P. Sundararajan: I think as of now we have reached a level where we will be able to maintain this cost control. And only scaling up will help us in bringing down the cost a little bit by going for two shifts in the factory. So this will definitely improve the margin by further reductions of overheads. But otherwise, it is an ongoing thing; cost controlling on the personal cost, efficiency of production, these things will continue to go, but it will increase marginally quarter-on-quarter.

Vikas Jain: So you are saying whatever cost control that we have achieved is all of it is sustainable?

P. Sundararajan: Yes.

Vikas Jain: And my last question is on the retail side. Sir, while other peers who are into the fashion and apparel retailing, they have posted recovery on a sequential basis. But what has led to a specific like margin that you clocked this quarter of around 5%, anything that is one-off or any special measures that you have taken and can we expect this 5% kind of a margin on a sustainable basis going ahead on the Retail?

V. Balaji: We have done so many things on the cost reduction front on Retail, non-performing stores vehave been closed, and we have moved people out where they are not performing. So, we have done a lot of work on the retail cost reduction work also. We have done even in terms of shifting the corporate offices to a smaller place so that there is cost reduction, and also negotiating with the rents to the landlord where at least for 1.5 years, 2 years reduction in rent may be effective. So, so, much of work has also been put on the retail front which may not be visible on the face of the record, but what happens is that we are able to save some huge cash losses that would have happened. So, we saved close to Rs.50 lakhs in terms of personnel cost alone per month. But what happens is that once the stores all open up, then there could be a small increase, but it will be on the performing stores only.

Vikas Jain: My last question is on our strategy for the Retail. Any concrete strategy that you have planned for the growth of this division?

V. Balaji: So, in the opening remarks, CMD has stated that we are expecting retail division to move forward considerably and doing sustainable growth over a period of time. So, that answers your question.

Vikas Jain: But any guidance in terms of the investment for the growth into this business?

V. Balaji: The board has already explained that. We will not invest much more into the Retail, a rental will have to work itself within the boundaries in which it is presently available. So, it is up to them to liquidate or manage the cash within the available resources.

Moderator: Thank you. Ladies and gentlemen, this will be the last question which is from the line of Naushad Chaudhary from Systematix. Please go ahead.

Naushad Chaudhary: Three, four quick questions I have. First one on the customer side sir, if I recall the last earning call, so, we had added around one U.K. customer, and we are in talk with two U.S. clients and this quarter also we have added one customer, so a total of four customers we have added. Just wanted to understand when this USA clients would start giving us revenue, and what is the potential of all these four customers in terms of business to us?

P. Sundararajan: The last time when I mentioned that we are talking about the one U.S. customer, but we have not gone ahead with because the minimum order quantity was not attractive enough, so, we have not gone ahead with that customer although everything all exercises then. So, we were a bit concerned about the minimum order quantities. So, we are not going ahead with that one U.S. customer, but instead of that we are adding one customer from Europe which will be much bigger and their volumes are much bigger. So, that will offset this replacement for this one.

Naushad Chaudhary: Can you give us a figure what could be the potential of all these new customers which you have added?

P. Sundararajan: New customers are as good as our existing customers volumes.

Naushad Chaudhary: And are these direct retailers, or these are distributors…?

P. Sundararajan: One is the Retail, another one is a licensed product supplier, which in other words, they will also be doing tie-up with our existing customers to supply the licensed products through us.

Naushad Chaudhary: And in terms of a number of employees in 2Q this year versus last year if you can share the figure?

P. Sundararajan: We do not have it right now.

V. Balaji: We will be in a position to share it to Ankit later.

Naushad Chaudhary: In terms of garment factories, we have consolidated some smaller factories, we have shut down, so how many garment factories we have today versus if I remember around 12 factories we had earlier?]

P. Sundararajan: We have 16, and probably after March we will be consolidating another two factories. So, it will become 14 factories.

Naushad Chaudhary: Going forward, this will be our strategy of having less number of bigger factories instead of having a large number of small factories?

P. Sundararajan: Yes, because a few years ago we wanted to increase the business volume, so we have to go for much smaller factories of rented buildings. So, now we are financially in a much better place, so, we are just consolidating them with the bigger and better factories where all the efficiencies will be much better which we have seen already by consolidating these two factories.

Naushad Chaudhary: If I remember it correctly, our strategy of having multiple factories was due to availability of labour, so, we had a plan to have a factory near to the labors availability, and that is how we stuck up into having a large number of factories?

P. Sundararajan: Even now that is the strategy, definitely we have to have satellite factories to strike a balance between the hostel migrants and the other hostel factories with the local workers also. So that strategy is still on, and still, it is working, but the number of small can be consolidated one big in those areas, that is what we are doing

Naushad Chaudhary: And lastly sir, what is the cotton inventory we have and the price that you can share the current balance sheet of 1H FY21?

V. Balaji: Can I share with you later?

Naushad Chaudhary: I have just a clarification, sir. If I understand it correctly, you have 6,100 machines, of which we are utilizing 3,000 machines, and you have a target of reaching it to 4000 by '21.

Management: Yes, March '21.

Management: Cotton stock as on 30th September 2020 is Rs.30 crores.

Moderator: Thank you. As this was the last question, I would now like to hand the conference over to Mr. Ankit Gor for closing comments.

Ankit Gor: Thank you, sir, for taking out time to discuss results. And I wish everybody at S.P. Apparels Happy Diwali and Prosperous New Year. Any closing comments we will be happy to hear?

P. Sundararajan: So, I would like to give a message that we are very optimistic about our business plans way forward. We had faced so many challenges at the time of listing Brexit and demonetization, GST things and MEIS withdrawals and now again this COVID-19 thing. So, once we have got listed and we were not able to focus on our core activities, only fighting with such kind of things. So, this has been one of the reasons why we have not really shown the big numbers and up to the expectation of investors maybe. But we are completely back on track, and we are very excited about the years to come, and we are very aggressive on our plan whereas I mentioned in my opening speech that we are all set with the customers order inflows and the supply chain management and the infrastructures capacities and internal systems to manage the whole processes, everything is in place and only we were facing until this last month was, mobilizing out a workforce as much as we wanted to fill our capacity. But now we have been working with aggressively in the last two, three months, and we have strategized certain things where we have got a regular inflow of workmen every month, and so regularly, we take say, 100 or 200 people and train them and place them in the factories on a monthly basis. So there is going to be a constant increase in the number of lines over a period of next 12-months, so this is a very interesting subject, and our whole team is all ready to start this assignment. So as we grow our capacities and the order inflow will also naturally increase, so we are very optimistic about it. Next financial year I hope it will have a new all-time high when compared to the last previous years. So, I wish to close the meeting. I wish to thank everyone for being a participant of this concall, having an interest in our conversation and wish you all Very Happy Diwali and good luck to you. Thank you.

Moderator: Thank you. On behalf of Systematix Institutional Equities, that concludes this conference. Thank you for joining us, and you may now disconnect your lines.