"Arvind Ltd Q1 Financial Year 2018-19 Post-Results Discussion Conference Call"

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Moderator: Ladies and gentlemen, good day and welcome to Arvind Limited Post-Results Discussion Conference Call for Analysts and Investors for Q1 Financial Year 2018-19. As a reminder all the 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. I now hand the conference over to Mr. Samir Agarwal – Chief Strategy Officer of Arvind Limited. Thank you and over to you sir.

Samir Agarwal: Thank you. Good afternoon and thank you for joining us. I have with me Mr. Jayesh Shah who is our Group CFO and the Executive Director of the group. We also have Mr. J Suresh who is the Managing Director of our Arvind Fashions Business with me on this call.

On the overall basis, we had a very good quarter with a strong growth. Our consolidated revenues increased by 10%. Leading this growth was the Branded Apparel business that continues to deliver strong performance in otherwise what has been a rather difficult market condition.

Adjusting for GST, this business reported industry-leading growth of 18%. As we have said earlier on these calls, the product portfolio behind this business is most suitable for the youth which is the fastest-growing segment in this business and hence, we get advantage of this momentum.

Branded Apparel also showed a very strong earnings growth on account of a very strong and stellar performance of our Power Brands, our EBITDA grew by over 75% as well our top-line was 18%. Unlimited, our value play, saw an increase of 20% in revenue and also increased the gross margin as well as store-level profitability.

In our Textile business, while the overall revenue growth was 2% if we deaverage that the woven business grew at 10% and the garments grew by 22%. In case of denim in the last year in this quarter what had happened is that there was a significant pre-GST buying and those high volumes have created very strong base and hence this quarter somewhat suffered from the base rate. Textile margins also were lower compared to both quarter 1 previous year as well as quarter 4 of last year and the two main reasons are the lower drawback rates as compared to Q1 in the last year same period, as well as lower elevation from our exports as our currency was hedged at much lower rate than the whole of last year. Based on current hedges, we will be near or at the market rate in H2 this year.

Thus far, we have a business called Advanced Materials (AMB) which was partly within textile segment and partly in the others. From this quarter onwards, we have regrouped our past and current segment figures and we will start reporting out numbers for this business separately. We are quite excited about this business in fact. The business grew by 10% current quarter and it saw a significant improvement in the profitability as well. We strongly believe that this will grow over (+20%) this year with further improvement in the margins and as we continue to invest in this business the idea is that we hit the Rs. 1000 crores mark in next year in terms of revenues. As an additional information, Advanced Material Business was Rs. 487 crores in terms of revenue and EBITDA was a negative Rs. 7 crores for the whole of last year. Our debt at the end of quarter was Rs. 3450 crores. We do not anticipate any significant change in this number in the current financial year.

Now I will turn to the topic of IndAS and the impact regarding that:

See thus far, we are required to report sales made on SOR at the wholesale value instead of full gross value. The difference would be booked as selling cost with no impact on profits. This resulted in sales increase of Rs. 58 crores during this quarter and Rs. 105 crores in the corresponding quarter of the previous year. Consequent to implementation of IndAS 115, some of the retailers requested for the change in the terms of business from SOR to OR. This resulted in increased sales of Rs. 69 crores, an incremental profit of Rs. 10 crores. All this we believe is largely a one-time impact and will become very small from the next quarter. As we look ahead, we continue to remain quite positive about the growth and improvement in profitability of each of our business segments.

As we have stated in the past, we are going to scale up our garmenting business significantly and we are busy setting up facilities or growing them in Ethiopia, Jharkhand and couple of locations in Gujarat. We hope to grow our garments volume by 30-35% this year. As we grow this garmenting business in the overall textiles, the share of garments will increase and as a result the blended margin will likely remain flat. With significantly improved profitability in Advance Materials and reduced investments in our internet business, we believe that the demerged Arvind Limited will see an improvement in EBITDA by about 1% for the year. We expect Branded Apparel business to see acceleration of growth and momentum and profitability as we increase investments in brand building.

And as a final input the demerger process is progressing well. It is in the last leg of approvals and we expect the same to happen in early next quarter, early Q2.

So, that concludes my opening remarks and I would like to invite you to ask any questions you may have to any of us. Thank you.

Moderator Thank you very much sir. Ladies and gentlemen, we will now begin the question and answer session. The first question is from the line of Dimple Kotak from SKS Capital, please go ahead.

Dimple Kotak: Sir my first question is that how much inventory do we have, because cotton prices are surging higher? Secondly by when our Power Brands all of them would get profitable? And I believe 3 Power Brands are expected to be profitable this year. And sir thirdly as you said, if I heard correctly, you said that Textile business will see 1% growth in EBITDA margins whereas in the presentation it is flat EBITDA margin. So, if you can just throw a light on that, thank you.

Jayesh Shah: We have a dynamic inventory purchase policy based on the views about the market and the order position, so as far as current season is concerned we are fully hedged on both currency as well as inventory. I think there is some misunderstanding about the brands business. As we have stated in the past, we believe that Power Brands are of course profitable and very profitable. Other brands including Unlimited would be profitable during the year. This is one of the lowest periods in terms of total revenue and the overhead remain constant. So, quarter 1 is not an indication of what would happen during the year. We are expecting that overall business will deliver about 1 percentage higher margin get aided by not only the Power Brand performance but also the reduced losses, I mean in fact all brands are likely to be closing the year with zero or positives.

Dimple Kotak: And sir for the inventory you have it till September or you have it till October, wanted to know till what time you are holding the cotton inventory? Till what time we have?

Jayesh Shah: No, we will not be able to tell you exactly but as I said that for this season we are covered.

Dimple Kotak: Sure sir, one more question. In engineering business, the margins, EBITDA margins as per the presentation including the other income, have come down to 24% from 28%. So, what is the reason and going ahead what do we expect?

Jayesh Shah: As we have stated in our earlier these things we are quite buoyant about this business. The margin percentages over a year, as you said, would be similar to what we deported last year. Quarterly numbers will vary based on what equipment supply happens during the period. So, that will not be an indicator of what would happen.

Dimple Kotak: So, then we should take the 26.6% reported -

Jayesh Shah: We would be delivering similar, not exactly same but similar performance, plus minus few percentages we do not know based on various things including steel prices, selling prices, rupee but our estimation is that we would be delivering similar high growth, high return results for this company.

Moderator: Next question is from the line of Rishabh Parikh from Sunidhi Securities, please go ahead.

Rishabh Parikh: Hi, just a couple of questions. One was, if you deconstruct the textile company versus the textile division margins, the textile company reported a revenue of Rs. 1811 crores of which textile was Rs. 1561. Advanced material was Rs. 128 crores and others were about Rs. 122 crores. EBITDA also if you deconstruct on the same method was Rs. 216 crores of which textile Rs. 185 crores, advanced material was Rs. 10 crores. That means others was Rs. 21 crores. So, the others section EBITDA margin was 17%. Does this include any element of FX gains or is this all pure operational EBITDA?

Jayesh Shah: I am not sure whether you had a chance to look at our review note, where we have given segmental profitability. As far as the others segment is concerned, it consists of a few divisions which are relatively small and as a result they are all combined. So, one of them is our, we do water management, water effluent treatment business. It is a project-based revenue that comes and, in this quarter,, there was a significant amount of business there, highly profitable. Secondly there are other divisions which are for e.g. Arvind Internet is part of it now that it becomes relatively small. Last year we had a Rs. 14 crores EBITDA loss, this year the losses have reduced to half. So, in others there is no foreign exchange gain, in fact this quarter the foreign exchange as my colleague, Samir, just mentioned, we are less on foreign exchange than what we are on in quarter 1 of last year and whole of last year as an average per dollar. So, this is entirely an operating profit.

Rishabh Parikh: So, this Rs. 22 crores is operational, okay, thank. And my second question would be if you look at brand and retail number for Q1 of last year, in the presentation it says that reported revenue was about Rs. 893 crores for Q1 FY18, which is Q1 of last year. But if I look at the presentation last year it was Rs. 773 crores.

Jayesh Shah: I think we just mentioned about it in the speech earlier that because of IndAS we were required to gross up our SOR sales from wholesale to retail. For comparing purpose, we have reported higher sales in last year as well as higher sales. So, it has been given separately as a line item in our presentation as well. The reason why we have ignored it because that does not show the underlying performance, so all our discussions have been on what has been the underlying performance, which is this year the turnover has been like Rs. 890 crores against Rs. 787 crores of last year.

Rishabh Parikh: And last year's figure of Rs. 787 crores, does this include component of excise or is this is a comparable number?

Jayesh Shah: No, it is not comparable. That is why if you see we talked about 13% growth on a reported basis or an 18% after adjusting the GST impact.

Rishabh Parikh: And my last question is if you look at your EBITDA from your brand and retail, from Power Brands it was Rs. 51 crores and on a consolidated brand & retail it was Rs. 29 crores which implies an EBITDA loss of about Rs. 23 crores from Unlimited another brands and this same number last year was about Rs. 20 crores. And the guidance given was that all brands would be profitable sometime this year. So, do we still hold onto that guidance?

Jayesh Shah: To your question – yes, we are looking at profitability across the brands this year. I think this quarter is not as I said earlier, like this is not an indicative quarter of any type on the brand margin because the overheads remain flat while the other contributions are low because this is almost a smallest quarter in terms of revenue. So, none of this quarter's performances will have to be seen only with respect to what we did last year, not necessarily what will happen during the year.

Moderator: The next question is from the line of Sagar Parekh from Deep Finance, please go ahead.

Sagar Parekh: Sir just one question, most of my questions are answered. If I look at your Q1 FY18 presentation which was given last year, the brand and retail EBITDA given that time was Rs. 16 crores.

Jayesh Shah: No, it is other way round. It is Rs. 21-22 crores. I will explain to you. Last year in quarter 2 at the time we decided to demerge the company, the shoe business which was part of Arvind Limited Others was classified and proposed to demerge in to Arvind brands. And from quarter 2 last year as we had mentioned in the note, we regrouped and transferred the entire business to the business segment of branded detail or Branded Apparel division. Quarter 1 was left out and so we had to do it this time. So, these figures of last year and this year are completely comparable because this year also the numbers that we are presenting has the shoe business and so was the shoe business last year. For your information the shoe business last year had lost about – I think because it was in a heavy marketing cost of about Rs. 5-5.5 crores, this year that loss has reduce to about Rs. 2-2.5 crores.

Sagar Parekh: And just coming to the last question, last participant asked, so I am comparing the YoY number excluding the Power Brands, so that captures the seasonality. So, YoY Rs. 20 crores loss last year has gone up to Rs. 23 crores this year ex Power Brands, so that captures seasonality.

Jayesh Shah: Ex-Power Brand you mean?

Sagar Parekh: Yes.

Jayesh Shah: Yes, it will happen because the base of cost will increase but not necessarily proportionate sales because as you possibly are aware that we are aggressively setting up new stores for Unlimited. Those costs are coming in but not necessarily the revenue. All of this will get addressed as we have stated in the past and even just now is that as you progress into the H2, which is the season where you actually make sales, all of these anomalies will get corrected. So, you will have to see this quarter only against the last quarter.

Sagar Parekh: And what was the sales to sales growth of Unlimited?

Jayesh Shah: We have given all the formats. Had a negative L2L this season because of the base effect. Last year for example, quarter 1 the Unlimited had a 39% like to like sales because of the pre-GST purchases. This of course has come down and it is negative, but we have reported again in our review note that if you look at July compared to last year which was again depressed because all the purchases happened in June. This year the July like to like has shot up to 10%. So, we will have to look at not quarter 1 sales on like to like basis because of the pre-GST purchases and the base effect. If you look at including July, the Unlimited or all formats have performed better.

Sagar Parekh: And this Textile business 10% growth for the full year, so which means that 9 months you will have to perform much better. So, we are still confident of that, right?

Jayesh Shah: Yes, so that is our internal plan to grow. The reason is that we have been currently in the investment mode in garments business and that should rectify in H2.

Moderator: The next question is from the line of Maulik Patel from Equirus Securities, please go ahead.

Maulik Patel: A couple of questions. First is on the garment business, if you could just give some update on the next phase of growth or expansion in Ethiopia and India, that is number 1. Number 2, as you mentioned that in earlier opening comments, as Samir has mentioned that dollar realization was not good compared to what you earned for the last year. So, what could be the improvement in the dollar realization and the revenue in the export business going ahead if we take the current one and what kind of margin expansion one is looking for, that is number 2. And number 3, on the brand side what is exactly happening on the other brands because there was hardly any growth in this financial year and this particular quarter. So, is there any significant expansion we are looking for that or probably are we looking to rejig the portfolio of the other brands?

Jayesh Shah: Okay, so let me address the garmenting. So, we are currently in the mode to expand in Ethiopia, India, in couple of centers in India apart from Bangalore and we are hoping that we will have an output of 8 to 9 million additional volumes this year as compared to last year. So, that is the current state. I would not be able to tell you exactly how many pieces, capacities we are installing because they are continuing expansion programs in each state. So, as a result as and when our facilities either we can hire or build. We are investing in one or another depending upon what is available where. This year as we speak we believe we should have 8 to 10 million extra pieces to sell. As far as dollar-rupee is concerned we will be near to market in H2. Whatever that may mean in terms of impact on revenue or profitability. As far as brand & retail, Suresh would you want to take this question?

J. Suresh: See as far as the other brands are concerned, now our focus is very clear. I think we have put in all the investments and expansion behind Power Brands and Unlimited and Sephora where we have delivered excellent growth in quarter 1 market-leading growth. And then we are also looking at opportunities of developing GAP, Aeropostale and Ed Hardy, these three brands are showing promise. Probably getting into a potential Power Brand kind of a format and I think this is where we are putting our focus. The other set of brands, we have five brands where they provide completeness to your portfolio. For example, if you take Children's Play supports us in gaining our leadership in kids wear. Gant and Nautica if you take we have two very strong actually completes our bridge-to-luxury portfolio, so what had happened in the current quarter is all these brands actually are retail dependent brand and since retail was not very good and we had a negative LTL, these brands have not grown because we have not expanded stores in these brands because of the focus of expansion in Power Brands and Unlimited. But going forward once the LTL comes back we expect to deliver a nominal growth. Of course, the focus is to make sure that by end of the year all these brands are either breakeven or profitable as Jayesh bhai mentioned.

Maulik Patel: And earlier last year around GST time, mostly around 30% of our revenue from Power Brands and other were coming from the wholesale channel and they were facing some liquidity issue, so I think that was the problem. Now are they back to the normalized?

J. Suresh: It is improving, in fact if you take purely quarter 1 our collection has been higher than sales which means we have been able to bring down the debtors. But we are expecting going forward the things to improve as the festival season comes in. We should end the year with committed reduction in debtor days.

Maulik Patel: And going back to your though process of Rs. 1500 crores of CAPEX you want to spend on a textile side, and some clarity is that large portion of the CAPEX will be going to the garment division as a whole. So, last year garment did around Rs. 1300-1400 crores of topline. Now probably in 3 years down the line, do you think that garment will become a largest revenue contributor? Can it double the revenue in the next 3 years?

Jayesh Shah: In a sense but I think the way we look at it is not exactly this garment versus fabrics because our intention is not to look at these two businesses independent of each other but as a vertical integration. So, I think the way we are looking at it is to say that how much percentage of our fabrics which was 10% last year, how much percentage of our fabrics have converted into garments and sold in a garment form versus the fabric form. And I think that is how we look at it. And eventually we would want to also look at the end to end profitability of garment instead of profitability of garment which is after fabric profitability. So, I think the way to look at it is to say as we become more and more vertically integrated with few or large customers doing a proper account management with them, how do we increase consistency and stickiness of business and continue to add value? So, I think that is how we look at it.

Moderator: The next question is from the line of Shalin Kumar from UBS, please go ahead.

Shalin Kumar: Just wanted to understand bit on textile. You have actually explained quite a lot on it already. Just to understand, the profitability has taken a big hit over here. So, what are the levers do you have for the next three quarters and what kind of a margin should we consider here, I am just trying to figure out that.

Jayesh Shah: I think you would not go wrong if you take the flat margin compared to last year because we believe that the textile or fabric margin will improve compared to last year marginally in H2. However, the blended margin will not improve because the share of garments will grow. So, as a very rough guidance we are suggesting that the margin will remain flat on textile side with a 10-11% overall topline growth. Levers to that are two. One is of course that we would be nearer to the market on the currency and number 2 our volumes are set to increase. This time it was at 2% growth but in H2 we see a much higher growth.

Shalin Kumar: Second question on that, previous participant has asked you that it is going to be towering task. Seems like if we have to maintain the 10% kind of a guidance, so do you think things are – here I see tricky part is denim where we have seen a decline over 15%. So, what do you think on that side?

Jayesh Shah: If we look at the total sales of denims that we had done last year, we are not seeing a significant change and we have been almost 96% to 100% of our capacity year on year. It was only the last year quarter 1 where there was a pre-GST heavy buying by the distribution channel that resulted into an increase. So, if you for example, look at sales of denim in last four quarters it was 28-22-25-25. This quarter we have delivered 23. So, that is what I was trying to say that it has not been a significant change from a long-term or mid-term average. It is the comparison to one that it looks acute.

Moderator: The next question is from the line of Rishabh Parekh from Sunidhi Securities, please go ahead.

Rishabh Parekh: Just to clarify on the previous participant's question, textile margin you said flat YoY compared to last year, so 14% is what we are working here, would that be accurate?

Jayesh Shah: Last year textile margin was below 14%.

Rishabh Parekh: Sir last year the textile demerged entity margin was 11% and the textile division margin was approximately 14%.

Jayesh Shah: Lower than that, it was between 13% and 14%.

Rishabh Parekh: Okay, so we should expect say between 13% and 14% for the textile division and for the textile company we had mentioned that 100 basis points improvement compared to last year. So, 11% can become 12% approximately.

Manag Jayesh Shah ement: That is correct.

Moderator: The next question is from the line of Nihal Jham from Edelweiss, please go ahead.

Nihal Jham: Sir my first question is on the brand and retail segment. Just specifically again on the other brands, I think someone else was also mentioning. So, here we have seen a limited expansion of a store count or even in terms of sq. ft. space, so any comments on that where maybe just this quarter where we have gone limited on the expansion?

J. Suresh: As I said earlier, it is by strategy we focused on Power Brands and Unlimited in the current quarter, that is the quarter gone by. So, we have not done any expansion of these brands and we will be a bit careful in expansion and the expansion as required because the priority is to deliver breakeven or profit by end of the year in all these brands and within that I also mentioned that few brands we have identified for focus because they are showing promise of beginning potential Power Brands which are Aeropostale which is of course doing quite well, Aeropostale, Ed Hardy and GAP. These are the brands we will be focusing and expanding going forward.

Nihal Jham: Okay, but we are looking at a growth being similar for this year at 20% in the branded retail segment 18-20% and if the focus is, say on Power Brands, so is it that we are expecting a higher growth from Power Brands in the coming year and say maybe the growth from the other brand is going to be similar to the overall number?

J. Suresh: Actually, the growth will be higher in Unlimited than Power Brands. Power Brands continue to grow at healthy clip, 15-18%. So, that is what will happen. So, it is not that the entire growth or a large part of growth will come from Power Brands. In fact there will be a good growth coming out of Sephora, GAP as well as Aeropostale.

Nihal Jham: Just one last question on Unlimited. We feel the performance has been good and understand that the LTL may be this quarter was impacted as you mentioned because of the industry, but overall on the margin front as you mentioned say for some of the value retail format which have been doing well, when can we expect say the margins in Unlimited start improving or have they already reached a very reasonable level?

J. Suresh: No, I think there has been a good improvement in our both gross margin and store level profitability, but the scale is still small for Unlimited. I think once it starts scaling up we will have a huge amount of operating leverage kicking in in the case of Unlimited. In addition to that we have also increased almost 1.5 basis points on sales. We have increased our advertisement sales during the quarter because we are now going to invest and build this brand so if you look at both the additional expenditure on advertising and also the improvement in store profitability. It is a good indicator that when the scale picks up we will have a good bottom-line on Unlimited.

Nihal Jham: Right, but is not that revenue per sq. ft. is comparable to some of the other value retailers and maybe the scale is already there in that sense?

J. Suresh: No revenue per sq. ft. is not a problem, it is about the total scale because we still have only 8 lakh sq. ft. of sale but some of the larger competitors will have more than double of that space, in fact more than triple of that space.

Moderator: The next question that is from the line of Arjun Singar from Reliance Mutual Fund, please go ahead.

Arjun Singar: I just went through your presentation on slide #25 you have given a breakup between Arvind Limited, Branded Apparel and Engineering for various parameters. So, here your EBITDA is given including other income for we see different segments, could you please give me the EBITDA excluding other income also?

Jayesh Shah: Yes, we can, I mean other income is very-very small as you can see.

Arjun Singar: For FY18.

Jayesh Shah: The whole of the year, okay sure we will give it to you. I do not have it right now, but we can give you divisionally EBITDA without other income that is not a problem.

Arjun Singar: So, should I get back to you later?

Jayesh Shah: Yes, so I would not have it off hand right now with me, but my colleague will get in touch and circulate it.

Moderator: The next question is from the line of Zecca Doshi from Sharekhan, please go ahead.

Zecca Doshi: Sir I have two questions. Mainly, I want to know your strategy of your innerwear business which has been growing consistently and this quarter you have seen a growth of 33%. And you are expecting to grow it at 50% during the year. So, what is the strategy and what are expansion plans going forward?

J. Suresh: If I understand the question right, I think innerwear business is doing exceedingly well for us, in fact US Polo innerwear has more or less doubled the sales during the quarter. Hanes also has started now picking up and this combined with CK, we are actually looking at Rs. 150-200 crores of sales for the year which will be double of what we did last year. I think very clearly, we are establishing ourselves as a strong #2 player in the premium inner wear segment.

Zecca Doshi: Sir do you have any expansion like exclusive stores you have to set up or you are looking out or you are looking out for just sales to LSF or something?

J. Suresh: No actually, this category more mom-&-pop store, 80% of the sales actually comes from small specialty underwear dealers so we are expanding coverage in these stores. In fact, last year we had an active dealer base of around 3500, this year we are going to have an actual dealer base of around 7500-8000 dealers by the end of the year. We have already moved 3500-5500 dealers. As far as exclusive store is concerned we already have a very large amount of more than 300 exclusive stores of US Polo where we will keep US Polo underwear. Exclusive underwear store, we currently have 5. We are looking at opening around 15 to 20 stores by end of the year, but the big expansion is going to happen through dealer expansion. That is specialty underwear dealer expansion.

Zecca Doshi: And sir my next question was on the online sales and omni-channel strategy, what about every brick and mortar retail is now speaking about, how are you working on the omnichannel strategy? How is your plan going ahead? And how much after sales are you expecting from that channel?

J. Suresh: In fact, I think we have been ahead of the curve as far as omnichannel is concerned because even almost 2 years back we had sort of put in place an omnichannel strategy whereby our store, we have a one view of the stock. And if you go to a store and you do not get your size you can order in the store from the nearby store or from the warehouse wherever it is and get it delivered at home. So, our sales in the store, I mean what we call sales a sales, where you do not get stock of your size or for example, we have say four colors of a particular shirt and only 2 colors are available in the store. We have a technological issue, the other 2 colors available in the warehouse and then get it delivered either from the warehouse, the store nearby. So, we have put this strategy in place quite sometime back and now that is working quite well, almost 2-3 store sales is coming through this. In addition to that, our online sales is really doing exceedingly well. In fact, in the current quarter we had almost 150% growth in online sales. A combination of both online and omni strategy, I think we have been ahead of curve and we hope to maintain that lead going forward.

Zecca Doshi: And sir this omnichannel, just one more clarification. Omnichannel has been throughout your stores or they are some of the number of stores where this omnichannel is present?

J. Suresh: No, we totally have 1400 stores and we are now omnichannel around 800 stores. The balance stores we are not doing it because they are small-sized stores and may not make too much sense at this stage but most of the stores are covered with omnichannel.

Moderator: Ladies and gentlemen, that was the last question. I now hand the conference over to Mr. Jayesh Shah for closing comments.

Jayesh Shah: Thank you very much for participating in the call and looking forward to talking to you next quarter again. Thank you.

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