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Trading Symbol : KDDL

Scrip Code : 532054

<u>Subject: Q1 FY22 Earnings Conference Call Transcript</u>

Dear Sir / Madam,

Please find enclosed herewith a copy of transcript of Q1 FY22 Earnings Conference Call.

Kindly take the same on record.

For KDDL Limited

Brahm Prakash Kumar
Company Secretary

Registered Office: Plot 3, Sector III, Parwanoo - 173 220 (H.P.) INDIA.

"KDDL Limited's Q1 FY'22 Earnings Conference Call"

August 16, 2021

Disclaimer: This document is subject to errors and may or may not contain words which have been included / omitted due to human error while transcribing the conference call. Any and all information should be verified with the company by the reader.

MANAGEMENT: **MR. YASHOVARDHAN SABOO – CHAIRMAN & MANAGING DIRECTOR, KDDL LIMITED**
MR. SANJEEV MASOWN – EXECUTIVE DIRECTOR & CHIEF FINANCIAL OFFICER, KDDL LIMITED
MR. RITESH KUMAR AGARWAL, CHIEF FINANCIAL OFFICER, ETHOS LTD.

Moderator: Ladies and gentlemen, Good day and welcome to KDDL Limited's Q1 FY'22 Earnings Conference Call. This conference call may contain forward-looking statements about the company which are based on the beliefs, opinions, and expectations of the company as on date of this call. These statements are not the guarantees of future performance and involve risks and uncertainties that are difficult to predict. As a reminder, all participant lines will be in the listen-only mode and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing '*' then '0' on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Yahoo Saboo - Chairman & Managing Director, KDDL for his Opening Remarks. Thank you. And over to you, sir.

Yashovardhan Saboo: Thank you. Good afternoon and welcome to everyone for our Q1 FY'22 Earnings Conference Call. I'm joined by Mr. Sanjeev Masown -- Executive Director and CFO of KDDL. And I would also like to introduce to you Mr. Ritesh Agarwal, who will be taking over as CFO of ETHOS from Mr. Rajasekhar. Ritesh is a Chartered Accountant with a rich experience of more than 17-years. His previous assignment was with Spencer Retail. We also have SGA, our Investor Relations Advisors on the call.

I hope everyone has had a chance to go through our updated "Investor Presentation" uploaded on the exchanges.

I'll start with a Quick Overview of the Overall Business. We had witnessed healthy recovery towards the end of the previous financial year. But during Q1 of this year, major cities and markets came under severe lockdown due to the second wave of COVID which has affected manufacturing operations and performance both at our factories as well as retail business. As you know, the second wave of COVID-19 was much more severe compared to the first wave and market sentiments and customer sentiment was much lower. However, I am very pleased and happy with the performance of both our manufacturing and retail businesses despite the difficulties and despite considering the demand suppression on account of the lockdowns.

Let me give you a Brief on the Financial Performance first on a consolidated basis for Q1 FY'22: Consolidated revenue for Q1 FY'22 increased by 162% YoY to Rs.139 crores. Now, you will appreciate ladies and gentlemen, in comparison with previous year first quarter is quite meaningless because the last year first quarter was a complete non-performance although this current year quarter had a similar even a more severe lockdown, but the performance has actually been very good. Nonetheless, I think the comparison with last year is a little meaningless. So I'll give you absolute figure and the comparisons are anyway there given in the presentation.

Consolidated gross profit for Q1 FY'22 increased to Rs.63 crores. Consolidated EBITDA for Q1 FY'22 stood at Rs.14.9 crores as compared to a loss of Rs. 6.3 Cr in the last year same quarter. Consolidated EBITDA margins in Q1 FY'22 were 10.7%. Consolidated PAT for Q1 FY'22 was Rs.2.8 crores as compared to a loss of Rs.15.6 crores last year for Q1.

You must be aware that our financials are impacted by the application of IND AS 116 accounting standard, which impacts EBITDA and PBT. IND AS 116 adjusted financials are also published in the "Investor Presentation" for reference.

Coming to the Business Wise Updates, starting with manufacturing, this comprises of Watch Components, Precision Engineering and Ornamental Packaging businesses. In Q1 FY'22, manufacturing businesses revenue increased to Rs.46.2 crores. The revenue share of Watch Components and Precision Engineering business for the quarter stood at 75% and 23% respectively. EBITDA for Q1 FY'22 was Rs.7.4 crores against a loss of Rs.1.3 crores last year. EBITDA margin for Q1 FY'22 stood at 15.9%. Profit after tax for the quarter stood at Rs.2.8 crores compared to a loss of Rs.4.8 crores in the same quarter last year. Revenue from Watch Components business stood at Rs.35.6 crores in Q1 FY'22 as compared to Rs.15.8 crores in the previous year same quarter revenue.

Revenue from Precision Engineering business stood at Rs.10.2 crores in Q1 of this fiscal year as compared to Rs.5 crores in Q1 of previous year.

During Q1 FY'22 the demand from domestic market was subdued as most customer operations were impacted. However, we expect the domestic demand to recover swiftly hereafter.

The demand from Swiss market remained healthy and encouraging and maintains the trend of last few years with declining volumes in the lower price points, while the higher price points have continued to grow strongly.

As I shared in earlier earnings calls also, we are moving up the value chain and catering more to the higher price segment. As the second wave of COVID-19 receded, we have witnessed revival in demand in Q2 and we expect the demand momentum to continue and accelerate in the coming months.

Precision Engineering business, EIGEN during the quarter reported a revenue of Rs.10.2 crores as compared to Rs.5 crores in previous year same quarter and Rs.11.6 crores in Q4 of FY'21. So, there is a slight fall from the previous quarter, but, overall, it is very encouraging.

In Precision Engineering business too, the demand from domestic market was severely affected, while exports market for most of the segments excluding Aerospace have witnessed healthy recovery.

During the current financial year, the company has acquired additional equity shares of ETHOS Limited, subsidiary of the company from some existing independent shareholders and invested Rs.7 crores. The rights issue proceeds have been partly utilized for the general corporate purposes and the balance unutilized funds have been temporarily invested in deposits, cash credit accounts and current accounts. The liquidity position of the company continues to remain healthy and strong.

Estima during Q1 FY'22 reported a revenue of CHF548,000 compared to CHF539,000 in Q1 of last year. EBITDA for Q1 of this year was CHF38,000. This was marginally lower than the last year, as the government's support for employees on unemployment account was lower in this year. Estima reported a loss of 61,000 during the quarter. We remain confident that in the coming period with normalization of market conditions, we will again witness healthy growth and Estima already is back on track for growth and profitability.

Now, let me discuss our Watch Retailing business, ETHOS. As I mentioned earlier, despite our retail stores been closed for a significant period during Q1 FY'22, we were still able to perform very well. During this period, many of the stores had to be shut down or operated for limited hours during the months of April, May and June. To give you a sense of it, our stores were operational for only 35% of the average total time during this quarter. Despite this, we recorded revenues which were close to 90% of what we achieved in Q1 of FY'20, which means the period that was marginally impacted by COVID, we came to 90% of that, despite stores remaining open only for 35% of the time.

The lockdown restrictions have started to ease in the month of July and August. Even during the first half of August, all stores were not operational, especially as most of Maharashtra was still under lockdown. These stores have opened recently and now we are hoping for a very strong festival season in recovery and we are poised to grow with it.

One of the most important factors which have led to a strong business recovery is our effort on building our digital capabilities. This has also been aided by the COVID-19 pandemic which has generally resulted in more fillip to digital segment. Having a well-established digital presence has yielded a strong results during this time, we recorded a highest ever quarterly billings due to online leads at Rs.43.6 crores in Q1 of this year as compared to Rs.17 crores in Q1 of last year. Online billings contributed a significant 42% of the total billings in Q1 FY'22.

Although sales will recover strongly from our retail channels as well, we expect digital presence to be an important focus area for us for our growth and profitability.

The omni-channel strategy that we have adopted is vital for our luxury presence and it will lead with the customers' offline as well as online in a seamless and very contemporary manner.

We have been able to significantly improve our stock carrying months from 8.7-months in June '20 to 6.8-months in June '21. This improvement has been on the back of careful planning of inventory. In addition to this, we have negotiated with landlords to obtain relief on rents during the quarter and we expect to obtain more relief in the coming few months. Post our last announcement, we have added two new stores in Delhi and closed one store in Navi Mumbai.

Let me now give you Financial Highlights of ETHOS for Q1 FY'22. I would also in this give a comparison with respect to Q1 FY'20 which was a normal pre-pandemic quarter to give you a sense of business recovery. Billing for Q1 FY'22 stood at Rs.104 crores as compared to Rs.32

crores in Q1 of FY'21 and in Q1 FY'20 it stood at Rs.118 crores, so, we are back to 90% of pre-COVID times despite the huge lockdown in Q1 this year.

Consolidated total income increased to Rs.94.1 crores. This compares with Rs.102 crores in Q1 of the pre-COVID year. Consolidated gross profit was Rs.30.4 crores and in Q1 of the pre-COVID year it stood at Rs.30.5 crores. So, in terms of gross profit, we are back to pre-COVID level despite the lockdown this quarter. Gross profit margin stood at 32.3% as compared to 29.9% in Q1 two years ago, that is a pre-COVID year. Consolidated EBITDA stood at Rs.11.9 crores compared to Rs.12.1 crores in Q1 of FY'20 the last pre-COVID year. EBITDA margin stood at 12.6% as compared to 11.9% in Q1 of FY'20 two years ago, the pre-COVID year. So, EBITDA margin is actually higher than pre-COVID time. Consolidated PAT stood at Rs.0.8 crores as compared to a loss of Rs.10.8 crores in the last year same quarter and compared to breakeven of Q1 two years ago. Stock at the end of June quarter was Rs.183 crores lower by Rs.15 crores compared to the stock level at the end of March 2021.

As our financials are impacted by IND AS 116, adjusted financials are published in the presentation where you can have a look.

I do wish to add some comments on our important growth business which is a pre-owned watch business. As you know, this business is being run through our website, secondtimezone.com. The website has been witnessing increasing visitors in the recent months. It is the largest platform by far for pre-owned watches in India, and we believe pre-owned watch business in the long-term has immense potential to scale up very strong profitability as well.

I am very pleased to share with share that out of the two new stores we have opened, one of it is launched for Second Time Zone in Delhi. We aim this to become the most trusted and transparent omni-channel platform in India for trading in pre-owned watches.

Apart from this, all our ETHOS stores will become touch points for Second Time Zone. We will not stock or trade or sell pre-owned watches because we want to keep the two businesses separated for customer touch points, but we will facilitate interaction with customers who wish to trade in pre-owned watches through our ETHOS stores as well.

We are investing in this business to build an ecosystem, which will become one of the important growth drivers for our company in the future.

The pre-owned business is not a simple business because we need a team of experienced watch experts, who have the ability to rightly value the watches, authenticate the watches, and repair the watches first to be able to give a credible warranty on the watches. As you know, trust is the cornerstone of everything we do.

As we move into the season period, and there are reports of an imminent third wave of the COVID pandemic, we are convinced that we are better prepared to face any challenges that may come up.

Robust recovery of consumer demand, strong digital presence and a comfortable liquidity position allow us to be optimistic of the overall performance of the company in the coming future.

I now welcome your questions and participation.

Moderator: Thank you very much. Ladies and gentlemen, we will now begin the question-and-answer session. First question is from the line of Amit Shah from ACE Securities. Please go ahead.

Amit Shah: My first question is how many stores you plan to open and close during next one year in ETHOS? My second question is, what can be the sustainable EBITDA margin you can expect for ETHOS business? What is the gross debt? in manufacturing and in ETHOS? Also, if you can give us cost of debt?

Yashovardhan Saboo: So on the store opening and closures, I estimate that in the next 12-months we have quite a few openings. In fact, some stores which were meant to open in March and they are ready for example of a store in BKC in Mumbai, that is now slated to open in September. So including that, I think we will have as many as five to six stores openings in the next 12-months. And many of them are new projects which have been scheduled and postponed. There will likely to be one or two closures. We have not yet decided that because it depends on the negotiations with the property owners, whether we can get an option of an early closure, but we foresee one or two closures in the next 12-months. Sustainable EBITDA in ETHOS? Our goal has always been an EBITDA of 10% in ETHOS. I believe we had a gap in these last two years, but we are now on the way to achieving that goal of EBITDA 10% over the next two to three years, every year we will see an improving EBITDA until it hits about 10%. Gross debt of KDDL and ETHOS, I'm going to let our respective CFO answer this and also the cost of debt.

Sanjeev Masown: Amit, the gross debt at KDDL is around Rs.65 crores and the consolidated debt if we look which is a combination of all manufacturing and retail, it's around Rs.150 crores. Our cost of debt is varying from 8% to 10%, mostly, the unsecured debts are at a high cost, but the average you can take around 9%.

Ritesh K Agarwal: The gross debt for ETHOS was Rs.56 crores and the cost of debt varies between 8% to 10.5% So on an average it would be close to 9% 9.5%.

Moderator: Next question is from the line of Vikram Suryavanshi from PhillipCapital. Please go ahead.

Vikram Suryavanshi: One question regarding consolidated other income. Was there one off in this quarter or what kind of sustainable other income we can see if you can comment on that? It was around Rs.5.7 crores this quarter.

Yashovardhan Saboo: Mostly, I think in ETHOS, that is because this expediency that we are taking for rental relief, it is now showing up as other income. And this is the relief that is showing up for the agreed and confirmed relief for the entire year is taken as benefit as other income in this current quarter. So, of course, this is not something that you can project at the same level going forward. It will be there in the next quarter also, because some of the malls we have not yet reached an agreement on rental relief. As and when the agreement is reached, then it will show up as other income. So, that is the main cause of that.

Vikram Suryavanshi: In case of manufacturing, how is the impact of this inflation in raw material in terms of margin, because we have seen a bit amount of correction if you compare to fourth quarter, obviously, it is not comparable, but trend looks that we have some impact in terms of margin in manufacturing, obviously, you commented that domestic is not doing good, but if you can highlight on margin expectation or how that business can recover in terms of profitability?

Yashovardhan Saboo: Of course, on the cost of raw materials, we do see an impact. However, typically, raw material cost in our manufacturing business tends to be on the lower side. So while the impact is there, it's not a very serious impact. And we are now in the process of negotiating prices with our customers to be compensated for this pricing in the inputs. The impact on the margin that you see is more because of product mix changes, which are a bit exceptional in this period where some of the higher margin production was impacted more than the normal margin production. So that is due to a change in the product mix. And this is not a permanent thing and you will see a reversal of this in the months to come. Overall, our trend in terms of margin on manufacturing will pretty much continue as it is. This is a temporary product mix change. We already see this correction happening.

Vikram Suryavanshi: And some book-keeping questions on ETHOS side. What was the revenue from exclusive brands in terms of growth and how many number of brands actually currently they have?

Yashovardhan Saboo: The revenue from exclusive brands was pretty good; it was Rs.33 crores and I think in terms of percentage, it also is at a very good healthy level of about 32%. So it's going above our long-term sort of trend line on our target for exclusive brands

Vikram Suryavanshi: Is there any change in number of exclusive brands or a total number of exclusive brands currently we are factoring for this Rs.33 crores revenue?

Yashovardhan Saboo: There is no change, there is no brand that has been dropped. So I don't think there is a change. In this quarter, I don't think we've added any, although I do know that some new exclusive brands, agreements are under discussion and hopefully, we will be able to finalize a few more exclusive brands in the coming months, and I'll be able to share this information when that happens.

Vikram Suryavanshi: If you can share that repeat sales as well as same-store growth?

Yashovardhan Saboo: Same-store growth against last year if I compare it, there is a growth of 246%. Last year is not really comparable. Compared to previous year there is a decline in same-store growth of minus 18%. I think the repeat sales percentage pretty much remains steady at about 32%.

Moderator: The next question is from the line of Avadhoot Joshi from Newberry Capital. Please go ahead.

Avadhoot Joshi: Two questions. First, about the stock carrying months which have come down which is really appreciable. Now, going further into footfalls or increasing and we are planning to open five to six new stores, so how do we maintain the stock carrying months at this level or what's the plan going further? Second question about the Second Time Zone. As sir mentioned, that could act as touch points for ETHOS. So what's our strategy over there and have we been able to move our customers from Second Time Zone to ETHOS in a way in the past that I would like to know?

Yashovardhan Saboo: As the demand is increasing and we step on the growth pedal again, I think the stock carrying months will go up because the stock come before the growth comes especially as they are going to add some more exclusive brands so the stock is going to go up. There is one more reason why the stock is going to go because we anticipate shortage of stock of the best-selling brands. So because of logistical reasons and other reasons, many of the best-selling brands have actually limited their production and availability for India as well. So, we are anticipating some difficulties in getting the stock over the next couple of months because we anticipate a very robust recovery, our strategy is to try to stock up as much as is reasonable so that we can capitalize on the demand growth. So I think some stock will increase in terms of carrying months going forward. However, overall, we do believe long-term trend is towards improving short term and reducing the stock carrying months. Coming to Second Time Zone and its impact on ETHOS and vice versa, so you see what happens is actually it's a very symbiotic relationship, they both help each other. I'll explain to you how and it's very easy to understand. When a person comes to buy a watch, if at that time the salesperson ask the person “Sir, are you also interested to sell any watch that you might have got which you are not using or you're not fond of?” So person will come to buy the watch is very happy. And he says, “Yes, I might be.” Many of them say, “Yes.” Then they engage with the Second Time Zone team and they get a good deal. If they get a good deal for their watch, what it helps ETHOS to do is to sell up. So let's say someone came with a budget of Rs.3 lakhs to buy a watch, but now he can sell a watch for 1 lakh or 2 lakhs, he will immediately think, yes, okay, maybe instead of buying the season gold watch, maybe I can buy the full gold watch at Rs.5 lakhs, I'll get a much better deal. So it helps very much to upsell. So this is how Second Time Zone helps ETHOS. How ETHOS helps Second Time Zone, of course, is by its contact with so many different customers and to give them the ability to connect with Second Time Zone. So both are helping each other and it's a symbiotic relationship. And I want to add this also that for this to really have scalable benefit, the business has to be a certain minimum scale. Now, if ETHOS is present in 16 different cities with 50 different stores, you imagine the touch points and we can reach and touch customers in every part of the country. Besides that, we have a large range of new watches and a huge inventory also of pre-owned watches in addition to the contacts. Now, compare this with one single retailer in some city, who may also want to deal in pre-owned watches. He will have fewer watches and he will have restricted geographical region and of course no digital presence. So, success in the pre-owned business, whether it is for watches, whether it is for car, whether it is for any product, depends on scale and digital presence. And that is where we are going to score above everybody else.

Moderator: Next question is from the line of Deepan Shankar from Trustline PMS. Please go ahead.

Deepan Shankar: Firstly, wanted to understand the outlook for watch components manufacturing. So is there any active discussion with the Swiss watch makers with regard to China plus one kind of strategy? On ETHOS, are we expecting very strong demand recovery during Q3 and Q4. And we had fantastic quarters in the previous year also. So are we expecting growth over that base as well?

Yashovardhan Saboo: Short answer to both your questions is "Yes." In the manufacturing, yes, Swiss brands are interested to, let's say shift or to hedge their risks and not rely only on China. So they are looking at India and they are looking at Switzerland buying more in Switzerland itself. And in ETHOS, as I already mentioned in my speech, we are expecting and preparing for a robust recovery in Q3 and Q4.

Moderator: Next question is from the line of Ronak Jain from Jain Capital. Please go ahead

Ronak Jain: I have three questions. Firstly, can you give any guidance in terms of revenue and EBITDA for ETHOS business for next couple of years? Secondly, at what valuation you've been buying shares of ETHOS from the shareholders? And lastly, is there any update on demerging ETHOS business from KDDL?

Yashovardhan Saboo: Ronak, we are very optimistic on long term outlook for ETHOS. And if this recovery is not hindered by any other surprises, we expect to be able to reach our goal. And our goal actually remain unchanged, it was to do Rs.1,000 crores of billing at a 10% EBITDA. And this was actually meant for FY'23, but since we lost now two years because of COVID and half a year because of 2019 because of other disturbances, we do expect still to be back on track, and to be able to achieve close to this around FY'25 at least come to the rate which will imply Rs.1,000 crores billing and 10% EBITDA. And this is not going to be a one shot increase, there's going to be a steady increase that we'll see from hereon. As far as the purchase rate is concerned, I think you know that it is a matter of record that KDDL purchased shares at a rate of Rs.250 per share and last purchase was a little bit lower from a shareholder who wanted exit. So, we believe it was an extremely good deal for KDDL to get ETHOS shares at that rate. Your last question was on the demerger. As you know, the difficulty has been the fact that SAIF Partners holds a significant shareholding in KDDL and demerger would require them to get shares in ETHOS but since that classifies as FDI, it is impossible to allot shares to them. So consequently, it's impossible to do a demerger while SAIF is still a shareholder of KDDL. Now, over the last 24-months, we have looked at several options, and a demerger in the classic sense doesn't seem possible unless we can persuade SAIF Partners to exit. So that is one of the routes that is, of course, has been under discussion. And the other route which has come under discussion is to look at other possibilities for listing, ETHOS by way of an IPO. These are again thoughts that are now being considered, and we believe we will come to some kind of a clear direction over the next few months.

Moderator: The next question is from the line of Pratik Poddar, as an individual investor. Please go ahead.

Pratik Poddar: Yes, hi, a couple of questions. One is, if I look at your presentation, one of the slides mentioned that in Q1 FY'20, the sales for ETHOS was roughly around Rs.100-odd crores and this quarter we had done Rs.90 crores and the EBITDA margins have gone down from 12% to 3.3%. So maybe you can help me understand where the bridge? Secondly, just on ETHOS, how much is the CAPEX requirement…

Yashovardhan Saboo: Rs.100 crores to Rs.90 crores I know compared to pre-COVID year. What are you saying from EBITDA margins?

Pratik Poddar: From Rs.12.1 crores to Rs.3 crores as per slide 25. So that's question number one. Second is just on ETHOS, how much is the CAPEX per store generally when you set up an ETHOS store and what kind of asset turns or revenue does that generate for you on a steady-state mature basis right? And similar economic if you can give me for Second Time Zone? If I may add, look, this quarter if I see your standalone results, the margin compression on a quarter-on-quarter basis is quite substantial. If you can help me understand what happened over there? There are four questions.

Yashovardhan Saboo: Let me first answer a question regarding CAPEX. So CAPEX on a store depends very much on the format of the store. So if you've been following earlier calls, we have multi-brand formats which are in the size of 800-to-1,000 sq. ft., these are fewer now as we are tending more towards larger stores and flagship stores and we're also doing mono brand boutiques for very high end luxury brands. Typically, on a multi-brand store of 800 to 1,000 square feet, the CAPEX would be about a crore and a half, could be a little bit less, could be a little bit more, but it could be above that. And this store would do a turnover of depending on the brand mix, it could do a turnover of about Rs.10 crores to Rs.12 crores in the first year, let's say six to 18 months,. On the other hand, a super flagship store or a flagship store, it could have CAPEX of as much as Rs.2.5-to-3 crores, the size of the store would be commensurately larger, could be 2,500-to-3,000 square feet, but then the turnover on that store goes up, could be as much as Rs.20-to-30 crores in the first year. That said, the big advantage of a flagship store is that the same-store growth is sustainable for a far larger period in a flagship store than a smaller store. The third format, mono brand boutiques, which can be typically of the size of 400, 500 going up to 800 square feet depending on the plan. And here the CAPEX can be about a 1 crore, 1.5 crores, and in some cases it is shared with the brand, in some cases it is not depending on the brand. And again, depending on the brand, the turnover could be anywhere between 8 to 10 to 15 crores per year. On the Second Time Zone, we've just done one store. We don't intend to do multiple stores for Second Time Zone. It's largely going to be a digital-led format, probably with one lounge in Delhi, which is already there, and one lounge in Mumbai, perhaps one more lounge coming up in Bangalore over the next two to three years. So we don't see any significant CAPEX in Second Time Zone. Largely, the investments are going to be to create a very vibrant digital platform for the Second Time Zone stores. You had another question, which was relating to the comparison of slide #25. We will have to get back to you

Pratik Poddar: Lastly, on your standalone operations, slide #5, if I look at your revenue on a sequential basis in standalone profit and loss is down 8% on a quarter-on-quarter basis, the EBITDA margins from 24.2% have become 16%. The gross profit is down just to 11%. I am just trying to understand what's happening over here -- is it a mix change or what is really adding this kind of sharp compression in margins?

Yashovardhan Saboo: I think this question came up. I get the question now. It is largely a mix change, because some of the more profitable segments with higher margins were more impacted during this quarter than they were in Q4.

Pratik Poddar: And this is coming back, right, that is what you said previously.

Yashovardhan Saboo: Yes, it will.

Pratik Poddar: One thing which I notice, you don't have an app, right… do we have an app on the Play Store?

Yashovardhan Saboo: For ETHOS an app is under development. We had developed an app. So, our strategy is that when we come out with an app, which should happen over the next eight to nine months, it's going to be really state-of-the-art. We do believe that 90% of business is going to happen through mobile platforms. And therefore the configuration and the capabilities of the app are critical. So that's something that we are working on. An app has been developed, but it was abandoned, because we believe that it is not really going to achieve what we wanted it to. So you're right, an app is extremely important in the future and it's work-in process.

Pratik Poddar: You talked about asset turn on the various three types of formats. Just a broad indication of EBITDA margins which we can achieve in all these three formats, the MBO, the big format stores and the exclusive store?

Yashovardhan Saboo: See, eventually, the EBITDA margins tend to pretty much go at the same level; however, as I mentioned, it will be a little bit lower in the mono brand boutiques, because we have to follow some principles and rules laid down by the brands; however, there's a huge strategic value to mono brand boutiques because of two things; number one, it cements a relationship with the brand, also for your multi-brand stores; and second, most importantly, it gives you access to some limited edition and hard to find pieces of that brand. The price that you pay for this strategic advantage and long-term advantage is a little lower margin. That is one aspect. And whether flagship stores or multi-brand stores, the EBITDA margin depends on much more on the brand mix that you have in the store, and sometimes the brand makes may not be entirely up to us, because it depends on which brand is willing to be present in a flagship store in which city. So it depends much more on that. But the main point, which I want to say is that the EBITDA margins improves over time and the same-store growth happens to be much more sustained and longer in flagship stores. So over the lifetime of a store, a flagship store will deliver much higher ROI than a normal multi-brand store.

Pratik Poddar: Given COVID wave-2 and achieving 90% of pre-COVID level sales is a phenomenal performance. Just wanted to understand how was that achieved? And secondly, in the month of July, a lot of other peers not in the same industry, but in retail per se have reported July to be far higher than even pre-COVID levels. Are you also seeing that?

Yashovardhan Saboo: July recovery is actually we see the same thing and we hope we can surprise everybody with Q2 results, while Q1 was good. When we started Q1, we were extremely afraid because the lockdown and the mood was so much worse than April last year, if you remember April last year, there was a full lockdown, but there was a mode of masti, right? there was no scare. Q1 this year when we started April, there was not a single family that we didn't know which was not impacted by COVID. In our own team, in our own stores, people were not only impacted, but people lost friends and family members. So the mood was extremely dark, very pessimistic, and we were extremely afraid how this quarter was going to turn up. What we were confident was having gone through six months last year, having a strong liquidity position, having a strong stocking position and a strong digital network, which continue to engage despite COVID last year, we knew that it was not going to be an existential problem. We didn't expect it to last six months. So we started Q1 in a very anxious way. However, as it went along, after two bad weeks of April, we saw the recovery happening and here I have to give credit to our sales team, our front end team, our merchandising team. Despite all that COVID was throwing at them, they went around, they attended to work, and they work from home, as soon as lockdowns opened, deliveries were made, and people went to houses people went to offices to deliver. And I think all of this put together, which has led to this great top line performance. Of course, it was helped by the fact that we announced very, very encouraging incentive schemes for the staff. We had an appropriate stocking. Investment in marketing was increased. The networking was increased. I think a lot of things came together. I don't want to take all the credit, and the end shakes out this COVID thing. Wedding started to happen again, and gifting started to happen again. So I think Indian consumers are also saying that look, get back to living. So I think it's a bit of everything and we're seeing the same thing, same with a better impact in July.

Pratik Poddar: Lastly, sir, just some comments on ETHOS on the trajectory of employee expenses and other expenses. Will there be further increase from here on? I'm saying ex of store increase. If you increase the store, you will have commensurate increase in cost and income, ex of that, but on your base business of Rs.46-47 crores.

Yashovardhan Saboo: Yes, there will be an increase in personnel costs as our network increases and sales increase. However, I think personnel cost as a percentage of sales will continue to steadily decline, it's not going to be a sharp decline, but as we get more operating leverage, I think that is going to happen.

Lalaram: Lalaram here. Firstly, I have some data points. So I will just quickly ask those; one is what is the gross profit from exclusive brands in terms of absolute amount, INR crores? Number two is the square feet at the end of quarter for ETHOS? Number three, what are the sales of pre-owned watches in this quarter? Fourth is did I hear it correct that we are now open to the possibility of direct listing of ETHOS via IPO and maintaining as a subsidiary of KDDL, that demerger and vertical demergers and shareholding is not possible. So, the point being, are you open to direct listing of ETHOS via IPO as a subsidiary and maybe exposing ourselves to a holding company discount, and which we will do unlock the value. Then, the other question is, when compared to the pre-COVID quarter, we are saying that we were only open 35% of the time. However, when I look at the OPEX, broadly, it is same what was the pre-COVID quarter? So, does it mean after the concession also, rent and maybe employee expense spend, they are like back to sort of normal steady state? Then on the rent concession which on the other income that you mentioned to a gentleman from PhillipC**a**pital, this other income was owing to rent concession. But I believe that we also have some part of that in revenue side, where if you compare the old accounting with the new accounting, there is a difference of Rs.4 crores, 90 crores versus 94 crores, that Rs.4 crores, I believe, is also due to some of the rent concessions which you are getting, which we are basically showing as income. So, want to understand, are those two things different or we double counting that, I'm not going to very clear on that, so, maybe the CFO of ETHOS can help me understand, that would be helpful.

Yashovardhan Saboo: I'm going to tell Ritesh, CFO of ETHOS to answer these queries, and Ritesh has just joined, if he is unable to answer some of them, we'll get back to you on that.

Ritesh K Agarwal: Lalaram, I have tried to capture your question. So, if you can go one-by-one, I can answer you.

Lalaram: The first one was I got the sales mix of between exclusive brands and normal brands. I wanted a similar split for the gross profit.

Rakesh K Agarwal: Gross profit on the exclusive brands definitely would be on a higher side, because that is our key strategy where we drive and the gross profit for the house brand goes close to around 40%, whereas the other brand is a little bit…

Yashovardhan Saboo: You want the numbers in actual rupees crore, right?

Lalaram: Yes, that's what we used to give historically, correct, the absolute number in crores.

Yashovardhan Saboo: Gross profit of exclusive brands in rupees crore, I am not sure if we gave that but let me share that with you offline because there is a certain gross margin on house brand that happens, which is about 40% of net sales and the billings of house brands has been about Rs.33 crores but billings on to net sale, so we'll have to do that arithmetic and get back to you on a more precise figure of gross profit on exclusive brand in rupees crores.

Lalaram: We can do that offline. Second question was, what is the billing for the pre-owned watches in this quarter?

Yashovardhan Saboo: So billing for pre-owned watches is about Rs.3.5 crores for the quarter.

Lalaram: So, it seems that the number has stabilized between Rs.3 crores and Rs.4 crores. I believe…

Yashovardhan Saboo: That's not true. You have to understand that the business of pre-owned watches cannot continue in a pure digital sense, because the pre-owned watch needs to be purchased for which you cannot have a lockdown. And then that watch to be examined and repaired, and re-warranted for which we need our service centers to be open. And the service center was under lockdown in Delhi for all of April and May. So, you cannot say that it has stabilized at this level. In fact, we are still projecting that our pre-owned business for the year will be more than 3x of the pre-owned business of last year.

Lalaram: And what was last year, sir?

Yashovardhan Saboo: Last year was just short of Rs.12 crores. I am estimating that, again, everything is with the proviso that there are no future lockdowns and disturbances, but I'm hoping that the pre-owned business will clock up to close to Rs.40 crores this year.

Lalaram: And in the previous quarter, I think I had asked that. This business can easily touch Rs.100 crores revenue run rate, that's what you had said. So, do you think this is possible within say two to three years?

Yashovardhan Saboo: Yes, it is.

Lalaram: And that is possible with only say three physical stores in Delhi, Bombay and Bangalore?

Yashovardhan Saboo: Yes, it is.

Lalaram: That's wonderful. That's good to hear. So, also want to understand some more color on this business. How different is it from the new watch business? And what kind of impact will this have apart from topline on the business in terms of P&L, balance sheet that would also be very helpful if you can comment there?

Yashovardhan Saboo: On this I can only get very little comments because it's a related business, but in many ways it's a different business, and in general, I can comment that there is a strong symbiotic relation between sales of high end new watches and trading in pre-owned watches. The closest analogy I can give is with art. If you're an art collector, you know that there are original works of art. But if you know that there is a good resale value of this, you will invest more in that and you will keep it longer. That is precisely how it works for collectors' pieces and some of these very, very high end watch pieces. People buy them knowing that there is a resale value and if there is a good resale and residual value, which in some cases may be more than the purchase value, that helps to sustain the interest and passion for high end watches. So what I would request you to do, if you want to understand this business more closely, is visit some of the auction in internet sites for watches and we did some of the watches where international websites for pre-owned watches. Watch Boxes is one of them, and there are two or three others which I can share with you. But if you go to pre-owned watches, and you go to the best website, you will see and especially on the auction site. So many of the values that pre-owned watches are getting several, several notches higher than the original price of the watch. And that is the real direction that this very high end business is taking. It's becoming like a collector's market with high end purchases and sustained value. In fact it is becoming like an alternative investment group.

Lalaram: So also what is our typical turnaround time someone comes with a watch, I want to send this watch, what is the time you take to give an estimate of the price and maybe all the negotiations and what is the typical….

Yashovardhan Saboo: All our watchmakers are there and the service center which is required to assess the watch. It depends on the type of watch. If it's a complex watch, which requires a lot of refurbishment, then it could take as long as three to four weeks. If it's not that, it could be done in a couple of days. Lalaram, we are focusing on watches at a price point of Rs.1 lakh and Rs.2 lakhs and more. We're really not diverting too many resources to sell pre-owned watches in the segment of Rs.20,000, Rs.30,000.

Moderator: Next question is from the line of Aditya from APSK Advisors, LLP. Please go ahead.

Aditya: We are very bullish on the luxury segment play in India. ETHOS fits this frame perfectly. But now that there won't be a demerger, how do the minority shareholders of KDDL benefit if ETHOS come down with an IPO? In your previous calls, you've been saying that minority shareholders will be taken care of. So, just wanted to know on that front.

Yashovardhan Saboo: Again, I think my comments have perhaps been misunderstood. We are examining every possibility that exists if demerger is not possible. Currently, the possibility of a demerger with SAIF Partners still invested, is not possible due to the current legal position. If the laws would change and would allow FDI to participate in a multi-brand store network like ETHOS, of course, that is possible or if SAIF Partners would agree to exit, of course, that is possible. So, perhaps, we will have an investor who will come and give an exit to SAIF Partners at a price which they will agree to exit at. However, if that doesn't happen, then a demerger is not possible because of the legal constraints and we have looked at every possibility and talk to experts across the length and breadth of the country and everybody has come to this conclusion. Of course, there is the option of an IPO which has been discussed. There are advantages and there are disadvantages are known. But no decision in this respect has been taken.

Aditya: Since you've discussed with so many experts, what is the percentage that SAIF needs to bring down its holding so that a demerger is possible?

Yashovardhan Saboo: They need to bring it down to zero, because their entire holding is now classified as FDI. That's my understanding of the law and their own understanding as well. There used to be a threshold limit of 10%. But with their second tranche, the entire investment is now considered as FDI and it needs to be brought down to zero.

Moderator: Thank you. Ladies and gentlemen, that would be our last question for today. I now hand the conference to the management for the closing comments.

Yashovardhan Saboo: So with this, I want to thank everybody for joining the call and I hope we've been able to answer all the queries, there are some queries that were left and we've taken note of them and we'll connect offline to answer them. Should there still be some left, please feel free to write to me or our CFO or to SGA, our advisor. Thank you very much and have a nice day.

Moderator: Thank you very much. Ladies and gentlemen, on behalf of KDDL Limited, that concludes today's call. Thank you all for joining us and you may now disconnect your lines.