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Trading Symbol : KDDL

Scrip Code : 532054

Subject: Earnings Call Transcript

Dear Sir / Madam,

Please find enclosed herewith a copy of transcript of earnings call held on 16th August, 2019 to discuss the Operational and Financial Performance for Q1FY20.

Kindly take the same on record.

For KDDL Limited

KDDL LIMITED

Brahm Prakash Kumar
Company Secretary

KDDL Limited

"KDDL Limited
Q1 FY2020 Earnings Conference Call"

August 16, 2019

KDDL Limited

CHORUS CALL®

MANAGEMENT: **MR. YASHOVARDHAN SABOO – MANAGING DIRECTOR – KDDL LIMITED**
MR. SANJEEV MASOWN – CHIEF FINANCIAL OFFICER - KDDL LIMITED
MR. RAJA SEKHAR – CHIEF FINANCIAL OFFICER – ETHOS LIMITED

Moderator: Ladies and gentlemen, good day and welcome to the KDDL Limited Q1 FY2020 Earnings Conference Call. This conference call may contain forward looking statements about the company, which are based on the beliefs, opinions and expectations of the company as on date of this call. These statements are not guarantees of future performance and involve risks and uncertainties that are difficult to predict. As a reminder, all participant lines will be in the listen-only mode and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call please signal an operator by pressing "*" then "0" on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Yashovardhan Saboo, MD of KDDL Limited. Thank you and over to you!

Yashovardhan Saboo: Thank you. Good afternoon and a warm welcome to everyone for our Q1 FY2020 earnings conference call. I am joined by Mr. Sanjeev Masown, CFO of KDDL and Mr. Raja Sekhar, CFO of ETHOS and SGA, our investor relations advisors. I hope everyone has had the chance to go through our updated investor presentation uploaded on the exchange and the company's website. I will start by giving you a brief on the financial performance on a consolidated basis for Q1 of the current year.

Consolidated revenue rose by 4% to Rs.152.7 Crores in Q1 FY2020 from Rs.146.2 Crores in Q1 of the previous year. Standalone manufacturing business witnessed a 9% year-on-year growth from Rs.44 Crores to Rs.48 Crores in the quarter. Our watch retailing business Ethos witnessed a growth of 1% on Y-o-Y basis to clock in revenues of about Rs.102 Crores. Consolidated gross profit grew by 11% Y-o-Y from Rs.61.3 Crores in Q1 of FY2019 to Rs.67.8 Crores in Q1 FY2020. Gross margins improved by 251 basis points from 41.9% to 44.4% in the quarter.

We continue to witness traction in our watch retailing business. We saw a gross margin expansion of 256 basis points on Y-o-Y basis to report gross margin of 29.86%. Consolidated EBITDA grew from Rs.13.4 Crores in Q1 of FY2019 to Rs.18.1 Crores in the current year same quarter. The growth in EBITDA has been largely on account of change in accounting standard with the applicability of Ind-AS 116 standard. The new Ind-AS 116 norms have resulted in recognizing right of use assets of Rs.88.6 Crores in the balance sheet and corresponding lease liability on the liability side of the balance sheet. This had resulted in the decrease in rent expenses to the tune of Rs.7.7 Crores from other expenses and an increase in finance cost by Rs.2.4 Crores and an increase in deprecation by Rs.7 Crores. The net impact is a decrease in PBT by Rs.1.7 Crores. Adjusted for this Ind-AS 116, the like-to-like EBITDA stood at Rs.10.3 Crores versus Rs.13.4 Crores in Q1 of the previous year. The margins stood at 6.8% versus 9.1%. Profit before tax for the quarter stood at Rs.1.5 Crores. The increased depreciation has resulted in an impact on overall profitability and therefore we would like to focus on cash PAT, which has grown at a healthy 38% on Y-o-Y basis from Rs.8.2 Crores in Q1 FY2019 to Rs.11.3 Crores in Q1 FY2020.

Our consolidated performance includes the performance of Estima, our newly acquired hands manufacturing company in Switzerland. This company incurred a loss of about Rs.2 Crores in Q1 FY2020.

I will now discuss the manufacturing business for the quarter and the full year. Our manufacturing business segments of watch components, Precision Engineering and ornamental packaging continues to grow as per expected plan. Our standalone manufacturing revenue grew 9% Y-o-Y from Rs.44.3 Crores in Q1 FY2019 to Rs.48 Crores in Q1FY20. The share of watch component business was 73% and precision engineering contributed 22% of the revenue. The gross profit expanded by 6.3% to Rs.35.6 Crores from Rs.33.4 Crores in Q1 FY2019. The gross margins stood at a healthy 74%. The EBITDA grew 1% Y-o-Y from Rs.8.2 Crores in Q1 FY2019 to Rs.8.3 Crores in Q1 FY2020. The margin was 17.3% versus 18.6% in Q1 FY2019.

The lower EBITDA margin profile was on account of product mix wherein the share of newly functional precision and engineering division in the new factory is increasing. After a healthy 2018, the Swiss watch business has slowed significantly. After reporting a 10% rise in the period January to June 2018 on a Y-o-Y basis, Swiss watch exports in the current year in the same period January to June 2019 reported only a 1.4% growth, so that is a deceleration of growth from 10% in the previous year to 1.4% this year. June 2019 was the first month in a long period, which actually saw the watch exports drops by 10.7% on Y-o-Y basis. We expect this situation to continue for some more time. The current turmoil in Hong Kong, which is one of the top markets of Swiss watches worldwide, is having an impact on the performance and this is likely to continue for some time before it will normalize. The Indian watch market though continues its upward trajectory, the leader in the domestic watch business has grown handsomely and we also benefit from this growth on account of our large presence in their supply chain and our dominant position in the watch components in the Indian industry. Accordingly, watch component business witnessed a growth of 10% in Q1 FY2020. This segment registered a revenue of Rs.35 Crores in the quarter compared to a revenue of Rs.32 Crores in the previous year same quarter. We remain on course to delivering 8% to 10% growth in this segment.

At Estima, our acquisition of the Swiss watch hand manufacturing company, we continue to focus increasingly on improving the utilization levels of the factory and we expect a turnaround over the next two quarters. Our strategy with Estima is to build a strong pipeline of customers in the mid price segment of the European watch market. We believe that our own skill sets in watch component manufacturing in India will help us to turn around this business faster.

Precision Engineering business witnessed a revenue growth of 20% over the previous quarter from Rs.8.8 Crores in Q4 of FY2019 to Rs.10.6 Crores in Q1 of FY2020. We are now focusing on improving internal efficiencies and streamlining the product mix of this business to achieve the target profitability. The order book in this segment remains healthy backed by our efforts to focus on focused digital marketing in specific segments and our ongoing participation at leading international trade shows.

Now I will discuss our watch retailing business ETHOS. After reporting a significant turnaround in FY2019 and having established the business model of ETHOS, we are now focusing on furthering our leadership position in India. The current slowdown in the macroeconomic situation in India coupled with the tight liquidity has impacted the sentiment of consumers in our market. We will now focus on the festive season starting late September to see how the situation improves and with it the customer buying.

At ETHOS, we have focused on providing the best customer experience and this has led us to realign our store strategy, which consists of the following main moves. Number one - Larger stores, which are like flagships stores and destination for watch shoppers. We have ventured in new geographies like Guwahati and Kolkata. We have roped in marquee brands on an exclusive basis and we have started the after-sales service network. All this is part of our strategy to consolidate the position of ETHOS as the number one destination for luxury watches across the country. With this strategy firmly in place, we not only occupy a strong presence in the minds of consumers, but importantly also in the minds of our partner brands. At ETHOS, we are clearly playing out on the inherent strength of the business model with which will continue to increase our market share. These include being the largest network of luxury brands on pan India basis. This enables both us and the brand to co-exist and grow together in the market.

The exclusive brand strategy, this is a unique proposition, which continues to play out well and contribute significantly to the growth in profitability of ETHOS. Our digital marketing strategy allows us to make a lasting impact in the minds of the customer for everything in the world of luxury watches. Our enhanced store experience in which we are continuing to invest in the renovation of major stores and the impact on sales of these renovated stores is evident from the performance.

Let me share with you some financial highlights for ETHOS. Our billings in Q1 FY2020 grew to Rs.118.1 Crores that is about 1% growth Y-o-Y. Billings of exclusive brands grew faster at 56.3% Y-o-Y to Rs.28.6 Crores in Q1 of the current year. With this the exclusive brands now contribute 24.2% to the topline in Q1. Our gross profit continues to report stable numbers and comes close to 30%. On absolute basis, there was a growth of 11% on Y-o-Y basis in our gross profits. Ind-AS 116 standard has impacted profitability as I have already mentioned. The like-to-like EBITDA margins comes at 5.2% versus 6.8%. This is lower on account of new larger format store openings in Q1 of FY2020. As the new stores mature and gain traction, we expect the operating leverage to kick in and improve both margin and profitability. PBT was impacted by Rs.1.3 Crores in the quarter on account of Ind-AS 116 and it de-grew by 37% on Y-o-Y basis. The cash profit increased coming in at Rs.7.8 Crores in Q1 this year. Stock carrying month at the end of June 30, 2019 was 8.7 months. This is slightly higher than the previous year as some of the new stores were launched towards the end of the quarter. During the quarter, we opened two stores. We opened our large flagship stores in Hyderabad with a size of 5250 square feet and the presence of many brands, we expect the Hyderabad store to give us excellent growth and brand strength in times to come. We opened another store in Guwahati in East India, which measures almost 1100 square feet. I am happy to announce that we have opened our 50th store in Pune just a few days ago. This is an ETHOS Summit store measuring 2200 square feet. The growth opportunities are immense in watch retailing in India. Our strategy of strong brand relationships, a strong network across India, and a dominant digital marketing focus will help us to maintain our leadership in this market. The support from a dedicated after sales service centre that we have opened in Delhi along with the preowned watches business will further make ETHOS the torch bearer of the luxury watch market in India. I now welcome your questions and participation.

Moderator: Thank you very much. We will now begin the question and answer session. Ladies and gentlemen, we will wait for a moment while the question queue assembles. The first question is from the line of Ritesh Bafna from RB Securities. Please go ahead.

Ritesh Bafna: Good afternoon. Thank you for the opportunity. Sir I have a few questions on ETHOS, during the Q1, we see that ETHOS has shown a bit of a degrowth so what is our outlook for the coming months say for this quarter may be coming quarter or so and further how many total stores do we have currently and how many do we plan to open in the coming times and any new brands that we have added recently or we plan to add that are in the pipeline? Thank you.

Yashovardhan Saboo: Ritesh good afternoon. So it is true that we are witnessing a slowdown in the market and which has had an impact on ETHOS as well. I think this is very significantly also based on the general softening of the macroeconomic condition. If we look at the slowdown in the growth when we analyse it price point wise, we see that the slowdown is almost entirely responsible because of the segment above Rs.5 lakhs, so I will just give you some figures. If I compare quarter-to-quarter that means Q1 of this year compared to Q1 of last year in the segment price point above Rs.5 lakhs, there has been a degrowth of almost 18% whereas in the segment below Rs.5 lakhs, there is actually a growth of 10%. So this clearly shows that while in the segment below Rs.5 lakhs, there is actually a very healthy growth of 10% right. It is compensated by the degrowth in the very high end priced watches, which again is not a surprise because in the macroeconomic conditions that prevail today where it is really a highly discretionary spend at the highest price points people tend to postpone or delay their purchase that is point number one. Point number two, as I had mentioned in the last call one of our strongest brands in our business portfolio is Rolex and currently there is a worldwide shortage of Rolex watches so there is an impact of that also because the number of watches allocated to us in this quarter by Rolex was much less than what we had got in the previous year, so that is one of the reasons.

Ritesh Bafna: Just to interrupt here. I am so sorry. Why is there a shortage of Rolex watches? What is the reason exactly for this?

Yashovardhan Saboo: Well the demand for the watches is more than the supply and as most luxury brands you will know that they are not very forthcoming in increasing supply. Most luxury brands tend to keep a very stable production and supply sort of a calendar or a program. One is because these are complicated watches and very high quality so they cannot really just bump up production whenever they feel like. It requires a lot of skill and a lot of investments and the second also that every luxury brand today wants to avoid a situation that there is a spurt in demand. They increase the production then demand subsides and then those watches fill the grey market and there is discounting everywhere right. So most luxury brands are very comfortable if their products are slightly waitlisted, which is true for Hermes, if you look for their Birkin Bag in Hermes, if you look for the bags of Chanel or any of the top luxury brands, their model is to work where there is always a certain gap between the demand and supply. Demand should be more than the supply. Over the last eight to 12 months the demand for Rolex has gone up a lot. Supply has not been able to keep up and therefore we have seen a certain shortage in the allocation of watches. However, I am very happy to inform that this seems to be correcting. Rolex has also told us that look overtime this will correct and I think over the next one or two quarters this situation will correct itself. That is also one reason why the price point above Rs.5 lakhs has declined a bit. So that is as far as outlook is concerned. It is difficult to say in today's situation how soon the macroeconomic conditions will change. I am quite an optimist from that point of view and I personally believe that in terms of sentiment and in terms of overall vibrancy in the market, I think we have hit the bottom. We are seeing the messages and the moves that the government is making to revive the business. I do not think it is going to revive from one day to the other, but I think over the next one or two quarters, we should see a pretty good revival, so I am quite hopeful that from Q3 onwards we should be back on the growth track.

In terms of number of stores, we currently have 50 stores and we will during the course of the year open another four stores that we will open and there will be two that will be closed down, so we plan to end the year at about 52 stores.

Ritesh Bafna: 52 stores, so the new stores that you have planned to open are these in the tier 2 cities or they will be in the tier 1?

Yashovardhan Saboo: So most of the stores that we are opening now are flagship stores. These are large format stores in tier 1 cities either in the big metros or tier 1 cities and you know few of them are also replacement of existing stores, but with larger flagship stores.

Ritesh Bafna: Got it and on my last question like do you plan to add more brands or are there any in the pipeline that you wish to add?

Yashovardhan Saboo: We have planned a few brands. I think our overall portfolio with exclusive brands I think we have about 20 of them now. I think that is quite okay however as you know we constantly monitor the brands for performance and we believe there is going to be a certain churn. There may be one or two brands that we may drop because they are not performing as well as they should and there may be certain brands that we may add. We feel very strong in our core segment, which is between Rs.1 lakh and Rs.5 lakhs. In this segment, we feel pretty strong. We have a very strong portfolio in fact. We wish to add something in the entry level pricing, which is in the price point between Rs.30,000 to Rs.40,000. That is the price point, which we feel we should add because we are seeing a certain slowdown there and we believe that we should add some also in the very high price segment. Now you may come back and ask me look if the very price high segment has degrown in this quarter why should we be adding more brands in that segment. I believe the degrowth in the very high price segment is a temporary phenomena. Worldwide the overall growth in the high price segments is actually higher than any other segment and we do not believe that in India it will be any different in the long run. This is a short-term correction, which is happening in India not even a correction. It is an aberration because of the sentiment, but we believe adding some brands in the very high end is going to be the right thing to do for keeping a long-term perspective in mind.

Ritesh Bafna: I get your point. Thank you so much for answering my questions and all the best. Thank you.

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

Vikram Suryavanshi: Good afternoon Sir. Sir how was the same store growth in this quarter?

Yashovardhan Saboo: Same store in this quarter was minus 3%.

Vikram Suryavanshi: In the last quarter, Q4 we have some losses from digital marketing division so how was the scenario in this quarter cognition?

Raja Sekhar: In cognition, the losses were not as extensive as they were in the last quarter.

Vikram Suryavanshi: So there are no losses in this quarter?

Raja Sekhar: There were, but it was very minor loss.

Vikram Suryavanshi: So now we are almost like breakeven in that?

Raja Sekhar: No there was not much expenditure that happened. In terms of revenues, cognition is pretty seasonal in terms of its digital revenues from the watch brand. We did not have revenues this time, but there were not much expenditure that we incurred in cognition, so it was not a large amount.

Vikram Suryavanshi: Got it and how is the debt position in standalone and ETHOS.

Yashovardhan Saboo Vikram I just want to add a bit to Sekhar's point. Obviously, we recognize that Q1 is the leanest quarter and number two we know that the macroeconomic situation and sentiment is weak, so there was also a deliberate effort to sort bring down marketing cost wherever possible.

Vikram Suryavanshi: Understood.

Yashovardhan Saboo: We did do the usual June sale, which helps a lot to boost up our sales of house brands or the exclusive brands. Overall, I think we are also implementing in this current situation a pretty serious cost control regime.

Vikram Suryavanshi: Got it and what is the debt position in ETHOS and in standalone as of June?

Yashovardhan Saboo: ETHOS has a debt of about Rs.79 Crores, and in KDDL standalone it is about Rs.65 Crores.

Vikram Suryavanshi: Sir in precision engineering obviously there has been slightly lower growth than what initially we thought of so how is the outlook on precision engineering given our order book is already there so what kind of growth at full year we can look for precision engineering?

Yashovardhan Saboo: Sanjeev would you like to answer that.

Sanjeev Masown: Vikram in the last speech when Mr. Saboo had shared that during the last year we were shifting our facilities to the new location and for some period the operations were disrupted and that is now fully shifted and completely in operation. This quarter if you see the Q1 of the current year we have grown almost 20% compared to the previous quarter. Our order position is good. We are confident of achieving around 25% growth year-on-year for this year.

Vikram Suryavanshi: Got it and are we seeing any favorable order mix where we can see the order or margin improvement in this segment and how is that scenario and we also added some of this electroplating and order capabilities so are we seeing traction in this value added orders?

Sanjeev Masown: Based on our existing capabilities, there are many customers and many more are iin the pipeline. There is a long gestation period for the product approvals especially with the MNC. It takes a longer duration for product approvals and we will see the margins improving gradually. Regarding the electroplating this was mainly to reduce the cost because this was a backward integration only. Now the range of capabilities, which we have there is a good traction from most of the MNCs and the reputed customers. Almost from all the segments there is a good growth, but we are ourselves calibrating and deciding, which customers to focus more and some to decline.

Vikram Suryavanshi: Thank you.

Moderator: Thank you. The next question is from the line of Nikhil Vora from Sixth Sense Ventures. Please go ahead.

Nikhil Vora: Just a couple of things. I just want to get your thoughts on this. One is that as a business we continue to have this challenge almost every cycle turn of market starting to look a bit challenging and so on, so the only way possibly to stimulate that would be to really push our owned watch business, so what has been the progress on that and how fast can be move on that, that was one? The second was on the ETHOS and KDDL demerger can we just have some more light on what the status is on that and the third is on the OEM brands that we are exclusively partners with what has been the experience? How have we been able to materially alter the market share of those brands and thereby have more brands started to look at us more positively and so what is your experience on that?

Yashovardhan Saboo: Sure. Let me start by tackling the last question first. So on the exclusive brands overall we can see how the growth with the exclusive brands whatever we are growing with it is far in excess of the overall growth of the market of let us say Swiss brands in India. For instance just to give you Q1 figures and I think we also reported these figures for the year, but let us just take Q1 figures. Our house brands that is exclusive brands, the billings in Q1 have grown by 55% year on year right whereas the overall Swiss export in India compared to previous year same quarter actually the growth is 1%, so you cannot really compare it because that is sell in and what I am reporting is sell out, but I can say that our growth with the exclusive brand is far higher than the overall growth of the Swiss brand in India. This means that the market share of the exclusive brand in India is growing faster. Why is it reflected let us understand this also? Now the house brands as a percentage of our business last quarter was 24%. In the Q1 of the previous year, it was 15.6%, so in our business in our larger business it has grown. Our business itself has grown let us say slightly better or similar to what the overall business has grown, so both these facts and numbers indicate that the share of house brands in the Indian market is growing. The house brands are growing faster than the rest of the market, which is a good sign because this is what gives the house brands confidence. Another sign I can tell you some of the house brands now are coming up for renewal. This was a strategy that we started about three or four years ago and you remember a lot at that time there used to be a question how long are these contracts and I had mentioned that contracts are typically for between three, four or five years, but I had no doubt that if we perform well all the contracts will be renewed unless we did not want to renew them because in the nature of the Swiss business they do not want to change partners when everything is going well. I am happy to report that wherever the discussions are now coming up on renewal most of the brands, I cannot think of any brand right now which is saying that no I do not want to renew, so that is another indirect qualitative indication that actually the brands are very happy with the progress that we are making with the brands. Are there other brands who want to sign on? Yes of course. There are. We ourselves have to be a little careful with how many brands we sign on. Let me explain why. Currently we have about 20 exclusive brands. We are going to prune down a few and we are going to add a few especially in price sensitive segments where we believe there is need for strengthening, but we must also understand that every exclusive brand with us must have a certain minimum size. It must be at least 1% of our business ideally 2% of our business because if it is less than 1% or 0.5% of our business, it is difficult to focus on that brand. It is too small to get the attention that it deserves. Also it must be a significant part of the brands business otherwise they do not get the attention that they need, so we are growing this business at a pretty rapid click, but we also need to be sure that over the next two to three years each of these brands becomes a certain minimum business for us and a certain minimum business as a percentage of the business of the brand that is when we are locked into a real win, win partnership. That is the strategy we are very conscious of these two elements, but as I said we will be expanding brands and we are already at the business in this quarter house brands will be 24.6%. That is actually well ahead of our target for the year, so we are very confident that our target for the year is about 20% to 21% of our business coming from house brands. We are actually well ahead of that target.

Nikhil Vora: Yashovardhan given that obviously we have done exceedingly well for exclusive brands does it mean that our ability to monetize these relationships become lot stronger beyond the tenure of the brand distribution that we have? Does the margin increase disproportionately beyond a scale?

Yashovardhan Saboo: Nikhil I am not sure how much room there is for further gross margin expansion because in many cases we are close to the best they provide anywhere in the market and so therefore I am not going to sort of count too much on the margin expansion of these brands. I am counting much more on the overall margin expansion due to increase in the proportion of these brands. With that said in some cases, so let me give an example. In some cases we get a gross margin of more than 50% on the MRP. This is after paying 23% of import taxes and after paying 18% of GST. These are extremely hard to get margins of more than 50% to 52% on this because in addition to that we also asking for marketing spend and we also ask for marketing contribution and participation in incentive schemes and so on and so forth. On the other hand there are some brands where there is certain I think there is some ground for improvement especially brands that we have signed on recently. They know what we have promised, but we still have to deliver on that promise. Over the next one or two years when we deliver on the promise whether we can negotiate slightly better terms or significantly better terms, yes, I think it is possible, but these would be rather exceptional rather than the rule for the house brands. Of course what we get as additional margin because the share of business increases of these brands. That is what we are counting more on.

I get back to your point regarding the demerger and the restructuring. This matter in fact as recently as the 14th we had a very long discussion on this in the board meeting at KDDL. Essentially as you know because of the fact that Saif Partners investment in KDDL is FDI, which we were informed was earlier not the case, but now the legal opinion provided by Saif Partners says it is FDI and therefore while Saif Partners is a shareholder of KDDL we cannot really list ETHOS directly unless Saif Partners either is able to transfer those shares to a domestic entity, which we have suggested to them or they actually disinvest. Now in the light of that Saif Partners have suggested we continue to examine the option of a structure where the businesses are demerged and the retail business is put under a separate entity. It is put as a subsidiary of another entity, which will be an operating company, which will allow FDI, but as an operating company it will still be allowed to invest in a multi-brand retail business. Obviously, this structure is not as good as the structure of direct listing because it will not entirely eliminate the hold co. discount that we know is a reality, but under the current circumstances, with Saif being there, this seems to be the only structure. This structure itself has some questions because when this structure is done how the debt of KDDL will be divided between these two companies. Will the new company be able to provide the necessary collaterals? Currently the debt of ETHOS is guaranteed by

KDDL, but when they become independent companies can those guarantees continue. Will the shareholders of KDDL under the revised conditions agree to continue with the guarantees on behalf of KDDL? I think these are all the questions, which have come up in the board meeting. These are identified by KPMG as well and we have told them to find us what are the ways around these both for the financing as well as for the other question. There is a third question that I should flag up here because it was also being discussed is that in the hold co. structure there will have to be some operations in the hold co. The operations would obviously have to be small operations because you cannot take the manufacturing operations of KDDL and pack it in that because then you are back to square one. When you pass some operations in the hold co. what should be the relative size of those operations compared to the size of the downstream operation that is ETHOS, so the ETHOS operation let us say it is going to become Rs.1000 Crores, will an operation of Rs.5 Crores to Rs.10 Crores in the hold co. will that suffice for meeting the conditions of this operating company being allowed to hold a multi-brand company with FDI in the hold co. Also one question that in such a structure, should ETHOS declare a dividend and this income in the hold co. become more than 50% of the income of that hold co. then the hold co. will be deemed to be an NBFC. What are the implications of that? This was a new thing that we were not quite aware of and we have now asked our advisors also to examine this that if that should happen what would be recourse available for us, so I think that if three or four sort of tricky issues involved with the hold co. structure, which we have now as said is part of the discussion that we have asked our advisors to give us clarity on this before we take a decision on how to move forward. So that is the current status on this restructuring business.

Your other question, your first question in fact was about the own brand, actually Nikhil we have not gone too far on this beyond the initial ideas that we had. Quite frankly we believe that with this new flagship stores and the momentum that we are gaining, I think it is would make a whole lot more sense to sort of concentrate on the strategy that we have put in place with the exclusive brands going to the flagship stores and using a lot more of social media for the marketing. So frankly that is an idea, which I think we would prefer to pursue that once at least not in the current financial year.

Nikhil Vora: I was suggesting the seconds market?

Yashovardhan Saboo: You mean the preowned market.

Nikhil Vora: Yes I guess the new discretionary purchases will always get a bit challenge when economy slows down, but the seconds could stimulate during the same period?

Yashovardhan Saboo: So we are seeing traction on that Nikhil and now with our service centre up and running we are able to get a lot more traction on that. There are two issues that we sort of continuing to deal with before we can really shift to a high gear. One of them is as I mentioned to you the legal position in India right. Currently the legal position is very clear that in the case of watches, which is one of 10 or 11 products, the burden of proving that import duties have been paid on the watch is with the person who is found in possession of the watch, not necessarily the owner. So this means that if we possess a watch, which is a preowned watch unless we have documents to prove that import duty is paid, we expose ourselves to the risk of the charge that we are holding illegally imported goods. That is a view that is a risk that we should not take so obviously that cuts down the number of watches that we can source. Frankly we need to be able to keep the watches to be able to show it to prospective buyers. We have tried the angle where we do not really keep the watch and you let the owner sort look at the watch on the website, but at the moment, it is not happening. Nobody wants to buy an expensive preowned watch without actually looking at it and seeing whether the quality is okay or not. Despite that I think we are seeing a good traction and we will be able to report figures at the end of H1 as to how this business is growing. The second issue, which is being flagged up is that some of the brands are unclear as to what is the policy for this business in India. I cannot really name the brands, but these are brands, which are quite comfortable and either by not mentioning or actually by expressly legitimizing they are actually supporting the preowned business in other developed markets. However, they did not foresee that such a structure could evolve so quickly in India and therefore their policies on this are not yet clear. In the situation of unclear policies right now many our partner brands have said look I know you guys are doing it. We understand this is a good move for the future, but please do not go very big. Do not advertise in big time until you get an express okay for us. We are pushing this. We obviously do not want to sour any relationships with brands, but we are pushing them and nudging them to say look if you can allow it in the US, if you can allow in the UK, and if you can allow it in Hong Kong why not in India. We hope that within this year, we should get the approvals because overall they understand the logic. This business anywhere exsist and this business is growing. It is better that it is done officially than under the table. It protects the brand and it protects the customers. So therefore, there is no reason why they should not promote this business so long as it was done by responsible partners. I am very confident that this will come through and we will see a great traction on this business Nikhil.

Nikhil Vora: Fair point. Super. Thanks Yashovardhan and all the best to you.

Moderator: Thank you. The next question is from the line of Atul Kothari from Progwell Securities. Please go ahead.

Atul Kothari: Sir thank you very much for the opportunity. Sir I would like to know as to what has led to the improvement in gross margins of ETHOS?

Yashovardhan Saboo: Atul are there any other questions?

Atul Kothari: Secondly Sir I would like to know about the sales, which we have been able to generate if you throw some light on the sales generated at Hyderabad store?

Yashovardhan Saboo: Sorry at which store?

Atul Kothari: If you can throw some light on the sale generated at the Hyderabad store?

Yashovardhan Saboo: Atul in general we do really want to speak about sales at any one particular store. That information we believe is valuable and confidential, but I can tell you that our Hyderabad store is clocking sales as per budget. In fact, in the opening month it was comfortably above budget. In the subsequent month, it was bit below and over the last three months, it has done a little more than the budget. So, we are pretty happy with what is happening at the Hyderabad the new flagship store.

On the question regarding gross margin, one of the main factors really is the higher share of house brands. As I mentioned to you house brands is 24% of our business compared to 15% in the same quarter of last year and you know that the gross margins on house brand is almost 15% to 18% higher than on the other brands, so this is the principle reason why we see an improvement in the gross margin, which is actually the strategy as well.

Atul Kothari: Sir that is all from my end. Thank you.

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

Lalaram: Good afternoon Sir. This is Lalaram here. Sir my fist question is that you said we grew 50% plus in the exclusive brands on a Y-o-Y basis so which means that in the non-exclusive space we have basically degrown right, significantly, and so is that something to do with the top selling brand in India, the Swiss brand, which is basically coming out with a partner from the Middle East in India and we losing some of the market shares because of that?

Yashovardhan Saboo: I will answer that Lalaram, but do you have other questions.

Lalaram: My second question is on the marketing entity, which we have so I want to understand that in the previous year I think full year we made a profit there, so what I understand is that we basically do marketing for ETHOS internally, which is our own budget and at the same time we also get some budget or some sanctions for marketing from the Swiss companies, which basically we implement so when we say we are making profit in that entity, I want to understand what does that actually mean? Are we actually using up less funds than what the Swiss company is giving us or the profit is purely is the incentive, which we get upon meeting those sales target, so if you can help me understand how the profit is generated in the marketing entity as of now because we are not doing this business for the outside customers? It is only for the watches the customers and Swiss watches, which we have right, so that is something, which I want to understand better? The third question is in this quarter Estima what was the revenue and operating profit or even net profit loss if you can give that figure?

Yashovardhan Saboo: Let me start with your first question, yes as we reported there have been a decline or degrowth in nonexclusive brands and a substantial part of this, there are two main reasons. Let me start by saying that the degrowth is only in the segment above Rs.5 lakhs. The segment below Rs.5 lakhs has actually grown, but above Rs.5 lakhs it has degrown. The expense above Rs.5 lakhs degrowth is partially because of the overall macroeconomic condition, so it is not only in one brand, which you are mentioning, but it is across brands at that price point including some house brands, but largely it is because of the brand that you are mentioning however I do not believe that it has much to do with the fact that Rolex has a new partner from the Middle East who is in India. I do not believe that is largely the case. The case is the allocation of watches was less, so I do not know if you visited our store in Mumbai, we do not have Rolex there, but if you visited our stores in Chanakyapuri in Delhi, Saket in Delhi or in Bengaluru there were times when we had less than 30 to 40 watches on stock. The consignment used to come in and within three days all the watches were sold to the extent that the malls were complaining that how it is possible that you have a boutique of 400 square feet and you have only 30 watches in the boutique, so the allocation of watches was low and that is not an India only phenomena and that is not a ETHOS only phenomena.

The allocation of watches was low across the board. You could go to any retailer and you will find that the watches in the boutique are much less than the place available for the watches. Everywhere in the world, you go to Dubai, you go to London, and you go to any place you will find the same situation. I think it is really largely due to a lower allocation because of the global shortage. As I mentioned this is now starting to ease out and we will see the beneficial impact of that as we go along. Because there is a new entrant in the market, is there going to be a big impact? I do not think so because what has the new entrant done. The new entrant has not taken over any business except if they had not come others would have expanded their footprint in the county. So if they are going to open a store in Mumbai, it is not that Rolex is going to open a store with them when they did not want to open a store. They would open a store anyway with someone else right. Rolex is continuing its growth strategy for the country irrespective of whether they have a partner from here or there. Now it may be that instead of a partner and instead of a let us say a partner from Chennai they chose a partner from Dubai, instead of a partner from Delhi, they choose a partner from Dubai. That is possible, but I do not believe our market share or share of market in this case is really going to be impacted that much because the market itself is going to grow. We have seen how it has grown in the past. We have seen our growth in the past and I am not at all concerned too much about the blip in the last three or four months. I think this is a soft market for reasons, which we all know. It is a soft market in almost every market segment, but I am also hopeful that if not in the next two to three months, definitely by the end of Q3 we would have seen a smart revival.

So in Cognition, it is true, a lot of the marketing programs and the marketing services that we are providing are directly to foreign brands. Why is this because a lot of foreign brands they prefer that for their marketing they want to deal with companies that are specialist in digital marketing not with the retailer itself because as per their internal rules if they provide marketing let us say a marketing budget to a retailer it gets clubbed with their margin because then they cannot distinguish whether it is margin or it is a marketing spend so therefore they want to separate the marketing spend from the margin and for us it is easier if we take up the marketing in a separate company, which is Cognition. So that is how the business really works. So obviously you have the revenues coming in from these clients and you have cost, which are the costs that we incur for the marketing, for the infrastructure, for the team of Cognition and that leads to the profits so we expect a profit this year as well. Sekhar you want to clarify anything.

Raja Sekhar: Lalaram I think your question is also regarding the revenues that Cognition is getting from ETHOS.

Lalaram: Yes it is a combination of both right?

Raja Sekhar: It is the revenues that are coming from ETHOS and these are again in the nature of brand agreements that ETHOS has and these are then reimbursed by brands to ETHOS. The profit element within this digital services is being kept at the Cognition level. ETHOS acts as a sort of an intermediary where the services are provided to ETHOS and these are then later reimbursed by the brands to ETHOS. So that is a very small part of the business that Cognition is actually generating. Much of it is actually on account of the direct billing that it does to brands. Does that clarify.

Lalaram: That is helpful.

Sanjeev Masown : On Estima, the sales and loss for this quarter. Lalaram, the loss in Estima for this quarter is Rs.2 Crores.

Lalaram: Net level right?

Sanjeev Masown : Sorry.

Lalaram: This is the net level or this is the operating EBITDA or EBIT, which you are mentioning.

Sanjeev Masown : This is the net level PBT.

Lalaram: And when do we expect these things to turn around in Estima one year? One year would be or more than that to break even?

Yashovardhan Saboo : We were quite hopeful that the quarter starting July actually not July because of July is the holiday season over there, but from September onwards we should start to see a breakeven. I am hopeful that in the quarter October to December we should be definitely at cash breakeven perhaps close to an overall breakeven and in the next year our fiscal year over there is still January to December we should overall have a breakeven so which will turnaround next year.

Lalaram: One more question Yashovardhan on the exclusive brands can you share the gross profit, which we generated, the split of gross profit between exclusive and nonexclusive? I do not know if you have shared this?

Yashovardhan Saboo: In terms of percentage.

Lalaram: In terms of absolute amount if you can give me so if you made X amount of gross profit in this quarter? How much was from exclusive brands?

Yashovardhan Saboo: The overall gross margin in Crores or rupees.

Lalaram: Yes in absolute number gross profit yes?

Raja Sekhar: Taking out the absolute value, but in terms of gross margin the exclusive brands contributed about 33% of the gross margin and 24% of the topline. I will just tell you in absolute.

Lalaram: Got it. Also the square feet what would be the square feet, which we would be having as of say June end and what was the average ticket size?

Yashovardhan Saboo: You can calculate from that.

Lalaram: By adding right and what is the average ticket size in this quarter? The average ticket size if you can give me for this quarter for us billing?

Yashovardhan Saboo: Square feet is 59700 square feet at the end of Q1.

Lalaram: And the average billing?

Yashovardhan Saboo: This is super area.

Lalaram: Got it and this number were 53000 I believe in the March end around 53000 odd?

Yashovardhan Saboo: Probably right. Correct 52800.

Lalaram: Got it and also one more number the average billing ticket size in this quarter, which we have done?

Raja Sekhar: 94000 at MRP. This was 88000 for YTD.

Lalaram: Got it so this steadily increasing for us and do you foresee that this trend this is what you believe will be happening in the coming years as well will steadily increase our ticket size?

Yashovardhan Saboo: I think overall it will increase. I do not know about the next two quarters because as you have seen in the very high price point there is some kind of softness, but overall I think this will increase. Actually the share of market of the price point below Rs.20000 is going down for us. As part of our conscious decision that we need not be too active in the price point below Rs.20000 to Rs.25000. So that share is going down and the share above the Rs.1 lakh price point that is going up so I believe the average price at MRP level will go up.

Lalaram: Got it. Thank you Sir and all the best.

Moderator: Thank you. As there are no further questions, I would now like to hand the conference over to Mr. Yashovardhan Saboo for closing comments.

Yashovardhan Saboo: With this I would like to thank everybody who is still on the line for having being part of this conference call and all the best until the next time we speak. Thank you very much.

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