gokaldas exports ltd

GEL/SEC/2022-23

February 20, 2023

BSE Limited
Phiroze Jeejeebhoy Towers
25th Floor, Dalal Street,
Mumbai – 400 001

Scrip Code - 532630

National Stock Exchange of India Limited
The Exchange Plaza
Bandra-Kurla Complex, Bandra (E),
Mumbai – 400 051

Scrip Code: GOKEX

Dear Sir/Madam,

Sub: Transcript of Q3 FY'23 earnings conference call

Pursuant to Regulation 30 and Regulation 46(2) (oa) of the SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015, please find enclosed the transcript of Q3 FY'23 earnings conference call held on February 13, 2023. The Transcript is also available on the Company's website at https://www.gokaldasexports.com/investors/.

This is for your information and records.

Thanking you,

Yours truly,
For Gokaldas Exports Limited

GOURISH GANAPATI HEGDE

Digitally signed by GOURISH GANAPATI HEGDE
Date: 2023.02.20 22:13:56 +05'30'

Gourish Hegde
Company Secretary & Compliance Officer

Encl: As above

Regd. Office : # 25, 2nd Cross, 3rd Main,
Industrial Suburb, Yeshwanthpur, Bangalore 560 022.
Tel : +91 80 68951000, Fax : +91 80 68951001
E-Mail : info@gokaldasexports.com CIN : L18101KA2004PLC033475

“Gokaldas Exports Limited

Q3 FY '23 Earnings Conference Call”

February 13, 2023

MANAGEMENT: MR. SIVARAMAKRISHNAN GANAPATHI – VICE CHAIRMAN AND MANAGING DIRECTOR – GOKALDAS EXPORTS LIMITED
MR. SATHYAMURTHY – CHIEF FINANCIAL OFFICER – GOKALDAS EXPORTS LIMITED

MODERATOR: MR. BINAY SARDA – ERNST AND YOUNG

Moderator: Ladies and gentlemen, good day, and welcome to the Gokaldas Exports Limited Q3 FY '23 Earnings Conference Call. 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, please signal an operator by pressing star then zero on your touchtone phone. Please note that this conference is being recorded.

I now hand the conference over to Mr. Binay Sarda from Ernst and Young.

Binay Sarda: Thank you, Darwin. Good afternoon to all participants on this call. Before we proceed to the call, let me remind you that the discussion may contain forward-looking statements that may involve known, unknown risks, uncertainties and other factors. It must be viewed in conjunction with our business risks that could cause future result, performance or achievement to differ significantly from what is expressed or implied by such forward-looking statements. Please note that we have mailed the results and the presentation and the same are available on the company's website. In case if you have not received the same, you can write to us and we'll be happy to send the same over to you.

To take us through the results and answer your questions today, we have the top management of Gokaldas Exports Limited, represented by Mr. Sivaramakrishnan Ganapathi, Vice Chairman and Managing Director; and Mr. Sathyamurthy, Chief Financial Officer. We'll start the call with a brief overview of the quarter gone past and then we'll conduct the Q&A session.

With that said, I'll now hand over the call to Mr. Siva.

S. Ganapathi: Good afternoon, everyone. Happy to have you at our earnings call for the third quarter of FY '23. We continue our exceptional trajectory, delivering performance with strength and resilience when the industry is encountering a challenging global macroeconomic environment. We reported a revenue of INR 528 crores, almost at the same levels of previous year. In contrast, the Indian apparel exports declined in the third quarter by 3.1%. Currently, major consuming markets are passing through uncertain times and there are sign of a global economic slowdown as macroeconomic factors and declining consumer confidence seem to undermine the past gains.

Having said that, amidst these, we continue to stay focused on operational excellence and customer service as these are cornerstones of our growth levers. During the quarter, as volume growth remained flat, we strongly focused on improving employee and operational productivity, balanced our orders on hand with capacities well and reduced operating expenses. We delivered a superior EBITDA margin of 13.1% after adjusting for one-off income of INR 3.3 crores. We continue to manage our working capital well and generated adequate free cash flow to support our growth ambition. While the US retail and e-commerce market so far has shown resilience and have performed well in CY '22, we anticipate a mild slowdown in the offtake going forward. This is already reflecting in our Q3 revenue.

On a sequential basis, our revenue has been falling from Q1 to Q3. We expect this to have bottomed out and we'll see that trends reversing starting Q4. We have done well in a downturn and this is no exception. We intend taking market share during such times and ride the growth curve in the aftermath of the downturn to deliver strong growth. We view the long-term macroeconomic factors are favourable for the growth of the business. In the short-term, we are closely watching the macroeconomic environment for any development that may be adverse to the business and further strengthen relations with the customers and ensure execution excellence and service delivery.

With this in mind, we continue to explore avenues for growth. We are progressing well with our capex plan. The unit in Madhya Pradesh is expected to commence commercial production in first quarter of FY '24. And our knits project in Tamil Nadu too is progressing well, setting the stage for a strong future. Further, we may explore other avenues of growth as well, including opportunities to invest in good assets that may fit in with the overall strategy of the company. Our growth trajectory for this financial year is intact, while we continue to build a firm foundation for strong growth in the years ahead.

I thank you for listening and would be happy to address questions that you may have.

Moderator: The first question is from the line of Mohit Khanna from Banyan Capital Advisors LLP.

Mohit Khanna: My question is related to the fourth quarter that you might have some visibility, because year-over-year, the last quarter, the base, it was very strong for you. And you have just said that you are a little -- we should witness some quarter-on-quarter improvement here on. So with that in mind, you had previously guided INR 2,200 crores of revenue for FY '23. Do you think you might still be able to beat that? That was the first question and I will come back.

S. Ganapathi: So answer is absolutely yes. We are very confident of doing that and definitely we will do that. You're talking of INR 2,200 crores, right?

Mohit Khanna: Yes.

S. Ganapathi: Yeah, yeah, definitely.

Mohit Khanna: And then how doa you see FY '24 panning out? Is the 15% to 20% growth over '23 is a good number to work with?

S. Ganapathi: So the way -- as I said earlier, we've had sequential decline from Q1 onwards, so Q2 over Q1 and Q3 over Q2. I think we are more or less hitting the bottom and now we will start -- the curve sequentially will start turning. So as we go forward, I'm expecting that H1 of next year sequentially will be slightly better than H2 of this year. And H2 of next year will -- we are hoping that will show a further growth. That's how I'm looking at it. So overall, I think we will get back into the growth trajectory on a sequential basis.

Mohit Khanna: And in terms of margins, because this quarter has also been very strong, there is -- the other income has actually improved for us from INR 2 crores in a quarter to INR 9 crores in this quarter. What exactly is the reason for that? And do we see the similar trend going forward?

A. Sathyamurthy: It has two components; one is on account of the interest income from the investments, in the form of, interest income and mutual fund income. The other one is about INR 3.3 crores we got one-off income which we have highlighted, some of them on the legal issues for which we got the settlement and has been recognized and another one from provision which was not required, has been reversed. This accounts for about INR 3.3 crores as one-off income. Otherwise, the rest is on account of the income from mutual fund investment.

Moderator: The next question is from the line of Abhineet Anand from Emkay Global Financial Services.

Abhineet Anand: First, I was slightly confused, you said, sequentially we should see better numbers in Q4. While commentary from US retail, you have been saying that it has been resilient till now, but you expect a mild slowdown in the offtake in expected short-term. I think those two probably doesn't match. So am I getting something wrong here?

S. Ganapathi: No, that's not -- so what happens is, the end user market influences the brands in turn to place orders on us. So the brands have been anticipating a slowdown already and had tapered down their buying even earlier. That's the reason why the brands have been buying a bit slow in Q2 and Q1. Now -- so whatever happens in end user market, the brands have to now plan two quarters ahead. So if we are seeing a slight uptick, then it just indicates that two quarters ahead, the brands may be seeing that the volumes may slightly pick up.

Abhineet Anand: Second is that, in terms of knits, what kind of margin versus the woven that we presently have? What could be the differential or how is it different?

S. Ganapathi: So the knits is a processing unit. So there is fabric processing unit and then we will of course have some downstream garment manufacturing also. So overall, while the capex investments, since we are putting a processing unit, the EBITDA margin in knits maybe about 6% higher, but then as -- its contribution to overall revenue will proportionately only it will contribute. You understand?

Abhineet Anand: Let's assume what is the investment at the knits factory and what is the asset turn in that?

S. Ganapathi: Little over INR 100-odd crores. It's about INR 120 crores.

Abhineet Anand: And the asset turns are different from a woven factory?

S. Ganapathi: Yeah, it's about 3.5.

Abhineet Anand: And last one. Now that the MP commercial operation expected in 1Q FY '24, what type of incremental revenue can we expect or utilization can we expect there in FY '24?

S. Ganapathi: So in FY '24, MP will be expanding or it will start progressing. So there are two parts to it. One is the manpower ramp up will start. So lot of people currently we have hired. They are undergoing training, which is almost a 45 day training cycle. And then slowly they will be inducted into trial production, commercial production, etcetera.

So the manpower growth will happen through the year and their productivity will also start growing with a phased manner. So if you ask me what is the expected revenue from MP in FY '24, I believe it will be about INR 55 crores to INR 60 crores or thereabout.

Abhineet Anand: So that is the only incremental revenue apart from some modernization, etcetera, that we might do in our existing units, right?

S. Ganapathi: No, it will also have -- that's not the only capex we are looking at. So we will also be looking at as things start opening up, we will also have other capacities come up. We may also do some brownfield capacity unlocking. So there are other avenues to grow as well.

Moderator: The next question is from the line of Sunil Kothari from Unique Asset Management.

Sunil Kothari: Sir, my question first is on this. Now we are reaching quarterly interest cost of around INR 9 crores to INR 10 crores, by when you feel this would be coming back to may be INR 4 crores to INR 5 crores per quarter, because I think now interest rate is also going up and/or debt is also I think has increased?

A.Sathyamurthy: The interest has got two components; one is on account of Ind AS and the other one is the regular interest. Ind AS interest is INR 4 crores during this quarter, Q3. So, our actual interest is only about INR 40 lakh, rest is on account of bank charges close to about INR 1.3 crores. So totally, the interest is less than INR 6 crores.

Sunil Kothari: So this is some exceptional we should take as a 9 months number whatever given that is the run rate we should expect or you feel any major change in interest costs next year?

A.Sathyamurthy: No, in the 9 months interest period also our interest cost is close to INR 7 crores. That is, about INR 1.4 crores is the interest, and INR 5.5 crores is on account of bank charges. Rest of the amount, the balance INR 11 crores is on account of Ind AS interest. So, the real interest cost and the finance charges for 9 months is only INR 7 crores, of which interest cost alone is INR 1.4 crores.

Sunil Kothari: So sir, basically I wanted to understand is, annual interest cost which you will be debiting to P&L, what we should count? That is what my question is. Finance cost I mean.

A.Sathyamurthy: Going forward – for the two components; our real interest cost plus finance charges is not likely to be more than INR 10 crores on a yearly run rate. IndAS portion is around INR 15 crores.

Sunil Kothari: So roughly INR 25 crores would be the cost of finance annual around?

A.Sathyamurthy: Correct.

Sunil Kothari: And sir, my broad question is -- somebody has also tried to clarify this. Your confidence of growth seems to be coming from what? Basically, it's an expansion of products, customer, market share. So if you can little elaborate? And if you can speak more about say next two, three year, how you see the opportunity after this, maybe some three, six months slowdown or whatever slack?

S. Ganapathi: Sure. So the way I see it is that the end user market in the US in particular has been by and large resilient. Even the February numbers seem to indicate that the market is somewhat holding up. We may experience some mild recession for a brief while maybe through fall or early holiday. But at least from 2024 spring onwards, we should start seeing growth.

Now why is that? Because I feel that by then the recessionary impact will be gone. The Fed is already loosening the interest rate hikes slowly. So the market situation may turn from '24 onwards. If that indeed happen, then for us, we manufacture for spring '24 in third quarter of FY '24. So we should start seeing an uptick in third quarter from an order book perspective in preparation for spring '24. Also remember that for spring '23, their purchases were muted and all of that. So there will be a base effect also. So I feel that overall there will be a growth opportunity given that the consumption is expected to come back in '24. So this is one narrative.

The second one, of course, is that the broader picture in the minds of retailers in the US and for that matter even in Europe is that the trend of moving away from China to other geographies is very strongly intact. They might have hit a slight pause button simply because at the moment they may not have too much of orders to move around, but the secular trend of moving out of China and moving into other geographies is very strong.

And what I understand from many of them is that the cost in Vietnam have become prohibitively high and increasingly buyers are looking at other options and in particular India. So India seems to be a good rising star in their estimation from a future production angle. So that movement will get accelerated going forward when the volumes increase. So I see that that's adding to the tailwind going forward.

Sunil Kothari: Sir, can you elaborate more on this Vietnam factor, which costs going -- how competitive we are compared to Vietnam?

S. Ganapathi: So Vietnam, while people say the average labor cost is around $300 per month, vis-a-vis say in India of about $170, $180 in India that too in the most expensive parts of India. I think from what I understand is that the Vietnamese cost even at $300 they may find it a bit difficult to get employees. They are finding that the other sectors are growing well. That's the economy which is heating up and the prices are going up further. So margins for Vietnamese players will come under pressure with rising wages. So that's the wage arbitrage that we have between Vietnam and India.

Sunil Kothari: And I think you have given some guidance for next year I missed that because of some phone disconnectivity. So if you can repeat sir, margin and revenue guidance for next year, if you have given?

S. Ganapathi: No, no, I have not given any particular guidance. We hope to hold the margins as far as possible at current level. That is the intent going forward. As far as the revenue is concerned, what I indicated was that sequentially we will start growing in the next financial year.

Sunil Kothari: And sir, my last question is, having this new capex and new factories coming up, over next two, three year, what size of business we can do given our order and capability?

S. Ganapathi: So we have already -- we have gotten one factory ready, which is in Bhopal, and we have the ability to start a second unit there. In addition, we have earmarked a plan to grow one more unit in the south. So all of these options we have in hand and we will start work on some of these soon. The reason I'm saying that is, any new factory will take about a year to fructify -- at least a year, if not -- in my estimation it will be about five quarters before we can start ramping up those capacities. And my belief is that this will given that the market is expected to come back up in the later half of next year, we should start pushing for on the capex -- as the capex also has a timeline to materialize.

Sunil Kothari: So what size of opportunity you will be able to cater maybe over next two, three year? Any -- your objective or target which I think you had given some years back also?

S. Ganapathi: So based on the capex that we have planned, we are anticipating that we can deliver about INR 1,400 crores of revenue in the three year or four year scenario, at least.

Sunil Kothari: From new capacities?

S. Ganapathi: From new capacities, correct.

Moderator: We have the next question from the line of Niraj Mansingka from White Pine Investment Management Private Limited.

Niraj Mansingka: Two, three questions. One, what is the capacity of the company in terms of the machines that you're having right now, sewing machines?

S. Ganapathi: So based on the sewing machines -- you are talking about a number of machines or you saying capacity in revenue term?

Niraj Mansingka: No, number of machines.

S. Ganapathi: Number of machines we may have about 13,000 to 13,500 machines.

Niraj Mansingka: Because it was 14,400 three quarters back. So have you seen some...

S. Ganapathi: It is at those levels. I mean, you're talking of 1,000 numbers only, right?

Niraj Mansingka: Yeah. And what would be the number of employees that we are holding, total employees?

S. Ganapathi: At moment, we are under 30k.

Niraj Mansingka: But this has also gone down from 32k. So have you seen a trend of reduction in employee and machines?

S. Ganapathi: Only because we have let the natural attrition play-out given the correction in the revenue. So we have allowed some bit of natural attrition to happen. We have not backfilled them. As soon as we start growth again, we will start building up power.

Niraj Mansingka: And of the total ongoing capex that we have, one we have of the Tamil Nadu unit, which is in two phases, and one is of the knitting capacity. Is there anything else which is ongoing?

S. Ganapathi: No. So there is a Tamil Nadu unit, which is the knits fabric processing unit. And there is one which is almost complete, which is the Madhya Pradesh sewing capacity or the garment manufacturing capacity. These are the two that are actively progressing and will fructify in FY

'24. In addition, we have one more unit in Bhopal, which we can bring up at short notice because a lot of the groundwork for that has also been completed.

And we can bring up two more units, one of course in South India and we are also keeping the Bangladesh option on standby, which we were holding. Given the demand scenario, we may start working on that also at the earliest once we start getting clarity on the demand.

Niraj Mansingka: So sir, we will be using our cash flows to repay the debt, entire debt and use those cash flows to keep on growing with new capacity. Is it the right way to do that?

S. Ganapathi: Can you repeat that question again? I'm sorry.

Niraj Mansingka: Sir, we will use our cash flows to grow and keep on adding capex as and when required?

S. Ganapathi: That is correct.

Niraj Mansingka: And sir, two more related questions. One on how are you getting ready for the UK FTA? And do you see a large opportunity there?

S. Ganapathi: So the way I see it, UK FTA is slightly on a slower track because of the change in government in UK and all that. We were earlier anticipating when Boris Johnson was there to get complete -- just to be -- to fructify the December, then it got deferred to March, but I don't know, it may take another three months before it can fructify. But we are gearing ourselves up for it. We have already in the process of inducting one UK based client, a new customer. We are in talk to one of our existing customers also to see if we can ramp up.

In the meanwhile, I see that UK brands have two opportunities available. One is diversify away from Bangladesh. India and Bangladesh will have identically low duty structure. So Bangladesh today exports about $3.5 billion to UK. So a portion of that become available to India simply because the lead times from Bangladesh are higher. Fabric goes from India to Bangladesh and they hit -- move the garments to the UK. So India can offer a superior lead time, while getting the similar cost structure.

Second is China, which exports about $4 billion to UK opportunity -- we will be about 10% or 12% cheaper than China, so some amount of both orders will also come to India. So I'd expect that Indian apparel industry will benefit at least by $1 billion incremental once the UK FTA comes. Now different operators will get a different piece of it, but that's the trajectory I'm looking at.

Niraj Mansingka: I think basically which type of general garments like…

S. Ganapathi: Say that again.

Niraj Mansingka: Which type of garments generally are imported from Bangladesh to UK?

S. Ganapathi: So Bangladesh does a lot of men's shirts, bottoms, all kinds of garments. So some of those garments will also come to India.

Niraj Mansingka: Sir, last question. You said Vietnam had opportunities opening for India. What I understand is, Vietnam is more on non-cotton side. And do you see India getting those non-cotton opportunities because what I knew was India was not so attractive destination for non-cotton side?

S. Ganapathi: You are right. Vietnam does not only do non-cotton, Vietnam also does cotton. It gets cotton from other places and do it. While the non-cotton opportunity will be harder, but we ourselves are doing a lot of non-cotton where we are competing with Vietnam-based players. We buy fabrics from China, Taiwan, Korea and all of that. So as the labor cost goes up, the labor arbitrage increases. So to the extent that it can even offset that transportation costs from East Asia of fabric into India.

Niraj Mansingka: Sir, just on this related question only. Do you see India has become very attractive to outsource for non-cotton fast fashion women's wear or fast fashion products?

S. Ganapathi: Fast fashion will be difficult because of lead time-related issues.

Niraj Mansingka: So they would still dominate that area, is that right?

S. Ganapathi: China, Vietnam could dominate until and unless some synthetic fabric ecosystem develops closer to India -- but it all depends on the cost structure. At some cost levels things will have to give way.

Moderator: The next question is from the line of Nirav Savai from Abakkus Asset Management Company.

Nirav Savai: Sir, I actually missed your initial remarks. Sir, I just wanted to understand about this employee expenses this quarter, sequentially there is a dip of around INR 10 crores. So what has changed on that side?

S. Ganapathi: So Nirav, there are two things. One is, of course, we let some bit of natural attrition play aligning it to the order volume that we had. So if you have seen, sequentially there is a bit of a volume -- revenue drop as well. Now having said that, even as a percentage of revenue, we have improved. Our employee costs have gone down. And the reason for that is because we have worked hard on productivity improvement. That is what you are seeing there.

Nirav Savai: So this kind of a number is sustainable or would it go higher on the fourth quarter?

S. Ganapathi: Productivity level -- productivity improvement related is sustainable.

Nirav Savai: And this MP Phase 1 would be what capacity? And you said about INR 50 crores of revenue which will be there in FY '24 is only from Phase 1, right, INR 55 crores to INR 60 crores?

S. Ganapathi: Exactly, exactly, but INR 50 crores to INR 60 crores will be in FY '24. But as it fully ramps up, we will have INR 175 crores worth of revenue coming from that unit.

Nirav Savai: So you're saying only from Phase 1. And what will be the optimal if we see the second phase or even third phase?

S. Ganapathi: Second phase will be of an identical size.

Nirav Savai: So roughly about INR 400 crores or INR 370-odd crores we can get from this MP facility?

S. Ganapathi: INR 350-odd crores. 175 times 2.

Nirav Savai: So that we can get from this MP facility and we'll see that happening in FY '25 or maybe later than that?

S. Ganapathi: Correct. So the Phase 2 will -- construction will start somewhere in the next financial year. So FY '25 is correct.

Moderator: The next question is from the line of Aashish Upganlawar from InvesQ Investment Advisors Private Limited.

Aashish Upganlawar: Sir, wanted to understand -- I mean, I heard your initial comments on how you see things panning out over the next four quarters. So you said it would be probably flattish maybe couple of quarters on the revenue side and then it would pick up in the second half of '24 I guess. So given the numbers that we have, I think we were closer to INR 600 crores in Q4 and Q1 of last year. So the base is relatively higher. So does it mean that we will be flat on those numbers or you think that it will be lower than those numbers on the sales side?

S. Ganapathi: No. While a lot depends on how the market turns, my assessment is that we should eventually work towards getting there or better.

Aashish Upganlawar: But the visibility that you have right now, I mean, there should not be a problem kind of meeting those last year numbers on the sales, right?

S. Ganapathi: So as I said, sequentially we will start climbing back. And the assumption we're making is that by early '24, the market in the US, and for that matter Europe, should start picking up and doing better. And if that indeed happens, then we should have no problem in doing it.

Aashish Upganlawar: But given your dialogs with your customers and reading of the entire situation, is it still very hazy kind of a outlook on how things are going to pan out or...

S. Ganapathi: Hazy, that is for near-term. So when I look at sometimes -- something like spring '24, I don't think -- the general consensus is that it should be strong across a large number of industry observers, people who are in the business in retail in the US. So that's the -- those are people who have been in the industry for years. So that's the expectation from such guys. But in the short-term, the economic indicators are all over the map. So there are some indicators which are favourable, some indicators which are not so favourable. So people are becoming a bit risk averse. But if let us say the recessionary trends are not protracted, then we may start seeing even earlier uptick.

Aashish Upganlawar: So in your business basically, from a retailer's perspective, the inventory kind of drawdown is that -- I mean, what has been playing over the past maybe couple of quarters? And is it -- does it work that way in bringing down the inventory in these times and then probably take a call?

S. Ganapathi: So they tend to bring down the inventory. So they are sitting with a little higher inventory because they bought -- overbought situation last year. So they are working their inventory out as we speak. And many brands are at different stages of working that inventory out. So some of them will work their inventory out in a quarter or two at most and then they will realign and start buying.

Aashish Upganlawar: And finally one more thing. I mean, from your balance sheet that you have reported right now, I don't see any issue on the working capital or receivables as such, but anything on the recoveries, any stress there or is it all normal?

S. Ganapathi: None whatsoever. We are closely tracking all of our customers. And none of our customers seem to have -- we closely track their financials and all of that. We don't anticipate any problem whatsoever there.

Moderator: The next question is from the line of Anush Kumar from Spark Asia impact Managers Private Limited.

Anush Kumar: My first question is a data-keeping question. Basically, see, if you could split the capex breakdown for FY '23 among the existing facilities at Krishnagiri, Bhopal and Perundurai, would be helpful?

A.Sathyamurthy: For the year FY '23, about INR 84 crores is being spent in Perundurai unit. Another INR 32 crores whatever we have highlighted is for Bhopal project. Krishnagiri project has been implemented last year itself and that was completed last year.

Anush Kumar: And this sustainability in margin considering the fact that the productivity is improved, can we expect about 25 to 30 bps improvement in the margin for FY '24?

S. Ganapathi: Over the current levels you are saying?

Anush Kumar: Yeah, over the current levels.

S. Ganapathi: No, I don't think so, because FY '24 will have all kinds of headwinds and challenges in terms -- in the early phase and there will be price pressure. So you might have seen that if our gross margins slightly dropped in Q3, but we more than offset it by productivity improvement in the quarter. So there will be those kind of headwinds, which may have a countervailing effect. So an improvement in margin of 3% or 4% above current levels probably is not sustainable, right?

Anush Kumar: Yeah.

S. Ganapathi: Our overall effort will always be to continue to improve productivity and thereby work on margin improvement. But to deliver a 3% improvement in one year is not possible. We will try our best to see how much of productivity gains that we can drive through.

Anush Kumar: So actually, my question was, I was talking about 30 bps, it's not 3%. So it was 11.9% for Q3. So anywhere between 12%, 12.2%, 12.3%.

S. Ganapathi: Yeah, that is possible, 30 basis points.

Moderator: The next question is from the line of Atul Mehra from Motilal Oswal Asset Management.

Atul Mehra: Sir, just couple of questions. One is that next financial year, FY '24, what is the revenue that we can do assuming that we can achieve the highest capacity utilization?

S. Ganapathi: So that's a theoretical question because we need orders to deliver those revenues.

Atul Mehra: Correct, correct. Theoretical, yes.

S. Ganapathi: In the first quarter of this year, we did a revenue of about INR 600-odd crores. So if it's our capacity, we will be -- with our machine capacity, we should be able to do that kind of a revenue. Theoretically those were the orders that are available today without those incremental capacities coming on stream, like Bhopal, etcetera. Having said that, the manpower capacity has been realigned to current revenue levels. Then we will -- if the revenue picks up, we will realign the manpower to those levels.

Atul Mehra: So INR 2,400 crores of the current capacity. And what you are mentioning is the new facility that will come on stream, in year 1, we can do about INR 60 crores of revenue or something, correct?

S. Ganapathi: That is correct. But by the time we get year 2, it will be INR 175 crores.

Atul Mehra: And sir, secondly, like one of the things about the slowdown and demand slowdown and so on and so forth. What I understand is that it has more to do with broader environment. And if we are able to plan capacities better in terms of overbooking and so on, like we can basically make sure that we try and achieve our capacity to the fullest extent.

So given that we have some time on our side for '24, would it be like reasonable to assume that like we will be trying our best to utilize that INR 2,400 crores, INR 2,500 crores threshold despite the macro environment because while the macro environment is there, but for our size of the company, the construct of the size of the market, it is not that big a constraint -- some comments?

S. Ganapathi: Very good question. What happens is that if you look at the global markets, the top three markets are US, Europe and China. And all the three of them put together have 43% of global market share. So the garments sold in these three countries -- these three regions are 43% of world consumption. And all of these three markets are at the moment underperforming for various reasons. US sort of a little bit of an overbought situation excess inventory and a mild recession expected in the US, Europe because of the war, but that also now seems to get baked into their equation and we may start seeing growth going forward. And China because of the COVID-related slowdown in buy from end consumers.

So what has happened is that there is a global demand-supply mismatch, which has currently resulted in the order book slowdown. Now theoretically, if we start pumping for incremental growth, one has to now start offering cut rate and bring down the rates and all of that. We have historically been extraordinarily reluctant to compromise margins and give an illusion of lower price, etcetera, to win the business because that would compromise us over the longer term. People will start resetting their price points with us to a lower level, which we are totally reluctant on. So I can compromise margins to drive revenue growth, but we have so far held back on that count. That's why we are more profit-driven than simply top-line-driven.

Atul Mehra: And sir, one final question. In terms of with all the expansions that we have under plan, you mentioned earlier, INR 1,400 crores in incremental revenue. So if you were to combine everything, all combined, then as of now, the capacities that we are having under plan can do a theoretical revenue of about INR 4,000 crores over the next 2 to 3 years' time?

S. Ganapathi: INR 2,400 crores plus INR 1,400 crores, right, INR 3,800 crores.

Atul Mehra: Yeah, INR 3,800 crores. And this is by FY '25 I guess?

S. Ganapathi: This would be by FY '26.

Atul Mehra: By FY '26. Got it. And sir, one other thing. I think you also as part of your commentary or in answer to some of the question, said that we are also opportunistically looking at any brownfield assets or like would this be in the form of any M&A or any asset purchase that you have in mind or it is more to do with the existing capacity in brownfield?

S. Ganapathi: No, no. So existing capacity brownfield is anywhere there. There are opportunities we are not averse to it. So as and when an opportunity comes to the table, we don't mind looking at those as well.

Atul Mehra: From an M&A perspective?

S. Ganapathi: That's right.

Moderator: The next question is from the line of Arvind Kothari from Niveshaay.

Arvind Kothari: Excellent performance given the situation, sir. I had a question that from the standpoint of the UK $1 billion opportunity that you said could open up, how are we planning what portion of that pie you think we'll be able to cater and going forward maybe those Eurozone might get opened up for our country? So what share of our total revenue do we plan to have Eurozone going forward?

S. Ganapathi: So Eurozone plus UK put together currently contributes to 4% of our revenue. Historically, we have operated -- when I say historically, even five years back, we were at about 20%. So our ability to ratchet up European share exists. That will not come at the cost of US, it will be an incremental growth. So we are open to doing more business as long as they are margin accretive and all of that.

At the moment, since FTA with UK is being planned, we have opened up more dialogues with UK based customers and have identified opportunities to expand in early FY '24 with UK based customers. So those discussions are going on specific styles, etcetera. So we will be ramping up UK based revenue to start with. As and when the European FTA is signed, then we will go all out after Europe. At the moment, we are going slow with Europe.

Arvind Kothari: And sir, the next part of the question is that the ramp up that happened in China was basically they're having more of opex kind of a model where capex was almost funded by the government where the land was basically provided by the government. And hence, the scale up happened very fast. So the tailwinds that our country has maybe in terms of the labor wages, do you think the capex bottleneck can maybe have the growth to be slower or how do you see that part?

S. Ganapathi: So it really depends on the company rather than industry as a whole. So people like us, we are not capex shy. And if we see an opportunity, we will go with capex. That is point number one. And we have the cash flows and the cash holdings to go for capex. Second is that, there are certain states in North of India, MP being a case in point, which are actively encouraging us with a lot of incentives which will allow us to recover our capex investments also at the earliest.

So net-net, while capex funding like China may not be possible, but the macroeconomic conditions now that exists in India is also moving in that direction. So that's a little more favourable to setting up capex these days in Northern geography. That's the reason why we chose Madhya Pradesh to expand.

Moderator: The next question is from the line of Danesh Mistry from Investor First Advisors.

Danesh Mistry: I just had two questions. One, I think you alluded to the fact that gross margins have been lower this quarter, I think roughly by about 400 bps. So is that a function of our product mix. We are making more t-shirts versus jackets? That's question number one. And your question number two is that, sir, regarding your other expenses this quarter, it came down year-over-year by quite a bit from about INR 45 crores to about INR 36 crores. So is this number sustainable? And what could be the component in it that have actually reduced? Is it shipping, transport or something else? And do you see this kind of number sustaining going forward?

S. Ganapathi: Let me answer the first part on gross margins. The gross margin reduction is on account of two things. One is, of course, the product mix in the third quarter changing from outerwear to fashion wear, because in third quarter, we produced more of spring wear and the garments are largely cotton and cotton viscose-based. So the margins are slightly lower there historically. But in this particular scenario, because in the third quarter we also had a fairly heavy headwinds on order placements, etcetera, we also saw that the brands were willing to place orders only on a tighter margin.

So while we let the margins slide a bit making sure that we can overcome with better productivity, we did not allow it to slide even more. So we stopped there. So part of the gross margin reduction is on account of product mix, part of it is because of the market condition. As far as the other expenses are concerned, Sathya, you may...

A. Sathyamurthy: Other expenses, it is primarily on account of the supply chain-related costs, air freight costs which we had incurred last year, almost close to around INR 7 crores that was a one-off item, which we ensured that in this quarter is not there, and that is the reason. And this is sustainable, going forward also.

Danesh Mistry: And sir, if I may just squeeze in one more question. So going forward, I heard you on the call saying that, essentially, because we are working on season, we essentially would not be too impacted by the inventory destocking at the customer there. So is it correct to assume that going forward at least whatever headwinds were there especially on volume are now passed, whilst margins would take time to catch up?

S. Ganapathi: So my expectation is that the volume impact has more or less is bottoming out and will start improving. Margins also, in my opinion, will be bottoming out in this quarter or next quarter. And then hopefully, our productivity gains will be here to stay. So we should start -- as the volumes return back, that is the business volumes return back, some of the productivity improvements that we have put in place will be there to stay. And hopefully, we should be able to improve our gross margins as well.

Danesh Mistry: So in that case, then the employee costs may not come back in the same fashion as the volumes would?

S. Ganapathi: Correct, correct.

Moderator: The next question is from the line of Pulkit Singhal from Dalmas Capital Management.

Pulkit Singhal: The first question is just to understand the inventory correction a bit. My understanding is that it has been going on for last 9 months odd, the destocking. So when you look at the top four, five customers, which are our largest from revenues, roughly what number of days of inventory were these taking at, say, 9 months ago versus now?

S. Ganapathi: So many of them are sitting on 3 months of excess inventory. So if they were sitting on 3 months inventory, they were sitting on 6 months inventory in the past. I think now they would have reduced half of that excess inventory or more depending on the brand.

Pulkit Singhal: So because my understanding -- so therefore, I would think from their perspective, I mean, the demand that you generate for your products, the worst is behind from that aspect. I mean, incrementally, China Plus-One...

S. Ganapathi: That is correct. But so far, the retail market has not slowed down much in the state. If that slows down, then the inventory, while they have reduced it, that inventory may bloat a bit. Though I'm not so sure that that will happen, because so far, the US market still has been resilient.

Pulkit Singhal: But we also -- one more thing was there during these last time 9 months was China was close. So I don't know whether it was an easier period for us to gain orders? Whether there was a supply issue from Chinese suppliers? And how does that impact going ahead?

S. Ganapathi: That is a misconception. Last 9 months, China was closed from a market standpoint. So people were not buying garments. However, the Chinese suppliers were all functioning. So Chinese capacities were fairly intact. So what we had was the Chinese capacity also coming and fighting in the global market. So a lot of Chinese capacity is directed towards China as a market. So we've had situations in the recent past where Chinese capacity were also trying to -- which were domestic capacity were fighting in the international markets. We may see some of that going away going forward because the Chinese markets are now opening up.

Pulkit Singhal: So it's a good thing for you in that case?

S. Ganapathi: That is correct.

Pulkit Singhal: And from a pricing aspect -- like-to-like pricing because our RM prices are also corrected, and therefore, asset turns assumptions would change. So what would be the like-to-like pricing decline you would think for a product which is sold in Q1 FY '23 versus what you might sell next year?

S. Ganapathi: It's a very, very difficult question to answer, because let's say, Q1 to next Q1, I would say the orders are still coming up. But let's assume that if I look at it from last Q1 to the current Q1, the Q1 FY '24, I would think that the raw material prices have come down. Raw material prices have come down by about 6% or 7%. And our realization or the price realization also has come down by about a similar margin. Usually, we should have price realization come down to lesser than the raw material price decrease, but it has been a little more than that this time given the softness of market. We hope that we will be able to recover that incremental going forward.

Pulkit Singhal: And the full benefit of China Plus-One would play out more in a scenario once the end market starts growing and you see higher share of incremental orders and not necessarily on the existing?

S. Ganapathi: That is correct.

Moderator: The next question is from the line of Surya Narayan from Sunidhi Securities.

Surya Narayan: Just to understand something, working of the -- from an operational point of view, the job works have been substantially declined by around 1% if you see in 9 months and so is the 3.5% of the employee cost. Just to understand whether -- how much out of the 30,000 employees we have casual labours and the regular employees, if you can give bifurcation? And why the job charges -- job work charges have declined significantly? That is the first part. I'll come next.

S. Ganapathi: 100% of the employees are on roll. There are no temp labours that we hire for compliance-related reasons. The job work charges are when we have very specialized task for which we may not have the capacity, we give out and get it manufactured. Second is, sometimes when there are very tight deadlines, et cetera, then we may outsource or something like that for completion. But at the moment, as we have improved productivity and capacity utilizations, etcetera, we are trying to reduce the job work charges. It has always been our endeavour and we have been able to control it quite a bit.

Surya Narayan: And sir, another critical question just now, just to -- if you can give answer. Out of INR 520 crores of revenue, just to -- if you can give a figure, how much of, let's say, potential orders we might have rejected due to our unacceptance?

S. Ganapathi: How much of orders we would have rejected due to what?

Surya Narayan: Our critical benchmark of margin and all.

S. Ganapathi: There is -- it's a little hypothetical because we just don't bid on those projects. So if I want to drop margins, I can get any amount of orders. So it's a bit of a hypothetical question. We don't pick those orders. So it's not like I reject it. When the customer solicits orders, we won't -- we'll only bid those which we feel we can make the money.

Surya Narayan: And what is about the status about our operations or our plan towards going to Bangladesh for partner, because we are not discussing any more. So are we dropping that?

S. Ganapathi: This is very much in the play. In fact, the asset has been identified also. I have deliberately slowed down the start of the work on that asset, primarily because of the current market conditions. We are actively considering whether we should now quickly start working on commissioning the work from that project as there will be a lead time to construction as well and that can time well with the market's turning. So that is where we are. So Bangladesh is very much in the play from that perspective.

Surya Narayan: And sir, last year, in the fourth quarter, we saw some hike in the employee costs. So is there -- will that be repeated this year for the older plants? I mean, I'm not including the MP plant, I believe that in MP, the employees will be on the learning curve and they'll open up -- definitely, the productivity will definitely drop there. Am I right, sir?

S. Ganapathi: So employee costs in MP as a percentage will be higher in the initial period because the productivity will be lower. As far as year-on-year is concerned, there will be wage hikes, etcetera. So there will be wage cost increases in line with minimum wages going up and the DA, which is inflation-linked, going up. So wages do go up and we will have to absorb those wage increases. So there will always be a pressure on wage going up and that will have to be offset by productivity.

Surya Narayan: So all those things -- the wage hike will happen in fourth quarter?

S. Ganapathi: So we have the DA hike going up in the first quarter of next year. We have already had a wage hike in the fourth quarter this year. So those are all factors being factored in.

Moderator: The next question is from the line of Jagdish Sharma S. an Individual Investor.

Jagdish Sharma S. I just want to know your perspective on our exposure to the Turkey country, like the country has been through a natural disaster and crisis. What are our exposure to Turkey and how are we going to overcome that?

S. Ganapathi: Our exposure to Turkey is zero. We don't supply anything to Turkey. In fact, Turkish manufacturers supply to Europe -- the US market. So on their customer side also we don't compete much. So from an opportunity perspective also, pretty much happening unless those guys come specifically for certain specific technical capability we have. But exposure to Turkey is zero.

Jagdish Sharma S.: Can I ask you some questions which is not related? Like what are our Indian markets exposure to Turkey? Can you explain that, please?

S. Ganapathi: What are Indian markets' exposure to Turkey.

Jagdish Sharma S.: Yeah, right. Anything we are exporting from Turkey and some direct...

S. Ganapathi: Of course, there will be spinners who are sending yarn to Turkey. There will be people who are sending fabric to Turkey. We are only in the garment manufacturing space -- So there will be definitely other people may have exposure to Turkey, which you have to go after the individual player.

Jagdish Sharma S.: So also when will debt be come down? It will be like , will it come to zero or something at that level?

S. Ganapathi: Our debt?

Jagdish Sharma S.: Yes, sir.

S. Ganapathi: Our debt is at near zero levels only.

Moderator: The next question is from the line of Sunil Kothari from Unique Asset Management.

Sunil Kothari: Just one question to understand. You have moved from Karnataka to Tamil Nadu, which is having a very good supply chain and ecosystem for garment manufacturing, but Bhopal and MP is new. So how you -- what's your experience? Which are the challenges you face? And what is your thought process for a future garment industry expansion for company point of view and at large also?

S. Ganapathi: So from our standpoint, we have to expand in places which are low cost in the long run. And from that perspective, we have identified Madhya Pradesh as a place to grow and we have also identified other places in India which are sustainable in the long run. The wage cost in the south eventually will grow and so will the availability of employees, while the condition in certain other regions of India may be more favourable. That's why we intend creating incremental capacities in those regions.

My early experience in Madhya Pradesh, like we've just started hiring trainees for training purposes, have given me the confidence that there is enough labour available and they have started joining. The training absenteeism are very low. The enthusiasm to work is very high because there is not enough of competing jobs available to them. So I think some of our assumptions are playing out as expected. So if further we are convinced that we are getting a good employee flow, then we should expand more and more in Madhya Pradesh and such regions in the north of India.

Sunil Kothari: But do you feel there is a good ecosystem for -- I mean, in terms of transportation, supply chain...

S. Ganapathi: No, that is not a problem at all. Fabric and all is available in the north. There are several mills like Arvind in Gujarat, Vardhman in Madhya Pradesh itself and so on and so forth. So mills are available from a fabric standpoint. Access to ports from Bangalore to Bombay or Madhya Pradesh to Bombay are all more or less equivalent. Labour availability is good. So we don't see much of a problem from any of these perspectives.

Moderator: The next question is from the line of Abhineet Anand from Emkay Global Financial Services.

Abhineet Anand: Just on the tax rate, seems to be every quarter has been quite different. So for '23 and '24, what could be the number one should be looking at?

A. Sathyamurthy: Mainly on account of recognizing the liabilities which are available for us to claim the deduction at a later point of time is recognized as the deferred tax asset during this year. So this year, our average effective tax rate, you can assume between 17.75% to 18%. Going forward, the effective rate of 25.1% will play out and we should be seeing a number around 23% is our estimation at this point of time.

Moderator: The next question is from the line of Anush Kumar from Spark Asia Impact Managers Private Limited.

Anush Kumar: Sir, what sort of currency assumptions have you taken for FY '23? And in case if we have hedged, would it be average rate at which you've done that?

A. Sathyamurthy: We book forward cover to the extent of about 60% of our revenues for the year ahead based on approved formula for rolling four quarters. And we normally hedge the currency through forward covers. We would have the dollars sold at a forward premium over the prevailing rates. And we also book our orders based on those rates.

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

S. Ganapathi: Thank you so much for all your questions. As a company, we continue to be focused on developing the market. We continue to be focused on delivering tight productivity level so that our margins can constantly be improved. We are margin conscious and profit conscious company. While we go after growth, we would prefer not to compromise on margins at any cost. The market conditions are what they are. But despite that, we have been able to hold on to our markets and we intend growing further.

I see a downturn as an opportunity for Gokaldas more than anything else. Whenever there is a downturn and overall demand from apparel manufacturers come down, we tend to hold the market share at our level from a revenue standpoint. And then when the demand climbs up, we will be able to ride the gains -- the consolidation gains that we have got. So we tend to consolidate suppliers. We tend to take share from other suppliers, which we have been doing at every downturn.

And then once the down -- aftermath of the downturn, we will start seeing a disproportionate growth. We hope to continue that journey going forward. And in the meanwhile, weather the downturn a bit, we will hold on to the margins through all of these. And hope that by the second half of the year, we should start seeing solid growth. But in the run up to that also, we will start seeing some growth.

Thank you so much for being with us at Gokaldas Exports. We will continue to work for the benefit of all our shareholders.

Moderator: Thank you. On behalf of Gokaldas Exports Limited, that concludes this conference. Thank you for joining us. You may now disconnect your lines.