Eureka Forbes Limited (formerly Forbes Enviro Solutions Limited)
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EUREKA FORBES
Friends For Life

August 16, 2023 EFL/BSE/2023-24/54

BSE Limited
Phiroze Jeejeebhoy Towers,
Dalal Street,
Mumbai 400001

Scrip Code: 543482
Scrip ID: EUREKAFORBE

Sub: <u>Intimation of Transcript of Earnings Conference Call held on Wednesday, August 09, 2023</u>

Dear Sir/Madam,

Pursuant to Regulation 30(6) read with Schedule III of the Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements) Regulations, 2015, please find enclosed herewith the transcript of the Earnings Call held with Analysts/Investors on Wednesday, August 09, 2023.

The transcript of the Earnings Call is available on the website of the Company at www.eurekaforbes.com.

Request you to kindly take the above information on record.

Thanking you,

For Eureka Forbes Limited
(formerly Forbes Enviro Solutions Limited)

PRAGYA KAUL
Digitally signed by PRAGYA KAUL
Date: 2023.08.16 19:56:04 +05'30'

Pragya Kaul
Company Secretary & Compliance Officer

Encl: As above

“Eureka Forbes Limited

Q1 FY ’24 Earnings Conference Call”

August 09, 2023

MANAGEMENT: **MR. PRATIK POTA – MANAGING DIRECTOR AND CHIEF EXECUTIVE OFFICER – EUREKA FORBES LIMITED**
MR. GAURAV KHANDELWAL – CHIEF FINANCIAL OFFICER – EUREKA FORBES LIMITED

Moderator: Ladies and gentlemen, good day and welcome to Eureka Forbes Limited's Q1 FY '24 Earnings Conference Call. We have Mr. Pratik Pota, Managing Director and CEO and Mr. Gaurav Khandelwal, CFO with us. 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 star then zero on your touchtone phone. Please note that this conference is being recorded.

Before I hand it over to Mr. Pratik Pota, please note the disclaimer. Certain statements made by the management in today's call may be forward-looking statements. These forward-looking statements reflect management's best judgment and analysis as of today. The actual results may differ materially from the current expectations based on a number of factors affecting the business.

I now hand the conference over to Mr. Pratik Pota. Thank you and over to you, Sir.

Pratik Pota: Good afternoon and I welcome you all to the Q1 Earnings Call of Eureka Forbes Limited. My remarks will be in two parts. I will first speak about the quarter's performance and then frame a performance in the context of a larger transformation journey, Project Udaan. Starting off with Q1, our Q1 performance showed an improvement in trajectory, both in top line and in bottom line. In a subdued demand environment, our net revenues stood at INR 505.3 crores, a decline of 3.8% over last year. This is in the context of an average of a 8% plus decline seen during the past two quarters.

Without the impact of discontinued businesses, our Q1 FY'24 revenues were flat. This performance was driven on the back of volume growth, both in Electric Water Purifiers and vacuum cleaners. Our margin improvement journey continued last quarter with an adjusted pre-ESOP EBITDA margin expanding to 9.8% versus 9.3% in Q4 FY'23 and 8.2% in Q1 FY'23. This is the highest ever quarterly EBITDA margin for Eureka Forbes.

Like I said, it is important to see and understand the quarter's performance in the context of a larger transformation journey. We began our journey by correcting the profitability and cash profile of the business, which has enabled us and given us the headroom to invest in growth levers. From a historical 4% to 5% EBITDA margin range, we have now stepped up to 9% plus in the last two quarters.

Equally, our net debt has reduced by 85% in just one year, which is allowing us to invest in capex to drive innovations and in digital transformation. We also moved fast on the people strategy and have built out a new leadership team at both CXO and CXO-1 levels. This along with some structure changes have helped us bring a lot closer to our customers and to our partners and the early results of this are becoming visible in terms of superior on-ground execution.

A transformation of this scale needs a sense of joint ownership and entrepreneurial energies across the entire organization. Towards that, I'm pleased to share that we have recently rolled out an industry-first inclusive ESOP program under which every single manager at EFL has been allotted stock options. With these foundational blocks in place, we are now much better equipped to drive profitable growth in the business.

In a category and a business that has not seen volume growth for some time, this quarter's volume performance is therefore an important inflection point. We believe that these categories of water and of cleaning and of air are ready for and amenable to expansion and as market leaders, it is upon us to take charge and drive the same.

Additionally, an important factor for us to keep in mind is that in our categories, a product sale is not just a single one-off transaction but opens up an opportunity for lifetime value creation through service revenues, cross-selling, and upselling. Going forward, we will drive growth through a number of initiatives. Number one, increasing penetration and driving category growth.

Our current campaign aimed at converting non-users through improved affordability, improved distribution, and functional communication has shown encouraging results and we intend to sustain the same. Number two, we will drive differentiated innovations with a focus on the premium price segment both in water and in vacuum cleaners.

Number three, we intend to provide our customers an elevated and industry best customer experience in terms of both speed of service and quality as well. Lastly, we will drive growth through best-in-class in-market execution in every store and in every home.

To summarize, under Project Udaan, we have witnessed encouraging progress on profitability, cash profile, and people. Going forward, we are confident that our growth interventions supplemented by our customer and digital initiatives will help in further improving the business trajectory, leading to a sustained and profitable growth.

We are excited about the journey that lies ahead towards the goal of transforming Eureka Forbes into a D2C health and hygiene powerhouse. On that note, I will now hand you over to Gaurav Khandelwal, our CFO, who will provide more details on the financial performance. Over to you, Gaurav.

Gaurav Khandelwal: Thank you, Pratik. Good afternoon, everyone, and thank you for joining us. In the backdrop of a continuing soft demand environment, our revenue at INR 505.3 crores de-grew by 3.8% on a year-on-year basis. Adjusted for discontinued businesses, our revenues were flat. This represents an improvement over previous trends driven by volumes across the portfolio in both water purifiers and vacuum cleaners.

Our gross margins improved sequentially as a result of our cost actions and operational efficiencies. On the cost side, overall expenses before ESOP charge were flat sequentially and declined by 6.6% on a year-on-year basis. Within expenses, our employee cost witnessed an increase primarily on account of increments and new hiring. We expect our employee cost to be range bound from here on.

With the objective of building ownership and alignment for the transformation agenda, ESOPs were given to the managerial cadre in this quarter. This resulted in a non-cash ESOP cost of INR 3.8 crores. It may be noted that, this is not the full quarter impact and we expect the quarterly impact to be approximately INR 10 crores. Given the above, while commenting at the key profitability matrices of EBITDA and PBT, we would be referring to the pre-ESOP EBITDA and PBT and calling them as adjusted EBITDA and adjusted PBT.

Adjusted EBITDA percentage witnessed an expansion of 164 basis points versus previous year and also a sequential improvement by 49 basis points. Our Q1 adjusted EBITDA represents a 15.5% year-on-year growth. Improvement in EBITDA margins was driven by a combination of cost initiatives, operational efficiencies and relatively softer commodity environment.

We recognize the criticality of the cost as a lever and will continue to drive various cost initiatives across the entire P&L value chain. Several initiatives have been executed and we will continue work on creating new pipelines of cost actions. Continuing process improvements led to a net debt reduction from INR 216 crores as of end June '22 to INR32 crores, an 85% reduction. This was also reflected in our finance cost, which reduced year-on-year by 46% from INR 6.3 crores to INR 3.4 crores in quarter 1.

Aided by EBITDA margin expansion and lower finance costs, our adjusted PBT before exceptional items grew by 42.6% to INR 34.8 crores. Adjusted PBT margin for the quarter was 6.9%, an expansion of 224 basis points year-on-year. PAT for the quarter was INR 22.1 crores compared to INR 17.8 crores in quarter 1, an increase of 24%.

To summarize, in a challenging demand environment, the trends on both top line and bottom line show an improving trajectory. We continue to remain focused on executing the transformation agenda under Project Udaan and intend to build on the improved trajectory and make steady progress on other transformation fronts. On that note, I would now like to open up the floor for Q&A.

Moderator: Thank you very much. Our first question is from the line of Ashwini Damani from Ratnabali. Please go ahead.

Ashwini Damani: Good afternoon, Sir. Congratulations on the number, Sir. It has been one year since Mr. Pota has joined the organization. And clearly his work on margin expansion and steadying the ship is visible and we like to congratulate you again on the same. However, as shareholders, we expected some growth on top line since it's been almost one year since the new management has taken over.

But by and large, we are still clocking that same INR 500 crores quarterly run rate on top line. Could you explain to me, what is the reason apart from the sluggish macro? We understand that the macro has been tough, but we expected that, now that the new management has been there for last one year. And when we mentioned that, the category is under penetrated, there has been a transition from old management to new management, we observed that, you have launched new products. We have hired so many people on sales and marketing front and also launched an advertisement campaign. Then, despite all of this, why are the numbers not translating into sales growth? What sort of quarterly or annual run rate are you targeting at least three years to four years down the line? I'll wait for the answer before I ask my second question, Sir, or whatever you suggest.

Pratik Pota: Thank you, Ashwini. Thank you for the question and for your remarks. Before I respond to the question, let me just recap a few data points that I spoke about in my opening remarks. In this quarter specifically, if we take out the impact of discontinued businesses, on a revenue basis, we were flat versus last year. If I double click on that further, the most encouraging green shoots for us came from the volume growth.

And this volume growth came from both water purifiers and vacuum cleaners. You'll remember, Ashwini, that this category and this business has not seen a whole lot of volume growth in the past. And growth has typically come on the back of pricing. And this category has, in many ways, become almost unaffordable for a lot of consumers.

So one stated part of our strategy, as you would recall, was to grow the category penetration, make the category more affordable, more accessible. And the first evidence of that, we have seen is in the form of volume growth coming out. So that's the first, so even as we look at the net revenue numbers and your remarks are valid, within that, it's important to recognize that we are seeing a fundamental change in trajectory as far as volumes are concerned.

And of course, we know that in this category, like I mentioned in my opening remarks, an additional unit sold, an additional customer acquired, is the gateway into a lifetime of value and a lifetime of a relationship being harvested through service revenues, through sale of filters and spares, through of course cross-selling and up-selling. So that's the other point.

Now it's also equally important to remember, Ashwini that, the first couple of quarters, and indeed more of the last one year of the transformation journey, was spent in rebuilding the team, strengthening the foundations, correcting some of the culture issues, and I would say that that's still WIP in many ways. And we now feel that we've begun to lay the foundations, the foundations have been laid. I talked about people earlier in my remarks. I talked about the fact that we've got our EBITDA margins in a range which is much better than where we were last year or before. The net debt has improved significantly, giving us the elbow room to invest in growth drivers.

So all of those are the significant positive news, if you will, which will help us drive growth in the future. If I take a step back, the reality is that these categories are, as you mentioned yourself, having extremely low penetrations. Water is a category which has a universal need, pure water is a universal need, and yet it's a very low penetration category. One large part of that is that the total cost of ownership between product cost and service cost has been kept prohibitively high. Therefore, as market leaders, we are now playing this role of making the category a lot more accessible, a lot more affordable, and therefore growing the category and growing the volumes.

Equally, we recognize that there are many India's, there are multiple customer segments. We also have a large base of installed customers and units who are looking for upgrades. So we are also investing in driving differentiated premium innovations targeted at this cohort of these segments. And you will see the impact of that coming out progressively over the next few quarters. So to pull back and summarize, I think foundations have been laid, volume growth is a very encouraging positive. The fact that our EBITDA margins have broken out from the earlier rebound level of 4%, 5% to almost 9.5%, 10% now, that's the other positive news.

Investments are being made and have been made in driving growth, in driving execution improvement on the ground. And the results of that in terms of net revenue growth, you will start seeing in the quarters ahead. But I would not belittle the work that's been done by the team in the last two to three quarters of just investing in strengthening the foundations that enable much faster growth and transformation.

Ashwini Damani: Thank you. Thank you, Sir. That was heartening to hear. And probably we are building the foundation even more stronger. Sir could you also help us to understand your employee costs? Every quarter, the number tends to throw up surprises. So I'll just take it down. Ex of ESOP cost, it was INR70 crores in June '22, then it shot up to INR105 crores in September '22. It went down again to INR70 crores in December '22, then INR60 crores in last quarter. And this year now, ex of ESOP it's INR72 crores. It's been all over the place and it sometimes comes as a surprise to us.

So I'm assuming there were a lot of new employees that came in, a lot of increments, bonuses that were given in. But still, if you could help us breaking it down as to how many full-time employees we have, how many contractual employees we have, why the employee cost fluctuates so much? The representatives at stores that we have, one or two representative at every, say, Vijay Sales, etcetera, are they on our company payroll? Similarly, the AMC people who visit our homes to do these services, are they on the payroll and how is that count increasing or decreasing?

Gaurav Khandelwal: Sure, Ashwini, hi, this is Gaurav. Thank you for your question. So I think you're right in pointing out that there has been a fluctuation over the past four quarters, but I think it goes back to the point that it's been a journey where we've been putting the foundations in place, and that has meant that there have been certain actions at different points in time.

I think it's important to call out two things. One, we are at a stage where if you look at a quarter 1 cost, that pretty much represents in some ways where we would want to be. It factors in the investments that have been made in capabilities. So from here onwards, one can expect that the cost is going to be range bound from where we are now. That's one.

The second is to your question on the breakup of the employees. That is something that we don't share, but I think it's important to call out two or three things. One, the service technicians who work with our service business partners, they are not on our payroll. So we just want to clarify that.

Number two, the sales force that is there with our distributors, with our partners, that again is something which is on their payroll and not ours. Whatever payout happens to them is covered through the trade margin which we give out and which is market benchmarked. So I just wanted to clarify that, but I think at a macro level, we are at a stage where we've built the organizational capability that we wanted, and from here onwards, one can expect it to be a range-bound employee cost line.

Ashwini Damani: Thank you Sir, thank you for the answer, I'll come back in queue.

Pratik Pota: Thank you.

Moderator: Thank you. Our next question is from the line of Atul Tiwari from Citigroup. Please go ahead.

Atul Tiwari: Yes, thanks a lot for the opportunity. So just two questions. What was your market share in the key categories that you are presenting in the first quarter?

Pratik Pota: So, Atul, thank you. Thank you for that question. Our market share, as you would know, is a combination of the shares that we have in retail, both general trade and modern trade. Our market share that we have in our e-commerce channels and the marketplaces, as also the contribution that we get from our direct channel where of course the market share obviously is 100%.

I'm happy to report that in the quarter 1 just gone by, we reported a sequential increase in market share in the water category. In the water category, as you know, we are market leaders and we are dominant leaders in the VC category.

Atul Tiwari: Okay, Sir. And Sir my second question is, beyond these two categories given the kind of distribution that you have on a pan-India basis, which other products, you could launch over the next three years to four years? I'm not asking about whether you have actually plan of launching them or not as of now, I mean those things can evolve in future but given companies strength in terms of distribution, brand name and after sales services, which other product categories are amenable to being launched by you?

Pratik Pota: So Atul, I agree with you that we have an extremely strong brand. We've got an omnichannel presence. We've got a national service network. We're beginning to put in place a very strong digital footprint, digital backbone. Those are very, very important foundational strengths. That said, we believe that the headroom that we see in our existing categories, which is water, water purifiers and water adjacencies, like water softeners, etcetera, cleaning, and in air, in these categories itself, there is so much of runway that we see for growth that for the immediate future, we intend to remain focused on these three categories. To drive both penetration and to drive through premiumization and through market share gains.

In many of these categories, as you know, there is a significant portion of the market that is unorganized. And therefore, it's also our intention to try and upgrade, convert these users into the organized segment. So to come back to your question, for the immediate future, this is our limit, and this is the category portfolio that we intend to operate with. Beyond the first, beyond the next two years, it's hard to conjecture now, but this is where we intend to remain focused right now.

Atul Tiwari: Okay, Sir. Thanks, thanks a lot.

Moderator: Thank you. Our next question is from the line of Aniruddha Joshi from ICICI Securities, please go ahead.

Aniruddha Joshi: Yeah, Sir thanks for the opportunity. Two things, can you indicate about the innovation and the new products that probably you would have launched in this quarter itself.

Secondly, now the margin has significantly improved. So what is the real cost that we would have cut or has this margin improvement come across the various cost. Can you articulate a bit more on how the margin is we are able to improve and what is the further scope to improve the margin over here. These are the two questions and I will come back with more questions. Yeah, thanks.

Pratik Pota: So thanks, thanks for the questions. I'll respond to the first question. And I'll request Gaurav to respond to the question on margins. I think on innovations, both in water and in cleaning, we have a portfolio that straddles multiple segments, multiple price points, and allows us to therefore offer different propositions to different customer segments. We have in the last three to six months rolled out a number of innovations at different segments. I'm happy to report that in most of these innovations, we have made significant progress.

To illustrate with one example, in the stainless steel segment of water purifiers, we have made two launches in the last three months, actually more than three months, last three to four months, and we have seen a significant impact of that in terms of both growth and in terms of market share. So that's one part of my answer.

Equally in our category, it's important to recognize that innovations, while product innovations will certainly play a role, we also have a lot of room for business model innovations beyond just product. So there's a lot of work that's going on and which we'll see light of day very soon in terms of different model innovations which will allow us to offer customers more affordable options both in terms of product and in terms of service, easier access and more convenient access through better control and through more digitization, as also in driving more of improved customer experience. And this will be across multiple categories.

So you will see that play out in the coming quarters. But I think the great news and what gives us a lot of encouragement and confidence is that whenever we launch an innovation, I think given the nature of our brand, there's a lot of acceptance, distribution happens, we get a lot of consumer interest, and then there is immediate pickup and immediate trials.

So excited to say that we have invested in the last six months now in strengthening our R&D and innovation team. We've got capabilities strengthened in electronics, in design and engineering, in the cleaning category, in water itself and water adjacencies, and in marketing we've rolled out a category specific structure. So between the new marketing structure and strengthened R&D and innovation capabilities, we are very, very confident about rolling out a very aggressive innovation plan, an innovation calendar in the coming few months. GK, on the margins, please?

Gaurav Khandelwal: Yes, Aniruddha, just to shed some light on the margin, I think first as a principle, the approach that we are taking is to look at the entire value chain of the P&L and see where the opportunities lie. And if I were to give you two examples of that, so one key enabler for cost efficiencies has been digitization. So if I were to just compare the number of customer complaints that came on app versus a call center over the last six months, it has doubled, which automatically means that there's a flow-through effect on a call center cost, for example.

Another example is that while we've built newer capabilities in people, and that is something that you see reflected in the people cost line, that has also gone hand-in-hand with reducing our dependence on outsource partners. So there are a lot of work which was being done by outside firms, consultants, etcetera. We've got that work in-house. So these are just two examples, but at a principal level, our work continues across the entire P&L value chain. There are still opportunities in COGS, there are opportunities in procurement, and we are striving across all opportunities.

Having said that, from our perspective, when we look at profitability improvement, we are not just seeing it from a lens of cost only. We're equally cognizant of the fact that operating leverage will come from growth. And hence, while we root out inefficiencies, we're equally very, very focused in investing behind growth as well.

And I think we spoke about our new campaign in the last earnings call, and I think the fact that a category which has not seen volume growth for a while, for that to appear in this particular quarter is a signal that this category is amenable to growth investments and we will continue to do that. But we believe that, there is still leeway in cost actions that we will take, but at the same time, invest in growth so that at an overall level, we're able to get operating leverage from growth.

Aniruddha Joshi: Okay, Sir, that's helpful. And last question, so there is a mention about B2B sales in the presentations also. So what exactly is the percent of revenue? Who are the major customers, etcetera and in this business? Yes, that's it from my side, thanks.

Pratik Pota: Your voice was breaking up a little bit, but I assume you're asking about B2B, so let me respond to that question. Yes, we also have, in addition to our B2C business, which is of course the more familiar business that we all know of, we also have a B2B business under the name of Forbes Pro. Under this, as part of this business, we cater to institutional customers and SMEs through both our own channel, our own company run channel, and also a network of partner run channels.

And we have a presence directly and through our partners in roughly the top 60 cities in the country. So that's about the B2B business. It's been an important part of our portfolio. And as part of this, we also service these devices. And the devices that we install also get a service revenue, which we then are able to benefit from.

Aniruddha Joshi: Okay. Understood, Sir. Sorry one more question. We have seen many brands which sound very similar to Eureka Forbes something like there is a brand called as Sureka Forbes and I guess they have a website etcetera and again business also, so probably Eureka brand has got more, you can say, awareness than the actual sales. So there might be some guys, who are there in the market. So how do we tackle this issue and what are the efforts done by the company in this regard? That's it from my side. Thanks.

Pratik Pota: Thanks Aniruddha. Let me be absolutely unambiguous and unequivocal about the first part of your question. Sureka Forbes is a fraudulent entity and it is cheating customers in its area of operation. We have filed, there's a legal case that's been filed, a criminal case that's been filed, the matter is sub judice and we will take this forward and make sure that, there is no further possibility of this entity cheating our customers and misrepresenting, who they stand for.

More generally, if I step back, and I refer to this point earlier as well, we are aware that there is a large market, which is an unorganized service market, which is catered to by small operators across most markets in the country. We intend and we have rolled out a very clear and focused program of converting this grey market and this parallel operation through a combination of three or four things.

First one, from a legal point of view, we are working with the authorities to identify these grey market operators, manufacturers of fake filters, distributors of fake filters and going after them. So that's one work stream. The other vector is about creating customer awareness, ensuring that our customers are able to discriminate and identify easily what is a genuine Eureka Forbes AquaGuard filter and what is not.

Number three, we are looking to differentiate our filters and to make sure that there is both a visible and a functional advantage that comes from Aqua guard filters. So through a combination of these work streams, we intend to attack this parallel market. Additionally, I spoke earlier about the fact that this category has kept the cost of ownership high. That has been, like I said, both in terms of product cost and in terms of service cost.

And the high cost of service actually is a barrier in driving data penetration. So we intend to make, just like we've done with product affordability, we intend to drive service affordability as well and open up a service offering to a much larger segment of customers at different price points with different segmented offerings. This we believe, combined with the other actions, I spoke about, will help grow our service universe and our service footprint significantly in the country.

Moderator: Thank you. Our next question is from the line of Parth Sanghvi from Nepean Capital. Please go ahead, Sir.

Parth Sanghvi: Yes, I guess my question is building on the previous question of the INR500 crores of top line, how much of that would be from your recurring annual maintenance contracts?

Gaurav Khandelwal: Yes, Hi, Parth. Thank you for your question. So we don't share the split of our product and service business. And to be honest, the reason for that is, in some ways in the previous question itself, this is, we believe, important competitive information. And given that, we are in a unique place where we have a large customer base and where there is an opportunity to convert that base into a service revenue, convert people who are from the unorganized market into a service revenue for us.

This is something that we believe is important competitive information, and hence we've kind of stayed away from giving the split of this. But while that's one part of it, the second part and the more important part is the fact that there is a very large universe of customers, who today are being serviced by parallel market or grey market operators. One of the names was taken on the call earlier and we believe that in itself is a very big opportunity. The more we make our service offerings, our AMCs, available, accessible and affordable.

We believe that this is a very big opportunity to unlock, and hence our focus is going to be on this area, both through demand side actions and equally supply-side actions that Pratik spoke about earlier.

Parth Sanghvi: Okay, that's fair enough. Let me ask the question a slightly different way, and I'll tell you where I'm coming from. I'm trying to gauge the opportunity out here in the years to come. So, right now you have 8 million customers. I'm assuming a fair number of them have some sort of management contracts, do you know how much that I am assuming everyone gets it serviced every year or periodically you only probably see a small portion of that. So, do you know how many of 8 million customers you are servicing right now, can you share that or is that something you want to keep to yourself right now?

Gaurav Khandelwal: But we don't share the split of how many of those 8 million customers are on contract. I think suffice to say that the number of people who are not in contract is more than the people who are in contract. And I think that gives you a sense of the opportunity that is there. And the reason we find ourselves in this position is the fact that one, there are these grey market operators that we spoke about.

But equally, as a company, how do we make our offerings more attractive, more differentiated, is something which would enable us to start converting this base. But the big picture is that there are more people who are not in contract than in contract and therein lies the opportunity.

Pratik Pota: And just to add to that part, I think the opportunity would require us to actually approach this from very different perspective. Like Gaurav said, there's a large universe of customers, our own customers with older devices who are not in our contract universe and they could turn to the grey market for service and for filters.

Now one reason for that is that we've not allowed ourselves to become easily accessible and available to read customers. So, one apart of the solution, apart from doing the work that I spoke about earlier and Gaurav spoke about earlier on making service more affordable, would also require us to have a go-to-market solve in making our filters, our service much more accessible to our customers who are not in contract. So that's the other work that's going on that will help us in the quarter ahead.

Also, I want to go back to what I said in my opening remarks, which is that today's volume is tomorrow's AMC revenue and tomorrow's service revenue. And the fact that we are seeing encouraging volume growth gives us that runway a few months from now, a year from now, in strengthening our service annuity stream. And like I said, this category's always been plagued with below par volume growth.

And the fact that we are now able to stoke volume growth, drive conversions, drive penetration, and drive more customers and increase the customer franchise tells us that down the road, we can expect to see an equally strong momentum build up in service as well.

Parth Sanghvi: Got it, and just to clarify, if I take an annual maintenance contract, the person coming to my house to change the filter, is he on the rolls of Eureka Forbes?

Pratik Pota: No, no, Parth he is not. The technician who comes to your home is employed by a business partner who are engaged with us and who get commissions on the AMC and on every product

Parth Sanghvi: And in that case, how do we ensure that they are selling Eureka Forbes product as opposed to a spurious product?

Pratik Pota: Absolutely. And that's one part of the challenge that I spoke about earlier, through customer awareness, through ensuring that we create differentiation of our filters, and the fact that we clamp down on the supply itself from the back end of these fake filters and various other means that you like to do and drive especially the digital interventions.

And you will see that play out in the months to come. But you're right, the fact that this network is a partner network requires us to put in place stronger controls and stronger governance to convert the AMC customer to a Eureka Forbes AMC customer.

Parth Sanghvi: Thank you so much. I'll get back in the queue.

Moderator: Thank you. Our next question is from the line of Praveen Sahay from Prabhudas Lilladher. Please go ahead.

Praveen Sahay: Yeah, thank you, Sir, for taking my question. The first question is related to the service expenses. There we have seen a reduction and also if I recall the last call you had said around 50% service request coming from the call centers and which you are transferring to the digital initiative. So, is it a result of that only or something more to that?

Gaurav Khandelwal: Sure. Thank you, Praveen for your question. So, the service charge line that you see on the P&L is a combination of the complaint call charges that we pay to our service business partners, the cost for call center that is there, the cost that is paid for installations, for managed services, and also the cost that is paid to our business partners as trade margins. The reduction that you see is largely attributable to the fact that we've been able to make decent progress on some of our digitization initiatives and that have helped in reducing this particular cost line.

Praveen Sahay: And there is a further room for reduction here as well?

Gaurav Khandelwal: We will continue working on it on an ongoing basis to see what opportunities can be extracted in this area.

Pratik Pota: Just to add to that, to what Gaurav said, Praveen, Q1 FY'23, in other words, same time last year, a dominant share of our complaints came from the call center, the voice channel, almost 70%. And the balance 30% came from unassisted means, digital, WhatsApp, etcetera. That number has completely inverted in Q1 of FY '24. More than two-thirds of our complaints now come digitally or through non-assisted channels, with only a third or under coming from our call center. So like Gaurav said, that has had some impact on call center savings, but more importantly, it's also improving, helping improve the customer experience and giving customers much greater visibility, much more control on their entire service journey.

Praveen Sahay: Okay. Next questions are related to the service revenue. So as you had also mentioned about the grey market operator in that, can you give some sense of how much of the market of servicing is done by the grey market operator?

Pratik Pota: Praveen, it's hard to give a precise estimate because of the nature of the grey market that exists. But I think it's important to pull back and go back to the earlier point that Gaurav made, which is that the share of customer service by the grey market or the parallel market, I won't just call it the grey market, is larger than the share that is serviced by the official Eureka Forbes channel, pointing to the vast opportunity that exists and the fact that with our effort, we can actually harness and tap into that and drive growth.

Praveen Sahay: Just to add on this, this parallel market is also, you know, service through the partners, channel partners only, right, Sir? So if you have also a channel partner, how to differentiate actually in the services?

Pratik Pota: So this parallel market for the larger part, Praveen, comprises local service operators with a few technicians. Sometimes it's just one technician himself who's almost like an entrepreneur servicing devices in his area. In some cases, these happen to be old Eureka Forbes partners who were trited many, many years ago and continue to operate in this space. And therefore the ecosystem of the parallel market is largely of this nature.

Gaurav Khandelwal: And Praveen, just to add, I think the unlock to this opportunity is not just from a supply side, where it is on grey market operators, but equally from a demand side. Because come to think of it, if most of us are asked, where can you buy an AMC or a water filter, we may not even know, you know, but that would not be the case in many other categories. Hence, while we focus on the supply side, there is equal focus on the demand side as well, where the focus is on making AMCs, filters, consumables more available, more accessible, more affordable.

Because then if it's a combination of both these things coming together, and when you marry this with consumer education, then it becomes a three-pronged approach to addressing this opportunity in its entirety. So our intent is to operate on all the three vectors because the opportunity is fairly substantial.

Praveen Sahay: Great, Sir. And the last question related to the more affordable range of product and the services as you had mentioned, which has driven the volume for you for this quarter. But same time also you had mentioned that the premium price segment more of SKUs launch the way forward. So can you give some sense the way forward, how is the mix going forward like affordable versus a premium in the services as well as in the product categories?

Pratik Pota: Thank you Praveen, I'll respond to that question. I think the very interesting and encouraging part of this category is that we see abundant room to grow both the economy segment by driving penetration as also the premium segment. Let me start with the first part, the economy range first.

You're aware that the penetration of water purifiers in the country is just about 5%. And the barriers are many, primarily being affordability, the total cost of ownership, number one.

Number two, sometimes perceived lack of need. So our campaign that we ran recently, wherein we offered an AquaGuard priced as low as INR 6499, accompanied by a campaign which talked about the need and created dissonance vis-a-vis our cloth filters has worked really well and helped drive growth of the economy segment. This is one area where we intend to stay focused and continue to do more work.

Just one data point here which gives us a lot of encouragement is that more than 80% of customers who bought this economy device were first-time users, who actually had not entered the category, and they were converted by the campaign along with the price point, and of course, the promise of AquaGuard brand, the brand trust. So that's one part.

Equally, we see that there are customer segments who are looking for differentiated offerings, looking for premium offerings with superior aesthetics, superior functionalities, very, very different form factors. And we are looking to innovate across these price points as well, across these consumer points as well, across these consumer segments as well. So as we go forward, you will see our innovations play out in the premium segment, in the mid-price segment, and also you will see us drive growth and affordability in the economy segment.

Praveen Sahay: Okay, great. And is there any focus on these categories for different channels, like for premium in the certain channels and the economy or affordable in the certain channels?

Pratik Pota: Yes, Praveen, and that's a really good question. And I think the advantage that we have as an omnichannel player is that we have a unique and advantage direct sales system, which allows us to go to customers' homes, evangelize and build categories, evangelize and sell premium products. And therefore, the role of the direct sales channel will remain focused on premiumization, replacement selling, and category creation.

Again, in a category like cleaning or even a category like water, there is room for us to grow penetration at the premium price points. So the direct sales team and their channel will be focused on premium offerings in water and in creating new categories. In retail, general trade, given the nature of the category, the task there is distribution expansion. And just to again put some numbers to it, the universe of small domestic appliances are available in more than 2 lakh outlets. And within that, water purifiers are available in a small fraction of that, under 19,000, almost 20,000.

So the task here is for us to grow distribution and that is best done with an economy offering taking the lead. Of course, once the economy product enters the outlet, we cross-sell our entire portfolio, but the pricing open of the outlet and the outlet opening is done by the economy range. Equally in retail, we have modern trade, which caters to a much more affluent, much more aware, much more discriminating customer, typically a replacement customer. And then the task again is to offer premium offering, differentiated offering, with outstanding and superior on-ground and in-store execution.

So the fact that, we've got the e-commerce, of course, the use cases are many, both in category creation, especially in Tier 2, Tier 3 towns, and also in premiumization. So the fact that, we have this mosaic of channels allows us to play our portfolio differentially by channel, and will also therefore drive growth, drive penetration, as also drive premiumization.

Praveen Sahay: Well explained Sir, thank you for this. Just one clarification that's, a direct is still the highest contributor in your channel, right?

Pratik Pota: I think Praveen, direct used to be as you're aware, the dominant channel. Over the last few years, we've built a very strong and a very robust retail channel as also a fast-growing e-commerce channel. So the contribution of these channels are equitable and symmetric and direct is no longer dominant.

Praveen Sahay: Great, thank you Sir. Thank you for the detailed explanation. All the best.

Pratik Pota: Thank you.

Moderator: Thank you. Our next question is from the line of Devika Jain from Ratnabali Investment Pvt. Ltd. Please go ahead.

Devika Jain: Hello. Congratulations, Sir, on the great set of numbers. So I basically wanted to understand the line item. Sorry. I would want this next question. What do you think will help us in revenue growth? So our typical levers would be product, price, reach, or availability and innovation. What is our geographical reach right now? What do we expect three years down the line? From availability point of view, can you bifurcate region by distributors? And also, if you can break it into urban versus rural, what will be our pricing strategy going forward to target those customers, who don't use a water purifier now? And lastly, what are we doing in terms of innovation and brands so that we don't get crowded out on such space?

Pratik Pota: Thank you, Devika. On a lighter note, your question is like the question that I asked in my internal reviews and pushed my team for more and more information. But coming back to your question, our strategy for driving growth is simple and is clear. Let's start with first water. In water, we have an exciting task to grow penetration by identifying category barriers, unlocking the affordability barrier, and driving distribution. So that's the first part.

Equally in water, we have an exciting task of premiumization through our innovations, through differentiated value-added offerings, both functional and otherwise and form factors and so on. So that's on water. Equally, like I said earlier, in water we have a distribution task and we have a larger category expansion task. So there is that work stream which is clear on water. In the non-water categories, the categories of cleaning of air, similarly we have a penetration task. Vacuum cleaners, if anything, have even a lower penetration than water purifiers as we know.

The task there is also premiumization. So even as we grow the category in cleaning, we also intend to double down on the premium segments of uprise of robotics, which are part of what we call the convenient cleaning segment. And this segment has grown significantly post-pandemic, where consumers are looking to have very accessible and very less effort-intensive cleaning solutions. So that's the second area of work for us.

The third area of growth opportunity for us is, as we mentioned earlier, in expanding the service universe. Recognizing that a large part of our customers do not avail right now of our AMCs and our contract service, how do we reach them through a combination of more affordable AMCs and affordable service, filter sales sold to them directly, and other means, and creating awareness as well. So that's the third revenue stream.

The fourth revenue stream and the fourth area of growth for us will be digital and D2C. The fact that actually Eureka Forbes was India's first D2C company many, many years ago, and still we have a very large access to a direct sales network and a service network. We will build on top of that a very strong digital backbone and use that to drive D2C sales, starting with service, but eventually your product as well.

The good part is that when we look at a growth profile of quarter one, we saw encouraging volume growth. We saw volume growth across the population strata, in both in metros and in Tier 1 towns, as also in the Tier 2 and Tier 3 towns. Equally, just like we see opportunity in growing penetration in the smaller towns, we also see opportunity in growing penetration and driving premiumization in the metros and the Tier 1 towns as well.

So more broadly, if I pullback, there is an abundance of opportunity. And the work that we've done in the last one year in strengthening the foundations, rebuilding the basics, put us in a very, very unique and a very, very strong place to harness and to drive the growth, both through category expansion and through market sharing.

Devika Jain: Thank you so much, but one more detail if you could give me, as on date, can you bifurcate the region wide distributors that you have and also urban and rural breakup?

Pratik Pota: No, Devika, I'm sorry, that level of detailing we don't give. But suffice it to say that we are lucky to have a strong nationwide and national presence across all regions. I think we are one of the few brands in this category who provide a national service network which goes down to even small towns. So both product availability and service availability is across Forbes Data.

And through combination of our direct sales channel, with a company-owned channel and a partner channel, retail channel, and of course, e-commerce, supplemented by the large service network that we have across 10,000 plus pin codes.

Moderator: Thank you. Our next question is from the line of Rajesh Kothari from AlfAccurate Advisors, please go ahead.

Rajesh Kothari: My first question is, I think a couple of times you kept insisting that the category is currently not affordable, and therefore as a market leader you would like to make sure that the affordability of it becomes more affordable product. Now in that endeavour to make it affordable it means are you saying that the current product pricing point you need to reduce or you need to introduce products which are a little bit completely different with a much lower price point? And if answer to that is yes, then how do you see that impact on it on the gross margin? That's my first question. I'll follow up with my second question once I get the feedback on this.

Pratik Pota: Okay, first question, okay, I got it. Well, thank you, Rajesh, thank you for the question. And you're absolutely right, we've talked about this a couple of times on the call, and we believe very strongly that one factor that has held back category growth and penetration and universalization has been the high cost of ownership. Both the high threshold entry cost of product as also the recurring cost of AMC. And we intend to expand the category by making the product and service more affordable.

We will do this by offering customers fit for purpose, customized segmented propositions at the right price points. We saw the impact of that play out in quarter one. Just one call out that I want to do, that the growth in quarter one did not come because of any price drop. We took no pricing action in quarter one. There was no price reduction.

And we saw significant growth come in our value offering. So going forward as well, we intend to grow the entire portfolio. We will drive the economy range, even as we drive the premium offerings, the premium segments, through innovation, through differentiation, etcetera.

I'll toggle the question on gross margins to Gaurav in a minute. But before I do that, I want to underline and call out that the right metric for us to look at is not gross margin, it's look at EBITDA and overall profitability. In this quarter, you saw us deliver good EBITDA increase with a muted revenue performance, but on the back of volume growth.

And going forward as well, we are confident and we believe strongly that as we expand the customer franchise, as we get more customers and grow volume, we will be able to deliver sustained and profitable growth progressively quarter after quarter. Gaurav, you want to respond to the other question?

Gaurav Khandelwal: Yes. And Rajesh, coming to your question on gross margin, I think I would see it slightly differently, because one way to look at gross margin is just from, let's say, a price lens and a mix lens and see what the downsides are. But I think there are two or three important things to keep in mind. One is that we have a fairly spread out portfolio. So our ability to mitigate any impact on gross margin is also very high, because we straddle across channels, we straddle across price points. That's one.

Number two is that for us, volumes also create opportunities for cost efficiencies. So higher the volumes also means that our procurement gets better, our freight gets optimized. And this, when we marry it with a cost program, also delivers efficiencies which, you know, can offset any mixed impact.

The third thing is that affordability doesn't necessarily mean just the pricing play. I think it's important to reiterate what Pratik mentioned, that fit for purpose is in a very important part. What you offer to a customer at let's say a INR 8,000 price point versus an INR 18,000 Rupee price point are different products with different specs and they also come with different cost structures.

So that's the way you know one needs to see it. It's not just while there are competing factors at play, while there are certain factors which may create a pressure on gross margin, but there are equally factors which provide a mitigation. But from our perspective, we are keeping two big things in mind. One is the fact that for us, a product sale is the first step towards creating a lifetime source of value in the form of an AMC revenue or cross-selling, etcetera.

The second is that we would be navigating the business basis an EBITDA margin. I think we believe there is adequate flex available across all P&L lines and without necessarily pegging ourselves to a gross margin line, what we will seek to optimize will be on the overall EBITDA profitability of the company.

Rajesh Kothari: So, Sir, your economy segment, correct me if I'm wrong, probably will be bulk of your revenue, right? I don't know, do you provide a mix? I'm not too sure.

Gaurav Khandelwal: We don't give the mix, but that would not be the case. I think the best manifestation of that would be the gross margin percentage that you see.

Rajesh Kothari: No, no I'm saying in terms of revenue mix, the economy would not be the largest, is it?

Gaurav Khandelwal: We have a fairly spread-out portfolio. We straddle across different offerings. Economy is just one part of it. There is a mid-segment, there is a premium segment and across the board we've got offerings.

Pratik Pota: Let me add to that, in fact that's not the case at all. I think we have a very strong presence in the mid-price and the premium segments and we have now as I said made increased efforts to grow the economy segment and to grow the category. As I mentioned earlier, a dominant share of the customers who buy economy products have come from being non-users earlier. They are new adopters of the category. So it would not be accurate, it would be in fact incorrect to say that a large share of revenue comes from the economy segment.

Moderator: Thank you, Sir. We move to our next question is from the line of Ravi Adukia from PGIM Mutual Funds.

Ravi Adukia: My question is Sir, you gave a good kind of color on your strategy, but if you could talk a little bit on your aspiration in terms of revenue growth over next three to five years? So, this is my first question. Second question would be if you can give some color on movement in working capital in the current quarter and the capex you foresee over next few years. So, that's all for my side.

Pratik Pota: Got it. No, thank you. I'll request Gaurav to answer the question about the working capital in a minute. But before that, let me respond to your first question, Ravi. I spoke earlier about the fact that we are fortunate to operate in a category landscape with extremely low penetration and the fact that this offers a strong and long runway to grow.

We are also fortunate to have an incredibly strong power brand in Aquaguard which has universal trust, of course universal familiarity, and universal acceptance. We are also fortunate to have a strong omnichannel mosaic, an omnichannel network, between retail, e-commerce, and the uniquely advantaged direct sales channels.

We also have a very large service network across the country. So these are very, very strong foundational enablers that we have in place to leverage the opportunity. Like I said earlier, our strategy is predicated on number one category expansion and growing volumes, even as we also differentiate and offer our customers premium offerings.

And it's also predicated on growing the portfolio by playing much more aggressively in cleaning, again across multiple price points, including the premium segment. The third area is about D2C and using our D2C platform and our growing D2C presence to drive direct to consumer revenues.

And the fourth piece, of course, is about service and how do we improve customer service and how do we expand our service network. We talked about earlier in the call about how do we tap into the battle market and the grey market and expand both our contract revenue and our filter revenue through a combination of a number of initiatives, including driving more and more customer awareness and improving service affordability.

I think all of these initiatives are beginning to play out. Some early results were visible in the results in Q1. And we are confident that as these initiatives get rolled out, we'll see more and more impact and more and more outcomes, and more and more visible outcomes play out across volume growth, across revenue growth, across EBITDA margin improvement, customer satisfaction improvement, and just in overall getting our business much more future ready. Gaurav?

Gaurav Khandelwal: Yeah, and we're coming to your question on capex and working capital. On capex, we'd last given a guidance of INR 75 crores to INR 90 crores for the year. We continue to stay to that. I think the important part to call out is that this capex is steered towards, one, creating an innovation pipeline for us, not just for this year, but beyond that, the idea being that this then becomes an enabler for growth.

Number two, this capex could be spent on digitization efforts. And as we progress during the course of the year, we will see the capex step up. Coming to working capital, it remains a very, very critical area of focus for us. You've seen our net debt numbers go down 85% year on year and a lot of it is driven by our focus on driving working capital efficiencies. This is an area where we will continue to keep working on because we believe there are still opportunities in this area and we take it from there on.

Moderator: Thank you. Ladies and gentlemen, that was the last question of our question and answer session. I would now like to hand the conference over to Mr. Pratik Pota for closing comments.

Pratik Pota: Thank you everyone for joining the call today. I hope that you were able to address your questions satisfactorily. And in case you have follow-up questions, or in case some queries have gone unanswered, or if you want more color, please reach out to us, and we'll be happy to respond. Thank you so much for your time and have a very good day. Thank you.

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

Note:

1. This document has been edited to improve readability
2. Blanks in this transcript represent inaudible or incomprehensible words.

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