Himatsingka

Himatsingka Seide Limited

10/24, Kumara Krupa Road, High Grounds, Bangalore – 560 001
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"Q2 Financial Year 2014 Results Conference Call"

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Participants: Mr. Shrikant Himatsingka, Executive Director
Mr. KP Pradeep, President Finance and Group CFO;
Mr. Ashok Sharma, AVP Treasury, Taxation and Company Secretary
Mr. T G S Gupta, AVP - Finance

Moderator: Ladies and Gentlemen, Good Day and welcome to the Himatsingka Scide Limited Q2 FY-'15 Earnings Conference Call hosted by Macquarie Capital Securities Private Limited. 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 this conference call, please signal an operator by pressing '*' then '0' on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Amit Mishra from Macquarie Capital. Thank you. And over to you Mr. Mishra.

Amit Mishra: Good Evening, everyone. It is our pleasure to host Himatsingka Seide Post Results Conference Call today and thank you very much all of you for participating on it. To represent the company, we have with us today, Mr. Shrikant Himatsingka – Executive Director; Mr. KP Pradeep – President, Finance and Group CFO; Mr. Ashok Sharma – Associate Vice President, Treasury, Taxation and Company Secretary and Mr. TGS Gupta – Associate Vice President, Finance. I would now like to hand over to Mr. Himatsingka for opening remarks. Over to you, sir.

Shrikant Himatsingka: Good Evening, everyone. I thought we could begin this call by me giving you an overview of where we stand as a Group and also share with you certain key focus areas that we are concentrating on as a Group today. It will help give you a perspective on both our Manufacturing and Distribution businesses and help you better understand our numbers.

So, to begin with, I would like say that we remain extremely focused on sweating our Manufacturing assets of the Group. As you are aware we have two manufacturing plants – one for Bed Linen one for Drapery and Upholstery – and what we are doing is we are focusing on raw material optimization across the manufacturing value chain, we are focusing on automation or enhanced automation I should say, we are focusing on asset productivity across all the kinds of asset bases that we have in these manufacturing facilities, and obviously we are also focusing on the manpower productivity at these locations. In addition, product mix remains a focus as well.

So if I look at these five themes that we are focusing on, as a result we have seen substantial improvement in our Manufacturing performance both for the quarter and for the 6-month period-ended September 30th and obviously as we go through this call, you will get a better feel for the

Manufacturing numbers, I would not get into that at this point but my point here is that all the efforts the Group has been making to sweat its Manufacturing assets have started to show results from a standpoint of EBITDA margins, from a standpoint of asset productivity and so on. So that is one focus area and we remain committed on that.

Secondly, I would like to say that we are exploring growth opportunities for our Manufacturing Operations given the maturity and stability of our current operations. So as you are aware the Bed Linen units is operating at a utilization of close to 89% and at this point the Group has begun exploring the various options on expanding this manufacturing capacity, which we will share at a more appropriate time, but we have begun that process, we are also looking at exploring various other opportunities in the manufacturing space in order to expand. So this is a second area of focus of our Group.

Moving on to the Retail and Distribution space, we have enhanced our focus on the Group brand portfolio. We are in active discussions to take on brands both national and proprietary, specific to the North American markets. This has been an important theme for the Group – we have shared this earlier as well – and the discussions are progressing well. We currently operate portfolio of 10-11 brands across the Group. For FY-'14 we had done 636 crores in Branded revenues. We should see some improvement on the quantum of Branded revenues this year, and we remain committed to see a serious upside on Branded revenues over the next couple of years.

In addition to the portfolio focus on Brands, we are also focusing on reorganization initiatives which are in progress in North America, and this is largely focused on integrating our two operating entities in that geography. So when I talk about "Reorganization Initiatives" it essentially involves the following: We are undergoing organizational restructuring from a perspective of the way the two companies will integrate organizationally from a talent perspective and also structure itself to be more brand-focused. We are incubating larger portfolio of brand and allied product development and design capabilities. So we are already in the process of aligning ourselves to be more focused with a larger Branded portfolio and therefore have already begun onboarding several initiatives that relate to allied product development and design capabilities for these brands. We are also focused on integrating our supply chain and warehousing capabilities as we have rationalized our supply chain into one zone from two zones. We are also on our way to launching SAP globally. Obviously, we have completed our Manufacturing activities, we have completed our India retail activities, we have completed our European distribution platform which has gone on to SAP in October and North America will be completing in the Q4 of this financial year. So there is a large amount of efforts that is ongoing on that front. And we are also looking at reorienting our brand positioning and price points vis-à-vis existing market conditions. What I really mean by this is if we have a significant presence or shelf space with a particular brand and we are seeing the price points are going to be changing as far as the markets are concerned, we are pulling out certain price points from the shelves, we are injecting new price point-based products into the shelves and taking greater shelf space if possible with a more attractive price point. Sometimes, these initiatives as you will see it, it will cost us upfront, and it will impact some gross margins on the Retail and Distribution front in the short-term, but we feel that it will keep us in good stead to drive growth and profitability for these divisions going forward. So these initiatives on the Retail and Distribution front will impact operating performance of North America through fiscal '15, but we believe it will give the Group a more brand-focused leaner and more efficient distribution platform to drive growth. So this is our focus on the North America side.

On the European front, we are focused on stemming our losses and turning profitable for this division, we have closed unprofitable stores, we have optimized our team strength, we have been leveraging the brand by looking royalty streams because the brand is a heritage brand and attracts various other category operators to look at licensing this brand from us, and in addition, we are also looking at increasing its geographical presence. As a result, the European division has turned EBITDA-positive for the 6-months period and we are focused on continuing to improve its performance through H2 moving into FY-'16.

What I would also like to say is whilst we are focusing on these initiatives and we are expecting a slight softness in operating performance on the Retail and Distribution portfolio through FY-'15, it is also correct for me to say that the Manufacturing performance has been exemplary for us and will more than compensate for the softness in Retail and Distribution in Fiscal Year '15. So as far as H1 is concerned despite this soft operating performance on the Retail and Distribution business, Manufacturing has more than made up for it. We have seen some flatness on the operating profit front which we will explain through the call. And as far as H2 is concerned we will continue to see a strong H2 both Q3 and Q4 in terms of Manufacturing and start to see hopefully some benefits trickling in on the efforts we are making on the Retail and Distribution front. So overall, we see a significant scope for sustaining and driving growth and profitability across our Manufacturing and Distribution businesses and the impact of these initiatives discussed will continue to unfold in the quarters to come.

With this I would like to hand over to Pradeep who will take you through the quarterly and 6-month performance of the Group. Thank you.

K.P. Pradeep: Thanks, Shrikant. Good Evening, everybody. I would like to give you a brief summary of Second Quarter Results for FY-'15, I will walk you through the performance of the Manufacturing division and then Retail and Distribution divisions followed by the consolidated performance of the Group. For Q2 FY-'15 on the Manufacturing standalone performance, we have a capacity utilization for the Bed Linen plant at 89% and that for the Drapery and Upholstery plant at 56%. For the second quarter-ended September 2014, revenues from Manufacturing Operations are flat at Rs.25.10 crores, which is Rs.251.22 crores during the same period last year. Operating expenses which includes employee benefit expenses, depreciation, and other expenses for the quarter decreased by 24.5% to Rs.59.49 crores which is Rs.78.79 crores in the same quarter last year. Employee benefit expenses were stable and stood at Rs.24.25 crores which is Rs.23.84 crores in the same quarter of the previous year. This is a year-on-year growth of Rs 0.41 crores translating to approximately 1.7%. Depreciation and amortization stood at Rs.8.66 crores Vs Rs. 11.97 crores in the same quarter last year, a reduction of Rs.3.31 crores, the reduction being on account of a change in the useful life of assets pursuant to the New Companies Act 2013 as disclosed during the first quarter of FY-2015. Other expenses stood at Rs.26.58 crores, which is Rs.42.98 crores in the same quarter last year, a reduction of Rs.16.4 crores, reduction was mainly on account of the difference between prevailing spot rate and realized rate amounting to gain of Rs.7.5 crores Vs a loss of Rs.13.72 crores in the same quarter of the previous year. For the quarter, the dollar realization stood at Rs.61.74. In addition, other expenses increased by Rs.5.79 crores primarily on account of Manufacturing expenses given increased sale of surplus power. EBITDA including other income from Manufacturing Operations increased by 43.4% to Rs.47.13 crores Vs Rs.32.87 crores during the same period in the last year. EBITDA as a percentage of sales stood at 18.8% this quarter Vs 13.1% in the same quarter last year. The EBIT including other income from Manufacturing Operations increased by 84% to Rs. 38.47 crores Vs Rs. 20.90 during the same period in the last year. EBIT as a percentage of sales stood at 15.3% this quarter, which is 8.3% in the same quarter last year. Standalone interest and finance charges for Q2 FY-'15 decreased by 2.6% to Rs.11.02 crores from Rs.11.31 crores during the same quarter of last year. The standalone profit after tax for the Q2 FY-'15 increased to Rs.27.45 crores to Rs.9.59 crores during the same period in the last year, an increase of 186%. For the half year, the capacity utilization for Bed Linen plant stood at 89% and that for the Drapery and Upholstery plant at 55%. For the half year-ended September 2015 revenue from Manufacturing Operations stood at Rs. 479.84 crores, a growth of 3.2% over Rs.465.13 crores during FY-'14. The total operating expenses which included employee benefits, depreciation and other expense for the half year, decreased by 14.7% to Rs.119.81 crore Vs Rs.140.49 crores in the previous year. Employee benefit expenses stood at Rs.48.83 crores Vs Rs.46.42 crores in the previous year. This is a year-on-year growth of Rs.2.41 crores translating to 5.2%. Depreciation and amortization stood at Rs.18.29 crores Vs Rs.23.51 crores in the previous year, a reduction of Rs.5.22 crores. As explained earlier, the reduction is on account of a change in the useful life of assets pursuant to the New

Companies Act 2013. Other expenses stood at Rs.52.69 crores Vs Rs.70.56 crores in the previous year, a reduction of Rs.17.87 crores, the reduction mainly on account of the difference between prevailing spot rate and realized rate amounting to a gain of Rs.14 crores Vs a loss of (-10.21) crores in the previous year. For the first half, the dollar realization stood at Rs. 61.76 to a dollar. In addition, there was an increase in other expenses by Rs. 9.25 primarily on account of manufacturing expenses given our increased sale of surplus power. The EBITDA including other income from Manufacturing Operations increased by 24.9% to Rs. 88.92 crores from Rs.71.17 crores during the previous year. EBITDA as a percentage of sales stood at 18.5% this year Vs 15.3% in the previous year. The EBIT including other income from Manufacturing Operations increased by 48% to Rs.70.63 crores from Rs.47.66 crores during the last year. The EBIT as a percentage of sales stood at 14.8% this year Vs 10.3% in the previous year. The standalone PAT for the year increased to Rs.50.19 crores from Rs.23.72 crores during the last year, an increase of 211%.

I will come to revenues now: The revenue from our Retail and Distribution businesses in North America during the quarter decreased by 3% to Rs.439.81 crores Vs Rs.453.26 crores during the same period in the last year. The revenues for the distribution division in Europe were at Rs.19.94 crores for the quarter compared to Rs.30.84 crores in the previous year, a reduction of 35.3%. To explain this reduction, 3% is on account of currency translation and 32.3% is on account of a constant currency decrease in revenue. This year-on-year decrease is because of launch of a certain large program during the same quarter in the last year and closure of certain underperforming stores during the course of the last 12-months.

Just to come back to the Retail and Distribution on the North America side, as I explained earlier, there was a decrease of 3% in the revenues to Rs.439.81 crores Vs 453.26 crores during the same period last year, this is on account of a 3.5% reduction on account of currency translation, offset by a 0.5% on account of constant currency increase in revenues.

Coming to the revenues for Distribution in India-Asia, the revenues for the distribution division in India-Asia represented by "Atmosphere" for the quarter is Rs.12.52 crores Vs Rs.14.40 crores during the last year, a decrease of 13.1%. The total revenues from the Retail and Distribution divisions therefore stood at Rs.472.27 crores Vs Rs.498.50 crores in the same quarter last year, a reduction of 5.3%. The consolidated EBITDA for the Retail and Distribution division stood at Rs.11.60 crores in the current quarter Vs Rs.26.98 crores in the same quarter in the previous year, a reduction of 57%. The reduction in EBITDA primarily being due to fact that Mr. Shrikant Himatsingka explained a little earlier relating to organizational restructuring, incubating of a larger brand portfolio and allied product development and design capabilities relating to this, integrating supply chain and warehousing capabilities in our new location and reorienting brand positioning and pricing. So we have had a combination of these factors which have resulted in a reduction in the EBITDA.

On the half year, Retail and Distribution performance, the revenue for the North Americas during the year stood stable at Rs.854.33 crores Vs Rs.853.40 crores during the same period in the last year. The revenues for the Distribution division in Europe was stable at Rs.49.58 crores for the year Vs Rs.51.65 crores in the previous year. The revenue for the Distribution division in India-Asia as represented by Atmosphere for the year was stable at Rs.24.90 crores Vs Rs.25.39 crores during the last year. The total revenue therefore from the Retail and Distribution division stood at Rs.928.81 crores Vs Rs.930.45 crores in the same period last year, a reduction of 0.2%. The consolidated EBITDA for the Retail and Distribution divisions stood at Rs.29.38 crores in the current year Vs Rs.42.44 crores in the same period last year, a reduction of 30.8%. The reduction in EBITDA, as explained earlier, on account of the factors relating to organizational restructuring, incubating on large brand portfolios, integrating supply chain and reorienting brand positioning and pricing, all of these have contributed in the half year to the reduction.

On the consolidated performance for the Group for the quarter to FY-'15, the Group consolidated revenues reduced by 5.8% to Rs.517.78 crores Vs Rs.549.79 crores in the same quarter last year. Total operating expenses which include employee benefit expenses depreciation and other expense for the quarter decreased by 20% to Rs.126.47 crores Vs Rs.157.99 crores in the previous year. Employee benefit expenses stood at Rs.48.35 crores Vs Rs.49.53 crores in the previous year, a decrease of Rs.1.18 crores. Depreciation and amortization stood at 11 crores Vs Rs.13.87 crores in the previous year, a reduction of Rs. 2.87 crores, the reduction as explained earlier on account of change in useful life of assets pursuant to New Companies Act 2013. Other expenses stood at Rs.67.12 crores Vs Rs.94.59 crores in the previous year a reduction of 27.47 crores the reduction mainly on account of the difference between prevailing spot rate and the realized rate amounting to a gain of Rs.7.65 crores Vs a loss of Rs.(-13.42) crores in the previous year and decreases on account of other expenses like Rs.1.08 crores on freight, a decrease of Rs.1.68 crores on professional and consultancy charges, a decrease of Rs.1.36 crores on selling expenses and a decrease of 0.75 crores on rentals. Consolidated EBITDA including other income decreased by 5.5% to Rs.54.29 crores compared to Rs.57.42 crores in the same quarter of the last year. EBITDA as a percentage of sales stood at 10.5% this quarter Vs 10.4% in the same quarter last year. EBIT including other income for the quarter decreased by 0.6% to Rs.43.29 crores from Rs.43.55 crores during the same period last year. EBIT as a percentage of sales stood at 8.4% this quarter Vs 7.9% in the same quarter last year. Interest and finance charges for the quarter increased to Rs.21.39 crores from Rs.20.22 crores in the previous year. The consolidated profit before tax for the quarter is at Rs.21.90 crores compared to Rs.23.33 crores in the same quarter last year. The consolidated profit after tax and minority interest is Rs.23.52 crores for the quarter compared to Rs.18.05 crores during the previous year.

Coming to the Group consolidated performance for the half year ended 30th September 2014, consolidated revenues reduced by 0.7% to Rs.1020.46 crores as compared to Rs.1027.49 crores in the previous year. Total operating expenses which include employee benefit expenses, depreciation and other expenses for the half year decreased by 8.8% to Rs.256.81 crores Vs Rs.281.57 crores in the previous year. Employee benefit expenses stood at Rs.98.95 crores Vs Rs.98.41 crores in the previous year, an increase of Rs 0.54 crores. Depreciation and amortization stood at Rs.22.84 crores Vs Rs.26.93 crores in the previous year, a reduction of Rs.4.09 crores, the reduction was on account of a change in useful life of assets pursuant to the New Companies Act 2013. Other expenses stood at Rs.135.02 crores Vs Rs.156.23 crores in the previous year, a reduction of Rs.21.21 crores, the reduction was mainly on account of the difference between prevailing spot rate and realized rate amounting to a gain of Rs.14.11 crores Vs loss of Rs.(-9.86) crores in the previous year. The consolidated EBITDA was Rs.109.68 crores compared to Rs.108.96 crores in the previous year, a growth of 0.7%. EBITDA as a percentage of sales stood at 10.7% this year Vs 10.6% in the previous year. The EBIT including other income increased by 5.9% to Rs.86.84 crores from Rs.82.03 crores during the last year. EBIT as a percentage of sales stood at 8.5% this year Vs 7.9% in the previous year. Interest and finance charges decreased to Rs.40.49 crores from Rs.40.54 crores. The consolidated profit before tax for the half year is at Rs.46.35 crores compared to Rs.41.49 crores in the previous year. The consolidated profit after tax of the half year is Rs.45.07 crores compared to Rs.34.59 crores in the previous year, a growth of 30.3%. The consolidated inventory as on 30th of September stands at Rs.609.27 crores as against Rs.638.25 crores as on the 30th September 2014. On the debt positions, the total debt outstanding as of 30th September 2014 is Rs.779 crores – Rs. 430 crores being the term debt and Rs. 349 crores being the working capital debt. The company's effective cost of debt is at 6.42% compared to 6.2% in the previous quarter. During the year 30th September 2014 ended term debt repayment was Rs.62.24 crores. The working capital is higher by Rs.26 crores on account of specific long-term sheeting program at the overseas subsidiaries necessitating some higher inventories for the short term.

I will come to a few ratios to share with you. The net debt-to-equity ratio is at 0.98 for the half year compared to 1.01 for the same period in the last year. Long term debt-to-equity ratio is at 0.55 vis-à-vis 0.76 in the previous year. The net debt-EBITDA is at 3.5 vis-à-vis 3.36 in the previous year. The long term debt-to-EBITDA is at 1.96 Vs 2.53 in the previous year. Our debt service coverage ratio stands at 1.06 vis-à-vis 1.44 in the previous year. Interest coverage ratios are at 2.14 Vs 2.02.

These are some of the ratios that we track on an ongoing basis. So this in substance sums up the performance for the quarter and the half year ended 30th of September 2014.

I will hand over to you moderator, and we will be glad to take questions.

Moderator: Thank you very much. We will now begin the question-and-answer session. Our first question is from the line of Niraj Mansingka from Edelweiss Capital. Please go ahead.

Niraj Mansingka: The first is on the US revenues. If I dollarize the revenues based on the realization that you just said of 61.74 for the quarter and if I see also the last quarter, what I see is that there is a sequential jump of North American revenues from $69.4 million to $671.2 million. But if you see across the board during a pick up, and this was for an economy which has been improving, also the Retail sales have been reasonably okay. During the last few years you have been actually gaining the growth in the revenues in the dollar terms were reasonably well. I fail to understand one, why was there not much of a growth on a sequential basis, because mostly Q2 is generally a good quarter for US sales, I understand you have taken restructuring, but the assumption here while restructuring is happening, you would not have taken off the revenues of the brands that the sales that is happening, so I just wanted to have some color on the same?

K.P. Pradeep: Niraj, Pradeep here. Just to give you a feel of the constant currency number in terms of the sales, we have had the sales of $72.58 million vis-à-vis $72.21 million in the previous year, so there is a growth of 0.5%.

Niraj Mansingka: But what I was talking of against the revenue sequentially quarter, generally the Q2 is a large jump over Q1…?

K.P. Pradeep: The sequential number is 69.36, so there is a growth over the sequential number too.

Niraj Mansingka: Yes, but we have seen a much more seasonality impact. Is the brand aging out? I am just trying to just throw some discussion here.

Shrikant Himatsingka: Niraj, it is difficult to answer your question extremely specifically, yes, Q2 and Q3 are normally more buoyant, we have held constant as far as constant currency revenues are concerned, we do not see anything worrying on the revenue front, and it has perhaps just been a slightly stable quarter. In these businesses certain timing differences do occur from time-to-time, perhaps there is some element of that. Our brand portfolio is absolutely well entrenched and we do not see any cause of worry on that front, but yes, we have been repositioning the brand, we have exited certain channels, we have reentered certain channels. And when these churns happen, there might be some side-effects on the revenue front which is difficult to quantify, but all in all we remain positive about this geography and our portfolio and that is how we look at the revenue front.

Niraj Mansingka: Actually, second question is similar on the European side. On a sequential side we actually saw some decline in revenues. So can you give some color that when can we see a stop in the decline in revenues? I understand you have shut down stores. So is that entire exercise over?

Shrikant Himatsingka: The sequential decline in revenues is because Italy, where a significant part of the revenues of that division are Italy-centric, and Italy goes on holiday in the month of August. So a sequential decline in revenues is absolutely natural to that division, it will happen every year as far as the sequential decline in Italy is concerned. As far as the overall revenues is concerned, despite the closure of unprofitable stores and so on, from a standpoint of absolute currency last year we did about €6.5 million in the first half and this year we have done €6.1 million in the first half despite all the store closures and so on. So there is an underlying growth which is visible for the operating assets because of closures, which is not visible here, because it is not really comparable. So I think the Italian division is looking relatively stable and I do not see a great trajectory of growth for this division given its size, but definitely it is moving north in terms of its profile of revenues and its profitability profile.

Niraj Mansingka: Again, you were planning to launch Bellora in North American market. Any color on that?

Shrikant Himatsingka: Yes, we have launched it in July-August, and it is just getting into the shelves. So, we will see how the response is, but the focus remains also in various other geographies including other countries in Europe. So we will come back to you with a more sort of observed position over the next couple of quarters, but let me tell you that, Niraj, as I said earlier, if I look at the growth profile of the Group on a consolidated basis, we have continued to grow at around 17% through FY14 over the last four years, and I do see FY15 being a little soft on the revenue front in terms of growth, but I see us resuming our growth trajectory going into the next year and the pulse in H2 as well.

Moderator: The next question is from the line of Bhautik Chauhan from Span Capital. Please go ahead.

Bhautik Chauhan: A couple of questions from my side. Our consolidated revenue has come up this quarter by 3% quarter-on-quarter basis. Could you highlight some of the reasons and how do we see going forward?

Shrikant Himatsingka: You have a right observation, it is on a sequential basis, up close to 3%. We track our businesses more year-on-year vis-à-vis sequentially. So like I said earlier, there has been some softness year-on-year, but I do not see any worrying signs on the horizon as far as our Manufacturing or Distribution businesses are concerned. I think H2 will continue to look good in terms of stable revenue front and better profitability year-on-year as we have seen in H1, and going into FY16 I think we are well positioned to reap benefits from the initiatives that we are planting at this point to see resuming healthy rate of growth as we have seen earlier.

Bhautik Chauhan: My next question is on EBITDA margins. So what would be the outlook going forward and is it fair to assume a higher digit growth or more or less the same?

Shrikant Himatsingka: We have been maintaining 10% to 10.5% consolidated EBITDA margin and that sort of kept pace with our growth in terms of the margins. We have demonstrated specifically in the first half of this year much superior EBITDA margin in the Manufacturing space by virtue of sweating our Manufacturing assets and we think that the Manufacturing EBITDAs we are clocking at this point are sustainable, of course they are subject to some cycles on the raw material side, but largely speaking, these numbers on the Manufacturing front in terms of EBITDA margins look sustainable. I have been asked a question before on earlier calls in terms of what is our expected EBITDA profile vis-à-vis Retail and Distribution businesses and we think it should be in the region of 6% to 7% in terms of stable state sustainable EBITDA margins on the Retail and Distribution businesses. Having said that we clearly are not clocking the 6% to 7% EBITDA margin on those businesses, because of which we are undergoing certain overhaul of our model in restructuring certain aspects of our operations which hopefully will deliver that number. That is how I see the EBITDA profile of the two operating pieces of the value chain and therefore the blended rate is something you can compute.

Bhautik Chauhan: What would be the primary reason for the slowdown in North American division – is it driven by DHF business or DWI business and going forward can we see margins to improve going forward.

Shrikant Himatsingka: First of all, I would request, while they are two operating entities, they are one business unit company, that consist of these two operating entities. I would not say there is a slowdown. Yes, our growth rate has corrected vis-à-vis in the past, but that is not for any particular reason other than some of the things that I have attributed the softness to during my previous answers to questions. But the stable state EBITDA margins for those businesses should be in the region of 6% to 7% at least is what we feel going forward. But I do see some softness on the operating performance of the North American division through the rest of FY15, but despite that softness I think on a consolidated basis, we definitely are looking at improving our YoY performance on a consolidated basis.

Bhautik Chauhan: My last question pertains to debt. So can you throw some light on how do we see debt coming off going forward let us say one to two years of timeframe?

Shrikant Himatsingka: The closing debt for 31.03.2014 stood at Rs.805 crores and the term debt at that point was Rs.482 crores and the working capital was Rs.323 crores, As far as September ended is concerned, it has come down to Rs.779 crores, the correction has been largely on the term debt front which has corrected from Rs.482 crores to Rs.430 crores. But the working capital has gone up a little from Rs.323 crores to Rs.349 crores. So I think our scheduled payments of term debt will continue and therefore the term debt component should keep going south as far as our existing businesses are concerned. If the Group announces any new initiatives for which it takes fresh debt that is mutually exclusive to this bucket of debt. And working capital cycles sort of are a little flexible depending on the season and time of the year. We have seen some increase in working capital, but that is really business-driven. So I would expect that we should see this organic movement of debt down, there could be some variations from Q2Q and term context to timing difference of working capital but that is about it.

Moderator: Thank you. The next question is from the line of Ankit Panchmatia from Dalal & Broacha. Please go ahead.

Ankit Panchmatia: I had two questions. First of all we have undertaken reconstruction regarding our North American side. So I just want to understand where actually the cost of reconstructing is sitting, because if I see apart from employee cost and other cost the raw material-to-sales ratio has increased YOY, so previously it was 65% and now it is 69%, so I was not able to reconcile. Ss this reconstructing cost sitting in raw material or where actually it is?

Shrikant Himatsingka: It is sitting in two areas; one is a slightly lower gross margin, because of cost of promoting our new channels of distribution, repositioning the brands, repositioning the price points, etc., which is hurting gross margin. And while you see certain constancy in the costs, it should have dropped a little further, but because of various expenses we are incurring for the various exercises we are undertaking, the expenses have not reduced to the quantum, by the quantum it is higher. So in both forms, the impact exists, but the gross margin impact is higher in this case.

Ankit Panchmatia: If I understand correctly, the rebranding costs have been a part of raw material cost or the other cost?

Shrikant Himatsingka: That is right, because it goes out in the form of various gross margin dilutions that are incurred in the form of returns and allowances to retailers, etc., So that is where it really sits.

Ankit Panchmatia: Can you help me out the realization with the Bed Linen as well as Drapery and Upholstery?

K.P. Pradeep: We will be happy to give you that offline, we have taken it off our concall because it is not really a relevant statistic.

Ankit Panchmatia: I see an interest expense which has been increased. I think we have changed our packaging credit thing from FOREX to packaging credit in INR. So what advantage I can see going ahead with this, what kind of smoothness in interest expense I can expect?

Management: In terms of advantage, what you will be able to do is capture the forward premium and that will be visible on your operating performance.

Moderator: Thank you. The next question is from the line of Dhwanil Shah from I-Wealth management, please go ahead.

Dhwanil Shah: My question is pertaining to our standalone business. We have done EBITDA margins of 19.5%. Is there any more scope of seeing margin expansion or the sweating of assets is on the verge of …?

Shrikant Himatsingka: I would not be surprised if there is upside of a few hundred basis points, but there has been a sharp improvement from approximately 12% to 18% of margins. I do consider this a fair manufacturing performance. Any fluctuations of a serious kind will now be a little more to do with cycles, but intrinsically we will not see a great deal of upward stretch on these EBITDA margins sustainably.

Dhwanil Shah: Just to understand that part a bit better, is it because our Drapery has picked up, because I think we have got better margins on that part, I think we have been doing 40 to 45%, now it is clocked to 56% because of that the margins have gone up or it is?

Management: The Drapery and Upholstery divisions EBITDA margins stand at approximately 23%, and the EBITDA margins for the Bed Linen division have gone up from 10% last year Q2 to 16% this year Q2. So on weighted average basis, what we are seeing in terms of 12%

to 18% in terms of margin movement has been caused by a much better operating performance in the Bed Linen division.

Dhwanil Shah: We said that we were looking on the expansion plan. Is there anything on the board right now or maybe in coming quarters you will be able to highlight it much better?

Management: I think it is an extremely interesting time for the industry, the Indian Textile industry is buoyant, the exports from India are on an upswing, India maintains extremely strong competitive advantage in the Cotton value chain, Home Textiles is an integral part of Indian Textile exports, and operating at 89% consistently, necessarily makes us explore our expansion options. So, I cannot give you any commitment or specifications of the outline of our expansion projects, but I would be happy to tell you that we are actively exploring these options and will communicate this as soon as we have some concrete direction that we have concluded upon.

Dhwanil Shah CAPEX figures for this year?

K.P. Pradeep CAPEX will remain range bound, just the organic maintaining CAPEX that ranges anywhere from Rs.10 crores to Rs.20 crores depending on the year, but nothing earth shattering on the cards.

Dhwanil Shah Our tax rates want to understand sir in this quarter?

K.P. Pradeep Between 18% to 20%.

Dhwanil Shah This year it has got a credit of Rs.1.12 crores, so wanted to understand that?

K.P. Pradeep This credit was on account of an excess provision in the previous quarter.

Dhwanil Shah So, effective tax rates for this year will be 18% to 20%?

K.P. Pradeep That is right.

Moderator Thank you. The next question is from the line of Prateek Poddar from ICICI Prudential. Please go ahead.

Prateek Poddar First question is on the inventory. I understand that the inventory levels were very high because of some special programs which we were running and it was expected that by Q2 of this year, there would be substantial correction in inventory levels. This is not seen in consolidated balance sheet. Any specific reason for that sir?

Management Yes, it is reflecting a small decrease from Rs.640 crores levels to Rs.610 crores levels and I think the momentum on decrease should continue.

Difficult to put up timelines to these things, Prateek, because there are timing differences and it is not about just the product launch or one product, there are the new things that go through a churning process but what is important is that the decline has begun and we should hopefully continue to see some decline on the inventory front, but from a broad trajectory, it should go sound.

Prateek Poddar So, sir how do we model this – do you look at inventory as percentage of sales and in terms of days, what would be the normalized inventory levels for…?

Shrikant Himatsingka: Manufacturing business, days model is appropriate, although there will be some movements, depending on various utilization levels, etc., but it is more applicable to Manufacturing. On the Distribution side, it is very difficult to modularize this statistics. So, I do not have a specific answer for you on that front. Typically, what we do is, it is measured in terms of time. So, days of inventory would also be a thumb rule that is applied to the Retail and Distribution businesses. Let us say Model-1 of a one type of Manufacturing business, let us say if 3 to 4 months is a more appropriate model, another Manufacturing business with a much larger SKU spread might be closer to 5 to 6 months. On the Retail and Distribution front, typically, cycles get a little long because product shelf lives are extended, lead times on new product introductions are a little stretched. So, typically, we can see sometimes 6 to 7 months movements on the inventory side there as well. Having said that, there are certain products which do not have any inventory at all because we directly ship it to the retailer. So, it really depends on where various things, but the answer to your question is it is always measured in terms of days and months, and of course you can have more detailed conversations with my colleagues and they will be happy to give you a more accurate metric, but it could be modeled as manufacturing facility-1 which has 'x' model, manufacturing facility-2 which is a different model and the Retail and Distribution businesses which fall under one gamut. So, the blended model of these 3 operating divisions can give you global consolidated model.

Prateek Poddar Sir, one more question on the Manufacturing EBITDA margins. What I understand is this margin expansion would primarily be on account of the currency depreciation which we could not realize in the last quarter same period?

Shrikant Himatsingka: That has been a contributor and there have been several positive contributions which we can take offline, Prateek. Optically, that is what appears to be the case, but raw material authorization, asset productivity, manpower productivity, these are not terms that we are rattling off because they are associated manufacturing. As a Group, we believe we are best-in-class in these statistics at this point rather. And so, they have also made very-very important contribution to this operating EBITDA number. So, I would request you to consult with Pradeep offline on this and he can share with you in greater detail.

Prateek Poddar: Sir, what is the capacity utilization in this Silk division and in the Bed Linen division?

Shrikant Himatsingka: In the Drapery and Upholstery, it is not the Silk division, Drapery and Upholstery was 56 and Bedding division was 89.

Prateek Poddar: Sir, as you mentioned in your previous remarks that in H2 and in FY'16 you see growth rates on the revenue front returning back to a normal ratio which we have seen 14%, 15%. Sir, I was just wondering what is giving us this confidence or if you can share some light on to this statement?

Management: I said, in H2, we should start seeing fruits of the various initiatives we are undertaking. So, I do maintain 2015 we will see some soft revenues in terms of stable, it could be marginally up, but going into FY'16, I see better growth rates more consistent with the past. In terms of what is going to fuel it, I do not have many other options other than Manufacturing, Retail and Distribution. So, a combination of this is what is going to fuel it.

Prateek Poddar: Sir, I think the board has taken an approval for raising potential funds. Obviously, this is an approval you might look at it into the future. I just wanted to understand, are you looking at something or what was the need for this?

Shrikant Himatsingka: It is an enabling resolution.

Prateek Poddar: But I am just trying to understand the thought process behind this enabling resolution?

Shrikant Himatsingka: As far as the enabling resolution is concerned fund raise, we are just keeping our options open, but I have shared on this call and earlier as well, that the Group is exploring, it is in the midst of exploring its options for growth both in the Manufacturing space and the Retail and Distribution space. And once we have a more concrete strategy to expand our businesses, we will a) communicate on that front and b) will really see if we need to raise funds for that or we do not.

Moderator: Thank you. The next question is from the line of Niraj Mansingka from Edelweiss Capital. Please go ahead.

Niraj Mansingka: Just regarding the Manufacturing side, we are already hitting 89% utilization and if talking of 15% maybe growth for next year, do you not see a gap in the volumes in the Manufacturing side in the next year itself?

Shrikant Himatsingka: Interesting question, Niraj. So, as I said, we hope to resume growth rates more consistent with the past going into FY'16 and this will be fueled both from Manufacturing and Retail and Distribution businesses. The Retail and Distribution businesses are not handcuffed by utilization levels and therefore that is not a worry, that is a function of sales, brands, and market depth that we enjoy. As far as Manufacturing is concerned, one of the units which are at 56% has fair amount of upside left on the utilization front, so that is not a worry. And as far as the Bedding Manufacturing division is concerned, until such time, that we may consider an expansion, we also are looking at debottlenecking some capacities through organic capital expenditure, which should see us through with some growth potential on that front.

Niraj Mansingka: Sir, how much would be the lead time for decision to execution or final expansion of capacity for that?

Shrikant Himatsingka: I cannot give you a definitive timeline, but we are in the midst of exploring our options and what works for us in terms of a model and how we would like to proceed forward. So, I cannot commit a timeline, but we will definitely keep you updated on the developments.

Niraj Mansingka: The reason I was asking is because the lead time will definitely be depending on how much work you do, I understand that....

Shrikant Himatsingka: If there is no decision to expand, then of course, there is no question of lead time, that is on a lighter note. But if we do decide to expand the lead time to implementation of new projects is largely driven by the specifications of these projects. And so, it could range anywhere between 6 months to a year from the time we say go.

Niraj Mansingka: Yes, so you are sitting already almost last end of FY'15 and you are talking of growth in FY'16. So, do you not see FY'16 volume itself will be on a risk on the standalone site or the Manufacturing entity?

Shrikant Himatsingka: In FY'16, like I said on the organic CAPEX we are scheduling some debottlenecking of capacities, and remember the capacity utilizations we state to you are net. So, technically we can be operating at 99% to 100%. So, a) we have 11% upside from where we are; b) we are looking at debottlenecking some capacities vis-à-vis the Bed Linen Manufacturing division and that should be adequate for FY'16. The Drapery and Upholstery division is 56%, so it has enough upside. And the Retail and Distribution division are not handcuffed by any interest and therefore it is blue sky. The gap really is in the Bed Linen Manufacturing division, and for FY'16 specifically our debottlenecking initiatives should take us through.

Niraj Mansingka: Any guidelines on the CAPEX in FY'15 and '16?

Shrikant Himatsingka: Like I mentioned earlier, we will maintain our organic CAPEX cycle which are anywhere between Rs.10 crores and Rs.20 crores typically per year, it could even go up to Rs.25 crores organic.

Niraj Mansingka: Which obviously means that this does not include that debottlenecking CAPEX, right?

Shrikant Himatsingka: It does, I said debottlenecking, we will explore it as part of our organic CAPEX.

Moderator: Thank you. The next question is from the line of Resham Jain from B&K Securities. Please go ahead.

Resham Jain: Sir, three questions which are interrelated. Just wanted to understand like from last couple of years we are importing Yarn. So what is the current status on that like; are we importing or are we procuring domestically? Secondly, we have seen some softness in the Yarn market. So how it is going to impact our Manufacturing division? And at the same time because we have two different models in US B2B as well as B2C, so how those two business will get impacted because of the same?

Shrikant Himatsingka: Answer to question one, we continue to import and source domestically, the ratio between the two keep varying from Q-to-Q, there is no specific reason other than price arbitrage that we seek such solutions. I do not see any change in the short to medium term on this strategy because it suites our operating model. As far as softness in Yarn prices are concerned, that is a correct observation and we should start seeing some benefits trickling in starting the tail end of Q3 and going into Q4. As far as your third question is concerned, the Yarn prices softening could have some impact going forward in terms of price revision. So, we have actually agreed to some price revisions marginal though, but I do not see that impact to be material in the context of the Distribution businesses in the North Americas.

Resham Jain: But will it impact differently to our B2B business and to our B2C business, because B2C business, we have the pricing control.

Shrikant Himatsingka: B2C business which is largely brand-driven will not get impacted by organic changes in Yarn prices, and as far as more chunky prices of business on the Private Label front is concerned, like I said we have already had some price revisions, but it will still entail some benefits for the group to be kept rather than leaked.

Moderator: Thank you. The next question is a follow-up from the line of Prateek Poddar from ICICI Prudential. Please go ahead.

Prateek Poddar: Sir, a couple of quarters back when we spoke you mentioned about certain debottlenecking activities that would basically on the Manufacturing side could double your turnover, that was basically setting up a processing house. Does that still hold true or you have again relooked at that plan, can you just talk about that a bit?

Shrikant Himatsingka: The discussion a couple of quarters ago as far as the potential of doubling our processing capacities was in response to a question. That is not debottlenecking, we cannot double our capacities given a debottlenecking, we can look at an increment of 10% to 15% with debottlenecking because it has certain restrictions on allied infrastructure. Having said that, I will remind the audience as to the context of the discussion in terms of doubling our sheeting capacities and the question that was posed was "What would be the capital expenditure that the company would incur if it were to look at increasing its processing capacities and so on and would we also add Loomage?" So, that was a mutually exclusive discussion pertaining to an expansion. I threw light on the fact that we could potentially look at scaling up processing capacities for the plant.

Prateek Poddar: This holds true or does not hold true is what I am trying to understand.

Shrikant Himatsingka: There are two buckets; bucket one is debottlenecking which we are …

Prateek Poddar: Which I understood sir what you meant by.

Shrikant Himatsingka: And bucket two is the expansion side and the expansion side is something which is under exploration. I did not commit previously and we continue to explore the specifications for our expansions, and as soon as we have something to communicate on that front, we will definitely let you know, but it is an active subject.

Prateek Poddar: This is one of the options in the second bucket?

Shrikant Himatsingka: That is right. We have expansions on expanding. So Brownfield expansion of capacities, we are exploring implications on backward integration, we are also exploring allied product categories and we are doing the whole gamut as far as our research is concerned.

Moderator: Thank you. As there are no further questions, I would now like to hand the floor over to the management for closing comments.

Shrikant Himatsingka: I thank you all for taking the time to join us. We did go through some changes on our formats. We will be delighted to receive feedback from you if you have any suggestions and we really look forward to interacting with you at the end of our Q3 results. Thank you again. Bye.

Moderator: Thank you. On behalf of Macquarie Capital Securities Private Limited that concludes this conference. Thank you for joining us and you may now disconnect your lines.