# "KDDL Limited Q3 FY'15 Earnings Conference Call"

**February 3, 2015**

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**Moderator** Ladies and Gentlemen Good Day and welcome to the Q3 FY'15 Earnings Conference Call of KDDL 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 the conference call please signal an operator by pressing '*' then '0' on your touch tone phone. Please note that this conference is being recorded. This conference call may contain forward looking statements about the company which are based on the beliefs, opinions and expectations of the company as on the date of this call. These statements are not the guarantees of future performance and involve risk and uncertainties that are difficult to predict. Now I hand the conference over to Mr. Yashovardhan Saboo – Chief Executive Officer, KDDL Limited.

**Yashovardhan Saboo** Good Afternoon and a warm welcome to all the participants. I am joined at this call by my colleagues Mr. Sanjeev Masown – CFO of KDDL and Mr. Raj Sekhar – CFO of Ethos our Luxury Retail arm. We also have with us SGA, our IR Advisors. I trust you have received our financial results and presentation, it is uploaded on the BSE website as well as our website www.kddl.com, and I will now give you a brief update on the business followed by a commentary on the financial results.

Let me begin with consolidated results. In 9-month FY-'15 the company registered a growth of 27% to Rs.304 crores from Rs.240 crores. EBITDA of Rs.29 crores representing a growth of 41% year-on-year and an EBITDA margin of 9.5% higher by 100 BPS compared to corresponding period. For 9-month FY-2015 the net profit after tax and minority interest is at Rs. 6.3 crores a growth of 114% year-on-year from Rs. 3 crores in the same period last year. Cash profit after tax of Rs. 15.1 crores for 9-months FY-'15 which represents a growth of 61% compared to the corresponding period. Now the standalone results.

For the financials of KDDL standalone business for the quarter the company registered revenue of Rs. 31 crores representing a year-on-year growth of 11% from Rs. 28 crores in the previous year. In the 9-months FY-'15 the company registered a revenue growth of 18% from Rs. 88 crore to Rs. 96 crores. Of the 9-months revenue for financial year '15, Rs.75 crores came from watch components growing at 18% year-on-year and Rs. 15 crores came from precision engineering growing by about 28% year-on-year. We believe we are still at the lower end of the value chain for the watch components and precision engineering components that we are currently working on. Our focus is going up this value chain. Going ahead, our growth in the watch components will mainly come from this value growth rather than volume and there is tremendous potential for this value growth. Similarly in the precision engineering segment there is great opportunity in various market segments such as defense, aerospace, electronic goods. We are currently evaluating the best options on the product and market segment metrics to determine our strategic growth in this business. In Q3 EBITDA stood at Rs.6.3 crores with a margin of 20% and for 9-months EBITDA stands at Rs.19.5 crores with same margin of 20%. For the quarter profit after tax stands at Rs. 2 crores growth of 41% year-on-year, margins expanded by 134 basis points year-on-year to 6.2%. For the 9-months period profit after tax is Rs. 5.3 crores, a growth of 87% year-on-year, margin expanded by 204 basis points to 5.5% from 3.5% in the previous year on the 9-month period.

Now I come to Ethos Our Luxury Retail Arm – As on the quarter ended the company has 45 stores across the country with 8 Ethos Summit stores, Summit stores I remind you focus on the high luxury end of the business and 37 Ethos stores including seven stores at airports of which 4 are duty free stores. Last quarter we have opened two boutiques for Rado, one in Mumbai, and one in New Delhi. We have also opened one mono-brand boutique for Longines in Mumbai, all three boutiques are in collaboration with the Swatch group, the largest international group in the watch business. The year so far, we have opened 5 stores and all 5 stores have been in collaboration with leading global brands three with Swatch and two with the Fossil group. With these new boutiques we have expanded our ongoing collaboration with leading watch groups in the world.

Our presence in India is spread and is not limited just to the store network; it is augmented very considerably by our online presence. Our website www.ethoswatches.com has helped us to expand our network, expanding the catchment area of our stores. So far in 9-months, we have received more than 4 million visitors on our website and we estimate to receive 6 million visitors in this financial year which us making us the No.1 website in the world among authorized multi-brand retailors of premium and luxury watches in terms of visitors.

To expand our reach and augment this growth, we will keep investing in advertising and marketing initiatives. Our marketing spends have almost doubled in 9-month period in the current year compared to the spend in the previous year in the same period.

We are also investing heavily in the required IT infrastructure which ensures that the entire chain of the transaction from website hosting, search engine optimization, lead generation, order management, and inventory management is monitored and coordinated closely and managed efficiently in an integrated fashion.

In the quarter, the company has raised funds by way of issue of compulsory convertibles cumulative preferential share on a preferential allotment basis totaling to Rs. 7.25 crores from various investors. KDDL Limited the parent company has also subscribed to these preferential shares. Total funds of Rs. 7.5 crores raised by Ethos Limited will be utilized for the expansion of its business.

Coming to the financials of Ethos, in quarter 3 FY-'15 the company has generated its highest quarterly sales ever with revenues of Rs.88 crores a growth of 33% year-on-year. In the 9-month period till December our revenues have grown by 30% year-on-year to Rs. 206 crores this is significantly higher than the estimated market growth. This growth is mainly driven by same store sales for which quarter 3 FY-'15 grew by 17% year-on-year and for the 9-month period grew by 13% year-on-year. Our sales are being aided by our online platform www.ethoswatches.com wherein we create leads for sales which are fulfilled at the store. This lead generating online platform has contributed over 23% of revenue in the current quarter as against 16.2% in the previous year same quarter. It has contributed 22.8% in the 9-month period against 15.6% of revenues in the same period last year. Thus you can see that sales from lead generated by our online platform are accounting for nearly a quarter of our overall sales. The online lead generated revenues has grown thus by 90% in Q3 and 91% in the 9-month period. Much of this growth has been achieved by better conversions. Our conversion rate from lead to sales has increased to nearly 7% in the quarter 3 from 5% in the same period the previous year. This reiterates our belief in the potential of this platform and also the success of our strategy to improve the customer experience leading to the improved conversions.

Growing proportion of revenue from this online platform has also enabled us to reduce front end expenses on account of rental and employee cost. So with the revenue growth of 33% the front end expenses has grown only marginally by 5% year-on-year. Looking at it as a percentage of sales perspective the front end expenses have reduced from 13% as a percentage of sales in Q3 of the previous year to 10% in the Q3 of this year representing a reduction of 261 basis points which is very significant. This quarter we have also improved our capital efficiency by reducing our inventory carrying months to 8.7-months in the current year from 9.2-months at the end of the same period in the previous year. For quarter 3 EBITDA has grown by 50% year-on-year to Rs. 6 crore and the EBITDA margin has expanded by 75 basis points to 6.7%. For the 9-month period EBITDA stands at Rs. 10 crores a growth of 58% year-on-year and in this year our retail business has already surpassed the full year FY-'14 EBITDA of Rs. 9 crores. Profit before tax for Q3 is at Rs. 3.1 crores a growth of 48% year-on-year, this growth has come even after the depreciation expenses have more than doubled from the previous year due to statutory changes. However due to higher tax rate in the current year our net profit for the company in Q3 FY-15 declined by 3% from 2.15 crores to Rs. 2.09 crores. Similarly for the 9-month period profit after tax is 1.35 crores as against Rs. 1.56 crores. It gives us satisfaction to see our strategy fructifying into sales and profits.

As you are aware from macroeconomic indices while there is an improvement in consumer sentiment, it is not yet reflected very much in consumer sales across product categories whether it is automobiles, white goods or other consumables. In this context achieving the growth that we have can largely be said due to our internal improvements optimization and the marketing strategy that we have followed. However we are also confident that the macroeconomic situation is steadily improving and this will further be reflected in solidifying of consumer sentiment and a growth in consumer sentiment in the months to come. A combination of our internal strategy and optimization together with improvement in the macroeconomic area can give us the confidence that the results that we have achieved are sustainable and sustainable for a long time to come.

The Indian luxury and premium watch market is still at a nascent stage of growth and the revenue growth potential is frankly speaking quite immense. With our online lead generating platform with the emphasis on marketing and service there is also lot of scope to expand the margins together with the revenue.

With this I would like to thank you all for participating and would like to open the floor for questions. Thank you very much.

**Moderator** Thank you. We will now begin the question-and-answer session. The first question is from the line of Sangeeta Tripathi from Sharekhan. Please go ahead.

**Sangeeta Tripathi** Sir, I would like to understand what would be the impact of this Swiss Franc appreciation, if you can highlight on that?

**Yashovardhan Saboo** Sure, I think that is a question a lot of people would be interested to ask, so I am glad it has come early in the queue. So while the change in the Swiss Franc was very-very dramatic for a period of about 2 weeks, but now it has settled down to something that is quite normal. For most of the part of the year the Swiss Franc against the Indian Rupee was ranging between Rs.65 to 66 per Swiss Franc, then the Swiss franc broke the Euro link early in January for a certain period it shot up to beyond Rs.70 even touching Rs.80 for a short period of a day. However, as you can see, it has now stabilized to about between Rs.67 and Rs.68 which against the average for most of the year of about Rs.65 to Rs.66 essentially represents 3% percent increase against the Indian Rupee. So with this background first of all I do not think the change is very significant and this is something which will not really have a great impact either way as far as India is concerned. There is however I would like to say that the Swiss Franc impact against the Euro and the US dollar is probably a little more pronounced and indirectly it may have a certain impact on the sale of Swiss watches in certain countries, where Swiss watches suddenly become a little bit more expensive. I believe the Swiss watch industry will respond either by adjusting some prices, especially if they believe that these changes are going to be permanent and not temporary. But I do not think there is going to be a very significant change impacted specially after this adjustment it has compensated some of the very early swings that had happened.

**Sangeeta Tripathi** So you believe that as far as our business is concerned for Ethos in India there would not be adjustment with respect to price?

**Yashovardhan Saboo** The whole of last year there was no price adjustment by most of the Swiss brands. And as you know there is a price increase of a few percent that happens every year in the Swiss brands. So in any case, a natural price increase is due. So we do expect a certain price increase to happen in the prices of Swiss watches in India, but that is pretty normal it has happened every year, it did not happen last year.

**Sangeeta Tripathi** So that would be in the range of single-digit, not to the extent…

**Yashovardhan Saboo** Usually it has never been double-digit I think with the exception of 1-year when the rupee suddenly slipped down from 15% in 2-months, it is usually a gentle increase of anywhere between 5% to 6%. So it is not really something which is going to be very-very impactful.

**Sangeeta Tripathi** When is it adjustment expected as in like how generally that happens?

**Yashovardhan Saboo** I really do not want to hazard a guess except to say that it should not be a surprise if it could happen sometime over the next couple of months or weeks.

**Sangeeta Tripathi** Secondly, I wanted to understand about our CAPEX plans which have raised Rs.7.5 crores through equity dilution and we are building up on the infrastructure and the back end development, so wanted to understand more from a CAPEX perspective in the next one to two years what are our plans and any rupee crores guidance on CAPEX?

**Yashovardhan Saboo** Sangeeta, we do not have a great CAPEX plan in Ethos, however, we do have a need for investment of between Rs.20-25 crores to sustain our projected growth of 25% plus year-on-year which we believe is sustainable for the next couple of years. Most of this investment is actually for new stock and this stock is necessary to build the depth and width of brands that we have. In a previous conference, I had mentioned that still a significant percentage of purchase of luxury and premium watches happens outside India, and one of the reasons is that customers feel that in India the range of watches that are available is still not up to international standards. That is actually true. And therefore we believe that by giving a better range of products or wider and deeper range of products which can only open by augmenting our stock levels, we can convert more people to buying in India, and that is going to be a strong engine for our growth. That said I would also like to say that although we will be increasing stock, our stock turns will be improving, so in terms of stock to month ratio, we will be showing a steady improvement year-on-year.

**Sangeeta Tripathi** And this Rs.20-25 crores what you are talking of that would be entirely for stock augmentation?

**Yashovardhan Saboo** Not entirely, but principally quite significantly.

**Sangeeta Tripathi** Because I believe that IT infrastructure and other costs which will be incurring to strengthen the backend team and the infrastructure team that is also kind of CAPEX?

**Yashovardhan Saboo** True, except that as I understand we are not allowed to capitalize, most of it needs to be expensed of revenue.

**Moderator** Thank you. The next question is from the line of Jeetu Panjabi from EM Capital Advisors. Please go ahead.

**Jeetu Panjabi** I have two questions: one, can you explain how do you fund your inventory of we have got 8.5-9 months of inventory on the Watches side, how is that funded and other payables in foreign currency or are they in local currency? The second question is on the Manufacturing business. Can you just tell us how do you think about that from the next 2-3 year basis – is that a growth business or is that just going to grow at moderate growth rates – how should we be thinking about it?

**Yashovardhan Saboo** So let me answer the first question which is about inventory, let me start by saying that we have 8.5-months of inventory at cost. While this does seem high but I just want to tell you that benchmarking with international luxury watch chains it is quite within the band, most luxury watch chains have between 7 to 8-months of inventory. Of course, we are conscious of the fact that in almost every other country where Luxury business is strong, cost of funds is much lower than in India. So we are that much more conscious that we need to be much more effective than other countries in our investments in stock. The question you had was about "How these are funded?" Partly, of course, these are funded by supplier credits, supplier credit can range from as low as 15-days to as high as 5-months these are negotiated and typically the stronger the brand the less negotiation power we as retailers have, but the larger we grow as retailers the larger leverage we have over some brands. So that is really how it is funded. More than 75% of our inventory is paid for in Indian rupees and about 25% maybe a little less is paid in foreign exchange which means they are importing it directly.

**Jeetu Panjabi** And receivables, does it have an interest rate attached to it or it is just a period where you…?

**Yashovardhan Saboo** No, it would be extremely rare where there would be any interest rate attached to the receivables. I come to the second question which is about the Manufacturing business. So as you know in Manufacturing we are really concentrating on two segments – the Precision Engineering and the Watch Components. Precision Engineering business is a smaller segment but it is a faster growing segment. Now this is a segment in which we are making precision stamping and sub-assemblies which go to various businesses outside the Watch business, so this goes into instrumentation, white goods, defense, aerospace, very-very wide range of applications, and given the fact of the way these businesses are likely to grow in India particularly as the "Make in India" campaign step up, we see there is a huge opportunity for growth, this year I think we have grown at about 30% and that is something which we believe is sustainable over the next couple of years until it becomes Rs.100 crores business. Of course, we are in the process of determining what kind of product and markets should we be specializing is because the potential across so many segments is so large that we really need to focus on few where we believe we can be the strongest. As far as the Watch Component business is concerned I believe that it has a growth potential though not as dramatic as the Precision Engineering business. Most of the growth in the Watch Component business as already mentioned is going to come from value growth. So in all the component be it hands or watch dials internationally we are at the lower end of the price pyramid. We are exporting most of our products go to well-known Swiss brands, but within these Swiss brands we are at lower end of the segment and there is a huge potential for value addition by making more complex higher quality products. And this is going to be the main strategy. We believe a double-digit growth is sustainable in this segment as well, but not as dramatic as it will be in the Precision Engineering segment.

**Jeetu Panjabi** Can you also just give us some sense on what the strategy is for Ethos in terms of new brand acquisitions and what that potential range of brands is going to look like in a few years' time?

**Yashovardhan Saboo** Jeetu, we already have a portfolio of more than 50 brands, and mostly across the price spectrum from Rs.5000 up to Rs.50 lakhs and more, I think some of the leading brands in the world which are also present in India are present with Ethos. So broadly speaking I think our portfolio is good, then we do feel that there might be some gaps which we might want to fill in the years to come and equally there may be some brands that we may have to shave off based on performance not matching expectations. I do not think we want to expand the number of brand that we deal with and the reason is very simple – today to sell Luxury products not only do you need to have an effective presence with customers, but your selling has to be based on knowledge and passion, you cannot just stock the products and sell them. And to develop knowledge, passion and experience, you have to become familiar with the brands, you have to know the DNA of the brands, our sales team, our purchasing team they have to know the brands almost as well as the brands themselves. This you can only do when you have a limited number of brands. Therefore our strategy going forward is to become the best partners in India for these 40 or 50 brands that we deal with and not really aim at having every brand, that is not possible, no multi-brand retailer has every brand. But if we have amongst the best brands that the world has to offer, and we offer the best customer service for these brands I think that is a winning combination.

**Moderator** Thank you. The next question is from the line of Hemal Parikh from Interface Capital. Please go ahead.

**Hemal Parikh** I would like to ask you a few questions: first, what would be the dilution of the capital once this CCPS gets converted?

**C Raja Sekhar** So currently on a fully diluted basis, KDDL holds about 70% of Ethos, and on a basic basis it is at about 79%. They already had issued in an earlier round preference shares for the investment of about Rs.12 crores about 3-years ago. So that and this combined the dilution would be to the extent of about 9%.

**Hemal Parikh** It will come down to around 61%?

**Yashovardhan Saboo** No, it will come down from 79% to 70%.

**Hemal Parikh** Second question on return on capital employed, for the last three months and over the last nine months?

**C Raja Sekhar** The return on capital employed for the first 9-month on an annualized basis is about 12.3%, the previous year for the same period it was about 3.6%, and for the entire year previous year it was about 5%.

**Hemal Parikh** Can you give me the breakup of rent and employee expenses as a percentage of sales because you have given a combined figure of about 9.9%, but if you segregate between rent and employee cost as a percentage of sales?

**C Raja Sekhar** Between the two, the rental cost for the quarter are about 7% of the sales, and the manpower is at about 2.9% on the sales for the quarter.

**Hemal Parikh** Your presentation talks about closure of four stores. Any specific reasons?

**Yashovardhan Saboo** I think we have been reviewing stores pretty actively and whichever stores do not seem to perform we do go in for closure. I think two of them were at Hyderabad airport duty-free stores. Frankly it was a mistake to go ahead with this duty-free location and we decided to close it down immediately within 1-year of starting, because we did not see traffic growth happening the way it was intended. The other two stores were Inorbit in Bangalore that is the store that we recently closed, the mall has not done well, and Inorbit in Pune both these malls have not performed very well. We have had very good experiences at Inorbit malls in Mumbai but unfortunately at Bangalore and Pune, I think these malls have been surpassed by other malls in the same vicinity, and rather than continuing over there we decided it is actually better to close down.

**Hemal Parikh** Any plans to introduce your own brand of say Ethos brand of watch or something like that?

**Yashovardhan Saboo** That is a question that we have been asked and we have been asking ourselves over the last 20-years since we have been in making dials, but frankly speaking I do not foresee this as something at least for the next 2 to 3-years; A), we have a very good portfolio of brands from world leaders. To create our own brand it starts to create friction which I do not think will be very positive. Second, quiet frankly, we are also waiting to see how a market leader like Titan which has actually bought a world famous brand like Favre-Leuba and developed its own brand Xylys a Swiss made brand, but is not really able to take them forward as well as intended in the Premium category. I think there is a resistance to new brands in the Premium and Luxury category, and we want to be very sure about what we are doing before we take this step. So over the next 2 to 3-years I do not see this as a goal for us.

**Hemal Parikh** Whom would you consider as your closest competitor in terms of the Ethos business?

**Yashovardhan Saboo** On the one hand there are competitors in every city, right, so as you know in Delhi there are two competitors, in Ahmedabad there is one competitor who has been there for some time, in Mumbai, there are one or two competitors, and similarly in Chennai and Bangalore so city wise there are competitors, I do not think there is any competitor on a national foot print with the exception of Titan and the Helios range of its stores. The Helios range of Titan store is focused on premium watches and many of the brands they represent are common to us; however, I think Titan has also declared its results and I think we have performed a bit better. So we always benchmark ourselves against Titan.

**Moderator** Thank you. The next question is from the line of Dipankar Sathi from Athena Divitie Investment. Please go ahead.

**Dipankar** I want to know on the store economic front. What is the average running cost for Ethos store and an Ethos Summit store?

**C Raj Sekhar** The biggest cost for us for running the store is rent and the next one is manpower. Again, the store economies vary depending on which mall and which city we are opening the store. A typical store is of the size of about 900 square feet and rental cost comes to about Rs.300 per square feet. So, on an average that is the rental cost that you can consider. In terms of manpower, we need to employ 4 to 5 people. The total cost per annum of all these people would be in the vicinity of about 15 lakhs per annum. So these are the major costs for running the store. In addition to this there are some costs for running the store in terms of power and other staff welfare cost and all and all which will be approximately again about lakh rupees per month. So these are the big chunks of the cost. If you are also referring to the investment that goes into a store, that is an entirely different thing. The biggest investment is in the stocks for stores and that again varies from store format and the region where the store is being opened.

**Moderator** Thank you. The next question is from the line of Chaitanya Adesara from Siddhesh Capital. Please go ahead.

**Chaitanya Adesara** One is the revenue share percentage from the airport stores?

**Yashovardhan Saboo** This includes the duty-free stores, right, it comes to just shy of 15%.

**Chaitanya Adesara** In the standalone business, the breakup of stamping and the component business revenue?

**Sanjeev Masown** Mr. Saboo in his speech also he has shared, the Precision Engineering has contributed Rs.15 crores for the 9-months period and the Watch component is Rs.75 crores.

**Chaitanya Adesara** I was referring to the quarter, if…?

**Sanjeev Masown** So in the quarter the Precision Engineering is around Rs.6 crores.

**Chaitanya Adesara** And Component?

**Sanjeev Masown** The Watch Components you are referring to that comes to around 25 to 26 crores comes into that.

**Chaitanya Adesara** Mr. Saboo, just want to know your thoughts on the official online platform which could be introduced by the large players, probably Rolex or Rado, they are getting into any online platform as such, similar to Ethos?

**Yashovardhan Saboo** If you go to the Rolex website or the Rado website, one of the things that you will read very prominently there is that they do not support any online sales. So they do not allow retailers to do online sales and therefore it is very highly unlikely that at least for the next foreseeable future these brands are going to go directly into online sales themselves. That is also the reason why we do not offer these brands for direct online sales, we are strong partners of these brands and we follow the guidelines laid by them. So our online platform is structured in the way we believe that all future Luxury sales is going to be. The online platform basically allows customers to research the watches, we share information about the watches, we dialogue, we discuss we chat about the watches, but to actually experience the watch, the customer eventually has to go to the store and that is why we call it a "Lead Generation" the platform generates the leads, the lead after certain development is transferred to the store, the store welcomes the customer, and the transaction is consummated at the store level, therefore to come back to your question we do not believe Rolex or Rado is really going to get on to online sales directly themselves anytime soon.

**Moderator** Thank you. The next question is from the line of Apurva Mehta from KFA Shares. Please go ahead.

**Apurva Mehta** Sir, going forward what do you see if economy does start doing well, so what will be the impact on our sales and what do you see that per store sales going up by how much per cent?

**Yashovardhan Saboo** For 10-years we have waited for India to start showing real growth, we have dreamt about it, we perhaps at the doorsteps. We are so conservative and afraid of what can happen that we do not dare to dream of what can happen optimistically. I can only say that in the decade 2000 to 2010 China market grew at 35% plus year-on-year, and the leading retailer in China Hengdeli the listed company, so you can benchmark Ethos against Hengdeli, Hengdeli grew by 40% year-on-year for 10-years. "Can you imagine the growth multiple that generates?" Why I am saying this is that today we are afraid to be very optimistic. Therefore I have to say that we have grown at 32% this year, I strongly believe that with the economic sentiment improving, with the consumer sentiment becoming good, we can sustain this very strongly with a lot of confidence I can say that. "Can it grow higher?" Of course, it can grow higher, but for 10-years we have hoped for so much and got so little that we dare not be more optimistic than this. But I think we have good times coming.

**Apurva Mehta** We are not adding stores, more or less we are sticking to the 45 stores to 50 stores level. So if the next growth level if you are thinking to come and the growth will spread across India and we are having that 45 stores, so do you not feel that we must little bit expand at different geographies and try to get ready for the growth level?

**Yashovardhan Saboo** Apurva, I do not know if you were there in the last investor call where we did speak a little bit about the change of our strategy. We do want to go to geographies beyond our stores but we do not want to do this by increasing too much the number of stores. "Why do not we want to do that?" Because we have got a perfectly functioning and a much more cost effective way of spreading geography and that is through our internet platform. Today, I do not have to open 10 stores across Delhi because with my 3 stores or 4 stores or 6 stores I am able to reach all the people I want to reach in Delhi through my internet reach. Why only Delhi? I can reach Agra, I can reach Moradabad, I can reach even Lucknow. Now that means that I do not necessarily have to open a store in these places in the years to come. So what I am saying is our goal is to achieve 25% plus growth year-on-year. If we believe that this is possible to achieve with fewer new stores, it makes it very cost effective, because what it means is that my rental cost as a percentage of sales will drop, my manpower cost as a percentage of sales will drop, my stocking cost as a percentage of sales will drop, and we will extract the much needed few percentage points more in our EBITDA. That is a strategy by which we will grow from 5% EBITDA to 10% EBITDA in the next 3 to 4-years.

**Apurva Mehta** But you said Delhi you are there having 1 or 2 stores, or in Mumbai you have 1 store, but different small town cities, do you not think that there will be any trigger coming there like if you have Nagpur for example, Nashik the growing cities are there, so do you feel that we would like to have some small size stores over there also?

**Yashovardhan Saboo** Apurva, our experience has been that small stores do not really work too well, they reach a saturation point too early well before they are too profitable, we are not ruling out going to smaller cities, but we are going to be very careful about going there, we would rather serve these cities through our internet and existing larger stores. In general, we want to focus on larger stores in larger markets with an extended reach through excellent internet services.

**Apurva Mehta** For marketing spends, so what is your take for next few years – are we continuously going to double it or …?

**Yashovardhan Saboo** I do not think we can double market spends continuously, but there will be a significant increase in market spends not only in absolute figure, but also as a percentage of sales, we will be investing heavily in marketing across channels.

**Moderator** Thank you. The next question is from the line of Sangeeta Tripathi from Sharekhan. Please go ahead.

**Sangeeta Tripathi** Wanting to understand that you just talked about the operating leverage that could be there in terms of rental cost, employee cost and your other inventory cost. So now what I understand is most of our stores are on revenue share agreement, is it not? And when the last mile sales are getting consummated at the store level, then where are we getting leverage on rentals?

**Yashovardhan Saboo** The first presumption is wrong, most of the stores are not on revenue share, most of the stores are on fixed rental, some of them are on fixed rental with a marginal revenue share and that marginal revenue share is significantly lower than the current percentage that we have. Therefore, going forward, with increase in sales, without increasing new stores, we will get leverage on rent.

**Sangeeta Tripathi** One other thing I wanted to understand is our customer acquisition cost as far as the online medium is concerned, what would be that?

**Management** It is on an average today we for the final sale generated, we have to spend something like Rs.3,000 to Rs.3,500 per customer from the internet.

**Moderator** Thank you. Our next question is from the line of Devanshi Dhruva from Dolat. Please go ahead.

**Devanshi Dhruva** I just wanted to ask that does KDDL have exclusive rights to open the boutique stores that have opened in of Rado and Longines in Mumbai and New Delhi and all?

**Yashovardhan Saboo** No, Ethos does not have exclusive rights. In fact all the brands, I do not think anybody signs exclusive rights anymore, but it really depends on the suitability of the location. What does happen is the brand and the retailers together, they do not really want to go in areas where the brand is already well established because that will just lead to cannibalizing of sales. So, in a sense, there is some kind of a regional autonomy that is there, but it is not an exclusive arrangement.

**Devanshi Dhruva** Does Helios also market these products, your longines and ….?

**Yashovardhan Saboo** To the best of my knowledge, Helios does not retail neither Rado nor Longines.

**Moderator** Thank you. Next question is from the line of Jehan Bahla from Motilal Oswal. Please go ahead.

**JN Bala** My question is on the investments that would be required to be made to open a store. So, that would occupy your inventories as you told. So, how much would that be and how much setting up a store, furniture etc.,?

**C Raja Sekhar** Again, this figure varies from store-to-store, but on an average the largest investment is in the stocks for the store, it again varies from the store format. Typical Ethos store requires something like Rs.2 to Rs.2.5 crores of stock initially. Summit store requires a much larger stock from Rs.6 crores going up to about Rs.10 crores depending on the kind of store. In addition to this investment in inventory, the other big investment is actually in doing up interiors of the store, so, the investment in the fixed assets for the stock. Normally, that varies from Rs.40 to Rs.50 lakhs per store. So, these are the big investments that are going to building a store.

**JN Bala** For a normal store, the investment would be Rs.2.5 crores in inventory and around Rs.3-odd crores. What would be the revenue say 3, 4 years down the line from this store?

**C Raja Sekhar** Typical Ethos store should generate about Rs.2.5 crores of net sales in first 12 months of operation and again these are stores that grow @25%, 30% Y-o-Y.

**Moderator** Thank you**.** Next question is from the line of Chiranshu Kumar from Girik Capital. Please go ahead.

**Chiranshu Kumar** How do you define a mature store?

**C Raja Sekhar** Any store that has had a full two years of operations is what we call as mature store. So, our benchmark is that a store which has had two years of operation should do a complete breakeven.

**Chiranshu Kumar** And sir, like if I see the past numbers also a little bit, the EBITDA margin of a mature store is somewhere around 10%, 11%. So, that is the maximum range that you can think a mature store does.

**C Raja Sekhar** No, in fact, we believe it can be higher. Just to also clarify, this is the EBITDA margin before allocating the central office expenses, and we do believe that this can be improved substantially.

**Chiranshu Kumar** Sir, because I tried and benchmarked that Hengdeli also, so, Handley maximum does an 11% EBITDA margin. Can it be increased beyond that that is what I just wanted to understand?

**C Raja Sekhar** So, as I said the 10% which you are seeing the allocation of before central office expenses whereas what you would have seen for Hengdeli would be the overall EBITDA. So, the comparable figure for us in the current quarter is about 6.7% and the YTD figure is about 5%. So, we do believe that there is a huge room for improvement.

**Chiranshu Kumar** Sir, this is after the allocation of central office expenses?

**C Raja Sekhar** Correct, the Hengdeli figure that you are referring to. The figure you are referring for mature stores, that is not after the allocation of central office expenses.

**Chiranshu Kumar** I also wanted to understand the ticket size of a physical store and the one that is generated from an online store. Is it still like 97,000 and 50,000, has there been any chance since the last quarter?

| | |
|---|---|
| **C Raja Sekhar** | The overall has improved marginally, it was about Rs.52,000 average MRP, has gone up to about Rs.56,000 average MRP, and the online still remains in the range of about Rs.1 lakh of average MRP. |
| **Chiranshu Kumar** | I wanted to understand in terms of inventory. So, like if whatever incremental sales that we are seeing, whatever growth that is going to come in terms of Ethos top line, side-by-side our inventory also has to increase proportionately or like majority of that is going to come from that online sales portion and the inventory need not be increased in that proportion because, otherwise, the ROCE would stay at the same level? |
| **Yashovardhan Saboo** | So, the inventory will not increase in proportion to the sales, and that is the reason why we believe that the stock turn would improve. So, the number of months of stocks that we hold will steadily go down. |
| **Chiranshu Kumar** | So, the incremental sales going to come more from the online thing and the inventory will not increase in proportion that is what should be taken? |
| **Yashovardhan Saboo** | Yes. |
| **Moderator** | There is one question that has come in queue from Sadanand Shetty from Taurus Asset Management. Please go ahead. |
| **Sadanand Shetty** | I want to refer one data point in presentation where you mentioned online as a percentage of Ethos revenue. Is this data reflects online billing revenue? |
| **Yashovardhan Saboo** | For this quarter is Rs.23 crores, you are right. |
| **Sadanand Shetty** | I am referring this online billing percentage is the same data, you have another data point which says online as a percentage of Ethos revenue. Is this the same data which is in crores, as Rs.23 crores. |
| **Yashovardhan Saboo** | Rs.22.7 crores which represents about 23%, right. |
| **Sadanand Shetty** | But if I calculate that for Rs.88 crores of your Ethos revenue, it should be 26% and that seems to be right also perhaps considering your last quarter online as a percentage of Ethos revenue was 23%? |
| **Yashovardhan Saboo** | The difference is really calculated over billing or net sales. So, there is that difference of 10% which comes because of that. The billing figure for the quarter is 98.4 and the net sale is 88. |
| **Sadanand Shetty** | Your absolute lead generated is that the absolute lead executed also? |
| **Yashovardhan Saboo** | These are executed sales from the leads. |

**Sadanand Shetty** There is a decline Q-o-Q. The lead generated in the last quarter is 33,951. So, is there a decline in lead generated?

**Yashovardhan Saboo** Yes, there is. Sadanand, our strategy is focusing pretty extensively on improving conversions because what is happening is that lead generation, there is a cost per lead. But so long as conversion remains low, we spend money without getting the fruit of it, and we believe there is a huge scope to improve conversion through improving the quality of interaction. We did a brand wise analysis and there are conversions ranging from 1% to 8% but the average was only some 3%, 4%. So, the strategy really is to increase this to focus on increasing the conversions, rather than increasing the lead. So, that does not mean that the leads are not increasing. What we are also doing is improving the quality of the leads.

**Sadanand Shetty** Can you also provide data if possible average ticket size on lead generated? Sales made on lead generated, average ticket size of that.

**Yashovardhan Saboo** Average ticket size or the sales from leads is about 97,000 what we were talking about.

**Sadanand Shetty** So, this seems to have gone up right now Q-o-Q basis?

**Yashovardhan Saboo** I think it is trending around the same figure; it keeps going around Rs.95,000 to Rs.1 lakh range

**Sadanand Shetty** And the mature stores remains around 50,000?

**Yashovardhan Saboo** The stores overall, yes, remains around 50,000.

**Sadanand Shetty** Any new catchment area that you have added where you do not have offline presence?

**Yashovardhan Saboo** Frankly, we are not really monitoring in terms of catchment areas too much, that is something that we want to do. But rather than focus only on geographical catchment areas, we are actually focusing online on Consumer segment. So, for example, one segment that we want to focus on quite intensively, is the so called Wedding segment. Wedding is one thing for which a lot of watches are bought, not only for the bride and bridegroom but for their families as well. And that is a very niche segment, but it is a large segment. But you have to be able to capture it in a very focused manner. So, how can we use the internet, how can we use the information available on social media to actually focus all our marketing efforts and sales promotion efforts at this segment. So, I believe segmentation and increasing our footprint not only in geographical terms but in terms of market segments. I think that is going to be more effective in the near future.

**Sadanand Shetty** No, you are talking about the new market segment, new product profiles?

**Yashovardhan Saboo** Not new product profiles, I am talking about a new market segment, for example, if you believe that the wedding market is a large market for buying watches, then how can you focus your marketing efforts on this market.

**Sadanand Shetty** Since you have reasonably established omni-channel model on the luxury product like watch, are you extending this to any other luxury product?

**Yashovardhan Saboo** I would like to start by saying that first of all, omni-channel, we have closely studied this and there are still many-many steps that we have to do provide a seamless experience. I believe this is the future for all retail and for luxury retail, it is extremely interesting and all. So, omni-channel, of course, we started on that way and we are going to be focusing very intensively on giving the customer true Omni-channel experience which is really seamless. I think that is the holy grail of retailers in the years to come. There is a lot to be done for Watches; I believe Watches can grow at +30% for Ethos over the next couple of years. Therefore, I do not want to dilute our efforts too much by starting to focus on too many other things. That said and done, we are conscious that there is another very closely-related segment, which is also large area of opportunity and that is relating to Jewellery, particularly, Jewellery which lends itself to being dealt with also on the internet, and we have started to examine this. On a trial basis, we have placed solitaires-related jewellery at two of our stores, in fact starting just last week, and this is really on an experimental basis, we want to learn, we want to know more about this business, and we want to see how our internet network combined with our physical stores can help us to get a foothold in this business also in the future. But, really at the moment, it is on a trial basis.

**Yashovardhan Saboo** Thank you. We have no further questions. I would like to thank everyone for joining in the call and I hope we have been able to respond to all the queries adequately. For any further information, please get in touch with SJA, our Investor Relations Advisors. Thank you very much and good bye.

**Moderator** Thank you Mr. Saboo. On behalf of KDDL Limited that concludes this conference. Thank you for joining us and you may now disconnect your lines.