Arvind fashions

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CORPORATE PARTICIPANTS

- Kulin Lalbhai – Non-Executive Director
- Shailesh Chaturvedi – Managing Director & CEO
- Pramod Gupta – Chief Financial Officer
- Ankit Arora – Head, Investor Relations and Treasury

Moderator: Ladies and gentlemen, good day, and welcome to Arvind Fashions Limited Q2 FY22 Earnings Conference Call. As a reminder, all participant lines will be in listen-only mode and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing * then 0 on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Ankit Arora – Head, Investor Relations & Treasury at Arvind Fashions Limited. Thank you, and over to you, sir.

Ankit Arora Thanks Ali. Hello, welcome everyone and thank you for joining us on Arvind Fashions Limited earnings conference call for the second quarter and half year ended Sep 30th, 2021. I am joined here today by Kulin Lalbhai – Non-Executive Director, Shailesh Chaturvedi – Managing Director & CEO, Pramod Gupta – Chief Financial Officer. Please note that results, press release and earnings presentation had been mailed across to you earlier and these shall also be available on our website www.arvindfashions.com. I hope you had opportunity to browse through the highlights of our performance. We'll commence the call with Kulin providing his key thoughts and brief update about financial performance for the second quarter and half year ended Sep 30th, 2021. He shall be followed by Shailesh who will share insights into business performance and key priorities for us moving forward. At the end of the management discussion, we will have a Q&A session.

Before we start, I would like to remind you that some of the statements made or discussed on this call today maybe forward-looking in nature and must be viewed in conjunction with risks and uncertainties we face. A detailed statement of these risks is available in this quarter's earnings presentation. The company does not undertake to update these forward-looking statements publicly. With that said, I would now turn the call over to Kulin to share his views. Thank you.

Kulin Lalbhai Thanks Ankit. A very good evening to you all. Thank you for joining us for the Q2 results. The previous quarter saw the markets opening up post the COVID second wave. What was very heartening to see is that the recovery was more than twice as fast as the recovery after the first wave. Most of the retail channel opened up by August and the market response to the end of season sale was also strong. AFL was able to make the most of this recovery and post a strong set of numbers with the cash break even in the continuing business. Sales for the quarter were up 113% year-on-year and 165% quarter-on-quarter. Higher sales and good cost controls led to 100 crores swing in the EBITDA compared to the same quarter last year and we ended the quarter with an EBITDA of 72 crores. The offline channel showed a lot of resilience while July remained affected by store shutdowns, August and September retail sales were almost back to pre-COVID levels. A highlight was the performance of the power brands which saw 145% growth over the same quarter last year.

The department store channel saw a slightly slower recovery but we do expect momentum to pick up in the channel in Quarter 3. The MBO channel also saw very robust tertiary sales due to fresh stocks and healthy footfalls. The offline recovery has seen further momentum building up post Quarter 2. This was one of the strongest Diwali seasons we have seen in many years. Customers came out in big numbers this Diwali and with a fresher and higher level of stocking in the channel we were able to post high double-digit LTL sales across our brands compared to the Diwali season which was before the COVID impact. We are also cautiously optimistic that this performance will sustain post Diwali due to a strong performance of the winter wear offering.

The online business continues to be a highlight, even on a very large base this business saw growth of 55%. We added 120 crores of additional sales in the online channel compared to Quarter 2 of last year. Marketplace sales have scaled up with an expanded offering in the core business, launch of new categories and by connecting a larger number of stores for Omni sales. FM continues to gather momentum with sales almost doubling year-on-year for Quarter 2. NNNOW.com has scaled up with a focus on fresh season launches, a scale up in the beauty category and the launch of more exclusive offerings.

We are well on track to achieve a 1000 crores online business run rate as we exit the year. Our focus on improving inventory turns have started showing results. Even though sales have gone up 113% compared to last year, inventory has come down by 60 crores from the comparable quarter last year for the continuing businesses. Overall inventory reduction is over 180 crores considering the business exits. We are on track to exiting the year with an inventory turn of 4. Q2 also saw completion of two important strategic actions. The first one was the exit of the Unlimited retail business to V-Mart. The transaction has been completed and the company has already received 166 crores from the transaction. In addition to the upfront amount AFL will also receive milestone link payments in the future.

Another critical transaction was raising 400 crores through the preferential allotment route. We are happy that marquee investors participated in the round and repose their faith in the company. Debt reduced by 70 crores compared to the quarter before. With the preferential fund which came in the month of October and strong collections from the festive season, we expect the debt to further reduce and settle around 600 crores by the end of the year. This would be the last quarter of losses from discontinued operations. The one-off charge largely comprises of the operating losses of the unlimited business before it was handed over and the complete exit of the GAP business. We have accounted for all future losses that would accrue for a complete business exit and hence there will be no other losses from discontinued business moving forward.

We are excited about the second half of the year. The festive season has gone off very well and the momentum for the autumn winter season appears to be strong. With healthy inventory levels and a high level of freshness, we expect a boost in productivity through the retail channel. Store openings have also accelerated and we expect to open 150 plus stores by the end of the year. The digital channel should continue its momentum with new category launches and the omni channel push. We will remain tight on costs and focus on further improvement in working capital turns. With the scale returning to the business, improvements in productivity, along with reduced cost structures and exit of loss-making businesses will allow us to achieve a positive PBT for the second half of this year. I would like to now hand it over to Shailesh Chaturvedi to talk about the brand level highlights, market recovery and the plans moving forward.

Shailesh Chaturvedi: Thanks Kulin. Good afternoon, everyone. Q2 was a quarter of robust recovery in business, both strategic gains as well as on recovery of revenue and profitability. Strategically, sale of Unlimited around second half July was a very key outcome. A month from then, we also raised 400 crores through preferential allotment in second half of August which capitalized the balance sheet adequately, leading to sharp reduction in net debt which stands at close to 420 crores at end October as the capital reached our banks in early October. By September end, we've also completed exit of discontinued brands and made all the adequate provisions for every anticipated hit there. Business of continuing brands reached cash breakeven in Q2 and with its high teen like-to-like retail (LTL) growth in pre-Diwali season, we are achieving higher level of business performance. The like-to-like growth has been even higher for our power brands like US Polo, Tommy Hilfiger and Calvin Klein. I am very excited to see double digit pre-IndAS EBITDA in USPA once again in Q2.

Overall AFL revenues more than doubled in Q2 and they continue to gain traction even after Diwali season. Finally, onset of winter has helped retail footfall, demand has been very strong in Q2 and it has continued that momentum Q3 also. With very high freshness quotient in merchandise in this fall holiday season and with significant strengthening of backend processes in terms of buying, stock planning, loyalty program, visual merchandising, we are pleased with high quality of our execution in this season. We have sharp focus on our six high conviction brands and our portfolio has unique consumer appeal in post-COVID scenario with inherent relaxed, casual and comfortable appeal along with multi-category play. Online channel grew 55% in Q2 and accounted for more than 40% share of our revenue with a scale of more than 300 crores from online. With the growth of 120 crores in Quarter 2 compared to the same quarter last year and more than 90% recovery over pre-COVID, we remain undisputed leader in online business in apparel, lifestyle and accessories space with a monthly run rate of more than 100 crores in this quarter. We added omni capabilities to another 150 stores taking the count of omni enabled stores to 750+ and we've achieved mid-teen percentage share of store business through omni linkages. We also added further capabilities in B2C warehousing for online for higher volumes and faster and cheaper fulfillment. With completion of exit strategy on discontinued brands at end September, 400 crores capital raise in Q2, full recovery of revenue by August, cash breakeven in continuing brands in Q2, sharply lower debt at end October and fantastic same store growth of high teen percentage in pre-Diwali season, AFL is poised for strong business performance in times to come. Our focus will remain on strong execution on six high conviction brands and on improving profitability. With that, we can now open the floor for question & answer.

Moderator: Thank you very much. Ladies and gentlemen, we will now begin the question-and-answer session. The first question is from the line of Rishikesh Ojha from Robo Capital.

Rishikesh Ojha: One question from my side, our EBITDA is 72 crores for this quarter but if we see majority of our lease or rent expenses, they are recognized into depreciation or interest expenses. In that case will it be fair to say that our real EBITDA is actually very less?

Pramod Gupta: In the results as per IndAS, the rentals are reflected under depreciation of ROU assets and interest on lease liabilities. Also, there has been a reduction in the operating costs and hence, our EBITDA performance has improved on Y-o-Y basis. Ankit or I can separately explain to you outside of this call on the same, if anything additional needed.

Rishikesh Ojha: I will take it later.

Kulin Lalbhai: One thing I would like to add is even without IndAS impact the EBITDA of the company has been enough that we achieve the cash profit for the continuing business. And since the offline recovery was not back to 100% and even without 100% recovery, we have posted reasonably strong set of numbers on the EBITDA side. I think as we reach full normalcy and we get back into LTL growth and full scale, you will see the percentage EBITDA improve in the quarters to come.

Pramod Gupta: If I just stack up the numbers without IndAS impact also, it's the positive cash profit quarter, which means that we have taken out the entire impact of Ind-AS and just talk intrinsic business performance.

Moderator: The next question is from the line of Nishid Shah from Ambika Fincap.

Nishid Shah: My question is what's the strategy now on beauty and fashion, especially on Sephora, given the fact that Nykaa has a dream run and a dream listing, how are we trying to capitalize on that? That's my first question.

Kulin Lalbhai: I can come in here. See I think one important thing to just keep in mind is I think one should not draw one to one comparison between different formats which are quite different in terms of their ASP and addressable market. Coming to the Sephora business specifically, Sephora operates in the prestige part of the beauty business. This is the Rs. 1500 plus ASP product. Within that product range, it actually has a very strong dominant market share. In fact, between whatever we do on the offline side plus online, Sephora does have a strong position in that market and we believe that market will continue to grow extremely well in India because as the per capita GDP goes up, there will be more and more women upgrading into that particular segment. So, Sephora will continue to operate in the prestige segment. I don't think there would ever be a strategy to get into the mass segment because that's not what Sephora is known for or what would be good at. In order to win in the prestige segment, the key aspects of the strategy that world over have worked very well is one, a very unique offering because Sephora private label as well as the exclusive brand which are launched through the Sephora franchise globally every year are the unique differentiation of Sephora. So some of the world's most exciting new beauty brands are born in Sephora because they get the whole huge global Sephora network to scale up. Every year there will be many of these new exciting brands coming into the country and with that exclusive catalogue, it really helps cement Sephora in the place of the prestige customer. The second aspect is the retail experience, one of the things that Sephora is known for globally is not just selling products but selling experience, selling makeup experience, the in-store wow that needs to be delivered and that is possible because of again the format and the kind of animations and in-store services that are made available. There also the idea is as digitization comes into the store and as more and more, the store experience is upgraded globally, we would want to bring more and more aspects of that global rich experience to the retail format. I think if we stayed true to what Sephora is known for globally which is its unique assortment and very high experiential retail, we believe that Sephora will have a strong place in the Indian market especially in the prestige part of the which is as such the real addressable market for a format like Sephora.

Nishid Shah: I'm glad you explained this in detail but when do we have Sephora India because if you go internationally on Sephora's site, you have a very different and a unique experience which is not available in any of the online sites right now. For example, a woman come to the site and looking at her skin color, they will suggest what kind of makeup has to be used and all of that. So right now on NNNOW.com, you do not have those kinds of options. So, when are you going to have Sephora india.com coming into play?

Kulin Lalbhai: We are working with our global partners on that thought process. Since it's a global tech stack which requires to be executed in a fully comprehensive way, we have to figure out how we can execute it perfectly but it is definitely something which is an ongoing discussion. We hope to bring that aspect also of the experience to the market as soon as we can.

Nishid Shah: My last question is, you mentioned and it's very good that you are now a leader now in the online space especially in segments you operate in. Now, how do we capitalize that like we are leader and have more brands and more prominence in the online space, if you can elaborate little bit on that.

Kulin Lalbhai: What we had discussed maybe even in the last call is that, online as a business model is evolving very quickly where rather than a wholesale mindset, it is a model where brands now will directly control the experience through own.com and through the marketplace model on third party websites. We actually will now be developing merchandise just for the online channels. The more you use analytics and a quick supply chain to quickly feed the online channels, one can grow very disruptively. Our company is building all of these new age capabilities along the signs of analytics, along the signs of flexible and quick supply chain, new category inciting, all of this allows us to build a very robust and quick efficient catalog for the online business. I think capitalizing online opportunity can be done with very strong portfolio of brands we have. In fact, a lot of the levers are also about getting into new categories like footwear for example where US Polo has become a #1 footwear brand. It could not have happened in the offline space but it can happen in the online space. A part of the reason you're seeing this kind of traction is, we have built all of these capabilities and we hope to keep doubling down on that and protecting the market share and continuing the growth momentum. I don't think we would lose the opportunity in any way and we would work to capitalize on it to the full extent.

Dhruv: I have two questions. One is, you mentioned that you will exit this year with a 4x inventory turn, so if I recollect correctly last time, you said that you want to end with 5x. Are we on course to deliver that?

Shailesh Chaturvedi: Yes. See what we mentioned last time and what our stated goal is to move towards 4 stock turn and we are on course for that. We've also done a lot of backend changes in terms of the way we place the orders for inventory, there is a supply chain project going on to reduce the lead time of supplies and improve the turns on the core products with the automatic replenishment model. So, our entire objective is to reach 5. We were 3, we are now improving it significantly to move close the year by 4. As we go along, we will definitely move forward. Our intent is to move towards 5 but it will happen through step by step approach. We are very committed. This is a key priority for our organization to continuously increase the stock turns. If you look at last few quarters that we have managed our inventory quite well despite COVID and stock turns are going up and our intent is to reach 5 times in the medium term.

Dhruv: Can you elaborate on the margins front for the online and offline channel? Since, the online channel is almost 30% of your revenues, so it will be good to know what is the margin difference between an offline and online? I am talking on pre-IndAS basis.

Shailesh Chaturvedi: Both online and offline margins for AFL are on the increasing trend. We are seeing the trend where both the margins are going up and also because as we recover fully post COVID, our margins are going up. Now if you say difference between an offline and an online channel margin, the way our online business is constructed it's a very profitable business already. Online and offline margins are very similar in the power brands and both are sort of converging and we are looking at moving to double-digit EBITDA in the medium term both across offline and online. So, It's a very similar percentage of margin we are seeing in both offline and online.

Dhruv: My last question is you mentioned about Tommy, Calvin and US Polo performance. Can you give us a word on Arrow, how much recovery have we seen in Arrow now that most offices have started?

Shailesh Chaturvedi: Arrow has also seen good upswing, July definitely the business was impacted by COVID and Arrow has a higher percentage of its business coming from department store & EBOs in the big cities. So, July was COVID impacted but September onwards, Arrow has started breaking even on EBITDA level. We are hopeful that in the Quarter 3, Arrow should deliver even better profitability. While Arrow profitability is improving on a slightly lower base to start with but we are seeing good traction in terms of like-to-like growth and also in terms of EBITDA profitability.

Moderator: The next question is from the line of Harsh Shah from Dimensional Securities Limited.

Harsh Shah: My question is on the gross margin front. If we look at the current quarter, we have been somewhere around 41.5% which has been in the range that we used to do when we had Unlimited in our revenue base. I would believe that Unlimited being an economical brand was a lower gross margin business. So, if we remove that then shouldn't our gross margin have been much higher and addendum to this, if I look at your numbers below the gross margins, then we have 4% royalty expense and then we have another 7% to 8% of commission expenses. If I deduct these from your gross margins then we come to roughly around 20% to 30% net gross margin if that makes sense. Then my question is from where can we get that operating leverage to reach the mid double-digit kind of EBITDA margins?

Shailesh Chaturvedi: If I look at our gross margin over FY20, the pre-COVID time, we are at 42% and another way we look at our margin is what is called as contribution margin where the variable selex is removed. So, at contribution level, we are seeing our margins going up by 2% to 3%. We've seen the trend in Q2 and we are seeing that trend continuing. Gross margins in this quarter and in the same quarter in ’19 we were similar at 42%. If you look at Quarter 2, there are two things which stand out as far as the gross margins are concerned. One, for an exceptional reason of COVID where recovery isn’t 100% and second, the entire end of season sale happened in Q2. Typically, this starts in June and then it comes into July. So, part of the lower margin of EOSS happens in previous quarter in our industry and then the remaining part happens in the early part of the Q2. This year because the malls were not open and the retail channel was not open, the entire discounting in the EOSS has happened in the Q2. So as an exception, the Q2 margin got slightly impacted because of the EOSS discounting that happened in this quarter rather than happening in Q1. That's a one-off thing and despite that our margins are holding up at 42% similar to what it was at the pre-COVID level and at contribution level we are going up by 2% to 3% because of all the efficiencies that we have brought in. Second thing is that we also have to look at gross margins in terms of channel mix change. Now here the online business comes into picture and online as the share of online business has gone up significantly in this quarter compared to the pre-COVID same quarter. Now online is a very profitable business as I said earlier, very similar to the offline profitability but there is a difference between the gross margins and the contribution level. So, in online business the difference between gross margin and contribution is very low. The retail costs, selex etc. that comes in offline doesn't come in online, so the right way to look at margin in our company and in our industry is to look at contribution level and online has a very good contribution level but it has a slightly lower gross margin. The gross margin will see an uptick because of all the efficiencies that are kicking in and the inherent profitability of our power brands and exit of less profitable businesses. We believe that in short-term horizon we should move from 42% up to mid-40s. We are very confident that in the couple of quarters it will hit the mid 40s gross margin. This should stabilize and we should improve further on that.

Harsh Shah: Can you explain us the difference between gross margin and contribution, how you calculate this number?

Shailesh Chaturvedi: When we remove the discounting and the taxation from the retail price we get to gross margins and from gross margin, we remove the variable expenses, the retail expenses which doesn't come in online business, it comes only in offline. Further, we remove the commissions, rental etc. So, all the variable components get deducted, to arrive at contribution margin.

Kulin Lalbhai: One other way to think about is, below contribution margin we only have advertising and fixed costs. The rest of variable costs are between gross margin and contribution margin.

Harsh Shah: My another question is on commission side which is nearly at 7% of revenues. I would believe, a lot of our sales also comes from the franchisee route. Then what exactly is this commission, whom we are paying at 7% because none of the peers have this line item which is so high?

Shailesh Chaturvedi: Yes, you're right. This is the franchisee margin that we pay. We have a smaller percentage of our company stores and we have a larger franchisee network, so that line item comes through as a commission.

Harsh Shah: What would be the split between franchisee and own sales?

Shailesh Chaturvedi: So, our own COCO share is less than of 20%.

Harsh Shah: So, 80% you are saying would be from franchisee route?

Shailesh Chaturvedi: Yes, higher than 80%.

Harsh Shah: And the store expansion which you're talking about would again mostly be from franchisee route?

Shailesh Chaturvedi: Our store expansion will be on asset light model, that's our stated policy. So, most of our expansion will be through the franchisee network. And we have figured out a method where we manage the operations very tightly in a franchisee model. Out of around 175 stores that we are planning to open, they will be largely from the franchisee route.

Harsh Shah: Another book keeping question which I wanted to ask is, just wanting to understand the accounting aspect of this. So, when we sell via franchisee, is the commission expense only the revenue that your franchisee earns or do we also give them certain discounts to the selling price?

Pramod Gupta: The discounts that we give to the selling price goes into the discounting line. If you would like to have more detailed understanding, Ankit can connect with you separately and explain to you a little more in detail.

Moderator: The next question is from the line of Sagar Parekh from Deep Financial Consultants Private Limited.

Sagar Parekh: So, my question was on the leverage, if I heard it correctly you said that by the end of the year, we are looking at about 600 crores of debt. Right now, if I adjust the cash, we are about around net debt of about 400-450 crores and we are talking about improving profitability and cash flows and H2. So, what is the missing link here because if we are at 400 crores right now and as the cash flows improve then ideally the debt should reduce further the from here?

Pramod Gupta: So, Sagar there is no missing link as such in this. The point is that as you know at September quarter end, we have to buy a fair amount of inventory in order to build up the stocks for the upcoming festival season and October month has been a great month for us in terms of sales. Therefore, while the cash had been received upfront because our sales have been pretty good but some of those inventories will have to be paid for. So around 100 crores or so will be going into our working capital. Also, at the end of September the money had just come in and hence, some amount of this will get utilized. That's what we had mentioned earlier also that we are raising these funds, both to make sure that we have adequate growth funds available as well as to reduce our debts. So, it will be significantly lower than what it was at the end of March'21. There will be a reduction in debt of at least 350 crores and we are completely focused on reducing the leverage even in times to come.

Sagar Parekh: In H2 FY22, as we improve our profitability, we would throw some cash in H2 or we would probably after working capital we'll just like break even what is the sense there?

Shailesh Chaturvedi: Our continuing business is already is at the cash breakeven stage even in Q2 and that had significant impact of COVID in July. So H2 looking very promising and it should throw up significantly higher cash than what we have seen in Q2. Our debt level that we are forecasting will be 600 or maybe slightly lower than that. However, our intent is to keep the debt level as tight as possible. We would like to conservative and other than building inventory for growth in channels for the season launch that will happen in spring summer in February & March, we will have no other reason apart from that. So, our debt level will be very tightly monitored. Our inventory in the last two quarters has been managed very tightly. Our execution has been good and we hope to continue on that.

Sagar Parekh: So now basically since Unlimited has gone, capex would largely be very minuscule going forward also in FY23 and H2 because the store additions are all coming through franchisee route. So, capex would be like 30-40 crores per year, is that right understanding?

Pramod Gupta: Yes, between 30 to 50 crores is the kind of number we should be looking at. But having said that, Sephora will not be franchisee and we are also committed to investing very heavily around IT systems etc. Further, if you look at the metro cities, we would invest behind some of the experience stores and renovation etc. but 30 to 50 crores kind of capex is the right number to think about.

Sagar Parekh: Sephora, how many stores do we have currently operational?

Pramod Gupta: 24.

Sagar Parekh: How many stores do we plan to add next year and H2 also, in the next 18 months how many stores do we look to add?

Shailesh Chaturvedi: We have dialogues on for six more stores and depends on how the malls open up but between four to six stores we will definitely open.

Sagar Parekh: That would entail a capex, what would be per store capex?

Pramod Gupta: Sagar we don't specifically talk about this level of details regarding our capex but you can rest assured that we will continue to maintain a very significant amount of capital efficiency when the store opens. Sephora stores will typically be prestige stores, so it will be a place where we would like to give an excellent experience to the customer and at the same time maintain the capital efficiency of investments we have done.

Sagar Parekh: And my last question would be on the margins pre-Ind-AS for next year. So given a normalized scenario what should be the pre-Ind-AS margins that we should look at broadly given that we have done all the cost cutting, some bit of permanent cost cutting and with improving inventory turns and the situation getting normalized. Obviously, the sales will pick up so what should we like the pre-Ind-AS EBITDA margins that we should look at?

Shailesh Chaturvedi: I wouldn’t be able to discuss specifics and provide you any guidance here. But, I would definitely like to tell you that since all our brands in continuing business are high conviction brands and near double digit EBITDA for power brands is the next goal for us in the short to medium-term. Now beyond that I wouldn't want to specifically answer that question, however, we would continue to make progress on profitability, that I can confirm.

Sagar Parekh: At 4,000 crores kind of top line for the 6 and the smaller brands, broadly you think we can reach there?

Shailesh Chaturvedi: I would not want to talk about a specific top-line number or a specific margin right now, but you'll see that there is a significant progress happening on sales & profitability from our side.

Sagar Parekh: Basically, double digit EBITDA is possible, let's say in 2 to 3 years from now at least?

Pramod Gupta: I think we should think about in the next year since your question was regarding specifically FY23 you could think of mid-to-high single digit EBITDA margins pre-IndAS for the next year.

Moderator: The next question is from the line of Miyush Gandhi from Canara Robeco.

Miyush Gandhi: Is it possible to share the revenue of the top six brands, the core business that we intend to pursue very strategically?

Shailesh Chaturvedi: No, we don't give a brand level forecast, so I'm sorry I won't be able to discuss that.

Miyush Gandhi: Will it be possible to share, what was the peak revenues of these continuing businesses in maybe FY19 or 20 whenever it is, because see the business has gone a lot of restructuring, so it becomes very difficult for us to kind of work with numbers and project the estimates. Some further disclosures will be very helpful in terms of understanding the continuing business. Maybe at least if you could share with us the peak revenues the continuing business had reached pre COVID?

Shailesh Chaturvedi: So, I am sorry we won't be able to discuss at a brand level, but one broad number you can look at is pre-COVID run rate was close to 800 crores sort of run rate every quarter

Miyush Gandhi: For the continuing business?

Kulin Lalbhai: Yes. You can consider that as a broad range and then there will be growth.

Miyush Gandhi: Is it possible to quantify how much network expansion would have happened in the last 2 years?

Shailesh Chaturvedi: This year we will grow our network by more than 150 stores, that's a guidance and we are on course for that. Last year was COVID impacted, so that number was close to 100. Our expansion rate is increasing as we’re expanding really rapidly into the Tier-III, Tier-IV cities. And, it’s likely to become 175 to 200 stores expansion next year. That's again a very focused area for AFL that we want to penetrate deeper into the Tier-III and Tier-IV cities and we have put a distribution structure already in place that will support this expansion.

Miyush Gandhi: Just one last question from my side on the online side, I'm sure you must be tracking it. Where is the incremental demand coming from, is it more urban centric or it's more rural areas? The reason for asking this question is whether our existing demand, which was kind of fulfilled from stores, has that moved to online or we've been able to find newer locations and geographies where we are not present and that is a new area where we are getting new sales from?

Shailesh Chaturvedi: If you look at the online data and we have a partnership with Flipkart group and Flying Machine and we work very closely with all the big portals, we are the leader with each one of them. Now what we are seeing is that what started as an urban metro phenomenon of online growth in the big cities, in last two years it has gone to the smaller town and COVID sort of accelerating that penetration in the smaller town and we are seeing very-very healthy pick-up from Tier-III, Tier-IV cities online. Also, in our core network which is metro centric, in Tier-II and Tier-III cities we are seeing good omni connect. We are already reaching mid-teen level of omni business where consumers are linking offline and online experiences. So, in urban cities we are seeing good growth, but percentage growth is much higher, because of the lower base of Tier-III Tier-IV cities and we are clearly seeing the convenience of online channel and also the performance of any omni-linked store which is going into the smaller tier cities, it's quite visible.

Kulin Lalbhai: One number which is interesting is that if you look at incremental sales, almost 50% now is outside of the metro and tier 1s, so what Shailesh was saying the growth is faster in Tier-II Tier-III and in fact it's a world where brands maybe first experienced online and then our stores follows. So, what we've actually done in some of our brands is when we see sales in certain pin codes reach a very high level, that's when one can open up a store in that catchment. I think the world is quite Omni and it's not a cannibalization but cohesive through put that comes from an online plus offline experience, irrespective of towns.

Miyush Gandhi: This quarter the online share of revenue is around 30%, right?

Shailesh Chaturvedi: No, it was 40%+ of AFL revenue which came from online channel and that was a growth of 120 crores over same quarter last year. So, we've seen very good traction in online business. It's little high because also offline was not fully back in Quarter 2, I think we believe that a normal kind of share will be around 30% and not 40%. One data point that really pleases us that in Q2, our online business was more than 300 crores and we were always aspiring to have 100 crores a month run rate in the short term and we crossed that consistently. Now that one milestone has been achieved and we will look at scaling the new peak. The journey has been very satisfying to have a leadership position on the online side.

Moderator: The next question is from the line of Yash Mandawewala from Mandawewala Family Office.

Yash Mandawewala: We've seen really unprecedented levels of inflation in raw materials, packaging and almost every line item. We also have potentially a GST hike on our products from Jan. So how much would the MRP's have to increase by in percentage terms for us to absorb both of these items and just broadly if you can also give a sense of how are we planning to tackle this?

Shailesh Chaturvedi: Your question is very relevant in the current context; we have seen a short-term increase in the cost structure and we hope that the situation improves in short to medium-term. But currently what we are seeing is that there is very little option, we have gone after efficiency in the last 2 years as we've made it very lean on cost structure. From this base we are looking at industry practices and what we are seeing in the market is that last part of this cost increases is likely to be passed onto the consumer, which could be will vary from category to category, brand to brand, but it could be from 5% to 8% right now and we see this is a very fluid situation. We don't know how much more the cost will go up or hopefully how fast the cost may come down, because we have seen that things cooled down very fast also, so we will wait and watch. We will take the decision very close to the event so that we take well-informed decision.

As far as the GST increase is concerned, that category of sales is not very significant portion of our business, so most of our brands and most of our categories will not impact. Because it will impact much lower price businesses. So, right now our focus will be to manage the cost pressure and to see what industry practices are on that and we will follow and pass whatever consumers can absorb.

Yash Mandawewala: Do you acknowledge it'll have any impact on final off take as well, if you know prices were to go up substantially?

Shailesh Chaturvedi: There are two parts, one that the demand side is very strong and we are seeing consumers are really shopping after 2 years as I think they got bored of the COVID situation and with revenge traveling and shopping, demand pull is very strong right now. Cost increase is also a reality. Now it's anybody's guess where how it pans out, so we will wait and watch as what happens.

Yash Mandawewala: Just one last question, which is on the footwear business. Can you just provide some more details on this part of the business? So, what would the size of the footwear business be and if we talk sort of mid to long-term, what are the margins and inventory turns on footwear likely to be in what range?

Shailesh Chaturvedi: Our footwear initiative has been largely on US Polo business and we invested ahead of time on adjacent category in our strongest brand. So, we created footwear business dedicated team, similar to inner-wear and kids-wear business and in the footwear business if I normalize Covid impact, it is now crossing 150 crores. So fairly profitable business with very good return on capital employed, so it's a very good business with very healthy financial profile. We don't give too much of details at a brand level at a category level, but I can tell you that this is a category where we invested ahead of time and we are very happy with that investment because in online space, in many portals including Myntra, our footwear business has been winning awards, we are a market leader in that segment. So, this has been a wonderful addition to our portfolio.

Yash Mandawewala: Do you think that the ROCE there for a power brand could be on par with the apparel business in the long-term?

Shailesh Chaturvedi: Currently higher than the apparel business.

Moderator: Thank you. Due to time constraints that was the last question. I now hand the conference over to Mr. Ankit Arora for closing comments.

Ankit Arora: Thank you everybody for joining us on the call today. If any of your questions have been unanswered, please feel free to reach out to me separately and I would be happy to answer them offline. Thanks so much for your time and look forward to interacting with you again next quarter.

Moderator: Thank you. Ladies and gentlemen on behalf of Arvind Fashions Limited that concludes this call for today. Thank you for joining us and you may now disconnect your lines.