Q2 FY2023 Earnings Call Transcript – Nov 15, 2022

CORPORATE PARTICIPANTS

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

Moderator: Ladies and gentlemen, good day, and welcome to Arvind Fashions Limited Q2 FY23 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 Seema. 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 2022. I am joined here today by Kulin Lalbhai – Non-Executive Director, Shailesh Chaturvedi – Managing Director and CEO and Piyush Gupta, Chief Financial Officer. Please note that results, press release and earnings presentation had been mailed across to you earlier and these are also available on our website www.arvindfashions.com. I hope you had opportunity to browse through the highlights of our performance. We will commence the call today with Kulin providing his key thoughts on our financial performance for the first quarter. He shall be followed by Shailesh who will share insights into business and financial 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 afternoon to you all and thank you for joining us for the results. Q2 was a landmark quarter for us where our strong execution helped us achieve record revenues as well as profitability. AFL saw an industry-leading growth rate of 46% year-on-year. This was led by strong like-to-like growth of close to 25% in retail and the MBO channel doubling its revenues on a year-on-year basis.

The strong topline growth was accompanied by even stronger bottom line growth with an EBITDA margin expansion of 2.7%. The bottom line performance was driven by higher productivity lower discounting and operating leverage. USPA has been a star performer for us this quarter and is poised to become one of the largest casual wear brands in the country in FY23.

Our hard work on working capital control is yielding results with meaningful reduction in net working capital days to 36 days during the quarter thereby allowing healthy free cash flow generation. This quarter has been noteworthy with the company achieving the milestone of going past the double digit ROCE target which we had set earlier this year to deliver annualized ROCE of around 15% in Q2.

We remain excited with the continued momentum and buoyancy in customer demand which positions us to continue focusing on improving profitability further.

I would like to now hand it over to Shailesh to take us through the specifics and more details about our financial performance.

Shailesh Chaturvedi: Thanks Kulin. Good afternoon everyone. With nearly 1200 Crores topline which is the highest ever in a quarter at AFL and Rs. 136 Crores EBITDA, we saw a very good quarter in Q2 at AFL. The growth in topline is 46% and growth in EBITDA is nearly 90%. The result is backed by some good execution of brand promises and activities in the market both online and offline. We saw record sell-through in SS'22 season and the good work on sell-through the continued in FH season also where we are maintained good sell through and continued to reduce discounting.

The result of this good execution is very healthy, nearly 25% like to like growth in our retail and increase of nearly 3% in gross margins. There is a scale momentum at AFL and many of our businesses have become big enabling growth and margins through operating leverage. USPA, US Polo Association, our biggest brand crossed Rs.1000 Crores NSV at end October and has now clearly established its leadership in casual space. Footwear is another adjacent category that has fired, with business at 2x pre-COVID numbers and a growth of more than 50% in Q2. Our portfolio of footwear business is likely to cross 250 Crores NSV market this year with healthy profitability and market leading position.

US Polo now a leading player in its segment in all key fashion portals and recently won award at the best footwear brand in this category on Myntra. Arrow also gained further momentum has now grown at 50% in Q2 and has delivered positive EBITDA. Tommy Hilfiger and Calvin Klein have also grown really well at 50% with very healthy EBITDA margins.

Q2 also saw growth across channels. Retail has grown 70%. MBO trade channel has doubled its business in this quarter over last year. Online is a very healthy 26% of our revenue mix and has delivered business of more than Rs. 100 Crores per month in this quarter. I am also excited about growth in Southern markets, which has been a focus area for company, and in this Diwali, we saw vibrant growth of business in key Southern markets. The revenue growth is supported strongly by omni linkages, and we have added 300 more stores in our omni network and stores with omni linkages see a high single-digit sales contribution coming through the omni route.

The scale and gross margin improvement has come at the back of a wholehearted refresh of our key brands, which we have improved in terms of brand appeal, energized consumer-facing touch points and have developed smarter designs. Our key focus remains improvement in profitability, and I am happy to share that we have delivered close to 15% ROCE in quarter 2 on an annualized basis. In the previous quarter, we had achieved high single-digit ROCE, and now we have reached close to 15% milestone in journey of reaching more than 20% ROCE in the medium term.

The increase in gross margin of nearly 3% has flown into EBITDA margin and AFL has delivered EBITDA of Rs. 136 Crores in this quarter, a growth of 90% over last year same quarter, and increase of nearly 2.7% in EBITDA margin percentage over last year. This improvement in EBITDA is due to reduction in discounting, higher sell-through, higher freshness of inventory, operating leverage and improvement in Arrow's profitability.

The business has delivered a PBT of Rs. 45 Crores with a very healthy cash generation. This has resulted in net debt reduction to Rs. 383 Crores. Through strong execution and tight controls, we kept inventory in check and the inventory days have come down by 6 days right at the start of the season. We had aimed for more than 4 stock turns. And in Q2, we have delivered 4.2 stock turns. There is overall focus on deleveraging of balance sheet. And besides maintenance of net debt level, despite a healthy 50%

growth in top line, our net working capital has come down by 6 days. Both inventory days as well as debtor days have shown healthy reduction.

Q2 also saw strong collections from the market with tight controls on trade policies. PBT of INR 45 Crores has resulted in a PAT of Rs. 18 Crores after minority interest.

Lastly, I want to call out our mega brand U.S. Polo and its strong performance. Q2 saw the highest quarterly revenue by U.S. Polo. Now it is a Rs. 1,000 Crores NSV brand at end October. Its NSV grew with whooping 45% in like-to-like retail. Its adjacent categories, including footwear and kidswear have grown at more than 50% in the quarter, helping the brand continue its double-digit pre-IndAS EBITDA margin trajectory.

In last 1 year, we have spent a lot of efforts in brand refresh in U.S. Polo. You may have seen the new ad campaign on the concept of twinning, featuring Bollywood actor Arjun Rampal and his family. We saw use of Indian celebrity for the first time in U.S. Polo campaign. We also refreshed the brand, store identity and energized product designs, including its denim division. We are very excited about prospects of dominance of USPA in the casual wear space, and we'll continue to wholeheartedly invest behind this brand to support its re-engineered profitability and growth.

I see a growth momentum in our brands in the season ahead, and AFL should cross Rs. 4,000 Crores top line this year. Our focus will be to further improve EBITDA margin and ROCE through profitable scale buildup, sharp execution of brand activities in the market, tight control on trade policies and de-leveraging of balance sheet. Thank you.

Moderator: Thank you very much we will now begin with the question and answer session. The first question is from the line of Sagar Parekh from One-Up Financial. Please go ahead Sir.

Sagar Parekh: Congrats for decent performance and good to see numbers finally taking shape, so congrats for that. A few questions from my side firstly on sequential gross margin reduction that could be purely because of this EOSS coming into July, is that the reason?

Shailesh Chaturvedi: Our industry is very seasonal. So you rightly said that quarter 1, which was largely a full price season, versus quarter 2, gross margin has gone down, but we are happy to say that our EBITDA at a pre-IndAS level has gone up sequentially. So from our quarter 1, the operating EBITDA to the operating EBITDA of Q2, it has gone up actually. While the gross margin has come down because of the EOSS discounting. But for all the other leverage in our expenses, which have not grown at the same pace. Our gross margin has gone up by 15% in absolute terms and because of that, our EBITDA has gone up by close to 1.3% pre-IndAS and it is similar post-Ind-AS, same number. So Sagar, EOSS discounting is a reality, and we do not really compare sequential EBITDA margin. But we are happy to say that our Q2 operating EBITDA is higher than Q1 EBITDA.

Sagar Parekh: But that Q2 to Q1 EBITDA higher of 1.3% as you said is also because of higher other income which is 20 Crores this year so if I remove the other income still the EBITDA is higher on quarter-on-quarter basis?

Shailesh Chaturvedi: Yes. So I reconfirm. Outside of other income also, our EBITDA margin in Q2 is higher, Sagar. As far as that other income is concerned, it's just an accounting IndAS entry. It does not have a bearing. But our pre-Ind-AS EBITDA has gone up in Q2, whereas, normally it tends to come down. But this year, because of the market transition and good performance, it has gone up. I can give you a little more color to that so that this whole question gets addressed squarely. See, there is a gross margin % drop in this quarter compared to last quarter, but that's because of EOSS. But our gross margin went up by 15% in absolute terms in this quarter compared to last quarter and I do not want to again and again compare Q1 versus Q2 because it is not fair. But since you asked that question, I am mentioning that the gross margin has gone up in value by 15%, whereas our expenses compared to quarter 1 have not gone up at the same pace and because of that, our operating EBITDA has gone up. It has got nothing to do with the other income or IndAS. I am talking operating business EBITDA here.

Sagar Parekh: Understood and this other income of Rs. 20 Crores anything to read here because it seems to be on a higher side?

Shailesh Chaturvedi: Yes. But it is just an accounting practice, whatever is as per the accounting rule. So out of that Rs. 20 Crores, Rs.14 Crores is account of IndAS 116 adjustment, which is basically pertaining to reassessment of leases and fair valuation of security deposits and there is a Rs. 6 Crores coming from the interest income and there is some small write-back of provision. So frankly, Sagar, do not read too much into the other income. Our fundamental business, operating margin in Q2 has gone up. But it is unfair to compare Q2 margin with Q1. I think the right way to compare is Q2 to Q2, because there is a large seasonality in our business, Sagar.

Sagar Parekh: So if I compare H1 EBITDA, reported EBITDA before other income of 208 Crores for H1 FY23, how much would be pre IndAS, so if in the past you have mentioned of about 4%, I think is the difference between post and pre, so fair to say that we would be at 6% EBITDA pre IndAS on H1 numbers on 2100 Crores?

Shailesh Chaturvedi: 11% EBITDA post-IndAS in H1 and as you said, there is a difference of close to 4%.

Sagar Parekh: Got it so it is about 10%, just correcting because I am talking about before other income?

Shailesh Chaturvedi: No but I mean that is accounting entry Sagar, 11% post Ind-AS.

Sagar Parekh: Okay fair enough and this is my last question, so this year as you said you will finish the year with about 4000 Crores of topline. Where would you like to see the margins pre IndAS I am saying and in FY24 as you have in the past indicated that we would like to grow our topline at about 12% to 15% well on a steady state basis going forward so how should we think of margins on a sustainable side pre-IndAS EBITDA, as we move ahead in FY24?

Shailesh Chaturvedi: See, if you look at Q2 power brands, we are at close to 13.1% post-IndAS EBITDA. As you can take your calculation of pre, we are very close to sort of the trajectory of double-digit EBITDA in power brands and our first focus on profitability is to reach that stated guidance of reaching a double-digit EBITDA in our power brands in 12 months; we used to say 12 to 18 months earlier and we have made that journey in the last 6 months. So Sagar, I think our first goal on profitability would be to reach a double-digit EBITDA profitability for power brands in the next 12 months and we are confident that whatever we are doing through the operating leverage, through efficiency of our execution, reduction in discounting coming from higher sell-through, improvement in some of our brands' profitability overall, we are guided towards that and we will have to work hard towards that and we are very committed to that journey of reaching double-digit EBITDA in power brands in the next 12 months. As far as the growth momentum, currently, obviously, you've seen our growth momentum is very, very strong, its industry leading. And our guidance on the top line growth is around 12% to 15% and currently, it looks more like closer to 15% because there is a strong growth momentum in our brands. All these 6 brands are very powerful market-leading brands. So that will help us to reach the kind of top line growth we are looking at. All the growth drivers be it digitalization, online business, be it adjacent category growth, be it same-store growth through better execution and also the expansion into the small tier towns, all are now becoming very live and green. So we are confident that we should be in that 12% to 15% growth, in the short term more like 15%.

Sagar Parekh: Great. I have a few more questions I will come back in the queue.

Moderator: Thank you Sir. We will take the next question from the line of Ritesh Choudhary from Molecule Ventures. Please go ahead.

Ritesh Choudhary: First of all congratulations on a very nice set of numbers and it is actually good to see margin shaping up upwards. My question is regarding there was several news articles floating around for the sale of Sephora. So what is the substance in this new?

Shailesh Chaturvedi: We never respond to market speculation. We have to focus on running the business, so no comments from our side on that.

Ritesh Choudhary: Okay fair point. Well that was it. Thanks.

Moderator: Thank you. We will take the next question from the line of Jay Shah from Capital PMS. Please go ahead Sir.

Jay Shah: Congratulations to the management for walking the talk and posting a good set of numbers. I am actually relatively new to the company. So if you do not mind, could you just throw some light that when it comes to these brands, what part of the supply chain do we control? Like do we control the entire manufacturing itself and even if it is that, then what are the geographies that we cater to with these brands and even the manufacturing is it like everything that is done domestically or we do even source something from other geographies?

Shailesh Chaturvedi: I think let us break down our 6-brand portfolio into 3 brands: U.S. Polo, Arrow and Flying Machine. Now Flying Machine is our own brand. We own the brand. We started this as a first denim brand many decades back. Arrow and U.S. Polo are licensed from international giants. In these 3 brands, we do the complete designing as well as production, sourcing, end-to-end everything we do and we pay royalty on Arrow and U.S. Polo to the principal. This is internationally known as a licensing model, where we are licensed to design, produce, and distribute these brands in our territory. Now Flying Machine, our brand, we can do what we want across the world. Arrow, we sell in India. We have a couple of stores in Middle East. We have 3 stores in Dubai. We have rights for many other countries, some small part of Africa. But the focus, frankly, remains on India. It's the largest opportunity, but we have some other geographies. U.S. Polo, which is our biggest brand, also is licensed. We design, develop the brand and a very large adjacent category in this. We have footwear, kidswear, women's wear, innerwear and we sell all channels in that. And we sell in South Asia. We have business in Nepal. We have business in some neighboring countries. But the focus again remains on India. So that's about the 3 brands. There are 3 more brands, which are international brands. So Tommy, CK, it is a joint venture with the principal. It is an equal JV with PVH, Phillips-Van Heusen of U.S., headquartered in New York. And we have been doing the business of these brands Tommy since 2004 we have a very strategic long, perpetual license on Tommy. And Calvin also is a very long-term contract with PVH. And there, we sell goods from their line. So the principal does the designs and the selection of the vendor and after that, we take the goods directly from the vendor into our system and then we pay the royalty to the principal. There is a lot of localization through the help of the principal because they see India as a very big opportunity, and we are a high-duty and depreciating currency regime. So we have gone and done very healthy percentage of localization in this brand higher than any other international brand of similar repute. So it is a very unique relationship and a very unique supply chain that we do and our gross margin performance is very good in these brands and market-leading brands. The final brand is Sephora. We are a distributor there and we source these multinational brands, megabrands, likes of the MAC and the Dior, HUDA, Pixy etc. We import them and we retail. So the role with Sephora is more of a distributor in India. Does that answer the question? Anything specific, more detail you want? I'm happy to sort of throw some more light on that.

Jay Shah: That was really helpful so I just wanted to know that in the geography is that when you say that you have all the rights from designing to distribution so then it is on your perusal that you can even get it manufactured from a third party player also, right?

Shailesh Chaturvedi: No, there are global guidelines on production. So they have to be vetted. In Arvind, our own manufacturing standards are very, very high, and we vet the factory on a lot of parameters so that they meet any international quality because AFL standards are very, very high and we produce in the approved factory that we approve and sometimes, in Tommy, CK, we source from approved vendors by the principal.

Jay Shah: Would it be safe to assume that the next lever of growth would primarily all be focused on India and not the rest of the geographies as much, comparatively?

Shailesh Chaturvedi: Right now, India is a very big opportunity. In times to come, we will take the brand even more strongly. But in the short run, our principal focus is to expand in India, and we see huge opportunities in small Tier towns, like I said earlier and we have a lot more to do to really exploit the large potential. It will take us many, many years to reach that potential. But we will be always open to other territory wherever we see opportunity.

Jay Shah: Thank you so much for all the answers and all the best for the future performance.

Moderator: Thank you. We take the next question from the line of Kunal Narsinghani from Alpha Invesco. Please go ahead.

Kunal Narsinghani: Thank you for giving me this opportunity. Sir, my first question is related to Arrow brand. I just wanted to know the progress in Arrow just using one of the matrices that, in FY20, there were 286 stores of Arrow and in 2022 it is down to 212. Approx. 74 stores have been closed, I assume, in the last 2 financial years. So what is management's strategy for Arrow forward? And could you just let us know the pre-and post IndAS EBITDA margin of Arrow specifically?

Shailesh Chaturvedi: See, Arrow has been a big focus for us in the last 2 years. COVID was not kind to many formal brands. And we had to really adapt the brand to the new realities of post-Covid world or work-from-home and we increased the proportion of it, smart casual line called Arrow Sport. We made the brand a little more ceremonial. We got a new logo on the brand, 'A' vector. We signed up with Hrithik Roshan as a big mega Bollywood celebrity to create demand for the brand. We created a new retail identity and which we have started opening doors. So Arrow has now turned around really well and is one of the fastest growing brand in our portfolio. In the first half, it has doubled the NSV. Second quarter is more than 50% growth in the Arrow business. Also, if I see the fall holiday, the current season, the improvement in sell-through in Arrow is significant, almost like 10%. It is like one of the highest in the industry. And because of this increase in sell-through because of lowering of discount linked to that, Arrow has now turned around. It has become EBITDA positive and it is a very good news. We are very excited about the brand where it is and with this energy that the brand has, we are getting now a lot of demand from the trade to open more stores of Arrow. And we're targeting that how fast we can open the next 100 stores for Arrow. It may take us probably 2 years. But we are very committed now to take the distribution footprint of Arrow forward with a position of strength, where we have done well on the current distribution. Our like-to-like growth in the business has been very, very healthy. Sell-through has been very healthy. Brand has become EBITDA positive and this is now the right time to accelerate and open many more stores. So maybe a year from when you asked this question, our store count would have gone up significantly higher. So we are very excited about what the short-term future holds for Arrow as a brand.

Kunal Narsinghani: Sir, my second question is for U.S. Polo. Sir, could you just tell me what is the sale of adjacent category as a percentage of overall U.S. Polo sale? Also, the management said once in their earlier con calls that stock turns and margins are better in footwear segment. Sir, if you could just give me the quantification of what is the stock turns in footwear segment?

Shailesh Chaturvedi: So let us start with the adjacent category. U.S. Polo, we have a lot of adjacent categories. Footwear is one adjacent category where we have invested ahead of the time. So we started with footwear business with a separate dedicated team. We set up an innerwear team, a separate dedicated team again. We have a very large kids' business in U.S. Polo. And now we're launching other accessories as we speak, things like belt and wallet and women line of footwear, etc. So adjacent category is close to, I would say, this season it will cross Rs. 300 Crores of NSV of adjacent category. It will be north of that actually. And we are hoping that, that number could touch Rs. 500 Crores NSV mark in next 2 to 3 years because there is a lot of energy going behind USPA and its adjacent category. Coming particularly to the footwear, if you look at our footwear portfolio, U.S. Polo is the largest part of that footwear portfolio. We have a good, healthy footwear business in Tommy Hilfiger also. And we are looking at designing some footwear line for some other brands as we speak. This year should touch close to Rs. 250 Crores of NSV. Bulk of it will be from U.S. Polo, which will be north of Rs. 200 Crores NSV mark. It is a fairly healthy double-digit EBITDA business. It has grown really well. In fact, the Q2 number is almost 2x the pre-Covid number. In quarter 2, growth is upward of 50%. It's a business which is doing really well, and it is a market-leading position. It has an online first approach. So on all the fashion portals if you look at Myntra or AJIO, it does very well. Last week, there was an event in Myntra for annual performance, and I am happy to share that U.S. Polo footwear won the best footwear brand in its segment. The turns on that business are quite healthy. So it's a profitable, fast-growing category, and we want to grow the footwear and other accessories, adjacent categories like the innerwear and small leather goods and kidswear strongly.

Kunal Narsinghani: Thank you. So it will be this really helpful if it is a good just give a ballpark number of what is the stock turns in the footwear segment, just any ballpark would be fine?

Shailesh Chaturvedi: See, as a company, we are at a 4.2 turns. And I can say that the footwear enjoys a slightly higher turn than that. It will be crossing 5 turns already. So it has a slightly higher stock turn than the company stock turns. I mean, does that answer your question? Or you want me to be a little more specific?

Kunal Narsinghani: It answers my question Sir. Thank you and all the best.

Moderator: Thank you. We take the next question from the line of Naysar Parikh from Native Capital. Please go ahead.

Naysar Parikh: Thank you for the opportunity. My first question is on the channel mix and how are the channels performing, especially the MBO channel where we had faced some problems in the past. So can you just give a sense of what is the mix by channel and the growth in them?

Shailesh Chaturvedi: Yes. So in Q2, obviously, you have seen kind of growth we have delivered. Across channels, there is energy and our brands have done well. So typically, if you look at our largest channel is retail, which is close to 40%. And based on the quarter and the seasonality, it can move from 37% to close to 45%. But around 40-odd percent at an annualized basis is the retail channel. The second largest channel is online. In the quarter 2, it was at the 26%. So this is a channel which has grown at 20% CAGR post-COVID. And we have like done around Rs. 100 Crores-plus monthly run rate in quarter 2 also. So this is around 25%, and it has grown at around 20-plus percent CAGR in the past. Then we have 2 other big channels: department store and the MBO, the trade channel. The trade channel tends to be at around 15-odd percent. Currently, in the quarter 2, it has gone higher because we do the primary filling for the season in September after the EOSS. So this quarter, the numbers are slightly higher than 15%, but that is where it is right now in terms of 15% and a similar number is expected from the department store channel. So that's the overall sort of mix we enjoy and we have a small export and institutional business. But this is how the overall channel has done across.

Naysar Parikh: Thank you. My second question is on the online channel. Do we have any plans to any kind of launch or acquire any kind of online first brands given that that is the focus area for many people? So is there any plan on those lines? Or the idea will be to just do our brands?

Shailesh Chaturvedi: Very, very focused on our existing brands and we have these 5 apparel brands, and Sephora, total of 6 brands. So we want to very single-mindedly stay focused on these businesses. And we see a huge opportunity for growth in the next many years in these brands to grow at 12% to 15%. We do not see any paucity of growth opportunity in our own existing brands. And make them bigger, more profitable, that is our focus. You have seen our last 1 year, we have demonstrated how sharply we have done our capital allocation and sharply defined our portfolio. So currently, we do not have any plan for any digital first brand, any acquisition or buildup. That is not on our cards. But in each of our businesses, we have a very large heavy online business and from wholesaling to the portals to our own NNNOW.com, to marketplace model, to omni linkage. We are very committed to online as a dominant channel and we want to grow that channel profitably aggressively. But we don't have any plan to do any other online for separate brand.

Naysar Parikh: Got it. And sir, if I can ask one last question, if we look at our minority interest, that has made Rs. 10 Crores of PAT, whereas we, as a whole company, has made Rs. 18 Crores. So we have made only Rs. 8 Crores, excluding Tommy Hilfiger and Calvin Klein, right, which is where the margin is, obviously, low. So how should we look at that? And when do we see obviously, it has improved, but as a margin, it's still low compared to TH and CK. So how should we think about that?

Ankit Arora: Ankit here. I think you are looking at the wrong numbers. The total PAT reported for the company consolidated is Rs. 28 Crores. Out of that, Rs. 18 Crores is excluding PVH, which is after the minority interest. So this quarter, we have had a landmark quarter, where we have meaningfully improved our PAT margins, if you really look at it and on an overall consolidated top line, despite me having top line of Rs. 1,182 Crores, I have done about close to 1.5% PAT margin for AFL after minority interest. So it is Rs. 28 Crores with Rs. 18 Crores coming from AFL after minority interest and Rs. 9 Crores or Rs.10 Crores coming in from PVH and as to what you would have seen, Naysar, I would just kind of really highlight the fact that our bottom line profitability has been on an absolute exponential upward trend over the last 4 to 8 quarters. Our first journey was to improve our PBT, which is what we did in H2 FY2022. And then since then, we have been improving our PAT profitability as well. That is the journey and our steadfast focus on improving bottom line profitability along with our EBITDA margins and as what Shailesh highlighted on growth of 12% to 15% CAGR moving forward.

Naysar Parikh: So, 10 Crores is for PVH and 18 Crores for the other?

Ankit Arora: Absolutely right.

Naysar Parikh: Thank you so much and all the best.

Moderator: Thank you. The next question is from the line of Yash Mandawewala from Mandawewala Family Office. Please go ahead.

Yash Mandawewala: Congratulations on a good set of numbers. I am just seeing a provision for slow-moving inventory of about Rs. 47 Crores in the cash flow statement. Can you just provide some more color on this?

Shailesh Chaturvedi: See, we have tightened our policy on inventory and one of the reasons why our gross margin went up is because we have kept our inventory very fresh and our gross margin does well when the inventory is fresh. So we've gone a little more conservatively and tight on our policy, and we've started keeping a little higher provision. It is a graded provision based on ageing, but we have created a little part of war chest pool going forward and that is what this value represents. It will help us to liquidate inventory fast and keep the inventory fresh so it will have a positive impact on our gross margins.

Yash Mandawewala: Perfect. The second question is, can you just provide some updates on how the festive season has been? Has it been a bit softer than your expectations, so October Diwali season?

Shailesh Chaturvedi: See, this season, that is the fall holiday season, is going as per our plan. We launched the season on time. We saw the festival season starts from Onam in Kerala, then to Pujo in East and some parts, and Diwali now and then heading into the winter season, wedding season and then Pongal in Jan. So the season there is buoyancy in the market and our brands are very, very strong. So the season is going as per our plan. Our sell-through are as per what we had planned. And we hope to end the season as per our plan.

Yash Mandawewala: Great. Thanks a lot Shailesh. That is it for me. Thank you so much.

Moderator: Thank you. We take the next question from the line of Rishikesh Ojha from Robo Capital. Please go ahead.

Rishikesh Ojha: Thank you for the opportunity. Only one questions from my side if you could provide some outlook on the debt, Sir?

Shailesh Chaturvedi: Yes. So if you really see our debt position, our net debt is at Rs. 383 Crores, which is slightly lower around Rs. 40-odd Crores. So we have always guided that our debt levels, despite the very large growth that we're doing, will be similar to what they were last year and we expect from now till the year-end, they will move sideways so similar levels as last year March'22 level.

Rishikesh Ojha: Thank you very much Sir.

Moderator: Thank you Sir. We take the next question from the line of Sagar Parekh from One Up Financial. Please go ahead.

Sagar Parekh: Thanks for the follow up. Just one, on the Sephora while you may not comment anything, but just wanted to get your sense that at what point will you eventually decide to exit the business as you have done in the past for all the others?

Shailesh Chaturvedi: You are forcing me to say something. We don't comment on such speculation please.

Sagar Parekh: No, but is there a thought for you to like probably look to sell eventually or look to exit this venture? Or there is no thought process at the moment?

Shailesh Chaturvedi: I do not want to comment on that. So just please pardon for that. See, Sephora is a business that we run 26 stores, and we have done really well. If you look at the quarter 2 numbers, like-for-like in Sephora is probably the best in the industry. We are delivering one of the highest sales densities in the mall. Ask any mall which is the best performing store in sales, Sephora will be right there. We have done a fairly good job when we took over the

Sephora from other distributors, and it has been a core part of our business and we will continue to sort of engage with women consumers in its premium offline driven appeal. And that's what Sephora's role in ours strategy. It is a beauty brand for our portfolio.

Sagar Parekh: Okay. Got it. And my last question would be on the Arrow. So you mentioned that you're looking at overall power brands reaching double-digit pre-IndAS EBITDA in 12 months. So on Arrow specifically, once the portfolio reaches that double digit, like Arrow would be on a lower side and probably U.S. Polo and Tommy would be on higher side for is that like a fair understanding? Or even Arrow can possibly reach about double digit?

Shailesh Chaturvedi: Arithmetically, you are right, because Arrow will also reach double-digit EBITDA. We are very committed. It will take maybe a year more or 1.5 years more to reach there, because it is just broken even while brands like U.S. Polo and Tommy are already double-digit pre-IndAS EBITDA. But we see acceleration at a higher pace in Arrow going forward and we are very committed to Arrow reaching double digit. But when the overall portfolio reaches 10%, maybe Arrow is a notch probably less. But it should also then soon reach double-digit EBITDA. Our ambition is on Arrow also is the same, to reach double digit.

Sagar Parekh: Right and Flying Machine?

Shailesh Chaturvedi: Similar. So see, Flying Machine is also at a scale where we will need to double the scale. It is now just a little south of probably Rs. 500-odd Crores and see, the journey of these brands will be interesting when we can grow them in next 3-odd years to Rs. 1,000 Crores with new categories in Flying Machine. We are focusing a lot on jeans and new categories being developed, including footwear, including innerwear, including kidswear in the next 1 to 2 years. It will take some time, but we have started thinking on adjacent category. We're also looking at some regions where it can grow faster. We can look at some channels where it can grow faster. So there is a lot of energy is going on to see how we can grow the brand from a slightly, right now, subscale in that sense to a scale where we can talk about a very, very healthy EBITDA.

Sagar Parekh: Right. So Flying Machine and Arrow will probably take some time to reach double digit, maybe 2 years out or maybe 2.5 years.

Shailesh Chaturvedi: You are right. And we are committed to that. But compared to Tommy Hilfiger and U.S. Polo, they may take a little longer time, a couple of more years.

Sagar Parekh: That is it from my side. Thanks.

Moderator: Thank you. We take the next question from the line of the Nishid Shah from Ambika Fincap Consultants. Please go ahead.

Dhruv Shah: This is Dhruv Shah. Congratulations on a good set of numbers. Sir, the question is pertaining to our U.S. Polo store, which we opened in Chennai, which was one of the largest stores which we have opened and if I am not wrong, this is because we are weak in South markets. So can you just tell us how has been the response and how we look the southern market going forward?

Shailesh Chaturvedi: Very good question and U.S. Polo is strong in South also now. U.S. Polo is an Rs. 1,000 Crores brand. It is strong across channels, across markets. Relatively, yes, I mean, you can say a little more deviation. But there are pockets: like Telangana extremely strong; Bangalore City, we opened 5 stores in the same week in Bangalore. We opened, like you said, in Express Avenue, which is probably one of the biggest, most important mall in South. So we opened a very large store and I am happy to share that U.S.

Polo now is the third biggest brand store in that mall, and that mall has all the brands. And so USPA has become like a top 3 revenue store in that mall and I am very happy with the progress there. If you go to the store, it looks quite nice. The standards of retailing are very, very high and from here, it will only grow faster and forward. So U.S. Polo now opened a lot of stores in Kerala, Telangana, Andhra Pradesh. Karnataka, we have opened 5 stores. In Tamil Nadu, Express Avenue store. So when we want to go even stronger in southern markets, I think U.S. Polo will be the first brand that will take us into that leadership or the strength position in South. So U.S. Polo is doing fairly well.

Dhruv Shah: When you say that we are trying to go into Tier 2, Tier 3, what kind of store size would that be?

Shailesh Chaturvedi: See, we are very clear that their store size will be similar to the current store size, maybe the smaller version of the current. We are not looking at necessarily a different format or a different, a smaller store, etc. Because what we have realized is that the well-to-do, affluent and even higher middle class consumers in the smaller towns, their aspirations are very similar to the big metros and otherwise, if the offer is different, then they end up going to the big metro to shop. So that is the learning in all our brands that we want the consumer to shop in their own hometown and not go to the nearest metro to shop. So our offer will be very, very competitive to an urban metro center in these towns also.

Dhruv Shah: Right. And do we intend to open more U.S. kids separate stores? Or you plan to merge everything in one and open one large store going forward?

Shailesh Chaturvedi: No. In fact, we are open to both the formats but I think a kids' separate store is a very interesting opportunity and some of other brands like Tommy Hilfiger, we opened very large number of kids' stores, the largest in the world, in fact, the number of stores that we have in Tommy in India and U.S. Polo also exploring that route and we have a multi approach, whatever works. But definitely, there is a scope of opportunity for kids' standalone store in U.S. Polo brand.

Dhruv Shah: Great and thank you for the opportunity.

Moderator: Thank you. We take the next question from the line of Shreyans J from Svan Investments. Please go ahead.

Shreyans J: Sir, I just wanted to understand how has been the response for women's wear in USPA?

Shailesh Chaturvedi: We had discontinued women's line in USPA for a couple of seasons, especially during the COVID. And then we are now restarting the efforts on U.S. Polo women's wear and it is on the drawing board, very early days of the effort and in a couple of seasons, you will see we relaunching the women's wear. So today, if you go to any of our stores, you will not see women's wear.

Shreyans J: Why I am asking you is because fundamentally women's wear, you need a lot of SKUs to stock, right? And you somewhere mentioned on the call where you plan to get into footwear for women as well. So what I am trying to understand is the need for higher SKUs and design, will that not actually lead to balance sheet again getting bloated and higher requirement for working capital going ahead?

Shailesh Chaturvedi: Yes. So we will do it very smartly. That is why we are very cautious right now. We are now prototyping our thought process. Footwear is a different opportunity, and online much easier to sell and we test launched the women's wear in last 1 month. Initial response is very good, but still early days for us to comment. Apparel will follow after that. So right now, I am not able to comment on what you're saying about the width options, etc. We are on the drawing board, and we will come back with hopefully a smart plan.

Shreyans J: Sir, a large part of the stores that we are opening would be company-owned, company-operated? Or are they franchisee stores?

Shailesh Chaturvedi: No, we have an asset-light franchisee model-led expansion plan. So you look at our capex, not too much of investment going. And most of our stores or a majority of our stores will be franchisee stores.

Shreyans J: We sell the inventory on an SOR basis? Or once sold, we don't take it back. How is that?

Shailesh Chaturvedi: We have many models. We have a consignment model also. We have outright model also and it changes from franchisee to franchisee, market to market.

Shreyans J: Sir, somewhere in the presentation, you spoke about a model where you want to like sell products which are not sold, at a discounted price. What is that model like? You plan to open stores for that?

Shailesh Chaturvedi: That’s outlet model, industry has very large outlets in physical stores, which are linked to omni and we did not have that. So a year back, we went ahead with that model. And now, we have these stores which sell our 5 brands, and dedicated to the 5 brands we have. Which city are you from?

Shreyans J: Mumbai.

Shailesh Chaturvedi: Bombay, okay. So we do not have a store in Bombay yet. But like, for example, Bengaluru, at the airport and at Marathahalli, we opened a large 3,500 sq ft. and these are pure outlet models. There is no other model there. It is not other brands. It is our own 5 dedicated brands and they are doing very well and it is an efficient way of liquidating old inventory in a controlled manner and this model is really working well for us. So we opened 20 of these outlet stores and by March, we should have close to 30 of these stores, which will help us liquidate old inventory at a faster pace in a very efficient way and good margin.

Shreyans J: That helps. Thank you so much.

Moderator: Thank you. Ladies and gentlemen that was the last question for the day I would now like to hand the conference over to Ankit Arora for closing comments.

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

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