"Lux Industries Limited Q2 FY2018 Earnings Conference Call"

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MANAGEMENT: **MR. SAKET TODI - PROMOTER & SENIOR VICE PRESIDENT - MARKETING - LUX INDUSTRIES LIMITED**
MR. AJAY PATODIA - CHIEF FINANCIAL OFFICER – LUX INDUSTRIES LIMITED
MR. JIGAR KAVAIYA – STRATEGIC GROWTH ADVISORS

Moderator: Good day ladies and gentlemen and a very welcome to the Lux Industries Limited Q2 FY2018 Earnings conference call. This conference call may contain certain forward-looking statements about the company, which are based on the beliefs, opinions and expectations of the company as on date of this call. These statements are not the future guarantees of performance and involve risks and uncertainties that are difficult to predict. As a reminder, all participant lines will be in the listen-only mode. 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 glad to hand the conference over to Mr. Saket Todi, Promoter & Senior Vice President - Marketing from Lux Industries Limited. Thank you and over to you Sir!

Saket Todi: Good afternoon and a very warm welcome to everyone. Along with me I have Mr. Ajay Patodia, CFO and SGA our Investor Relation Advisor. I hope you have received our result and investor presentation by now for those who have not you can view them on our website.

This is the first conference call with investors and analysts, so let me start with the brief introduction on our company Lux Industries Limited. Lux Industries is the number one drive in a way company in volumes having annual manufacturing capacity of 1825 lakh garment pieces manufactured at six facilities having over 5000 SKUs. We are currently selling over 100 different products across 12 brands. Our brands are Lux Venus, Lux Classic, Lux Karishma, Lux Touch, Lux Cozi, Lux Cozi Bigshot, Lux Cottswool, Lux Inferno, Lux Mozze, Lux CoziGlo and ONN. We currently have approximately 15% market share in the organized men's innerwear market.

We have a diverse product portfolio, which present across all categories, mass, medium and premium. On mass category that is the Lux Venus category provides us revenue of around 25% with EBITDA margin of 8%. Lux Venus is one of the largest vest brands in the economic category. Our medium category which is Lux Cozi provides revenue of 45% with EBITDA margin at a range of 13% to 17%. Our premium category of products includes ONN, which provides around 10% of the revenue with EBITDA margins of over 20%. We manufacture to maintain high quality standard. We are one of the lowest manufacturing cost companies in the business with higher capacity to achieve maximum economies of scale.

Critical processes are done in-house whereas we outsource processes such as stitching, which help us to be asset light and even our employee base is low. We currently have 900 distributors with over an average age of 35 years of relationship with them serving 4.5 lakhs retail outlets. We have 160 large format doors pan India, which enables us to showcase entire product range and portfolio under a single roof. This shows that Lux is available where is the customers are.

Our multipronged strategy includes providing quality products at low cost, increasing our premium in value added products and increasing our market penetration through increasing a share of wallet by offering wide range of products and also through focusing on tapping the underpenetrated markets in our country. All our expansions in the future are going to be technologically advanced. We have integrated units across knitting and cutting functions, which strengthened the efficiency, productivity and profitability.

Our new state of the art 12 lakh square feet manufacturing facility at Dankuni, West Bengal has a capacity to produce 5 lakh units of finished product a day. Our company is also creating an online presence in e-commerce website enhancing access and brand image. Our products are available on all leading websites like Amazon, Snapdeal, Myntra, Paytm, Flipkart and others also. Exports contribute to around 10% of a topline. We have increased the number of countries we export from 22% to 47% over the past five years. Currently our export turnover is around 102 Crores and plan to increase it going forward.

We have been consciously looking to invest a brand over the years. We have always had celebrity endorsement throughout the history. In 1992 we launched Yeh Andar Ki Baat Hai the first television advertisement in the industry to 2017 when we signed Varun Dhawan as a brand ambassador. We have recently tied up with Mr. Amitabh Bachchan also who will be a brand ambassador in the Lux Venus category.

The brand is skewed elements of faith and dependability and has a rich legacy of ruling the choices of the markets for more than three decades. Marking another first in the Hosiery segment for Lux Industries by signing Mr. Amitabh Bachchan as a brand Ambassador in the economic category. We believe the endorsements of Lux products will further strengthen the bond with masses, give our users a great sense of offers and help the brand scaling new heights over the course in the next few years.

Artimas Fashion Private Limited a wholly owned subsidiary of Lux Industries acquired manufacturing and marketing rights on the Indian Cricket Team Captain Virat Kohli's brand One8 known for its innovative and customer-demand driven product offerings. It is on a question that drives to disrupt the stereotype with pioneering initiatives in the organized innerwear category of the country. This agreement of Virat Kohli was signed very recently in the last month of November.

As a continuous strategic innovation, Artimas is collaborating with CSE consulting and LLP, the licensee owner of One8 to establish the brand as the most successful trendy innerwear brand for the youth in the premium category. These products under the brand One8 name will be created in collaboration with Lux Industries, who will provide the knowledge and expertise in manufacturing, designing, marketing and retail for the brand. Lux industries have also invested over Rs.277 Crores in branding over the last five years and will continue to invest 7% to 8% of our revenue in its further years. Now I hand over to our CFO, Mr. Ajay Patodia to provide you an insight of our financial performance for the year. Please Mr. Ajay Patodia.

Ajay Patodia: Thank you Saket Sir. I will take you all through the financials of the company.

Revenue grew by 8% to Rs.486 Crores in first half of FY2018 as compared to 448 Crores in first half of FY2017. We expect growth to be better in the second half of the year. For the full year we exact revenue to grow around approx 12% to 15%.

Our EBITDA grew by 13% to Rs.61 Crores in FY2018 as compared to Rs.54 Crores in first half of FY2017. Our EBITDA margin also improved around 12.5%.

Profit after tax grew by 9% to Rs.29 Crores in first half of FY2018 as compared to Rs.27 Crores in FY2017. Our PAT margins have also remained stable at around 6%. With this I open the floor for question and answer.

Moderator: Thank you very much. Ladies and gentlemen we will now begin the question and answer session. We will take the first question from the line of Uma Choudhary, Individual Investor. Please go ahead.

Uma Choudhary: May I know what is the reason of decline in the results from Q1 to Q2 where your competitors like Rupa, Dollar and Page Industries have shown a very good result?

Ajay Patodia: This is generally due to the impact of GST in the second quarter. **Uma Choudhary:** GST was the same for all the other competitors also.

Saket Todi: If you see the half year results for all the companies, all our peer companies have degrown and we are the one company that has grown. GST was hit in the month of June, so we have gained most of the sales in the Q1 of our current financial year. If you see that our Q1 growth was around 45% topline whereas all our peer competitors degrew by 20% or 5% and we grew by 45% for the Q1 of this financial year. So if you see the overall first six months first H1 of the current financial year in comparison to all our peers we are the only company, which has grown, all the companies either have remained either the same or they have degrown.

Uma Choudhary: My another question is where do you see yourself in the next two to three years?

Saket Todi: See as GST had come in and our main season starts from the month of January, February, March so it will be easier and will be more advisable to answer after the fourth quarter of this year, where we come to know how impactful GST has been in our current market because our market is mainly dominated by the unorganized segments. So we believe that the unorganized segments would definitely go down and the organized will go up, but actual scenario will come to know after the fourth quarter of this financial year that where we are standing, where the unorganized segment is standing, how they are degrowing and how the organized segments are growing.

Uma Choudhary: So far there has not been any shift from unorganized to organized market right?

Saket Todi: No the season starts from January, February, March so right now it is not the right time to test how the shift has been. The retailer and the distributor starts buying from the month of February, March, April, May and after that GST has come in. They stock the products in those four months for the next four to five months. So currently the retailers are selling like those unorganized unbranded products, which they procured four to five months back.

Uma Choudhary: What is your sale product mix like premium product how much of your premium product constitute to propel sales and normal product?

Saket Todi: Premium range is approximately 10%, export is approximately 10%, our mass segment product which is Lux Venus is approximately 25%, Lux Cozi, which is mid segment, is approximately 45% and approximately 10% is the winter wear.

Moderator: We have the next question from the line of Abhishek Jaiswal from Ratnabali Capital. Please go ahead.

Abhishek Jaiswal: My question is again related to the previous one only, you cannot give the entire impact of GST as of now and only after the fourth quarter you will be able to provide a better sense of that, but however can you provide some light that what could be the growth way or trajectory that you might be going on to like we are facing a lot of competition from the fragmented market like the unorganized sector, so my question is that where do you stand now, what is your market share and where do you see this going after GST has kicked in?

Saket Todi: See our market share is approximately 15% of the total organized segment, so we do not know how much the unorganized segment will grow, but what we estimate the industry growth will be approximately 8% to 10% whereas we will move from 12% to 15%. The industry growth can be more than that and we can be more than that, that can be ascertained after the fourth quarter, but right now the estimations goes up to this.

Abhishek Jaiswal: And are there any wild guess sir that how large is this unorganized market?

Saket Todi: Unorganized market would be approximately 50% - 55% of the total segment.

Abhishek Jaiswal: And what could be the price difference is it like the branding size or there is something else that we need to calculate it like what would be the price point of an organized market share and unorganized market share

Saket Todi: Approximately 10% was a difference before GST.

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

Nishant Agarwal: My question is on the volume side that when you are saying that you are the largest in volume term is it possible to provide your last two quarters' volume?

Ajay Patodia: Last two quarters' volume we don't have it right now, it will take us some time.

Nishant Agarwal: But is it possible to provide the volume growth when your half year revenue has gone 9% so how much is from the volume and how much is from the realization that?

Ajay Patodia: The volume growth is around 4% to 5% remaining is the value growth.

Nishant Agarwal: Second question is that our EBITDA margin was stable at 12.7% on a Y-o-Y basis while your gross margin has improved significantly, so is there any reason that despite a huge improvement in the gross margins your EBITDA margin has remained stable?

Ajay Patodia: The main reason is for our GP ratio going up is due to optimization of cost. We optimize the cost, we lower the cost value at our cutting stage due to which the gross margin is higher from the last quarter.

Nishant Agarwal: So it means your fixed cost has increased and it would continue right?

Ajay Patodia: Regarding?

Nishant Agarwal: For the EBITDA margin purposes means your EBITDA margin would remain at the range bound of 12%, 13% or it would improve?

Ajay Patodia: We try to improve but once we close our fourth quarter then we can say that. We will try to improve this.

Nishant Agarwal: Because if your in-house consumption is improving I think that your margin should improve going forward?

Ajay Patodia: That is right.

Nishant Agarwal: My third question is about your fabric and yarn requirement how much is your yarn requirement in-house and how much is the total yarn requirement for the full year?

Ajay Patodia: We purchase the whole yarn. There is no in-house production of yarn. Our raw material starts form yarn. We purchase the yarn, which is approximately 50,000 kilos every day.

Nishant Agarwal: Sir, I want to understand that of the total fabric requirement, how much fabric is required in-house?

Ajay Patodia: This 50,000 kilos of yarn which we purchase, we net it 100% in-house.

Ajay Patodia: So, it is converting yarn to fabric kilos. In Hosiery, fabric is not in terms of meters, it is always in terms of kilos, so those 50000 kilos of yarn is converted in to 50000 kilos of fabrics.

Nishant Agarwal: So you want to say that 100% of your fabric is in-house you do not procure fabric from outside?

Ajay Patodia: No we do not.

Nishant Agarwal: Thanks very much.

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

Kunal Bhatia: Sir just I missed out on the numbers you are mentioning about your Lux Venus, Lux Cozi and brand wise if you could give the revenue in terms of percentage?

Saket Todi: Lux Venus is 25%, Lux Cozi is 45%, ONN is 10%, export is 10% and winter segment, which consist of Cottswool and Inferno are 10%.

Kunal Bhatia: Sir and your Lux Venus is your mass brand then Cozi is the mid segment brand. Sir just wanted to know how they are different in terms of the production cost.

Saket Todi: We can get an idea of the production cost through EBITDA margin, the EBITDA margins in Venus category is approximately 8% and the EBITDA margin the Lux Cozi category 13% to 17%.

Kunal Bhatia: Sir but is it that the manufacturing or the raw material cost is very different or it is more to do with the trade or the dealer margin in that case?

Saket Todi: It is more to do with the trader and the dealer margin, the percentage would remain approximately the same.

Kunal Bhatia: Sir so if you could just give some more sense on how different is the trade margins in this case.

Saket Todi: We want to give you the defined trade margin but in Lux Venus it is more because if you see the MRP, the MRP here also is low, the average MRP for Lux Venus category is approximately Rs.35 to Rs.40 and the average MRP in the Lux Cozi category is about Rs.60 to Rs.65.

Kunal Bhatia: And Sir how would be the average price for ONN and the winter earnings.

Saket Todi: ONN is approximately Rs.100 and Rs.105 and winter is approximately Rs.160, Rs.170.

Kunal Bhatia: And Sir I was just looking at your EBITDA margin remaining Y-o-Y we have done around the same percentage or have grown by 50 basis points and I understand that the raw material to sales has come down from a 43 to 29.7 but at the same time our other expenses has gone up significantly so if you could explain the math's because net-net we are again on a 12.5% kind of margins. So where going forward one could expect the improvement in margins coming from? What has led to the rise in other expenses which is at 23% for H1FY18 vis-à-vis the 17% last year H1FY17

Saket Todi: The other expenses include the Administration part, the selling part and the advertisement portion. During the first half, the sum spent on advertisement has increased i.e. from Rs 76 crs in H1 FY17 to Rs. 111crs in H1 FY18. However, it is balanced in the current quarter. So when you see the result for the full year it is on the sales.

Kunal Bhatia: So we should see some drastic improvement in the other expenses in H2.

Saket Todi: Yes.

Kunal Bhatia: In that case the 12.5% kind of EBITDA margins would be one of the highest in the last five, six-year period.

Saket Todi: Yes, this has been growing at year-on-year.

Kunal Bhatia: So what kind of improvement do we foresee going forward? I am not asking you for a very specific number, but looking at the way the other expenses for last year and looking at the way there has been improvement from the gross margin front and even jobbing expenses front, do we expect a 200 to 300 basis point improvement going forward.

Saket Todi: No, right now we do not expect that. So the main cost control would be towards the cutting part where we will lessen our consumption which is the raw material cost where that is the main part where we will control the employee expenses. Jobbing expenses and other expenses would remain the same, we are not expecting much growth in that segment but in the raw material cost we are expecting to at least increase by 100 to 150 basis points over the next two years.

Kunal Bhatia: Sir and what would be the reason for that?

Saket Todi: Because we are doing the cutting in-house and we have fully automated cutting machines, so what has happened because of that is our cutting efficiency has improved, the main cost among the total cost is raw material cost and there we are doing the maximum saving.

Kunal Bhatia: Sir and in terms of capex what would be your capex requirement in the coming year or how much have you spend because I just have your depreciation cost – depreciation going up by 48% Y-o-Y so what has led to that how much have you done in capex?

Saket Todi: The depreciation is because of the new plant at Dankuni and we do not have any capex requirement for the next three to five years at least.

Kunal Bhatia: The new plant is fully utilized currently.

Saket Todi: No. We have utilized it around 80% till now still more spaces are left to utilize this optimally.

Kunal Bhatia: Sir so currently how much your in-house manufacturing and outsourcing vis-à-vis and going forward how would this pie change.

Saket Todi: In manufacturing there are five processes which is involved, we purchase the yarn which is the raw material so yarn is fully outsourced as the raw material. Then we knit the fabric, the fabric knitting process is fully in-house. Then after that is processing where the raw fabric is converted into processed fabric white color bleached so that is completely again outsourced. Then is the cutting after we receive the finished fabric we cut it into pieces where we control the costing where I just said we have improved that is now completely in-house. Then is the stitching, stitching is 90% outsourced and then is the packing and dispatch which is in-house. So if you would see in a particular product, there are processes, which is in-house and there are processes, which is outsourced. So no particular product is completely in-house or completely outsourced.

Kunal Bhatia: Got it fine sir and finally I had one question on sir you mentioned something about the fill rate which we stand at 95% versus the industry at 80% so could you explain a bit on that.

Saket Todi: Supply rate is 95%, our fill rate is 95% because we are very certain on what we manufacture will get sold in the market. So our efficiency in forecasting the figures is highly efficient. It is too early right now to speak on this. Again I would like to see the same in the month of May after our annual results. I would like to speak to you about it then. I can explain this to you further. Please remember this question when will have an investor concall then we will discuss about this question again.

Kunal Bhatia: Okay Sir no problem thank you so much.

Moderator: Thank you. We will take the next question from the line of Mehul Mehta from Sharekhan Limited. Please go ahead.

Mehul Mehta: This is with regards to your guidance for 15% revenue growth for full year FY2018.

Saket Todi: Yes approximately 12 to 15%.

Mehul Mehta: So first half we have grown at about 9% in terms of revenue so second half if I look at, it gives us like 15% would give us like an 20% kind of run rate so what gives us this sort of confidence.

Saket Todi: There are few things, which I have to add to it. Firstly in the first half we are comparing the last six months to the current five months. Because here we have lost one month of sales which is approximately 20, 25 days of sale in the month of June we have lost that.

Saket Todi: Because of the GST, we have lost that month of sales so it is like comparing last. If we compare apple-to-apple, it is like comparing last six months of sales to current five months of sales.

Mehul Mehta: No so that is fine like and if you take this is still run rate is on the higher side so is there anything which you are feeling because of shift from unorganized to organized because of GST or what is giving you that confidence?

Saket Todi: When you see the Q4, the Q4 sales has been the highest quarter sales in our company, in our industry if you see any company the Q4 because that is the starting of the season.

Mehul Mehta: Same would have been the base sir like if you look at e last year Q4 would be like that way higher only, so we are talking about the growth on that base.

Saket Todi: So that you would see approximately 18% to 19% it is mainly because of GST.

Mehul Mehta: So are you seeing that kind of traction during this quarter we are already in December so are we seeing like in that kind of upside?

Saket Todi: Yes there is a sense of acceptance of more mass products or more mid segment products because of GST, there is acceptance in the market of organized segment products. That is why we have endorsed Mr. Amitabh Bachchan in the Lux Venus category. If you would see in that category, there is no celebratity or brand event in our whole industry. That is the reason Mr. Amitabh Bachchan has endorsed the brand. When we launch it in the month of January, we will see the result of it that the people will be choosing the branded product and even in the branded segment you will see the first for brand of celebrity which is endorsing a product so people would like to go for that brand. So we are expecting a huge growth in that segment as well.

Mehul Mehta: Sure one more question is there is one press release dated in February 2017 which talks about Lyra brand in women’s category being part of the group, so is it not part of listed entity.

Saket Todi: No it is not part of the listed entity.

Mehul Mehta: So are there any plans to merge everything under one roof.

Saket Todi: No, we cannot say anything right now, we are just discussing about Lux Industries right now.

Mehul Mehta: So Lux industries consist of what in the sense it is only men’s innerwear?

Saket Todi: Lux Venus, Lux Cozi, Winter segment, ONN, premium segment and export.

Mehul Mehta: Thank you so much.

Moderator: Thank you. We will take the next question from the line of Saurabh Ginodia from Stewart & Mackertich. Please go ahead.

Saurabh Ginodia: I missed your opening commentary with respect to the capacity per day and what would be your average capacity utilization across those facilities.

Saket Todi: Last year we have a manufacturing capacity of 1825 lakh garment pieces annually and we are utilizing approximately 75% to 80% of the total capacity, it is according to the current product mix.

Saurabh Ginodia: After taking Dankuni into consideration?

Saket Todi: Yes.

Saurabh Ginodia: And Sir your premium product would account for roughly 10% of your overall sales mix where do you see premium category shaping forward for the next couple of years.

Saket Todi: See the premium category is growing around 25% as the base is very small for us. It might be that in future when it reaches a turnover of 500 Crores might be 15% and then the growth might be 10% to 15%, but right now it is growing around 25% for us.

Saurabh Ginodia: And do you have the figure for average selling price per unit for the current quarter or for the half year.

Saket Todi: It is approximately Rs.55 to Rs.60.

Saurabh Ginodia: Thank you Sir all the best.

Moderator: Thank you. The next question is from the line of Brij Shah from Brij Shah & Associates. Please go ahead.

Brij Shah: Sir I have few questions. Sir first one is that in the last six months we have signed Amitabh Bachchan and Virat Kohli so Sir can you provide some insights for this signing regarding the cost incurred and as well as has our branding cost drastically increased after the signing.

Saket Todi: No, we cannot provide any figures that is our agreement between them. Secondly we have signed only Mr. Amitabh Bachchan. We have not signed Mr. Virat Kohli. With Virat Kohli we have a license agreement so there is no signing involved into. It is a different agreement all together.

Brij Shah: Okay and in relation to export what is our current turnover and margins in export and what sort of opportunity we see in future?

Saket Todi: Current turnover in exports is approximately 10% which is 102 Crores and our EBTIDA margins are around 18% to 20% for exports.

Brij Shah: And Sir in next two years what we see to increase our turnover as well as the increase in margin in relation to exports?

Saket Todi: We are there mainly in Africa, Middle East, Australia. We are trying to expand to other countries as well because the whole of Europe, America, and South America So we had tied-up with a few European companies and we are planning to start selling in Europe in the coming few quarters.

Brij Shah: And Sir what is the current capacity utilization at Dankuni plant?

Saket Todi: It is approximately 75% to 80%.

Brij Shah: And Sir the last question Sir what would be our sustainable margins going ahead and will we see any improvement in them in next two, three years.

Saket Todi: Yes, as I said that we have installed automated cutting machines where we will control the costing so our margins are going to improve in the next few years by 100 to 150 basis points.

Brij Shah: Okay. Thank you Sir.

Moderator: Thank you. We have the next question from the line of Niya Malhotra, Individual Investor. Please go ahead.

Niya Malhotra: I wanted to ask you what are you plans for reducing your debt going ahead.

Saket Todi: We have only working capital loans with us.

Niya Malhotra: Okay. Can you tell me about your capex plan in the next two to three years?

Saket Todi: We do not have any plan for any capex of next two to three years. We have the Dankuni unit which we have just commissioned it last year so our first aim is to utilize it optimally and we can change the product mix at same unit to increase the revenue as well. For the next two to three years, four years there are no plans.

Niya Malhotra: Okay. Thank you Sir.

Moderator: Thank you. We have the next question from the line of Swati Gupta from Julius Baer. Please go ahead.

Swati Gupta: Just wanted to know when we are looking at entering the European market, are you also looking at being a supplier for getting ahead with the brand from Lux itself.

Saket Todi: We are looking in both the terms as well as being a supplier that is supplying in their own brand as well as supplying in the brand of Lux.

Swati Gupta: Thanks Sir all the best.

Saket Todi: Thank you everyone, I take this opportunity to thank everyone for joining on the call, I hope we have been able to address to all your queries. For further information kindly get in touch with us or SGA, our investor relation advisor. Thank you once again.

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