



SKNL's Q2 & H1 FY2011 Results Conference Call Investor/Analyst Conference Call Transcript November 04, 2010

Moderator Ladies and gentlemen, good day and welcome to the SKNL Quarterly Results Conference Call. As a reminder for the duration of this conference, all participant lines will be in the listen-only mode. There will be an opportunity for you to ask questions at the end of today's presentation. Should you need assistance during the conference call, please signal an operator by pressing * and then 0 on your touchtone telephone. Please note that this conference is being recorded. At this time, I would like to hand the conference over to Mr. Salil Bawa from SKNL. Thank you and over to you sir.

Salil Bawa Thank you Melissa. Good morning and welcome to SKNL's Q2 & H1 FY2011 analyst and investor conference call. Today on this call, we are joined by Mr. Anil Channa, CEO and Deputy Managing Director and Mr. Anees Fazalbhoj who is the Group Director, SKNL. We also have with us Mr. Dara Avari who is Director Corporate Affairs, and Mr. Jagadeesh Shetty, CFO. Here, I would like to point out that we had fixed the conference call for discussing the Q1 FY2011 results, but we were not able to do it at the last minute as our lawyers, who were helping us on QIP, suggested that we should not be doing it at that point of time because of the QIP.

Before we begin, I would like to point out that certain statements made during this conference call maybe forward looking and may involve certain risks and uncertainties. A disclaimer to this effect was included in the conference call invite as well as the investor release sent out earlier.

I would now like to invite Mr. Anil Channa to give you an insight on SKNL's performance for the quarter and half year ended 30 September 2010. Over to you sir.

Anil Channa Good morning friends, I wish all of you a very happy Diwali. I welcome you to SKNL's Q2 & H1 FY2011 results conference call. I will begin the call by sharing my views on the business activity and operational performance during the quarter and half year under review. After which, our CFO Mr. Jagadeesh Shetty will run you through the financial performance followed by the Q&A session.

I am happy to announce that our Q2 & H1 performance has been very promising with the total income increasing by 27% to Rs. 12,114 million and net profit after minority interest improving by 9% to Rs. 639 million during the quarter. The strong performance witnessed during the quarter is an outcome of well-defined growth strategies for each of our SBUs, which is sustained by a robust operating model for efficient execution of plans. A clear focus on creating a diversified brand portfolio catering to all the socioeconomic strata and expanding our global footprint, with strategic acquisition of international brands has started to yield results for the company. Enhanced contributions from Consumer Textiles, Luxury Textiles, Total

Wardrobe Solutions, and Luxury Cotton divisions remained key to the healthy performance delivered during the quarter. With a marketing network that is well spread across the globe and operations in six countries, SKNL is one of India's only multinational conglomerates in the branded apparel segment. A strong brand portfolio of 45 brands which includes international names like Hart Schaffner Marx, Hickey Freeman, Exclusively Misook, Austin Reed, Jag Jeans, Bobby Jones, and DKNY - our latest addition to name a few, further leverages our leadership position as a branded player in the apparel business.

The Total Wardrobe Solutions segment witnessed a marked growth of around 47% driven mainly by higher sales across product offerings. Similarly, Belmonte in the Consumer Textiles division that caters to the economy and mid-price strata of the society continues to remain the key growth driver of this segment while Luxury Textiles division delivered a healthy growth owing to robust performance reported by our Reid & Taylor brand.

As you may be aware, we launched 'World Player' in Q1 FY2011 in some parts of South India and I am happy to share that we are highly encouraged by the response. Subsequently, we launched it in North, Southern, and Eastern parts of India during the second quarter. Following this, we plan to launch 'World Player' across India in the next financial year. Going forward, we are confident that this brand will capture the full potential of the economy segment at which it is aimed.

Continuing with our strategy to extend our presence across demographic segments in the near future, we also intend to launch 'Kruger', a brand in the casual premium segment.

Coming to our operations at the Baruche Superfine Cotton facility at Jhagadia, Gujarat that has a capacity of 12.75 million meters per annum - the operations have stabilized and it has reported substantial growth during the quarter. We expect this facility to reach its full potential in the coming months. This will provide further impetus to our revenues and profitability.

During the quarter, the Total Home Expressions division witnessed a growth of nearly 5%, which has been a bit of a laggard, which is consistent with probably what is happening in this product category. However, we expect the performance to improve as the home textiles unit becomes functional at Baruche in the next couple of months.

During the period under review, as you are all aware, we raised Rs. 2,316 million by issuing fresh shares to Qualified Institutional Buyers at a price of Rs. 80 per share. We did this issue with the primary objective to facilitate our growth plans and enhance our capacities in India and this we expect will enable us to further consolidate our leadership position. Here, I would like to point out that we were not able to discuss our Q1 results over a conference call with you as we were under the silent period regulation owing to the QIP issue at that time.

Keeping in line with the rate at which we are growing, we are confident that the future looks equally promising with the domestic as well as international business segments strategically poised for enhanced performance. Presence across the value chain from procurement of fiber to finishing and sale, a back-end front-end synergy model, well-diversified and strong brand portfolio catering to diverse customer segments across the globe, expansive marketing and distribution network and state-of-the-art manufacturing provide us with a solid foundation to continue delivering sustainable growth going forward.

Our financial performance truly reflected the operating performance for the quarter and half year ended 30 September 2010 with an improvement in profitability and enhancement of operating margins. All financial ratios are at healthy levels and we

are looking to grow above our benchmark level. Further details, in this regard, will be shared with you by Mr. Jagadeesh Shetty, our CFO. He will now take us through the company's financials. Thank you.

Jagadeesh Shetty

Thank you Mr. Channa. Good morning everyone. A strong operating performance reported during the quarter converted into equally strong financial performance reported for the period under the review. I am pleased to inform you that SKNL's total income from operations for the quarter has reported a healthy growth and has enhanced by 27% to Rs. 12,114 million from Rs. 9,545 million during the corresponding quarter of the previous year. This was primarily on account of strong volume enhancement across all brands and SBUs witnessed during the quarter. Kindly note that the results under review are consolidated with Reid & Taylor, Leggiuno, SKNL UK, and HMX Corporation - our subsidiaries.

During the quarter, EBIDTA increased to Rs. 2,421 million from Rs. 1,833 million marking a growth of 32%. EBITDA margins reported a marginal improvement from 19% to 20% over the corresponding quarter. This was mainly due to the enhanced margin reported by the Consumer Textiles division, Luxury Textiles segment, and robust 47% growth in the revenue from Ready-to-wear Garment division in the domestic market.

Overseas EBITDA margins too have marginally improved from 2.65% of the corresponding last year's quarter to 3.56% during the year. Increase in the total expenditure is in line with the expanded scale of operations. Depreciation for the Q2 FY2011 increased by 71% to Rs. 282 million primarily on account of the commencement of the high value fine cotton plant in Gujarat along with the consolidation of overseas businesses.

Interest for Q2 stood at Rs. 937 million, up from Rs. 589 million for the Q2, 2010, owing to the increase in the working capital requirements in preparations for the incoming peak season.

Production levels in all the divisions particularly in the wake of winter season in Reid & Taylor and the upcoming festive season has been higher requiring a higher utilization of working capital requirement in all the divisions.

In Q2 FY2011, profit after tax before minority interest stood at Rs. 779 million as compared to Rs. 693 million in Q2 of 2010 indicating a healthy earnings performance.

Net profit after minority interest for the quarter under review stood at Rs. 639 million compared to Rs. 584 million.

Earnings from the domestic businesses have continued to grow at a robust pace. Going forward, the overseas ventures are expected to report significant growth in revenues and profitability as volumes and cost efficiencies improve.

I would like to briefly take you through H1 2011 financial performance; total income during the period increased by 44% to Rs. 24,026 million from Rs. 16,654 million. EBITDA improved by 36% to Rs. 4,676 million from Rs. 3,452 million. Profit after tax and after minority interest enhanced by 16% to Rs. 1,266 million from Rs. 1,096 million during the last year.

As on 30 September 2010, the Net worth of SKNL on a consolidated basis was Rs. 27,384 million and the total consolidated debt including the debt of working capital facility and independent debts on subsidiary companies was Rs. 30,805 million. This result in a total debt to net worth ratio of 1:12, which I would think, is a comfortable leverage for SKNL. As compared to the position as on 31 March 2010, there is a marginal improvement.

In terms of current asset level as on 30 September 2010, the inventory was at 3.6 months as compared to 3.5 months at the end of the last year that is on 31 March 2010. The sundry debtors were at 4.6 months as compared to 4.5 months as on 31 March 2010. The marginal increase of 0.2 months is on account of the higher production level during the last quarter in the wake of a busy and strong winter season for worsted fabrics. So the levels in my sense are comparable and if one accounts for the huge increase that is taking place, they are effectively lower. This is all from the finance side. We may now move into the question and answer session. Thank you very much.

- Moderator** Thank you. Ladies and gentlemen we will now begin with the question and answer session. Anyone who wishes to ask a question may press * and 1 on their touchtone telephone. The first question is from the line of Nirav Shah from Antique Stock Broking. Please go ahead.
- Nirav Shah** Good morning sir, can you provide us the breakup of revenues and EBIDTA for our overseas operations for HMX, Leggiuno, and DKNY - for both the quarters, Q2 FY11 as well as Q2 FY10?
- Jagadeesh Shetty** For Leggiuno, for this quarter ended September 2010 is Rs. 35.3 crore as compared to Rs.34.4 crore during the previous quarter of the last year. HMX USA revenues are Rs. 233.7 crore as compared with Rs. 195 crore during the last year. SKNL UK is Rs. 18.74 crore as compared to Rs. 15 crore during the last year.
- Nirav Shah** Okay sir, was SKNL UK there in Q2FY10? Because what I understand is that it started only from the December 2009 quarter onwards when we started the JV with DKNY?
- Jagadeesh Shetty** That is true, but there was an initial sale which was recorded during that quarter. So actually, this Rs. 18 crore in that sense is not comparable. But, that was recorded during that quarter. So the total sale is Rs. 287.7 crore as compared to Rs. 245 crore of the previous year, which represents 17% of growth.
- Nirav Shah** In terms of EBIDTA performance, can you provide figures for the same?
- Jagadeesh Shetty** The operations have been in stream and they are all positively contributing to the EBIDTA except SKNL UK. The DKNY business is a new venture, which would require some time to stabilize and go to a volume that we are expecting out of it. Otherwise, we are happy that despite the fact that in HMX, this is a vacation period in US as everybody would know and in spite of that we have recorded sale of Rs. 233.7 crore and an EBIDTA of Rs. 9 crore and 21 lakh.
- Nirav Shah** So EBIDTA for HMX in the second quarter FY11 is Rs. 9.21 crore?
- Jagadeesh Shetty** Yes.
- Nirav Shah** Can you just share the figures for Q2 FY10 as well?
- Jagadeesh Shetty** Q2 revenue is Rs. 195 crore and EBIDTA was Rs. 8 crore.
- Nirav Shah** What is the EBIDTA for Leggiuno and DKNY?
- Jagadeesh Shetty** EBIDTA for Leggiuno for the quarter is Rs. 1.49 crore positive as compared to Rs. 2.03 crore negative for the last year's quarter.
- Nirav Shah** and DKNY?

- Jagadeesh Shetty** DKNY - it is negative Rs. 0.47 crore that is 47 lakhs as compared to negative Rs. 0.2 crore during the previous year.
- Nirav Shah** I am just looking at Hartmarx's numbers. Our Hartmarx consolidation happened from August 2010 and in those 12.5 months of operation, you have done around Rs. 195 crore of revenues. Any particular reason why the absolute figure for HMX revenue appears to be slightly on the lower side, if we compare the duration, at which it was operating last quarter?
- Anil Channa** Essentially, when we took over the company in August 09, there was lot of inventory that was lying with the Company which we went into a liquidation mode. Therefore, that was not the path on which we wanted to go, but that was necessary so that complete inventory got disposed off at a suitable time, the earlier the better. Now, once Doug and Joseph Abboud are onboard entire team has been restructured. The entire product offering has been redesigned. So, we are now focusing on the top 10 brands. Lot of brands that were not making commercial sense at that stage we have actually parked them for the time being. So we decided to take a small hit on the sale rather than take a hit of the EBIDTA. That has been a strategy there. But then in July 2010, the company has come out with a brand new collection which has been well appreciated by the trade. The results will start coming in from next year because as you typically know, these industries move one year in advance in terms of booking as it is a fashion industry and not a commodity business. Incidentally, just to supplement what Jagadeesh is saying, even in Leggiuno, the Italian companies are always closed for almost around 3 weeks during August. So that also impact the actual sales and actual dispatches this quarter. But Leggiuno, if you can see that it has already turned from a negative situation last year to a positive situation and has gone up to Rs. 1.49 crore during this quarter. So that has been very positive and overall our EBITDA has moved from Rs. 6.5 crore in the Q2 of last year to Rs. 10.23 crore in Q2 of this year. As we stated earlier also, the process of consolidation, the process of reinventing the wheel, process of rearranging the product line all those actions are in place. These two things are just gearing up for the coming season and we see very positive results coming up from the overseas at that position.
- Nirav Shah** Fair enough sir. Sir, December quarter will be the peak for our HMX operations. So this quarter you have done somewhere around Rs. 234 crore of revenues, if you compare it with likely December figure, could we be clocking around Rs. 120 crore a month, somewhere around Rs. 350 crore for that particular quarter. Will that be the kind of increase we will be seeing, on a seasonal basis - for September to December quarter?
- Anil Channa** Not that December quarter will be the peak. Actually, it could be the January-March quarter that is the peak. December again, lot of sales would happen and thanks giving would be coming up by end of November and then Christmas sale will also happen. So lot of fresh goods will start moving out only by end of December that expand into January. So actually, the peak sale is split into two different quarters.
- Nirav Shah** But can you expect a run rate of at least around Rs. 100 crore per month for HMX?
- Jagadeesh Shetty** Yes I would think so.
- Nirav Shah** Fair enough and on the interest cost front, our interest cost is somewhere around Rs. 94 crore in the September quarter against Rs. 73 crore in the June quarter. So can you just provide the breakup between our standalone operations. I believe that primarily this will be because of HMX, the difference between the standalone and consolidated. So can you please provide the breakup of interest cost?
- Jagadeesh Shetty** We have already published the standalone results. The interest cost in the standalone of SKNL is Rs. 75 crore and the consolidated is Rs. 93 crore. The

difference between Rs. 93 crore and Rs. 75 crore on account of consolidation of the overseas business.

- Nirav Shah** But could the incremental interest be attributed to HMX because Reid & Taylor is not a very high debt Company. In fact, that company has given loan to the parent. So I believe that it should be because of HMX. Is my thought process correct?
- Jagadeesh Shetty** It is mainly because of what happens during the September quarter. See, September quarter is mainly a high production based quarter. There is a festive season coming, Diwali season. So all the divisions will gear up their production and particularly in Reid & Taylor division, in anticipation of the winter sale booking, the production level during this quarter is very peaked. Hence, all the divisions would use up their working capital limits fully. You must have known that we have placed the QIP towards the end of September. Since the QIP funds came into the company, the divisions' use the working capital limits to the full and hence you have found a spurt in the interest level.
- Nirav Shah** Fair enough sir. Thank you.
- Moderator** Thank you. The next question is from the line of Abneesh Roy from Edelweiss. Please go ahead.
- Abneesh Roy** Congratulations on a good set of numbers. My first question is on 'Kruger', if you can tell us what is the timeline that you are looking at and how big is the opportunity in the first year?
- Anil Channa** Essentially, the prototype of the product has already been made. We have an Italian designer onboard and teams are in place, the design team, the merchandizing team is already in place. So as we said, we intend launching it by the Q4 of this year.
- Abneesh Roy** Will this be again in some particular market?
- Anil Channa** It is aimed at the casual premium segment where we find that there is a gap right now. While in Reid & Taylor also, we do some casual apparel, but then the proportion is more focused on the formal apparel, whereas this would be focused only on the casual premium apparel.
- Abneesh Roy** My question was more from a geographical entry point of view. Will you launch it at all India level or will it be more in the South?
- Anil Channa** This would essentially be going through the EBO format, that is, we will be setting up 30 stores over the next one year. It will also be going into the large format stores. So that is where the primary focus is going to be.
- Abneesh Roy** So would you want to do an all India launch in Q4?
- Anil Channa** It will always be an all India launch, otherwise if we do not do an all India launch, then the width and the depth of the merchandize will not be able to justify the existence of our top-notch brands.
- Abneesh Roy** 'World Player' was done in a phased manner...
- Anil Channa** Here, essentially there is no other organized player in the economy segment. Now, imagine as a corporate, we wanted to target our market where the shirt price let us say retailing at Rs. 250 to Rs. 500. Now this is the segment currently being catered to by lot of regional players. So we just needed to be very sure. While our model building, our hypothesis was that, there is lot of turnover to be had and the ROIs can be very good in this particular segment. But we needed to test the hypothesis before

we went into all India launch which is what we have done because essentially we have to create a supply chain to be able to match it. We have to have a distribution network to be able to support it, which is different from what our existing distribution networks are. So there is a whole lot of ground work that had to be done by the business head and his team before we actually went on all India scale.

Abneesh Roy How have you seen the growth for 'World Player' in the different regions, South, North, East, and how is the pricing difference compared to the regional players. For the customer, how does it make a difference to go for a 'World Player'?

Anil Channa Essentially, the pricing points are more or less the same as regional players. But then, it will become a national brand promoted by a very strong brand ambassador. So naturally, it will be a different ball game altogether. But again you would be amazed - we all know that Rs. 250 shirt would be actually the highest selling shirt contrary to that I believe at least Rs. 350 and Rs. 450 is higher seller because probably people do not even want Rs. 250 shirt any more. So we are also having a learning process in this test marketing which we have done. Since there are no other organized players in this category, we think that it is a great potential area to get into.

Abneesh Roy And for a full year, when operations are stabilized in FY12 or may be FY13, what is the number you are looking at from World Player in terms of sales?

Anil Channa I do not know whether I am at liberty to share that number on the call. I think we can have a separate chat on this. I am not too sure, whether I am able now to do a forward-looking.

Abneesh Roy But how big is the market, can you tell me that?

Anil Channa The market is more than Rs. 2,500 crore. It is a huge market.

Abneesh Roy If I see your 2 key segments, SBUs, Consumer Textiles and Luxury Textiles, this time consumer has grown faster 29% versus luxury at 25%. Is that a trend, which will continue because if urban spending is recovering, urban incomes are recovering, I thought luxury might grow faster?

Anil Channa We have to understand that the Consumer Textiles is operating in the mid premium segment. Now mid premium obviously is the largest market in India. So Reid & Taylor has been in existence. It has got 23% market share, but that market is not growing as fast as the mid premium segment and since Belmonte is a relatively newer introduction in the market, naturally we need to come up to that level. So that is why the growth in consumer textile is phenomenal. I hope I am able to explain.

Abneesh Roy So Belmonte, being, I think base effect may be favoring it more compared to Reid & Taylor?

Anil Channa The base effect is favoring more and definitely it is a bigger market and that market is growing very rapidly. So those are all the favorable inputs to us.

Abneesh Roy Sir lastly on the Home Expressions front, just 5% growth, you said is a laggard, so wanted to understand that better?

Anil Channa It is laggard because essentially I think lot of capacities were set up in India looking at the international potential of home textiles. I think everybody was gung-ho about mid-2008. Due to hit in western world, lot of companies lost order book positions with the result that they started dumping the product in the domestic market. In the last 6 months, again the order book has been revived. But then, end of the day the retail business has still not picked up in the US and the Western world. So that is a source of anxiety while the order books are very good, but end of the day, the retail has not

really picked up in the U.S. and in the European markets. It is definitely not going the way it should go. That is my concern. That is why we are not trying to be aggressive in getting into a higher growth number here because right now the margins are also relatively lower and the market is a little crowded.

Abneesh Roy And sir one question on international front. If I see HMX, you mentioned there were some weeks in which sales are not happening because of seasonality. My question is more from margins perspective. Last year the margins were 4.1% based on the numbers you gave and this year it is 3.9%. You also mentioned that last year, there was some disposal of inventory, which obviously will happen at a lower price point. So how is it that the margins were better last year?

Anil Channa As far as the inventories are concerned, the valuation is done as per U.S. GAAP. So it is always at the fair market value. So it is not a discounted value. Whatever discount was there that has already been factored in doing the valuation. So that does not really impact us. Now during this quarter, the EBIDTA margins are definitely a little lower because as I said we have started getting into a new product offering. We have started doing a little bit of advertising campaign because the whole company was not running it as a brand company. We are actually taken the product to a different level altogether and naturally to be able to demonstrate our capability we have to do a little bit of advertising campaign. So those expenses have been built into this quarter.

Jagadeesh Shetty We do not amortize the brand expenses, advertisement expenses. They have been fully written off during this quarter.

Abneesh Roy Just now you said that in U.S., retail sales have still not picked up. So is it a right time to launch a new brand?

Anil Channa It is not a new brand. What I said is that in home textile – yes, the offtake is not happening the way it should happen. As far as HMX is concerned, we have already taken a beating from the peak level. Please remember that HMX at one stage was marketing USD 600 million worth of merchandise. We have already pruned it down significantly looking at the downturn in the market and looking at some of the brands which were not viable right now until a better efficient supply chain system is established. Therefore, whatever numbers we are achieving are based on our reduction of the budgeted numbers. That already has been factored in and all these brands are not new. They are all well-entrenched brands. They only need to be pictured by the American consumer in a different line. It was becoming more like a fuddy-duddy American brand with very baggy suits. Now we have brought in a much younger look. We changed the silhouettes of the merchandise. We made it more fashionable, we brought in more sports, and more casuals, which is in-sync with what the other international brands are doing. But, for us to demonstrate that, we need to do some campaigning, otherwise nobody will know.

Abneesh Roy So this benefit you will start getting in the next one year?

Anil Channa Yes next one year obviously.

Abneesh Roy So margin should also start improving over a one-year timeframe?

Anil Channa Absolutely, we are very confident of that because of the way the company is getting restructured - that process is already done. Now the merchandises will start rolling out in the next 3 to 6 months. I think within the next one year, you would see a change in the HMX operations.

Abneesh Roy Thanks for the opportunity.

- Moderator** Thank you. The next question is from the line of Rajesh Pherwani from HDFC Mutual Fund. Please go ahead.
- Rajesh Pherwani** I just wanted to understand - your Consumer Textile business has done very well, 30% growth this quarter and for the first half as well. How much of that is coming from pricing and how much of raw material price increase has been passed through that is one. A related question is where are we seeing the large growth in tier II, III cities or in the metros? How is the growth factor in these cities or in the segments?
- Anil Channa** Coming to the first part, I think part of it is due to a price increase because the input costs have gone up. Our average increase in Belmonte has been in the region of about Rs. 10 to Rs. 12 a meter at wholesale level. If I translate it to percentage, it will be almost around 6-7%. Rest of it is coming through volume. Now as far as the particular segment goes, we do not find any preferential consumption centers. During this quarter, of course, there was a pooja sale. So naturally, East was a little dominant. But then overall if I look at the numbers, I do not find that any particular region is predominant. I think we have even distribution across all the regions.
- Rajesh Pherwani** More than region, is it that the tier II, III cities or regions are growing much better than the metros?
- Anil Channa** It is very difficult to say because we are supplying to a wholesaler. Whether it is going to tier II, it is very difficult to say. I think because the wholesalers are definitely not in tier II, they are mostly in tier I. So now, whether they are selling it through their sub-brokers or other tag agents, tag dealers to tier II or rural areas is very difficult. We do not get statistics to that extent.
- Rajesh Pherwani** The reason why I asked is because the lower price points are growing at a faster rate. Is it obvious that the mid-tier towns and cities would be larger buyers of these price points?
- Anil Channa** That is obvious.
- Rajesh Pherwani** The other thing is the 6-7% that you mentioned, is it entirely due to RM costs increase or is it also part of it due to pricing power that you are getting right now?
- Anil Channa** So basically, the difference here is that whenever there is a raw material increase, we are able to pass it on because we are a branded player. There will be lot of companies who would be operating in the commodity segment. They would not be able to pass it on because they will come under pressure, the margins would come under pressure. That is actually the key strength we have here. Since we are a branded player, we are able to pass on these kinds of increases to the consumer.
- Rajesh Pherwani** Effectively, it was 20% growth in volumes roughly.
- Anil Channa** That is right.
- Rajesh Pherwani** And what about the premium segment?
- Anil Channa** Same formula applies there also. There also, we had an average price increase of about 4-5% because there the unit value is higher and there the price increases have not been as volatile as in the consumer textiles.
- Rajesh Pherwani** What would be your market share versus Raymond's?
- Anil Channa** According to independent market researchers, I think we were at around 23%. Reid & Taylor was at around 23%.

- Rajesh Pherwani** Okay and any clue on what could be the competitor share?
- Anil Channa** Should be in mid 50s.
- Rajesh Pherwani** Okay fine, thanks.
- Anil Channa** Thank you Rajesh.
- Moderator** Thank you. The next question is from the line of Vibhor Rastogi from IDBI Capital. Please go ahead.
- Vibhor Rastogi** Congratulations for the good set of numbers. I just wanted a couple of clarifications regarding the interest cost. It has increased this quarter to Rs. 93 crore as compared to Rs. 58 crore in last quarter and as you mentioned there is a lot of working capital loan. So do we see, post QIP issue, this interest cost to go down and by how much quantum. If there are any short-term loans, how much has been repaid?
- Jagadeesh Shetty** We could certainly say that this quarter, as I explained earlier, the working capital utilization was at the peak. Naturally on account of the oncoming winter season for worsted fabrics and also festive season for rest of the division, the utilizations were high up and they were peaked out and this peak utilization would not be there in the coming quarters. In that sense, they should also come down and the second factor you said that at the end of the quarter, we raised QIP of Rs. 230 crore, impacting this equity raising, the other utilization of the funds was higher. So this is exclusive to this quarter. I do not think this kind of trend increase should be there for the rest of the quarter.
- Vibhor Rastogi** Could you provide us with the breakup in this quarter - if you have raised some short-term loans or working capital - how much quantum?
- Jagadeesh Shetty** We have not raised any loans in terms of short-term. We work with a consortium of regular bankers. There are net working capital limits sanctioned and utilization would depend upon the production levels. There have been no short-term loans raised at all.
- Vibhor Rastogi** And sir second question is regarding the international operations. How do we see them by end of the year, you see them going positive in the green or what position are the estimations?
- Jagadeesh Shetty** As Channa Sahab has explained to you that we have been in the international operations and they have become EBIDTA positive as we have cut downs the flab, cut down the administration and selling expenses. So we have poised this business to grow and strengthen in the future quarters. We have every indication that having achieved this we should be doing significantly better in the international business.
- Vibhor Rastogi** Sir any numbers that you have in your estimates, like by end of the year, how much you want to reach.
- Jagadeesh Shetty** I do not know. Mr. Salil Bawa, in charge of the investor relations is looking at whether I could make that forward-looking statement in terms of numbers. But I think we would welcome you to visit our office sometime and we could discuss more in detail than in this call.
- Vibhor Rastogi** Thank you so much and Happy Diwali.
- Moderator** Thank you. The next question is from the line of Sejal Doshi from IL&FS. Please go ahead.

- Sejal Doshi** Good morning sir. Sir just wanted to have an update on Reid & Taylor IPO.
- Jagadeesh Shetty** We have been working with merchant bankers for the preparation of DRHP. We are poised to file it as early as possible. There are certain auditing requirements. The numbers need to be audited. That is on the way and I would think we should be in a position to file it as early as possible.
- Sejal Doshi** But can we see that unlocking could happen by the end of this financial year? Have you set any timeline?
- Jagadeesh Shetty** It is an estimate. The way we are planning, I think may be January or December end should be a right time, but there are lots of ifs and buts. There is a queue with SEBI in terms of clearance of prospectus' filed.
- Anil Channa** Just to add to that, I think we will be able go ahead with our filing in the next one week by mid-November. So given that normally takes around 2-2.5 months or 3 months maximum to get it cleared through the various regulatory mechanisms. So I think we should be in a position to do it definitely within this financial year.
- Sejal Doshi** Okay fine, thank you very much sir.
- Moderator** Thank you. The next question is from the line of Murtuza Rohawala from SKS Capital. Please go ahead.
- Murtuza Rohawala** Congratulations everyone on a very good set of numbers. I just have one question and it is largely about the clarity on the numbers with respect to your Luxury Textiles segment. If I understand correctly, the entire Rs. 220 crore in this Q2 is coming from Reid & Taylor.
- Anil Channa** In the fabric business - yes.
- Murtuza Rohawala** So how much would your Reid & Taylor topline be, is this the same?
- Anil Channa** The top-line is Rs. 296 crore for this quarter.
- Murtuza Rohawala** So is this entirely Reid & Taylor?
- Anil Channa** Yes.
- Jagadeesh Shetty** Reid & Taylor fabrics as well as Reid & Taylor ready-to-wear garments. We have Stephens Brothers in the garment division.
- Murtuza Rohawala** So what would the top-line be for Reid & Taylor as a subsidiary?
- Jagadeesh Shetty** As you see in this quarter, our sales are Rs. 296 crore and that could give you an indication and this is not necessarily....
- Anil Channa** Half year it is Rs. 567 crore already.
- Murtuza Rohawala** Great. That is all I wanted to know.
- Moderator** Thank you. The next question is from the line of Abneesh Roy from Edelweiss. Please go ahead.
- Abneesh Roy** One followup question regarding the price hike - you mentioned 6-7% in Belmonte and around 4-5% in Reid & Taylor. So in terms of the raw material trends, which are

visible as of now, is this price hike enough or you would like to take some price hike post the festive season?

- Anil Channa** I think whatever price rises have happened, we have already been able to pass it on and we are not expecting any significant increases going forward. But, if it happens, we are in a position to pass it on. That has been the strength of our brand and strength of our model.
- Abneesh Roy** In terms of growth rate for the domestic business, do you think that Q3 should be much better than Q2 because this time festive season has been delayed. So to that extent, should Q3 be much faster compared to Q2 as per the trends in October?
- Anil Channa** Actually, it is very difficult to say. Typically, what happens is in the fabric businesses, yes what you say is right, lot of growth can happen. But, in our apparel business, actually the peak starts only from January-March quarter because the composition of our business is changing so rapidly. Our apparel business was only 12%, last year we ended at 25% and gradually over the next 2 years it will go up to almost 40%. So that probably will actually help in trying to even out quarter-to-quarter because sometime the fabric is strong, sometime the apparel is strong. That is consistent with the market requirements actually.
- Abneesh Roy** Where do you see the interest cost in the coming quarters? Largely should it be at these levels?
- Jagadeesh Shetty** All I could say is that the increase that you are seeing between the last year and this year - this kind of increasing trend would not be there.
- Abneesh Roy** So it can still go further, but it may not increase significantly.
- Jagadeesh Shetty** It will not grow as much as it has grown in this quarter. As I explained to you, the production levels were higher and the international business for the first time got fully consolidated. So it is the consolidated number. The cost as a percentage of sales would remain the same for the year.
- Abneesh Roy** And sir lastly on the Gujarat Baruche facility - you said it is getting stabilized and full potential will be seen in the coming month. Could you give us a sense in terms of some numbers if possible, say margins or production or whatever?
- Jagadeesh Shetty** This division has the potential to do a sale of Rs. 280 crore on a full year basis - that should happen in the year 2011-12, and the EBIDTA margins will be close to about 34% and that's the potential of the business as we have set it up.
- Abneesh Roy** What would the current margins, Q2 margins, be from this facility?
- Jagadeesh Shetty** This year, we should be half the way in terms of margins since we have a budget of 34% for the next year, if the production would get stabilized partly during this year and fully during the next year. We should be at least half the way.
- Abneesh Roy** And current capacity utilization will be what, 50-60%?
- Anil Channa** Around 40-50%. It is getting scaled up gradually. Typically what happens is you start on one particular product range which is yarn type product, then you get into little bit of dyeing get into stretch kind of fabrics, stretch fabrics. So it is a gradual step up of the capacity.
- Abneesh Roy** And what is the confidence level for doing this because in one year you are saying...

- Anil Channa** Our order book is very healthy. The product has been well accepted in the market. God help us. That is all I can say. The team is very committed and we are booked almost till February.
- Jagadeesh Shetty** Just a point to add here, normally in the way we do the business, we focus on the marketing arrangement first and then at the production. So, the marketing arrangement in terms of Leggiuno being there for the consumer of this fabric is already in place. There is a strong market there. So I don't see any ifs and buts on this.
- Abneesh Roy** And sir lastly on price hike - have most of the competitors also have taken similar hike or basically have you been the only one to take it.
- Anil Channa** No, naturally the competition has also taken, but of course the degree could be a little 1 or 2%. After all there is no cartel here. Everybody has to take his own decision. We have taken an aggressive decision.
- Abneesh Roy** Okay sir thanks a lot, all the best sir.
- Moderator** Thank you. The next question is from the line of Kesvinder Suri from Span Capital. Please go ahead.
- Kesvinder Suri** Yes, good morning gentlemen thank you for taking my question. Your response to the Reid & Taylor top-line, sorry your voice was not clear at that moment. Could you reiterate the numbers please?
- Jagadeesh Shetty** Reid & Taylor for this quarter is Rs. 296 crore of revenue and for the 6 months ended September 2010, the revenue is Rs. 568 crore.
- Kesvinder Suri** Thank you.
- Moderator** Thank you. The next question is from the line of Divya Damodaran from Dimensional Securities. Please go ahead.
- Divya Damodaran** Good morning. I would like to know how the QIP proceeds are going to be utilized.
- Jagadeesh Shetty** The QIP - as you might know, the company has taken up quite a few expansion plans to supplement the existing business and to take care of the overseas market, which has come about by acquisition of HMX and Leggiuno. While most of the requirements are funded through TUF loan from the bank which is subsidized and we just need to take care of the equity component that would be required for completing all these projects majorly.
- Divya Damodaran** Thank you and next question. Do you have any outsourcing plans on the foreign business from India?
- Anil Channa** Outsourcing plans means the Indian business is already supplying to them and this activity would definitely increase because we are setting up our factory for making suits in Bangalore. We are also going to be setting our factory for making shirts. So there will be a lot of supply to the overseas businesses. It has already been started from our Baruche project and from Reid & Taylor. It is already started in fabric form right now.
- Divya Damodaran** And it will be helping in reducing your cost on a very high level?
- Anil Channa** Essentially the way it works is the transfer pricing is absolutely in arm's length to which it is absolutely market determined. So while the additional volume comes up, it

does not really impact anything else. Instead of supplying to domestic customer, we are only supplying to the overseas companies because the buying fee or the selling fee actually decide what price points, what quantities. We don't get involved in the corporate office. It is an ongoing activity.

- Jagadeesh Shetty** But that will be a telescopic value addition that is possible as we may have said earlier. So in the given situation we would have production that would start from import of wool from Australia, then spinning this into yarn and weaving, processing, finishing, making fabrics and making suits and then turning over to US to be sold in the US counter. So that is a huge value addition umbrella happening within the group.
- Divya Damodaran** Thank you so much.
- Moderator** Thank you. The next question is a followup from the line of Rajesh Pherwani from HDFC Mutual Fund. Please go ahead.
- Rajesh Pherwani** I wanted to understand what your CAPEX plans are for the next 2 to 3 years.
- Jagadeesh Shetty** In terms of amounts, we would be spending about Rs. 730 crore in the current year and in the following year, FY 2011-12, to complete all the projects that we have undertaken.
- Anil Channa** See the objective here has been that with our overseas companies and lot of synergy possibilities, naturally we need to enhance our capacities in Reid & Taylor, which we are already doing. **It is going up from 8 million to 10 million.** We are also setting up a suit factory to be able to cater to the international market as well as our own overseas companies. Similarly, we are doing the same thing for shirt making also, which will help Baruche. It will also start helping Leggiuno. So it is a very well planned and a well thought out CAPEX strategy.
- Rajesh Pherwani** This was Rs. 730 crore cumulative right - total over two years?
- Anil Channa** Yes, lot of backward integration also to be able to improve the profitability, the margin, and the serviceability to the customer and reduce our working capital cycles. It is aimed at several things
- Rajesh Pherwani** And when do we see the CAPEX figures coming down. Should it be after two years or you further plan to....
- Anil Channa** Why you don't want us to grow?
- Rajesh Pherwani** No I don't mean in that sense...
- Anil Channa** Why? You don't want us to be grow? at **1.2 or 1.5 million?**
- Rajesh Pherwani** No absolutely not. My point is that in the last three-four years, you have seen large CAPEX in the business contrary to what you saw in the past. Just wanted to understand...
- Anil Channa** See Rajesh, actually of course it can be a different discussion, but essentially I think the way the Eastern world, our world, is emerging, I think the time is coming where a lot of consolidation will start happening over the next couple of years. So I would not say that the CAPEX will ever come to an end. I don't want to be sounding if there is a consolidation possibility, lot of Indian businesses would actually start merging with the large companies. This is what we have seen in the Western world. So I guess the same order would start emerging in India also. I think it is very difficult to do a kind of a forecast on that right now.

- Jagadeesh Shetty** I will just add one more thing. The way we are doing the business, Rajesh, is that normally as a corporate strategy, we will look at the marketing first, look at the demand first, create an atmosphere, create a marketing situation and a backup of that demand first and then go back and put up production facility. So when we are investing in production facilities, for example we are setting up a suit factory, the demand for which is already created and what we are doing is going back and putting up those facilities. It is not that we have put up a facility and then looking for the customer. So in that sense if you are as an analyst looking from a perspective of risk of investment and whether we will be able to sell, that has been already addressed.
- Rajesh Pherwani** Okay and any update on the TUF scheme, anything that you can share?
- Jagadeesh Shetty** The government - I think politically it is a very sensitive issue. I don't think the government would ever be able to take it out. The government would want to give support to the textile industry because that is the major Forex earner to the government. Of course, there can always be some tweaking, whether some spinning equipments will be added or otherwise, I think in my sense it would be continued.
- Rajesh Pherwani** Okay, thank you
- Moderator** Thank you. The next question is a followup from the line of Kesvinder Suri from Span Capital. Please go ahead.
- Kesvinder Suri** Thank you for taking my question again. Could you throw some more light on your proposed DKNY business as to when it will start contributing significantly and what are the facilities being set up for the same?
- Anees Fazalbhoy** The DKNY business is a joint venture with DKNY, SKNL UK's joint venture. The business there right now - you see this is the first time that DKNY has actually licensed out the menswear brand and in-house they do the women's wear which is worth about US \$1 billion. It was doing very well earlier while it was with them, then the market for them with their concentration on the women's wear they move to, they licensed out the menswear. So now as we are beginning this relationship, there is no manufacturing of this product in-house. We have outsourced the entire operation. It is run from our London office and we supply to about 70 DKNY stores, which currently exist. They are opening up many more stores; even in the US they will be opening up; DKNY themselves will be opening up more stores and we will be supplying directly to them. The relationship with DKNY also permits us to appoint our own new distributors for the DKNY line up in markets where they have no existing relationship. So that is in Australia, in Russia, and some other eastern European countries are also being approached right now. I think, basically, the market where it has started to reduce for menswear because of the concentration on DKNY women's wear, now we will see a very substantial growth. And also DKNY is planning an advertising promotion campaign worldwide and we also get a lot of visibility both through the women's wear and through the fragrance market which DKNY is promoting very strongly. We get a lot of spill over benefits, but this is relatively a newer business and I think going forward the brand is very strong, very highly recognized. So we should be looking at healthy growth here.
- Kesvinder Suri** And what is our share in the JV, how much the stake we have?
- Anees Fazalbhoy** We have 80% and DKNY, which is a Louis Vuitton group, has 20%.
- Kesvinder Suri** And how do the economics of this work? So essentially SKNL India through any of its facilities wouldn't be supplying any fabric or anything to DKNY lineup right?
- Anees Fazalbhoy** Yes I mean, see essentially whatever our strategy has been for front-end back-end synergy, whatever assets we have acquired overseas, whether in HMX or Leggiuno

or the DKNY business, we hope to grow it through back-end front-end synergies. So wherever we can support from domestic sources, we would like to do that. Now each of the activities are being run independently. But specifically talking of DKNY, as there is no specific manufacturing facility for this business, they can source London office product from all over the world. So something from Italy, something from Turkey, a lot from China and there is product coming out of India. We of course look forward to that sourcing business out of India increasingly over a period of time. So definitely, SKNL will look forward to supplying more products whether from the garment division or the fabric divisions because the DKNY range has formal wear and casual wear. So we look forward to all that developing out of India. DKNY also includes an accessory line up. So as we start adding accessories to our ranges here, we are sure that will also be something we can look at sourcing. But ultimately SKNL UK is independently run and we hope that relationship with Louis Vuitton and DKNY, specifically that relationship, in itself will help us develop other businesses and other activities as well.

- Kesvinder Suri** And what has been our investment in this JV till date?
- Anees Fazalbhoy** Two million pounds at this time
- Anil Channa** Essentially, it is just the working capital because there are no capex plans for setting up manufacturing. Most of it is been outsourced. So it is the investment in the working capital.
- Kesvinder Suri** I mean what about the initial license fee or how much have you paid for this partnership.
- Anees Fazalbhoy** No, we had negotiated that there was no upfront fee. We do pay royalty and contribution to advertising.
- Anil Channa** Which is coming out of the revenue stream itself
- Kesvinder Suri** Okay, thank you
- Moderator** Thank you. Ladies and gentlemen that was the last question. I would now like to hand the floor back to Mr. Anil Channa for closing comments. Please go ahead sir.
- Anil Channa** Thank you all of you for a very participative discussion. I hope we have been able to, our team has been able to clear all the queries which were raised. Anyway, just to sum up, I think we are confident that future looks equally promising with the domestic as well as international business segments strategically poised for enhanced performance, presence across the value chain from procurement of fiber to finishing and back-end front-end synergies model and a well-diversified and strong brand portfolio catering to diverse customer segments across the globe. Our expansive marketing and distribution network and state-of-art manufacturing plants definitely provide a solid foundation to continue delivering sustainable growth going forward. So again, I wish you a very happy Diwali and look forward to talking to you in subsequent calls. Thank you.
- Moderator** Thank you gentlemen of the management, ladies and gentlemen on behalf of SKNL that concludes this conference call. Thank you for joining us and you may now disconnect the lines.

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