"Shoppers Stop Limited Q2FY16 Earnings Conference Call"

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Moderator: Ladies and Gentlemen, Good Day and Welcome to the Shoppers Stop Limited Q2FY16 Earnings Conference Call. As a reminder, all participants' 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 this 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. Govind Shrikhande – Customer Care Associate and Managing Director, Shoppers Stop. Thank you, and over to you, sir.

Govind Shrikhande: Good Afternoon, everyone. Welcome to the Q2 Con-call. Although the numbers look muted, let me explain to you as we go through the results about how the Q2 muted is impacting Q3 in a very positive way.

Starting on Page #3 Business Overview: We opened three new stores -- one in Meerut, one in Kolhapur and one additional store in Kolkata. We also close down two stores which have been impacting on profitability for some time now -- one Delhi Ansal Plaza; Ansal Plaza has been one of the most well-known malls in India since its beginning but it has been losing ground as newer malls have come up and we finally decided to shut it down this quarter. Jaipur Suncity although we have shut down the store, we actually relocated into another mall in Jaipur, so we still have two stores in Jaipur now, and this new store opened about a week back in this quarter. MOTHERCARE we opened a SIS in Kolkata and one SIS shutdown which was part of Jaipur Sun City. One Crossword store opened at Bangalore Airport and we also closed one more store in Bangalore overall.

Loyalty Program continues to grow well; as of now 3.9 million members and contributing to sale of 70% overall. We are also targeting to open four stores in the second half of this year, one more in Delhi, one more coming up in Noida, one coming up in Goa and one more coming up in Bangalore.

Various awards that we received during the quarter apart from Most Admired Retailer of the Year, also Most Admired Enterprise Solutions Implementation and Digital Marketing Campaign of the Year; in the World Retail Congress got the Excellence Award for Supply Chain Sustainability as well; and National Award for Marketing Excellence in Retail sector for Crossword as well. For HyperCity also we won five awards at the National Award for Excellence in Training and Development, in Best Customer Service Program, Best Organizational Development Program, Best Onboarding Program, Best Differently Abled Recruitment Program and Best Innovative R&R Program, all related to HR practices in HyperCity.

Moving on to Page #6: You can see the overall view of all formats and their presence across India. As of Q2-end we have 74 Stores in Shoppers Stop Department Store, 50 Crossword Store, 19 HomeStop, 4 MOTHERCARE standalone Doors, 73 M.A.C. Estee Lauder Clinique BOBBI BROWN Doors and 17 HyperCity stores, totally covering 234 stores in 36 cities and 5.74 million square feet

Page #7 you can see the total square feet format by format and the addition that we have done during the quarter. At net level, there was no addition because of closure of two stores.

Page #8, 9 and 10 you can see the photographs of all the new stores -- Meerut, Kolhapur and Acropolis Kolkata.

We also launched one more exclusive brand in our portfolio. This is RS by Rocky Star. This is along with Rocky S who is one of the most well-known designers within India. It has taken off pretty well and we believe this can again go on to become a big brand within our format.

Coming to Q2 results: Overall sales growth at 3.2%, all formats at 3.5%. Shoppers Stop Department Store like-to-like growth is flat and greater than five years stores running at (-0.4%) and stores less than five years at 1.1%.

Let me explain to you why this growth is looking so muted. Fundamentally, during the quarter a big change event that has happened is the movement of Puja and Dussehra which are pretty big for us across East and South which is Telangana, Andhra and some part of Karnataka. Last year Puja was part of Q2, this year it has moved to Q3. And as a result we have seen during Q2 as far as each store is concerned running at almost (-6%) like-to-like growth and South region running again a similar kind of a negative growth. Now we have mapped that growth vis-à-vis the actual Puja period of four weeks, and right now the Puja period is running at very high double digit growth which really compensates for this negative growth. So our belief is that if Puja has not moved, the like-to-like growth impact would have been a (+5%) on account of the Puja event.

The other big event during the quarter which is actually a good step that we have taken is reduce our sale period by one week. So earlier the sale period used to be eight weeks, this year onwards we have taken it down to seven weeks, and the positive impact of that has been on gross margin earning which has gone up by 80 basis points which has also helped us to improve our EBITDA numbers, EBITDA is up by almost 11%.

On the ground, as of now, just to give a heads up: The Puja, Dussehra period and Diwali pre-buildup period is doing pretty well and we are seeing very good traction on the ground, as I mentioned high double-digit like-to-like growth is what we are right now witnessing. So pretty confident of the Q3 numbers and I will also tell you later on what steps are we taking during the quarter as well.

Moving on, the Q2 numbers please look at it in terms of the shift of the festive period and that is why you are seeing a very high like-to-like degrowth in entry and volume down at 1.6 and price increase of 1.7 although conversion is up in like-to-like stores by almost 10%. So please look at all these numbers in light of the shift of festive period.

Moving on to Page 14: Private brand share has dropped whereas Exclusive brand share has gone up from 2.7 to 3.4. Overall trading model, no big shift there.

Page 15: You can see Non-Apparel going up by almost 170 basis points and typically during the sale period Apparel sales always grow higher than Non-Apparel but as I mentioned earlier because of the shift of festive period as well as lesser sale period, we are actually seeing the non-apparel gaining more traction. Categories which continue to grow double-digit is MAC, Beauty, Personal Accessories and they are still continuing to do well even in a muted sales growth. You can see in the four categories -- Men, Ladies, Children all of them reducing their share and Non-Apparel increasing its share as well.

Page #16: You can see the shrinkage still on track with the earlier numbers and even for H1 last year we were at 0.38, this year we are running at 0.36. So very much under control of our target of remaining at 0.5 or lower.

Q2 numbers: If you look at the top line sales up by 4% at Rs.1,004 crores versus Rs.967 crores last year. Margin on sale is up from 32.1% last year to 32.9%, a jump of 80 basis points and 6% growth from Rs.306 crores to Rs.324 crores. Our operating expenses have been pretty much under control growing only by 6% and that is our EBITDA is up from 5.9% to 6.3%, a 11% jump. Finance charges not really grown so much but depreciation is up by 58%, almost a jump of Rs.11 crores Vs last year of Rs.19.5, we are running at Rs.30.9 crores and this is on account of the closure of the two stores namely which is Ansal Plaza and Jaipur-2 and that is impacting the PBT which has dropped from Rs.27.7 crores to Rs.21.9 crores. PAT is accordingly lower at Rs.12.8 crores.

What are we really doing in Q2 to Q3 to take the sale head on. So there are a number of actions that we have planned during Q3. One of the definite advantages is the shifting of the Puja festive period, but Q3 basically has a bumper offering of Puja, Dussehra, Diwali, then a big marriage season, then Christmas and then New Year. So as it is, it is lined up pretty well with various events that are happening.

#2: Choose Your Own Gift, which is an event that we planned only for First Citizens. This year we have opened it out across the chain for every walk-in customer as well. So we believe we will get an advantage out of that and we are currently seeing good results of that scheme running in Kolkata and the entire East.

#3: We had promised while executing Hybris that just before Diwali our new site, the Refresh site will be on, you can check our site, in fact you can shop on our site right now. Far superior navigation, far superior digital content and we believe that Hybris is working well and it should stabilize over the next 45 to 60 days' time but it is right now up and running.

#4: We were supposed to sign and start off our Snapdeal site. Shoppers Stop on Snapdeal has Anchor. That is also up and running right now and we believe in the next 15-days' time just before Diwali we should see the site assortment further improved as well.

We also signed on a deal with Recharge to accept Mobile Wallet not only in store but also online and that should also give a fillip to bringing in newer customers on site as well as in the physical store.

We also signed on for our Phase- II of our Online Journey WMS which is a software from JDA called RedPrairie. This will enable us in our journey towards multi-channel. This will start getting executed from December of this year and will become live by June next year and January 2017 will be truly Omni-Channel. So journey of three stages: Journey First stage is already over with Hybris execution. Stage-II which is WMS will get completed in June next year and January 2017 will be fully Omni-Channel. We are pretty confident that with this journey we should be able to hit 10% share of sales over a three-year period through our Online journey.

Apart from that, on the ground level, where in the brick-and-mortar store we need to create more excitement and make customers to come back again and again and have interactivity. We have launched Magic Mirror as a concept in the Kolkata Store. The first feedback from the customers have been pretty exciting. We are very happy with the kind of interaction that they are finding and the way they can make choices within the shop floor without entering the trial room and I believe that we can roll it out across India over the next 12-month period once our learning from this first trial have been taken onboard and we have further more lot of other digital initiatives that will be rolling out from Q4 onwards.

Before I get on to the consolidated numbers for Q2, let me take you first through the HyperCity numbers and I will come back there. Moving on to Page 25: For HyperCity the results definitely have been soft. Overall, like-to-like growth is flat at 0.3%, like-to-like sales per square feet have grown by 2.7% due to reduction of space in a few stores. Fashion Mix still a positive sign growing well at 15.4% share versus 14.2%. Gross margin is lower by 20 basis points and OPEX growth still under control at 3.1%. Store operating profit positive at Rs.5.5 crores versus last year Rs.9.07 crores. Company EBITDA after almost six quarters we have seen a negative EBITDA at the company level of Rs. (–4) crores versus positive of last year Rs.20 lakhs. Between this quarter we did experiment a lot on our assortment and price offering, but none of those experiments that we tried to drive volume up work for us. And while volume did not grow we also lost margin because of the offering that we made of lower than MRP price points in a key stores. So we are reworking on the assortment and we believe that we have got some corrections to make in the store, in the assortment, in the circulation of some of the stores and all those actions we have planned out throughout Q3. So we believe by Q4 we should be back on track and our target of hitting EBIT is still looking about four to six quarters away from today.

Moving on, there are property options booked in this quarter. As far as sales growth is concerned overall at 3% and as I earlier mentioned we are in a 0.3% on store greater than five years.

On Page #27 you can see that the like-to-like stores degrew by 5%. The big challenge has been volume degrowth of 5% and average selling price growth of 5%. Overall, it has been a flat like-to-like growth at overall sales level. Transaction size is up by 2% and conversion is also up by 2% but really has not helped the business to really drive it harder.

On Page #28 you can see the Financial Numbers: Sales up by 3%, margin on sales down from 21% last year to 20.8%, so 80 basis points drop in margins both at gross margin level as well as shrinkage you can see has gone up from 0.6 to 1.1, 50 basis point loss there. At a store EBITDA level we are down from 3.9 to 2.3 from Rs.9 crores to Rs.5.5 crores, and at company EBITDA level as I mentioned earlier from (+20) lakhs we are at (-4) crores. At a PAT level from Rs.16.3 crores loss last year, we are at Rs.20.7 crores. Currently, out of the 17 stores, 10 stores are EBITDA positive and as I mentioned that we are planning a lot of corrections in the assortment as well as the store mix. We will be launching two stores during this second half. One of them is coming up right now in Noida. In fact it is just opened today and one more store is coming up in Delhi either at Q3 end or Q4.

Coming back to the consolidated numbers on Page #18: Sales is up by 4%, marginal sale is up by 6% from 30.6%, it has gone up to 31.3%. EBITDA is up from Rs.53.2 crores last year to Rs.56.3 crores, 4.3 to 4.4 as a percentage. Because after minority interest canceling off the impact, the PAT is up from Rs.3.7 crores to Rs.7.6 crores, 100% growth at PAT level.

That is all from my side. I would now leave the forum open for all Questions.

Moderator: Thank you very much, sir. Ladies and Gentlemen, we will now begin the Question-and-Answer Session. We have the first question is from the line of Avi Mehta from IIFL. Please go ahead.

Avi Mehta: In the depreciation, what was the impact because of the store closures, could you quantify that?

Govind Shrikhande: Rs.7 crores out of the Rs.11 crores , so Rs.7 crores has come because of the write off.

Avi Mehta: On HyperCity, you said that third quarter also you see impact because of the correction in assortment coming in, so EBITDA is likely to remain. So what is the revised guidance for EBITDA positive for HyperCity, or is there any change?

Govind Shrikhande: We were looking at four to six quarters EBIT positive if you recollect at quarter one end and looks even now still four to six quarters away.

Moderator: Thank you. The next question is from the line of Chanchal Khandelwal from Birla Mutual Fund. Please go ahead.

Chanchal Khandelwal: Firstly, did I hear it right you are talking about high double-digit same-store sales growth for this season…?

Govind Shriikhande: That is right.

Chanchal Khandelwal: Just to understand a bit more on this, how has the response been for our eCommerce tie-up because Shoppers Stop available in the Snapdeal, how has the response been and what is the launch plan of our eCommerce website and how and when it will be up and running?

Govind Shrikhande: The refresh site is up and running right now, but we are not really focusing on launching in a big bang right now, we want it to stabilize, #1; #2, same thing for the Snapdeal, it has just gone live right now and we believe in the current market where everyone is trying to do Monday or Tuesday or Thursday, we still want to focus on the basics of retailing and allow it to scale up over a period of time.

Chanchal Khandelwal: So your own website, like Myntra will you be focusing it as a store or will there be a high focus, what is the plan there?

Govind Shrikhande: As I mentioned overall our target is over a three-year period. 10% of our sales should come out of online. We are not really going to be a market place. It is going to be a reflection of our physical store and yes, there will be additional brands, categories available, but we will not be a market based, we will be a real store.

Chanchal Khandelwal: On the private brand, this quarter it was a little lower, right, it was 13.9% which was 15.1% last quarter. Although the gross margin has improved, but what is the plan there, how big do you want to make this because now that you are also doing sales through a Snapdeal, that is an important strategy?

Govind Shrikhande: The overall idea is how do you really differentiate your assortment vis-à-vis not only physical brick-and-mortar retailers but also online retailers. And that is why both private brand and exclusive brand share is going to be very-very important. Our idea is overall in three years time to raise this 17% with private brand and exclusive brand to 35%. We plan to double it over a three-year period and that is what we are trying to chase. This quarter we have not been able to achieve growth that we targeted, but I would leave it aside and really focus on the next few quarters.

Chanchal Khandelwal: On the HyperCity business, a little disappointment this quarter. We have seen the competition scale up. What is our thought process in that business – you are going to get a partner, how much investment is going to go for next 2-3-years, I am not talking about immediate?

Govind Shrikhande: Currently, there is no partnership that is feasible because of the FDI regulation as far as international partner is concerned. We have always stated that we are open to that but because of current government regulations we are not able to get international partner, #1; #2, we will continue to open two stores a year. So whatever funding is required within the group and the promoters, we will continue to invest in it. But the key focus definitely is to move towards EBIT-positive which we have slipped this quarter and we believe that yes, it has been a soft performance this quarter because HyperCity does not have each performance that can impact it. It has been our own underperformance in the quarter but we believe we should be able to be coming back on track by Q4.

Moderator: Thank you. The next question is from the line of Puneet Jain from Goldman Sachs. Please go ahead.

Puneet Jain: You mention about high double digit growth. Will it be systems sales growth, will that be including store additions or …?

Govind Shrikhande: High like-to-like double-digit same store growth.

Puneet Jain: Will you actually call it as a change in trend because double-digit like-to-like growth has actually been elusive for various retailers for some time?

Govind Shrikhande: Q1 we were 11%. We had achieved double-digit growth in Q1. High double digit means much higher than that. That is something that we are seeing right now on the ground.

Puneet Jain: Could you throw some light as to what is driving it – are you actually seeing that your consumer is willing to spend more at this point of time compared to what has been the case over the last couple of years?

Govind Shrikhande: I do not know whether the trend is a sustainable trend. That is why would not really qualify it, but I would say there are two or three elements to it -- One element is inflation in India which actually now slowed down if you look at last 3-4 quarters. #2, if inflation is low, oil prices are low and your incomes have risen that really means that you have higher disposable income. Now, the question is are you spending it on mobiles or are you spending in daal roti or are you spending on clothing? It depends basically on your prioritization during that quarter or whatever else is happening around you. My guess is the spending will catch up over a period of time. If this is the inflation level, overall Retail should grow much faster.

Puneet Jain: So any particular category which is driving this growth – is it apparel or any particular category which is non-apparel which is driving faster growth or any particular….?

Govind Shrikhande: The one month that has already gone by we have seen growth across all categories, yes, and the two or three big categories during Diwali typically are personal accessories that goes very well, Beauty, MAC we are seeing again growing well and Clothing does come back again well during this period.

Puneet Jain: Will it be driven by more footfalls or increase in transitions for customers?

Govind Shrikhande: As of now, I do not have any indicate around that, may be post-Diwali we should be able to tell you, but overall conversion is going up, ticket size is also going up, but ASP is not going up so much because inflation is under control.

Puneet Jain: Difficult to estimate the impact of eCommerce, but could there be some metrics to understand that what could your same-store growth could have been had eCommerce not played a part over the course of last couple of quarters?

Govind Shrikhande: Last year this quarter Q3 was the first time when eCom starting impacting the Physical Retail in a very big way because of large amount of discounting and large amount of advertising. Now what really happened is I call it the Laxmikant-Pyarelal phenomena. In Laxikant-Pyarelal phenomena, what used to happen is he used to play the same song 25 times and it will become a hit, but after some point of time it will lose its nature. Right now if you look at it, you pick up any newspaper starting June you will find four pager, eight pager, twelve pager. After some time that four pager, eight pager is not going to impact you. You will shop where you want to show. Definitely eCom will continue to grow, but the impact on the brick-and-mortar is not going to be so significant that people will stop coming to brick-and-mortar. They are continuing to come to brick-and-mortar and even I would say 24-months down the line 80% to 85% of share of sales would still be brick-and-mortar. I think we should not get overly worried about that, we should focus on actions that we need to take and we need to also ensure that we are omni-channel. So we are taking all the three steps -- we are going omni-channel, we are improving our footprint and at the same time we are creating more exciting things on the ground in the store that customers come back to the store again and again.

Puneet Jain: On growth plans, given the fact that your new locations possibly are becoming more difficult given the fact that new malls are very hard to come by. So, are you seeing a change where you are targeting a large number of new stores opening in non-mall locations and is that possible?

Govind Shrikhande: Currently, mall location or non-mall location, number of locations available is dropping dramatically. There was a time when we could actually target to open 10 or 12 stores a year. Now after this year 9 store opening if I look at the target for the next 24 months it would be about 4 stores each year, overall could be eight or nine stores only over the next 24-months. Not too much of a pipeline available and that is why I believe that we will have to look at omni-channel much more aggressive way.

Puneet Jain: But even beyond that I think mall locations will be very hard to come by because no new mall has started construction over the last two years, which means that even after two years there will be no finishes possibly for next 3-4-years in terms of mall locations, which means that the omni-channel will be more and more important?

Govind Shrikhande: That is what I am saying.

Moderator: Thank you. The next question is from the line of Prashant Kutty from Emkay Global. Please go ahead.

Prashant Kutty: Firstly, is there a way to probably strip off the Dussehra impact and probably what is the growth in terms of SSG?

Govind Shrikhande: I mentioned that if Dussehra was in Q2 this year you could have seen a like-to-like growth of about 5% instead of the flat that we are seeing.

Prashant Kutty: In terms of the eCommerce, obviously, you did highlight that this is something which has been continuously happening and obviously over a period of time eventually people would come back to the brick-and-mortar site. But if you could just actually tell us the impact as to what is probably a change in last year and in this year in terms of eCommerce sales or any qualitative comments on the same?

Govind Shrikhande: This year when all the "Billion Dollar Sale" was happening for one week 10 days or 12 days, I actually did not see any impact on the sale in the Physical Store because the Dussehra was at peak across East and South and we actually did not see any impact and as I mentioned we actually are seeing a high double-digit like-to-like growth.

Prashant Kutty: But just to take it a bit forward over here in terms of this is obviously everybody is banking a lot on the upcoming festive season and the fact that this is a fairly well spread festive season, there is a belief that typically it will continue its momentum as well. Do we continue to have the same belief that this could actually continue into the end of the fourth quarter as well or maybe even beyond that as well, how we are looking at that post this quarter?

Govind Shrikhande: Q3 definitely looks promising and it has started off pretty well and as I mentioned Diwali is yet to happen which will happen in the next two weeks time, post Diwali there is a big marriage season that comes up in November to December first week and then there is obviously the whole December month of Christmas, New Year, festivities that are there. So Q3 I do not see any issue at all, should sales do pretty well. Q4 typically starts off with a sale period and generally speaking is pretty good, March is always very-very slow. I am still confident on the entire second half.

Prashant Kutty: What is the store addition target for next year, what are the planning and which will be the possible locations over here as far as store addition could be concerned?

Govind Shrikhande: This year we are targeting six store openings, we will end up opening nine in fact because two of the stores of next year are actually opening up this financial year. So balance there are the four stores to open in the next financial year and there are another four stores in the next to next financial year. I cannot tell the locations right now because it is an iterative number right now.

Prashant Kutty: What could be the kind of locations – is it like a Tier-1, Tier-2?

Govind Shrikhande: Majority of them are Tier-1.

Prashant Kutty: Any differentiation as far as the growth trends are concerned vis-à-vis Tier-1 or Tier-2 or Tier-3 kind of in the quarter gone by or let us say in the October month?

Govind Shrikhande: Not really analyzing that much but Q1 or overall when you look at it Tier-1 Vs Tier-2 there are certain categories that work very well in Tier-1 and those categories really do not work very well in Tier-2. Primarily it is Women's Western Wear and Formal Men's wear which works always very well in Tier-1 because there are a lot of corporates there. Tier-2 there being no corporates and no working women, these two categories do not perform as well. Personal Accessories is a category that performs always very well in Tier-2 as well as Kids Wear.

Prashant Kutty: But in general, if I have to probably make an assessment over here, any such sense that okay, maybe Tier-1 has done better than Tier-2 or any such thing visible let us say vis-à-vis the two-three quarters back or something of that sort?

Govind Shrikhande: Actually, it is not about tiers, it is about zones more because if you look at it as I mention, East and South have underperformed this quarter because of the shift, North for some strange reason continues to always grow whatever happens, we have seen it for almost three years now and West is up and down depending on how the stock market performs.

Prashant Kutty: The tax rate is higher for the quarter. What is the tax rate that we can assume for the full year?

Sanjay Chakravarti: 40% would be the right assumption. I do not know if you are looking at the quarter or the half. If you are looking at the half there is the impairment impact that we had taken which is not allowable under tax. So do not take that because that is going to skew your rate to almost 50%. If you take it on the PBT pre the impairment it should be around 40% which should be a fair ETR to take for the year.

Prashant Kutty: Any specific reason as to why our other expenditure is a little higher, anything to …?

Sanjay Chakravarti: That is to do with the growth… the non like-to-like.

Moderator: Thank you. The next question is from the line of Harit Kapoor from IDFC Securities. Please go ahead.

Harit Kapoor: A couple of things on the store closures: I just wanted to understand Delhi and Jaipur store closure. In your assessment, what would be the impact on the top line contribution on account of this store closure?

Govind Shrikhande: I would say below Rs.100 crores.

Harit Kapoor: This was done when?

Govind Shrikhande: In the middle of the Q2.

Sanjay Chakravarti: Harit, this is Sanjay. Just one thing to add, even though the number Rs.100 crores of top line appears big, it is actually profit-accretive because these stores going forward would have slipped into the red.

Harit Kapoor: Also that you opened another store in Jaipur so that impact was very less?

Govind Shrikhande: In Jaipur, the impact would not felt, in Delhi the impact would be felt on top line. But, on the bottom line both put together it is a very positive impact.

Harit Kapoor: You said that there are four more stores to be opened in the current year, right and four more in FY17?

Govind Shrikhande: Four more in FY17 and four more in FY18.

Harit Kapoor: On HyperCity, how much more of the giving up of this space is left now in the overall scheme of things or…?

Govind Shrikhande: I would say about 50,000 square feet approximately.

Harit Kapoor: That would happen in this year itself?

Govind Shrikhande: Some part of it may happen by the end of Q4, but cannot really predict right now, we are working on it.

Harit Kapoor: On HyperCity, you said lower than MRP offerings did not really work as well. What were the promotions you are running and how you are taking it back or how is that working out?

Govind Shrikhande: If you look at HyperCity as a model, the overall positioning earlier was big store, big experience, in between we went into big store, big sales and we also realize that there are competitors who are selling permanently on MRP less 5% or 8%. The big challenge that we clearly see in this business is a lot of customers come to us for the monthly shopping but they are not coming in for the top ups. So typically a customer should normally shop with us at least twice a month, but majority of them are shopping only once in a month. So, we tend to be losing the top up opportunity completely. Why is the top up opportunity being lost is because we are mostly in malls in which to do a top up of Rs.300 or Rs.500 or Rs.1000, it is not looking worthwhile for the customer. So we thought that okay by making the offering sweeter in terms of price point can you make the customer come back again and again. That is why we tried MRP less discount offering in four or five stores, but did not really help us in getting the volume back, in fact, we lost out on margin. That is what you can see there. So we are going back to our original thought process that create a great experience, create a great assortment, and continue to focus on your positioning rather than looking at what the competition is trying to do.

Harit Kapoor: On HyperCity, what is the store addition plan now?

Govind Shrikhande: One is open today in Noida and another is coming up in Delhi in Q4 and then there are addition of two stores for the next two years we have signed.

Moderator: Thank you. The next question is from the line of Manish Poddar from Motilal Oswal. Please go ahead.

Manish Poddar: Just wanted to get some clarity on the online bit. You mention that 10% of your sales would come up from online in the next 3-years and you want to take a private label share to 35% over the next 3-years, right?

Govind Shrikhande: Private brand plus exclusive brand.

Manish Poddar: So what is the strategy actually for online – are we going to push up more of a private label and the exclusive brands out there or …?

Govind Shrikhande: Just to clarify, really what is happening is, if you look at the online space there are three of four kinds of players there -- there is one player which is market place which is Myntra, Amazon, etc. There is Jabong which is a brand play or a retail play but not really a market place play. Third is players like us who have online play as well as a physical store play. What we are trying to do is we are extending our offering of the physical store on online. So, we are basically offering the customer omni-channel option. It is not a different store, it is not a different offering, it is the same offering may be slightly more deeper assortment than what we have in the store because a store would have physical limitations. So it could be slightly extended offer there, but fundamentally we are leveraging our physical store with online store and expanding our channel.

Manish Poddar: Is there a possibility that the online players are also getting their products in the offline channel accordingly?

Management: Some of them are already doing it. If you aware, Pepperfry is having a physical presence in our stores of HomeStop, two of them.

Manish Poddar: We are not seeing with the larger players. Are we in talks with them?

Govind Shrikhande: As of now we have not really seen Amazon or Flipkart or Snapdeal wanting to go physical in India although Amazon is talking many strategies of going physical in US, I have not really heard anything in India as of now.

Moderator: Thank you. The next question is from the line of Abhishek Ranganathan from Ambit Capital. Please go ahead.

A Ranganathan: A couple of questions; one is where you mentioned on the like-for-like growth for high double digit growth for the third quarter compared to last year third quarter?

Govind Shrikhande: Yes, that is right.

A Ranganathan: What would that number be if I were to combine the Q2 and Q3 of last year versus maybe just Q2 and Q3 of this year?

Govind Shrikhande: I would say we should still end up at that 8-9% like-to-like growth plus.

A Ranganathan: So there would be two things which would be contributing to this – one is the shift of the Dussehra and second is also last year the base was quite low?

Govind Shrikhande: So last year if you look at it Q2 was double-digit and Q3 was flat.

A Ranganathan: So that is when all the “Big Billion”, etc.?

Govind Shrikhande: Correct. So this year the positions are reversed.

A Ranganathan: On the private brands, the share has come off. Is it also because of the fact that you said you will be rationalizing your private brands count?

Govind Shrikhande: Correct, we are rationalizing assortment, we are rationalizing number of brands that we have and we are also relooking at the positioning. So it will take according to me two quarters for us or maybe three quarters of us to get everything aligned better. In the meanwhile, we are trying to raise the exclusive brand share higher. If you see that, exclusive brands have been growing well and we have further added one more brand and we are also targeting to add two more brands by Q4.

A Ranganathan: The reduction in private brand share could be attributed to the reduction in assortment largely. Is that how we read it?

Govind Shrikhande: Assortment as well as correction or exit of one or two of those brands. Because I cannot exit overnight, it will take me some period to exit a particular brand out of all stores.

A Ranganathan: The reason of gross margin is primary just one week of sales, the reduction of one week of sales, how would we see – it is quite a steep jump?

Govind Shrikhande: Lesser discount directly helps you, #1; and #2, yes, some positive growth in the private brand margin as well. Although the share has not gone up, the lower discounting does help it.

Sanjay Chakravarti: The exclusive brand share has gone up. So that also kind of helps.

A Ranganathan: But otherwise, no one-offs in this quarter?

Sanjay Chakravarti: No one-off there.

A Ranganathan: With respect to your portal, I have already seen it is looking a lot different and lot better. In terms of cataloging cost and so on, all the investments are being made, are they expensed out or are they being capitalized, how are the expenses being accounted for?

Govind Shrikhande: There are costs that can be capitalized and there are costs that cannot be capitalized. So, some of the costs like the cataloging, etc., they are operating cost, so they will go into operating cost. The investment in CAPEX is basically the software that you buy, the licenses that you and the hardware that goes along with it. So it is typically the normal treatment, whatever is CAPEX will be stated as CAPEX treatment, whatever OPEX will be treated as OPEX.

Sanjay Chakravarti: The thumb rule is that what is at the front end that is facing the customer on the website is typically OPEX. What is at the back end which is behind the website, which the customer cannot see, is typically CAPEX.

A Ranganathan: On the festival portion of it, Dussehra sales have been here. What are the like for like sales looking like for this Dussehra to last Dussehra?

Govind Shrikhande: It is high double-digit, I do not want to quantify the number, but it is a very strong like-to-like double-digit growth, you can surmise from my statement that if Q3 and Q2 combine together, it is still going to be 8-10% plus like-to-like growth, really is a very-very strong growth.

A Ranganathan: On HyperCity, there is no impact of eCommerce on the business and just…

Govind Shrikhande: I did not say that for Hyper actually, because Hyper what we are seeing is the Hyper local business does impact specifically in certain catchments, especially in cities like Bangalore, where travel time is really becoming very-very painful, we are seeing some impact there, but it is not really eCom, it is hyper local.

A Ranganathan: **I**t is an alternative…?

Govind Shrikhande: Correct.

A Ranganathan: You are seeing impact of that but are you able to leverage on the same even if the hyper locals are able to use your stores or is just that the hyper locals are happy to use any of the stores around and…?

Govind Shriikhande: No, one of the strategies we are working upon and we are trying to leverage hyper local player like ZopNow right now in Bangalore, we are already leveraging that, we also plan to leverage it across other cities over the next two quarters period. So, the only way as we keep on saying is we cannot keep on fighting what is the trend, you have to join the trend, and so we will join the hyper local trend over this quarter and the next quarter.

Moderator: Thank you. The next question is from the line of Amit Kumar from Investec Capital. Please go ahead.

Amit Kumar: Just a question on this tax rate all over again. You seem to indicate that impairment is not being allowed by tax authorities, but what we are seeing is a very high tax rate for the last couple of quarters really. I would presume that even if the normal sort of depreciation on those assets, which would I presume will be allowed, you should see your tax rate normalized to the 33-34% sort of levels. When do we expect to see that?

Sanjay Chakravarti: I will give you the background; the background really is we are at a maximum marginal rate of tax because the Retail industry does not have any tax sops as you are well aware. The extra 7% that you have seen is really a disallowance of the interest component of the ratio of investments in group companies divided by the total assets in the balance sheet. This is a particular disallowance section called Section 14A in the Income Tax Act which disallows that portion of your interest cost which is on the ratio of investments in group companies divided by total assets. So even as the investments in our group companies reduce by way of equity and preference and our PBT keeps going up, which is the denominator, in the next one to two years, you should see the tax rate coming down to the 33% to 34%.

Amit Kumar: I am not sure I understood, but let me take this question offline. My second point is that this private label share piece, I was looking at last year's presentation. This number was about 17.1% as reflected in last year's…

Sanjay Chakravarti: That included exclusive rights.

Govind Shrikhande: It was a combined number. We have started splitting it into two now, showing you both private and exclusive separately.

Amit Kumar: My next point is that when I look at the Shoppers Stop and HyperCity financials as reported, so PAT in both of these have declined. But when I look at the consolidated PAT, that has actually grown. So, could you just highlight which particular business unit is sort of driving this?

Sanjay Chakravarti: That is essentially on account of the minority interest being added back.

Amit Kumar: No, I am not entirely sure, because even when I look at the PBT numbers for both HyperCity as well as standalone, they have declined much sharper than the consolidated PBT and PBT will not include the minority interest piece of it. So, any sort of business unit besides…?

Govind Shrikhande: Two businesses that you cannot see the numbers – one is Nuance, airport duty-free business but the numbers are small, and the other is Crossword, which has seen a very-very good improvement in its EBITDA and PPT. That is what is impacting post minority interest, PAT changing from 3.7% to 7.6.

Sanjay Chakravarti: Therefore, the lesser degrowth in PBT as you said preminority interest.

Amit Kumar: Crossword you talked about in the last couple of quarters as well, but Nuance piece is this a sustainable trend, was there anything…?

Sanjay Chakravarti: Nuance, it is a one-off write-back that the business has seen which has kind of given a fillip to that business, this is not a sustainable number.

Moderator: Thank you. The next question is from the line of Nilay Shah from Morgan Stanley. Please go ahead.

Nilay Shah: On your eCom bit, how much of the fulfillment will happen from the stores upfront?

Govind Shrikhande: Not right now, Nilay. So fundamentally we are taking it as three stage; the first stage that we are right now doing is getting the online better; second stage when we have executed our warehouse management system which will connect the warehouse, store, pick, pack station, everything then you can also do the click and collect and fulfillment as well.

Nilay Shah: So as of now it is going to come from the warehouse?

Govind Shrikhande: Warehouse or from pick pack station, fulfill by the store but not directly picked from the store.

Nilay Shah: Your logistics ability at the store, is it sufficient to handle eCom number that you are talking about?

Govind Shrikhande: Not right now, right now we are not doing any logistics from the store to the customer.

Nilay Shah: So the fullness of time will there be some changes required out there, and if yes, how much CAPEX is required for that?

Govind Shrikhande: So, overall 24-month period what we said is there are three phases that are happening; first phase is Hybris which is getting site better; second is WMS which is the Warehouse Management System; third is the Master Data Management. So between the three we are also ensuring that the infrastructure at both store level, warehouse level, and pick-pack station level, keeps on improving. So 2017 Jan is when we will be really omni-channel and the total investment is about Rs.60 crores over the sale over this 24-month period.

Nilay Shah: On your exclusive brands and private label, as you increase your percentage contribution from this channel, what is the impact on your working capital that we should forecast going forward?

Govind Shrikhande: Should not impact dramatically, it also comes with a larger credit period and if you improve efficiency of throughput should not be really big because the gross margin change is much-much higher.

Nilay Shah: Sure, but the inventory levels?

Govind Shrikhande: So that is what I am saying. If you look at current gross margins at overall level versus gross margin of private brand, the gap is almost 10%, and even if your working capital cost goes up by 2% the net-net impact is much-much higher.

Nilay Shah: But it just brings in more risk to the business, that is it?

Govind Shrikhande: That is right.

Moderator: Thank you. The next question is from the line of Pankaj Tibrewal from Kotak Mutual Fund. Please go ahead.

Pankaj Tibrewal: A couple of questions; when you assess your margin trajectory performance and the thought that you want to move to 8% kind of margins, Shoppers FY17 now we are standing in the first half almost completed, how do you assess the performance on the margin side over the last 3-4-quarters and what needs to improve, what do you think you have done a lot better and how is the trajectory looking like, first? Second thing is if I replicate the same question to your HyperCity where earlier you guys have thought about PAT breakeven somewhere next year, how do you assess that situation in the light of what it is today again where you have slipped on the profitability? So two questions on the margins.

Govind Shrikhande: So, let me first handle the EBITDA on the Shoppers Stop Limited part. If you look at the EBITDA in Q2 definitely, there is improvement from 5.9% to 6.3%. In Q1 we were actually lower than the previous year's first quarter. But biggest contribution on EBITDA growth actually comes in Q3 because of the festive season, where the top line grows well and there are not any discount. So I would say we should assess it post Q3 number, but I believe we are on the right track towards moving to that 8% number in Shoppers Stop limited and further levers to that should be the share of private brand and exclusive brand, split on that in this quarter and I believe that we will only catch up post-Q4, most probably we will catch up on the share from Q1 next year which should further give fillip to the direction of growing the EBITDA percentage number. So overall, I would say pretty confident that we are tracking on the right direction may be a quarter or two behind as far as Shoppers Stop is concerned.

Pankaj Tibrewal: The store openings which had impacted us last year and a year before that, should have actually been a margin positive lever again in the first six months and going forward. But somehow that is not getting reflected out there somewhere. So can you help us understand what is really pulling it down further?

Govind Shrikhande: No, so right now it is not pulling it down. If you look at Q2 number, actually half over last year because all the new store additions that are currently happening are not impacting the EBITDA margin because they are starting contributing either to zero or positive EBITDA, they are not bringing it down further and all the store openings that we have done throughout this year are still tracking on the similar side. So, we believe that the kind of openings that we are doing and the kind of numbers you are tracking should be margin-decretive. They will either contribute to margin or going to be positive. That is the way to look at the further progress on it.

Pankaj Tibrewal: As I understand there is no need to revise that thought process of 8% margin as of now as we stand today?

Govind Shrikhande: As I mentioned may be a quarter or two behind, but directionally, I think we are on the right track. As far as Hyper EBITDA to EBIT to PAT is concerned, we had said about six quarters to hit PAT and about three to four quarters to hit EBIT, I would say we are two quarters behind now. So from today also I would say that we are still chasing five quarters for EBIT and about seven quarters for PAT.

Pankaj Tibrewal: And the slippage is mainly on the …?

Govind Shrikhande: On the top line. The challenge in this business has been our consistent improvement if you look at over the last four or six quarters, very-very good improvement in terms of cost control and very good growth in share of fashion which is directly leading to margin growth, but we have not really grown as much in the top line which is now the prime requirement to really take off the EBITDA to the next level.

Pankaj Tibrewal: But is it now reflecting on the gross margins for you because if your mix is improving at some point gross margin should also be…?

Govind Shrikhande: So, you can see on the gross margin level 20 basis points drop actually you are saying in this quarter whereas if you look at it for the first half you are actually 10 basis points up, Q1 also we had improved the margin, Q2 we have seen definitely a set back and we believe that to get it recovered it will take us another quarter or so. So Q4 onwards we should start tucking back.

Moderator: Thank you. The next question is from the line of Prashant Kutty from Emkay Global. Please go ahead.

Prashant Kutty: Just wanted to understand what is the difference in the gross margin on your private labels and for the exclusive ramps?

Govind Shrikhande: So, private brand margin typically would be 50% plus, exclusive brand would be anywhere between 45% to 50%.

Moderator: Thank you. The next question is from the line of Harit Kapoor from IDFC Securities. Please go ahead.

Harit Kapoor: Just a few follow-ups; just wanted to check with you any more property auction sales in this year which we are looking at for Hyper?

Sanjay Chakravarti: Hopefully, Harit, difficult to quantify at this stage, currently not on the radar, those are around priority for selling on the real estate side of business, but as of now we do not really have clarity on that.

Harit Kapoor: Any more store closures in Shoppers that you have planned for as of now?

Govind Shrikhande: We are actively looking at two in the second half.

Harit Kapoor: So basically the net addition would be two stores if those to happen basically?

Govind Shrikhande: You are right, for the second half.

Harit Kapoor: On the HyperCity business, assuming that the deflation or lack of inflation is there over the next 12-months as well, the pricing growth in food and FMCG will not be there to that extent. So do you see that as a concern or a challenge in order to get some issues of operating leverage on the EBITDA level in HyperCity?

Govind Shrikhande: So, when the year started we were actually aware of this challenge that if inflation does not continue, we will have to really drive volume up. And that is why we did some experimentation in trying to drive volume up, but we were not successful. I think we will go back and attempt it. But, I am not sure about inflation being content even in the next year**.** When inflation is directly linked, primarily, one is to the oil price and then various other commodity prices. I think the cycle my mind… I am not a predictor of commodities but my guess is by April-May inflation should start coming back. The rains have been weak this year and they should directly have an impact in pricing of products.

Moderator: Thank you. As there are no further questions from the participants, I now hand the conference over to Mr. Govind Shrikhande for his closing comments.

Govind Shrikhande: Thank you, Friends for joining in the Q2 Con-Call. Looking forward to a great Q3 and Wish All of You and Your Families A Very-Very Happy Diwali. Enjoy but carefully.

Moderator: Thank you very much members of the management. Ladies and Gentlemen, on behalf of Shoppers Stop that concludes this conference call. Thank you for joining us and you may now disconnect your lines.