



“V-Guard Industries Limited
Q1 FY2021 Earnings Conference Call”

July 28, 2020



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Moderator: Ladies and gentlemen, good day, and welcome to the V-Guard Industries Q1 FY2021 Earnings Conference Call, hosted by ICICI Securities. As a reminder, all participant lines will be in the listen-only mode and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing ‘*’ then ‘0’ on your touchtone phone. Please note this conference is being recorded. Please note that the conference is being recorded. I now hand the conference over to Mr. Hitesh Taunk. Thank you, and over to you, Sir!

Hitesh Taunk: Thank you, Ayesha. Good afternoon to everyone present in this call. ICICI Securities welcomes you all to the Q1 FY2021 earnings call of V-Guard. From the management, we have with us today, Mr. Mithun Chittilappilly, MD; Mr. Ramachandran, Director and Chief Operating Officer; Mr. Sudarshan Kasturi, Senior VP and CFO. I now hand over the call to management for their opening remarks, post which you can take a question from the participants. Over to you, Sir!

Mithun Chittilappilly: Thank you, Hitesh and ICICI Securities for hosting this call. A very warm welcome to everyone present and thank you very much for joining us today to discuss the operating and financial performance of our company for the first quarter ended June 30, 2020.

During Q1 FY2021, revenues declined by 42% Y-o-Y to Rs.406 Crores. Non-South markets declined by 47%, while south declined by 38%. Non-South markets saw a larger impact due to more extended lockdowns, whereas opening up in South saw progressively improved demand in states such as Karnataka and Kerala.

Similarly, all three product segments were impacted in the quarter marked by various stages of lockdown and disruptions. While electrical products were the least impacted electronics segment saw a sharper decline based on its linkage with larger appliances, which sees large demand and summer season like ACs.

Gross margins contracted by 334 basis points Y-o-Y to 29.2%, moving to lower capacity utilization and product mix. However, gross margin improved in each successive month and had reverted back to normative levels in June.

EBITDA margin for the quarter was 2.2% as compared to 10.2% Y-o-Y due to decline in turnover.

Profit after tax during the quarter was accordingly subdued at Rs.3.6 Crores. PAT margin contracted to 0.9% as against 7.5% in Q1 last year. While these headline numbers indicate



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the effect of COVID-19 pandemic along the expected lines we believe the business has demonstrated strong resilience in facing these extremely challenging times. We have put in place cost containment measures, which will partly offset the impact of loss of turnover.

Working capital has improved steadily as available inventory has been used to drive revenues. Collections were strong, and we have been able to reduce our debt to days, resulting in a total cash generation of Rs. 215 Crores during the quarter.

Even before COVID-19 pandemic, there was weakness in consumer demand based on conditions of tight liquidity and reduced discretionary spending. FY2021 had opened in difficult circumstances, but we believe that as the situation reverts to greater normalcy, we have the requisite framework to drive volume growth momentum by expanding further into non-South markets, introducing new and innovative products and entering additional product categories.

We have put in place best-in-class processes and systems to future-proof the organization and create the framework for a secular growth. We will continue to build upon our competitive positioning in the consumer electronics and consumer durable industry to drive value for all stakeholders.

On that note, I would like to thank you once again for your participation, and I would like to hand over the floor to the moderator for question and answers. Thank you.

Moderator: Thank you very much. We will now begin the question-and-answer session. **(Inaudible)** 04:40. Your line is on talk mode, you can go ahead please.

Unknown Speaker: Sir, I just wanted to check with you. In terms of demand from metro and non-metro, how different has it been for across the products? Second question is with respect to July demand, how it is panning out?

Mithun Chittilappilly: Ram, you want to take this one?

Ramachandran V: I think the non-metros have been better than metros. I think metros are impacted for various reasons. So I mean, that is the first question. Non-metros have been better than metros. I think that the early part of the lockdown, the non-metros have been operational formally, informally also it looks like based on the inventory level and the offtake that we have been able to observe. Coming to July, I think July is comparable to June, a bit better, actually. But what has happened is after about 12th or 13th right, many areas have gone into lockdown. So as an example, let us say that around 75%, 76% of the outlets that we serve



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were open at the beginning of the month and that has dropped to about 55%, 54% by around 17th, 18th, yes and this has now recovered around 23rd, 24th to something like, I would say, closer to 70%, yes? So that basically happened because many places progressively got added into the lockdown, right? Like Karnataka went in as an example or some parts of Maharashtra. So it is a very dynamic situation and even the outlet numbers are changing week-on-week and month-on-month.

Unknown Speaker: Got it, Sir. In terms of cost price, so basically, say, we had seen employee costs drop by around 10%. So was it a salary cut or something like which we have given to employees and how we look at employee costs for the year?

Mithun Chittilappilly: Sudarshan do you want to go for this?

Sudarshan Kasturi: We have not resorted to any salary cuts or whatever. We are saying, both on-roll employees and contract labor. On a full year basis, again, I mean, that call we will take perhaps in six months or eight months. For now we have held on to the increments. So there has been no cost increase, therefore, it is flat. We will review the situation later and see if we decide to give an increment or not. So we will know it.

Mithun Chittilappilly: The reduction could be because we are not paying variable pays because our targets are not getting achieved.

Unknown Speaker: Got it. In terms of ad spends also, how is it likely to pan out? Usually, we spend around 3%, 4% of topline mostly so?

Mithun Chittilappilly: See, that business is not back to normal. Even today, like Ram mentioned, we are serving only 70% of customers. So when business goes to normal at that time, we will review this. But as of now, we are not planning to spend I mean it is like bare minimum, as you can see, ad spend. I guess, it will be a very similar kind of a strategy taken by all peers.

Ramachandran V: Just one more point. The supply side is also very dynamic, right? So different areas get into containment zones for different suppliers or supply sources can get impacted and also the attendance is thin and weak, generally operating between 50% and 70% at these places. So I think marketers will take some more time before they own their purse because supply has to be streamlined also.

Unknown Speaker: My last question is with respect to commodity prices then softening. Will it be a big advantage to us in terms of gross margins and all these things?



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Mithun Chittilappilly: I do not think commodity prices have softened. Specifically, if you ask copper actually has shot up by close to, I do not know, some write offs figure, but thereabouts 20% increase in copper has happened. Plastic prices have come down. But unfortunately, when the prices were at it is lowest, we were not able to buy anything because of the lockdown. Sudarshan, you want to just explain this?

Sudarshan Kasturi: Next year, the copper prices have gone up and that sort of gets reflected in the wire selling price than we see in the next. Okay. Otherwise it is not much of an impact because the other materials do not make too much of an impact.

Mithun Chittilappilly: We have not seen huge reduction in commodity prices vis-à-vis let us take January or February, in other materials.

Moderator: Thank you. The next question is from the line of Renu Baid from IIFL. Please go ahead.

Renu Baid: Just to understand a bit more on the inventory side, you mentioned that as in, the company has pretty much used to inventory, which it had to drive revenues. So how would be the inventory across the channel partners also and have we seen the channel partners starting to up stock again? Or they continue to remain a bit more averse on the pre-stocking trend?

Mithun Chittilappilly: Ram, you want to take this?

Ramachandran V: Yes. Yes. Channel partners today, I mean, inventories, what I would say, inventory has normalized, I would say, a little lower than normal. I think on an average, what we are observing is inventory would be down to about 30 days, including we are looking at our, I am talking about a total channel inventory, which is a bit lower than normal because this includes the direct and indirect. So yes, they are thinner than what they would be before. But I think this is also how they are operating now compared to the way they were operating before.

Renu Baid: Sure and Sir, based on the fillers that you have from the market in terms of consumption patterns, what is the expectation of we getting back to normalized 100% levels as last year's? Or should festive season be the next catalyst for demand to pick up? Or do you think the demand trends have been much more significantly impacted from a medium-term perspective?

Mithun Chittilappilly: See, I think we are in a position where we are not able to predict. Please understand this is a health issue. So without a health solution really neither me or Ram or Sudarshan will be able to give you an answer on this. It is really depends on when the country is able to tide



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over this crisis together and the markets one by one can open fully. Every day, every district is a different case. So it is very volatile in that sense. So it is very difficult to make any kind of prediction. Ram, if you want to add anything to this?

Ramachandran V: No. I just wanted to say the same thing. For example, we started this month, and we were feeling that it would go well and then one by one, the lockdown started to get announced and the number of outlets that which we could supply shrunk by 30-odd percent, right and then now we are seeing from 23th to 24th, the outlets are coming back, right and we can see the consequence of the directly in numbers coming through, yes? So I think...

Renu Baid: So what I was also trying to ask was that probably in the next couple of months or by the end of 2Q is the situation normalizes...

Ramachandran V: No. That is what Mithun was saying. That is what Mithun was saying, right? See, it all depends because both the supply side and demand side picture is changing from time to time because it is not only a matter of demand, right? It is also a matter of supply.

Mithun Chittilappilly: So I think as you supplement, see Kerala had the best way of managing COVID in the beginning part of this pandemic, okay? But right now, we are hitting 1,000 to 1,500 cases a day. What it means is that no state can effectively manage this so whenever the cases go up, they will lock it down and then they will restart again from 0. So this process is going to continue over and over again till we have a vaccine. That is what I think. So we cannot really comment when we will go back to 100%.

Renu Baid: Sure. But in general, what has been the feedback or inputs in terms of the demand pattern, both from secondary as well as tertiary sales? Have they also moved in line? Or how is it?

Mithun Chittilappilly: Yes. So wherever markets are opening and cases are relatively lower and people are feeling relatively safe to come out, the sales are happening. So that is definitely there. We cannot really split this between what is the pent-up demand and what is the real demand, okay? That is the split, that none of us have. But what we can safely say is that 70% to 80% of last year's sales should happen provided we do not have a nationwide lockdown. This is what we believe. Certainly, so that is the broad number, I can say. It can go up, provided there are no localized lockdowns and stuff like that. It is really difficult to say. I mean we really cannot give you any guidance. That is the honest truth.

Renu Baid: Sure. Sir, I have couple more questions. I will get back in the queue.

Mithun Chittilappilly: Yes.



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- Moderator:** Thank you. The next question is from the line of Sonali Salgaonkar from Jefferies India. Please go ahead.
- Sonali Salgaonkar:** Sir, my first question is regarding the unfavorable product mix that you have mentioned in the presentation. Any more color you would like to add as to which appliances have led to the maximum impact on our gross margins?
- Mithun Chittilappilly:** So if you look at the stabilizer business is the most impacted because in Q1, we typically sell air conditioner stabilizers, and that pretty much has not happened. So they have taken the biggest hit, and it is a product with higher gross margin. So it has definitely pulled down overall gross margin for the company. This has been one of the biggest impacts.
- Sonali Salgaonkar:** Understand. My second question is, I understand that there is a lot of uncertainty in the overall demand and the business scenario. But any rough EBITDA margin you would like to point out as to what we should expect in FY2021? Any range, considering that the first quarter was quite lower than what we generally register?
- Mithun Chittilappilly:** See. I think what we have seen is that we have given in the analyst presentation month-wise gross margin for April, May and June. So that gives you some color that, that kind of a revenue in June, what we did, that kind of a gross margin is possible. That is all I can say as of now. Sudarshan, do you want to add anything to this?
- Sudarshan Kasturi:** Yes. That is all. I think if you are able to sell maybe 80% to 90% of last year, margins will look like that. That is the best we can say.
- Mithun Chittilappilly:** So I think if you are even to do 80% to 90% of last year, we could hit between 8% and 10% EBITDA margins, correct?
- Sudarshan Kasturi:** Yes. Something like that. Yes.
- Mithun Chittilappilly:** Something like that. But that is all we can say.
- Sonali Salgaonkar:** Understand. Sir, in our factories right now, what kind of utilization are we updating at?
- Mithun Chittilappilly:** Ram, do you want to take this?
- Ramachandran V:** Yes. Yes, I think wire factories are running full stream. So the electrical categories are having good demand, right, as I think Mithun outlined in his statement. So there, the capacity utilization is very good, yes and in the other cases, the utilization is in line with normal business requirement at this stage because what we did is our focus initially in the



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first 2 months was to make sure that we collect all the moneys, and our cash position gets better. So our focus, I would say, in May and June, was primarily towards collections and that we have been able to get to a reasonably decent place and mostly, therefore, we are focused on utilizing the available inventory on hand and our factories have started somewhere around middle of June, barring the wire factories. So what I would say, June, July, their run should be okay. It should not be an issue, yes?

Mithun Chittilappilly: So we are basically supplying to whatever demand that is there. We are not going to produce and then force the sales team to sell. So that is what I think the basic point is.

Sonali Salgaonkar: Thank you.

Moderator: Thank you. The next question is from the line of Achal Lohade from JM Financial. Please go ahead.

Achal Lohade: Yes. My first question was with respect to in terms of the demand pattern, are you seeing any down-trading in general, in the industry as well as for our product and two, are you also seeing any disruption in the unorganized industry?

Mithun Chittilappilly: So as of now, we cannot get any clear trends on down-trading. Like Ram mentioned, one of the products that is selling very well as wires, where we only have really one or two SKUs in terms of pricing positioning so really, we cannot measure that. We have not seen that premium product is not selling and non-premium product is selling. We have not seeing that kind of a trend. Sales are secular in that sense. I think we have to understand that what is right now happening is a pull demand. That means actually, retailers and distributors are calling us for stocks and then we are supplying. We are not shoving anything down the pipe or channel. So what we believe is, what we are supplying to is kind of like the normative demand. That is the first part of the question. So no, we do not have any evidence of down-trading as yet. What was the second one?

Achal Lohade: With respect to the unorganized industry?

Mithun Chittilappilly: Yes. In the case of wires and cables, definitely, we are feeling that there is an absence of the unorganized industry and definitely, all the brands are benefiting as of now. Yes. That evidence is there. Yes.

Achal Lohade: And in the other product categories, Sir?

Mithun Chittilappilly: No. No evidence.



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Achal Lohade: No evidence. Got it and the second question was with respect to the debtors, I see that Q-o-Q we have seen a reduction in the inventory. Can you help us with the channel financing which was as of March 2020 and June 2020, could you please help us with that?

Mithun Chittilappilly: Sudarshan?

Sudarshan Kasturi: Between March and June, there is not much difference. It is about the same.

Achal Lohade: Would you be able to help us with the quantum, Sir?

Mithun Chittilappilly: Reduction in debtors is an actual reduction in debtors, not because of channel financing if that is what it is. I think it is actual reduction in debtors.

Achal Lohade: Sure. Would you be able to give the quantum, what is the channel financing outstanding as of June?

Ramachandran V: The outstanding?

Achal Lohade: The channel financing done as of June 30, 31?

Mithun Chittilappilly: What is the total book of channel financing?

Sudarshan Kasturi: Total outstanding will be about Rs. 80 Crores or Rs. 90 Crores.

Achal Lohade: Thank you.

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

Mayank Bhandari: Sir, I wanted to understand, particularly the consumer daily life. How has been the growth in different categories, like fans, kitchen appliances and considering that we have a low base, the growth looks I mean, this is a pretty sharp degrowth given that other competitors have given good commentary in terms of kitchen appliances, air cooler and fans?

Mithun Chittilappilly: Ram, do you want to take this?

Ramachandran V: Yes. I think we, as Mithun said, see, we are not aggressively pushing numbers into trade at this time. We are just feeling whatever demand is coming from the market, yes and across channel, our inventory is a little lower than desirable in our key markets, yes, particularly south, yes? So that is the situation. Second thing is, yes, you will generally see a trend in



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this environment that what I would say as leading brands and brands which withstand depth of distribution will have some advantage over the other brands. That is the second point. The third point we want to make is, by and large, our performance is similar to others. Maybe it is possible, the weightage of e-commerce in some of our newer categories is not comparable as they are slower to enter e-commerce compared to, let us say, a stabilizer or a water heater. So I think whereas in some of the players where you might have sense better demand in kitchen and all, they have a stronger presence in e-commerce. Also, kitchen and all is a category also has a stronger presence in organized retail also, okay? So I think those influences are also there, yes, in the overall number, yes? But I think by and large, we will not be way off.

Mayank Bhandari: Sir, any other cost-saving initiatives, apart from the employee cost and the advertisement expense?

Ramachandran V: No. By and large, like anybody and everybody in the marketplace, right, the cost sets are same across companies, yes and we are focusing on these cost sets, whether it is what, I would say, establishment costs like rent, travel, yes, or whether it is what I would say as people and stuff like that.

Mayank Bhandari: Yes and anything else which is discretionary in nature is...

Ramachandran V: So whatever is discretionary in nature, we are tackling, yes?

Mayank Bhandari: Okay and lastly, Sir, what would be the capex? Any guidance for capex to this year?

Mithun Chittilappilly: Sudarshan? This year capex?

Sudarshan Kasturi: See, right now, other than essential capex, things are on hold. We have got a couple of plans to finish. There is not too much of outstanding things left other than certain IT, infra and things like that, we do not see much capex happening at least.

Mithun Chittilappilly: See, we may have a capex for a wire plant, that is about Rs. 15 Crores to Rs. 20 Crores and then probably another Rs. 10 Crores of IT and all that so maybe Rs. 30 Crores, Rs. 32 Crores Rs. 30 Crores, Rs. 35 Crores of capex would happen at the max.

Mayank Bhandari: Thank you.

Moderator: Thank you. The next question is from the line of Bhavin A from SBI Mutual Fund. Please go ahead.



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Bhavin A: Mithun, just one question from my side. Given the current pandemic what is it that you are doing differently, which will help the company improve more on a structural basis and if it would be interesting if you could talk about the investment that you will be doing in terms of people which would be difficult to hire in other circumstances or the investment in research, development, innovation, will be helpful to know your thoughts on this?

Mithun Chittilappilly: So we are working on a digital workplace as a concept, we have got started from 2 years back. So we started with world-class VC system. We started with a world-class integration of VC system with Teams, Microsoft Teams. Then we invested in something called Degreed which is a learning platform, which can be used for both company-created content and external paid content as the manager, so we shift. So we have invested a lot of tech, not knowing that this pandemic is coming in our way and now we are actually using a lot of that. We have constant training programs for not only our own employees, but even for key channel partners and their staff on how to sell particular product to customer, technical selling. So we are using this time to beef up those kinds of activities because there is absolutely no visibility on when people can go visit the market, whether it is safe to visit the market and all that so all the work is done over phones and videoconferencing. So I think we will probably accelerate that journey into a digital enterprise a little faster. I mean we had put some milestones, but COVID has forced us to fast track some of those milestones. This is one side. In terms of people hiring, I think from 2015 to 2020, we have hired quite a lot of people, and you will see our ballooning of employee cost that has happened. So I do not think we need to hire any more key resource. Not a lot of people and positions are left to be filled, in my view. There are very few and far between, which when we find the right resource, we will take them on board. The second is on e-commerce. We started the journey on e-commerce 2 years back, and now we are getting very good traction. Our margins on e-commerce are far superior than what we do in any other channel, and it is growing very, very fast and we have even launched certain products where e-commerce is the first channel of choice and we only will launch them in off-line much later so all these experiments are working well. I will also ask Ram to supplement anymore to these comments.

Ramachandran V: So actually, we have been having a long-term journey for organizations capability building, yes? Much of the focus in the last 5 years has been on the supply side, yes and mainly, we have been working on cost. We have been working on in-sourcing manufacturing, yes and we have also been working on working capital, yes? So that is been our work and there are some proofs related to that, which we should be able to capture over a period of time. But more than the financial benefit or the capability that is getting built, these are also built on robust digital friendly, what I would say, tech ecosystem, yes? So I think that a lot of focus in V-Guard has been on this over the last 5 years, and which I think may be another year or 2, we will continue so that our work on the supply side there will be complete and



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comprehensive, yes? We have commenced work on the market side, fundamentally, to help us to build leading capability on the market side, where we are trying to embrace the technology into our, what I would say, marketing process, yes and this work just we started about 6 months back before the lockdown has started. That is something that we will continue over the next 3 to 4 years. These are like long-term journey and fundamentally, what this journey is doing is helping us to deep rouge our capability, whether it is manufacturing, whether it is products, yes, whether it is go-to-market, yes? It is fundamentally building leading capabilities in this area and also, what it is doing is, this is all being accompanied with the road map for the enterprise digitization that Mithun was earlier referring to, yes? The near-term benefit of enterprise digitization is basically connecting the organization for employee productivity, which I think we outlined and the long-term business will be related to some of the areas that I talked about. So we have a pretty robust program. I mean this is a program which has been on for the last 4 to 5 years, and we have a road map for the next 3 to 4 years and we are busy focusing on that, and we are busy putting that in place.

Bhavin A: Thank you.

Moderator: Thank you. The next question is from the line of Akshay Bhor from Premji Invest. Please go ahead.

Akshay Bhor: I actually wanted to understand a little on the historical performance. If I look at pre-COVID about 4 to 6 quarters, the performance has been slightly tepid, both as compared to your own historical performance and then even with respect to peers as well and this is in light of very good summers last year should have been favorable to some of the portfolio, and then the winter as well. So I just wanted to understand what is it that is kind of how can we attribute this performance, what can we attribute and within that, specifically, is there any component of competitors, new competitors that are coming into especially in the Kerala market that you have pointed out sometime in the past, any color would be helpful?

Mithun Chittilappilly: So see, what has been happening is, I think, post demon and GST, the market growth had slowed down significantly for all players. So every company in India was getting into every product category and we also got hit in that mismatch, wherein which maybe 20, 30 brands and the water heater business, which is a Rs. 1,500-Crores category and then the same thing happened with even stabilizer. I am told that Philips also now has stabilizers. So people started looking at companies with decent margin and they have started entering categories. I should not be talking about it because we have also entered a different category. But the thing is when everyone in the market tries to enter every category, there is going to be a blood bath and that you will see not only with us, in time, you will see with other



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companies as well. So yes, there is a period where we had to show restraint, not react by dropping price and all that. We have lost share also. We have lost revenues also. But our margins are intact. I think after 4, 5 years, many of these people will leave. I mean, again, you will hear about many of these companies getting into trouble also. I do not want to specifically name them, but we have some companies who are into batteries that got into kitchen appliances that got into trouble. So stuff like that, it keeps happening. So we cannot really stop competition. It is a free country. Anyone can do pretty much anything. So we are not really worried about 1 or 2 quarters. But if you look at last 5 years, we have worked significantly to improve our gross margin and this has also happened because we chose to do where we will do business. We chose to walk away from categories. So we have shut down a loss-making power cable business that was doing close to Rs. 90 Crores 6 years back. We have shut down agricultural pump business that was doing Rs. 40 Crores 5 years back. So last 5, 6 years, we have also restructured a lot of our portfolio to have a sharper focus, which what does it mean is that, yes, year-on-year, you will not see such great revenue growth, but our business is very healthy, and we are more sharper focused and it gives us bandwidth to go after categories that are of better margin profile. Ram, do you want to supplement to that?

Ramachandran V:

Yes. A couple of things. So I think we have to see the macros also. So if you broadly look at the macros, see, the nominal growth, which used to be at around 14-odd percent, has dropped to about 8% to 9%. That is on one side. On the other side, if you look at the last 4 years, a significant part of this growth has happened on e-commerce and organized trades, yes? I think we have been led to enter e-commerce and organized trades on one side. The other side is, while the nominal growth has almost come down by 40% and part of the remaining growth has gone into organized trade and e-commerce, in the remaining part of the market, a lot of people have entered, which is what Mithun has been talking about, right and mainly, we have been focusing on the traditional trade as a company and if this macro is understood, I think the performance would seem as strong and as good, okay? Because when 30%, 40% of the growth is happening outside the area that you focus, right, and you have not participated in that adequately. Because, as Mithun said, right, last few years, we have been working on building capability, and we are not very happy now that we have the right, what I would say, we are in the right place to scale up and therefore, because it is required a lot of preparation. So that is one context I would like to bring to your notice, right? Second thing, I would like to say is, post the demonetization and GST, right, the companies, which we used to be an outsourcing company, yes, most of our business was outsourced. So when we move from outsourcing to manufacturing, right, our competitiveness got impacted to the extent of about 4%. So that the outsourcing gave us the advantage to be able to compete with people who had strong and deep market positions and which is why you will see now that progressively, in the last 3, 4 years, we have gone in for



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in sourcing manufacturing to the company, yes? So I think this period also a period where we have overcome this challenge where we lost this competitiveness, and we were able to restore our margins and hold and improve our margins in this environment because it meant that relatively, we have to improve our price positioning in the marketplace, yes and the 4% is a huge, huge impact, yes? That is the second thing. The third thing is, we have been focusing on making sure that we are able to generate and convert our profitability into real cash, yes and you would see that in our books today and you will also see that much of the capex investment that has happened where we have set up 5, 6 factories over this period four or five factories over this period, and some of them are work in progress, this is the consequence of our ability to generate cash in the business, yes? So our focus has been fundamentally to make our business strong and robust, make sure that we become healthy, and our gross margins are protected and improved. I think we have improved our gross margin to the extent of around 6% to 8% over the last 5 to 6 years. Half of it has gone back into the business in terms of investment, right, to meet the cost on people that we have added and the investment that we have made on the technology side, right? So we are putting money back into the business so that we become strong and we become competitive, yes? So we have invested in manufacturing capability and R&D and product design and development, yes and the fruit of this will be visible over a period of time, right? So...

Akshay Bhore:

This is a very detailed and candid as well. Just a quick one, if I may? On the margin front, the EBITDA margin front, any aspirations that you have? I have seen your gross margins have seen a very smart improvement last year, any targets and also, if you could indicate what is the price differential in the non-South region now, which you used to indicate earlier, anything on that front would be helpful here?

Mithun Chittilappilly:

See, we had earlier stated that we would like to hit 10% and then improve 0.5% EBITDA every year. But this is at a time when sales were at a normal run rate. Today, sales this quarter had grown by 60% of what it should have been. So it is very difficult to say that. So the gross margin will get converted in the EBITDA margin the moment sales at 80% to 90% of the usual business, and which I think it has happened in the month of June, and we are hoping that it can happen going forward. That is as far as the EBITDA margin is concerned. What was the second one?

Akshay Bhore:

I am trying to understand the pricing differential that you used to talk about in the non-South...



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- Mithun Chittilappilly:** Okay. We now do not have much of a price positioning difference between South and non-South. We have kind of normalized. I would say it is very negligible. Sudarshan, you want to add anything to this?
- Sudarshan Kasturi:** Yes. The prices of South and non-South more or less are the same. There could be some tactical schemes here and there that we run, but otherwise, there is not much difference that we speak about.
- Mithun Chittilappilly:** Yes. For example, there are some markets in non-South which mirror our margins in South or probably better in terms gross and EBITDA, yes.
- Akshay Bhore:** Thank you.
- Moderator:** Thank you. The next question is from the line of Charanjit Singh from DSP Mutual Fund. Please go ahead.
- Charanjit Singh:** Sir, now you talked about market share changes, which you would have seen over the last couple of months and now also in this recent quarter. So can you highlight any major segments where we would have lost or gained share or region wise, we would have seen the intensity much more significant in any particular product segment if you can give color on that aspect?
- Mithun Chittilappilly:** Ram, you want to take this?
- Ramachandran V:** No. You mean last couple of quarters? I think nothing particular. I think from time to time, we see aggression in different categories, yes? So we have seen more intense activity in stabilizer sometime, sometime we are seeing it in water heaters there. But before that, sometime we saw in wires, sometimes it is geographic, yes? But usually, what happens is then, of course, we, of course, try to protect our interest, yes? But in the reply that comes with a lag. So I think these are some major categories which have impact on us and where we have witnessed these kinds of issues and usually it is geographies. I mean, in one of his strong pockets, we see this coming up. But it takes once we sense that it is getting strong, I think we react but then will lose some time in the process here but nothing sustainable.
- Mithun Chittilappilly:** So I think let me answer it in this way. We decided that we will not buy market share by giving discount. So let me put it that way.



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- Ramachandran V:** So we block. So what happens is we block. So we will block if we find that the action of someone is hurting us, so we will block that in that place, yes? But then in that place, yes, yes.
- Akshay Bhor:** Okay and Sir, in the last couple of quarters, we have been working on our product portfolio, upgrading it, more feature-rich products and now with the COVID scenario and a lot of fears in terms of down-trading and the kind of sales which are happening, so how do you see the reaction to our product portfolio, which could be more feature-rich and more towards the profitable segments, which we had moved earlier?
- Mithun Chittilappilly:** So we have completely revamped our NPD process, and we have a very, very clear strategy in place. It follows from the automotive strategy of standardization, simplification and platformization. So the chassis will be the same. The Belgium Whistles we can add. So if someone does not want the Belgium Whistles we can remove and sell it at a lower price. So this gives us the flexibility to create a platform and then make it into a super premium product or a super economy product as the case maybe.
- Akshay Bhor:** Okay and Sir, lastly, on the channel mix front, how is our channel mix, e-commerce versus a wholesaler driven or direct distribution, how is the mix and how do you see now with a lot of technology investments which you have done, do you think that channel mix can change in the favor of e-commerce significantly and which product segments are you seeing more traction on the e-commerce platforms and how is the pricing differential in that, yes?
- Mithun Chittilappilly:** So Ram, you want to take this?
- Ramachandran V:** Yes. So I think you can look at it at company level or related category level. I say related category because if you eliminate some categories like wires, switches, switchgears, pumps, right? These are not e-commerce friendly category. But otherwise, at a company level, we would be at maybe 2% to 3%, closer to 3% and at a related by category level, we will be about 5% to 6% today, yes? But this is growing fast because the fundamentals are in place, and we have tested that over the last 2 years, yes and as we are able to bring more offerings in, we expect to see traction. Obviously, the traction will be more in categories where we have historical strength. So typically, you will see a stabilizer or water heater getting a pan or kitchen getting good traction, yes? So I think, obviously, in order of our strength in the different categories, yes?
- Akshay Bhor:** Okay and Sir, in terms of wholesaler versus retailer?



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- Ramachandran V:** So we are not generally a wholesale focused. So see, mainly, we have been focused on inform category that is distribution, yes and what we are doing now and we have been able to build the foundation for e-com and we will be focusing on growing our business in e-com in organized trades. So that is going to be our focus going forward, yes, and we are working towards that, yes? So that is a huge opportunity that is available to us, yes, which we could not participate when the business shift happened about 3 to 4 years back as we took time to build our internal capabilities, yes?
- Akshay Bhor:** Thank you.
- Moderator:** Thank you. The next question is from the line of Manish Agarwal from Edelweiss. Please go ahead.
- Manish Agarwal:** Just a couple of questions from my end. Firstly, is there some fatigue at the dealer channel level basically where they are not willing to keep high inventories like maybe if they are carrying a 30 to 40 days of inventory, now they were kind of not willing to take more than 15, 20 days of inventory. Are you seeing something like that happening?
- Mithun Chittilappilly:** Ram, do you want to take this?
- Ramachandran V:** Yes. The channel is operating on lower-than-normal inventory because there is still uncertainty that is visible. So in general, the inventory has come down over a period of time, yes and the regular stocking that one would typically see is not visible today, right? That is also visible with which even cash has come back from the market, yes?
- Manish Agarwal:** Sir, is it something to do with any pricing arrangement that channels would have of themselves with?
- Ramachandran V:** No, no. I think that they have thinned their inventory, yes, and they have thinned their inventory, probably because the situation is uncertain, right and so people are, what I would say, not stocking too much and I think mostly, not just us, but all companies are at this stage, they are more busy feeding demand because I think that if everybody were to push sales, I am not sure supply will keep pace, okay? If you are looking at because the suppliers, all those factories are open, many of them are operating at 50% to 60% manpower is what we are observing. I am talking about raw material, packaging material and stuff like that and some of these are periodically going into containment and coming back after a week or a fortnight and stuff like that also. So all these things we are observing and therefore, what we feel is it will take some more time, before things will normalize and I think maybe couple of months down the line, we would be in a better position to develop a point of view



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on this. I think right now, I think people are just buying hand to mouth. So what we are observing is, we get more even sale through the month, right and practically, we are getting flat sales every take to the month. This is something we have seen before because in the past, it would be more sales towards the month end. But now it is more even right through the month right and it is replenishment. There is no urgency to buy on a first or a second or a third or a fourth, right? But typically, what we see is, we see almost the same number running right through the month.

Manish Agarwal: Okay. So the standard demand pattern has also changed you can say?

Ramachandran V: No. I think that they are just buying to requirement, right?

Mithun Chittilappilly: Yes. So I think, see, earlier, what was happening was they were having 45 days of inventory and during the month end, they will negotiate and then they will buy more as a bulk volume. But now they are buying 25% each week or 20% each week like that.

Moderator: Thank you. The next question is from the line of Prashant Kutty from Sundaram Mutual Fund. Please go ahead.

Prashant Kutty: Sir, the first question is in terms of you just spoke about even before COVID, there was a lot of competition, which kind of entered the market and probably will not want to respond to it. But just want to ask, is the overall landscape itself changing? So because you are also hearing a lot of strong players also entering into a lot of these markets be it appliances market or be it the kitchen appliance offers a matter of switchgears, lighting and so on and so forth. So is the competitive landscape even more severe as compared to what it was thought by you earlier and any changes in strategy which would like to make on account of that?

Mithun Chittilappilly: See, what will happen is when like I said, after demonetization and GST, when there was a crash in the GDP growth rates in the country, every company was the core categories were growing at 4%, 5%. So obviously, it does not look nice to show 4%, 5% growth. So everyone decided to get into every category. Usually companies give it 5 to 7 years. After making losses for 5 to 7 years, they usually shut it down. So that will start now.

Ramachandran V: I think also right, I think we could see from our point of view, right? So we could see these phenomena coming up. So immediately after GST, a couple of things became very clear to us. One is the hyper competition became very clear to us and the second thing that became clear to us that companies which had sourcing based model, we are losing advantage, okay and there are 2 kind of issues that happened for us because invariably we are going to a



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category, you rely on the capability of a supplier. So we are able to differentiate locking this is weak, okay and second thing is, of course, as I said, there is for us, at least, we could see a clear 3.5% to 4% gross margin erosion relative gross margin erosion happening because of GST coming in. Because the larger companies, which were manufacturing, they could have some advantages and so based on that, about two years back, we have reset our strategy, and we are working that path and I think some part of the dividends you would have seen this year in terms of margin growth, yes and our priority initially is to be fit for growth. Being fit for growth means making sure that your business has the right margin structure, yes and is churning sufficient amount of cash so that we can invest back into our business, yes? So that is our focus and we are running business with that mind. I think that is what Mithun was trying to say earlier, yes?

Mithun Chittilappilly: One more point to make is, like if you say, if the period of growth, if there is a strong growth happening in the country, it is much more easier to get into a new category and grow than in like in a reflationary kind of an environment, like what it is today. So when market is growing at 15%, market leaders may not even notice that their share is getting lost. But whereas when market growth is 5% for you to grow literally someone has to degrow. So that is when the hyper competition starts. So I think now the Indian companies would have realized that it is not easy to enter new categories. It is a long-term haul. So probably the only serious players will remain. Of course, someone will launch and then they will drop price by 20%, 30% and get some share and all that. But then how long you will do this? You will do it for 3 years, 4 years after that, eventually, you will have to somehow think about making money out of it, right?

Prashant Kutty: My second question is, given the current environment, you spoke about, driven channel is probably not really liquid well it could be a short term phenomenon, but you said the channel is also being a very more agile in terms of stocking inventory as well. In this period, are we also looking at probably cutting off some of those low-churn products for us or probably any of those-churn categories for us. Anything on the production, which you are trying to do that probably focus on certain categories and which would they be, if I may ask? So anything on that front, if you could tell us on that?

Mithun Chittilappilly: So see, we did not wait for COVID attack to start doing this. Like I said, we stopped LT cable in 2018. We stopped agriculture from last year. So we are not afraid to admit mistakes and shut it down because if ROCE for a product is not happening, the strategic value of the product is not there to the company, we will shut it down. We have no problems in disclosing it. We have no problems in taking the hit. We have written off an entire plant of some Rs. 20 Crores, which is LT cable that was done about three years back. So as a



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company, we are not afraid to do these things, and we will continue to do it, whether there is COVID or no COVID.

Prashant Kutty: Thank you and all the very best.

Moderator: Thank you. The next question is from the line of Santosh Yellapu from Ashika Stock Broking. Please go ahead.

Santosh Yellapu: I had a couple of questions. First, Sir, what are the challenges we see going forward to roll out the new products and also addition of the dealers or distributors across the non-South markets in FY2021 and 2022 and the second question is, Sir, on the Consumer Durables segment, with just Rs. 80 Crores kind of a topline, we did a segment level loss of almost Rs. 8 Crores, Rs. 9 Crores. This is somewhat a repetition of a mix we have seen in Q1 FY2018, could you throw some colors that despite new breakfast appliance launches, why we saw this kind of a loss?

Mithun Chittilappilly: So first of all, the challenge is, of course, India is whatever said and done, we have video conferencing and all that, but in India, business is still done the old way. They prefer meeting face to face, especially our retailers. They are a specific stereotype that they really believe in meeting face to face. So this as long as this face-to-face meeting and product launch functions and tours and all those do not happen, it is always going to be slightly challenging to go to a new dealer. I mean you cannot just call up a new dealer on the phone and say, can you be my dealer, I mean, so that is going to be one task. But however, we hope that there is some vaccine that is coming in our way and then probably, our sales team can restart travel. We have to also keep in mind that right now, retailers are also scared. They do not want any company representatives coming into their store because if one of the retailers catches this, then he has to also shut down the store and all kinds of stuff happens so retailers are also very scared to allow company people to come into their stores so most of the business gets done on salesforce.com and video conferencing and phone calls and all that. So that is definitely one of the challenges. What was the second question?

Santosh Yellapu: Sir, consumer durable segment.

Ramachandran V: Can I take that question. Yes, can I take that question?

Mithun Chittilappilly: Sorry, consumer durables. Ram, do you want to take it?

Ramachandran V: Yes. See, see, this last quarter, as I said, it is more like 45, 50 days of sales, okay? A mature category where we have higher market share and significant volume to market scale,



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obviously, the profitability will be better, and you will see a better health even on lower volume, okay? But many of the consumer durable categories, right, either you have a water heater, which is off-season, okay? Or you had air cooler which was just getting out of season, okay? So that is on one side and on the other side, you have kitchen and other products, right? These are products that we have entered in the last 3 to 4 years, okay? Obviously, they are going to have fixed up costs associated with the entry into these categories, yes and therefore, the breakeven point, in this case, will be much, much higher as opposed to breakeven point in a mature company. So as you can see, we have done about 58%, and we have been able to be profitable, yes? But probably, when you will break the number by segment, you will find that maybe the breakeven point in the mature categories is at about 40%, 42% and the breakeven point in the emerging categories will be about 60%, 70% because they have still not achieved the scale commensurate with the investment that gone in, both at the back end and the front end, in terms of manpower and other resources, by R&D resources. So I think you have to see it in that light, yes? I hope that is clear?

Santosh Yellapu:

Thank you.

Moderator:

Thank you. The next question is from the line of Achal Lohade from JM Financial. Please go ahead.

Achal Lohade:

What I wanted to check was, a, in terms of the festival season now given our product portfolio, so how important is the festival season for us in general, especially for the South market?

Mithun Chittilappilly:

See, so this year, Onam will be the first festival. So once Onam is over, we can tell you how it was. See please understand that these are not normal times. It is kind of like World War is happening or something like that so people are not really in a mood to go celebrate festivals. I mean people are not in able to get out of their own house, forget festivals. So I do not think they are in a mental frame to really do it, go and splurge money and all that. What people are doing is something is breaking down in the house, they are replacing it. We see a lot of demand for TV stabilizers because a lot of TVs is getting sold because now TV is the only source of entertainment for every person. We also see that a lot of demand for UPS systems because everyone is working from home, all the schools are starting school children are studying from home. So at any cost router should not go. That is a key asked by all households. So if you look at Kerala Onam, I mean the TV sales are one of the biggest ones and I think Onam TV sales should be decent not because people want to go and buy TV because of Onam, but because TV is the only source of entertainment. So maybe any number of TVs not enough because we are sitting at home all the time, right? So



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I think the behavior will change like that. I think what behavior we saw last year in terms of people going and buying stuff on auspicious day and all that will change into a need-based buying. I mean, if I need a TV, I will buy it; if I need a UPS or an inverter, I will buy it; if I need a router, I will buy; if I am doing some renovation, I will complete it, et cetera, et cetera. It would not be that of because it is Onam, I will go buy some clothes and then I will buy some gifts and all that. I do not know whether that will happen this year, but we will have to wait and see. But definitely, we can see that there is increased demand for televisions. There is increased demand for dish washing appliances, vacuum cleaners, et cetera. So we have stabilizers, dishwashers and micro-oven. So we expect all these to do well. So that is my primary expectation. Ram, you want to add anything to this?

Ramachandran V:

Yes. I think pretty much what you said. I think my sense would be that I think we should not analyze this situation too much because whatever numbers are coming, right, they are a consequence of, what I would say, demand-supply challenges of various companies, yes? They are a consequence of, what I would say, essential purchases being made by people, right? So I think unless the COVID scenario changes, this picture is not going to change. I think our industry is in that way, it looks like we are more fortunate than some other industries that demand has not hit us so hard because we are still able to post lockdown able to do 80%, 85% as you saw in the last 2 months, yes and we think that we should be able to do that in the coming 2, 3 months for sure, yes? So I think we should not analyze this too much and I think we should wait and watch, yes? I do not see any companies taking an aggressive posture and making investments because we do not know. Because see, the number of people who are taking calls, right, on how future will be that has increased, right? So see, every district authority is an independent authority and is authorized and empowered to take steps and measures as may be required to safeguard people in that area. So a lot of local decisions are getting made. There is no certainty to say how things will go. Therefore, I would say, I think that we should wait and watch, and I think this is a passing phase, and we should not spend too much time analyzing this because anybody who is making a prediction is speculating, right and that is what we are observing. Because if you take Kerala, we were in a good shape in Kerala and now look at what is happening, right? The cases are much, much more and this is in spite and despite best efforts, right? So I think there is a lot of uncertainty still associated with this and that would be good to watch, yes?

Mithun Chittilappilly:

So one more point is, I think the key thing to watch is number of cases per district because definitely, when the cases do drop in a particular district or an area, people do feel confident and they go and spend. So I think the best way to judge how things will go is keep analyzing that, and that is one lens. I do not think festive demand is going to be a key consideration this year. Because see, the festive demand is a hype created by all companies by advertisements. I mean the kind of money, all the durable companies spend during Onam



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and Diwali, it is huge. I do not know whether this year, they are in a financial position to do that and even if they do that and after 1 week, they realize the entire country goes to lockdown, what do you do with the money you spend? So these are the questions that are staring us in the face and then that is why we cannot really make an answer now.

Achal Lohade: Got it and just the second question, in terms of the inorganic, I know these times are trying times; we have been looking at or considering inorganic opportunity. So given the current context, are you keen on doing or you think this is now kind of pushed by at least couple of years in terms of any acquisition, et cetera?

Mithun Chittilappilly: I would not say a couple of years, but definitely a couple of quarters. I think we have been fortunate to have targets that have been engaging with us and we have been fortunate to mutually agree to keep it on a deep freezer or a backbone as you call it. I do not think we require 2 years. I think by January, we will be in a position to better perform.

Achal Lohade: Thank you.

Moderator: Thank you. As there are no further questions, I would now like to hand the conference over to Mr. Hitesh Taunk. Please go ahead.

Hitesh Taunk: Thank you, Aisha. Thank you, Sir, for your comments and insights, Sir. Are there any closing remarks, Sir? Mithun, Sir?

Mithun Chittilappilly: No closing remarks. Thank you, ICICI, for hosting this call and let us hope that we can overcome this pandemic, and everyone, please stay safe and listen to your local authorities. Thank you.

Hitesh Taunk: Thank you, Sir.

Mithun Chittilappilly: Thank you.

Moderator: Thank you. On behalf of ICICI Securities, that concludes today's conference call. Thank you for joining us, and you may now disconnect your lines.