"Arvind Limited's Post-Results Discussion for Q1 Financial Year 2022-23 Conference Call"

August 01, 2022

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Moderator: Ladies and gentlemen, good day and welcome to the Conference Call for Analysts and Investors for Post-Results Discussion for Quarter 1 Financial Year 2022-2023 of Arvind Limited. 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 that this conference is being recorded. I now hand the conference over to Mr. Samir Agrawal. Thank you and over to you, sir.

Samir Agrawal: Thank you. Good afternoon to all of you and thank you for participating in this call to discuss the first quarter results of Arvind Limited for the financial year FY22-23. Joining me today is Mr. Jayesh Shah - Executive Director and Group CFO, Mr. Swayam Saurabh - our CFO of Arvind Limited, and Mr. Kaushal Shah - Head of Investor Relations.

The business environment in the recent months has been quite volatile with multiple forces at place. In our key markets, inflation has emerged as a primary concern for the policy makers and all central bankers are busy with interventions including interest rate increases. Consumers have also been feeling the pinch of expensive fuel and food though government support and high asset prices had kept the consumer demand strong thus far. Two quarters ago, our key US customers were busy preponing their buying to pre-empt the potential shipping delays. This has led to an inventory buildup in the supply chain. Now, this trend has been reversed and with the first signs of consumer demand softening visible, our export customers have started to partially postpone their purchases.

In UK and Europe as well, inflation has been a matter of serious concern. In the prospect of Russia-Ukraine war driving for long is further adding to a weak consumer sentiment. In domestic market, demand has been good including through this ongoing EOSS season and most players are expecting this to continue through upcoming festival season and are hoping for a good Diwali. Commodity prices peak during this quarter and have finally started to come down. In case of cotton, the decline is quite pronounced and as we speak, the normal deliveries are quoting at almost 35% discount to what was the peak price few weeks back. Other raw materials and shipping costs have also started to come down. Anticipating price decline, some of our customers, especially in the trade segments, have started to delay their ordering as far as possible. So, on the whole, this market environment is quite interesting and complex as is playing out.

Coming to the performance update, our first quarter result was best ever Q1 in terms of both revenues as well as net profits since the demerger of Anup Engineering and Arvind Fashions. Q1 revenues were Rs. 2,352 crores, which was 64% higher than last year Q1 and 7% higher on the sequential basis compared to Q4 last year. Excluding other income, EBITDA stood at Rs. 220 crores, which transits into an overall operating margin of 9.4%. Profit after tax was reported at Rs. 106 crores, excluding discontinued operations. Our internet business is classified under discontinued operations subject to sale of Arvind Internet to Bigfoot Retail Solution Private Limited for a consideration of Rs. 152.3 crores, effective 30th June 2022. This transaction is expected to close next month. Textile volume especially export markets were robust during this quarter. Denim sold 20 million meters of fabric, which was same level as last year's Q1. More volumes rose from 23 million meters in Q1 of last year to 32 million meters in this quarter. Price realization in both these segments of Denim woven fabric increased by approximately 35% compared to last year's Q1. Garment volumes excluding essentials stood at 10 million meters for the quarter. Overall textile revenues were up at 68% to Rs. 1,976 crores.

AMD started this quarter on a strong note and its revenues were up 45% to reach Rs. 279 crores and an EBITDA of Rs. 32 crores. Demand for AMD products continues to be strong among our customers. Our input RM cost and expensive shipping kept the pressure on AMD margin, which stood at 11.5%. Overall, we expect Q2 to be marginally muted compared to Q1 given all the volatility in the business environment and the rest of the year will depend on how the demand is impacted given the recessionary situation in global markets and the quality prices which are also quite volatile.

At the start of the quarter, the RM prices were high translating in higher evaluation and temporary increase in the working capital required. We expect to correct most of this excess working capital during the quarter and continue our debt repayment program as planned and communicated to you. We continued our trajectory of producing our long-term debt and in this quarter, we have repaid Rs. 56 crores, taking the balance to Rs. 901 crores. Overall, net debts to that Rs. 1,809 crores at the end of the quarter, which was Rs. 127 crores higher than the March ending quarter and this was driven by working capital as I explained. So, this concludes my opening remarks and I now invite you to ask any questions that you may have. Thank you.

Moderator: Thank you. Ladies and gentlemen, we will now begin with the question-and-answer session. The first question is from the line of Biplab Debbarma from Antique Stock Broking. Please go ahead.

Biplab Debbarma: Sir, first question is regarding the real estate business, you have a joint agreement JV agreement kind of agreement with Arvind Smart Spaces, just trying to understand, is it like you get the share of the revenue and entire cost and everything responsibility of execution goes to Arvind Smart Spaces or you get the entire cost and debt in your books and Arvind Smart Spaces just develop it and get the share of the revenue? Sir, that is my first question?

Management: So, this question was asked last quarter as well, Arvind Smart Spaces acts as a developer for us and the land is owned by us which is basically developed. We get cash directly, which is the cost is getting booked as project expenses and later on once the project gets completed, revenue will get recognized. Right now, only cost is what you see in the P&L**.**

Biplab Debbarma: So, it is booked in your P&L cost?

Management: Yes, it is a development cost.

Biblap Debbarma: My second question is on your net debt, it is a good thing that long-term net debt has gone down, but if you see for the last 7 consecutive quarters, we have seen consistent reduction in net debt, so this quarter if I am not mistaken, the net debt has increased a bit, so just trying to understand what led to this increase in overall net debts?

Management: So, net debt has increased by Rs. 127 crores this quarter and this is primarily the value of inventories which has gone up as you know input prices have continuously been going up. This we expect to largely correct by the time we exit Q2.

Biblap Debbarma: So, directionally net debt reduction would continue, that is what you were saying that?

Management: That is correct.

Biblap Debbarma: One final question, sir. Sir both RM prices, elevated level and you also mentioned about muted demand in an export market, just trying to understand, which is more concerning? I mean both are, but just from your point of view, what will bring you in a more relating, like more better demand or the RM prices going down?

Management: So, you know both are interrelated. Demand is, let us say, getting impacted because of discretionary nature of apparel, at least large part of apparel. RM prices coming down could make it more affordable to buy, but it depends on different segments. They are not really one to one, but RM prices going down and demand continuing to improve should help outlook for a textile company like ours.

Moderator: Thank you. The next question is from the line of Prerna Jhunjhunwala from Elara Capital. Please go ahead.

Prerna Jhunjhunwala: Sir, I have two questions on the business side. You mentioned that the demand is muted in the near term, but just wanted to understand the relationship between RM and SG prices going forward at least for the near term, generally we say that it takes time for the fabric prices to correct, so are the customers really wanting the prices to reduce in line with cotton prices? How are they behaving actually in terms of product pricing, in terms of order booking? Whether they are ordering 50% of their general order book or 40 or 80? Just wanted to understand how is the customer behaving in both domestic and export market to understand the underlying business scenario?

Management: Sure, Prerna, so let us talk about domestic and exports separately. As per our export markets are concerned, like we shared even couple of quarters back, there was clearly a preponement of buying which was happening because large customers especially in the US, they had seen significant shipping delays and some of them has even incurred air freight charges and they wanted to avoid that and hence, in our Q3 and Q4, we saw a slightly preponed demand compared with season in which normally buying happens. So, that played out and obviously we have been aware that the inventories have been slightly higher than what we usually see in the pipeline. Now having said that, we are also seeing that going forward the consumer sentiment itself is going to become a bit of an unpredictable one because all the COVID support from the government has come down and then overall interest rate environment is going up, price going up is making it seem like consumer sentiment is likely to soften. So, if you put this two together, quite obviously from a demand for our products point of view, there is a beginning of uncertainty. So, far, we have not seen any major cancellation, so our businesses work on, in the long contracts and lead times, so we are seeing some small postponements, but not any major cancellations. Now if you track the results also, the global company results declared until April or May have been reasonably strong. Now from this point onwards, how things unfold is something which we are also going to see and will update you as and when things will happen, but so far like as I said, it is a cautious situation, but nothing which tell us things have reversed for us from our export market point of view. In terms of domestic market, it has been really good. The whole domestic markets have done quite well right through the end of the season sale in July and those participants believe that we should continue to see a good holiday season for us, the festival season coming up as well. So, on the whole, I would say that there is the possibility of things being a bit muted, but from what we see, there is nothing which kind of concerns us too much.

Prerna Jhunjhunwala: Sir, can we assume that the sluggishness in the export market should more or less be compensated by the domestic market because we had in the past increased our share of export market volume in the last 1 to 1-1.5 years, so will that rebalance in the near-term is how we should look at?

Management: Yes sure, so from quarter to quarter, it has changed our export domestic mix and it will be fair to say that in the coming days, we will see stronger uptake from the domestic customers and thus possibility is there for sure.

Management: If I can add to that, so obviously the risk which we see on export, the goal will be to try to compensate and the goal will be via domestic, but it is also the fact that it is a little bit uncertain to what extent, let us say further deferment of orders could happen, how fast the inventories would liquidate, hence, sort of a conservative view on the fact that quarter 2 likely to be muted. It is a little bit uncertain out there.

Prerna Jhunjhunwala: And just wanted to know current utilization, is it higher lower than the numbers reported?

Management: Current utilization of what?

Prerna Jhunjhunwala: Across capacities in denim, woven and garmenting.

Management: So, you would have seen already in woven and as well as garmenting, we are quite close to the total operating capacity we have, but in denim, we are not fully using capacity because the cotton impact as you know as a percentage highest is in denim fabric and as cotton prices start to subside, we would see improvement in denim capacity utilization.

Moderator: Thank you. The next question is from the line of the Biblap Debbarma from Antique Stock Broking. Please go ahead.

Biplap Debbarma: Sir, just on the cotton, you have mentioned that the cotton prices have been now trading at almost 35% discount to the peak prices which is heartening and I think again the cotton output in the next cotton season hopefully would be better, just trying to understand in terms of availability of the cotton, how is the situation? I mean, we have been hearing that many of these companies are buying cotton, not building an inventory, can you give us some idea if people are not buying, a few are not buying, a few have small types of shutdown shops**,** then how this price level, 85,000 with elevated level, how they are trading? What is the availability situation? Just trying to understand what is happening in cotton?

Management: Sure, just to be very precise, when I put the word 35%, it is for the November deliveries. So, it is a power looking price. I am not saying, currently the cotton is trading at 35% less, right, that is one small precision there, but to answer your question more broadly, see what is happening is, if you see the global sort of supply-side situation, that is also a little bit more nuance and complex. So, like if you take American cotton which is on the big sources, that best excess crop has been spoiled by situation that developed there, so one part of supply is impacted there. The Chinese cotton continues to be outlawed to be used by any of the Western buyers, so that part also is impacted. The Indian cotton outlook is yet to be a kind of slide in certain, so we will know only by September and or October which way the rains will play and how much of a good harvest we will see this season. So, on the whole, all the sources of supply which impact our availability and prices are still in a way uncertain and hence, it is very difficult to say, which way things will go. Yes, from our demand point of view, we do believe that the pressure which was there may not be as deep, so we expect some softening, but at the same time given all the supply side challenges, I talked to you about, we don't expect that the market will crash down completely. So, market prices, we believe will hold and of course it is difficult to say which way**.**

Biplap Debbarma: And sir, a final question on the water business, what is happening in that water business? Are you getting orders and are we going to see as added in the next one quarter or so? You would see some profitability or breakeven kind of thing in water business?

Management: So, water business is going as planned and we have never given specific numbers around performance. We have basically talked about other segment not being a drive on overall EBITDA and water business is progressing as planned and it is profitable.

Moderator: Thank you. The next question is from the line of Riddhesh Gandhi from Discovery Capital. Please go ahead.

Riddhesh Gandhi: Just I have a couple of questions, just to understand this implication of your cotton price and the spinning price being extremely low right now, given the differential in Indian price and international price, is that expected to impact us in terms of actually on the denim side or how should we be thinking about this?

Management: If, assuming demand remains constant, cotton prices starting to come down and spinning margins start to get thinner, this will help our cost in denim as well as in woven.

Riddhesh Gandhi: So, if spinning spreads are lower, it helps us, is it or it hurts us?

Management: Yes, because we do not have 100% in-house spinning capacity. The spinning spreads when they were higher, we were paying those charges.

Riddhesh Gandhi: So, how much of our capacity do we use internally for spinning as opposed to purchasing outside yarn?

Management: At textile level, it will be about half-half.

Riddhesh Gandhi: But then, I am just assuming that when overall spreads in spinning are higher, it would also be helping the other half where we have our own spinning right because effectively other people who actually aren't integrated wouldn't be able to pass it on?

Management: That is correct. In-house is on cost, but the other half on which you would pay what market would pay. So, if that margin starts to get thinner, they should help.

Riddhesh Gandhi: So, right now if you see, from what we understand is that spinning spreads are extremely low, so would that sort of imply that this is slightly higher than our normalized rate of profitability?

Management: Of course, I answered it already when spinning spreads are low, by design this would aid, but there are just too many variables to determine ultimate profitability of cotton cost, consumer pricing, customer pricing and demand.

Riddhesh Gandhi: So, on the garmenting side of things, what I understand is that obviously people look at the current cost of fabric and materials, RM etc., and your pricing is a little, more or less it has been a little dynamic. In denim also is it like cost plus effectively where your buyers look at or is it looked at a bit differently?

Management: No, not really, we don't do any customer contract on a cost-plus basis. We either sell them fabrics for a given variety or per meter basis or we sell fully made clothes and that output is based on a per unit output pricing. It has got more direct linkage to our cotton price.

Management: It is linked to cotton but there are other variables in place, the design, the R&D which goes into it, the relationship with the customer, correct.

Management: There is no cotton price link clause if you are asking that.

Riddhesh Gandhi: And the other question was, on the garmenting side, how are you guys just seeing overall like demand because obviously on one hand we are hearing stories about excess inventory at a retailer's end, on the other side we are hearing that India is gaining shares as a percentage, so how should we be looking at our order book, our discussion, our ability to pass on increases in prices etc., to our customers?

Management: Good that you asked, so garmenting in quarter 1, we have done well and also we have spoken about it, garmenting and AMD being two growth engine, also accretive from an EBITDA perspective. Garmenting we have done well, so have on AMD and this should continue also going in the future quarters.

Riddhesh Gandhi: So, the reason we aren't seeing any impact on overall demand is because of us gaining the share?

Management: No, future quarters demand does make things uncertain. Garmenting as a business for us, has underperformed, but have last 3 quarters stepping up quite significantly and I was just making a point that garmenting has done well in quarter 1 in line with what we have guided and should expect it to continue that trajectory subject to demand holding work.

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

Chinmay Kabra: Sir, I just had a couple of question, the first was that we have witnessed preponement and postponement like you said in the orders, so by when do we expect the orders to arrive at the normal flow, like any estimated duration or estimated time?

Management: I think the core inventory correction cycle should kind of play out in next quarter or so and we should be a kind of pass that by the next quarter or in second. Then after that obviously things will depend on the market level demand and supply and this whole inventory correction story will be over.

Chinmay Kabra: I just had one more question, I am not sure if this was asked previously, but just wanted to know if whether we are passing any of the benefit of lower rates, the current lower rates which have fallen, are we passing on the benefit of the customers for this?

Management: No, not like that, not yet. Obviously, overtime as the cost structure changes with a quantitative market, so our pricing will reflect that in the medium term, but there is no direct linkage like as said, our price contracts are not linked to input prices directly.

Moderator: Thank you. The next question is from the line of Nirmal Shah from Seraphic Management. Please go ahead.

Nirmal Shah: I just wanted to understand what is your exposure for domestic market in denim, woven on the fabric side?

Moderator: What do you mean by exposure?

Nirmal Shah: How big the domestic market for you in terms of supplies vis-a-vis exports?

Management: The domestic market is about 35% of denim and woven combined.

Nirmal Shah: So, when you expect some sort of buoyancy in domestic market to compensate for the slowdown in exports, you mean the entire thing can be taken care by the buoyancy in the domestic market or you think there will be some?

Management: No, we do not know how bad export can get. Right now, there are two situations, one is inventory which some of our customers are sitting on and others could be how demand could deteriorate. It is a very evolving situation. We do see that domestic has been very positive so far. We will have to just wait and see how next 2 months evolves and of course our goal will be to respond, but it is difficult to put a number to it, what would be the level of impact and if it can be entirely absorbed by domestic market.

Nirmal Shah: But in that case, for your garment business, you would have already started receiving the orders to be supplied for the Christmas and the December quarter, right? So, if you can just give us how does it look like the order book for garments?

Management: Correct, but at any point in time, we have forward order books across our businesses and at this moment, order book is a little weaker than a normal quarter, hence we expect the future months to be a bit muted.

Nirmal Shah: So, can you sir quantify or give some range on a Y-o-Y basis how short it is?

Management: No, at this point we will not be able to quantify because very dynamic, it changes every alternate day.

Moderator: Thank you. Ladies and gentlemen, that was the last question. I now hand the conference over to Mr. Samir Agrawal for his closing comments.

Samir Agrawal: Sure, thank you everybody for joining us today. We will meet in one more quarter. Bye now. Thank you.

Moderator: Thank you. Ladies and gentlemen, on behalf of Arvind Limited, that concludes this conference call. We thank you for joining us and you may now disconnect your lines. Thank you.