"TCNS Clothing Company Limited Q2 & H1 FY22 Earnings Conference Call"

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Moderator: Ladies and gentlemen, good day and welcome to the TCNS Clothing Company Limited Q2 FY22 earnings call. This conference call may contain forward looking statements about the company which are based on the beliefs, opinions, expectations of the company as on the date of this call. These statements are not the guarantees of future performance and involve risks and uncertainties that are difficult to predict.

As a reminder, all participants' 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. Anant Daga – Managing Director, TCNS Clothing Company Limited. Thank you and over to you sir.

Anant Daga: Thank you. Good evening, everyone and welcome to our Q2 and H1 FY22 earnings conference call to discuss operational and financial performance for the quarter and half year. I am joined by Amit, our CFO and SGA our Investor Relations Advisors. First of all, I hope you and your near ones are safe and healthy. While the number of cases have sharply declined, we must keep up the guard and continue to remain disciplined and take all necessary steps to contain the pandemic.

While Amit can share the detailed financials, let me share some key highlights of Q2, our perspective on the situation, progress on key focus areas for FY22 and beyond that:

It's heartening that Q2 saw a sustained recovery vis-à-vis Q1 despite starting with a severely impacted July. Overall, Q2 revenues grew sequentially to 2.5x compared to Q1 with both online and offline showing some traction. What's encouraging is that it is much more widespread between different channels, geographies and type of stores. For Q2 the offline channel recovered to reach closer to 75% levels against pre-COVID on a like-to-like basis. In Online, business continues to see robust growth on a significant base that we have already achieved. On consumer secondary sales basis the online business grew to over 1.25x vis-à-vis last year, with our D2C business contributing more than half of the overall online revenues. As on date, our overall revenue numbers are tracking near pre-COVID levels. We are encouraged by the market trends including gradually easing of restrictions on public celebration and events and offices reopening for physical attendance. We have also embarked on an aggressive store expansion program which will help build on these numbers. Online continues to demonstrate significant traction and MBO business is also getting back on track. With all of this, we are gunning for business to hit pre-COVID levels and go beyond in H2 FY22.

Now coming to key focus areas for FY22:

The first area shared is growth of online business. As shared above, the business has continued to grow across own website and marketplaces. Omni channel stores fulfillment, which was launched last quarter has scaled up well to cover most of the large demand centers and is now contributing to over 5% of revenues for select channels already. As communicated earlier, we were working on an online only collection which got launched recently. The newer channels added last year have built up well and have grown to 2.5x over last year.

Second focus area this year is an accelerated store expansion plan. As shared, our target this year is to add 60+ EBOs. We have an aggressive store opening pipeline in place and we are on track to open one new store every third day in H2. This will take the total EBO count to over 600 for the first time. I am particularly excited about project Rise, our initiative of upgrading presence in key markets. We have already opened 5 stores so far, and I'm happy to share that within a short time these stores are already clocking an average of 1.5x of pre-COVID sales numbers. Project Rise will massively increase our brand presence and consumer experience across some of the most important retail spaces in the country and give a chance to present all our new categories and brand extensions in full glory.

Third focus area is cash conservation and cost control. We are happy to share that Q2 has been a cash accretive quarter. Overall, three out of the last four quarters have been cash accretive taking our cash reserves to Rs 160 crores from Rs 110 crores in the same period last year. We have significantly reduced our working capital from Rs 400 crores as on last September to Rs 350 crores this September. On cost front, we expect to see at least 20% reduction against our regular rent commitments. The full impact of the same has not been considered in H1 as many of the deals are still in process of getting signed. Some of this will flow in Q3 as well. As we prepare for next level of growth, we continue to invest in people, processes, and infrastructure, and hence one should not factor any major savings on these heads.

On the focus area of swifter thought-to-shelf , we are moving nimbly on all our initiatives. Our automated inventory management system, consolidation of warehousing operations, express replenishment mechanism and design incubation cell are all fully on track.

Now, with focus clearly back on growth. I would like to share a few initiatives from a median term perspective:

We have spoken about creating strategic growth levers, and last 18 months have been extremely eventful on this front. With a clear purpose of empowering the contemporary Indian women with her fashion choices and building on our inherent strength in understanding the Indian women consumer, product capabilities and omni channel play, we have been incubating new brand, product lines, adjacent categories which are all in different stages of evolution.

Let me talk about three of them. We have built a differentiated footwear range which has found great acceptance with our consumers. Despite COVID disruption and the loss of learning time therein, the footwear range is already contributing close to double digit numbers in our number of EBO stores. We are also set for a full-scale rollout of footwear in SS22 with presence across more than 150 EBOs, select LFS counters and online portals.

Folk song is a new addition which is a slow fashion authentic craft inspired fusion wear range which has been piloted through 20 W stores. We have seen good traction and now this will be rolled out to 70 plus W stores, select LFS counters and leading online marketplaces in SS22. As of now, this is part of W identity, but certainly has a potential to be an independent identity in the long term.

Elleven, our bottom wear foray hit rough weathers as GTM channel chosen was standalone stores and this got launched one month before COVID struck. Now with the expansion plans back in focus, we are all set to have 15 stores for Elleven by SS22. We will also be testing the same out in select LFS stores. Full scale pilot in SS22 will pave path for future growth strategy. This is one initiative that can be scaled massively in a short time post a successful pilot.

In keeping in line with our vision to transform W to a complete lifestyle brand, we are also piloting a beauty range in select EBOs and online. We have got a huge thumbs up from our consumers during our research and have co-created a vegan cruelty-free vita enriched color cosmetics range. This positions W a step closer to emerge as a go-to brand for consumers offering a complete top to toe look. We are excited to see initial traction on these initiatives and others that we have taken which could add meaningfully to business growth in the long term, help us build stronger relationships with our consumers and drive our brands in realizing full potential.

I will now request Amit to take you through key financial highlights for Q2 and H1. Thank you.

Amit Chand: Thanks Anant. Good evening, everyone. I'll be giving you an update on our financial performance of Q2 and H1. I'll start with the Q2 performance. Our Q2 revenue was Rs. 239 crores which is a growth of 66% over last year's Q2 and a growth of 155% over our Q1 revenues. Our gross margin has improved to 62.7% which is a significant improvement over last year's Q2 gross margin of 51.6% and this year's Q1 gross margin of 55.8%. In Q2, we accounted for rent concessions of Rs. 17 crores under Ind-AS 116 accounting. With this, we have so far accounted for Rs. 20 crores of rent savings in the current year and are on track to get annual 20% savings on our rent bill. Some rent concession deals are still under discussion and will be accounted for as and when they are finalized. Our spends on employee cost and other expenses reflect the investments that we have made in people, processes and infrastructure. As we have mentioned earlier, we expect limited savings on these heads for the full year. In Q2 the company generated a positive EBITDA of Rs. 45.1 crores vis-à-vis a loss of Rs. 6.9 crores in Q2 of last year and a loss of Rs. 20.4 crores in Q1 of this year. PBT for the quarter was also positive at Rs. 14.1 crores versus a loss of Rs. 38 crores in Q2 of last year and a loss of Rs. 49 crores in Q1 this year. PAT was a positive Rs. 11.1 crores this quarter versus a loss of Rs. 27.6 crores in Q2 of last year and a loss of Rs. 36 crores in Q1 this year. During the quarter we opened 17 new stores and closed 9 stores taking our net store count to 557 stores. We have embarked on an accelerated store expansion plan and basis the pipeline of store sign, we will be opening 60 plus net stores in the current fiscal which will be in line with what we set out for at the start of the year.

Now I'll be talking about H1 performance:

Our FY22 H1 revenues were Rs. 333 crores versus Rs. 176 crores in H1 of FY21 which translates into a growth of 89%. EBITDA in H1 FY22 was positive Rs 24.7 crores versus a loss of Rs. 33 crores last year. PAT for H1 FY22 was a loss of Rs. 24.9 crores against the loss of Rs. 72.9 crores. Our working capital as on September end was at Rs. 350 crores versus 352 crores as of March 31st and Rs. 400 crores as of September 2020. Our cash reserves as on date are Rs 160 crores. This is in addition to the unutilized bank limit.

Thank you. We are now open to questions. Since we are the only listed entity in our segment, we might not be able to share granular details that would be competitive information. We request your understanding of the same.

Moderator: Thank you very much. Ladies and gentlemen, we will now begin the question-and-answer session. The first question is from the line of Nehal Jham from Edelweiss. Please go ahead.

Nehal Jham: Three questions from my side. The first is, it's good to see that the gross margin which is the number we keep discussing about that has obviously seen quite a good improvement. And at the level it is there, it is nearly similar to what we used to do pre-COVID. But just the slight difference that exists versus pre-COVID, is it right to put that everything else is the same, just that the channel mix being towards e-commerce could be the reason that we see this small difference versus pre-COVID.

Anant Daga: So Nehal, good evening and yes, because of the slightly higher e-commerce sale the margins would be lower. So, 62% to 64% is what we believe would be the margin range overall. So it's much closer to that. Having said that with sales increasing this number could have been slightly higher.

Nehal Jham: The second question is that on the online sales, we see that you've maintained the traction. I just wanted to understand that, is there any portion of sales in this where you would have shift already in the other model to your e-commerce marketplaces or this sales mainly reflects more or less the sales, we have done this September and all the festive sales that are going to happen will reflect in Q3 only?

Anant Daga: Nehal, it's a mix model and as we have discussed earlier also it has two areas. One is marketplace, which is direct to consumer, and second is B2B. So, there always will be this mix, and that's the reason in our commentary we mentioned that our secondary sales increased by 25% vis-à-vis this number, so there would be some overlap.

Nehal Jham: My last question was on the brand extension that you mentioned about W. Now, beauty seems an interesting category. Just wanted to say that other than footwear and beauty, are there any other categories you have identified which you can discuss about? And given that you are looking at brand extension, is it that W as a format in the future will see larger stores sizes going forward and maybe from the current store formats, we are going to ideally keep it bigger to accommodate more of the initiatives in the future?

Anant Daga: When we talk about top to toe look, obviously there are categories like footwear, fashion jewelry, there are bags and cosmetics and other such products. So, we have all that in radar, but we just want to take it one by one. So there are more areas. For example, plus size again, we can also extend the business in plus sizes. We are doing a small pilot. In Aurelia we are doing kids. So, these are smaller other initiatives which we thought are really interesting so we will again speak about it in coming quarters. But there are these areas which will be investing in. In terms of store size, yes, one of the biggest constraint we faced in the markets were 800-1000 square feet current size of stores. In project Rise the endeavor is to at least increase these sizes to 1500 to 3000 square feet range depending upon the market. And those are the stores where you will see all these categories represented fully. In smaller stores we will have to, depending upon the size, probably leave out one or two categories, but these bigger stores as we open more and more, you'll see full brand representation.

Moderator: The next question is from the line of Jignesh Kamani from GMO and Company. Please go ahead.

Jignesh Kamani: After a gap of almost 1.5 to 2 years, wedding season has been lined up. So, how is the performance for extending Wishful collection?

Anant Daga: We had discussed last quarter also; we had dialled down on Wishful till spring summer. Monsoon festive we have again built it up and as we speak in festive, we saw a significant spike in Wishful sales. So, hopefully with the wedding season in December, you're right, we should see probably a higher spike in Wishful numbers this season. In October, we already saw a spike.

Jignesh Kamani: What are the learnings from Elleven, and have we finalized the model stores size, the right SKU mix, color combination or still we are evolving the business dynamics on Elleven?

Anant Daga: In the pilot there were a couple of attempts, one obviously to find the right product customer fit. And second was to test the commercial and economic model for our distribution. So, on the first part of product we have got enough and more learnings. In fact, the new ranges that we have launched is incorporating all the learnings that we had from customers. As far as the economic distribution model viability is concerned that we will be testing out in the next few months when we open 15 odd stores.

Jignesh Kamani: Any feedback from the customer in terms of the footfalls, repeat purchase or any other parameter you take?

Anant Daga: See, for Elleven it's too early frankly. Because there will be a lot of pilot and it has all been very-very structured so far. Give us another 3-4 months. Maybe we'll have much more meaningful data for you.

Jignesh Kamani: Once you finalize you can easily appoint the 60 to 100 stores anywhere because the small stores size are reachable.

Anant Daga: Once the successful pilot is done, see, we are also taking a cluster approach. So, we have checked four markets to experiment this and then we have to replicate it. So, frankly from a product point of view, from supply chain and from retail experience, we have all the know-how. So, it can be scaled up very fast.

Jignesh Kamani: In the supply chain side, right now your supply chain is more focused towards the north. On Elleven it would be focused towards South India because it's more, you can say, lounge-wear and there I supply chain cluster around south?

Anant Daga: See, when you talk about bottom wear, of course, there is a mixed sourcing for which even in north you have Ludhiana, in south obviously you have Tirupur and other markets. So it will be a mix. For non- woven, obviously all our existing bases also work very well.

Moderator: The next question is from the line of Varun Singh from IDBI Capital. Please go ahead.

Varun Singh: A couple of questions, now that first time we have mentioned in our presentation that we are aiming for top to toe kind of category. There are lots of categories which we can kind of venture into. And as you mentioned that we will be picking one by one. So, just wanted to understand that why we are shifting our focus from a very niche kind of category to now almost every category, including cosmetics, and as you pointed out bags and accessories, footwear, etc., and even increasing the size of stores, as you mentioned 1500 to 3000 so that you can have kind of a full presentation. So, my question is why now, and why were we not doing this earlier? Objective is to understand that what kind of aggression in revenue growth that you wish to drive for. So, how are you thinking in terms of driving the entire category growth? Also, you have given a very nice presentation on the industry data front in terms of all the different categories, but why to lose focus and kind of venture into every other category instead of driving aggressive growth in areas where were already present.

Anant Daga: Varun, I think there are multiple parts to your question. Let me try to answer them. See, first of all, we have to figure out what are distraction and non-related categories and what is the perfect center for that we need to put a consumer lens. I don't think business lens works there. So, from a consumer lens, she is looking for a top to toe look. This is coming out of our research. This is very clearly demonstrated in our purchasing behavior across channels. So, if you look at it, what are we trying to do? We are trying to give her the fashion choices under the same roof. So, footwear, jewelry, fashion jewelry, cosmetics, all become part of a coordinated look. And that is why we are getting into those. And the consumer herself is answering these questions. The way our footwear sales have picked up, it was an in demand. It was clearly an opportunity for a brand like W to give that look. So that's why we are building these categories. Now, if we look at the evolution of W over here, W probably 10 years back was just a summer cotton kurta brand. Then we added a whole new bunch of fashion bottoms, then we added a category called fusion.

We have moved into winter wear. So, there are a lot of those additions which have happened over here. Now at that point in time one could have taken a view that, western fusion bottom wear is not core of ethnic but today it's core of ethnic. So, I think this a journey which W has spread itself much earlier. Frankly, again all these initiatives while it is occurring at the same time to outside world, those have been incubated at different points in time. So, footwear got incubated almost two years back. Cosmetics is just getting incubated. Talking about bigger stores, of course, When we have these categories which we can build up and, in the size, while we have a very small sample size of 5 Rise stores but look at the kind of contribution new categories are doing and over our revenues. So, I think it's a very natural consumer led demand, which I think a brand like the W should fulfill. And that's the whole idea frankly behind this.

Varun Singh: That's quite interesting, but this will also change the business economics in terms of margins and the revenue growth, etc., that we were targeting earlier compared to the way we would be looking forward to now. So, it would be very useful if you can share in terms of any objective change in the growth and margin numbers. That will be very helpful.

Anant Daga: See, what we have said if we keep doing more of the same and the market is growing at a double-digit kind of number, obviously you can grow at 1.5x so we are pretty sure of that. All these categories should ideally add to those. And independently these are all big segment in itself, but right now let's do a proper rollout and then talk about how big these can be. If you look at from an 18 to 24-month perspective, things like folk songs, things like footwear, they all can be easily 75 to 100 crores business which could be built over the normal growth rates that we have. So that's the intent. In terms of margins, see, some of these opportunities are more margin accretive, some of them are marginally lower. But overall level, I don't think it is going to make a huge change to the margin profile.

Varun Singh: Still if you can some objective guidance like net profit margin 8% to 10%, 10% to 12%, can we make an assumption of roughly a 100 basis points net profit margin expansion? I mean, anything on that front if you can give some guidance that would be helpful.

Anant Daga: At this stage of evolution of all these initiatives, I would refrain from giving any guidance. Frankly see, whenever you get into a business, you are very clear that it should stand up to our existing metrics. And that's the kind of range and that's the kind of offering that we have for our consumers. Maybe let these business scale up meaningfully and this should happen in the next couple of seasons, we will have a better answer on that.

Varun Singh: Last question on project Bharat, you mentioned that we are looking forward to expand network in Tier 3-4 markets through a franchisee led model. Two parts to this question is, currently what percentage would be a franchisee model in our total store portfolio and why we are obsessing about franchisee led model expansion into Tier 3-4 market and will that not be a risk of diluting customer experience the way we want customer to experience our brand? That's the last question. Thank you.

Anant Daga: As of now in our business about 35% to 37% odd is franchisee stores and balance is company owned. Now two questions that you have asked. One, why in Tier-3 Tier-4 through franchisee route. Again here you will have to take the consumer's lens. See, the idea is to open stores through a model which can best service our customers. In bigger cities we have the entire infrastructure within the company to give that experience. In smaller towns where our reach would be limited, it's best that we find the right franchisee who already has a knowledge of running a marquee brands in those markets. So, we are partnering. We are very selectively choosing our partners, the right franchisees who have that exposure. And from that city standards they run best retail. Obviously, there would be some difference in a Tier-4 experience and a Tier-1. But in Tier-4 also it will be a differentiated superior experience. So, that's the reason why we are going through that route and how we are going to ensure it is through consistent design, through training, through all the VM help that we extend to our franchisees and choosing the right partner to run these stores.

Moderator: The next question is from the line of Ankit Kedia from Phillip Capital. Please go ahead.

Ankit Kedia: My first question is regarding the franchisee stores; how do we do the accounting for the franchisee? Do we book the full revenue, and the commission is accounted in distribution expenses, or we net out their share and then we book the revenues?

Amit Chand: It will depend on the model that we follow with the franchisees. Most of our franchisee stores work on an outright model where the revenue is recognized net of the margins that we pass to them. There may be a very small proportion of our franchisee stores which also are on SOR model, where the revenue gets recognized on the consumer sales basis and the margin gets recorded under selling and distribution expenses, but that will be a smaller part of the overall franchisee network.

Ankit Kedia: So, is it fair to assume that a MRP sales or the revenue which we show, brand sales could be at least 10% to 15% higher than what is reported number?

Amit Chand: When you talk about brand sales, you are talking about the consumer sales, the price that the consumer paid for our products, right?

Ankit Kedia: Yes.

Amit Chand: That will be higher.

Anant Daga: That will be higher for even MBO channel for franchisee stores because these are all recorded after netting of the margins. You are right.

Ankit Kedia: My second question is regarding the beauty. The photograph which you have shared in the presentation, it looks like kiosk out there. Do you think the manpower in the store out there, you need a separate beauty salesperson to be with the consumer out there to help them? And that would also entail extra cost to you? Or the same apparel salesperson has been given training to actually sell beauty at the stores?

Anant Daga: Ankit, as we speak, we are experimenting with both models. There are few stores where we are taking beauty advisors and there are a few stores where we have trained our existing staff to do. And depending upon how much difference we see; we will select our model going forward. Having said that, when we have created the economics for every store and the store sales, we are taking beauty advisor cost into account. Just to give you another input, we have launched in very few stores, right now a lot of them don't have beauty advisors and our existing team is very excited and they are also doing a reasonably good job. So we will see.

Ankit Kedia: My last question is regarding quality real estate available in the market. All the retail companies are guiding for big stores expansion over the next 1.5-2 years. According to you is the quality real estate available in Tier-2 Tier-3 cities along with metros because we are also guiding for big stores expansion plans. Where do you think is the challenge for the retail industry in terms of quality real estate, or it is in abundance for everybody to take?

Anant Daga: So Ankit, it's very market specific question. We understand there are few markets, for example, let me just take example of Mumbai. In Colaba it’s not very easy but in Linking Road it’s not a challenge at all. So, we will have to see this market by market. And in most of the places you will find quality real estate space. Now, the thing is, till about last quarter the rentals were far lower. Right now it's building up, but even then, finding the right space at right rental from a near term perspective should not be that big an issue barring few markets.

Moderator: The next question is from the line of Shusmit Patodia from Motilal Oswal AMC. Please go ahead.

Shusmit Patodia: My first question is, the number of days the stores were open was 90% as you have illustrated. While the topline is still quite a distance from its peak. So, just wanted to understand how are you tracking this? How should we look at this? Because unfortunately there's no market share data that's out there. Are you happy with the performance? So just wanted to understand that perspective.

Anant Daga: If the question is are we happy, of course, we are not happy. Because obviously we were running for more. Having said that, as you rightly said there's no comparable data, but if you look at the ethnic wear space, I think we have posted a reasonably strong performance. Whatever little data is in public domain clearly shows that ethnic recovery had slightly lagged behind other categories like casual, kids, innerwear, and obviously we all know that even now all the restrictions on celebrations, events have not been lifted, offices have just started to open. And some of these things impact ethnic wear slightly more than other categories. So, when you look at broader market, I think ethnic itself has lagged but within ethnic I think we have done a reasonable job. But overall ethnic should build on from here. Number two, something which is more internal, if you look at it, our recovery rates are right now on base of slightly depleted EBO presence. To compare to September 2020, we still don't have the equivalent amount of stores. We have all planned it for H2. Hopefully, you should see numbers building on that account also in the coming months.

Shusmit Patodia: My second question is, first of all, congratulations on this whole strategy roadmap sharing with us and it looks very exciting. Wanted to understand probably some of the categories that you are now talking about from a supply chain perspective, it is very different from what you have done in the past. So, any initial thoughts on supply chain or it's easy. If these are all outsourceable, then it is not a worry.

Anant Daga: If you look at some of the categories like say footwear, cosmetics, what we have done is to start with the, we have got a team of experts who have been doing this for years. So, we have picked people from leading companies in these segments, and we have got the team, who understands product supply chain, to come and build it afresh. Now, for example, footwear, because we are making a slightly differentiated product, we realize that we need to have an exclusive development center which can work for us all the time. So, this is what we have established now. In terms of other suppliers, obviously right now the quantum are lower so there is some challenges in terms of cost and time-line. Given the scaling up, we already have quality suppliers ready. Same with the cosmetics. So these are good international suppliers we have access to, and that should not be a big challenge in the medium to long term.

Shusmit Patodia: My third question is, just want to understand what is the rental expense, because again, FY22 looks like a big saving year. So, can you point us out from the balance sheet? So there is a right of use assets that you disclosed. So, what percentage of that would be normalized rental going forward? If my understanding is right, if that is the base to look at?

Amit Chand: Actually, it is very difficult to correlate the rental base by looking at right to use assets. What essentially happens is the rental saving that we get during the COVID period, whether we talk about this quarter, last quarter or any period, essentially all the rentals' savings get knocked off against the rental expenses and whatever is remaining gets recorded in the other income. Whatever rent, atleast the larger part of the rent which is the standard rent that we used to book pre-COVID still gets recorded under depreciation and interest expenditure. So, there you'll be able to build a state line in terms of what would be our standard rental. We disclose in our note what kind of a rental saving we recorded, how much of that got recorded in rental versus other income. So, I think the better number to look at is the interest & depreciation which practically is standard across different quarters, even during the COVID times and separate out the rental savings

Moderator: The next question is from the line of Devanshu Bansal from Emkay Global. Please go ahead.

Devanshu Bansal: My question is on a recovery seen during festive season, you indicated getting back to pre-COVID levels. If you could also share the channel-wise recovery and region-wise recovery during the festive season, it would be helpful.

Anant Daga: If you look at offline, offline recovery was close to 90%. In terms of region south did well. West, barring Mumbai, was good. In terms of regions, we didn't do as well was frankly north. So, these are the broad trends that we saw.

Devanshu Bansal: Secondly, B2C is now more than 50% of our online channel and even the share of own website is also increasing, just wanted to pick your thoughts on how does this increasing share of D2C help our P&L and balance sheet?

Anant Daga: See, margins are more or less comparable. While we make slightly higher margin on marketplace, it's not very significant. So, I don't think it's going to make a big impact. In terms of balance sheet obviously when we bill it in the B2B, the inventory goes out of book. Out here it is still there in our stock but again, it also gets somewhat set off with debtors. So, not too much of a difference. Amit you want to add anything.

Amit Chand: I think, from a balance sheet perspective, Devanshu the way we have to look at it as when we do B2B billing inventories goes out of our book, but there's a receivable equivalent that sits in our book depending on the commercial term that has been agreed, could be 60 days, 90 days. In case of marketplace, essentially inventory continues to be with us at our warehouse or stores and the receivable period is typically between 15 to 20 days.

Devanshu Bansal: I was assuming margins should also be better since we would be doing the entire cataloging and also maintaining the number of discounts being offered. So, doesn't that help our margins if we do more D2C?

Amit Chand: On a net margin, yes, it's slightly better. Gross margin is definitely better in case of marketplaces because they are cost below the gross margin but when we talk about net margin only slightly better as compared to the B2B business.

Devanshu Bansal: Lastly, PPT mentions that there is a plan to revamp MBO business, so what is the run rate that we can expect from this channel going ahead?

Anant Daga: See, we have already mentioned in the past that we are taking a slightly more conservative view on the MBO channel, at least in the short term to mid-term. And the new model that we have rolled out would be more focused on ensuring good credit quality and a much cleaner business. It is a secondary sale focused. It's difficult to quantify the number right now, the model has just got launched but we believe that MBO business could contribute to about, a mid-single digit kind of number going forward at least from a short-term perspective.

Moderator: The next question is from the line of Prolin Nandu from Goldfish Capital. Please go ahead.

Prolin Nandu: Two questions, one is that again to this 90% store being operational in Q2 and we have a salience of online sales which is 25% of our overall revenue. So just wanted to understand that in the catchment areas or in the pin codes where stores were operational nearly 100%, the drop in online sales has it been significant, or has it been sticky at a higher level so what I wanted to conclude was that obviously in COVID times online sales as a percentage of ours is much higher and it was expected to decline but would it settle at much higher rate than what we had earlier envisaged? Obviously, it could be higher than pre-COVID level. Would it settle at much higher rate than what we had earlier envisaged?

Anant Daga: While I don't have exact numbers right now handy. But see obviously during the COVID period when offline retail was not operational to the max, online numbers were abnormally high. Having said that even with gradual opening of stores, final online share is going to settle at a significantly higher level than pre-COVID. So, if you would remember pre-COVID we were somewhere in the vicinity of 12%-13%. We believe stable state right now should be anywhere between 20%-25% so that kind of base should stay.

Prolin Nandu: I was not comparing with pre-COVID. I was saying that versus your expectation of where it will settle, is it going to settle much higher? Because despite 90% store operational 25% number looks a bit encouraging. So, that was what I wanted to understand from you.

Anant Daga: So, this is in light of offline coming back 100% operational levels, we believe online should still contribute (+) 20%. It is also because lots of effort has gone into creating this. So, for example, while we don't have exact number on a lot of our peers and other fashion brands, I think we are already sitting on a strong base and that is because of all the investments that we have already made in online only, D2C, not only in front end but also in operations, in backend. So, there has been a very-very conscious effort and we surely expect it to settle at a higher rate.

Prolin Nandu: The second question is on this whole franchisee model, and you said that currently 30%- 35% of our stores are on franchisee level and increasingly that is the model that we intend to expand our EBOs. Just wanted to understand over the years when we first started this franchisee model, how has been our experience and how have we sweetened the deal for a franchisee owner in terms of IRR, in terms of meeting their expectation, in terms of inventory turns, in terms of getting the **season** at their stores in time. Could you just give some more granularity, just want to understand as to how attractive is it for a franchisee to go with TCNS and that's the final proof of the pudding in some sense as to how the brand is perceived in some sense.

Anant Daga: First of all, let me just make a small clarification, it's not that majority of the stores would be franchise in future. So, I think there still will be a very-very healthy mix. In fact, most of the Project Rise stores and stores in bigger cities are all company owned. Similarly, a lot of Tier-2 markets are also company owned. It's not that overall term of volume per sales throughput, franchisee suddenly will become a much bigger share, that's one. Second, see as you rightly said, the proof of the pudding is when the franchisees come and ask for more stores and that's been happening with us for long now. I think in terms of our store economics, see our payback period typically is short and given the reasonable amount of investment, I think franchisees find it pretty attractive. Now, just to clarify another point on this, in lot of Tier 4 towns, stores are on project Bharat model. We are also opening franchise store on SOR, so that again that is very-very attractive from a franchisee point of view. And it also gives us the flexibility to shift stock from store to store. The fact that we are getting franchisee enquiries, we have already signed more than 12 to 15 Bharat Project, Bharat stores we don't see much challenge in that.

Moderator: We have next question from the line of Jay Gandhi from HDFC Securities. Please go ahead.

Jay Gandhi: A couple of things I want to understand our gross margin are just about 200 bps lower versus pre-pandemic, but our online share is really doubled from 12-13 to 22. Since you alluded earlier also there's likely to be 20% odd consistently. I just want to understand what has changed pre and post, for gross margins to not meaningfully change. It's just about lower. So, is it that our product mix has changed, it's likely to be more margin accretive? Because the full price has gone up which is likely to

Anant Daga: On the margins you are right, the online shares panel share would be there. But in online also there's a marketplace and there is B2B so that share also determines some level of drop. On the plus side the dormancy has been lower because our inventories have come down. Also if there's an impact of channel and product mix, which would be some basis points here and there.

Jay Gandhi: So is that sustainable, what I'm saying with 20% online consistently?

Anant Daga: Yes. With 20% kind of stable state scenario all these gross margins are sustainable and that's what we have been telling over last few calls.

Jay Gandhi: I'm getting a little conflicted of how to look at this, if I compare your inventory for future FY22, that's around Rs 200 crores, it's the same as slightly lower than pre-pandemic, 10% lower to your YoY. If I compare this to some of your peers, most of them have a handsome pickup in inventory buildup before the festive season. So, is it that we are bearish on our demand outlook, that's one for the second half? But then the conflicting view is that you are adding 60 odd stores also in the second half. I was just trying to understand why is the inventory buildup so low relative to peers.

Anant Daga: Jay, it's a very fair question and I will try to answer this two parts. There are two parts to it. One is, of course we took the opportunity of this COVID time to really down stock bulk of old season inventories. So there our ratio of fresh season to old season has improved. So we have not really cut down on new season inventory, but the proportion of old season has come down and subsequently you can say that it was like one-time down stock correction kind of stuff that happened. Second, we have been speaking about express replenishment mechanism. We have also spoken about quicker turnarounds in the supply chain, and I think all those things are now getting in action. Hence probably those could be few factors which makes our inventory look slightly lower compared to others. But frankly it is very difficult to comment on what others would have done. Another reason is we have also dialed down on our fabric inventory right now. Because raw material prices had increased in the market, and we have used significant amount of existing fabric therein. So that ratio should also come down. Probably those are the factors that would happen. Now again see as we move in future quarters, obviously, now we are seeing a strong recovery and you might see some built up coming in next couple of quarters in line with our expectations of spring, summer and monsoon thereon.

Jay Gandhi: One last thing I want to ask you was you are selling and distribution expense it used to hover between 18% to 19% in a typical year pre-pandemic. It's moved consistently for the last 4-5 quarters to 23%-25%. Now is it that we had to incentivize the channels more and this is not just us but in general the ethnic wear category has seen this happening. So is it the way had to incentivize sales more?

Amit Chand: No, I don't think that is the reason. If you look into the selling and distribution expenses even for, let's say the first three quarters of FY20, which is pre-pandemic, the selling expenses used to be in the range of 23%- 24%. Obviously, there is some difference that happens because of change in channel mix. Now, what is also happening as I mentioned earlier in the call that when the D2C part of the online is also increasing and it is now more than 50%, some expenditures pertaining to that business also sits under selling and distribution. But broadly there has not been much of a change. This quarter, we have 24.2% as the selling and distribution expenses, this is in line with what we had even in the first three quarters of FY20.

Moderator: The next question is from the line of Ishpreet from Motilal AMC. Please go ahead.

Ishpreet: Just wanted to understand on the adjacent categories, what is the kind of investments that the company has already made in terms of your R&D team that you are doing for the footwear, jewelry and the new cosmetics side that we are adding?

Anant Daga: While I won't have granular details ready but if you look at adjacent categories like footwear, jewelry or folk song or cosmetics, most of the capital has gone in building the team and investing in working capital. We have units which are very low cost so there's not much CAPEX out there. It's mostly working capital and the team cost. When you look at Elleven, when we open 15 stores, we will be incurring a CAPEX of about Rs 5 to Rs 6 crores apart from the working capital and the team investment.

Ishpreet: In terms of team investments if you could specify as to what is the amount that we would have invested?

Anant Daga: At this point of time we won’t want to share these granular details, but all these teams would consist of about 4 to 6 dedicated resources and balance the front end the finance and support functions, all are shared.

Ishpreet: And internally what are the targets when you think of entering into these core categories, and now there are multiple of those, as to say 4 -5 years down the line what would be the revenue from the core categories and these adjacent categories, anything in mind?

Anant Daga: See, all these opportunities if done right and if we get the right product customer segment and get the distribution strategy right, could easily be 200-300 crore opportunities each from 4-5 years perspective. If you look at 18 to 24 months perspective, obviously these numbers should all clock at least 75 crores plus on our run rate.

Ishpreet: Just one on the book-keeping side, on the rent to sales ratio if Amit you could help in terms of our own EBOs what the ratio of rent to is sales, for normalized rent not IndAS rent.

Amit Chand: It depends on the format. Typically what we target is the payback period because rental is one particular component as a % of sales, could be very different. Broadly, it could be as low as 17 and it could be as high as 25.

Anant Daga: Overall it is usually in the lower 20s or high teens and with new kind of stores that we are opening, I think it will change somewhat.

Moderator: Our next question is from the line of Pankaj Pobre, an individual investor. Please go ahead.

Pankaj Pobre: Thanks a lot for taking my question and congrats on the strategy you have put on board. A complete revamp of the whole business strategy taking in account what has happened over last 18 months. So just wanted to understand, do you foresee developing this company or maybe transform this company into platform where you'll be selling everything from clothing to all the needs of a woman over a period of time? And if yes, whether you will be following asset like model or asset heavy model? And I would like to understand your vision for the company for next 4 to 5 years?

Anant Daga: I think there are multiple parts to your questions. To start with, we already said what the purpose of the organization is. It's very clearly empowering the contemporary Indian women with her fashion choices. Now talking about the categories in businesses that we get into, well there are very clear guardrails. What we believe is in our understanding of Indian women consumer, understanding of apparel and adjacent categories and understanding of omni channel play. Whatever comes in this gamut could be potential opportunity for the organization. Now in how long-term we will take all these opportunities is another question to be answered. In terms of vision, see, we want to create a leading women's fashion platform and we want to create a multi-brand multi-category, multi-channel business. So that's where we are headed to.

Pankaj Pobre: If you could share your internal target, if possible, what is the current share of clothing and non-clothing and what you would like to perceive it or take it to maybe 4 or 5 years down the line?

Anant Daga: See, rather than talking about a company level, I think it would be too premature. If you look at our stores till about 18 months back 100% of the sales in the stores or 99% was coming from apparel category. If you take the top 50 stores where we have experimented with footwear and others, we are already clocking close to 10% sales from non-apparel. Ideally, for a fashion brand like us given the right product in accessories and right representation, our escalation would be to at least get a contribution of (+) 20%-25% from non-apparel. But these I'm talking right now about the channels where we have launched these. We'll see how it breaks over time.

Moderator: Our next question is from the line of Anuj Sehgal from Manas Asian Equities. Please go ahead.

Anuj Sehgal: I just wanted to understand on the omni-channel front, while you mentioned in your presentation that omni-channel fulfillment at the store level has stabilized and has scaled up. Can you give us a sense of how many of your stores are actually omni-channel enabled and of that 20% revenue contribution from the online business, how much of it is actually getting fulfilled from your stores?

Anant Daga: Right now, in terms of number of stores we have 100 stores across multiple cities which probably would cater to demand in excess of 80% of demand centers. In terms of contribution 5% of that 20% is coming from omni but this is just the first few months for us. And as of now we have our own website plus three leading marketplaces which are on omni model, we are adding more.

Anuj Sehgal: Just to be clear, when you say 5% that means almost one-fourth of your online sales are actually getting fulfilled from your stores?

Anant Daga: 5% of 20%, so 1%.

Anuj Sehgal: 5% of 20%. Okay. So, it's still very small. So, what I also want to understand is that, so if it is 1% of the overall online sales, what are the learnings that you have seen so far in these 100 stores in terms of enabling omni channel fulfillment? And how do you see this part of the business growing as your online business stabilizes? And I also wanted to crosscheck, earlier you had mentioned that the online share of the overall business would settle at, was it 20% to 25% or 30% to 35%?

Anant Daga: In the immediate future it should be 20% to 25%.

Anuj Sehgal: On the omni-channel piece, how do you expect this to shape up let's say over the next few years and what are the learnings in the initial phase that you've seen and what are the challenges to get this business up and running?

Anant Daga: Let me first start with learning and challenges. While it sounds very simple, omni actually is an extremely complicated process. You need many-many interfaces to work with each other. Many parties are involved, so that's one challenge. And as we speak, for even the biggest largest players, it is still evolving. So there are a lot of learnings which is happening overall. One practical challenge that we face is staff training at EBOs. All our EBO staff is trained to sell. They are not trained to run a mini warehousing kind of operation. So that learning, that awareness also takes lot of time. Data integration again. So, these are some of the key learnings and challenges that we have seen as far as omni goes. Where this could land, it’s a difficult question to answer right now because it will also depend upon what our merchandising strategy is, what kind of models finally will evolve with our marketplaces, how our distribution centers would pan out. But to my mind, a double-digit number in the next couple of seasons is that we should have aspire for. That will really help us in getting better consumer experience, faster TATs and, of course, build on our inventory optimization as well.

Anuj Sehgal: So when you say double digit meaning double digit percentage of your online sales?

Anant Daga: Yes, right now I am talking about online only, that's right.

Moderator: Thank you. Ladies and gentlemen, due to time constraints that would be our last question for today. I now hand the conference over to Mr. Anant Daga for closing comments. Thank you and over to you.

Anant Daga: Thank you. We take this opportunity to thank you for joining the call. We hope we have been able to address your queries. For any further information, please do get in touch with SGA. Wish you all a very-very happy festive season and a great year. Have a nice evening. Take care. Stay safe Thank you.

Moderator: Thank you very much. Ladies and gentlemen, on behalf of TCNS Clothing Company Limited that concludes this conference. Thank you for joining us and you may now disconnect your lines.