"Titan Company Limited Q2 FY'21 Earnings Conference Call"

October 28, 2020

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Moderator: Ladies and gentlemen, good day and welcome to the Titan Company Limited Q2 FY'21 Earnings Conference Call. 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. C K Venkataraman, Managing Director, Titan Company Limited. Thank you. And over to you sir.

C K Venkataraman: Thank you very much. Hello everyone on the call. Happy Dussehra and Diwali season to all of you.

The quarter that went by was quite satisfactory. At the first level, we were focused significantly on the safety of all our stakeholders, starting from the workers in our vendor premises, karigars to our employees, all the way to our customers and did not relent on the intensity of that through this period continuing to be the gold standard particularly in our stores for customers in all our formats to spread the word about how safe it is to shop in any Titan company store and therefore in a way persuade their friends and others to come and shop with us.

The second was a much higher level of innovation exhibited by all teams across the company, whether it was manner of delivering the product through try at home, video calling, live chats or pre-dispatch inspection being done remotely or designing for above the keyboard new life that we have or management of cash in a smart way using inventories that we already had and so on.

The third was a very high level of team work and collaboration in these challenging times when most people are sitting by themselves in their homes, unable to meet their colleagues despite offices having opened up, overall restrictions on social distancing and the density of the workplace meant that a lot of people continue to work from home, thereby constraining the normal way of working but we saw a greater teamwork and collaboration despite these challenging circumstances.

The fourth is a fabulous effort by all leaders, all managers on operational excellence on containing costs, managing assets and coming out on top exceeding budgets.

Fifth is an explosion in terms of what we call "Phygital" which is the combination of the knowledge that we have about our customers digitally at the center and the hundreds ofthousands of deep relationships that we have through our sales staff in the front with our customers. So combining this knowledge and that relationship to build the business even when people were perhaps not really needing the kind of discretionary products that we make and sell.

And last and perhaps most importantly a resolve across the company from vendors to franchisee partners to employees to make sure that we come out of this crisis at a brisk clip and at a rate which exceeds targets that we have set for ourselves.

So, all these were either strategies or ways of behavior ratcheting up some of the things that we were already doing, the combination of all this made sure that our Q2 was very-very satisfying to all of us and I would not go into the actual performance, that presentation has been shared with us, all my senior colleagues are here in the room and they will speak to you as you raise questions about the individual business in the next part of the session.

We are all very-very satisfied in the manner in which all parts of Titan company have risen to this challenge and in a way made sure that this crisis has not been a waste in a sense even though it has been a tragedy of huge proportions, but considering that there is only so much that any organization can actually do to deal with the crisis, we have dealt with it in the best manner, in the most humane and fair manner and we believe that we have sharpened all our faculties, all our weapons to be much better prepared for the improvement in the overall sentiment and demand that will surely come soon.

Thank you very much. I am there for questions as well and I hand over to Subbu.

S. Subramaniam: I just wanted to clarify a few things before we get on to the call. This is more to do with some of the accounting aspects of the results. You might have noticed that there were a few exceptional things which have been called out separately, particularly on the ineffective hedging portion. So, we did put out a presentation sometime back in August to all of you on how we go about hedging and what impact it has on our bottom line and for the matter even on the disclosure purposes. The situation is no different in Q2, we have had significant ineffective hedges, but let me explain to you the impact of these so that some of these terms may look very disturbing in a way but frankly they do not have much of an impact on the bottom line. So, going back to the hedging principle, we do cash flow hedging and we designate contracts based on expected sale periods. And if there is a mismatch between the sale period and the contracts taken, we end up with what is known as an ineffective hedge. Ineffective hedge by itself is not a problem. The value of the ineffective hedge depends not just on the mismatch in the quantity, but importantly also in the gold rate increase or decrease as the case may be. In our case we have had significant variations over the last two quarters. In the first quarter of course we had the pandemic which impacted sales very-very substantially. So our sales was far lower than what was originally planned, and therefore you had an ineffective hedge because quantities were low. But it also got compounded by the fact that gold rates also went up substantially during the period. Therefore the value of the ineffective hedge which is basically a product of the two, was substantially high.

We have had a similar situation in this quarter except that the situation was slightly different. In this quarter actually we had expected to sell less than what we actually ended up selling. So the quantity that we sold was higher, that was one. Secondly, if you remember we also got a moratorium from the Reserve Bank of India to delay our payments on gold on loan. That also contributed to the ineffective hedge in a way because we had assumed that we would be utilizing the gold on loan in this quarter and therefore hedges were taken for a quarter later. But because there was a second deferment of this gold on loan, we ended up advancing the usage of the hedges which were designated for Q3 which has resulted in the ineffective hedge that you have seen. Rs.484 crores is what we are saying is the entire amount.

Now the point I want to clarify here is that if the hedges have been effective essentially they would have reduced revenue and the impact on bottom line. In this case I do not think there was any impact on our bottom line. So the bottom line that you are seeing the Rs.238 crores of profit that we are showing is a true fair view of what the performance for the quarter also was. It is just that these have to be called out separately because of accounting standards and therefore ineffective hedges shown separately. The revenues to that extent possibly higher. But as I said, there is no impact on the bottom line. We had said something similar in the previous quarter as well.

So now going forward we expect this variation to come down dramatically. The reason being most of the contracts that we had taken before March which is before the pandemic hit us are expiring by October number latest and we are now also changing our hedging practice in a way which should hopefully reduce this difference going forward. Therefore, all I want to say is that the numbers that you are seeing the profits there are true and fair representation of the actual performance during the quarter. So, this is something I wanted to start with. And now we are open to questions.

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

Abneesh Roy: My first question is on the mix of jewelry business. So, studded has been a good recovery quarter-on-quarter quarter from 18% to 26%, but it is still much lower than last year. So, will it be fair to say that now worst is behind on studded also because last quarter you had said the big cities are not recovering. So now in big cities also lockdown is not there and plus overall sentiment we are seeing across consumption is much better than initial expectation. So will the gap keep narrowing versus the previous year? And the margins in studded, when I look at just the studded segment, how is the margins versus last year because if something is not selling well, the normal strategy will be to give some more discount, some more promotion, so, if you could comment just on the margins in studded, how are they versus last year?

Ajoy Chawla: Hi, Abneesh, Ajoy here. You are right, the buyer recovery in studded is improving month-on-month and we have seen it improve right through the quarter, July, August, September. But it is still lower than last year and we are unsure whether it will completely narrow down, it is certainly narrowing down even in Q3, but as you know this Q3 we are still not able to make a comparable figure because the season was timed differently. But, yes, it is we are seeing that. I am hopeful that by Q3 it should narrow down considerably and then Q4 onwards we start looking up closer to what it was. In terms of margins, we are seeing no major impact on margin actually. The discounting is in fact for the quarter, slightly lower than what it was last year and it is as per budget. There is some squeeze on the gross contribution because the gold component in the studded material cost is a little more because of the value of gold and the gold prices having gone up significantly, but it is not very material, it is a very marginal drop which can be easily made up. So we are not seeing any margin pressure on studded.

Abneesh Roy: So, just one follow up there. So gold coins also as a mix if you see 14% is too high I understand gold prices play a big role here. So, would we need to wait for two more quarters for gold coins and overall mix to revert back to its mean, so gold coins used to be more like mid single in the last many years, so if any comment you can give on that?

Ajoy Chawla: I think sentiment wise gold coins continue to be popular, and in this quarter also we are expecting it to remain higher than last year and in double digits. Perhaps once the uncertainty around the overall economic scenario comes down or gold prices start correcting downwards, only then we can say. As of now it is going more on sentiment on the street. People think gold prices are going to go up and there is a safety in buying bullion.

Abneesh Roy: My second and last question is on the 34 crores provision. So if you could elaborate why your own subsidiary, how that will eliminate this kind of a risk in the future? And second will it not recur in the coming quarters, so is it just one-time?

S. Subramaniam: This is a one-time thing. This is the entire exposure that we have to this broking house. We have provided prudently and maybe rightly so because it has been some time we have been following up. We do hope that we get this money back but we are not sure when exactly this can happen and that is the reason we made the provision. We have set up our own commodity broking company and once it is operational, we could possibly move all our business into that and therefore this risk of margin money being stuck with somebody else will not happen.

Moderator: Thank you. The next question is from the line of Latika Chopra from JP Morgan. Please go ahead.

Latika Chopra: My first question was on the festive sentiment. You mentioned in the press release it seems good and I understand the timing of the festivals is different this year versus last year. But any color on the Dussshera 10-days of Navratra know how sales were versus last year same period? And also what is the feedback you are getting from franchisees in terms of them taking up inventory ahead of Diwali?

Ajoy Chawla: I will respond from the jewelry side since it has a material impact. The way we looked at this quarter and especially the festive period of 30-days, we have tried to spread it out because of social distancing and safety consideration and the fact that not 100% of the staff will be working in the store all the time. We have tried to spread out in such a way that we reduce the peaks of Dhanteras and Dussehra and some of the weekend and we also put our promotions and schemes accordingly so that there is minimal impact on the stores. As a consequence, even looking at the 10-days of Navratri and Dussehra this year versus last year may be inaccurate. We are happy. It is positive. We are seeing a marginal growth but unable to comment whether you can kind of project it for the entire festive season of about 31-days which is Navratri to Dhanteras and Diwali because we are consciously trying to advance sale from Dhanteras and other peak days across the 30-day period. But so far positive, happy franchisees and on the ground, feel is good and so far we are able to manage it with a good amount of social distancing which is the biggest concern in our mind to ensure that we are able to navigate this season well.

Latika Chopra: The second question was on your store addition plans across jewelry, watches and eyewear. How are you thinking about these considering the recent trends and the expectations on consumer sentiment towards discretionary purchases? And also if you could comment on a franchisee front, is L2 the most preferred manner for jewellery in particular?

Ajoy Chawla: So on jewelry we have opened 14 stores so far. A large number of them was spillover from the previous year. And we after the pause that we had in the first few months of this fiscal, we are now recommencing our growth in terms of expansion. We think we may end the year somewhere between 30 to 34 additions for the year. We are at 14. We have stuff in the pipeline. So we are not holding back, in fact, we are seeing a benefit in going into catchments and towns where presence is not there because people are more comfortable shopping locally and we do not have too much dependence on malls for jewelry, so, to that extent that is not bothering. Yes, L2 is the preferred mode. L3 is in very small towns where we think there may be potential law and order issues or very remote town, but otherwise by and large L2 is our preferred mode.

Suparna Mitra: Suparna from Watches. We never had any substantial expansion plans for our retail stores and that continues even now.

Saumen Bhaumik: This is Saumen from Eyewear. We have opened about 14 stores right now. We also had shutdown 38 stores. But going forward we do not have any major drive but my sense is around 25-30 stores might get added up in the year overall.

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

Aditya Soman: So firstly, in terms of this hedge accounting, would it be fair to say that retail sales for the quarter were 14% lower than on YoY basis?

S. Subramaniam: If we adjusted this, you are right, that is the case.

Aditya Soman: And then if that is the case, is this largely a function of lower footfalls because I am assuming there will be some benefit coming through with higher gold prices as well, right, gold footfall, then down close to 40% to 50% or that would not be right?

Ajoy Chawla: Retail sales actually without considering this hedge related thing is around 96% on MRP basis for jewelry. I am not able to answer your question on account of hedging whether it has…

S. Subramaniam: Because it will reduce, our hedges are based on old rate, so it would be lower, correct.

Ajoy Chawla: Yes, so just to give you a sense, 96% of value business is about 74% on buyer level if you want to look at number of customers and bill.

C K Venkataraman: So that 74% went up to 96% because of the price of gold but may have come down to 90% or 89% because of this matching the price of gold of sales and budget.

Aditya Soman: Secondly, we are seeing this disparity in the performance say for watches and eyewear compared with jewelry. Now again part of it is explained by gold prices and maybe partly by exporter to malls. Would these be the two main factors or are there any other reasons why watches or eyewear have done some significantly worse?

C K Venkataraman: Actually it is not a very easy thing to put your hands around but some of the additional points to consider is that eyewear despite being a product of necessity is also a product where relatively older people from a high share. It is also a product which involves proximity in terms of the testing and therefore worries about infection and stuff like that because we have heard these in the conversations. Jewelry despite being a high ticket size is a store of value product, does very well when the sentiments are poor and people are feeling worried. Watches are a discretionary product, very much a part of dressing up and therefore you do not really need a new watch when you are most of the time sitting at home and not going out anywhere, going to office and stuff like that. So actually it is a combination of these three things. And the share of the brand in that category is another both Eyewear and Jewelry operate with single digit shares and therefore in a secular way of formalizing that is happening in the industry, both tend to benefit whereas watches is a goliath in that market with maybe 45%, 50% customer share and therefore the upside on that is low. So it is a combination of multiple things, but if you go back to July and start looking at month-after-month, in every category, the recovery rates are improving even though the absolute levels are sort of trailing jewelry.

Aditya Soman: And just one sort of accounting question. So the impact on gross margins this quarter, that is again a function of the hedge accounting, right, I mean where your sales have gone up?

S. Subramaniam: So two things you have to adjust the hedge accounting, there is also the other operating revenue, Rs.390 crores of gold sale. So it will complicate issues a little. Yes, it is not going to be very comparable unfortunately.

Moderator: Thank you. The next question is from the line of Arnab Mitra from Credit Suisse. Please go ahead.

Arnab Mitra: My first question is on the margins. So if in the jewelry business we were to add back the Rs.34 crores loss and subtract the rent waivers, would that be an accurate representation of the EBIT of the jewelry business? And if we look at that as a number it looks like a significant drop YoY. Is that entirely explained by the mix effect of higher gold coins and lower studded?

S. Subramaniam: Why would you want to reduce the rent waivers? These are your savings.

Arnab Mitra: No, is it a permanent saving which you maintain or would it be a…?

S. Subramaniam: They may not be permanent.

C K Venkataraman: It does not recur.

Arnab Mitra: And the gap, would it be entirely explained by mix in terms of the drop YoY therefore we see in the margins in the jewelry business?

S. Subramaniam: There are two aspects to it; one is the mix itself, yes, the coin sale being much higher, studded being much lower, combination of the two is going to reduce gross margins and the operating leverage. If we have grown in much gold, that also had EBITDA margin.

Arnab Mitra: My second question was in terms of GHS, so there would be a period from maybe March to June, July where new enrollments would have been very low in GHS. So, do you see this as a kind of a headwind for the second half when your natural redemption cycle gets broken for three, four, five months or do you feel that the consumer would anyways kind of come back and it is not a net effect where you may lose some sales because enrollments were not happening for those three, four months?

Ajoy Chawla: Lack of enrolments will impact us in Q1 next year. So far, the recovery on Golden Harvest is also good, if I look at Q2, it is at 85% recovery of fresh enrollment. We are trying to see through other means if we are able to generate some load for Q1 over the next few quarters. We have launched a shorter duration scheme for wedding, and we are seeing if we can build that up sufficiently for Q1 next year. But you are right, there will be an impact to some extent in Q1 next year, not for the current year.

Moderator: Thank you. The next question is from the line of Prasad Deshmukh from Bank of America. Please go ahead.

Prasad Deshmukh: So, a couple of questions: Firstly, after the lockdown now incrementally the stores are opening up. How do you see the competitive intensity panning out especially with the local jewelers sitting on the inventory gains and interest rates also having come down which probably would have eased the working capital situation for them?

Ajoy Chawla: So from a competitive track that we have seen in Q2, while we have seen the recoveries I mentioned to you, our sense is that local jewelers are under greater pressure and standalone jewelers are having much lower recovery rates ranging from 55% to 70% or thereabout and some of the larger chains are better off but not as us is what we understand. So overall there is a shift. There is not so much impact. In fact, in Q2 we saw an improvement in the gold prices, but in the month of October we are seeing some gold rate related let us say competitive intensity in select markets. But it is not too much, it is not anything out of the ordinary and not as high as we might have anticipated earlier.

Prasad Deshmukh: The two other questions, firstly is new stores of Tanishq which have been opened, seem like these are larger stores in size. So is that the correct interpretation? And if so then in current situation, what is the logic of opening larger stores?

Ajoy Chawla: We have not really opened larger stores. Some of the stores are in bigger cities and catchments where we were not there. So there may be 3,500-4,000 sq.ft. but otherwise when we go to smaller towns it is in the 2,500-odd square feet. So we have not changed the strategy in terms of square footage and we think we have got the right optimal size. It is a function of cities and catchments.

Prasad Deshmukh: And the last question on the balance sheet. There is a marginal decline but there is a decline in fixed assets from March to September. So is this like a gross or it is a net number?

S. Subramaniam: Net number.

Moderator: Thank you. The next question is from the line of Vivek M from Jefferies India. Please go ahead.

Vivek M: Subbu, one again a follow-up or a small clarification. Just to get it right, hedging has no impact at EBIT level that I understood, but from a revenue perspective there is no impact, is that correct?

S. Subramaniam: No, what I said was that had the hedges been effective, the revenue would have been lower, the cost would have also been lower, Rs.484 crores would have moved from other expenses to reduce revenue, that is what would have happened.

Vivek M: So when I am looking at margins, if I am trying to calculate like-for-like margins, since EBIT number is any which way is not accounting for that, I should not change the revenue number as well, right?

S. Subramaniam: Actually, see, what you could possibly do is reduce Rs.484 crores from the revenue, add back that Rs.391 crores which is the gold sale that we made, knock off the cost of materials purchase stock and trade and changes inventory, you will get an idea of the GC.

Vivek M: See, my question is what one of the earlier participants asked, if I look at on a YoY basis the jewelry margins are down which you clarified is because of let us say mix change as well as operating leverage working the other way, but should not there be a big pricing leverage also the fact that gold prices moved up, and outside of gold the costs are generally fixed rather than being variable, so in an environment when gold prices are moving up, ideally margin should have moved up, so is that understanding not correct?

S. Subramaniam: See, on a making charge, as a percentage of gold, yes, there would be an increase, right, but the cost of gold, there will be no margin really on gold itself because if the hedge is as effective as can be, then your purchase price and your sale price of gold will be similar, and in this case it is almost that. So you will not make margin on that. Making charges percent, yes, absolute amount may be more, as a percentage while if we see…

C K Venkataraman: But the commission that we give to our channel partners is a percentage of making charges. So as the price rises, their commission also increases. The labor charges that we pay to vendors, if I recollect about two-thirds of that total, is designated in percentages and one-third in rupee terms, so that also rises. Therefore, per gram the rupee rises, but percentage margin on gold rate remains by and large same.

Vivek M: If I look at the last let us say eight quarters, four quarters, you have roughly done around 12% percent kind of EBIT margin in case of jewelry. As and when the normalization sets in case of a studded, do you think that is the number that we should be looking at again?

Ajoy Chawla: Yes, that is what we should be looking at as we normalize.

Vivek M: And lastly on the watches business, could you just give your thoughts on this marginal loss in this quarter, so how do you think about the second half of the year?

Suparna Mitra: So the watches business recovery, as Venkat mentioned, has been more muted but the festive season has been good and as we had stated earlier to exit the Q4 at roughly what was our last year level, we are seeing channel differences, so some channels are performing better, some others are not, but overall the business should recover to a 100% of last year level by Q4-end.

Vivek M: In the context of cost savings that are underway, would you believe that the margin profile on a full year basis let us say exit should be better than what it was let us say the last year?

Suparna Mitra: Better may be difficult, but definitely it should go back to what it was before COVID.

Moderator: Thank you. The next question is from the line of Amit Sachdeva from HSBC. Please go ahead.

Amit Sachdeva: Just wanted to sort of take Ajoy's brains on how we should think about the festive quarters especially considering how month-on-month things have recovered, so if I may say, we made some observations from your release and other channels, etc., is that August was very good recovery in tier-2, tier-3 towns and maybe September as well but July may have picked up that momentum while coins were also promoted when you are exiting this and looking at Q4 how one should think about wedding season being now bunched up in Q3 and some of the other tailwinds are there, which segment actually are doing well, is the coin sales are sort of fueled by pre-emptive wedding purchases, what really consumer is saying and doing, how do we make sense of the recovery that you have seen in Q2 and exit that you have seen in September and how the October has been going, what expectations not for a guidance, but what should we think about Q3 as a quarter, would you think that would be like a strong quarter for you like this recovery, the way September has exited?

Ajoy Chawla: Many questions. Let me first give you a sense on what has worked. Tier-3 towns have done better than tier-2, tier-2 have done better than the top-12 towns. Out of the top-12 towns, 8-towns which are excluding Mumbai, Pune, Bhubaneswar, and Kolkata, all the eight out of the twelve have seen a 80%-plus recovery. So, there is an improvement and even in the Bombays and Punes, we are seeing as we go forward an exit, it is showing an improving trend. So, that is one. Second piece for the quarter, wedding contribution has been good, in fact on wedding, segment-related sales we have seen a growth as opposed to a recovery…marginal growth, so therefore people have been buying up for the expected bunched up weddings in Q3 and Q4. We are betting big one weddings in the second half and therefore we are not holding back on any of inventory or promotion, etc., for wedding. We will go all out. On studded, high value studded is still a little sluggish but last few days maybe we are beginning to see some improvement. It is too early to say anything. But I must say on studded Q3 is hopefully good, we are chasing it aggressively and if we get to the goals of Q3, the gap should have narrowed down as I mentioned earlier, and therefore from thereon we can hope that Q4 then becomes pretty much back to normal, maybe not 100% percent but at least studded should be pretty up there. See, Q2 last year was a depressed quarter because of the spike in gold prices that happened. And therefore our recovery in Q2 of 96% on retail or 98% on the NSV, to some extent is overstated. I would still adjust it downwards to maybe around 90%, it is just a approximate figure. We are gunning for anything between 90% to 100% kind of recovery we want to try and get into this quarter. Where we will end is very difficult to say. So far it is good, I am hoping that it is better than the like-to-like 90 that I told you about Q2. Q4 of course our target remains to get back to growth which means it should be a 100%-plus which is what we have said even in our previous investor calls. I do not know if this answers your question but this is the broad sense that I can give you.

Amit Sachdeva: I think this is very helpful, Ajoy ji. Why I am asking this question is because see metro cities have not done well, tier-2, tier-3 which is much smaller percentage of revenue, has done exceedingly well, so much so that your actually revenue is almost flattish. So if I were to simply extrapolate, maybe August, September would be like 15%, 20% up for those towns, right, on like-to-like basis. I may be wrong. I am just guessing, right. So in that sense when metros have not participated and tier-2, tier-3 showing at least double-digit growth momentum to make it national picture look like this, then probably if metros come back to some extent, are you not being slightly conservative for shaping expectations for Q3 or is it something that you are really worried about? That is what really where I am coming from because I saw your initial comment on the Q3 and I thought that probably you feel very uncertain or is it something that you want to be very conservative at this stage?

Ajoy Chawla: The reality is that metros have started kicking in. Having said that I would still be worried about Mumbai and Pune. Ahmedabad, for example, has picked up very well. Hyderabad has been lower but Bangalore and Chennai have picked up well. So it is a little bit of mixed bag. Delhi

NCR which is an important has seen a 86% recovery in Q2. I think we are actually midway through the season; we are only about 11-days into the season technically out of the 31-days. Unlike last year when we met in November, by then the season had got over. So we could give you a better feel and also because we structured things is becoming slightly difficult to gauge where we will be by the end of Diwali.

C K Venkataraman: So the point that, Amit, Ajoy was making about the conscious effort by the division to advance the sale to manage the crowd better within the safety protocol, they believe they have been reasonably successful in advancing which means that whatever has happened in the 10-days is higher than last year to that extent and what that extent is very difficult to figure out at the moment and therefore only by Diwali we will be sure that the spike whatever we are seeing is going to continue for 30-days or compensate for a drop in the next 20-days or whatever. So that is the reason for what you may perceive to be a conservative picture.

Amit Sachdeva: What is the implication for margins here because I see that you would like to maximize revenue in festive, like the revenue has been focused in the last quarter as well because if I would perhaps pick up correctly, the coins were also promoted where the making charges were reduced significantly for coins and if I hear you correctly, probably you will have the same objective in Q3 as well while studded is not picking up to the last year's level, I think is it safer to say that promotional intensity will be higher over last year in the quest for maximizing revenue and hence we should not expect margins to really hold up and probably the underlying like-to-like margin decline should be expected in Q3 as well, should the margin expectations be like-to-like same, lower? My sense is that you are trying to suggest, it should be lower.

Ajoy Chawla: So in terms of promotions, we are pretty much more or less along similar lines as last year. So, our gross margin level should be good. We are also pushing studded more aggressively in this quarter because we are beginning to see that recovery. So the studded ratio for Q3 should be better than Q2. I do not know. We hope it is as good as Q3 last year but cannot say for sure right now. So far it is looking decent. And because of that I think overall we should start getting pretty close to our EBIT margin if things go well in this quarter. I do not see gold coin further being pushed because I think whatever natural demand is there, it is there.

C K Venkataraman: Also, Amit, it is not in a way substituting jewelry sales, it is an additional sale which may come at a lower percentage gross margin but we get some more crores in extra because of that, so nothing wrong in that.

Ajoy Chawla: I will give you another response which may be useful; we are also trying to chase absolute profits and absolute gross contribution as well besides looking at the percentages, we are looking at. So we are maximizing the opportunity from a total profit and total gross margin.

Moderator: Thank you. The next question is from the line of Rakesh Jhunjhunwala from Rare Enterprises. Please go ahead.

R Jhunjhunwala: Ajoy, fair enough that you anticipate that the sale for the festive period cannot be predicted because you maybe following a different strategy. But why do you not tell us in absolute numbers that what is the growth in the first 11-days of a festive period? We understand that you cannot extrapolate it for the whole festival season, fair enough, there could be differences which are unknown, there could be or there could not be. So then what is the actual growth in the festival period you know no?

Ajoy Chawla: Rakesh, I would say it is a single digit growth right now. I cannot say beyond that. I will tell you why I am saying this. First 16-days of October, we actually started off the offer in order to spread this out. So we have also clocked in some figure in the first 16-days. This first-16 days of October is not comparable to any period last year because it did not exist, it was an Adhikmas. So it becomes a little complex to try and figure out.

R Jhunjhunwala: Except all that you say, Ajoy, that factors may change and you may not extrapolate, but what is the growth in the festivities for the first 11-days and what will happen in the future is a matter of speculation. So we would like to know what you actually had?

Ajoy Chawla: So, I would say it is in the high single digits as of now, those 10-days-to-10-days.

R Jhunjhunwala: And my second question is the sales that means in the previous quarter if we reduce the sales because of the way recognizing the sale at the full price, then add the provision of 34 crores, so Rs.320 crores becomes your gross EBIT and your sale comes to about Rs.2985 crores?

S. Subramaniam: I understand that.

Ajoy Chawla: No, no, he is reducing NSV and…

C K Venkataraman: You are adding the Rs.34 crores back…

R Jhunjhunwala: That is a one-time, right and I am reducing the recognition of the gold at the regular price because if it is not the effective hedge, your sales would have been lower. As the profitability would have been the same no?

S. Subramaniam: Yes, profitability would have been the same.

R Jhunjhunwala: So your sales effectively was around Rs.2,983 crores and your EBIT is Rs.320 crores, effective margin around 10.8%, 10.9%?

S. Subramaniam: Yes, if I add back the Rs.34 crores.

R Jhunjhunwala: And my another question is that in the watch division, we record 55% in the second quarter and the eyewear division also, so what is percentage in terms, is our aim or our estimate, it could go wrong, what percentage of sales we could do in this quarter like we did 55% last quarter in watches, am I right?

Suparna Mitra: Yes, for watches, our estimate is about 75%.

R Jhunjhunwala: 75% of the corresponding quarter?

Suparna Mitra: 75% of Q3 last year.

Saumen Bhaumik: For eyewear, we expect around 75-80%. Q2 was 51% and of course Q1 was 12%.

R Jhunjhunwala: Now, there has been a marked improvement in the breakeven sales amounts in the watches and eyewear both, but your sales are lower, and your profits are higher, am I right?

Suparna Mitra: Yes.

R Jhunjhunwala: So now what do you think this is a permanent reduction or these are one-time or how much your margin profile would improve because of this, how much is a permanent improvement?

C K Venkataraman: Rakesh, actually this is a complex question. In the eyewear business, we were anywhere wanting to dramatically transform the financial performance of the division and we had chartered out a course for FY'22 and '23 and multiple initiatives have been identified by Saumen and team in the first six months of calendar '20 and the results in Q2 are actually evidence that those are starting to work and we are in fact a little ahead of our target for FY'22 itself. So there will be a big turnaround in eyewear. As far as watches are concerned, the watches division was in any case a very profitable division, and it would be our endeavor to actually grow the business in FY'22 in terms of sales, not just in the wearable side, but in the main analog quartz and mechanical watches side, you may end up investing in it for a while as opposed to going to the 16% and 17% that you have been talking to us for the last many quarters I certainly know that, but we will come back to you on this because we were never dissatisfied with the profitability of the watches division, in fact, we are now thinking of the growth side more than the profitability side.

R Jhunjhunwala: My last question is, first we advanced money to IL&FS, now we lose Rs.34 crores by advancing a broker. Do we not have some system of process in the company that we classify whom we are dealing with? How can we be giving money, what kind of broker is this, and what kind of process and system are we having in the company?

S. Subramaniam: Rakesh, these are brokers who are very reputed who we worked with. We have a risk profiling for all of these people. These are commodities. We have to do through MCX, right, and therefore only a few people that we have to deal with. The exposure to this particular broker was less than 10% of our total exposure. Now, unfortunately, something goes wrong we still believe we should get that money, let me put it this way, we are going after them and we know that they are doing some restructuring and they are getting some cash and so on and so forth. This is not equivalent to an IL&FS. Let me restate it; it is not an IL&FS here, but…

R Jhunjhunwala: The provision made out of abundant caution and could get reversed in future.

S. Subramaniam: Which is why we also now set up the other company that we are talking about, Titan Commodity Trading which is to take over even this element of risk.

R Jhunjhunwala: And one thing also I wanted to ask you, does this not dramatic reduction in the outstanding cases and the number of cases coming up every day, improve our prospects?

C K Venkataraman: We should encourage everybody who is sitting at home to step out of the house and go to their offices, go to shops and buy…

R Jhunjhunwala: No, Venkat, today the number of active cases has dropped from 10,25,000 to 6,00,000.

C K Venkataraman: What I am saying is despite that the tendency is still to change, people need to actually get that confidence to start moving out is what I am saying. But the watch division have done a beautiful campaign called, “Let’s get India Ticking.” So, that is the kind of thing that needs to happen for us to realize what you have described.

R Jhunjhunwala: So what we are saying is that it does not have much of an effect now, but if things keep improving, people will then move out more?

C K Venkataraman: It is no because what is happening is also a result of the improving sentiment and people stepping out of their houses and moving.

R Jhunjhunwala: And if the improvement in cases continuously takes place, sentiment can further improve?

C K Venkataraman: Correct.

R Jhunjhunwala: One question I had is that you are going to make public targets for cost saving.

C K Venkataraman: Rakesh, there were two things that we spoke on the call last; one was on hedging and the other was on the war on waste program. We did not have a proper opportunity to speak about it at that time, but the thing is that Titan Company is not in a situation where it is saddled with huge fixed costs and the only way to improve its performance is by a dramatic reduction in the fixed cost of the company. So, therefore the imperative to work on the cost as well as disclose it to everybody is not on Titan Company as much as it may be with many other companies who are in that situation. That is why we have chosen to…

R Jhunjhunwala: You do not want to disclose it for whatever reason. Fair enough, we accept it.

C K Venkataraman: Yes.

Moderator: Thank you. The next question is from the line of Manoj Menon from ICICI Securities. Please go ahead.

Manoj Menon: Just a couple of questions over there. One question to Ajoy is on the industry update on the trend of fixed making charges which we have started seeing a few quarters back or a few months back and what is the industry update and what is our response or no need for response?

Ajoy Chawla: No, actually, as I mentioned in the last call we did put out a few KVI products at the entry points on fixed making charge. I think it helps in just providing something to the store staff to talk to the customers. It has not had any material impact and we are not worried about that at all. I know you have been worried about that, but it has not really had an impact on our plain gold products and in fact, we have done reasonably well on our plain gold margins in Q2 and we will continue to do so.

Manoj Menon: My only objective was to understand, is there any material changes in the way industry operates so that is the only objective actually. Secondly, on the expansion if we heard you correctly previously in the call, you mentioned the 34 stores and if I take an average of 2,500 to maybe 3,000 square feet, you are talking about 100,000 square feet approximately. So is it fair to then say assume that FY'21 will have a largely the normal 100,000 square feet type expansion?

Ajoy Chawla: I am not able to react to your square footage but as I mentioned the range of stores that we expect to open, I do not have a single figure because we decided to pause in between, so between 30 to 34 stores for the year. So if you apply the metric you are saying…

C K Venkataraman: Actually, from a number of stores point of view, it would be a very good achievement for a COVID year.

Ajoy Chawla: Yes, last year we opened around 41 or 42.

S. Subramaniam: Average is 3,000 square feet. 100,000 square feet may go.

Ajoy Chawla: Yes, number is pretty much there.

Manoj Menon: One follow up on this if I may. Given the context of real estate, etc., in a normalized scenario in two, three, four years time, would these stores will have a better IRR given you might have better rentals and is there an angle there to consider?

Ajoy Chawla: I would not give it so much because the material impact there marginally better IRR on the overall base would not be so much and most of them will be L2.

C K Venkataraman: So the IRRs will be for them.

Moderator: Thank you. The next question is from the line of Chirag Shah from CLSA. Please go ahead.

Chirag Shah: Hi, Subbu. You mentioned in your opening remark there will be a change in hedging accounting and some bit of volatility that you have seen because of gold prices moving and ineffective hedges, that would anyways be taken care of going ahead. Now is this to do with you moving towards your in-house subsidiary for Titan Commodity Trading?

S. Subramaniam: This is just about designation of hedges, nothing to do with our in-house.

Chirag Shah: Can you just explain what are you trying to do going forward on the ineffective hedges?

S. Subramaniam: Let me very quickly explain this. Whenever we hedge in the past, we would expect to sell in a certain month. So if I buy a 1 Kg gold today, we expect to sell in a certain month and therefore the designation on the hedge for this 1 Kg would be a specific month. Now instead of a specific month, you may take it over a broader period, say three months so that any variations therefore within the three months can still be effective. Do you understand? So the idea is to reduce the variance as much.

Chirag Shah: So essentially what you are saying is you take a broader bucket while looking at allocating the gold required?

S. Subramaniam: That is right.

Chirag Shah: And that should considerably reduce the volatility even if there is an ineffective hedge, right?

S. Subramaniam: Yes, that is the whole idea. It would bring down hopefully the ineffective hedge substantially.

Chirag Shah: And as regards hallmarking, now mandatory hallmarking of gold has been deferred. So given that a large part of the competition that Titan competes with is compliant, how do you perceive the impact of the same on Titan?

Ajoy Chawla: As we see it, it got deferred to June next year ’21. It was supposed to be earlier by Jan ’21. In fact we have got the hallmarking licenses, etc., I think it will still be some time before all the industry manages to become totally compliant and their purity is matching because even the quality of hallmarking centers, etc., to really pick up. We do not know. If the question is will we be able to command the premium on gold vis-à-vis gold rates vis-à-vis other jewelers, etc., I think we should be able to command until of course we see that their purity levels have also come to higher levels, etc., But right now we are not seeing much of issue on that and I do not know whether this June ‘21 will also remain or it will get further pushed because there is again enough and more lobbying with the government by the jewelers to try and push it further.

Chirag Shah: Just one last question on the franchisee support. So, what kind of support have we extended to franchisees? We spoke about extending some additional working capital loans to the franchisees last quarter. So, can you just quantify what is the number this quarter?

C K Venkataraman: This is not something that we would like to quantify. It is an important aspect about a stakeholder that we wanted to share through grants as well as through working capital support, we are enabling the Titan ecosystem to flourish in these challenging times and we will continue doing it as long as we deem it necessary to do that because we are all part of a very large family.

Chirag Shah: But that number is not very material is what you would say?

C K Venkataraman: No, it is not material.

Moderator: Thank you. Ladies and gentlemen that was the last question. I now hand the conference over to Mr. C.K. Venkatraman for closing comments.

C K Venkataraman: Thank you very much everyone in the call as usual for probing deep into the business, giving us perspectives which are always fresh and take us forward and also keeping us on our toes all the time by asking piercing questions at the right time. Thank you very much till February first week. Bye-bye.

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