"Titan Company Limited Q2 FY 17-18 Earnings Conference Call"

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Moderator: Good day, ladies and gentlemen and a very warm welcome to the Titan Company Limited Q2 FY17-18 Earnings Conference Call. As a reminder, all participant lines will be in the listen-only mode. There will be an opportunity for you to ask questions after the presentation concludes. All the representatives of the media are welcome to join the call for management commentary and are requested to disconnect before the beginning of the Q&A session. Any recording or reproduction of any recording of this call is strictly not permitted. 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 am now glad to hand the conference over to Mr. Bhaskar Bhat from Titan Company Limited. Thank you and over to you, sir.

Bhaskar Bhat: Thank you and welcome to this post Diwali investor conference. We have had a good quarter and I just want to, this interaction we have had for several years now and we have learned over the years the kind of questioning and the kind of facts that are being sought from us and I believe we have kept investors well informed. We would like to conduct this entire interaction in as cordial a manner as possible and if there are any errors on our side, please do point out to us and please allow us similarly to point us any errors on the part of investor as well. So let us get on with it. We do not wish to express any opinion and wherever possible, we will provide some peek into the future, but we are not in the habit of providing guidance.

So we have had a great quarter and thanks to several things, it is all up there. The Diwali season specifically if I were to analyze which is 21st of September to 31st of October if I were to take that, it covers Diwali in both the years. The growth rates have been healthy especially in jewellery and watches. Jewellery has faced some challenges by way of the PMLA which was introduced and thereafter withdrawn but that was only in October. So to an extent, the September sales were impacted. However, the actions that the company have taken and certain impact of the formalization of the economy has benefited us quite significantly in jewellery and is beginning to help us in watches as well as eyewear. It is a significant part of our competition in unorganized and their ability to gear up for the GST regime before that demonetization etc. would have impacted them rather more than us. Therefore, all the negatives of having an unorganized sector as your competitor is now perhaps beginning to flow to us and we expect this to continue for a while, maybe for a couple of years.

So coming back to the fact market share gains in jewellery, good growth in watches and therefore 30% growth in revenue and very big jump in profits. And that is a combination of, of course the margin improvement as well as cost reduction on a like-to-like basis we have had the VRS benefits flowing in into this second quarter. GST transition has been a challenge and you are aware that there was an advancement of sales especially in jewellery which we could almost calculate to Rs.250 cr and somewhat in watches as well. Despite that, this growth has been achieved. Because of the upcoming festival season end of September, there was some upstocking at the level of the L3 in jewellery and in addition because of the PMLA, we have to encourage purchasing by the L3 and so we have to extent credit and so on. So there has been an increase in the working capital deployed in the jewellery business, but all that has reversed in October which is not visible of course in this number.

The company is moved on to the new office. We are speaking to you from the new office of Titan. Whenever you can, we welcome you to visit us. It is called Integrity. I think everything is up there and we put it on the website and I am sure a lot of you are waiting to ask questions. We move into the question mode straight away. Thank you.

Moderator: Thank you very much. Ladies and gentlemen, we will now begin the question and answer session. We will take the first question from the line of Avi Mehta from India Infoline. Please go ahead.

Avi Mehta: Sir, essentially my question was first on the margins. So in the jewellery segment, you highlighted towards higher L3 sales. You also highlighted towards lower studded ratio, but you moved to almost 13.5 on the back of product margin increase. So is this the new normal that you are looking at and is that the case even in the watch segment?

C. K. Venkataraman: This is Venkat. We had a pretty good margin both in the diamond jewellery category as well as in the gold jewellery category because of good management of prices and product mix within. As a result of which, the margin growth despite the studded share dropping was very good and the costs were kept under tight control and the combination of these two gave us that kick-in in terms of the EBIT margin expansion. As for whether it is a new normal, I would not connect.

Bhaskar Bhat: I think there is an upward movement even within the plain gold segment which is what is, I am not saying the new normal, certainly the brand's ability to garner a better making charge at higher price points is also good indication of where it is moving, but we really do not know with the increasing wedding segment, whether those will be realized every quarter, but the effort obviously is…

C. K. Venkataraman: We are quite happy with what we have achieved and we will continue to strive.

Avi Mehta: No, because all the drivers that you said are more structural rather than one cyclical. That is why I was asking sir.

C. K. Venkataraman: No, the product mix is not necessarily structural. The product margins are structural, but within gold as the wedding segment increases, this advantage we obtain will dilute, but if the studded share increases, it will add. So it depends on the quarter-to-quarter. Also, the emphasis is on the particular category now.

Avi Mehta: And sir on the watches well if you could highlight?

Bhaskar Bhat: Avi, I think a similar story in watches which is the biggest reason for this margin during the quarter is the high growth that we managed to get, if we correct it for the NSE, NSR, I think it is about 13.6%. Now that is the biggest driver. Apart from the fact that margin in watch business is also determined by the mix of portfolio and channels and brands. And the channel margins vary from one channel to the other from e-commerce to brick and mortar franchise, our own stores they trade multibrand outlet. So the mix was most favorable. As far as this quarter goes, it may not get repeated. We also had a big jump because of the big billion day from Flipkart and the great India sales from Amazon where we did extremely well apart from cost cutting measures and I think during this quarter we had about a 10 crores benefit on account of VRS. So all this put together contributed to the high growth, high margin that we got under this product.

Avi Mehta: Okay. And sir secondly, just the question that you know regarding to your comment, I just wanted to confirm. So there is a perceptible shift that you are witnessing in sales on the back of GST and demon to organize players and that has it sustained, I just wanted to confirm that?

Bhaskar Bhat: No. Let me correct you. Perceptible, I wouldn't say. It is our judgment because the news is that the jewellery in general, the others have declined, and we have grown. So how could be there is such a vast difference, whereas in other quarters it is not so different. So we are assuming that there is what is known as, what we call as migration and watches, it is not so perceptible. But we believe it is the way it will go because watches is not so effective like say by PMLA and pan card and so.

C. K. Venkataraman: See, the difference between demon time and GST is this that demon pushed the migration of customers in our direction because customers wanted to shop with a reputed jeweler, but GST is not that. GST is the inability of many of the players in the industry to deal, to do business in the new environment and therefore they are increasing weakness. But it is too short at the moment to comment on, but we are like Bhaskar said our opinion, our view is that we will benefit certainly in the near and longer term.

Moderator: Thank you. We have the next question from Amit Sinha from Macquarie. Please go ahead.

Amit Sinha: My first question is on your last quarter commentary that FY18 jewellery segment growth can be in the range of 25 odd percent. So just wanted to confirm, are we on the same track?

C. K. Venkataraman: Yes. We are on the same track.

Amit Sinha: Secondly sir, request you for an update on wedding while you have given a commentary in the presentation but wanted some more detailed update on the wedding jewellery and high valued diamond jewellery, how the growth rates have been and broadly what is the contribution if you can share that. Thanks.

C. K. Venkataraman: I won't speak about the contribution. Their growth rates have been higher than the nonwedding and the lower studded value segments. But in Q2, there has been complicated little bit by the introduction of the PMLA which was there for about 5 weeks and naturally PMLA affected those segments more than the lower end segments. So it is a little difficult to unravel all that. But including or despite introduction of PMLA, the wedding and high value have outperformed the lower end of the same categories, but less saw in this quarter because of the introduction of the PMLA. But we hope with whatever new thing comes, they will sort of get back to their differential performance.

Amit Sinha: Okay. Just one followup on the first question. So is it fair to assume that the weakness due to PMLA during the quarter was kind of compensated on account of upstocking due to the festive season. This is just for like to like comparison between the last year same quarter.

C. K. Venkataraman: Actually, not so much compensated, but because this year the season is earlier, Diwali is about 10-12 days earlier than last year. The purchases by the L3 for that season happened in quarter two, since last year it happened in quarter three. So the primary sales of L3 to L3 were higher than the secondary sales of L3 in Q2. And therefore the difference in the growth rate you see in the company's report versus the retail sales which is there in the presentation is explained by this buying, I would not call it upstocking, but advance buying by this channel.

Moderator: Thank you. We will take the next question from the line of Latika Chopra from JP Morgan. Please go ahead.

Latika Chopra: My first question is on jewellery side. Could you share is there any kind of a differentiation or a divergence between market share trends or your growth rate versus peers in metros, tier-1, tier-2, tier-3 cities and also if you could comment on your new customer addition metrics over the quarter?

Bhaskar Bhat: Latika from whatever we can gleam as well as sense, the market share gain appears to be happening across large medium and small towns and even on for example Dhanteras Day which was pretty good for us. We observed that many of the competitors' stores across the country were either closed in much earlier than we did or did not have the kind of crowds that we had. The migration of customers from others to us even in the medium and the higher ticket segments which began in November-December of 2016 continues to happen. So all these give us the sense that the market share continues to increase at least of the same rate as it was happening earlier. The exactness of that is it would be impossible to figure out because the industry size and all that is more a estimate than anything else. The new customer share remains good and I would not like to share what exactly it is.

Latika Chopra: The second thing is on store openings for jewellery. You have mentioned that the first half was a bit slow and you expect a considerable increase in the second half. Does not that put an upside risk to your full year growth guidance of 25%?

C. K. Venkataraman: I do not know because the PMLA was not something which was anticipated by us, it came in quarter 2, it got reversed, but the signals are that the PMLA is going to come back in a more liberal form. So that may depress like-to-like sales in the new store sales may chip into compensate and all that. So I would not start building that into making 25 into 30 and all that that you may be basically asking me to do.

Latika Chopra: And lastly on diamond side. You have mentioned business men preoccupied with GST led to some bit of a fall in diamond studded ratio. Are you seeing any reversal in that trend in the following months?

C. K. Venkataraman: Somewhat of it, yes, but since it is just 25 days after the PMLA reversal, I would like to sort of hold on and look at the specific categories where the businessmen typically buy, are they showing a consistent return back to their normal levels to control that. But immediately yes, there is a glimmering of hope in the post quarter 2 results, the sales trends.

Moderator: Thank you. We will take the next question from the line of Abhishek Ranganathan from Ambit Capital. Please go ahead.

Abhishek Ranganathan: On the reported numbers, I have a few questions. One is the fact that other expenses have fallen quite significantly year-on-year and so have our gross margins. Has there been some reclassification of expenses on the COGS we have expenses?

Bhaskar Bhat: I think we tried to explain that, Abhishek. If you go through our presentation on the company performance slide, we mentioned that most of them has actually got to do with the GST rate and disclosing changes. Excise duty on inventory etc. is a reduction given in this. So in our internal MIs, these are listed against GC. So it is not making a very big difference in the GC. Unfortunately when we reported, it is not shown at the GC level, but as a separate level and that is the major reason why and along with this of course, also the LBT, local tax as Octroi etc. which are not there this year. So to that extent, we mentioned that the big shift is actually because of reclassification more than anything else.

Abhishek Ranganathan: And other question is I have never seen an inventory jump of this extent in any quarter for you, 1,400 crores, that is a serious jump and does it imply or indicate the kind of growth we are expecting in the second half?

Bhaskar Bhat: We have explained about the extraordinary situation that was prevailing because of PMLA and the…

C. K. Venkataraman: And the building up of stocks. The Diwali is earlier this year. So even those 10 days actually make a difference because what would have been inventory on the 10th of October last year becomes 30th of September, that is one. So the second is we have also been ramping up this entire wedding programs to some extent the completion of that filling in of all the hub and spoke stores and all that. And third is we have a situation where we went below target, some late August till end September because of PMLA. So we ended up, we could not correct stocks in that short period of 4-5 weeks.

Abhishek Ranganathan: Sure. So what we are talking here is about us building up stock as well as franchise building up stock in terms of or having stock of this nature in the buildup for the third quarter?

Bhaskar Bhat: Abhishek, typically what happens is this quarter September is when our inventory level generally are very high and if you see that, traditionally you have seen that thing. What tends to happen is immediately after Diwali, the stock level falls substantially and which is what has happened now as well.

Subbu Subramaniam So Abhishek what you cannot view is same period last year, Diwali was 31st October, the stock would have risen on 20th of October, that is not visible. So whereas this year it was visible on the 30th of September.

C. K. Venkataraman: So every time when Diwali happens like this….

Bhaskar Bhat: 10-15 days it was….

Abhishek Ranganathan: And so Subbu, you would have bought gold and spot and started hedging again because I see some debt on the books.

Subbu Subramaniam: Yes. We have debt. Debt was largely because of the inventory buildup. But as I said that has come down substantially, I think by end of October, there is no debt and there is substantial cash as well. So it is shifted significantly, inventory and debtors both have fallen very sharply.

Abhishek Ranganathan: Sure. And one last thing on the margins because we would have had a significant portion of L3 sales come through and those wouldn't have any associated cost additionally with the store. Would that be also one of the reason why our margins have gone up in terms of EBIT?

C. K. Venkataraman: These sales would actually dilute margins because they are at the lowest margin. So it is not L3, it is an overall sales, the sales growth is excellent, the 36% of them. The jewellery division NSV growth is 36% and the cost are tight, margin management was good. So margin growth is very good, cost growth is very low and the ratios of cost and margin is kicking in the EBIT expense.

Moderator: Thank you. We will take the next question from the line of Amit Sachdeva from HSBC. Please go ahead.

Amit Sachdeva: So Venkat, if I may ask specific question on how the festive demand has been and if you could give some color on the demand for the weeks especially on the Dhanteras and Karva Chauth because I know both of these fell in October. So if I look at Dhanteras was 17th October this time and 28th last time and Karva Chauth was 19th and 8th. So if you could give me some Y-o-Y numbers that you have seen around these two weeks which are key weeks for jewellery buying in October that is number one.

C. K. Venkataraman: So Amit, the growth in the festive period including like 21st of September till 31st of October which covers Poojas and Diwali in both years, the growth was about 16%-17%.

Amit Sachdeva: Which is YoY around these times, is it?

C. K. Venkataraman: No, 21st of September 2016 to 31st of October 2016 compared with 21st of the same days in 2017. So it is Y-o-Y for the 40 days.

Amit Sachdeva: I also know that you expanded the quantity discount prior to Karva Chauth and also Dussehra. Has it not benefited because 16-17 numbers look to be little muted, isn't it, considering the trend that we have seen so far?

C. K. Venkataraman: 16-17 was a very good base. In FY17, we had a huge growth.

Amit Sachdeva: In October, I agree.

C. K. Venkataraman: Dussehra-Diwali season. Dussehra-Diwali season was 33% and 34% growth.

Bhaskar Bhat: 55% growth.

Amit Sachdeva: October was very strong…

C. K. Venkataraman: On top of that, we have grown 70% and this certainly was muted, some 15 days out of this was PMLA influence. 21st September to 5th October this year was PMLA influence.

Amit Sachdeva: And Venkat, can you break up between July, August and September trend because September I assume that would have been a very strong growth which may have not been in July. So September was any disproportionate jump up in growth in this quarter?

C. K. Venkataraman: Actually, September was also affected because 25th of August was the PMLA introduction. Too many parts to this, but fortunately…

Amit Sachdeva: I got it, but Venkat just one small thing. Can you give the comparable basis of like revenue growth for jewellery adjusting for GST. What would be the comparable margin if GST were not there just to get a sense of where we are on the previous trajectory of margins versus now?

Subbu Subramaniam: No, there is no impact of margin on GST on the jewellery division.

Amit Sachdeva: It looks like same comparable number.

Subbu Subramaniam: Yes.

Moderator: Thank you. We will take the next question from the line of Rakesh Jhunjhunwala from Rare Enterprises. Please go ahead.

Rakesh Jhunjhunwala: I have two questions. Has the FX regains all losses whatever there maybe of GST has been fully pass through or there is going to be some and have we adjusted our pricing in accordance with the increase in taxes or decrease in…

Bhaskar Bhat: Rakesh, let me give you the overall point on GST. The answer is no as in as everything being factored in into the quarters what you view or you can see as quarter, no, essentially because of two things. There is still uncertainty on the watch side as to and you are seeing it in the press as well as to where this is likely to end. So the certainty is that with 28%, there is a direct impact on the earnings of franchise and other business partners, MBOs and so on. So we had to take a kind of temporary, it is called GST support 2% additional margin and should the GST reverse, it will be reversed. So that caused sitting in any case. Now the price increase we did not take at that point in time for definite reasons. One is competitiveness and the other is as a company we also did not want to be seen as unjust enrichment, but nevertheless in jewellery, it is all there. It is as it is.

Subbu Subramaniam: There is no impact in jewellery.

Bhaskar Bhat: And the last bit is the excise duty benefits that were flown to the company. Even there, there is this 58% on CGST and is supposed to be refunded to us. There is a doubt about also a possibility of claiming it from the state 42% as well. There are many things there and we have to wait and watch and we are hoping that it will come down to 18%.

Rakesh Jhunjhunwala: So essentially although there was an increase in GST on watches effectively, 2% we have given is that we have not passed down to the consumer and the 2% which we give additional to the franchise on additional cost. Therefore, if GST comes back to 18% and we do not divide our prices, then our margins will go up. So that means this is the margin after losing because of and this is a substantial loss because of GST.

S. Ravi Kant: This quarter has been along with GST support being managed with many other things which cannot be sustained for long. You know things like postponement of activation, we have had planned the fast track activation and so we tried to manage our growth with the least cost to ensure that the margin is retained. So you have seen the margin improvement despite that additional payout of 2%. Let us hope how it pans out and if there is a need to increase the price, we will not hesitate to do that.

Rakesh Jhunjhunwala: And how will you account for the excise benefit?

S. Ravi Kant: We have taken a large portion of that 58%. We have accrued it.

Rakesh Jhunjhunwala: 58, not any more.

S. Ravi Kant: Not any more.

Rakesh Jhunjhunwala: So that means what is right by what the government policies that you pass on the increases to the customer, we have not done that. So rightfully our margins can be higher if we pass on that cost to the customers which are government also says?

Subbu Subramaniam: Rakesh, you are right. The point is we didn't want to do a kneejerk because there is a competitive situation which we were evaluating and we didn't want to do it immediately because there are too many moving parts in the watch business, as in margins are stock that they were holding, compensation of that and then we were looking at the festival season coming up, so that is the whole point. I think they postponed the Fastrack activation and went ahead with the Titan activation.

Rakesh Jhunjhunwala: And what was the effective excise on watches and jewellery, the effective Octroi?

Bhaskar Bhat: Octroi is about 2%-3% overall, LBT and all that put together. But 24% or so was the overall cost that we had. Excise duty, VAT and these local taxes.

Rakesh Jhunjhunwala: So that means effectively when the correct thing you said, government only says to perform the tax prices. Our margins of what division can further improve?

Bhaskar Bhat: Yes, exactly.

Rakesh Jhunjhunwala: Good, so I think 20% margins should, with the price rise should be in range. Anyway thanks for a very great performance.

Moderator: Thank you. We will take the next question from the line of Abhishek Roy from SMIFS Capital. Please go ahead.

Abhishek Roy: Sir I have couple of questions and first one is regarding, can you just give me the idea of the same store sales growth in all the segments you have?

Subbu Subramaniam: It is in the presentation. Please look at the presentation, it is there already.

Abhishek Roy: Okay sir. And can you just tell me what is the margin…?

Bhaskar Bhat: Just to tell you quickly, since you are curious, I will tell you. World of Titan 5%, Tanishq 18%, Helios negative 9, but that is activation has been shifted. Fastrack 2%, Large Format Stores 1%, Titan EyePlus 3%.

Abhishek Roy: Thank you sir. The next question is regarding the market share gain. So did you see any improvement during this quarter, in terms of the jewellery and watches?

C. K. Venkataraman: Yes, certainly, market share but we wouldn't be able to quantify. All we know is that our growth is significantly more than what we understand other people grew by.

Abhishek Roy: So what will be their outlook, like to grow in double digit on the market share by the end of this year?

C. K. Venkataraman: No. If we go to double digits in the next 4-5 years, we will be happy.

Abhishek Roy: And sir one last question, is regarding the Gemstones, so are you into the Gemstones business?

S. Ravi Kant: Not really.

Bhaskar Bhat: Carat Lane.

S. Ravi Kant: So we get concrete information on the department store channel that we are present in. So we have gained market share there, one percentage point which itself is quite big.

Moderator: Thank you. We will take the next question from the line of Vivek Maheshwari from CLSA. Please go ahead.

Vivek Maheshwari: Sorry, but my first question is again on jewellery margins. When you buy gold and you sell it to the customer and you charge making charges. So there is a cost which is gold, in your revenues also gold and the bulk of the cost is gold. So in that context, there cannot be a big operating leverage in the business, number one. Number two, it is not the first quarter where you have grown 36%. There are 10 quarters in the past where you have grown faster than that, way faster than that. I still can't understand 13.5% margin, what is driving this. Any color on this will be helpful. Is it anything to do with GST related changeover or Octroi, LBT not being there?

C. K. Venkataraman: Vivek, we have grown 36% in sales, correct?

Vivek Maheshwari: That is right.

C. K. Venkataraman: Is it possible for us to have grown 36% in margin also, gross margin?

Vivek Maheshwari: Yes.

C. K. Venkataraman: Is it possible for us to have kept the cost in cheque and not grown at all?

Vivek Maheshwari: Grown only 5%.

C. K. Venkataraman: I am just asking a hypothetical question, but just answer me. Is possible? So if we grew margin in 36% and not grew in cost at all, you know the relation broadly between the margin and the share of cost in the margin. The maths will be there.

Subbu Subramaniam: 36% of 10 is 3.6 which is 13 points.

Vivek Maheshwari: A followup on this, suppose in a business our gross margins are let us say 15% it is possible what you are saying. Also it is not that you know Titan was not an efficient company or Tanishq as a brand was not efficiently run?

C. K. Venkataraman: No, I am not talking about that. We are not taking about efficiency. We are only talking about our quarter where the gross margin could have grown 36% and the cost did not grow and the everyday expansion happened because of that. That is all. It is not that efficiency or otherwise. There are some quarters where maybe the gross margin grew 36%, the cost grew 40% also and therefore the EBIT margin fell.

Bhaskar Bhat: So very shortly put, the big cost in jewellery, let us say are sitting as head office cost, let us say. So that doesn't rise with scale at all. Now when you have 17% same store growth, obviously even rentals haven't gone up and you don't have a very big expansion of stores and you haven't put in CAPEX in the stores, so that is the kicker. It may not be the same every quarter but certainly in this quarter the 17% same store growth plus head office cost is….

Subbu Subramaniam: And there was no GST impact at all. Vivek, no GST impact at all.

C. K. Venkataraman: Also Vivek, you also know that we sell products at 8% making charges. We also sell products at 14% making charge. Now, the weighted average of all these are making charges. Now it is possible for us to increase the average making charges that we realized and increase the gross margin of gold, all that is sitting there while I won't want to share all that but very much sitting.

Vivek Maheshwari: And since we are in the profession of forecasting, you won't give formal guidance, I understand but you know it is very confusing, right? So shall we look at, what would you advise, the second quarter number as the base, first half margins at the base, how should we go about for second half and therefore next year?

C. K. Venkataraman: See the question that was asked of us in the last call, in the context of that 2.5x in FY22 was shouldn't therefore your early years be at a higher growth rate than the 20% CAGR that it represents. I said yes, so we gave a 25% guidance and we are staying with that. We did not give a guidance on margin at that time. We are not giving guidance on the margin now. Somebody asked me earlier that whether the 25% we are staying on, so the jewellery 25% we are staying on for the year. Margin itself is a more complex thing and I have also said that our focus is on sales growth and market share gain and if it comes to it, we will give up margin expansion, not given to margin dilution but give a margin expansion for sales growth.

Vivek Maheshwari: So that is what I would say in conclusion but the 25 will continue. I cannot say anything about the EBIT margin in Q3.

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

Rakesh Jhunjhunwala: My question was about don't you think that last year we have had a very bad year comparatively which disturbed this November and December. And also, I understand you can't forecast, but also there is a much more wedding season in November and December. So would it be right to say that sale in November-December growth should be as compared to what happened in October-September, you feel much better in two months because of demon immediately, December.

Bhaskar Bhat: May your wish come true Rakesh.

Subbu Subramaniam: So I think there is one other thing. Last year the entire festive season was in October.

[00:39:46]Management: Both Dussehra and Diwali.

Subbu Subramaniam: This year it got split between quarter two and quarter three. So last year was entirely rare and it was an exceptional year and we just mentioned sometime back, there is a 55% growth in that season. So the base itself is high up to 8th of November. After that, there was a slump which we are all aware of.

Bhaskar Bhat: But we also pulled back with our exchange scheme and all that.

Rakesh Jhunjhunwala: But in spite of that the base was low and the reason is we don't have such rich a wedding season, not yet we have that focus on wedding as we have today.

Bhaskar Bhat: I understand that, but there is also intense pressure from the government on the PMLA reintroduction and all that. And we don't know how that is going to go, at what level they are going to cut it off from 50,000, take it up to what level and all that.

Rakesh Jhunjhunwala: It is my feeling I don't know, I could be wrong. But I feel on November-December should be much better compared to last year because of the demon period.

Bhaskar Bhat: You are right in the basis from which you are coming. So we will wait. Let us now celebrate what has just gone past.

Rakesh Jhunjhunwala: But we have invested all in anticipation of….

Bhaskar Bhat: I know.

Rakesh Jhunjhunwala: Another thing, I wanted to ask you was, what were the number of shops. How many shops do you think you can open in the next 6 months?

Bhaskar Bhat: We had a rough 180 store months target, Rakesh and my last assessment of that was would be about 80% of that number of store months by the time March 31st happens. So far, I haven't heard anything to the contrary from my team.

Rakesh Jhunjhunwala: So that means we have, the sizing only 5-6 crores of Goldplus are left for conversion?

Bhaskar Bhat: Goldplus was not part of this, the new Tanishq I am talking about.

Rakesh Jhunjhunwala: So how many new Tanishq has opened, forget the store November or March may not be so important?

Bhaskar Bhat: In quarter two you are asking?

Rakesh Jhunjhunwala: No, in financial year, in October and…

Bhaskar Bhat: We have opened 5 so far, but are not in the pipeline and about I remember right, 22 or 23 was the new estimate.

Rakesh Jhunjhunwala: So that means open about 20-25 shops in the two quarters?

Bhaskar Bhat: 17.

Rakesh Jhunjhunwala: I think that is why, now the kind of profit we will be having and the kind of sale that the other jewelers are in. I mean, if we reach, we will sell. And what about the party which is field in Madras, very large jewellery in this field.

Bhaskar Bhat: Atelier.

Rakesh Jhunjhunwala: You are taking over…..

Bhaskar Bhat: Rakesh, that model very difficult to such jewelers. The only thing you can take over is if at all is the retail outlet, you can take over the franchise because the practices of such jewelers, the customers are used to those practices. So that way a whole lot of jewelers are available in that sense but it would be quite impossible for us to continue with their name or their skill or their franchise as in customer base. Better if the customers actually migrate to us.

Moderator: Thank you. We will take the next question from the line of Nillai Shah from Morgan Stanley. Please go ahead.

Nillai Shah: Subbu, my first question is for you. Is the gold exchange still around 40% for this quarter?

Subbu Subramaniam: Yes. Actually gold exchange was high. But yes, you are right. It is in the ballpark of 40%-45% between gold exchange and what we buy on spot, yes. So we are about 50% roughly I would say on lease.

Nillai Shah: Okay. So is the gold exchange because we don't need to hedge the gold out there?

Bhaskar Bhat: No, we have to hedge the gold. It is like buying gold on spot.

C. K. Venkataraman: It is buying from customers as opposed to bank.

Bhaskar Bhat: Yes. We need to hedge.

Nillai Shah: You still need to hedge that. Second question is for Venkat. The last quarter or indeed the start of the year Venkat you had said that you expect the jewellery business margins to be flat and the reason you are excited was that you would like to spend behind acquiring new customers and getting the growth coming through. Has that view changed in context of the growth that you are seeing or broadly is that view the same. I am not asking about margins. All I am asking you is about your view on the spends that you need to accrue to get that growth?

C. K. Venkataraman: Actually when you say spend, you are talking about resources put into the business, whatever, in various ways, right?

Nillai Shah: Like one thing I cited was that we are giving the carat off on the gold exchange to try and get the…

C. K. Venkataraman: That is one way of spending, but 1,400 crores of inventory is another way of spending.

Nillai Shah: I am not talking about that. I am talking about the impact on margins?

C. K. Venkataraman: The impact of margins comes through sales and then cost and finally margin, right? I am only saying that the resources, just go back to the question that you asked. I had said that our focus is going to be on sales growth, not on margin expansion. So even if margin remains flat, we would push for sales growth and the market share gain that comes with the sales growth. But what has actually happened is our sales growth has been off target or even better and our gross margins, we have been able to manage exceedingly well, even extra and in some parts and keep the cost more under control than what was budgeted and therefore our margin is actually expanded more than what we may have indicated. But we are now not getting more bullish on this for the next 6 months. If not again, we are going back to the same principle, but we will push for sales growth and market share gain even if the margin in the next 6 months is flat.

Moderator: Thank you. We will take the next question from the line of Harith Kapoor from IDFC Securities. Please go ahead.

Harith Kapoor: Just two questions. Firstly, said 17 stores next two quarters what would that be ballpark in terms of square foot. Do we assume a similar average as you have done in the first half?

Bhaskar Bhat: About 50,000 square feet.

[00:46:23]Management: No, 40,000.

Bhaskar Bhat: Yes, similar to what first half because our emphasis this year is all small towns.

Harith Kapoor: Understood and you know the second question was on the cost part that you had spoken about you kept cost quite low this quarter, you know anything in that, that can be factored in as a more permanent change of something that you are trying to do consistently on the cost management part, that we can lookout for?

Bhaskar Bhat: Not really because advertising is a reasonably large cost of division and when things are down in the public sentiment side, we pull down the advertising, it makes no sense to spend that at that time. Whereas if I take PMLA as an example, the PMLA has withdrawn, mood is better, so we spend. So it is not a circular change. It is more dynamic based on the situation. So I wouldn't…

Subbu Subramaniam: I think the cost base for the company as such if you take the overhead, it won't change significantly going forward. I mean, as in the rate of growth of sales will be higher than the rate of this cost. The significant benefits of cost cutting which is to do with VRS etc. that has already…

Bhaskar Bhat: Will continue to flow.

Subbu Subramaniam: Yes. It will continue to flow but for the quarter two, captures that almost completely. And quite clearly there is some…

Bhaskar Bhat: We are working on cost. We have been working on cost as a program internally which will yield whatever we get.

Harith Kapoor: Just a followup of that would be that, are you calling out how much of the other expenditure in the quarter was due to a reclassification impact?

Bhaskar Bhat: I am not calling out but a very sizeable portion of that is actually that. It is between two things, one is actually gold ineffectiveness. It is just an accounting treatment again. Last year, there was a significant ineffectiveness amount, the figure was about 40-45 crores which is a reverse in this current quarter. So ineffectively, it goes in the P&L. It doesn't go and get adjusted in the margin. So that was one major component and the other one of course as mentioned was the GST related excise duty on inventory etc. So the bulk of that is actually there.

Moderator: Thank you. We will take the next question from the line of Lalaram Singh from Vibrant Securities. Please go ahead.

Lalaram Singh: My question is on the watch segment. So overall, what is the outlook or what is the business plan for Titan over the next 5 years for the segment, is luxury watch which is a much higher growing segment a key focus area or we are still going to focus on the economy segment?

S. Ravi Kant: We are actually neither in the real economy nor in luxury, we are in the middle. That is going to be the area of focus for the next two years. Luxury is an opportunity for sure. We have not decided whether we will play in that market in a big way. The luxury market has also been affected by various regulatory interventions which have been impacting the jewellery business. So it is going to be largely in the mid segment, in the mid premium I would say. You must have seen, we have introduced quite a few international brands that we license to climb up the price ladder in a way, but not really luxury.

Lalaram Singh: Okay. So do you think that there is still a long way to go for luxury market to become a big chunk. So is that the understanding correct?

S. Ravi Kant: Everybody actually defines luxury in a very different manner, so for somebody luxury is Rs. 50,000 to Rs. 1,00,000. Luxury is actually 1 lakh or 1.5 lakhs plus. So what we are looking at is this whole price band between I would say 25,000 and 1,00,000 right now. We have crossed the 25,000 level with introduction of some of our smart watches, couple of license brands. We will gradually climb up that ladder. So it is I would say moving to like I said mid premium and not real luxury which is 1,50,000 – 2,00,000 plus apart from introduction of our own brand that we acquired which is Favre Leuba which obviously has limited presence given its price point. So that operates between 1 lakh and 3 lakhs, but it will take a while to build that brand and for it to grow.

Bhaskar Bhat: Also this story of luxury in India has been very tumultuous if you ask me. Primarily because the primary retailers who have strived on this luxury market growth have operated below the radar and they have got devastated by demonetization and GST. So in the Diwali period, every former or unorganized so called luxury retailer in India has seen a poor Diwali, which is rather surprising and it is only because of this significant transfer of sale I think to overseas. I mean, that is our judgment, I am not saying. So luxury has not played out as a profitable segment in watches at retail. There is only clean large retailer which is Ethos who has developed reasonably good franchise. But even there, the numbers are not as attractive as what Ravi calls the midmarket and I think the watch division's premiumization programs is watch is more interesting rather than play in the luxury. But that doesn’t mean we will ignore luxury.

Moderator: Thank you. We will take the next question from the line of Manish Poddar from Renaissance Investments. Please go ahead.

Manish Poddar: I have just one question for Venkat. Venkat, if you could give any indicative that whether the jewellery industry is actually growing in size and what is the outlook let us say from a 2-3 year per se?

C. K. Venkataraman: I don't think it is growing in size. How much it is declining, it is very difficult to grasp. All we know is that people generally who we talk to they are on the back foot, so it could shrink is the conditions continue to remain unfavorable like that, but given the very large upside potential that we have for the division, for Tanishq, we are not for….

Manish Poddar: And have you called out any space expansion for the next year FY19?

C. K. Venkataraman: Not yet.

Manish Poddar: And should we factor in something similar to what we are doing in this year, we will up the game?

C. K. Venkataraman Not yet, no we will speak at the appropriate. See the network expansion is one of the five pillars of our 2.5x strategy in any case. So you can expect us to exist, but I don't know the number to tell you today because I don't have.

Moderator: Thank you. We have the next question from the line of Amit Purohit from Emkay Global. Please go ahead.

Amit Purohit: Just continuing with the question the previous person has asked. I mean, one, on this entire thing you indicated during the demon period that you will see significant unorganized players coming and ready for a franchise kind of thing. So if you could share some experience on that and we have been doing 5-6 kind of stores addition for the past and now the guidance is about 17 store addition in the next two quarters. Would it be a scenario wherein every quarter probably we will be adding 7 or 10 stores for FY19 and how the ramp up and what are the criteria that you look at when you are looking at a franchise who is already into the business of jewellery?

Bhaskar Bhat: We don't touch. Actually we don't take on people from the jewellery Industry at all. So the fact that many of them may now be open and we know that they are open is not making any difference to us because we make it a point to pick people from outside the industry because we want them totally aligned to our philosophy and value. So therefore this is not going to make the expansion. What is making the environmental expansion better is because a lot of potential businessmen and retailers are looking at Tanishq as a more exciting opportunity, there also perceiving the increase in our competitive advantage. How it will play out in a more aggressive expansion for FY19, I won't comment now like I said to the earlier person. We will comment at the appropriate time on the specific plan for FY19.

Amit Purohit: And is this the enquiry levels have increased quite significantly and how do from those businessmen or individuals who are looking at?

C. K. Venkataraman: The response is very positive. Whenever we put an add or we reach out, a lot of people is interested in signing up.

Amit Purohit: And just on, you said the GSS scheme balances off now. I mean in the half yearly what is the standing balance which you get used….?

Bhaskar Bhat: Yes. It is about 800 odd crores.

Moderator: Thank you. We will take the next question from the line of Amit Nigam from Peerless Mutual Fund. Please go ahead.

Amit Nigam: I have two questions. One, if you can just explain the margin levers, do they work better when you have a volume growth which I assume would have happened this quarter compared to a pricing change? Second question would be, if you can just share some update on Carat Lane, how business has been progressing there. Thank you.

C. K. Venkataraman: Certainly the scale leverage that we have on margin is very good and you would see it, if you go back in time and look at those boom years of the jewellery division. So in a way the 36% growth of Q2 is playing out to the same potential especially with the cost controlled being what it was.

Amit Nigam: No. My question is earlier quarters, the higher growth rates were more driven by price and so much of volume.

C. K. Venkataraman: Price of gold?

Amit Nigam: Yes. So 36% of growth this quarter which we had seen should primarily be driven by volume is my assumption.

C. K. Venkataraman: This is price change. Earlier price changes are much significant, right and those don't come to us. They buy and sell at a high rate. The turnovers are higher whereas this is a volume growth which means the leverage does come back in the company. On the second question, Carat Lane had a very good quarter and the more detail…

Bhaskar Bhat: I think you can make out the difference. That is about a 50% growth that we had in the quarter for Carat Lane. Overall, about 75% growth in the year so far. So topline, we are growing quite well.

Moderator: Thank you. We have next question from the line of Vicky Punjabi from JM Financial. Please go ahead.

Richard: This is Richard here. I am tempted to ask this, looking at the margin expansion that has happened in the jewellery business. After having been through now four months of GST and having seen what are the kind of additional costs or tax charge from the implementation and weighing this against the benefits that you are getting there from, input tax credit, availability etc., is there any sense you are getting any sort of price adjustments that could be required in the form of lowering making charges to pass on any quantum of input tax benefit that is available?

Bhaskar Bhat: Mandated, no. On our own if we want to, that will be dependent on the competitive situation. Our competitive situation is only improved, I don't think we would be thinking of any such thing, Richard.

Richard: So if I were to look at GST right now, the rate of about 3%, I guess it is about 100 bps higher than that, one odd percent excise duty and…

Bhaskar Bhat: It was 2.

Richard: You know 100 bps more than take away all the input tax credit benefits…

Bhaskar Bhat: Actually it was not 100 because there were LBTs and other taxes as well. So the cascading effect of that was also there. So to that extent, it is not actually a 100 bps, it is about 30-40-50 bps is the difference actually.

Richard: And that 30-40 bps has taken away the benefit of all the input tax credit that you would now be entitled to all your let us say media spends, rentals…?

Bhaskar Bhat: We were getting input tax rate also on a substantial portion earlier. So you are right, we are getting some more additional benefits now, but it is not as materials as, it is in the case of watch business. In watches, it is very different because the scenario there was very different.

Richard: Okay. It is the jewellery that 30-40 bps compensate for everything else?

Bhaskar Bhat: Yes. That is it.

Moderator: Thank you. Due to time constraints, we will take the last question from the line of Arnav Mitra from Credit Suisse. Please go ahead.

Arnav Mitra: Subbu, just one question just carrying on from the last question. So if I look at the GST rate of 3%, so now obviously you are charging customers 3% GST, but the benefit of the Octroi, LBT, entry taxes and also purchase tax on the recycled gold, does that all not now sit as margin expansion in the jewellery division?

Subbu Subramaniam: It is not margin expansion. It is actually getting charged. I mean, we collected and paid back. The only difference that we have is the incremental input tax credit that we are now getting for some areas which we were not getting earlier. Otherwise, it is not much of a difference. Secondly, on first of July we also changed the price of gold. We reduced the price of gold to pass on this net benefit. So we passed on that as required by law. Making charges are different, okay. I am talking of the gold price per se. We did that readjustment from the 1st of July.

Arnav Mitra: That is pretty clear. And just one last question, the 22% retail growth in Tanishq versus the 38% growth in jewellery overall, so the gap is basically the upstocking into L3, would that be a correct understanding?

C. K. Venkataraman: Difference between primary and secondary, yes. We are stocking for the season, yes.

Moderator: Thank you very much. Ladies and gentlemen, due to time constraints that was the last question. I now hand the conference over to Mr. Bhaskar Bhat for closing comments.

Bhaskar Bhat: Thank you everyone for participating, a large number of you and we look forward to talking to you again at the end of the next quarter. Thank you.

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