"Metro Brands Limited
Q2 FY 23 Earnings Conference Call"

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Moderator: Ladies and gentlemen, good day and welcome to the Metro Brands 2Q FY23 Results Conference Call, hosted by ICICI Securities Limited. As a reminder, all participant lines will be in the listen-only mode, and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing "*" then "0" on your touch-tone telephone. Please note that this conference is being recorded.

I now hand the conference over to Mr. Aniket Sethi from ICICI Securities. Thank you, and over to you, sir.

Aniket Sethi: Thank you, Kathy. Hi, everyone. A very good afternoon. Thank you for joining us. It's our absolute privilege to host the 2Q FY23 earnings call of Metro Brands Limited. We have with us the senior management from the company. Mr. Rafique Malik, Chairman; Ms. Farah Malik Bhanji, Managing Director; Mr. Nissan Joseph, Chief Executive Officer, and Mr. Kaushal Parekh, Chief Financial Officer.

I would request Mr. Nissan to share some perspectives on the quarter gone by, as well as the recent acquisition, post which we can open the floor for questions. Thank you, and over to you, Nissan.

Nissan Joseph: Thank you, Aniket and good afternoon, everyone, and thank you for joining our Q2 FY23 earnings call. We delivered another great quarter for Metro Brands, very much in line with our expectations. It is reassuring that we have now lapped a full year of operation in the post COVID era and the consumer demand continues to be strong. We had two major festivals in the quarter, as we caught Janmashtami in the middle of the quarter and caught most of the Dusshera Festival at the end of the quarter.

To give you a quick overview of the quarter, Metro Brands has delivered consolidated revenue of INR476 crores for the quarter, an increase of 47% against the corresponding quarter of the previous year, with a PAT of 16.4% and EBITDA of 31%. Our consolidated gross margins for this quarter came in at 57.4%, which is in the range that we target, of typically being between 55% to 57%, and this despite the end of season sales that we typically run in Q2, along with the anticipated inflation to input costs that we had.

We saw our biggest growth come from the over INR3,000 price range, which continues to reinforce our strength as we cater to the affordable premium segment of the footwear market. On the growth side, Metro Brands continues to see strong growth in terms of volumes and value across all formats and tiers. While we're excited about our growth in brick-and-mortar stores, our growth trajectory continued in E-commerce as sales grew by 50% year-on-year for the first six months of the year. We opened a total of 37 stores. We relocated four and closed five for net growth of 28 stores for the quarter across all our formats. We are on pace to open the 260 stores over the next three years that we guided to in our RHP. Despite lapping sales that includes pent up demand from last year, we anticipate demand to remain through the wedding season.

Now coming to our recent share purchase agreement that we signed to acquire Cravatex Brands Limited, this is a very exciting and synergistic acquisition, which is aligned with our expertise with footwear retailing in India and fills the athletic and athleisure whitespace in our portfolio of brands. FILA is an international brand with a rich heritage in the athletic space, and Proline is a well distributed sports apparel brand, also with a rich heritage in India. In the coming weeks, we will be working on integrating the companies to unlock the potential of this acquisition.

With that, I will turn it over to our CFO, Kaushal Parekh to take you through more details of Q2.

Kaushal Parekh: Thank you, Nissan. Good afternoon, everyone and welcome to Q2 earnings call of Metro Brands Limited. As you all know this quarter marks closure of one year of reopening of Indian economy post COVID-19 restrictions. Metro Brands started FY23 on a strong note, both from operational and financial performance standpoint. During this quarter also, Metro Brands has continued to demonstrate strong resilience.

Before moving on to the financial numbers, I would want to discuss two points which will help understand this quarter numbers in the right perspective. Although these points have been called out in our earlier discussions, I feel this is relevant to mention and repeat them again here. The first point is on the seasonality that we see in our business. In our case, Q1 is generally about 25% of the full-year revenue. Q2 is the smallest with around 22% to 23% of annual revenue. Q3 is by far the biggest around 27% to 28% of the revenue, and Q4 is again around 25%, in that range. Q2 generally is the smallest quarter and hence revenue number needs to be seen considering this point.

Second point is on the gross margins. In our industry, we generally see two end-of-season sales, one in Q2 and another in Q4. Hence, gross margins for Q2 and Q4 gets impacted due to end-of-season sales. So, if you're seeing absolute performance for Q2 and Q4, as on a standalone basis, you will see impact of end-of-season sales coming in.

To summarize in brief, our revenue for this quarter is to be seen considering point number one, on seasonality, that is Q2 being the smallest and gross margins needs to be seen in light of point number two, that is adverse impact that we see on account of end-of-season sales.

With this, let me start with a quick snapshot of financial performance of MBL, starting with revenues. On a year-on-year basis, Q2 FY23 revenue was up by 47%. On a half-year basis, our revenue was up by 116%. Because of seasonality, as I discussed, on QoQ basis, quarter-on-quarter basis, revenue was down by around 6%. Now if we compare it with pre-COVID period, that is, if we compare with H1 FY20, our revenue was up by 66% on a standalone basis. Similarly, if you compare it with Q2 FY20, our revenue was up by around 70% on a standalone basis. So, the growth that we saw even in Q1, similar growth percentage continues even when it is compared for Q2 and H1 together.

Also, on a revenue front, key highlight for the quarter has to be our performance of E-commerce sales. We achieved highest ever E-commerce sales of INR41 crores, which was up by 21% on our y-on-y basis.

Moving on to gross margins, this quarter we delivered stable gross margins of 57.4%, which is more or less in line with margins that we saw in Q2 of last year. For H1, gross margin reading is strong at 58.6%.

Lastly, moving on to bottom line performance. For Q2, we delivered EBITDA of 31% and PAT of 16.4%. If you see it for H1, EBITDA is 33.6%, and PAT was 18.7%, respectively.
With this, I'll close and hand it over back to commence with our Q&A session.

Moderator: Sir, should we open the floor for Q&A?

Nissan Joseph: Yes please.

Moderator: Thank you. Thank you very much. The first question is from the line of Tejas Shah from Spark Capital. Please go ahead. The current participant has moved out of the queue. We take the next question from the line of Gaurav Jogani from Axis Capital. Please go ahead.

Gaurav Jogani: Yeah. Sure. Thank you for the opportunity, sir. My first question is, we know with regards to the store openings. So, if you see specifically in terms of Crocs, the store addition there have been just two or three stores in the past two quarters that we see. So, anything on that front?

Nissan Joseph: Okay. I will take that first question. So, we typically try to open as many Crocs stores as we can before the monsoon season because the monsoon season is one of the largest for Crocs. And at the end of it, we don't want to be disruptive to our stores. We continue to want to expand and see opportunity for all our five concepts to grow as part of that 260 stores that we guided to.

Gaurav Jogani: Okay. Okay. Sure. Thanks. And sir, my next question is with regards to, if you can help us out how the demand conditions are panning out in Q3. The reason why I asked this question is because unlike the normal year, this year, some of the festivities have fallen in Q2. So, in that light, how do you see the Q3 panning out? And does your yearly percentage, as Kaushal had mentioned earlier, does that changes it in that light?

Nissan Joseph: So, we did have a shift of a couple of festivals into Q2. But actually, we did, we only caught the starting of this Dusshera, and with the tail end of Dusshera fell into Q3, so there was not much of a significant shift. When we look at the shift in the total business, it's not going to be significant. We believe that the numbers, the contribution of each quarter is going to remain about the same year-on-year. And you know, we continue to monitor our business. This is not the first time we've gone through a shift in demand caused by shifting festivals or wedding seasons and we're aware of how to measure through it. We believe that consumer sentiment is strong.

However, you have to remember last year, this was the first time we came out of COVID. And there was some pent-up demand. That demand is fungible from the standpoint that you're not going to buy 3x number of shoes, just because you haven't bought shoes in three years. So, we do understand that we are going to be looking at some very steep numbers. So, we're able to read through that, and we continue to feel that, that demand in the consumers in our segment, as I indicated in my opening remarks, the section over INR3,000 saw the biggest increase. That premium consumer is still out there shopping and wants to shop and hasn't finished the pent-up partying yet from COVID.

Gaurav Jogani: Sure. And sir, just last question from my end is with regards to the other expenses and the employee cost line items. So, if you see, quarter-on-quarter, they have kind of increased around 8% odd. This against the revenues have not actually commensurately increased, and as you mentioned that Q2 is generally a lean quarter. So, anything to read in that front?

Kaushal Parekh: So, Gaurav, we've seen some increase in salary costs, both at the back end and the front end. There are specific reasons for the same. At the back end, obviously, this is also preparing for having talent right on time, for all the growth initiatives that we have. FILA, we've already announced one acquisition in this quarter. At the front end, we have seen some increase. This is predominantly on account of opening of new stores. Again, based on the opening numbers, the staff comes in a bit early. So, these are basically two reasons we have seen some slight increase in costs. Obviously, revenue would start flowing from new stores, say which opened up in the second, later half of this quarter. We will have full revenue coming in from next quarter and salary costs would start getting absorbed from the next quarter onwards for all the new stores.

Gaurav Jogani: Sure. So, likewise, that could be also used for the other expenses, I am guessing, maybe a higher marketing cost in Q2?

Nissan Joseph: During COVID, I think we were very conservative in our marketing spends, in our travel spends. Those aren't sustainable, right. You have to do marketing. You have to travel when you have a geographically dispersed fleet of stores. So, we have started instituting that back into our system and have been doing it for a little bit, but it has picked up considerably in the last few months. And we think that's important for whether it's scoping out real estate in different geographies, or if it's just ongoing supervision of our 672 stores.

Kaushal Parekh: Also, Gaurav, we opened 28 stores in current year. So obviously, when you open the stores, the marketing costs goes on day one. Also, in current year, you would have seen that Diwali is slightly preponed. So obviously all the marketing activities just goes in time so that we hit the customer segment right on time, before the festivities sort of starts.

Moderator: Thank you. The next question is from the line of Tejas Shah from Spark Capital. Please go ahead.

Tejas Shah: Good afternoon. Sir, first question pertains to, since we have COCO network across and then you spoke about pent-up element of demand also visible in the last part of, last year, mainly. The number that we are generating now, what percent and this is a slightly vague question, but what would you attribute to pent-up demand or do you believe that there's a real demand buoyancy that you're seeing the market and pent-up is behind us?

Nissan Joseph: As I mentioned earlier, the pent-up demand was there, but it was really at when COVID finished. If you hadn't bought shoes for three years and if you buy one shoe every year, you're not going to turn around and buy three shoes to make up for it. You're going to buy that shoe. It just all happened to be, I would say was more a concentration of buying more than it is really pent-up demand. That demand is over. And so, when we look at our numbers and we see ourselves growing against those numbers, I think it speaks to both, the strength of our business positioning and also the strength of our consumer.

Tejas Shah: Great to hear, sir. Second, you spoke about seasonality between 1Q and 2Q. So, just wanted to understand, is it that the realization drops because of EOSS and mix change or even volume of pairs sold also drops dramatically between 1Q and 2Q in our business?

Kaushal Parekh: So, Q2, Tejas, in India, that's the peak monsoon season. So, for us, we are not big in rainy shoes. And hence for us, Q2 is slightly smaller. Obviously, in the end-of-season sale, we see, because of the discounts, we see volumes there, however, realization is slightly lower. But predominant reason for lower sales is the monsoon season rather than anything else.

Nissan Joseph: Though it favors Crocs, which is only one of our five concepts. The other four concepts unfavored by monsoon.

Tejas Shah: Fair enough. And the last one, if I may. On FILA and Proline, FILA in particular, the brand has bigger aura than the revenue unfortunately generated in the country. So, what are your plans in terms of route-to-market strategy and sourcing strategy? And what is the royalty that will have to be paid to run it in the country?

Nissan Joseph: Okay. So, I agree with you, Tejas. I think FILA is under penetrated and under indexed in the Indian market today. We see huge opportunities for that brand to grow and become a significant player in the athletic brand space. The other exciting part to it is, it's not only a distribution agreement, where we can distribute the global products developed by FILA. It is also a licensing agreement, where we're able to make certain categories of FILA under license from them for the Indian market. So that's the two facets of it that is very exciting to us. To do that, you need scale. And fortunately, for us, our fleet of stores are able to provide scale as we start expanding into the license business. We also see opportunities to build the brand from a mono brand, an exclusive brand outlet perspective. The brand is going to need to be catered and curated through the inception.

So right now, we're focused on first of all, integrating the two operations. As you imagine, any acquisition, any merger requires a great deal of integration to happen. First and foremost, ensure that you've built the foundations for that business to grow, both from a technology standpoint, and from a human capital standpoint, but also to figure out, not to figure out, but to position it to and then take it start the march of the journey down towards where you want to position the brand over the next 10 years. And we see it as a long term play. It is a long-term license. The licensing royalties, we believe are more than competitive, and is in line with what we would generally see in such an agreement, but we believe it is even more advantageous than most.

Tejas Shah: Thanks, and Happy Diwali to the whole team there.

Moderator: Thank you. The next question is from the line of Aliasgar Shakir from Motilal Oswal. Please go ahead.

Aliasgar Shakir: Yeah, thanks for the opportunity, and congratulations on that fabulous numbers. I have three questions. First is on, if you could just help us with, in this year, what would have been our price increase versus 2Q of FY22? So out of the total growth, if you could help us with the volume price mix?

Nissan Joseph: So, to answer your first question, our average price increase is somewhere in the 5% to 7% range. And that is that is a factor of two things. The factor one of inflation costs, but it's also a factor of the basket of goods that we're selling. So those are the two drivers to it. And I hope that answers your question.

Aliasgar Shakir: Yeah, that does answer. Just a quick follow up there. So, I mean, you did speak about the market demand traction that you are seeing, but, in the lower end of the market, we see a lot of players seeing a lot of pain. So, are you also seeing at any of your lower end, I understand that you are at a much higher ASP, but at any of your lower end, any kind of pain and I mean if you could just help us understand this demand in the ongoing festive season does continue or you see any kind of change in the demand situation on the ground?

Nissan Joseph: So, I think you have got to read between the lines in our business of the lower end of the segment. We vacated quite a few price points because of the GST hike that happened at the turn of the calendar year, right. So that was one reason for exiting some of those price points.

We were forced to, when there was a 7%, 700 basis point increase in the GST rate. So that was number one.

But the second thing is, our focus to become an affordable premium major player in that space and continue to hold that space and we operate with a totally different client. So, to give you perspective on the lower end of the pyramid, I don't think we're the right people to ask for that. What I can tell you is, we continue to see the demand for our products, priced at mid-to-premium range to be very strong.

Aliasgar Shakir: Understood. Second question is on your store addition. So, during our IPO, we had guided for about, I think to 240, 250 store in the next three years. Now that we have Fitflop, as well as contracts with FILA, as well as Proline, should that store addition pace accelerate significantly?

Nissan Joseph: So, just to clarify, we had guided to 260 stores, without counting Fitflop in there, right. That was the actual count. So Fitflop would be incremental over that 260. FILA will be incremental. However, I think the timing of that incrementality needs to be seen, simply because we will rationalize stores that are either unprofitable and currently in the network, or that don't add to the brand ethos that we want the brand to build to. So, while you might see some initial fluctuations of store count, strictly attributed to FILA, net-net, it is going to be accretive to us, that have both in value to the business and also in value of stores, in the count of stores. That's the short answer, Ali. By quarter, we might see a few fluctuations in which we will be transparent about where those fluctuations are coming from. So, people will have the sense of confidence that we're continuing to be on track for our 260 for our core base business.

Aliasgar Shakir: Would you be able to quantify if this will go up by what you know, I mean, probably 20, 30 stores or it could be significantly higher given that FILA has a much larger opportunity in the market?

Nissan Joseph: See, FILA has a significant opportunity in the marketplace, right? You look at our Crocs fleet, it is north of 180 stores. We believe that brand like Crocs and FILA and all of them play in about the same pace of demand. And maybe even more like you rightly pointed out, with FILA having a wider and a deeper demand than a Crocs might have in the Indian market. We are going to evaluate that very carefully. We, as you know, at Metro Brands are very, have a deep operational rigor and financial discipline. So, we look and we also look at things from a long-term perspective. We have performed consistently over many, many years, and we intend that to continue. And we intend to, FILA to be accretive to us at that same level of performance that we maintained in the past. So, whatever we feel is the best course of action to get to that point is what we will execute as opposed to try and hit a target number of stores that might be a little bit less than at this stage of the game. Having said all that, there's definitely opportunity like you said, in the FILA brand in India.

Aliasgar Shakir: Got it. And just last question is, with this acquisition, we also have a play in the apparel, as well as I think, Proline also has equipment business. So how do you see that? Will this be periphery business along with your footwear, or you expect, you your brand to kind of even expand in categories beyond footwear now with these brands?

Nissan Joseph: I think the easiest way to look at it is, we don't think apparel plays a space in our Metro, Mochi and Walkway stores, right. And we don't see that needing to come into that space. In the other spaces, we believe that apparel has immense opportunity. The size of the athleisure and the athletic apparel market is considerably bigger than even the footwear market is. So, we think there's an opportunity there. How we slice and dice then, and I'll be very candid with you. While we know what we're very, very good at doing, which is operating retail shoe stores in India, we also know that, that requires some talent and a team put together, and we're assembling our best way forward on the apparel business. But we do see that as an opportunity for India as well, both, not only in direct apparel, but also the adjacent categories that go with a brand such as Proline.

Moderator: Thank you. The next question is from the line of Nikunj Gala from Sundaram AMC. Please go ahead.

Nikunj Gala: Yeah. Good afternoon, everyone. So, I have a few questions with respect to FILA only. So, currently how many EBO stores they have right now?

Nissan Joseph: Well, I think, Nikunj, thanks for that question. I think it's a little early to count those stores, because we believe we need to rationalize that store number considerably. And to give you that number of stores today, we don't think would be a good representation of what we think it needs to be right size to, before we set on our growth trajectory for it, right. So, in a rough number, if you want to know, it's about 20 to 30 stores, and I say that simply because we are in the process of rationalizing them.

Nikunj Gala: Sure. Okay. No issues. And secondly, you're like, during your due diligence, did you find any inefficiency in the operation or the low hanging fruit, which, because when we look at the margin profile here, at the due operating profit level, so still, it's very low as compared to the other brands? So, do you see any low hanging fruits where, due to your expertise, you can easily bridge that gap?

Nissan Joseph: Well, obviously, the low hanging fruit that you mentioned is, is that they are under-indexed in India, right. So right there, that is the low hanging fruit of sorts. We have a big network of stores. Our Metro Mochi stores are capable of selling footwear. As you know, we do a large business with Skechers, and Adidas and now Puma as well. All of those are opportunities for FILA as well. And we believe we can grow the athletic business in our existing portfolio of multi branded stores. So that is something FILA didn't have before.

So immediately, if you were talking about a low hanging fruit, we do have our own store chain and fleet, that we can grow the brand there. I think there's numerous other low hanging fruits that we're evaluating, and we'll continue to evaluate. And that, I think we remain excited for it simply because we know that we can have line of sight on some of the low hanging fruit out there.

Nikunj Gala: Sure. And when we look at the gross margin profile of the product, which they have, and the similar to the other companies, that is lower to what we are enjoying right now, 55% to 57%. So, from the margin perspective, or the ROC perspective, do you think it will be dilutive initially, till the time you integrate, and when you take over the entire business, you will reposition the brand to match your margin and the ROC expectation?

Nissan Joseph: I'd rather speak to a long-term plan. I think in the short-term, there might be blips, a little bit left, a little bit, right and I don't want to start commenting on every little blip that we might face along the journey. What you need to know is that, we have a long-term view on FILA. We have a long-term view where it's going to be accretive to the value of the business. It's not going to be dilutive. We've done these kinds of things before, not to this scale. So, we know what it takes to run a business that is at par or accretive to our existing business. The really exciting thing about the whole thing is it is speaking to a whole different consumer. But we believe that the financial fundamentals of FILA will be very much in line with our expectations.

Kaushal Parekh: Also, Nikunj, adding to the gross margin that you referred to for other players, without naming anyone, they, you also need to study composition of the sales that they do. See, our focus is, as Nissan mentioned, over a period of time would be on EBOs, MBOs, our own dotcom website and obviously, marketplace sales. We will also do selective distribution, which will be predominantly on the outright terms basis. Whereas if you see for others, they also have good quantum of franchisee stores, and when you have those franchisee stores coming in, obviously it takes hit on the gross margins, because you pass on certain margins to franchisee for them to run their operation. So, that needs to be seen in that light.

In our case composition we may continue to follow our COCO, Company Owned Company Operated store approach and hence, this is strictly not comparable as such.

Nikunj Gala: Yeah. Thanks for that. Any incremental investment have you planned for this plan apart from the INR200 crore acquisition? Like any rough work you've done on the incremental capital you would need to allocate here?

Nissan Joseph: We've carefully considered the capital allocation required for both, the acquisition and also to reposition the brand. Repositioning of brand does cost capital. The good news is, Nikunj, all of this capital would be done without raising any more debt, given that we do have cash as a company. So, it's one of those things we'll continue to evaluate what gives immediate payback, what gives long term payback and it needs to be a balance between those two as we do our capital allocations.

Nikunj Gala: Sure. Thank you. And lastly, just from the revenue perspective, how much, how big would be the non-footwear revenue contribution in the existing INR150 crore of sales what they are doing?

Nissan Joseph: It's about 50%-50%, 40%-60%, 50%-50% coming from both, the Proline business and the FILA business.

Farah Malik Bhanji: But also, you need to remember that once we take it on, this is a business that has a long gestation period, unlike our current business. So, for instance, in most sports brands and in imported brands, you see that they've already bought in for spring summer. So really, you'd see the change in the third quarter of next year, in terms of how we're going to run it, and what we do with it. So that's something to keep in mind. And I think all these numbers will get fine-tuned once we can evaluate, dig deep and just take on and put our stamp on how we want to grow this business.

Nikunj Gala: Okay. But from your perspective, your focus would be largely in footwear or you also want to focus on the non-footwear part or build the team there? Like just want to understand that thing.

Farah Malik Bhanji: Like I shared with you, once we evaluate, we do realize there's a lot of opportunity in there. It would be too soon to comment on that. So maybe in a couple of months, once we have a little more clarity about how we want to run the business, we'll be able to sort of help you with that.

Moderator: Thank you. The next question is from the line of Prerana Amanna, from Shome Partnership. Please go ahead.

Prerana Amanna: Yeah. So, first of all, thanks for the opportunity. And congratulations, especially to the management. Very few people are able to walk the talk, especially with the store addition. So, congrats for being on track. My first question is based on Walkway. So last quarter, we saw that Walkway didn't perform well in Tier-1 cities and in Tier-2 and Tier-3, it performed well. And even this time, we're seeing that growth has been more from the INR3,000 range above categories. So, are we losing market share in that category, like Walkway and below INR3,000?

Nissan Joseph: So, I think the way that I would read that is even Walkway is seeing price increases driven by inflation costs and driven by the GST increases, right. So that's what you're seeing a culmination of that. It is not that we're seeing the business dramatically differently in Walkway, compared to the rest of it. We think it's a different business than the rest of our business.

Prerana Amanna: Okay. And how about Fitflop? I know Fitflop is a bit premium range, but since it is priced at extremely high, like how is the consumer demand over there?

Nissan Joseph: We don't think it's priced extremely high. We think it's priced well, but the consumer demand on Fitflop has been very strong for us. We know we opened our first store in Chennai, in Express Avenue Mall and it performed above our expectations. So, we're pleased with that. We also are seeing Fitflop sell very well in our multi-branded stores of Metro and Mochi.

Prerana Amanna: Okay. And my last question is based on price increase. I know, last quarter, we had an average price increase of 7%. So, have you taken any price increase in the last three months, that is between Q1 and Q2?

Nissan Joseph: No. In fact, the good news is we're starting to see the input cost stabilize. And while there's always the possibility of a spike, caused by some geopolitical macro reason, we don't see that as, as much of a threat today, though, we're acutely aware of that threat. And we constantly try to hedge our inventory to make sure that we don't increase, we don't have to increase prices right now.

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

Ankit Kedia: Sir, couple of questions from my side. First is on the channel mix. If you can share for the acquisition, how much comes from EBO distribution and online?

Nissan Joseph: So, most of the businesses, a distribution business, followed by E-commerce, followed by EBO business.

Ankit Kedia: Sure. And is it for both the brands, Proline and FILA?

Nissan Joseph: I'm giving you the average between the two.

Ankit Kedia: Sure. Kaushal, a question for you. We see nearly INR50 crore of inventory and INR90 crore of debtors on the books. Do they also come with the acquisition to us?

Kaushal Parekh: No. So acquisition, we've just signed the agreements. Obviously, post the completion of CP conditions only after that consolidation would happen. What you see currently is obviously built up for the upcoming seasons and the new store opening that you see. Even from an E-commerce point of view, we were approaching the season in slightly higher debtors.

Ankit Kedia: Yeah, I was speaking more from the acquisition balance sheet of Cravatex. If you look at their balance sheet, they have a INR50 crore of inventory and around INR90 crore of debtors on their books. Do they also come with the acquisition or we need to…

Kaushal Parekh: Yes. So, obviously, since we're doing 100% buyout, all the net assets that will be there in the business as of the closing date would come. We will be taking it over.

Ankit Kedia: And are all the 20 to 30 EBOs which Nissan mentioned are COCO EBOs or FOCO EBOs for FILA?

Nissan Joseph: It is a combination of both, predominantly franchise.

Ankit Kedia: And do you think over the period of time, you want to convert those EBOs to COCO EBOs or you predominately feel that franchisee model is good for FILA?

Nissan Joseph: So, we believe in relationships and partnerships and honoring partnerships that Cravatex might have entered into, right. So, it's not a question of do we want to convert them to company owned, company operated stores? The question is, you know, what is right for the franchisee? If it's right for us to do right by the franchisee to keep them on, we will be more than happy to support them. Having said that, though, the future models of the business, we will be strongly leaning towards the company owned, company operating model. And having said that, I say that only because you know this is a different space to our other business. So, we want to be acutely aware that we want to be open to different ways of slicing this. But we would be tempted, if that is the word, to opening company owned, company operated stores first and foremost.

Ankit Kedia: And one last question. From a three-year perspective, do you think the margins of the Cravatex can be near the Metro Brands' margins or it will take some more longer?

Nissan Joseph: Within three years, I think the answer is yes, it will be accretive to our business. And we have no reason to believe that it wouldn't be, otherwise, we wouldn't be acquiring the company. I think we all know that FILA is a well-known international brand. A few years ago, FILA was actually the number one selling athletic brand in our stores. So, we do see the opportunity. We know that we have that customer in our stores. It is a matter of positioning that brand correctly for the Indian market, given the competitive landscape in India as well.

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

Devanshu Bansal: Thanks for the opportunity. My questions are on the margins front. So Q3, should see higher fresh sales versus Q2. So, what is the reason behind sort of gross margins remaining at 55% to 57%, when we have already done about 57.3% in Q2?

Nissan Joseph: So, Devanshu, we like to run a financially disciplined business, right. And we believe that by setting our targets at 55% to 57%, it ensures that we're not missing opportunities of certain price points, even in the premium segment. Even in the premium segment, we do have key price points that we want to hit. Sometimes to hit those price points, you might have to move your margin points, a few points to the left. We think the best way to capitalize on the market share in the Indian economy is to not be rigid about trying to move a margin up and be more focused on ensuring that you're delivering value for every product that you bring out to the market and driving revenue and incremental sales through that. And hence, this position we've taken to say, we're comfortable with 55% to 57%. We're comfortable with 30% range of EBITDA. We're comfortable with 15% plus of profit. And, the three engines on that plane seem to work really well for us. Have worked well for us over the last 10 years, and we believe will continue to work well for us going forward.

Devanshu Bansal: Got it. And sir broadly, it just wanted to check on the EBITDA margin front also. So, for a longer-term, medium-term perspective, since your focus is on value, sort of providing value to consumers, 30% is a good estimate with some operating leverage built in with scale?

Kaushal Parekh: Yes, Devanshu. I think that could be a correct assumption.

Moderator: Thank you. The next question is from the line of Vikas Jain from Equirus. Please go ahead.

Vikas Jain: Hi, sir. Thanks for the opportunity. Sir, my first question, just to, I heard in one of your comments, you mentioned that we are assembling, in a process of assembling a team to run an operational, operationalize our athleisure wear brand business. Right? Is that correct? Is that we have recently acquired? Sir, are we in the process of assembling a team to them, our athleisure wear business that will be coming out from these two new acquired brands, is that correct understanding?

Nissan Joseph: That is correct. Yes.

Vikas Jain: Okay. And sir, one more thing. I was like, reading the previous annual reports for Cravatex. There I found that the FILA, the date which it started with Indian operations, till FY20 numbers that I'm talking about, what according to you, so it incurred EBITDA losses in FY20. Whereas it was largely a normalized year of operation. So according to you, what is the missing part into the growth strategy for FILA that we would actually fill in? What was wrong with it in the past?

Nissan Joseph: I don't want to comment about what's right or wrong in the past, specific to FILA, but I can tell you, for a brand to be successful in India, it needs a couple of things. What it needs first and foremost is scale and velocity through door counts, right? Profitable door counts. It can be in doors that are costing you more to do business, and then you're making in business. And that's something that Metro Brands offers any brand in the footwear space is scale, at a profitable level. So that's number one.

Number two, is to have a steady supply. And to have a steady supply of goods, you need to be well capitalized. You need to have sourcing capabilities, not only domestically, but internationally. Right. And so for that, Metro Brands is positioned for any brand, to be capitalized and source products on a timely basis, and make sure there's a good steady flow of products, because if you don't have products for a season or two, the consumer migrates from you, and it's very hard to get them back.

Number three, you have to make significant investments in marketing on a consistent basis. That's another thing that requires capital and Metro Brands has the capital to do that, and the wherewithal to do that. So that's the third thing you need.

So, when you look at all the things that a brand needs, you know, many brands stumble on a lot of these areas through the journey. And when they do stumble, it becomes quite a vicious cycle for them to try and pull out of it. And we believe that with a steady strategy, after we evaluate the business, and we look at its potential and we put a roadmap together, that we would be able to unlock the potential that FILA brings.

Vikas Jain: Sure, sir. Understood. And sir, one last question. The products or the footwear that we are manufacturing, the FILA used to manufacture, we will have these manufactured at our vendor base only, right? They won't be imported at least, right? Is that correct?

Nissan Joseph: We're going to have a combination of both imported and localized products. Don't forget, our consumer wants the global trends. And so that's why we want to have to give them access to the gold global trends in product. We also believe that there's a lot of elevated products that exist in the global range that we would like to bring to India to elevate the brand. At the same time, we do have good sourcing capabilities right here in India and we're proud of those capabilities, that we would continue to source that group of products that makes sense on the local for local production, but we want to have a holistic 360 brand that offers the consumers what they perceive an international and expect from an international brand.

Moderator: Thank you. The next question is from the line of Sagar Jethwani from Phillip Capital. Please go ahead.

Sagar Jethwani: Yeah. Sir, what was the revenue contribution of discounted product during the quarter? This is my first question. And my second question is on that, we have been focusing on the sports category although we have other four brands in the sports category now. I believe that the revenue contribution of the sports category would be less than 20% in our case. So, we have been more focused on you know, party wear formals, casual footwear, etc. So now, coming to the four sports category, there are already established players. How do we plan to position ourselves in this category, sports category?

Kaushal Parekh: Sagar, I'll take the first question. The end-of-season sale or discounted sales contribution in Q2 was around 8%. And if you see it for H1, it was sub 5%.

Nissan Joseph: And to answer your second question, Metro does stand for a family footwear store, right. And that means, especially in the Indian market, we sell a lot of dress, ethnic, formal wear and casual ethnic wear too, right. And we don't want to go away from that. Having said that, we believe that we want to own the footwear wardrobe of a consumer. And this gives us an opportunity to further increase the breadth of the wardrobe that we would command for our consumer.

You are right, today, actually, the sports contribution is less than 20%. But when I look at the growth that was first induced by COVID, it has been quite phenomenal. It has been very strong for some of the other sports brands that we bring in from the outside where their largest customer in India. So, Metro has the capability of selling athletic shoes. Having said that, we're not going to get far away from our DNA of being a family footwear store, or a complete holistic footwear store in our Mochi store as well. We believe the opportunity lies not only in our MBOs, but also building the brand as a standalone.

Now, you rightly said there is competition in India. But there's also a huge growing market, a market that comes from two sources. One is the organized sector growing faster than the unorganized sector. Our middle-class incomes rising and consequently, aspirations rising, the whole awareness of health among the Indian population and an overall leaning towards sports as a way of life as opposed to just PT session in school and the fourth period, right. So, all those things create tailwinds for this category. So, while the competition is always something to be considered, let's not forget, it's a fast-growing wide category that has a lot of headroom left in it to grow. And we just want to make sure we position FILA correctly with a competitive advantage that can sustain that growth.

Sagar Jethwani: So, any growth number that you have in mind that you achieve to clock in next two years, only in the sports category? Any thoughts on that?

Nissan Joseph: I think the financial discipline that we have doesn't go that way. What we go is the other way. we say how do we have healthy growth? And what's the number for us to have healthy growth, right? Healthy growth. When I say healthy growth, I mean, gross margins, I mean, EBIT, and I mean, PAT. We start there, first and say, what's the best we can make? How do we hit that triangle, that vortex the best? And then we figure out what kind of growth that can then lead to and that's how we work it. So, we come from financial rigor first, as opposed to sales enthusiasm first.

Moderator: Thank you. The next question is from the line of Sabyasachi Mukerji from Centrum PMS. Please go ahead.

Sabyasachi Mukerji: Yeah. Hi. Thanks for the opportunity. I have two questions. First, on the acquisition part. So, I understand that you are kind of building a team for the athleisure apparel segment. And with this acquisition, do you intend to come up with your own brand, a new brand altogether for the apparel athleisure segment?

Nissan Joseph: Okay. So, we are fortunate that it's not like Cravatex did not have a team in place, right. So they have a team in place that has been running the business and we think we can support them better, given our scale and given our operational capabilities. So that's number one. And we are adding talent to ensure that it has adequate fuel and firepower in that segment of our business. We do have the brand Proline and we do now have the brand, FILA. Both of them we believe completes this spectrum of goods that you would expect to see in the athlete and the athleisure market. So, as of today, there are no plans to launch another brand in that space.

Sabyasachi Mukerji: Okay. Thanks. Next question. My second question is a bit of bookkeeping one. What was the ASP numbers, average sales price for Q2? If I may know.

Kaushal Parekh: It was around INR1,450.

Sabyasachi Mukerji: So, the INR1,450 number is for Q2, not H1, right?

Kaushal Parekh: This is for H1. So, for Q1 it was INR1,500 and for Q2, if you see, because of the reduction sale, it was around INR1,400. So, on an average, for H1, it is INR1,450.

Sabyasachi Mukerji: So, the presentation that contains the average realization for each brand, all the numbers are for H1, right?

Kaushal Parekh: Right. Right.

Moderator: Thank you. The next question is from the line of Akshay Kothari from Envision. Please go ahead.

Akshay Kothari: Thanks for the opportunity. Sir, what would be the current ASP of FILA?

Nissan Joseph: Probably somewhere in the INR3,000 to INR5,000 range.

Akshay Kothari: Okay. And sir, I was just checking out the Cravatex website and there are other brands like something called as, Vans - Off the Wall. These brands we have not acquired, right.

Nissan Joseph: We're in the process of discussing that with Cravatex, to how to best migrate the other brands. But today, we are focused on FILA and on Proline, because we know that we have deep focus on those two. But we're not close to some of the other brands that they have in their portfolio. That we'll evaluate once we finish the due diligence and close the deal.

Akshay Kothari: So, this INR202 crore is only for FILA and Proline.

Nissan Joseph: No, it includes all the brands.

Farah Malik Bhanji: It includes all the brands. And we acquired all of them. It's just that we have to evaluate which ones we continue to grow and which ones we may change.

Akshay Kothari: Okay. And the BB UK one also? BB UK. It's something foreign 100% foreign subsidiary they are having.

Farah Malik Bhanji: Yeah. So basically, we've acquired the 100% shares of the company. So, whatever comes with it.

Akshay Kothari: And Paragon has of course, taken the full exit.

Farah Malik Bhanji: Correct. That's correct.

Akshay Kothari Yeah. And I think you mentioned so far, there are certain obligations relating to license fee. So, could you clarify something on that?

Nissan Joseph: As with all brands, you have to pay some form of licensing fee or royalties, right. And so, FILA comes with that as well. Proline does not. Proline is the brand that we will own outright. So, we don't have to pay any licensing fees to anyone. But FILA has licensing fees, and from what we know in the market, the licensing fees are more than competitive.

Moderator: Thank you. The next question is from the line of Tanmay Gupta from Motilal Oswal. Please go ahead.

Tanmay Gupta: Yeah. Hi. Thank you. Sir, we have studied that the cost-to-MRP for the international brand is near about 1:7 or 1:8. So what could be the cost to MRP for FILA?

Nissan Joseph: We have no reason to believe that it would vary. But as you know, to do it right, we would evaluate how do we position it from a price standpoint, from a position standpoint, and ensure that we work on that from a customer backward lens, as opposed to a markup lens going forward. But we believe, bottom line though, Tanmay, is that FILA, once we are able to set it on its course will be accretive, both, in value in all our three segments of our how we count our business, margins, EBITDA and PAT.

Tanmay Gupta: And sir, like what would be the cost-to-MRP for our Metro and other formats?

Nissan Joseph: So, a simple way to look at it is, our gross margins are 57%. Right. That gives you a good indication of what at least the range that we will be looking at. And we believe that FILA would fall in that range as well. And simply, don't forget, when you have a wholesale business, that moves the numbers a little bit to the left, a little bit to the right, but it also moves your costs equally in that same pace. So, if you have a wholesale business, all of a sudden, you have no retail costs associated with that sale. So, what we really like you to take away from this, Tanmay is, we are committed to maintaining our performance of Metro of 55% to 57% that we've done for many, many years and we intend on maintaining that going forward with both, FILA and Proline in our mix, in our portfolio.

Tanmay Gupta: And sir, is there, like the margin for sports and athleisure brands are a little higher than the formal brands or the other categories. Is that so?

Nissan Joseph: Here's you got to understand those businesses tend to be a little bit more of a fashion business. So, while it looks like it might have better margins on the front end, you may not have it on the exit end. Having said that, that's why I keep sticking them and trying to let you know that what we focusing on is, we want to make sure that this hits our price ranges and margin ranges of 55% to 57% and is accretive to what we're doing and not dilutive.

Moderator: Thank you. The next question is from the line of Rajiv from DAM capital. Please go ahead.

Rajiv Bharati: Oh. Thank you. Thank you for the opportunity. Sir, in between you made a comment that FILA and CBL could have similar kind of sensitivities. So possibly, in terms of store size, and also the clear thing, Crocs, you basically have Crocs India as an intermediary and in FILA you won't? So, what is that delta in terms of where you source via Crocs India?

Nissan Joseph: Yeah. Again, I think I have to really guide you back to the 55%. Because when we source from Crocs, though there's a margin in between for the intermediary, as you pointed out correctly, Rajiv, they also have costs associated with it, too, whether it's design development, import costs, duties that they pay, running staff, running marketing. So, you got to be careful that you don't get overly drawn by the sexiness of what factory exit prices and what the MRP is. You've got to really consider the cost structure in between, and the input costs that go in from when it leaves the factory, to when it actually gets sold, and actually to get it made at the factory even, right. So be careful is what I say in focusing on that. I want to assure you again, that we believe, we will be able to get FILA and Proline and in the run and to be accretive to the three pillars of our financial pillars, which is our EBITDA, our PAT and our gross margins.

Rajiv Bharati: Sure. Sir, In terms of distributions, sir, LFS is off the table. Is it? Apart from doing MBO on Metro and Mochi, otherwise, LFS is not focused in the FILA distribution?

Nissan Joseph: Overall, today, LFS is a big part of their distribution, right, So what we saw, I spoke to on MBO and EBO business as the low hanging fruit that somebody brought up. It's not that LFS is off the table. You know, right now, as we evaluate it, we look at all those opportunities to see what those lines of distribution will mean, to position the brand correctly in Indian market. Positioning also comes with the word access, right. We want to make sure that our consumers have access to the brand. So LFS do offer access to many consumers that we need to respect.

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

Ankit Kedia: Sir, just a clarification needed. When you talk about the ASP of INR1,500, does this include accessories, because if I look at your price range, more than 85% of your products are about INR1,500. So, if I exclude the accessories, then what could be the ASP of footwear alone?

Kaushal Parekh: So, Ankit, yes. The number that you see is inclusive of accessories. If you just take footwear, the overall ASP would be in the range of INR2,100 to INR2,200, broadly.

Ankit Kedia: And this ASP is including of GST, right?

Kaushal Parekh: This is on net sales. So, this is net of GST. At MRP level, it could be higher. You need to add approximately 17.5% to18%.

Moderator: Thank you. Ladies and gentlemen, this was the last question for today. I now hand the conference over to the management for the closing comments. Over to you, sir.

Nissan Joseph: Thank you all for being on the call this afternoon. We had a terrific Q2. Metro, our team has performed and delivered well in line with our expectations. We are excited about the FILA and Proline opportunity with the acquisition. We believe it has a runway, it's the white space for Metro Brands and we believe in capitalizing on it in a strategic and careful method. Thank you all again. Happy Diwali.

Moderator: Thank you very much members of the management. Ladies and gentlemen, on behalf of ICICI Securities, that concludes this conference call. Thank you for joining us and you may now disconnect your lines.