

Crompton Greaves Consumer Electricals Ltd.

Conference Call

February 09, 2016

Moderator: Ladies and gentlemen, good day and welcome to the Crompton Greaves Consumer Electricals Limited Conference Call. As a reminder all participant lines will be in the listen-only mode and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing '*' then '0' on your touchtone phone. I now handle the conference over to Mr. Shantanu Khosla. Thank you and over to you sir.

Shantanu Khosla Thank you. Good evening and I would like to first of all apologize for the slight delay but we were just waiting for the upload of the numbers to happen on the site. I am Shantanu Khosla. I am here Bombay and with me I have Matthew Job – our CEO, Sandeep Batra – our CFO, Yeshwant Rege – our Strategy & IR Head and Geetesh Ahuja who is part of Yeshwant's team. I would like to first of course welcome you all and thank you all for dialing in this evening and joining this call, which is our first call with our company Crompton Greaves Consumer Electrical Limited. What I will do is I will give some brief overview remarks but we would like to keep most of the time for questions that you may have and dive straight into that. So let me begin.

This quarter our business continued to perform strongly delivering sustained double-digit growth both on top and bottom line. For the quarter ended December 15 revenue grew 12% to Rs. 810 crores versus Rs. 723 crores in the corresponding quarter of the previous year. Operating profit at Rs. 99 crores was up 14.6%, a little under 15% versus a corresponding period last year. Since numbers are not directly comparable what we have done from an operating profit and growth point of view is we have taken the reported consumer business segment PBIT as reported by Crompton Greaves last year and compared it with our comparable operating profit this year. All categories, all broader groups continue to perform strongly, delivering a double-digit growth largely behind some key new initiatives across most of our brands and strong go-to market programs to drive reach and availability. Now the operational transition of the business is largely complete. For me and my team it has been quite a hectic past 3 months as you can imagine but it is now largely complete from an operating point of view and has been in my opinion extremely successful. I would like to point out that the strong business results were achieved while we were transitioning into the new company. An experienced management team is now completely in place. This team is a mix of both great external talent and also outstanding talents that have been working on the Crompton Greaves consumer business earlier. We have appointed 3 eminent independent directors, created our own independent go-to market organization and set up the required corporate functions to enable the company to operate as a completely independent entity. From a regulatory and legal point of view also things are going well and are on track. As most of you probably are aware we gained approval for the demerger scheme from the Honorable Mumbai High Court on the 20th November. This was then filed with the Registrar of Companies Maharashtra. Accordingly the effect of the scheme has been given from October 1st, 2015 the appointed date. Subsequently we have also received formal approval from the registrar of companies. Additionally Crompton Greaves Consumer Electricals Limited (CGCEL) is in the process of moving forward and on the next key steps on listing of the new company. We see this also on track. In fact, CGCEL has filed the appropriate application with the stock exchange and the Part B approval for the same has been received. We expect the listing process to continue and get complete in due course. Obviously it is difficult for me sitting here to predict the exact time because it will have to go through the appropriate processes at the stock exchange and regulatory authorities but expect that we should be in a position to have the listing around April. While we are very happy with both the transition and our continued business results, moving forward of course we see great opportunity to continue to drive and

grow the business. Our key focus areas as we look forward to grow the business is going to be one, investing and building the Crompton brand. It is a wonderful brand. It has great opportunities, outstanding equity but we need to invest in it. Second, we need to identify build and succeed with consumer meaningful innovation in our core categories. Third, we need to further build and invest in our go-to market reach and also invest in improving our capabilities in new and emerging channels like the modern trade and eCommerce. Fourth, we will be leveraging systems and best in class processes to drive operational results and efficiencies and finally last but in no way the least we will be building organizational capabilities across the length and depth and breadth of our organization. These will be our focus areas moving forward and we do see potential to continue to successfully grow this business. So that is really it in terms of what I wanted to share with you in terms of an overall perspective and now we will be very-very happy to take any questions you may have. We will do our best as a group to answer them on this call itself. Thank you.

Moderator Thank you. We will now begin the question and answer session. The first question is from the line of RenuBaid from IIFL, please go ahead.

RenuBaid So the first thing that I just wanted to understand is though we have seen sales growth coming a tad little slower in this quarter, can you just elaborate a little more with respect to how the individual categories have performed for the YTD or the for the quarter and if you can also share little more details with respect to the medium term growth outlook across categories and for the company as a whole from say 2 to 3-year perspective?

Shantanu Khosla Okay, first just to clarify so we have our data points right. This quarter's growth is higher than last quarter' growth i.e. than the July, August, September quarter as a total company. Secondly, all our operating businesses fans, lights, pumps and also appliances all grew in double digits, so there is healthy strong growth across all the categories. The fans market based on the best data that we have looks like over the last few quarters it has slowed down and if I look even at the published results of the last 2-3 quarters of other competitive businesses their fans growth in total, though there are exceptions seems to have slowed down. So in spite of the market seeming to have slowed down possibly because of factors such as slow construction, less investment in new housing etc, we continue to grow ahead of what we see the market growth. I think the last part of your question was on the future. I will refrain from right now talking about immediate forecast and how we think the future in the near term would be. However, what I would mention is we would expect of ourselves that we consistently grow ahead of market growth.

RenuBaid And for the particular quarter would it be possible to share individual category wise growth rates for fans, appliances, pumps?

Shantanu Khosla I am sorry but at this state, and we will definitely as we work out our segment definitions in the future, we will be more than happy to share that in the future but at this stage because we are still in interim, have not worked out segmental details yet.

RenuBaid Sir my second question is, it clearly seems from a margin perspective that despite being a seasonally weak quarter, compared to the historically reported numbers under Crompton Greaves Segmental numbers, margins are ted lower. So can you elaborate a little with respect to the increased cost structure after the demerged entity has come into shape and also what has been the incremental spendings on branding, advertising of the new logo, the brand etc?

Shantanu Khosla First just to get the facts on the table, you are absolutely right, the October, November, December historically has been a lower margin quarter because of seasonality. However, versus last year October, November, December the margins have actually improved. In fact the number I have is the growth is 14.6% quarter on quarter with about 20 basis points improvement in margin quarter on quarter. I think your second question was in terms of what has been the change in investment. In this quarter there has been no change in investment levels versus historical threats.

RenuBaid Okay, so no incremental spending that we have seen on the new brand and advertising per se.

Shantanu Khosla Not in the October, November, December quarter.

Moderator The next question is from the line of Harish Biyani from Kotak, please go ahead.

Harish Biyani Sir my question is on the corporate expense, is it possible to share either this quarter's number or the 9 months' number and related question would be on the A&P, what would be possible the A&P number in this quarter and likely path ahead is more important given that we would want to focus more on brand building and where you suggested in your initial comment that investing in CG brand is going to be a key focus area. How much is the A&P spending potentially going to increase in the next 1 to 2 years?

Shantanu Khosla Let me take the second part of question. Very clearly one of the articulate choices I have shared just now and we have made is that we are going to invest in building the Crompton brand. I would not at this point in time like to start giving specific A&P numbers because that is forward looking but definitely without a doubt we are going to invest in building Crompton brand because we believe it is a right thing to do for the business and the brand and value creation. It is a significant opportunity, we will be investing in A&P to build the brand. I think your second question was regard to details on corporate expenses. If you do not mind me ducking on that a bit right now Harish

Harish Biyani Second question is on the lighting market where we have seen the increase in LED procurement from the government. Given that fact, what is the kind of impact that you are seeing overall on your lighting business growth (a) and (b) impact on margins if possible if you can share in the outlook for the next one year and the appliances business from Crompton has been relative small, so what is the focus area and new product that you would want to launch in the next one year?

Shantanu Khosla Okay let me try that because there are a couple of parts for your question which Harish I am sorry but for competitive reasons I will not go into too much details, which is like what are our specific plans and choices on margins and appliance focus areas for the future because that for me is business proprietary and I would not like competition to find that out. On the first part of your question without a doubt in our opinion the move to LED which is supported and helped by the government programs is an outstanding thing. We are seeing that LED is growing fast but frankly it is only at the beginning of its potential and the inflection point is what we are seeing in front of us right now. I believe it is a fantastic thing for two reasons. Number 1, it is good for the country simply because of the amount of energy saving LED conversion can create. But number 2, it is great for the consumer. It actually gives a far-far better consumer experience and it is just much nicer to be in an LED environment whether you are looking for concentration, you are looking for eye strain, whatever may be your need. So it is a wonderful thing in every way. Now it is up to us and the industry but we do what is in our control to best deliver propositions and cost structures, which delight the consumer, so the consumer wants to buy LED thereby resulting in significant power saving for the country. I think we have only just begun the journey but the faster we can make this transition the better we can manage the uncertainty of any such significant transition, the stronger we will emerge out of it. So it will be a critical focus area of us moving forward.

Moderator The next question is from the line of Ankit Babel from Shubhkam Ventures, please go ahead.

Ankit Babel My first question is can you provide us with the balance sheet details or how the net worth you are starting with and what is the net debt on the book?

Sandeep Batra Without going into the specifics, this business is quite an asset lite business, works on negative working capital. So as on the appointed date i.e. 1st October we had an obligation to allot shares, one share for each shareholder of CG so that will mean an equity capital to be allotted of about Rs. 125 crores. There is a loan of Rs. 700 crores that has transitioned to this company. On the assets side there is some amount of fixed assets and there is a negative working capital. So the entire residual amount will sit as goodwill as per the demerger scheme, so which will be about Rs. 750 crores odd.

Ankit Babel But sir net worth including this share capital is it negative or positive?

Sandeep Batra It will be positive. We have not made any losses.

Ankit Babel No, no it is not about losses, because you have a negative working capital.

Sandeep Batra No, no if you look at only equity plus results it will be positive.

Ankit Babel Okay, so what is the fixed assets sir?

Sandeep Batra Fixed assets is about 70-80 crores is the book-value of assets.

Ankit Babel Sir my second question is now you have a debt of around Rs. 700 crores, can we expect that this will be your first priority to repay the debt whatever cash flows you generate in the next couple of years?

Shantanu Khosla I think that is a decision which I think we will take as we go forward. It is not always bad to have some debt on the balance sheet. And as long as our cash flows are adequate to service the debt I would not see personally any great hurry to try and repay that debt.

Ankit Babel What will be the utilization of debt sir?

Shantanu Khosla Sorry just one point to add to that on the debt. We see that we will be able to generate sufficient funds given the strength of the brand and the positive cash flows that we forecast that we will be sufficiently robust to make the appropriate investments to drive the business. These will be investments in brand, these will be investments in innovation, these will be investments in systems and processes, these will be investments in go-to market.

Ankit Babel But sir all these investments including your increased A&P, will it come at the cost of margins or you expect whatever are the annualized margins of the segment historically you can maintain that?

Shantanu Khosla Again, I would not like to comment on what are forward guidances on margins, what I can assure is that everything we do, everything we invest will be tested against the filter of our confidence that it will create value. And at least operating value is created by only building three things, top line growth, cash growth and profit growth.

Ankit Babel And sir lastly can you just give us what was the corporate expenditure for this quarter which was excess because you said that your PBIT before that was around Rs. 99 crores and the reported number is around Rs. 80 crores.

Shantanu Khosla About Rs. 20 crores is the total corporate expenditure which includes some amount of expenditure which we have separately shown for demerger and in that corporate expenditure there will be some amount of one-off expenses.

Ankit Babel How much would it be one-off because just wanted to understand what could be the recurring number?

Shantanu Khosla I do not think at this stage we are very clear of what the overall structure will be of the corporate function which will include recurring cost. I think by the time we have our next call we will have a much greater idea.

Ankit Babel How much was one-off in this quarter?

Shantanu Khosla One-off would be about 2-3 crores.

Ankit Babel So it is fair to assume a Rs. 15-16 crores quarterly run-rate is possible.

Shantanu Khosla Well your assumptions I guess you need to make but I think what Sandeep is saying we are still settling down in our structure, we still have some areas which we need to potentially invest in. We have got other areas where we could drive efficiency and I think how this pans out in terms of actual rupee spending quarter on quarter. We need to see how it comes over a few quarters but I guess it is not going to suddenly become three to four times more or one tenth the amount but it is only one quarter numbers.

Moderator The next question is from the line of Venkatesh P from CitiGroup, please go ahead.

Venkatesh P Before the Crompton consumer business actually lists on the stock exchange; will you be providing disclosures on the – see effectively this is like a new company to everyone because under the previous fold of consumer we did not have that much amount of information about the consumer business other than broad headline. So will you be providing like a document or a disclosure under stock exchange which gives a description about the business and some numbers and may be an audited balance sheet as of date. Audited balance sheet will it be provided on the stock exchange before it lists?

Sandeep Batra I think for getting the shares listed there is a document which the stock exchange requires the company to provide. It is called an information memorandum which has some prescribed information to be provided and that we will provide.

Venkatesh P As of now you do not know the date when this listing will happen, right?

Sandeep Batra No, we do not know because that is not something which is totally in our control. So first of all Crompton Greaves will have to fix the record date to decide which shareholders will be given shares of CGCEL. Those shares will be allotted post the record date after which we will make an application to the stock exchanges for listing depending on when the stock exchanges give their approval. One more information memorandum will have to be filed and then the share gets listed. So it is a process which has to be gone through.

Venkatesh P Okay. A broader level question for Shantanu. Now, I guess you have been appointed by the private equity holders, so what exactly is your mandate?

Shantanu Khosla Just to clarify I have been appointed when I first came into this entity I was appointed by the Crompton Greaves company with a Crompton Greaves appointment letter as an Executive Vice President as of July 1. As of current now I am appointed by the Board of Directors of CGCEL. My mandate is very clear. My mandate is to build shareholder value for all shareholders. My personal approach to building shareholder value which is we are incorporating in our strategy is to build a strong sustainable business and a strong sustainable organization. I believe that if you do those two things that is the best way to build sustainable shareholder value, which is my fiduciary, moral and professional responsibility via the board to all shareholders of Crompton Greaves Consumer Electrical Limited.

Moderator The next question is from the line of Inderjeet Singh from Macquarie Capital, please go ahead.

Inderjeet Singh My first question is to Shantanu. Shantanu I have looked at this business for now almost 7-8 months and now this being a separate company. What are the key things that you are likely to do differently compared to what Crompton Greaves used to kind of do on the side of the business? If you could kind of just throw some light on that.

Shantanu Khosla I would be happy to. Thank you for the question. It is actually pretty much encapsulated in what I said are the five choices and focus areas which we have developed. A lot of them do require some amount of change but importantly also understanding and retaining the current stand for the business. Crompton fans did not become market leaders by accident. First what I believe needs to be stepped up is investment in building the Crompton brand. Over the

previous few years there has been very limited investment and for example, it is very seldom that you see the market leading brand have low awareness. So one is definitely investing in the Crompton brand, building its equity. Second is bring the consumer at the center of our innovation. Crompton has done some great innovation. The innovation tends to be technically driven. So the second key area which we want to focus and we have already building capabilities in that area is bringing the consumer and the consumer need at the center of the innovation process in the core category. The third is go-to market. Now like I said we actually are very-very strong in one critical channel for this business and that is the electrical channel. However new channels are emerging. We are getting into new businesses, such as small appliances. Consumer LED is a huge area of potential growth. To maximize these opportunities we need to strengthen our ability to win in other channels also. The fourth is systems and processes. Like a lot of you may be aware, we currently have a service agreement with Crompton Greaves to provide us information and data etc. from the current system, we are ever fully intending to invest in our own system. For that we want to ensure that we are designing the best with processes which are robust so we can truly maximize the opportunity this business gives. The fifth and last but definitely not least is capabilities. How do we really strengthen our capabilities and as we build our business strategy we have actually identified which are the critical capabilities which today we may not be as strong in but to achieve our business strategy and goals we need to build those capabilities. So the last is invest in that capability building.

Inderjeet Singh

Actually my second question is on this quarter and second quarter numbers. Now, though we had a 12% year on year growth in this quarter do you think that there was some slip up in revenues because of the transition which was happening in terms of the company structure, people being moved around and would you be able to kind of give a broad path number if there was indeed some kind of a slip-up on revenues?

Shantanu Khosla

Actually one of the things I am proudest about the organization is that there was nothing which we could quantify and identify as an impact on revenue in this period and if you think about it that is a huge testimony to the quality and the commitment of our people and employees. They went over and above. One of the areas for example, which could have been a potential risk was the fact that we had to switch packaging across every one of our brands from old company name to new company name etc. on the 1st January and people were working 48 out of 24 hours to manage to make that happen all along the supply chain. So there is nothing actually which we looked back and said, here is the significant loss because of the transition. Now moving forward there are growth opportunities which we need to leverage as I talked.

Inderjeet Singh

Last question is I may squeeze in. Now, at some point of time as this new share start to get listed and the existing promoters or the new promoters of Crompton Greaves Consumer would be required to make an open offer as mandated in the SEBI and there will be certain discussions by the investor groups regarding what should be the open offer price and those kind of things. Is there anything that the management would want to talk about as to what is the thought process behind that or update us what discussion you guys had with the SEBI on that?

Shantanu Khosla

From a management point of view, we will ensure that whatever is required from a regulatory point of view is done. That goes without saying. Now, how the prices determine the etc is to beyond and something between the promoters and SEBI. It really is not anything which involves the management. We will ensure that appropriate regulatory authorities aspects are followed, it is transparent, it is correctly done. That is our responsibility but process for open offer and the price at which open offer is made, that is up to really promoter and SEBI.

Moderator

The next question is from the line of Deepak Agarwal from Elara Capital, please go ahead.

Deepak Agarwal

Sir my first question is can you elaborate more on the growth opportunities that you are looking especially like is there any path that the management is thinking of inorganic growth combined with organic growth in each of these verticals?

Shantanu Khosla We are open to any growth opportunities that make sense to the consumer and to your stakeholders. So we are not approaching this with any do's and don'ts. I would mention however that in my initial look at the business I see plenty of opportunities if we do our job right for organic growth. Beyond that I am afraid, do I have a plan or do we have a number, I cannot comment on.

Deepak Agarwal Secondly you mentioned like there is lot of new alternative channels that are emerging apart from your traditionally strong electrical channel, so can you comment on the number of distributors that you plan to add over the next few years and what kind of strategy that you plan to improve your penetration in each of the segments?

Shantanu Khosla I can answer the second one. I am sorry I will not answer the first one, which is how many numbers we plan to add. Our strategy is simple. We want to make sure that we have the right product available in the right store at the right time when the shopper wants to buy and deliver this at the lowest cost. So it is all like I said that we want to make our brands consumer centric. We want to make our go-to market shopper centric. So it is our responsibility to have our brand available at the right shelf in the right shop at the right time that the consumer wants it there.

Deepak Agarwal And can you share what is the approximate number of employees that has been transitioned to the new entity?

Shantanu Khosla I think in total around 1500.

Deepak Agarwal So almost the entire consumer portion, whatever employees were there they have been transferred to the new company?

Shantanu Khosla More or less.

Deepak Agarwal And my last question if I can squeeze in, just a bookkeeping question, what would be the cash and cash equivalents as on December 31st?

Shantanu Khosla Cash and cash equivalents would be about Rs 50 crores as on 31st December.

Deepak Agarwal Because I did see hardly any other income during the quarter.

Shantanu Khosla So these are all end of month flows.

Moderator The next question is from the line of Vijay Raghvan from Spark Capital, please go ahead.

Vijay Raghvan Basically on Crompton they have two distinct channels, one is electrical channel and other is appliance channel. And Crompton is not something new into the appliance channel. So we have seen Crompton's stoves in some of the markets, Crompton's mixtures in some of the markets. So how are we basically trying to ramp up this category going forward basically?

Shantanu Khosla Thank you for the question and I am sorry but I am going to sound like a tough record. This is as applicable for appliances. #1 invest in building the brand. #2 have consumer meaningful innovation. #3 further building our go-to market reach. #4 leveraging systems and best in class processes to drive efficiencies and #5 building organizational capability. These are the five critical choices and focus areas and it is as true for appliances as it is for LED lighting. Now our job is to obviously make it more granular and then to have us execute against these choices brilliantly.

Vijay Raghvan There have been a lot of management changes, senior management level. Can you spend couple of minutes on what all the kind of people we hired both at the top and the middle management level?

Shantanu Khosla All the people who are in the critical positions or running our categories and running our regions are from Crompton Consumer. They have been ranging from 30 years to some 3 years. Myself, Matthew with his very-very relevant strong successful experience and track record in first many years in Phillips and then running the Racold Company. He is from outside as is Sandeep who has brought outstanding relevant experience that can really help us on this journey from his previous role as CFO of Pidilite.

Moderator Due to time constraint the next question will be the last question. The next question is from the line of Bhargav Buddhadev from Ambit Capital, please go ahead.

Bhargav Buddhadev Sir one point you highlighted was reaching to the customer at low cost. Can you elaborate a bit on that sir?

Shantanu Khosla Think of this as the cost from our factory gate to the customer shelf and this is our job. How do you get the right product at the most efficient cost all the way from the factory gate to the customer shelf. And this involves a number of things as part of the supply chain, right. It is all the way from your ability to forecast that correctly, ship effective truckloads, have the right warehousing network, leverage the scale that we had in Crompton with multiple categories etc. So that is also our responsibility because it is very easy to get the right product everywhere. If I put it on a plane and air ship it out to Lucknow but not very cost-effective. So how do you do this with the lowest inventory levels across the entire channel, that is more profitable business for everyone and ultimately the consumer benefits.

Bhargav Buddhadev So does this also imply that possibly we could also look at increasing our promotions and basically doling out some schemes to distributors to get an edge over competitors?

Shantanu Khosla Not referring to that area because that is a different area. That is how much are you investing in the customer. I am talking about simply what is the cost of getting the product off the shelves.

Bhargav Buddhadev Okay, because we were interacting with a few channel partners in December and they were saying there is a marked difference in terms of promotional schemes which are being offered from December compared to the earlier months, so that is where I was coming from.

Shantanu Khosla With my 30 plus years in Proctor & Gamble and my 7 months in Crompton is that whenever you speak to a channel partner or your shopkeeper the first thing he will complaint about is promotion and margin.

Bhargav Buddhadev No, I mean this time around they were very happy so I am sure you are taking good care of them.

Shantanu Khosla I think they are happy more because you know ultimately the #1 thing that any customer or retailer wants is for a consumer to come to his store and ask and buy the product. So I think things which make the customer happy is not really just discounts, and we tend to get fixated on that. It is ranks with a consumer pull. It is a service to the customer. We get the product there at the right time in the right way. It is how you work with the customer to build his business. Now though we have got a lot of work to do, we have already begun implementing over the last 3 to 4 months, better approaches to improve our service, better approaches to improve the way work Joint Business Plans with customers and a better demonstration of our customer's business tool, it matters to us and we grow together as partners. So may be the feedback you are getting is a part of that and if it is I am actually very happy.

Bhargav Buddhadev And sir lastly is manufacturing on the agenda, I mean are we looking at setting out factories or we will continue with outsourcing out module given of asset light approach to the business.

Shantanu Khosla Well today we roughly manufacture about 50% of what we sell. Now again we will source in the way that makes sense. It does not have to necessarily be A or B. Whatever is the way that makes two criteria. #1 Delights the Consumer and Consumer. No 2, maximizes value creation.

We will choose to source that. Along this journey somewhere of course we plan to sell more than what we sell today. So obviously we will have to source more than we sourced today. And as we come across though having to take the decision, we will take the right decision for the business and for the customer and consumer.

Bhargav Buddhadev

Thank you very much for the clarification and all the best.

Shantanu Khosla

Thank you so much. I think that was the last question but thank you all very much. I really appreciate all of you taking the time to join in and I hope we have clarified some, if you have further clarifications, you may contact Yeshwant but as we list and as we move forward we will ensure that we maintain the process of engagement and sharing of information because our desire to be consistently open and transparent.

Moderator

Thank you. On behalf of Crompton Greaves Consumer Electricals Limited, that concludes this conference. Thank you for joining us and you may now disconnect your lines.