"PDS Limited
Q1 FY '24 Earnings Conference Call"
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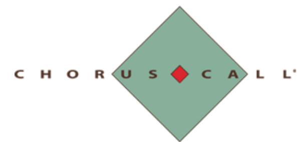

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MODERATOR: **MR. IQBAL KHAN – NUVAMA**

Moderator: Ladies and gentlemen, good day, and welcome to the PDS Limited Q1 FY '24 Earnings 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 star and then zero on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Iqbal Khan from Nuvama. Thank you, and over to you, sir.

Iqbal Khan: Hello. Good afternoon, everyone. On behalf of Nuvama, I welcome you all to PDS Limited Quarter 1 FY '24 Earnings Call. Today, we have with us Mr. Sanjay Jain, Group CEO, Mr. Rahul Ahuja, Group CFO; and Ms. Reenah Joseph, Head of Corporate Finance, M&A and Chief Investor Relations Officer.

Before I hand over the floor to management, I would like to highlight that the safe harbour statements on the second slide of the analyst presentation are assumed to be read and understood. With this, I now hand over the floor to Sanjay Jain for opening remarks. Sanjay, over to you.

Sanjay Jain: Thank you, Iqbal. A very good morning, afternoon, and good evening to all our stakeholders across the time zones, and a warm welcome to our Quarter 1 earnings call. There has been a bit of a connectivity issue at this end. So, for any logistics issues, the line drops from our end, kindly stay put, we should be back in a few seconds. And I apologize if there's any inconvenience because of this.

I would begin by saying that the performance for this first quarter, should be seen in light of three-four key aspects. Firstly, the macroeconomic uncertainties have an impact on the demand scenario as we have been mentioning over the last 6 months that the first 2 quarters of the financial year '23- '24 could be a bit choppy because of the market condition.

Secondly, quarter 1 in terms of seasonality, usually is our leanest quarter. However, the Quarter 1 FY '23, last year, on one hand, I'm saying the Quarter 1 is leanest, the Quarter 1 last year also benefited from the tailwinds of the pent-up demand in a post-COVID restriction scenario. So, these are a couple of factors that one should look at. And one more thing is that the Bangladesh operations, usually, in the first quarter, there is one Eid break and then there is a second Eid break in the second quarter, but both the Eid breaks happened during the first quarter, that kind of increased the number of idle days for which the factories were shut, our factories and also factories in general for production from about a little close to 9 days to about 16 days or so.

And we, however, have cautiously navigated the last couple of months and anticipate to do so in a muted environment. But the good thing is that the signals that are coming in from our main markets wherein we operate where U.K. and Europe are about 75% of the top line of the company, the signals that we are getting are good with anticipated recovery in the second half of the year have all started to crystalize.

It is also important that while on one hand, the reported top line which is largely coming in from the design-led sourcing business has shown a decline, the gross merchandise value that we have handled during this quarter, has actually increased 13% over the same period last year. And if you observe that the gross merchandise value that we have reported as part of our investor release

is about INR3,000 crores, whereas the top line of the company is about INR2,100 crores. That means approximately INR900 crores worth of business that we handled during the quarter actually is a contribution from the new initiative of sourcing as a service and the newly acquired Ted Baker business.

So therefore, this makes us feel that with the passage of a few months, while the design-led sourcing business should bounce back because of these signals that are coming in. There is already a good contribution setting in from the new initiatives that we have taken.

And the interesting thing is, on the one hand, while there is a demand disruption that is there, but it is also unfolding into newer opportunities for us. We have earlier shared with you that sourcing as a service was one opportunity. We also mentioned about complete sourcing solution contract that we got from one of our retail customers in Germany. So, therefore, the company is actually gradually migrating the journey of being a solution provider to our retail customers, and therefore, also building in businesses with higher margins. That's also one of the reasons that amongst others, the gross margin directly expanded close to 2.75% in the quarter as compared to the last year's same quarter.

And of course, while we remain positive about the anticipated recovery, but we also have the lever in hand in terms of any cost optimization that we may have to ever do in the later part of the year. But at this stage, we remain very positive.

During the quarter, we also successfully completed the acquisition of Ted Baker design business, and we are currently in the process of integrating it. And if I take the first almost 2 weeks plus we completed the acquisition sometime in June month, and we already have achieved good financial performance.

But before I come to the numbers from Ted Baker, The Ted Baker Design Group will serve as the global hub for the Ted Baker brand and help us manage the global design and merchandising functions. Further, this entity will function as a core licensee and operating partner for Ted Baker having the wholesale business in the U.K. and Europe.

So, what I mean to say is, on one hand, there is a service fee that we are getting for handling the back end with respect to designing, merchandising, and enabling sourcing. But at the same time, having got the wholesale business, these are the two revenue streams that are coming in from this business, while we spent close to about INR150 crores for which we actually got an equivalent amount of working capital in the business, we anticipate that this business we are gearing up, we are working towards annualized turnover of about INR475 crores to INR500 crores in that range, broad range. And we believe this business has a potential of about 7% to 9% profit margin. So therefore, there is, from a ROCE perspective, we are already foreseeing this business to be the 30% plus range. And now if I come to the first 15 days of the performance post our takeover, the business has reported INR30 crores top line with approximately 9% bottom line in the two-week course of the takeover.

And another interesting aspect is that the Ted Baker acquisition is actually leading to many more such opportunities now before us. So, if I rewind the clock from a Hanes sourcing as a service

business, we actually saw Asda sourcing as a service business coming our way. And we close similar such contracts and got $1 billion worth of orders. And you saw a contribution of INR900 crores coming in from such businesses in terms of GMV on top of our top line of INR2,100 crores that we handle.

And now the Ted Baker opportunity, the first step unfolding well in a silo in terms of its own viability but also leading to unfolding of many such opportunities. So therefore, in these turbulent times, while we anticipate the main design led sourcing business to bounce back the new initiatives are beginning to contribute a lot to what we are doing.

Now if I come to the manufacturing capabilities, we feel as a very responsible, PDS on the whole in terms of ESG compliances, we're going to make sure that our own 2 factors in Bangladesh keep embracing the highest trend of ESG governance standards. So, we saw the installation of solar power panels in our Bangladesh factory, Greeng Smart Shirts; and this would enable us not only on one hand, further the path of cleaner power, but also would lead to cost savings of annualized approximately INR70 to INR80 lakh per annum. And about 12 to 18 months back, we had brought in a change in the leadership team of our factory Progress that actually has resulted into Progress factory making money. We believe there was a need to also augment the leadership team of Green Smart Factory, wherein we have actually brought in a new team of CEO and a Chief Operating Officer, who spend close to 20 plus years in the industry of manufacturing and selling garments to global retailers.

So therefore, having achieved the turnaround, we want to make sure that there is permanency in terms of making profits and then gradually taking up the curve. But as I said earlier, the manufacturing operations this quarter does have an impact of longer Eid break and also on the whole there has been a muted demand or so. So, with this, I would hand it over to our CFO, Rahul Ahuja, and who will take you through the financial performance for the quarter.

Rahul Ahuja: Thank you, Sanjay. Good afternoon, and good evening to everyone. On the commentary for our financials for the first quarter, we concluded FY '23 on an optimistic note. That you were aware of the headwinds in the coming quarters. For the quarter ended June '23, we reported a topline of INR2,115 crores with a gross margin of 18.7%. Quarter 1 is usually a lean quarter in our industry. However, Q1 FY '23 was exceptional as we benefited from the pent-up demand and re-opening of economies post Covid 19 lockdowns. Other than coming off a high base of last year, Q1 FY '24 experienced a slowdown due to the global economic headwinds impacting spending power and demand, leading to an inventory buildup with large retailers and brands. We believe that this phase is temporary with some spillover in Q2 and have a positive view for the latter half of this year.

The muted demand enabled us to capture better margins. Gross margins have improved by 279 basis points from 15.9% to 18.7% quarter-on-quarter. We reported EBITDA for the quarter of INR67 crores with an EBITDA margin of 3.2%. The EBIT for the year stood at INR51 crores with a margin of 2.4%.

Profitability, however, was impacted by interest costs mainly attributable to the increase in the base rate, average SOFR increased from 0.7% same time in the same quarter last year to about 4.9% for Q1 FY '24, approximately a 7times increase in the interest rates.

Tax outflows were primarily attributable to the profitability of companies, including Ted Baker in the UK jurisdiction attracting a higher tax rate. As a result, in spite of operating profit being at similar levels as that of last year, our profit after tax witnessed a decline with a profit of INR23 crores.

Revenue from our sourcing segment stood at INR2,031 crores with an EBIT of INR45 crores and a return on capital employed of 38% for the quarter.

Our Manufacturing segment reported a revenue of INR117 crores and an EBIT of INR4 crores. As Sanjay mentioned, given the Eid holidays, wherein both the Eid's were in the same quarter this year, during the month of April and June, two of our factories were shut down for the holiday period impacting our production base. Roughly the number of holidays were more as compared to the same quarter last year by about 7 to 8 days.

Moving on to our balance sheet, net debt stood at INR26 crores versus INR115 crores reported in June 2022. The reduction in our cash balances compared to our position in March '23, was mainly attributable to the acquisition of Ted Baker business that we did in June. We operated on a net working capital of 2 days. The company delivered a 31% return on capital employed and a return on equity of 27% for the quarter ended June 2023.

The company maintains a stable financial position with a net debt-to-EBITDA ratio of 0.06x. We will continue on our growth journey having prudent on operating costs and retaining our balance sheet size to achieve higher returns for all our stakeholders. We will now open the line for any questions that you might have.

Moderator: Thank you very much. The first question is from the line of Akshat Sam from SAM Capital.

Akshat Sam: So, there's a couple of questions at my end, so first question is more about our unique partnership model. So, we have over 100 subsidiaries, and we are adding more every year because of our unique model as I said. But also, there are a lot of multiple subsidiaries operating in the same geography. And then they compete against themselves to win businesses also haven't we better served by consolidating some of the subsidiaries as I say, operating in the same geographies, I mean, which will lead to more cost savings and other synergies. Mean it will also help with management on where you have better oversight and then a smaller number of subsidiaries in say a particular geography. So yes, that's the first question.

Sanjay Jain: Yes. Let me take the question then on one by one. So, on the subsidiaries, I think this is an inherent part of our business model. Where in a normal company, one would take an employee on board and then kind of incentivize employees, whereas we actually take an entrepreneur on board in lieu of an employee and the entrepreneur actually has a share profit.

And this is very clearly identifiable in hands of a prospective entrepreneur when he or she has a shareholding in that legal entity. So, therefore, this is very much an inherent part of what we do

and how we operate. And this is likely going to be in a similar manner as we take along because we were in a given geography, for example, I would say, in Hong Kong, I have a Simple Approach business, primarily catering to customer Primark in U.K. but then it's a design led sourcing business. I have a business led by a gentleman called Eric Leddel in the name of Casa Collective in Hong Kong that focus on the home category. And there's a third business led by Gaurav PDS Far East focus on Walmart. So that's the reason entities are existing. What is important for us as a management team is to ensure that the governance continues to be strong and keep going higher and up. That is where, as we learn from our investors, we are increasing constantly our disclosures on the top 10 verticals and so on, plus the strong board that came at the listed company level. We're also institutionalizing the growth culture to the next level in terms of 10 largest verticals as well.

Auditors are largely EY or GT across the various subsidiaries. so, I guess, of course, in our company in due course of time, there are some redundancies that we can address by optimizing some legal entities. But I think this is core to what our business is, but last point, we are very sensitive to the cost aspect that you mentioned. And at this stage, the central team that manages this entire close to $1.5 billion top line and $2.5 billion GMV is about 1% of sales. And we are making sure that we don't allow it to go up, and in fact, all the CFOs that we wanted to hire in the central team are all done in using more of technology to take it ahead.

So, a long answer to your short question, but I think it's important to kindly understand this is an inherent part of our structure through which we operate.

Akshat Sam: My second question is, we are trying to position us as more of a solution provider to a lot of these companies. So, what are the business segments within the holding value chain? Are we looking to get into or expand the total addressable market? For example, we started sourcing as a service 3 years back. And also, we recently got into a logistics company in Bangladesh. So is that the other segments we are looking to expand into and what other segments within the value chain we will look to expand into going into the future Yes, that's it from me.

Sanjay Jain: I think one more point, which is a little bit reflecting on the first point that you raised, even our customers require a new entity to be put in place, for example, when Hanes signed up an annual sourcing as a service $400 million business contract, they wanted it to be done as a separate entity. In fact, the CEO there has actually has a joint reporting relationship to Hanes as well as to PDS, wherein Hanes is actually able to see the cost per business, so that's also a bit of reflection on the first question you mentioned.

Now on yes, sourcing as a service, we believe from a concept stage 18 months back to actually, it is now institutionalized. Our management team across the various verticals have got very much tuned to up to speed on sourcing as a service. So, across all the relationships, this is being offered. And let me remind you that this is not something that I'm pushing. This is also the need of the customer as well, wherein the retail customers are actually wanting to focus on their core offerings. And there were searching for credible counterparties like us.

So, therefore, to that extent, it has become institutionalized. It is a constant that we will keep increasing now in terms of our offerings. We went a step beyond while sourcing as a service for

Hanes was actually procuring from one geography of Bangladesh for them. But then for Gerry Weber in Germany, it is the entire global sourcing. So that's going up the value chain and now brand management in the Ted Baker. So, therefore, if I got your question right, we would keep endeavoring on, actually, a customer's pain is actually my gain.

So, they want somebody to take care of the entire backend. So, for example, Authentic Brands Group in U.S., they do, they own a lot of brands like Reebok, Ted Baker, Forever 21, the annual revenue that we generate from these brands is about $25 billion. So, when they are now acquiring brands, they are actually looking for an operating partner who works alongside with them, while they derive royalty, they want the operating partner to manage the brands for them as well.

So therefore, PDS is actually foreseeing a lot of such opportunities unfolding. So, our core business of design led sourcing will keep remaining intact, but the opportunity of value-added services plus new categories. In fact, about one year back, 12 to 18 months back, we mentioned to our stakeholders that we've got into home as a category. And with our existing customers, we want to do that business. With Asda, one of our large U.K. based customers, on one hand, this was a customer on design-led sourcing, we've got a $400 million plus of sourcing in a service contract, and we've got a $250 million agency contract for home business. Agency is the beginning of the journey. So that's the answer that, yes, we believe there is humongous potential, now to engage more with the customers in terms of the larger wallet of share.

Moderator: Thankyou. The next question is from the line of Sarvesh Gupta from Maximal Capital. Please go ahead.

Sarvesh Gupta: Good afternoon, sir, you said that this business is seasonal, and hence explains the Q1 fall. But how do you see the full-year FY '24 growth trends as they are as of now? And if you can break it up between H2 and H1?

Sanjay Jain: I think as we have mentioned earlier that we were kind of anticipating a single-digit growth throughout the year, because as we said, the first 6 months would be muted and the next 6 months you should see the recovery. So, therefore, that's fair answer to question, kind of single-digit growth for the entire year. And I think we are gearing towards making sure that somewhere profit should improve closer to 15% to 25% for the entire year. That's the target with which we are working in the year-end.

In terms of split in the H1 and H2, as we had said earlier, H1 at least should, anticipated to show a decline over the last year, but then H2 should see a strong recovery. So therefore, H2 quarters should be significantly better than H1.

Sarvesh Gupta: So, you are seeing 15% to 25% in terms of profit growth for the full year?

Sanjay Jain: I think I would say optimistically, it may go in that range of closer to 20 plus or so. But I think if the demand doesn't improve, then the profits could be about 10% or so in terms of, I think there's nothing like an absolute number that we're working towards. We anticipate that range that in a tough scenario about 10ish or so, but there is potential that you can actually go better than that as well as the recovery happens in the second half of the year.

But at this juncture, when we are talking to you today, all the signals are very good. Customers are taking a little bit of extra time to close their orders. But the engagement level with our customer is very intense and the signals are all very positive.

Sarvesh Gupta: And the margin improvement trajectory that you have been guiding for a 50-basis point per year sort of that holds for even now?

Sanjay Jain: Yes. I think while notwithstanding closer to 2.75% improvement, I think a maintainable gross margin improvement year-over-year is yes, 50 basis points. There is seasonality, while every effort is there to add more value-added businesses. But to one line answer to your question, yes, we are geared up for 50 basis point improvement year-over-year.

Sarvesh Gupta: Understood. And sir, on your finance cost now, there are two questions. First of all, in your business, when you say net working capital days is only two days, but if I look at your working capital debt, it almost comes to like 25 days. So, what is the, why is there a difference between the two? And why in a sourcing sort of a business, why should you carry working capital debt at all in your balance sheet? So, if you can explain this discrepancy between these two figures of two days versus 25 days.

Rahul Ahuja: So as far as our working capital is concerned, these are largely post-shipment clients. And so we will always need once we manufacture the goods to finance our receivables, so largely, our working capital comes from there.

As far as our number of working capital days is concerned, if we were to net off our cash position, the cash margin that we carry or the cash surplus that we carry in our balance sheet, if we net them off from our working capital, that's two days. If you were to calculate just the working capital, that is the number which comes more like 22- 23 days.

Sanjay Jain: I think just to add to what Rahul said, I would say this is not a discrepancy. This is an opportunity that operating working capital days length, yes, it is two days of working capital, inventory, receivable and minus the payable days. And you rightly observed from a borrowing perspective, the number of days are much higher. We have not calculated, but I hear you, they are higher. So why the discrepancy or where is the opportunity? The opportunity is that there is always cash in the system. on one hand and then there is borrowing. And when we report net debt, we net of cash. But Rahul, our CFO, is close to about 27 years in the industry, and the first half of it was as a banker the GE and Standard Chartered and other leading banks. And I think a few of the areas that we have identified that our cash margins on the lines are much higher than what they should be.

So therefore, over the next few quarters, we anticipate that the cash margins that is there should get released. And therefore, the real debt utilization will actually come down. So therefore, what you observe as a discrepancy allow us to work towards as an opportunity to make sure that the debt itself is down rather than cash knocked off against the debt and then we talk about net debt.

So, I think I agree with the observation. We would gear towards bringing it down in terms of the real utilization of debt.

Sarvesh Gupta: And these are not the LCs that you are opening for your vendors. So, are you taking any risk on their default on your balance sheet?

Sanjay Jain: I think our LCs are a very small portion of our procurement from the vendors. If I have to say circa approximately, 20%-25% or so, as we proceed during the call, Rahul can get the number. But that's a broad number of LCs being issued. I don't think there is any kind of for default risk because every factory that we bring on board is taken on board with our comprehensive preceding 6 to 12 months of vendor onboarding process. And therefore, we are in constant touch. We have a strong team of 800-plus merchandisers on ground. For example, in Bangladesh, I pick up as one location where maximum number of factories are located that we deal with. So therefore, through our teams on ground through our factory onboarding process, we believe the exposure is low.

And I think, it is also well spread across. That's also important thing that do I have a concentration risk on our given factory, and therefore, there is any theoretical default risk, that risk is also, if at all, we say this is a risk, low risk, that is also mitigated and spread across close to 600 vendors that we deal across the globe as well.

So, therefore, to summarize careful onboarding process, being in touch through the on-ground teams. It is not that my designer team is sitting in U.K. and therefore, they are through a remote-control managed factories. There are people on ground and well spread across. So, the risk is well managed proactively and the probability of it hitting us is extremely low.

Sarvesh Gupta: So, 20%-25% of the entire sourcing is through via LC stand?

Sanjay Jain: On a given point of time, that could be the peak situation that might be there, wherein we facilitate the factory in terms of fabric procurement or trims procurement, etcetera, in the value chain. But then I think the important thing is that on the front end as well, the customer profile is also carefully looked into, credit insured, customer track record. So therefore, one should not look in a silo in terms of that fact that I'm taking an exposure on the factory. The exposure is coming because at the first step, there is an order that is emanated from a reputable customer with a track record. So that's how I need to request you and encourage you to look at the entire picture.

Moderator: Thankyou. The next question is from the line of Karan Premchand Gupta from CAVI Capital.

Karan Premchand Gupta: I'll just take over from the last question and just delve a little bit deeper, when you are factoring in your accounts receivable, are those on a recourse or nonrecourse basis to PDS. So what I was trying to ask is in case the customer defaults, then whoever is doing the factoring, can they come back to you for restitution?

Rahul Ahuja: So, our factoring is of two kinds. We largely do insurance-backed factoring wherein the risk is taken by the bank. So, the day goods are dispatched we get our money, and the risk then lies with the bank because they have taken back-to-back insurance. Largely, this is the facilities we have from our banks as far as post shipment is concerned.

Sanjay Jain: In fact, I would give the answer that the recourse to us is zero. It's under no eventuality that once the receivable is factored that they can come to us.

Karan Premchand Gupta: Fair enough. And then next, I just wanted to get a little bit more understanding about this acquisition of the Ted Baker business in the U.K. Now given my understanding is that the total acquisition cost was about INR150 crores, and you mentioned that this was all related to working capital.

Now it's a very sizable number given that you generally don't carry any working capital. So, is there a plan or a timeline by which you will be able to bring this amount in line with the overall consolidated level and thereby free up that capital? Or how do you think about this?

Sanjay Jain: Yes. I think it's an interesting observation. Yes, we have upfront written a cheque of about INR150 crores, and there is a corresponding working capital to that. And as firstly, even on as is where is basis, we mentioned about the anticipated turnover that we think this business could generate somewhere between INR450 crores to INR550 crores with about a 9% circa 7% to 10% range profitability.

So, we anticipate that this business in year 1 should give us 30% on capital employed on a INR150 crores cheque that we've written. But the upside is that we are working towards factoring these receivables on a non-recourse basis. So, therefore, it may take us about 3 to 6 months because the whole process of getting the insurance in place and getting the factoring lines activated. It takes time to get all these operational things on the ground up and running.

So as these things on the ground takes about 3 to 6 months, there is a big chunk, for example, of receivables of approximately $16 million to $17 million, which we got in our hands on day one. So, if I talk about, approximately 60%-70% of that getting factored which is about $10 million to $11 million. That means about INR80 crores-INR90 crores worth of cash would actually come back to us. 50% of cash, there's a potential, basis the existing factors through which we do our business of non-recourse factoring.

So that's the answer to your question. In about 6 months' time, we are working towards trying to recoup this back through a non-recourse factoring program. Then that should hopefully, even further increase the return on capital employed of the business as well.

Karan Premchand Gupta: Okay. So, when you say INR150 crores in working capital, is that all in receivables? Or is there a chuck of inventory? Or what else is there in that working?

Sanjay Jain: It's actually, for example, on a gross asset basis, there was about $40 million of assets wherein the inventory was what, 50%, about $20 million or so there was about $16 million to $17 million of receivables, about $1.5 million of cash, that's about $40 million, and there were current liabilities of about $20 million or so. That gives me about $19 million- $20 million of net working capital. That's giving an answer to your question as to what is the breakup and the inventory in hand largely belongs to the wholesale business that we have also got a license to do as a franchise, so therefore, this inventory would get rotated.

And when we have taken the inventory on hand, we have taken due care in terms of diligence and in terms of provisioning prior to we getting it into our balance sheet. So, therefore, this inventory comes into our hands with a careful process. But I've answered the question in terms of the breakup, $20 million receivables, $17 million on inventory, $ 20 million payable and on a wholesale business for which we are the licensee and we will keep rotating it in the normal course of business.

Karan Premchand Gupta: No, that's very heartening to hear and also thank you for discussing the inventory, and how you went about looking at the inventory because I was going to ask about that. So I appreciate it. Finally, like are there any other similar transactions in the pipeline that you can talk about? Or if you were to come across something like this, do you think you would like to take similar transactions forward and what is your appetite for those, both in terms of the number of transactions and size of transactions? That's it from my side.

Sanjay Jain: There are numerous opportunities that have actually gotten the funnel post-PDS actually getting success in sourcing as a service business and signing a complete sourcing solution and now brand management, a numerous number of opportunities, many retail customers have actually got engaged with PDS as a counterparty. And on the one hand, I'm talking about retail customers. On the other hand, the likes of Authentic Brands Group, and there were similar reputable private equity funded, well-funded, large conglomerates, companies in the U.S. who acquire brands and they look for operating partners.

So, therefore, those are the opportunities that are actually getting up in the funnel with us. But having said that, we are very careful as to how we take them ahead. We are analysing them carefully. I think the Ted Baker integration, touchwood has started on a very positive note. So, therefore, for the next few months, I think while sourcing as service contracts, we'll keep signing up where the upfront investment is minuscule.

But for any such brand management contracts, wherein there is a balance sheet allocation. I think for the next few months allow us to stay focused on Ted Baker, and bring it to a stage that I mentioned that we believe in a 3 to 6 months' time frame, there's potential to squeeze cash out.

That is where we would like to lock in if all other factors are looking good into the next deal. But we are carefully engaged, focusing on Ted Baker, but at the same time, now engage across customers. So, it's looking positive at this stage. But cautiously positive because we got to the initial 15-day experience of the Ted Baker because we got to make it up a habit over the next few months.

Moderator: The next question is from the line of Shrinjana Mittal from Ratnatraya Capital.

Shrinjana Mittal: My first question is on Ted Baker. I wanted to understand the arrangement that you have with Ted Baker. Firstly, in the revenue stream, one part of the revenue stream is a fee-based model, if I understand correctly, it is similar to sourcing as a service, is that correct?

Reenah Joseph: Hi Shrinjana, Reenah here. So, there are two streams One is where Ted Baker's, all the distribution partners, have to procure the merchandise for the categories that we have license and the design team of. So whenever they procure it, they have to book the orders through us,

where we do the design and the other elements, and on that we get a service fee, upfront as part of buying agency agreement with them. Other than that, we have a wholesale business where for the UK, and Europe, we will be taking the product in our books landed in the UK and then distributing it. We will, it's largely three-fold, we're getting the orders, getting the product manufactured, getting the products to the UK, and then sending it to the distribution partners. That is a higher-margin business where I get around 35% plus margin, and then I do a marketing spend so on and so forth. But the design team works across both the agency business or the design services and as well as the wholesale business. So, the same team has two streams of income.

Shrinjana Mittal: Sure. Understood. Sir, just the wholesale business, we'll be taking the product or the products on our book. So that means that would be all on a pre-order basis or we'll also see some inventory and then sell it, how does that work?

Reenah Joseph: Yes, it will be on a pre-order basis, where the distribution partners, the retailers currently actually coming and visiting the Ted Baker office, they are looking at the merchandise and the next season stock, they place the order, and we get it manufactured.

Shrinjana Mittal: Understood. Okay. And the INR30 crores revenue that we generated, that's a mix of both the streams and for the service, and for the fee one, it is the fee component of that, right?

Reenah Joseph: That's correct. But the largest chunk of the INR30 crores is actually the wholesale business if you see because yes, a larger part of it is on the wholesale side. And yes, the fee that comes that also is part of the sales.

Shrinjana Mittal: Understood. And like on a full-scale basis, what is the expectation revenue potential? I think last con call was mention about 90 million count, if I am correct?.

Sanjay Jain: Yes, I think, we would be kind of conservative for our first-year aspiration. So we believe somewhere around $ 475 million to upwards is what we should get in the first year of operations. And we're looking good to get there. And also, just a point to add to your initial question, which Reenah answered. For the wholesale business, the kind of cheque that we've written upfront, INR150 crores or so, is the investment that actually has gone up front. So we would be now leveraging it, to rotate it over a period of time, kept rotating it to generate that kind of wholesale business turnover. So that's the kind, and on which you mentioned about a potential 30% plus ROCE. And thirdly, the ability to squeeze the receivables out through the non-recourse factoring over a period of six months. That's where the business stands.

Shrinjana Mittal: Understood. And also on the last call, you mentioned a new contract with Gerry Weber. How where are we on that? Can you say throw light on that?

Sanjay Jain: The contract is signed. And right now, it is being operationalized. So, therefore, the integration process is underway. So, it should start contributing to our top line from this particular quarter.

So, to answer the question, contract signed, execution integration process is underway. and we should see it start contributing to our business from this quarter.

Shrinjana Mittal: And just one last question. So gross merchandise value, which you mentioned is around INR3,000 crores. So that includes sourcing as a service as well, right? Like the merchandise that we handle for sourcing as a service, but eventually, in our revenue, the service fee portion comes. So that includes that way?

Management: Yes. I think, yes, INR3,000 crores is the GMV. INR2,100 crores approximately is a topline, so INR900 crores is the GMV. The commission that we got is approximately INR40 crores-INR41 crores plus/minus a little bit here in there. It's the number that we got from this INR900 crores. There's approximately 3.5%-4% that we earned from, as an average number from handling this sourcing in the service and similar such contracts.

Shrinjana Mittal: Right. And for sourcing as a service, what would be the merchandise value that we had for this particular quarter? Okay. So 3.5% out of and INR40 crores is the revenue that you got that?

Sanjay Jain: To further give a breakup, when I said INR900 crores is a difference in GMV and sales. So that INR900 crores approximately has about 75% as the portion under sourcing as a service and 25% is the agency commission that we get from customers. That’s kind of been going on for a while. So therefore, specific to your question, 75% of INR900 crores is the GMV that we have handled in quarter 1 from sourcing as service contracts.

Moderator: Thank you. The next question is from the line of Iqbal Khan from Nuvama. Please go ahead.

Iqbal Khan: So, my question is on the income statement only See, on gross margin, we have done well, right, around 280 bps improvement. However, EBITDA. So gross profit actually increased by 6% Y-o-Y.

However, if you look at EBITDA, it has degrown by 9%. It's easily because of the employee expense, which is around. Which is now contributing around 9.5% of the revenue right? So just wanted to know why, what was the, what was this 14% growth Y-o-Y, what does this comprise of? If had it been in the range of 8% to 8.5%, the EBITDA margin would have looked up, similar to what we had done in Q4. Right. So just wanted to get a sense on this on the employee expense.

Sanjay Jain: If I get your question right, when we talk about 4% plus operating margin that we achieved in quarter 4 last year, quarter 4 is usually our best quarter. One is getting an opportunity of achieving the highest sales among the four quarters. And therefore, the costs are actually getting amortized over a larger base. And quarter 1 is usually the leanest quarter. And therefore, the margins are about 3.2 or so. And now I also mentioned that the last year first quarter also should have been the leanest, but there was a pent-up demand benefit. So pent-up demand overcame the lean factor, and we, if I recall, we were at 3.1%, 3.2% last year.

But despite the sales fall, the benefit of better margins, gross margins, whether they are coming in from procurement efficiencies, whether they are coming in from better margin business proportion in the top line increasing or the entire value chain all the way of we placing the order to third-party factories or even the cotton yarn prices, big prices declining is all benefiting.

So, therefore, these three-four factors have actually benefited. And as things unfold in the later part of the year, we believe the sales traction should give better results, number one, there should

be continuation of revenue and profit from the better margin business that we have got added in the trajectory. The procurement centralization effort should keep adding as well. So therefore, we believe that what we achieved in quarter 4 last year in terms of 4% is margin, all indicators are that we should get back to those levels in quarter 3- quarter 4 and hopefully improve thereafter as well.

And other thing also is that the entire industry, all industries in India and across the globe have been getting impacted by the interest rate cycle. And as our CFO, Raul was earlier saying that there is a 6x-7x increase in the base rate, this quarter versus last quarter. So therefore, somewhere, we all anticipate in about two quarters, the interest rate should peak, and they will start coming down as well. So, therefore, below the EBITDA level as well. We believe in the latter half of the year, more so towards quarter 4, when all of us in the industry should see the benefit of interest rates beginning to come down as well.

So these are some, if, I as I said in the beginning, I hope I got your question right, and these are some of the factors that could influence the gross margins, EBITDA margins, and also the PBT margins.

And somewhere when the first question came about the legal entities, and wherein I mentioned that this is our inherent model of having entrepreneurs on Board. And why I'm bringing that point again that there is an entrepreneur in a business like a hawk, working very closely keeping a close watch.

Therefore, that ability, that agility to actually prune down cost as well, in case while we're all anticipating recoveries are here happening, hopefully, in the second half of the year, but therefore, the first point that I answered on the legal entities, also there's a plus of that, that in case the situation continues to be very tough, very unlikely. But if that is the case, then that lever exists, and that entrepreneurial fabric of the organization would also see that an initiative taken from the corporate is executed in a very shorter span of time in terms of bringing the cost structure down as well.

Moderator: Thank you. We have the next question from the line of Amit Doshi from Care PMS. Please go ahead.

Amit Doshi: Yes. I just wanted to understand on this slide in the presentation where the financials are there, it mentioned that gross margin has improved because of better pricing due to lower demand. Can you just help me understand that part?

Sanjay Jain: Yes. It's an interesting English written over there. What it means is that, on one hand of the continuum, you have the retail customer. On the other hand of the continuum, say, you have a factory. And of course, at the end of the continuum, all the goals, we have to go to fabric supplier, and we are in between adding value to our customers, and channelizing orders for our factories.

So, the factories are kind of serious dire situation across the world because of the demand being low. They have been severely hit so therefore; they are claiming for orders even at low margins so that they can fill in their factories.

So that's where if the demand is low, if the orders that we are getting are slowing down, then PDS as a solution provider in between is having the ability to generate orders and therefore, sit down with the factory and say, yes, the orders are there, but then let's discuss margins. And I think we are as a responsible company; we are not trying to unnecessarily squeeze the factory.

We also got to be there that there are mills at the back-end supplying fabrics and the supplying trims as well. So that also, in turn, is the entire value chain, I think is wanting to make sure that in a muted demand scenario, let us make sure that there are orders and there's a recovery of fixed cost. Let's keep floating for better times to head. That's the premise behind that statement in terms of a low demand rightly also translating to a better margin scenario.

Amit Doshi: Okay. So, the difference that you negotiate, you keep it with you rather than fully passing it on to the ultimate

Sanjay Jain: No. our endeavour is always to pass on the full benefit to our customers. In fact, the customer decides the price. But then we've very humbly worked towards the back end. For example, I mentioned that we also have now centralization of procurement. And I have to admit that I'm away from the eventual retail customer.

So, therefore, there have always been asked for my customer to bring down the prices. So, I want to make it very humbly there that I don't want to be seeing that somebody who's going to increase prices or not pass on the benefit.

But very importantly, I need to keep adding better margin revenue streams in terms of my engagement with the customers. That is how we believe that through my centralization of procurement through my augmentation of trajectory on better margin categories that I go back to the statement that we anticipate an average 50 basis point improvement in margins year-over-year.

Amit Doshi: Okay. On the manufacturing front, of course, there is a significant reduction. You also mentioned about the Eid holidays and the resulting lower production. But I'm sure that was expected. So accordingly, the inventory would have been maintained. So, this is purely a reason of lower demand only? Or this Eid holiday something significantly to play with this reduction in the manufacturing operations.

Sanjay Jain: There are two external reasons and one internal that impacted the manufacturing in quarter 1. One is the Eid factor, which is a critical factor. It's almost a one week of sales, production and sales from factories. That's number one.

And number two, our factories have been on an average somewhere 50% to 65% range, doing direct business with the customers by the remaining coming from an internal sourcing verticals so therefore, while the demand or the orders for any factories are getting impacted, they also impacted our factories as well to the extent they are doing direct business.

The third factor, which I mentioned in the opening remarks is that we did our change in management in our Progress factory, the bottoms factory, and we did the same in the beginning of the quarter 1 in our Green factory as well. That's taking a bit of time to stabilize.

So that's an internal factor. So, this is the answer to your question as to why our manufacturing top line actually came down in this quarter.

Amit Doshi: Okay. Regarding this Ted Baker transaction, you mentioned there's a 9% bottom line. When you say bottom line, what exactly that means like an EBIT, EBITDA, or PAT level? And in our books, so is it recorded in other income, or it comes in the top line? How exactly it gets reported. The INR 40 crores part that you mentioned.

Sanjay Jain: 9% is actually the PAT from Ted Baker's transaction and 9% is the actual achievement. But as I said earlier, somewhere the full-year horizon is about 7% upwards for the entire year. And as Reenah was explaining in response to one of the earlier questions, to the extent of, our top line was about approximately INR30 crores odd in the 15 days.

The bulk of it was actually the wholesale business. That's actually gets recorded because we purchase and sell and the commission or the service fee that we get on the design service or the sourcing service that we provide only the service fee portion gets added to our top line.

But the combined impact of that is INR30 crores top line and the combined impact of that is circa 9% PAT in the first 15 days of the acquisition.

Amit Doshi: Okay. So it doesn't come under other income?

Sanjay Jain: No.

Amit Doshi: Okay. And this tax rate for this quarter is slightly higher. It's just what ,like I do understand that we have to look at the annual figure. But just to confirm, there are no changes in the any tax bracket that we fall into or anything of that sort?

Sanjay Jain: I think, Rahul, you want to answer that? Go ahead. Why the tax is higher by?

Rahul Ahuja: **S**o, there's a couple of reasons for why the tax rate is higher by about USD2,00,000 in the quarter. One is the profit of Ted Baker's being, Ted Baker in the geography of the UK, where the taxation is higher. That contributed about USD1,00,000 out of the USD2,00,000. And the second reason is in Bangladesh, the government from July of last year, changed the taxation wherein earlier it was 0.5% on the collection of receivables, now it has become 1% on the collection of receivables, and that contributed to the balance of about the USD75,000 to USD80,000. So, these two reasons largely explain why our tax was not much very higher.

Moderator: Sorry to interrupt sir, but we have a paucity of time, we need to proceed with this conference. I would now like to hand the conference over to the management for closing comments. Over to you, sir.

Sanjay Jain: Ladies and gentlemen, thank you so much for joining us. It was a pleasure to have an engaging audience like you and we look forward to connecting with you again in the near term. Thank you so much and stay safe all of you. Thank you, Nuvama team for organizing our conference. Thank you.

Moderator: Thank you. On behalf of PDS Limited, that concludes this conference. Thank you for joining us. You may now disconnect your lines.