"V-Guard Industries Limited –

Acquisition of Sunflame Enterprises"

December 13, 2022

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MODERATOR: **MR. RAHUL AGARWAL – INCRED EQUITIES**

Moderator: Ladies and gentlemen, good day and welcome to the conference call to discuss V-Guard Industries acquisition of Sunflame Enterprises hosted by InCred Equities. As a reminder, all participant lines will be in the listen-only mode and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing '*' then '0' on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Rahul Agarwal from InCred Equities. Thank you, and over to you, sir.

Rahul Agarwal: Thanks, Stephen and good afternoon, ladies and gentlemen. InCred Equities is pleased to hold this call for V-Guard Industries to discuss the acquisition of Sunflame Enterprises. We have with us the senior management of V-Guard Industries led by Mithun, Managing Director of the company; Mr. Ramachandran, Director and Chief Operating Officer; and Mr. Sudarshan Kasturi, Senior VP and Chief Financial Officer for V-Guard. We thank the management and the Investor Relations team for their continued support and giving us the opportunity to host the call.

I now hand over to Mithun to share his brief thoughts on the proposed acquisition, after which management will be happy to take questions. Over to you, Mithun.

Mithun Chittilappilly: Thank you, Rahul and InCred for hosting this call. A very warm welcome to everyone present for this call. I trust all of you had a chance to refer to our press release, which was sent out on Friday.

We have signed definitive agreements to acquire 100% stake in Sunflame Enterprises Private Limited for a consideration of INR 660 crores. This will be on a debt-free and cash-free basis, subject to customary closing adjustments. We expect this transaction to close by the middle of January 2023. This acquisition, once completed, will significantly enhance V-Guard's presence in the Kitchen Appliances segment.

Sunflame is a well-established pan-Indian brand, with a wide portfolio and strong product development capabilities. We plan to finance the transaction through a mix of internal accruals and debt. We strongly believe that this acquisition is highly complementary to V-Guard. There are multiple levers for unlocking synergies in areas like geography, product portfolio and trade channels. Further the recently established, integrated manufacturing facility of Sunflame will enable significant scale up of the overall Kitchen portfolio.

The acquisition is a key milestone in V-Guard’s journey to build deeper engagement with our consumers. We believe that this will be value accretive to the shareholders of V-Guard.

With that, I conclude my opening comments and would like to thank the team at InCred and Rahul Agarwal for hosting this call. I would like to request the moderator to open the floor for Q&A.

Moderator: The first question is from the line of Rahul Gajare from Haitong Securities India Private Limited.

Rahul Gajare: Hi Mithun, congratulations on this acquisition. I've got couple of question and I'll just start with the breakup that you are indicating – that you're looking at internal accruals and debt. Can you give us some sense on what is the kind of debt you're looking at? Have you already tied up the debt or cost of debt, etc.? That's the first question.

Mithun Chittilappilly: Okay. Sudarshan, do you want to answer the first part regarding debt?

Sudarshan Kasturi: Yes. We are looking at a debt of about INR 350 crores to INR 400 crores and the balance will be from internal accruals. We have not tied up yet, we are just speaking to a few people. We should be finalizing in a few days.

Mithun Chittilappilly: The indicative cost, I think Sudarshan, we have not tied it up.

Sudarshan Kasturi: We have not tied up so I didn't want to get into that number. We will discuss that once we are tied up.

Rahul Gajare: My second question is, with revenue of almost INR 350 crores that the company has done last year, could you give us a sense of the breakup coming from North, South, East and West? What was the margin last year, because I think you did talk about the profit margin and you didn't talk about the EBITDA; so how has the company done in the first half of this year on the financials?

Mithun Chittilappilly: I believe that the South to Non-South split for Sunflame is roughly 80:20, that means 80% coming from Non-South and about 20% coming from South, roughly. As far as the EBITDA number is concerned, I think it's around 12% to 13%, Sudarshan?

Sudarshan Kasturi: Yes, it's around 12% EBITDA.

Rahul Gajare: How has the performance been in the first half of this year?

Mithun Chittilappilly: I don't think we will be able to answer that. What I can say is that we have been in talks with the promoters of this company for the last five to six years. We have seen this company up close, on a fairly granular level and I can tell you that it's fairly consistent. It has probably got one of the strongest cash flows that we have seen in the industry. The business is managed in a very steady and safe manner and that's what I can say. I think that, even this year they will have a reasonable growth.

Rahul Gajare: I was looking at the last 10 years of growth and we've seen about 6%-7% revenue growth in the last maybe 8-9 years, from 2012. I think even at the bottom line, the number was probably around 5%-6%. So the growth has been muted. I wanted to understand, is there a reason why the company was not able to grow in the last couple of years?

Mithun Chittilappilly: I think there are a couple of reasons. We're not going to go into too much detail. However, I can tell you that the company is under indexed in e-commerce and modern trade channels. These two channels, today, contribute roughly 25% to 40% of the revenue of our category, depending on which category you take. The promoters had not decided to participate in this channel for various reasons – margins, for cash flows, etc., thus they have suffered in that sense. However, the growth in GT (general trade) has been according to what the market has grown, which has also been of the same level as we indicated. Ram, anything you want to add on this?

V. Ramachandran: If you look at the last six to seven years, organized retail has significantly expanded. It's now more than half the market, but they are extremely under indexed. So, they have not been able to participate in this shift and they've done so consciously.

The other thing is their operating model which is, by and large, their GT (general trade) business that is on cash. So, that's the other part that in hyper competitive markets, they are running the business on cash.

Mithun Chittilappilly: Sunflame operates on mostly cash and carry business. They are one of the few industry players who do not offer credit to distributors. So, you can understand the strength of the brand.

Rahul Gajare: I'll just ask one last question before I go back to the queue. In terms of the total sales – how much is manufactured in-house for the company, what does the factory in Faridabad really bring to the table and how much is outsourced? If you could discuss on the manufacturing side of things?

Mithun Chittilappilly: I don't have the outsourced data with the way we produce the products, but I can tell you that the factory in Faridabad has been set up with an eye to substitute imports of Chimney. Chimney is a very large part of their business, maybe the second-largest category of their sales. That's one of the few facilities in India which actually manufactures Chimneys. Chimneys are mostly our hobs, sorry not hobs, hoods. Hoods are generally imported into India from China and other countries. But with Sunflame, we have an opportunity to manufacture and they've already started manufacturing, I'm told, the Chimneys in India.

Sudarshan Kasturi: I believe the in-house manufacturing is about 65%**.**

V. Ramachandran: Mainly, the major categories – Gas Cooktops, Induction Cooktops and Chimneys are made in these factories and that should be the most significant part of the business. I'm sure that's upwards of 70% so these three categories.

As far as Chimney is concerned, this new facility is very new and is probably just over a year old. Chimney manufacturing has just commenced and it is about three to four months old. So I think the part of the Chimney transition, to fully transition will take some time.

Moderator: The next question is from the line of Bhavin Vithlani from SBI Mutual Fund.

Bhavin Vithlani: Good acquisition, Mithun. I joined a little late, if you could help us with the key categories which are contributing to the INR 350 crores revenue that will be useful to start with?

Mithun Chittilappilly: So it's Cooktops in the sense of both – on the counter cooktops and built-in cooktops, Chimneys and Induction Cooktops. So all types of Cooktops and Chimney will be roughly 60%, 70% of revenues.

V. Ramachandran: It's a full platform with a wide range of Kitchen options. The dominant ones are these that are mentioned, but they have a complete range of Kitchen equipment.

Bhavin Vithlani: What will be the contribution of each of these sub-categories?

Mithun Chittilappilly: I would not be having that readily with us and we would not like to share at this stage as the business still belongs to the parent promoters.

Bhavin Vithlani: Could you help us with this geographical breakup? You mentioned modern trade and online contribution as well, but what is it currently?

Mithun Chittilappilly: I think 12% or something like that, e-com plus modern trade, maybe 10%-12%. Whereas the market may be closer to 40%-45%.

Bhavin Vithlani: What is the geographical breakup in terms of what was East, West, North and South. Also, what are the critical strengths of the channel?

Mithun Chittilappilly: The brand is extremely strong in Non-South. Non-south contributes roughly 80% and South is about 20%.

Bhavin Vithlani: We have been told, is it very significantly strong in West and North India?

Mithun Chittilappilly: Strong in North and West. North and Western market is the bulk of the revenues.

Bhavin Vithlani: Within these regions, is it true that they are strong more in the metro and the larger cities and not as strong in the rural areas?

Mithun Chittilappilly: Like we mentioned earlier, this is a company that does not give any credit to distributors. Yes, we don't have the exact data on what is rural and metro and all that, but chances are that they are stronger in cities because that's where the stronger distributors will lie and they don't offer credit.

Bhavin Vithlani: Correct me if I'm wrong, larger metro cities and especially West and North are not as strong for V-Guard so it seems like there is a complementary channel that we are getting. How would we be able to leverage this channel and brand for some of the other Kitchen categories, let's say for example, Mixer Grinder, Juicer, etc., where we have the product categories already?

Mithun Chittilappilly: V-Guard is extremely strong. V-Guard is selling these Kitchen products only in South India. We hardly have any presence outside of South India. We are mainly selling in the South and across e-com channels. In that sense, it's extremely complementary where this company has good network in the Northern and Western markets. V-Guard is traditionally into Electrical products and Consumer Durables, so we are present in the White Goods channel and the Electrical Goods channel. Whereas Sunflame is predominantly present in the Kitchen channel. Kitchen channel is also different because it also includes vessel stores and all that where V-Guard is currently not present. So yes, in that sense it's complementary.

Bhavin Vithlani: For us to actually scale up some of the non, like just your thoughts, would we want to continue this brand? I mean, what is the kind of timeline we have got the Sunflame brand and how do you want to leverage that?

Mithun Chittilappilly: Sorry, can you repeat the question?

Bhavin Vithlani: So have you got the brand rights, Sunflame brand?

Mithun Chittilappilly: The brand is owned by the company. The brand is owned by the entity. It is not owned by the promoters. We intend to keep the brand separate. Ram, you want to add anything?

V. Ramachandran: So mainly, Sunflame is a highly reputed and a well-known brand. It enjoys very high top-of-mind awareness, which is the fundamental reason why we have put this kind of money. Fundamentally, the investment is towards the brand and not so much towards the underlying business. The brand has the strength. Of course, that's an integral part of the transaction.

Sunflame will continue to operate as an independent platform and it enjoys enormous opportunities to scale up the business. Fundamentally, as we said, emerging channels are extremely under-indexed. Although it enjoys very high levels of awareness, but from an availability standpoint, it is quite weak. There is a good opportunity for Sunflame to grow in the South. So yes, these two brands and these two business systems will operate independently.

Bhavin Vithlani: So what is the thought process? We were looking to grow in some of the categories like Mixer Grinders and some of the Kitchen Appliances. Would we now use the Sunflame brand for the Kitchen and keep V-Guard for the Electricals? If you could just help us with what's the longer-term plan for us.

Mithun Chittilappilly: To put it in perspective, the combined – V-Guard and Sunflame, business will cross something like INR 500 crores. V-Guard does about INR 150 crores, INR 140 crores and Sunflame does about INR 350 crores. We will independently continue to drive both the brands and we will come out with the real/correct strategy on what will be the brand architecture and the price position segments in due course. However, at the moment we are not planning to integrate it. It will be running as a separate team.

Yes, there are some complementary situations, for example, there are certain products that Sunflame is selling where V-Guard has the manufacturing capability and sourcing capability and there are a lot of products where Sunflame is having manufacturing and sourcing capability where V-Guard is selling. So we will use these networks, but they will continue to operate independently as independent brands.

Bhavin Vithlani: Just last question from my side. In the agreement, we cannot restructure the employees. I mean do we have to retain them and if there are any of these clauses that you could help us with?

Mithun Chittilappilly: Ram, you want to take this?

V. Ramachandran: No. As we said, these two are separate, Sunflame will operate as a subsidiary of V-Guard and it will operate with its business system. See Sunflame is an extremely successful business, generating very strong cash flows and is highly profitable, even on a scale of around INR 350 crores to INR 360 crores. It has unique attributes and features which contribute to making Sunflame and giving it the strength that it has in the market. It is our desire to maintain and build on these strengths. As these will be independent entities, they will continue to operate the way they are operating their side.

Mithun Chittilappilly: From our end, we are very keen to retain all the team members of Sunflame. There are roughly 300 to 350 employees in Sunflame. Our focus will be to retain all of them as much as possible. There is a lot of wealth of knowledge, product planning, product development capability in the company, which we would like to harness.

Moderator: The next question is from the line of Achal Lohade from JM Financial.

Achal Lohade: Congratulations for the acquisition. Couple of questions from my end. One was if we look at the FY '22 revenue, there was a substantial growth. Can you explain it to us, because last five years was not much of a growth, while FY '22 it saw a significant 20%-plus growth, is it possible to get some more colour on FY '22, the growth?

Mithun Chittilappilly: Some of FY '21, I think they had a dip in revenue. So some of it is pent up demand. So maybe what we should look at is a 5% to 6% growth from FY '20 to FY '22. I think FY '22, shows a big growth because in FY '21, smaller companies had a bigger impact with COVID with the first, three to four months of not being operational.

V. Ramachandran: Mithun, the growth should be looked at over '20, '21 and '22 because from March '20 the COVID impact started. So '20, '21, '22, you should average and then look at the growth. Then, that CAGR will be like what Mithun explained.

Achal Lohade: You said that you're going to keep it as an independent entity. How do you look at the growth given where it is currently, given our bandwidth? How do we look at growth? Can this be 15-20%? Can this be more 10-15% for next two years or three years at least?

Mithun Chittilappilly: We don't want to give out any numbers, but I can say that with the products they have, with the brand recall it enjoys, with the awareness and top of mind awareness and with the consumer base it has over the last 40 years, Sunflame should be definitely much larger than what it is today and that's our aim.

Achal Lohade: Just to add on to the same point, would you be required to make any investments further on the sales, distribution, branding, etc. to pick up that growth trajectory?

Mithun Chittilappilly: Like we said, we don't want to give out any specific numbers, but yes, there is a lot of work to be done on the distribution side, because we do think that Sunflame is not represented adequately in certain geographies like the South and partly in East. We also think that they are not properly indexed in the modern trade and e-commerce channels, where V-Guard has a good team running those categories, running those type of channels. So there will be the initial low-hanging fruits that we will go after.

Achal Lohade: Just one clarification. You said that the distributor sales are cash-and-carry, did I hear that right?

Mithun Chittilappilly: Yes.

Achal Lohade: If I look at the balance sheet, I see the debtor days somewhere between 50 days to 60 days in the past. How do we explain that? Does that mean the non-distributor, the credit...?

Mithun Chittilappilly: So, Sunflame also has a CPC and CSD business – canteen business, wherein which it gives credit. The general trade is mostly on cash-and-carry. Sunflame also used to supply to some modern trade outlets, but it is very small compared to the actual percentage of the market.

Achal Lohade: What would be the CSD mix, because the debtor days seem to be very large, the non-distributor sales, the receivables days are very large, if you could clarify?

Mithun Chittilappilly: Ram?

V. Ramachandran: I think it's about between 20% to 27%, 28%. The cash flows, that can be variable. So sometimes if there are delays, then I think at that point in time, if you look at the picture, it maybe higher or lower. Also, they had some organized retail businesses in the past, but because of their philosophy to maintain a profitable and a fast cash flow business, they have vacated some of those customers also. That's also one of the reasons why if you look at that three-year growth, it will be more like 5% to 6%.

Moderator: The next question is from the line of Khadija Mantri from Sharekhan.

Khadija Mantri: Sir, I understand that we would be raising debt of about INR 450 crores for funding the acquisition. So could you just tell us how the debt will be raised and what would be the interest rate for the same?

Sudarshan Kasturi: We are still negotiating the terms, so I don't want to put out a specific number as it might come in the way of the negotiations.

Khadija Mantri: But the rest of it could be funded by internal accruals; I understand, we have cash and investment of about INR 150 crores, so that should be sufficient?

Sudarshan Kasturi: Yes, the cash balance has gone up since the last reporting. Approximately INR 400 crores will come from debt and balance from internal accruals.

Khadija Mantri: In Consumer Durables, so in Kitchen Appliances, we have INR 140 crores to INR 150 crores of revenue, but are these products profitable? If we exclude Fans and Water Heaters, then for the rest of the Kitchen Appliances, are we making an operating profit on these?

Sudarshan Kasturi: Yes, in the Kitchen Appliances, the gross margin is good. Even EBITDA is positive, but the EBITDA is low and it's a question of scale. But even within our portfolio, at the INR 150 crores, the gross margins are still good.

Moderator: The next question is from the line of Rahul Agarwal from InCred Equities.

Rahul Agarwal: Congratulations to the team for the acquisition. Sir, I have two or three questions. Firstly, on the distribution channel and service network of Sunflame, could you explain how the company is structured in terms of distributors, dealers, retail touch points and what's the reach for the company right now?

Mithun Chittilappilly: Yes, Ram you want to take this?

V. Ramachandran: Yes, I would like to avoid discussing too much in detail because the promoters still manage that business. It's not our business at this stage and it's not fair for us to comment on that. But yes, their business model is comparable. The GT (general trade) business is through distributors and dealers and there are probably somewhere in the region of around 10,000 to 15,000 touch points in the country. I hope that would suffice.

Rahul Agarwal: Secondly, there is a question to Mithun, essentially on the ROI of the acquisition, assuming that V-Guard always has been very careful on the return on investment and the ROC has been broadly ranging upwards of 20%. Mithun, any thoughts, how would you rate this INR 660 crores investment, how would you get up to 15%, 20% return on the capital here?

Mithun Chittilappilly: I think we are fairly confident of getting there, otherwise we would have not gone for it.

Rahul Agarwal: On this balance INR 25 crores payment to be paid after two years, what could be a reason for this?

Mithun Chittilappilly: It is basically the escrow amount and the promoters felt it was okay to leave the cash back with us rather than in the bank.

Rahul Agarwal: So essentially we pay the entire INR 660 crores and of that INR 25 crores stays in escrow?

Mithun Chittilappilly: No. Ram, you want to explain?

V. Ramachandran: Yes. Typically what happens is that, after the acquisition is done there are sometimes some adjustments that happen once the post-closure data is available and thus, there may be some adjustments that may happen because of externalities and all that. They're typically in any transaction where some amount of money is set aside in an escrow.

In this case, the promoters of the entity have felt that it is better to leave this INR 25 crores behind with us rather than have it put it in a bank, maintaining an escrow. That's the background to this. So this INR 25 crores will be paid to them at the end of two years. This is normal and customary in every transaction. It varies from transaction to transaction based on the comfort between the two parties. This is the number in our case.

Rahul Agarwal: Lastly, assuming 7%, 8% final closure on the debt to be taken of about INR 400 crores, would you agree FY '24 would be EPS accretive? My sense is that the EBITDA would be in the similar range of INR 40 crores and you would also lose some interest on your cash. So how do you look at FY '24 on EPS level?

Sudarshan Kasturi: First year will at least be EPS neutral if not accretive. But year two onwards, it will be.

Moderator: The next question is from the line of Naveen Trivedi from HDFC Securities.

Naveen Trivedi: Congratulations for the deal. A couple of questions from my side. Considering that the South contributes around INR 60 crores, INR 70 crores revenue for the business, if you can highlight – how has the market share been for the brands in the Non-South market? Considering you have been following the brands since last four years or five years, any particular challenges in the South side?

Mithun Chittilappilly: Yes, Sunflame as a brand started out from Delhi. For any company, that starts out from Delhi, North will be the largest market. It's not surprising that the South market share is low or maybe it is because they got into South late or that there is more competition in South from locally present brands like Preethi, Butterfly and the like. It's not a big surprise that it happened. It always happens like that.

We don't want to comment on any market share and all that. I can tell you that overall as a business, in the last four to five years, it has been fairly stable. Yes, it has not grown as fast as some of the other Kitchen players but it has probably demonstrated better and predictable cash flow than any other company I have seen.

Naveen Trivedi: Do you think that the brand requires more innovation type of a drive or do you think that the pricing strategy should also be correct to attract most of the business in the South side?

Mithun Chittilappilly: These are all very premature questions at this stage. As Ram mentioned, for another month at least, stake still belongs to the promoter family, so they will continue to run it. Once we take over, once we analyse, put a management team in place and hire our advisors, then we will come back with what should be the strategy on how to scale up. Once we crystallize it, we will come back to you. It's very premature sitting here and deciding what is to be done and how to grow.

But we are very confident that the brand has the strength to grow. How to do it, we will come back.

Naveen Trivedi: Just last question. Any ad spend number if you can share?

Mithun Chittilappilly: Ad spend? It's about I think 5-6%. Ram. Am I correct?

V. Ramachandran: Yes, 5% to 6% is the ad spend.

Moderator: The next question is from the line of Nirav Vasa from Anand Rathi.

Nirav Vasa: With regards to the revenue booking of INR 350 crores versus, with what I am seeing, is that historically the average run-rate was around INR 250 crores and last year we had seen unprecedented commodity inflation. So, what percentage of this INR 350 crores revenue would you attribute to higher commodity price or growth?

Mithun Chittilappilly: I think the price growth for that particular year was between 6% to 8% if I'm not mistaken. Ram?

V. Ramachandran: Yes. It's about 6% to 8%.

The right way to understand this growth is that 2020 March, was when COVID had hit and '20 March, was not normal for most companies and '21 was a disturbed year. So that's why '22 is looking like a very big year. Just average it across all three years and you will find that it's about 5% to 6% growth.

Nirav Vasa: Exactly, sir. The number that I was seeing was coming to around INR 250 crores to INR 260 crores of revenue on an average for last three years. So on an average revenue of around INR 250 crores…

V. Ramachandran: Not like that. The exit number is correct, but the growth number you should divide across three years. INR 360 crores will remain, it will not shrink. But what will happen is that when you are looking at the growth, please look at it as average growth across three years.

Mithun Chittilappilly: I think FY '20 to FY '22 the CAGR is about 5% to 6% is what we can tell you. That's how we should look at it. It's not INR 250 crores, it was above that. Please also understand that it had other companies and other promoter owned entities which were merged into Sunflame Enterprises only in the last year.

Nirav Vasa: That is what brings me to my next question. Are we to share some number or colour on the related party transactions?

Mithun Chittilappilly: There is no related party transaction today because there is only one company. Ram you want to explain?

V. Ramachandran: The business was organized differently till a year back. At the point where the business is being offered to us, I think as you know, all of these have got consolidated progressively over the last 18 months.

Mithun Chittilappily: What you are looking at INR 250 crore is a standalone number, it does not include some of the other promoter owned entities which also carried out business.

Nirav Vasa: On their website, I see that they are present in FMEG as well. So in FMEG they are present across some product categories like Water Heaters and other categories. So do you intend to keep the brand in FMEG as well or do you want to consolidate under V-Guard only?

Mithun Chittilappily: So Sunflame has its own customers and its own distributors. There are customers and distributors that are willing to buy some Sunflame Water Heaters and Sunflame Fans. So we will -- like we said, we will continue all the product verticals of Sunflame.

Now sometime in the future, we may decide, to ensure better profitability and sourcing, we may source the products through our factories where V-Guard has a larger presence in Fans and Water Heaters. So those are the calls we will take going forward. But yes, those product lines will be maintained, but it's not very large.

V. Ramachandran: It's not significant. And I think as we have said earlier, we have acquired Sunflame as a very strong platform in the kitchen space. It will run as an independent entity and it will be driven by the management team.

The management team will get added as the promoters move out. So this team will decide the direction of this entity. Fundamentally synergies will be leveraged, so if we have a better supply chain cost advantage, maybe extending our supply chain to any of their product categories, that will certainly be explored.

Nirav Vasa: Sir, my final question is based on the existing manufacturing capabilities which this company has, what is the maximum revenue that can be generated from it? Thank you.

V. Ramachandran: I think they have adequate capacity to meet their growth objectives for the upcoming 3 to 4 years. This particular place has also got the land for further expansion.

Nirav Vasa: Sir, any number if you can give with regards to some capacity that we have for the capacity or something like that?

V. Ramachandran: No. I'm saying it's not material because the capacity in this industry is flexible. A lot of it is also assembly and the second thing is they can run shifts also. They are running two shifts, they can go to three shifts also and there is space also there. So I am just saying that it is not material, let me see if I have a specific capacity number with me.

Sudarshan Kasturi: Given that we are not owners of the business yet, there is only limited amount of granular data we can give out at this stage. We will come back on these once we have run the business for a couple of quarters.

Nirav Vasa: Got it, thank you very much.

Sudarshan Kasturi: At that time we may be able to disclose more.

Moderator: The next question is from the line of Renjith Sivaram from Mahindra Mutual Fund.

Renjith Sivaram: Hi sir, sorry, my line got disconnected last time. When I look at Sunflame, it has INR 265 crores kind of revenue and since a long period of time and suddenly last year it has come to INR 350 crores. If you could help us understand that what were the categories that brought this INR 100 crores of incremental revenues, what will be the percentage of revenues that come from the normal categories and what made the additional categories go down?

V. Ramachandran: I mentioned this earlier on that it's not the right way to look at it. March of 2020, sales were not normal because of COVID. After 20th or 15th, typically in most companies, 60-70% of the business happens after the 20th of the month. So that particular year's number is not a correct number. '21 was also disturbed year due to COVID. '22 is a year where they could get the full normal, proper and regular revenue. There is also an impact of increase in input cost. That's one thing and the other thing is that there were other entities of the promoter family, which also used to do business in this space and which have all got consolidated in the past year which you see is the year that went by '22.

So please don't read too much into these trends and numbers. That's all I would say.

Mithun Chittilappilly: So if you look at a like-to-like basis, the CAGR would have been not more than 5% to 6% for the last 5 years.

Renjith Sivaram: What is the percentage from Stove, which is I think the main product of Sunflame's, on the top line?

Mithun Chittilappilly: I think Hoods, Hobs, Chimneys – all put together is about 40%-45%, and also includes – Stoves, Cooking Range, Inbuilt Chimneys, Induction Cooktops. So all Cooking and Chimneys, it's about 45% to 50%.

Renjith Sivaram: So the modern hob top, which I think the market share is 1% to 2% is what we understand, that will be what percent? The hob top, which is the modern that goes inside, there what will be percentage?

Mithun Chittilappilly: I don't think we are carrying that level of detailed information to share at this point in time. I think they have a decent presence in Inbuilt as well and are not the numbers you mentioned.

Renjith Sivaram: Okay. As per what we understand the reason for you to get into this will be like being competitive to a Faber or Elica or will it be completely that we want to be a competitor to TTK Prestige or Butterfly's of the world. If you can explain the thought process in buying this company?

Mithun Chittilappilly: Okay. Ram?

V. Ramachandran: Fundamentally, we got into the Kitchen business somewhere around 2012 or 2013, and it has taken us 7-8 years, with the progressive introduction of models, to build about INR 150 crores, INR 160 crores business in Kitchen that we have, as we speak today. These might grow by some 15- 20% in the current year that we are talking about.

Now Sunflame on the other hand is a business, which is extremely strong in the Non-South market and building a position in Non-South would take us a long period of time. Also, in Kitchen unlike in other categories, brand recall and brand connection with the consumer is a very critical driver. Thankfully, because of the heritage and history of V-Guard in South, this was a lesser barrier thus far.

So looking at the time that would be required for us to build our market presence in the Non-South, we thought it would be wiser to go for a platform so that we can start to build a strong position in Non-South markets also, equally fast.

Mithun Chittilappilly: Sunflame has a strong position even in Chimneys. So it's not that it competes only with the traditional Kitchen players, but it also competes with in-built Kitchen players.

V. Ramachandran: They have a decent business in built-in and in Chimneys. Growing these categories will also require one to grow their own channel; in a lot of these cases, one would have to expand on their own brand shop kind of network or invest in shop-in-shop.

The promoters have been conservative. They have a fairly decent lineup in this space and they do decent numbers. They're not as insignificant as you may have mentioned, that is there, but the primary reason that we are getting into this is for speed, to hasten our national presence in the Kitchen category and have access to a brand, which has equity and heritage in the Kitchen space.

Renjith Sivaram: What's a percentage of trade that goes through the online market or is it all offline for Sunflame?

Mithun Chittilappilly: I think almost 90% is offline, 10% maybe coming from e-com.

Renjith Sivaram: Any geography-wise split that you can share?

Mithun Chittilappilly: No, we can't provide it at the moment.

Moderator: The next question is from the line of Nikhil Kale from Axis Capital.

Nikhil Kale: A couple of questions. First, I just wanted to understand, what was the motivation of the founder promoters to exit the business considering that, as you mentioned the business was really profitable with really good return ratios and cash flows; any succession issues, anything of that sort?

Mithun Chittilappilly: See, this is still owned by family. They are all sensitive matters, so we don't want to comment. However, we can say that the founder promoter is almost, I think, close to 80 years of age. So that is the primary reason.

Nikhil Kale: And secondly, sir, you rightly mentioned that the business has been really profitable and perhaps one of the reasons has been that they have not been as aggressive on the e-commerce side. Going forward do you see that as you, may, expand the presence in e-commerce and maybe in modern trade, that you may need to spend more on the ad spend and all other kind of expenses?

Mithun Chittilappilly: Doing business in the current environment, where you have a very high growth in e-commerce and modern trade, requires a different set of skills which many smaller companies may not have. However, we have a good platform and a team of people to deal with these kinds of businesses today, which they might not have.

So, in that sense, yes, once we take over, we will try to align and index the market share with what the total market looks like rather than what it is today.

Moderator: The next question is from the line of Achal Lohade from JM Financial.

Achal Lohade: A couple of more questions. One is, given whatever you have said, is it fair to say that there are plenty low-hanging fruits with respect to leveraging the e-com part; and given the operating leverage, could there be a possibility that this 12-13% can actually become 15-17% EBITDA margin on a sustained basis?

Mithun Chittilappilly: I think this has been mentioned earlier, we don't want to give this kind of a statement. All we can say is that – let me put this in another perspective. When I saw the business and the numbers it was very much like the V-Guard of 2006-2007, which I joined after my studies and all that.

So, that is the first thing that attracted me – because the promoter's character is very similar, you know; the ethos and the culture is very similar to what we have. That's all we can say at the moment. We don't want to talk about how much percentage of EBITDA it will make in the next year or year after that.

Achal Lohade: Just one more question – given that this acquisition is kind of now already done, would you be open to more acquisitions or you'll wait for first integrating this and then look at more acquisitions? I think in a passing remark you mentioned about certain ROCEs or IRR on this investment, so if you could clarify on your thought process on the same as well?

Mithun Chittilappilly: We have done a projection on the combined ROCE of the combined entity, going forward and we're confident that we can go back to the ROCE of the company, what it was before. We have to understand that we have about INR 300 crores of cash, which is not earning anything today.

In that sense the combined ROCE should look good. We may not look at anything big at the moment, because we will be busy expanding and putting a team in place to run Sunflame and then getting the synergies out. So at the moment, we are not looking at anything.

Moderator: The next question is from the line of Rahul Gajare from Haitong Securities India Private Limited.

Rahul Gajare: Sir, you partly answered the question that the earlier participant asked about capacity constraints and like you said, you know that 50-60% of the production is manufactured locally or domestically in-house. So therefore, revenue should not be a factor of growth.

Now, given that we've seen a CAGR of about 5-6% for the last couple of years, that's the reason why I wanted to understand how the first half performance has been. Any color, whether it is similar to FY21 levels or similar to FY20, or current or last year's numbers, any sense on the first half performance?

Sudarshan Kasturi: It's a private entity, not a listed one, so they don't publish first half numbers. All we can say is that it's been a steady business over the years and this year also will be somewhat similar.

Rahul Gajare: Because being EPS accretive will be a function of the revenue growth and that is the reason why I want to just look at that.

Sudarshan Kasturi: There is a limit to how much data we can give out at this stage because it's very premature. So if you're looking at the EPS, just look at the PBT and the interest cost. It will be EPS neutral at worst, in the first year.

Moderator: The next question is from the line of Hitesh Taunk from ICICI Direct.

Hitesh Taunk: Sir, I wanted to know what is the overall industry size in which Sunflame is operating? I wanted to know the industry size of Cooktops and Chimneys, if you can throw some ballpark numbers, it would be very helpful?

Mithun Chittilappilly: I don't have the numbers of the specific categories with me. We don't have it at the moment. We'll have to get back on that.

Hitesh Taunk: And sir, last question is, have we signed any kind of non-compete agreement with the existing promoters or family members?

Mithun Chittilappilly: Yes. We have signed a non-compete agreement with them.

Moderator: The next question is from the line of Mukul Deshpande from DAM Capital.

Mukul Deshpande: My question is, what are the medium-term growth drivers in this Kitchen Appliances space? How are we aiming to expand our market share with the help of Sunflame?

Mithun Chittilappilly: So like I said, one, there are geographical complementary situations – for example, V-Guard is extremely strong in South, and we have like INR 140 crores Kitchen business in South. Sunflame largely 80% of the sales come from Non-South – extremely strong in north.

V-Guard has relatively low presence in the Kitchen channel and V-Guard's Kitchen's business is primarily through Consumer Durables retail outlets. Whereas for Sunflame, it comes from all types of Kitchen channels, Utensils channels and Consumer Durable – any trade outlet that sells Kitchen products.

So in that sense, it is complementary – so there are channels and then geography-wise it is complementary. Product-wise Sunflame has a much broader range than V-Guard – we have a very narrow range from where this revenue comes in. Sunflame has got a much more broader Kitchen range, which V-Guard does not have.

So there are complementary products, complementary channels and complementary geographies. We also have a complementary supply chain in the sense that V-Guard's Kitchen supply chain may not be the most mature, whereas it definitely is for Sunflame. So these are the low-hanging fruits we see, where we can leverage on each other's strengths.

Moderator: Ladies and gentlemen, as there are no further questions, I now hand the conference over to Mr. Rahul Agarwal for closing comments. Over to you, sir.

Rahul Agarwal: Yes, I think it was a good discussion. Thank you so much for letting us host the call. Over to you Mithun, for closing comments.

Mithun Chittilappilly: Yes. Thank you, Rahul and InCred for hosting this call. Thank you all for participating. Thank you.

Moderator: Thank you. Ladies and gentlemen, on behalf of InCred Equities, that concludes this conference. We thank you all for joining us, and you may now disconnect your lines.