"V-Guard Industries Limited
Q2 FY23 Earnings Conference Call"
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MODERATOR: **MR. ANIRUDDHA JOSHI – ICICI SECURITIES**

Moderator: Ladies and gentlemen, good day, and welcome to the Q2 FY23 Earnings Conference Call of V-Guard Limited, hosted by ICICI Securities. 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 touchstone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Aniruddha Joshi from ICICI Securities. Thank you and over to you.

Aniruddha Joshi: Yes. Thanks, Yashasvi. On behalf of ICICI Securities, we welcome you all to the Q2 FY23 results Conference Call of V-Guard Industries. We have with us the senior management, represented by – Mr. Mithun Chittilappilly, Managing Director; Mr. V. Ramachandran, Director and Chief Operating Officer and Mr. Sudarshan Kasturi, Senior Vice President and Chief Financial Officer.

Now, I hand over the call to the management for their initial comments. We will then open the floor for the question-and-answer-session. Thank you and over to you, sir.

Mithun Chittilappilly: Thank you, Aniruddha and ICICI Securities for hosting this call. A very warm welcome to everyone present today on the call. My best wishes for the festive season and wishing all of you a very prosperous year ahead. Thank you for joining us today to discuss the operating and financial performance of our company for the second quarter of FY23.

We reported revenues of Rs. 980 crores in Q2, which represents 8.6% growth YoY and 16.6% CAGR over a three-year period (consolidated basis). It was a fairly strong performance in YoY terms, considering the high base of the corresponding quarter of last year. We witnessed some slowdown in consumer demand in the latter part of the quarter, but for which, we would have had seen a higher top line growth.

On a segmental basis, the Consumer Durables segment reported strong growth in this quarter. The Electronics segment has sustained its improved growth trajectory. The Electricals segment was nearly flat due to price reduction in Wires and related to the dip in copper prices.

During the quarter, South and Non-South markets delivered YoY growth of 2.6% and 17.8%, respectively. With consistent growth in Non-South markets, we have a more balanced geographic portfolio today. Contribution from Non-South regions rose to 42.7% of total revenue in Q2 FY23 from 39.4% in the last year. We are attaining scale in all the regions and this will deliver benefits from operating leverage going forward.

Gross margin for Q2 FY23 was at 29.2%, a drop of 210 basis points YoY (consolidated basis). A&P spends were higher at 2.2% vis-a-vis 1.5% in Q2 FY22. As a result, EBITDA margin dropped 7.4% from 10.5% last year (consolidated basis). There was a Rs. 16 crores impact due to the copper price movement as we had to reduce selling prices while carrying higher cost inventory. But for this commodity-related impact, we would have been close to 9% EBITDA margin for the quarter. Apart from the Wires impact, there is continuing margin compression in Durables due to pricing gaps compared to input cost increases. We expect the gross margin in Durables to improve from Q3 and to reach pre-COVID levels by the end of Q4.

As we have shared before, our shift from outsourcing to in-house manufacturing impacts certain line items in the presentation as per accounting standards. As own manufacturing increases, there is a shift from material margin to the 'other expenses' line. Some volume-related costs like freight and warranty are also classified under other expenses. This has a significant impact as the turnover has increased by 36% in the first half.

We remain positive on improved margin performance going ahead. The recent softening of input prices meant that further price increases won't be required. As the existing inventory flows through the pipeline, the pricing gap will reduce. We expect the gross margin to revert to their normative levels by the end of the financial year.

COVID-related disruptions had led us to hold higher inventory than normal. With risk of supply chain disruption diminishing, we intend to reduce our inventory holding. Due to lower sales than forecast during September, the inventory reduction has proceeded slower than anticipated. While it may take longer than planned, we will revert to normative stock levels in the coming months.

With that, I conclude my opening comments. I would like to thank the team at ICICI Securities and Aniruddha Joshi for hosting this call and would like to request the moderator to open the floor for Q&A. Thank you.

Moderator: Thank you, very much. We have our first question from the line of Aditya Bhartia from Investec. Please go ahead.

Aditya Bhartia: Sir, my first question is on the Consumer Durable vertical. When we looked at some of the other companies in ECD and FMEG segments, we saw that their revenue growth was actually being fairly muted, while we have managed to deliver 20% plus growth. So just want to understand, has growth in South also been fairly strong, or is this growth being driven largely by Non-South India for this segment in particular?

Mithun Chittilappilly: For V-Guard, the Consumer Durables segment has a lot of categories with some categories that are faster growing than our peers. For example, we have Kitchen Appliances which is small and is growing fast. We have a Fans segment, again, that is small compared to some of the market leaders but is growing faster. So some of these would have contributed to higher growth.

Aditya Bhartia: Would it be positive for you to share how large the Fans business would have become now? Given that we had made operational our Premium Fans' facility some time back, how is that contributing to overall sales?

Mithun Chittilappilly: We do not give out product-wise numbers. Once we complete some milestones, we will give out some information. However, nothing to speak on this today.

Aditya Bhartia: The second question is on the margins for this particular vertical. How would gross margin for this segment be different from the Electronics segment? What we see are low EBIT margins for this segment. Is that a reflection of lower gross margin or is it overexposure to, maybe, the economy segment or is it just that overhead costs are currently not getting properly absorbed given the smaller scale? As we keep building scale, do you again see margins heading towards high single-digits or low double-digits of EBITDA?

Mithun Chittilappilly: In the Consumer Durables segment, both in the Fans and Water Heaters businesses, the business units and their margins are impacted. They are largely on account of pricing gaps, in the sense that the commodity prices have gone up to some degree and the players in the market, due to whatever reason – may be hyper-competition, poor season, whatever it is, are not passing on the full effect into the market.

Second is that in the Fans segment, especially, there is some flux in terms of changeover in the new BEE norms. So, there has been some slowness in the market, in that sense. The commodity prices have come down, which also means that no company had taken any price increase since April. Also, it is not required with the current level of commodity prices. As soon as the older materials are consumed and we buy fresh materials – raw materials, the gross margins should revert back to normal. We expect this to happen in Q4.

Regarding the gross margin percentage for Consumer Durables pre-COVID, Sudarshan, do you have the number? What is the normal gross margin for Consumer Durables?

Sudarshan Kasturi: The overall gross margin is higher than the company average. That is at 20% steady state. Currently, we are going to say that there is a margin compression.

Mithun Chittilappilly: So to answer your question, the Consumer Durables margins were actually higher than the company average gross margins pre-COVID.

Aditya Bhartia: So it is mainly about an absorption of some of the overhead costs. As the business scales up on a steady basis, can we see a significant margin expansion at the end?

Mithun Chittilappilly: Yes, that is happening. Also, the commodity price inflation has not affected all the products in the same way. So for something like Fans, this has been more sharper, because aluminum is one of the key components and aluminum prices have gone up very high because of the war situation.

Aditya Bhartia: The last question from my side is on the BEE rating change – are you expecting significant pre-buying to happen just before these new norms become applicable? Once these norms become applicable, do you anticipate some market share movement within the brand?

Mithun Chittilappilly: I think the trade will be up-stocking in the current quarter, not only for us but across brands, because brands will have to stop selling them before 31st December. There will definitely be up-stocking by the trade in this quarter. Going forward, I believe that market will normalize. I suppose that every company has brought out products that are conforming the BEE norms. This is not a new thing, it has been in the works for at least three years. We have all had adequate time to prepare to change over. Of course, the companies who are better prepared with the BLDC products, will have more hedge because the BLDC segment is fast growing and is growing fairly fast as a sub-segment of the overall Fans business.

Moderator: We have our next question from the line of Rahul Agarwal from InCred Capital. Please go ahead.

Rahul Agarwal: First question was on the industry rather than the Company. The demand has been pretty much all over the place and dealer expectations in the first half and rural, being slower than the urban market because of inflation. So after this festive season, let's say, November, December and beyond, do you think things look okay? Would you think the jury is still out there whether demand can actually sustain at a decent level, especially when customer pricing is still at the same level and then hardly any price cuts being taken by brands with input costs actually being lower? So any thoughts?

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

V. Ramachandran: Yes. I think input costs have come down, but also the input correction has not been fully reflected in the market. What we are witnessing today is the stress as a consequence of that. This stress is still going to remain on one side. When it comes to demand – in the immediate run-up to the festive period, some stress in demand is observed, particularly, 30-45 days; we found that we fell short of our plan.

Having said that, if we take a three-year view of how we have performed for the last quarter, then we find that actually we have still grown at about 15% or something like that, even on a half year level, or maybe around 17% if you just look at for the quarter. One of the issues when we are comparing with the previous period, the COVID impact for the first quarter of last year is also affecting how the numbers look when you make comparisons.

At this point in time, it is difficult to say how the demand will pan out in the next half, but I think it is fair to say that there is a stress on demand in rural markets, smaller towns or entry-level products. That definitely that has been there for some time now. I have seen that from the early stage of the commodity run-up and it was initially reflecting in stress for passing input cost increases. So the companies were stressed in terms of margins on entry level products because of the inability of the market to absorb.

This challenge will continue for some time. I think the business has been living with this challenge from the last 12-18 months. So in that respect, that's a continuing challenge. But I think there are some other factors also, like the transition to the new energy standards, it is causing some destocking in Fans. The price reductions in Wires is causing some reduction in the Wire inventory and so on and so forth. So these kind of factors are also playing out because trade is down stocking.

I think some of the slowness that we are seeing is a combination of these two factors also, where there is some short-term destocking happening in the channels, so that they are able to adjust for any potential risks arising out of this energy change or any further downward impact from copper, which is fundamentally reflected in the Wires business, right? But yes, there is some stress because, we found that in Consumer Durables and all, the planned selling that we wanted to do did not happen. So there is some stress in terms of sell-out. We will know better in the upcoming two months once the post-Diwali uptakes are replenished by trade.

Rahul Agarwal: On gross margins – South and Non-South are almost becoming equal, so we should not even discuss regional sales henceforth. Is the gross margin difference is still there? The pricing is still lower in the Northern market versus South for V-Guard and how is that moving?

Mithun Chittilappilly: Yes, Sudarshan?

Sudarshan Kasturi: Well, there is no difference between gross margin in South and Non-South and pricing is also uniform. So there is nothing really to call out.

Mithun Chittilappilly: For the last, maybe, three years or so, this has been the case. It has almost been that for three years to four years that we have had a uniform pricing.

Moderator: We have our next question from the line of Sonali Salgaonkar from Jefferies. Please go ahead.

Sonali Salgaonkar: My first question is regarding the demand in the industry right now. You did mention that the latter half of Q2 saw slower demand. What are the initial demand trends that you have witnessed in the festive season and what is the level of channel inventory right now across most of your product categories?

Mithun Chittilappilly: So Ram, take this?

Ramachandran: Yes. Wire sales have been slower because of down-stocking by trade, as wire copper prices have been coming down; they have been adjusting their inventory to adjust risk. We have also seen a bit of pressure on Fans as the trade is preparing for the post BEE scenario, so they are slower to up-stock and they are slow to up-stock even on growing categories like BLDC because they want to correct their overall portfolio. They are focusing more on liquidating fans which fall in line with the old energy standards. So I think these are the two areas.

I think in Water Heater sales also, our plan has been more bullish, but what we have seen is that although the growth is good, it is less than what we would have wanted. These are some areas where we have seen some stress points.

Having said that, there is also an issue of appreciation of the subject because, when you are making - for example, we have grown at close to about 8.5%-odd, and that is like 8.7%, 8.8%, and if the wire prices were constant, this would be more like 11% or 11.5% kind of growth, which will not be bad because the base period was a higher base as there was shift of sales from Q1 to Q2. So I think there is a bit of maybe -- I mean we also anticipated a much higher sales.

Definitely, some slowness was observed in some of these categories. It may also be because of this 'Shradh' period was coming, especially for the month end, right? As far as the channel inventory is concerned, yes, I think that is also reflecting some increase in terms of the number of days and that is also one of the factors why we still said that there may be a slowdown in the last 30-45 days. There is some increase of channel inventory, it is not alarming or anything, but we are seeing that there is some increase in channel inventory.

Sonali Salgaonkar: What about real estate demand, you have two categories?

V. Ramachandran: Real estate demand is also a bit slower, yes. However, that is a bit difficult to derive because there may be some amount of -- see, in our portfolio, we primarily need to look at Wires, Switches and Switch Gears. We are not a very big player from an industry standpoint on Switches and Switch Gears, and most of our Switches and Switch Gears' sales are primarily retail.

But yes, Wires is also retail and we have a reasonably large Wires business. There is a bit of slowness. We are finding that collections are getting a bit slow and rotation of money is getting a bit slow. So some of these are some of the indicators which are contributing to the feeling that there may be some slowness in the last 30-45 days of last quarter.

Sonali Salgaonkar: My second question is on price hikes – last quarter or this quarter that we are in, have you taken any notable price hikes also in the Fans with respect to the new BEE norms? How much of price hikes do you expect?

Mithun Chittilappilly: Ram?

Sudarshan Kasturi: If you were asking about price movement during the current quarter, prices have largely been flat compared to Q1, except for Wires.

Mithun Chittilappilly: There has been no price increase per se between Q1 and Q2. I think in Wires there would be a drop of prices. Other than that, there is no change. On BEE, I think there are primarily going to be new models. So I think in the entry segment, the price increases are about 5%, if I am not mistaken. Ram, do you want to clarify?

V. Ramachandran: Yes. It is in that range. Fundamentally what will happen is that the newer models will get launched. It will not represent an increase in price per se. But the newer models will probably be positioned at higher prices anywhere between 5-8% depending on the segment that we are talking about.

Sonali Salgaonkar: How much percentage or rather how much portfolio of our Fans is into premium fans right now?

Mithun Chittilappilly: I think mid and premium would be about 40% I think. Ram?

V. Ramachandran: Yes. It is a bit more than that, Mithun. I think in the last year or year and a half, I think the sales in entry level have been also stressed relatively. So I think it probably would be over 50% now, 40-50%, is what you can take it as.

Sonali Salgaonkar: Could you give us the broader idea of volume versus value mix in Cables and Wires this quarter?

Mithun Chittilappilly: We will share that offline, Sonali.

Moderator: We have our next question from the line of Nirav Vasa from Anand Rathi. Please go ahead.

Nirav Vasa: What are the kind of growth prospects that you are seeing in our core product category of Stabilizers and how do you see that for the second half of the year? The second question is pertaining to the range in reach expansion. Already in South and Non-South we are favorably placed, but what would be our next steps with regards to expansion of our channel base?

Mithun Chittilappilly: Ram, you want to take this?

V. Ramachandran: I will address the second question first. You are basically looking at what are our plans for channel expansion. The mix of South and Non-South is favorably progressing, but we have probably covered 60-65% of the journey. We still have significant scope in Non-South to increase reach and improve extraction also. There is the throughput for counter and the reach. The reach will continue to expand at the rate of around 5,000 to 6,000 outlets every year. We will continue to add as far as Non-South is concerned and as far as the distribution reach is concerned.

Additionally, we are increasing focus on the organized retail. We have been weaker in organized retail and this is an area that we will be focusing on in the next two to three years,. That will also lever an opportunity for us to expand our business here.

So these are the two broad levers that we will be focusing on – 5,000 to 6,000 new counters annually – as we have been doing over the last 5-6 years and improving our width and depth in organized retail. That is a lot more easier relatively, in terms of access compared to retail expansion.

Nirav Vasa: On growth in Stabilizers?

V. Ramachandran: The Stabilizers growth has been in the region of around; if you look at our Electronics growth, for example, it is in the region of around 7% odd, if you look at a four-year CAGR for Electronics as a segment. It is, of course, lagging the growth in Electricals and Consumer Durables. That being said, that is part of our growth trajectory. If you look at our three-year CAGR of 15% that we have achieved, the Electricals and Consumer Durables segments are segments that we are focusing on to drive for faster growth.

Just one more point. I think one of the key challenges with the Electronics segment and Stabilizers in particular is that, I think COVID stress has impacted at least, two of the three or four quarters over the last two years because COVID typically has come in and impacted in the summer months. So I think a couple of years of free and open summer should give us a better sense of how Electronics growth CAGR will move.

Nirav Vasa: Since we are a very strong player in the Stabilizers market, can we target export markets using this product?

V. Ramachandran: There is an export market and exports are certainly possible. The only thing is that each market has a different requirement. That requires a lot of focus and there is a lot of competition particularly in Africa and those kind of markets where this kind of product has some opportunity.

There is a lot of competition from China also. We have chosen to focus our energy on the Indian market and the Indian business fundamentally when it comes to Stabilizers and build V-Guard as a consumer brand in the Electricals and Consumer Durables space. Thus, I believe that that is more value creating, and this is why we have chosen that kind of a path.

Moderator: We have our next question from the line of Dipak Saha from Savart.

Dipak Saha: In terms of high-cost inventory that you all have. Is the amount of high-cost inventory that you have compared to the current level of copper prices still significant or is it almost gone? If you can share some color on that side?

Sudarshan Kasturi: On copper, the issue is gone. It was during July and the first half of August that we were having the higher cost inventory. Once that was gone out, Wires' margins are back to normal in September. Thus, it is not going to be an issue with Wires anymore.

Dipak Saha: On the aluminum front?

Mithun Chittilappilly: It is primarily in the case of Fans where we are holding some high-cost inventory, though by the end of Q3 even that will get exhausted. We are not too concerned about that, but yes, that would mean that the margin improvement in Fans will take some more time to kick in.

Dipak Saha: If the commodity prices kind of stabilize at this level, do you think that by the end of this year, you will be able to reach the similar EBITDA margin level of 9-9.5% of where we ended last year, given the operational efficiencies that we have or it will again take some time for the operational efficiencies to reflect in terms of EBITDA margin?

Mithun Chittilappilly: Given the current cost environment, prices do remain where they are. I think by the end of Q4 we should hit the kind of gross margin that we had before all the inflation started. That is our expectation as well.

Dipak Saha: On the Electricals side, if you can share some idea - is there any softness in terms of demand on the Electricals cost, given the growth that we recorded on a YoY basis or is it a high base impact that we are having on the Electricals front?

Mithun Chittilappilly: No, Electricals it is primarily for us; if you look at Electricals, its largest component is Wires. So whenever there is a copper price decrease, the trade destocks. When the trade destocks, obviously the sales will slow down. That is when the trade will wait to see a bottoming out of copper before they restart stocking. That is what we are seeing. It is probably more to do with the pricing environment rather than the demand environment.

Dipak Saha: As you said, by the end of Q4, we will be able to get back to this high level of margin. Does it mean that we will get back to this level of margin, but we will not end close to somewhere where we ended last year, in terms of full year basis?

Mithun Chittilappilly: I do not want to give out any specific numbers, but what we believe and hope is that, given the inventory we are holding, given the current price environment and given the pricing in the market and the overall scenario, our expectation is that by somewhere in Q4, we should start to be in the gross margin levels, where we were before COVID. I think in COVID what happened is that there was an expansion of gross margin also, because initially the copper prices, I mean the commodity prices came down and then it shot up. So what we will look at is probably the pre-COVID margin number.

Moderator: We have our next question from the line of Pranjal Garg from ICICI Securities. Please go ahead.

Pranjal Garg: My first question is regarding the inventory days. You highlighted that inventory days will get normalized. What will be the target range, where should we expect inventory days going forward?

Sudarshan Kasturi: Yes, we normally operate at about 70-75 days of inventory. Currently, we are holding more than that and we would want to come back to those levels.

Mithun Chittilappilly: We are probably having maybe 20 days more inventory than what we used to hold before COVID. During this time, we decided to increase a few stocks and such. So we wanted to reduce it significantly by the end of this quarter.

As Ram mentioned, the sales are less than what we anticipated, so we are still carrying some inventory. We hope that by the end of Q3, we can reduce inventory by 15-20 days.

Pranjal Garg: An earlier participant has also asked about the distribution strength in Non-South states; can you quantify your South versus Non-South distribution stream as of now?

Mithun Chittilappilly: You are talking about the number? I do not know whether we have the exact numbers with us today.

V. Ramachandran: I do not have those numbers right now.

Mithun Chittilappilly: We will share the retailer numbers offline.

V. Ramachandran: One important point to understand is that it is simply not the number but also extraction. We could try and sell it to 100 dealers in a town or to 20 dealers in town with, you know, 30% share of the counter which will be more meaningful. So both of these are important.

Pranjal Garg: Apart from that, the Company has started its Roorkee facility which was a Greenfield CapEx, - Does it need any new Greenfield CapEx in the near term to meet its growth targets in the near term? What are the CapEx plans for FY23 and FY24?

Mithun Chittilappilly: We have three more plants under construction and it will take over 18 months to complete them. This year and next year, Rs. 70 crores of CapEx has been earmarked for that. Some part of the CapEx this year has already been spent out of the Rs. 70 crores.

Pranjal Garg: Regarding the new categories in which V-Guard is entering, like Water Purifiers – what is the strategy for this new category, in what geography has it been endorsed and how has the traction been?

Mithun Chittilappilly: Ram, you want to take this?

V. Ramachandran: Yes. We are still in the early stage of introduction and roll out of the Water Purifiers business. We are still expanding our product portfolio and lineup to improve the addressability. Our current focus is to work through e-commerce and build a decent business through the e-commerce focus. That should give us comfort on the competitiveness of our mix, based on the depth of extraction that we are able to make in the category. After that, we would open out into organized retail and then only will we get into GP. That is how we are going to travel with Water Purifiers.

Moderator: We have our next question Aniruddha Joshi from ICICI Securities. Please go ahead.

Aniruddha Joshi: Yes, sir, two questions. One, how do you see the Kitchen Appliances growth panning out and how is the penetration of the category in South India as well as Non-South India? Do you see any competitive intensity with the acquisition of Butterfly? The second question is on the effective tax rate, as the products and the unit ramps up, how do you see the effective tax rate panning for FY24 and FY25?

Mithun Chittilappilly: On the Kitchen Appliances part, Ram, do you want to take it?

V. Ramachandran: Yes. See, Kitchen Appliances business is currently mostly focused in the South for us. It is growing much faster than the overall company growth. Still, we are in the very early stages. I think we have established the product breadth, the supply chain and these competitors of our category. We are currently working on putting in place a manufacturing facility which should come up in the next 12-18 months so that our competitiveness in this category can be enhanced. So that is our near-term focus. We believe that in doing so, it will help us to improve our ability to grow this category and business aggressively. Mithun, do you want to take the second part?

Mithun Chittilappilly: Yes. Regarding Butterfly, we do not want to make any comments on competitors. So I will skip that. Regarding ETR, Sudarshan?

Sudarshan Kasturi: Yes, the new manufacturing entity will have a tax rate of about 17%. So there is some amount of tax benefit that can come from there. FY24 is going to be a ramp-up period, so we may not see a very significant effect, though there will be some reduction. In FY25, we can expect a 2% ETR benefit coming from there.

Aniruddha Joshi: Any change in market share that you would have noticed in our categories in the last six months or so?

Mithun Chittilappilly: I think market share is not to be seen on a quarterly basis. When we complete a year then we shall talk about it. Maybe it is too premature to talk about market share.

Moderator: We have our next question from the line of Aniket Mittal from SBI Mutual Fund. Please go ahead.

Aniket Mittal: Just a few questions. Firstly, wanted to understand the margin trajectory a little better, as you are guiding for the margins to recover by Q4 to the pre-COVID levels. What would this be dependent on? Is it largely a function of the high-cost inventory being absorbed or are you seeing certain amount of volume pickup or price hikes that you are basically building this in?

Mithun Chittilappilly: Our gross margins are off by 2.5-3% from where we should be, from normative levels. We believe that the current level of commodity price offers that reduction, provided the current high value, high-cost inventory sells out and we are purchasing cables at today's prices. So I think this entire process will take 4-odd months when the supply chain will keep liquidating the current inventory and buying raw material and manufacturing goods at the current prices going forward. That is going to be the main reason for the margins to come back to normal.

Aniket Mittal: This assuming it would largely be on the Wires business and the Fans business?

Mithun Chittilappilly: Wire is more faster. This will be primarily on the Consumer Durables business where we are having more stress. Mostly Consumer Durables and maybe even Inverter Battery, little bit of Inverter Battery, but I think it is mostly Consumer Durables business. In the Wires business, we do not carry much inventory, so the impact – we would have already seen the reduction of prices would be immediate and the consumption of new materials will also be immediate. So it happens more faster in categories like Wires.

V. Ramachandran: So then, the recovery has to happen in Electronics and Consumer Durables segment and the Electricals segment will come back faster.

Aniket Mittal: In one of your remarks, you mentioned that the growth in Water Heaters has been less than what you would have anticipated in the quarter. Just wanted to get more light on how that market is panning out and why has the growth not come in this quarter?

Mithun Chittilappilly: See, Water Heaters business, we lost some market share a couple of years ago. Thus, last year and this year, we plan to grow more aggressively than we have been growing. Of course, we have regained all the market share that we had lost, but we still have lost a year that we need to catch up on. In that sense, yes, our growth has been less than what we anticipated, but we probably still have grown faster than the market.

Aniket Mittal: This is just to understand a bit better on the growth in certain individual categories. If I look at, let's say, the ECD segment of Fans, Water Heaters and the Electricals segment of Pumps and Wires, could you give a broad understanding of what has been the YoY growth for this quarter and the first half?

Mithun Chittilappilly: No, we do not give out product-wise numbers.

Aniket Mittal: You had acquired the Simon brand on the Switches front, it is fairly positive in Switches and Switch Gears in the segment. Just wanted to understand what is the traction that we are seeing within the segment and how are we planning to merge the Simon brand in our portfolio?

Mithun Chittilappilly: Ram, you want to take this?

V. Ramachandran: Yes. So I think we are still in the acquisition process and this is not complete yet. It is going to be a merger, which means this is a NCLT driven process. If you take another couple of months maybe for the process to be complete and for the entity to join hands. This has not yet materialized on the ground in terms of initiatives. The merger is a work-in-progress and we should come back on this sometime in next quarter.

Aniket Mittal: Is it by the next quarter that we would expect it to be completed?

V. Ramachandran: Yes.

Moderator: We have our next question from the line of Keyur Pandya from ICICI Prudential Life Insurance. Please go ahead.

Keyur Pandya: The question is on the overall profitability and operating profitability. As you mentioned that as high-cost inventory is consumed at current prices we will go back to pre-COVID levels' gross margins. Now if I look at pre-COVID gross margin which we had in those years, from that level, our sales levels have gone up. In that backdrop, how should we think about our operating margins? Just to add another layer, as you hinted that there is some slowdown in the demand and you are seeing competitiveness in pricing as well, do you see any risk to this increasing gross margin as people go for volumes over profitability to push the demand? How do you see this equation playing out and the net impact on the operating margins of the Company?

Mithun Chittilappilly: We have a portfolio of products and when we see it as a portfolio, yes, this particular issue is there in, maybe, some of the categories, but not all. However, as a Company, we do not foresee it as that much of an issue. Like I said, we were off by 2-3% in gross margins on a Company level. The price reduction since May have been almost in that same range. So that is what gives us the belief that it is possible to go back to the margins.

We will see the hyper-competitiveness happening either in category A or category B, but it does not happen across. This may not be an entire portfolio problem but in individual categories this issue may be there. We also found that these are transient issues and after some time, people do understand that cutting prices is zero-sum game because everyone else will also do the same and then finally, there is very little evidence that someone will actually gain market share by cutting prices. Once that realization happens; we have seen these things are transient and they will move on. For example, about four to five years ago, Kitchen Appliances was a very hyper-competitive category. Then after five years, we found it to have mellowed down. Then few years ago Water Heaters was in the same position. Today, we are seeing it mellowing down. I think it will keep happening, but as a Company or as a portfolio we do not see it as a risk.

Keyur Pandya: So when we talk about the pre-COVID gross margins, from those levels, our sales are at a much higher level. Would it boil down to a much higher EBITDA margin also as we improve gross margin?

Mithun Chittilappilly: I think it is not that high. If you look at a three-year CAGR, we are talking about 15%, because three years have also passed after COVID has started. We should also look at it from that lens that time has also passed. Yes, there has been some increase in prices, but this has been only maybe for one year, that there is really an increase in prices. If you look at the previous year, the price increases were very minimal because commodity prices have remained flat since maybe 2016 or 2017.

V. Ramachandran: Just to add to what Mithun said, we continue to grow at 15% per annum, but we are also a company which is continuously making investments. We have got into manufacturing and by maybe another 12-18 months, we will complete the manufacturing footprint expansion. We are investing in talent, we are investing in technologies, we are investing in the future. The other part is that these investments will also come at a cost, this also you need to keep in mind. It is not just matter of saying that this kind of growth will automatically translate into bottom line. There will be investments for the future and those needs become more stronger, because of the changes in environment that have happened in the last three to four years. So that also you need to factor in. That is why it would be fair to say that the margins will be similar to what we were enjoying in the pre-COVID years.

Moderator: Thank you. I would now like to hand the conference over to the management for closing comments. Over to you, sir.

Mithun Chittilappilly: I would like to thank ICICI Securities and Aniruddha Joshi for hosting this call and thank you all for participating on the call.

Moderator: Thank you. On behalf of ICICI Securities, that concludes this conference. Thank you for joining us and you may now disconnect your lines.