"Pearl Global Industries Limited Q1 FY'23 Earnings Conference Call"

August 16, 2022

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MANAGEMENT: **MR. PALLAB BANERJEE – MANAGING DIRECTOR, PEARL GLOBAL INDUSTRIES LIMITED.**
MR. SANJAY GANDHI – GROUP CFO, PEARL GLOBAL INDUSTRIES LIMITED.

Moderator: Ladies and gentleman, good day and welcome to the Q1 FY'23 Earnings Conference Call of Pearl Global Industries Limited.

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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 '*' and then '0' on your touchtone telephone. Please note that this conference is being recorded.

I now hand the conference over to Mr. Pallab Banerjee - Managing Director of Pearl Global Industries. Thank you and over to you, sir.

Pallab Banerjee: Hi, good morning, and I welcome everyone to our Quarter 1 Financial Year '23 Earnings Conference Call. Along with me we have our group CFO, Mr. Sanjay Gandhi, and SGA our Investor Relation Advisors.

I hope all of you have gone through our Investor Presentation uploaded on the exchange and our company website. Since this is our maiden call, I would like to give a brief overview of our Company and the industry, followed by a review of the financial performance of the Company during the quarter.

Pearl Global Industries Limited founded in 1987, is a leading apparel manufacturer, offering end-to-end sustainable solutions to the fashion industry. We have a multinational presence across eight countries, India, Indonesia, Bangladesh, Vietnam, for manufacturing and USA, Spain, Hong Kong and UK for client servicing and designing.

Our diversified product offering across categories includes knitted tees, polos, and dresses, woven shirts, blouses, and dresses, denim jeans, outerwear jackets, active performance wear, and athleisure wear. And we produce for men, women and toddlers. Our 75 plus designers across these eight locations leave the journey for us from concept to the finished product.

Pearl Global has a well-diversified and derisked manufacturing base with 22 dedicated manufacturing units. Our total capacity to manufacture is around 82 million units per year.

Some of the key clientele includes Kohl's, Macy's, Tommy Hilfiger, Gap, Old Navy, Next, Nordstrom, Muji amongst others. In other words, we are a one-stop solution for the needs of retailer.

Our goal is to innovate the way fashion is created across the globe. And we are constantly working towards our mission to exceed customer and shareholder's expectations. We do this by strategically driving sustainability, technological advancement and bringing innovative solutions. Our design and product development team analyze the fashion trends and use modern technologies of 3D rendering. We do use 3D tools like CLO, Browzwear and Optitex to craft our products. Each of our locations are equipped with these digital technologies.

Talking about the industry, after a subdued start of Financial Year '21 owing to the COVID-19 lockdown and restrictions, garment exports did witness a fast turnaround. This was despite the high cotton prices and the supply chain delays arising due to the container shortages.

Especially the U.S. market had a pent-up demand for apparel as the economy opened up post-COVID. Whereas now for a short run we do have a challenging macro-environment globally. These are due to abnormally high rates of inflation and huge inventory backup with large U.S. retailers.

The looming energy crisis in Europe, on the backdrop of Ukraine War, and at the same time, on the other hand, we are looking at a continuous shift of apparel manufacturing out of China. Other Asian countries will continue to gain from this shift. Vietnam, Bangladesh, Myanmar and India has been steadily gaining due to this shift. While Pakistan and Sri Lanka due to their own economic turmoil, the exporters would get a mixed bag of benefits and concerns in the short run.

Now, Indian textile and garment exporters have a significant opportunity to grow with the shift of business from China. This is both due to the Xinjiang cotton which is banned, and its owned recent policies. There is high likelihood of India signing an FTA agreements with Europe and UK. The other government initiatives like the PLI, MITRA, RoSCTL schemes, the free-trade agreements provide a huge impetus heading to the growth opportunities.

With favorable Indian demographics and the industry dynamics, India is capable to position itself as a global textiles hub. India textile exports are expected to grow at 11% CAGR, to reach about $65 billion by 2026 from a pre-COVID level of $36 billion happened in 2019.

Now for Pearl, despite these headwinds on account of high inventory levels in USA retailers, and the H1 being a weaker season for Indian apparel industry, that is due to the seasonality of the products that we made in India, despite these headwinds, we are able to clock the highest ever revenue in Quarter 1 since our inception. Now this was facilitated by increased volumes aided by the new customer acquisition, better product mix and our existing ones, with an improved efficiency of our operations.

Our multinational presence works as our strongest synergy as customers continuously aim to shift sourcing from China to other countries. We envision a growing order book for the year of on the backdrop of these tailwinds. The new customer acquisition, continued improved performance and H2the second half of the year being seasonally stronger quarters, thereby yielding a growth in our Financial '23 versus Financial Year '22. Our multinational presence ensures we are present in two of the four major textile and apparel supply chains of the world. We aim to act as an end-to-end supply chain provider who can do concept to the store. This helps us in increasing the wallet share from our existing customers. Our endeavor is to improve our return ratios. And we are making conscious efforts to make that happen.

Our partnership model strategy is working for our planned growth initiatives. In the partnership model, role of Pearl Global and the partner are clearly defined where Pearl provides the working capital investment, the designing and product development, appoints execution and monitoring teams and the partners factories, procures fabric and is responsible for optimum capacity utilization of these partner facilities. Whereas the partner undertakes the CAPEX and we have a contract with the partner on per piece basis. The partnership model provides the following synergies; it helps us to faster capacity planning or ramping up the capacities as required, the capacities in proximity to the supply chain areas, thereby making us asset-light as we improve our return ratios.

Our strength lies in all these mentioned factors coupled with strong customer relationship, setting us apart from the others. For our way forward, in nutshell, our next leg of growth will be driven by the following strategies:

i) New customer acquisition

ii) Geographical expansion

iii) More automation in our facilities

iv) optimum utilization of the existing facilities

v) Growth through partnership facilities

vi) explore PLI scheme for our growth engine in India.

With this, I would like now to hand over the call to Mr. Sanjay Gandhi, our Group CFO, who will run us through the financial performance of the Company for this quarter.

Sanjay Gandhi: Good morning, everybody. And welcome to our first ever earnings conference call for Quarter 1 FY23.

Coming to the financial and operational performance of the Company, we have reported the highest ever Quarter 1 performance since inception. Our strong financial performance during the quarter was aided by improved product mix, increased contribution from in-house manufacturing and partnership facilities and improved performance in Bangladesh and Vietnam factories, have been the key driver of the growth in this quarter.

On a consolidated basis, total income for Quarter 1 FY'23 increased by 95% year-on-year to Rs. 851 crore, facilitated by improved volume due to better capacity utilization and increased contribution from partnership facility. Partnership factory contribution to overall revenue, increase from 2.8% in Quarter 1 FY'22 to 21.3% in Quarter 1 FY'23, translating to 1.9 million pieces on a standalone basis. EBITDA for Quarter 1 FY'23 increased by 370 bps year-on-year to 7.9%. PAT for the quarter stood at Rs. 36.4 crores versus a loss of Rs. 0.8 crore in Quarter 1 FY'22.

The increase in profitability is due to improvement in margins aided by operating leverage, better product mix and improved capacity utilization.

Going ahead, we are confident on the industry growth and we believe that our Company is best placed to capture the larger pie of this opportunity.

Thank you. We shall now open the floor for question-and-answers.

Moderator: Thank you very much. Ladies and gentlemen, we will now begin the question and answer session. Our first question is from the line of Keshav Kumar from RakSan Investors. Please go ahead.

Keshav Kumar: I just wanted to ask if our partnership model is similar to what our Related Party, PDS is doing with this sourcing business or is there a difference?

Pallab Banerjee: Our model is definitely different from PDS model. In PDS, basically, it's a more of a trading and sourcing model. Their business in terms of trading would be I would say close to about 80% plus, whereas we present ourselves to our customers as a manufacturer. We do have the partners who are working for us where certain capacities or certain factories we undertake for our production, which is completely dedicated to us. So, that capacity is completely dedicated throughout the year for us as manufacturer, whereas in trading it is as per the need. I hope the difference is clear to you.

Keshav Kumar: And when we onboard a partner, do we have any return metrics in mind or are we trying to build our business for now and not like scale and not focus that much on the returns? I mean I am sure that our geography of where we get the partner would be essential. So, just trying to understand how do we if there's an internal model that we follow?

Pallab Banerjee: So, let me add to the last question that you had. See this kind of model do exist in countries like Bangladesh and Vietnam, where we have partners who have been working for us with a dedicated capacity for us for some time, for more than couple of years, I would say. And in India, this concept is still quite new. So, we have started with at least one arrangement or two arrangement at this point of time, where we take that capacity and feed continuously throughout the year, and we develop it as our own factory. That's the way that we work with our partners.

In terms of return, definitely, as we have mentioned, that we do have a contract on per piece basis, where it is beyond a simple subcon, it has a little bit of profit sharing is included into it, but we do our arrangement on basis of a number of pieces that we do, Sanjay, you want to add something.

Sanjay Gandhi: Yes, just to add we do like you said, we do have a internal benchmarking standard, where we are looking at, overall return on capital employed for any incremental partnership arrangement to be close to 20%, that's the target, we really work towards it. So, this is normally the threshold hurdle which we try to say, at least a 15% plus it should start and then we reach to that level.

Keshav Kumar: Secondly, the bulk of our manufacturing as per the presentation comes via Bangladesh. So, just trying to understand the EU FPA we have signed, will it be detrimental to the production via Bangladesh versus India, would it not affect us --?

Sanjay Gandhi: So, you see that in terms of our turnovers from the respective countries, if I look at it, close to about 70% comes from India and Bangladesh, both in between, I would say, between 30% and 40%. It should vary. So, some sometimes, like this particular quarter, if you see that India is slightly more, almost close to 38% of the turnover. So, we would continue to maintain that, of course, Bangladesh, we did recently one acquisition, so the percentage will grow up by couple of points. But more or less, it would still remain similar. India and Bangladesh doing about almost anywhere between 70% to 75% or close to 80% and Vietnam and Indonesia will do the balance.

Moderator: Thank you. The next question is from the line of Hemant Shah from EdhaWealth. Please go ahead.

Hemant Shah: I just have two questions. Now, since we have done great sales in Q1, and one of the highest sales actually in the history of the Company, Q1. And it's a dull quarter, first half is usually the lean quarter. Is it fair to assume that we can comfortably do a top-line of say around Rs. 3,100 crore or so for FY'23?

Pallab Banerjee: So, I think this is where we are really looking at it, I think in terms of the number definitely this is in our target line of achieving crossing Rs. 3,000 crore in this financial year. The Quarter 1 has been really very encouraging and it's moving in this direction, with all other facilities really coming into place and utilization improving we are quite hopeful of going in that direction.

Hemant Shah: Because usually even if we now do not grow for the next three quarters, I mean we can comfortably achieve Rs. 3,000 crores since the Q1 was extraordinarily strong. So, what was the reason for this traction in Q1, I mean if you can just elaborate?

Sanjay Gandhi: So, as I mentioned, like, we had all the three strategy working for us, like, we were acquiring new customers, we were going for better efficiency that means utilizing more of our capacities. And we also had the better mix. So, where the per piece value or per unit value goes up for --

Hemant Shah: That is going to continue the per mix revenue, I mean, the value-added products will contribute more going forward do you think so?

Pallab Banerjee: That's an endeavor, definitely. It definitely helped that U.S. market had a very high demand for that particular period. So, it's how the market changes like everything is not in our control, but when this is the strategy and this is the endeavor, and this is the way that we are progressing.

Hemant Shah: So, my second question would be, can this margin of 7.8% or around 8% level be maintained, because I mean, if we try to pursue this Rs. 3,000 crore of turnover, the efficiency and the utilization will be definitely good. So, is it fair to assume that margin should be in this range for the whole year, I am not talking of any quarter.

Pallab Banerjee: Yes, whole plan and strategy is made for that. As I said, like, there could be certain risks in the market, or in the macro factors that we are seeing otherwise, if it doesn't go overboard, like this risk doesn't become too much, or it doesn't go too much out of control. We are on that journey and that's our endeavor.

Hemant Shah: And if you can just give some more elaboration on this China Plus One strategy, since we are located in India, Vietnam, Indonesia, Bangladesh, and I am sure we are witnessing some positive traction with respect to China Plus One strategy. And if you can just elaborate something what kind of traction we can see or what kind of new customers or added volumes we can see, going forward?

Pallab Banerjee: See, due to the geopolitical situations like U.S. definitely brought out policies in which they were discouraging sourcing from country-of-origin China, major being the Xinjiang cotton, which got banned in the U.S. So, the cotton products started moving fastest I would say, that is still continuing, most of the U.S. customers have moved their garment or apparels of cotton, maximum out of China. The one who have got a strong supply chain or a strong sourcing base so they are able to move faster; the companies which did not have or do not have a very strong sourcing so they are following. So, that trend will continue, because see, China used to be for U.S. market almost like I think about $35 plus million. So, it's a huge market. So, it will continue to move for some time.

Apart from that, there are certain ones, the big ones who have very established sourcing arms. So, they are trying to now work on the non-cotton product as well.

Now, the countries who have immediately benefited out of this is definitely Vietnam and Bangladesh, which numbers can tell you like you can see that they have grown at a very higher percentage compared to other countries like Myanmar, India and Sri Lanka, Pakistan so far. So, this trend will continue. And as Indian policies are becoming better and FTA discussions are on, and with the Indian demographics that we have, we do expect some more investment coming into India and India should benefit as well.

Moderator: Thank you. Our next question is from the line of Parth Desai from HCM. Please go ahead.

Parth Desai: I have a quick question of the capacity utilization. So, what's the current capacity utilization, let's say for FY'22 and the 1st Quarter, if you could share with me? What is the capacity utilization was for, let's say, the last year and this quarter?

Pallab Banerjee: So, if you see, the way that we have established our factories, and the partner factories, we do have a capacity of almost about 80 million plus. So, out of that, we are at this point of time in the range of 65% utilization, I would say. So, definitely we are going towards from 65% to 75%, that's the kind of growth plan that we had for this year. And we are continuing on that journey.

So, by capacity, I mean, the infrastructure that we have created, but we are not utilizing all the machines or the workforce, like we have not put in as of yet. So, we can, without any major CAPEX investment, we can go towards this number. So, that's what I mean by the capacity.

Parth Desai: So, essentially, without any significant CAPEX, you can get to 80 million type --.

Pallab Banerjee: Yes.

Parth Desai: And then in terms of, let's say, geographic revenue, you have shared I think manufacturing revenue, but from let's say, a client perspective is the majority of your client base in the U.S., and is there so called geographic expansions done?

Pallab Banerjee: So, from the customer point of view, our major business is U.S. at this point of time. We would like to have a better percentage mix across the globe. But what we experienced during the pandemic period, and just after the pandemic period, there was a huge demand, which U.S. came in first, Europe still was slow. And then the war happened, which slowed down a little bit more. And also, we saw that Japan and Australia has been really slow in terms of the demand for the last almost, if I look at one to two years period, so that definitely would change. So, to give you numbers, like at this point of time, I think in this last four or five quarters, if I look at, our presence in U.S. would be maximum, would be more than 80% or more towards 90%, I think it is 80% to 85% plus. So, that should change a little bit, as we go forward.

Parth Desai: And a follow-up question on that would be your most of your clients are mighty global clients like let's say Tommy Hilfiger or Calvin Klein or even Ralph Lauren. So, let's say, give you orders only for the U.S. and not, is it something to do with some trade agreements or?

Pallab Banerjee: No the clients that you mentioned, like for example, Tommy Hilfiger have got a big presence in Europe as well. So, we are, of course like we started with them with the U.S. manufacturing, and now they are starting to source for the Europe as well from us. So, the brands which are global, definitely we would like to serve them across the globe. And then apart from that, there are other customers like Primark in UK, or the Inditex Group, which is the Zara and Bershka and all. So, we are quite big with them as well. And in Japan, there is Muji, in Australia there are Target, Kmart and Big W. So, those are also in our folio. So, those are also we are seeing substantial growth, as well as now those markets or the economies are opening up in terms of, the retailers are opening up more number of stores. They were quite shut for a long period of time due to COVID.

Moderator: Thank you. We will take our next question from the line of Akshay Kothari from Envision Capital. Please go ahead.

Akshay Kothari: As you mentioned, our majority of business comes from U.S, so any discussions with the customers because there is ongoing recession, any slump in demand which we are expecting, any guidance on that?

Pallab Banerjee: Recession or not recession, I think apparel is normally like after once your food and petroleum is taken care of, I think apparel is the next need, which will continue to happen, that is #1.

#2 At this point of time, U.S. is undergoing a high inflation and fear of recession. So, let's see how that evolves. We are impacted more in the short run due to the inventory level or high inventory level with some of our customers, which definitely is the result of the inflation and to certain extent, maybe the fear of recession. So, because of which what we are seeing is some of our clients like from U.S., which are the large format retailers they have cut down their buys, anywhere between 10% to 30%.

We do not have a big exposure with very large format retailers like Target or Walmart in a big way, Walmart USA, I mean, where this cut or the inventory situation is even more steep. So, that is why some of the large exporters of the world like the Taiwanese or Koreans are majorly affected at this point of time.

We are seeing lack of demand from the kind of customers that we work with that is the Gap Inc. or the Kohl's or the Macy's where anywhere the reduction is between 10% to 30% on the seasonal basis that we see in terms of their booking.

As I said like part of it is getting compensated because the Japan market, the Australia market is opening up more, demand is going up in those market in comparison, I would say like what I have seen in the last couple of years or simultaneously as I said like we continue to add a new customer in our profile, so that we can continue to utilize our capacities.

Akshay Kothari: Also I wanted to know what would be our current revenue from the partnership facility?

Pallab Banerjee: So, like, Mr. Sanjay mentioned a number like the percentage in this year what we saw grew up from almost about 2% level to high 20%

Sanjay Gandhi: It's on a standalone basis the point grew from 2% to 20% in India. The standalone revenue is Rs. 320 crore plus. So, that's the region Rs. 50 crore to Rs. 60 crore we have now, in India that is the contribution. If you take overall Rs. 851, I think it will come around 7% is coming from the partnership factories of India.

Akshay Kothari: And in the opening comments you mentioned that improvement in margins was due to product mix operating leverage and better capacity utilization, so wanted to know, how are we trying to increase? So, first of all, what is our current average selling price? How are we trying to improve it? And can you please elaborate regarding the product mix change which we are trying to achieve?

Pallab Banerjee: So, I won't go into detail of numbers in this, but I can give you the concept, conceptually like what is happening. We have a presence like I told you, like almost 20% of our total revenue is coming from Indonesia and Vietnam, where we do a lot of high-end products, lot of value-added products like outerwear, jackets, high-end athletic wear. So, those are of high values. And those are also supplied to the customers like who are looking for high-value product, high input in the garments.

Similarly, like in India, Bangladesh, it is generally like we are trying to upgrade our facilities to serve better and go for better price points, compared to what we have done in past. But that also depends like one is our intent and the second would be how the macro factors are playing out, like how much of those customers are buying and what kind of volumes they are driving.

So, yes, this is how it plays the outerwear, the high-end athletic wear, the high-end technical garments that we make out of Indonesia and Vietnam, definitely those have increased quite a lot. And that is shown in some of the results and also in Bangladesh or in India, like the products which cater higher FOB like more of the knits to denim, or certain outerwear jackets and all so that continues. I would say that will happen seasonally and in some seasons like we will see a mix which would be better, although like as a Company, we are focused to increase our revenue and the product mix to get better margins.

Akshay Kothari: In India which branch do we sell, can you just name them?

Pallab Banerjee: The names that I mentioned, most of these are in India that means for U.S. market, we do Kohl's, we do Gap, Tommy Hilfiger. We do in markets of Australia, we do Target, Kmart, Big W. For UK, we do Next, Primark and other brands same for even Japan we do Muji, so this it's a mix of brands, it's like we try to service these brands or these companies from multi-location and for multi-product. So, that's the strategy that we work on, its not a particular set of brands only for a certain particular set of country, that's not our strategy.

Akshay Kothari: Currently 55% comes from woven and 45 from knit. So, what was this share, 5 years back, if you can give a sense of that?

Pallab Banerjee: So, traditionally woven has more, during the pandemic period, we saw that the knit demand was more and we enhanced our capacity for knit products as well. But I think this 55:45 is a ratio is the capacity that we have the readiness for. Now, depending on what is in demand. So, you see like for Pearl, we go to the customer as a multi-product vendor or supplier. So, depending on the need, we can flex us. A certain percentage of our factories can do both the product and can switch the lines. So, that's the kind of technological advancement that we spoke about, in our first speech is that. So, those are some of the strategies and I would say innovation that we are working towards.

Akshay Kothari: And knit is of course, higher margin business, right.

Pallab Banerjee: No, not necessarily.

Akshay Kothari: And you mentioned that around 70% of the revenues comes from India and Bangladesh, whereas our capacity in India is around 28% and in Bangladesh 45%. So, our capacity utilization in India is significantly higher in Bangladesh or our product mix is better in India manufacturing?

Pallab Banerjee: So, one the capacity the number of factories that we have, and where we can ramp up to that 80 million to 82 million without very significant CAPEX. So, that is the capacity that when we speak about capacity. And depending on the product and depending on the need of the customers, we do product. So, India basically like we are very strong in a women's products, in the lighter weight fabrics, that means the shirting fabrics, both for women's and men's and kids. And we do a lot of knit jersey products also in India.

In Bangladesh, the trend has been more towards heavier weight of fabrics, that means denim, the pant weights, the heavy drills and twills, those kinds of fabrics capacities more in Bangladesh.

Now, from customer point of view, these are the bulk of the buys. So, that is why India and Bangladesh we do have about 70% of our capacity, and 70% of our turnover is coming from.

Now, if I go for a particular product mix, like during the pandemic period, we saw a decline in the bottoms wear, that means the pants and denim were selling less. Now, as the pandemic is coming to an end and the markets are opening up, that demand for pants and people are going out to the offices and outside, so, pants and denims are going up.

So, that kind of variation, season to season will continue. But in majority, in a big picture like if you talk of Pearl, we are poised to deliver multiple products to the customers, and we come to the strategy so that our capacity utilization is optimum for both the countries. So, we won't say that on one season India would be slow or Bangladesh will be for more and Bangladesh will slow down and India will go up. It is not like that. So, we know what is the capacity, how to go to the customers, what kind of designs they need. But yes, general trend, the macro trend, as I spoke about the denim and pants were low during the pandemic, now that is coming back. So, those kinds of changes, you will see.

Moderator: Thank you. We will take our next question from the line of Vignesh Iyer from Sequent Investments. Please go ahead.

Vignesh Iyer: I just wanted to know, considering we are at 65% capacity utilization so, we can fairly say that FY'23 would be taken care of without any need for CAPEX as such. So, I just wanted to know, are we planning to utilize the cash flow to pay off some of our debt, because we have got around like Rs. 500 crores debt. And what is the level that the management is looking into which they feel comfortable, having in balance sheet.

Sanjay Gandhi: So, just to answer your question on the debt and cash part, I think the first thing you talk about the capacity, right. So, I think the FY'23 capacity existing one is sufficient to take care of the revenue growth what we are looking at it so there is no need for any CAPEX to build, any major CAPEX.

There will always be a maintenance or some additional expansion will keep on happening, some laundry machine to be added, some kind of a specialized machine, technology has to be added. So, those things will keep on continuing, but not the major one, like any Greenfield or Brownfield acquisitions really to add on the capacity. That's the first part.

The second part, you mentioned about the debt component. So, if we really look at our debt, composition of our debt, in terms of the long term & the short term. The long term debt is as we speak is Rs. 115 crore only, and the rest is all about the short term capital, which is a self liquidating by itself because it's largely represented by the current assets of the company. So, that is in line with the growth of the company, if you see the 95% growth in this quarter and overall, if you see FY'21 to FY'22, also we saw a significant growth and that's where the short term debt has gone high.

Now, having the cash and bank balance it only helps the Company which is growing like ours, it always provide an optionality of really looking at various opportunity which can come across, whether it's value buying or it is the need for working capital for any good opportunity in terms of the business expansion, in terms of the volume growth in the current set of scheme. So, we do not have any plan of retiring any debt from the cash and bank balances which we have as of as of now, in our balance sheet, it is to bring more optionality and also it gives us financial resilience to really meet our customer requirements well on time in any situation.

So, given the context of long term and short-term composition where the long term is only Rs. 115 crore at a group level. We don't feel any need of retiring those debts as of now.

Vignesh Iyer: Have we frontloaded any inventory as such, because working capital looks quite large as such, as in the working capital debt when it comes to?

Sanjay Gandhi: No, no working capital, see it's always as a percentage of if you really look at it number of days, if you see net working capital days compared to FY21 to FY'22. It has actually come down, it has not increased. though the reduction is only by three to five days, but still it is a reduction. So, as such, there is no inventory pileup, which has happened in anticipation of the order, because in our case we procure the fabric only when there is backed with a firm order from the customer. So, whatever the inventory is there, it is likely to be shipped in the coming 90 to 120 days time period. So, hedging is very clearly monitored in that sense. So, all the inventory as a percentage wise has actually improved only compared to last financial years, so, that's where we are.

Moderator: Thank you. We will take our next question from the line of Pulkit Singhal from Dalmus Capital Management. Please go ahead.

Pulkit Singhal: If you could just help explain the last two quarters, Q1 of this year and 4Q I mean, you had high revenues in both the quarter. So, capacity utilization will be similar in fact higher previously. But the margin difference is quite huge. I mean, the previous quarter was 4.4, this time it's 7.9. So, what could be the reason for such volatility between two neighboring quarters?

Sanjay Gandhi: One of the reason what we have seen is that I think Mr. Banerjee mentioned that in terms of the product mix, which we have in overseas countries like Vietnam, the outerwear, therefore, the price realization has been a pretty good, improved. So, there is a good amount of the product mix, which has changed in Vietnam, which has really led to higher FOB and then resulting into higher margin. That's the major one contributor.

The second is the style which were manufactured in Quarter 4 vis-à-vis what got shipped in Quarter 1, normally, we don't make a comparison from Quarter 4 to Quarter 1 because Quarter 4 is only summer-spring, but to really address that question, because some of the product as we mentioned, I think in the last quarter also in some of the discussion, that those partnerships factories, were actually starting the first phase of production. So, initially it was very important to ensure that the ramp up of the production lines is there, so, that, the workers get used to producing those many number of pieces. So, initially the pieces which were produced were on a lower margin side, rather than the higher margin, that's about India.

And in Bangladesh also, if you really see from Quarter 4 perspective, I think the product mix have slightly changed and the efficiency has also come in the volume which has shift on the new factory has really gone up, which has resulted in operating efficiency really kicking in. And this is precisely our whole thinking was there in last time when we presented that, in going forward, I think all this factors is likely to play out and will definitely help the Company in improving the margins.

Pulkit Singhal: Second question is, Mr. Banerjee if you could just one of the questions which is on everyone's mind is honestly how deep is the U.S. issue, I mean, it is just one or two quarters kind of impact or will it be longer? So, if you could throw some news on that.

And secondly, in that context of those issues, I mean, how is Pearl placed? Can we see this quarterly performance that you have showed in 1st Quarter, can that be suddenly impacted in another quarter by lower revenue and similarly, very low margin or do you think you have been able to do, kind of mitigate that significantly by alternate sourcingif you can touch upon that?

Pallab Banerjee: So, as I just mentioned, in U.S. market the big customers that we have like the Kohl's, Macy's, the PVH. So, they are projecting at this point of time a drop in numbers anywhere between 10% to 30%. So, at the same time, like our focus is to grow the other markets, so, that we do not get impacted completely due to this drop that is coming in. So, that is point number one that we are working upon.

And the other benefit as I mentioned is that thankfully, Pearl has got the option of multiple countries. So, the need of the product and the diversification of our production base, like for example, Bangladesh has got duty advantage for the European market already or like the FTA that we are talking about, which we are definitely talking to our customers and asking them to build up the base from now. So, those are some of the mitigation strategies that we are working upon.

And this particular drop, what I see is for the next two quarters. So, Q2 orderbook is already there with us. Q3 is also now almost like confirmed or getting confirmed at this point of time. So, we see a slight dip, but you see we had the huge tailwind of utilizing more of a capacity increasing with the new customers and establishing ourselves with the old ones. So, that momentum is continuing. So, if we talk about year-over-year, definitely the base has grown, the number growth will be there, but yes, what we would have expected if the market had been normal then we would be less than that. We would have gone into a much bigger number if the market had continued to be like what it was.

Pulkit Singhal: Just to clarify, so obviously on revenue front you say there might be a slight dip, depending in Q3 or Q4, but from a margin standpoint, do you see a risk to your margin from what you have just delivered or that part you can mitigate through --?

Pallab Banerjee: So, in terms of margin also, like what Sanjay just mentioned, the challenges that we had or like of the new facilities or the new, whether our in-house facilities in Bangladesh or some of the partnership factories, like as we start a new production lines and all the first few months or quarters definitely it is slow and then it picks up, the efficiency level goes up. So, as Pearl, our endeavor would be to continue to grow on those efficiencies, and thus deliver you a better EBITDA or a PAT. So, that's something, the journey that we have undertaken and you will see that continuity.

Moderator: Thank you. We will take our next question from the line of Mohit Khanna from Banyan Capital. Please go ahead.

Mohit Khanna: I just wanted to understand a little bit more what's happening on the U.S. side of the business. You said that you already have the Quarter 3 bookings, so just talking a little bit more on that. So, is it something that you are seeing in terms of rates that are coming down? Or there's a simple volume hit by the retailers?

Pallab Banerjee: So, yes the volumes are coming down. In terms of rate, what happens is certain portion is market driven. If like the big players like Walmart or a Target or some of the other big players drops in number then certainly market has got more capacity and less orders. So, during that time, definitely the price becomes more competitive. But thankfully, in our industry, normally the selling cost has got a proportionality to the raw material price. So, the customers normally don't expect us to absorb the increase in raw metal price.

And again, the second part is that when the demand becomes a little softer, even the raw material prices also comes down. So, we don't expect that just to survive, or just to have the capacity feel like we have to really take a huge hit on our margins. Some, definitely it would be when you are trying to place most of your capacity and maybe a little bit more competitive to ensure that, but I don't see a major change or major fluctuation in that.

Mohit Khanna: And when you say that these retailers are clogged up with inventory flux so to say, can you pinpoint any categories where you see the inventory a little bit more than the others? I mean the winter wear or the summer wear or maybe in the kids or the women's section?

Pallab Banerjee: See historically, if we look at U.S. market in 2021 what was happening was definitely the pent-up demand was high and people were going into the shops and most of the goods were delayed, at that point of time to reach the store, Most of the retailers went into a holiday season of U.S., which is one of the largest seasons with about 50%, 60%, 70% of the inventory in stock. So, that means almost 30% to 50% of the goods had not reached them at that point of time when they went on sale for the holiday season.

So, those goods were received by them in the month of January, February and even in March. Holiday season is supposed to be October, November and December. And by March, definitely it is spring, and the goods for a holiday and spring is very different. So, most of the U.S. retailers preserved those goods and they are bringing those goods in this particular holiday, they plan to bring in this particular holiday season.

So, that's one impact that we saw that the demand started slowing down. And then the cascading effect happens in the spring season as well. So, those are the two seasons which we are seeing majorly this correction would need to happen. From the summer onwards, I think they should be able to plan better and most probably they would be exhausting this the stocks which is lying there. So, if you talk of today, the U.S. market, there are very high markdowns and most of the retailers to liquidate most of these inventory, because for a retailer to have so much of inventory is also killing isn't it.

So, that's what is undergoing at this point of time. August is an important month, because this is back to school for them and it's a big season again for the U.S. retailers. So, let's see how this particular month goes and we shouldn't be able to this is the month where they should be able to liquidate most of their spring summer inventory that they have.

Mohit Khanna: Any categories in this let’s say?

Pallab Banerjee: Category wise if you need to get into detail then during the pandemic and immediate post pandemic was there was a huge demand in athleisure product that was those heavy knits and all, a lot of these brands have been bought, which then immediately they had to cut down. So, they have asked us to reduce as much as possible, hold some inventory for them, some numbers, smaller numbers, but yes, from this year to next year. So, those kind of things they have requested and those decisions are on.

On the other hand, the product which I just mentioned in earlier part of the call is that the bottom or denim, which was not selling much because most of the work was happening on video calls and all, where the tops were more important than the pants and denims. So, those kinds of goods definitely we saw an uptick in the in the demand and which is still continuing.

Moderator: Thank you. Our next question is from the line of Shubham Jain from Revanta Funds Management. Please go ahead.

Shubham Jain: I had one simple question taking on from the earlier participants on the quarter-on-quarter movement of margins. You mentioned that the outerwear contribution was a little higher this quarter. So, on an H2 and H1 basis, will the margins again start moving downwards because H2 will start serving the summer-spring and the outwear will be lower so have higher revenues in the second half. But our margins can be a little subdued?

Pallab Banerjee: This is where a company like Pearl is able to make a balance because on one hand we have the outerwear production that we majorly undertake in Vietnam, Indonesia and some in Bangladesh and which is very much in this particular quarters is heavy, because now all the goods are getting shipped for the holiday season. And then comes the spring summer product which is majorly coming out a lot of fashion goes out of India and some out of Bangladesh and Indonesia as well which comes because of our presence in all the four locations so we are able to balance that. And going forward we are more confident that we have the right customer mix and the right product mix we should be able to balance it better. So, that's the opportunity that that Pearl has been working on for many years and now those factories are able to churn out these expectations. So, you will see that like you know one season like when the winter season the foreign holiday imagines like which would be coming out of from the outerwear and spring summer it will be coming out from the other products like the fashion tops, dresses, the bands. So, that's the fluctuation that we can absorb.

Shubham Jain: To frame it in a different way, right, what I am trying to understand is essentially, we have done an 8% margin this quarter, and there's an improvement of 400 bps more or less at gross margin level quarter-on-quarter, which has helped us improve our margins. So, in the second half, when we will do a summer-spring kind of collection, can we still expect to do this 8% kind of margin or it will still be lower?

Pallab Banerjee: As I mentioned, the Vietnam acquisition had happened about four to five years back, so which has played. So, that's why this particular H1 numbers used to be affected earlier, because the non-existence of the Vietnam profit that was there. So, if that has come up, so that doesn't mean that we should lose out on the benefits that we already had in the second half, where like our India Fashions and Bangladesh Fashions would continue to give us that margin.

Shubham Jain: So, you believe it will sustain in the second half?

Pallab Banerjee: Yes, as of now, we are on that path. As I mentioned like the risk is definitely like if the war happens, or another that kind of big, I would say macro changes, if it doesn't happen than we are on our path.

Shubham Jain: My second question is just an accounting question. In our segments that we report there is another piece which is around Rs. 130 to Rs. 140 crores of revenue, but the profit is quite volatile. So, what gets accounted for over there, because we did like Rs. 4 crores of loss in the 1st Quarter 22 and the 4th Quarter 22, but this quarter, we have reported a Rs. 12 to Rs. 13 crores profit at an EBIT level.

Sanjay Gandhi: Actually, the segmental part of others it include our overseas company like Vietnam and there are certain standalone also get combined here. So, actually speaking, our segmental, there is a line item for inter-company elimination. So, if you look at the structure of our transaction probably the segmental will not give the clear picture unless we do the inter-company elimination and reach a final number there. Currently, the regulation requires us to put in this way, but if you really look at it, because most of our sales from the Bangladesh and Vietnam, Indonesia is billed through Hong Kong entity and that's why the other category will have certain portion of the sale which is being routed directly. So, it does not really reflect in that way the segmentation allocation in terms of the profitability unless we do the inter-company elimination.

Moderator: Thank you. Ladies and gentleman, we will take our last question from the line of Nirmal Shah from Seraphic Management. Please go ahead.

Nirmal Shah: Just I had two questions, just to summarize what you mentioned during your opening comments, is it fair to assume that Bangladesh, Vietnam and Indonesia, from a margin seasonality point of view, the first half would be at peak and probably second half would be at a little bit lesser than what you show in the first half; while the India operations would achieve its peak margins in the second half of the financial year, is it fair to assume?

Pallab Banerjee: See that's the trend of the industry, like when I was explaining to, I think Mr. Jain earlier was that if you talk of the seasonality of the market, then these markets are poised to do this kind of product. Now, as a company, our endeavor would be to go for better margins, better product with better customers, independent of the season or the location. So, yes, like what you are talking about are the general setup of the industry and the countries. And of course, then we come in where we have to work and we have to build up our strategies so that we can deliver the best on all the four quarters.

Nirmal Shah: Just follow up to that, like when we will enter the second half of current year where it's probably the cotton basket would be significant from our overall spring summer collection. And if at all the various forecasts, what they are talking about some 40% to 60%, sort of a drop in cotton price. If at all that scenario plays out, then, despite let's say you retain the similar volumes, can there be an impact on the top-line? And if that happens, how will your profitability overall look like, if the cotton prices really fall through once the cotton arrival start coming from the month of October?

Pallab Banerjee: So, Mr. Shah, what happens in the apparel product when these big retailers are sourcing from us so they do a lot of nominated fabrics and they do a lot of negotiation along with the vendors. So, that is why a direct impact of cotton, major impact doesn't come or should not come. Whereas, if you talk of a spinner or a textile fabric manufacturer, maybe I think more in the spinner's case like it definitely would affect more, my guess I am not an expert on that. But generally for apparel manufacturer, our negotiation is to pass on the raw material prices fluctuation to the retailers and at most we have to absorb it for one season that means the order has been placed and by the time that we are looking at raw materials if there is a fluctuation, which is normally a very small percentage, or should be low percentage.

Moderator: Thank you, ladies and gentlemen, due to time constraints, that was the last question. I now hand over the floor back to the management for closing comments.

Sanjay Gandhi: Thank you everyone. I hope we have been able to answer all your questions satisfactorily. However should you need any further clarification or would like to know more about the company, please feel free to contact our team or SGA our Investor Relations advisor. Thank you once again for taking the time to join us on the call.

Moderator: Thank you. On behalf of Pearl Global Industries Limited that concludes this conference. Thank you for joining us and you may now disconnect your lines.