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Subject: Transcript of Investors' Conference Call for Sheela Foam Limited-Q2 FY 2022-23
Financial Results.

Dear Sir/Madam,

Please find below the transcript of Investors' conference call organized on November 08, 2022 post declaration of Financial Results for quarter and half year ended 30th September 2022 for your information and records.

Thanking you.

Yours faithfully,
For Sheela Foam Limited

(Md. Iquebal Ahmad)
Company Secretary and Compliance Officer

SHEELA FOAM LTD.

#14, Sleepwell Tower , Sector 135, Noida- 201301

Ph: Int-91(0)-120-4162200 • Fax: Int-91-(0)-120-4162282, 4162283 • Email: contactus@sheelafoam.com
Regd. Office: 604 Ashadeep, 9 Hailey Road, New Delhi-110001, India • Ph: Int-91(0)-11-22026875-76

Toll Free: 1800 103 6664 • www.sleepwellproducts.com • www.sheelafoam.com

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“Sheela Foam Limited
Q2 FY 23 Earnings Conference Call”
November 08, 2022



MANAGEMENT: **MR. RAHUL GAUTAM – MANAGING DIRECTOR – SHEELA FOAM LIMITED**
MR. RAKESH CHAHAR – WHOLE TIME DIRECTOR – SHEELA FOAM LIMITED
MR. TUSHAAR GAUTAM – WHOLE TIME DIRECTOR AND CHIEF EXECUTIVE OFFICER – INDIA BUSINESS – SHEELA FOAM LIMITED
MR. DAVINDER AHUJA – GROUP FINANCE CONTROLLER – SHEELA FOAM LIMITED

MODERATOR: **MR. KARAN BHUWANIA – ICICI SECURITIES**

Moderator: Ladies and gentlemen, good day, and welcome to the Q2 FY '23 Earnings Conference Call of Sheela Foam 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 star and then zero on your touchtone phone. Please note that this conference is being recorded.

I now hand the conference over to Mr. Karan Bhuwania from ICICI Securities. Thank you, and over to you, sir.

Karan Bhuwania:

Good evening, everyone. It's our pleasure at ICICI to host Sheela Foam's earnings conference call. From the management today, we have Mr. Rahul Gautam, Managing Director; Mr. Rakesh Chahar, Whole-Time Director; Mr. Tushaar Gautam, Whole-Time Director and CEO of India Business; Mr. Nikhil Datye, Group Chief Financial Officer and Mr. Davinder Ahuja, Group Finance Controller.

I'll now hand over the call to Mr. Rahul Gautam for his opening remarks. Thank you. Over to you, sir.

Rahul Gautam:

Thank you, Karan. Thank you, thanks a lot. As usual, we will begin with our vision statement. Our vision, we will continue to be recognized as a leading organization in quality comfort products while practicing values of integrity, reliability, proactivity and transparency to do business with a smile for customer delight and their commitment to society. Thank you, thank you very much.

So thank you, Karan, once again for hosting this call on behalf of ICICI Securities, and a very good afternoon to everyone joining us today and wish you all a very happy Gurpurab. It is my pleasure to welcome you all to the earnings conference call for the second quarter and first half of the financial year 2023.

I just wanted to say something upfront as far as participation is concerned. So Mr. Nikhil Datye is today unwell and is not able to attend the conference. However, at the same time, I also want to add that he was originally from Mumbai, but he's in the process of transferring and changing, and there were personal difficulties in getting admission for children, etcetera. So he is unable to continue with Sheela Foam. And with effect from early part of December, we will then put the process on to get a replacement.

Let me first take you through the quarterly and half yearly financial highlights and then discuss some of the operational and industry highlights. For the second quarter under review, on a consolidated basis, we reported a revenue of high INR 722 crores, which were down by about 8% on a year-on-year basis and about 1% on a quarter-to-quarter basis. EBITDA margins for the quarter were reported at 10.84% which was an improvement versus previous quarter but still down against the same period in the previous financial year. Net profit stood at INR 54 crores, which was down by about 30% or so on a quarter-to-quarter basis.

First, to talk about the raw material scenario. Both are basic chemicals, which is polyol and TDI have been experiencing a little bit of a downward trend. Polyol prices continued their consistent movement downwards, while TDI prices also cooled off and then have been fluctuating thereof.

This has definitely resulted in an improvement in the gross margins across various geographies that we update on.

Uncertainty still looms large, though clear indications of the volatility settling down are on the horizon. The year-on-year decline in revenues were primarily due to softer demand in our India and European business, while Australia continued to perform well. For India, we have registered a growth of 15% in the H1. And Australia, as I said, has been doing well, while Spain whatever has been happening in the European continent due to the Ukrainian war has been experiencing a downward consumption and therefore, a downward production.

In India, the revival in consumption patterns is slow due to the inflationary pressures seen across consumer durable companies. The global economies do continue to face headwinds due to certain geopolitical situations and high inflation. The rising interest rates across the globe to fight inflationary pressures are weighing in on the economic activities and consumption patterns.

Similar to last quarter, the auto industry continued to do well for us in India, resulting in good volume and revenue growth in our technical foam products on a year-on-year basis and quarter-on-quarter basis.

Although this quarter, the mattress segment, furniture foam products and comfort foam products witnessed some decline year-on-year on basis. Decline in consolidated EBITDA margins are primarily due to the increase in sales and marketing expenses by 37% year-on-year and 24% quarter-on-quarter.

For the first half of the financial year 2023, consolidated revenues stood at INR 1,451 crores, reflecting a growth of 9% with EBITDA margins at 9.94% and a net profit of INR 96 crores.

I must share with you that in our recently concluded Board meeting, just a few hours back, the Board has approved a 1:1 bonus on the existing shares. So I think this should bring some shares to the investor community. Also, the Board discussed in detail the dividend policy, which will be -- which is being fine-tuned, and we will be ready as and when the time comes.

In conclusion, despite the macro challenges, we believe that the inflationary environment is slowly cooling off. And with our revised efforts in sales and marketing and the extra expenditures that we have done there we believe that the financial revival is around the corner.

We can now open the floor for the question-and-answer session. Thank you very much. Over to you, Karan.

Moderator: Thank you very much. The first question is from the line of Ritesh Shah from Investec. Please go ahead.

Ritesh Shah: A couple of questions. First on cash flow, second on manufacturing and third, more to do with the revenues, fees that we are looking at. So first on M&A or cash flow, I think prior to conference call, so we had indicated that could be looking at a few acquisitions on the timeline,

which was cited was October end. If you could provide some color over there on what we could be looking at, any numbers that would help. That's the first question.

The second question is on third-party manufacturing. I understand that we have started this at a top of places in India. If you could please highlight the rationale behind this? What is the product -- so I think I understand Starlite is one of the products, which will be under third-party manufacturing. So more of rationale and some numbers over here. That's the second question.

And the third question is into four parts. So one is exports hasn't really come out from the Nandigram facility. I think [inaudible 0:09:30] problem of most of it, that seems to be pulling off. Any numbers over here will be useful.

Second is any feedback on the e-commerce side. Last quarter, you indicated that we have launched Sleepwell, how is it effective if adding in the marketplace. So that's the second part of the third question.

Third is, Indian railways, any numbers over here, any updates and fourth is timelines on Jabalpur expansion along the launch for our mattress for every Indian?

Rahul Gautam:

That's a lot of questions. So let me first begin with the first question that you have asked regarding acquisitions. You see we don't do this day in and day out. And what we are experiencing that these things always take a little longer time than what you think they should when you especially go down and for details. I would only say that a couple of them is -- have progressed well. They are close to the final run. However, giving any more details on that will be a little out of place at this point of time. On the third-party manufacturing, I presume that you are talking about outsourcing manufacturing of Starlite. Is that correct?

Ritesh Shah:

That's right.

Rahul Gautam:

So we are doing that on a standard basis. And I think there are two units who do that for us. And the products, however, are completed there, and they come to our place for the final quality inspection and then we are going ahead with that. However, let me just say that we continue to have some flexibility on that in the sense that if the markets are down and or the volumetric productions are less, then we do that more of that in-house and lesser from outside. So there is flexibility on it. There was a question on the Indian railways. So...

Ritesh Shah:

Sorry to interrupt. Sir, can I just ask you for the rationale for this particular outsourcing or third-party manufacturing. Is it purely lead time? Or is that we are looking to improve the ROCE, working capital? How should one understand it, sir?

Rakesh Chahar:

I'll take that. I think the rationale for that is very simple. It's a very low value item. We are anyway sourcing bulk of the core and fabric materials for that. Whenever we have capacity constraints in Nagole facility, it makes sense to outsource it as a finished product and bring it into our warehouses and then distribute onwards rather than putting up any fresh capital investment and things like that for a product like this. But like Rahul ji said, during the year with

seasonality, it's volume of outsourcing moves up and down depending on how much free capacity we have ourselves.

Rahul Gautam:

Okay. So before I let Rakesh take the railways question, I just want to update you on the Jabalpur project that is a mattress for every Indian. Last time and even the time before that, I had shared with you that there was some delay in the supply of equipment from England on account of steel, etcetera, which was actually available only from a Ukrainian plant. However, all that has been kind of sorted out. And the machine is on its production. We should begin to receiving parts of it by the end of this year. And I am sure that by the -- in the first half of next year or the middle of next year is when the production will start.

The civil facilities and the infrastructures are all complete and some of the ancillary equipment, etcetera, is already in place or getting in place. We are looking at possibilities where we can manufacture before the machine arrives. If we can manufacture some small quantities of the grade and the quality that we want, so that the project can probably start a bit earlier. And while being on that project may add that the front-end work is also in full swing, which is the products, the markets, the way of distribution, etcetera.

Now just I request Rakesh to update us on the railways a bit, please.

Rakesh Chahar:

So railways is progressing well. The material has got very well established now. So whatever kind of opposition specifications, so the existing material lobby, so that all seem to kind of getting settled down. And so we are now getting to a good run rate monthly, and it's progressing well.

Ritesh Shah:

So wouldn't it be possible for you to give some numbers or some titling into what all regional divisions that we're already supplying to, what's the opportunity size?

Rakesh Chahar:

So we are supplying to seat and board manufacturers who in turn supply to the coach factory. So the current run rate is close to -- we started doing about 200 coaches or 250 coaches a month, which is growing month-by-month. In terms of revenue, it will be about INR 4 crores to INR 5 crores a month, that's our current run rate that we are doing.

Ritesh Shah:

And sir, two more questions pending. One was on exports. And secondly was on e-commerce, feedback on Sleepwell.

Rahul Gautam:

Tushaar, do you want to take one on the export?

Tushaar Gautam:

Yes. So Ritesh, the export side is like we discussed last time, was primarily struggling on account of extremely high freight charges from India. Those have eased off in the last quarter. They have normalized. The other thing that's normalized is, because of the slowdown in the US market, sort of our customers had stuck inventories, which they had already imported. All of that's kind of eased off. And from first week of October or so, we are starting to see our existing customers buy more and more, and those orders have started coming in. So this quarter should be a good quarter for exports. And that ramp-up that we had planned for should actually start to accelerate now.

- Rahul Gautam:** And Rakesh can you just respond to the e-com position, please?
- Rakesh Chahar:** So Sleepwell is introduced on the both the platforms, Amazon and Flipkart in late September. So the response in October was very encouraging both on the marketplace and also on our website. So now we are ramping that up, and we also will be running our campaign for promotion of the three SKU that we've introduced. And this is actually an omnichannel. I mean these projects are -- can also be booked from the offline channel. So I think it is settling down, but the initial response has been quite encouraging at the price point that we have positioned it.
- Moderator:** Thank you. The next question is from the line of Nihal Jham from Nuvama. Please go ahead.
- Nihal Jham:** Sir, couple of questions from my side. First, you did highlight that the current environment remains a little impacted, specifically on the mattress side, but if I were to just ask you that at least the activity from a lot of the other D2C brands in the mattress space has started getting very aggressive. Would you believe that there could be any impact from that specifically happening and that also being added to you in -- to the overall consumer sentiment?
- Rahul Gautam:** Nihal, I'm just going to repeat the question so that I have understood well. You are referring the competition activity in the market, which is heightened at this time. And the question is that is it going to make any big impact as far as Sheela Foam is concerned. Is that correct?
- Nihal Jham:** Yes. And I was specifically referring to a lot of the direct-to-consumer mattress brands that have come up over the last three years, I would assume at least four or five of them. So is that a bigger reason than maybe the overall slowdown would just say, impacting the performance across the offline mattress industry? Not just say specifically to Sleepwell, Starlite or Sheela Foam?
- Rahul Gautam:** Rakesh, why don't you take this?
- Rakesh Chahar:** Yes. So I think you're referring to the e-comm brands which have been aggressive. So yes, it has an impact on offline in two ways. One is, there is a consumer who is now looking at the price at the offering and he is also looking at the same kind of bargain in the offline, which is not easy to get because dealer also has to make his money. So that is one disruption which does impact the offline.
- And second is, I think it's -- because it's still a small market growing at a faster rate than offline, about 25%, 30%. So but it is still in the realm of 1,200 about maybe 6%, 7% of the total market. So I would say that, yes, it is an upcoming channel, which is getting evolved. But the impact on offline is more a new channel, having its own ways of servicing customers, offers, COD, 100 free nights. So those are the things which the retailers are not kind of equipped to handle, but the brands are, I mean, more-and-more brands are kind of working with the retailers to bridge that gap. So, but I would not attribute it only to the e-comm, I think it is more to do with the environment with the consumer sentiment.
- Rahul Gautam:** And Rakesh, if I may add to this, that all this heightened activity that is there, to my mind, it's only expanding the organized mattress market, which derives its source from the unorganized sector, which is an extremely large sector. Therefore, my take on this is that all this activity is

helpful. And the other little comment that I would want to say because we are also present strongly in the e-commerce market. That e-commerce business, as it stands today, it's not a very profitable business here. I mean eventually, people will have to figure out ways to exist there. That is by margins or reducing discounts, etcetera. But otherwise, it's not a sustainable business.

So just these two points. One, or whatever activity is going, whatever rupees are going into advertisements and talking points, etcetera, and the noise, it's creating good for the business, not so good for the companies who are doing this.

Nihal Jham: Understood. And just to follow-up on that would be that from our side, we have SleepX as a brand, which is purely online, and we have limited SKUs Sleepwell which you have recently got on Amazon and Flipkart. That is the way we are approaching this channel. That could be a right understanding?

Rakesh Chahar: That is correct. And also ensuring that there is some sanity in this wild thing, which is going on now where the brand has an opportunity to grow where you still make some money out of it, etcetera, and give your larger market of offline enough foundation and enough strong fleet to stay strong.

Nihal Jham: This is helpful. One last question would be that given the recent correction in raw material that we've seen, how do we plan to use this benefit? Do we plan to reduce our prices? I know you've highlighted about sport in sales and marketing, but would there be pricing action on our products if raw material stays lower?

Rahul Gautam: Sorry, I didn't hear that clearly, but you are talking about reduction of prices, are you?

Nihal Jham: Yes. So given that we've seen a correction in the raw material prices, and I'm assuming that sustained, would we reduce the prices of our products?

Rahul Gautam: Generally, we don't do that. In fact, when the prices are to be increased, we also do not exactly comments rates with the increase of raw material that has happened, because the market is being structured in a way cannot take these wild fluctuations as the raw material people do. Therefore, we have increased prudently, we generally do not reduce the prices. If an offering needs to be tweaked up, we will do that. If some other thing, additional thing needs to be given with a mattress, we will do that. But price reduction is not the order of the day.

Moderator: Thank you. The next question is from the line of Sohini Andani from SBI Mutual Funds. Please go ahead.

Sohini Andani: I just wanted a little more understanding on the increase in sales and marketing expenses that we've seen both year-on-year and quarter-on-quarter. And also the fact that our mattresses sales have actually declined during this period. So if you could just explain on what areas have we spent this and the dichotomy a bit in terms of actual mattresses sales being lower. So it would be good if you could explain this in some detail?

- Rahul Gautam:** Yes. All right. I think Tushaar will do that, which is, I think, primarily your question is increase in the sales and marketing expense, while the number of mattresses have declined. So there's I think both are following a different curve. Tushaar, can you just explain that?
- Tushaar Gautam** The way that we are looking at that is from a baseline, let's say, of H1 last year or even quarter 2 last year, which were very-very unusual. There was, Q1 was virtually a dead quarter and a lot of these, especially the marketing side of it and even some trade promotions and channels and all of that was in there. Over a period of 12 months, it's certainly come back to what the normalized level used to be two years or three years ago. That's on the sales side. So what is really extra is marketing expense. And that's something that we are focusing on getting the brand more visible, also investing in some of these newer channels where we are starting to expand the Sleepwell brand like the e-comm side has come now. But there are a couple of other developments like this that are ongoing of special channels, special businesses in which we intend to expand the Sleepwell brand. So there are some marketing investments that are related to that, which has gone up or which have been front loaded at the moment.
- Moderator:** Thank you. The next question is from the line of Resham Jain from DSP Investment Managers. Please go ahead.
- Resham Jain:** So I have a few questions. So first one is on the, in the past, when we didn't had Starlite and Feather Foam or rather the high-value products where the mix was higher, I think the larger contribution is to come from the marriage-related buying patterns. Obviously, last two years, those events got postponed and stuff like that. But what we are hearing now is that the upcoming marriage season seems to be quite strong, and that is another way you used to market in the past. So any comments around this specifically on the marriage-led demand of your products?
- Rahul Gautam:** So I would say, yes, wedding time continues to be a strong time for us to market or to sell. And this time, what are the dates, Rakesh, that the wedding, they have started yesterday or on to 4th, right through up to 19th of December, I think, is it?
- Rakesh Chahar:** 13th of December.
- Rahul Gautam:** So this is a strong season, and you can always fill the feel in the air that mattresses are being sold more. But definitely, this is a strong time and we should have.
- Rakesh Chahar:** I think it's a phenomenon more in North, which is related to marriage. It has a very little impact on the other zones. But not for sure, I mean the impact is large.
- Rahul Gautam:** Yes, because I think the other zones, they marry whenever they want. So for sure, the point that you're making, Resham, is strong. This is a good time, and you would see good sales at this time.
- Resham Jain:** Okay. This should improve the mix as right? The price points?
- Rahul Gautam:** Yes.

Resham Jain:

Sir, the second part is, I think on the digital spend because, as you mentioned, e-commerce is where the competition is. And I could see that in terms of Google searches and also earlier, whenever we use to type Sleepwell, the competing brand is to come at the top. I think that has changed a little bit, but not fully. So how much spend has to happen on this site to be relevant? Because with the aggression on the e-commerce side, the relevant spend also has to happen, which is unlike a traditional company where the economics are quite different. Some of the competing brands are, okay, not earning money. So how will you approach this whole competition in this regard?

Rakesh Chahar:

So generally, I hope, I'll take that question. You're absolutely correct. And like you're saying, you're starting to see some green shoots there, which is primarily on account of, I would say, 1.5 months of extra spend and extra work on the digital platform, not just Amazon, Flipkart, but on Google, Google Search, Facebook, YouTube, all of that stuff. More and more as we move along, we will focus primarily on television and digital. That's where the breakup of the brand spend will be.

And a lot of the traditional spends are slowly ramping down. And those resources are getting transitioned into digital. That's one side of the efficiency. On the other side, just to give you an example, in September and October, we would have resourced the digital spend at least 7x to 8x of what we normally do in a month. And I don't see that slowing down. So as we move along, you will see more-and-more of that.

Resham Jain:

Can I ask one more? Just to understand on the e-commerce side, the SleepX and Sleepwell now both will be present online. So from a differentiation standpoint and marketing, because marketing there is a limited budget in terms of how you want to position your brand and spend. So how will you now do because earlier you used to do more from SleepX perspective, but now you have to do for Sleepwell as well. So how should one think about this?

Tushaar Gautam:

So I think, just think about it in a way that we started SleepX a couple of years ago when all of these other brands who were coming in, looking at the model, looking at the conflict between online and offline, we thought it's better to do it with a separate brand. Of course, it's grown. It's competing with the other e-comm players, and it continues to compete.

The long-term play, the sustainable play is for Sleepwell to be present in that channel and take a larger share of it, which we started about a couple of months ago, like Rakeshji said, good first indication. It's a product and a model which we worked very hard to develop an omni-channel experience where I can compete on an Amazon, Flipkart, website and compete with all of these other new e-comm brands, but at the same time, a consumer can also access the same product, the same offer at the same time at any of my retail outlets.

So from our perspective, we think the Sleepwell brand getting access to this new channel, which is, let's say, about 6%, 7% of the overall market is the sustainable way to progress. And therefore, the resource allocation of marketing will be more-and-more towards people.

Rahul Gautam: And if I'll just add to that, that number one, Sleepwell is the brand, is our flagship brand. That's a sustainable one, and that's what we would be working on. This is a new territory, new unknown territory and therefore, all the exploration, all the initial experience, etcetera, was done using SleepX and not to sort of fool around with the Sleepwell brand. Now that we are learning the trade, we are learning the processes, it would be more and modestly for sure.

Moderator: [Operator Instructions]. The next question is from the line of Chetan Shah from Jeet Capital. Please go ahead.

Chetan Shah: Sorry, I'm just looking at your company for the first time. So my question may be a little novice. Just wanted to understand our geographical growth opportunity. So I have kind of historical data, but how do you see the things moving in the next two years to three years time horizon? How do you see the opportunity size and scale? One is that question. And second is are we looking at any complementary businesses apart from mattresses what we sell as of now, as an opportunity to give a kind of a bit of product to the customer who walks into our store or buy our products?

Rahul Gautam: I'm just repeating the first question, so that, again, we've understood it properly. You are saying that how is the geographical growth going to be in the next two years to three years? And that geography of India we are talking about. Is that correct?

Chetan Shah: That's right, sir. One is India, and how do we see the global opportunity also. If you can share some form of opportunity in that? Yes.

Rahul Gautam: So our philosophy or our thinking on this is clear that when we look outside of India, we look at an opportunity, which is on the operations side, manufacturing side, where all the experience of sourcing of raw materials, formulating the products and manufacturing them on the best possible equipment with the best possible technology, that is what we excel in, and that is what we will look at outside. So whether the current ones also, which is Australia and Spain, we limit ourselves to manufacturing the best possible foam and the best variety and giving it to the customers.

When it comes to going beyond that, that is the consumer, the distribution and the consumer and the customer, that is where we look at India, and that is how we are structured and integrated here, because we understand the culture, we understand the ethos, we understand the consumer outside, we don't do that, and therefore, we don't. So just to simply put it, consumer business, India, just manufacturing of foam and excellence in foaming and foaming processes outside India as well as outside India.

Coming back to the question of geographical growth. Undoubtedly, we are strong in the northern part, the western part. We're getting stronger on the southern part. We may be a little weak on the eastern part. But eastern markets are also relatively small compared to the other ones. It's completely the way that the country is. If you look at it, it's an inverted triangle and then you have the rivers flowing and that's where the people live, and that's how what we call as the northern part of it.

So though we are strong, but where we are strong, the opportunity is also larger and because the opportunity comes from the unorganized part of it. The other places, we may not be that strong, but we have the processes in place to get stronger to get to the position where the brand has similar kind of dominance as we have in the northern and western part of it. And therefore, the growth to me, my mind will come all over the country, different places for different reasons.

The second question that you had on the complementary business. We do things like pillows, we do bed sheets, we do comforters, we do bed sets and anything which goes on top of the bed. They are doing it, and this is going into the stores. And in times to come, we'll act as extra attraction for the consumer when he or she comes into the store.

However, beyond that, the only other category, which is somewhat related, both in terms of consumption of foam as well as in terms of the way that the markets are structured that you generally have furniture and mattresses or bedroom beds and mattresses, and they are generally kind of sold together. So it's very fragmented. It's very, the varieties and the SKUs and all that are phenomenal. However, we have a play on this, and we have some programs. At this point, I'll only say that we have some programs, I may not be in a position to discuss them any further.

Chetan Shah:

Yes. Just one a broad last question from my side. In terms of while answering one of my previous question, you kind of alluded about technical capability and also manufacturing excellence. Could you also give us some sense on, because historically, if you see a decade back also, people were not very choosy or a selective about the form in which they sleep or they sit or they're using their furniture.

But now that awareness has kind of improved. So how do you see this change of consumer mindset, which has evolved can help you and you also want to take advantage of that with your maybe R&D capability or technical capability and give a better product at a better price point. Any thought on a broader sense will be very helpful. That's it from my side, sir, and I wish you all the best.

Moderator:

The next question is from the line of Resha Mehta from Green Edge. Please go ahead.

Resha Mehta:

Again, fairly new to the company. So the first question, again, is on the e-commerce channel. So if you could just comment on how big is this channel for mattresses in India, and also, what would be our market share? And would Feather Foam and Starlite be also available on the e-comm channel? So that's the first question.

Rakesh Chahar:

Tushaar, would you answer that? It is there, how big is the e-comm channel? What's our share on it?

Tushaar Gautam:

The overall mattress market would be approximately INR 15,000 crores to INR 16,000 crores for the consumer. E-comm this year projected is approximately anywhere between INR 1,000 crores to INR 1,200 crores. And we should finish the year at about 10% market share. On your second question, Feather Foam, Starlite will not be available now.

- Resha Mehta:** So what will be, is the positioning of, or rather what is the difference in the positioning of Starlite and Feather Foam brands? Because I believe both are sold through MBOs, are in the price range of INR 5,000 to INR 20,000 if I'm not wrong?
- Tushaar Gautam:** Starlite is lower. Starlite is a lower-end brand, and that's only anywhere from INR 4,000 to INR 8,000, INR 9,000. Feather Foam is the little more premium larger offering brand from INR 5,000 to INR 20,000, that's it or now a little higher as well.
- Resha Mehta:** And out of the total mattresses in your revenue, how much would be coming from Starlite and Feather foam?
- Tushaar Gautam:** About 10%.
- Resha Mehta:** And on the export front, if you could just give a general sense on that after China seeded this place, which are the major countries that are exporting to US and EU. And would our exports be branded or white labeled and just the margins and working capital here?
- Rakesh Chahar:** Yes. So exports generally from the China Plus One piece, what's really happened in the export of mattresses to the US is step 1. There were antidumping duties and resistance to buy from China, primarily the Chinese mattress exporters shifted shop to Vietnam, Indonesia and places like that, even some in Eastern Europe and things like that. Those have all got covered under the antidumping regime of the US.
- And therefore, India is still in a good position to export. That was primarily our play there. In the interim, two things that are negative has happened. One was the escalation in transport costs. So container freights from India, which were normally \$3,000, \$4,000 went up to \$18,000, \$20,000 in the last 12, 18 months, and they've now come back to normal.
- The other thing that happened was consumable demand in the US really dropping and a lot of inventory stuck in the system and all of that. So all that's kind of one. That's why we are starting to see good traction from customers for supply of white label mattresses into the US. That's starting to happen for the last 45 days a year. The only other thing, sorry, did I answer all your questions?
- Resha Mehta:** Yes. So margins and working capital here. And also, what we sell is essentially white labeled mattresses, right?
- Rakesh Chahar:** That's correct.
- Resha Mehta:** And the margins and working capital here and also, India is not seeing any antidumping duties?
- Rakesh Chahar:** Well, not yet. Not yet. And let's hope not always. So that's why we kind of hedged that US supply by also supplying product out of our Spanish entity with the assumption that a European Union country coming under antidumping from the US will be a very-very tougher. Even if India gets covered, we have the capability to service customers from space.

- Resha Mehta:** And working capital and margins here?
- Rakesh Chahar:** So working capital, we are generally very conservative on, and payment terms are at best 20 days or so from dispatch at best.
- Resha Mehta:** And lastly, on the rural distribution plan, if you can elaborate on this? And also, I think it was mentioned that we may enter the furniture segment. So any progress there?
- Rakesh Chahar:** So I'll park the furniture question maybe for three months down the line. Like Rahulji said, we're not in a position to respond to that at the moment. On the rural side of things, Rahulji has already commented on the capital expenditure in Jabalpur with this intent and the status of that. What we are doing parallelly is to really do the product development, the distribution development, the brand development in a small piloted territory, so that all of that is good to go by the time the facility is up and running, which is probably anywhere from nine to 10 months away. That's generally the outlook on that.
- Resha Mehta:** Right. And if I can squeeze in one more. What would be our revenues from metros, Tier 1, Tier 2, Tier 3, rural currently, like, let's say, on an annualized FY '22 basis?
- Rakesh Chahar:** So I'd say metro Tier 1 is about 70% and Tier 2, Tier 3 would be about 30%. The rural will be virtually zero. I mean, so if I look at my retail outlets and their sales, that's what I'm telling you right now, there would be consumer behavior of rural consumers coming to the closest big town and buying some Sleepwell products from an existing retail outlet, that's standard consumer behavior for all big purchases in rural, and that would be happening even now.
- Moderator:** Thank you. [Operator Instructions]. Next question is from the line of Pankaj Tibrewal from Kotak Mutual Fund. Please go ahead. Sorry to interrupt Mr. Tibrewal, we cannot hear you, sir. You are sounding very low, sir.
- Pankaj Tibrewal:** Yes. So my first question is that though we have seen improvement in gross margins on a consol basis, but that has not slowed down to the EBITDA and the PAT. And finally, what you explained is the marketing overheads, which you have done. As you move into the second half, maybe comfort you can give us on the margin expansion from an overall profitability and PAT margins. That's one question.
- The second is that the observation is that Spain has seen a very sharp gross margin expansion. Any one-off there because in a rising in a bad environment where revenues have gone down, we have seen a very sharp expansion on margins in Spain. And that has led to overall company gross margin also kind of improving. And the last one is that cash flows have been weak in terms of generation. Can you help us understand how do you intend to improve the cash flow as you move into the second?
- Rahul Gautam:** Thank you, Pankaj. Thanks a lot. Tushaar, will you take the first one on the H2, I mean, to give some comfort without giving all the details.

Tushaar Gautam: I think on two fronts. One, I would just say the quarter two results that have been released right now are also distorted from July, August, September perspective, September being extremely good on the margin front. The average, of course, is what has been released. What that means is that the September P&L or the margin issue of September is going to continue or we're seeing it continue in October, November, coupled with better mix and higher sales on account of quarter three season, marriage season, Sleepwell products selling more than -- or having more of a ratio in overall sales, etcetera.

So just reiterating that point. So September was better than August. August was better than July in terms of margins and we see that is continuing. And of course, the extra sales and the better product mix for quarter three. So that should be maintainable and comfortable. What's the second question?

Pankaj Tibrewal: The second question was on Spain.

Tushaar Gautam: Spain, Pankaj ji, I think something very strange is going on. Yes, the market is depressed, raw material is short. But prices of raw materials are still a bit higher than India or significantly higher. But because there is a shortage of raw materials, we are able to maintain our margins, we're able to pick our customers, we're able to hold on to prices and maintain our margins in Europe.

I'd say Europe is going through something which is very unusual, and we have stability probably after this winter, that's what everyone in Europe is waiting to see how the winter progresses, how is the European Union able to sustain itself with the energy issues and things like that. However, I'd say for us, what we have said is, yes, there is a drop on existing customers and existing markets.

But because we are only 1% of an overall extremely large market, there are still opportunities for us to grow. We were constrained a little bit by availability of raw material, but those supply chains we have changed over to Asia now. And now that we have enough raw material, we have started to go out after growth. And I don't think there should be any limitations to growing that business, irrespective of what's really happening in the overall market. That is on Spain. On the cash front...

Rahul Gautam: Cash flows, I think, primarily, Pankaj ji, it's because of lower sales and -- or Davinder, why don't you answer that?

Davinder Ahuja: Yes. So there is sales and there are certain expenses which have gone up this time which resulted into lower cash from operations. Besides that, there are also working capital requirement in the market, where we have extended certain credits, which is well tend to lower operating cash flows.

Rahul Gautam: So I think it's just lower sales and an extended credit, which is brought out. But the credit is temporary and very secured.

- Pankaj Tibrewal:** And just last one, Spain has seen abnormal increase in gross margin from 22%, 23% to 31%. Do you see the situation where in the second half, India does much better, recoup all our gross margin losses, Australia continues to be steady, but Spain again sees a setback on gross margins and then the overall control margins again. Is that a probability? Or you think Spain can sustain the margins as the situation is today?
- Rahul Gautam:** So I think the 20-odd percent that you were talking about, that was the unsteady point. I mean that was the bottom point that was there, that is when the raw materials were violently fluctuating around. But actually it's slowly kind of steadying down -- slowly kind of -- even if the Ukraine war continues, that people are finding ways, whether it's getting the raw material from the Asian region or importing elsewhere doesn't and manufactured out of here, etcetera.
- So I think the 20-odd percent, 22% versus the low one it will go up. I think it should be steady between 35 and 40. And as far as India is concerned, we are also experiencing the raw material kind of reduction, which is there. So I see that the margins are going to be much higher than where we are, in the coming times here.
- Moderator:** The next question is from the line of Resham Jain from DSP Investment Managers.
- Resham Jain:** Sir, just on the export side, as you mentioned, things are looking up now. So how much time do you think it will take to ramp up the export facility, which we have set up? And what could be the optimal throughput from this plant?
- Rakesh Chahar:** The facility is up and running completely. Just to keep it when the export side was a bit slow, just to keep it going we put some of our interim products through this. I mean it's ready to respond to any demand that comes from the export side. So there are no issues on ramping up the facility at all.
- Resham Jain:** No, my question was to ramp up the whole facility to, let's say, 80% to 100%, how much time will it take? Do you think it will take three months, six months, one year? And once it reaches that level, how much throughput can come from this plant additionally?
- Rakesh Chahar:** You're talking about the demand side then, right?
- Resham Jain:** Yes. On the export because that plant is dedicated for exports. So I was just thinking from that plant perspective because those kind of products can be manufactured only from that particular plant?
- Rakesh Chahar:** Approximately from the customer order side, approximately five to six months to ramp that up to full capacity. And at that point in time, it should be doing close to five containers a day.
- Resham Jain:** In terms of revenue sales, because containers doesn't -- we will not be able to understand what will be the revenue potential?
- Rakesh Chahar:** Roughly about between INR 1 crores to INR 1.5 crores a day.

- Moderator:** The next question is from the line of Ritesh Shah from Investec.
- Ritesh Shah:** Sir, just wanted your views on the distribution side. Most of the online-only players in the marketplace, they are also now looking at omnichannel and looking to aggressively add stores. I think based on the recent checks we did find out that we have been appointing new MBOs as well and also basically putting some accountability in the system, I think we didn't have any targets for EVOs and MBOs over the last two years to three years, probably it could then, go back for COVID. So sir, I just wanted to have your sense on distribution. Also, if you could give numbers on how many Shoppes, Galleries and World we have right now? Yes.
- Rahul Gautam:** So Rakesh, would you take that question that the total number of Worlds, Galleries and Shoppes. And the question is, that because of the COVID times, etcetera, there were no incentives for those people. So are you thinking anything in that direction?
- Rakesh Chahar:** Yes. So as far as the showroom format, which we call them World and Gallery, they are 1,500 plus. The Shoppes are about 2,200, and rest would be the exclusive dealers. And they also, the network has been also growing, like just to give you a sense, since April, we have added about 100 showrooms in the first half.
- As far as the sales targets are concerned, how we are approaching EBO is a little different. We are focusing on improving the productivity inside the store, which is the conversion, the ASP and the attach ratio. So we have a program which is wherein we have deputed people to help retailers to get on to these metrics and start with the baseline and then start improving on the conversion on the ASP. And because that's where we believe the sale is going to come from the same store. So that's the EBO part of it. I hope I have answered your questions.
- Ritesh Shah:** Yes. And on the MBO side, I think we were not very aggressive on adding MBOs, that is something which has probably changed over the last six months. Also, I think on the incentives on how we are actually incentivizing the guy to actually also put to Sleepwell into the shop to make the sale happen actually?
- Rakesh Chahar:** So we have started a new network. We are calling it a cushioning partner. And so we've started this program in this year from end May between June, right? So we have created about 1,500 such people who have some products of Sleepwell and a complete range of Feather Foam. So here, the belief is to instead of approaching thousands of MBOs to focus on this set of we have the plan to go up to 2,000 dealers in this year and focus on them and push them towards its usability.
- So that's what our plan is with this network. And MBO, since we also deal in comfort foam and Starlite, so that is the less for MBO where, I mean, there is a team which is working on that, both on the comfort foam and Starlite MBO. But there also, we are growing not by the number but to deal with maybe 1,000 MBOs and get better extraction out of them. Because our learning in past has been that though we were able to appoint many MBOs because they all wanted some connection with K12 and Sheela Foam, but the extraction was very poor. We were spending far more energy and time in visiting those dealers and not getting enough business. So there's a

change in that outlook that we've -- I mean we are approaching more for extraction now as the MBO business is.

Ritesh Shah: Sir, this is very useful. Just one follow-up. Sir, what is the end result that we are looking at? Do we have any metric when we are looking at revenues for EBO or MBO?

Rakesh Chahar: What we are looking is that we need to expand our EBO network. Currently, it stands at 5,000-plus what I, this new network that we're developing another 2,000, 7,000. So we want to expand it to about 10,000 in the next two years, which would be having a retail footprint of 20%-plus.

Moderator: Thank you. Ladies and gentlemen, this was the last question for today. I would now like to hand the conference over to the management for closing comments.

Rahul Gautam: Thank you. Thanks a lot, and thank you, everyone, for participating and actually making some positive suggestions for us to take home. As usual, it was a great learning exercise for all of us. I hope we've been able to answer your questions satisfactorily. And if you do have any further questions or would like to know more about the company or it's working, please reach out to our investment relationship managers at Valorem Advisors.

I want to conclude today with this note, that whatever recently reports that I have been reading from all authorities, whether it's the World Bank or IMF or Morgan Stanley, etcetera, I think the whole world believes that India is a country of the decade or is going to be the country of the decade with at least a 6% to 7% growth. And soon, recently, of course, we have become the 5th largest but soon, we would become the third largest, which is a good feeling to have and a good hope to have. So thank you very much once again, especially that today was a holiday and that all of you turned up and we could have this meaningful interactions.

With those words, I'd just say good night and sleep well.

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