Pokarna Limited

Date: 16TH August,2023

BSE Limited, **Phiroze Jeebhoy Towers,** **Dalal Street, Fort** **Mumbai – 400 001** **Scrip Code: 532486**	**National Stock Exchange of India Ltd.,** **Exchange Plaza, C-1, Block G,** **Bandra Kurla Complex, Bandra (E)** **Mumbai- 400 051** **Symbol: POKARNA**

Dear Sir/Madam,

Earnings Call Transcripts

Pursuant to Regulation 46(2)(oa) of the SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015, as amended, the transcript of the audio call recording of the Company's Analyst Call held on 10th August, 2023, on the Unaudited Financial Results (Standalone and Consolidated) of the Company for the quarter ended 30th June 2023, is attached herewith.

The transcript of recording can also be accessed on the Company's website using the following link:

https://www.pokarna.com/wp-content/uploads/2023/08/CDC2720230810148720.mp3

This is for your information and records.

Thanking You,

Yours Faithfully,
For and on behalf of Pokarna Limited

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Digitally signed by DISHA JINDAL
Date: 2023.08.16 13:02:40 +05'30'

Disha Jindal
Company Secretary and Compliance officer

Pokarna Limited
Q1 FY '24 Earnings Conference Call
August 10, 2023

Moderator: Ladies and gentlemen, good day, and welcome to Pokarna Limited's Q1 FY '24 Earnings Call.

Please note that this conference is being recorded.

I now hand the conference over to Mr. Gavin Desa from CDR India. Thank you, and over to you, sir.

Gavin Desa: Thank you, Aman. Good day, everyone, and a warm welcome to Pokarna Limited's Q1 FY '24 Earnings Conference Call. We have with us today Mr. Gautam Chand Jain, the Chairman and Managing Director; Mr. Paras Jain, Chief Executive Officer at Pokarna Engineered Stone; and Mr. Vishwanatha Reddy, the CFO.

Before we begin, I would like to mention that some of the statements made in today's discussions may be forward-looking in nature and may involve risks and uncertainties. I now invite Mr. Paras Jain to open the proceedings and share perspectives and performance and outlook. Over to you, Paras.

Paras Jain: Thank you, Gavin. Good day to all of you and thank you for joining us for this call. I won't go over the numbers as they are already in your hands, but I'd like to provide some insights into the current landscape of the engineered stone industry. These insights will help contextualize our financial and operational performance.

The global environment remains challenging, especially for residential remodelling due to a slowdown in U.S. home sales and project delays. This challenge is compounded by heightened competition, particularly from manufacturers in India and Southeast Asia using Chinese technologies, impacting both demand and pricing. Also, our understanding indicates that channel excess inventories haven't fully depleted, suggesting that there might be more time before hitting the bottom. This insight encourages us to create cautiously, maintaining a balance between our efforts and exercising patience and foresight.

In this backdrop, as mentioned earlier, the present situation is so dynamic that offering near to mid-term forecast would be premature. Amidst these challenges, our primary focus is on improving efficiency, exploring new markets and expanding our distribution network. The quarter's robust gross and EBITDA margin reflect our efforts to enhance productivity and manage costs. Our goal, as previously mentioned, is to maintain EBITDA margins between 25% to 30%.

To address certain rumours, I want to clarify that we haven't encountered any client loss. In fact, our customer base has expanded previously compared to the previous financial year. In terms of diversification, we are pleased with the advancements in markets such as Canada, France, Mexico and Russia. We are also actively exploring opportunities in India. While these endeavours are still in their early stages, we hold optimism regarding their long-term potential.

Our priorities to effectively address current challenges and position ourselves to seize opportunities as the environment and demand stabilizes. An example of this proactive stance is our focus on developing alternative product formulation, meeting the demand for low, respirable crystalline silica products, which helps mitigate the risk of silicosis. This approach ensures we are prepared to meet evolving needs as and when they are needed for the market.

While the near to medium term remains uncertain, I have confidence in Pokarna's capabilities. Our design expertise, robust manufacturing infrastructure, strong customer base and relationships and expansion across certain other markets reinforce my confidence in our ability to perform and continue creating value through our quartz business.

With that said, we are now ready to address any questions you may have.

Moderator: The first question is from the line of VK Karthi keyan from Suyash Advisors.

Karthi keyan: Very, very impressive results in terms of profitability, but just wanted to understand, how much of that would have been driven by product mix, which you had spoken about elaborately last time around and cost reduction? And while you indicated 25% to 30% EBITDA margins, how much of that is general conservatism?

Paras Jain: Yes. So largely, what you see the benefit of margin improvement is coming from the new design introductions. And maybe some part of it, but not a large part of it, comes from the cost initiatives which we have undertaken at the moment.

Karthi keyan: Okay. Okay.

Paras Jain: And EBITDA, see, always we have maintained a range of 25%, 30% in the recent past. So while this is a conservative number, but considering the fact that the demand outlook is still to be stabilized, we will want to be a little more cautious, rather than more optimistic.

Karthi keyan: Fair. If I may ask you one question regarding share. So if Q4 volume was 100, what would have been the volume number in Q1, sir, on an indexed basis?

Paras Jain: So volume is typically more or less -- its range bound, so we don't see much coming because of the volumes out here in the Q1.

Karthi keyan: Correct. But I'm saying Q4 and Q1 were similar volume revenue numbers, but the profitability was substantially higher, and you said new design introduction...

Paras Jain: I cannot give you the absolute number for certain reasons. But I can tell you that whatever is coming is coming largely from the product mix, which is a high-priced designs.

Moderator: The next question is from the line of Sonaal Kohli from Bowhead India.

Sonaal Kohli: Congratulations on great improvement in your margins. So I had 4 questions, with your permission, may I ask them?

Paras Jain: Yes, go ahead.

Sonaal Kohli: So sir, firstly, the U.S. housing market has not revived in last 3, 4 months. So if you see the sales are same about 4 years ago, in the 3-week, 4-week period in absolute terms, and now the trend has been there for about 3, 4 months. But what lag would this impact your business? I understand there would be a lag in your business. So whatever slowdown happened 18 months back would be impacting you now. But what is a typical lag? A broad range would be very helpful in getting the context of what could happen in the company over, let's say, next 12 to 24 months.

My second question was regarding hospitality industry. We've read some reports about capex revival in hospitality industry in terms of renovations. So how much are we seeing this? And are we geared up to benefit from it? And what could be the context of the benefits, how historically those numbers were before the COVID period? The third question was we have taken several new initiatives which you started mentioning from December quarter onwards in terms of new geographies, new products, designs, but you also alluded that these are long-tail cycles because of the distribution and the pre-pack and the initial orders are small and always ramp up.

So what is the right time frame for you to say that whatever you've done so far, not the incremental asset, would fortify, if they have to fortify, would that be a 6-month period, would that be a 12-month period? The last question was that your Q3 margins were highest ever in history in terms of gross margins, your Q4 was the lowest. So was there any one-off in Q4? And can we say that we wouldn't see a Q4 kind of situation again because the margins are in ended very strongly?

Paras Jain: Yes, Sonaal. Thank you for the question. So typically, the U.S. housing, while the U.S. housing starts also have increased compared to what it was in the recent past, it typically takes 12 to 15 months for the demand actually to start picking up because the countertop is one of the last elements to be installed in the house. So we typically feel that if this trend continues what we are seeing in the last quarter, also for next couple of quarters as well, then I think by end of this financial year, probably the lag time should be more or less be done or maybe plus or minus 1 quarter is what I can say.

Coming to hospitality industry, yes, definitely, the inquiry funnel is increasing. And in good times, we had almost 10% volume of our business coming from this segment. And right now, that's not yet at that level, but definitely, things have improved than what this was in the last quarter. So if things go like this, I think definitely hospitality would be one of the segments where we can see a good demand picking up in the near future.

And typically, the new markets and the new product designs take anywhere between 12 to 18 months depending upon which market you are, and like in Russia, it can take a little more longer time because the shipping time, initial shipping time itself are typically quite longer than what it used to be for a place like France or a Mexico market.

So depending upon what products we are offering and which market we are going, anything, it takes 12 to 18 months for the relationships to stabilize, the products to start generating recurring demand and acceptance in the market, supply chain situation is getting completely addressed. So that's typically 12 to 18-month period is what we have seen on our historical experience.

Now coming to what you saw in Q3 was largely the case driven with the product mix, in which we believe that can be considered as a one-off event. And we don't think that type of situation would come very often in our business.

Sonaal Kohli: So you meant Q4 basically.

Paras Jain: Yes.

Sonaal Kohli: And sir, even in counter to what you just said, sir, you said that it takes certainly 12 to 18 months, but for the existing designs in the existing markets, such as U.S., would that also take 18 months? Or there, the period would be more like 9, 12 months?

Paras Jain: Basically, again, there are 2 aspects to this, why I say 12 to 18 months. It depends upon what channel the product is going. Suppose the channel -- if the product is going to a home improvement center, like let us say, our customer is offering to Home Depot, then the cycle is relatively lower because Home Depot has 1,900-plus stores. And sometimes, actually, the cycle is more because the customer is supposed to get the samples done at 1,900 stores before the demand start generating out of that store.

And vis-a-vis, if somebody who's just not carrying in the home improvement center, but maybe it is 30, 40 locations what they have across U.S., there, it typically has to just start unveiling the product and start going and replacing the product in this marketplace. So depending upon which channel the product is finally -- because ultimately, when we launch a product, we are not aware whether the customer of ours is taking the product to the home improvement market, home improvement centers or is it going directly through distributors. But sometimes we know, and those products, we think that if it is going through home improvement centers, typically take a little longer time compared to what is getting distributed directly.

Sonaal Kohli: Sir, my last thing on the hospitality side itself, what was the peak revenue share from hospitality? And considering relative weakness in the U.S. housing and boom in hospitality, is there a possibility that in next couple of years hospitality could be back to that peak level? You mentioned about 10% in pre-COVID, but my question was more about, during the good years or the best year, what has been a hospitality contribution to your revenues?

Paras Jain: The hospitality business, if it is really peaking out and reaching the good level, and especially with a lot of hotels postponing their renovation in the past for several reasons they're now going back to it. I think considering the capacity, product and the pricing needed for the hospitality segment, all those factors, anything around 10% to 15% typically could be the revenue which can be factored in, if all the metrics are properly met. And that typically, I think it would take anything between 1 year or 2 for it to happen.

Moderator: The next question is from the line of Ritik Chopra from Buoyant Capital.

Ritik Chopra: **Sir,** can you throw some light on the domestic demand?

Paras Jain: Yes. So basically, we've just started like -- as I was telling you in our previous calls, we started building up the market in the domestic by tapping into the kitchen and bath segment. Now we are realigning our strategy for India market because we see that the product demand and acceptance in the market also has grown substantially. So we are looking at building up new channels of distribution as well, both company-owned and even through different channel partners. So, demand is definitely good, but of course, it's going to take some time by the time the sales and marketing strategies are fully implemented.

Ritik Chopra: Sir, do we have any company-owned store right now?

Paras Jain: Right now, we do not have any company-owned stores at all. So around 110 stores, you can see our product, and all those are our dealers, basically, those who sell our products in different parts of the country, right, from Kochi to Dehradun.

Ritik Chopra: Okay. And sir, can you tell the capacity utilization?

Paras Jain: Yes, I think I have already -- we've already stated that in our presentation as well, if I'm not wrong, that the capacity utilization has been muted and has stood lower actually. I can't give you the number for certain reasons, but definitely, the capacity utilization, we have a good amount of capacity to utilize.

Moderator: The next question is from the line of Ajay Vora from Nuvama Asset Management.

Ajay Vora: So sir, just wanted to get a sense in terms of post the action taken by the U.S. authority against the competitors for the cartelization or whatever the allegations were. Have we started seeing any sort of benefit out of it? Or how is the U.S. market behaving post that action taken by the authorities?

Paras Jain: I think reaction is a little different from what you understood. So basically, there was an anti-dumping and a countervailing investigation which was launched against China first, and then India and Turkey. So today -- and of course, then subsequently, they had certain other transhipment related issues against next quarters out of Southeast Asia. So basically, quartz from India today is subject to antidumping duty, countervailing duty in the U.S.. So I don't think it has benefited anyway and -- any of the exporters out of India.

Ajay Vora: But I thought that the percentagewise was much higher for players from China, and therefore, we would have benefited in terms of pricing.

Paras Jain: Basically, by the time India subject got stabilized, COVID came in. And by the time COVID went out, the Chinese uprooted majority of their production lines and put this production line in Southeast Asia like Vietnam, Cambodia, Philippines, Malaysia, Indonesia. So all that also got out there. So India typically did not get any price advantage. Of course, India has got some volume advantage, which I think majority of the players, especially using the Chinese technology, did not take any advantage of and other started selling at very low prices.

Ajay Vora: Okay. Okay. And just lastly, say, over the next 3 years, where do you see the domestic revenue as a percentage of our total revenue? I know it's very small right now, but where do you see that over the next 3 to 5 years?

Paras Jain: We think India would definitely be 1 of the top 5 markets in terms of our volume in the next 5 years.

Ajay Vora: Can you just quantify the total volume; how much would that be?

Paras Jain: There is a certain reason because the ongoing proceedings and all, I cannot give the number, but I can tell you that it's going to be one of the focus markets.

Ajay Vora: Okay. And lastly, where do you see our debt levels moving over next 2, 3 years? So do you think that has peaked in terms of the capex and everything, and going forward, what is the plan to reduce that?

Paras Jain: Basically, as a growing company, we keep evaluating different capex opportunities coming to us. So I don't think that the -- we are like looking at the operating cash flow, what we have and the current debt position, I think we are nicely positioned in terms of like term loan about Rs.63 crore and promoters -- loans on promoters and advanced unsecured loans are around Rs.83 crore in Pokarna Engineered Stone. So I think -- and our annual obligations are around Rs.35 crore to Rs.40 crore completely.

So I think we are not risk averse to take more capex if need be, if we are really willing to help our business. At the same time, we're not going to be overboard because we have to keep everything in mind that what the demand for the product is, how the capacity utilizations are.

Moderator: The next question is from the line of Dixit Doshi from Whitestone Financial Advisors.

Dixit Doshi: Can you just mention the debt number again?

Paras Jain: Okay. That's the only question, or you have some more questions on...

Dixit Doshi: Yes. So other 2 questions, firstly, on the -- we are developing the alternative product formulation, so respirable crystalline silica product. So does this -- so is it that we have to make the raw material composition and it's more of an R&D thing? Or does it require the change in the -- our facilities as well? If you can elaborate slightly more on that. And one more question was on the -- you mentioned that the newer market takes typically 12 to 18 months for the reordering. But all those markets which you have mentioned, Russia, Canada, there, the first time delivery have we done over last couple of quarters?

Paras Jain: These are your 4 questions or are there any more?

Dixit Doshi: Yes. No, that's it.

Paras Jain: So if you look at -- I'm now giving the numbers, both Pokarna Engineered Stone Limited and Pokarna Limited, right? So term loan at -- consolidated term loan is around Rs.267 crore. And working capital, consolidated, is Rs 68 crore and unsecured loans from Promoter Group are Rs 98 crore. So this is our consolidated debt basically as of 30th June. That answers your first question.

Now coming to your second question on the alternative product formulation, which we spoke about. So basically, quartz engineered stone has crystalline silica, which is found in the quartz, what is used in the quartz. And in certain markets, there is a concern about respirable crystalline silica being generated when there is a dry cutting of the engineered store. So there is certain regulatory scrutiny which is happening in certain markets. So as a strategy to make sure that we are also ready should the situation arise, we've spent a lot of R&D time on developing alternative formulations, and we are ready with the product. Should the market start asking for it, we can quickly align ourselves. That's one part of it.

So whatever technology, what we're -- in R&D we have developed, ensures that we typically do not have to invest anything on upgrading our facilities as of now for producing this new formulation product. And new markets, what I told about Mexico, France, Canada, Russia, yes, the first shipments have been delivered to the respective customers out there.

Moderator: The next question is from the line of Devansh Nigotia from SIMPL.

Devansh Nigotia: Sir, your initial remarks on the gross margin. So if you look at over the long periods, our gross margins have structurally become lower. So some thoughts, if you can share on what is the mix between the premium products and the basic products of quartz? And overall, we do you expect this mix to be you with the next 2, 3 years?

Paras Jain: Currently, the new product mix on a quarter basis is what we reported was higher compared to what traditionally it has been. So as of now, it is still not at the level which we want it to be. So if one really looks at the historical margins, one would look at that 30%, 35% high-margin products around -- and another 30%, 35% were medium projects -- products, and then 20% around lower and then a mix of hospitality.

So I think if all those metrics are considered and, of course, the mix of 2 and 3CM as well, then typically, the numbers can be anywhere between -- if we're considering especially the current scenario of demand and raw material pricing and the pricing pressure, considering that you have low-cost technology products coming out from India and Southeast Asia, I think the healthy margins would be around 45% on the gross profit -- on the gross margin side of it. So I think the 60% margin level seems to be relatively difficult to attain. But I think 45% is the number of what we feel is the right number to look at.

Devansh Nigotia: Okay. And the build-up on the premium portfolio further because to utilize our capacity, who do you think we have to acquire market platform in U.S., will it be the locally from local producer of the U.S.? Or I mean which country we will be competing with?

Paras Jain: Typically, when we produce a product, largely, our competition comes from North America and Europe on the exotic high-end designs. But then the handcrafted products from Southeast Asia also have become some of the products where we compete with.

Moderator: The next question, a follow-up question from the line of Sonaal Kohli from Bowhead India.

Sonaal Kohli: Sir, 2 follow-up questions. Firstly, you referred to gross margins being 45%. I presume you're talking at a company level, including granite, you're not talking about the quartz segment only.

Paras Jain: Yes, I think I have to correct myself. I was referring to quartz.

Sonaal Kohli: You're referring to quartz segment?

Paras Jain: Yes.

Sonaal Kohli: Your lowest gross margin in history in any quarter has been 49% and this quarter was about 61%. And you said Q4 is not a replicate -- it won't be repeated, it was a one-off. And now you're seeing the gross margin of 45% in quartz. So can you please throw some light because it's not adding up.

Paras Jain: Just a second, because I think what we have reported seems to be around 42%. So I don't know from where...

Sonaal Kohli: Gross margin at quartz level.

Paras Jain: Yes.

Sonaal Kohli: What do you include when you say gross margin? Because every company internally may be using different terms than what the market will be using. Can you help us understand how do you define gross margins at the company level?

Paras Jain: Yes, let me just check with financing. So we've taken raw material and direct material costs and direct overheads.

Sonaal Kohli: Okay. So that's called contribution margin. So in stock market parlance whenever any analysts refers to gross margin what they're actually referring to is 100% minus raw material cost as a percentage of sales. So none of your direct costs, none of your other cost are included, only the raw material cost is included when people refer to gross margins? Just to clarify.

Paras Jain: Okay. Thank you for the input.

Sonaal Kohli: So basically, the current margin range should sustain, right? Or am I missing something? Whatever you report is, broadly speaking, sometimes up, sometimes down.

Paras Jain: I think except for last couple of quarters where there were a little ups and down. But I don't think that those type of scenarios would be reported, and I think that I have clarified before also on the call.

Sonaal Kohli: Okay. So current gross margin range should broadly sustain, a little bit here and there?

Paras Jain: Yes.

Sonaal Kohli: Got it, sir. And sir, is the pricing pressure for whatever little, is more on, as you said, on the entry side, the lower end side of the market, because Chinese firms cater to that and in your historical calls you referred that we don't compete with Chinese, strictly speaking. So can you give the context of the competition? So is the competition, at a broader level, and for us, lesser? Or we are increasing in equal amount of rate? And if so, why? Because we don't, strictly speaking, compete with Chinese and that is the stand of the company since ever.

Paras Jain: See, basically, the technology also has evolved over a period of time, what Chinese were doing 5 years and what today they are doing in different markets, whether it is Vietnam, Malaysia, Philippines, Cambodia, Thailand, has definitely evolved over a period of time. And they also produce products which compete with our products. So saying that we typically do not compete with Chinese anymore is probably an understatement. Actually, we do compete with Chinese. But of course, the type of products, what we are currently focusing, are completely different from what the market is offering at the moment.

So that's where we think that the temporary monopolies can be established for a time. So that's what our current strategy is basically to make sure that we have temporary monopolies which can help us to sustain the position, improve the position and then start working on something else which would be our next temporary monopoly.

Sonaal Kohli: So sir, this competition is more at that 35% of the market, which you referred to broadly speaking? Or it's up to 65% of the market with China as the larger competition?

Paras Jain: We see the competition across. See, basically, there are good companies out there who are able to produce product which is handcrafted and has certain other challenges, but then there is a market for those products as well. We see competition at every price bracket, but then differentiation is what is driving all these changes what we are seeing today in the marketplace on our revenue side of it.

Moderator: Thank you. Ladies and gentlemen, that would be our last question for today. And I'll hand the conference back to the management for their closing comments. Thank you, and over to you.

Paras Jain: Thank you so much and look forward to catching all the investors in the next conference call. Thank you. Thanks, everyone, for coordinating all.