“Kaya Limited Q3 FY-18 Earnings Conference Call Hosted by Ambit Capital”

February 07, 2018

MANAGEMENT: **MR. RAJIV NAIR – CEO, KAYA INDIA**
MR. DEBASHISH NEOGI – CEO, KAYA MIDDLE EAST
MR.NAVEEN DUGGAL – CFO, KAYA LIMITED

Moderator: Ladies and gentlemen, good day and welcome to Kaya Limited Q3 FY '18 Earnings Conference Call hosted by Ambit Capital. From the management, we have Mr. Rajiv Nair – CEO, Kaya India; Mr. Debashish Neogi – CEO, Kaya Middle East; and Mr. Naveen Duggal – Chief Financial Officer. As a reminder, all participant lines will be in the listen-only mode. And there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing * then 0 on your touchtone phone. Please note that this conference is being recorded.

I would now like to hand the conference over to Mr. Naveen Duggal from Kaya Limited. Thank you, and over to you, sir.

Naveen Duggal: Good evening, everybody. I welcome you all to the conference call on our company's behalf. Let me begin the conference call with a very short update on the third-quarter performance, which is already in public domain and uploaded on our website www.kaya.in. The Kaya group posted a consolidated revenue from operations of 100.3 crores for the quarter ending 31st December 2017, a growth of 3% over corresponding quarter ended 31st December 2016. Kaya India's net revenue grew by 8% and Kaya Middle East revenue has de-grown by 1%.

Consolidated EBITDA is 1.4 crores, which is 1% of revenue as compared to an EBITDA loss of Rs. 9.1 crores that is (-9%) of revenue in Q3 FY17. Profit after tax for the quarter ended December 31, 2017 is (-3.9) crores, compared to (-10.7) crores for the corresponding quarter last year. Overall in India, Kaya has 103 clinics, 151 outlets and operates 24

Reg. Office: 23/C, Mahal Industrial Estate, Maha kali Caves Road, Near Paper box Lane, Andheri (East), Mumbai-400093
Email: investorrelations@kayaindia.net
CIN: L85190MH2003PLC139763

clinics in the Middle East. The detailed information update is filed with the stock exchanges and uploaded on our website.

I now open the session for questions, and my colleagues and I will be glad to answer them. Thank you.

Moderator: Thank you very much, sir. Ladies and gentlemen, we will now begin with the question-and-answer session. We will take the first question from the line of Sahil Jain from MoneyCurve Investments. Please go ahead.

Sahil Jain: Sir, I wanted to ask what is the cash balance do we have now because I remember the last time the cash balance was 106 crores and you did an acquisition of shares in the Middle East for 52 crores. So what is the cash balance now, sir?

Naveen Duggal: So the cash balance of Kaya India at the end of 31st December is 23 crores.

Sahil Jain: 23 crores, okay. So I mean for the Middle East, you've bought the shares from the Middle East, sir?

Naveen Duggal: Yes. The transaction for Middle East has already been completed.

Sahil Jain: Okay. And at what valuations have we done the Middle East buyback, sir**?**

Naveen Duggal: Basically, we have bought over 1% of the share capital or rather 0.99% of the share capital at a multiple of 6 times. The valuation of the firm has been done roughly at about Rs/ 890 crores.

Reg. Office: 23/C, Mahal Industrial Estate, Maha kali Caves Road, Near Paper box Lane, Andheri (East), Mumbai-400093
Email: investorrelations@kayaindia.net
CIN: L85190MH2003PLC139763

Sahil Jain: So 6 times of what, sir, multiplying with the other?

Naveen Duggal: No. So actually, if you read our FY '17 financials, there we have disclosed that an eligible employee of the company is eligible for 6% of the share capital as an ESOP. This ESOP scheme was changed in May -17 pursuant to a Dubai Municipal Regulations, instead of 6% of Authorized Capital the 2017, scheme provides for issue of 1% of the Authorized Capital, with an option to buy back shares issued upon, exercise of option at a multiple of 6 times of 1% basis fair value of the firm. So, essentially, both the schemes are same in terms of percentages.

Sahil Jain: I also had a follow-up question, sir. Of the 103 centers, sir, how many centers has actually breakeven and how many centers are still making losses, sir?

Naveen Duggal: Yes. So, basically as on quarter ending December 31, 2017, there are only three stores which are tracking a negative clinic level EBITDA out of 103 and they are also at an almost breakeven level. The losses are not significant.

Sahil Jain: Okay. Sir, it's a very rare question, but I was just trying to understand, what is your fixed cost? I understand most of your expenses are fixed cost, so, what percentage of your total expense is a fixed cost and what is the variable cost, sir if you can have a ballpark.

Naveen Duggal: If you look at it at a Kaya India level, at a COGS level, our variable cost is about 21%. And then we have an incentive scheme, which is another 6%. So the total variable cost would be somewhere around 30%.

Reg. Office: 23/C, Mahal Industrial Estate, Maha kali Caves Road, Near Paper box Lane, Andheri (East), Mumbai-400093
Email: investorrelations@kayaindia.net
CIN: L85190MH2003PLC139763

Sahil Jain: On Kaya Middle East level, sir?

Naveen Duggal: Kaya Middle East also would be at the same level.

Moderator: Thank you. We take the next question from the line of Ishit Sheth from Anvil Wealth. Please go ahead.

Ishit Sheth: Sir, a couple of questions basically. This is for sir, Rajiv Nair. Sir, if you see the last 10 quarters for Kaya India, I think revenue has almost remained flat for the last 10 years. I mean, you can put into slow economic environment in India. But how do you see this playing on because what we see is that revenue is almost flat, you've done a great job its the cost at almost the same level over the last 10 quarters despite inflation, which comes into these costs, which is pretty good, but then there is no revenue traction that we are seeing in Kaya India? So I'd like some comments on that.

Rajiv Nair: For the first three quarters, overall, net revenue has grown by 8% for the business. And the real measure of performance in our business is consumption of services leading to Net Revenue growth. So for the last three quarters, overall, while we have grown 8% in net revenue terms, , collections in Q3 grew by 13%.

Ishit Sheth: Correct. But sir, then the net revenue which has grown and also coming off of low base of last year which was the demonetization quarter.

Rajiv Nair: No, the revenue number is based on consumption, demonetization didn't impact consumption. The collection which is basically the advances we get for these services got impacted. So during the demonetization period also last year, maybe collections would have

Reg. Office: 23/C, Mahal Industrial Estate, Maha kali Caves Road, Near Paper box Lane, Andheri (East), Mumbai-400093
Email: investorrelations@kayaindia.net
CIN: L85190MH2003PLC139763

dropped but consumption actually continues because you have already paid for most of the services. You only either pay a part of that value during that period or you have already paid and you're consuming those services. So just to give you a sense of why our net revenue has been at an 8% growth - on an average basis, our consumption has grown by over 15% in the clinics in terms of number of sessions consumed by customers. Last year, November, December, we were tracking about 51,000, 52,000 sessions, on an average and till the second quarter FY18, we were at 55,750 sessions, which actually went up to almost 57,000 sessions in the month of December. So what has actually happened is that the number of repeat walk in's of a consumer to consume services have actually gone up by 15%. Of course, the net revenue translation out of that consumption is based on the services that the customer actually takes. So to give an example, in November-December, we've actually tracked higher consumption on high-ticket doctor-led services which is basically the anti-ageing services, which is also a good sign because that's where the specialization of the business actually comes in. I had mentioned this in our previous calls as well that our sole objective is to grow the stagnant net revenue number. Of course, we can do better than what we have done in the last quarter, that is better than 8% but that's the growth that we have actually got and I don't think there's a demonetization effect in that 8% at all.

Ishit Sheth: Sure. Sir, in that case my next question would be that, say, we are at about this level of close to 200 crores for the India business. Now, how do you see that scaling up over, say, next three to five years, I'm not asking you for quarter kind of a guidance, but over next three to five years because we've seen it almost stagnate at 200 cores over the last

Reg. Office: 23/C, Mahal Industrial Estate, Maha kali Caves Road, Near Paper box Lane, Andheri (East), Mumbai-400093
Email: investorrelations@kayaindia.net
CIN: L85190MH2003PLC139763

few years? We obviously had a lot of transitionary issues facing in the meanwhile. So how do you see that playing out because as we understand, it's a highly unorganized market, highly underpenetrated market? So what is it that is hindering our growth basically in the India business?

Rajiv Nair: Okay. So, don't want to look at two or three years out in this call today but I think the purpose is to highlight what we have done and what are the growth engines that we have put in place for us to grow further. So I'll give you an indication of what we have done. So in the last couple of quarters, in quite a few of our clinics in India, especially the older clinics where our average EBITDA is close to about 35%, 36%, we wanted to make some fresh investments, especially building capacities, in some cases relocating the clinics, and in some cases upgrading the facilities of the clinics. So we completed renovation of almost 14 clinics in the last nine months, out of which, barring maybe about 3 clinics out of 14, we've got double-digit growths in all the clinics. Our objective was that by the end of this financial year, we'll have the 20 clinics which account for almost 32% of our total turnover, fully renovated. So as we speak, about six clinics are under renovation today. Second, some of our older clinics had technology that was maybe 8-9 years old. Not necessarily obsolete technology, but at the same time the machines were procured about 9-10 years ago. Obviously, there are some improvements we can make there. Therefore, in the last quarter, we have invested about 20 new laser machines which will help democratize the service to a large number of customers. So that is something that we've done in the last quarter. So there are two areas -, one is pigmentation reduction, which is basically nothing but brightening or lightning, which is a big service

Reg. Office: 23/C, Mahal Industrial Estate, Maha kali Caves Road, Near Paper box Lane, Andheri (East), Mumbai-400093
Email: investorrelations@kayaindia.net
CIN: L85190MH2003PLC139763

in India; and second is laser hair removal, which is a big alternative to waxing, which is a large market in India, and one of our growth areas for the last three quarters at least.

Now, as we have brought in these machines, we have also democratized the pricing of these services to the consumer. So as an example, in the month of December, we actually reduced the price of laser hair free from as high as 89,000to a 69,000 price point. And we see double-digit growth in these category, which account for more than 25% of our turnover. So here's what we have done. One, we have upgraded several facilities. In some cases, relocating stores to be able to get better facilities and larger capacities, which also helps our consumption, adding more machines, which we have done and that's actually helped. Lastly, if you have observed, we have got a 30% growth in our product business. We have made some modifications to the way we convince our doctors to prescribe products in the clinic because otherwise, it is sold by the clinic operations team. We've seen a 30% growth in products overall, partly driven by clinics, and product sales outside of Kaya. So we have also built a business around modern trade, shop-in-shops and some amount of general trade. We've also started to enlist some distributors in the business for selling of products outside of Kaya. So already, as we speak, we have signed up and started to work with distributors in Bangalore. In Mumbai also, a distributor has been signed up. So at least, the top five or six geographies, we will be looking at product expansion outside the Kaya business as well. So that's the other thing. Third is, even now, hair is a very small business, about 5.5% of our total mix, and it has grown by about 22% in the last quarter. So that is an area that we want to focus. There are some high-

Reg. Office: 23/C, Mahal Industrial Estate, Maha kali Caves Road, Near Paper box Lane, Andheri (East), Mumbai-400093
Email: investorrelations@kayaindia.net
CIN: L85190MH2003PLC139763

level segments, like anti-ageing, for example, in the last quarter also showed a 15% growth, which was again our area. And we've discussed the fact that this is something that we want to drive as a business because there are specialties that are higher-end and niche. So at one end what we are trying to do is to attract younger consumers with better pricing. So we've made quite a lot of price modifications in the business. We are democratizing technology, so it's available in larger numbers to more customers across the country.

Last but not the least, we are also looking at the rationalization of some of these clinics. So we haven't taken decision as yet but we are analyzing it - we are doing a complete high performer, medium performer, low performer clinic analysis. And if there are we see any concerns in specific clinics, like Naveen mentioned just now there are about three clinics, which are negative in terms of EBITDA, we definitely will take some calls on those clinics.

Ishit Sheth: But in terms of India business at the operational level, say, we had an objective of probably breaking even this year at the operational level for the Kaya India business. So for us to do that, maybe say next year or be profitable, what kind of SSG do we require at this kind of overheads that we have today?

Rajiv Nair: Yes. So two things we need to do. One is also look at it from a margin line perspective, cost line perspective and the SSG growth that we need. Obviously, we need a little bit more than what we are doing today. So against an 8%, I would say double-digit growth, so maybe in 12%, 13% growth is what we would need to be able to get there. But more importantly, we are also working on the margin line. So if you

Reg. Office: 23/C, Mahal Industrial Estate, Maha kali Caves Road, Near Paper box Lane, Andheri (East), Mumbai-400093
Email: investorrelations@kayaindia.net
CIN: L85190MH2003PLC139763

look at it, our gross margins have actually increased from 76% to 78.4% for the year as of now. If you look at our employment cost lines, for example, the back office overhead cost has been minus 1% in this quarter. And even in the front-end while we have paid some increments for people, we have also looked at the productivity and also done some reallocation of staff and that's why the overall employment cost in the business has grown only 2%. The entire fixed overheads, which is the clinic operating expenses, has grown by just 1% over last year. So there are some cost line opportunities, there are some margin opportunities and definitely there are some top-line opportunities ahead of us.

Ishit Sheth: Sure. But are you confident that next year at least that we will see more in breakeven at Kaya India level because you are burning cash in the last four years?

Rajiv Nair: I would not like to give you a guidance at this time. I would like you to track us against the commitments that we've been making quarter-on-quarter. And I would like to highlight the changes that we've been able to make and the results we've got out of them. Let me call out some of these - So you can see the result in margin improvement, you can see the result in terms of net revenue growth and also in terms of customer repeats etc. In this quarter itself, we had a 7% growth in customer entry into the clinics. We had a 15% growth in terms of the consumption volume in the business. So I would say these are all important indicators of improvement in performance. On next year's guidance, I think it's a little early for me to do that.

Reg. Office: 23/C, Mahal Industrial Estate, Maha kali Caves Road, Near Paper box Lane, Andheri (East), Mumbai-400093
Email: investorrelations@kayaindia.net
CIN: L85190MH2003PLC139763

Moderator: Thank you. We take the next question from the line of Agam Shah from Raj Trading. Please go ahead.

Agam Shah: I had two questions. So basically, on the Middle East front. On the Middle East front, if I understand the last con-call which I had heard, so you were saying that there were some issues you're facing on that side and maybe you were saying that second half could be better. So can you show some guidelines on it like how we're seeing the business out there? And second question being so now, since they have breakeven on the EBITDA level in India operations, so how is it going ahead in the sense for the next few quarters going ahead?

Debashish Neogi: On Middle East, the last time we said that we are facing some headwinds from a macro perspective, and this is equally true for all the players in our industry and this is reflected in the GDP numbers of the GCC countries which was close to 3% and now the GDP as of last year was 0.7%. So we also faced this headwind and this is why our growth, which used to be in double-digits earlier, has come down. So we are working on getting back to growth and getting into new services. Because of some new services that we launched two months ago, we got the benefit of that in quarter three, which is why in quarter three, our performance from our EBITDA or our PAT perspective is better compared to the previous quarters, and especially with respect to the first two quarters of this year. Now going forward, I cannot give you guidance because there has been one more macro change, which will impact us in Middle East from a short-term perspective. In Middle East GCC, VAT has been introduced. So VAT is a consumption-based tax, which is the first of its kind in Middle East history. So that will have a

Reg. Office: 23/C, Mahal Industrial Estate, Maha kali Caves Road, Near Paper box Lane, Andheri (East), Mumbai-400093
Email: investorrelations@kayaindia.net
CIN: L85190MH2003PLC139763

negative rub-off for a few months, and post that, we are hopeful that we can get back to the growth that we used to deliver earlier. There are some additional changes at the macro level - crude oil prices have risen and that is a good change from a business perspective. Then there is Expo 2020, which will happen in Dubai. Also, the projections of GDP for the coming year is more than 2.5%. So, we are hopeful for next year, for the next two, three months, we will get impacted from the taxation change which is similar to what India would have experienced when GST was implemented. So, I cannot give you guidance, but obviously in the subsequent quarters, things will be better with respect to growth.

Agam Shah: So maybe after a year, let's say, for second half next year maybe things might be better in the Middle East?

Debashish Neogi: We hope so given where crude oil price is and also given that VAT implementation would be over by that time. We have a huge pipeline of innovation and this contributes to 15% plus for the overall business and with this pipeline, we are very hopeful that from a post six-month perspective, definitely we'll be much better.

Rajiv Nair: On the India question, I think we have improved on a few parameters with respect to the EBITDA at a corporate level. The evidence of that is the fact that while there is a loss, it's a reduction of about 50% over last year. This is a very important point. This same quarter last year, we had a 6 crores loss, now it's about 3 crores for this quarter. In last quarter also we had an 8% growth and this quarter also we had an 8% growth but because of the type of consumption that we did in this quarter, which is largely anti-ageing where the margins are a little low. Anti-

Reg. Office: 23/C, Mahal Industrial Estate, Maha kali Caves Road, Near Paper box Lane, Andheri (East), Mumbai-400093
Email: investorrelations@kayaindia.net
CIN: L85190MH2003PLC139763

ageing grew quite substantially in this quarter and that's why the percentage margin went down from 78% to about 76%, but that will come back to normal from this quarter onwards. So only the last quarter, which is November-December where we have some impact there. Cost line seems fairly under control. The gross margins over the last year have also grown. So we have seen a growth of almost about 10% in terms of cash margin, we've seen an 8% growth in terms of net revenue, and costs have been largely flat. The only investment that we made was a little extra in certain areas on the advertising line during this particular period, especially to promote certain specific cities. Otherwise, even corporate costs for the quarter are down 1% over last year. So, we are maintaining a tight control on cost. Definitely, there is scope to manage the cost line better and we can do a little better on the growth number as well. So the growth number can be better than what we have done as of now, but for that, we are actually doing this drive on consumption and you can see the evidence in terms of the number of sessions of consumption that we do in the business today, which is a 15% increase over last year.

Moderator: Thank you. We take the next question from the line of Hem Agarwal, an Individual Investor. Please go ahead.

Hem Agarwal: I have a couple of questions on the products business. Sir, I'd like to know what the product revenue is in terms of breakup of e-commerce and stores? And what are the margins in this products business? Is this profitable? And what is the product sales growth in e-commerce, in the same-store sales growth, you have mentioned a 30%, what is it in the e-commerce product sales growth?

Reg. Office: 23/C, Mahal Industrial Estate, Maha kali Caves Road, Near Paper box Lane, Andheri (East), Mumbai-400093
Email: investorrelations@kayaindia.net
CIN: L85190MH2003PLC139763

Naveen Duggal: Overall, currently about 18% of our total revenues come from products within the clinics. We also do business with shop-within-shops. Yes, we do shop-within-shops and we do business with modern trade and general trade. So we are present in stores like Shoppers Stop, Lifestyle, and such stores. We are also present in counters like Health and Glow, Dabur NewU and Religare. And we are also present now in certain specific slightly higher-end chemists in cities like Mumbai. So that's basically what it is. If you look at the growth, which is coming out of products within the clinics, on an SSG basis for the last quarter, it is about 12%. But if you look at the growth outside Kaya business, it's fairly substantial. We are seeing more than 30% growth coming out of businesses outside Kaya. And in the case of shop-within-shops, it would be roughly in a similar range of about 12%. But where we are growing higher is the modern trade business, where we have actually expanded footprint in some of the companies like Health and Glow. So I think this is a decent business. Our average margin in this business sits at about 76%. The KSB business, where we are heading towards a breakeven will still have some loss there this year. But I think we are progressively moving towards rationalizing some of the counters where we are not making money and I think we will progressively move towards breakeven in this business at a store level in the non-Kaya businesses.

Hem Agarwal: Okay. And what is it in rupee terms, the total product revenue which you're doing in rupee terms? How many crores?

Naveen Duggal: About 38 crores is what we will end up at the end of this financial year, out of which about 7 crores comes from non-Kaya retail businesses. E-commerce will end at close to 5.7 crores in terms of business in net

Reg. Office: 23/C, Mahal Industrial Estate, Maha kali Caves Road, Near Paper box Lane, Andheri (East), Mumbai-400093
Email: investorrelations@kayaindia.net
CIN: L85190MH2003PLC139763

terms. All of this is net of margins to partners. So that's actual rupee wise. So, overall, the product business for this year at a net level would be about 38.67 crores.

Hem Agarwal: Now one more question, sir. What about male grooming business, any status on that?

Rajiv Nair: You're talking with respect to product?

Hem Agarwal: With respect to product or even in the clinics, what's the status of the male grooming business?

Rajiv Nair: Going forward, there are certain services that we've added in the portfolio, especially around hair care, which have the potential of targeting more men into the business. So for example, the transplant business today is heavily dominated by men. It's still a very small scale, we started off in January last year, so roughly about 2 crores worth of revenue for the year coming from this and largely dominated by men. Otherwise, quite a few of our services are actually unisex in nature. So for example, facials, advanced facials, brightening, pigmentation, all of them are quite unisex in nature. In the product business, we don't and won't do a special range only for men because there are certain product segments like, for example, aftershaves and shaving foams and shaving gels etc. That's not within the portfolio what we are actually trying to do. In Skincare for example, we do a sunblock cream or we do a moisturizer, all of these are unisex products within the business. To attract men, I think hair care is a segment that we are tackling, where we would see more male input into the business.

Reg. Office: 23/C, Mahal Industrial Estate, Maha kali Caves Road, Near Paper box Lane, Andheri (East), Mumbai-400093
Email: investorrelations@kayaindia.net
CIN: L85190MH2003PLC139763

Moderator: Thank you. As there are no further questions from the participants, I would now like to hand the conference over to the management for closing comments.

Naveen Duggal: Just to conclude, we will continue to drive the journey of sustainable, profitable growth through expansion as well as same-store growth. Thank you all for attending the conference call.

Moderator: Thank you very much, sir. Ladies and gentlemen, on behalf of Ambit Capital, that concludes this conference. Thank you for joining us, and you may now disconnect your lines.

(This document has been edited for readability purposes)

Reg. Office: 23/C, Mahal Industrial Estate, Maha kali Caves Road, Near Paper box Lane, Andheri (East), Mumbai-400093
Email: investorrelations@kayaindia.net
CIN: L85190MH2003PLC139763