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Spice Mobility

Investor/Analyst Conference Call Transcript

November 16, 2010

Moderator: Ladies and gentlemen, good day and welcome to the Spice Mobility Q2 and HI FY2011 Earnings Conference Call. As a reminder, for the duration of this presentation, all participant lines will be in the listen-only mode, and there will be an opportunity for you to ask questions at the end of the opening remarks. Should need any assistance during this conference call, please signal an operator by entering "*" and then "0" on your touchtone telephone. Please note that this conference is being recorded. I now hand the conference over to Mr. Ravi Sathe from Citigate Dewe Rogerson. Thank you and over to you Mr. Sathe.

Ravi Sathe: Good afternoon everyone and thank you for joining us on Spice Mobility Q2 and HI FY2011 Results Conference call. We have with us the Chairman of the Spice Group Dr. BK Modi. Before we begin I would like to add that some of the statements to be made in today's discussion may be forward-looking in nature and a statement in this regard is available in the conference call invite, which was e-mailed to you earlier. We will begin the call with opening remarks from the management following which we will have the forum open for an interactive question and answer session. I would now like to invite Dr. Modi to make his opening remarks.

B. K. Modi: Good morning everybody. I hope you have received the presentation, which the Company has mailed to you earlier. You must have gone through the results, which were published in the newspapers. Let me start by first informing all the investors that the consolidation process is now complete and the new shares have been issued. The equity capital now stands at 238 million shares and the market cap of the Company now stands at ~ Rs. 3,300 crore with current share price of ~ Rs 138 – Rs 139. Spice Televentures has created two separate independent trusts, which hold shares with respect to the treasury stock and the employee stock.

As you may be aware, the Company is preparing itself for Mobility-2.0 play, the second phase of Mobility. In this emerging area, we are looking at mobile internet and related products being introduced in the market and this is just the beginning in India. There are already some products launched in the market and the complete 3G rollouts are expected by the end of this year. So, you will see a major change taking place in India next year. In the meantime our sister (group) companies in Malaysia and Singapore is already selling these products in 3G markets there and we will learn and practice the experience for Indian markets. In fact the strategy which the Company has adopted is keeping in mind the overall strategy of Spice Global, which is to create “consumer-centric business model” constituting of three businesses, namely Device, Retail and VAS as there are significant synergies between all these three businesses.

Speaking of financial highlights, there are certain advantages the Company got because of the consolidation. Spice Televentures, which was a part of Spice Global, has now been merged with Spice Mobiles, which was renamed to Spice Mobility. We have three main group companies amongst the others. They are Spice Global, Spice Mobility and Spice i2i. Spice Mobility, the Company we are looking at, is listed in the Indian stock market and Spice i2i is listed in Singapore. The brand belongs to Spice Global. The brand is available to both Spice Mobility and Spice I2I as Spice Global has an agreement with Spice Televentures (now merged with Spice Mobility) as well as Spice i2i. The brand is offered on the basis of certain norms. Basically, for the first three years brand is available free of cost starting from April 1st, 2010 and after that there will be a charge 0.25% of revenue for 4th year, 0.50% for fifth year, 0.75% for sixth year and 1% from 7th year onwards.

The consolidated accounts have been put together for first time. The combined revenue stands at ~ Rs. 961 crore and PAT stands at ~ Rs. 73 crore. The company has been benefited from the said brand agreement in terms of recovery of brand spend to the tune of Rs.31.9 crore this year. In the reverse merger process BPO and other business has been excluded out of the company which resulted in gain of Rs. 23.9 cr. from sale of interest in BPO business. Combined net worth now stands at ~ Rs. 828 crore and cash & equivalent stands at ~ Rs.385 crore. Spice Televentures was cash rich company and as a part of the merger that has come to Spice Mobility.

The Company financially as well as fundamentally is very strong now and we feel, should be able to grow to level projected for next five years. In the last six - eight months starting from January we have been working with McKinsey and they have enabled us to create a unified Company which has clear business plan, projections and road map. We call this project “Lakshya 2015”. And as a Group we are only focusing on Mobility from here. We feel there is a huge Mobility play which is related to the mobile internet, device, 3G and there is more than $90 billion mobile ecosystems which come into play and this is the area the Company is looking at.

As far as the business highlights are concerned, handset sales (including retail) in volume over the last six months increased to 3.6 million against 2.4 million in the corresponding period last year. The major change is evident in devices segment where most of the new phones are QWERTY phones. These phones have been introduced across the world and have recently been introduced in India. Retail business, which has been negative, has achieved EBIDTA break even in Q2/H1. VAS continued to do well. We hope that with the introduction of 3G, VAS will change significantly as next gen. VAS will be applicable on both the service side as well as on the device side. Voice and data vas together will come into play. Spice Mobility consolidated results, the net sales stood at ~ Rs. 960.8 crore, an EBITDA at ~ Rs. 68 crore and PAT at ~ Rs. 73 crore. The earnings per share (EPS) stand at Rs. 2.94. The detailed financials are included in the presentation we shared.

Device is the business which was rather worrying last quarter. We had issues regarding liquidation of stocks. In the next six months you will see major improvement here. However looking at the numbers on the device side, revenue has gone up by 11.5% to Rs. 449 crore in H1 this year against Rs. 402 crore for the corresponding period last year. PAT increased mainly on account of recovery brand spend which has been absorbed by Spice Global. We are increasing the product range and new handsets and will continue to focus on innovation. We have launched View D phone which is India's first 3D phone, S-1200 phone with 12 megapixel optical zoom and load of flash memory has been launched, Smart phones like Mi300 the Android have been launched. The introduction of new phones is well received.

As I said, the Retail story looks very robust. The revenue figure against the last half year of 2010 of ~ Rs. 284 crore has increased to ~ Rs. 440 crore which indicates a growth of 55%. Corresponding Quarter growth for retail stands at 60%. We now have about 760 stores across 160 cities. The quarter to quarter growth in retail is continuously increasing and brand changeover from Hotspot to Spice Hotspot is playing it role in it. In our VAS business, we have observed a revenue growth of 29% against the corresponding half year and a 35% growth in the corresponding quarter. We have lot of new products, which we have started offering. We now have Live Aarti, to include banking USSD services for large banks made live with multiple operators allowing inquiry services, mobile top ups and other offerings. We have developed number of applications which can be embedded in our devices as well. This is the first time we trying to embed large number of services/apps on our devices which will aid our revenue not only from the operator but also from the device manufacturer. Spice Digital is at a very advanced stage to buy a Company based in Malaysia which is area of mobility and mobile internet. This Company is currently selling products based on mobile internet and software that can be embedded on devices as well. And as I said in the future VAS will not only be dependent on the operator but on the device as well and with this acquisition we are now further equipped within VAS keep ourselves ready for the mobile internet business.

Manufacturing has already commenced at Baddi. The current installed capacity is 4 lakh handsets per month and we plan to take it up to one million handsets per month in the next six to 12 months time. We are also planning to produce some components and boxes from this plant.

On an overall basis, we feel we are in a field which is growing rapidly. Mobile internet has been projected as the next biggest revolution in the world. It is not only going to affect the field of telecommunication, it will have it affect in the field of entertainment, healthcare, in fields of education, information and finance and all will be greatly benefit from this. All these areas are now exposed to mobile internet and will be part of a huge revolution, which is going to happen in the coming time. Thank you very much for listening and I am happy to answer your questions.

Moderator: Thank you very much. The first question is from the line Himanshu Shah of HDFC Securities, please go ahead.

Himanshu Shah: One is on the handset business. Our volume has been up 40% quarter-on-quarter whereas our sales has declined in the handset business by 16%, which probably implies that our average selling price during the quarter will be lower by 30% and I believe our ASP was Rs. 2,000, so is it fair to assume that it will come down to Rs. 1,400 and what has led to same?

B.K. Modi: We had some old stock, which we have liquidated at comparatively lower prices. We have introduced a number of new phones in QWERTY and mini QWERTY series. They are comparable to products like Blackberry. These phones are comparatively costlier (in terms of ASP), and will be main selling products among others as there is a huge demand for QWERTY phones in India. These products have been a big revolution in Malaysia and Indonesia. In fact our sister Company in Malaysia sells them as blueberry phones as they are compared with the Blackberry. In India we are selling them as QWERTY and mini QWERTY phones. The mini QWERTY phones are being sold at about Rs. 2,300. The drop you see in the average price which is partly reflected by inventory liquidation and party by fact that these new phones, were not available before in our portfolio. I feel that the average selling prices will not be less than Rs. 2,000 as we go along as lot of new phones are going to be introduced which can handle both voice and data. Consumers are now looking at phones which can handle data as well for instance SMS has become a reality, products like the Blackberry are used by people to communicate through data and SMS has become very common. Everybody is looking for those types of phone today. So Phones are now not only used for voice but also for data. Keeping all these factors in mind we feel the average price will rise in coming quarter.

Himanshu Shah: But is it fair to assume that it was in the range of around Rs. 1,400 during the quarter?

B.K. Modi: Stock in trade declined by nearly Rs. 50 crore for the three month period. That reflects the old stocks which have been cleared now. The old stock was cleared as we were getting ourselves ready for these new products to be launched, and we did not want anything pending from the past. When you look at the next quarterly result you will see that improvement. This decrease in stock in trade has partly affected the average selling price of the phone.

Himanshu Shah: Sir, despite this particular liquidation of stock, our EBITDA margin in the handset business has moved up quite sharply basically from 16% to 22%, so what has led to this contrarian movement because I am assuming that liquidation of stock could have happened at in fact lower margins compared to the normal business margin.

B.K. Modi: As I said earlier, due to brand agreement lots of brand spend / expense incurred by the company has moved to Spice Global. These benefits were earlier available to Spice Televentures, which was part of Spice Global and is now merged with Spice Mobility, thus the benefits of it has come to the Company (Spice Mobility). Brand building is now being done by Spice Global. It (Global) is also supporting other companies of similar vicinities. Secondly, we are focused on tightening our costs and other expenses. There are also synergies derived as a result of the three companies coming together. Previously Spice Mobility was working separately now as the synergies coincide costs are cut down.

Himanshu Shah: Sir, third question is on the retail front; retail business has shown quite significant improvement, the revenues were up Rs. 33 crore quarter on quarter Whereas EBITDA is gone up by almost Rs. 18 crore, so this showing like incremental EBITDA margin of 50% so what is driving the sharp improvement in retail business quarter-on-quarter – just in a single quarter?

B.K. Modi: If you observe, the revenue has gone up and the fixed cost and other factors like rentals and manpower are the same. Also when Spice brand entered retail store (rebranding), people view them as part of large entity/ belonging to a large Group. Hotspot was not as well known brand as Spice, Spice is big, established and well known brand. We are now also selling VAS through devices and through retail, which is giving us a higher margin. In fact we see major improvement once the 3G operations come into existence. Most of the operators are approaching us for special schemes for launching 3G phones, 3G Packs etc through retail and the average selling price is nearly more than double than that of normal mobile devices. At present we are discussing special arrangement with service providers like Airtel, Vodafone and other players to see how they can launch 3G through our retail.

Himanshu Shah: Thanks.

Moderator: Thank you Mr. Shah. Our next question is from the line of Shobit Khare from Motilal Oswal Securities Limited. Please go ahead.

Shobit Khare: Sir first on this branding side just wanted to check again what are the expenses right now which are in the part of P&L and what expenses from here will not be a part of the P&L account?

B.K. Modi: As I said, Spice Mobility now has an agreement with Spice Global and any brand expense of nature of creating corporate Spice Brand will be absorbed by Spice Global and this in line with large MNC Companies practices where corporate brand expenditure is undertaken by the main company owning the brand. However product related brand exercise will continue to go into respective books. And for the next three years you would not see any of these expenses going into this. Even in the future i.e. after three years by virtue of agreement in place, Spice Global will charge some percentage of revenue which will go up to 1% of revenue in phases over six-seven years. In other words up to 1% of revenue will be taken as brand expenses to recover the cost of the brand creation by Spice Global in future.

Shobit Khare: Sir on the VAS business, we have seen a very good revenue growth, just wanted to check what is the mix product wise, broad mix of our VAS business and which products are driving the growth and after 3G what kind of new products we expect to get more growth in the future?

B.K. Modi: Some of our products which become very famous and successful are devotional, regional based, “Bhakti” and “Faith” based products as they touch people and their lifestyle like live aarti, and similarly through our Malaysian counterpart we also have Islamic based VAS. In other words we have VAS that is related to different religions in the world. According to me this is becoming a lifestyle product. We are now involved in the banking and finance sector through VAS products and we are proud to work with the operators to see how to provide services in that area. We feel that VAS will increase substantially in the area of finance, entertainment, education and healthcare segment. Also we have got our presence extended in regions of Uganda, Congo, Nepal, Iraq, Tanzania, Nigeria and Kenya. Also we are in pursuit of acquiring a Company in Malaysia. Once the acquisition is complete then Spice Digital will have its presence in Malaysia, Singapore and Indonesia. It operates basically in the mobile internet space. They have a VOIP product called Suno, which has some very advanced features. To give you an example, yesterday I went to one of the hospitals opening and they were using the VOIP products for patients who want to talk to their relatives, So I believe there is a new world which will be exposed to Mobile internet and this space specially is going to grow substantially. The major factor that VAS depends on is how much the device can handle and that depends on the chip inside it. There are various chipsets manufacturers. Apple uses their own chip, which is specially manufactured through a Company in the US. The chip supporting android and Google is used by various people in android and Google based products, Nokia works with chip manufacturers designed for its Symbian software. We are looking at possibilities of working with MTK and strategizing to develop advanced chipsets which can support VOIP, Other OS and apps.. VAS capabilities apart from the operator will depend on the device and the new devices we are offering in November end, will have VAS embedded inside the device, like Apple. There is major change which is coming through and the VAS industry will ramp up as the company is getting ready to play it role in the booming VAS requirement for mobile internet.

Shobit Khare: VAS margins if I see Q-O-Q, the EBITDA is almost flat, where our revenues are quite a bit, was there any one of costs in Q1 and how you look at this 22% EBIT margins?

B.K. Modi: VAS margins are pressurized because the operators continuously try to squeeze margins. The voice and non data related VAS margins will be under pressure but data VAS will see margins growth and that is why I said that we have been putting efforts to leverage on data VAS. If you look at the VAS industry voice based, VAS in India will go from $1 billion to $3 billion but data VAS will go from zero to $2 billion. VAS, overall, in the next five years is likely to go from today $1 billion to the $5 billion mark. Your Company is moving towards being more data dependent. The VAS industry as I said will go through major change and the company is getting ready for data VAS as well but at present margins will remain under pressure as currently it is all voice driven.

Shobit Khare: Okay and handset side what kind of device volume growth we expect this year and has there been any early trends of 3G demands when it will start contributing to our volumes and the ASP increase, which is expected along with 3G?

B.K. Modi: 3G demand will come only in the second half of next year because the rollout will happen by end of this year. There will be some demand now but real demand will start from June onwards only. There will be some demand between January and June next year as well, as most of the companies are getting ready to launch their 3G products. One of our group companies in Malaysia has already tied-up with Maxis to launch a device which can be compared to iPad. So we feel that most of the 3G operators will try to work with us and we will complement them. Mean while the 3G people are still trying to position themselves.

Tata has taken the initiative by launching their services at competitive prices and we feel that the operator margin will come down than expected. Hence they will try to gain revenue through VAS, as for them to make money only through voice would not work and they need to shift to data and VAS to make money. I believe the whole game is shifting to VAS in terms of 3G services. If you see, in the process of preparing for 3G, people use SMS more effectively and on a higher scale and that is the reason behind success of QWERTY key pad based products amongst the masses. We have recently launched a significant amount of products that can be compared to products like Blackberry which can handle data and have the QWERTY key pad. Our sister company has already achieved success in similar phones called Blueberry and we will soon move that to Indian market as well.

I have to educate you quarter-on-quarter about what is happening because predicting how far this change will happen will depend on, how fast operators, device, manufacturers MVAS and VAS people move and how do we train and educate the customer. It will depend on how fast the organized retail moves and how they make the customer adopt better technology. We are present in all the three areas i.e. Device, VAS and Retail. We are not present on the carrier side. So we are and will work along with the operator to make sure that this changeover to 3G in India moves much faster than any other country. That is anybody's guess at present, but all indications are that it will go faster and not slower.

Shobit Khare: Any target for the number of new stores opening on the retail?

B.K. Modi: We have studied the Indian market and are targeting to significantly ramp up the number of our stores over the next 2 -3 years. We are looking at opportunities to consolidate. We have few deals in the offering where we are looking at acquiring/buying companies in this space. Also we can grow organically. Now our confidence level is higher because we have achieved break-even. Having achieved break even, we will roll out the stores at a rapid pace and we will continue purchasing stores which come along. Next year we are trying to double our no. of store and size. Retail is one of our main story titles because it is not easy for a new player to enter the market. Retail is now a part of Spice Mobility. It has no problem in terms of funds and finance availability. We have enough cash at the console level with zero debt. Retail is what we are going to push this year.

Shobit Khare: Thanks a lot.

Moderator: Thank you Mr. Khare. Our next question is from the line of Udit Garg from Religare. Please go ahead.

Udit Garg: Just a couple of questions; firstly on the Spice handsets, can you give color on how the Android phone has picked up and what is the sort of sales that you have seen for that that segment. Secondly, on the retail guidance, what is the sort of long-term EBITDA margins or EBIT margins that you can in that business. Thirdly, just on the tax rate can you give any future guidance on the tax rates for this year and the next year. Thanks.

B.K. Modi: The demand for handsets exceeds the supply today. There is a shortage of chips, which has started happening recently. We have good orders for our Android phones, the new QWERTY series phones and other which we have launched, but we are not able to supply as demand is outstripping supply. So our focus today is at the supply chain and not the sales. As I said earlier we are looking at agreements to closely work with MTK and to procure all the supplies we need. On the handset side there is a huge demand. You may be aware of the fact that Android based devices, worldwide, are doing very well. It has beaten Apple. It is selling faster than any other device in the market. Apart from Android all the other products will move in a similar manner. On the retail side, our projection is that we will move up to 5% in terms of EBITDA on business model which exists today. What we now sense is that operators want to grow more aggressively with introduction of 3G and they require organized retail support to achieve the growth. We will get higher margins as of operators need organized retail to push their 3G based products and launch of special schemes. On retail side with operator push we feel that we can achieve (EBDITA) margins between 5% to 10% but 5% is manageable without operators push If there is tough competition between operators then they would like to push and as it happened in other places like China, the margins for organized and overall retail will improve.

Udit Garg: What are the current monthly sales run rate that you having, both at the retail and at the device level?

B.K. Modi: In the Retail business, our average sale price is nearly double than it is in the device business. Looking at top line numbers of Retail and Devices, they are almost equal. But devices, in terms of volume sell much more than retail. On the device front, we hope to sell one million handsets per month in the next six months going forward. On the retail side we are looking at selling 0.5 million handsets per month. As you are aware, ASPs in retail are double and should increase further.

To answer your tax query on Retail is we have carried forward loss of nearly Rs. 200 crore to offset against profits. We are now manufacturing our devices in Baddi; Himachal which is also gives us tax benefit. We qualify for about five years tax benefit as we started production before April 1, 2010. We do not think our tax rate in any case will be more than the MAT in devices. In digital we have advantage because we have put operations in Dehradun and Himachal where again we have tax benefits. We feel that we have lot of tax brackets and our overall tax rate will not be more than MAT which is 20%.

Udit Garg: Thank you.

Moderator: Thank you, Mr. Garg. The next question is from the line of Srinivas Rao of Deutsche Bank. Please go ahead.

Srinivas Rao: I have two questions, first on your VAS business. In your last conference call you had indicated that the business was kind of slow but coming out of the slow growth scenario. I noticed that your Q2 revenue numbers and EBITDA numbers are largely similar to the Q1 numbers. So what is your view, as this business stabilized now both India and abroad?

B.K. Modi: Spice Digital numbers quarter-to-quarter shows 17% of growth. I said the real growth will be evident once 3G comes and 3G itself is delayed. But now every operator has announced that it is going to happen before the end of the year. This will drive growth. Further as I mentioned earlier we are looking at acquisitions as a result of which you should see growth coming from operations outside India as well. In VAS we are creating opportunities not only in India but outside India also. We are going to expand in regions of Asia, Africa and in the Middle East, in fact Africa we have already started. If you see VAS is becoming a very regional because we have to localize the content. VAS is dependent on culture and lifestyle. We have prepared a whole regional strategy which we call the i2i strategy we are going right from Ivory Coast to Indonesia in field of VAS. We feel that we are at the final stage of first acquisition. We have already started operations in Africa, through Company which we started about nine months back, which is now giving results and we are looking at a Company in Middle East. You will also see growth because of both acquisitions as well as organic growth.

Srinivas Rao: What percentage of the revenues is from India now?

B. K. Modi: At present, it is mainly India because others have just commenced operations. You will see them coming next year as we are gearing up for mobile internet and 3G. One of the reasons we are buying these Companies is for acquiring technology, which we can bring to India. As I was just explaining that this Company, which we have bought in Singapore and Malaysia, has products, which are like BB messenger. It has products like voice over internet. It also has products like Fun Club which is between group of people and other networking products are also there. We are going to have products, similar to what Apple has and what Facebook does; we have an edge as we will localize it. This Company already does that. We have a whole strategy of mobile internet in VAS which we call Mobility 2.0

Srinivas Rao: Sure. On the device sales, what will be your estimation of the market share in India and any color on market share trends of domestic manufacturers versus the global majors, can you throw some light?

B. K. Modi: Globally there is a huge change that is evident for mobiles. The big winners at present are three - they are Blackberry, Android and Apple. All the rest are adjusting to these three new challengers. If you look at the American market, more than 70% of the market is owned by these three players. In Europe and other places Nokia has been the major player and captured market through bundling its product with the operators. I think that thing is going off with the introduction of the 2 sim phones. We have a 4% market share at present, but now with the whole new range of products, and with the special deal we are trying to work out with MTK, which produced half the total chips in world based out of Taiwan, we believe we should be able to go up to 10% market share in India. In certain markets, like Malaysia today, we have about 20% market share. Even in India, if you look at some of the markets, where we have a good distribution network. We have a market share in excess of 20%. What has happened in India is that we are not in all the regions of India. We started from north. In south we have a negligible market share. In certain areas like Maharashtra, Orissa and Bihar our market shares is very small so we have started focusing on these areas. It is more about the distribution network which we need to build. Previously, Spice Mobiles had limited resources, but with the merger taking place and Rs. 350 plus crore cash in the Company we can geographically expand ourselves in all these areas. That is what we are planning to do in the next year. You will see a major growth coming in the next six months and trend will continue in coming years.

Srinivas Rao: Finally one more question. Is there a plan for any fund raising by this Company over the next 18 months?

B.K. Modi: We have already announced that the Spice Televentures has created two separate independent trust and one of them has treasury stock of 3.5 crore shares. Discussions are going on with investment banker and we believe that these shares will be placed before the end of this year. We have proposals to buy some companies which are available to us and we may raise funds for that.

Srinivas Rao: Thank you so much sir.

Moderator: Thank you Mr. Rao. The next question is from the line of Ricken Gopani of Infina Finance. Please go ahead.

Ricken Gopani: I wanted to understand more on your retail business, currently what would be our sales per store or overall volumes that we do in retail and what would Spice handsets be as a percentage of sales? Some color on the overall retail business?

B.K. Modi: At present, the Retail business earned revenues of Rs. 440 crore in six months so if you even project it similarly; we are talking of more than Rs. 1 crore per store. We hope to take it to Rs. 2 crore per store. We now are adding more products and services there and with 3G coming in, the revenue per store will increase substantially. If you compare what happened in China, the revenue per store increased more than 250% to 300% post 3G was introduced. We will see a major growth in that as far as store revenues are concerned.

Ricken Gopani: Okay. Generally, whenever we open a new store, what is the kind of investment that we need to put per store or that is not very significant as such?

B.K. Modi: We are building our brand by putting the Spice brand in the stores so that stores are seen to be Spice branded stores. We have to do all the fittings and the branding, which costs less than Rs. 50 lakhs (on maximum side) and depends on the size of the store. It could be anywhere between Rs. 10 to 50 lakhs. Avg. size store cost between 10-15lacs. The main thing is how we do the branding which is most important as the customer visits the store as he sees the brand out there, organized atmosphere and the trained staff. It is a retail game which we need to play.

Ricken Gopani: Okay. Sir since we only have the PBIT margins for that particular business, if you could just share how does the gross margins there stand, if I were to just understand that? Is there any scope for the gross margin itself to improve because of sales mix of our own Spice handset or other handsets increasing in the overall mix?

B.K. Modi: The gross margin varies from product to product. Nokia is the lowest; Samsung is highest among the foreign brands. We are already getting about 13% of store sales via Spice branded products and we hope to increase it to 30% over period. There are also accessories available, which have nearly 100% to 200% margins. In Malaysia, we have acquired a Company via Spice i2i, which is an accessory Company. They have been very successful in Singapore, Malaysia, and other countries. We are now going to use our own accessory in India from January next year. In that the margins are as high as 100%. Depending on the product mix the margin moves in retail. We hope that the overall (gross) margin, should be in the region of 15% to 20%. At present, it is at around 10% and from 10% we are planning to move to 15% to 20%.

Ricken Gopani: Okay. Secondly on the manufacturing side, we said that the capacity currently is about 4 lakh units that is the monthly capacity we are talking about?

B.K. Modi: Yes, monthly.

Ricken Gopani: So how is it currently being utilized, if we were to just look at the current volumes from there?

B.K. Modi: Presently capacity utilization levels are low. However we expect to quickly progress towards the 1 million mark over the next 1 – 2 years

Ricken Gopani: Okay and in this capacity most of the components would be again imported from China or other markets, and we will assemble it over here right, will that would be the plan over here?

B.K. Modi: No, in India there are some component manufacturers, which have been developed and they are already supplying components to Nokia and Samsung. Those suppliers are also available to us. For example, we buy the battery from the same vendor who supplies to Nokia. The manufacturers are available and we have common manufacturers between Nokia, Samsung and Spice.

Ricken Gopani: Okay. So to put it the other way, what would be the benefit or rather overall cost per handset? Will that increase or will that remain the same by manufacturing it here?

B.K. Modi: No, manpower cost is certainly lower in India compared to China. Manpower cost in India is still one-third of China. Manpower cost advantage does exist. The issue is about how many components can be made in India because the industry is still small here and it is predominantly led by Nokia. Nokia is using it for export purposes. In the future this industry will develop both for the local as well as for the export market. There is a tax advantage. Tax advantage is not only in terms of manufacturing; it also gives advantages of income tax which is a major. We are looking at this on a long-term basis and I feel in longer run India will become a manufacturing hub for mobiles for sure. VAS is also going to be dependent on mobile so what will happen is you are making a consolidated product which is VAS and mobile together. Whether we will involve ourselves in chipset manufacturing is something which is being evaluated because China has just set up two chip manufacturers, so far it was only present in Taiwan and America. The chip manufacturing in India will take some time. The other components which are plastic, metal, and other products are available including the SMPT lights and all that we will do here.

Ricken Gopani: Okay and lastly on the handset side, I wanted to understand what are components that you are seeing shortages on currently apart from chip sets or it is only chip sets that you are seeing a shortage?

B.K. Modi: Mainly chip sets. Because Android has a huge demand along with MTK handset phones. There may be a sudden changeover in the habit of consumers who wait till changes are confirmed and then buy the product after it is well established. The mobile internet revolution is rapidly establishing. As soon as 3G comes in, there will be a huge demand. If we do not prepare ourselves, we may have this shortage, which spans out to a few months. This is not a long shortage. It is just that it takes two to three months to pick up with the demand-supply situation. Suddenly these phones have become very popular, but in the future we are keeping in mind that we need to be well covered for 3G products because now with the vendors, we have a common strategy, so what we are buying for Malaysia, Singapore, Indonesia and Thailand, will also apply for India. We are creating a common brand. In Malaysia we have Spice CSL, but S as a logo will be common. We have just adopted a strategy and we will be launching the Spice brand like Apple, printed on every phone. This will be accompanied with a new design, which we are launching from January. Every phone will have an S, whether it goes to Malaysia or Indonesia. There is a lot of commonality, which you will see in the future.

Ricken Gopani: Okay and in the discussions that we have with the chip set manufacturers, do we have a minimum quantity off take arrangement over their or what kind of an agreement have you entered with them?

B.K. Modi: At present, we are looking at getting into agreement with the chip manufacturer where we are looking to work with them right from the source code stage. When the chip is manufactured, the certain software works on it and some don't. One of the issues is that the software/apps, which we have developed, works on Apple and Blackberry, but does not work on MTK. In fact, we have one product, which is now a #3 trend in Blackberry. Nokia also wants it for the N8 phone. N8 has three soft wares which are part of the phone and one of them was Spice. Spice has gained lot of experience in terms of VAS products, some of those are accepted by the chip manufacturers.

Ricken Gopani: Okay, and sir lastly on this advertising cost that we have, if you look at FY'10, about 8.5% is what we spent on advertising expenditure for the full year, so now with this change where in the Spice brand related expenditure will go to Spice Global, what do you think will this as a percentage of sales come down to?

B.K. Modi: We have taken into consideration the revenues generated from total sales along with Spice Retail. If you look at advertisement revenue, the hoardings in the store are also included as a part of the advertisement revenue. This helps us showcase our own brand and stores. You have to look at the bigger picture, but I believe overall it will be lesser than 9%.

Ricken Gopani: Okay, from 9% it will decrease. The overall money that we will pay is about 1%, about four to five years from here as a royalty for the brand, is that the correct way of looking it?

B.K. Modi: Yes, after five years. For three years it is free then it starts building up. The same agreement also exists with Spice i2i. After three years, it stands at 0.25% for the fourth year. In fifth year it stands at 0.5%, sixth year is at 0.75%, and after six years it will stand at 1%.

Ricken Gopani: Okay, thanks a lot sir.

Moderator: Thank you Mr. Gopani. Our next question is from the line of Umesh Gupta of Reliance Wealth Management. Please go ahead.

Umesh Gupta: I just wanted clarity on this deal, with whom have you done this brand deal, I am not able to get exactly is that?

B.K. Modi: We have a Company called Spice Global based out in Singapore, which actually owns the Spice brand.

Umesh Gupta: Is this a group Company or is this a subsidiary of the listed Company?

B.K. Modi: This is a group Company.

Umesh Gupta: Sir in that Company, the listed Company in India does not hold any stake?

B.K. Modi: No. This Company holds stake in this Indian Company and not the other way around.

Umesh Gupta: Spice Global hold stake in the Spice Mobility, and you have sold the brand to the Spice Global.

B.K. Modi: No, Spice Global owns the brand. We have an agreement with Spice Televentures and now Spice Televentures is merged with Spice Mobility. Spice Televentures previously was owned by Spice Global. Now Spice Televentures has merged into Spice Mobility, because of this merger, the brand cost which was previously booked in Spice Mobile does not need to be booked because the benefit of Spice Televentures agreement has come into practice.

Umesh Gupta: Okay. So going forward this Spice brand will continue to be owned by the Spice Global and Spice Global will spend on the advertisement and Spice Mobility will not?

B.K. Modi: Spice Mobility will also spend on its own expenditure, but there are certain expenditures which are global in nature, which are related to brand building.

Umesh Gupta: Okay. So on what basis will you pay to Spice Global?

B.K. Modi: We have an agreement that for the first three years it is free, because the first three years is the buildup stage. After three years, fourth year onwards it will be 0.25% of the turnover, then one year after that 0.5%, 0.75% after 2 years, and after six years it would stand at 1% of turnover.

Umesh Gupta: And what Spice Mobility gets in return is the advertisement expenditure done by the Spice Global internationally.

B.K. Modi: Yes, internationally as well as locally, because they are the brand ambassador. They sponsor big programs which are mostly TV programs and movies. It is like any other global Company practices.

Umesh Gupta: Okay. Thank you.

Moderator: Thank you. Ladies and gentlemen that was the last question. I now hand the conference over to Dr. Modi to add closing comments.

B.K. Modi: Thank you very much for all your enquiries. I do appreciate the fact that the investor community showcased keen interest in our Company. We feel that we are on a high growth trend. This Company stands out amongst the rest of the Companies currently present in the same space and market. We are the only Company, which is active in all the three areas of VAS, retail, and device. We feel this is necessary to be able to face the challenges of the future, which is the mobile internet, and if you look at the companies like Apple and others, they are active in all these three areas, which are device, VAS, and retail. We are in the right strategy and we look for your continued support. Thank you very much.

Moderator: Thank you Dr. Modi and other members of the management team, and Mr. Sathe. Ladies and gentlemen, on behalf of Spice Mobility that concludes this conference call. Thank you for joining us on the Chorus Call Conferencing Service and you may now disconnect your lines.