"HSIL Limited Q4 FY17 Earnings Conference Call"

May 23, 2017

MANAGEMENT: **MR. SANDEEP SIKKA – CFO, HSIL LIMITED**
MR. R B KABRA – PRESIDENT (BUILDING PRODUCTS), HSIL LIMITED
MR. NAVEEN MALIK – HEAD (CORPORATE FINANCE), HSIL LIMITED

MODERATOR: **MR. DHAVAL MEHTA – EMKAY GLOBAL**

Moderator: Ladies and gentlemen, good day and welcome to the Q4 FY17 results call of HSIL Limited, hosted by Emkay Global Financial Services. We have with us today Mr. Sandeep Sikka – CFO, Mr. R B Kabra – President (Building Products) and Mr. Naveen Malik – Head (Corporate Finance). As a reminder, all participant lines will be in the listen-only mode and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing '*' and then '0' on your touchtone telephone. Please note that this conference is being recorded. I would now like to hand the conference over to Mr. Dhaval Mehta of Emkay Global. Thank you and over to you, sir.

Dhaval Mehta: Thanks Inba. Good evening everyone and welcome you all for Q4 FY17 Earnings Con Call of HSIL Limited. We would like to thank the management for giving Emkay the opportunity to host this call. So, we will start with opening remarks by Mr. Sikka followed by the Q&A. Over to you, sir.

Sandeep Sikka: Thank you Dhaval and I just thank all the participants on the Conference Call for joining us in this post results call. So as a standard we have to start with the disclaimer, which means so that I would like to refer to the disclaimer from our investor presentation which is on our website. Certain things in this conference call concerning our future growth prospects are forward-looking statements within the meaning of applicable security laws and regulations and may involve number of risk and uncertainties beyond the control of the company that could cause actual results to differ materially from those appearing in such forward-looking statements. So, you are requested to refer to the disclaimer from investor relation section of our website under investor presentation before acting or taking any decisions on the basis of this conference call**.**

So, we just closed the results on 18th of May 2017. The results for the quarter and twelve months ended 31st March, 2017 have been prepared in compliance with the new applicable accounting standards which is IndAS, as notified by Ministry of Corporate Affairs. The corresponding results for the quarter and twelve months ended 31st March, 2016 have been restated for the purpose of comparison. Apart from this we had a scheme of demerger in the subsidiary where in the Honourable National Company Law Tribunal of Kolkata, West Bengal vide its order dated 4th May, 2017 has approved the composite scheme of arrangement between the company and it's wholly owned subsidiary as HHRPL their shareholders and creditors. The effect of that scheme has been taken, I would request all the participants on the call to please refer to the notes to the published results. We have explained there the full details of the effect of the scheme.

Further, the company has also reorganised and changed the composition of reportable segments. Accordingly corresponding segment information for the segments identified has been restated. I would again request the participants to refer to the notes to the published results, wherein we have explained this in detail. So HSIL Limited, for the quarter and the twelve months ended 31st March, 2017 achieved a gross sales of around Rs.637 crores and Rs.2,230 crores, representing a marginal growth of 0.40% on the quarter and 6% over previous year's corresponding sales figure.

The operating profit that is EBITDA, for the quarter and twelve months ended 31st March, 2017 is around Rs.74 crores and for the year is Rs.294 crores respectively as compared to previous year corresponding figure of Rs.99 crores and Rs.337 crores respectively. Now, the company operates through the four business segments. In terms of segment revenues, building product division for the quarter and twelve months ended 31st March, 2017 achieved sales of Rs.304 crores and for the year Rs.1,038 crores, representing a growth of 5% and 8% over the previous year corresponding figure. And the EBIT for the building product division for the quarter and twelve months ended 31st March, 2017 is around Rs.47 crores and for the year Rs.165 crores as compared to previous year figures of Rs.50 crores and Rs.171 crores.

Packaging division performance is slightly subdued during the quarter and the packaging product division for the quarter and twelve months ended 31st March, 2017 achieved sales of around Rs.260 crores and Rs.969 crores as against previous year corresponding figures of around Rs.310 crores and Rs.997 crores respectively. EBIT for the packaging product division for the quarter and twelve months ended 31st March 2017 is around Rs.24 crores and for the year is Rs.99 crores, as compared to previous year corresponding figure of Rs.46 crores and Rs.125 crores respectively. There has been a drop-in sales and also slight pressure on EBIT also due to the slowdown in the sector and also the change in the product mix.

In terms of consumer product divisions, now this is the first time we have separately shown as a part of the segment. The consumer product division for the quarter and twelve months ended 31st March, 2017 achieved sales of Rs.43 crores and Rs.128 crores and this represents a growth of 226% and 124% over the previous year corresponding figure. And if you see for the last 2 years this business has grown more than 100% year-on-year. EBIT for the consumer product division for the quarter and twelve months ended 31st March, 2017 is around Rs.8.82 crores negative and for the year is Rs.24 crores negative, as compared to previous year corresponding figure of around Rs.8.48 crore negative and Rs.16 crore negative. So, the incremental cost which is there is further strengthening of the team and also due to the marketing activities off late which we have started during the Q4 of the financial year.

Then we have a new business which is the retail business. Not exactly new, which is the part of the demerger which is of the HHRPL, the retail undertaking which has come in now as the part of HSIL Limited. So, that division which we call as a retail business division for the quarter and twelve months ended 31st March 2017, achieved the sales of around Rs.30 crores and for the year Rs.96 crores and this is against previous year corresponding figure of Rs.21 crores and Rs.93 crores. The EBIT level of retail division for the quarter and twelve months ended 31st March 2017 is Rs.1 crores negative and for the year is Rs.15 crores negative as compared to previous year corresponding figure of quarter of Rs.5 crores negative and Rs.16 crores yearly negative.

So, during the financial year 31st March 2017 there is a drop in overall EBITDA as well as the respective business EBIT as compared to previous year corresponding figure and if we try to primarily see what are the main reasons. So, one is the reduction in the overall other incomes and one main item of the other income is there was an incentive of Rs.17.41 crores, which was received by our packaging division from the government of Telangana as a part of the mega project scheme and the previous year figure was Rs.17.41 crores, as under the head other income. So, this year we have not got anything from the government although we still may have a claim for around Rs.8 crores to 9 crores which we will account for them when we have certainty that money will come through.

Additional EBIT level expenses there on the consumer product business of around Rs.7.89 crores which as I have explained is on account of the media spend which was started and the further strengthening of the distribution team. There is increase in power and fuel cost, all across basically on account of rise in power prices on the fuel prices across which are linked to the global fuel prices and there is a reduced M2M gain. So, last year we had M2M gain of around Rs.9 crores and the difference between them is Rs.9 crores under the IndAS conversion and this has been explained in notes to the published results also.

So, for the quarter and twelve months ended 31st March, 2017 PBT is around Rs.40 crores and Rs.150 crores, as compared to previous year figure of around Rs.60 crores and Rs.182 crores. Profit after tax for the quarter and twelve months ended 31st March, 2017 is around Rs.31 crores and Rs.103 crores, as compared to previous year corresponding figure of Rs.38 crores and Rs.116 crores. As regards the bank debt, the total net bank debt which is net of the cash items as on 31st March 2017 is around Rs.667 crores with an overall loan cost funding of around 6.12%. Of this, the working capital limit utilization net of cash is around Rs.305 crores. That is the broad contours which we have discussed all the way also from a part of the published results. And we hope all the participants would have got an opportunity to glance through the results which have been published, submitted with the stock exchanges and also put on to the website.

And I would now request, if you can go into the question answer sessions, we will be happy to take the calls.

Moderator: Thank you very much, sir. Ladies and gentlemen, we will now begin the question and answer session. We have the first question from the line of Anshuman Atri of Haitong Securities. Please go ahead.

Anshuman Atri: Sir, my question is regarding the projects which under execution. Sir, what is the latest progress and what can these projects add in the next 2 years in terms of revenues and also in terms of EBITDA?

Sandeep Sikka: So basically, if you see we had 2 projects on the line. One was our pipes project which is CPVC & UPVC pipes and the other project which was security caps and closure project. So, I will talk first about the security caps and closure project. So, the first phase of the trial production in this project has already started in the first week of April 17 and we expect the commercial production to start by the early quarter 2 of this financial year. So, we will start with the capacity of around 275 million pieces of the small caps and over a period of time, next 12 to 15 months will increase the capacity to around 600 million pieces. And this is the combination, this is the product mix of a large cap and the small cap and we feel that with 600 million pieces of caps, we should be able to touch a turn over exceeding Rs.100 crores in this business. Second is on the pipes project, so there is a good progress on the project. So, we feel that the trial run production in this business should start somewhere in August 2017 and within one or two months we also expect the commercial production of this business. Initially we will kick start with installed capacity of around 12,000 metric tonnes and CPVC of 3,000 and normal of 9,000 tonnes and overall in next 2 years as the market also builds up, we will build the capacity to around 30,000 tonnes as we have been historically telling. And that is the broader contours from both the projects fairly good progress and I think this is a year wherein both the projects will start and next year onwards they will start showing major chunk of the revenues.

Anshuman Atri: Sir, in terms of CAPEX, what is your CAPEX and for FY18 and FY19 what kind of CAPEX we are going to see?

Sandeep Sikka: So, we have spent good amount of money in last 2 years in terms of development of these facilities. So, when we are talking overall CAPEX which we have spent in fact till now over last 2 years is around Rs.380 crores. So, which includes the up-gradation of building product division, which includes certain CAPEX in the glass plant, we also acquired the surplus factory land in Rajasthan. Then we have spent money on closures which is around Rs.60 crores-70 crores and then pipes we spent money, which is again around Rs.50 crores-70 crores till now and as we move forward we expect that in 2017-2018, the total CAPEX which we intent to do is somewhere around Rs.200 crores plus, in terms of completion of the ongoing projects.

Anshuman Atri: Last question is on demand. So, how is being the demand panning out in different product categories for FY18 after what we have seen improvement, say after demonetization and when will the growth be back to its earlier levels?

R B Kabra: See demand in terms of faucets that we mentioned in the last call that the faucet growth in the whole year has been extremely good. The faucet growth is around 25% and we are number 3 manufacturer in the country now for faucets. For sanitary ware the growth this year has been around 8%. This includes the mix of volume and the conversion of the product from low value added to high value added products. So that is the sanitary ware. Normally sanitary ware grows anywhere between 12% to15% and from last 2 years the growth has been subdued because we have been more concentrating on high value products than the low-end products. So, that is why the growth in terms of that segment is little, the lower segment is little lower and the faucet is growing as per our expectation and I think in next 18 months we should be number 2 player in the country. So that is how it is. The consumer product division the growth as Mr. Sikka just mentioned for last 2 years has been more than 100%. The kitchen business is growing, the geysers are growing, the water coolers which were trial launch last year are giving a very good growth even in this last Q4 also. So, I think that product segment will still grow around the same kind of a growth rates which you have been talking of and going forward we see that yes, the real estate market should improve as per the new legislations which have come and now the builder should be moving forward to complete the projects in time because of the new legislation that they have to complete the projects in time and handover the projects. And the sanitary ware is purchased and fitted at the last when the project is ready to be delivered. So, we expect now that there should be pickup in the market. Last quarter Q4 the institutional segment has not grown at all, actually it has de-grown. It is only retail which has been growing and keeping our number up. So now we expect that even going forward the institutional segment should also grow.

Anshuman Atri: This 25 and 8 is value terms?

R B Kabra: Yes.

Moderator: Thank you and next question is from the line of Prashant Kutty from Sundaram Mutual Fund. Please go ahead

Prashant Kutty: if you could tell us what are the growth rates for faucets and sanitary ware in the 4th quarter?

R B Kabra: If quarter specifically, we are not reporting.

Sandeep Sikka: I think Prashant, we have given a broad guidance. We have been giving broad guidance's that what is the percentage share of faucets, so for the year we can say that faucets constituted around 29% of the overall portfolio of the building product division.

Prashant Kutty: Sir, just moving on to the consumer product segment, if you could tell us to what are the kind of spends that we are looking at as well as next year is concerned because right now we are looking at about Rs.120 odd crores of revenue. And sorry for just heard the comment you said you are looking at a similar kind of a growth rate in the next year as well on consumer products, so are you talking about the 100% growth rate in consumer products? I am sorry if just heard this wrong.

Sandeep Sikka: Yes, the thing is it is difficult to project the future but internally. We are trying to say that we should be able to demonstrate the similar level of growth. But market has number of uncertainties attached and definitely this year target was also higher but due to the demonetization and other things we lost part of the turnover. But we feel that by Q4 of the next financial year, I think, we should get the EBITDA positive around in that way, so will endeavor to be EBITDA positive. Although the differences may come in terms of higher spending in terms of advertisements or investments which we do towards the development of the newer brands and other things.

Prashant Kutty: Just again taking this back, again in this year are we again looking at this distribution expansion as the consumer product is concerned or are we looking at adding some more new products as well, in the consumer segment?

Sandeep Sikka: So, now we have kitchen appliances, we have water heaters, we have air coolers, air purifiers, water purifiers these are the main items. So, the focus right now is to develop these items and build them up. So, we have got good success on the kitchen item, we have good success on the water heater side. So, this year focus will be more on further growth of these segments and also the water purifier, which we launched in the month of January 17, February 17, the focus is to further nurture that and essentially considering the fact that water purifier is on the Moonbow brand. So, we may have to spend little bit on the advertisement to develop the brand and bring the product up in the market.

Prashant Kutty: I am sorry, just said that what is the kind of spends that we have looking at as per as this year is concerned on consumer products?

Sandeep Sikka: So last year we had given a guidance that the total spend in the next 12 to 18 months should be somewhere around Rs.25 crores to -30 crores. Of which Rs.24 crores we have said is spent last year and we think that another Rs.10 crores – 15 crores may be required this year, in terms of bringing this business to the full line and if we are able to grow between let's say 70% to 100% range, then ideally, we are fairly, we got a fair strength in the business then to move forward.

Prashant Kutty: And a typically assumption over here is that consumer products would have a gross margin of about 25% to 30% is that is the right assumption?

Sandeep Sikka: We try to bench mark our gross margins about 30% but certain products one or two products may be below, but on an overall kitty basis we try to benchmark about 30%.

Prashant Kutty: just one bit on retail what is the full year losses for retail at the PAT level?

Sandeep Sikka: We have disclosed the EBIT losses.

Prashant Kutty: I know the EBIT number, just ask you about the PAT loss.

Sandeep Sikka: We do not, I think we will stick with what we have disclose at the part of the segmental reporting. So, we had a total EBIT level loss, around Rs.14.81 crores so it covers a depreciation also.

Prashant Kutty: And just one last that you actually just mention in the notes that you are probably setup a committee to evaluate this potential restructuring, if you can just speak a little bit of this side?

Sandeep Sikka: So this is, board had discussed few options that how should we grow going forward, how should we unlock the value. So there is nothing concrete today. It is just that board has constituted a committee so that committee can work around and see what are the various options available and if any of the options work through take it back to the board and once it is done then appropriate disclosures will be made.

Prashant Kutty: Sir, just last one bit from my end. The accumulate losses the tax reversal which is there that is expected to come up in FY18 right, of the retail business?

Sandeep Sikka: Yes, now this due as we have taken the effect of the scheme and there were some losses in the retail undertaking which has now is part of HSIL Limited. So, we will have to revise the tax returns and we feel we will have a refund of Rs.50 crores plus once we resubmit our income tax returns.

Moderator: Thank you. Our next question is from the line of Nehal Shah from ICICI Securities. Please go ahead

Nehal Shah: Sir a couple of things, one on the packaging side. So, what are we seeing in terms of visibility, where are we heading in terms of margins, if you can throw some light on it?

Sandeep Sikka: So, on the packaging side I think there are number of factors which have affected us in Q4. Now if you see the overall trending in the last 4 quarters. So, we had very good first 2 quarters wherein we were seeing around 10% growth on the glass side and but then all of a sudden, we got hit by the demonetization and in Q4 number of events have happened like recent Hon'ble Supreme Court directions to close all liquor vends across the national highways. So, this has given a temporary flip downwards to the demand and we lost turnover of around Rs.50 crores if you refer on Q4. Generally, in this business we operate with an EBITDA margin of around 19% to 20% and so that also resulted in loss of absolute margin and also on the other side the soft drink industry also demand also melted away little bit. So, due to the product mix we had to off load more on the liquor side. So, it is a combination of the lower demand and also the combination of the change in the product mix. In terms of the market guidance, I cannot say that it is bullish right now but I can say it is, we are just trying to work around that if you can match the numbers for the last year on an apple-to-apple growth but market looks difficult today.

Nehal Shah: So, any sense for next couple of years in terms of the growth we are looking at?

Sandeep Sikka: I think commenting on next number of year's is difficult. We are just trying to see quarter-to-quarter first of all. So, that we can load the plant fully and right now the loading on the plant is not that full. So, I think commenting on long term will not be that advisable from our side.

Nehal Shah: So, are we looking to reopen a fourth furnace then?

R B Kabra: Not really, not currently because as you mention that the current demand itself is low we are not able to sell even the production of three furnaces. Yes, we repaired the fourth furnace because the demand was very bullish in the H1. So, in quarter 3 and 4 we repaired the fourth furnace which we thought we will be required to light up in this quarter because normally quarter 3 and quarter 4 remains better than the H1 in the glass business. But this time because of the various reasons as Mr. Sikka just mentioned the demand is subdued, so we have not lit up the furnace. and the current capacity utilization for the three furnaces is around 83%-84% and so, till we reach around 90%, 92%, 93% we will not be lighting up the 4^{th} furnace. So, I think it is now therefore another 4, 5, 6 months because quarter 2 is not really good because there is a monsoon and demand for beer and demand for soft drink goes down during this period and which again start picking up sometime in September-October, October-November basically. So, I think the lighting up has been postponed at least for 4-5 months and by that time will see how the market improves.

Nehal Shah: Sir, the final question would be on GST, so how would it impact the sanitary ware and faucets segment in particular going forward?

R B Kabra: So, sanitary ware the rates has been 28%, which is more or less the current rates with excise and VAT put together in most of the states, the VAT is anywhere between 12.5% to 15%. We average out this is more or less around 27%-28%. But the faucet, the GST rates are 18%. So, there going forward there will be advantage, in terms of pricing going little down for the customers okay and now coming back to the input, yes, the 2% CST which was currently the cost for all input purchases or the trading goods purchases because CST, the credit is not allowed. Now going forward to GST, 100% credit will be allowed. So, I think to that extent, to the extent of 2% on the purchase goods are domestically sourced as well as the raw material there will be advantage of 2% in terms of the cost.

Nehal Shah: Do you see, do you expect faucet growth to further increase considering that the end consumer prices likely to go down which will …

R B Kabra: We are positioning around similar kind of growth 25%-30% even this year.

Moderator: Thank you. Our next question is from the line of Siddharth Rajpurohit from JHP Securities. Please go ahead.

Siddharth Rajpurohit: My question is more on the sanitary ware side. So, are we will be looking at some structural changes with respect to demand because if you look at the HSIL focusing more on the premium products but with respect to volume growth and lot of volume growth is probably more coming in because of the affordable housing in the lower end. So, how you are looking at the things from your end?

R B Kabra: What we have recently done is that under one of our brand which is Benelave, we have launched the low end sanitary ware with 100% outsource, which is not manufactured by us and by selling sanitary ware under that brand, we will be targeting those affordable housing. So, your assessment is correct that Hindware yes, with the Hindware and Hindware Italian, Hindware Art brand we will not be able to get that kind of business which I think I will be mentioning in last 2-3 calls that the Swachh Bharat thing, we read that so many toilets have been built but we hardly got any order, except for few thousand pieces which were also purchased by corporates who build toilets under their CSR scheme and the corporate people they like standard and the branded materials and they have been buying from us for their offices, for their residence they bought from us. Rest of the business has not come to us because our prices were not competitive for that segment. So, similarly going forward we realized this opportunity and under brand Benelave, we by outsourcing this material from the small-scale manufacturer, we will be pitching in for that particular segment of affordable housing.

Siddharth Rajpurohit: So, in extension this very question, so would it be fair to understand that now we are looking at opportunities at both the spectrum. So, will there be what kind of growth you are expecting in the sanitary ware itself because I think if we compare on a year-to-year basis then this is the 8% spoke about purely on the value terms. So, what would be the volume growth if you can just share some detail on that if it is possible?

R B Kabra: Volume growth we have been not talking about last 2-3 years now and since we do not disclose **it** earlier we were disclosing this in balance sheet, so we were happy to share it but now we are not doing it,.

Moderator: Thank you. Our next question is from the line of Jaspreet Singh Arora from Systematix Shares. Please go ahead.

Jaspreet Singh Arora: Just on the margin pressure on the building products side both on a full year basis as well as quarter, quarter again looking it from a Y-o-Y perspective the 1.5% dip. So, what could be the possible reasons for this and what is your outlook?

R B Kabra: This is largely because of the fuel prices going up Jaspreet compared to last year, we talk of like natural gas pricing and LPG pricing which has they were very low and the last Q4 of last year and from the second quarter of this financial year these prices started going up and because of this largely this is the impact of power and fuel prices.

Sandeep Sikka: And also due to the fact that the growth in the faucet business is higher. So, on the percentage margin it gives sort of an illusion with the percentage margins are shrinking. So, that we have discussed number of times.

Jaspreet Singh Arora: So, from the high number of 21% we are about 13% at PBIT margins. Do you think this could be the bottom or do you think the pressure would, may continue for some more time and given that the growth has also not as great as it was in the recent past and the limited price hike. What is your future in the margins sir, if you could help us understand?

R B Kabra: Jaspreet, I will answer your question in 2 parts. When you talk of percentage that Mr. Sikka, just mentioned I have been telling that the EBITDA margins or the EBIT margins on faucet in terms of percentage is lower in comparison to sanitary ware But at ROCE level they match because the capital turnover ratio for sanitary ware is anywhere between 1 to 1.25 whereas the faucet it is 2 to 2.25, okay. So, suppose I sell a sanitary ware of Rs.100 crores and I sell faucets of Rs.100 crores, the absolute amount in terms of faucet will be lower if I compare on the sales. So, the percentage that is why because the share of faucet has been growing higher in the sales as you mentioned that for last 2 year faucets has been growing more than 25%-30%. So, this is an illusion that the percentage is coming down. It is not that the sanitary ware margin is come down from 21% to 13% EBIT level that is not the case. So, the percentage falls because of the power and fuel going up by 1.5% and then the ratio of faucets going up. Otherwise, the sanitary ware margins are protected.

Jaspreet Singh Arora: And on the retail business, any change in the view that in terms of store additions or cut downs or we broadly look to consolidate as earlier?

Sandeep Sikka: We may set up few more stores because we have cut down stores in last two years, the stores which were not performing. And the business has the turnover of around Rs.96 crores-97 crores and although we have a loss still on this business but we are just trying to evaluate. So, we may come up with the plans to open few new stores may be smaller store at a lower cost of development, so that just test those stores and if profitable then we can ramp it up.

Moderator: Thank you. Our next question is from the line of Sunil Kothari from Unique Investment. Please go ahead.

Sunil Kothari: Sir, can you little bit elaborate on this strategic initiative which we are planning, may not be commitment or some very clear guidelines but what is thought process to do this, I mean 3-5 years back we promised to divide this into one is packaging division, one is that is building products. So please, if you can little bit more on this?

Sandeep Sikka: So, as I told you initially there is nothing concrete. I appreciate the question which you were asking. So, until and unless anything is firmed up it is difficult to talk just that Board had discussions and they formed the committee, now committee will explore. Historically, I think we never promised anything that we will do anything. I think, although market interprets in its own manner but from my side, I can say that Board or company never promise that they will do something. So, this is just an evaluation by the committee of the Directors, which has been appointed by the Board of Directors. So, they will evaluate over a period of time, then come back to the Board and if anything works out then we will make proper disclosure and then definitely will let you know at that time.

Sunil Kothari: And sir, next question is this retail business, it has fallen substantial in latest quarter, just less than 1 crores. So still we assume this we have curtailed the loss which we were trying to do since last so many quarters?

Sandeep Sikka: Not exactly to be very frank but these losses also include certain mark-to-market gains also on account of the import material and other elements. But I think, our objective is that next year we should substantially reduce the loss that is our internal target, with the growth or the turnover we want to just turnaround this business but making a commitment that will go off, it is difficult as of now but as the quarter evolves I think we can talk more about it.

Sunil Kothari: And sir last question is just broadly because of this now GST rates are already open and we have 3-4 different segments, so would you like to comment something on how you see over a year or two, what type of changes or what type of benefits because of this structural change from unorganized to organized sector of the business?

Sandeep Sikka: So on a broader thing we feel that we should get some advantage on the sanitary ware side because now most of the players which were operating out of Morbi at a lower VAT rates and other things may get some pressure. And but it is very difficult to judge the market, especially the Indian market in a short run. The rates have been disclosed on 18th of May 2017. So, as Mr. Kabra has stated that our sanitary ware fallen under 28%, faucet is around 18%. So, we see opportunity on both the sides with the GST coming in and this should happen transforming the unorganized trade which were not paying the duties appropriately, so that the whole distribution shifts to a more formal transparent manner and that was the objective of GST and if that happens we should be the gainer out of it.

Sunil Kothari: Sir, consumer products division we see any strategy changing because of this GST because now at present we are outsourcing completely?

Sandeep Sikka: Yes, thing is there is a subset. We were out sourcing and we were importing. So, there was an element of CVD, there was element of excise duty which till now was the cost. And as we move forward, in consumer there are wide ranges because some of the products are 18%, some of the products at 28%. So, we are still trying to create a balance but there we should get at least some items which are 18%. We may have some advantage but 28% is more or less in line with structure rate, may be percentage here and there adjustment may be required in terms of how we protect our margins and how distributors protect their margins.

Sunil Kothari: Sir, in terms of competitiveness, will it be comfortable to have outsourcing rather than manufacturing or how is outsourcing …

Sandeep Sikka: It is not plain vanilla mathematics, it is subset of various factors. Intangibles, quality, the assurance on the distribution, your ability to develop newer products, and new designs to the market. So, it is not sacrosanct that if you work on an entire outsourcing model that will be of an advantage. So, ideally the most appropriate is the mix of both of them and that is how we also intent to move forward.

Moderator: Thank you. Our next question is from the line of Dimple Kotak of SKS Capital & Research. Please go ahead.

Dimple Kotak: Sir, what is the CAPEX which are planning this year?

Sandeep Sikka: So, the CAPEX is in 2 or 3 buckets. One is the bucket for pipes, caps and closure projects which we started way back in 2015. So, there will be some expenditure there. Then there is a normal CAPEX, so we feel that the overall CAPEX during financial year 2017-2018 should be in a range of Rs.200 crores-225 crores on an overall basis but it does not mean this is a new CAPEX.

It is the capital expenditure which was historically contracted and we are just completing those projects in phases.

R B Kabra: And this also includes the CAPEX of around Rs. 40 crores for expanding faucet capacity by 50%. The current capacity is around 2.5 million pieces and we would be adding another capacity of 1.2 million pieces and the Rs.40 crores CAPEX for that. So, that may be spent may be partly this year and partly next year but we have budgeted this year.

Dimple Kotak: And sir, as you said that your faucet division is growing faster than the sanitary ware. So in future also we are looking at this kind of mix at least for FY18. So, then do you think some margins will be lower than the 21% which were earlier because of the product mix?

R B Kabra: See, when you talk of overall margin comes of percentage yes it may fall by a percent or so because the sanitary ware business is very large in comparative to faucet business in terms of absolute numbers. So going forward yes, if the sanitary ware grows 12%-15% and faucet grows by 25%-30% as budgeted, then in terms of percentage it may fall but the absolute amount will grow.

Dimple Kotak: And sir 8% we had a sanitary ware growth this year, so what is the kind of growth we are looking at for next year?

R B Kabra: Anywhere around 12% to 15% that is what I just mentioned.

Dimple Kotak: And sir I missed on the trial production you said from August, I just missed on that part?

R B Kabra: The trial production with the two projects which are going on, Mr. Sikka just mentioned the trial production for the caps and closure has started in April 17 sometime and the trial production for the pipe is going to start sometime in August 17.

Dimple Kotak: And how much revenue will they add at a full capacity?

Sandeep Sikka: Pipes I think when it is fully with 30,000 tonnes capacity with all the machines installed, it should achieve the turnover should be around Rs.400 crores and caps and closure anything between Rs.100 crores - 120 crores.

Dimple Kotak: Sir, for caps and closures, we are looking at starting the commercial production in first half of this year?

Sandeep Sikka: In quarter 2 of this financial year.

Dimple Kotak: And sir overall, if you can just throw some light on overall what do you see how the year panning out?

Sandeep Sikka: This is the year of consolidation to be very frank. All the actions which we did in last two years, various analysts had issues on capital allocation and other things. So, we have lived with this for last two years and this is the year wherein all the projects are starting. So, going forward we feel that all the initiatives which have been carried on since 2015 in terms of the development of the consumer business, the development of the pipe business, the development of the caps and closure business, the growth in the faucet business, the sanitary ware brand wise segmentation all these should start giving effect from 2018-2019 onwards. So, this is the statement, I think we have been telling everybody that 2017-2018 you will see number of new projects starting. So, this is a year of consolidation.

Dimple Kotak: And sir finally just one question in consumer business. Will it turn positive from Q4 FY18?

Sandeep Sikka: We expect that from Q4 onwards it should get into things. But if we have to spend more on advertisement then it may be slightly below the breakeven.

Moderator: Thank you. Our next question is from the line of Samar Sarda from Kotak Securities. Please go ahead.

Samar Sarda: I had a few questions starting from the BPD business now like we mentioned the comments on RERA. Now what we see is like supply is already coming down and institutional supply after RERA coming in will come down. Probably there might be a little spike where developers might hurry to complete projects but given the market conditions and legislations, supply will come down. So with this, how do we pan out our institutional focus with the overall supply and the market coming down?

R B Kabra: As I mentioned, the sanitary ware is the last item which is fitted when the project gets near completion or ready to be delivered. Because every thing else is done before, the piping, the tiling, the sanitary ware and faucet is the last item to be fitted. And there is so much huge inventory in the country currently of the project which are WIP, so we think that next 2-3 years even if the new projects are not launched, the current projects completed it is going to be matter of 2-3 years and thereafter we think that lot of new initiatives with the government, the smart cities and the housing for all which I just mentioned that we have launched a low-end branded sanitary ware to take share in that. And similarly, urbanization is not only that smart cities we will take care of whatever urbanization taking place more and more people are moving to urban areas with job, for education, for other things and I have been telling that we are Rs.130 crores people even 1% population moves every year to cities, 1 crores people will be moving to cities and they have to be housed somewhere. So new starts could be delayed for sometime but I think for next 2-3 years the WIP of the uncompleted inventories of the builder is good enough for us to continue to sell to the projects.

Samar Sarda: And you did mention about Benelave and like the focus on affordable housing.

R B Kabra: Yes, so that is the Benelave brand which there we will be outsourcing the good quality but low-end sanitary ware and will be trading in that.

Samar Sarda: Kabra Ji, did we do any business FY17 in Benelave on this segment and what could be the idea, if you could get some idea for FY18?

R B Kabra: Yes, we did around Rs. 30 crores of sanitary ware business in Benelave in the financial year.

Samar Sarda: And the CAPEX like the point 0.4 million pieces addition, is that already happened or like that will happen sometime in FY18 now?

R B Kabra: 0.4 million pieces that CAPEX is already over. Small amount is left which will be over by end of this June 17. So that is all done. The Rs. 40 crores what I mentioned additional was for the enhancing capacity of the faucet plant at Kaharani.

Samar Sarda: So the 3.8 million pieces like before this?

R B Kabra: It is now 4.2 million pieces.

Samar Sarda: So what was the utilization of this 3.8 for FY17?

R B Kabra: Around 92% to 93%.

Samar Sarda: And we have started commercial productions for the entire 4.2 now, like an incremental 0.4 also.

R B Kabra: The furnace, actually the casting and everything is already ready. The furnace, which is the important part where the sanitary ware is fired, the trial runs are going on that furnace and once that stabilizes, actually it takes around a month or so to stabilize because we have to adjust the temperature for refire and for one fire and few trials are run on the different product mix to make sure as the warranty from the kiln supplier is that they have to ensure that we get a better efficiencies in terms of good pieces coming out of the furnace than the existing one. So those trials are going on, maybe by end of June 17 that will be completed.

Samar Sarda: One last question on the segment, are we looking or will we be looking to increase export for FY18-FY19 versus what is happen in the last 2-3 years?

R B Kabra: Yes, we have been looking for the export but today the problem with export is the sanitary ware is bulky cargo and both our plants are not near to the port. So we have to spend around Rs. 1 lakh even for taking a container from plant to the port. So, that makes our product less competitive for the OEM sourcing people but yes, I think we are seriously looking at increasing the faucet export. So, if that happens because that is not a voluminous cargo when you talk of freight in terms of value as a percentage is substantially lower because faucet is a high value product, brass being the raw material for that, so that possibility we are exploring.

Samar Sarda: Just a couple of small questions on pipes and caps given that the commercial production will start later this year for pipes and like second quarter for caps. At what revenue will we do operating breakeven for both these businesses?

Sandeep Sikka: I think caps, we should breakeven within the first year of operations. And on the pipes, we may enter the second year with the turn over exceeding around Rs.120 crores-130 crores.

Samar Sarda: And you also mention that you might increase some ad spends for the water purifier business in the CPD so, like few comments in the last conference call, so like around 200 crores you might breakeven in the CPD business with the ad spend increasing you did mention about 4th quarter you might breakeven but if you could just quantify on the revenue side also.

Sandeep Sikka: I think in the last conference call we told that we should be touching a turnover of somewhere around Rs.225 crores to 250 crores and at that we should breakeven. But the market is evolving and if you feel that there is a need to spend more towards the stabilization of the brand and the product for then we have to do that.

Moderator: Thank you and next question is from the line of Girisha Saraf of Ambit Capital. Please go ahead.

Girisha Saraf: Could you please give us a little more light as to what is our strategies for the pipes business, have you already started tying up with someone in the retail network and just a little sense on the pricing and product launch strategy please.

R B Kabra: Ma'am the pipe is sold through our distributor network, directly it is not sold to the retail by the manufacturers.

Girisha Saraf: So have started building on that distribution network already?

R B Kabra: So with the distribution network, our people have already started speaking to the large distributors which are near to the plant because the plant is coming up near Hyderabad in Telangana. We will start distributing into the nearby areas. So that it is freight competitive and I think we have already spoken to few distributors and they are quite willing. Because good thing what we have done is that normally when people launch the pipes they do not launch with the fittings and without the fittings the product basket is not complete and dealers and the retailer is not ready to keep your products. But simultaneously we are developing moulds for around 620 fittings. That will also go into production as soon as the pipe goes into the production. So we have a complete product basket and we do not foresee any problem because we are good brand, we will be giving good quality products including the complete product range. So, I do not foresee any problem in terms of selling.

Girisha Saraf: So when it launch, all of these products at once and not one by one that is what you are saying?

R B Kabra: So, when we talk of the launch product yes, fittings we will have to go like we are launching pipes starting from 0.5 inch to 4 inches. So that might take may be a month or so to put dies, try everything because we are not putting so many extruders that we will start manufacturing everything from one machine. So may be in a month's time because all fittings are manufactured on the injection molding machines and pipes are manufactured on extruder. So in a month's time the complete range should be there.

Girisha Saraf: And sir secondly another question is, do you see a lot of increase in competition in the premium sanitary ware segment?

R B Kabra: Yes, that has always been there because all imported brands are there in the country. 1991 was the first year when American Standard launched their large range of products in India.

Girisha Saraf: Yes sir, because we see a lot more people like even brands like Toto, they are getting a lot more aggressive in the Indian market because we position our product in the premium segment as well. What is our strategy with respect to such increase in premium competition?

R B Kabra: So now you all know that we have the various brands to address the customer needs at the various price points. We have Hindware, we have Hindware Art, we have Hindware Italian collection and few years, 4 years ago we launched our super premium brand which is Queo and now about the affordable housing we have launched another brand called Benelave, as I just mentioned. So, we have different brands to address the various customer requirements at the different price points and today we have the largest product basket under each category. So that we give lot of choice to the customer to select, it is not that at a particular price point I have only one kind of wall mounting at a Rs. 100 – Rs. 200 difference people can have 4 to 5 to 8 models in a particular brand. So the product offering is the largest from us and since we cater from the smallest to the highest price point, dealer find it more reasonable for them to keep our brand and sell other brand because then they can service any kind of customer and we being the oldest in the country, we have the largest retail distribution network which is helping of course, in any way.

Girisha Saraf: So, the kind of advertisement strategy that we have for these various brands and the various segments would be a lot different, if I am correct?

R B Kabra: Yes, that is right.

Moderator: Thank you and next question is from the line of Harsh Dhanuka from Ncubate Capital. Please go ahead.

Harsh Dhanuka: So, my query is more on the water purifier segments, the launch of the new brand. So, what is the kind of the distribution network that we are planning to grow in the coming year and what is the stage that we have reach in terms of the distribution network and the product placement kind of things?

Sandeep Sikka: If you see on the consumer product side, we already have retail touch points exceeding around 4,000 retail touch points in India. And essentially all these counters are selling all these consumer durables only. So we have a fair level of distribution to start with and definitely this year onwards we are building more towards the distribution as the product portfolio has broadly stabilized in terms of Kitchen hoods and hobs, water heaters, water coolers or air coolers and then water purifier. So we has been working on this for last 2 years and we have disclosed over the time that the distribution growth is happening also in this segment and we feel confident that we will be able to address that issue.

R B Kabra: I will add to it that our internal target is the next 2 years the retail touch point should be increased to 10,000 from 4,000.

Harsh Dhanuka: Any new launches in terms of the premium segment within the water purifier also planned?

Sandeep Sikka: No, I think very recently did few models in the month of February 17. We will consolidate that, I think only may be in Q3-Q4 we may look at new models but right now not on the table right now.

Harsh Dhanuka: And one thing in terms of how do you see the growth for the segment per se in terms of with new players coming in, every branded player launching this water purifiers as the new offerings, so how do you see the competition, competitive intensity and the growth for the segment for the coming year?

Sandeep Sikka: Market has always been competitive you see on the consumer product side. So, whatever product you may talk of, let's say you talk of kitchen hoods and hobs, even water heaters, even air coolers. So we have been able to demonstrate historically in last 2 years that we have ability to grow within these segments, especially when we see that with the almost 2- 2.5 years operations, we now have some 5% to 6% share in a chimney market which is highly segmented, all these markets are very highly segmented. We have around 3% to 4% market share on the water heaters within less than 2 years of operation. So similarly, we feel that on water purifier's side also we should be able to imbibe distribution and strategy and we have a good market share in next 2 years.

Moderator: Thank you. The next question is from the line of Kinjal Jagani of M Savla consultancy. Please go ahead.

Kinjal Jagani: Can you please give some color on the rationale behind demerging that only retail business from our wholly-owned subsidiary and merging it with us whereas what are the other business activity is still left in that wholly-owned subsidiary. And what is the kind of synergy that we are expecting out of it?

Sandeep Sikka: So basically, if you see there were two undertakings in the subsidiary – we used to do 2 businesses. One was the sales, which we used to do through the retail shops. So, we had these 14 stores. Then other was direct OEM business like we used to set up various offices, which we used to call as an institutional business. Institutional business was small around 2% to 3% of our turnover and since in the bottom line if you see that subsidiary was losing money and on the top, we were paying full taxes. So, it would have been more efficient if we club it together, so other than that they had their own paraphernalia of the whole administration of offices and other things. So, once they are now part of HSIL in the retail undertaking they have an advantage of all the support staff services which are there and they should be able to optimize their cost as we move forward.

Kinjal Jagani: So, there is no further chance of merging it with our main company?

Sandeep Sikka: That institutional business left over will operate in the subsidiary itself.

Kinjal Jagani: It will remain independent company?

Sandeep Sikka: Yes, in the wholly-owned subsidiary.

Moderator: Our next question is from the line of Sunil Kothari from Unique Investments. Please go ahead**.**

Sunil Kothari: Sir, normally this water purifier business is always it requires so much of service-oriented activity, I mean every now and then every quarter or every half year serviceman comes and clean and do so many things. So, are we comfortable with this type of activity and we have set up enough for this service providing after this when you sell the product?

Sandeep Sikka: Yes, your point is very right. In fact, what we are trying to do is that we have communicated this over last many conference calls that on the consumer side we are trying to develop a new distribution. When we do a distribution services and after sales services is an integrated part of the distribution. So, when we see products like kitchen appliances, water heaters the service level required in these products may be slightly lower as compared to water purifiers. So, water purifier everybody will have to give an AMC for maintenance of the water purifiers. So, we are aware about it and that is why we have invested heavily in terms of creating that service structure also. So, we have more than, I think 150 people servicing all across the country now and they provide services right from installation as well as after sales service. So, that is the whole infrastructure we have created both in terms of distribution as well as the service.

Moderator: Ladies and gentlemen, that was the last question. I now hand the floor back to Mr. Dhaval Mehta for closing comments. Over to you, sir.

Dhaval Mehta: Thanks everyone for participating on the call. Now I would like to hand over the call to Mr. Sikka, for his closing comments. Over to you, sir.

Sandeep Sikka: I think Mr. Kabra will give the closing comments.

R. B. Kabra: Thank you everyone, for joining us and I hope that we have been able to answer your questions to your satisfaction and as Mr. Sikka just mentioned and we spoke that going forward we are very hopeful that the growth rate should go up in all the businesses and thank you very much once again.

Moderator: Thank you members of the management. Ladies and gentlemen, on behalf of Emkay Global Financial Services, that concludes this conference. Thank you for joining us and you may now disconnect your lines.