"HSIL Limited Q4 FY2016 Earnings Conference Call"

May 25, 2016

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Moderator: Ladies and gentlemen good day and welcome to the 4Q FY 2016 Earning Conference 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 phone. Please note this conference is being recorded. I would now like to hand the conference over to Mr. Prashant Kutty, Research Analyst, Emkay Global Financial Services. Thank you and over to you, Mr. Kutty!

Prashant Kutty: Good evening everyone. I would like to welcome the management of HSIL and thank them for giving us the opportunity to host this call. I would now like to hand over the call to Mr. Sikka for his opening remarks.

Sandeep Sikka: Thank you Prashant. Good afternoon to all of you to all the participants who have come. To start, we would like to refer to our disclaimer that is in the industry standard stated in our corporate presentation on our website. Key points in the statement include but not limited to all that stated in this conference call may be concerning our future growth prospects or the forward-looking statement within the meaning of the applicable securities, laws, and regulations and may involve a number of risks and uncertainties beyond the control of the company. That would differ materially from those stated in our forward-looking statement. We would request all to refer to disclaimers from our investor presentation on our website before making any decision on the basis of the conference call.

Now I would like to go into the results. I hope everybody would have got the copy of the results either by mailer which we have sent or it has been posted on to the stock exchange websites and also on our own company's website. HSIL as for the year ended March 31, 2016 achieved a total income from operations at 1944 Crores compared to the previous year's corresponding figures of 1857 Crores. This represents a growth of around 4.7%. The company operates through two business segments, the year-on-year sales growth of building product division and the packaging product division for the 12 months of operations is 10.15% and the packaging is negative 2.4% respectively.

The operating profit that is EBITDA for the 12 months of the operation is 338 Crores down from 345 Crores last year. The reasons we are disclosing subsequently but the overall EBITDA margins for the financial year for 2015-2016 is 17.4% as compared to last year 18.6%. The lower EBITDA and EBITDA margin during the year is on account of certain factors including higher marketing spends as compared to last year. As the company invested in promotion of brands using elite Bollywood stars.

Also during the year the company made growth plans for its consumer business, which now is being developed as a separate distribution vertical into the consumer market. The performance of the building product division includes the development cost related to the new consumer business, which has already built a footprint of around 225 distributors across India, and 4000 active sales touch points which the company intends to double in the next one year. The products launched under the consumer business like water heater, kitchen chimney, hoods & hobs, air purifier, air coolers, etc., have been well accepted by the market.

During the year ended March 31, 2016 the total sales attributable to consumer business is around 60 Crores as compared to previous year's sales of around 26 Crores and this is actually getting clubbed into the BPD division turnover. The EBIDTA level development cost which is an expense charged to BPD of this business during financial year 2015-2016 is around 16 Crores for the year. The packaging product division has during the year 2015-2016 demonstrated superior profit performance with EBIT growth of around 35% as compared to last year figures despite lower level of sales as I said above. Higher profit growth is attributable to cost reduction initiatives undertaken by the division coupled along with the lower fuel prices during the year.

Interest cost during the year has been lower at 38 Crores as compared to previous year figure of around 73 Crores. This is on account of low utilization of working capital limits and repayment of long-term debt amounting to Rs.240 Crores during the year.

So as we close the year the long-term debt and the total bank debt as on March 31, 2016 is 328 Crores which is long-term and 556 Crores is the total bank debt. The overall loan funding cost as on March 31, 2016 is 5.32% as compared to last year 5.85%. Company closed the year with a profit before tax of 185 Crores which is up 21.5% as compared to previous year profit before tax of 152 Crores and board of directors have proposed a dividend of 200% on the paid up capital which means a dividend of Rs.4 per share on a Rs.2 fully paid up share.

The Q4 results basically represent the balancing figure between the audited figures of the year as I said above and the published figures to the date as disclosed by the company for the results up to December 31, 2015. That is the broader sense of the overall results both in terms of turnover as well as EBITDA. I would request if any questions are there, we are ready to take up the questions now.

Moderator: Thank you very much. Ladies and gentlemen we will now begin the question and answer session. We have the first question from the line of Venkat Subramanium from Organic Capital. Please go ahead.

Venkat S: Thanks for taking my question. We have a consistent pretax loss of about over 20 to 25 Crores on the consolidation. I think they probably are coming from the subsidiaries. Can you give us a road forward on what to expect on this and why do we have recurring losses?

Sandeep Sikka: This is retail business. If you see the overall concept on which the company is working is to create an overall building solutions company and anything, which goes inside the house, we intend to cater to our customers in that range. So we were very strong till now into our sanitaryware or faucet, which is our bathroom and now our new initiatives, which is the consumer business is more focusing on the kitchen side. One of our subsidiaries, which is Evok, which is a company, called HHRPL, Hindware Home Retail Private Limited and they sell through a brand called Evok. They are focusing on the furniture and the other home furnishing part of the business, but what has happened is in retail till now the cost of maintaining the retail is very high although we are trying to optimize the thing, we are trying to push forward lower cost structure, lower rentals, we are trying to optimize the manpower cost and we have also cut down certain discount and increased our margins in that business in the last two to three months, but last year we still had a loss in this business and as we move forward we see that at least for one or two years this may continue till we reach a threshold of a turnover after which this entity can also start performing.

R.B. Kabra: I will add here is that we have taken a few initiatives in the last three to four months, to downsize the stores to save on the fixed cost of rent, we are also optimizing the manpower and also controlling the warehousing and logistic costs and we hope that going forward of course there will be losses in the coming financial year as well, but we expect that loss level should be reduced substantially provided the economy does well and we are able to see the growth in the sales as expected now.

Venkat S: Are we to understand that you need this current structure through the subsidiary of Evok for sustaining our building products division revenue?

R.B. Kabra: No.

Sandeep Sikka: I think the more important is, it is not that critical I am saying, but it is a strategic thing. So our core remains sanitaryware and faucets which is our building products and as I said, we are moving towards the consumer products business which will cater more to the kitchen and the other household goods, electrical goods and this entity is focusing just on the furniture and the home furnishing. So this has nothing to do with sanitaryware and the faucets.

Venkat S: Can you guide us as to what kind of losses that we need to provide for in the coming years? When you say you are going to optimize the sales you are also bringing down costs?

R.B. Kabra: We are expecting the reduction of loss around 35% to 40% in this coming year, which is 2016-2017 from the current levels and from the next year it should be breakeven at the EBITDA level?

Venkat S: Thanks.

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

Sunil Kothari: Thank you. Thank you for the opportunity. Sir, again my question is related to the subsidiary, which is related to furniture and home furnishing. Sir, is it possible or may be viable or feasible to hive of this business and not continue with this? Because what I am observing is last year or two, we are on the same similar topline. We have already eroded whole networth and we are not getting, and I do not know why? But any tax benefit of these losses also because we are paying almost more than 40% tax. So is there any timeline from where you will try to focus on your core strength rather than furniture and furnishing, just broadly please?

R.B. Kabra: As we just mentioned that there is no proposal of shutting down this business and as we just mentioned because we are quite hopeful that in the next two years, it should be breaking even at EBITDA levels and then we will see that how we can grow it profitably.

Sunil Kothari: Sir, you feel this is a promising opportunity for you in a longer term?

Sandeep Sikka: If you see furniture market in India it is a huge market, but predominantly it is just controlled through the unorganized sector, but there are a number of opportunities. People actually want a quality furniture and our initiative is focusing on that that we provide a good quality furniture to our customer, and also the hard furnishing and soft furnishing we call HDHF along with it. The real challenge of this industry is that retail footfall in very recent times in few of the places have not come up fully, and ultimately the cost structure and the revenue structure is trying to get an appropriate mix. So as Mr. Kabra said that in the last four months, we have taken certain initiatives in terms of our cost improvements, and reduction of discounts and giving better products to our customers definitely in retail if you see on the overall other players also in the market there is some stabilization time although I am not saying that we have not taken the time. The company has taken a substantial time here and the venture is already out now for seven to eight years, so definitely we want to revive this entire profitability in this business that is the thought on which we are working on it now.

Sunil Kothari: Sir, how many retail outlets at present? Last year I think it was 18?

R. B. Kabra: Currently the outlets are 16, two loss making outlets we have closed. This is like we thought that those outlets were making losses continuously and the revenues per square feet was not increasing so two of the stores have been closed so now currently 16 stores are operating. One more store will be closed during the year. Decision has been taken, but simultaneously what we are doing is that with this franchise route, we are increasing the customer touch points. Now we are not opening the company operated stores because the brand is now well established and we are differentiated at the customer level because we largely sell solid wood furniture. The other people are selling MDF and HDF furniture. We largely specialise in the solid wood furniture, which differentiates us from the other people in the organized segment in the retailing furniture. So with the franchise we have opened around 10 to 12 stores in the tier II towns, so the company operated stores are 16 currently which will go down to 15 sooner and currently we have 12 franchise points which may grow by another 10 or 15 in this coming current year.

Sunil Kothari: Sir this loss in segmental others from 14 Crores to 28 Crores that is mainly because this is related to Evok only?

Sandeep Sikka: Yes.

Sunil Kothari: Just last question is the building product segmental profitability has fallen substantially compared to year-on-year or may be previous quarter also. So the 16 Crores what you said related to this consumer business related that is the reason of this last quarter lower profit at segmental level?

Sandeep Sikka: Basically if you see on a segmental level building product division without considering any consumer product adjustment has made a sustainable margin which we have in a range of around 20%- 25%. Without the consumer product the building product is doing that business. Definitely consumer business is building up, we have strengthened our teams. As I have told you we have already established now 225 distributors across India and we are already selling through 4000 touch points, so you know the creation of this entire new distribution vertical to the market do have some costs. Technically, we cannot capitalize this because this is a yearly thing because money is going into salaries and also into the warehousing infrastructure and other things.

R.B. Kabra: Also brand building, we created a separated brand for the purification business, in the last call we mentioned that we have created a new brand called Moonbow and as you know that whenever you create a new brand initially for one or two years or three year period will be cost because people have to be made aware of the brand what we have launched?

Sunil Kothari: True. Sir, during last quarter this 315 Crores building product segmental revenue; how much is related to consumer business?

Sandeep Sikka: In Q4 it is around 13.5 Crores.

Sunil Kothari: It must have hurt this segmental profitability also?

Sandeep Sikka: Yes, because it has not reached that size and last year we did a full 59 to 60 Crores so next year I think it should reach good levels and around 150 Crores. At that time you know we may have started disclosing it separately so, I understand from the analysts point and from the market side, definitely that is why we have come up openly and saying that this is our turnover and this is our cost involved and this otherwise would have gone up.

Sunil Kothari: Thanks a lot.

Moderator: Thank you. The next question is from the line of Kaushak Poddar from KB Capital Market. Please go ahead.

Kaushak Poddar: Because of your focus on consumer business are you losing market share in the sanitary products?

Sandeep Sikka: It is not that we are losing the market share on the sanitaryware products and other things, because as we have been telling that the focus of the company is to move on a high end of the market because if you see HSIL is the only company which is present across the entire value chain and if you see our corporate presentation we have stated that we go from the bottom low brands, which is Benelave and Raasi to a very high end premium brand starting from Art, Italian and also Queo. So focus on the sanitaryware and the faucet does not get impacted by the consumer products because these are two separate sales vertical within the organization. So the head of the sales and head of the sales for sanitaryware and the head of the sales for consumer products they have a different team altogether.

Kaushak Poddar: In the last quarter, of the 315 Crores turnover for the building products probably you are saying 14 to 15 Crores belongs to this consumer business and for the segmental result out of 41.35 is it a negative for consumer products business?

R.B. Kabra: It is around 9 Crores negative of the consumer products.

Kaushak Poddar: So 50 Crores is the EBIT for 300 Crores turnover of building products, is it?

R.B. Kabra: Yes.

Kaushak Poddar: Secondly in case of the packaging products, how is the glass business doing?

Sandeep Sikka: This year I think glass has given one of the best performance if you try to see in the last four years of our performance although we are down in the revenues slightly around 2.5% but if you see the profit numbers so they are the best in the best of the industry and also best in terms of year-on-year EBIT growth is around 35%. This is predominantly attributable to the lowering of costs. We have improved the product mix also and we have been able to slightly improve our realization on account of product mix although there has not been a price hike, but more to do with the higher usage of petcoke and our ability to bring down the operational costs.

Kaushak Poddar: How do you see the packaging product business performing in this year, this current financial year?

Sandeep Sikka: I think the most critical factor till last year was the entire market had viewed that packaging will keep losing money as we go more forward as main chunk of debt was taken for the packaging division. Now if you see our debt profile major chunk on that has been paid up last year. We have paid up 240 Crores. This year's packaging product has given a good EBITDA and this is definitely before unallocable expenses around 190 Crores plus and as we move forward we feel that market on the liquor side is not that bullish, if you see. There are a number of instances wherein the state government restrictions and other things coming up but I can say that the unit has come out of woods in terms of overall cash planning, so they will keep generating the EBITDA and since that the repayment is lower as we move forward, so they would have some surplus cash going forward.

Kaushak Poddar: But do you see a similar EBIT in case of packaging division in this financial year?

R.B. Kabra: What I would like to add here is that most of you must be aware that we had four furnaces for our two glass plants and we shut down one furnace two years ago when there was an overcapacity in the industry. Currently we are only operating three furnaces. So the current capacity utilisation is more or less 95% to 96% run rate at the end of February or March 2016 so whatever growth of 3%, 4%, and 5% in volumes is expected from only by reducing the inventory. We have specified that we will light up the furnace which was shut for the last two years that we will see at the end of September 2016 as to whether we decide to light up this furnace this financial year or not and that will depend how the demand moves, because that furnace will be generating around 200 to 220 tonnes of glass per day, and if we have a guaranteed customers for 60% to 70% of the volume then only we will light up the furnace otherwise we will not light up the furnace because then it starts getting into the inventory and then the pressure for sale and there is a pricing pressure from the current customers so because of the current capacity utilization the volume growth may not be more than 4% to 5% as we are working on the product mix change there could be high single digit or lower double digit growth in terms of revenue in the coming year.

Kaushak Poddar: In terms of EBIT?

R.B. Kabra: EBIT this is a very healthy EBIT.

Sandeep Sikka: I think if you see the competition it is much better, so we do not expect any improvement on the margins as of now.

Kaushak Poddar: This huge cash generation, you will use it to pay off your debt or what you will do?

Sandeep Sikka: If you see we still have a total long-term debt which is around 328 Crores which is there on the balance sheet, so next year the payment is 125 Crores and the year ahead is another 125 Crores, the figures will change slightly on the foreign exchange and other things. So I think one year more focus is to be payoff the further debt and then we will see but definitely most of the analysts have asked on the sideline whether you will expand further on the glass or there is no decision as of now.

R.B. Kabra: We already have a furnace. So there is no need of capital expenditure. The only thing is if we decide to light up the furnace, whatever the lighting expenses for replacement of some refractories and repairing a few machines, because those are lying idle for two to three years that expense will be there otherwise we do not need a full expense of putting one furnace at Rs.400 to Rs.500 Crores because that furnace is already lying idle, which can be used and the capacity of that out of 1600 tonnes, 300 tonnes is idling which is around 25%, 22% so we do not need additional capacity for the next two to three years.

Kaushak Poddar: Understandable. In case of building products what is your expansion plan?

R.B. Kabra: With the expansion plans we have been mentioning that current capacity in both our two sanitary plant one at Bahadurgarh and one at Bibinagar is combined at 3.8 million pieces. Expansion is going on for 400000 pieces to take the capacity from 3.8 to 4.2 million. This was announced two years ago, but we went a little slow because real estate market was not as buoyant as we expected to be and the volume growths were not as per our budgets, but now the work is on and we expect this capacity to be on stream by end of this year.

Kaushak Poddar: And that should be sufficient to take care of the demand?

R.B. Kabra: It is sufficient to take care for two years because current capacity utilisation is again around 90% to 91% of the existing plants. So with 9% we are adding another 11%, so that should be good enough for next two to three years.

Kaushak Poddar: My last question you were planning to put up an export oriented plants in Gujarat some time probably last year or a year before you had announced. Are you going through with the plan?

R.B. Kabra: That was not really export oriented. That was we were planning another sanitaryware plant in the western part of the country because we have plant in south, we have plant in north, and we thought that we will be putting up a sanitaryware plant, but as I just mentioned the markets are not good enough currently the plan is on hold currently.

Kaushak Poddar: Thank you.

Moderator: Thank you. The next question is from the line of Gunjan Prithyani from JP Morgan. Please go ahead.

Gunjan Prithyani: Thanks for taking my questions. Just two questions; firstly on your building product division, if I adjust for the consumer topline, the growth in the building core sanitary faucet would have been in low single digit. So how are you looking at growth in this business going into FY2017? Have you seen any improvement in the demand per se and also on the margin front not factoring in the investments that you are doing for the consumer business do you see any improvement from these 20% levels that you have right now?

Sandeep Sikka: Our first focus which is there, we have been telling historically on conference calls is strategically if you see the company has not reduced our margins, so as I told that on an overall basis our BPD margins without consumer products is still about 20% for the year ending last year so we are not compromising on our margins to eat away the market right now, but definitely our thoughts and our strategy is to focus on the high end growth and which actually is our composition. Now if you see our premium composition to a normal composition products we sell around 55% plus mix of premium brands and we keep focusing on that. As Mr. Kabra already stated that the real estate sector right now is not in a good state, and it is moving slow, but our focus is again on the retailing and we do not promote our products predominantly into the project side and there our mix is 85:15. Our 85% is still focused on the retail as we see on the last quarter and 15% going towards the projects. So we are focused in terms of brand segmentation, we are focused in terms of creating a niche in terms of giving a premium product to our customers. We are focused on retaining our margins and focusing more on retail sales and the brand creation as and when the project sales.

R.B. Kabra: One thing I would like to add here is which I have been telling since we put up this faucet plant that the margins in faucet plant in terms of percentage to sale in the faucet business is not as high as in sanitaryware, but at ROCE level these are same because the EBITDA levels may be 25% of sanitaryware products but the assets turnover is double of capital invested which is 1:1.1 or 1.2 at best in sanitaryware, it is 2:2.25 in the faucets. So at ROCE level they match, but percentage because when the faucet business is growing, we have put up a large capacity and faucet used to be 6% to 7%, which is now 24% of the revenue of the building products division so the percentage might look down, but absolute will keep increasing. That is what we are trying to clarify also.

Gunjan Prithyani: The concern mainly would be on when the volume or the value growth comes back in this core business because if I really adjust for the consumer business topline the business is growing only at about low single digit. So is there any visibility that that FY2017 could be meaningfully better than this number in terms of growth. Of course margins I do understand that 20% is a fairly decent margin profile?

Sandeep Sikka: This depends on the market. Company is taking all necessary steps to promote. As I said focus on a brand segmentation is our key, because if we move on the bottom side of the market wherein actually the turnover can be built, if we start selling the low end of the market, we can build a turnover then what is going to happen in the margin is going to take a hit. So the competition at the bottom of the pyramid is too high. The company wants to create a premiumness in the brand, when a consumer buy today Hindware Arts and Italian he feels proud about buying it because it is a product which gives value to him. So strategically the company does not want to move into the bottom end because that bottom end now is getting serviced by our brands called Benelave and Raasi, so they are also growing as such but margins are not there at the bottom of the pyramid.

Gunjan Prithyani: Sir, just on your consumer business the topline that you mentioned for FY2016 was about 60 Crores, right, full year?

Sandeep Sikka: Yes.

Gunjan Prithyani: How do we look at it for next year and in terms of even the profitability how should this business pan out over the next two years? Also if you could, I am sorry if I missed this that which are the products, which are already there in the market in your brand and what would you be launching in the next 12 to 18 months?

Sandeep Sikka: I will take Gunjan question a little bit back and to just because since there are many who have logged on to this call. So allow me to explain what is the rational of taking all these new businesses. A company today has a one distribution channel to the market, which is sanitaryware and if you visit any market hub in that you will find a consumer electrical channel, you will find hardware channel. So right now the company has taking an initiative to develop two more channels to the market one is the consumer electrical channel and another is the hardware channel. The insight into the consumer electrical channel is with the products like water heater, air purifier, and we will be launching water purifier as we move forward and also kitchen hoods and hobs. Another channel which we have opened up, and this is a channel through which will open up next year is the hardware channel through which we will be selling the pipes and these are basically plastic CPVC pipes and UPVC pipes. If you see the consumer electrical product market which we are targeting especially water heaters, water purifiers, air purifier these are all huge markets and we are targeting total potential market size of around 10000 Crores. So the growth is there and again we are not walking at the bottom-end of the market here. Our focus is to sell the products wherein we can earn a gross margin of somewhere around 35% to 40% that is the target broad level gross margin levels on which we are focusing on. So that the resulting EBITDA once the full level of turnover gets generated, so we could have an EBTIDA margin of somewhere around 10% to 12% on the overall basis. Since no major capital investment is going into this projects all in the consumer business so it is more working capital intensive but the return on capital employed we expect more than 20% once the business gets stabilized from here in 12 to 18 months.

Gunjan Prithyani: So consumer electrical is basically on outsourcing and none of it will be manufactured in-house?

Sandeep Sikka: A few of them we may take up subsequently but right now we are taking it from the market checking the quality control. Like water heaters we have done with Atlantic group of France, so they have been very well accepted in the market as also stated last time on the call and we have good market share in the segment in which we are operating.

R.B. Kabra: Actually manufacturing will depend on the kind of volumes. We have internal benchmarks that if we reach to this kind of volume then we will think of first putting up an assembly unit, which normally cost anywhere between Rs.5 and Rs.10 Crores and once we reach another benchmark of volumes then we may think of manufacturing in India, but currently there is no plan for manufacturing as such.

Gunjan Prithyani: In the hardware what is the kind of capex commitment that is there in the pipes business?

Sandeep Sikka: In the pipe business we are starting with the capex of around 105 Crores but they will be definitely another 10 and 10 Crores each for next two years and pipe business we feel it will start selling pipes in the market in the first quarter of the next financial year. So that market target market, which we are doing in the pipe side to start with on the hardware is somewhere around 7500 Crores market, which is UPVC and CPVC market for home segment and ROCE there is also expected to be good EBTIDA margins we expect there in the range of around 12% to 14% for that product.

Gunjan Prithyani: Thank you so much.

Moderator: Thank you. The next question is from the line of Mehul Savla from Ripple Wave. Please go ahead.

Mehul Savla: Sir my question is more not to with the immediate results but if two to three year view on the packaging products since you cater primarily one is through the liquor beer industry and the soft drink industry, how do you see the volume growth panning out because soft drinks pet seems to be replacing glass fairly quickly and within liquors, spirits and beer also with as you said lot of state level restrictions and the policies politically that are being followed could face, so do you see a challenge in achieving any volume growth in this segment over the next two three years.

R.B. Kabra: As I mentioned normally historically the volume growth in glass business has been in line with GDP growth, but barring last two, three years and sometime there is a cyclical impact that because if there is some lot of stock of old bottles you must be aware that India recycles bottles whether it is a Coke, Pepsi, beer people recycle for six times and Coke, Pepsi people recycle for 20, 22 times that is why they are able to sell the contents with the glass bottle cheap at Rs.10, Rs.11 whereas if you talk of can and that will cost you Rs.30 or more or less the same kind of content, the 300ml bottle sells for Rs.11 and 330ml can sell for Rs.30 that is largely difference of packaging cost, so industry cost remains the same. So industry cost of the glass bottle will always be lower in India as we know that most of the consumers are very, very price sensitive consumers and the tier II and tier II and rural areas where Coke, Pepsi still treated as a aspirational product, people will spend some money but will not be spending Rs.30 on it, because you know how the conditions are there when you go to the smaller towns and cities. Yes, your comment of the liquor and beer is right because we sell around 60%, 65% volume to liquor and beer, so like Bihar had the prohibition. Now I understand that Tamil Nadu has also decided over a period of time slowly, slowly they will put prohibition so initially may impact the volume growth yes, but another thing is happening is that beer consumption is the country is growing up substantially, the beer consumption which was treated as a alcoholic consumption was taboo for many people, now they do not think that beer is an alcoholic drink. They think it like any other drink, so beer consumption we expect it to grow substantially, the beer growth should compensate the degrowth in the alcohol or the liquor as we call it, but yes we have to see that how it is going to impact. Normally you see initially there will impact but then there is a lot of transportation from one state to another state it’s like in taking place because people who consume liquor the result in consume liquor only at a higher cost. But going forward yes we will have to see, we have to watch for two, three quarters and that is why we say that we have not yet decided though our current capacity utilization is 100% on three furnaces we have not yet decided to light up the fourth furnace which is idle with us because we want to see another two quarters that how the market moves.

Mehul Savla: Sir and how is the competitive scenario in the glass side because there are only like still the large players right in the country yourself, HNG and the Piramal?

R.B. Kabra: HNG is the largest in the country and they have a capacity of double than ours and their one furnace is still shut but we understand from the market sources that the capacity utilization at their end is around 78% to 82% on the various locations but you must be watching their results if you have invested.

Mehul Savla: Yes that is what so I think the fear the apprehension is more that…?

R.B. Kabra: That is what is we are saying that we can only say that our business is much more smartly managed and we have turned around much faster than the competition though we are number two and we do not aspire to be number one, we are happy at number two, but our margins till last quarter result HNG has not yet come out with their results for the Q4 but till Q3 they were still making losses, whereas we have been making profit for last four quarters now.

Mehul Savla: Correct, so that is what a bit difficult to understand why there is such a decrease?

R.B. Kabra: We have a company called Haldyn Glass which always been leader in terms of margin today our margins are 50% higher than even Haldyn Glass.

Mehul Savla: That was really the question Sir in terms of with such players larger players out there with lower capacity utilization does that kind of put a limit on the pricing capability over there?

R.B. Kabra: The whole last year we did not have any price increase, which is right.

Mehul Savla: Just a last question on this again the glass furnace only is that so I think when you say the product mix so as kind of also largely contributed to the improvement in profitability now is it a higher mix of from a end-user industry point of view sort of a mix or both?

R.B. Kabra: I mentioned I think a year, year and a half ago that we started manufacturing a specialty colored bottle. We and HNG we have been making historically bottles in three colours which is flint which is white, green and amber which is yellow which is used for beer largely. Three colors we do have been making. So other people either make Amber or make white nobody even makes green which go for 7UP and other things. Two years ago we have put up a specialty line for make any special color which could be dark blue, dark green, red, yellow whatever, furnace being large the whole furnace can be converted for the amber or for the white but if we convert the whole furnace to that color and the requirement on these special colors were used to be very small like you do Antiquity blue or somebody launching wine in a green bottle and these all were being imported in the country. So we put up a special line having capacity of 1000 tonnes a month and that helped us and now that line is completely sold and we are converting one more line to this kind of a product manufacturing that is also a higher realization.

Mehul Savla: Thank you Sir.

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

Samar Sarda: My questions have to do with building products division, the revenue growth if I adjust for CPD 7% year-on-year and you mentioned 22% for this year has been faucets contribution shall we assume that the volume growth in sanitary ware has been lower it is not been there in FY2017 if that is the case, one? What is the margin improvement, which has actually taken because of premiumization of products?

R.B. Kabra: Margin improvement because of…

Samar Sarda: Premiumizing your products?

Sandeep Sikka: I think if you say on a broader basis definitely the growth has come from faucets and within the sanitaryware sector as I told you our focus is more on a value creation and if you see our product mix enrichment is already happening and also like our premium product kitty as compared to the overall sanitaryware kitty is somewhere around 59%, 60% today. So we get a good growth within the premium sector, because we earn more in that sector as compared to the others, because we focus on profitable growth as a bottomline rather than just focusing on the creating sale. So if you see your contentions are right in the sense of faucet growth remain contributor so the other contributor has been the higher growth in the premium sector but on the baseline definitely it is almost a flattish growth.

Samar Sarda: So what was the faucet contribution in FY2016?

Sandeep Sikka: Around 24% of the overall building product sales other than CPD.

Samar Sarda: 24%.

Sandeep Sikka: Yes.

Samar Sarda: And what was this number in FY15.

Sandeep Sikka: We grew by around 4% plus.

R.B. Kabra: Last year it was around 19%.

Samar Sarda: Sir if you could just help with the EBITDA numbers adjusted for CPD for this year then?

Sandeep Sikka: If you take a BPD without CPD the year EBITDA number for BPD without CPD is about as around 20.25% and please note that we did a big media coverage this year using all celebrities and other things so there has been definitely a higher marketing cost which is more evident from the Q1 and Q2 absolute figures if you see and this numbers is after that spending money on promoting the brand.

Samar Sarda: Which is the key reason why our BPD margins are slightly lower?

Sandeep Sikka: Yes and also due to one fact that as Mr. Kabra said our margins on sanitaryware and the faucets the percentage margins create little bit of deception here because brass is a costly product so although we earn absolute more but percentage margins looks lower as a percentage to sales so that also is the fact that as the faucet sales is increasing the percentage margins looks lower to us.

Samar Sarda: The other question is with regards to the set up cost on your CPD business and the hardware distribution for your pipes business earlier in the year you mentioned you will require and about 30 Crores over a period of six quarters to set up CPD?

Sandeep Sikka: Yes, so this statement we made in around February so I think we will still hold that statement from that although Q4 expenses have been build in to that but we may spend another 20-22 Crores in next 12 to 15 months which is essentially come as a development cost in the charge to EBITDA of the BPD.

Samar Sarda: I am sorry 20 to 22 Crores.

Sandeep Sikka: Because out of 30 a part has been spend.

Samar Sarda: Would you also spend some cost in setting up pipe businesses in FY2017?

Sandeep Sikka: That may not be the substantial cost right now as we move forward.

R.B. Kabra: FY2017 all costs will be capitalized as you know till we go for the commercial production all cost related to that business will be capitalized.

Samar Sarda: Okay, so why I am asking is so if I combine like all these three aspects that BPD the margins will be stable for sanitary or for BPD business your margins might improve a bit and there are some setup cost here, so if you could just help us on your guidance on FY2017 EBITDA margins on an overall basis?

R.B. Kabra: So if we say that we will be remaining more or less the same level maybe increasing by 150 basis points that will be the right estimate.

Samar Sarda: Thank you and all the best for the next year.

Moderator: Thank you. The next question is from the line of Sameer Tulsian from JM Financial. Please go ahead.

Sameer Tulsian: Sir I want to understand like what are the current gross debt levels? Gross debt?

R.B. Kabra: It is 560 Crores.

Sameer Tulsian: Including the current maturity now.

R.B. Kabra: Yes, so a 50% is long-term and 50% is working capital that is the total bank debt as on March 31, 2016.

Sameer Tulsian: Board has proposed leasing NCDs of Rs.500 Crores so what is that cost?

R.B. Kabra: That is only enabling resolution because as you know that we are putting up these two projects one is for the closures and one is for the pipes so which capex is approved last year and announced last year very little has been spent in the previous year and capex for both these projects actually will be going this year. So we will have to borrow some amount whatever the shortfall from the cash generation because from the cash generation we have to pay 125 Crores of the current debts balance will be used for capex and whatever extra required we have to borrow so that we will see whether we borrow from the ECB or we borrow through the NCDs so that is only enabling resolution today.

Sameer Tulsian: What was the capex for the current year and what is the expected capex for coming two years?

Sandeep Sikka: As we disclosed last time because there are few capexes which are flowing on from the last year so we had a capex on a pipe which is 105 Crores now we have a capex on caps and closure project which is 112 Crores. There is capex of around 45 Crores for the capacity expansion of CD1, CD2, and apart from it there is a normal capex which ranges from somewhere around 30 to 50 Crores every year and that gets board approves it as and when required because few things in the plant do keep changing for the productivity improvement and the cost efficiency.

Sameer Tulsian: So the current year's capex was around?

Sandeep Sikka: This year next year we will spend somewhere around 300 Crores plus in terms of development of the facilities.

Sameer Tulsian: You are saying total for FY2016 to 2018 would be around 300 Crores?

Sandeep Sikka: 350 Crores and but this is the flow out of last year's capex also like it is accumulating like Pipe projects have started now on the ground it start building up even caps and closures expenses have started coming up.

R.B. Kabra: 105 for the pipe, 112 for the closures project around 30 Crores on the sanitaryware capacity expansion so that makes it around 250 Crores and balance will be maintenance capex for all these seven to eight plants what we have.

Sameer Tulsian: So this is the total effect for next two years?

R.B. Kabra: 300 Crores for next 15 months.

Sameer Tulsian: Our tax rate keeps fluctuating it might be due to some subsidiary losses so how to keep a track of it or any guidance on that like tax rate?

Sandeep Sikka: Subsidiary losses are right now separate from the parent company, so we do not get a benefit right now but definitely our tax rates are higher as on date because in the last few years there has not been major capex and the tax shield which we used to enjoy that tax shield is slowly, slowly coming of and all these new projects coming and definitely the tax rate in next one or two years should get normalized now.

Sameer Tulsian: Do we see any impact of rising pet coke prices or fuel prices in the packaging product margin going ahead?

Sandeep Sikka: I think it will have some forbearance on the cost definitely because the last year the main advantage has come with lower prices but if the fuel price start increasing definitely we will have to see as an industry as a whole whether if you are able to slightly pass on, but it depends on the entire market because rest of the players as we discussed they are still operating at a lower capacity utilization and if they are still under priced their products as compared to the competition then we will have to see as we move ahead, but definitely any fuel price hike will have some cost increase.

R.B. Kabra: I will give you some comfort. The LPG prices for the period last year this last financial came down 30%, the furnace oil prices came down 40%, pet coke prices came down 25% but that has not happened in one go, that was over a period of one year. So we have actually accounted for the weighted average cost because what was the cost at particular point of time that has actually been build so even if prices go up they will not come 40% or 30% in one go. So basically at least for this year there could be very marginal difference in terms of fuel prices going up.

Sameer Tulsian: Now what is the growth in faucet ware in the current year FY2016?

R.B. Kabra: FY2016 faucet has grown around 22%.

Sameer Tulsian: Sanitaryware side?

R.B. Kabra: Sanitaryware around 7%.

Sameer Tulsian: It is like all mostly volume led growth or there is some price rise also?

R.B. Kabra: It is a mix of both.

Sameer Tulsian: What is the utilization of the current faucetware facility?

R.B. Kabra: Let me tell you the when we say the revenue growth is mix of three things. One is price increase in a year if it happens and what percent it happens then the changes in the product mix and the volume growth so three things contribute to the value growth. Coming to the capacity utilization the sanitary ware capacity utilization is around 90%, 91% and faucet capacity utilization is the run rate at the end of March is 65%.

Sameer Tulsian: Thank you.

Moderator: Thank you. The next question is from the line of Prashant Kutty from Emkay Global. Please go ahead.

Prashant Kutty: Thank you Sir. Just firstly couple of bookkeeping question I am sorry if I missed out this number if you could just tell me what is the contribution of the building products, the segments in the building product segment for FY2016 in terms of revenues, how much would have been sanitaryware, faucets, bathware and the consumer?

Sandeep Sikka: If you see the mix of the building product division without consumer products 22% is faucets, another around 10% to 12% is the other, 65% is sanitaryware.

Prashant Kutty: I am sorry you said that the sanitaryware grew by7% for FY2016 and in faucet grew by 22% for FY2016?

Sandeep Sikka: Yes.

Prashant Kutty: Just one thing I just want to ask you I guess to another question which was asked in the past that if we adjust for the growth rate numbers of consumer appliances, both in the base year as well as in the particular quarter the growth rate is just about may be 3% to 4% I guess might be that lower in that as well, while obviously we are looking at faucets number also improving on the back of capacity utilization so if you could just help us understand as to what is exactly happening as far as the base sanitaryware business and the faucetware is concerned because I understand that the real estate has been having an impact but in the other side if you look at certain other competition over there the growth has been yes it has been muted but it has been relatively better. So if you could just help us understand this math actually and if you could just give us some sense on the next year as well how much is it going to be led by distribution led growth or new products for that matter in both these segments, because this just typically I believe is the core?

R.B. Kabra: To answer you that the growth in other companies has been higher is probably yes to some extent but the differential is not too large basically if you see the number from tile companies or any other companies in this business growth is anywhere between 10% and 12% and we say our growth has been around 7.7% barring this CPD growth and if you get the other companies growth also there is a trend in last two years that each company has been adding new products. If you talk of Kajaria they had a sanitaryware that you talk of Somany's and if you talk of the business growth in the core business it may be very similar to ours.

Prashant Kutty: But Sir in that case of faucets also we have actually seen?

R.B. Kabra: For the other products the base is technically zero very small so in terms of growth percentage will be very high for those products so ultimately if you talk of the business average has been growing 10% to 12% for the last two years but as somebody has the new product we suddenly gives a jump and then there is a variation like you buy at CPD our growth is also 11%, somebody at tile suddenly then that is the growth so ultimately the core business if you talk off in average has been growing 10%, 12%.

Prashant Kutty: Sir the point over here is that we have also seen a new product addition in the form of consumer appliances the consumer division but despite that if you look at the quarter growth rate for the building product segment it still shows about 9% number so and obviously as I said whether if you probably strip off the number for the fourth quarter then the number actually looks like a 4% kind of a number so I was just trying to understand this math?

R.B. Kabra: I think you are jumping probably numbers here. The growth is there but CPD is not created only this year. We have been selling three products of CPD as a part of BPD for last three years, which was the kitchen chimneys, kitchen hoods and hobs and cooktops. We also had revenue so like whole of last year revenue of CPD were around Rs.26, Rs.28 Crores, which this year is Rs.60 Crores. Even the last Q4 had some revenue coming up from the CPD, which is now transferred to CPD vertical so ultimately minus CPD the growth is around 7%.

Prashant Kutty: You just had told that you are looking at spending another 20 to 22 crores on the consumer appliances segment in the next year right is that the right thing? What is your outlook as far as our margins are concerned on the CPD business? Let us say a couple of years down the line how are we anticipating the business in that end and also on the growth front, because obviously we are going to see some new product additions over there, so how are we looking at the growth in the CPD segment over the next couple of years if you could just give us some sense on that?

Sandeep Sikka: As I told you the overall target market which we are looking at is around 10000 Crores here and we feel and we have a strongly feel that in next four to five years we should be able to get that at least 5% of that market. Second is we are not going at the bottom of the pyramid product wherein we are operating at a very low gross margin, the product wherein we are able to sustain our presence from even 45% on an average of around 40% and this should be able to cover our distribution cost and also have a net resulting EBTIDA down the line maybe three four years down the line EBITDA somewhere around 12%.

Prashant Kutty: Lastly in terms of our sanitaryware faucet business obviously because the fact that or this year our base is relatively lower and obviously there have been talks about initiative in the rural side of the business and obviously there have been talks about overall government focus on homes and all given those government initiatives and also the fact that there is a relatively lower based are we expecting something kind of a double digit growth rate number in the base sanitaryware in faucet business can we actually potentially look at that kinds of a number in the next year?

R.B. Kabra: Yes, faucet will certainly grow double digit, sanitaryware we will try to grow double digit but basically the Swatch Bharat Abhyan is not helping any of the organized players. Pricing there is so low we are not able to compete and as you know that the sanitaryware industry or faucet industry only 50% is organized in faucets 50% is unorganized. Sanitaryware 60% organized and 40% is unorganized, but you talk of volumes 60% volume of sanitaryware industry comes from the unorganized sector. So basically for Swatch Bharat the product from the small scale sector is going on so that is where the issue that we have not able to take any major part of that business and majorly has been from the small scale sector, we have got very little part of it which is through the CSR spending of some large corporates who decided to build toilets but that will not add to any percentage in terms of revenue or anything for that matter.

Prashant Kutty: Thank you sir and all the very best to you.

Moderator: As there are no further questions in the queue.

Sandeep Sikka: Thanks all for joining us.

Prashant Kutty: I would like to thank the management again for participate in the call and Sir if you would have any closing comments?

R.B. Kabra: Thank you very much. I thank once again taking time for participating in the call and taking participation. The only thing is that for the last year and this year the sanitaryware both the plants will be completed by end of financial year. The closure business will also be commissioned and pipe should be able to launch in the market by first quarter of the next financial year. The consumer sentiment can of course improve our business should also improve. Thank you very much.

Prashant Kutty: Thank you Sir.

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