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HSIL Limited

Q1FY16 Conference Call Transcript

Moderator:

Good day ladies and gentlemen and welcome to the Q1 FY 2016 Results Call of HSIL Limited, hosted by Emkay Global Financial Services. We have with us in the call today Mr. R. B. Kabra, President, Building Products Division, Mr. Sandeep Sikka, CFO, and Mr. Anil Chandani, Senior Vice President, Corporate Finance of HSIL Limited. As a reminder all participant lines will be in the listen-only mode and there will be an opportunity for you to ask questions at the end of today's presentation. Should you need assistance during this conference call, please signal an operator by pressing "*" then "0" on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Prashant Kutty, Research Analyst of Emkay Global. Thank you and over to you Mr. Kutty!

Prashant Kutty:

Thank you. Good evening everybody. Thank you for joining on the call today. We would like to welcome the management of HSIL Limited and thank them for giving us the opportunity to host this call. I would now like to hand over the call to Mr. Kabra for his opening remarks. Over to you Sir!

R.B. Kabra:

Thank you Prashant. Good afternoon, good evening to everyone who have taken out time to join us on the call on which we will be discussing the performance of quarter one for this financial year and I will request Mr. Sikka our CFO who is with us now for four months to take you through the financial and once he is through then I will come back to you with whatever clarifications and anything or what else is required. Over to Mr. Sikka!

Sandeep Sikka:

Good evening everybody. The company closed its Q1 financials on July 30, 2015 for the period ending June 30, 2015. Profit after tax has shown a good number in terms of growth which is around 15.75% PAT growth and profit after tax is 17.35 Crores versus year-on-year figure of 14.99. I understand most of the participants who are there on the call they would have either taken it from our stock exchange and they would have received it otherwise the results. Broadly I will run you through the key highlights, the turnover of the company, the gross turnover of the company grew slightly from 440 Crores to 441 Crores is just a marginal growth lakh growth I can say. Building product segment had shown a net sales growth of 6.83% with sales of 205 Crores versus last year year-on-year 192 Crores packaging product sales has slightly de-grown but the packaging product division otherwise has given good results in terms of EBITDA margins and the EBIT margins have gone almost three times of what it was last year. The EBIT margins of BPD divisions were slightly under pressure on account of higher allocation of sales and marketing expense as the company took certain media coverage during the year for its both Hindware Brand as well as the Premium Brand which is Queo and for both this marketing initiatives the Bollywood celebrities were hired by the company.

Apart from this company in the last board meeting also approved two new Capex and one Capex is relating to the pipes division, which is further integration of the product into the BPD division and this Capex is up 105 Crores which involves setting about manufacturing facilities for both UPVC and CPVC pipes. CPVC pipes are now being used extensively in India for carrying both hot and cold water and this product further will be part of the building product division basically it constitutes the whole or aura of product which will constitute as a building products segment. The other project which has been approved is a caps and closure project which is part of packaging product division and the cost there was 112 Crores and this project

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is more focusing on providing security for the counterfeit of the liquor and the other pharmaceutical things and this product will go to our existing customers and also maybe to the new customers, and both these projects, they are high yielding projects and thanks to come with the ROCEs which are focused more somewhere in the range of 20%, 25% and with the payback ranging around four years, on a broader range based on the assumption for the market scenario as on date. On the operation side I will request Mr. Kabra if you can show some light on the overall performance of the company.

R.B. Kabra:

Once again the numbers of course you all have seen and basically as told by Mr. Sikka the packaging product division has done very well and that is in line with what has been happening in the packaging product division for last three quarters, all of you have seen quarter three and quarter four results when we mentioned that there has been a complete shift to the extent possible for the fuel from costlier fuel of LSHS to Pet Coke, which gave us substantial saving in terms of cost and also we got price increase spread over four months starting from July last year till October last year and the full impact came in quarter four last year so that benefit of cost saving in terms of LSHS prices and the Pet Coke prices continued with us and this will which is a kind of a permanent saving and normally a question is asked that is Pet Coke is still cheaper after the crude price is going down to below $50 a barrel but in India of course the prices of furnace oil, prices of LPG, prices of LSHS come down, but it is never in proportion to the fall in the prices of for example the crude oil the prices do not fall in the same ratio because crude oil went as high as $135 to a barrel and remained for a very long-time from $8000 to $9000 a barrel and now it is less than $5000 so prices actually has come down by 60%, but the petroleum product prices which are free marketing prices though in India but has not come down with same proportion that could be because of the various reasons maybe the custom duties are higher or anything, but yes Pet Coke today is the cheapest fuel and still continues to be cheaper to a very great extent then the petroleum product which have been using so we will continue to use this and the savings will continue to achieve in intervening times to come the price increase what we got is still there and that has shown in the results of EBIT increasing more than threefold in this quarter in comparison to same quarter of last financial year. Of course there has been a de-growth in sales and that is because the general scenario which all of you must be reading in the newspapers that the demand situation in the country is not good, everybody is expecting this future to be good and people are waiting for some kind to start consuming more, but yes it is not happening truly speaking because the bottles what we sell are basically used for packaging various consumer products and as those consumer product consumption does not go up certainly bottle sale will not go up, so the bottle or the packaging product division de-grew by around 6% and building product division grew by 7% year-on-year in the quarter and that is the reason that you do not see any growth at the total revenue level at the company level, building product grew by 7% and as I mentioned during my last call, this lower growth has the impact of around 3% of the tile business which we have exited so actual growth you can take around 10%, we see the sanitary ware has also grown, faucet has also grown, of course faucet has grown in higher percentage because of the commissioning of the new faucet plant which was done last year and sanitary ware growth is also there other product if you talk of which contribute around 11%, 12% they have also grown in the similar lines, the margin screech in the building product it is not be worrying all of you because it is largely as mentioned by Mr. Sikka is on account of specific event, which are known to everyone now like we have two Mr. Shah Rukh Khan as a brand ambassador for Hindware and Jacqueline Fernandez as a brand ambassador for our luxury brand Queo and we are going all out for 360 degree advertising campaign so that has resulted in a higher cost because these people had to be hired and we had to make the film and now we have to commit some resources but yes, otherwise there is no pressure on the margins and going forward you will see that we will be returning back to the kind of margins we were there.

As mentioned the product category the CPVC pipe the total market size for the PVC pipes in India is around 19000 Crores and the product which we will be making, so the addressable market size for the product segment which we will be manufacturing around 7200 Crores growth in this business for last five years has been more than 25% CAGR these CPVC pipes are very well accepted mostly these remained in short supply because the CPVC resin are manufactured only by few manufacturers across the world and we have been able to tie-up with one of Japanese manufacturer which is Sekisui it is a $9 billion company, they have made an arrangement with them to supply CPVC resin in a long-term basis. The work will start on the pipe plaint initially on the Gujarat land which we had acquired for putting up a third sanitary ware plant it is a large piece of land so it is decided that we will because the land acquisition might delay projects so we decided that we will start putting up the first plant for the pipes at Gujarat land which is at Jagadia and of course there is enough land when we want to put up a third sanitary ware plant so that is one and the second is a specialty closure project, this will be a very, very special kind of technology which actually helps in controlling the counterfeit which is high-end licker or pharma products which will be in India most of the manufacturers feel that counterfeiting is a big problem and as well all know yes there is a problem so these special kind of closures are only one way that you can only take out product from the bottle you cannot fill it as long as the closure is there on the bottle and if you remove the closers then it cannot be fitted back onto the same bottle. So the consumer will know where it is original packing or refilled packing we have applied for patent for this kind of a product and we will be looking for a worldwide patent going forward, yes there is a India there is a one manufacturer this is as international manufacturer but the product is in short supply even today and therefore we have decided to add this product to our basket of product because the customers are the same and it used for the similar kind of purpose so that is where we are the investment we have already reported on the pipe projects 105 Crores the closure project around 12 Crores to spread over 18 months, because any project cannot be commissioned anywhere between 12 to 18 months so that is the time period and the projects which we were talking last time are going on well the expansion project at Bahadurgarh and Bibinagar for adding 1 Lakh pieces module at Bahadurgarh and 3 Lakh pieces module at Bibinagar is on track and that is where we are work out plant commission is currently running at 50% capacity utilization last time I mentioned it was around 35%, 40% so it has gone up by around 10%, 12% and we foresee that by year-end this financial year-end we should be running at around 85% capacity utilization that is why I have to say and now we are open for any questions or clarifications.

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 Sameer Tulsian from JM Financial. Please go ahead.

Question and Answer Session

Sameer Tulsian:

Couple of questions. Firstly how much was the tile sales in 1Q FY15.

R.B. Kabra:

Tile sale in FY15.

Sameer Tulsian:

1Q FY15 like we have already exited there or it was like something…

R.B. Kabra:

No I think this is the last quarter and after that I think quarter one of last year we did tiles and after that we stopped.

Sameer Tulsian:

How much of the tile sales in 1Q FY15.

R.B. Kabra:

That was contributing about 3%, 3.5% of the revenue.

Sameer Tulsian:

And how much was the additional advertisement expenditure because of the ad campaign of Shah Rukh Khan?

R.B. Kabra:

Total additional sales and marketing expenses put together in this quarter versus year-on-year quarter last year is around 8 Crores.

Sameer Tulsian:

That was all due to this additional campaign correct.

R.B. Kabra:

Yes various activities related to sales and marketing.

Sameer Tulsian:

So from next quarter onwards it should stabilize or it should take a couple of quarters to stabilize.

R.B. Kabra:

I think about a two quarters because as I mentioned that we are working aggressively on the 360 degree campaign so of course the expense will not be to this extent but you might see 1%, 2% higher expense, but to compensate we are working on the revising our sales prices for the products so I think we are confident of margin which I just mentioned.

Sameer Tulsian:

So how much price hike are we expecting?

R.B. Kabra:

We are just working out so at today the percentage is not decided but yes the price increase is on the offtake.

Sameer Tulsian:

And how do we see the demand scenario basically in the last quarter and the current month in terms of sanitary ware and faucet?

R.B. Kabra:

The demand is market is tough because as you all know that our product is are related to real estate business are largely because only around 10%, 12% go for the replacement and balance 88%, 90% goes for the new construction and as you all know that new construction activities all across the country barring few places is really slow so the demand is not as expected and the impact of the Swachh Bharat which we were expecting but it is also on the growth it will be not taken off though you see and we also see lot of verticals so many toilets being built but I do not know where from these toilets were built or not built but actually there is very little momentum on the ground market is tough and but we are really working hard to see to get the kind of growth we are expect and we are working hard to get that is why there is a 10% growth but yes I cannot say that the market is as won it and similarly for the packaging product there is a demand as I just mentioned that there is a little slowdown in terms of demand like quarter three was quite good in terms of demand but maybe the monsoon set in early and that is why the bottle demand especially for the beverages sector and bear sector is little slow.

Sameer Tulsian:

And if we were to see sanitary ware faucet ware growth during the quarter how is the growth on a YoY basis in sanitary ware, faucet ware.

R.B. Kabra:

The growth in terms of faucet and both in terms of sanitary ware.

Sameer Tulsian:

Yes and the growth in the faucet ware business and the sanitary ware business during the quarter.

R.B. Kabra:

The faucet growth is around 25%, sanitary growth is around 4.5%, 5%.

Sameer Tulsian:

And what would the revenue potential new geezer business which were entering.

R.B. Kabra:

Geezer we have just launched in the month of July though we have been working on the project for last few month and actually the market seeding has started in the July and ultimately in the next three years we are looking at around 8%, 10% of the market share of the total Geezer market and we are expect the revenue of anywhere between Rs.80 to Rs.100 Crores in coming three years.

Sameer Tulsian:

And do we see any further margin benefits coming from low commodity prices or it is like all in the margin.

R.B. Kabra:

Yes, I think we should see some benefit in the faucet market or in the faucet business and not really market faucet business because there we use drugs otherwise the sanitary ware the raw materials are various kind of clays and those really not get affected because of the commodity prices, but yes in one of our plant in the use LPG on the sanitary ware plant the North India plant we use natural gas which prices of course is not coming down India because we have that long-term contract with gate authority of India and they also get guided by a very complex formula how to arrive at these fuel prices so these prices despite as I just mentioned the crude oil prices coming down more than 60% actually year-on-year in natural gas prices has gone up by at our Bibinagar plant we have been using LPG, we have seen a price reduction of anywhere between around 30%, 35% so if the crude prices further go down yes the pre market prices of LPG will go down and we can see further benefit coming down because of the commodity so two areas where the LPG use is there number one and number two the faucet business where we use that we can see the advantage coming in the coming quarter.

Sameer Tulsian:

And one last question our interest cost has come down substantially so is it only on account of the debt repaid or there are some reasons of the debt.

R.B. Kabra:

No, we raise that 250 Crores QIP in march you are aware and those net of all the expense is the balance of around 243, 240 Crores had been used for debt repayment so that was one loan repayment number one and during this quarter we have been able to with the generation and with the better management of working capital we have been able to generate now additional 60 Crores by that also our bank limit utilization has gone down so truly speaking in last one month we have paid one quarter we have paid more than Rs.300 Crores is the debt repayment which is reflected in the reduced interest.

Sameer Tulsian:

So working capital days if you have to see for the quarter it is reduced five days.

R.B. Kabra:

Yes it is reduced by five days.

Sameer Tulsian:

Thank you sir.

Moderator:

Thank you. The next question is from the line of Vishal Chopra from UTI Mutual Fund. Please go ahead.

Vishal Chopra:

Sir my question is with regards to the Capex in the glass division sir at the time of the QIP we were given to understand that we will try to follow our asset light model and do not do any further Capex in the glass division so just wanted to understand your rational why are we going doing the further Capex in that division where we just come out of trouble after two, three years of struggle and we have just started making first…

R.B. Kabra:

There is no Capex on the glass business we never said that we are spending money on glass business.

Vishal Chopra:

Can you just explain the rational why are we doing this Capex and do we have any commitment from any customer that there will be off take or do we have back-to-back order for this Capex.

R.B. Kabra:

This material actually if you see this is in the value addition we are already doing one part of that this is the packaging division and this is just an extension of the existing business which we are doing in a business there are various segments of value additions which we need to capture and there has been a demand or relationship with most of our liquor companies and soft drink companies they get more than three decades and company seeing a very natural customer into the security kept and company has already worked very expensively on it, works on the design of the product and also taken the pattern and part of this pattern our products have been tested also along with the existing customers. So based on the overall rational only and they are seeing the value addition both to us as well as to the customers this project has been the consideration of the board has approved this project.

Vishal Chopra:

Sir but the problem is if we see as the packaging products division as a whole if I see last ten years we have invested close to 1000 Crores in that division and we are barely generating single digit ROCE why do we want to further invest in that division.

R.B. Kabra:

No, when you work on a system you always work on a system on a working of penalty the ROCE over a period of time, now if we do not capture into this market like even the existing investment how do we increase our overall ROCE of the product so we are doing as I said this initial part of the discussion most of these projects I cannot disclose what are the EBITDA margins but on a broad range these projects have been conceived with the ROCE ranging between 20% to 25% once the product gets fully stabilized.

Vishal Chopra:

Sorry for repeating the question again, do we have had talks with the few of our existing customers that day we have got assuring that we will do this Capex and we will in terms of higher revenue or higher margins do we have such kind of assurances.

R.B. Kabra:

To answer your question straight we have had the samples prepared of the product we have got those samples tested from our customers we have assurances from them or certain volumes but we do not want to commit those somebody is wanting to sign in even single-handedly for the complete output but we do not want to do it because when becomes dependents yes we are working with three large people and everybody has given very positive response to this project.

Vishal Chopra:

And for both these projects what will be the Capex, we are doing what kind of incremental turnover can we generate for both the products separately.

R.B. Kabra:

We have the pipe plant in five years' time will be doing anywhere between 400 to 450 Crores.

Vishal Chopra:

And this Capex of 105 Crores.

R.B. Kabra:

And the closure business we will be doing around 150 – 160 Crores.

Vishal Chopra:

But the Capex of 115 Crores.

R.B. Kabra:

Yes.

Vishal Chopra:

And that will take five years to reach the turnover.

R.B. Kabra:

No that will take three year story is the turnover.

Vishal Chopra:

For the closure and for the pipe you are saying five years.

R.B. Kabra:

Because fifth year we are seeing 400 – 450 Crores.

Vishal Chopra:

And when do we expect both the plants to get commissioned.

R.B. Kabra:

Anywhere between 12 to 18 months.

Vishal Chopra:

So from that time onwards the five years for the pipe and three years for the closure plant.

R.B. Kabra:

Just to clarify I am sure you must be knowing this but once the first pipe is start rolling out the sale will start so first year revenue first full year operational revenue is around 150 Crores second year revenue is around 230 Crores so this way progressively in the fifth year and this expense will also be incremental over a period of time, we will not be putting in whole money in one rope so by the fifth year our internal estimation for revenue from the pipe business under 400 to 450 Crores.

Vishal Chopra:

And sir in the CPVC business one of the most important factor is the fitting part of it so we are doing Capex for only for the pipes or what are we doing for the fitting and the inventory management also is very difficult there.

R.B. Kabra:

Pipes and fittings both.

Vishal Chopra:

How do we plan to sell it the existing channel or do we have to set up a new channel and again how do we manage the inventory there because the…

R.B. Kabra:

The part of our dealer I will not say 100% but maybe 50%, 55% of dealers already are selling pipes but the pipes selling is little different than sanitary ware selling here in the pipe there is a distribution distributor concept so the company have a large distributor in a state and then he will supplies to the dealer because this a freight sensitive cargo so to that extent that is how it was so we will be creating the distributor and then outsource the dealers are there in any case to tariff so there will be one more channel which will be created in between.

Vishal Chopra:

Sir but we already started with the tile business which was much more closer to the sanitary ware business and we were not very successful in that and what makes us believe that will be successful in this CPVC business.

R.B. Kabra:

I will just ask you. One failure does not mean that everybody will fail in rest of the projects right. Have you been successful all the time?

Moderator:

The next question is from the line of Chanchal Khandelwal from Birla Mutual Fund. Please go ahead.

Chanchal Khandelwal:

The previous speaker has asked most of the questions but we will like the sanitary ware business, we like the amount of money you are able to come out in the premium you are able to come out in that business but again the same question here on the capital allocation, we have seen time and again I am not doubting your ability to be successful in CPVC business I am only saying that time is again we have seen that any is on capital allocation decision there is not let to value creation for the shareholder. So from that perspective we just want to understand why this decision of entering into CPVC business and the other capital allocation you are doing because at the time of QIP also we were make to believe that the large business maybe hipped off at some point in time but now that you are committing capital to this business I think you will have to focus on that business also so what is the thinking process and how do you think this business will help you create value more a longer period.

R.B. Kabra:

We never said that glass business will be hived off, the question was asked that are you willing to make these two separate business and the statement was management was not averse to it, provided there is a right thing to do for everybody's benefit so we never committed that, the statement of yours is incorrect that is number one, number two the investment in glass business, this is not an investment in glass business but yes it is a customer base is the related customer and we feel that this business will give us much better margin and much better ROCE thereby resulting in higher ROCE improvement in the packaging product division so that is what we are doing. Similarly for the pipe as I mentioned it is a very large market and market is growing more than 25% CAGR and more and more people with the education level raising are converting from GI pipe to CPVC pipe and you must be aware that the CPVC manufacturing or CPVC resin is a very, very proprietary kind of a process. Only four companies all across the world make it. Always there is shortage so it is not that CPVC pipe do not sell. It is the matter of tying up the raw material. Now we have been able to tie up. We have been working for quite some time and once we have been tied up and we know that we can make success of this business then we have taken the approval from the board that is all.

Sandeep Sikka:

Also if you see from the overall perspective like we have been telling that we are a building products company and there are various elements to that building construction, which happens like there is behind the wall concept and there is something in front of the wall concept. So we are pretty strong in terms of as far as in front of the wall thing is concerned now this is a new initiative which the company has focused on behind the wall so as to create synergy one of the brands as well as the product. Definitely your point in terms of the tiles and other thing is there but tile is the different market, pipe can be different market, but if you see in the overall leveraging perspective also the company total debt as on March 31 2015 was 550 long-term debt with the net worth of odd 1000 Crores without reevaluation under the BRR and once the another 220 Crores of debt is paid during the year the leverage position is 0.3. So company has to take some risk in order to enhance the shareholder value over a period of time and it does not mean that the company will invest only into the sanitaryware or faucets. So company has a very strong sanitaryware business. Company is now a leading player into the faucet business also and this drive further extension into the new building construction segment side.

Chanchal Khandelwal:

The only doubt is may be you could have started this business and then committed capital because once the capital commitment is there working capital also will be required so you may end up spending some 150 to 200 Crores over a five year.

Sandeep Sikka:

From a shareholder perspective I totally take your point but you have to appreciate the fact.

Chanchal Khandelwal:

You are a bigger shareholder.

Sandeep Sikka:

Yes everybody we treat all shareholders as equal about the perspective of the business. The business need to take some risk in order to further enhance the ROCEs and that is what the company is looking and that is what the board decision is deliberately taken after a lot many deliberations this has been finalized.

Moderator:

Thank you. The next question is from the line of Anshuman Atri from Espirito Santo. Please go ahead.

Anshuman Atri:

Thanks for the opportunity. My question is related to the CPVC and what is the capacity for UPVC and CPVC?

R.B. Kabra:

It will be 30,000 tonnes per annum.

Anshuman Atri:

For both combined or?

R.B. Kabra:

Both combined.

Anshuman Atri:

Okay what will be the ratio?

R.B. Kabra:

Ratio in terms of revenue I can tell you it will be around 60% CPVC and 40% UPVC.

Anshuman Atri:

What could be the volume capacity expansion growth in this over the next fiscal?

R.B. Kabra:

This capex is for next four years as I just mentioned that we will be adding some moulds and dyes for the additional fittings, which we may add over a period of time. Otherwise this is good enough for up to four years.

Anshuman Atri:

Second question is in terms of margins. So what would be the sustainable margins for the building product and as well as the glass business.

R.B. Kabra:

As I just mentioned building product this quarter is margins are low because of the specific action what we have taken and as I again repeat myself we are confident of returning best with the similar kind of margins what we had last year.

Anshuman Atri:

SG&A expense as percentage of sales how will it be this year and say next year going forward as compared to last year.

R.B. Kabra:

For what?

Anshuman Atri:

SGA expense as percentage of sales say in this current year FY'16 versus last year and FY'17 onwards.

R.B. Kabra:

That is reported into the balance sheet now.

Anshuman Atri:

I am talking about the full year what would be the expected?

R.B. Kabra:

This year will be may be 1% and 0.5% higher going forward for the whole year otherwise more or less is similar of last year.

Anshuman Atri:

One last thing is when you are talking about the back part behind the wall versus in front of the wall what other initiatives can we expect in behind the wall?

R.B. Kabra:

We already have one product line which goes behind the wall concealed system which in terms of volume we have been doing a reasonable business. Of course in terms of value in the total business of building product the percentage of that is not too high but we are already there in this business for quite some time and in terms of numbers we are telling reasonable numbers of concealed systems. The pipe is the next and that we keep looking at product, which can be sold through the same distribution channel and the similar customer and through the same customer. So we keep working what else can be added we will keep our eyes near open.

Anshuman Atri:

One final thing is you said there was 10% growth excluding the tile part, so what were the volume growth and also the value growth?

R.B. Kabra:

Volume growth was not there at all in the sanitaryware.

Moderator:

Thank you. Next question is from the line of Hardik Jain from White Stone Financial Advisors. Please go ahead.

Hardik Jain:

Good evening Sir, you said current quarter margins were mainly impacted due to sales and marketing expenditure. I think I missed that point. Can you share with me the numbers for sales and marketing this quarter and the same quarter last year?

R.B. Kabra:

Specific I think numbers we cannot share as I mentioned largely this is impact of instant marketing expenses under different heads in this quarter.

Hardik Jain:

So in terms of amount what is the impact.

R.B. Kabra:

Around Rs.8 Crores.

Hardik Jain:

So it is 8 Crores more than what it was in the same quarter last year.

R.B. Kabra:

Yes.

Moderator:

Thank you. Next question is from the line of Umesh Patel from Sharekhan. Please go ahead.

Umesh Patel:

Thanks for giving me opportunity Sir, couple of questions as you highlighted that we are putting a plant of CPVC and UPVC in Gujarat. I just wanted to understand why we choose only Gujarat as I mean it is a large unorganized players and already there and why not the other parts like Northern and Eastern region because no doubt for UPVC market Gujarat is huge due to the significant agriculture activity, so just wanted to know your thought process on that.

R.B. Kabra:

The largest market for CPVC pipe in India today is south and second largest market is the western part of the country and logistically what you say is correct that ultimately because pipe is the voluminous cargo and once you have ceded to the one part of the country and you want to go another part of the countries and you have to go to that region to put up a plant. That is few year Hyderabad once you make success of this plant so western part location because raw material is imported logistically it is closer to the port and from the western part of the India we can service to the western and the southern part of the country which is the largest market for the CPVC pipe.

Umesh Patel:

So as you highlighted I missed earlier one who is the supplier with whom we have entered into long-term agreement.

R.B. Kabra:

Sekisui of Japan.

Sandeep Sikka:

Sekisui Chemicals Company Limited Japan; it is a $9 billion turnover company.

Umesh Patel:

Are we looking for exclusive distributors for this product or in the initial stages we will leverage our existing distributors?

R.B. Kabra:

I think you did not hear what I just said five minutes ago. The distribution system for the pipe is that you have a distributor for a particular area and he sells through the various dealers like our sanitaryware dealer sell pipes many of them today manufactured by somebody else we will have to create this additional channel of distributor area who will then supply to our dealers.

Umesh Patel:

Sir the last question is do we accept the same run rate of 10 Crores as an interest outgo for each quarter of FY'16?

Sandeep Sikka:

Interest will remain same almost for this area. For this year yes.

Moderator:

Thank you. Next question is from the line of Vikas Mantri from ICICI Securities. Please go ahead.

Vikas Mantri:

Sir, the location of the capex in the glassware plant it has to happen along with the glassware plant itself currently that we have as additional machinery the way I understand it.

R.B. Kabra:

This is the plastic product so machinery has to be entirely different and location is the same place.

Vikas Mantri:

Is the location the same place given you are looking at 150 odd Crores.

R.B. Kabra:

Same place in the sense that yes surrounding Hyderabad.

Vikas Mantri:

So does it mean that it will be supplied along with the bottle separately.

R.B. Kabra:

Not this will be supplied separately but customer will be the same. It will not go with the bottle because once it is fitted it cannot be taken out before without breaking it. So we cannot supply fitted into the bottle because somebody has to fill the content and then put this particular closure on it.

Vikas Mantri:

So how does it impact, does it impact recycling of bottles?

R.B. Kabra:

Not really it does not impact recycling of bottles. It only helps the customer to make sure that he is not getting a counterfeit product. This is a one way gap that you can only decant bottle you cannot put any content into the bottle as long as the particular closure is there. And if you take out this closure it gets damaged and you cannot get it back.

Sandeep Sikka:

You are right, the recycling means reusing I think you want to say. For that bottle cannot be reused for us as a broken bottle can be recycled. So Mr. Kabra was answering recycling is possible for those bottle but the consumer the customer cannot reuse it clean it or reuse it.

R.B. Kabra:

So just to make you simple with an example that cannot happen.

Vikas Mantri:

People will be ready to so you are currently having 850 odd Crores of sales in this glassware so 20% more payment will happen just for this product that is the right thing to assume. Is that such a big market?

R.B. Kabra:

Yes the product is store supply I just mentioned.

Vikas Mantri:

Margins approximate margins that we can estimate in this kind of business Sir.

R.B. Kabra:

Margins are much better as Mr. Sikka just mentioned in the payback for another four to five years.

Moderator:

Thank you. Next question is from the line of Jasprit Singh Arora from Systematic Shares. Please go ahead.

Jasprit Singh Arora:

Good evening Sir, starting on the building product side the 8.5 Crores extra that we spent on the add on marketing expenses if I adjust for that our PBIT margin seem to be coming at the normalized rate of 18%. So is that correct way to interpret and how should one look at the balance three quarters in terms of you highlighted the run rate will continue but broadly what kind of margins?

R.B. Kabra:

The yearend I mentioned barring this quarter for the balancing we will be running at the same rate like we did last year.

Jasprit Singh Arora:

In terms of specifically on the ad-spend you mentioned the higher run rate will continue but not at the same absolute amount. Is that correct?

R.B. Kabra:

Basically some expenses in this particular quarter are higher as we had these kinds of campaigns but in any case we have been spending money on advertising. We have been spending money on below the line activities in the market place, so not that we have been not spending and only this year we started spending money on marketing after many, many years that is not the case. Only thing is this year especially this quarter there are some additional expenses for this decision what we have taken to put this brand ambassadors for the product.

Jasprit Singh Arora:

To understand correctly all this would go in terms ultimately for a better brand recall and in terms of getting a better realization and subsequently margins because we do not have any new capacity make up with sanitaryware so.

R.B. Kabra:

Sanitaryware capacity is coming in I think you are just.

Jasprit Singh Arora:

1 lakh and 3 lakh pieces but I am saying broadly this is given the kind of brand that we have.

R.B. Kabra:

That is around 11%, 12% from the existing capacity what we have and you know we have been talking of the Gujarat plant for last more than two years now but work is not being started because market prospects are not as good actually when we acquired the land four years ago we were growing at 18% CAGR 40%, CAGR and we thought that we will have to immediately start work on the third sanitaryware plant but then 2008 happened and after that the economy of course it comes back and goes down but the kind of recovery we were expecting and real estate market going back there is not the kind of volume growth we were expecting. So that is why little slow on putting capex on the third sanitary ware plant and whatever capacity addition we are doing at the minimum capital cost so that we are quite cost effective in terms of spending capital on the new expansion. So the brown field expansions are already cheaper than the green field expansion. So that is why if I get that whatever best we can get out of the existing plant we should do that.

Jasprit Singh Arora:

Follow up on that the expansion of 1 lakh and 3 lakhs business that you are on track as you said for March 2016.

R.B. Kabra:

Yes that is on track.

Jasprit Singh Arora:

For March 16 specifically right. Coming back to this new project you mentioned the ROCE of 20% plus so the underlying assumption as far is that the peak sales of 400 Crores plus in pipes and 150 Crores plus in caps for the fourth year and for the fifth year and third year respectively is that correct.

R.B. Kabra:

Yes.

Jasprit Singh Arora:

If you could help us understand the funding mix for this in terms of what kind of debt you would be looking at.

Sandeep Sikka:

Company may look at a fresh debt both the projects targeting on a debt equity of 2:1 because debt is the very natural thing for us considering the fact that we are full tax paying company and the leverage on March 16 is expected at 0.3% and 0.4%. So it makes a natural sense to have the debt on the balance sheet to reduce overall VAT.

Jasprit Singh Arora:

For a 220 Crores total capex is broadly 150 plus debt and balance internal.

R.B. Kabra:

Somewhere in that range.

Moderator:

Thank you. Next question is from the line of Achint Bhagat from Ambit Capital. Please go ahead.

Achint Bhagat:

Good afternoon, just couple of questions. You mentioned about the CPVC expansion that you are undertaking and the market that you are targeting is 7000 Crores am I right? In this 7000 Crores what is the market mix right now. What is the percentage of unorganized in your view?

R.B. Kabra:

The number what we are giving is 7000 Crores it is around 65% is organized and 35% is unorganized. CPVC there is very little unorganized because of as I mentioned not available it is only manufactured by four companies all over the world so you do not get CPVC regime from the market. So the CPVC if you talk to many of the unorganized may be less than 5% but UPVC of course will be around 30% to 35%.

Achint Bhagat:

What our sense is that there are three four established players who are scaling up who have experience of running this business for multiple years. So how is the company planning to position itself differently to compete on a similar quoting to them because they already have their brand established, they have the channel established?

R.B. Kabra:

We also have a brand Hindware brand is much older brand can the kind of people you are talking it and as I mentioned we are already into the building product. The brand is really well known. The dealers are in place. So we are confident that whatever kind of market studies we have done we are confident that we will be able to do this successfully.

Achint Bhagat:

Sir but if our checks suggest that the channel itself for sanitaryware and pipe is slightly different. So is it do you thing is fungible 100% that you can use your product.

R.B. Kabra:

I think I have to repeat myself as 50% to 55% of our dealer they sell pipes. So you may be correct yes distributor is entirely different and sanitary business there is no distributor kind of a thing. The sanitaryware is directly sold from company or its depot to the dealer, so either he sales or he sales through the retailer. In case of pipe there is one additional channel called distributor, which is created and then he sales to the dealers and retailers. So we have to create that the distributor which normally dealing five store or similar kind of a product but they do not sell in retails they only distribute to the dealer so that channel we have to create and back these people to work fall.

Achint Bhagat:

My last question here is that you mentioned sometime in the call that your capex is 105 Crores and you expect full revenues after 100% capital of 450 Crores it should mean roughly a 4.5 times gross block turnover. So the sense that I get from looking at the other companies is that the industry benchmark here is in between 3 and 3.5 time. So what drives the confidence of 4.5 times GB turnover?

Sandeep Sikka:

It is a higher allocation of CPVC business as compared to other. If you see most of the other players I cannot name on a call but they have a various produces wherein CPVC component is less than 10% and may be less than 20%, so their overall allocation the price of CPVC is much higher as compared to UPVC and that is why the revenues to the head is high.

R.B. Kabra:

Average realization for CPVC pipes and fitting is much higher than UPVC pipes and fitting.

Moderator:

Thank you. Next question is from the line of Ankit Jain from Equirus. Please go ahead.

Ankit Jain:

Thanks for the opportunity. Coming back on to these additional 8.5 Crores spent towards the NP. I think spent towards QUEO might not have captured in the standalone because QUEO comes under subsidiary?

R.B. Kabra:

No QUEO brand is owned by our subsidiary but what we sell in India is imported and sold from the Indian companies. So it is on the standalone.

Ankit Jain:

Now coming on to apart from CPVC facility will there be enough land in Gujarat for future sanitaryware expansion.

R.B. Kabra:

Yes the total area around 70 acres plus. The pipe business requires around 10 to 15 acres so balance will be available for the sanitaryware operations.

Ankit Jain:

Now what will be the revised capital plan for 2016 as well as 2017?

Sandeep Sikka:

There is a normal maintenance capex which generally runs somewhere around 1.5% to 2% of the gross block on the organization and apart from this these two projects are there which will be the timeline of spending under this project will be 12 to 18 months but for the rest of the organization I think total maintenance capex of somewhere around 40 to 50 Crores would be.

The 40 to 50 Crores is not the only maintenance capex, this is also for two brownfield expansions which are going on for the sanitaryware plants. So that includes that there is a Rs.5 Crores or Rs.6 Crores maintenance capex for the sanitaryware division and around Rs.10 Crores to Rs.12 Crores for the glass business put together there will be around Rs.50 Crores to Rs.60 Crores including the brown field expansion for sanitaryware.

Ankit Jain:

The volume growth has been a bit muted on the sanitaryware side. How do you think that we might have shared well in terms of competition?

R.B. Kabra:

Competition volume information we do not have because ultimately earlier we used to publish the volume information but today it is not required so we cannot comment on that.

Ankit Jain:

Do you think that lower than lower sales growth in case of sanitaryware might be because of different positioning versus the competitor or is it like market itself has grown in the lower single digit.

R.B. Kabra:

It is very, very difficult for us to comment because every company has a long range of products. There are faucets, there is plastic system, there is seat cover, there is fitting, there is tank, there is sanitaryware, there is tiles. So we do not have breakup of the competitor that in what business they have grown to what extend so we cannot comment what kind of volume they have grown in a particular product segment or what kind of value growth they have but what you see is only the total growth.

Moderator:

Thank you. Next question is from the line of Girish Chaudhary from Spark Capital. Please go ahead.

Girish Chaudhary:

This is Girish Chaudhary from Spark Capital, good evening Sir. Just have couple of questions. Firstly on your packaging product we have seen a 6% Y-o-Y degrowth this despite we taking price hike just wanted to understand what kind of volume degrowth we have seen overall.

R.B. Kabra:

Volume degrowth in the glass business is around 7.5% to 8%.

Girish Chaudhary:

What is the capacity utilization we are running at presently in the glass division?

R.B. Kabra:

The capacity utilization this again to repeat what we said three months ago approximately that we have four furnaces totaling capacity of 1600 tonnes. One furnace shutdown for last two years because there was a less demand so we shut it in August of 2013. Current operating capacity is 1300 tonnes per day and we are currently utilizing 80% to 83%.

Girish Chaudhary:

I have other question on the EVOQ business. So can you throw some light how it has performed this quarter and what is the thought process on this business going forward?

R.B. Kabra:

This because we are not declaring separately for the subsidiaries. I do not think it is right for us to give those numbers currently but yes separately required we can share separately you send us a mail and see what information we can give.

Girish Chaudhary:

What is the thought process on this business going forward, are we looking to exit or we will continue to pump in fresh capital in this business.

R.B. Kabra:

We are currently focusing on encouraging the sale and bringing it to the 0 loss level that is the focus currently.

Girish Chaudhary:

So no fresh capital will be going in this business.

R.B. Kabra:

To the extent of cash losses we have to fund in any case because it is wholly owned subsidiary.

Moderator:

Thank you. Next question is from the line of Kamlesh Kotak from Asian Market Securities. Please go ahead.

Kamlesh Kotak:

Good afternoon Sir, just wanted to check how much was the thought process out of the total sanitaryware revenue faucet wellness and sanitaryware if you can breakup.

R.B. Kabra:

The sanitaryware goes around 67%, faucet was around 21.5% to 22%, balance are other products.

Kamlesh Kotak:

What is the status of our Greenfield project now in Gujarat for sanitaryware? Is it still on track or we are using this line for the pipes business how is that business.

R.B. Kabra:

Mentioned that is the large piece of land only may be 20% of it will be used for the pipe business balance will be available for sanitaryware plant.

Kamlesh Kotak:

Then that commissioning will happen I mean the capex on that will start.

R.B. Kabra:

Sanitaryware plant.

Kamlesh Kotak:

Yes.

R.B. Kabra:

Not yet we have not decided as I just mentioned the volume growth is very, very muted and additional 12% of the existing capacity will be coming on the existing plant. So we have not yet decided when to start work on the third sanitaryware plant. That will depend how the market revised.

Kamlesh Kotak:

What kind of growth outlook you will put for this year for both the business segment.

R.B. Kabra:

12% to 15% for the building product and 7% to 9% for the glass.

Kamlesh Kotak:

This 12% to 15% is adjusting the tiles or without that.

R.B. Kabra:

Without that.

Kamlesh Kotak:

7% to 8% in glass you take.

R.B. Kabra:

Yes.

Kamlesh Kotak:

Lastly just wondering that when the market is so distressed what is the rationale for going aggressively on marketing spend, is it prudent way to look at when there is completely no growth in the market, cannot it be something which can be deferred to the latter years?

R.B. Kabra:

Basically the marketing expends is not attached to the whether there is a growth then you do not need to spend money in any case. If the market is automatically growing 20% to 25% then you do not need to do any kind of expense on marketing. So it is basically marketing is for the brand building increasing the brand awareness and the brand recall.

Moderator:

As there are no questions from the participants I now hand the conference over to Mr. Prashant Kutty for his closing comments.

Prashant Kutty:

Sir just a couple of question before we close the call. Firstly we have been actually listening to lot of conference calls and in the consumer space and everybody have been talking about some bit of uptick in the urban demand. If you could give us some comments on the same and also the fact that we are having favorable base going on to this next three four quarters and over a year if you look at it you just highlighted that you are looking at a building products growth of about 12% to 15% that seems some cut down is what you expect earlier 18% to 20% growth, so your comments on the same.

R.B. Kabra:

That is right; two reasons that, urban uptick in the consumer product largely the consumer. If you talk of consumer durable with sanitaryware it is like consumer durable business. You do not see too much optimism from any of the manufacturer and the real state the inventory is very, very high in all big cities. What we see in the growth is the complete tier II and Tier III towns basically. If you talk of large towns which are metros and mini metros some does bad and some does good. So ultimately at the end of some total of all metros mini metros there is not too much optimism at least for next two, three quarters that you must all the read lot of articles that you talk of Mumbai, you talk of Delhi NCR is lot of unsold inventory of the apartment and the new launches they have also been very, very limited in last few months. So I do not too much coming out of the builder segment but yes the individual home builders who have been making their own houses they have one off money, they have one off resources to get their expense finance through the home loans. So those segments will continue to grow in any case.

Prashant Kutty:

We also been hearing that rural rate has been pretty much muted, has actually been weaker again any comments on that because now you allotted the tier II and tier III is growing. So do we foresee that number could actually go down further given the fact that rural has seen some bit of pressure?

R.B. Kabra:

Rural market the sanitaryware we have been selling very little in any case because rural most of the people more than 70% to 75% is still go for open defecation and whenever they convert to toilet I think the first product they buy is from the unorganized sector and when they replace after then they are our customer. So this the rural demand in terms of sanitaryware is directly not affecting us number one and number two the central government scheme of clean India really picks up then I think there would be direct demand for sanitaryware but at the ground level the work has yet to start in big way.

Prashant Kutty:

Lastly one thing if I could know what is the distribution network growing at every year at I mean.

R.B. Kabra:

We added around 100 plus dealers last year and when you say 100 dealer average we presume that they would be adding around 20 sub dealers to them. So when we add 100 dealers they will be around 2000 retail outlets which of course on multi brand but they start stocking our sanitaryware as well. So last year we added around 100 plus dealers and another 2000 retail outlets, which we call them, sub dealers.

Prashant Kutty:

So typically it is growing at about 8% to 10%.

R.B. Kabra:

Yes.

Prashant Kutty:

Thank you very much on behalf of Emkay Global Financial Services, I would like to thank you also join in the call today. So if you have any closing comments.

R.B. Kabra:

Mr. Chandani will give the closing comments.

Anil Chandani:

I think we should appreciate that there is a need to grow and with the leverage at comfortable levels as Mr. Sikka also mentioned if you want to grow in size we have to see alternative opportunities and unfortunately sanitaryware market and faucet market are not too big to meet our aspirations for growth, so we have to take some risk and one quarter blip should not be taken as trend. We have shown our trend for years and years now to all of you and we have always attempted to create value for the shareholders. That vision and mission remains with us. With those comments I urge all of you to visit us in growth path and we will see that the value of the shareholders or value creation for the shareholder is the focus for us. Thank you again for your valuable time.

Moderator:

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

Note: 1.This document has been edited to improve readability.

2. Blanks in this transcript represent inaudible or incomprehensible words.

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