

Transcript

Conference Call of Huhtamaki PPL Limited

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Presentation Session

Moderator: Ladies and gentlemen, good afternoon and welcome to the Huhtamaki PPL Limited 4Q CY16 earnings conference call hosted by Aditya Birla Money. As a reminder, all participant lines will be in the listen only mode. Later there will be an opportunity for you to ask questions after the presentation concludes. Please note that this conference is recorded. I would now like to hand over the floor to Mr. Jaymin Trivedi of Aditya Birla Money. Thank you and over to you sir.

Jaymin Trivedi: Thank you. Good afternoon everyone. We welcome you to the 4Q CY16 earnings conference call for Huhtamaki PPL Limited. Today from the management we have Mr. Parag Vyavahare, who is the CFO of the company. To start with the call, we will have a brief update from sir on the results, after which we will open the floor for questions. Over to you sir.

Parag Vyavahare: Thank you Jaymin. Good afternoon ladies and gentlemen. Thank you for being patient and thank you for joining us on this call. The quarterly and whole year results, which we have published yesterday, they are I think with all of you. So, I will just quickly cover the key points in the whole year's performance.

This year results were impacted by various factors. On one side, we had the Q1, which went quite well because of the low raw material prices, which really helped us in that quarter and the growth was okay. Profitability was quite good. Q2 and Q3 were really soft. The raw material prices situation was very volatile and they were challenges on the profitability and as we entered the Q4 and in the middle of the Q4, we saw the demonetization coming in and hitting. So, as a result if we really look at it as a consolidated entity, on proforma basis, considering the last year and the whole year performance of the Positive vis-à-vis the current year and everything put together, we have roughly grown on sales, on roughly proforma basis by 3.4%, on the whole year basis. However, if we look at only the Q4 compared to the Q3, we are down by 6%. And that is primarily driven by the demonetization effect, which really hurt us. However, if one looks at the PBT, the whole year, our PBT is up by around 21% and the PAT is up by around, close to around 9.9%-10%.

So, overall I will say it has been a very satisfactory situation, because considering the fact that were challenges on the exports market with the oil situation and the currency crisis continuing in many of the markets, primarily the African markets, where we are predominantly exporting. Those were the challenges. So, the trading conditions in those economies were very difficult. And despite that I think we have managed to hold our water in those markets and managed to keep our export line largely flat. So, that I think is a positive feature. Even that at circumstances when the domestic situation

turned adverse. Obviously we had some challenges in the Q4. But, I think overall I will say, we have been able to come through with this time period reasonably quite okay, I will say.

With that I would like to throw the floor open for the questions from the participants. Thank you very much.

Question and Answer Session

Moderator: Thank you Mr. Parag. We will now begin the question and answer session. Participants, if you have any questions, please press * and 1 on your telephone keypad and wait for your turn to ask the questions. If you would like to withdraw your request, you may do so by pressing * and 1 again.

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Sir, the first question comes from Mr. Rajesh Ranganathan from Toric Capital. Please go ahead.

Rajesh Ranganathan: Thanks a lot for arranging this call. Hello?

Parag Vyavahare: Yeah, yeah, I am here. I am listening Mr. Ranganathan.

Rajesh Ranganathan: So, for the Q4 and for the full year, can you give us an understanding of the break up between the domestic and export sales?

Parag Vyavahare: Sorry, I lost you. Could you repeat, because in between there was certain changes from the operator side. So, your sentences were cut. So, could you repeat that question please?

Rajesh Ranganathan: Yeah. For Q4 and for the full year, what is the break up between domestic and export sales?

Parag Vyavahare: The proportion roughly constitutes the same. Roughly 25% of our sales are coming from the exports. So, there is not major variation compared to the whole year and the Q4. Of course in Q4 there were small variations coming because, the exports have grown by roughly around quarter two, 1.75% in the quarter four compared to the earlier period. But, of course the domestic sales had a de-growth in this quarter because of the demonetization effect which came. So, they have de-grown roughly by this thing. So, if you look at it purely as Q4 functionality on the this thing, I think the exports proportion maybe would have been slightly at around 25½% to 26%.

Rajesh Ranganathan: And in terms of your exports, do you export directly or through Huhtamaki now or global?

Parag Vyavahare: No, no, we primarily export directly. We primarily export directly. Directly.

Rajesh Ranganathan: And is there a difference in the product mix margins and things like that, between domestic and exports?

Parag Vyavahare: There is some. There is some. Because, the kind of the servicing cost and challenges which you face and the expectations of the customers in terms of the quality and service standards which are there in the exports markets are very stringent. So, with the cost of (not clear) being high and the risk involved also being high with the currency risk, (not clear) risk, the longer distances which we are travelling, so the overall cycle is much longer. So, considering that risk, the returns in our export markets are definitely better than the domestic markets.

Rajesh Ranganathan: And with oil prices now having gone up compared to the lows at the same time last year, what is the impact on our margins going ahead?

Parag Vyavahare: We as a policy, we unfortunately Mr. Ranganathan, we do not give any guidance. So, I won't be able to comment on that question.

Rajesh Ranganathan: No, not from a guidance perspective, but from a strategic perspective, how did it impact our margins historically and how will it impact in the future?

Parag Vyavahare: Surely. This industry operates is that when the raw material prices increase beyond a certain point; we do typically go to the customers for getting the price increase to be able to protect our margins. But obviously as you can understand, in the process, always there will be some time lag involved. So, generally what happens is that when the raw material prices increase, the margins tends to come down, because you are not able to instantaneously pass on the whole cost increase impact to the customer. So, for some point of time you do get some amount of hit. But, you do correct it over the period of time. That is the general situation.

Rajesh Ranganathan: But, did you also benefit when the oil prices fell quite sharply earlier?

Parag Vyavahare: Yes. That is what has really happened in the last year Q4 2015 and Q1 2016, when the oil prices went down substantially and hence the raw material prices were very low, we did benefit.

Rajesh Ranganathan: So, if you look at 2016, I think your margins, EBITDA margin was maybe 12% for the full year, but we see it was lower in the second half. So, structurally in this business, what is the sustainable margin, because historically you have done anywhere between say, slightly below 10% to 12% over the last three-four years?

Parag Vyavahare: Just give me a second. Again as a policy, I cannot give the guidance in terms of what kind of sustainable margins we can keep on earning. But, what has generally been our endeavor has been that and what has been in the past I can say is that, our EBITDA margins have ranged anywhere between 10% to 12%. And generally our endeavor will be to maintain them in that range.

Rajesh Ranganathan: And if you look at the debt currently, we have roughly about 400 crores of debt or something like that?

Parag Vyavahare: Yes, yes.

Rajesh Ranganathan: What is the expectation going ahead, is that in rupees or is that in dollars? Is it likely to go down or go up going forward? What are the CAPEX plans?

Parag Vyavahare: The debt will primarily go down going forward. The debt will go down. There is a small portion of debt which is in the foreign currency, very small portion. And the major portion of debt is in the rupee. And we do not, at least as of now our plans do not envisage any major increase in the box.

Rajesh Ranganathan: Because, if you look at our return on equity, we are roughly making 13%-15% return on equity. But, from a point of view of your long term targets, I presume they would be higher. And what needs to happen for you to reach say, 20%-25% return on equity?

Parag Vyavahare: It is too, too subjective. I don't think I would be able to give.....

Rajesh Ranganathan: In the sense, is there a significant scope for you to improve your utilization? Is there a significant scope for you to, you said margins cannot improve much from here. So, it is essentially about utilization increase. So, is that the main driver for us going ahead?

Parag Vyavahare: Yeah, the margins and the sale growth, those will typically be the main drivers for the growth.

Rajesh Ranganathan: So, what would be the current capacity utilization do you think?

Parag Vyavahare: We would be roughly at around, I will say around, of course it becomes very ballpark, because in this industry the capacity becomes a bit misnomer, because you produce very, very different, different kinds of materials using the same machines. So, your capacity utilization in that direction is always very subjective. But, roughly I can say that we will be closing at somewhere at around, somewhere between 77½ to 80½%.

Rajesh Ranganathan: Okay. And if you look at our top say, five customers, what percentage of our sales are they?

Parag Vyavahare: I will not say top five. I will say top fifteen customers roughly will constitute roughly around 60% of our sales.

Rajesh Ranganathan: Okay. And what would be our market share within these customers?

Parag Vyavahare: It will vary from customer to customer. But, generally it will vary from the customer to customer. Few customers it could be high. But generally it will be anywhere between 20% to 50%-60%. But, I am not talking about only the fifteen

customers, I am talking about in general I am talking of. That is where it generally ranges.

Rajesh Ranganathan: Okay. Because, if I look at the capacity utilization, say 80% right now, that is already quite high, given the seasonality. So, that means for us, to improve the asset turn from the current levels, there is not that much room, isn't it?

Parag Vyavahare: That is right. The present capacity, there is a small amount (audio break) maybe 7%-8% or maybe maximum 9% we can try to squeeze out from the existing capacities, maximum we can squeeze out that much and not really more than that.

Rajesh Ranganathan: Okay, go ahead.

Parag Vyavahare: So, that is it.

Rajesh Ranganathan: But, that goes back to my previous question, so in that sort of situation, if you want to improve your return on equity, what are the levers in your hand, because there is not that much room in the capacity utilization?

Parag Vyavahare: But, you always can keep on improving your product mix, through the innovations. And you can always keep on improving your expense efficiencies by improving your productivity. You always keep on doing something. You always keep on doing something, some innovative ideas and squeezing out the cost. And that gives you some room obviously.

Rajesh Ranganathan: Okay. Thanks for your feedback. I will follow up later. Thanks.

Parag Vyavahare: And also the debt reduction what we have been doing, that also gives us a reasonably good trigger for improving the return on equity.

Rajesh Ranganathan: Okay, thank you.

Moderator: Thank you sir. The next question comes from Mr. Sunil Kothari from Unique Investment Consultancy. Please go ahead.

Sunil Kothari: Thank you very much. Good afternoon Parag-bhai.

Parag Vyavahare: Good afternoon.

Sunil Kothari: Sir, broadly if you look at this acquisition of Positive Packaging last one to one and a half years is almost completed. So, broadly this benefit of synergy which we were expecting over two-three years period, they are yet to come. Where do you feel there is a scope of improvement in productivity or cost efficiency, if you can say a little bit more on this synergy (not clear)?

Parag Vyavahare: The real synergy benefits were in three areas. One was the market expansion or the more customer coverage and more extensive product portfolio. That is one. But, unfortunately with the export markets being down and because of the currency and the commodity pricing challenges, so the export markets have not afforded

much of an opportunity for the growth. So, that is why I mentioned export have remained largely flat. So, that is on the one side. The other opportunities primarily were in the raw material sourcing. Because, once you optimize the resources and those things, so that is one. And third would be on the expenses. And fourth was on the working capital management and cash flows. So, I will say the large amount of benefits from these already has been derived. It is not that and that is why you are able to see the kind of results you are able to see today. They do reflect that thing, because the kind of debt reduction we have gone through in the last two years is also a reflection of that thing, plus the expenses efficiency, despite the challenges on the growth which we have faced, the expense as a percentage to the sales have not grown, they rather have come down. So, that is another area where we have benefited. And the margin pressure, despite these challenges and the sales growth being low in this period, we have been able to sustain. So, that shows that we have been able to realize certain benefits there, which have helped us in (not sure) through the situation.

Sunil Kothari: Okay. And this market expansion and this new client acquisition, plus new market because of these synergies, fine, that is a matter of time where you will be definitely acquiring something more.

Parag Vyavahare: It is not that we have not acquired any new clients, but new clients we have kept on adding. But also what happens is that when the growth rate of many of these markets have come down, so what happens is that the effect remaining is subdued and you are not able to see that very clearly.

Sunil Kothari: So, what will be the focus area now? For growing this company maybe over the next three-five years, new segments, any product related things you are developing, any new or new market or you feel only this growth in volumes, only those can be the growth drivers? What are the.....?

Parag Vyavahare: It will be all core areas, geographical expansion and trying to expand in the various markets and trying to increase your hold in those markets, acquiring new customers, launching innovative products, which can give growth and at the same time while being more cost efficient.

Sunil Kothari: Okay. So, these are the areas in which you will be focusing in next year and then onwards?

Parag Vyavahare: That is right.

Sunil Kothari: And Parag-bhai, what about this Webtech? Last year what I understand is, it was little bit slow and very steady. How that segment particularly is growing now?

Parag Vyavahare: The current year, the Webtech has performed quite well. In the last year there were certain challenges, because prima facie as you know, Webtech operates in this pharma segment. And in 2015 we had lot of challenges coming because of the fact that many of the Indian pharma exporters faced challenges with the US FDA. So, that period there were challenges, because the derived demand which was there for the packaging, obviously got affected because of Indian exports to the US company, to the US markets had taken some amount of beating etc. But, current year

we have been able to see a very nice turnaround. And the growth has been reasonable and the profitability also has seen good rebound. Very good rebound, I will say.

Sunil Kothari: How do you see (audio break), particularly in this Webtech segment?

Parag Vyavahare: It should grow quite, it should grow reasonably well.

Sunil Kothari: Okay. And we have enough capacity there now?

Parag Vyavahare: Yes. Wherever needed, we are adding capacity. So, it is not that, because capacity is a very broader sense, there are different applications and areas. So, in a specific area where you find that there is opportunity for growth and the capacity is falling short, we do keep on adding capacity.

Sunil Kothari: Fine. And last question Parag-bhai.

Moderator: Sorry to interrupt sir. Mr. Sunil, could you please be a little louder?

Sunil Kothari: Sure. Sir, this consolidated quarter four margins, very respectable 11 point something, it is better than quarter three also. But, standalone we are falling very far, so any major specific reason or are we doing now enough effort taking to improve that to double digit, at least standalone margin, which has fallen to 9 and below 9 in Q3 and quarter four?

Parag Vyavahare: In the quarter four, what has happened, Sunil-bhai you need to understand that in HPPL, the ratio of the exports is lower compared to the domestic, whereas in Positive, the ratio of the exports is much higher. And in Q4, what we saw is that the domestic market tanked due to the demonetization effect. So, what has happened is that the substantial effect of that has come and hit the HPPL. And there has been some impact on the Positive also. But, Positive has the highest proportion of exports, has been able to better absorb that effect, I will say.

Sunil Kothari: Okay. But, we are taking now enough effort for standalone, this HPPL to....?

Parag Vyavahare: Yes very much. As you know we are going ahead with the merger. And the merger should get through in another sometime or whatever, few days. It is a matter of now few days or few weeks. So, for us practically we are looking at one individual enterprise. So, it is no more for us, whether it is HPPL making money or Positive is making. We are looking at ultimately the combined entity. Of course any portion, if they don't make money, the combined entity can't make money. Our whole focus has to be, how do I ensure that the combined entity and each of the three engines in the combined entity delivers the returns.

Sunil Kothari: And Parag-bhai, what is your observation, how things are moving now after this November, December event? Volume is picking up or it will take, what is your opinion?

Parag Vyavahare: Our understanding is that, even the Q1 2017 will have some effect. It will have some effect. The effect will not vanish so quickly. For the effects to really go off, it will be more, we will be able to see a reasonably, the effect getting largely neutralized from the Q2 onwards.

Sunil Kothari: Right. Thank you very much. Thank you.

Moderator: Thank you sir. The next question comes from Mr. Ankit Gor from Systematics. Please go ahead.

Ankit Gor: Thank you sir for taking my question. Sir, my question is with regards to Webtech first. What was the revenue in CY16 for Webtech and profits also?

Parag Vyavahare: Ankit, I would not like to talk specifically about any separate entity.

Ankit Gor: Okay. And sir second question is with regards to PIPL, where we still face many challenges we talked in couple of quarters, since couple of quarters about oil driven countries and exports. Is those challenges remains there or it is improving?

Parag Vyavahare: No, I will not say that the situation has improved. There is some minor improvement. But, there are no dramatic improvements. And there are challenges in various countries, whether you look at countries like Egypt, or you look at countries like Nigeria or South Africa or Ghana, Ivory Coast. These countries are facing their own challenges. And currency availability is a challenge in these countries.

Ankit Gor: Got it sir. Sir, it will be safe to assume that standalone business was mainly driven by Webtech performance, which you had suggested that it is a kind of a turnaround this quarter. So, is it safe to assume that?

Parag Vyavahare: Sorry, I didn't get your question very clearly Ankit.

Ankit Gor: So sir, my question was, as you said standalone was affected due to demonetization. PIPL, still challenges persist there. And whatever we see some ray of hope coming in, in consol basis was mainly because of Webtech.

Parag Vyavahare: No, I think only if you are looking at the Q4 basis, yes both Webtech as well as the Positive performed quite well in this quarter and that has really helped us maybe overcome some of those challenges of standalone business being slightly down.

Ankit Gor: Correct. So, in Q4 as well PIPL was not doing good or some respite was there?

Parag Vyavahare: No, it did quite okay. It did quite okay. And that is why we are able to see a reasonably good effect on the consolidated results.

Ankit Gor: Okay. Sir, roughly our capacity currently stands at around like a ton, if I am not wrong. What is the production number for CY16 sir, in that case?

Parag Vyavahare: In terms right now Ankit I don't have that number in front of me anyway, so you will have to excuse me for that thing and maybe you will have to.....

Ankit Gor: Okay sir. My next question is with regards to debt. Sorry I missed that part. What does the current debt stands at sir?

Parag Vyavahare: Just one second. Consolidated debt now is standing roughly at around 436 crores.

Ankit Gor: Sir, and I also witnessed the scene that this short term debt has reduced, short term borrowings have reduced drastically. So, what was the adjustment there or what was it sir, if you can explain to us?

Parag Vyavahare: Short term borrowing is basically vis-à-vis working capital related borrowings. So, these have been substantially repaid off. So, now whatever is remaining is basically are the long term borrowings, which will get repaid over a period of time. So, that is what you are able to see the effect.

Ankit Gor: Okay. So, have we started paying the debt of PIPL, which we acquired?

Parag Vyavahare: Yeah, very much, very much. So, the Positive there which we acquired was almost at the level of 250 crores. And today that debt has come down to substantially to around 40 crores level.

Ankit Gor: Oh wow, that seems okay. Then in that case, cash generation was decent, right sir?

Parag Vyavahare: Yeah, yeah, cash generation was decent.

Ankit Gor: What was it? If you can give us some amount their side?

Parag Vyavahare: Just one second. So, operating cash flow was something like, in the year 2016 was around 190 crores.

Ankit Gor: And free cash flow was?

Parag Vyavahare: Free cash flow, how do you define the free cash flow?

Ankit Gor: So, what was the CAPEX sir?

Parag Vyavahare: CAPEX was around 23 crores.

Ankit Gor: 23 crores was the CAPEX, okay. So, probably 170 crores is kind of the free cash flow.

Parag Vyavahare: Yeah, 167 crores.

Ankit Gor: Sorry sir?

Parag Vyavahare: 167 crores. But each one will take their own definition of the free cash flow, that is why I will say that it is always better to ask.

Ankit Gor: Right sir. Sir, my question was with regards to the new facility which we have talked about last quarter in the Eastern market. What is the status there sir?

Parag Vyavahare: We are constructing two facilities, one for the HPPL flexible business in North East in Assam, on the outskirts of the Guwahati and second is, for the Webtech, we are setting up a factory again in North East, but in Sikkim. But, right now the activities of construction are in full swing and the equipments already have been ordered. And we expect that the equipments are already on their way. And equipments should reach somewhere in the end of February or the beginning of March. And if everything goes alright, everything goes as per the plan, then we should be into the commercial production by end of March.

Ankit Gor: Sir, after this what would be our capacity in flexible side of the business sir?

Parag Vyavahare: The capacity roughly will go up by around, roughly you can say around 4000 tons capacity should go up.

Ankit Gor: So, currently around a lakh capacity, right?

Parag Vyavahare: Yes, yes, whatever capacity we are having, you can add to that thing the 4000 tons.

Ankit Gor: Sir, I am asking what is the current capacity there sir?

Parag Vyavahare: No, you said lakh tons, like you mentioned. So, I said at the same capacity, you can add that 4000 tons.

Ankit Gor: Sir, lakh is the right figure to work with sir?

Parag Vyavahare: More or less you can say, more or less. What happens Ankit, in this industry is that measuring the capacity at times in tons is very misnomer. It becomes very, very misnomer, because same capacity you are using for producing sometimes very thinner material and sometimes very thicker materials. If you are going to produce thicker materials, your capacity in tons will substantially go up. And if you produce only thinner materials, your capacity in tons or tonnage can substantially come down. So, that is where we are getting this challenge. And that is why, I sometimes feel very lucky that the Government has said that we need not show anymore the capacity, because that capacity figure you show and then you used to get into challenges, as to how do you say that what is capacity utilization and why you produce so much and why you produce less or why you produce more or couldn't you have produced more? It becomes very misnomer.

Ankit Gor: Right sir, I absolutely get that. And sir, CAPEX would be for this facility would be around 65 crores, if I am not wrong?

Parag Vyavahare: No, no, the CAPEX for these two facilities will be roughly in the range of around, I will say around 45 crores.

Ankit Gor: 45 crores. And apart from this, what would be the any other CAPEX we have for the next two years?

Parag Vyavahare: Yeah, we do have various capacities. Of course we are now planning to shift this Mahape unit of Webtech from there to, from the existing premises, because they are slightly falling short on the space. So, we are trying to shift it to some other premises. On that we would be spending a reasonable large sum. And plus of course there are plans to procure certain (not clear) either for the capacity balancing or for enhancing our capabilities or capability to be able to produce value added products or new format products.

Ankit Gor: Sir, what would be the amount in terms of capital outlay sir, apart from this 45 crores?

Parag Vyavahare: We are looking at roughly around 120 crores of CAPEX in 2017.

Ankit Gor: In 2017?

Parag Vyavahare: Yeah, in FY17, calendar year 2017, we are looking at 120 crores of CAPEX, provided the market.

Ankit Gor: Yeah, totally get that sir. And in 2018 sir, what would be that amount, in CY18?

Parag Vyavahare: Right now we haven't frozen any numbers for 2018.

Ankit Gor: Okay. But, definitely lower than this what we have.

Parag Vyavahare: Right now I would not like to put any estimate on that.

Ankit Gor: No problem sir. Sir, my next question is with regards to the volume numbers. In Q4 how much volume declined because of demonetization at the consol level?

Parag Vyavahare: Just one second. Ankit, I don't think I have got right now the figure for Q3 to Q4, specifically on the volume. But, compared to the last year Q4, we have grown by roughly around 5% or so.

Ankit Gor: Okay. So, last year Q4 to Q4, we increased by 5%?

Parag Vyavahare: 5%.

Ankit Gor: Okay. And sir lastly, if you can help me with just the revenue number of Webtech, because in every quarter, in every concall you mentioned the revenue of Webtech.

Parag Vyavahare: Webtech is roughly around, today is around roughly 110 crores of business or slightly lower than 110 crores.

Ankit Gor: Okay. So, you are talking about CY16, right sir?

Parag Vyavahare: Yes, yes.

Ankit Gor: Okay sir. Thanks a lot. Thank you very much.

Moderator: Thank you sir. The next question comes from Mr. Koushik Poddar from KB Capital Markets. Please go ahead.

Koushik Poddar: Thank you. You have talked about the capital expenditure of around 125 crores this year as against around 35 crores last year. Can you tell me the reason for the sudden increase in capital expenditure?

Parag Vyavahare: What happened was that when we acquired the Positive Packaging, in the years 2015 and 2016, we haven't spent much on the CAPEX. So, we are basically focused on trying to utilize the existing available capacities to the maximum extent possible and only spend on small, small sums in both the years, on small capacity balancing exercises etc. Now, the time has come where for the next level of growth, if you have to go, the spare capacity with us is not really very large. As I explained, somewhere it is around compared to my total turnover of 2150 crores, only we may be able to catch another 150 crores to 160 crores of turnover, around that by squeezing the existing capacity. If I have to grow beyond that, then I need additional capacity. And that is why we are looking at adding the additional capacity. And that is why you are able to see the jump in this thing.

Koushik Poddar: Okay. And as per my understanding, one of the levers for higher margin is having more newer products of innovation. So, can you give a sense of innovation of the newer products that you launched in the last three years, which hopefully has a higher margin?

Parag Vyavahare: Typically what we do is that, we generally try to achieve a mix of somewhere between 25% to 30% of our turnover should come from these new products. And generally we have been able to hit that ratio.

Koushik Poddar: And you normally maintain this margin 25%-30% being new products, is it?

Parag Vyavahare: No, no, I didn't say margin, I said basically 25% to 30% of turnover comes from the new product.

Koushik Poddar: Okay. And that ratio is normally maintained both the years?

Parag Vyavahare: In a year, it could be down by 1% or 2% or in a year it could be up by this thing. That is why I said, it more tends to be in that range of 25% to 30%.

Koushik Poddar: Okay. And lastly, a good amount of your long term debt is accounted for by borrowing from your parent company, right?

Parag Vyavahare: Yes, yes.

Koushik Poddar: So, is there any proposal from their end to reduce it or to convert into equities or something of that sort?

Parag Vyavahare: No, this is the non-convertible debenture. So, there is no option with them to convert the same into equity. So, that is completely ruled out. Now, this only has a bullet repayment facility, which we took it in January 2015. So, this loan is repayable in January 2020. But, we do have a prepayment option after one year.

Koushik Poddar: Okay. If you have the requisite cash flow, you can repay off?

Parag Vyavahare: And if we feel comfortable and if we feel that, okay, I did not require that cash for other purposes and then I can, we can always do that.

Koushik Poddar: So, the option is at your end?

Parag Vyavahare: Option is at our end.

Koushik Poddar: Okay. That is it. Thank you.

Moderator: Thank you sir. The next question comes from Mr. Udit from Catamaran Capital. Please go ahead.

Udit: Thank you sir for taking my questions. Sir, my first question is like, when you are bidding for a product, what is the internal metrics that you look at? You are looking at conversion margin, EBITDA margin, like how are you deciding?

Parag Vyavahare: This industry works on a slightly different parallel. This industry works on what is known as the value addition what you generate. So whatever, from the sales price whatever raw materials you are using for producing a product that you minus and then you say that, okay, I should get X amount of or X percentage of the value addition. And you will look at that thing and you will say, okay, are we comfortable with that thing, considering the complexity involved in the product or the various processes involved etc. And then based on that thing you take a call, whether you are okay with that price or you are not okay with the price.

Udit: Okay. It is basically you incorporate the total raw material cost that you have to buy for the printing and then you add some X percentage of the raw material cost, is that the right way sir?

Parag Vyavahare: No, no. A very, very arbitrary example if I have to give you, if a product to manufacture, the raw material cost is let's say Rs.70, I will generally, as a very ballpark figure, generally I will be very comfortable to sell this product anywhere between Rs.97 to Rs.100.

Udit: Okay, understood. And on the exports, as you mentioned you have lot of, 25% of your revenue is coming from exports. So does the, is it like the Huhtamaki global is bidding to the customers and then it says that, okay, this customer Huhtamaki India supplies or is it like one of your Huhtamaki India sales person who is going there and trying to win that customer, how is it?

Parag Vyavahare: In this selling effort, there is no Huhtamaki global as such coming. So, it is each country to country and each unit, which is there with you, has its own technical capabilities and based on that thing, you showcase those capabilities to the customer. So, you go yourself individually, market those capabilities to the customer and you create your own sales opportunities.

Udit: So, it will be possible that even in Africa as well, you might be competing with one of your sister companies there?

Parag Vyavahare: To some extent, yes. To some extent, yes, in a small way. But, always what happens is that, those entities which are operating there, they also have their own certain skill sets, because not everybody can be expert in everything. So, I would be having my expertise in certain areas and my stronghold and hence I would be competing with those guys in the stronghold areas, whereas they will be having their own strongholds. So, typically then what will happen, we will not generally try to just, for heck sake of it, build a stronghold in their area and then try to go and undercut them and then destroy the value for both of us. And this exactly applies the same to them and they also will not generally try to bid this thing, because then what happens, because the group tries to say that overall how it can be cooperative competition rather than being pure competition.

Udit: Yeah, got it sir. And sir, many FMCG companies are talking about lot of sustainable packaging. So, any thoughts on that regard, like how you are seeing or how are you working with them to identify this?

Parag Vyavahare: This depends on specifically the own approach of these FMCG companies, as to how much they are comfortable. Because, this sustainable packaging etc. that means a different kind of situation in terms of the whole manufacturing processes, in terms of the cost structure. And also one has to look at it that what does the word sustainability mean or what kind of (not clear) etc. it mean and what kind of set up (not clear) and depending upon that thing, we do have knowledge base with us and we embark with them. But, it is really too early in the case of the Indian environment to see any material movement on that side, I will say.

Udit: In HUL India I think has made a comment that they are trying to reduce the plastic wastage and just wanted to have your thoughts like, is that already.....?

Parag Vyavahare: What happens is that, what one needs to understand is that the packaging material which they want is a specific tailor made product packaging which we are making. So, if the customer designs, if he builds more plastic, I will have to put that more plastic. If he say no, he doesn't want plastic and he wants let's say more foil or more paper or some other material, I will have to put that material and to that extent, it is the customer's call as to what kind of content he wants to have and hence what he calls a sustainable or non-sustainable etc. So, because it is a tailor made product. Somebody is like, you go to the tailor and give him, telling him that I want a cotton shirt, he will stitch a cotton shirt for you. If somebody goes to the tailor and says, I want nylon shirt, he will make a nylon shirt for you.

Udit: Understood. And sir, when people talk about product mix, are you referring to premium product versus value products or how is it like? By premium I mean, like HUL is a premium product, so per unit of premium product process generally gives you a higher margin. Is that the right way to think?

Parag Vyavahare: It is not necessarily really like that thing, because a customer's definition of the premium, if I keep on going by that thing, things may work differently. But, we will have to look at the position from our perspective as to how difficult it is to manufacture that product. How complex the product is that or what kind of specialty you are able to build into that thing. And that really determines whether the product is a premium product and hence it can afford me the ability to charge at slightly premium, because it is fairly run of the mill product or really simpler product I will say.

Udit: So, how do you internally define what the product mix is like? Is it like the complex, like you want the X percentage of your revenues to come from products, where you have to do a lot of value addition, is it something like that? That is where is your internal target or how do you see that?

Parag Vyavahare: You try to improve the ratio of the value added product, that definitely you try to do. But, one needs to bear in mind that in our industry, it is derived demand. So, ultimately I will have to sell what the customer wants. I may like to sell more value added products, but if there is no demand for that thing or let's say I may like a value added product to grow by 25% or 40% or 50%, but if the market is not growing for those products in that proportion or if the customer's product, where this kind of packaging is getting utilized is not growing in that proportion, then obviously my sale of those kind of products cannot go up. So, it is also something what is dictated to you by the market.

Udit: Okay. And sir, if I have to understand, so which industries are have you seen adding more value added packaging and how is your end industry composition? So, is it like the (not sure) industries, where you are seeing a lot of value addition there happening or is it the FMCG industry or food packaging industry?

Parag Vyavahare: No, we really call all these as a broad FMCG industry. Because, within that trying to make those many segments and sub segments becomes at times very, very, it becomes too complex and then really that kind of data is not really available in any space, to really say that, okay, this industry gives better. So, it varies from the customer to customer and it varies from product to product. It varies from the pack prices and multiple factors. So, it really becomes very difficult to generalize like that thing.

Udit: Okay. And sir, if I have to understand the flexible industry structure, can you help me understand like who are the top players and what is the size of the next biggest competitor apart from you?

Parag Vyavahare: Next biggest competitor would be Uflex. Uflex, they will be almost on like flexible packaging, largely they may be almost of equal size to us, I can say, or around that level or whatever. And next level players will be, typically they all will be all 500 crores-600 crores turnover players.

Udit: Okay. And sir, once again on the margins, you mentioned that you will try and keep the EBITDA margins of 11%. But, if I understand like, when you are pricing your customer, you are pricing for gross margins and then it is up to your operational efficiency, whether you will be able to maintain the EBITDA margins, right?

Parag Vyavahare: Sure, absolutely. Absolutely.

Udit: Thanks a lot for this.

Moderator: Thank you sir. The next question comes from Mr. Vipul Shah from Sumangal Investment. Please go ahead.

Vipul Shah: Hi sir. Can you give separate operating margins for all three entities, Positive, Webtech and standalone?

Parag Vyavahare: No Mr. Shah, it would not be possible.

Vipul Shah: But, you are going to merge it very soon, but still at least you will not like to share that?

Parag Vyavahare: No, for practical purposes, we are looking at it as one enterprise from our perspective. And we would not like to talk about the margins of the three enterprises in three different....

Vipul Shah: Can you give any broad indication, how much margins are higher for Positive as compared to standalone?

Parag Vyavahare: No, I would not like to put any guess on that thing.

Vipul Shah: And sir, with this 125 crores of CAPEX, how much capacity will go up?

Parag Vyavahare: As I mentioned, our capacities will go up by roughly around 4000 tons to 5000 tons per annum.

Vipul Shah: Once this 125 crores CAPEX is complete?

Parag Vyavahare: Yeah, because lot of this CAPEX also is for upgradation of the equipments or for capacity balancing or for adding new formats of materials, so which will not lead to substantial increase in capacity. That is why I mentioned it is 4000 to 5000.

Vipul Shah: Okay. And lastly sir, now since GST seems to be becoming a reality, what impact will GST have on our company?

Parag Vyavahare: It is slightly premature to say, because final version of the GST law is still to be out. Various factors what they will be applying to the packaging material and to the FMCG industry are still not known. So, it is premature. But, one broad principle which you can keep it in mind is that, we are largely a B2B industry. And hence, in our case the indirect tax impact always is a pass through mechanism.

Vipul Shah: Okay sir. Thank you and all the best for the future.

Parag Vyavahare: Thank you.

Moderator: Thank you sir. Participants are requested to ask two questions in the initial round and may join the queue again for more questions.

The next question comes from Mr. Bharath Bhagnani, an Individual Investor. Please go ahead.

Bharath Bhagnani: Hello sir. I just wanted to ask that, since you said that there will be a capacity expansion whereby you will be spending about 125 crores, so is it fair to assume that we are not looking at any more acquisitions or how is it?

Parag Vyavahare: As of now there are no specific plans or nothing specific to talk on that thing.

Bharath Bhagnani: Okay. So, you are not looking actively at any, acquiring any other capacity, since you are putting up your own capacity?

Parag Vyavahare: Yeah, that is right. That is right.

Bharath Bhagnani: Okay. And sir, just one last thing. During the demonetization period, how is the industry as a whole been impacted, if at all?

Parag Vyavahare: What really happened if you see, I think the impacts are in the form that the real major effect what we are able to see is that the prices really got.....because the customer was not able to, the ultimate consumers were finding it difficult because of lack of availability to purchase from retailers on one side. On the second side, the retailers were finding it very difficult to pay to the distributors and the wholesalers. So, that is where the trade line started getting choked up. And when the order flows back to the FMCG companies started getting reduced and consequently, the consequent effect came on us, because as their sales started going down and they were getting into a bit of a destocking situation or reducing their production, their order flows to us came down.

Bharath Bhagnani: Okay. Was there any order flows from others....from some smaller companies, who were maybe not able to deliver at that point in time?

Parag Vyavahare: Not much, not much. Small pluses or minuses keep on happening, but it is very difficult to discern a specific pattern out of it.

Bharath Bhagnani: Okay. Thank you sir.

Parag Vyavahare: Thank you.

Moderator: Thank you sir. The next question comes from Mr. Udit from Catamaran Capital. Please go ahead.

Udit: Hi sir. I just wanted another question. Sir, when there is more, which carton based packaging or generally flexible packaging is there more scope for value addition, I just wanted to understand that?

Parag Vyavahare: Sorry, your voice has got slightly bugled up, so I couldn't understand your question. Can you repeat your question please?

Udit: Sir, if I compare between cartons based packaging and flexible packaging, generally where is more scope for value addition?

Parag Vyavahare: Carton is a very small business for us. So, this differentiation really doesn't matter for me, because out of my 2000 crores turnover, cartons surely will be just around 1% of the turnover. All along I have been primarily a flexible packaging manufacturer. Carton is a small, very, very small tiny portion of that portfolio to me. So, I really can't comment as to, whether the cartons give me better margins or flexible gives me better margin. That really is not just relevant.

Udit: Just from my understanding of the overall industry level that was my.....

Parag Vyavahare: Unfortunately in the carton industry, there are not many listed players. So, it really becomes very difficult to offer comments on what is the general behavior of the carton industry. Rather that has been the problem of the both flexible as well as the carton industry. The packaging industry is a very fragmented industry. And that is why you will find very less players in the public space.

Udit: Okay. And how do you see the growth of the flexible industry over the next year, like where do you see the end demand? Which industry is driving the end demand in both?

Parag Vyavahare: As the penetration in the rural market is increasing and as the demand for the ready to eat, ready to drink products or the unitary packs or single serve packs is increasing, that is where we see a very clear cut demand increasing. And also, to some extent if it (not clear) which keeps on coming, that also is leading to the demand for more and more utility oriented packaging or let's say, a very ease of use of products etc. and for those kinds of packaging, the demand is going up.

Udit: Okay, thanks a lot. That is it.

Moderator: Thank you sir. The next question comes from Mr. Ankit Gor from Systematics. Please go ahead.

Ankit Gor: Hi sir. Thanks again. Sir, my question is again on debt sir...sorry on CAPEX side, just to confirm this, sir next year 125 crores CAPEX will include this 45 crores of CAPEX we are setting up capacity, correct?

Parag Vyavahare: Yes, yes.

Ankit Gor: So, for flexible it will be around 45 crores, for flexible and remaining for Webtech.

Parag Vyavahare: No, no. Sorry, I think you are slightly getting this thing. Three facilities what we are doing, which is the flexible factory in North East, the Sikkim factory and the relocation or the reconstruction of the new factory for Webtech. All that put together roughly is going to be around 65 crores. And remaining 60 crores will be basically for capacity expansion, upgradation or adding new format etc. That is how you will look at it and that will I think be more appropriate.

Ankit Gor: Okay, that is the relocation and everything. And sir, if you can elaborate now relocation, that is what you are shifting Mahape Webtech facility to shifting where sir actually, other area means?

Parag Vyavahare: It will be nearby, just outskirts of Bombay.

Ankit Gor: Okay. And adding some machinery into the existing plants, right?

Parag Vyavahare: Yeah, other thing will basically be adding machinery to the existing factory or adding some balancing (not clear) or replacing few old equipments or adding some capacities for new formats, basically ability to build on the current portfolio.

Ankit Gor: Okay, thank you sir.

Moderator: Thank you sir. There are no further questions. Ladies and gentlemen, this concludes your conference call for today. Thank you for your participation and for using Door Sabha's conference call service. You may all disconnect your lines now. Thank you and have a good day everyone.

Parag Vyavahare: Thank you.

Moderator: Thank you sir.

Note:

1. This document has been edited to improve readability.
2. Blanks in this transcript represent inaudible or incomprehensible words.