Prozone CSC Limited FY14 Research Conference Call
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Moderator Ladies and Gentlemen, Good Day and Welcome to the FY14 Results Conference Call of Prozone CSC Limited organized by Dickenson Seagull IR. We have with us today, Mr. Nikhil Chaturvedi - Managing Director, Mr. Bipin Gurnani – President, and Mr. Amit Sabarwal from Dickenson Seagull, IR. At this moment, all participants' are in listen-only mode. Later, we will conduct a question-and-answer session. At that time if you have a question please press * and 1 on your telephone keypad. I would now like to hand over the floor to Mr. Amit Sabarwal. Please go ahead Sir.

Amit Sabarwal Good afternoon everyone. Thank you for taking time out for attending the conference call for Prozone CSC. Just before commenting on the results I would like to take this opportunity to brief you everyone about the company. Prozone CSC is promoted by Provogue India Group and participated by UK based Capital Shopping Centers Plc presently known as Intu Properties Plc. The business model is to set up, develop, and manage world-class regional shopping centers and associated mixed-use developments pan India. The strategy is basically to participate and dominate in the retail space in Tier-2 and Tier-3 cities where robust urbanization is going to take place over the next decade. So currently the promoters hold around 35%, Intu properties holds around 32.3% and the balance is held by the public.

Just to give a brief about the Intu Properties, Intu Properties is UK's largest retail real estate company. It is a FTSE-100 company owning and managing more than 7 billion pounds of assets. It has around 14 properties and 10 of which are among the top 25 properties in the UK representing around 38% of the market share in UK. Prozone CSC as a company has a fully paid-up land bank of more than 17 million sq. ft in prime locations spread across six cities, out of which 1.2 million sq.ft. is already developed and raised and another 16 million sq. ft to be developed and yet to be monetized.

Just briefing upon the business strategy for the company, the business strategy of the company is to acquire large land parcels and use 25% of the land bank basically to develop the retail, Build & Lease assets and the rest 75% of the asset is basically residential and commercial that is the mix use development in the Build & Sell model. The entire rationale behind this business model is basically the cash flow from the build & sale model gets into the build & lease model and help them to get debt-free asset over a long period of time.

Also, in the Residential segment, I would like to highlight the strategy for Prozone CSC which is to develop the entire infrastructure for the project that is the entire clubhouse before the launch of the project. It helps in two basic things: One it provides a lot of credibility to the business and also accelerates the sale of the project that we have actually witnessed in our recent launch that we had done in Nagpur where we had sold more than 315 units in the prelaunch phase itself.

One of the key things that I would like to highlight before commenting on the results is that, the company has been over the years in incubation & development phase wherein as per their business model they have developed the entire land bank and the monetization phase has just started, and if you can see the trend basically their profit which in Q1 starting this year was in loss making phase of around 45 million has been reduced to just 65 lakhs that is just 6.5 million and we believe that the trend is positive going forward and the company is getting into the green as we move on.

Now coming on to the results, the total income for this quarter is basically at around 128.4 million as compared to 121.8 million which is a 5.4% increase on YOY basis, but the EBITDA has increased drastically by 138% to around 65.8 million as compared to 27.6 million. This is basically because of the revenue recognition that has taken place in the Saral Bazaar and the PTC project that we have been executing. The Saral Bazar is well on track and the phase I is to be delivered by February this year that is Q4FY14. Commenting on the mall basically the rental income has been flat on quarter-on-quarter basis at around 44 million. However, there has been a strong traction seen into the last quarter in the mall with all the operational parameter showing us an upward trend whether it is retailer sales which has increased by around 9.8% from around 413 million to around 453 million on an YOY basis. At the same time, the foot falls have increased by around 15% to around 17.8 lakhs on YOY basis as compared to 15.6 lakhs. Commenting on to the leasing activity basically an addition of 11,695 sq. ft. has been added in this quarter with key marquee brands coming into the malls such as Killers, Lee, LG, Saajan Sarita during this quarter. Also 5 new stores are into the fit out state, equivalent to around 12,500 sq. ft. into the coming quarter. So strong traction is seen across in leasing activity as another 7 new stores are under discussion.

Commenting on to the residential project that we have, on the Nagpur project actually we have received a very overwhelming response where we have sold more than 315 units till date and currently the bookings have been stopped. We only intend to start the bookings once we start the construction of the residential towers. The construction for the residential tower is about to begin in Q4FY14 and post that we intent to start the bookings again. Coming on to the Coimbatore project where we have initiated the pre-launch this month itself, so it is very early to say much about it. But recently we participated in an exhibition on 18th and 19th of Jan during the occasion of Pongal and where we have got a very good encouraging response by the buyers.

Now I would like to hand over to Mr. Nikhil just to give us closing comments before we start the Q&A.

Nikhil Chaturvedi Hello everybody, I think Amit has covered a lot of ground. The only thing I would like to say is that we started this process last year where we said that we will build a club houses and because the club houses are complete or because the marketing offices are standard, people will show traction. Our first effort was to do this in Nagpur. Nagpur has already shown success. The marketing office of Coimbatore has just been opened on the 15th of January on the date of Pongal. I believe that Coimbatore too will show a trend similar to Nagpur and it will take us 5 to 6 months. If you realize that last year we sold out PTC and we have sold out Saral Bazar, the effect of that is showing on the balance sheet now. The effect of Nagpur will show you in the next financial year and I believe that by the time the effect of Nagpur comes in, Coimbatore will follow with that. So we should by the end of the next financial year, be on a very solid footing for this company.

Amit Sabarwal I believe Mr. Nikhil has given his view on to the way forward and I believe we can start with the Q&A right now.

Moderator Ladies and gentlemen, we will now begin the question and answer session. If you have a question, please press * and 1 on your telephone keypad and wait for your turn to ask the question. If you would like to withdraw your request, you may do so by pressing * and 1 again. First question comes from Mr. Ritwik Sheth from Span Capital. Please go ahead.

Ritwik Sheth Actually I am new to the company. So can you just give me which properties are operational and which all properties come under operation in the next financial year.

Nikhil Chaturvedi Currently on the retail side, Aurangabad center has been operating. Coimbatore retail is under construction and expected to operate in FY15. Nagpur the construction of the retail center is yet to start but as of now on the retail side we have got Aurangabad operational, Coimbatore under construction and Nagpur where the planning is complete. On the residential front, we have already launched Nagpur and as Amit had earlier mentioned that as a strategy we normally complete all our amenities space first. That has happened in cities where we are coming up with residential. But of course now we have already done the launch and our construction is scheduled to start, we have just pre launched the residential phase and also the infrastructure and development is already complete in terms of civil works.

Ritwik Sheth Basically do you have any plan to come to the metro or you will be concentrating on such cities like Tier-2 cities

Nikhil Chaturvedi Currently what we have is in Tier-2. We are open to opportunities in Tier-1 cities as well subject to the feasibility.

Moderator The next question comes from Ms. Aditi Murkute from Iden Investment Advisors. Please go ahead.

Aditi Murkute I would like to ask two questions. One is could you comment on the demand environment for housing and also on retail phases for rent given the slow down?

Nikhil Chaturvedi The demand for housing across India has slowed down, but last year when we came up with our strategy, we came up with a strategy that we will build up the entire club house upfront, build up the entire infrastructure and then we will start bookings. As a consequence of that, customer confidence is very, very high. So whatever sales takes place, it takes place with people like us because the space level is extremely high. The best part of it is that there is still a very strong demand in India for mid-priced housing. When you sell Rs. 3500 a sq. ft. to Rs. 4000 in that range where the demand in Tier-2 is extremely strong because the process of urbanization is extremely positive. Places like Bombay it becomes difficult because the housing is very expensive but urbanization in smaller towns is a phenomenon which is happening almost every quarter you see more and more people shifting and urbanizing.

Aditi Murkute But across the companies the different companies across the board are saying it has been slow both for the development or the housing or the sector?

Nikhil Chaturvedi I will just put it like this may be if the market was very fast, then I would have sold off 1000 apartments in Nagpur. But we had planned to sell only 300 this year. So we are very, very satisfied we met all our targets. We have stopped booking. So we are in a reverse situation. I am not able to comment on which company's targets what are. If someone wanted to sell 3000 flat and says that I have not got adequate demand, it might be a true case, but in our case whatever we have targeted we have managed to sell off. In terms of retail, your question, I will tell you that our first center is running in Aurangabad and have gone through 3 years of a cycle. And if you see from the data which Amit gave, is that our foot fall growth has been over 15% even this quarter. What you will realize is that good centers take time to establish and as they get established new and new retailers want to come and establish their foot prints there, which is very visible from the fact that in our center now we have car retailers who come in. So they have got

Jaguar Land Rover before Hyundai there, so there is a different sort of tenant who is coming in and we are also the most dominant in the whole of Aurangabad region that makes a difference. So retail depends on location to location. So you will find Palladium very attractive, but in some other place it doesn't work as such. So retail is all about location. In Aurangabad, we are super mall.

Aditi Murkute Are these retail rentals linked to the foot falls and consumption?

Nikhil Chaturvedi No, retail rentals are linked to revenues not to foot falls, but a jump in foot falls obviously it is unpledged normally into a revenue jump. If percentage conversion is there then the percentage conversion goes up because there is more foot fall. Because retailer sales in our centers have increased and trading density also has increased which Amit has read out to you earlier.

Aditi Murkute And you get the revenue from that?

Nikhil Chaturvedi Yes, we have an understanding with the retailers where there is a minimum guaranteed rent for a percentage of their revenue whichever is higher. So currently it all depends, I mean, there are few retailers who hit turnover rents with us and there are few people who are still on MG. So it depends on retailer to retailer, but yes we have an understanding with all retailers that we have a fixed guaranteed rent or a revenue percentage whichever is high.

Aditi Murkute And the occupancy and the levels?

Nikhil Chaturvedi Currently, the operating occupancy is 80%; sales occupancy would be at 82%. So we still have certain amount of sq. footage which is under pickup and it is scheduled to open in maybe this coming quarter.

Moderator The next question comes from Mr. Nikhil Parekh from Individual Investors. Please go ahead.

Nikhil Parekh I have one question on the Aurangabad mall. Now the mall is open for over last 3 years, however; we are not witnessing the rental income to pickup. So just wanted to understand when can we expect the rental income to start showing an uptrend? And also the presentation says that the rental income has been impacted by the renegotiation, so given that the current occupancy levels of the mall are around 80%, so I would like to get an indication as to what occupancy level would the mall be in a stronger position or a better position to bargain for higher rentals?

Nikhil Chaturvedi Actually what normally happens is that you have to work around what the environment is? Currently, if you would see that the overall economic mood is not as positive, so obviously the buyers are shying away from or spending less, the consumption patterns are lesser, people are playing safe, they are saving more so from that perspective we have to do some rental renegotiation. But on the other side, what we also been able to do are that these rental negotiations are only for a shorter term period. Second is that anytime that we do rental review or renegotiation for a short term period, we are also able to get something which is towards our benefit so for example we have been able to extend lock in period. Our sense is that things should start changing. The mall has started to get a much better traction as we can see from the foot fall increase that we have had. So as the trading densities of these retailers will move up, we will obviously start seeing better returns from these retailers from the point of view of whether it is pure rental or a turnover rent basis.

Nikhil Parekh So just wanted to understand at what point in time will the rental start moving in tandem with the increasing revenues because now over the last two to three quarters, the retailer revenues have been going up by around 8 to 10%, but the same is not being translated into the higher rentals?

Nikhil Chaturvedi I think first is that we are doing catch up right now and we feel that in the coming financial year we should start seeing positive trending and because all this while for the last two to three quarters basically we are doing the catch up part where we have done all the rental renegotiation that we had to do and hopefully now moving forward with the commensurate of recent foot fall and trading density, obviously the revenues will start hitting and looking up.

Management Our expectation is that we might have a revenue jump next year only due to higher occupancies. We do not expect that we will start getting more money from the same clients. Once that occupancy goes up, then we will be able to renegotiate and get better rentals from the existing retailers. I think the whole process will be almost two and a half years to three years.

Nikhil Parekh My second question is on the residential project, so given that in Nagpur we have sold around 315 units which translate to sales of around Rs. 170 crores at a price of around Rs. 3000, so in FY14 how much portion of that do we expect to be recognized? Any guidance?

Nikhil Chaturvedi Basically, we expect that the construction start from February onwards and if we are able to cross the threshold of basically 25%, we will be able to recognize the proportion accordingly. But our focus is completely on execution and we believe that we would be starting the execution for the residential towers from February onwards. So we are hopeful that in the coming financial years, we would be able to start recognizing around 30 to 40% of the sale that we have done.

Moderator The next question comes from Mr. Chintan Seth from SKS Capital and Research. Please go ahead.

Chintan Seth Regarding our Aurangabad experience, we had 3 years of operations and in 3 years we have started renegotiating our rental rates because of slowdown in demand and overall environment in Aurangabad. What is the strategy of the management in terms of what we are experiencing we have learnt from the Aurangabad and how it will help us in putting our safeguards in the Coimbatore Mall?

Nikhil Chaturvedi I will just put this into perspective that in Aurangabad we built a center which is extremely large. It was 800,000 sq. ft. Later, in Coimbatore it is 465,000 sq. ft. We believe that we have adequate demand today itself. So the center would start with a 95% occupancy.

Chintan Seth It is in FY16 onwards?

Nikhil Chaturvedi Yes. We expect the center to start with a 95% occupancies that is one. We have spent in Aurangabad a lot of money on the building of basements. In Coimbatore we haven’t spent that much CAPEX on the basement. It is built on stilt and the rooftop is being used for parking. And the CAPEX which has already been deployed in Aurangabad, out there the CAPEX is going to be divided. So when the Phase-II comes up, my demand will also be stronger, my CAPEX will also go in then. So these are the three main changes we have made, except for that obviously on design and everything whatever learnings we have got, we have implemented and we believe that for the newer centers all our learnings of Aurangabad has been incorporated.

Chintan Seth We have been talking about launching of our projects Nagpur has been brilliant in terms of pre-launch and in crisis, the question again comes like quarter-on-quarter we are not seeing the revenues getting into the P&L because of the only 25% completion and related revenue recognition policy you have. What we want is like a time line in terms of projects when we can see or we can look forward in terms of checking the projects as well as those revenues getting in stream in P&L. Now management is doing perfectly well in terms of losses getting reduced from to Rs. 60 lakh this quarter. That is a tremendous achievement, but again we want this into black and when we can see this getting reflected in the P&L?

Nikhil Chaturvedi Let me just put it like this, it is that anything which you sell revenue recognition will always come 12 months later. We had sold Saral Bazar a year ago; the revenue recognition has come now. So in the next financial year like we mentioned earlier, we expect that about 40% of Nagpur sales will be recognized. So basically we don’t know, we might sell more apartment also. Everything will have an impact but what we are saying is that because we have a conservative policy, we are slowly trending towards positivity. Once it is positive, it will stay positive because there is a lot of inventory IRR. So it will stay positive. So we are taking our time. We are not overly concerned about that, but what you will find is that we have a very conservative revenue booking policy and we will be appreciated by our shareholders.

Chintan Seth Given the inventory we have, you are quite optimistic about getting this into the demand is there for the fully absorption on those units, what is your view on it? Given the current situation like interest rates raising, on the demand side, the environment is a little sluggish overall so what is the management view in terms of absorption of those projects?

Nikhil Chaturvedi I will just put it like this again. The demand is extremely strong for good projects. The fact that I have stopped booking to tell you that what is the situation on the ground, we have stopped booking all together and we believe that whatever supply we have, we will peacefully be able to sell off. We study the absorption of every market. So let us say for example Nagpur, they have registered 21,000 agreements last year, out of that how many are in our price range of new flats. So let us say over 9,000. Out of that top 5 companies sold how much? All the top 5 companies sold about 350 to 400 apartment let us say for example. So we put our target at 350 and once we sell 350, we stop and that make sure that there is enough pent-up demand for the next year. If you keep supplying the market with more than the demand you would obviously say that the market is slowed down but it is not true. If you build 5 million houses and there is not enough demand for 5 million you should not be building it, so all I am saying is our target for the year was selling 300 apartments.

Chintan Seth And we have achieved that.

Nikhil Chaturvedi We have achieved that and I am very confident that next year also I will peacefully achieve it because we have stopped bookings.

Chintan Seth What is the update on Jaipur project? We have three projects currently like Nagpur, Indore and Coimbatore on residential front. We have also some interest in Jaipur I think I am not sure I didn't get the update on Jaipur?

Nikhil Chaturvedi We are not planning to start Jaipur till almost next year end.

Chintan Seth So post FY15 I think we will start looking at?

Nikhil Chaturvedi Strategy will be exactly the same. We will go there and make the entire club house, make the entire infrastructure, then start bookings. And Jaipur also the prices have risen one of the fastest in India so the pattern in Jaipur is extremely strong, but believe that the catchment in which we are, we should be able to capitalize best if we come in after a year.

Chintan Seth Okay that is the management's view to delay it for a year.

Nikhil Chaturvedi Yes.

Chintan Seth One data point on gross debt side, what is the gross debt we have currently and cash position?

Nikhil Chaturvedi Basically the debt we have is around Rs. 120 crores on the Aurangabad project and we have taken around disbursement of Rs. 40 to 45 crores in the Coimbatore project that is the overall debt that we have.

Chintan Seth And the cash balance and current investments?

Nikhil Chaturvedi Cash balance would be in the range of Rs. 15 to 20 crores.

Moderator The next question comes from Mr. Pankaj Chopra from Shanthi Asset Management. Please go ahead.

Pankaj Chopra My question is about your strategy of actually building it and selling of course probably it gives higher returns, but it is extremely stressful on your cash or in your capital employed. How do you manage that?

Management I will just put this into perspective. Most developers buy lands worth Rs. 150 crores or 200 crores. The total investment in the club is Rs. 8 crores or 10 crores. If you want to be a differentiated proposition in the market, you have to create credibility. The way people understand credibility is when they see work at site. So while we are investing Rs. 8 crores more or Rs. 10 crores more than a competition, we are not investing for today, but we are investing for the future. So we are not really worried whether we will be able to sell today or not because that Rs. 3500 or Rs. 4000 will sell. But we had actually conducted market surveys to understand the consumer might hesitate and the biggest consumer feedback was they said we get the house from the developer always. But the amenities which he promises you never get upfront and we said if we make the amenities stand upfront, will it add creditability to us and basically that is what we have managed to do. And it is resulting in, it is like saying when you study the Nagpur market or you ask anyone in Nagpur market, you will realize that we are one of the fastest selling housing colonies there. So our strategy helps us and does not take away from us. And in addition to that you get a premium also. So you get a goodwill, you get a premium and it creates a very, very credible company. You need to understand that in Nagpur we were competing with Mahindras, with TATAs, with Godrej all the big boys were there and we have outsold all of them.

Pankaj Chopra About your retailing thing, what kind of anchor tenants do you have, what you guys look out for or you have currently?

Nikhil Chaturvedi We currently have Shoppers Shop, Westside, Globus, Pantaloon, Croma, Reliance Trends, Satyam, Fashion at Big Bazaar. In terms of food we have Cookieman, and KFC. Our basic logic is we create regional shopping centers. So the shopping center we create is not only for that particular place, but for the entire region. And the basic thought process is that we should be the most dominant in that region.

Pankaj Chopra So you share a percentage of revenue or minimum guarantee is that is right? With the anchor tenants is there? Are they agreeable on that?

Nikhil Chaturvedi With everyone.

Pankaj Chopra I have a very broad generic question maybe it is not the right time to ask a question in India. You probably in the world as said you would maybe make it more relevant, but the likes of Myntra and Flipkart, etc., they seem to be doing pretty well and the growth is exponential. Do that actually impacts these retailers, the brick and mortar retailer or can India just escape that transition and go on to e-tailing much faster? Will that happen and does that impact companies or businesses like yours? Do you have any comment? I am just leaving it. It is a very broad general question. I hope you got the sense of what I am asking.

Nikhil Chaturvedi I totally agree with you that e-tailing is here to stay in India and it is going to be extremely big. Now if you see e-tailing internationally or in India, the most successful e-tailers in any part of the world are the ones who have a combination of brick and mortar and online. So if you will see it is not pure or what you call e-tailers who become the most dominant, but it is people who have combination. So retailing is here to stay. There will be particular product categories which do not need any testing, which can happen on the net directly, which will get wiped out from this market altogether, which has new challenges. So just for example, it is like a book store or that trend whatever are the trends in America are happening in India also. But you need to understand is that the experience is equally important part of retailing. So while we will have retailing, but I don’t believe that retailing become 100% of the business, so you know whatever retail is built in India, you need to understand that demand also keeps going up. When number of malls were built in Bombay there were 14 malls everyone said 14 is too much. Now suddenly people are saying “oh there is space for 4 more malls now.” What I am saying is that there is absorption in the market for hardcore retailing and for e-tailing and the combination will last and this will go on for the next 20 years.

Pankaj Chopra Do you think that these pickup in Tier-2 towns for modern retail is as strong, is it stronger? The sense I got was that maybe it is not all that exciting in the Tier-2 and Tier-3. I would like to have your comments on that?

Nikhil Chaturvedi My comment is only one thing. What happened with India was that everyone went to Tier-2 India and it is like saying that if you bring a Mark & Spencer's store which doesn't look like the London one, are you as excited about buying in. So if your retail experience is as superior, the person gets habituated to buying it locally. It is like when we used to go to America or England 10 years ago, we used to have bags and bags of goodies while coming back. Today when we come back we buy nothing. We say everything is available in India. So that difference will happen to Tier-3 and Tier-4 India and Tier-2 India also because today they are still habituated to coming to Bombay to shop. They are still habituated to going to Pune to shop. Now when they are seeing that it is all available at my doorstep, they say I don't need to go out to Pune to shop, I don't need to go to Bombay and shop. Habits take a lot of time to change. What we have observed in Aurangabad is that the most important part of what we are doing is the changing habits and once habits change it is a habit impossible for someone else also to change their habit very easily. So it will take time but we do have challenges but that is how it is going to grow and the people who do it well are obviously going to be on top of winning games there.

Moderator Thank you, sir. There are no further questions. Now I hand over the floor to Mr. Ameet Sabarwal for closing comments.

Amit Sabarwal Thank you everyone for participating for the Q3FY14 conference call for Prozone CSC. We believe that we are on the right track and we are turning green in coming financial year we look forward to surprise you on the positive side. Thank you.

Moderator Thank you sir. Ladies and gentlemen this concludes your conference for today. Thank you for your participation and for using Door Sabha's Conference Call Service. You can disconnect your lines now. Thank you and have a pleasant day.