



Ester Industries Ltd. Q4 & FY19 Earnings Conference Call

May 14, 2019

Moderator: Good day, ladies and gentlemen and welcome to the Q4 and FY19 Earnings Conference Call of Ester Industries Limited. Please note that this conference is being recorded. I now hand the conference over to Mr. Suraj from CDR India. Thank you and over to you.

Suraj Digawalekar: Thank you. Good afternoon everyone and welcome to Ester Industries Limited's Q4 and FY19 Analyst and Investor Conference Call.

We have with us today Mr. Arvind Singhania – Chairman and Mr. Pradeep Kumar Rustagi – Chief Financial Officer. We will begin this conference call with opening remarks from the management, following which we will have the floor open for interactive Q&A session.

Before we begin, I would like to point out that certain statements made in today's discussion maybe forward-looking in nature and a note to that effect was stated in the Concall Invite sent to you earlier. We trust you have had a chance to receive the documents on the financial performance and also would have gone through the same. I would now like to hand over the floor to Mr. Singhania for his opening comments.

Arvind Singhania: Thanks, Suraj and thank you everyone for joining us on our Earnings Call. I have Pradeep Rustagi with me our CFO, who will run you through our financial performance for the period under review. But before he does that let me summarize the key operating highlights and thoughts for our individual businesses going forward:

To start off, FY'19 was a strong year for us. The year wherein we reported revenue and profitability growth of 16% and 43% respectively for the quarter ended March 2019 and revenue and profitability growth of 27% and 488% respectively for the year.

While the performance during the current year was largely Films business driven, we are confident that you will see greater contribution from the other two businesses namely Specialty Polymer and Engineering Plastics in the coming years. The confidence stems from a hard work and on-ground positive developments which I will talk about during the course of the call.

Beginning with Films business: We delivered a value-driven revenue growth of 37% for the year. Performance of the business improved due to continued strong demand, improved product mix and better cost management. As we have been mentioning in our previous call, the sector fundamentals for the business has improved for the better with demand remaining strong and with limited supply in the offing, we expect

realizations to remain steady. Domestic demand continues to grow at healthy rate and we expect the market to absorb with minimal disruption, the incremental capacity of Jindal which is to come on stream shortly. Further, we are also undertaking measures towards improving our product mix by increasing the share of value-added products to 30% by FY21 from present levels of about 20%-21%. We expect the Films business to continue its growth momentum.

Moving on to Specialty Polymer Business: While the performance during the year was soft, we did see things picking up in the latter part of the year. While we admit that the performance has been below our expectation in the last few years, we certainly believe the business is on the cusp of delivering steady and consistent performance going forward. Volume of sales of Stain Resistance Master Batch MB 03 has been in the range of 300 to 400 metric tons per year during the last three financial years. However, during the last two to three months, we are seeing certain traction and a strong surge in demand for MB 03 from across the carpet industry in USA and China. The sales orders and volume forecast that we have received now from customers in USA in the month of April and May 2019 gives us confidence that we would be able to achieve sales of about 1,500 to 1,700 metric tons of MB 03 during FY20 and 1,800 to 2,200 metric tons during FY21. Expected dispatch of MB 03 based on firm orders in hand during the quarter ended June 2019 will be in the range of 350 to 400 metric tons.

Another major development that has happened during the year was a tie-up we entered into with the global chemical leader. We signed manufacture and supply agreement effective April 2019 to supply innovative Polybutylene Terephthalate (PBT). This agreement is renewable by mutual consent after two years. While the quantity of supply in the first year would not be very significant, there is a great possibility of substantial upside.

Just to give you a brief background: Innovative PBT finds applications across varied industries and products and applications, automotive to consumer and from consumer electronics to fibers. Further, we are also making progress on few of our other products like Deep Dyeable Master Batch MB 07 and Cationic Dyeable Master Batch MB06. MB07 has already been approved and the commercial sale has begun albeit with small volume. Approval for MB 06 is in the final stages. Both these products have very good potential and we can expect volumes to start picking up during the course of FY 20. We expect FY20 to be a much better year for Specialty Polymer business on the back of such encouraging and positive developments. We have always maintained that this is R&D-driven business wherein the gestation period is generally long and it takes time to deliver the returns. However, we believe that the initial learning curve is now complete and we should be able to accrue returns for our investments in the business going forward.

Moving on to Engineering Plastics business: Revenue growth of about 14% driven primarily by higher polymer rates was significantly higher than volume growth of 1.2%. Lower demand and increased competition coupled with polymer rate crash in H2, impact of US-China trade war, led to higher cost inventory resulting in margin and profitability compression. We are undertaking measures towards strengthening the business by improving its product portfolio, increasing the share of value-added products.

We are also working towards containing the cost and expenses for the business, which would help us improve the margins. In addition to the above, our cost rationalization exercise is also progressing well. As most of you must be aware, we had embarked on cost cutting initiatives wherein we had identified certain areas and measures by which we will be able to significantly cut down on the expenses.

I am happy to report that we have been able to achieve annualized savings worth Rs.10 crore during the year on the back of such initiatives. This initiative will further continue during the course of the year and we expect to bring in further cost reduction by March 2020.

To conclude, I would just like to state that we expect the business momentum to continue. We believe the current year to be more productive and profitable as the same we see positive contribution from the other two businesses, more so from the Specialty Polymer business. We expect Films business to continue to perform well and we are confident that we can significantly create value for our shareholders in the coming years on the back of improving performances.

With that I hand over the floor to Mr. Pradeep who will run you through the financial performance.

Pradeep K Rustagi:

Good afternoon, everyone and thank you for taking the time out for our call. I trust that all of you have received the investor document circulated by us earlier. Let me quickly summarize the key financial highlights for the quarter following which we can begin the Q&A session.

Starting with the top line: Our revenues from operations for the quarter ended March 19 stood at Rs.255 crore as against Rs.220 crore reported during Q4 FY18, higher by 16%. While on annual basis the same stood at Rs.1028 crore as against Rs.824 crore reported during FY18, higher by 25%. The growth was primarily driven by Film business which grew 37% for the year. Performance of the other two businesses remains relatively muted; however, we expect the same, especially Specialty Polymer business to pick up and contribute positively to the overall growth in the coming years.

EBITDA for the quarter stood at Rs. 29.47 crore as against Rs.22.67 crore generated during Q4 FY'18, higher by 30%. While on yearly basis, the same stood at Rs.108.78 crore as against Rs. 65.63 crore generated during last year, higher by 66%. Higher revenue growth coupled with prudent cost management resulted in delivering higher profitability and margin expansions. Finance cost for the quarter stood at Rs.7.79 crore while on yearly basis the same amounted to Rs.34.21 crore. As on March '19 our outstanding interest-bearing term debt stood at Rs. 75.97 crore while interest bearing working capital liability stood at Rs. 166 crore. Interest-bearing debt as a multiple of EBITDA on an annualized basis stands at 2.15 as at 31st March '19. Term debt tangible net worth ratio stands at 0.38 and total outside liability tangible net worth ratio stands at 1.12 as at 31st March '19. We are confident of maintaining debt: TNW ratio at prudent level going forward. Term debt repayment obligation since last many years has been in the range of Rs.40 to Rs.44crore as mentioned in the previous calls starting from FY20 the term debt repayment obligation will reduce to about Rs.20 crore per annum. Prudent level of debt and reduced repayment obligation has helped the company achieve comfortable cash flow position. Comfortable cash flow situation would enable the company to spare funds for expansion in future. Liquidity position of the company as indicated by net working capital and current ratio has improved significantly with net working capital at Rs.54.62 crore and current ratio at 1.26 as at 31st March 2019 as compared to net working capital of Rs. 3.92 crore and current ratio of 1.01 as at 31st March 2018. Depreciation for the quarter and full year stood at Rs.8 crore and Rs.32 crore respectively. Profit after tax for the quarter stood at Rs.8.05 crore as against profit of Rs.5.61 crore reported during Q4 FY18 while on a yearly basis PAT stood at Rs.31 crore as against the profit of Rs.5.29 crore reported during FY18.

To conclude: We believe that due to traction and positive development seen in the last two to three months, Specialty Polymer business would contribute significantly to the profitability of the company going forward. While we believe that Films business will continue to deliver consistent performance Specialty polymer business will drive the overall profitability. We are hopeful that our efforts towards strengthening the Engineering Plastics business should also compliment and contribute to the overall growth of the company.

That concludes my opening remarks. We would be happy to answer your questions now.

Moderator: Thank you very much. The first question is from the line of Aman Sonthalia from AK Securities.

Aman Sonthalia: Sir, my question is how is the current International and domestic scenario for BOPET?

Arvind Singhania: The current domestic and International scenario for BOPET is quite strong as can be seen from the results. The margins are strong, the demand is very strong and we expect domestic demand to continue to grow at about 11%-13% per annum which is very strong.

Aman Sonthalia: What about the international scenario because I think we export some quantity of BOPET in the international market also?

Arvind Singhania: Yes, we export substantial volumes in the International market and the international markets are also quite strong.

Aman Sonthalia: So, the margin in Indian market is higher or the international market is higher sir?

Arvind Singhania: More or less the same give or take a few rupees.

Aman Sonthalia: What is the split right now in the BOPET and what was it in the previous quarter?

Arvind Singhania: If I take a 12 micron commodity product, approximately gross value additions are in the Rs.55 range, that means the selling price minus raw material cost.

Aman Sonthalia: What it was in the December quarter?

Pradeep K Rustagi: December quarter was less; about Rs.42,

Aman Sonthalia: Any new capacities coming up in India and the international markets?

Arvind Singhania: India, one line, Jindal is expected to start around June or July.

Aman Sonthalia: Whether it will impact demand/supply balance?

Arvind Singhania: No new line has come in for many years and we expect this line to get absorbed with minimal disruption.

Aman Sonthalia: Any fresh major capacity coming in the international markets apart from India?

Arvind Singhania: I think there are two lines – One is Polyplex coming up in Indonesia and one is SRF coming up in Hungary.

Aman Sonthalia: While lot of the companies are setting up Plant in Hungry. Whether the Company is also planning to set a plant outside India?

Arvind Singhania: We are not at the moment planning to set up any plant outside India.

Aman Sonthalia: Recently, I have seen an article in the newspaper that there may be a slowdown in FMCG sector. So, whether it will impact our demand?

Arvind Singhania: We do not expect the demand to be impacted for us because the demand for low value packs is not disrupted where our products have used. The demand for the high value packs is affected, but not for low value packs, so for example, people are buying less of shampoo bottles and increasing their purchase of shampoo sachets. Our product goes into sachet, our product does not go into bottle. So, in fact the slowdown in FMCG for large value packs may impact, help improve the sales for our product.

Aman Sonthalia: What is the current turnover of Specialty polymer?

Arvind Singhania: Specialty polymer we ended the year with Rs.30 crore.

Aman Sonthalia: How much we are expecting in the year 2019-20?

Arvind Singhania: In 2019-20 we expect our turnover to be anything between Rs.80-100 crore.

Aman Sonthalia: What is the cost of setting up 30,000 tons plant for BOPET?

Arvind Singhania: To go to a Greenfield location it would be about Rs.300-350 crore.

Moderator: Thank you. The next question is from the line of Saket Kapoor from Kapoor & Company.

Saket Kapoor: The first point is we see our revenue declining QoQ sequentially and I think so the fall in the raw material prices that has boosted the margin. So, how has the raw material basket behaved for the last quarter and how are things as on today?

Pradeep K Rustagi: The raw material cost if you look at the March quarter it was Rs.73-Rs.75 and now it is reduced to about Rs.71, December quarter it was close to Rs.76-Rs.78.

Saket Kapoor: More granular details of how have the MEG and the other component prices been for the March quarter vis-à-vis December quarter?

Arvind Singhania: There has been no major volatility in the raw materials in the last quarter.

Saket Kapoor: MEG prices remained in a band only in the last quarter?

Pradeep K Rustagi: MEG current price is about Rs.45 / Kg and PTA is about Rs.65 / KG as of now.

Saket Kapoor: What was the average prices for the March quarter for MEG and PTA?

Pradeep K Rustagi: MEG was about Rs.49-Rs.50 and PTA was about Rs.68-Rs.69.

Saket Kapoor: So 5-6% decline was there in the raw material and it is in that band only also as of now?

Pradeep K Rustagi: Yes. Since January the prices have not been very volatile, October to December was very volatile and so was the case with July to September.

Saket Kapoor: Now the prices have plateau-ed out sir?

Pradeep K Rustagi: Yes.

Saket Kapoor: Sir, we also find in the P&L account that the employee benefit cost has gone up sir from Rs.11-14.5 crore. Is there any one-off that has been factored for this quarter? What should be the annual rate for the next year?

Pradeep K Rustagi: There is a provision for increment of Rs.1 crore that we have made in this quarter for the staff and then there is a commission payment to the directors.

Saket Kapoor: What is the commission percentage paid for the directors?

Pradeep K Rustagi: Overall it is 11%-12% at PBT level as per Section 198.

Saket Kapoor: For the shareholders, have we formulated any dividend distribution policy, any laid-out path that we will be distributing this ex-percentage of the profit after tax as dividend?

Arvind Singhania: We do not have written down dividend distribution policy; however, we have maintained the 10% dividend payment for FY'19.

Pradeep K Rustagi: Face value is Rs.5 per share, 10% is 50 paise per share.

Saket Kapoor: We have an EPS of Rs.3.75. In that case it is likely in the vicinity of 13-14% if I am not wrong?

Pradeep K Rustagi: Yes, at PAT level it is 15% dividend.

Saket Kapoor: We should look at this payout ratio maintaining, since you are guiding for better cash flow for next year also, this is the minimum we should expect in terms of the dividend distribution, just to have an understanding?

Arvind Singhania: I cannot comment on that right now. This is something that the Board has to take a view

Saket Kapoor: Sir, for this quarter, there was a sequential decline in revenue also sir from the December quarter to the March quarter. What was the major reason for the same sir?

Pradeep K Rustagi: Because the raw material PTA, MEG rates were lower in March quarter as compared to December quarter. So, the margins improved but overall selling price was lower than December quarter.

Saket Kapoor: Mr. Rustagi, could you explain the cash flow how it has been for this year and how has been the utilization of cash for the entire year?

Pradeep K Rustagi: This year we made EBITDA of Rs.114 crore, Rs.10 crore has been paid as MAT and Rs.44 crore has gone for the repayment of **debt** we have spent Rs.22 crore on the CAPEX during the year.

Saket Kapoor: Balance will be there for improving the working capital?

Pradeep K Rustagi: Yes, the gap between current assets and current liabilities. So, Rs.10 crore plus Rs.44 crore plus Rs.22 crore, that is the major expenditure. If you look at PBT plus depreciation is about Rs.80 crore, out of these 80 crore, Rs.76 crore is finance cost, balance Rs.4 crore is in the working capital.

Moderator: Thank you. The next question is from the line of Giriraj Daga from KM Visaria Family Trust.

Giriraj Daga: My first question is related to the MB 03, this guidance of 1,500-1,700. Can you just tell me what are the number of customers we are assuming in that?

Arvind Singhania: Three customers.

Giriraj Daga: About four months back, we gave the guidance which included one of the leading global carpet manufacturer, So, would they be the largest customer there?

Arvind Singhania: They are also part of the customer list.

Giriraj Daga: Second, when we talk about let us say Rs. 80-Rs.100 crore of revenue, is it like entirely coming from MB 03 or we have assumed some other products also to be part of this?

Arvind Singhania: No, majority will come from MB 03 and then we have also signed a long-term agreement with one of the largest petrochemicals companies in the world for supplying the innovative Polybutylene Terephthalate product. This is a very interesting agreement that we have signed. The volumes in the first year are not very substantial, maybe 400-500 tons but in this business is to go up to maybe 4,000, 5,000 tons over a period of the next two, three years.

Giriraj Daga: What is the revenue we assume for this year?

Arvind Singhania: So, 400 tons if we do this year as per the contract, it will be about Rs.18-20 crore. We expect to do at least about 1700 and given a guidance of about 1500-1700 but more likely we will be closer to 1700 tons in MB 03 this year and is Rs.70 crore will come from MB 03 and about Rs.15-20 crore will come from PBT contract and then there will be some other smaller products.

Giriraj Daga: My next question is the sustainability part like last time we guided, we could not deliver that. You also get the first quarter good. So, obviously that will give confidence to the investor. But do you expect this to be now a recurring exercise or it is still trial and error the customer will take it and he might review again, he might not give the second time order, what is your take on that?

Arvind Singhania: I think this time around we expect it to be very sustained. While we talk this quarter itself we will be dispatching around 350-400 metric tons of MB 03 in June quarter and we have a clear line of sight from all the customers of the volumes that they intend to pick up. We are very-very confident that we will be able to sustain this volume and grow them as time goes on.

Giriraj Daga: My last question is on the BOPET side of it. So, when the Jindal capacity will be coming in the industry, do you expect any spread reduction or do you think even if higher export, the industry has to make, the spread will sustain?

Arvind Singhania: We expect that with the increased exports, the spread should be maintained, there may be some minor disruptions that initial jerk when the new capacity comes in maybe for a few weeks or so. But we expect this Jindal capacity to be absorbed without major disruption.

Moderator: Thank you. The next question is from the line of Parth Adhiya from B&K Securities.

Parth Adhiya: Sir, my first question would be towards the Engineering Plastics side. I wanted to know if you manufacture ABS in your company?

Arvind Singhania: We do not manufacture ABS. We buy ABS and compound it.

Parth Adhiya: What will be your market share in BOPET in the domestic market?

Arvind Singhania: 9-10%.

Parth Adhiya: Another thing was again on the ABS side. Recently there has been a US-China trade war. China has actually planned to impose tariff on the ABS part or the other Engineering Plastics. I wanted to understand the impact of that if it would be possible?

Arvind Singhania: We have very miniscule volume in ABS at present. There is not much impact at all.

Pradeep K Rustagi: We also do not source it from US.

Arvind Singhania: In any case the tariff war is between China and America. India is not really involved in that.

Moderator: Thank you. The next question is from the line of Sunny Agarwal from PNB Investment Services. Please go ahead.

Sunny Agarwal: Sir, would like to know what is the CAPEX plan for FY'20 & FY'21

Arvind Singhania: FY'20 CAPEX plan is about Rs.35-Rs.40 crore. FY'20 about Rs.20 crore will be spent on setting up offline coater to produce higher value-added polyester films, this is what is going to help us take the volume of value-added products in polyester films from 20% up to 30%, Rs.20 crore is being spent there, about Rs.13-Rs.15 crore is being spent on an extruder system for recycle material which is primarily to service the contracts we have got with the international petrochemical company and products on this will also be used to make other specialty polymer from recycle material.

Pradeep K Rustagi: Another Rs.10-15 crore would be for various other CAPEX.

Moderator: Thank you. The next follow up question is from the line of Saket Kapoor from Kapoor & Company.

Saket Kapoor: Sir are we expecting Rs. 80 core topline from Specialty Polymer business for FY20?

Arvind Singhania: Rs.80-100 crore.

Saket Kapoor: Sir, with this fixed and the variable cost part should also play in the EBIT level, we should be better off than what we posted for this year as a whole?

Arvind Singhania: Basically, we expect Specialty Polymer turnover to go up from Rs.30 crore to Rs.100 crore approximately and EBIT which was negative will be at about Rs.40 crore, Specialty Polymer business will give EBIT margin of about 40%.

Saket Kapoor: How should we look for the Polyester Film and the Engineering Plastics contribution for the coming year, what should be the ballpark figure?

Arvind Singhania: As far as Film business is concerned, if you see top line should improve marginally because we have been able to debottleneck our line and we expect production increase by about 8-10% in FY'20 over FY'19. So, there will be 10% increase in volume and if I take the blended margin for FY'19 and compare it to the expected blended margin of FY'20, the FY'20 margin will be better than the FY'19 margins.

Saket Kapoor: So, there is a clear-cut understanding that the EBIT in the Polyester will also grow for this year with the improvement in margin, that will also add incrementally with the improved turnover?

Arvind Singhania: Yes.

Saket Kapoor: Sir, Engineering Plastics somehow has its vagaries with the raw material fluctuations. So, now has the prices of raw material plateauing out, how are you seeing this segment contributing going forward?

Arvind Singhania: In FY'19 Engineering Plastics was hit the most because of this America-China trade war, there was a crash in raw material prices in September-October and this particular business of ours was hit maximum. Now like you rightly said the prices is stabilized and if no other unforeseen event takes place, we expect the Engineering plastics to do a much better performance than FY'19. If this problem had not occurred in Q3, Q4 of last year, Engineering Plastics itself would have performed better.

Saket Kapoor: So, for the revenue front, what kind of top line are we looking for Engineering Plastics going forward, a ballpark figure, we did Rs.195 crore?

Pradeep K Rustagi: It should be about Rs.200 plus/minus Rs.5 crore could be in that range.

Saket Kapoor: We did Rs.200 crore for the last year only. So, we will be in that ballpark only?

Pradeep K Rustagi: Last year the first six months the prices were very good, then it dropped and then it started to stabilize. So, I am taking an average and we should be in Rs.200 crore plus/minus Rs.5 crore.

Arvind Singhania: But there will be improvement in the margin.

Saket Kapoor: what kind of margins should we expect in this business sir? Because this was abnormal year considering the fluctuation in raw material, had this been a normal year for us, what would have been the contribution from the Engineering Plastics segment at the EBIT level?

Arvind Singhania: I would imagine that going forward the margin number for Engineering Plastics will be much better than FY'19, that is what I can tell you right now.

Saket Kapoor: No ballpark figure?

Arvind Singhania: No ballpark figure.

Saket Kapoor: Is SAP in our system implemented?

Arvind Singhania: Yes.

Saket Kapoor: All across?

Arvind Singhania: We have SAP for 15-years.

Moderator: Thank you. The next question is from the line of Aman Sonthalia from AK Securities. Please go ahead.

Aman Sonthalia: Sir, we said margin in BOPET is around Rs.55. So, going forward for the next one or two years, how do you foresee the margin in the BOPET?

Arvind Singhania: Two years is a very long to predict but certainly for the current year we expect the margins to be sustained with minimal disruption because of the start-up of Jindal.

Aman Sonthalia: Why most of the companies are setting up plants outside India, what is the reason for that?

Arvind Singhania: That is something that you have to ask them, but we are not planning to set up a plant outside India.

Moderator: Thank you. The next follow up question from the line of Saket Kapoor from Kapoor & Company.

Saket Kapoor: My last point was on the finance cost part. I think you spoke about this Rs.10 crore saving for this year. How is that factored in? What kind of finance cost are we looking for the coming year with improved revenue?

Arvind Singhania: The savings of Rs.10 crore that we achieved during last year has not been fully factored into the FY'19 results, because it was achieved during the year, the full effect of this will come in the balance sheet of FY'20.

Pradeep K Rustagi: Our average interest cost has been about 11% and depending on the repayment schedule that we have and the level of current assets, etc., we should be seeing a reduction in the overall interest cost by about Rs.2 crore as against Rs.34 crore we should be at about Rs.32 crore next year.

Moderator: Thank you. Ladies and gentlemen, that was the last question. I now hand the conference over to the management for closing comments.

Arvind Singhania: Thank you everyone for joining us for the Q4 FY'19 earnings call of our company. We look forward to be in touch with you again after the end of Q1 of FY'20.

Pradeep K Rustagi: Thank you.