



Greenply Industries Q2 and H1 FY16 Earnings Conference Call Transcript October 28, 2015

- Moderator** Ladies and gentlemen, good day and welcome to the Q2 and H1 FY16 Earnings Conference Call of Greenply Industries. As a reminder all participants' lines will be in the listen-only mode and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call please signal an operator by pressing * then 0 on your touchtone phone. Please note that this conference is being recorded. I would now like to hand the conference over to Mr. Gavin Desa of CDR India. Thank you and over to you sir.
- Gavin Desa:** Thank you. Good day everyone and thank you for joining us on the Q2 and H1 FY16 earnings call for Greenply Industries. We have with us today Mr. Shobhan Mittal – Joint Managing Director and CEO and Mr. V. Venkatramani – the CFO. Before we begin, I would like to state that some of the statements made in today's discussions maybe forward-looking in nature and may involve certain risks and uncertainties. A detailed statement in this regard is available on the Q2 and H1 FY16 result presentation that has been sent to you earlier. I would now invite Mr. Shobhan Mittal to begin the proceedings of the call.
- Shobhan Mittal:** Thank you Gavin. Good evening everyone, I would like to welcome you all to the Q2 and H1 earnings conference of Greenply., I will hand over the call to Mr. Venkatramani our CFO shortly, , he will take you through the business highlights and the numbers after which we will be open to questions from your side. I will pass it on to Mr. Venkatramani now.
- V. Venkatramani:** Good afternoon friends. I welcome you to this call to discuss the earning numbers of Q2 FY16 for Greenply Industries Limited. The net sales for the quarter were down 2.4% at Rs. 400.77 crore. Plywood revenues were down by 7.8% at Rs. 287.72 crore. MDF revenues grew by 14.5% to Rs. 113.05 crore. Gross margin expanded by 360 basis points to 45.1%. Operating margins were higher by 130 basis points to 14.1%. PBT growth was 12.9% at Rs. 36.42 crore. PAT growth was lower at 1.5% primarily due to the increase in tax rate from 17% in the corresponding quarter to 25% in the current quarter. We improved the working capital situation during the current quarter which had deteriorated in the first quarter, so there was an improvement of about 8 days in the current quarter as compared to the first quarter. And our debt equity has improved to 0.54 as compared to 0.79 in the corresponding quarter of last year.
- With regard to future guidance, we had guided for a 10-12% growth for financial year 2016 but considering the existing demand situation and also liquidity which continues to be a serious concern we are scaling down our guidance and we now expect topline growth of 5-6% for the balance of the current year. We had a similar kind of growth of about 5.4% in the first half of the current year. Hence we are

expecting about 6-8% growth in topline for the current year but again this is subject to market conditions not deteriorating further. I know that this is surprising but then something which we have seen quarter-on-quarter. We were expecting things to improve in the second quarter but that the situation has not improved and could possibly see further reduction in demand in the current quarter, hence we are scaling down our guidance by 5-6% for the FY16.

Now I request you to start the question and answer. Thank you.

Moderator: Thank you very much sir. Ladies and gentlemen, we will now begin the question-and-answer session. First question is from the line of Anshuman Atri from Espirito Santo. Please go ahead.

Anshuman Atri: My question is regarding the demand for plywood, so which all categories of plywood are witnessing demand slowdown, or is it across the categories?

V. Venkatramani: I think it's across the categories but we are still seeing some growth in demand for the mid-segment plywood as compared to the premium segment of plywood. So possibly while we are witnessing lower demands for the premium plywood there is still some growth left in the mid-category segment.

Anshuman Atri: Any specific region which is facing slowdown or is it pan-India?

V. Venkatramani: I think it's primarily linked to increasing of inventories in the real estate segment. We are primarily raw material manufacturers for the furniture segment so our products are required only when secondary sales happen in the real estate segment. Over the past 6 to 8 quarters we have been seeing increasing inventories primarily in the premium segment of the real estate. So I think we will witness an improved demand situation only after secondary sales start to improve in the real estate segment.

Anshuman Atri: The second question is regarding the MDF segment which is seeing a much better growth. So is it primarily driven by taking market share from unorganized players moving from low grade plywood to MDF or is it also you are seeing some new demand coming in for MDF category?

Shobhan Mittal: Yes, there is a shift because unorganized plywood prices have been going up so there is a shift in that segment. We have also been able to foray into certain government sectors with new CPWD specifications and the product getting approved in the CPWD platform, so we have been getting some demand from the government side as well. And, of course, we have been a little aggressive with our schemes and discounting certain profitable products to gain some market share from competition as well. Imports with the increased foreign exchange valuations, imports are also becoming a little more expensive so we are able to compete in certain segments there as well. So overall markets are challenging but we are trying to find new avenues to continue the growth of MDF sales.

Anshuman Atri: One last question was regarding the margins. How much of raw material benefits can we see in the next two quarters?

V. Venkatramani: We are not expecting any major benefits on the raw material front because I think we have already seen raw material prices softening over the last 2 to 3 quarters, so we don't expect any further reduction in raw material prices.

Moderator: Next question is from the line of Girish Choudhary from Spark Capital. Please go ahead.

- Girish Choudhary:** Following up on the MDF question basically, so just wanted to assess what is the current price differential between unorganized plywood and MDF, so just wanted to know is there any scope for further price hikes in this segment?
- Shobhan Mittal:** Unorganized plywood also comes in a vast range of prices. Certain plywood is lower than the MDF, whereas prices higher by 20-25% from our MDF also falls in the unorganized category so there is no definitive unorganized segment with a definitive price segment in the plywood area because it is a very vast range of unorganized plywood with vast range of pricing. So basically we are, of course, trying to compete with different segments and like I said certain cases where the plywood prices are very low and yet the raw material prices increase has affected them to a large extent to a very high percentage level in that case, of course, they are becoming uncompetitive. But as far as price hikes are concerned if you see we had taken a price hike at the beginning of this financial year. We see a resultant average realization increase of about 2.5% even though we had discounted and launched some incentive schemes in the market to the dealers, so in the immediate near future I do not see any major possibility of any further price increases in the MDF business. I mean maybe towards the end of this financial year looking at the market scenario, looking at the demand, looking at our costs and raw material scenarios we can take a call on that but at the moment there is no plan for any price increases.
- Girish Choudhary:** Secondly I have a question on plywood segment, so we have seen a volume de-growth of 2%. It will be helpful if how the premium products have fared or let's say how Ecotec brand has fared, just give a sense?
- V. Venkatramani:** Coming to the volume front if we look at the current quarter we had a volume growth of 16% in the Ecotec category and if we remove that from the plywood business our plywood volumes have de-grown by 8.7%.
- Girish Choudhary:** Which is all premium plywood?
- V. Venkatramani:** Yes, that is all premium plywood.
- Moderator:** Next question is from the line of Kartik Gada from Val-Q Investment Advisory. Please go ahead.
- Kartik Gada:** A couple of questions. One, in the opening remarks you mentioned some issues regarding liquidity. Can you please elaborate on that?
- V. Venkatramani:** Like I said, since there is a reduction in demand, demand is at a premium so dealers are willing to lift material only if you are prepared to give a higher credit period. We had given some higher credit during in the first quarter but then we took a policy decision that we would not extend further credit and in fact we would reduce the extended credit which we had given in the first quarter. So that obviously has had an impact on the topline of the plywood business.
- Kartik Gada:** Secondly, somewhat linked with one of the earlier questions, so when demand is under so much pressure and you mentioned that in some of the categories of MDF the unorganized segment is also under pressure. Are you seeing whatever demand growth is there is it coming more in the organized segment, is in anyway unorganized segment feeling the pinch more than us?
- V. Venkatramani:** Yes, would definitely say that the unorganized segment is feeling the pinch higher because they are being hurt both on the margin front as well as the working capital, so it's more difficult for them to arrange increasing working capital requirement. So

definitely most of the unorganized segments are either reducing production or in some extreme cases they have also closed down their production unit. So definitely the unorganized segment is facing a tighter situation as compared to the organized segment.

Moderator: Next question is from the line of Karan Desai from L&T Mutual Fund. Please go ahead.

Karan Desai: In the presentation you had mentioned that our expectation of growth in the range of 8-10% while in the opening remarks you mentioned that 6-8%. Could you throw some light on it?

V. Venkatramani: I think that was the guidance we had given at the beginning of the year. We are reducing our guidance and scaling down to about 5-6% considering that we have grown only about 5.4% in topline in the first half of the current year and we are not expecting any major improvement in the second half. Considering the existing demand situation we are expecting that we will have a similar growth in topline in the second half of the current year.

Karan Desai: So that would be in the range of 5-6%.

V. Venkatramani: Yes.

Karan Desai: And majorly lead by MDF?

V. Venkatramani: Yes, that's right.

Karan Desai: So your MDF capacity for the quarter was almost at 90%. Post once it reaches that 95-96% how do we expect to fulfil the demand because our plant won't be coming for at least a year now.

V. Venkatramani: We can scale up our production to at least 115% of capacity if there is sufficient demand in the market. So while we are currently operating at about 90% of capacity once the demand situation improves, we can scale up capacity utilization to about 115% which I think should last us till end of FY17 or say the first half of FY18. So possibly we would have a lower growth level in FY18 till the new plant starts commercial production in FY19. But we think we have sufficient capacities for the current year and the next financial year.

Karan Desai: What would you attribute to the much better growth numbers in the MDF division compared to the plywood division because since last 2-3 quarters this division is doing quite well? Is it because of the pickup in commercial because you also mentioned that Ecotec which is the commercial ply is also been doing well. What are your observations?

V. Venkatramani: See, if you compare MDF to plywood, I would say that the competition is far more organized in MDF. There are very few domestic manufacturers, including Greenply there are currently about five manufacturers in India and imports of MDF have also been hit to a certain extent because of appreciation of the Dollar versus the Rupee. So all these have contributed to some extent to growth of MDF and also rising cost of raw materials in the plywood segment primarily the price of say veneers over the past one year. These have all together contributed to a better growth rate in the MDF segment. And secondly yes, regarding the Ecotec category we feel that since the inventory increases are primarily happening in the premium segment and there is still some growth happening in the mid-segment or the economy segment in the real estate segment, so mid-category plywood has been doing reasonably well.

- Karan Desai:** Do you think it's also because of commercial leasing been better since last two quarters in the metros?
- V. Venkatramani:** I wouldn't think so because we are not supplying too much to the commercial segment, so it's primarily about plywood whether it's premium or residential finally it goes to the residential category.
- Karan Desai:** Market share has been intact across categories?
- V. Venkatramani:** I wouldn't know about across categories but if you look at the total plywood segment I would say yes, our market share has been intact.
- Karan Desai:** And even in MDF, right?
- V. Venkatramani:** Yes definitely.
- Karan Desai:** In MDF there are these rumors of anti-dumping duty coming in, what could be the benefit?
- V. Venkatramani:** It's not a rumor anymore it has already been implemented. Like previously if you look at the anti-dumping duty structure on MDF in the past it was linked to price levels that it was fixed at different levels for manufacturers in different countries but now it has been linked as a percentage of the import price. So I think this will benefit the domestic industry to a far greater extent, this came into effect only during the current month, so I think that should have a far better benefit than the past anti-dumping duty structure.
- Karan Desai:** And what is that percentage?
- V. Venkatramani:** Karan, I don't remember the exact percentage. I will check that up and come back to you. It's a certain Dollar value per cubic meter of MDF. I will give you the specific details later.
- Karan Desai:** So we can see some realization growth over there in the coming quarters?
- V. Venkatramani:** I don't think we would be concentrating on increasing realizations rather we would be concentrating on improving the capacity utilizations, I think that would have a better impact on our overall profitability if we could increase capacity utilizations to 100% and beyond.
- Karan Desai:** Last question, one of the observations from the Balance Sheet is that although the growth rates have not been poor for you, your Balance Sheet has not deteriorated in fact your Working Capital cycle has improved, so was it a conscious decision?
- V. Venkatramani:** Yes it was a conscious decision. In fact we had a meeting after the Q1 numbers where the Working Capital situation had deteriorated and we took a conscious decision that we would reduce the credit to the market especially the additional credit which we had extended in the first quarter of the year. So we have reduced credit to the market and that has definitely had a negative impact on the topline. But I think it's a conscious decision to do that so that we don't have bad debts in future and we feel that it would have a beneficial impact on the long-term.
- Karan Desai:** Because of that have you seen that a particular dealer who was keeping an 'x' amount of inventories keeping 'x' minus 10% or 15% lesser?

- V. Venkatramani:** It possibly is. I haven't had time to analyze that for the current quarter but yes looking at the fact that we have de-grown in the plywood business I would definitely say that decision has had a negative impact as far as topline growth is concerned.
- Moderator:** Next question is from the line of Bhavin Cheda from Enam Holdings. Please go ahead.
- Bhavin Cheda:** You said the topline growth in FY16 would be in line with the first half growth of 5-6%?
- V. Venkatramani:** Yes, that's correct.
- Bhavin Cheda:** Actually we were looking for double-digit growth at the start of the fiscal, so what has changed dramatically?
- V. Venkatramani:** You are absolutely correct Bhavin. We were projecting a topline growth of 10-12% at the beginning of the year and we thought it was a conservative guidance but then the demand situation has deteriorated than what we had expected. In fact we had expected the situation to improve from Q2 of the current year but we feel that it has deteriorated further from what it was in the first quarter, so we are revising our guidance.
- Bhavin Cheda:** And this is mainly in the plywood segment, right?
- V. Venkatramani:** Yes it is in the plywood segment but I think we are facing a challenging situation on the MDF business also. So as far as demand is concerned I think it is challenging across all categories of products but it's not affecting the mid-segment plywood or MDF to the extent that it is impacting the premium category of Greenply Plywood.
- Bhavin Cheda:** And the other thing is on the tax rate. I think this quarter you took a tax credit, so what would be the effective tax rate going forward because I think this year there was a benefit of Rs. 10 crore.
- V. Venkatramani:** There isn't any benefit of Rs. 10 crore. Like I mentioned our tax rate was about 17% in Q2 of last year which has gone up to 25%, so I had given a guidance of about 23% for the full year. So I think we will be somewhere in the range of 23-25% for the current year.
- Bhavin Cheda:** What would be the CAPEX in the first half and for full year what is the number?
- V. Venkatramani:** We haven't had any project expenditure but there have been some maintenance CAPEX, so I think we would have about RS. 30 crore of maintenance CAPEX for the current year.
- Bhavin Cheda:** And the Andhra Pradesh project would you be spending something this year?
- V. Venkatramani:** We might be because we are still in negotiations with MDF vendors. So I think possibly I will be able to give you better clarity by the end of November or beginning of December once we come to a conclusion on the technical as well as the commercial aspects of the new plant.
- Bhavin Cheda:** On the margin front this 14.5% margin in first half, will that be maintained, or you see a margin pressure also going forward?

V. Venkatramani: Like we had given the guidance of about 100 bps improvement in margins for the current year, so I think we should be able to maintain that somewhere between 100-130 basis points.

Moderator: Next question is from the line of Dhiral Shah from GEPL Capital. Please go ahead.

Dhiral Shah: By FY17 do you expect double-digit recovery in your plywood as well as MDF segment?

V. Venkatramani: See, I would not like to give any numbers for FY17 because if you look at the demand situation we don't have clarity even for the current financial year, so I wouldn't look beyond a quarter at the current time.

Dhiral Shah: Do you expect margin expansion in MDF segment in second half also?

V. Venkatramani: I think we should be able to maintain operating margins somewhere between 27-28% for MDF.

Moderator: Next question is from the line of Kuldeep Khanapurkar from Barings Asset Management. Please go ahead.

Kuldeep Khanapurkar: I am a bit confused with your commentary actually. Your second quarter if I see the plywood de-growth is 8%. You are saying full year growth of about 6-8% and in the first half, rather first quarter you had a decent 18% growth in the plywood business, so why there is a big swing happening in terms of growth inter-quarters. So can you help me understand that part? And the second thing if you see across the categories, be it paints or tiles, there is a demand deceleration but not to the extent that probably plywood seems to suggest, so why is there a significant deterioration in the plywood business in general, can you just explain that also?

V. Venkatramani: There are two factors, one is the demand situation and the second is the liquidity situation. So if we are prepared to extend higher credit period we could possibly achieve a topline growth of 10-15% for plywood. But we took a conscious decision not to increase working capital in the plywood business because we have to conserve resources for the new MDF plant, we have decided that we would not extend credit period, higher credit period in the plywood business. If you have noticed our credit working capital situation position in terms of number of days had increased in the first quarter. We gave a clear message to the sales team that we wanted a reduction in the working capital days and if you observe our working capital days has reduced by 8 days in the second quarter and we would continue to keep a tight rein on the working capital situation. So primarily because liquidity is a serious concern, we are giving a lower guidance of 5-6% for the current year. If you look at the first half, we have achieved a topline growth of about 5.4% across both the businesses put together and we think we would be able to achieve a similar sort of growth because business was under pressure in the second half of last year also. Am I clear?

Kuldeep Khanapurkar: Well that's fine but on the other side you are also saying that you have not lost market share. So when you have degrown on 8% you have not lost market share so most likely industry level de-growth is about 8% that seems to be significantly higher than other categories of building material, so not able to reconcile.

V. Venkatramani: If you look at other categories of building material products and compare them with our products there is a timing difference. Like if you look at tiles, sanitary wares, etc., these come into use when a project is being put up and it happens irrespective of whether secondary sales are happening or not happening in the real

estate segment because tiles and sanitary wares are used when the project is being constructed. Our products come into the picture at a much later date only when the units are occupied by the final residents, so furniture manufacturing happens at a much later date. So as long as inventories are increasing in the real estate segment there would be demand pressure on our products.

Kuldeep Khanapurkar: Okay but then you are guiding for full year growth of 5-6%. So what will cause that swing from (-8) to (+5)?

V. Venkatramani: If you look at it we had about 14.5% growth in the first quarter and we had 2.5% degrowth in the second quarter. If you compare to the last year's numbers the market was not as bad in the first half of the last year as it was in the second half of last year, so since we have a lower base effect coming into the second half of the year we think we would be able to maintain the growth numbers. The second half of last year was significantly lower than the first half.

Moderator: Thank you. As there are no further questions from the participants I would now like to hand over the floor to the management for their closing comments, over to you sir.

Shobhan Mittal: Thank you very much everyone for being on this Earnings Call and I hope we have been able to answer any concerns. If there are any further queries feel free to contact us and we hope to see you during the next call that we'll have for the next quarter. Thank you.

Moderator: Thank you very much sir. Ladies and gentleman, on behalf of Greenply Industries that concludes this conference call. Thank you for joining us and you may now disconnect your lines.