AYM Syntex Limited
Q3 FY19 Results and other Business Update Conference Call
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Management: Mr. Abhishek Mandawewala – Managing Director & CEO
Mr. Himanshu Dhaddha – Chief Financial Officer

Moderator: Ladies and gentlemen, good day and welcome to the AYM Syntex Limited Conference Call to discuss the Q3 FY19 Results and other business updates. On behalf of AYM Syntex limited, we have with us the key senior management including Mr. Abhishek Mandawewala – MD and CEO, and Mr. Himanshu Dhaddha – CFO.

As a reminder, all participants' lines will be in the listen only mode. 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 touch tone phone. Please note that this conference is being recorded.

Before we begin, I would like to state that some of these statements made in today's discussion may be forward looking in nature and may involve risks and uncertainties. I would now like to hand the floor over to Mr. Himanshu Dhaddha for the opening comments. Thank you and over to you sir.

Himanshu Dhaddha: Thank you. Good afternoon everybody. I welcome you all to our conference call on company's behalf. Let me begin this conference call with a short update on Q3 results which is already in the public domain as well as on our website. AYM Syntex posted revenue from operations of Rs.245 crore for the quarter ended December 2018, which grew by 8% over corresponding quarter last year and slightly de-grew by 3% over Q2 FY19. On YTD basis we have grown by 15% on account of higher exports.

In terms of tonnage, we did about 11,975 tons, which was about a 6% less as compared to Q2 of this year. However, while comparing with the Q3 of last year it de-grew by 13%. On YTD basis we are almost at similar levels in terms of tonnage as compared to the last year nine months.

Demand in Q3 was severely affected with the pricing pressure continued on account of persistent volatility in the raw material prices resulting in lower utilizations at the plant level which has now largely got stabilized in Q4.

Exports as a percentage of net revenue was at 36% in Q3 as compared to 32% in overall last year FY18. BCF expansions got operational in Q3 FY19 was into stabilization mode and the benefit of it might accrue in the Q4 FY19.

EBITDA for the quarter has improved and it is at 19.9 crore which is 8% to NR as compared to 18.5 crore in Q3 FY18 and 18.3 crore in Q2 FY19. EBITDA per ton was also on the higher side this quarter at around 16600 per ton as compared to around Rs.14400 in the previous quarter and 13,400 in the Q3 FY18.

Profit after tax because of the higher depreciation and interest cost on account of the increase in CAPEX in BCF lines which got operational in this quarter, profit after tax stood at around 0.8 crore as compared to 2.3 crore in previous year same quarter and 1.4 crore in Q2 FY19.

The net debt figure stands at around 263 crore as on December which is more or less at similar levels as compared to Q2 FY19 although net debt to EBITDA ratio is at 4.2, I think we have almost reached peer debt levels and debt will continue to actually decrease from now onwards.

Total gross debtors was at around 96.9 crore with increase in sales in this year as compared to 87 crore in March 18. Out of this debtors, above 180 days is hardly at around Rs. 1 crore. Current ratio is currently maintained at 1 as against 1.2 last year.

Update on CAPEX is that, in the current quarter we have spent around almost around 16 crore on CAPEX, however capitalization was done to the extent of 11 crore. All other projects except project six already has been completed. In project six, till now we have spent around 95 crore out of 119 crore sanctioned amount. We are almost at the fag end of the CAPEX cycle with few more machines or some nominal CAPEX which are likely in Q4 of this year or Q1 of next year. With this information note, I am handing over to my colleague Abhishek who can provide some more business updates on Q3. Over to you Abhishek.

Abhishek Mandawewala: Good afternoon everybody. I will start with the business updates for Nylon and Polyester. It was once again a tough quarter. In line with some of the comments which made last time if you remember, we had a sharp fall in the raw material prices as a result of the price decrease of oil in October and purchases from many of our customers that actually come to an absolute standstill in the month of late October, throughout November and it continued onwards until the middle of December. Utilizations and sales for this quarter dropped to levels that were seen previously only post demonetization and GST implementation months. But, however in the last few quarters there has been a focus on rationalization of cost, several of our initiatives are on track and we are internally seeing some cost go down. We have closed down our one warehouse and are planning to close down another. We have shuffled raw material suppliers however some more churn is remaining and some further opportunities can be exploited. We have achieved significant cost savings in the area of steam generation. We have also consolidated our organizational structure leading to reduction in personal cost. While continuing on this journey, we have now taken up through put improvement projects which should hopefully play out in the next three to four quarters. The negative thing is that some of the impact of these improvements has been negated by the disproportionate rise in power cost over the last three to six months.

Coming back to the business, In last quarter, We have also had an additional impact of raw material inventory particularly in Nylon as we import most of our needs and because of imports, our lead times and volume of inventory are higher, as a result of which some of the old purchase as and when they arise leads to inventory loss. This impact was also seen in January in Nylon and should start easing off by the end of February or beginning of March. In Polyester, however our inventory value has started already to match market rates from January onwards, the reason for the quick equalization with the market rate is that the inventory in Polyester is significantly lower because the raw material of Polyester is very well available in the local market. On utilization front, We are now back to normalcy levels since the middle of January, lot of existing work is still going on in the customer addition front and we have added one international automotive customer in last quarter and a couple of new carpet customers with whom discussions and approvals had been going on for fairly long.

I will move to Palghar business, in Palghar, We have again face very similar challenges that I described to you in respect to Rakoli the BOI text since then again the volume have picked up. We have faced some margin pressures in few markets and have decided to discontinue some businesses instead of denting market image and dropping prices but against this reduction, we have several initiatives of new product and customer development in the pipeline and we have also seen some successes in the last quarter. Carpet segment for Palghar is progressing fairly well and our sales in January in this segment although small are growing fairly rapidly and I hope that we will see some volume pickup in this area over the next few months or quarters. Moving to the BCF segment, BCF volumes were relatively less affected as compared to the other two segments by this price volatility. As of now, as we now have extra capacity, active canvassing of customers is now in full flow. Earlier, because our capacity was fully utilized, we were not able to commit to customers about the volumes which we are now in a position to do so. While we have not been able to occupy our tri- color line which is the new product that we have introduced as part of our expansion. In pipeline, we have several prospects for business in this segment which is under approval for color as well as quality. We are excited about this new line as it is a differentiated segment and we have few good opportunities which we hope to capitalize over the next few months or quarters. SDN volumes continue to increase and as said before this is valuable business for us due to the high quality of competition. We have had also huge interest from customers in the automotive segment which is the highest quality segment. In BCF again, there is a buyer of solution dyed Nylon products. Few of our products have been approved and we hope to start business soon in this area. This has been a three plus year project for us and hopefully we would like to take this to the logical conclusion soon with all the efforts that have been put in. Now, while I capacity has expanded by almost

60% it will be difficult to immediately occupy all the lines at full capacity right away. However we hope that the developments is SDN Solution Dyed Nylon tricolor and auto segment should soon start contributing to increase in volumes. The CAPEX cycle as Himanshu mentioned is more or less over and we have not planned any more CAPEX from here on apart from some minimal residual payments of CAPEX already committed such as the guarantees which you pay after few months which again is very minimal we are more or less touched our peak debt in the month of December and from here on, would like to use bulk of our cash flows towards repayment of borrowings and reduction of interest expense. I remain gung-ho about prospects of the business. We have lot of levers to improve the profitability from here on including the cost rationalization that we have undertaken, the utilization of the BCF lines and better utilization of POY- Tex as well as utilization of Palghar capacities. With that, I would like to hand over the floor to any questions that any investors have.

Moderator: Thank you. We will now begin the question and answer session. Anyone who wishes to ask a question may press * and 1 on their touchtone telephone. If you wish to withdraw yourself from the question queue you may press * and 2. Participants are requested to use handsets while asking a question. Ladies and gentlemen we will wait for a moment while the question queue assembles. The first question is from the line of Ankit Gupta from Bamboo Capital. Please go ahead.

Ankit Gupta: Abhishek, if you can highlight how is the demand on the Polyester side? I think in last quarter, we had been facing issues on Polyester side so with the post Q3 as you had mentioned, in January are we seeing pickup in demand on Polyester side as well?

Abhishek Mandawewala: Yes, so from the middle of January, all the volatility reduced slightly and customer again came back into ordering mode and from January onward, I think we are back to where we were before this increase and decrease that happened.

Ankit Gupta: Okay. So most probably, at least the volumes will not see much decline going forward like what we saw last quarter.

Abhishek Mandawewala: Yes, so last quarter was an abnormal quarter. Our volumes were much lesser.

Ankit Gupta: Okay. And any issues on Nylon side. Nylon has also stabilized or are we facing some issues there also?

Abhishek Mandawewala: Since the time that the antidumping duty has gone, whatever the impact on the margin is there that is there but apart from that, it is stable. There is nothing. Whatever little bit decrease happened, it happened in November-December. Now we are back to the normal mode.

Ankit Gupta: Okay. And on the BCF expansion side, I think last quarter also you have highlighted that we already have orders in hand for at least some of the capacities or more than 50-60% of our capacities, so how is the ramp up there for the customers whom we have already tied up for the additional capacity.

Abhishek Mandawewala: It is not a small volume. It is almost 60% increase in capacity. So just of it, this way the first five years of our existence whatever we have sold, we are now 60% more than that, the target is or what we need to do is we need to sell 60% of what we sold in the last five years immediately. So, it is not easy to do that maybe some of that 60% we will use to lower end opportunistic kind of orders to fill up some of the capacity but as soon as we started the lines there was some backlog of orders and the volumes went up but it is not easy to sustain at that level unless some new programs materialize and that we see a lot of traction and lot of new prospects and we are just literally waiting and there are some programs which we are expecting very shortly and as and when that materializes we should be able to start filling up the capacities. And you must also remember that the tri- color was a completely a new area for us. So, out of all the capacity, 50% of the new capacity is actually tri color. Now, in this tri- color, we have to start from zero, and we could not do anything in tri color, hence, now we have started canvassing. There are three or four good potential programs that we have now getting and I do not know how long it will take to materialize, typically we have seen that it's a yearlong exercise to add a customer but we are also looking at some opportunistic orders in the mean while but even then, it takes some time to match the colors exactly match within the delta- E the exact color and get the customer to switch over from his current source to us. So we are patient, hopefully it will all workout in time.

Ankit Gupta: Okay. So out of this, 50% is tri- color and 50% is what we are currently manufacturing. Correct? At least this 50% you expected the ramp up should be significant next year FY20.

Abhishek Mandawewala: Yes, I am pretty sure that at least in FY20 across the year we should be able to utilize the full. We should be able to utilize more or less the complete expansion of the capacity.

Ankit Gupta: Even tri- color or not the tri- color?

Abhishek Mandawewala: Hopefully, even tri- color because the tri- color if we are, until we do not get right now, we have extra capacity but if there is a delay in getting the approvals of the tri- color then we will start to use the tri- color as mono color as the existing line.

Himanshu Dhaddha: That machine has that flexibility.

Ankit Gupta: Okay.

Abhishek Mandawewala: And, in such a way that we didn't want to be stuck for too longer time that would have been very risky, so we designed the machine in such a way that tomorrow, if there is any delay then we can go for mono color.

Ankit Gupta: Okay. And in your opening remarks, Abhishek you had talked about some of the margin lever which are available in the business. If you can briefly talk about the major ones which you see which can materialize in FY20.

Abhishek Mandawewala: I think, the biggest lever is always the, if you ask me the highest impact that anything can have on the profitability or the business is the volumes because our fixed cost is actually fixed and whatever additional volume we are able to get that contributes directly to the contribution and that contribution then becomes almost equal to the bottom line. So our first objective is to make sure that whatever volumes we can increase that has the most disproportionate impact on the bottom line. Then, we have of course several cost reduction initiatives. So right now in terms, if I go back to volumes for example in BCF, I have that opportunity and in Palghar also, I have that opportunity you know. You are very aware we have been struggling with ramp up of Palghar volumes for quite some time and hopefully soon rather than later we should be able to make up for that and start ramping up there also. So, in these two areas, there is biggest opportunity for us to improve the bottom line. As I mentioned in my opening remark, there are some in POY- Tex. In Nylon Polyester, we have some new initiatives that we have taken up to increase the throughput of some lines. Again those opportunities we have to improve the volumes and as a result of that the profitability and then we have the cost rationalization and then finally the improvement of the product mix which is happening as a result of better quality of customers getting added on board.

Ankit Gupta: Okay. And this debottlenecking will happen across all the three years of plan let say Nylon, Polyester and Palghar or it is limited to a specific product that we manufacture.

Abhishek Mandawewala: Debottlenecking as in what do you refer to as debottlenecking.

Ankit Gupta: Debottlenecking, not spending much on the CAPEX and doing some.

Abhishek Mandawewala: No, there is no capital expenditure required at all for any of the three things that I mentioned whether cost rationalization or better quality of product mix or improvement of volumes. From here on, there is absolutely no capital expenditure required. These are things which are there in our hand with whatever investments have been made. If you go back in the last three- four years, we made sizeable investments in capability as well as capacity. So, from here on, I do not think, at least for the next year, as I said there is no CAPEX plan we do not have until we don't. From here on, we would like to see our return ratios get better. We would like to see our debt coming down. We would like to see our margins going up and only then it makes sense to commit further CAPEX. Until then, it does not make sense to just keep doing CAPEX without realizing the full potential of whatever we have already spent.

Ankit Gupta: Okay. And lastly, my last question on the margin side, I think margin, over the past four years in the nine months we have touched almost 7-7.5% kind of margin which have been the lowest in the past four years at least. So, do you think that this is the bottom that we are seeing in terms of margins and things will improve significantly going forward?

Himanshu Dhaddha: Are you referring to EBITDA margin?

Ankit Gupta: Yes, EBITDA margin, operating profit.

Himanshu Dhaddha: It is close to around 8%. I agree that its level has come down in the last two- three years. So, from here on since with all these initiatives and the volume pickup, I think we should pick up and our goal is to take it to the double digit levels in next three- four quarters.

Moderator: Thank you. The next question is from the line of Dhwanil Desai from Turtle Capital. Please go ahead.

Dhwanil Desai: I have three to four questions. I wanted to cover quite a few, so first question is I think on Y-o-Y our gross margins have declined by couple of 100 basis points. So, is that largely because of the inventory loss that we had because of the volatility or it also because of product mix?

Abhishek Mandawewala: Sorry come again the last one.

Dhwanil Desai: I mean on Y-o-Y basis, we saw some decline in gross margin. Is it largely because of the inventory loss on the Nylon side that you mentioned or it is more of a product mix issue?

Himanshu Dhaddha: So, it is both actually. If you had seen various quarters, it has different impact but to answer you for example in Q2 and Q3, it was more of because of the inventory losses and the price volatility which is impacting the inventory cost. So that is there but overall if you ask me about the levers, yes, the product mix is also one of the greater lever which we have and the margins can further increase because of the product mix change.

Dhwanil Desai: Okay. So, I think last Q1 and Q2 we had a very tough environment in terms of wire and prices and in some of commodity businesses in Nylon and Polyester that was definitely impacting our gross margins. Now, RM side that is some respite for us so at least if whatever loss that we are making or whatever trend that we have taken on that side is it kind of normalizing even for commodity business or there you have to pass on the cost saving on the RM side and there, it may gain because of the softening RM prices.

Abhishek Mandawewala: See, in absolute prices generally in a commodity business you have to pass through whatever up and down. The only difference is let say if your margin is on a raw material of Rs. 100 is Rs. 10. It means on a raw material of Rs. 90, your margin is Rs. 10 and you are selling it for 100. Now, instead of Rs.10 on Rs.100, let say 10% now you would probably make Rs.10 on Rs.80. So, sometimes percentage that could go up but in absolute terms generally we see that it does not make much of a very big difference.

Dhwanil Desai: Got it. So same way, it works the other way round also in the increase RM that your absolute terms may not change but percentage looks lower than that so.

Abhishek Mandawewala: The only thing that I have generally seen is what happens is, it is not just the RM right. You also have other utilities and you have other master batches, dyes and the packing materials and generally I do not know, I am not an expert in this subject but at least in this what happened is things are cooling down and if you look at it is not sustainable. So what happened is in China, something happened and many of our suppliers in China, they had to shut down their operations because of some rule of the government or something like that. And the dyes prices went up like anything and they have not yet corrected, the same thing with the master batches, paper price, everybody is very well aware how they have just short up through the roof so everything went up at the same time and for different reasons it was not all linked or something. So we are hoping that, while the raw material plus minus generally it gets pass through but these other increases it is very difficult to pass through, for example the power cost I mentioned in my opening comment is now has a huge impact on our bottom since if you look at from last year to this year we are talking I mean it's a big impact. So, if I look at the bottom power cost in Rakoli last year maybe three, four months we had an abnormally low price versus if I look at the price today I mean we are the difference annual impact is more, monthly impact is more than 1.2-1.3 crore. So, this cannot be passed on. Ultimately, hopefully with raw material prices falling everything else will fall, and we will be able to retain some of that but only time will tell.

Dhwanil Desai: Okay. And sir coming back to this power thing, if I look at your other expenses they have actually gone down Q-o-Q and even on Y-o-Y basis they have not kind of significantly moved they have kind of increased more or less in line with the increasing top line. So in spite of rising power cost, the other expenses have remained in control so I am sure that it is because of the initiatives that you have talked about right, or there is anything else which is not factored in this quarter and maybe come in next few quarters or anything like that.

Himanshu Dhaddha: If you are comparing on absolute terms, on quarter-on-quarter basis, Q2 versus Q3 whatever decrease is there at around 5 to 6 crore in other expenses, it is partly on account of volumes dip or your dyes and chemicals, commission, freight and power, etc. and all to that extend actually cost you less as compared to Q2, but yes there are some expenditures like repairs and maintenance and legal and professional which are not so equally spent quarterly. So those are then one of the few quarters and then it goes in another quarters it is like that.

Abhishek Mandawewala: But some of the savings that I mentioned earlier in the call those are real savings, so those are savings that from here on we will not have incur those costs and we have few more of them in the pipeline and hopefully if there is further any cost increase maybe tomorrow power increase more, at least we have some so far it was just increasing, increasing, increasing and against that increase there was nothing decreasing, at least now, there is something decreasing against the increase. If it decrease, then it is like a double benefit for us.

Dhwanil Desai: Got it and my last two questions. So I think one is on the, we were getting very good traction on Comfeel and foreign Sorenyl so any updates on there in terms of new customer addition or new business or ramp up in existing if you can provide that. That will be very helpful.

Abhishek Mandawewala: So Comfeel, containers are now in the sea as we speak, As I mentioned in the last quarter, a bulk buyer has ordered some volumes. Out of which, some of that was consumed and some of them are in the sea and now we have to see how the product performance in the market place. so while our customer likes it but ultimately the end buyer has to also like the product. Right? Because it does not matter if our customers likes it or not, he can push it but ultimately the end user has to like it so it all depends on that. But, if you ask me in terms of customers all over the world we are getting interest and samplings are happening in many places. And with respect to Sorenyl as I said, for solution dyed Nylon, actually the volumes itself are picking up and for us that is a thrust area and focus area for the next, the next big area for us is Solution dye Nylon and Comfeel because the activity has started three, four years back. And already some of the results we are seeing and the volumes are picking up and couple of customers are also getting added. So hopefully, that positive trend will also continue.

Dhwanil Desai: Okay. And my last question is on Palghar. At what capacity utilization we are operating currently and we were planning to kind of ramp it up to 80-85%. So again given the outlook that we have or whatever feedback that you are getting from customers any time lines around that, it would be very helpful.

Abhishek Mandawewala: Okay. Difficult to provide timeline but if I can do 100 in Palghar I am currently doing 80, so that 20 is very valuable. Let say, bottom line left on the table from AYM point of view, the business that extra 20 can add disproportionately so at least in terms of the volumes, maybe the volume of Palghar is not as big but that 20 can add very well and unfortunately in Palghar we had some margin pressure and we let go off some business, we got some new business and in the end that 80 remained 80, but again in this area also, I am excited with the initiatives that we have taken up in the last year or so and with some of the success that I am seeing particularly in the carpet segment, these are high volume segment if this can ramp up it can be good for us to go from that 80 to 100 level.

Dhwanil Desai: Sir, basically to understand correctly it was around 80 on 100 before also and today also it remains 80 on 100.

Abhishek Mandawewala: No change.

Dhwanil Desai: Not much change in the capacity utilization.

Abhishek Mandawewala: Exactly. There is no bottleneck. Nothing. The plant is ready to produce that 100 and we are having one month that we have produced that 100 also, one month in the mid of the year but to be able to produce it consistently on a 12 month basis we need that support from marketing.

Moderator: Thank you. The next question is from the line of Riddhesh Gandhi from Discovery Capital. Please go ahead.

Riddhesh Gandhi: Just a few quick questions. So how much would be the operational free cash flow for the quarter?

Himanshu Dhaddha: Overall it is around 7.5 crore.

Riddhesh Gandhi: 7.5 crore of operational free cash flow?

Himanshu Dhaddha: Yes.

Riddhesh Gandhi: Got it. And if we were to look at the actually CAPEX going forward excluding any new CAPEX which you mentioned in terms of the ongoing business. Is there anything there or could be expensing out?

Himanshu Dhaddha: There would be some operational CAPEX you can take it say around 10 crores per year.

Riddhesh Gandhi: Okay. But 10 to 15 crores is the maintenance in the CAPEX which you will be spending?

Abhishek Mandawewala: I think if I talk just maintenance it will be around 5 crore and an additional 5 crore.

Riddhesh Gandhi: In case there is some opportunity?

Abhishek Mandawewala: Absolutely. But, I do not think beyond 10 crore we should go in the next 12 months part from the residual CAPEX that we have committed but even that residual is a very small amount. Bulk of our cash flows from here on will go into now repayment of debt.

Riddhesh Gandhi: And just on the debt front, the actual amount has remained approximately the same but your interest cost has gone up by slightly over a crore.

Himanshu Dhaddha: Yes.

Riddhesh Gandhi: Is it high interest rate or you have just.

Himanshu Dhaddha: So, for example BCF expansion actually commissioned in Q3 so there has been lot of drawdown in terms of project six CAPEX but at the same time we would have repaid at the end of the quarter. So, the quarterly installments which is at around 12 crores has also got repaid. Overall, if you will see on a quarter end basis the debt remains the same but in between you would have increased and then it has decreased.

Abhishek Mandawewala: In the end of I think the beginning of January would be the peak debt & peak interest cost, from here on it will start reducing.

Riddhesh Gandhi: Got it. So if we are looking ahead into Q4, we should look at the Q2 interest rate is being the steadier.

Abhishek Mandawewala: No, I don't think so, I don't think it will be that fast in fact. Q3 slightly more actually, and then it should start reducing from there off.

Riddhesh Gandhi: Got it. And regards to get payment how quickly how much of ticket debt would you expect to pay now.

Himanshu Dhaddha: So yearly, we plan to repay our debt payments by around 40 to 45 crore.

Riddhesh Gandhi: Got it. Which you delivered to pay down, this is excluding interest or including interest?

Himanshu Dhaddha: No, this is excluding interest.

Riddhesh Gandhi: 40 to 45 crore of debt payment. But if you are doing about 7.5 crore of operating free cash flow won't that be enough.

Abhishek Mandawewala: So the 7.5 is not actually enough. We have to take into account the increase and decrease of inventory which can happen the increase and decrease of working capital which happens temporarily but if you look at the average it will be I think significantly higher than 7.5 crore.

Riddhesh Gandhi: Got it. So we are comfortable to be paying down about 40 to 50 crore of debt even in FY20.

Abhishek Mandawewala: Absolutely.

Riddhesh Gandhi: Got it. And just to understand, are there any alternatives that you guys are looking at to mitigate the hike the power cost?

Abhishek Mandawewala: Actually the supply is from the Rakoli DNHPDCL. They are monopoly suppliers so there is nothing really that we can do apart from represent the case because everybody knows that in Silvassa, the employment has not been increasing and the consumption of power has gone nowhere in the last five years, so somewhere we hope that even DNHPDCL will take steps to reduce their own cost and reduce the power tariffs over a period of time but in the last one and half year there has been a disproportionate increase of almost 50% which I don't thing happens every year or even every 10 years but that has what happened and we have no choice there apart from initiatives to reduce the per ton consumption of power.

Riddhesh Gandhi: Got it. But is it likely that they could reduce it in the near future or it is going to compete with black box with regards to how it works.

Abhishek Mandawewala: I would actually not wanted to comment only in that area so it is not something within our control. All we can do is to go and plead our case and represent our interest but beyond that it is very difficult to say anything.

Riddhesh Gandhi: And if we were to look at other expenses which you are baring in terms of R&D and business development expenses all those things how large approximately would that be?

Himanshu Dhaddha: Total R&D expenses would be at around 7 to 8 crs.

Riddhesh Gandhi: 7 to 8% of revenue?

Himanshu Dhaddha: 7-8 Crs, including CAPEX.

Riddhesh Gandhi: That is including CAPEX but linked to R&D which you think productive in revenue earning at the moment.

Himanshu Dhaddha: No, so if you take out the CAPEX and everything I don't think it is that high, difficult to put a number to it, there is a big investment in terms of CAPEX which has already happened but going forward I don't think on an operational front there will be significant investments. So we made already lot of investments in terms of capital expenditure but going forward I don't think we will have that many R&D capital expenditure. So, whatever expenses will have will be operational.

Riddhesh Gandhi: Got it, so in the quarter is there any connect CAPEX that is going to be captured in the R&D?

Abhishek Mandawewala: Yes, of course. So every time, a product development activities don't stop and for whatever R&D we do, we consume raw materials, we consume master batches, the salaries are there so that expense is always there. We will not put a number to it but we do not put that in the balance sheet that is actually expensed out.

Riddhesh Gandhi: Alright. Now, look at the end of the day because the profit margins are quite low, even a small incremental change in your EBITDA moves your profitability materially. So, effectively just wanted to get a grip on the overall levels which you mentioned should be able to get that along with a combination of debt pay down as well.

Abhishek Mandawewala: Absolutely.

Riddhesh Gandhi: Got it. And just to understand in terms of just broadly your target say for a period to achieve ROEs and ROCs a company would.

Abhishek Mandawewala: I would not like to comment on that, again we can make whatever target we want ultimately the numbers have to speak for themselves but right now I would not want to comment on that.

Riddhesh Gandhi: Got it. And a last question was that effectively you guys have issued some **–**warrants at a reasonably high premium to where the stock is currently trading is the intent to convert it still.

Abhishek Mandawewala: I think it is still few months away we haven't had any discussions surrounding that but as of now, yes.

Moderator: Thank you. The next question is from the line of Rohit Poti from Marshmallow Capital. Please go ahead.

Rohit Poti: So just wanted to take a couple of questions from the previous participant forward. With the CAPEX pretty much done and the intent to pay down the debt, is it the managements expectation that we would require the capital from the equity infusion and if so is it to pay down debt or is there any other use that you see for the capital.

Abhishek Mandawewala: I don't think there is any further capital infusion required, I think whatever free cash flows we generate from that part of it should be used to pay down debt and whatever little bit surplus we have, we can do some capital expenditure, for which right now we do not have any plans but I do not think any further dilution or anything is required from here on. I think the internal accrual should be enough.

Rohit Poti: Okay, so the conversion of warrants is not because you think the company needs the capital over the next year for any particular purpose.

Abhishek Mandawewala: For that we had already done it quite some time back, right about may be 6 or 8 months back that it was already announced and it was done keeping in mind that in the future, if there is any capital required by the business, then we can do it. So, I do not think that is absolutely necessary to do it but of course, in order to have a prudent balance sheet, which will definitely help us to reduce the debt equity ratio.

Rohit Poti: Okay. So we are self-sustaining operationally but to just strengthen the balance sheet is why we might go ahead and complete the dilution I understand. The second question I had is with the intent to, so it was very nice to hear the clear intent to reduce debt from the current year onwards so what I wanted to understand is, what level would you want the debt to go to before we think of the next strategic plan to either expand or move into other areas.

Abhishek Mandawewala: That is a very good question, the comfortable level for us 2.5 times EBITDA maximum three times EBITDA. I would say between two and three times EBITDA is the absolute maximum. Hence, I do not think I will commit fresh CAPEX at three times EBITDA. So, as we get to 2-2.5 times that is when we talk about doing fresh CAPEX. Thus, either the EBITDA has to go up significantly or the debt has to come down before we commit any CAPEX.

Rohit Poti: So it is not an absolute number of debt per se that we look at? It is more this ratio that will guide you on how.

Abhishek Mandawewala: Correct.

Rohit Poti: So, in the beginning of the call you mentioned that you had 2-3 methods you would look at before committing. So, one was the return, the second was the debt to EBITDA and the third was to basically utilize the entire capacity that you have, entire capacity and capability that you have within your setup right now. So, if we don't hit the return matrix that you want to hit so will you be focusing more on coming out with new products or will net debt to EBITDA will be the only figure that we would look at?

Abhishek Mandawewala: No, of course at the end of the day what is most important is the return on equity, right? There is nothing more important than that. That will always be the driving force of further CAPEX and this expansion that we have done has been done keeping that same thing in mind and we are hoping that this expansion will lead to expansion of return on equity and that is the only reason why we have done it, otherwise we would have not done the expansion and that will always be the guiding force.

Rohit Poti: Okay, great. The next question I have is, it is again an extension of the previous participants question so I think over the last couple of years we have done as he mentioned considerable investment in operational avenues like product development and you mentioned in the last few concalls on how you hired plant as well as business development people. So I know it might be difficult, but is it possible for us to understand as a percentage of revenues or any other way that you think you can portray it how much that has increased over the last couple of years because it sort of gives an idea of the operating leverage.

Abhishek Mandawewala: I gave a bit of flavor of that in the last quarter, so we have had some segments which have jumped up, I mentioned about the industrial segment which is now ramped up to almost 70-80 tons by next quarter and hopefully we should be at almost 120 tons which is a significant volume we started this less than two years back. The automotive segment that has ramped up to more than 100 tons now, in the POI text division the carpet segment has now started to ramp up, this quarter I think the volume should be good in the carpet segment which, in the carpet segment we are not doing very good volumes apart from our own sister company Welspun. So, that has started to ramp up and in pockets, we have got some other speciality segments for the Palghar that like narrow weavings that has ramped up, some export customers have come in that has ramped up to 70-80 tons, So, we are getting some good. This, I am talking about monthly figures we are getting some good responses and there is progress, slow progress but none the less there is progress.

Rohit Poti: Okay, I got it. So the question I had was more on the cost side, is it payable to, would you be able to quantify what incremental cost we have incurred over these even though we have to expense it operationally these are more long term benefits, expenses like we business development as well as the product development expenditure is it possible to quantify that in any way?

Abhishek Mandawewala: I can get back to you so to how much we have spent operationally don't have the figures off hand. Generally, what we do is all the R&D expense is considered as a part of the production itself and so for all the consumption of raw materials, we do not consider it separately but just to give you a flavor, we have four single positions lines and we have 28 production lines in the POY- Tex division. So, those four single position lines typically whatever is produced on it, it is all R&D sampling or some new experiments or new developments. Whatever we produce on that is not sold and the residual value of all that material is generally very low because the sample is very difficult to sell in market, quantity of sample is too low, so that get sold at the downgrade rate in the market or at very low residual values. We have not quantify that but it is not a small figure, it is not a very large figure but it is difficult to quantify.

Rohit Poti: So broadly you said 4 out of 28 lines.

Abhishek Mandawewala: Yes, but see the 28 lines are multiple positions the 4 lines are single position. So, let say out of the 28 lines, some lines might be 4 position, 6 position, 8 position but 1 position line is only 1 position.

Rohit Poti: Okay, I got it. Could you speak a little more about the Welspun because I think last year you were mentioning that they were setting up their own capacity and this volume might go away in this BCF.

Abhishek Mandawewala: Not in BCF, in BCF I think we have less than 2% or I don't think even we have 2-3% sales to Welspun, the major sales was in the POY- Tex division. In POY- Tex division, we have already taken several steps to de-risk and the volumes we have already has come down. So, I think we should be able to, there might be a hiccup for the quarter, but it will not be a major hiccup but there will be a small hiccup when they actually commission their lines and start producing but we have already taken the steps to de-risk that and for example the new carpet customers that we have added in the POY- Tex was actually a step in that direction only and I am not too concerned.

Rohit Poti: Okay, that is hardening to hear, so one last question from my end. In the beginning that you mentioned that as part of the cost factorization method you are reducing the personnel as well so what personnel are these because I think in lot of different segments you are adding personnel at least over the last year that is what was happening. If you could explain that.

Abhishek Mandawewala: So we just rationalized the structure wherever there is fat in the system we have tried to cut out that fat. I think, it is more of a rationalization exercise more than anything else. There is also some natural attrition which we have tried to not recruit against those position as that iteration happens both on the staff as well as the labour front. So, small steps to bring cost under control.

Moderator: Thank you. The next question is from the line of Ayush Mittal from Mittal and Company. Please go ahead.

Ayush Mittal: If I look at the volume numbers of company, we have been in a range and over the last few concalls you have mentioned about success in several new products, carpets, and other things so, I wanted to understand if you would like to highlight about the product exchange in our overall portfolio in terms of how much would be having typical commodity product range, how much would be a normal range or how much would be a speciality something on those lines.

Abhishek Mandawewala: Ayush, difficult to answer that question in quantitative terms. Internally, we do not have any measuring system where we can say that this product is a commodity or this product is a speciality. If you look at my previous answer to one of the previous question that was asked, there are four five segments that we have focused on in the POY- Tex division. Where we are seeing success, I tried to quantify some of those segments in terms of monthly volumes same thing we are doing in Palghar and BCF. As I said, for us, the focus area apart from some other good quality business is that we are doing is the solution dyed Nylon and Comfeel. And also now, new product tri- color, so in all areas we are making progress, but for me it is difficult to say that this is commodity and this is speciality, internally we do not say that this is volume of commodity and this is the volume of speciality.

Ayush Mittal: Because if we see the kind of quantities that you have mentioned as overall the quantities of this products still be very small in our overall numbers. Yearly numbers are maybe 45,000 ton plus that we are doing. And when we take each of the projects maybe we are doing 1000 ton monthly or 2000 tons as of now.

Abhishek Mandawewala: Correct.

Ayush Mittal: So if you combine all of these initiatives what kind of a numbers would we be making up or maybe some kind of hint over, what kind of changes happened over the last year, because if we see the numbers there has been no change in margins, it has only gone down despite some of these products.

Abhishek Mandawewala: Absolutely. So let me answer the last part of your question. First, which is with respect to margin, so the positive impact of this additional volume is more than been overwhelmed by the negative impact of some of the reduction in margin that we have seen particularly in the Nylon space and the impact of cost increases that we have had in the last couple of years. So, the small benefit that these new products give was more or less negated, overwhelmingly by the negative impact that we had over the last two years with prices of Nylon or margins of Nylon reducing. So, to answer your margin question is that and with respect to the volumes of this product if I see the percentage of overall just roughly speaking some of the segments which I mentioned, for example industrial yarn, we do not have major volumes it is just maybe 70-80 tons and we are expecting this to go to 120 tons in a couple of months but this was like zero if we saw couple of year back. From zero, we have scaled it up to 120 tons and for an entirely new segment of business where we are actually converted an old line which was making a low margin product at that time to this product which is a very specialized product and it is an import substitution suddenly to go from that situation to this situation while the volume might only be 100-120 tons but for me it's a huge success and what is the potential of this, if I just look at where can I go with this 120 tons, it's a big run way for me. And in fact, forget export, today I am not able to sell to the largest customers even in India in this segment because they are telling that my volumes are too small for them to consider me seriously as a supplier. So I am very-very happy with the progress that we have made in segments. Similarly, with the carpet segment in POY- Tex, we have been struggling for 2.5-3 years and we are next to negligible volumes to today this quarter we are going to do very-very healthy business in this segment and till today we were very much dependent on Welspun and to go from that situation to a situation where we are fairly de-risk we feel very happy with the progress that we made. It has all happened in the last two or three years. So, while it is not showing on the bottom line but there are lot of other factors which are causing the positive impact of this initiative to actually go down, but over a period of time as they start contributing and every year we are not going to have as bad a year as we have had in the last two, not going to have demonetization, GST, not going to have antidumping duty go away, not going to have chemical prices and paper prices going through the roof. So we look at all these things in perspective over a period of time it should start paying off. That is all I can say.

Ayush Mittal: So, as you mentioned that your customer are looking to take more quantities so is the challenges of scaling production in terms of can we do it from the same lines but just dropping the old work that we are doing.

Abhishek Mandawewala: So it is not that easy this particular product that we are talking about, we had some lines which we converted we have some more lines which we can convert but some very small CAPEX 50-Rs.70 lakh CAPEX will be required and when we feel it's the right time we will convert. So, as I said, we are going from Zero to 70-80 tons right now and we will be going to 120 tons. So, that is an additional volume which has come from somewhere from my existing system, as and when I start getting more and more response, as and when I start feeling more comfortable, I will slowly and steadily convert lines. I am in no hurry, I am not looking to go from 128 tons to 500 tons in one month, and no point of thinking in that way. So, slow and steady will win the race ultimately.

Ayush Mittal: Okay. And when you talk about the negative margins or poor margins from the other segments then when I look at the bended margins that is around 8% is it which I have asked earlier also is it that in some segments we are making losses is it so bad that it negates the good work if so, then why are we not closing down those kind of businesses rather than incurring such kind of negative.

Abhishek Mandawewala: As you know, there are two types of cost, there is a variable cost and fixed cost. So, there is a contribution margin and an EBITDA margin. So, let me tell you we have no products in our portfolio which are negative contribution margin.

Ayush Mittal: It might be giving you negative because of the inventory for sometime.

Abhishek Mandawewala: No, somehow the products are not able to cover up the fixed cost. There is nothing that does not cover the variable cost but there are some products that contribute more towards the fixed cost and by fixed cost I mean the interest, depreciation, the manpower expense. But there are some products, which might not even cover the full fixed cost but cover some part of the fixed cost, which does not mean I should stop those products because if I stop those products it will become negative, my contribution will go down and as a result of which my margin will go down even more.

Ayush Mittal: You mean to say to need to be keep running certain quantities till you are not able to scale it up then you cannot shut down the business which is not giving you any loss it is okay?

Abhishek Mandawewala: Absolutely.

Moderator: Thank you. The next question is from the line of Ankit Gupta from Bamboo Capital. Please go ahead.

Ankit Gupta: Abhishek, just one question over a medium to long term basis. Like, last two years have been challenging for us and certain steps we have taken, some of them we have resulted in the business profile improving to more towards the speciality side, let say a theoretical question on future basis. Let say two- three years down the line, do we think that in our business the proportion of speciality products would have increased to such an extent that if there is any such disruption that we saw in terms of Nylon pricing or GST or demonetization, at least the impact will not be as severe as what it was let say two years back or in the past two years that we are facing.

Abhishek Mandawewala: Absolutely. With every passing day, there is an improvement. So, as and when more and more of these sales start coming, we become more and more resilient but right now it might be a very small portion. But, as the time passes by, it will become more and more resilient. See, good quality of business does not come in one day or one year. If it was that easy, then everybody would be doing it by now, right? I mean, if it was so easy to do it, all my competitors would be doing everything. So over a period of time, that is exactly precisely the objective with which we have started all these exercises.

Ankit Gupta: Okay. But you think you can achieve that in the next two- three years so it will take you much more than that.

Abhishek Mandawewala: Very difficult to comment so I cannot say how much of the impact will come or not? All I can say is that I am fairly confident that in two years we will be more resilient then we are today.

Ankit Gupta: Okay. And just wanted to understand your thought process on setting down to warehouses as we pan I think this was the investment that we did in past two- three years for, this was the investment which was done to not expand capacity but to improve the business policy and also why are we shutting that now.

Abhishek Mandawewala: No, I am not referring to the internal warehouse. In fact, we are doing to use the internal warehouse to the fullest extent. The warehouse that we are shutting is the external warehouses that we have taken in order because we were running short of space.

Ankit Gupta: Okay. So now we have our internal warehouse, we will not be using external warehouse that is very good. And just last question on BCF, for this incremental 50-60% incremental capacity for BCF, what kind of asset turns do you think can be generated from this the asset turn.

Himanshu Dhaddha: So, I think it would be similar to what we are doing currently in the range of 1.6-1.8.

Ankit Gupta: 1.8 times approximately.

Moderator: Thank you. Now we will take the last next question for this conference, next question is from the line of Dhwanil Desai from Turtle Capital. Please go ahead.

Dhwanil Desai: So two questions and so the first question is on the BCF new expansion so I think my understanding is that 50% is mono color and so I do not know about the numbers but my sense is that if you are talking about 60 crore of investment and two times asset turned and roughly around 100-120 crore of additional revenue and 50% of that is coming from mono color so 50-60 crore of additional revenue from mono color is what I can kind of co-relate. So is it likely that in the next one two quarter, at least that kind of capacity can be filled up or you think that will even take longer time.

Abhishek Mandawewala: Difficult to comment. It is a dynamic situation, so we are certainly not absolutely full and it is not expected that we will be full but I can say that we are certainly running more than what we were running before the expansion came up. We are doing more sales than we were doing before the expansion had come up and now how much more time it will take. It is a dynamic situation depending on how quickly our customers decide to switch over, how quickly our products get approved.

Dhwanil Desai: So even in mono color you see that transition taking whatever time it takes.

Abhishek Mandawewala: Correct. So to add the new customer, there is a process and you have to go through that process. So, in one day it cannot be utilized, when the new capacity comes up, pent up demand but that is there, that you can finish off but that is not the rate at which you will always keep going. Until the new programs come, you will have to wait.

Dhwanil Desai: Okay. And my last question is so, the only comparable that we at least I could find which is doing similar kind of work which is very specialized work, & which appear to compare with and again I do not know whether that is a right comparison or not but you can guide me on that, but if that is a right comparison they in the worst of the time frame make 14-15% EBITDA margin and maybe 20% in good times. So, aspirational do you think that those are the kind of margins i.e. at least 13 to 15% kind of margins that we should be looking at some point of time. I do not know the time frame but is that how you position yourselves too?

Abhishek Mandawewala: So, if you just look at our own past, let me not refer to another company, I have no right to comment about any other company, but if you look at our own past I think we have done 14 to 15% margins at the peak.

Dhwanil Desai: But, that was more of a cyclical in nature, I am talking about more sustainable margins that was Nylon cycle in our favor and you are making 14-15% margin. I am saying on a sustainable basis, are we seeing that kind of margins emerging for us?

Abhishek Mandawewala: I do not want to say yes because as soon as I say yes everybody will put 15% in their spreadsheet, but certainly.

Dhwanil Desai: No, I am just talking about the directional part I am not talking about the number.

Abhishek Mandawewala: Let me put it differently. My first step is let’s get to double digit and then from there step by step one percent at a time that is what we should think off. 15 % is a very long way out.

Moderator: Thank you. I now hand the conference over to the management for closing comments.

Himanshu Dhaddha: Thank you very much for attending the call. That is it from our side, thanks.

Abhishek Mandawewala: Thank you everybody.

Moderator: Thank you. On behalf of AYM Syntex Limited, we conclude this conference. Thank you for joining us. And you may now disconnect your lines.

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