



“Shaily Engineering Plastics Limited Q2 FY16  
Earnings Conference Call”

**November 02, 2015**



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**Moderator:** Good day, ladies and gentlemen and welcome to the Q2 FY16 Earnings Conference Call for Shaily Engineering Plastics Limited. Please note, this conference call may contain forward-looking statements about the company which are based on the beliefs opinion and expectations of the company as on the date of this call. These statements are not the guarantees of future performance and involve risk and uncertainties that are difficult to predict. All participant 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 this conference call, please signal an operator by pressing '\*' then '0' on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Amit Sanghvi, Managing Director. Thank you and over to you, sir.

**Amit Sanghvi:** Thank you. Good afternoon everyone and a warm welcome to all the participants to the maiden's earnings call of Shaily Engineering Plastics. Today I am joined by Mr. Sanjay Shah, our Chief Financial Officer, and SGA our Investor Relations Advisors. I understand that we were late in uploading our Investor Presentation but I hope that you had a chance to look through it or looking through it right now. This being our maiden call, I will take the opportunity to introduce our company to you.

Shaily Engineering Plastics Limited was incorporated in 1987 with the sole purpose of manufacturing precision component with high performance engineering polymers to fulfill the gap that existed in the plastic processing market in India. Through the years, we have worked with various companies across multiple user industry such as IKEA in Home Furnishings, P&G and Hindustan Unilever, Pepsi in Consumer and FMCG, Honeywell in Automotive, Sanofi, Wockhardt, and Sun Pharma in Healthcare and many more companies both from Appliances and Switchgear industries.

The strength of the company lies in its capability to offer end to end solutions to OEMs for any of its plastic requirements beginning right from conceptualization to commercialization including project management, design, industrialization and scale up, going up into managing their entire supply chain. In this journey of almost three decades, we have been successfully partnered with large corporate MNCs to meet their very unique requirement and introduce uniquely designed and manufactured products into the industry. To mention a few in the early 90's P&G came to us with a problem that they have their Vicks containers leaking because of climate conditions in India. We changed their design to suite adverse climatic conditions in India. When Pepsi first launched 'Aquafina' they launched with a regular tamper evident cap which are prevailing on most water bottles today. The problem that they faced was that these caps people would use them and then refill it and seal it again. We designed the unique cap incorporating their logo where the ring would essentially break-off and could not be resealed. Another one of our coveted achievement had be designing and manufacturing World's First 100% Plastic Insulin Pen which we did for Wockhardt in 2005-2006.

Today a large portion of sales or revenue comes from IKEA. The relationship with IKEA began in 2004 and today we are one of their most preferred plastic suppliers globally. With this trust we managed the entire supply chain of products right from our factory to IKEA stores. We service this demand from 100% EOU facility at Rania, Gujarat and I am sure all of you would be aware now with IKEA plans to enter into India with a total investment of about 10,500 crores over the next several years. Shaily is well poised to capitalize on this upcoming opportunity.

As you may have noticed, the company so far has been working with products which are customized to customer requirements. In order to manage the risk of contract manufacturing and in order to improve margins to achieve the next level of growth we have forayed into our own products in the Healthcare segment. With this objective in 2014, we went into a tie-up with Global Closure Systems to offer closure solutions to pharmaceutical companies. GCS is a European multinational company with patents for child resistant closures. They are basically the pioneers when it comes to CRC and European market leaders today. We are an exclusive licensee for GCS for our CRC caps in the Indian market.

In 2015, we set up our second ISO Class 8 Clean room Facility also at Rania to Gujarat to manufacture CRC Caps and HPP bottles for regulated markets. These products are currently under validation by various pharma companies and we believe that such validations would take anywhere between six months to eight months. We believe that India being the second largest exporter of generic drugs globally this presents a large opportunity for us to capitalize on.

So from an overall business perspective that is all from my side. I will handover Sanjay Shah, who will take you through the financial performance of the company. Thank you.

**Sanjay Shah:**

Thanks Amit and a good day to all the participants. I will share highlights of our financial performance following which we will be happy to respond to your queries. To begin with Q2 FY16 Company registered revenue of Rs.62 crore with a year-on-year growth of 34% from 46 crores in the same quarter last year. EBITDA is at 11.0 crores from 7.1 crores in Q2 of FY15 which represents a growth of 57% year-on-year. EBITDA margins are at 17.8% in Q2 of FY16, up as compared to 15.5% in Q2 of FY15. This basically represents an expansion of 230 basis points over last year. Profit before tax is 7 crores on Q2 of FY16 as compared to Rs.5 crores in the same quarter last year, a substantial growth of 40% year-on-year. PBT margin is at 10.4% in Q2 of FY16 as compared to 9.8% in Q2 of FY15 basically leading with expansion in margins by about 60 basis points. Net profit for Q2 FY16 is at 4.1 crores as compared to 3.9 crores in Q2 of FY15. This represents a growth of 7% year-on-year. Net profit margin is at 6.7% in Q2 FY16.

Coming to the half yearly results for FY16, Company registered revenue of 116 crores year-on-year growth of 36.5% from 85 crores in the same period last year. We see Growth in top-line across all segments mainly driven by strong traction in business from IKEA. The new ISO Class 8 Clean room Facility for pharma packaging at Rania, Gujarat is now ready and as

mentioned earlier by Amit products are under validation stage with clients now. With positive response and feedback from these customers we expect to see tailwinds by the end of the year.

EBITDA during the first-half of FY16 is at 20 crore which represents the growth of 52% year-on-year as compared to 13 crores last year. EBITDA margins in the current year have expanded by 170 basis points to about 17%. Profit before tax for H1 of FY16 is at 11.3 crores this represents a growth of 58% year-on-year from 7.2 crores in the same period last year. Profit after tax in the first-half of FY16 is at Rs.7.5 crores as compared to 5.7 crores in the comparable period last year. Profit margin during the first-half of FY16 is at 6.5%. This is all from our side and now we can open the floor for question and answers from people.

**Moderator:** Thank you very much, sir. Ladies and gentlemen, we will now begin the question and answer session. We have the first question from the line of Saket Bansal from Dinero Wealth. Please go ahead.

**Saket Bansal:** Sir, there was high interest cost in this quarter like 3.2 crores as compared to 1.44 crores. And there is one more question you said you will be producing 100 million caps and bottle with the new facility is this already started and if it has started what is the realization in this caps and bottles?

**Amit Sanghvi:** I will let Sanjay answer your first question on the interest cost.

**Sanjay Shah:** Saket, on interest cost the interest cost for the current half or current half year includes 77 lakhs of FOREX expense. So it includes that basically predominantly on a FOREX borrowing which was repaid in the current quarter. Second is we had taken on loans for setting up our new facility which was put into operations sometime in March 2015 so, post that the interest on that was charged to revenue that is the reason you will look at a little higher interest cost or compared to the comparable quarter in the last year.

**Saket Bansal:** Sir, going forward what would be the interest cost, will remain same?

**Sanjay Shah:** Interest cost would remain same we expect some improvement in our interest rate. So you see some interest savings there but the interest cost would remain the same.

**Saket Bansal:** And the margins would remain same sir?

**Sanjay Shah:** If you look at the last four quarters you have been seen gradual improvement in margin and as we scale up the business and also move into the pharma space we expect improvement in margin going forward also. Amit, you can answer the first one.

**Amit Sanghvi:** To answer your second question regarding the 100 million caps and bottles. We have supplied samples batches and trial batches to a lot of customers; most of it is under different stages of validations right now. There are about ten steps involved before when you set up

manufacturing to when you can start commercial supply. We had various stages with various customers and we have said and I am not sure this is in the presentation or not. We will basically start seeing larger commercial supply starting in quarter four of this financial and the balance of the next financial year is when we will scale up to a large portion of our capacity.

- Saket Bansal:** Okay. Sir what will be the contribution in this quarter from IKEA business?
- Amit Sanghvi:** About 50%.
- Saket Bansal:** About 50%, okay.
- Moderator:** Thank you. The next question is from the line of Pritesh Chheda from Lucky Investments. Please go ahead.
- Pritesh Chheda:** Just a couple of questions. One on the IKEA side of the business, now which is about 50% of our total business. What is the scalability in that part of the business from three year to five year perspective and second on the pharma bottle side if you could tell us a little bit on the scalability angle the capital investment we have done and corresponding out come from a three year to five year perspective.
- Amit Sanghvi:** Let me talk about the opportunity first a bit. We have all read about IKEA now coming into India. We have all read about where they have bought land. Essentially IKEA is going to be close to I would say increasing their sourcing and plastics by 60% to 70% uptill 2020 and being a supplier that has consistently preformed with IKEA I definitely see a lot of opportunity for us to grow with them. As far as exact projection goes it is too far out for us to give you indication but if IKEA is opening 25 crores in India alone you can imagine what the potential for the revenue would be including other markets.
- Pritesh Chheda:** If you could tell from the global supply angle where we are to the next peer and what size it would be and what size we can achieve?
- Amit Sanghvi:** Today IKEA source is about €1.2 billion worth of plastic globally. We are at €20 - €22 million of that.
- Pritesh Chheda:** And what would be the largest supplier size?
- Amit Sanghvi:** Difficult to tell right now but the largest supplier is about €150 million.
- Pritesh Chheda:** Okay. On the Pharma Bottle side, sir?
- Amit Sanghvi:** What was the question on the Pharma Bottle side, sorry?

**Pritesh Chheda:** I think the opportunity there and the scalability which the current capital expenditure we have done?

**Amit Sanghvi:** To the current capacity we have put in place will enable us to manufacture 100 million caps and 100 million bottles all in all. When I look at market size and when I look at players in the industry as far as caps are concerned even today about 90% of India's generic player's requirement is imported. So while there are some cap manufacturers in India they have not been very successful in commercializing the caps. Indian generic market is going to grow at a CAGR of roughly 13% to 15% if I remember my numbers correctly. So just that itself tell us that even if we capitalize on the new opportunities, where it is easier for us to enter and eat into the current market share even by 10% to 15% of current market share we would be well in the range. We would have basically ended up selling our capacities.

**Pritesh Chheda:** Even if, you get how much market share?

**Amit Sanghvi:** If I get 15% of the current market share and new opportunities so, India grows at about 13% to 15% annually on the generic business.

**Pritesh Chheda:** Okay. And how different is the gross margin in this part of the business? Versus this the current that we have?

**Amit Sanghvi:** Our margin are...

**Pritesh Chheda:** Pharma gross margins.

**Amit Sanghvi:** Sorry, go ahead.

**Sanjay Shah:** The margin business is better as compared to our normal business that answers your question.

**Moderator:** The next question is from the line of Sangeeta Purshottam from Cogito Advisors. Please go ahead.

**Andre:** Yes, this is Andre here **Sangeeta's** Partner. We were looking at some of your products that you have displayed on the website and the ones for IKEA from a lay person's perspective we were not able to figure out what the level of manufacturing complexity is here which explain your stickiness and why IKEA can be so keen to work with you. So, could you just explain to us as to what is that creates the stickiness with IKEA with respect to your specific skill in terms of your technical skills your manufacturing skills and any other skill that you might have which would explain why you would be able to leverage the growth of IKEA in this country significantly.

**Amit Sanghvi:** So, let me first start to answer that question with what is that IKEA looks for in a supplier. First and for most the most important thing to IKEA is something that they have referred to as

Iway. If you refer to our presentation we were awarded the best Iway supplier in South Asia in the year 2009. Iway is nothing but a social compliance requirement that IKEA has put up. Social compliance means environment means how you treat your workers we talk about child labor obviously we would not be involved in any such activity and sustainability. Sustainability means how is that you are able to incorporate your renewable and recycled materials and energy into your manufacturing operations. And we should not forget the most important is our performance with products. See IKEA only sells finished products in their stores so everything we manufactured is a finished product. Now they would not does any inspection or further value add on our products which means that they have to be confident in the quality that we are manufacturing that enables us to supply directly from Shaily to their stores worldwide. So one is making sure that the stores never stock out, second is making sure that the customer remains happy with the quality of products supplied. Third is the Iway System that I spoke about and fourth is going forward we talk about being sustainable as a supplier. Keeping all these things in mind and our performance our historical performance there is detailed KPIs and what not behind it but we have been one of the better performing suppliers in their portfolio. And Now that we talk about the technical aspect behind the products, I agree with you, that from layman's terms you look at the products and they look quite simple. But most of our products are non-straight shoot and ship when I say shoot and ship it is not that we just put a mould in the machine take out the parts and send them out. Most of our products have assemblies, most of our products have are made up engineering plastics not commodity plastics we manufactured kitchen legs for IKEA. IKEA's bread and butter is their kitchen's so each one of our leg is supposed to take 250 kilos of load and it is a fixed component assembly that we manufacture for IKEA we do all the testing. We ensure it is made to the right specification so that tomorrow when their kitchens are being used worldwide they should not just fall flat on the floor. So that is a bit on the technical part, and we offer very innovative assembly solutions and that does not mean that we have the highest level of automation that means we have the right combination of automation and labor that makes the product cost effective, okay. I hope that answers your question.

**Andre:**

Yes. But how unique is this proposition to you and how confident would you be being able to garner and increasing share of the IKEA business as it expands in India. Who are you competitors for the IKEA business in India and how would they rate on these same parameters as you do?

**Amit Sanghvi:**

I will not comment on my competitors, I can give you names as to their performance not something that I will be able to comment on. Our current competitors for the IKEA business in India are is a company called All Time Plastics based out of Vapi, Gujarat. There is another company called Fancy Fittings based out of Surat, Gujarat. I am sure to work with IKEA they need to be good supplier so I am sure they are and must be performing as well. But that is the extent of that answer.

**Sangeeta Purshottam:** This is Sangeeta here, I have a follow-on question to this that you have talked about growing with IKEA as it expands in India what about the IKEA worldwide requirements would not that be a big kicker for growth?

**Amit Sanghvi:** Absolutely, I think IKEA's worldwide requirement is going to be just as much as driver of growth as their India venture. China as we all know that cost are increasing in China and there has been movement we currently supply to the Chinese market as well for IKEA product and they will be moments where there will be chance for our products. Time scale is not something that we will be able to tell you. But what we can tell you that if you look at our historical figures even given in the presentation which is currently only corresponds to export products, products being exported from Shaily. From FY13 to FY15 we have seen a 170% growth in revenue for IKEA.

**Sangeeta Purshottam:** Right, okay. So would it be fair to say that in the near-term which means next year your growth is actually going to be driven by exports to IKEA and it is really post FY18-FY19 onwards that IKEA's India presence also start contributing because it is going to take them a while to get themselves established here, right.

**Amit Sanghvi:** Yes, that is correct.

**Sangeeta Purshottam:** Okay. And just in terms of your non-IKEA product, could you give some flavor what the client actually looks for in you and where the stickiness really arises and how do you see those opportunities is it the pharma space that you are looking is the next big opportunity if you could just give us some color on the non-IKEA groups.

**Amit Sanghvi:** When we look at the non-IKEA side let us start with Healthcare for instance. In Healthcare we are actually not doing anything for the domestic market while we supply these closures and bottles to players in the domestic market they sell the product and it get exported basically primarily to the United States, Canada. And when you look at the device landscape essentially there is no one but Shaily in all of India that manufacturer pen injector or auto injectors. In the past we have done dry powder inhalers as well. That portion of the business has much more to do with regulation, compliance, understanding of polymer, understanding of process, the processing window and the tolerance is required are very-very tight for anyone to just come in and take that share of business away from us. And when you look at the trends in the pharmaceutical industry there are key patents that have expired over the past 12 months and will continue to expire over the next 36 months. With there is two opportunities for Shaily, one is that innovative companies based out of U.S., Europe, Canada will be looking for cost effective solutions on their devices. So, I am sure that we will be approached for some of those opportunities and Indian generic companies looking to get into the business where the patents are expired and will also be looking for cost effective solutions from India. So there is going to be a portion of business that hopefully comes from the innovators and a portion of business that comes in from the generic as far as pharma is concerned. When we look at our other growth drivers and we are focused on FMCG and automotive. In the automotive again we do



not do anything for domestic automotive, we manufacture some very-very niche products high value added products for GE Lighting, Honeywell, FAG and for a company called Amvian Automotive. Most of these are either engine components they are either traffic components, they are either components for breaking systems, or they are components for safety. In the first three that I have mentioned, we have done a few metals to plastic conversions. So this is where it is not that easy you need to really understand the application of the component and you need to have the knowledge of polymers on how you can make that. There is a process that we do for the Honeywell, Rods which is maybe I would not be able to call it a proprietary process. But it is a process that we have developed in house and there are several post processing, post molding, processes involved to get the integrating of the product. So these are all area where we are quite strong, quite competent and we have seen a lot of growth over the last even over the last financial year.

**Andre:** And have the metal to plastic conversion in the automotive space in India been rather slow. And if so what are the reasons for it?

**Amit Sanghvi:** I will not be able to comment on the metal to plastic conversions in India yet. There was a time back in 2009 where we were involved in domestic automotive industry we have kind of exited out of that industry it is not a high margin or a high value added industry it is more of a conversion model and Shaily as a company you could call this is a converter because we are doing injection modeling but we are more of the service provider and a solutions provider. Our proposals are not based on shift rates or per kilo conversion cost. In FMCG we have received quite a few enquiries over the last several months again I think one of the driving factors is maybe the tax benefits which will expire in 2017 and there are companies which are looking for solutions other than provided by our competitors in the tax free zones and we are able to give them some innovative solutions which is what our forte.

**Sangeeta Purshottam:** Right. If you look at this whole combination of opportunities that you have, what is the broad sense of how do you expect let us say what do you expect the size of the company to be in maybe about three years' time and how are you geared up to take advantage of these opportunities if your CAPEX is in place or are you likely to be investing in a lot of CAPEX in the next two years to three years. If you could just give some sense on how as a company you are also gearing up for this growth and also what level of growth is you comfortable with? The growth opportunities can be huge but each company has its own sort of comfort zone and beyond which sometimes it does not want to grow what would that be if any for you?

**Amit Sanghvi:** I am 32 years and obviously my passion to grow as fast as possible which is the case with most people from my generation but as far as the next two years ago I mean you have seen the presentation our vision is to get to a \$100 million by 2020. I think we are looking to grow at 25% year-on-year. In terms of CAPEX there is not much visibility beyond the 2016 and 2017 figures but I do not think we will be raising further debt or equity at the moment.

- Moderator:** Thank you. The next question is from the line of Rukun Tarachandani from Kotak Asset Management Company. Please go ahead.
- Rukun Tarachandani:** Sir, if you can just elaborate on what kind of the peak revenue potential of the new pharma facility that you are building? I mean just a ball park number.
- Amit Sanghvi:** It will be about two times the investment number, so about 60 crores.
- Rukun Tarachandani:** Okay. And what is the capacity utilization in existing products right now?
- Amit Sanghvi:** Our capital utilization overall on all our plants combined would be about 75%.
- Rukun Tarachandani:** 75%?
- Amit Sanghvi:** Yes.
- Rukun Tarachandani:** Sir, that 60 crores that you mentioned that is the investment made or that is the revenue?
- Amit Sanghvi:** No, we have invested 30 crores and the revenue potential is about 60 crores.
- Rukun Tarachandani:** Right. And sir you can elaborate on you said that your pricing is not based on a fixed margin EBITDA (30.00) per ton or kg kind of a model if you can just elaborate on how do you price your products what is that you are targeting there?
- Amit Sanghvi:** I do not know how much I can elaborate but what I can tell you is product pricing is done we are present across six different industry segments in each segment there is different pricing strategy. In Healthcare industry you would price the products based on regulatory and compliance requirements, so a lot of validations a lot of testing, trials, you have to do a micro build count of your facility, you have to test your employees for diseases on a regular interval to make sure that there is no communicable diseases for instances. So based on the industry there is a costing done. In the complexity of the component more than a shift rate model.
- Rukun Tarachandani:** Right. But so there is a target return on equity or return on capital employed that you are targeting that this is what we should get?
- Sanjay Shah:** Any incremental business which we look at we would look at improving ROC or ROA from the long-term basis is what we are going to do.
- Rukun Tarachandani:** Okay. And sir we can give a revenue break-up of Healthcare, Auto, and FMCG?
- Amit Sanghvi:** For this quarter?

- Rukun Tarachandani:** Yes, for the last financial year or this quarter, I mean what is the approximate ball mark number?
- Amit Sanghvi:** I know the last financial years but how about this how about we uploaded in our next presentation.
- Rukun Tarachandani:** Yes, sure that will do. And one final question, as you have said that the product that you are making do require some technical knowhow and expertise so how did you begin with this, how did you get the requisite technical expertise to begin with?
- Amit Sanghvi:** So I was born into it but my father came with that expertise. He has spends about 20 plus years in plastics in North America prior to in moving back to India and starting Shaily obviously, that knowledge has been transferred to our people and to our engineers and technical teams.
- Moderator:** The next question is from the line of Nidhi Agarwal from Sharekhan. Please go ahead.
- Nidhi Agarwal:** I want to understand the tax rate which has been low historically has risen this quarter. So how should we view the tax rate for the full year and for coming years?
- Sanjay Shah:** Maybe for the last year we were under MAT so MAT credit is about to offset in the next year so we basically had minimal tax rate. In the current year we will be at a full tax rate it will be a 33.99% so we will be at that tax rate.
- Nidhi Agarwal:** Okay. And what is the CAPEX requirement for the next two years to three years?
- Sanjay Shah:** For the current year we are looking at investing 20 crores. For FY17 and FY18 it would dependent on the business needs with various customers' need we are in discussion so...
- Nidhi Agarwal:** And how you are going to finance it?
- Sanjay Shah:** We would basically be looking at internal accruals.
- Nidhi Agarwal:** But last year our cash flow from operation was like 4 crores so this year we are going to make enough cash flow for financing CAPEX?
- Sanjay Shah:** Yes, we have already received. Last year we have raised, 25 crores of equity also which has not been deployed till now so part of the CAPEX in the current year would be out of the equity which we have raised.
- Moderator:** Thank you. The next question is from the line of Ritesh Shah from Investec Capital. Please go ahead.

**Ritesh Shah:** Sir, if you could provide some color on how should one look at the margins for the company going forward. If you could give some color regarding say the revenue mix that you have and incremental higher percentage say from consumer or pharma that will drive the revenues or how should one look at say raw material prices going down?

**Amit Sanghvi:** Yes, I will answer that. Let me start by giving you some history. If you look at historical figures of the last two years to three years our margins have seen improvement. So why have they seen this improvement. There are three to four factors on why these improvements have happened. One is that it is sheer scale, you see whatever capacities we have set whatever people and human resources that were available we are using that scales to it efficiently today. Secondly, we have consolidated our business which means that we have gotten out of some low value, low margin businesses we have gotten out of businesses that required a lot of our technical resources but they do not add much to revenue. Third is that over the last two years to three years we have focused on adding high value and high margin businesses across various segments. So the example of the connector rods, the example of the insulin pens and we have also focused largely on operational and financial efficiency that is how we have improved our margin so far. Going forward your question was that how much is the margin going to improve I am not sure if I can give you an answer directly on how much it is going to improve but I can tell you that it is going to improve.

**Ritesh Shah:** So, just to take us forward basically you indicated that focus has been to drive scale, I think in the earlier questions you did said that we are currently operating at 75% utilization if I am not mistaken was that number, right?

**Amit Sanghvi:** 75%, yes.

**Ritesh Shah:** Okay. So one can expect incremental margins if we go to 100% so probably that might be one of the levers. Secondly you also indicated that focus on high value-high margin so, is it possible to dissect the sales into two parts higher value-added products and say something like others and probably if we have some target on value added products over the next two years based on the pipeline that we have...

**Amit Sanghvi:** We can of course do that but we would not be able to put it in the public domain it would create some bad blood with customers.

**Moderator:** Thank you. Next question is from the line of C. Srihari from PCS Securities. Please go ahead.

**C. Srihari:** I notice that you have a DMF filing for an applicator SEPL tropical underarm, can you please throw some light on this I mean which molecule is this and when do you expect to commence supplies or whatever?

**Amit Sanghvi:** I am sorry Srihari that is confidential with the customer we will not be able to divulge details at this point.

- C. Srihari:** Okay, if not at least the product I mean if not the molecules?
- Amit Sanghvi:** We would not be able to. Whatever you have in the public domain from our filing is what is available.
- C. Srihari:** Okay, is it for something like a Sun screen I mean what is the therapy area?
- Amit Sanghvi:** I cannot answer that question.
- C. Srihari:** Okay. Or when is the window opening? I mean something in that trigger.
- Amit Sanghvi:** Let us say it is an opportunity that is 24 months I mean will take an additional maybe 12 months to commercialize how about that?
- C. Srihari:** Okay, is it a first still under patent or it is off patent?
- Amit Sanghvi:** No. I am not sure to be honest.
- Moderator:** The next question is from the line of Maulik Patel from Equirus Securities. Please go ahead.
- Maulik Patel:** As you mentioned earlier that you are not a typical converter but you are a service provider, right.
- Amit Sanghvi:** Yes.
- Maulik Patel:** So how do you manage raw material volatility because we have seen a lot of raw material volatility in the last few months and are your margin is on a percentage basis or is it per unit basis how one should look at it?
- Amit Sanghvi:** Okay, let me split that question into two. First – how do we manage the raw material volatility? See our business is about one-third commodity plastics and two-third engineering plastics. All the volatility you see is primarily on the commodity plastics basically like polypropylene, polyethylene styrene. On the engineering plastic side you see much less volatility. It would be less than maybe a quarter of the volatility on the engineering plastic side. As far as how do we manage the volatility on the commodity side is concern with most of our customers we have raw material neutral agreements so, whichever way it goes it is taken care of, whether it is give or taken.
- Maulik Patel:** The raw material is a pass through for you?
- Amit Sanghvi:** Correct. It is not a job work model so..
- Maulik Patel:** Pardon?

- Amit Sanghvi:** It is not a job work model.
- Maulik Patel:** It is not a job work model, okay, yes. So let us say if any so you will have probably one month of moving average or three month lag you will pass on the raw material to the customer, right?
- Amit Sanghvi:** Basically quarterly reviews it is a very simple mechanism.
- Maulik Patel:** How do you target it is percentage basis or the per unit basis because let us say the raw material prices goes down significantly lower than how do you will make on the percentage wise or you make money on the per unit of the volume?
- Amit Sanghvi:** So I think there are different model in place for different products we have about 200 SKUs that we currently manufacture. I do not know the split overall it might be 50-50, might be 30-70 but there are both.
- Maulik Patel:** So it is both?
- Amit Sanghvi:** Yes.
- Maulik Patel:** Okay, I understand that. And as you mentioned about when you started work with IKEA here in which year the relationship with IKEA started?
- Amit Sanghvi:** We started late 2004 with IKEA.
- Maulik Patel:** Late 2004 so I mean in the last 10 years old?
- Amit Sanghvi:** Yes.
- Maulik Patel:** Okay. And we manage to do around close to around about 70 crore kind of top-line?
- Amit Sanghvi:** Yes. It is in our presentation by the way.
- Moderator:** Thank you. The next question is from the line of Pritesh Chheda from Lucky Investments. Please go ahead.
- Pritesh Chheda:** Yes, sir I quite did not get the answer on that interest cost increase in the quarter. I actually could not understand if you could tell again?
- Sanjay Shah:** See the current quarter's interest cost includes 77 lakhs of an FX expense which was on foreign exchange borrowing which we had taken which was repaid in the current quarter. So it includes that. Second is in the last year we are basically setting up the pharma plant and also expanding our EOU facility where we do manufacturing for IKEA. The pharma increase both

capitalize to operation which was sometimes in March. The pharma increase is being charged to revenue and that is the reason you say for an increase in the increase cost in the current year.

**Pritesh Chheda:** So until it was capitalized which is now getting charged to the P&L?

**Amit Sanghvi:** Up till March it was capitalized, post March it has been charged to revenue.

**Pritesh Chheda:** Okay. And what is the cost of borrowing that we have and we have about 22 crore funds in liquid assets also, if you could tell us what is the cost of borrowing today?

**Sanjay Shah:** Our average cost of borrowing would be because we have a mix of FX and rupee borrowing so our average cost of borrowings would be somewhere between 8.5% to 9%.

**Pritesh Chheda:** But that does not correspond with the reported numbers so, let us say half year reported is about 5 crores in which 77 lakhs is the transaction cost on the borrowing which you will refer to which makes it about 4.2 crores. Even if I annualized then it is well about 12%-13% because I think borrowing which we can see in as on the reported balance sheet which you reported is about 78 crores.

**Sanjay Shah:** You are right. The interest in finance cost also includes bank charges which are there.

**Pritesh Chheda:** So your cost of borrowings average you said is 8%.

**Sanjay Shah:** Yes about 8.5% to 9%.

**Pritesh Chheda:** This is when the foreign currency loan was there?

**Sanjay Shah:** Yes.

**Pritesh Chheda:** And now when it is repaid then what it becomes?

**Sanjay Shah:** I have talked about the current cost?

**Pritesh Chheda:** Okay, this is the current cost.

**Sanjay Shah:** Yes, the current cost.

**Pritesh Chheda:** So best way to look at it is basically look at annualizing this half yearly number without the 77 lakhs?

**Sanjay Shah:** Yes.

**Pritesh Chheda:** And when does the commercial operations or revenue booking on the pharma plant starts?

- Sanjay Shah:** We have started commercial operations in March. We expect some income to start from quarter four of the current financial year then going forward in the next year we expect that there will be substantial ramp-up in the next year.
- Pritesh Chheda:** What kind of utilization level one should expect next year?
- Amit Sanghvi:** Overall utilization level, are you asking for the pharma plant?
- Pritesh Chheda:** Pharma.
- Amit Sanghvi:** I would say 45% to 55%, about 50% utilization next year.
- Moderator:** Thank you. The next question is from the line of Sanjeev Kumar Panda from Sharekhan. Please go ahead.
- Sanjeev Kumar Panda:** Sir, just wanted to understand how is our terms with all our clients primarily the large clients because they are pretty large in terms of company so, when they would be sourcing from us what are the terms, conditions normally we supply to in terms of like in the bulk prices or is it linked with the commodity prices or how if you can help us to understand the pricing situation?
- Amit Sanghvi:** This is a slightly larger question but let me try to address it. With each customer we have different pricing strategy based on the segment in which that customer is. We price our products based on the complexity, value addition, compliance requirements and capacity utilization. These are the factors that play into the pricing. With most our raw material is neutral in the sense whether the raw material prices go up or go down it is passed on to the customer it is a customer who use an increase or take the decrease that is only to do with one third-of our business which is commodity plastics. Two-thirds of our businesses comes from engineering plastics where the volatility is much-much lower but even in that you will see pass through of material pricing. It is less volatile that is all.
- Sanjeev Kumar Panda:** And largely if I segregate among all the three-four areas that we are I know Healthcare, Automotive which is you see as a most profitable and most prospective within the space in terms of profitability and returns basis if you can just categorize?
- Amit Sanghvi:** I feel that today actually I can very confidently say that we have a very good mix of business of course this can be improved further but there are businesses which are cash generators, there are businesses that utilize capacity, give us efficiencies and scale that give us buying power from suppliers. There are businesses which are very high value-added and high margin. But you cannot segregate the two businesses. You need to balance. If I were to just do one, we would not really have a substantial portfolio it is about growing both simultaneously at the right ratios.



- Moderator:** Thank you. The next question is from the line of Ashutosh Garud from Reliance Portfolio Management. Please go ahead.
- Ashutosh Garud:** Could you give the reason for the revenue decline in FY13?
- Amit Sanghvi:** We talked about consolidation when I was answering questions. Consolidation also meant that we basically got out of low margin, low value, and low volume business and there was one in particular which led to a revenue decline but it was negative contributing.
- Ashutosh Garud:** Negative contributing in terms of is it a loss making business?
- Amit Sanghvi:** You can call it that, we were not generating much profit out of it I would not say loss making but we were definitely not generating healthy margin out of it.
- Ashutosh Garud:** Okay. And in the call you also mentioned that you are looking at a 100 million turnover by 2020 and so that would mean a growth rate of about (+25%) whereas if we look at even recently after the consolidation your growth rate is in the range of about 20 odd percent so could you tell us the reason for this uptick in the growth rate and are you seeing some inflection point in your business in terms of either because of some sectoral tailwind in certain sectors where you are present or is it more client specific or if you could give some idea on that?
- Amit Sanghvi:** There are multiple answers in the sense if you look at we have made significant expenditures in capacities over the last 18 months. You look at our results from last half year to this half year you will see a 37% increase. So maybe when you look at yearly financials from 2013 you do not see that much of a jump but when you look our year-on-year results for the last two years and amount of money that we have invested in creating capacities for specific customers you will see that we will definitely get to a \$100 million by 2020.
- Ashutosh Garud:** Yes, so more on that only. Last four to six quarter obviously the traction is there which can take you to \$100 million. So I just wanted to know more that. Is it the client sourcing has increased and you have reached a certain size where the client is more comfortable to give you more order or is it coming from the more number of clients or is it primarily by the mining of the existing client?
- Amit Sanghvi:** It is with the existing clients. We have not had too many new customers to our portfolio. We are growing with our existing clients. We are becoming larger with our existing clients and like you said, when you do that and you perform, clients become comfortable and they want to give more business to you.
- Ashutosh Garud:** Okay. And what are the investments which you have done in the last 18 months which you are referring in terms of overall CAPEX value term?

- Amit Sanghvi:** Last 18 months in the pharma plant itself we have invested 30 crores total CAPEX is about 60 crores. Total CAPEX done is about 60 crores in the last 18 months.
- Ashutosh Garud:** Okay. And given your product profile what kind of revenue it can generate?
- Sanjay Shah:** See there are three segments of the business that we look at: one is IKEA, one is Pharma and one is other businesses and each of these business has a different aspect to sales turnover ratio so, if you average it out I would say you probably look at between 2 to 2.5 somewhere in that range in terms of asset turnover
- Ashutosh Garud:** Okay. Around 2 to 2.5?
- Amit Sanghvi:** Right.
- Ashutosh Garud:** Okay. And where do you see your margins going forward with this operating leverage also kicking in so, you think that you could increase them by 100 basis points - 200 basis points year-on-year?
- Amit Sanghvi:** I would not like to give you a number but I think you will see improvement. As you have seen improvement over the last half and this half?
- Moderator:** Thank you. Next question is from the line of C. Srihari from PCS Securities. Please go ahead.
- C. Srihari:** Considering that your pharma business has not yet commenced, what is the kind of growth next fiscal year see on the base business ex-pharma?
- Amit Sanghvi:** Sorry, that is slightly incorrect. We have been in devices for several years now. We will successfully compliance drop delivery devices for regulated markets globally not sales for what has not commenced is our primary packaging products. And so I think I mentioned two or three times earlier that we are going to start seeing commercial orders in quarter four of this financial year ramping up over the next financial year.
- C. Srihari:** Right. So I mean ex of this the base business what is the kind of growth you would see next fiscal year let us say?
- Amit Sanghvi:** I anticipate utilizing 50% of the capacity next year of the pharma business.
- C. Srihari:** No, I mean ex this the new unit that you have set up I am not talking about that. I am asking about the base business I mean what is the kind of growth forecast you have for next fiscal for the base business?
- Amit Sanghvi:** About 25% overall in the company.

- C. Srihari:** But that would include the new pharma unit as well?
- Amit Sanghvi:** Yes, that will include the new pharma unit as well?
- C. Srihari:** Yes, so I wanted to know what you expect from the new pharma unit.
- Amit Sanghvi:** I would not want to give you a break-up on that.
- Moderator:** The next question is from the line of Sangeeta Purshottam from Cogito Advisors. Please go ahead.
- Sangeeta Purshottam:** So what I wanted to check with you was that given the businesses that you are in what are the kind of peak margins do you think business could actually get to so we are currently about 17.5% what is the maximum it can go to would it be 20, would be it less than that just some sense on that? And my second question relates to working capital, how does the whole cycle really work? Could you shed some light on kind of working capital that you enjoy? Is there any scope for improving the working capital management, etc.?
- Amit Sanghvi:** There is always scope for improvement in any aspect of our business but specifically on working capital I will ask Sanjay to answer that.
- Sanjay Shah:** On the working capital Sangeeta, if you again look at last four quarters or five quarters there has been an improvement in the overall working capital cycle but we have been able to compress the working capital cycle and improve the overall working capital cycle, that we achieve in a year we are now at about 4 times a year and going forward we would be looking at improving that.
- Sangeeta Purshottam:** Okay. And is there a typical I mean given that your customers are very large. Do you have any scope for negotiating with them in term of the kind of receivables periods that you have or credit terms that you need to give them?
- Sanjay Shah:** We would obviously look at negotiating on that but I think probably Amit can throw more light on that in terms of the discussions we have with customers on that.
- Amit Sanghvi:** When it comes to credit it is actually to be very honest with you most of our larger customers always pay on time. And there is no follow-up required. With the smaller customers even if even credit terms of 10 days or 15 days are given you have to spend 45 days in following up with them. So with large customers one is that whatever the payment terms are it would get billed into pricing. And second is that whatever that term is they actually pay on time so it does not really towards it makes not much of a difference because it is billed into their pricing anyways.

**Sangeeta Purshottam:** What kind of improvements have you actually made in the working capital management because if your terms with your clients are more or less fixed and they are being generally paying in time or they kind of stick to their payment history what is the scope for improving working capital? Which areas have you actually put your attention and what would you do going forward?

**Sanjay Shah:** See there are two or three things which we have been doing. One is we have been focused on when we basically looked at removing or basically exiting some small customers that is when our working capital improvement cycle started happening because these were customers who were the drag on the working capital like one of the question which was there on the call was we exited a large supplier and so a drop in sale that large customer was a huge drag on our working capital and one of the reasons for exiting the customer was the overall working capital cycle which we were having in addition to the margin issues which we had with the customer. At the same time with scale what also happens is our ability to buy material was quite a lot so you basically end up having the supplier stock material and then supply you on a regular basis. See typically give you an example there was a material which we were using we were probably using 20 tons a month we are now using 100 tons of that material so, we could change the shipment to come in every week so basically that gives us drag basically it pace up your payment to that supplier within that whole month. So that is how we have been trying to do and also look at how we are can improve overall working cycle improve debtors recovery and everything so it is a combination of all this which we have been trying to do in terms of improvement in working capital cycle.

**Amit Sanghvi:** To answer your question very honestly we have just gotten our feet wet when it comes to performance I think there is a lot of scope of improvement in all factors of our business.

**Moderator:** The next question is from the line of Rukun Tarachandani from Kotak Asset Management Company. Please go ahead.

**Rukun Tarachandani:** Sorry to come back to pricing again. But you have mentioned that for some of the SKUs the pricing is related to your margins. So just getting a clarity on that does that mean that if the raw material prices falls drastically your realizations and your revenue also falls and your absolute EBITDA also gets impacted on those products specifically?

**Amit Sanghvi:** On those products specifically, yes.

**Rukun Tarachandani:** Right, okay. And finally, sir you mentioned that the three segments: IKEA, Pharma, and the rest have different asset turns. Can you just mention the asset turns for individually for each other?

**Amit Sanghvi:** Rukun, even within those customer there are products which will have asset-to-turns 1:2 there products which will have to turns 1:3 that will be for us which will have assets turns 1:4. The bulkier the product gets then the more volume your asset-to-turn goes up, and it is also it is

margin sensitive. It is very difficult for us to generalize this but on your raw material question what I would like to add is that we are pretty much in all time low right now. Raw material prices are not going I hope they do not fall forever.

**Moderator:** Thank you. The next question is from the line of Saket Bansal from Dinero Wealth. Please go ahead.

**Saket Bansal:** Sir, I have question like you were saying that 20 crore CAPEX would be done in this year also. This is for Pharma sector sir?

**Sanjay Shah:** This is partially for Pharma portion and partially for IKEA.

**Saket Bansal:** Partially for Pharma. How much would be Pharma and how much would be IKEA can you give me any numbers?

**Sanjay Shah:** I think it would be split 50-50.

**Saket Bansal:** 50-50 would be split and when this CAPEX will come online?

**Sanjay Shah:** We have spent about 10 crores which have been put to use in like September balance will be sent in the current financial year.

**Saket Bansal:** So total in Pharma is then 40 crores with 30 crores already in place?

**Sanjay Shah:** 30 crores are only in the Pharma packaging plant.

**Amit Sanghvi:** We have two Pharma businesses – one is the device business and one is the primary packaging business.

**Saket Bansal:** Okay. So these 10 crores are for the device business then?

**Amit Sanghvi:** Right. The new investment is in the device business right now.

**Saket Bansal:** Okay. How much can we generate on this 20 crores?

**Amit Sanghvi:** I will not be able to answer that. You take the ratio of our asset-to-turn.

**Saket Bansal:** What will be the asset turn over in this 20?

**Amit Sanghvi:** It is between 2 and 2.5.

**Saket Bansal:** And these 20 crores CAPEX are you taking any new debt or it would be from the cash reserves?

- Sanjay Shah:** We would not be taking any new debt there was some debt which was a spill over which we had to grow in the current financial year from last year which has been drawn which has been shown in the results which have been published. Post that we would not be looking at taking any further long-term debt in the current year. It will be basically from the equity which we have raised and internal cash accruals.
- Saket Bansal:** And sir, your employee cost is increasing will the pattern remain same. It is basically because of the new plant, is it sir?
- Sanjay Shah:** If you look at employee cost as a percentage of sales in fact as compared to half one of last year has come down. Half one of last year we had an employee cost of 11.26%.
- Saket Bansal:** No, I am saying just quarter-on-quarter like from last quarter to this quarter.
- Sanjay Shah:** Yes, there will be some changes on that but there will not be very big changes in that.
- Saket Bansal:** Okay. And about the gross margins like it was marginal dip like 3.7 and this were 40 basis points only. So it will be the same throughout the year?
- Sanjay Shah:** Just one moment please, I did not get your question again Saket.
- Saket Bansal:** The 37.5% basically was your gross margin would it remain same?
- Sanjay Shah:** It should more or less remain the same, it would remain same.
- Moderator:** Thank you. The next question is from the line of Sangeeta Purshottam from Cogito Advisors. Please go ahead.
- Sangeeta Purshottam:** Yes, I am actually just coming back to the question I asked earlier on peak margin and also return on capital employed. Just wanted to get a sense whether this kind of business or aim does it do the margin at what level would margin sort of peak out and what is the kind of return on capital that you expect to generate over the next couple of years. Do you have a number in mind that you are targeting or what is that this business can generate just wanted to get a sense?
- Sanjay Shah:** Sangeeta this is Sanjay if you look at return on capital employed again I go back if you look at last four quarters you have been seeing an improvement on return on capital employed with an exceptional of March when the return on capital employed took a dip for the reasons that we had raised equity in December commercialize the Pharma plant in March which did not yield in your results so, that was the reason you saw that. Post that if you see June and if you look at September number you will see an improvement at an ROCE level. We expect the ROCE improvement trend to continue. If you look at next year with Pharma coming in you will see

some further improvement. To give a number would be too premature right now and we would refrain from giving them.

**Amit Sanghvi:** See Sangeeta, in terms of range in our businesses with EBITDA levels as low as 14%-15% to as high as 30%-40% but again I reiterate we like to maintain a good balance between all of our businesses this is how we keep our competency and capability portfolio.

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

**Amit Sanghvi:** So, I would like to sincerely thank everyone for joining this call. I hope that we have been able to response your questions adequately. I know that there have been some callers to whom we have refused to answer it is not our willingness to do so maybe it is too premature to answer those questions right now. Thanks once again and we look forward to hosting you again after the next quarter. And if you have any further questions you can get in touch with our Advisors which are SGA. Thank you.

**Moderator:** Thank you very much members of the management. Ladies and gentlemen, on behalf of Shaily Engineering Plastics, that concludes this conference call. Thank you for joining us and you may now disconnect your lines.