PPAP AUTOMOTIVE LIMITED

"PPAP Automotive Limited Q2 FY17 & Half Year Results Conference Call"

Transcript

October 28, 2016

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Moderator: Good morning ladies and gentlemen. I am Rohan Mehta, moderator for this conference call. Welcome to the conference call of PPAP Automotive Limited arranged by Concept Investor relations to discuss its Q2 FY17 and half yearly results. We have with us today Mr. Abhishek Jain - Whole Time Director and Manish Dhariwal - CFO. At this moment, all participant lines are in the listen-only mode. I would now like to hand the floor over to Mr. Abhishek Jain. Thank you and over to you sir.

Abhishek Jain: Thank you Rohan for the introduction. Ladies and gentlemen a very good morning to all of you and welcome to the conference call to discuss the financial performance for quarter 2 of financial year 2017 of our company. The company's Chief Financial Officer, Mr. Manish Dhariwal is also joining us on this call. To begin with, I will provide you a brief background about our company. I apologize if some of you have to listen to this introduction again. Kindly refer to the presentation already shared with you. The company was originally incorporated in 1978 for the manufacture of custom made extrusion products. The company commenced the automotive part business in 1985 with start of production of Maruti Cars in the Indian markets. The firm was converted into a public limited company in '95 and was listed on the Indian stock exchanges in 2008. In May 2014, we changed the company's name to PPAP Automotive Limited. We are a leading manufacturer of automotive sealing systems, interior and exterior injection molded products. Our company's state of the art manufacturing facilities are located in Noida, Greater Noida, Chennai and Pathredi in Rajasthan. All our plants are environment, quality, safety and health related certified which are TS 16949, ISO 14001 and OHSAS 18001. We are working with 3 Japanese companies for our technology requirements. Our relationships with these companies are up to 25 years old. Apart from our main company we have established a joint venture company with our technology partner as well. After the establishment of this company, as a group, PPAP can cater to the requirements of the entire automotive sealing systems of our customers. Today, the company manufactures over 500 different products for its customers and continuously targets to achieve zero defects and zero PPM in quality and delivery performance for all its customers. Our company is led by Mr. Ajay Kumar Jain who is the Chairman and Managing Director. He is currently serving as a president of Toyota Kirloskar Suppliers' Association as well. I am myself part of the Executive Committee of Honda Suppliers Association. Our company's target is always to be our customers' number one supplier. We strive to proactively meet the customers' expectation and are continuously evolving our products and services to meet their enhanced requirements. All our policies and decisions are in line with what the customer desires from us. It is this strategy that has resulted in our leadership position in the respective product segments that we cater to. The company's core competence is in automotive sealing systems and injection molded products. You can see the products that are manufactured by us, in the automotive sealing systems as well as the interior and exterior injection products in the presentation which is already shared with you. The company primarily services the passenger car segment and has recently started supplying to the LCV segment as well. All Japanese OEMs operating in India are our customers. A few European and local car makers like Tata and Mahindra are also being catered by us. About 10% of our products are CKD exports through our customers to countries like Japan, Europe, Mexico, Venezuela and many other countries. We are also capable of doing in house product designing to manufacturing as well as testing and validation. This integrated capability gives us a very strong competitive edge over our competitors as we are able to give our customers an integrated, cost effective solution for their product requirement. We have a track record of superior performance with all our customers and we will continue to be amongst the preferred suppliers for our customers. In our continuous process to add new customers and to expand our product portfolio, we are happy to announce that we have recently added SML Isuzu, which is a leading LCV manufacturer as a new customer. We would be manufacturing instrument panels for them.

Now I will take you through the financial performance for the period under review. The detailed slides, have already been shared with you. I would like to give you a brief summary of the same. For the second quarter ended September 30, 2016, PPAP recorded a total income of Rs. 81.97 crores as compared to Rs. 80.67 crores in the corresponding quarter last year. EBITDA grew by 3.34% in quarter 2 of financial year '17 at Rs. 15.15 crores compared to 14.66 crores in the same quarter last year. Sequentially, the EBITDA was up by 20% as compared to 12.62 crores in the first quarter of the current year. The companies EBITDA margins stood at a robust 18.48% in the second quarter this year, as compared to 18.18% in last year and 15.58% in the previous quarter of this year. Profit after tax stood at Rs. 5.27 cores in this quarter as compared to Rs. 4.55 crores last year same quarter and Rs.3.57 crores in the first quarter of this year. The company recorded a PAT margin of 6.43% as compared to 5.64% last year and 4.4% in the previous quarter.

I will also briefly take you through the half yearly financial figures. The total income stood at Rs. 162.96 crores compared to Rs. 153.91 crores in the same period last year. EBITDA stood at Rs. 27.77 crores in the first 6 months of this year compared to Rs. 26.94 crores in the previous year. The net profit stood at Rs. 8.84 crores which is up by 17.4% compared to Rs. 7.52 crores last year. The Board of Directors in our meeting concluded yesterday have reviewed the performance of the company and have declared an interim dividend of Rs. 1.25 per share. The total dividend that we paid out last year was Rs. 2 per share. The market saw strong recovery in the second quarter of this financial year compared to the first quarter. We expect the growth momentum and the increasing sales strength to sustain in the near future. Improving efficiencies across all areas of operations is a never ending exercise for us and we are focused towards the same. Alongside, we are consciously exploring growth opportunities. Together this robust combination will take the company to higher and new heights.

As I stated earlier, we are continuing developments of parts for many new models which will be launched by our customers in the current year and upcoming years and are continuously discussing with them about new models and new products thereafter. In this quarter we commenced part sales for the Kwid model mainly for the Brazil market which is the CKD export for us.

The debt equity ratio of the company as on September 30, 2016 stands at 0.27. Our CAPEX commitments are capable of being met by internal accruals.

Now I would like to leave the floor open for questions that you may have. I and Mr. Dhariwal will try our best to answer your queries. Over to you Rohan.

Moderator: Thank you sir. Ladies and gentlemen, we will now begin with the question-and-answer session. First question comes from Mr. Rohit Chawla from Axis Securities.

Rohit Chawla: Actually we are into 2 main products, automotive sealing systems and injection molded products, Sir, I wanted to know the market size of this and how much is catered by the organized and the unorganized segment, what is your market share and which are the other players which you are competing with?

Manish Dhariwal: You asked number of questions, so I will answer them one by one. From the automotive sealing side, you can break the market into 2 parts, one is the polymer based that is plastic based extrusion products and the second is the EPDM or the rubber based extrusion products. On the plastic based extrusion products, we are clearly the market leaders and our market share would range around 90%. On the EPDM or the rubber based automotive sealing parts, we have made a recent entry and our market share in that sense would be very small. The size of both the segments you could say is broadly equal. May be on the rubber side it will be slightly higher. Now coming to the interior and exterior injection parts, this market is a huge market and we are a leading supplier to Honda in this particular product segment. We also sell similar parts to Maruti. There the market size is huge. So we are one of the key players in this business. In terms of the competition, on the automotive sealing side, there are players like Anand Nishikawa, TG and such players. On the injection molded side, the competition is from players like Krishna Maruti, Motherson etc.

Rohit Chawla: How many catered by the unorganized players?

Manish Dhariwal: See unorganized segment actually doesn’t exist if you ask me, as we are primarily into OEM automotive business. So in this OEM automotive business, unorganized players do not exist. They are all legitimate big companies; some of them are listed companies, some of them unlisted companies. But there is no such unorganized segment in the automotive industry with the OEMs.

Moderator: We have our next question from the line of Lalit Kumar from MCA Management.

Lalit Kumar: I see from the financials that as on 30th September I think the debt on the book was about 58 crores and I see for this particular quarter the finance cost has reduced from 1.6 to 1.4, so can you please let me know the current debt position as on 30th September?

Manish Dhariwal: The total debt position as on 30th September stands at 58 crores and the interest cost as you rightly noted in that 1.43 crores for the quarter. If you would look at our previous transcripts you would know that, an underlying element with us is continuing efficiencies all across.

Lalit Kumar: So any further plans to reduce this debt?

Manish Dhariwal: Part of this debt is term debt and our annual repayment is of about Rs. 14 crores. We also get interest free loans from PICUP which is the investment arm of the state of Uttar Pradesh. Some money will be coming from that side but the Rs. 14 crores, it is going to be an annual repayment which shall continue. So we are at this point of time not looking at raising any more debt. So on a consolidated basis, the debt reduction is expected to continue. This is subject to new opportunities and the growth plans that come across which then will be decided at that particular point of time.

Lalit Kumar: So who is your top customer and how much of revenue concentration comes from them?

Manish Dhariwal: Maruti is the leading customer for us. Maruti also happens to be the leading car manufacturer in the country and it contributes around 45% to our sales turnover.

Lalit Kumar: How much of the pricing power do you have with such a concentrated player?

Abhishek Jain: I didn’t understand the question.

Lalit Kumar: The pricing power, since Maruti constitutes about 44% of your business and there is always a risk or a fear for a shareholder that touchwood, nothing goes wrong, but how much of pricing power in terms of negotiation is there with Maruti?

Abhishek Jain: See today it's a very competitive scenario. So actually everyone's selling price is actually determined by competition. And apart from being leaders in this industry, we have a very fair policy with all our customers. So we never try to take advantage of our leadership position to them, because we got to have a continuous and an everlasting relationship with all our customers.

Lalit Kumar: So what is the plant utilization capacity?

Manish Dhariwal: The capacity utilization obviously has improved in the second quarter., you could say that our capacity utilization would be in the region of 85%.

Lalit Kumar: And so what do you see the demand growth in say H2?

Manish Dhariwal: We believe that the trend is expected to continue.

Lalit Kumar: So seems to be the same as what we did in H1?

Manish Dhariwal: Better, you could say that.

Lalit Kumar: Because you have added SML Isuzu also right?

Abhishek Jain: But that is going to take some time. We generally in automotive industry, once you get some business it takes about 2 years to mature that business and to start supplies.

Lalit Kumar: How big is that opportunity?

Manish Dhariwal: The opportunity is big in the sense that our plans of expanding into the different areas which is like LCV, 2 wheelers, which is like other areas, that has fructified. So if you look at the opportunities in terms of the revenue perspective, that will not be as big as you see in Maruti or Honda but certainly it is a very good beginning and it is expected to grow. We are also obviously to pitching other customers and on overall basis LCV business we believe is going to play a bigger role in our fortunes.

Moderator: Thank you. We have the next question from the line of Paras Adenwala from Capital Portfolio Management Services. Please go ahead.

Paras Adenwala: Just had a couple of questions, considering the fact that close to half of your business comes from Maruti, which is really growing at a rapid pace, why is it that you are really struggling to grow the topline?

Manish Dhariwal: You know Paras, we are not just supplying to Maruti, I am happy to share that each and every Japanese car manufacturer in the country is our customer. Alongside we also supply to Tatas, we also supply to Mahindra, we also supply to GM and Ford in a small way. So market for us is basically the sum of production, from all these players and as we noticed that Maruti has grown very well but i cannot say the same for some other customers. So if you look at the sum of the whole, then that is how the situation is emerging.

Paras Adenwala: Would you say that Maruti plus Honda would be about $3/4^{th}$ of your turnover?

Manish Dhariwal: Yeah more than that.

Paras Adenwala: So probably that explains, Honda hasn't being doing too well, right?

Manish Dhariwal: Yes unfortunately.

Paras Adenwala: So that brings once again to the same question, that one of the participants kind of asked, is the concentration risk while it is very hardening to note that you are trying to reduce the concentration, but it is going to be a while before rest of your customers kind of scale up.

Manish Dhariwal: Paras, you have observed very correctly, but we are very confident that our policy of de-risking our business in the overall car segment has paid off. There were times when Maruti used to be 80% of our turnover. Today it has come down to half, and in fact last year it went to even lower. As Mr. Jain also shared in the call, that we are looking at other areas and have made a very good beginning in LCVs and we also are also looking at two wheelers, we are also looking at other opportunities, so the policy of de-risking is very much on and it is certainly going to bring results.

Paras Adenwala: And again if you look at from the categories, while breakup of your turnover, a large part of your turnover comes from passenger vehicles?

Manish Dhariwal: Yes.

Paras Adenwala: Almost everything. You are just trying to get into the LCV segment. Even if LCV picks up, I think you will continue to depend on passenger vehicles for topline growth at least in the next couple of years or may be even more, would you say that?

Manish Dhariwal: I would like to mention that in the passenger car market also there is a fair amount of traction taking place like we have already mentioned that we are in talks with the second largest player in the game which is a Korean company, Hyundai, and now we are hearing talks of Daihatsu and also Kia coming in. We are talking to them as well. And as the OEM continue to sell for the overall international market, CKD export size will also increase, we in fact mentioned that in this quarter, we started supplies for the Kwid, which is meant for the Brazilian market. So when you look at the overall picture, we believe that de-risking policy that we are very strongly working on, is going to bring very good results and soon.

Paras Adenwala: When you say soon, would you say that your topline growth will start improving over the next couple of years or may be from the next year?

Manish Dhariwal: Topline growth as usual should start improving from next year onwards, yes.

Paras Adenwala: I think the way I see it right now, while it is very heartening as I mentioned to see that you are really adding customer at the faster clip, but looking at the customers that you cater to locally, on one hand you have Maruti and Hyundai who are really loading over the passenger vehicle market. The rest of the guys are really struggling to have growth and if you have new product launches from these guys that has also kind of slowed down, from some of the Japanese guys. So considering that fact, until the time Hyundai also scales up, Maruti doing very well but on the other hand Honda which is also a large heavy weight your kitty, that keeps on slowing down so it kind of neutralizes the growth that Maruti is kind of doing, so that is really putting an impact on your top line growth. Would you like to concur with that or do you have any other observations?

Abhishek Jain: I think Mr. Paras, your observations are correct to some extent, we are virtually dependent on Maruti and Honda primarily for most of our businesses but there is lot of other opportunities also that we are exploring like the CKD exports market, we are expecting almost 10% contribution coming from that area. So that is why we are getting more aggressive in getting new customers on board. We understand that it is a risk being focused only on Maruti and Honda and if these 2 players don't do well, then that reflects on our performance as well.

Manish Dhariwal: See in a way, if you look at the total Indian car market, you will notice that it is Maruti that the people are buying and what is good is if they buy Maruti, they buy parts from me. If they buy Honda they, buy parts from me, if they buy Innova, they buy parts from me, if they buy a Kwid, they buy parts from me. So how I have managed is that I can do everybody. So basically if Indian car market grows, then we basically grow.

Paras Adenwala: That's pretty much it from my side; I only hope that you could de-risk your portfolio as soon as possible.

Moderator: Thank you. We have our next question is from the line of Rohan Korde from Prabhudas Liladhar. Please go ahead.

Rohan Korde: Sir just wanted to know, since Maruti's new model is commencing in the next quarter; are planning to set up a line over there to supply to that plant?

Abhishek Jain: Yes in fact we are discussing with Maruti for the injection molding requirements. And for Gujarat area, we have already procured the land and currently we have submitted some plans for approval to the government. So once those plans are finalized from the government side and the Maruti expectations from us are clear, then we will go ahead with investments in the Gujarat plant as well.

Rohan Korde: So our plant is not within the vendor park for Maruti, is that the scene right now?

Abhishek Jain: Our land location is about 30 kilometers away from Maruti. As a strategy, we don't like to be very close to our customers because of IR issues primarily.

Rohan Korde: Say the plant starts in 4Q, our plant will be commissioned may be somewhere in the second half of 18 or 19, would that be a scenario?

Abhishek Jain: Yes around that time.

Rohan Korde: Maruti after the first line of 2,50,000 units may look at expanding it further with a second line as well. So when we set up a plant, would it be considering the exit capacity for Maruti in Gujarat plant or would it be for the initial 2,50,000 capacity?

Abhishek Jain: What Maruti has planned is this line number 1, and line number 2, two lines they are planning. So one line will be for the existing model which is being produced in their plant in Manesar. So that product will get transferred from Manesar to Gujarat. And 2,50,000 will again be primarily for Swift vehicle which is going to be transferred again from Manesar to Gujarat. So as such there is no special requirement of any additional capacities to meet these requirements. But since the manufacturing location has changed from Manesar to Gujarat, and it is being made by SMG, so therefore we might need to have capacities in Gujarat to cater to their local requirements.

Rohan Korde: And what is the capacity expansion amount that we might need to spend for this?

Abhishek Jain: That is still under review because Maruti has not told us about their confirmed parts and confirmed plans from us. So whatever we do has to be in line with what our customer requires. So that is still under review right now.

Rohan Korde: We are supplying to Swift and Baleno both which will be shifted to Gujarat?

Abhishek Jain: Yeah, we are supplying to both the models.

Rohan Korde: In terms of the debt, as of March '16, it was about 58 crores. So what would be the debt as on September?

Manish Dhariwal: See it was 74 crores total in March 16 and that has come down to 58 crores in September 16. Basically what happens is, the current years repayment are not shown as part of debt but they are shown as part of other current liabilities, as required under the Companies Act. So if you total everything, then you will know from 74, it has come down to 58. But this 58 is not sacrosanct because 58 includes short term debt which is a working capital, OD facilities, which goes plus and minus, depending upon what point you look at it, but the fact of the matter is, our debt levels are going to be coming down and as they have been over the last few quarters and that is expected to continue.

Rohan Korde: Any further expansion in capacity will then be internal accruals only I guess.

Manish Dhariwal: As of now whatever plans we have, they are all going to be met by internal accruals. So we are not looking for any debt.

Rohan Korde: And on the 2 wheeler and LCV side, when will the new products start contributing meaningfully to our turnover?

Manish Dhariwal: If you look at SML, now we are going to be making tools for them and then the supplies will begin. So it is a very structured process. I guess will take some time, a year or so.

Moderator: Thank you. We have our next question from the line of Punit Gulati from HSBC, please go ahead.

Punit Gulati: Is it possible to share that what products are you supplying to Kwid, Innova, Ignis?

Abhishek Jain: Kwid, we are primarily supplying the sealing system, the outer belt, roof molding, and inner belt. So these products have been in fact designed by us only. With the local engineering team in India, in Chennai area. And we are also working on with them for their future platforms.

Punit Gulati: And for the other, Innova Ignis?

Abhishek Jain: For Innova, also primarily it is the sealing system. So there the products are much more, where we have outer - inner roof molding, wind shield moldings. Now Fortuner is also coming out. So Fortuner also similar products are there. We have one special product also starting up with Fortuner.

Punit Gulati: For Ignis and Vitara?

Abhishek Jain: For Ignus and Vitara we have a combination of both sealing systems and the injection products. But the injection products are like small injection products not as big as what we do for Honda like door lining or something, like side protectors and some other interior components.

Punit Gulati: And what would be the content value for these products that you would be supplying?

Abhishek Jain: For these particular models?

Punit Gulati: Yeah, for these models.

Abhishek Jain: For these models it would be around Rs. 1500 to Rs. 2000.

Punit Gulati: And for the existing products what is the content per car?

Abhishek Jain: See for Honda we have a substantially higher content which is about Rs. 7000 to Rs. 8000 per car. For all our customers, currently we are about Rs1100 to Rs1500 range.

Punit Gulati: If once these products are announced, is it possible to increase the content supply or this is the max you will be able to supply to them?

Abhishek Jain: See what this Rs. 1500 per car business I am talking to you about, is primarily the plastic sealing system which is done by our company and the Rs. 6000 per car comprises both of plastic extrusion, plastic sealing system and interior and exterior components. So this Rs. 1500 and Rs. 6000 does not include the rubber parts. Rubber parts add about another Rs. 1500 to Rs. 2000 to a car, which we are doing in our joint venture company. One is that area of expansion for these parts. Second area is this injection parts. So for injection parts; primarily our customer is Honda because of which the business per car is Rs. 7000. But the other customers we are doing some small parts or something for them. So we have an opportunity to grow further especially with the start of our Chennai plant, our Pathredi Rajasthan and soon to be Gujarat plant.

Punit Gulati: So will it be fair to say that sealing system business is growing much faster for you?

Manish Dhariwal: See you can't actually say that. Basically the customer is the same. Barring the recent times when Honda actually is not growing that well, but otherwise the growth rate by and large is the same. Actually in the injection business will grow at a faster rate because as we sign on more customers.

Punit Gulati: What is the current break up now between injection and sealing?

Manish Dhariwal: 50 – 50. Plus minus here and there but otherwise it is equal in terms of the size.

Moderator: Thank you. We have our next question from the line of Dheeraj Shah from GEPL Capital. Please go ahead.

Dheeraj Shah: What was the volume growth in Q2?

Manish Dhariwal: Volume basically as what you see on the car numbers. It's exactly the same.

Dheeraj Shah: Means? I didn't get it.

Manish Dhariwal: We are a pure OEM player, so our volume growth is compatible to what the industry growth has been over the same levels.

Dheeraj Shah: So between 10 – 15% right?

Manish Dhariwal: If you look at the total then not, but if you look at just Maruti, then more than 10%.

Dheeraj Shah: What was the tool sales in this overall income?

Manish Dhariwal: The tool sales were 1.23 crores in this quarter.

Dheeraj Shah: And what was it last year?

Manish Dhariwal: Last year it was just a few lakhs. Rs. 70 odd lakhs in the September quarter.

Dheeraj Shah: And when do we expect this Korean customs to fructify?

Manish Dhariwal: The talks are on with them and it is in process actually. We are not in a position to exactly put a timeline as to when it will happen, but the talks are on.

Dheeraj Shah: By FY17 - FY18 may be some time we can expect because one side Maruti is doing well but on the other side, Honda is not doing well. So net net your topline is on flat side. Although margins have improved but we need topline growth also.

Manish Dhariwal: You are right. See we are working on it. Now our discussions with the Korean group, they are proceeding. But it's a new geography, new set of people, different mindset, so obviously it is taking some time. But then it is something that we are confident, sure will happen.

Dheeraj Shah: And what is the full year guidance in terms of revenue because if we see in H1 FY17 it is only 6%, do we expect double digit growth?

Manish Dhariwal: You are right but we can't give futuristic guidance as a policy but as we also mentioned as a trend that we have seen, it is expected to continue. So that basically is a fair indication.

Dheeraj Shah: And in terms of margin sir? Do you expect the margins, to be sustainable in the next 2 quarters?

Manish Dhariwal: We are really working very hard and in a focused way to protect and improve on these margins.

Dheeraj Shah: And sir in this quarter, you have added SML Isuzu also right? So may be in the next 2 quarters, any plans to add a new OEM?

Manish Dhariwal: Our fingers are crossed and our discussions are on and I am confident that something will come up.

Dheeraj Shah: So this is in which category? 2 wheeler, may be LCV, MHCV, 4 wheeler?

Manish Dhariwal: The conversations that are on right now are numerous. Which one clicks first is something that is not in our control. But growth is a focused area for us and we are working on all fronts. So there is expected to be some news on this in a short while from now, something will happen yes.

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

Manish Dhariwal: Well Thank you Rohan and team of Concept to organize this conference call. I would like to pay my gratitude to all my analysts and investor friends who took time out of their busy schedules to listen to us today. Please feel free to contact Concept IR in case you have any questions. Also if you happen to be in the NCR region, do give us an opportunity to show you our operations. Wishing everyone a very happy Dhanteras and a very happy Diwali. Thank you.

Moderator: Thank you all for being a part of conference call. If you need any information or clarifications, please mail at parin@conceptir.com. Ladies & gentlemen, this concludes your conference for today. Thank you for joining us at Chorus Call Conference Services, you may now disconnect your lines.