"Essel Propack Limited

Q3 FY2020 Results Conference Call"

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Moderator: Ladies and gentlemen, good day, and welcome to the Q3 FY2020 results conference call of Essel Propack hosted by Emkay Global Financial Services. We have with us today Mr. M. R. Ramasamy, Chief Operating Officer; Mr. Vinay Mokashi, Whole Time Director, Mr. Parag Shah, Chief Financial Officer, Mr. Amit Jain, Head Corporate Finance; Mr. Suresh Savaliya, Head Legal, Company Secretary and Compliance Officer; Mr. Deepak Ganjoo, Regional Vice President AMESA; and Mr. Ashok Vashisht, Regional Finance Controller AMESA.

As a reminder, all participant lines will be in the listen-only mode and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing "*" then "0" on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Varshit Shah of Emkay Global. Thank you, and over to you, Sir!

Varshit Shah: Thank you Bikram. Good evening everyone. I would like to welcome the management of Essel Propack and thank them for giving us this opportunity to host the earning call. I would now hand over the call to management for their opening remarks, post which we will take up Q&A. Over to you, Sir!

M. R. Ramasamy: Thanks Varshit. Hi everyone. Welcome to the third quarter earnings call for the financial year FY2020. Investor presentation has been shared with the stock exchanges and I will refer to that presentation in my opening remarks. As a reminder, this quarter is the second quarter since Blackstone became the new controlling shareholder of the company. We as management team are very excited about this partnership. On page 4 of presentation, I want to recap whatever new mission in our new avatar EPL 2.0 and our progress in Q3. There are four key messages on this page that I want to remind everyone.

Message one in this Avatar, our mission is to deliver capital efficient consistent earnings growth. I would like you all to know three key words in this mission, capital efficient, consistent and growth. Message number two - we have the building blocks in place to deliver on this mission. The entire board has been revamped with fit for purpose experts who continue to be deeply involved in the key strategic initiatives being undertaken by the company. I would also like to formally welcome Parag Shah who joined as our new CFO in November 2019. Parag comes with 25 plus years of consumer and pharma industry experience with Unilever, Nike and most recently at ACG Group. In addition, we as management team continue to work closely with Blackstone's global advisor and portfolio company network to support us deliver on this mission. Mr. Harish Manwani, ex-chairman Hindustan Unilever and CEO of Unilever globally, he is helping with the key account management and various growth initiatives of the company, Mr. Dhaval Buch, Ex- supply chain Head for Unilever Globally is leading what we are internally calling project phoenix, a productivity improvement program, finally Mr. Dawn Anderson, who is a global energy expert with Blackstone he is helping the company optimize its energy utilization globally. The effects of this lean and productivity initiatives has started to reflect in the improved margin, you are all seeing in Q3.

Coming to message 3, the key levers to deliver on this mission are one, accelerated growth in personal care; two, continued leadership in oral care; three, innovation and sustainability solutions and four prudent capital allocation across regions and finally we as a team are proud to report that the early results of these efforts are reflected in our Q3 financials.

Coming to next page, Q3 reported revenue up by 2.4% year-on-year, EBITDA is up 20.1% with margin expansion of 328 basis points; PAT is up 32.3% year-on-year. As promised last time, we as management team will measure ourselves on the progress we have made on our mission. The relevant matrix on a recurring basis adjusted for any one-time items are on page 6. Q3 revenue grew by 3.7% year-on-year on constant currency basis. This growth was achieved despite a tough macroeconomic environment in India and China and 1.5% revenue growth impact due to pass through of lower raw material to contracted customers. Adjusted EBITDA grew by 17.3% year-on-year on a recurring basis and adjusted EPS grew by 40.8% year-on-year. This growth has been driven by improvement in revenue mix, productivity and cost optimization across regions. Focus on capital efficiency is also visible in the numbers; against Rs.304 Crores of capex spend in FY2019, capex spend in nine months of this year has only been Rs.96 Crores; as a result return on capital for the business has increased from 16.7% to 17.8% and the net debt has reduced to Rs.361 Crores which is at healthy level of 0.7 times of EBITDA.

The key message on page 7 is that this quarter has been the strongest quarter in terms of absolute EBITDA in the history of this company. The strong operating performance has been achieved with prudent capital allocation and lower capex spend. The improvement in ROCE to 17.8% from 16.4% last quarter is a testament to it. With the recent volatility in macroenvironment and raw material prices we got a few queries from some of you asking what it means for the company's margins. Given EPL's presence across end to end value chain and being a value add partner to many of our customers, variation in key raw material that is Polymer prices do not translate to margin variations. Despite significant movement in the polymer index over the last eight quarters, our gross margins have remained in a narrow band. In many of our long-term contracts, the raw material prices are pegged to the relevant index and any movement in those indexes is contractual pass through to our customers.

Now I will hand over to the Parag Shah to walk you through the key business highlights of Q3 FY2020.

Parag Shah: Thanks Ram. It has been two months; delighted to be here and be part of the journey to deliver our mission of capital efficient consistent earnings growth.

Let me start with the first business highlight. Accelerated growth in personal care segment. Personal care has been a major growth driver for the company for the last eight years growing at a CAGR of 17% and now contributes to 45%

of the company's revenue as compared to 34% of revenue five years back. We have been industry leaders in driving conversion to laminated cubes in newer subcategories like haircare and we continue to expand the market in categories like eye care and hand care. Personal care grew by 14% year-on-year in the first nine months of FY20 despite a weak demand environment in India.

Coming to the regions, personal care segment grew by 23% year-on-year in Americas, 20% year-on-year in Europe, 12% year-on-year in EAP and 6% year-on-year in AMESA in the first nine months of FY20. We continue to provide innovative lamitube solutions to our customers in beauty and cosmetic as well as pharma categories across the globe.

Second; Oral care continues to provide solid ,stable base to the company and EPL continues to strengthen its market leadership in the oral segment globally. We continue to be preferred suppliers to major global and local oral players worldwide. This has been enabled by our constant product innovations and agile supply chain models suited to our customer needs.

Third, Europe continued its strong revenue growth and profitability improvement in Q3. Q3 revenue grew by 12.4% year-on-year and 16.7% in constant currency with 10.8% year-on-year growth in personal care category. The strong revenue growth is driven by new customer wins as well as wallet share increase in existing customers, on the back of several initiatives which includes strengthening of the front end sales team and investments in manufacturing capabilities. The EBITDA margin for the region improved to 13.5% in Q3 of FY20 compared to 8.7% in Q3 of FY19. The margin improvement was driven by fixed cost leverage as well as productivity initiatives taken under Project Phoenix.

Fourth, we continue to be the industry leader in innovation and providing eco-friendly solutions to our customers. As mentioned in last quarter, we now have Platina laminate, which is 100% recyclable and has been certified as recyclable in code 2 stream by the Association of Plastic Recyclers, USA. We are happy to report that our new laminate has seen strong traction with customers globally. One of the largest global oral players recently launched its first recyclable tube in partnership with EPL. Similarly another popular oral brand in the United States has commercialized its sustainable tubes on the back of EPL's Platina laminate. We continue be the torch-bearers for the industry in the sustainability journey. As you all can see, we continue to make solid progress across all dimensions to deliver on our mission of delivering capital efficient consistent earnings growth.

Now I will hand over back to Ram to conclude the presentation.

M.R. Ramasamy: To conclude, we are excited about the momentum we are seeing towards achieving our mission. We continue to have strong business development pipeline across regions. The results of the various growth and productivity initiatives underway are starting to show. We are excited about the many opportunities in front of us and remain committed to deliver capital efficient, consistent earnings growth. Now we will pause here and take any questions you all may have.

Moderator: Thank you Sir. Ladies and gentlemen we will now begin the question and answer session. The first question is from the line of Percy Panthanki from India Infoline. Please go ahead.

Percy Panthaki: Sir congrats on good set of numbers especially on the margin front you have delivered sort of good margin expansion. However, just a little bit of concern on the top line growth because out of four of your geographies three of them are in a plus or minus 1% kind of a band almost all three geographies except Europe is flat, just wanted to understand what is the reason for the sales growth not picking up in these three geographies?

M.R. Ramasamy: Percy you know the macroeconomic conditions in India, it has continued to be tough, we are working on many fronts. Oral care has it own challenges but we are able to grow in personal care as Parag was saying - AMESA being India driven; and going back to Americas, the December quarter is always soft - we do not work for 10-15 days because of year-end holidays and things like that and in November we have Thanksgiving; China is growing - as we have explained in many of the concalls, our growth comes from newer customers and that we see a traction going forward we should see more and more.

Parag Shah: Percy just to add in case America's in constant currency terms it grew by 0.5%.

Percy Panthaki: Okay Sir just some follow-up questions so in India basically you are saying the main sort of thing pulling down is oral care category; if you can just give me some color in India what is the growth separately for the oral care business and for the beauty and personal care and pharma?

M.R. Ramasamy: Percy it will be 1.5% or so lower in oral care and about 6% growth in personal care. Personal care being beauty and cosmetics and pharma put together.

Percy Panthaki: Personal care would be what percentage of the portfolio?

M.R. Ramasamy: I think India will be somewhere close to 48%.

Percy Panthaki: Sir then the math does not add up no, because the overall is minus and if oral care is minus -1.5 and personal care is +6 then the overall growth should be in positive territory what am I missing here?

M.R. Ramasamy: See there are difference in ASP and things like that, right. Percy let me check and come back to you.

Percy Panthaki: Maybe I will take it offline. Sir then I can understand India macroenvironment is poor and that is why your growth is poor, but in EAP and America basically what is the plan to accelerate the growth especially in Americas. The reason which you gave is that there is soft quarter with closure due to festivals but that would have been true even in the last year because we are comparing a Y-o-Y number right?

M.R. Ramasamy: Yes, correct, see what happens is that iwallet shares of all our customers are intact. There are offtake variations which come from their earlier stocking and things like that right and we see a very strong traction in Q4 and we already have done well in January so we will see a strong growth in America.

Percy Panthaki: Second question was on margins. This quarter you have done about a 22% EBITDA margin for the company overall consolidated so is there a seasonality in the margins or should I take this 22% as a sustainable number for annualized basis.

Parag Shah: Percy, this improvement in margin would be sustainable in narrow band.

Percy Panthaki: Okay so there is no seasonality in the sense that December quarter would be higher than the annual number so there are no such things?

Parag Shah: Yes; as I said narrowband.

Percy Panthaki: Okay and same for Europe I think this quarter the EBITDA margin has gone up to about 13%; again any one off so should we take this sort of within a narrowband 13% as a sort of manageable number going ahead?

Parag Shah: Percy, this nicely answers your earlier question. If you see my quarter two margins also the margin in the Europe were 13% plus so that answers a bit of your sustainability questions and as explained even earlier this is nothing but operating leverage you are aware we had invested earlier and this year our business has grown in terms of volumes and therefore clearly a case of operating leverage.

Percy Panthaki: I understood Sir clearly over the last two to three quarters you have been able to expand margins very visibly and now the margins are at 22% for the overall company and 13% for Europe, so do you think most of your margin expansion journey is done or would you believe that even on this base there is a margin expansion potential over the next one to two years.

Parag Shah: So this is a journey, ongoing journey and I already confirmed that it will move within a narrowband. There are many levers to it, there is revenue mix, there is productivity and cost optimization and it is a journey.

Percy Panthaki: That is all from me. I will come back in the queue if I have any further questions. Thank you.

Moderator: Thank you. We have next question from the line of Naushad Chaudhary from Systematix Shares & Stocks. Please go ahead.

Naushad Chaudhary: Congrats for a decent set of number and margin improvement Sir. Two, three questions I have. First if you can share what was the personal care revenue share in the current quarter, other question related to this segment only and on growth path I believe last year we had shared quite a bit about our EAP and America segment, we had some decent pipeline and we had acquired some new customers in America region, so what has happened to those things and when should we expect growth from our new initiatives in these two regions?

Parag Shah: To your earlier question the share was 43.6% personal care in Q3. Can you please repeat your second question?

Naushad Chaudhary: The follow-up one is, can you share the reason behind shrinking of this revenue share versus last year if I have the correct number it was around 44.5% and our overall revenue growth is quite flat, so there would have been a degrowth in personal care segment in this quarter, so any specific reason for this Sir?

Parag Shah: There is no degrowth I am not too sure from where you have got your information and I would sort of redirect to say that look at our growth nine months 14% year-on-year growth on personal care, this is a journey, to deliver a mission is a journey and we are confident of keep tracking to our mission. So

I would encourage that look at a longer term there is not a decline versus last quarter same period.

Naushad Chaudhary: For this quarter should we consider it flat, how should we look at it this quarter in a personal care segment Sir?

Parag Shah: I would recommend you see the nine months' picture that gives you a better picture of what is sustainable and what it will drive it going ahead.

Naushad Chaudhary: In our EAP and America region last quarter we had guided some good things about strong business pipeline and we had some new customers in our America region, so if we can throw some light more there and when they will convert into revenue?

M. R. Ramasamy: Americas region continue to do well and the pipelines, we will see the impact in Q4 going forward and structurally what happens in this business, as we explained in many calls that 1% here and there growth is depending upon the supply chain efficiencies, otherwise the traction on personal care growth will be visible in across regions.

Parag Shah: In case of EAP if you look at constant currency growth even in this quarter was 3.6% and the growth in personal care for nine months was 13%, so clearly this is evidence of the fact that the pipeline is playing out in terms of gaining share in personal care.

Naushad Chaudhary: Any specific number you are working with to have this personal care revenue share in next three to five years anything you have in mind?

Parag Shah: No. This is something that we will continue to work aggressively and expand all the time, but like I said earlier it is a journey and there is effort to be put in.

Naushad Chaudhary: Last question on capex side Sir any guidance for FY21 capex number Sir?

Parag Shah: No. There is not any guidance for FY21 capex number. I humbly just take you back to my mission, which is capital efficient consistent earnings growth, so when it comes to growth we will find ways and means to do prudent capital allocation and still grow.

Naushad Chaudhary: Thank you so much.

Moderator: Thank you. We have next question from the line of Arjun Sengar from Nippon Mutual Fund. Please go ahead.

Arjun Sengar: First question is on the competitive landscape if you can throw some light on that and our positioning within that landscape and the edge that we may have over the peers?

M.R. Ramasamy: As we explained in earlier calls what is needed to meet competitive positioning most of the investments have been done in the last year. That is the reason last year capex was higher in terms of zero defect, in terms of flexibility in printing, necessary capex, which has been done, so I think we being an industry leader in many regions we will continue to grow and you will see the traction going forward too.

Arjun Sengar: On this recyclability, is that a race, that peers are participating and in terms of products and all that stuff and how are we positioned in that race, are we ahead of competition?

M.R. Ramasamy: We are – our Platina laminate is under testing with most multinational brands, we already have first launch with our products in two brands in the region. I think as we said earlier people will catch up, but currently we are the lead supplier and most MNCs are testing our products already. Two launches have already happened.

Arjun Sengar: My last question is on this coronavirus situation, is that causing any disruption to us in terms of demand from China and our manufacturing over there if there is any?

M.R. Ramasamy: First of all let us take this slightly different. Employees are our first concern. I am happy to say most of our employees are safe and nobody is impacted by this so far and their families are safe that is very good news and we are continuing to monitor the situation there. There are two aspects to it, one the domestic market we are in continuous dialogues with our customers as well as business partners and we will continue to watch. We cannot predict anything, but we will continue to watch and where our supplies used to go from China to our other units, which has been completely protected by alternative arrangements we have done from India. So other regions are secured.

Arjun Sengar: What I understand is the supplies to other regions are secured, but the demand from local customers will be monitored is that what you are meaning?

M.R. Ramasamy: You are right absolutely.

Arjun Sengar: As of now there is no major dislocation as far as you see?

M.R. Ramasamy: No. See January business has been as usual. The current situation is same for me as well as my customers. We need to closely watch and see. We are in continuous dialogue, each one is working with each other to see how we will work on the situation.

Arjun Sengar: That is it from my side.

Moderator: Thank you Sir. We have the last question from the line of Mr. Varshit Shah from Emkay Global. Please go ahead.

Varshit Shah: Just wanted to ask you in terms of your sales pipeline going ahead where are you seeing more traction across geographies, is there an outlier in terms of growth especially the Europe and how is the America is doing in the sales pipeline?

M.R. Ramasamy: All the four quarters we are doing well in terms of pipeline maturity; as you know this business has its own lead time to get customer acquisitions so we work at least sixmonths' to one year in advance, so we see a very, very strong traction in developments.

Varshit Shah: Just a followup, structurally do you see that when you are building the sales pipeline probably for FY2021 are you offering with a higher value added products and trying to get more high value orders in terms of value addition, so is that traction coming in now since you have now host of offerings especially on the recyclable offerings?

M.R. Ramasamy: Yes personal care and recyclable offers are based on those factors.

Varshit Shah: That is it from my side.

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

M.R. Ramasamy: Thank you very much Varshit. Thank you very much everybody for your participation and asking questions. In case you have any followup questions then you could connect with Amit Jain and Parag Shah and they will be happy to answer. Thank you very much.

Moderator: Thank you very much Sir. Ladies and gentlemen, on behalf of Emkay Global Financial Services that concludes this conference call. Thank you for joining with us. You may now disconnect your lines.