"Indo Count Industries Limited Q3 & 9M FY20 Earnings Conference Call"

February 12, 2020

MANAGEMENT: MR. K.R.LALPURIA – EXECUTIVE DIRECTOR AND CEO, INDO COUNT INDUSTRIES LIMITED

Moderator: Ladies and Gentlemen, Good Day and welcome to the Indo Count Industries Limited Q3 FY20 Earnings Conference Call. This conference call may contain forward-looking statements about the company which are based on the beliefs, opinions and expectations of the company as on the date of this call. These statements are not the guarantees of future performance and involve risks and uncertainties that are difficult to predict. 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, please signal an operator by pressing '*' and then '0' on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. K.R.Lalpuria – Executive Director and CEO of Indo Count Industries Limited. Thank you and over to you, sir.

K.R.Lalpuria: Good Afternoon and a very warm welcome to everyone. Happy to connect with you all once again to discuss the Q3 FY20 performance. I hope everyone must have got a chance to look at the presentation and the press release by now.

Let me start with giving you some industry perspective and then move on our strategy. US retail sales registered growth for third straight month in December strengthening the view that the economy maintained a moderate growth pace at the end of 2019. On expected lines India continues to perform well in made-ups category.

I am happy to announce that we have clocked a volume growth of 21% for Q3 FY20 and 10% for 9M FY20. I am also happy to announce that we have recorded the best ever quarterly revenue of Rs. 637 crores registering a growth of 20%+. The growth was on account of market penetration through innovative products, modern designs and functional products. We continue to increase our utilization levels thereby increasing our revenues and market share.

With the focus on ensuring environmental sustainability, our company has joined Walmart's "Project Gigaton" to reduce greenhouse gas emissions resulting from manufacturing operations and supply chains. The company has been recognized "Giga-Guru" status for the contributions made towards environmental sustainability. The company has collaborated with CITI-CDRA to launch project Gagan, to improve sustainability in cotton farming for farmers in Maharashtra state. These initiatives will help farmers in increasing productivity of their farms along with judicious use of water, pesticides and fertilizers.

Now let me discuss on the exceptional item reported on a quarter:

The Ministry of Textile and the Ministry of Commerce, Government of India have issued notification dated January 14, 2020 and January 29, 2020 respectively withdrawing the benefits entitled under MEIS with retrospective effect from March 7th, 2019 on certain products exported in the past by the company. Without prejudice to the company's legal right as a matter of prudence, the company has written off an amount aggregating to Rs. 36.91

crores in Q3 and 9M FY20 towards amount accrued on the affected products for the period from March 7, 2019 to September 30th, 2019 and this is shown as an exceptional item. Further, the company has not accrued MEIS benefits of Rs. 19.34 crores for the quarter ended December 31,2019.

Now coming to the financial performance starting with the volumes:

For 9M FY20 volumes stood at 48.9 million meters as compared to 44.6 million meters in 9M FY19 a growth of 10%. We are on track to meet our volume guidance of 63 to 65 million meter for FY20. We strongly believe that Indian manufacturers are gaining a stronger foothold in the global home textile markets. Brands are very keen to create a credible supply chain and derisk themselves from the large supply exposure coming from a single geography. With integrated manufacturing base for textiles in India we believe we have a significant opportunity for sustainable growth in times to come.

Consolidated total income:

The consolidated total income for the company stood for Q3 FY20 at Rs. 637 crores as against Rs. 517 crores for Q3 FY19 registering a growth of 23%. The total income for Q3 FY20 does not include MEIS benefit of Rs. 19 crores. For 9M FY20 consolidated total income stood at Rs. 1,743 crores as against Rs. 1,503 crores in 9M FY19 registering a growth of 16% on a YoY basis.

Consolidated EBITDA:

Consolidated EBITDA for Q3 FY20 registered a growth of 176% and stood at Rs. 81 crores versus Rs. 30 crores for Q3 FY19. EBITDA margin was at 12.8% in Q3 FY20 versus 5.7% in Q3 FY19 registering a growth of 709 bps on YoY basis. We are pleased to inform that the company has reported an EBITDA of Rs. 235 crores for first 9M of the financial year surpassing the FY19 EBITDA of Rs. 166 crores even though we have not accrued MEIS benefits of Q3 amounting to Rs. 19 crores.

Consolidated EBITDA of 9M FY20 registered a growth of 56% and stood at Rs. 235 crores versus Rs. 151 crores for 9M FY19. EBITDA margin was at 13.5% in 9M FY20 versus 10% in 9M FY19 registering a growth of 348 bps on YoY basis.

PAT:

Q3 FY20 PAT stood at Rs. 20 crores as against 9 crores in Q3 FY19. Q3 FY20 PAT is derived after accounting for exceptional item of Rs. 36.91 crores on account of reversal of MEIS benefit earned from 7th March 2019 to 30th September 2019. 9M FY20 PAT stood at Rs. 65 crores as against Rs. 64 crores in 9M FY19 even after considering exceptional items totaling to

Rs. 131 crores pertaining to Rs. 37 crores reported in Q3 FY20 on account of reversal of MEIS benefit earned from 7th March 2019 to 30th September 2019 and Rs. 94 crores towards refund of excess export benefits of earlier years.

Net worth:

As on 31st December 2019, the net worth of the company crossed the milestone of Rs. 1,000 crores.

Net debt:

The net debt position of the company as of 31st December 2019 stands at Rs. 402 crores. The net debt-to-equity ratio is at 0.39x.

Further on the domestic business, we are focusing on this business and have recently strengthened our team and are taking appropriate steps to improve this business. Our long-term view is to see our own brand finding reasonable space in the domestic market.

That is all from my side. I now leave the floor open for the question and answer.

Moderator: Thank you very much. We will now begin the question and answer session. The first question is from the line of Vikram Suryawanshi from PhillipCapital. Please go ahead.

Vikram Suryawanshi: Sir, I just wanted your view on cotton pricing and what is happening in China currently, how that will impact in overall textile or home textile in particular?

K.R.Lalpuria: The Cotton Association of India has provided estimate earlier which is still maintained at 355 lakh bales. The crop is good, the supply is expected to meet the demand very well, cotton yarn and raw cotton exports to China are impacted due to coronavirus and enough cotton is available. So we believe that the cotton prices would remain stable unless the exports are happening to China once again. We expect that to remain in the range.

Vikram Suryawanshi: And what is current price of cotton?

K.R.Lalpuria: The current prices are around Rs. 41,000 a candy.

Vikram Suryawanshi: And compared to last year for us?

K.R.Lalpuria: Last year the prices were around Rs. 44,000 plus.

Vikram Suryawanshi: And sir was there any FOREX gain in this quarter compared to last quarter, so if you can give that because of the hedging policy how it has impacted this quarter compared to last quarter?

K.R.Lalpuria: Basically, we have in place a hedging policy to cover around 65% to 70% of our exposure. So, the rates realized this year are far much better than last year. In the last year we had realized around Rs. 68.50 / USD and this year we are realizing Rs. 71+ / USD. So, this year we expect on an annual basis a gain in the foreign exchange rather than a loss.

Vikram Suryawanshi: And the MEIS amount for last year also for every quarter would be in a range of 18 to 19 crores, is that right if you look at last year just at the MEIS amount?

K.R.Lalpuria: MEIS amount is derived as a percentage of value of exports. The MEIS benefit was to the tune of 4%.

Vikram Suryawanshi: And a last question sir if you look at it, though is not right way, but broadly what we see that along with the volume we also seem to be better pricing this quarter, so is it mainly because of revenue mix or how basically that is shaping up?

K.R.Lalpuria: This is mainly due to change in product mix. However, it should be seen at an annual basis since we supply both replenishment, promotion and all other types of products through different channels. So, you have to take into consideration our annual numbers to really understand the gain.

Vikram Suryawanshi: And is there any significant change in our share in fashion bedding and revenue from this value-added activity?

K.R.Lalpuria: So, we had reported earlier that the fashion, utility and institutional business is around 15% which we still maintain.

Vikram Suryawanshi: And how is growth in domestic retail expansion what we are basically looking at?

K.R.Lalpuria: We are focusing on the domestic business and we have just restructured our team and strengthened it. Going forward we have a five-year plan and we have already started promoting our brand in the domestic market.

Moderator: Thank you. The next question is from the line of Dipan Mehta from Elixir Equities. Please go ahead.

Dipan Mehta: My question is regarding the volatility in the EBITDA margins, so at some point of time in 2016 it was 32%, FY17 was 21% and for FY19 around 8.8% and turnover remain more or less the same, so can you explain that why there is so much fluctuation in the EBITDA margin and even quarter-on-quarter we see lot of fluctuation in the EBITDA margin, can you please explain why such volatility is there in margin structure?

K.R.Lalpuria: First of all, you have to see our EBITDA on an annualized basis because in between the quarters we are supplying to both the existing customer as well as new customers and new territories. So, you have to look at an annual basis Secondly, the structure of the incentives provided by the government keeps on changing and plus there are other moving averages like the raw material cost, forex rates and product mix. So, we have to consider everything and the geopolitical changes between different countries like Europe, UK and the developed nations also impact the business to certain extent. All these things put a pressure on the pricing as well as on the margins. That is the reason you see volatility is there, but the good thing is that the margins will improve going forward.

Dipan Mehta: And any guidance on what stable EBITDA margin one can expect from an annualized basis just to factor into our forecast?

K.R.Lalpuria: See we have already guided in our last concall that the EBITDA margins will be maintained around 12% to 14%.

Moderator: Thank you. The next question is from the line of Prerna Jhunjhunwala from B&K Securities. Please go ahead.

Prerna Jhunjhunwala: Sir, wanted to know the quantum of FOREX gain or loss in this quarter?

K.R.Lalpuria: As I mentioned earlier, the realizations are better from the last year because last year the exchange rates were quite volatile. Last year, realizations were around Rs. 68.50 / USD as against Rs. 71+ / USD this year. So, whatever the accounting part that impacts the FOREX gain are in the books.

Prerna Jhunjhunwala: Yes, I just wanted to know the quantum of it so that we can understand the quantum?

K.R.Lalpuria: This quarter the forex impact is negligible, like it is around Rs. 1 crore loss.

Prerna Jhunjhunwala: Sir, could you just explain us the factors that can help us go back to our earlier margins of 20% odd which is it possible and by when if at all we can foresee coming in one or two years timeframe?

K.R.Lalpuria: See we put a lot of effort into increasing our margins and we have given the guidance of 12% to 14% and I also explained there are so many moving averages like raw material prices, forex, geographical mix, and the geopolitical reasons and the relationship which the country enjoys with different countries like EU and UK. So, there are various factors in this, there is an always an endeavor to improve the margins by selling a better product mix. We have introduced different product categories like fashion branding utility and institutional in order to improve our margins. Our endeavor is to improve margins going forward. So there is always an endeavor to do that and we expect that the margins should come about 20% in the future so that is our endeavor. We strongly believe that we are well positioned, we have a good capacity in-house, we have State of the Art facilities, we are trying to utilize our capacities to the maximum, marginalizing the expenses and doing all sort of innovations and investing into R&D so that we can make some path breaking innovations in order to improve our margins, so that is what we are doing.

Prerna Jhunjhunwala: Sir, any outline that you can tell us about if there has been any major customer gain in the last 9 months or in any kind of product innovation that is leading to improve market share in the system which is sustainable over longer period of time?

K.R.Lalpuria: Customer gain is not the only reason for the volume or value increase. We have invested heavily in innovation and product development in the last few years and a lot of effort has been put in, which is now paying rich dividend.

Moderator: Thank you. The next question is from the line of Yogansh Jaswani from Mittal Analytics. Please go ahead.

Yogansh Jaswani: Sir, just wanted to understand on our revenue growth so like if we look at FY19 on a quarterly basis we were around at 15 million kind of a run rate which has now touching 17.5 million run rate, so can you just throw some light on what is driving this growth, have you added any new clients or have we sort of got more orders from the same client so just throw some more light on this growth?

K.R.Lalpuria: As I already explained, the efforts put in by the company in the last three, four years are generating good results. As we have already informed that we have put in efforts into promoting our fashion, utility and institutional bedding and that is really moving ahead in the right direction. We are also seeing that the business model which we are pursuing with our existing customer by providing them end-to-end solution is also helping us achieve better business. The customers whom we serve are also doing well so that also explains the increased volume and value and our endeavor is to keep the run rate much higher because we already have a capacity of 90 million meters to sell. So, we have a consistent growth plan and we have a good set of customers we are already well positioned in the market place from mid to high segment and we as a company are putting in a lot of effort into product development and innovations which also help us to differentiate in the product mix from our peers.

Yogansh Jaswani: So, the point I was trying to understand is I was trying to ask was is this growth more from the new customers that we added or from the old customers and going forward are these sustainable like even FY21 are we looking at maintaining this 17.5 kind of a quarterly run rate?

K.R.Lalpuria: It is mix of many factors, like the existing customer business also grows and we get in new customers as well. So, it is a mix of both and also new product categories as I explained because that also adds on new channel of business which we are attempting to drive on like supplying to regional customers, ecommerce, domestic business. So all round effort is being put into different channels of businesses and we expect that going forward as what already we have indicated a volume guidance of 63 to 65 million meter and we have already clocked in 48.9 mn metres and we are confident that we will achieve the sort of run rate what you are saying around 17.5+ million meters.

Yogansh Jaswani: So, it is safe to assume that we have clients like Amazon and Targets of the world?

K.R.Lalpuria: We supply to all these major clients as mentioned to you earlier, we in fact have a brand called 'Colour Sense' also.

Yogansh Jaswani: What will be the percentage of revenue that comes from Amazon sir of the total turnover?

K.R.Lalpuria: It is still negligible. In this business, the customers still pay a lot of importance to touch and feel. So, in home textile category particularly the ecommerce has not grown, you still make attempts. We have all the means on the backend to deliver the product with a pick and pack warehousing in Charlotte. So, we are making attempts to make really a good business for the company, but so far it is at a nascent stage.

Yogansh Jaswani: But this one will be the one your own brand sir and what about the business that we do for Amazon for their brand, just applying them without our brand, will that be also part of your turnover and is that a significant amount?

K.R.Lalpuria: So, we do supply both like our own brand and other brands, but we cannot disclose that which brands we supply because they have many brands across.

Yogansh Jaswani: Sir, secondly moving on the export incentive side so last quarter you had given us a breakup of duty drawback ROC and then MEIS, so now that MEIS is gone , can you again just share that breakup that going forward we will be…?

K.R.Lalpuria: See the drawback is 2.6% and the RoSCTL is 8.2%. So, totaling 10.8%, but the realization is around 10% because the RoSCTL is provided in the form of script which we sell it at a discount and secondly there are price caps in RoSCTL wherein when we ship higher value products, the incentive is limited as per the price cap. So, we lose on account of that. So, I think overall the government incentive should be in the range of 10% in the form of duty drawback and refund of central & state taxes.

Yogansh Jaswani: Sir is RoSCTL website working now are they accepting claims?

K.R.Lalpuria: So, the notification has come they are working on that and we feel that sooner or later they maybe by the next fortnight it should happen as what we have been told by the ministry as well as our associations and councils.

Yogansh Jaswani: Sir, if I go back and see the whole incentive scheme that was ruled out, so I think RoSCTL was a combination of ROSL and MEIS it is adding roughly 8.2% and during this period we were having 4% extra if MEIS which is now taken away. So, net-net if we speak about the one off that you are supposed to receive, which we did not get and so this 10% kind of incentive team is to be maintained.

K.R.Lalpuria: Yes, I think so. But MEIS and RoSCTL are two different schemes. MEIS was towards promotion of exports, and RoSCTL was refund of taxes and levies by Central and State when GST was implemented. The government promised to refund central levies. So RoSCTL was framed up and thus they are two different schemes.

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

Ankit Gupta: Sir, in your PPT it has been mentioned that US retail sales growth is around 5.5% and sir but our growth we have shown is 22% so sir is it a case that inventory with our customers have piled up or how we have grown such higher despite only 5% growth in the retail sales in the US?

K.R.Lalpuria: No, the numbers are for overall retail sales including all categories and all product range and different retail models. It is overall US retail sales number. So, we look upon like if the retail trade is growing, we get some share of it in home textile so that is why we gave this outlook that the retail looks positive and it is growing positively. It has nothing to do with our volume and value.

Ankit Gupta: And sir can you give me breakup of domestic sales and exports out of our volume sales?

K.R.Lalpuria: No, domestic sales are still negligible as what we have reported earlier that we had not focused on it, but as I informed you just recently, as a company we have reorganized our team, we have strengthened it with the right talent, we are focusing as a company on this and we have laid down a five year plan in order to promote this business in a structured way. So as and when it starts growing we will report to you again.

Ankit Gupta: Just one more question sir in the domestic market so are we looking to open our own stores or through MBOs and LFS we are attempting to sell?

K.R.Lalpuria: We are not into retail and not planning to do so going ahead. We are going to sell through distributors and LFS.

Moderator: Thank you. The next question is from the line of Rakesh More an Individual Investor. Please go ahead.

Rakesh More: Sir, just wanted to reconfirm you said that you will be meeting your guidance, so would you be meeting the upper end of the guidance of 65 million meter for the next year?

K.R.Lalpuria: We are quite positive and confident about it. We are on track to meet our guidance and our endeavor is always to meet the higher side of the number.

Rakesh More: And what would be the next year number?

K.R.Lalpuria: We shall provide with the next year guidance on our Q4 call.

Moderator: Thank you. The next question is from the line of Vikram Suryavanshi from PhillipCapital. Please go ahead.

Vikram Suryawanshi: Just to take update on this CAPEX how much CAPEX we did in this quarter or 9 months so far and is there any change in full year guidance?

K.R.Lalpuria: Till now, we have incurred a routine capex of Rs. 28 crores for the 9 months.

Vikram Suryawanshi: And full year would be how much is the expectation?

K.R.Lalpuria: For the full year, routine capital expenditure should be around Rs. 30 crores.

Vikram Suryawanshi: And any thought on this earlier plan of this during the expansion and all that?

K.R.Lalpuria: The government is coming out with a national textile policy, we have to wait and see what sort of benefits they provide and how the overall textile is being supported by the government which they have promised. So, we still need to believe that and then there is a new state government which is taking appropriate steps into deciding upon their industrial policy. So, combining these two, we will take a view.

Moderator: Thank you. The next question is from the line of Prerna Jhunjhunwala from B&K Securities. Please go ahead.

Prerna Jhunjhunwala: The cotton prices are lower by approximately 10% as we mentioned to some other participant in the call right now, but just wanted to check if the benefits of the same are being visible in third quarter also or will it be visible from fourth quarter any further?

K.R.Lalpuria: As we had mentioned earlier, the season has just started and we are sourcing new cotton for Q1FY21 and Q2 FY21 because we are already covered for this year and so we will be able to give better guidance in Q4 on how our material cost will pan out.

Moderator: Thank you. The next question is from the line of Suman Kawatra from Taxen Consultant. Please go ahead.

Suman Kawatra: I have just one question what percentage of total exports have been to China so far?

K.R.Lalpuria: None. **C**ouple of years back we had exported to Walmart China since we are a supplier to Walmart, but currently we do not have any exposure in exports to China.

Suman Kawatra: So, you do not expect any significant changes with this coronavirus problem?

K.R.Lalpuria: At the moment no, we are watching the situation closely and as and when we see some material impact we will come back and report.

Moderator: Thank you. The next question is from the line of Dipan Mehta from Elixir Equities. Please go ahead.

Dipan Mehta: Sir, can we have a geographical distribution of the revenue sir?

K.R.Lalpuria: We had already informed that 70% of our exports are to the US market and 30% to the rest of the world.

Dipan Mehta: And second question is regarding any new product launches we have made for our success story and are there other aspects of home textile which you pursuing and is that something which is viable for the company to get into?

K.R.Lalpuria: We keep on evaluating new product category being viable out of India and the Board will take appropriate decision as and when we find opportunity.

Moderator: Thank you very much. That was the last question in queue I would now like to hand the conference back to the management team for closing comments.

K.R.Lalpuria: At Indo Count we are expanding our footprint to newer geography and penetrating deeper within existing one. Our focus going forward continues towards increasing utilization levels and increasing our revenue and market share. Once again, I would like to reiterate our volume guidance of 63 to 65 million meter, and we are optimistic on the future performance of the company. With this, I would like to thank everyone for joining the call. I hope we have been able to address all your queries for any further information kindly get in touch with me or Strategic Growth Advisors, our Investor Relation advisors. Thank you.

Moderator: Thank you very much. On behalf of Indo Count Industries that concludes this conference. Thank you all for joining us ladies and gentlemen, you may now disconnect your lines.