



“Century Plyboards Q2 FY17 Earnings Conference Call”

November 04, 2016



MANAGEMENT: **MR. SAJJAN BHAJANKA – CHAIRMAN, CENTURY PLYBOARDS (INDIA) LIMITED**
MR. ARUN KUMAR JULASARIA – CHIEF FINANCIAL OFFICER, CENTURY PLYBOARDS (INDIA) LIMITED
MR. KESHAV BHAJANKA – EXECUTIVE DIRECTOR, CENTURY PLYBOARDS (INDIA) LIMITED

MODERATOR: **MR. ACHINT BHAGAT – AMBIT CAPITAL**



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Moderator: Ladies and Gentlemen, Good Day and welcome to the Century Plyboards Q2 FY17 Earnings Conference Call, hosted by Ambit Capital. 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 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. Achint Bhagat from Ambit Capital. Thank you and over to you, sir.

Achint Bhagat: Good afternoon, Ladies and Gentlemen. Welcome to the 2Q FY17 Conference Call of Century Plyboards. We have with us here today the Chairman – Mr. Keshav Bhajanka who is Executive Director and Mr. Arun Julasaria who is the CFO of the company to take you through the performance of this current quarter.

So, I will ask the management for their initial remarks and then Chorus Call will open up the floor for questions. So, over to you gentlemen.

Sajjan Bhajanka: I welcome you all to this con-call. Now I would request Mr. Julasaria to go through the statutory disclaimer.

Arun Julasaria: Good afternoon, Ladies and Gentlemen. It is nice to speak to you again. I welcome you at this Q2 conference call of Century Ply. Before I go ahead, I would like to state the purpose of this call is to discuss company's historical numbers and future outlook. It should in no way be construed as an invitation to invest in the company. Our Chairman – Shri. Sajjan Bhajanka and our Director – Mr. Keshav Bhajanka are also on the call to take your qualitative questions. The financial results and analytical presentation is already circulated to you. I will only summarily speak about financial results.

Year-on-year net revenue has gone up by 5.5% to Rs. 462 crores. Quarter-on-quarter net revenue has gone up by almost 14% to Rs. 462 crores. On six months' basis, net revenue has gone up by almost 7.5% to Rs. 868 crores. While, overall EBITDA margins have been maintained at more or less same level with slight adverse variation, the EBITDA margin in case of plywood segment has been affected more and EBITDA margins of laminate segment improved. During the quarter, we have almost slowed our furniture division, so losses in other segments are terminal losses. EBITDA margins in plywood are on lower side, mainly because of lower average realisation in face veneer which was on peak last year. In laminates, capacity utilisation has further improved and has gone up at almost 100%. The value of laminates has gone up substantially, we have used operational leverage for improving both topline and bottomline.

Now, I request our Chairman sir to address the conference.



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Sajjan Bhajanka:

Ladies and Gentlemen, I again welcome you all to this conference. I admit that this quarter also we are missing the historic 20% growth because the real-estate market is sluggish and many of our peers are struggling to even keep their figures. But that way I am happy that still we could manage some growth in the earnings, in net profit, even in the turnover. And during this period we kept on investing in future. So, like our particle board we have already reached 80% of the production capacity. And last month we have almost sold what we have manufactured in the last month. But during the previous month where we did not start marketing, so that is carried forward but we are very hopeful that next month we will dilute all the inventory of finished products. And at the same time we will keep on growing. And our people are confident that in the next two months, during the next quarter we shall reach 90% of the capacity and thereafter we shall operate at 100% capacity in particle board division. And what is heartening is that almost 50% of our raw material is available in house. The wastage from our plywood division is meeting the 50% raw material required, another 50% wood we are buying and that also we could source at price below our expectation. So we are getting timber now at Rs. 2,200 a tonne for our requirement. This is below our earlier projection.

And MDF, yes the construction is going on in full swing and the original projection was July next year, we have already revised that, I informed you last time. So we are 100% sure that within March we will commission the MDF plant. And again, there the price of raw material has further come down and now timber is available in the vicinity of Rs. 2 a kg in North India. So that is a good indication and MDF demand is there. Still India is importing huge quantity of MDF despite there is anti-dumping duty, it is regularly being imported. So, as soon as we are commissioned we will meet a lot of demand and particularly North India we shall insulate from imports. And other way is okay, we are geared up for the increased demand expected on the promise of GST being applicable from 1st April, which seems to be a reality now. And maybe we can have some questions from you in the light of recent development on GST, so I will take up all the questions as and when they come.

So, now we open house to all of you for your queries.

Moderator:

Sure. Thank you very much. We will now begin the question-and-answer session. We have the first question from the line of Basudev Banerjee from Antique Finance. Please go ahead.

Basudev Banerjee:

A few routine questions. Your overall ply volume was down year on year, so within that how much was Sainik and how much was non-Sainik? And if you can segregate revenue between Sainik and non-Sainik.

Sajjan Bhajanka:

No, overall it was never down. Yes, we had happy growth and this quarter also we are maintaining it. And quarter on quarter this is 13-14% up, but previous year, yes, it is only around 2% up. So, this is there and here there is a reason that we are not tampering with the price, although there is some recession in the market but we are maintaining our price line. It has been our past experience that if we reduce the price then it is very difficult to recover it. So



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we are maintaining our price line. Whereas some of our peers they have reduced price, so they have attracted some additional sales but it is at a huge cost of probability that we have avoided.

- Basudev Banerjee:** Sir, out of 51,000 CBM how much was selling?
- Sajjan Bhajanka:** I beg your pardon?
- Basudev Banerjee:** Out of the reported number which you have given in the presentation, 51,067, how much was CBM Sainik?
- Sajjan Bhajanka:** Sainik is near about 13,400.
- Basudev Banerjee:** And sir, Sainik's revenue?
- Arun Julasaria:** Sainik's revenue is Rs. 45.73 crores.
- Basudev Banerjee:** And sir, what is your outlook for the overall growth per say, like the kind of sluggishness which is there as of now, as you rightly said the real-estate part, so when do you see any element of uptick and why? Anything on that line sir.
- Keshav Bhajanka:** See, while demand has not been very good this quarter and while we have not grown much this quarter, the reasons as we stated earlier that last year the particular quarter had been very good, this was due to the fact that October of last year we had taken a price increase in plywood and due to the same there was a huge amount of inventory pileup that took place with dealers. Because of the same you will notice Q3 of last year was not very good in particular. This year there has been no price increase, in fact the prices of raw materials have remained constant. And going forward we believe that quarter three should be much higher in terms of growth outlook, I think we should be looking at double-digit growth figures for the company as a whole in this quarter.
- Basudev Banerjee:** And sir, if I see your commercial veneer realisation seems to be on the lower side, any specific reason behind that?
- Sajjan Bhajanka:** Yes, in comparison to last year there is a lot of capacity addition in Myanmar also, then this is a paucity of traditional veneer which is being used by the Indian market manufacturers in India. There are some other expenses which have entered the market like some expenses from Africa and this thing entered the market, then Solomon Island, from there CQ and CL there are two varieties, they have entered the market. There is a cumulative effect because the supply is more. So there is some reduction in price of veneer. This is one thing. And at the same time, because there are many units in Myanmar, so even the timber price has increased. Both the ways revenue is a little down and the profitability is little down. Veneer, yes earlier in the past it was a big contributor to our profitability by way of reduced raw material cost. This year the selling

price of veneer is under stress due to the reason I have explained. And maybe the things will stabilise at the present level.

Basudev Banerjee: So one should look forward to present level of realisation as a sustainable level down the line?

Sajjan Bhajanka: Yes, well there are plus and minus over it because due to this change many units in Myanmar substantially reduced their production and some of them closed it down. And in India, almost other than Century most of the people have stopped manufacturing veneer. So, again, maybe in future balancing factor would be there by reduced production in the country and again, from Myanmar. Elasticity of demand and supply always plays important role, but we are intact, our capacity at Myanmar is intact, in India we are importing Solomon timber and in three of our factories we have decided to stop veneer at Calcutta and Chennai factory, except for our own use. And Kandla and Karnal, these two factories because the landed cost of Solomon timber is lowest at the Kandla port and Kandla port is a filling port for Karnal and Kandla units. Both the units are near to the market. North India is a major market for veneer. So that way we have adjusted our strategy and wherever the operations are profitable we are continuing. Like Calcutta and Chennai, **are not for veneer point of view in India**, are not very profitable, so we have decided to reduce production at these two points, other than our captive production.

Basudev Banerjee: Last thing, what is the updated view on the capex for the year, including maintenance and MDF plant?

Sajjan Bhajanka: In the coming financial year we will be adding two more laminate lines, so whatever we informed in the last call, there is addition of near about Rs. 45 crore on account of two laminate lines. Then in 2016 – 2017, we have already incurred Rs. 156 crore capex, Rs. 221 crore more we will incur this year and estimated in 2017 - 2018 is near about Rs. 100 crore and in 2018 - 2019 it is near about Rs. 40 crore.

Basudev Banerjee: So this year close to Rs. 280-odd crore?

Sajjan Bhajanka: Rs. 222 crore more.

Arun Julasaria: But we have to complete the MDF plant, so the projection was around Rs. 390 crore. Now the projections have come down because we have reduced the implementation time. And again, we have made some savings on shipping freight and some saving on duty. We have got a special licence from DIPP which reduces our duty implication from 7.5% to 5%. We could save around 2.5% in duty on the import of machinery. These all factors are likely to reduce and there was a contingent factor, so that also now not seems to be applicable. So with these all things I think we shall be able to reduce the cost by 10% of the project.

Moderator: Thank you. We have the next question from the line of Anshuman Atri from Haitong Securities. Please go ahead.



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Anshuman Atri: Sir, my question is regarding the MDF. As you are putting up a new plant and you are seeing sustained imports despite hike in duty, so what are other measures you are proposing to the government to ensure that the quantum of import goes down and how are you going to target different markets given the MDF would be largely catering to the coastal markets?

Sajjan Bhajanka: Yes, the nearest importing port is Calcutta on the eastern side and Kandla on the western side and then all those southern ports. So, South India is mostly fed by the imports and then the Central India is a mixture, the material comes from Northern India, indigenous production and the remaining quantity is being imported. When we shall be commissioning our production, then this territory would expand, so the import for Central India would reduce. And it will be met by us and then the additional demand of North India again we will take care. The demand is growing, demand for MDF is growing because there are many applications where MDF is not being used now, like for decorative veneer. So instead of plywood decorative veneered, MDF can be used. Like for the beds 6x3 there we can use, for photo frames and for many uses. When it is available in all the thickness then it will be used in big quantity and like OEMs for readymade furniture, for pre-laminated factories, so they are already using, their number would increase.

Anshuman Atri: Second question is regarding the quality difference between the imported one and the ones you will be manufacturing, I presume you will be manufacturing a better quality MDF as compared to imports. So will it help in terms of substitution?

Sajjan Bhajanka: In this quality is a management decision, so anybody can make better quantity, better quality and in Century it's management's decision. Better quality means more expenses, you have to give higher density, you have to give little more glue, you have to do better finishing and sanding. As far as we are concerned, like all the finishing plants we have taken from Europe and even this plant, the country press and country line is like more accepted production tool in this industry. And particularly our supplier, he has already more than 25 country lines operating in China and all have very good results, our people they have seen the quality. So, obviously keeping in pace with the Century we still make the best quality. Our particle board quality has been accepted by market better than any other indigenous outside producer. So basically we have to give better glue, we have to give better density, so we have to give more pressure, so that we can do, it is management's decision only. And we shall never compromise on quality.

Anshuman Atri: In terms of capacity absorption, given that new capacity is coming by other peers also, do you expect it could be absorbed in the next couple of years, yours as well as that of peers?

Sajjan Bhajanka: It should, I am expecting that in another five years India shall be producing five times of the MDF in comparison to the present capacity and entire thing would be sold in the indigenous market. In past, like in Turkey, in China, once MDF started then the growth is phenomenal. Until 2013-2014 India was consuming only 200 cubic meter or having 200 cubic meter indigenous capacity and then in 2012-2013, 2013-2014 we added more than 1200 cubic meter



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capacity and everything was sold. So, this appetite of the market would also increase with availability of indigenous material.

Moderator: Thank you. We have the next question from the line of Gunjan Prithyani from JP Morgan. Please go ahead.

Gunjan Prithyani: I just wanted to understand the growth a little bit more, because if I look at the plywood segment there seems to be a realisation increase of almost 9% YoY and the volume decline has been fairly sharp versus what the competitor reported. So, I just cannot tie this up, I mean I understand you tried to maintain the prices but what has lead to this 9% increase in realisation?

Keshav Bhajanka: So, last year we took a price increase in Q3 and post that we have not had any substantial discounts, any reductions in price till date. So I think that carried forward is a very hefty increase in realisation for plywood. Whereas in terms of volume, like I told you last year the base effect took place.

Gunjan Prithyani: Sir, when were the realisation increases taken?

Keshav Bhajanka: The first increase was taken in Q3 and the second increase was taken in Q4.

Gunjan Prithyani: Okay, last year second half basically?

Keshav Bhajanka: So, I think when you compare realizations Q3 to Q3 you will see a much more stable figure.

Gunjan Prithyani: You basically did not discount in the market but you think that others did discount and hence the volume growth for the competitor has been higher?

Keshav Bhajanka: Definitely, I believe that is also substantiated by our margins. If you look at our EBITDA margins, I believe plywood we will be higher than the rest of the competition by quite a distance.

Gunjan Prithyani: And what is our strategy, of course the demand environment per say remains still fairly subdued, so we are okay to lose market share and stay and stick on with the prices here?

Keshav Bhajanka: I do not think we are losing a great deal of market share, I think that in quarter three and quarter four you will see a good growth on our behalf. I cannot speak about competition but I believe that we should be **there or there about** in terms of growth. So, I do not think we are going to lose market share, but yes we will be maintaining our market share and our prices and not at discounted rate.

Gunjan Prithyani: And secondly on the face veneer, I am just struggling a bit because this segment has been very volatile in terms of sometimes realisation, sometimes volumes. So if you could just give me a

sense how should we look at the volume here, I mean the value that we should be selling on an annual basis in this segment and the margins we should be looking at because this has been extremely volatile.

Keshav Bhajanka:

In terms of realisations, face veneer is a commodity product and it is driven by market standards. So, as per rates, if the market rates increase or decrease our realisations will vary. In India, currently the type of timber that is being used for face veneer is different, earlier it was purely Gurjan, now other species are coming into the market. These other species are cheaper variant. So going forward I think you can take today's rate as more or less constant in the market or more or less the market standard going forward. But once in the next or two there is a correction and as the Chairman was saying, once these units start closing I think realisations should pick up next year.

Sajjan Bhajanka:

I would like to add one more thing. Like the total number of face veneer required by the industry would be more or less constant in short period of time. And now Gurjan is the costliest face veneer and it's being replaced by certain veneers like Acume which is now being sold at almost 50-55% price. The Solomon timber, again it is 55-60% price of this. So, total value-wise it is coming down our realisations. But now we save more money in Acume or in Solomon timber than in Gurjan timber. So their profitability is being maintained. Maybe the volume is more or less constant, the price has come down but not all profitability. So that one factor is there. What we need is the bottom-line, the profits should be intact. If suppose we produce more Gurjan we sell at a higher price but we do not earn money, so that does not make sense.

Gunjan Prithyani:

The value growth that we have done in 1H, is this something that should continue and I should annualise this or it will come down from these levels?

Sajjan Bhajanka:

I will explain it in other way. We have two source for supplying veneer, one is our overseas unit, Myanmar and Laos, and another is our domestic unit. In domestic unit, we have 100% shifted to lower cost timber that is like the landed cost, which earlier used to be around \$600 for Gurjan timber into India and now we are using Acume or Solomon timber which is available at 50% of the price and whereas like veneer we sell at 60% of the price. So we are maintaining our margin, or rather increasing it, but yes value-wise it has come down. From Myanmar we are selling. From Myanmar and Laos we are using only Gurjan timber at the same price, at same this thing we are selling to niche customers who want to use only Gurjan. And we are using only Gurjan in our own production.

Gunjan Prithyani:

Sir just on the laminate segment, anything specific that lead to such a huge growth in this quarter?

Sajjan Bhajanka:

Yes, the person responsible for that and who was instrument in achieving that is Keshav, so I think I will give Keshav to explain it.



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- Keshav Bhajanka:** When you see laminates historically we have a low base, and we differentiated our positioning in the past two, three years. We have established ourselves as a design leader and I think this is giving us huge dividend. If you look at the previous quarter, we had launched our catalogue, the look book which is our most successful catalogue till date. It is India's first digitally smart catalogue and this is a really differentiator item in the market. So I think this year we can look at a sustained high growth for laminate. For next year we already are meeting our strategy to best take benefit of GST and I think we should be able to grow at the same or maybe even at a slightly higher rate.
- Gunjan Prithyani:** Congratulations for this achievement, it is really a commendable growth in that segment. All I want to understand is that are we the price leaders now in this or are we still at the discount to be number one?
- Keshav Bhajanka:** We are the price leaders in the market, we have been the price leaders in the market for the past year and a half and we are further strengthening our position. If you look at our realisations in 1mm we are the highest in the country. If you look at our realisations in terms of exports, we are the highest in the country. So I think we have firmly established ourselves as highest priced laminate or the market leader. The ratio of 1mm in our total production capacity domestically is the highest, 90% of our total volumes in India are from the 1mm segment. In line with this, we have decided to expand the capacity by 50%, you should see the first half of the expansion come into play by August next year. So hopefully by then we will be geared up to increase our sales.
- Gunjan Prithyani:** What capacity utilisation are we operating at currently?
- Keshav Bhajanka:** Currently we are at 100%, but through certain initiatives we are able to take our capacity up to 120%. So I think by the time the next line comes in, we will be operating at close to 120% capacity utilisation.
- Gunjan Prithyani:** So you are doing capacity growth of around 50% here which will come on stream in next one year?
- Keshav Bhajanka:** 25% will come on stream in August next year and the balance 25% in January 2018.
- Gunjan Prithyani:** Just last question, what lead to the realisation decline in the segment?
- Keshav Bhajanka:** The realisation decline was primarily due to the increase in the percentage of exports that took place in this quarter, I do not think that will sustain. I think going forward we are going to see high realisation.
- Gunjan Prithyani:** Domestic was also down, about 11%, I think it probably has to do with base...



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- Keshav Bhajanka:** No, the domestic realisation being down could be as a result of the pre-lam division which is reported to that.
- Moderator:** Thank you. We have the next question from the line of Anand Bhavnani from Sameeksha Capital. Please go ahead.
- Anand Bhavnani:** I wanted to understand the MDF market a bit more. So, if you could just give me the numbers of the present capacity in India and the overall market size and how exactly this dynamic will change over the next two years?
- Keshav Bhajanka:** We currently predict the MDF market to be at about Rs. 2,000 crore per annum. And according to us, the market size is close to 10 lakh cubic meters and it is growing by 15% to 20% per annum.
- Anand Bhavnani:** So it is 10 lakh cubic meters as of today for MDF?
- Keshav Bhajanka:** Yes.
- Anand Bhavnani:** Out of this 10 lakh cubic meter what percentage is imported?
- Keshav Bhajanka:** Close to 40%.
- Anand Bhavnani:** So 6 lakh cubic meter is domestically produced?
- Keshav Bhajanka:** Yes, combination of all the domestic manufacturers.
- Anand Bhavnani:** And all of the 6 lakh cubic meter, the capacity is running at 100%, is it?
- Keshav Bhajanka:** I do not think the total capacity is running at 100%, I think that quite a few plants are running at 100%, Green is running at +100%, Action is running at +100%, but some of the smaller manufacturers...
- Sajjan Bhajanka:** Russell is also running at +100%.
- Keshav Bhajanka:** Some of the smaller such as Shirdi, etc., could be running at maybe 60-70% capacity utilisation, but their volumes are negligible.
- Anand Bhavnani:** So, since our plant is coming up I think a year from now, in Q2 next year, so which other manufacturer would be having their plant up and running before us or immediately after us?
- Keshav Bhajanka:** No, I think you got that slightly wrong. As the Chairman had said earlier, our plant will start manufacturing in Q4 of current financial year.



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- Anand Bhavnani:** So are we expecting any other plant to start production before that or maybe after in the next year or so?
- Sajjan Bhajanka:** As far as MDF is concerned, I foresee that there would be huge growth in MDF, from the lower segment, from low income group, the mass housing and other things, so most of the furniture will be made of MDF and particle board. And the margin in particle board, like buying same timber, same thing manufacturing in particle board, so it does not give that much profit, unless you have some wastage in-house or you use it. So that's why MDF is more profitable. And I think future growth will come mostly in MDF. And MDF, again it needs less levers because lever is gradually becoming costly in India, though country press and other things are not labour intensive. So in Turkey, say 13 years or 14 years ago first MDF plant was setup, and then within no time or maybe in six, seven years they had 25 MDF plants. In China now more than 240 MDF plants are operating. And again, the first plant might have come maybe around 20 years ago. So the thing is, when MDF comes it is a good product and it is very competitive, like price is costing domestically after all the duty and this thing it is \$800 plus, whereas MDF is available below \$400 plus, including delivery to the customer. So, price is almost half. And particle board, it is almost one-third.
- Anand Bhavnani:** So just to understand, what would be the size of MDF market in China, because India and China in terms of population number are similar, maybe let's say if you are 10 years behind them or five years behind them, what is the current size of MDF market in China in terms of cubic meters?
- Keshav Bhajanka:** We do not have exact details or exact figures, what estimates say is that the Chinese market is close to 50 million cubic meters. I mean, we do not have exact figure but as on date China is the largest manufacturer of MDF in the world, more than America, more than any other country. So it should be huge, we do not have exact figure but maybe you can go to Google or internet, you will get it. But, like out of these 240 or so plants, many of them are 1,000 cubic meter plus. So that way it is minimum 40-50 times of India. So this 50 is underestimate, 50 million is under estimate.
- Anand Bhavnani:** Sir, I think apart from us maybe Action is coming up with capacity in the near future?
- Sajjan Bhajanka:** Action is also planning, then Green they have just started work, so Green's plant is coming in South India.
- Anand Bhavnani:** I think, according to the publicly available sources I think Action is coming up in Q2 next year, around one year from now and we are coming up six months from now?
- Sajjan Bhajanka:** Green may be one year or one and half year.
- Anand Bhavnani:** So we would not have price competition maybe say until Action comes in and initiate capacity?



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Sajjan Bhajanka:

I think they have just taken decision, so it will take minimum one year plus, if they can also establish as fast as we are establishing. But there is no reason that they would not be able to do it because they are already in this line, they are putting up the plant at the same venue, in the same area, so it will facilitate more and it will make it faster. But I do not see there would be any demand problem because this readymade furniture market is increasing. Over the period, like with Wall-Mart, with other people they are entering the market and IKEA, so their all furniture are based on MDF and particle board. They do not use plywood, they do not use anything. So one of these manufacturer would consume the whole production of one plant. We are planning doors in big way and big portion of that would be our own production which would be used for doors. We are also planning flooring, so a part of that of our own production would be used for flooring. So that will replace the imports.

Anand Bhavnani:

Sir, just about our plant, there was some news in the media round 24th October - 25th October that there is agitation by farmers for the chemical unit which is coming up along with our MDF plant, can you throw some light on that?

Sajjan Bhajanka:

I will explain. Usually, all the plants either we have to make our own glue or we have to buy glue from outside. So far most of the plants are buying glue from outside. We thought, with GST and other things, formalin is a major component of glue. Till today none of the plywood factories or MDF or particle board factories have their own formalin plant but wanted to establish formalin plant at this site only. We have applied for the environment clearance and we are expecting that it should be through but somehow the people like villagers and others are very sensitive about the chemical and other things, and somehow there was opposition to this. So for time being we are dropping that plan of making formalin here. And like glue caters and others, that is general part of the plant. So, all the factories in India, all the ply factories and other things, they are mixing the resin imported or brought from outside with extender and they are using in the factory. There would be no problem. The only thing is manufacturing our own formalin and the glue. Now we have to buy or establish it at some chemical zone, either in Punjab or nearby. There we do not need environmental clearance, because the clearance has been taken by the chemical zone itself and there we can buy the land and start the plant. Most of the plants are in chemical zones only, like near Chandigarh there is one chemical zone, so many plants are there. Even some plants are **(Inaudible) 41:08.2 also**. From that to our plant maybe around 150 kilometers and all the materials would be imported at Kandla port like methanol or other things, raw material for formalin or even phenol, it is not manufactured in India. Only very small quantity is manufactured by HOC, but about 80% is imported. So that imports are taking at Kandla port. Otherwise also at Kandla port we already have plant, for our Kandla plywood factory again there we had the same problem. We did not get permission along with the plywood factory, so there we have established **plant at chemical zone, industrial zone at Kandla**. So we have a plant, now that is feeding our Kandla factory and from the same factory we can make glue and bring to Hoshiarpur.



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- Moderator:** Thank you. We have the next question from the line of Nehal Shah from ICICI Securities. Please go ahead.
- Nehal Shah:** Sir, a couple of things on the particle board and the MDF side. Now on the particle board side our turnover for this quarter was Rs. 2 crore and we did EBITDA of Rs. 1.5 crore, so the EBITDA margin would be around 70- 75%?
- Sajjan Bhajanka:** No, it cannot be. Maybe some mistake is there, EBITDA margin cannot be 75%.
- Nehal Shah:** And second thing, it is really commendable to see on a sale of minimal crores in MDF you are still doing 19% even while we are trading in MDF?
- Sajjan Bhajanka:** Yes.
- Nehal Shah:** So what are your targets as far as the new capacity, when it comes in what is your target as far as your margins are concerned there?
- Sajjan Bhajanka:** First would be to sell the entire production. So we like to optimise our plant at the earliest possible, first thing, like we could do for particle board. We have almost crossed 80% capacity and within this quarter we are selling close to 90% capacity and maybe in final quarter with 100% capacity. So similarly, MDF being the country press, once we start the plant generally we like to keep it running. And if we have not to stop it then it will give optimum capacity. So the challenge would be to sell that material. So we shall cross the bridge when we reach it, we will use all the raw materials to reach full capacity. And for that bottleneck would be filled. So initially we may struggle because we are still new entrant into that market, but if we are able to sell 100% in Central India or North India or Western India, Northwest India or Northeast India, so that will be more profitable. Then the alternative would be import which has to be nearest to Calcutta port or the Kandla port. So, that way we will incur additional cost. And like for us to go to beyond Central India to Southern India would definitely be not be possible because we have to incur more transportation cost and we have to reduce the price in competition to the imports.
- Nehal Shah:** But sir, what kind of internal targets are you setting in for your MDF in terms of margins? Any number you would want to achieve once your plant starts kicking?
- Keshav Bhajanka:** Nehal, we are looking at 30% plus EBITDA margin once we reach 80% capacity utilisation.
- Nehal Shah:** And what be your breakeven level?
- Keshav Bhajanka:** Breakeven level would be 50% plus.

- Sajjan Bhajanka:** It is going to be lower than that, but we have to operate the plant at 50% plus because that is the minimum, below that it cannot sustain.
- Nehal Shah:** In the first year of operation you mean?
- Keshav Bhajanka:** Yes, it will start with minimum 50% and then once it starts it will run at same capacity. Then if we are not able to sell or if there are breakdown then production may be less, if there are no breakdown then we have to stop the plant, if there is accumulation of finished material and we are not able to sell it then we have to stop it. **Other manufacturers they did not because** it took some time for them to reach 100% capacity and now almost everybody is running at 100% capacity, or rather more than 100%.
- Nehal Shah:** And sir, have we also accounted teething problems, generally what we have seen in case of a lot of manufacturers, there are lot of teething problems, the quality takes lot of time to stabilise, so are we confident that from the first quarter itself we will be closer to stabilise our capacity and kickstart with the sales volumes?
- Sajjan Bhajanka:** Like particle board we took all precaution that quality is stable, production is stable and in particle board we were successful. And here for the MDF plant, because our supplier is from China, although he is very successful in China but that is a challenge for him because if we are successful with smooth starting and without much of teething problem, so it will bring a very good name to him. So he has already sent many people at this construction stage and he has promised us that he will fully support for first three months, his entire manufacturing team will come because he has supplied to many plants and he himself has an MDF plant in China. So he will depute his people and he will train our people and his experience has been good in China. His plants are generally trouble free.
- Nehal Shah:** So you do not see much of a teething problem coming in?
- Sajjan Bhajanka:** Some problem would be there, some problem was there with MDF, some of the parts they are not giving away, we had to redo it. So, some teething problem would be there. Say, we sell commission to the plant within March this year and first quarter let us presume that it would be little troublesome but by the end of the first quarter definitely we should reach more than 60% capacity.
- Nehal Shah:** So, effectively we should take into account that the production should start near about by June, July effectively?
- Sajjan Bhajanka:** The production would start from April and the first quarter itself will reach minimum 60% capacity utilisation and thereafter it will keep on increasing.



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- Nehal Shah:** And sir my last question is, in terms of guidance what are we looking at in plywood and laminates, the growth?
- Keshav Bhajanka:** Nehal, overall for the company I think we are looking at 10% plus growth for the year, we are going to look at double-digit figures. In plywood there will be single-digit growth whereas in laminates we will be looking at higher growth.
- Nehal Shah:** And in terms of margins for the overall company?
- Keshav Bhajanka:** I think currently the margins that we are operating at are good.
- Nehal Shah:** Yes, they are 16.5%.
- Keshav Bhajanka:** And I think we should be able to sustain these margins for the rest of the year.
- Moderator:** Thank you. Our next question is from the line of Ajit Motwani from Bharti Axa Life Insurance. Please go ahead.
- Sajjan Bhajanka:** Earlier you were one of the chief analyst for Century, one of the initial people who started covering century, so I think you are most knowledgeable about Century.
- Ajit Motwani:** Thanks for the compliment, sir. Just a few queries on MDF. So, when I was looking at Greenply's first unit when they commissioned, it took them about three years to reach about 80% utilisation and about 20% margins. I just wanted to understand your confidence on the fact that you will be able to reach 80% in less say about a year's time and this 10% margin differential between them and your plant?
- Sajjan Bhajanka:** I would like to thank Greenply for many reasons. One is that they took the trouble to educate the people about MDF and they faced a lot of problem. They made certain mistakes too, but those are known to us. First thing, MDF plant machines are very sensitive, the country press, so there had to be a very good supply of power. In their case, they took from the normal grid and had lot of power problem. And we are aware of this, so we have dedicated line around from 4-5 kilometers from major service stations in Punjab where they have high Kv line, need to be taken from there. So the Punjab Government has assured us uninterrupted power. That would be one thing. And then the second thing is, like prior to them when they started production, there was only 200 cubic meter capacity, Manglam and new plant, and both of them by debtors were struggling, both of them were referred to BIFR as they eroded their net worth, so they were referred to BIFR. That was the scenario and so I would like to compliment them that these people could not sell 200 cubic meter of MDF for 18 years and then Greenply came and worked, and along with them Bajaj came, along with them Action came, along with them this Shirdi came and all of a sudden more than 1200 cubic meter capacity was added. There was a period they were selling everything which they could manufacture. Apart from that, import was

growing at 50%. So, there was a change, because now I can conclude that Newchem or Manglam they were ahead of time, there was no forward integration, no furniture industry was existing in India, there were no OEMs to consume their materials. But now the situation is different. And it will grow, this is not the end of the capacity. Maybe after five years I shall be talking with you that we are putting two more MDF plants in eastern India, maybe one in southern India. There are now other raw materials suitable for MDF, even we can make MDF from bamboo.

Ajit Motwani: In terms of, one is this power line, any other competitive advantage that you have against let's say plywood or MDF unit that is there in south?

Sajjan Bhajanka: South is a very big market, south is a manufacturing base for furniture, there are a lot of readymade furniture business in south. So, south yes, because north again, imported MDF is not cost effective, so most of the furniture unit came in south. But now furniture units are growing in north. And in north another thing is that MDF is being used as a replacement of plywood in the domestic use for sealing, for partition, for wardrobe. People making furniture, they have started using MDF as a replacement of plywood at a 50% cost.

Ajit Motwani: One last question, if I were to import MDF from Vietnam or any other Chinese market to India and from there to north, so what would be the landed cost there and how much our costing or pricing will be cheaper than them?

Sajjan Bhajanka: Now import price is like \$260, (\$+/-10). And if it is being imported from Vietnam or Thailand being FTA countries, being Asian countries, there is no import duty. So the only thing is anti-dumping duty which varies from \$0 to \$50 for different countries, like China it is around \$50, Vietnam it is \$0 and two, three companies it is 15%, so around that. From Thailand again there is some anti-dumping duty.

Ajit Motwani: Vietnam if I import at \$260 that is a Chennai port price, from there I will have to transport to northern India?

Sajjan Bhajanka: See, nowadays container freights have come down drastically, so it does not make much difference whichever port it is. So almost it is similar for all the ports. Kandla is the cheapest port. Kandla in India is the cheapest port because frequency of ships are more, big ships are coming. But again Chennai is also competitive. So these MDFs are coming for anything between \$400 to \$600 per container, so cost is hardly around \$20 per cubic meter.

Ajit Motwani: But how much competitive we will be if import substitution happens for us and that is primary augmentation of ramping up the utilisation so far?

Sajjan Bhajanka: Major difference between costing is more or less same in Vietnam or Thailand or in India, because timber price in North India is one of the cheapest, it is say Rs. 2 a kg. So it is less than

\$30 per cubic meter. It is one of the cheapest in the entire area. Glue is more or less same. So that way the cost would be same and in India our benefit would be the transportation cost, shipping cost and then if any duty or anti-dumping duty is there that is to our advantage. Then the inland logistic, suppose we import and then bring it to the market. If in south market for Bengaluru it is little costlier, for Mangalore it will be cheaper, for Chennai it would be cheaper, for Trivandrum it will be cheaper because it is near to port. Bengaluru and Hyderabad would be little costlier because there is distance from the port. So that way it will vary depending on logistic and other thing and it would be market specific.

Ajit Motwani:

And on GST, now that the rates are declared, what is our sense on it?

Sajjan Bhajanka:

Now, details are yet to come so it could be anything between 18% to 28%. So either we would be in 18% bracket or we would be in 28% bracket because many states in India they are imposing the rate of 5%, many states they are imposing a rate even up to 15%, like Gujarat it is 15%. The rate for most of the southern states is 13-14%. So if that is taken into calculation, it would be 28%. If it is matching duty leverage is maintained. In the Eastern Indian states like Bengal, Bihar and Assam the rate is 5%. So it comes into the 18% bracket. Another thing, their explanation that the mass consumption item for furniture they are **keeping in the lower segment, so it is part of the furniture, plywood is sold. Plywood, MDF and particle board are sold solely for the furniture** making. If it is tagged with the furniture then it will come into 18%. It is very simple, if it is 18% we have to reduce price because our present cost is 28% plus, our present cost of the duty and these all things, except in these few markets, say 30% of the market, it is less, in 70% of the market it is around 30%. For that then we will not make any adjustment, it will remain at the same level, and if it is 18% then we have to reduce the price, we have to pass on the benefit to the customers. But the only benefit to us would be level playing field, because now our competitors from unorganised sector are enjoying SSI benefit, which is if their last year's clearance is less than Rs. 5 crore then this year, on first Rs. 1.5 crore they will get 100% exemption **and they have to pay normal duty of around Rs. 1.5 crore to Rs. 5 crore**. With that some people they limit to Rs. 3 crore, Rs. 4 crore, so their average costing is much lower than us. Now with criteria being changed from Rs. 1.5 crore in last year to Rs. 20 lakh in last year, none of the unit will be eligible to have any exemption because all have turnovers in crores for last year. Our entire sector will go out of the exemption and then there would be some level playing field. One very important feature of GST is bill-to-bill matching, earlier it was value-to-value matching. How much you have purchased and how much you are selling. But in this platform they are making it very particular, it would be invoice-to-invoice matching. So, they cannot replace the sale by some steel or some other thing, the plywood is to be replaced with plywood or plywood sales would only be eligible for input of plywood purchased. And similarly, for MDF they cannot switch it from plywood. That is a magnificent scope which will come and then all invoice and everything are irreversible. Earlier some people in Punjab were sending material to Mumbai and after it reached Mumbai they asks them to tear

off their document as it becomes tough to understand. Now that is not possible because their portal, their things where they have put the document are related with the central portal.

Ajit Motwani: But what is the input duty we pay? We will be paying custom duty on the imported log and nothing on the domestically procured timber, right?

Sajjan Bhajanka: Yes, nothing on domestic timber, because yellow forestry product it would be out of that duty. There would not be any because it is an agriculture produce, entire timber. Veneer and timber which are being imported, there it would be appreciating because then there would be, it is yet to be notified, maybe timber they may keep at lower bracket but usually section is the same to our Chapter in excise 44. So if it remains in the 44 Chapter then it may be in 28% bracket.

Moderator: Thank you. Our next question is from the line of Jignesh Kamani from GMO. Please go ahead.

Jignesh Kamani: As you mentioned, MDF, I think first priority would be you can say utilise the capacity and the ramp-up phase as early as possible which means you would be incrementally selling more and more to OEM than you can say normal B2C channel. So what is our estimate for B2C and OEM share in first year and how it will pan out gradually?

Sajjan Bhajanka: We looked for all the options, we are planning along with this we are putting up pre-laminating plant, so part of that would be consumed in-house and we shall pre-laminate and sale. Then we are also planning flooring, so part of that would be used for flooring. Then we are already increasing our door sales, so in China most of the doors are manufactured from MDF. So we are also exploring the possibilities to tie-up with some leader in China for doors manufactured from MDF. We are in a dialog with a lot of people. Maybe either in joint venture or technical collaboration with them we shall establish door manufacturing capacity based on the MDF. So our plan is to not to sell raw board in the market. The minimum would be pre-laminated board and then it would be value-added products like doors. But yes, to start with, maybe doors like other things. But yes, to start with maybe the substantial part would be of raw board and then really we will shift to value-added products.

Jignesh Kamani: So 50% plus will be the OEM share including the bare board?

Sajjan Bhajanka: Yes, like particularly in South India mostly it is used by OEMs, like furniture manufacturers and domestic use of MDF is comfortably less. But in northern India it is used for beds, so earlier 6x3 size of plywood was used, now it has been replaced and again credit goes to Greenply. They have educated a lot of people, they have introduced it in a lot of various range. So that way we are lucky that some existing demand is there, some sectors are there which have accepted MDF for alternative reasons.

Jignesh Kamani: Adding to that, if you take about 50% plus will initially be bare board of OEM, and OEM share if you talk about our competitor including Greenply, they are not getting more than 15-17%

kind of margins, so in that case how we reconcile 30% margin where our exposure to OEM will be much higher than industry standards, at least initially?

Sajjan Bhajanka:

Here what we have tried is to keep our cost at the lowest. So, even like we have generated sufficient money in the company, we are very comfortable about the case. So whatever pursuit we are putting our equity or money reserves available in this, and whatever we are borrowing, most of that initially would be at buyers credit. So the total implication of interest would be around 2%, subject to dollar fluctuation. So that way interest cost we are keeping low and the raw material cost, already it has substantially come down. When Green planned that time raw material cost was seven to eight years back it was Rs. 1.50 per kg, but when they started manufacturing that time it gradually it increased to Rs. 4.50 to Rs. 5 a kg. But fortunately now again it has come down. So for Green also it has come down and for us, and particularly in Punjab which is the largest manufacturer of plantation timber, there is no off take of this, like residual timber. So prime timber is going to plywood, next is going to block board and residual timber it is only being used for firewood. So price has come down below Rs. 2. And earlier paper mills were using this timber, now they have also shifted to wheat straw or some other agricultural waste. So that way, and not like Milanpur is already in problem, they are not manufacturing with capacity, so demand from paper has decreased and at the same time replacement for paper is available and price has come down. So it is a good opportunity to us.

Jignesh Kamani:

And my last question is, if you want to sell 180,000 entire RCBM capacity entirely to B2C channel, how many dealers we will need for MDF?

Keshav Bhajanka:

We have (+2000) dealers already pan-India who are regularly billing with us. We also have a network of 18,000 retailers pan-India. So I do not know what exact number there will be but I am sure that a vast majority of this network already deal in MDF. A number of our larger dealers have been putting pressure on us to put MDF for the past five year. Now catering the same, I am sure that large percentage of our offtake will be taken up by our larger dealers and they will be supported by smaller retailers to ensure that our total capacity is consumed.

Jignesh Kamani:

But are we planning to have a separate distributor-dealer for MDF, at least distributor for MDF or it will be same distributor for plywood and MDF?

Keshav Bhajanka:

We will be looking at different distributors for MDF but the dealer shall remain constant.

Jignesh Kamani:

And how many distributors we will need if we want to supply entire quantity to B2C?

Keshav Bhajanka:

Different geographies will have different requirement. So if you look at a market like Delhi, traditionally we have seen that a minimum of five distributors are required to cater to only Delhi, Noida being a separate area and Gurgaon being held as a separate territory. So it depends on the geographical band that we target at that point in time. It will also depend on the capacity of these distributors to invest in the business, it is not necessary that every distributor being



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able to invest equally. If I get somebody who can finance x amount, I might be able to put him as a sole distributor for Ludhiana. But if I get somebody who can only finance x/4 amount, I might require two more distributors for Ludhiana. There are a lot of different dynamics in play, I cannot give you an exact quantity at the moment.

Moderator: Thank you. Due to time constraints, we will be able to take one last question. The last question is from the line of Prashant Kutty from Sundaram Mutual Fund. Please go ahead.

Prashant Kutty: Firstly, just wanted to understand with regard to the laminated part of the proportion, so obviously the base is also increasing pretty much aggressively, almost we would be selling about Rs. 250-odd crore of laminates in a year.

Sajjan Bhajanka: Sorry, your voice is not clear Prashant.

Prashant Kutty: So I was just saying that with regard to laminated part of the business, our base is also catching up, our base is becoming bigger now. When do we really expect the base of let's say the growth rates in laminates to converge with plywood? Because typically laminates is usually a feeder for plywood growth, so just wanted to understand that, till when do we expect this high double-digit growth rates to sustain in laminates segment?

Keshav Bhajanka: Post-GST we expect our plywood growth to increase drastically, at that point I think both will converge. But on a more serious note, yes the base has started to increase, yet growing is now more difficult. However, we are barely at 4% or 5% of the total market for laminates. There is a long way yet to go. And I think that given the steps that we are taking, we are soon going to be in the position of market leader. Once we reach that position then to target the same growth again will be difficult, but I think that is two years away. So for the next two years I do not see a problem in maintaining this growth rate. Post the sale we will have to relook how to grow at the same pace.

Prashant Kutty: The reason why I asked this is because just want to understand, you just spoke about one of the initiatives, if you could highlight a couple of initiatives over here which you are typically taking on the laminated side of it which should sustain this growth rates for you?

Keshav Bhajanka: There are a number of initiatives, like I just said earlier; catalogue is our first sales move and we have invested very heavily in development of the catalogue every year, we have created a separate PM group, a product management group which focuses on development of marketing collateral and so on so forth. So I think by investing in such initiatives and by investing in manpower, we have been able to create a differential structure. Today, no other company can generate a catalogue every year, no other company can change hundred designs per year, no other company can supply to any part of the country within 24 hours. We are able to do all of this because we have invested in necessary infrastructure to do so. And I think all of these initiatives together with the team that we have created are the drivers behind our success. So



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going forward, I think all of these shall remain competitive advantages for us and they should continue to benefit us.

Prashant Kutty:

And incrementally if you have looked at the margin performance, it obviously continues to improve even on a sequential basis as well. Do we really feel this is the most sustainable number if we look at it? Because I also want to understand one more thing over here, we also typically have a margin differential when it comes to a 0.8 mm or a 1 mm kind of this as well. So just want to understand what the mix is currently as well.

Keshav Bhajanka:

Close to 90% of our domestic sale is in the 1 mm category and maybe 10% or maybe if it has increased slightly, 10% to 12% would be in the 0.8 mm category. We are not into lower segments such as 0.6 mm, 0.45 mm and so on so forth as the competition are. Going forward, I think that the 0.8 mm contribution could increase from 12% to close to 15% at the max, whereas the 1mm volume shall continue to increase at the pace at which we are today. In the 1 mm category there are differences because there are designs which are plain designs that fetch you a lower realization and then there are texture design which fetch you higher realization. So in terms of textures we are increasing quarter-on-quarter, this is one of the primary reason behind the high EBITDA you see. Going forward, I think we are investing in textures and in new designs and this should help us to maintain these EBITDA numbers, if not increase them further.

Prashant Kutty:

And just one last bit from my end, a little more longer-term view kind of a thing. Now, obviously you spoke about the MDF market, I guess a lot of it is being currently serviced for the OEM side of it. We are obviously talking about the retail demand increase as well over a period of time. I am sure you would have been asked this question many a number of times, but just want to understand how much we really expect of that cannibalization to happen from plywood and MDF on account of that, let's say over a longer period of time?

Keshav Bhajanka:

I would broadly classify it into four categories, so assume 100x. So there is a plywood category which is 100x plus, one that is 100x to 80x, there is one which is 80x to 50x and then the last category is 50x and below. Now, largely the market is split into 10% being 100x plus, the next category being 45%, next category being 25% and last category being 20%. So the sub-50x category which is 20% of the overall market, that is going to come under severe threat from MDF, there is going to be a drastic substitution from MDF to this category because once you see that ply you will realize how low the quality is. If you make a table out of it, it could collapse in two years. Now if a customer has to pay a higher value to construct something that lasts for shorter duration, I am sure he shall refrain to do so once a substitute comes up. And I think MDF has already begun on that journey. This lower category of the market is going to be severely, severely hampered by MDF and going forward MDF is going to increase in this particular category. So I think that substitution effect is going to predominant in the next three to five years, and going forward I do not see that category continuing to exist.



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- Prashant Kutty:** Alternatively, it could also impact maybe something like Sainik as well, while it does not fall in that category but could it impact the Sainik incrementally?
- Keshav Bhajanka:** See, Sainik is a different product category, it is far higher. So going forward over the course of the next two decades, maybe that category shall also all under this thing.
- Prashant Kutty:** Okay, but that is a very long-term thing, it is nothing near term at all?
- Keshav Bhajanka:** I do not think for the next decade or so that category has any effect from MDF.
- Moderator:** Thank you very much. That was the last question, Ladies and Gentlemen. I would now like to hand the conference back to the management for any closing comments.
- Sajjan Bhajanka:** Yes. We thank all of you for regularly participating and coming out with some very good questions. And all are what we feel are very, very positive and very objective and very linked to understand us, so we welcome it. And we commit that whatever is at our disposal, with full honesty, with full sincerity we will work for the company and we wish that we give the best possible return to our investors. Thank you.
- Moderator:** Thank you. On behalf of Ambit Capital, that concludes this conference. Thank you for joining us, Ladies and Gentlemen. You may now disconnect your lines.