“Vardhman Textiles Limited
Q3 FY2019 Earnings Conference Call”

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Moderator: Ladies and gentlemen, good day and welcome to the Vardhman Textiles Limited Q3 FY2019 earnings conference call, hosted by IIFL Capital Limited. 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. Avi Mehta from IIFL Capital Limited. Thank you and over to you Sir!

Avi Mehta: Thank you Aman. Good afternoon everyone. On behalf of IIFL, I would like to welcome all of you to 3Q FY2019 conference call for Vardhman Textiles. From the company, we have with us the key senior management, including Mr. Neeraj Jain – Joint Managing Director, Mr. I.J. Dhuria – Director (Materials), Mr. Rajeev Thapar – CFO and Mr. Mukesh Bansal - Senior Vice President, Fabric Marketing, and Akshay Jain, Finance Head. I would now like to handover the call to the management for their comments. Over to you Sir!

Neeraj Jain: Thank you. Welcome to all the investors on this conference call. We have announced the number and this quarter has been a little different in terms because there was a changeover of a new cotton crop and lots of other changes, which were found during the quarter.

First of all on the cotton side, I think since the crop had some so the prices of the cotton new crop was much higher as compared to the previous period for different seasons which Mr. Dhuria will explain to you, all of you in a while, but still the advantage to the company was since we were covered for part of the quarter because we have generally covered mid of November so I think that advantage was available without new cotton crops, there was some improvement in the yarn prices also and since we were partially using the old crop, I think that advantage in terms of the numbers also came to the company.

Also this was a quarter where there were lots of issues with the USA and China though no direct impact on us is yarn and fabric producer, but I think because of the uncertainty there was a period in between the demand of the yarn was relatively low especially from China, but I think as they reduced their inventories of yarn, slowly they again started picking up and as of now their normal buying get started but during the quarter there was a time that there was issues and their overall imports from India or other parts of the world were relatively less, which had had an impact on many companies but fortunately Vardhman never had any issue in terms of difficulty in selling the yarn. That was yet another uncertainty.

Third was I think there are lots of issues and difficulties in the domestic market on account of the cash crunch situation available so as a result of that lots of fabric producers they reduced their capacity especially the Denim segment, so the Denim has not done very good in last three to four months, as a result of that, I think there was impact of the yarn demand on that also, which also impacted the industry. Having said at the same time the mean time since the lots of new capacities are coming up in India especially Gujarat because of the old policies, because of the policies announced by the government, I think the capacity kept on coming into the production and whatever capacity came into the second quarter that became fully effective in the third quarter so the overall increase of seamless spent kept on happening in India so on one side we had an issue, where the demand by the builder, on the other hand I think some small capacities are coming up every quarter, which also has an impact on the overall demand and supply situation of the business.

In spite of that I think as Vardhman there was no issues, no difficulty in terms of selling the products and all our customers, keen cotton customers, product mix, everything was by and large intact and we could sell most of the materials and in terms of the margins also I think if you go by the pure replacement cost of cotton would have been lower but definite reason is the part of the cotton or raw materials as on the older prices so I think the additional advantage came to the company in this quarter as well.

Before we go to the raw cotton I will request Mr. Mukesh Bansal to give some brief on the fabric business side also then we will request Mr. Dhuria to give us some update on the financials.

Mukesh Bansal: Good evening to all. On the fabric side also the quarter have been reasonably well. We saw there was no sluggishness of the demand from the domestic segment even though the third quarter typically is the festive season for the Indian retail but then majority of this fabric booking for the same happened in the second quarter itself, so third quarter typically is the largest quarter for the export segment wherein which is typically streams of quarter wherein the cotton dominated fabrics openly stores so we had pretty decent booking and reasonable capacity utilizations and as we mentioned in the previous calls that we started to work printing project, which has been received very well and we are supplying to some of the top brands of US, Europe and also the Indian subcontinent. If there are any questions, we can take up later that is all from my side Sir. Over to Neeraj Ji!

Neeraj Jain: Thank you. I will request Mr. Dhuria to give us some inputs on spontaneous raw material.

I.J. Dhuria: First of all the international world cotton demand supply situation for the year 2018, 2019, world production in the year 2018, 2019 is likely to be as per the USDA number is 25.85 million which is 4% less than the last year. The major reduction is happening in India and US. US production is less by 0.6 million ton and Indian production will be less by almost more than 300000 tonnes whereas on the demand side USDA is indicating 2% increase in consumption over last year which was 26.8 million tonne this year we are indicating 27.35 million tonne but looking to the overall situation this may not happen so difference between the production and consumption it is going to be around 1.5 million tonne and major reduction will be happening in China, where the production will be around 5.8 million tonne and demand will be about 9 million tonne and China will be importing about more than 1.5 million tonne from the rest of the world, whereas rest of the world balance sheet, the production will be around 20 million tonne and consumption will be 18.3 million tonne and 1.5 million tonne they will be selling to China, so rest of the balance sheet will remains same as that of the last year, now opening and closing will be more or less same.

Coming to the Indian number although CAB numbers were 36.1 million bales and today the trade body of Cotton Association of India, they have revised their number to 33 million bales, but according to us the Indian production will be about 34.5 to 35 billion bales and with the opening stock of 3.6 million bales as on October 1, 2018 and with the import of 1.5 billion bales, consumptions of 32 million bales, export of 4.5 billion bales, the total take off will be about 36.5 ending stocks will be about 3.1 million bales. There will be reduction is stock or it is a possible that county may export more cotton already 2 and 2.5 billion bales have already been exported from the country up to January 31, 2019 and this 4.5 million bales we are taking on the very conservative side, if there is a more export then there will be further reduction in the stock.

This is all about the international situation and as far as the cotton situation is concerned, but if we compare the cotton prices, which was prevailing in the month of December, January and February year 2017-2018 versus this year and looking to the dollar rupee relationship at that time, which was in the range of Rs.63 to Rs.64, in terms of US trend this year the cotton is comparatively cheaper one, two but at the same time this cotton could have been much cheaper this year, if there could have not been any MSP support to the market, today there is an increase in 28% MSP over the last year, there is a support to the market, but in spite of the liquidity crunch market is under pressure may be looking to the demand and supply situation during the off season the cotton price will be higher or the gap between the international price and the local price will reduce. That is all from my side.

Neeraj Jain: About the expansion plan, I think as we have been discussing the total expansion plan of the company, which has taken out two years which is 2018-2019, 2019-2020, it is close to about Rs.500000 most of the expansion plan is as per schedule as of now and may be we will be typically spending close to about 1000 Crores in this financial year and another Rs.500 Crores in the next financial year. Most of these plants would be fully operationally by May next year, May 2019 so we will start operating asset, most of the spinning May-June we will be completing these projects so I think during FY2019-FY2020, the part of the expansion will start showing the results because yarn may be stabilized a little better or little early, but fabric generally take some time to build up the order so which may take some time, but I think 2020-2021 the full impact of all the expansions could also be available, though major part will be available during FY2019-FY2020 as well.

I think this is from our side as of now so I will request for to go in for the question and answer, remaining things any clarification required we can discuss along with the questions and answers.

Moderator: Thank you very much. Ladies and gentlemen we will now begin the question and answer session. The first question is from the line of Gagan Talreja from Kotak Investment Advisors. Please go ahead.

Gagan Talreja: Good evening Sir. Sir if one were to compare cotton prices that you would have this year versus the average cotton procurement prices, last year because I think last year there was lot of volatility, year-on-year what could be the sort of difference between cotton procurement prices for you?

Neeraj Jain: In generally, I think our feeling is the market prices of cotton are in the range of the difference is almost in the range of about 10%-12% as of now. In rupee terms, but if we look at the impact of even dollar rupee then practically the prices are almost same, compared to the last year prices, so it was almost 77, 78 cents last year and I think prices as of now are also same, it depends upon how much and how we can procure to, I cannot give any comment on Vardhman purchase as of now, but going by the market prices, I think the prices in US strength is almost same as of the last year.

Gagan Talreja: If one were to compare, the yarn prices as they prevail now versus the average of last year where would they stand?

Neeraj Jain: As on date, it will be almost comparable, may be a little better, almost comparable I will say.

Gagan Talreja: Sir one were to look at the cotton yarn spreads have we sort of right back to the long term averages and do we sustain and what is your outlook on the yarn prices and the yarn cotton spread?

Neeraj Jain: Yes, the long-term outlook of 18 to 22 I think this will come at committing to the term. EBITDA margins to sales, the cotton to yarn spread whatever is the normal spreads will be available but last year there was an extraordinary spread available to us because what I mentioned to 78 cents cotton was on the yearly basis whereas we bought cotton last year at a much earlier so our spread was better compared to the normal spread.

Gagan Talreja: Okay so in that case the current margin that we have seen in the last two quarters, this quarter and the previous one, you feel that the trajectory could be somewhat lower in the coming quarters, simply?

Neeraj Jain: For cotton it is very difficult to say because historically the season is there lots of arrival so cotton will be at a lowest prices, but by the time we go to the off season generally the prices tends to increase so we cannot commit what will happen in future, but if we look at the last 10 years, 15 years history that how was generally it has been moving so it is very difficult for me to say that if tomorrow the prices increase and we are covered it as a reasonable prices, we may still get the similar opportunity so difficult for me to say what will happen on the cotton prices in future, but yes definitely last year, we had the advantage, better business this year or not, is time will tell but last year that advantage typically has come to us.

Gagan Talreja: You also indicated that there were some disruption in procurement from China which is thereafter normalized. Given the situation, the political situation between US and China and the capacity that are available in China, what are your thoughts on the export business for yarn both in terms of volumes and prices for you?

Neeraj Jain: You know if we look the capacity which Chinese have for the government export they are exporting almost $300 billion of government so even if there is any issue between the two countries, I do not think there is any other country which would take that position as of now, so effectively I think there is some uncertainty, there was some issues in the meantime, but I personally feel it is going to be very difficult for any country to replace, in the two to four year's time so whether there is a more duty on the Chinese product or not, but still I think supply will continue to be the biggest supplier for the next couple of years, so if they are bigger suppliers then the will continue to buy the yarn because their own spinning capacity, their cost are increasing so they are not really as country expanding in a bigger way, so I think their dependence on India is good. So India and Vietnam are the two biggest exporters to Chinese as of now, which will continue in our opinion.

Gagan Talreja: Hypothetically if at all there were to be some crucial movement away from China to some other countries would you still be in a position to capture that movement let us say if there is a movement from government exports from china away to a Vietnam or Turkey some of these countries?

Neeraj Jain: There should not be any issue because both countries they will be requiring the yarn so unless they decide, all these countries decide to move in a bigger way for the spinning whether they want to or they will do it or not because going by the normal margins of the spinning or setting a factory of 18000 and the new capacity it does not make really much of a chance to any spinner as of now. So whether they are really going for these kind of big expansions on the spinning side is a big question mark so I still feel wherever the garmenting may happen ultimately yarn requirement would be there and those opportunities whether it is in China or any other country my belief is we should be in a position to capture that as well.

Gagan Talreja: Last question from my side, you bought out the recent stake in the joint venture I think that is for garmenting how should we think of this for you hereon and you in the past indicated that this is a business area learning the roads? Has anything changed do you now hereafter feel that there is scale that we had in this business and you want to in a calibrated way grow this up?

Neeraj Jain: The business is definitely better compared to the last year and I think my belief going by today's situation we might turning into black in this year. Now whether we will be in a position to really expand it or not only time will tell but I think as a business definitely we are doing better so we were looking at in case we have the grow the business and we have to look at the points of business I think Japanese had some issues and difficulties in terms of further commitment of the plant and we also had some limitation in terms of the market or some of the ideas where the Japanese had for our agreement there were some issues and difficulty in selling products to the different customers within the time as well. So I think it has been a very happy division and we are looking at whatever could be the better for the business we should try to attempt the same rather than looking at only the partnership so in terms of selling arrangement or in terms of the other arrangement, I think we are talking to the Japanese and it is on a right track. So my belief is if the business does good, yes definitely we look at how we can really expand it in a big way that could be one opportunity or we sustain do the marginal investment for next two or years so that our base on the business is far better and when we take a final view.

Gagan Talreja: Finally, you are outlook on the weakness or the softness in the domestic market how do you see this sort of evolving over the coming financial year?

Neeraj Jain: To me, I think the worst is over for whatever capacity utilization which has come down because of this financial crunch and those things again it is linked with the NBFC funding, it has been linked with the banking funding, NCP and so on. The capacity utilization even in the denim sector has started improving. The market is a little better. The financial market is also a little better and banks are also coming there for funding etc., so to me it looks like the worst is over and we are looking definitely an improvement as of now. Looking at outside the business over the last couple of weeks so I think it is definitely at a better stage.

Gagan Talreja: Thank you Sir. That is all from my side.

Moderator: Thank you. The next question is from the line of Siddharth Mohta from Principal India. Please go ahead.

Siddharth Mohta: Sir my first question is what can be revenue growth we can assume in FY2020 and FY2021?

Neeraj Jain: Like in terms of the volumes I think on the yarn stage we will be adding may be about 12%, 13%, 14% capacity, which will be partially on the fabric and fabric side, also will be adding almost 25 to 30 million meters of fabric. So once that is fully streamlined I think it has a potential to increase the sales by another about 800 to 1000 Crores.

Siddharth Mohta: With our product portfolio moving more towards this value added fabric so one can assume this EBITDA range to move more toward like 20 to 21% once our entire capacity is stabilized that is FY2021?

Neeraj Jain: Definitely it should be better than today's level. We have not decided what kind of medium term range it should give for the guidance but you are right once our model is moving more on the fabric side I think the margins would be more stable as well as it should logically grew once we start all these capacities maybe then we look at after a couple of quarters that is how should we keep guidance on this.

Siddharth Mohta: Thank you and best wishes for upcoming quarter Sir.

Moderator: Thank you. The next question is from the line of Ujwal Shah from Quest Investment Advisors. Please go ahead.

Ujwal Shah: Thank you for the question. Sir I just wanted to know what percentage of external sales is fabrics for the quarter and for the nine months, what kind of growth have we seen in fabric business for this period?

Neeraj Jain: The period, you are talking about the volumes number or what?

Ujwal Shah: Sir, in terms of volume growth for our fabric business?

I.J. Dhuria: Volume has already been given to the stock exchange.

Ujwal Shah: In terms of value ____?

I.J. Dhuria: It is not in terms of value. It is in terms of quantity.

Ujwal Shah: If you can share in terms of value Sir, of the external sales?

I.J. Dhuria: Separately we have not disclosing it that is the reason we are showing the textile as a single segment for the result purposes.

Ujwal Shah: That is all from my side. Thank you.

Moderator: Thank you. The next question is from the line of Kunal Shah from IIFL. Please go ahead.

Kunal Shah: Thank you Sir for the opportunity. Sir my question is related to the gross margin. So if you see in this quarter versus last quarter, Q2 FY2019 and Q3 FY2019 our gross margins have improved by almost 200 BPS, now you commented that we have had the benefit of old cotton but that benefit is already there in the last quarter as well?

Neeraj Jain: When the new crop in, the prices of yarn also improved. Using the cotton, which was at much cheaper prices so I think the advantage, was more.

Kunal Shah: So it was somewhat a function of increase in yarn prices and second thing so how did the margins behave on the fabrics side this quarter let us say FY2019?

Neeraj Jain: That was also a little better only.

Kunal Shah: Okay, both an improvement in fabric and yarn margins and so till January and February what you are saying has yarn spreads improved from 3Q levels because of the new crop or they have been worse off?

I.J. Dhuria: The margins would be similar compared to what it was last year on the market price of cotton and the market price of yarn. Our margins are better because our cotton was much cheaper so our margins were better so if I go by the market prices replacement cost of raw materials and market price of yarn today will be comparable to the last year.

Kunal Shah: That is all from my side.

Moderator: Thank you. The next question is from the line of Arjun Sengar from Reliance Mutual Fund. Please go ahead.

Arjun Sengar: Good evening Sir. Versus the performance that we have had in this quarter, Q3, I was just trying to figure out what are we likely to do in the upcoming quarter which is Q4 so from the market prices, which are visible I think the yarn prices are largely stable so far in the previous month in January, but we would be using the new season for the full quarter in Q4 versus our EBITDA margin that we reported in Q3 is the margin likely to be lower in Q4 because of the new season cotton that we will be using for the whole quarter?

Neeraj Jain: As of now, yes.

Arjun Sengar: What is general outlook you have for yarn prices from here because you said there has been some kind of relief improvement in demand from China of late?

I.J. Dhuria: It is basically yarn prices the market indication, we came down to most of the industry segment I think there is definitely an improvement of 5 to 7 cents in the yarn prices along with that the devaluation of rupees also helped so if you look at on the domestic segment from the worst rate we have definitely improved by Rs.5 or Rs.6 per kg. I think if the demand continues to be good and there is no other disruption and we are maintaining this then I think for the industry the problem will be less but of course as we discussed our numbers were different for third quarter because of the reasons already mentioned.

Arjun Sengar: Sir for our fabric segment what proportion of our yarn requirement is manufactured in-house?

I.J. Dhuria: Almost 35%

Arjun Sengar: 35% of yarn requirement in fabric is manufactured in-house?

I.J. Dhuria: Whatever yarn we produce 35% goes in our internal fabric yarn.

Arjun Sengar: That I am aware of, but I saying for fabric division what percentage of the total yarn consumption is manufactured in-house?

I.J. Dhuria: 95% yarn they consume it is from in-house.

Arjun Sengar: Okay.

I.J. Dhuria: Other yarn, specialty yarn only 4 to 5% from outside

Arjun Sengar: Thanks. Sir, our other income was slightly higher this quarter was there any nonrecurring item in it?

Neeraj Jain: There are some forex gains this quarter, which was not there in the Q2 that is the reason.

Arjun Sengar: How much is the quantum Sir?

Neeraj Jain: Within the range of Rs. 21 to 22 Crores.

Arjun Sengar: Thank you.

Neeraj Jain: Arjun one second. Every quarter end we have to do the mark-to-market so depending upon what prices are there at the close of the quarter I think those gains or losses will have to be provided but otherwise in terms of our policy on forward selling I think consistently we are pursuing the same.

Arjun Sengar: Sir one final question. China, I think mostly largely exhausted its cotton inventory close to exhausting his cotton inventory can you throw some light on that and post this can that lead to higher imports of yarn into China?

I.J. Dhuria: As per USDA numbers, as on August 1, 2018 all opening stock of China including reserve, it was about 8.3 million ton. Now out of this 8.3 million ton, 3.86 million ton was in their reserve and balance was either with the mill and commercial stock. In FY2018-2019 it is estimated to be that they will be having total stock of about 6.6 million ton that means reduction of about 1.6 million ton which I have already said and out of this reserve stock will be about less than 3 million ton they will start selling their reserve stock somewhere after March then we are estimating it will be less than 2 million ton and may be that most of its quantity which we have been having may not be usable or may be usable for lower end of the yarn. So China prices for import of cotton as well as yarn will continue to be there.

Arjun Sengar: Sir the textile industry textile industry I am sure may be representations to the government on the MSP issues so that the market price is not affected, but farmers are compensated indirectly. Is there any update on that front?

I.J. Dhuria: Yes Sir we had been giving representations to the government regularly either through Ministry of Textile or Ministry of Agriculture that this year increase in prices, which has taken place while in MSP was more than 28% it is this year by chance the things have happened to be like that the global demand and supply position is getting tight that is why prices are earlier it was a little higher than the MSP and today it is very close to MSP. The country has received almost 57% to 58% of estimated production, but maybe later the rest of crop will also be marketed accordingly. So there may be a little interference by the CCI in the market at MSP operation. So far they have stores about 700000 bales and everyday today they are sourcing between 20000 and 25000 bales per day on MSP operation, mainly it is happening in Maharashtra, Telangana and Andhra. The next year if your look at the scheme building the major cotton economy the cotton farmers they have received a better prices in the current year and we can safely estimate in the next year the area under cotton cultivation particularly in US, India is going to increase so the next year again the world is going produce record production keeping everything on from the monsoon perspective or other hurricane perspective in USA are going to be normal. So next year if things moves like that, international prices are likely to go down but this MSP operation can create a problem for the Indian textile industry and it will be to their disadvantage until and unless a government takes a decision to give a difference between the MSP price and the market price directly to the farmer. If it is given directly to the farmer definitely then there will not be any distortion in the market.

Neeraj Jain: The question here was we are also in touch with the government and government in all our talks has agreed to the arrangement that the direct subsidy should be given to the farmers, but I think they have to make the arrangement and all the modalities to do the same as of now they are not prepared but principally they also agree that it should be done in this way only because fortunately this year as Mr Dhuria mentioned did not be a bigger issue, because the overall prices were higher. So we hope by the next season starts after a year or so by that time government will be in a position to make some modality because principally they also agree that it is a minimum support, price has to go to the farmer should not be at the cost of the industry but the same time whether they will be in a position to do it or how fast because the number or the number of farmers those are the administration issues which they have to handle, but principally they are not denying what our request is.

Arjun Sengar: Thanks Sir. Suppose that does not materialize and MSP operation continues like this what implication you see for the sector from a medium to longer, does it mean that the 18% to 22% margin range may shift downwards is that a possibility?

Neeraj Jain: There are two factors to this one is may be the next year as one is expecting whether because of the huge crop size the international prices could go down, but we also have to bear in mind with the China reserve stocks today if you look at the balance sheet in two parts. One is China and second is the world rest other than the China. Every year there has been some improvement or some increase in the stocks of rest of the world, but once China's own consumption differences almost 2.5 to 3 million tonnes their own production and consumption and they import about 1 million tonne as of now, so the moment they start importing another 1.5 to 2 million tonnes from the world market over and above what they are doing today to maintain whatever spinning operations they have as of now. Then the possibility of world prices to go below a level will also not be there. Today it is only there because China is buying only 1 million tonne and they are consuming out their old stocks about 1.5 million tonnes or so, but once that stock is not there the demand supply of cotton is almost same 27, 26, 27 million tonnes will be the production. This will be the consumption. Then the prices of cotton going down below a level will also not be there, so there could be a disruption or an advantage for a year or so, but in the medium term, I do not think that risk is there that India will be really suffering from a MSP because the world prices will be much lower. That does not like as far as our opinion.

Arjun Sengar: Sir this rupee depreciation that has happened, which I think last quarter you had told us that generally these depreciation benefits we have to pass on because it is an open market, so how has it panned out?

Neeraj Jain: There are two factors one is our rupee depreciation and the second is also that what is happening to the competing countries. So in this period we were fortunate that Indian rupee was devaluing where as the Chinese Yuan has been appreciating, so from 6.90 they have gone to 6.72, 6.73 or 6.74 as of now whereas the rupee has been devalued, so what is happening to the other countries like Pakistan, Bangladesh, which are the major competing countries for this currency there has not been much of a change in those countries also in the last couple of months, so I think the advantage or even if this happened the raw cotton prices will get adjusted immediately because they are all commodities and their prices in the US hands will be comparable, but on the value addition definitely there is some gain, which will be available and that gain is available to us even today also.

Arjun Sengar: Thank you very much. That is it from my side.

Moderator: Thank you. The next question is from the line of Kush Gangar from Care Portfolio. Please go ahead.

Kush Gangar: Sir you mentioned that we are doing expansion of Rs.1500 Crores whereas new addition in topline can lead to the tune of Rs.1000 Crores, so the asset term what you are doing is fairly low can you please explain on this part?

Neeraj Jain: Yes it is true because there are two projects, which are coming up. One is spinning and the second is the fabric, so most of the new spinning addition whatever we are doing practically they will be going similar figures and similar quantity will be going for the fabric expansion as well, so on a practical side, I think the overall net sales will increase only from the fabric side as a result the capital turnover ratio for the new projects will be a little lower, but the margins will be better because your sales is one and so you are transferring Rs.100 yarn to the fabric and the fabric is selling that though your capital turnover ratio will be less, but the margins to sale theoretically in the composite sector will be better compared to the standalone businesses.

Kush Gangar: Thank you.

Moderator: Thank you. The next question is from the line of Resham Jain from DSP Mutual. Please go ahead.

Resham Jain: Thank you for the opportunity. Sir my first question is with respect to the Chinese import of cotton yarn what we hear in the news that Chinese mills are currently sitting on a very tight cotton yarn inventory just want to have your view on the same because what the news we are hearing is that post the Chinese New Year probably we may see some pickup and demand from China yarn?

Neeraj Jain: This historically happens because during the Chinese New Year they try to reduce their inventories, but they start booking before going for the holidays because it is not that they will doing business only after coming back, so their physical inventory comes down during this period, but the business continues, but the other reason, which I mentioned earlier because of this uncertainty with the USA everyone in the system was trying to reduce stock, so our belief is the overall pipeline in China is much thinner as of now because of the Chinese New Year, but because of the other reasons and any positive news on that side because if things do not improve then probably this is already one of the lower level inventory they are working with, but if any improvement happens then definitely the demand could be higher, but only linking it with the

Chinese New Year may not be true because they try physical inventory to be lower at this period and they to do the business so that by the time they come back inventories are available to them. The currency is also appreciating, so it makes lot of sense for them to import and also their raw materials because yarn is raw material for them.

Resham Jain: Sir just to get a more clearer picture on cotton India whatever estimate we had earlier at the beginning of this season we are in terms of production are much lower and also the export has been quite higher as compared to what it was projected so net-net I think the cotton situation is expected it will be very tight so what is your feeling going into the next two to three quarters till the beginning of the next season in terms of cotton prices?

I.J. Dhuria: Today in US terms our cotton is around 76 cents a pound to 77 cents a pound and gap between Cotlook Index and our cotton is about 6 cents a pound to 7 cents a pound. Going forward we are estimating that this gap will be reduced. This will be in the range or maybe at the same price at 82 cents to 83 cents, so India needs to import more cotton. There is going to be definitely a shortage of cotton in the country.

Neeraj Jain: The estimate of cotton as explained by Mr. Dhuria earlier will be about 34 million to 35 million bales this year. Export will be surely lower compared to the last year and suppose four to four and a half million bales are exported on a production base of 34 that means that the country will be left with 31 million bales during this year. Our consumption is almost 31 million to 32 million bales, which means we will be importing about 1 million to 2 million bales and with that also the balance sheet of the closing stock will be very, very less, so last year we completed or closed the year with an estimated range of about 31 to 35 million bales. Different agencies are giving different figures, which is a very, very low inventory compared to the consumptions we have and this year also I think we estimate the balance sheet of cotton to be very tight and by the time we will be closing the year, we will be at a very, very thin physical inventory available to us. In case India starts importing then in any case, the cotton prices will start going up in the world market as well.

Resham Jain: Net-net what you are saying is there can be some increase in the cotton prices?

Neeraj Jain: It is light as of now whether it happens physically or not is a different issue, but going by the balance sheet definitely it is a very tight balance sheet some four months to five months down the line.

Resham Jain: Sir the other question, which I have is with respect to the new capex, which you are doing so this is integrated facility so the current margins, which we earn is predominately still coming from yarn so is it fair to assume that since the asset turns are lower and it is an integrated capacity your

EBITDA margins will not be 18% to 20% for the incremental revenue, which will get contributed in the next one to one and a half years, it will be much higher than that?

Neeraj Jain: On the new capacity yes, generally it will be better, but again I think if you look at the overall machinery, newer expansion on the yarn side will be only about 14% to 15% of our existing capacity on the fabric side also will not be more than 15% to 20% so any major increase or decrease over there will not have that kind of a very big impact on the overall EBITDA margin of the company so that is where we are still feeling that the range, which we have given though it is a little bigger range, but we still feel for the visible times to come this range should be workable for us.

Resham Jain: My question was that incremental revenue will have a much higher EBITDA margin is that right?

Neeraj Jain: That is true.

Resham Jain: Which will be in excess of 25% is that a right assumption?

Neeraj Jain: It is a correct assumption.

Resham Jain: Right Sir and Sir one book keeping question what is the gross debt and the cash level at the consolidated level?

Rajeev Thapar: Total debt is in the range of Rs.1600 Crores and investments are in the range of Rs.1200 Crores to Rs.1300 Crores as well.

Neeraj Jain: As of December 31, 2018.

Resham Jain: This is consolidated right?

Neeraj Jain: Actually we do not have much of debt. Of course investments are there, it could be other investment, it could be in the range of Rs.1500 Crores.

Resham Jain: Because Vardhman itself you have?

Rajeev Thapar: It could be Rs.1500 Crores to Rs.1500 Crores or almost equally you can say.

Neeraj Jain: The debt is only Vardhman Textiles whereas all the other facilities will have investments only practically.

Resham Jain: The net debt at the consolidated level will be zero?

Neeraj Jain: Yes almost zero.

Resham Jain: Wish you all the best. Thank you.

Moderator: Thank you. The next question is from the line of Jayant Mamaniya from Portfolio Management. Please go ahead.

Jayant Mamaniya: Sir in case of global surplus cotton production and the prices are down globally and as per Indian MSP the price is high, will it be feasible for the company to import cotton?

Neeraj Jain: The commercial call can be taken at any stage and there is no restriction in importing, so we still import some specialized cotton, but anytime where the international prices are much lower it is all open. No problem to that.

Jayant Mamaniya: Sir how is the government support for the textile industry?

Neeraj Jain: I think government is otherwise supportive, but as such there is no specific disadvantage or advantage, which has been created in the recent past. There is no disadvantage also for the government whatever are our issues and concerns they are trying to resolve it, but I think it is not on the textiles, but overall whether the ease of operation could be done and I think that is the only support, but specifically on the textile as of now, there is no extra advantage given to us as of now.

Jayant Mamaniya: Sir in case of exports how is our geographical distribution?

Neeraj Jain: Both yarn and fabric we are fairly distributed, so I think we are working with almost 35 to 40 countries for the yarn as well as fabric exports, so of course China is a big number. They are the biggest exporting destination for us as far as the yarn is concerned, but again in terms of geographically or a customer wise distribution I do not think there is any specific consultation anywhere, so I think we are fairly placed to that extent.

Jayant Mamaniya: Due to this China and US trade wars whether India is witnessing any advantage?

Neeraj Jain: There is no dispute as of now. There are only questions going on whether they will continue to import or not on the tariffs, so I do not think any advantage has come to India as of now or we will be in a position to cater to their demands because the capacities required, which are available with the Chinese is too big, so I think it is going to take a long time for any country to create those kind of advantageous capacity. It is too small a period to think even.

Jayant Mamaniya: In this environment what is our production capacity in unit terms?

Neeraj Jain: It is almost ranging between 4000 shirts and 5000 shirts per day.

Jayant Mamaniya: That is all from my side. Thank you.

Moderator: Thank you. The next question is from the line of Arjun Sengar from Reliance Mutual Fund. Please go ahead.

Arjun Sengar: Sir just one question on the commentary on the domestic sector you made of denim wherein you said that denim market is extremely weak right now, so can you be more elaborate on the denim market specifically and what is the outlook going forward?

Neeraj Jain: It is very difficult for me to comment on their economics what is happing over there because we are not into that segment, so as far as I am concerned I am not a yarn supplier, so that is how I am trying to monitor them, but I understand because of the overcapacity created in that segment as well as because of lot of denims get sold into India so there was lots of liquidity crunch, new capacity came in, which was non-operational because of no working capital available so I think those were the issues with that industry and I learnt their capacity utilization has started improving so from our estimation is from a lower level of about 40% to 45% have already gone to 50% to 55% as of now, so their own business model because the concerns have happened because huge capacity has been added in the last four years to five years time, which is also giving them a pain, but otherwise denim if you look at the over consumptions or word by pattern, I do not think there is any big concern as of now, so I am sure as the situation improves their capacity utilization will continue to improve.

Arjun Sengar: Sir this 45% capacity utilization, which has increased to 55% as you said, has happened when in the last two months or some other period?

Neeraj Jain: In the last one and a half months or so. That is what we understand from the industry players only who are our customers so in the informal talk these are the kind of things they share generally with us.

Arjun Sengar: Thank you. That is it.

Moderator: Thank you. The next question is from the line of Resham Jain from DSP Mutual. Please go ahead.

Resham Jain: Sir just one more question on the cash utilization, so we are actually in terms of debt most of the debt is tough debt, which will be available at a lower cost so which will keep, but how are we planning to use the cash over the next two to three years because we will be generating good amount of cash flow next year as well and we have not outlined any major capex going forward, so just to have an outlook on the cash utilization going forward?

Neeraj Jain: There are no specific thoughts as of now, but yes there could be an opportunity if we find some good assets to require but though there is nothing in the pipeline as of now. Two, I think it is a very, very uncertain period, so it is always safe to have some cash available so that any good opportunity come or any difficult time then at least one could pass through the same. Third during the last year also there was lots of cash available, which was distributed to the investors by the Board of Directors by the way of buyback, etc., so I am not very sure how we are going to work on this. I think as of now there is no specific plans how we are going to utilize this cash so it is only may over a period of time the company will be in a position to give their final plan.

Resham Jain: Any capex plan going ahead because next year?

Neeraj Jain: There are a lot of things on the drawing board, so we keep on looking at those ideas as well, but I think again it all links with the overall scenario of the industry in terms of margins, etc. If things go well probably we will start revealing those as well, but as of now only at the drawing board stage.

Resham Jain: Thank you Sir.

Moderator: Thank you. The next question is from the line of Kunal Shah from IIFL. Please go ahead.

Kunal Shah: Thank you Sir. Just one question the acrylic business saw a bit loss this quarter what was the reason for the same?

Neeraj Jain: The crude prices has been coming down as a result of that the prices of the raw material also came down and since it is all imported raw materials so they have to import the raw materials as a cycle of almost three to four months in the inventory pipeline, so they have done their mark-to-market of all their raw materials and the fiber their finished goods as of December 31, 2018 that is why this loss has happened and all that happen is market is growing up, so they will always at an advantage because the inventory pipeline would be there for three to four months so that advantage will come to the company. This was because in the reverse cycle I think there has been this commercial loss.

Kunal Shah: The second question is on the fabric margin you said they have improved somewhat versus 2Q is that the mainly because of an improved mix as in exports have done better than what they were last quarter?

Neeraj Jain: Export and domestic I do not think that is really big difference in the margins, so I think it depends upon how much capacity utilization they are in a position to do that and based upon that may be some product mix and some customer base so there is specific reason on the product mix has changed or the customer or the destination of the quantum is changed. I think there is a mixture of the cost saving initiatives, their product mix, their capacity utilization and so on.

Kunal Shah: Thanks. That is all from my side.

Moderator: Thank you. Ladies and gentlemen, as there are no further questions from the participants, I now hand the conference over to the management for closing comments. Thank you and over to you Sir!

Neeraj Jain: Thank you very much for all the support all of you have given to us. Though our numbers we have shown as a numbers are very strong for the Q3, we have given you the reasons and the advantages and disadvantages we created during this period, but I think in terms of the internal management and in terms of our internal cost cautiousness or in terms of finding opportunities wherever we can improve the yield margins, the management is really working hard to find out all those opportunities and lots of new ideas being generated by the team, so I think we are working very, very hard onto that and how the margins could be improved or sustained as well. So we once again thank all the investors and participants for this call who have always supported us and we try to give them the answer based upon our judgment and our thoughts and I once again thank all of you. Thank you.

Moderator: Thank you. Ladies and gentlemen, on behalf of IIFL Capital Limited that concludes this conference. Thank you for joining us. You may now disconnect your lines.