



“Salzer Electronics Limited
Q4 FY2019 Earning Conference Call”

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Moderator: Ladies and gentlemen, good day, and welcome to the Salzer Electronics Limited Q4 and FY2019 Earning Conference Call. This conference call may contain forward looking statements about the company, which are based on the beliefs, opinions and expectation of the company as on date of this call. These statements are not the guarantees of future performance and involved risks and uncertainties that are difficult to predict. As a reminder, all participant lines will be in the listen-only mode and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal the operator by pressing “*” then “0” on your touchtone telephone. Please note that this conference is being recorded. I would now like to hand the conference over to Mr. Rajesh Doraiswamy, Joint Managing Director and Chief Financial Officer. Thank you and over to you Sir!

Rajesh Doraiswamy: Thank you. Good morning everyone and thank you all for joining our earnings call for Q4 and full year ended March 31, 2019. I have with me Mr. Baskarasubramanian, Director (Corporate Affairs) & Company Secretary and Mr. Murugesh our Assistant Company Secretary, Ms. Savli Mangle and Mr. Smit Shah from Bridge Investor Relations. We have shared our results update presentation and I hope you all must have received it and gone through the same.

Our company started as a single product manufacturer, manufacturing CAM operated rotary switches way back in 1986 in India and over the years we have evolved from a single product manufacturer to a company that offers total complete customized electrical solution to all our customers. Our four state of the art manufacturing facilities are located in Coimbatore. We also have our in house R&D lab, which is recognized by the Government of India. Through all these initiatives, we have been able to bring in high quality products of international standards in India. Be it our association with Larsen & Toubro since 1993 to Plitron from Canada in 1995 or Trafomodern from Austria in 2016. We always focused on getting into new technologies that are not only niche, but also of great value. Through this focus and sheer determination to come out with products of highest quality we have been able to get a preferred vendor status with global giants like GE and Schneider. All our products are internationally certified. Though we are operating under the electrical and electronic product group for the ease of analysis, we have classified our businesses into four different divisions namely the industrial switchgear business, the wire and cable business, the building segment business and the energy management business.

Now coming to the developments that happened during the last financial year, two of our plants that is our magnetic wires plant and the wire and cable division received the prestigious PS16949 certification. This certification is prepared by the International Automotive Task Force and the Japan Automobile Manufacturers Association with the support from ISO. This technical specification in conjunction with ISO 9001 defines the quality management system requirements for design, development, production and relevant installation and service of automotive related products. This will enable us to enter a new sector of automotive across different segments adding newer innovative and high margin products and further diversifying our business in wire and cable. I am also happy to share that the promoters have increased their stake in the company. In fact the promoters have increased the stake from 25.9% in FY2016 to nearly 36% in FY2019. The credit rating of the company was upgraded by CRISIL to A stable from A- for the long term

borrowings and A13 affirmed for short term borrowings reflecting a leading market position in the domestic rotary switches market and an adequate financial risk profile. This is the second upgrade that we have received in three years from CRISIL. The Board of Directors has recommended a final dividend of Rs.1.6 per equity share for the financial year subject to the shareholders approval. Our company has been a dividend paying company since the last 19 years and the Board has approved and formalized a dividend distribution policy. Going forward all distribution of dividend will be as per this policy. I am also delighted to announce that we have entered into a definitive share purchase agreement with the promoters of Kaycee Industries Limited to acquire 72.32% shares in Kaycee Industries Limited on May 24, 2019. Kaycee Industries being pioneers in the CAM operated rotary switch product that will help further to increase our market share in the industrial switchgear industry and consolidate our market leadership in this niche product. This acquisition is in line with our strategy of strengthening and growing our suite of product offerings. The resulting synergy would enable us to connect it further into the market on the back of enhanced product offerings and additional distribution channels that comes along with Kaycee.

Now coming on to our Q4 and full year financial and business performance. Our financials for the current and the past quarters have been restated as per Ind-AS accounting guidelines. I am happy to share that we have registered an increase in revenue of 22% year-on-year at Rs.155 Crores for Q4 FY2019. Our revenue for the full year ended March 31, 2019 is at Rs.559.8 Crores as compared to Rs.442.8 Crores in FY2018, which is a year-on-year growth of 26%. The contribution from domestic sales at 86% was mainly driven by increase in demand and good traction for products in almost all our business divisions like the building segment, industrial switchgear and wire and cable business. During the year, our legacy products such as rotary switches and toroidal transformers have shown growth and uptick in demand along with other products like three phase dry type transformers and wire harnesses. The EBITDA for the quarter stood at Rs.16.9 Crores as compared to Rs.16.4 Crores in the corresponding previous quarter, which is a growth of 3% despite increase in raw material prices, which was managed by various value engineering ideas from our team. The EBITDA for FY2019 grew 19% year-on-year to Rs.63.6 Crores from Rs.53.3 Crores in FY2018. The profit after tax was at Rs.8.4 Crores in Q4 FY2019 as against Rs.4.9 Crores in the corresponding previous quarter. For FY2019 the PAT grew by 20% to Rs.24 Crores compared to Rs.20 Crores in FY2018.

Now moving on to the breakup of revenue as per the business divisions. Industrial switchgear division contributed 40% to the total revenues in this quarter and 41% in the full year FY2019. This segment has grown by 14% year-on-year in FY2019. Our new products of three phase dry type transformers, wire harnesses and others have continued to show growth and uptick in demand. The wire and cable division contributed around 49% of our revenues this quarter and 48.5% for the full year FY2019. From the start of this financial year, we have started to manufacture and sell wires and cables under the Salzer brand, which is seeing good demand and also seeing a growing opportunity here. This is apart from our regular brand labeling business that we are doing for Larsen & Toubro, Crompton and a few other large brands.

Moving on to the building product division, this business is the only B2C business that we have. Going forward we are confident of increasing contribution from this division in the coming two to three years to around 10% of our total revenue levels as it has opened up new opportunities in real estate sector for us where we have got some annual rate contracts with major builders. This division has contributed around 7% this quarter and 7.6% for the full financial year driven by increase in sales and good traction for our product offerings such as modular switches, MCBs, distribution boards, changeovers and Salzer branded wires and cables. We have also increased our focus on retail segment and are formulating strategy to further strengthen our presence in this segment. The fourth is the energy management division, which has contributed 4.1% revenue in this quarter and 2.6% in the full year. This is an order book driven business and this quarter we have been able to book revenues, which was due to us for the second year of the contract that we have been doing in Tamil Nadu.

Now coming to the balance sheet highlights for the financial year. The net worth of the company as on March 31, 2009 was at Rs.287.2 Crores. Our total debt as on March 31, 2019 stood at Rs.139 Crores. This has increased by Rs.4.4 Crores on account of increasing working capital requirements. Despite this increase in total debt we have maintained our debt to equity ratio at 0.48. Also we have improved our working capital requirement reducing the inventory days by 18 days and the overall working capital days by around 30 days. Our ROCE improved during the year to 16.7% in FY2019 from 15.2% in FY2018 an increase of nearly 150 basis points. We continue to focus on adding new high margin products under our product portfolio, reach out to new geographies and offer total customer solutions to our customers besides strengthening the revenue drivers, improving ROCE and working capital cycle also from the part of our core strategy. We are also working on system and process management to grasp better visibility on orders based on which we can plan our inventory level. The collaborative efforts taken internally will lead us to improve efficiency, reduce working capital and inventory levels. These initiatives will also improve our ROCE from the current levels to around 18% to 20% within the next two to three years. With a very competent team in place, we are confident of achieving the milestones we have set for ourselves. We are also constantly on the lookout for new opportunities and technical associations to strengthen the base of our product offerings. This is all from our side for now. I would once again like to thank everyone for your time and attention. We can now take questions.

Moderator: Sure. Thank you very much. Ladies and gentlemen, we will now begin the question and answer session. Ladies and gentlemen, we will wait for a moment while the question queue assembles. We take the first question from the line of Keshav K from IDBI Capital. Please go ahead.

Keshav K: Congratulations on the acquisition. Sir the first question was on the tax impact in this quarter, it is substantially lower than last year, so what is it over here?

Rajesh Doraiswamy: We had a deferred tax credit this year.

Keshav K: Because it changed where most of the PAT is driven by the lower tax impact so just wanted to understand over there and Sir the second question is on the acquisition, so on the valuation front

Sir just wanted your thoughts on the valuation because it seems like we have traded much more than what we are trading at today, so just wanted to understand the thought process behind acquiring the company and the price that you paid for it?

Rajesh Doraiswamy: To explain this a bit in detail, Kaycee Industries was the first company to manufacture CAM operated rotary switches in India, so it is a 70-year plus old company and they have been our main competitor for the last several years. They are number two in the market today, so the valuation that we have paid is considering of course the enterprise value of the company valued by the chartered accountants and investment bankers. Apart from that I think we also have to see the goodwill that the company brings in, in terms of their brand and the approvals that they have with various government agencies. So we consider all those things, I think the value that we have paid is quite normal.

Keshav K: Sir just to understand is there any excess capacity that Kaycee has?

Rajesh Doraiswamy: I think we believe Kaycee is operating at around 50% to 60% capacity levels.

Keshav K: Sorry I did not get that can you repeat?

Rajesh Doraiswamy: We believe that Kaycee is operating 50% to 60% capacity levels.

Keshav K: The next question is on Salzer Magnet Wires what will be the contribution of that this year?

Rajesh Doraiswamy: This year Salzer Magnet Wires contributed around Rs.65 Crores with an EBITDA of around 7.5%.

Keshav K: So majority of the growth driven this year has been through the Salzer Magnet Wires acquisition correct?

Rajesh Doraiswamy: I would not say so because I think around 12% of the growth came from our own products and the rest 12% came from Magnet Wires.

Keshav K: Sir in terms of project development, I think you were developing some energy management product as well and something for the electric vehicles as well, so any progress on that?

Rajesh Doraiswamy: Energy management product is already in place and I think we have already done projects and that is the revenue that we are realizing under energy management business, so that is already in place. On the electric vehicles, I think we are incubating the product and we are still in the development stage. We hope that the market also will pickup for EV segment going forward in the next two to three years, by that time I think we should be ready to take advantage of that.

Keshav K: Sir just to understand our thought process so while developing a new product is it that we have some fixed ROE and ROCE in mind that we are developing a new product because most of our recent products that we have developed over the last three years they have not really performed

up to our expectations till now, so is it that we have a fixed process in mind or how do we go about introducing new products into our portfolio?

Rajesh Doraiswamy: We always pickup products that is related to our line basically that is the first thing that we look at whether it forms part of the core of our capabilities. Secondly we always see that it gives an EBITDA of at least between 17% and 20% depending on the product and the product commodity. Thirdly I think in the last three years the products that we have all developed in my opinion I think it they there performing well. The only thing is any new product takes at least two to three years to stabilize and give growth, so both the three phased transformers and wire harness we have achieved almost Rs.20 Crores plus in the last two to three years on topline with an EBITDA of around 14% to 15% in both products and we hope that these two products to double going forward in the next two years at least.

Keshav K: In transformers our total capacity was around equal to Rs.1800 Crores am I correct?

Rajesh Doraiswamy: The market size in this product in India was Rs.1800 Crores.

Keshav K: So with the current capex that we have done what kind of demand we cater to?

Rajesh Doraiswamy: Around Rs.90 Crores is what we expect.

Keshav K: Is this also order book driven or how is this transformer business right now?

Rajesh Doraiswamy: No, it is not order book driven.

Keshav K: Got it. I will come back in the queue Sir.

Moderator: Thank you. The next question is from the line of Zaki Abbas Nasser an individual investor. Please go ahead.

Zaki Abbas Nasser: Congratulations on very good set of numbers I would say and also best of luck for your new acquisition. Sir I have two questions. One is the last quarter at least in terms of topline seems to have panned out pretty healthy, so would you fairly say that this would set the trajectory for the current financial year that is number one Sir and number two with your acquisition of Kaycee what are the synergies, what new products do they have and you mentioned that their capacity is working at 50% when can you be confident of ramping it up kind of stuff? Thank you.

Rajesh Doraiswamy: Thank you. For the first question I would say that traditionally the Q4 has always been good for us and for the industry as well because of various reasons and this has been the trend over several years, so having said that I am confident that definitely we are seeing a topline of at least between Rs.640 Crores to Rs.680 Crores for this year, so that means it is I think the strength will definitely continue. Both the Q1 may be a little lower, but we see that the growth trajectory between 15% to 20% coming up definitely for next year.

Zaki Abbas Nasser: This would be combining with taking Kaycee into account?

- Rajesh Doraiswamy:** No. We are talking about standalone unit.
- Zaki Abbas Nasser:** How would Kaycee work Sir, would it be a subsidiary or would you like to merge it with Salzer?
- Rajesh Doraiswamy:** Kaycee Industries is already a separate listed company and for now the idea is to run it as a completely separated listed company and it will be a 72% subsidiary for Salzer Electronics and the financials will be consolidated at the end of the year and on Kaycee Industries on the synergy as I told you that they have a topline of around Rs.25 Crores for last year with CAM operated rotary switch being the main product for them and they also have some new products that we do not have like toggle switches, water meters and counters. These are some of the other products that we get in addition. On the capacity and ramping up, I think we are yet to analyze the facility and the process that they are involved in, so it will take at least for us next two quarters to really see the status of the capacity utilization that they have and what ramping up we can do, but our feeling is that based on the analysis that we have so far done this is a good strategy that we are forming because Kaycee Industries being number two in rotatory switches business and by acquiring them and particularly Kaycee Industries is very strong in markets like Eastern India and also in Maharashtra where our presence is a bit lower compared to Kaycee, so this gives us additional geographical strength and also gives us additional distribution channels that Kaycee has apart from what we already have.
- Zaki Abbas Nasser:** Will you consider co-branding and things like that Mr. Rajesh because I believe their client is also pretty strong?
- Rajesh Doraiswamy:** Quite popular definitely yes and we are not really looking at co-branding as of now, but we will have to see how things pan out going forward. As of now we would treat Kaycee as a separate brand and Salzer as a separate brand.
- Zaki Abbas Nasser:** Thank you Sir.
- Moderator:** Thank you. We take the next question from the line of Shalu Asija from Invest Researcher. Please go ahead. Since we have lost the line for the current participant, we move on to the next question it is from the line of Vipul Shah individual investor. Please go ahead. Mr. Vipul Shah you may please go ahead with your question. Your line is unmuted. It looks like no response from the current participant. We take the current question from the line of Abhijit Sinha from Pi Square Investment. Please go ahead.
- Abhijit Sinha:** I just wanted to understand what kind of future growth expectations are we keeping and especially about the margin side because our interest expenses are also increasing and what kind of margins are we looking going ahead?
- Rajesh Doraiswamy:** On the growth we are expecting between 15% and 20% topline growth without considering the acquisition as a standalone company and we are confident of maintaining the EBITDA between 11.5% and 12%.

- Abhijit Sinha:** If we add Kaycee numbers in the data then what kind of topline growth can we see going forward?
- Rajesh Doraiswamy:** Actually topline is not very big. Kaycee's topline is around Rs.25 Crores, so that will add to us around 5% on the topline in the current levels.
- Abhijit Sinha:** This is surplus in the margin?
- Rajesh Doraiswamy:** Kaycee is also making a PAT margin around 4-5%, so basically Kaycee, Kaycee will help us in improving the bottomline for both Kaycee as well as Salzer.
- Abhijit Sinha:** Perfect Sir. Thank you so much.
- Moderator:** Thank you. The next question is from the line of Vipul Shah an individual investor. Please go ahead. Mr. Vipul Shah we have again unmuted your line. You may please go ahead with your question.
- Vipul Shah:** Good morning Sir. I am sorry there was problem in the line. Thank you very much for the opportunity. Just wanted to understand although you have given a bit of light on the acquisition and you have said that both these entities will remain listed is it for now or how do you plan it to take it forward this association?
- Rajesh Doraiswamy:** Right now we are acquiring 72% of Kaycee and we are going for open offer on that, so our plan is to keep it listed for now and keep it as a separate entity because the company also is a 70-year-old plus company manufacturing the product that we also manufacture and Kaycee as a brand also is very well known in the electrical industry and in all government projects Kaycee is an approved brand automatically, so we would like to capitalize on that because we are buying the company including the brand, so for now in the near future our idea is to keep it as a separate listed company as a subsidiary for Salzer Electronics.
- Vipul Shah:** How do we see the topline and bottomline of Kaycee per say going forward because in my opinion the valuations are not that cheap if my understanding is correct?
- Rajesh Doraiswamy:** Kaycee is a listed company. I think we are paying around 15% more than the current market prices.
- Vipul Shah:** On EBITDA front valuation front multiples?
- Rajesh Doraiswamy:** On EBITDA multiple if you see, we are paying approximately around eight times.
- Vipul Shah:** What is the growth potential in Kaycee per say that is the reason of my understanding, do we see a huge opportunity in the sense of growth coming in from Kaycee or how is it?
- Rajesh Doraiswamy:** In our opinion, I think Kaycee has been held by a large group called CMS Computers. It is a very large group and Kaycee kind of an unrelated business for the entire group and the business that

they were doing, so the management has not been that focused on this particular business and that is one of the reasons the company has not grown in the last seven years, so we expect that the company is a small company and very agile and hope that we can grow the company at a much faster pace than even Salzer.

Vipul Shah: That is great. That gives some clarity on it. As far as the products are concerned some of the products you have mentioned are there, which are not there in our portfolio and which are relatively newer products for them as well?

Rajesh Doraiswamy: For us, it is a new product. For them it is an old product.

Vipul Shah: For the product, which yields them the highest revenue there we are competing with them if I am not mistaken?

Rajesh Doraiswamy: You are right.

Vipul Shah: So how do we see that, will there be some kind of a cannibalization of brands or we will not be competing there is a product differentiation, can you explain this part please?

Rajesh Doraiswamy: Our idea is not to cannibalize and also not to lose market share for both the companies and that is one of the main reasons that we want to keep it as a separate brand and separate channel and what Salzer is doing should be a separate brand and separate channel, so in that way I think we will still compete in the market as two different brands, but we will not cannibalize each other and that is the part we are trying to form and that is how we are going to go to the market.

Vipul Shah: Will there be some kind of product differentiation between the two?

Rajesh Doraiswamy: Yes the product differentiation is already there.

Vipul Shah: Fair enough Sir. I hope this takes us to a new level and the next level of growth potential. Thank you.

Rajesh Doraiswamy: With all your wishes. Thank you.

Moderator: Thank you. The next question is from the line of Shalu Ahuja from Invest Researcher. Please go ahead.

Shalu Ahuja: Sir my question is what is your capex and debt position during this year?

Rajesh Doraiswamy: The working capital debt has increased by Rs.4.4 Crores, long term debt is actually come down.

Shalu Ahuja: Sir my question is regarding this FY2019-2020 what will be the capex and debt level?

Rajesh Doraiswamy: FY2019-2020 we are in the process of implementing a project for data cable so that will take a capex of around Rs.20 Crores apart from which we will do our regular maintenance capex of

around Rs.7 Crores to Rs.8 Crores. That will be the capex for this year and there will be an addition of debt of around Rs.14 Crores long term, which will go into the data cable project.

Shalu Ahuja: This is separate from this total Rs.14 Crores or Rs.27 Crores and Rs.14 Crores?

Rajesh Doraiswamy: No total Rs.14 Crores. The borrowings will be Rs.14 Crores.

Shalu Ahuja: Others will be internal accrual?

Rajesh Doraiswamy: Yes.

Shalu Ahuja: Sir what is the current market share and after acquiring Kaycee what will be the market share?

Rajesh Doraiswamy: For rotary switches, I think we were already enjoying around 20% market share. With the surplus of Kaycee I think we will be at around 35%.

Shalu Ahuja: Combining both?

Rajesh Doraiswamy: Yes.

Shalu Ahuja: Rotary switches and in any other company product?

Rajesh Doraiswamy: No I think Kaycee's major business is around 85.

Shalu Ahuja: Before rotary switches?

Rajesh Doraiswamy: Yes.

Shalu Ahuja: Thank you Sir. That is all from my side.

Moderator: Thank you. Ladies and gentlemen that seems to be the last question for today. I would now like to hand the floor over to Mr. Rajesh Doraiswamy for his closing comments.

Rajesh Doraiswamy: I once again thank all of you for your time and attention and look forward to see you again for the next quarter earnings call. Thank you.

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