CHAIRMAN'S LETTER 2022-23

During the year, our consolidated net worth increased by Rs.566 million, which increased the per share book value by 100%. Over the last sixteen years (that is, since the present owners took over) per share book value, has grown from Rs.35 to Rs.364 (Rs.440 after ignoring the effect of goodwill write-offs), which, after factoring in dividend paid during this period, works out to a rate of 16.9% compounded annually.

Over the years, I have been sharing annual updates with my business partners, the shareholders of Semac Consultants (erstwhile Revathi Equipment). Generally, these updates have been about the performance of the various businesses during the course of that year. I think it is helpful, from time-to-time, to be able to zoom out from the day-to-day and look at the bigger picture. Last year's commentary had some perspectives on how the Revathi and Semac stories have unfolded over a couple of decades. This year, I intend to share some thoughts on how I think about both businesses, going forward.

Unless there is a problem with corporate governance, shareholder value is driven primarily by two variables, i.e., year-on-year growth in earnings (profit after tax, not EBIDTA) and efficiency in capital utilization (as measured by return on capital employed, ideally unlevered, i.e., without use of much debt). Nature likes optimal utilization of its resources. Which is why, nothing is ever wasted in the natural environment. Business is also a natural system in a way. Hence, the same principles apply here as well. The more efficiently a business uses capital, the more valuable the business becomes. Generally speaking, due to the competitive forces a business faces, it is very hard to consistently deliver high returns on capital. Michael Porter's book, "Competitive Strategy: Techniques for Analyzing Industries and Competitors", first published in 2004 is a great read to understand why this is so. Therefore, it is rare to find businesses that consistently deliver high returns on capital despite growing profitability over long periods of time. Such businesses are valued very richly by investors. Rightly so.

Over the years, we have been iterating the various moving parts of both the businesses to try and find a method to deliver on the above two metrics consistently. Historically, we have failed miserably and I take full responsibility for that. However, this year (FY23), we have reached a point where all the hard work put in over the last five years has come to fruition. Of course, it is always a journey and the iterations will continue as we go along to keep refining the business model. This journey of iterating is usually filled with missteps, wrong turns, accidents, etc. Plus, the external environment (market, customers, competitors, suppliers, etc.) keeps changing. Which is why, one must expect metrics to bounce up and down. Ultimately, as the quality of management improves, the amplitude (of variability of the key metrics defined above) must go down.

This year was the first year when several things finally clicked in place to deliver the performance that the teams have delivered. Over the last ten years (FY13 to FY22), we were delivering a consolidated profit after tax of about Rs. 7-8 crores, which on a net worth of Rs.131 crores (FY13) would work out to a return on capital employed of about six percent. This climbed to an average profit after tax of Rs.10-12 crores over the last four years (FY19 to FY22), which on a net worth of Rs.161 crores would translate to a return on capital of seven percent. Rs.32 crores of profit after tax in FY23, on an average capital employed of Rs.222 crores translates to a return on capital of fourteen percent. Things are certainly looking up.

By the look of things, FY23 doesn't look like a one-off year like FY16. In other words, I expect some consistency in the profitability of the businesses going forward. Which means, we will aim to grow our year-on-year profit after tax by fifteen percent. It is entirely possible that some years may be way better (higher rate of growth) and some years may be worse. But if one takes a five-year view, one should be able to assume a rate of earnings compounding of about fifteen percent and a return on average capital employed of at least fifteen percent.

As you know, Semac has had a very difficult journey ever since the last of the Founders left in FY16. In the six years since then until FY22, we had three years where we lost money. If we aggregate the profit made in these six years, we lost money. As mentioned in last year's letter, the bad news ended in FY22. FY23 was the best year in the history of the company, which was founded, over five decades ago, in 1969.

It is a true Amrit Kaal moment. We are being propelled forward by a combination of global and local factors, none of which we have any control over. The big global factor is that the world is now looking for an alternate to China for their supply chain. Local factors include India having among the lowest corporate tax rates in the world, the government launching the production linked incentive scheme for several industries, cleaning up of bank and corporate balance sheets over the decade 2010 to 2020, introduction of the goods and services tax and better infrastructure (thus making movement of goods faster, making India more competitive globally), etc. We feel these factors have created a potent mix, which will see sustained investment in capacity expansion of Indian industry. Given industrial projects is squarely our playing field, we expect sustained growth in our business as well.

What did all this translate to, for our business, in FY23? While we booked record orders in FY22 (Rs.189 crores), we beat that record in FY23 by booking orders worth Rs.294 crores. Similarly, while our previous best in revenues was Rs.138 crores in FY19, we clocked Rs.330 crores in FY23. With such a big jump in Revenues, obviously, our profit after tax also jumped from our previous best of Rs.11 crores (FY14) and an average profit after tax of less Rs.3 crores over the past decade to Rs.20 crores this year – a 7x jump.

I am quite confident that our team is capable of continuing this performance in the coming years. Again, nothing in life is linear and therefore there are no promises of a straight line sloping upwards from left to right. That said, the line will slope upwards over time and we should be able to grow our profit at fifteen percent annually and achieve a return on capital employed of at least fifteen percent.

Some of the initiatives we are working on to deliver this outcome include setting up of a procurement team to improve our margins, collaborating with the best minds to reduce project cost for our clients, strengthening our existing teams in all areas to build a foundation for the growth that we see ahead. And of course, improving our systems to make our business more robust.

Last year, I had mentioned that our business does not need much working capital. I would like to clarify that while we do not need working capital as commonly understood, we do need to place money into bank fixed deposits to secure bank guarantees. As our business grows, this need will only grow. Hence, one must assume this as being part of working capital. We should be able to fund our growth plans through internal accruals without needing any significant bank debt or diluting equity. However, if the growth rate accelerates beyond our expectations, we will need to raise some capital, most likely through the usual banking channels.

I had mentioned that we are in the process of getting

Semac listed independently. That process is almost complete, and we are finishing the final steps. I expect listing to happen within the second quarter of FY24. It has taken longer than we had anticipated. Thankfully, we are now towards the end of that journey.

I expect this listing to bring greater visibility in the quality of the two businesses, Semac and Revathi, and for the market to evaluate them independently of each other. I am hopeful that this step will help better price discovery and consequent unlocking of shareholder value.

The teams in both businesses have worked sincerely and diligently to deliver the above results in our seventy fifth year after Independence to launch us into Amrit Kaal. I feel happy with the progress made so far and am excited to see how the future unfolds. While there will be surprises, overall, I expect the journey to be much happier than the past decade. All this will only be possible if we have the right team, which is aligned and motivated to achieve ever higher goals. I have my job cut out for the next five years

MR. ABHISHEK DALMIA
Chairman and Managing Director
DIN: 00011958

PLACE : New Delhi
DATE : 29.08.2023

ACQUISITION CRITERIA

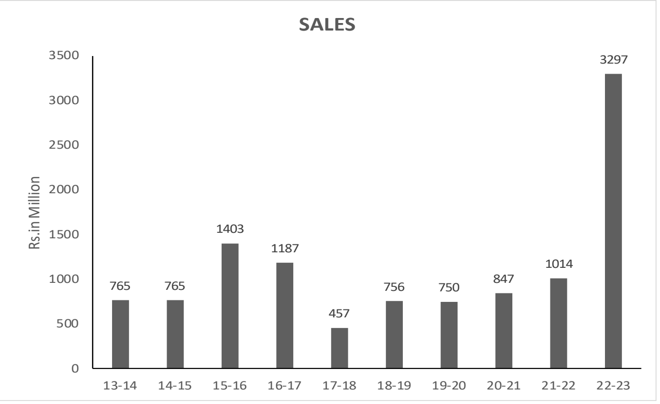
We use this space to communicate with potential sellers and their representatives, what we look for in a potential acquisition. If you, the reader, have no personal connection with a business that might be of interest to us but have a friend who does, perhaps you could pass this message on to him.

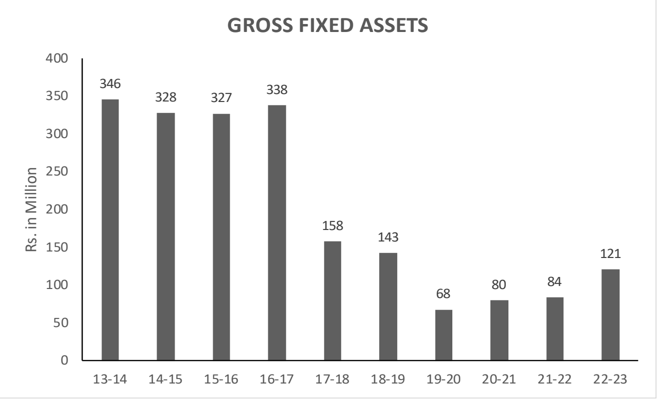
Here's the sort of business we are looking for:

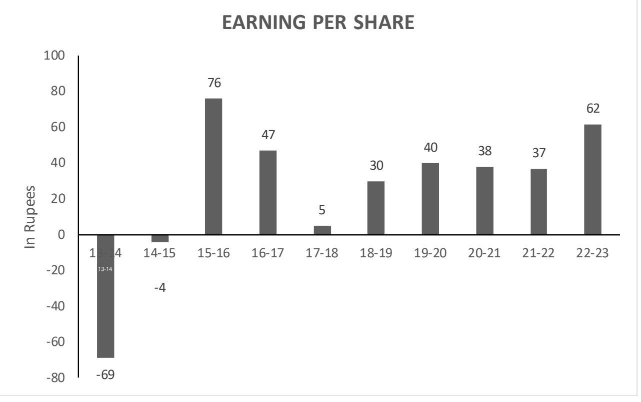
1. Enterprise value in the region of ₹ 100 crores (₹ 1 billion),
2. Demonstrated consistent earning power (future projections are of little interest to us, nor are "turnaround" situations),
3. Businesses earning good returns on equity while employing of no dept
4. Management in place,
5. Simple businesses,
6. An offering price.

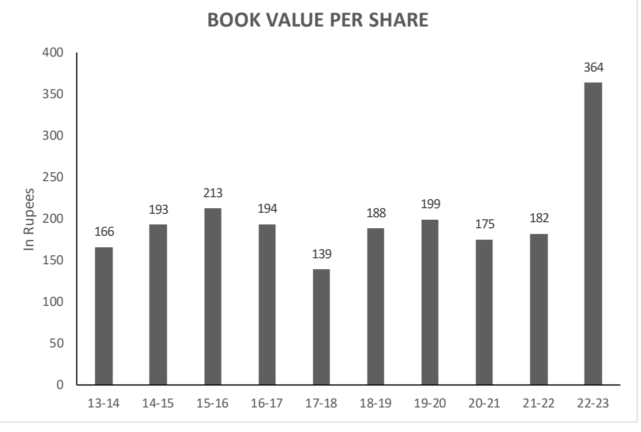
We will not engage in unfriendly takeovers. We can promise complete confidentiality and a very fast as to whether we are interested. We prefer to buy for cash, but will consider issuing stock when we receive as much in intrinsic business value as we give.

Our favorite form of purchase is one where the company's owner-managers generate significant amounts of cash, sometimes for themselves, but often for their families or inactive shareholders. At the same time, these managers wish to remain significant owners who continue to run their companies just as they have in the past. We think we offer a particularly good fit for owners with such objectives. We invite potential sellers to check us out by contacting people with whom we have done business in the past


SALES
Rs.in Million
3500
3000
2500
2000
1500
1000
500
0
765
765
1403
1187
457
756
750
847
1014
3297
13-14
14-15
15-16
16-17
17-18
18-19
19-20
20-21
21-22
22-23


GROSS FIXED ASSETS
Rs. in Million
400
350
300
250
200
150
100
50
0
346
328
327
338
158
143
68
80
84
121
13-14
14-15
15-16
16-17
17-18
18-19
19-20
20-21
21-22
22-23


EARNING PER SHARE
In Rupees
100
80
60
40
20
0
-20
-40
-60
-80
-69
-4
76
47
5
30
40
38
37
62
13-14
14-15
15-16
16-17
17-18
18-19
19-20
20-21
21-22
22-23


BOOK VALUE PER SHARE
In Rupees
400
350
300
250
200
150
100
50
0
166
193
213
194
139
188
199
175
182
364
13-14
14-15
15-16
16-17
17-18
18-19
19-20
20-21
21-22
22-23