



“IFGL Refractories Limited Q3 and 9 Months FY18 Earnings Conference Call”

February 14, 2018



**MANAGEMENT: MR. KAMAL SARDA – CEO, IFGL REFRATORIES
LIMITED**

Moderator: Good morning, ladies and gentlemen. Welcome to the IFGL Refractories Limited Q3 and 9 Months FY18 Earnings Conference Call. This conference call may contain forward-looking statements about the company, which are based on beliefs, opinions and expectations of the company as on the date of this call. These statements are not the guarantee of future performance and involve risks and uncertainties that are difficult to predict.

As a reminder, all participant lines will be in the listen only mode and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal the operator by pressing “*” then “0” on your touchtone phone. Please note, that this conference is being recorded.

I now hand the conference over Mr. Kamal Sarda – CEO IFGL Refractories Limited. Thank you and over to you, sir.

Kamal Sarda: Thank you, good morning everyone. On behalf of IFGL Refractories, formerly known as IFGL Exports Limited, I warmly welcome you all to the Earnings call of Quarter 3 and 9 Months FY2018 financial results of our company. I have with me today Mr. Pratik of SGA, our Investor Relation Advisors. I hope you all have got a chance to go through the investor presentation which is uploaded on the stock exchange and our website.

Let me give a small brief on the industry. On the global front steel utilization rates are expected to increase up to 86% by FY20 from the current level of 77%-78%. Increase in utilization rates will also lead to an increase in refractory demand thereby benefitting global players like us. Indian market share in the global steel production is expected to rise from 6% in 2016 to 7% by 2020. This is further aided by favorable policies enacted by the government. Such as, imposition of anti-dumping duty on various steel products which shall be applicable till 2021 and 2022.

The budget for the current year 2018-2019 was also very positive for our industry. The budget has a strong focus on infrastructure creation including rural electrification, housing and roads. With the increased spending on infrastructure of around Rs. 600,000 crores the sector is being pegged as a key growth driver. This will boost the manufacturing sector and also help create demand for steel and cement sectors which are primary consumer of refractories.

Refractory manufacturing in India is likely to get a boost from rationalisation of custom duty on refractory items. This is done in the current budget. The custom duty on refractory item has been increased from 5% to 7.5% in the budget this year. With this the effective basic customs duty on refractories have increased from 5.15% to 8.25%, thus meeting a long-standing demand of the industry. This will provide much-needed impetus for growth in the coming financial years and future also.

Strong global prices coupled with steel import restriction measures are likely to protect margins for the domestic steel manufacturers. Further domestic steel players have also announced expansion of their capacities which will further boost the demand for refractories domestically. With the global steel industry expected to pick up and the domestic industry also looking very good. Refractory industry is expected to be in a good shape going forward.

I am now giving you a brief on our financial performance of quarter 3 and 9-months ended FY18. On the IFGL consolidated level for the 9-months FY18 total income stood at Rs. 610 crores up by 8% year-on-year. EBITDA was Rs. 76.3 crores with a margin of 12.5%. Goodwill which was created on merger of two companies was written off to the tune of Rs. 20 crores for this 9-months. PBT was Rs. 41 crores and cash profit was Rs. 69 crores.

On IFGL India standalone performance the 9-months total income was Rs. 322 crores up by around 20%. EBITDA was Rs. 52 crores up by 30% with the margin of 16%. Goodwill again was written off in these books only about Rs. 20 crores. PBT was recorded at Rs. 21 crores showing a growth of 115% Y-o-Y with a PBT margin of 6.6%. Cash profit was Rs. 49.5 crores Y-o-Y growth of about 33%.

With respect to our International businesses:

EI Ceramics- total income in 9-month was \$ 12.5 million with an EBITDA of \$ 1.88 million and a margin of 15.1%, while PAT was \$ 1.14 with the margin 9.1%.

Monocon, our UK subsidiary with its own group subsidiary companies - 9-months total income was £18.94 million representing a growth of 5.7%. EBITDA stood at £ 1.45 million at 7.7% while PAT was about £1.02 with a PAT margin of 5.4%.

Hofmann Ceramic our German subsidiary under performed during 9-months period the total income was 7.34 million Euro. It had a very nominal small loss of 0.16 million Euro. The CAPEX towards capacity increase, automation, efficiency enhancement is on track and will be most likely be completed in first quarter FY19..

So, this is in nutshell about the Group and the industry and I will be happy to take any questions and answers.

Moderator:

Thank you. Ladies and gentlemen, we will now begin the question and answer session. We will take the first question from the line of Udit Bokaria from Catamaran. Please go ahead.

Udit Bokaria:

Sir, you were mentioning about the steel industry growth in India. So, just wanted to understand like what is your view like is it large integrated players that will be growing faster than the industry or you see that the small steel players getting benefited from the budget and they will grow at a faster pace and the second question is sir, when you are speaking about global steel demand growth, are there any particular countries in South East Asia where you believe that is expanding very fast and the steel demand will grow from their?

Kamal Sarda:

On your first question on Indian steel industry, I think major growth will come from the integrated belt. So, you must have seen all the expansion happening in SAIL, Tata Steel, JSW and like, those are integrated steel mills. Having said that the medium steel mills with the Electric Arc furnace will also grow but the major quantum will come from the integrated steel

mills. And on the international front Middle East segment is growing now at a faster pace than it was about a year back. The reason being the oil prices have gone up from \$ 30 to about \$ 70. So, they now have again come back to a good cash surplus situation. Like all the Middle East region there is a growth in all other neighboring countries. Iran will grow much faster than any other country in that segment. So, in all those areas -the steel plants which were like either shelved or stopped or held for the time being will again start reviving. So, overall, I think the steel industry is poised to grow, so this is the first time if you look at the 9-months steel figures from the World Steel Organization all the countries have shown a positive steel growth Y-on-Y. So, this is a good sign I would say.

Udit Bokaria: Sir -in our revenue mix like how much is it coming from flow-controlled devices and how much from advanced refractories in the domestic business?

Kamal Sarda: You are talking of the terminologies which usually used by Vesuvius. The Vesuvius has a big flow control and the big advanced refractory. I would say we are not like that but yes, if I am trying to use the same terminology our major part of the business is flow control, having said that we also have non-flow control refractory which does not fall in the advanced refractories also in the Vesuvius terminology or parlance.

Udit Bokaria: And sir like, so are there any like since the commodity prices which is used for refractories are increasing, right. So, how are you negotiating with your customers and like how will it impact the gross margins for the refractory industry in general?

Kamal Sarda: It is a continuous process. This is something which I cannot tell you offhand. It is a continuous process.

Moderator: Thank you. The next question is from the line of Zain Iqbal, an individual Investor. Please go ahead.

Zain Iqbal: I just wanted to know the key business metrics or operational matrix which you track on a going basis which tells you the condition of the business. Like if you were to stay away for 1 year and you want to check how your business is doing which key matrix would you track operationally?

Kamal Sarda: We supply consumables to refractory industry. So, ours is the consumable product for the steel industry. So, the only matrix which is applicable to us is the growth in the steel industry. So, there is no way I can say that this one year I will stay away from this particular sector that particular sector. The other key factor would definitely be the health of the particular steel plant. So, depending upon that health of the steel plant whether they are in a position to pay us back or not, that is the another key factor which we see basically the growth in the steel industry and the health of a particular company that is the 2 key factors which we are going to look at.

Moderator: Thank you. The next question is from the line of Amritha Vivek from iThought. Please go ahead.

Amritha Vivek: My question is with regard to the shaped and unshaped products produced by your company. So, if you look at the standalone numbers it is about 88% of shape to 12% of unshaped in FY17. Now in FY16 the portion of unshaped was about 0.3%. Sir, now this is gone up to about 12% in FY17 not sure this is solely attributed to the merger. My first question is are there any plans to increase the share of unshaped refractories in the coming years and two I also wanted to understand the breakup of shaped and unshaped as a consolidated level and my last question is with regard to the infrastructure. So, just wanted to understand the possible extent of switch ability between the two products that is the same infrastructure can be used to produce the two products?

Kamal Sarda: One and first and foremost question you are asking this question because this is the first balance sheet post-merger. So, the March 2016 figure which is there on the printed balance sheet which is available is not comparable with March 2017 figures. So, March 2016 figures you can take the standalone numbers as per the previous annual report and add the March 2016 figures which is the erstwhile IFGL Exports figures and eliminate the intercompany transaction by doing that related party schedule if you look at and you can see the sale purchase. You will come to a particular figure. So, the shaped and unshaped figures in March 2016 in the March 2017 annual report is not comparable. Our matrix has not changed in these two years. That is number one question. Number two, honestly speaking we do not share these data on a wide basis. Number three, the manufacturing facilities cannot be switched between the shaped and unshaped. We have enough capacities in both the segments, so I think switch ability is not so easy, or in fact maybe it is not possible, and we have enough capacities in both the segments.

Moderator: Thank you. The next question is from the line of Brij Shah from Brij Shah & Associate. Please go ahead.

Brij Shah: Sir, I have couple of questions. First, is there any write-off during this quarter?

Kamal Sarda: Yes, we have a provision policy for receivables. So, this is definitely a continuous process and this quarter has been slightly higher than the normal.

Brij Shah: So, sir can you just throw some light regarding how much increase in the write-off in terms of percentage?

Kamal Sarda: I do not have the percentage handy. But our internal control procedures are strong, whereby if the outstanding's are above a particular limit we have to provide for it. So, unfortunately this quarter on a standalone basis there has been a slightly higher write-off and one of the reasons for the lower profit is that. But let me also tell you as a rider, big chunk of that write-off which we took in December 2017 quarter we have received in this current quarter. So, possibly there will be a sharp reversal of those provisions in the current quarter.

- Brij Shah:** And sir with respect to Hofmann, has there been any significant under performance this year. So, can you throw some lights on that
- Kamal Sarda:** There was no significant under performance, there was one particular product group which was a highly profitable product group for us. The demand for that product group in this current 9-months was substantially lower, number one. Number two, as it is you must have seen in the last few quarters we have announced that we are going in for CAPEX there for operational efficiency improvement and productivity improvement. This plant was a pretty old plant. Obviously, the cost of production is slightly higher. The margins are very wafer-thin margins as it is for Hofmann. So, this CAPEX will get over by say, I think latest by first quarter of FY19 and we see the operational efficiency improving there. We will see a positive in fact we are looking at a positive in the quarter 4 also. Definitely going forward FY19 should be a better one. The product which I was mentioning I think is showing a sign of improvement as far as uptick is concerned. So, hopefully the next FY19 financial year should be a better year but yes, it is bit of a concern as of now.
- Moderator:** Thank you. We will take the next question from the line of Pritesh Chheda from Lucky Investment Managers. Please go ahead.
- Pritesh Chheda:** Sir, just few questions on the EBITDA performance from the 9-month basis. So, if you see the standalone operation has growth in EBITDA and that entire EBITDA seems to have been eaten away by the declining EBITDA of the international operations. So, my first question is on the standalone operations, is the EBITDA growth largely driven by IFGL Export merger because I think that is where the capacity is, one, and what would be the color of EBITDA growth on standalone operations next year and second how do you improve the EBITDAs on the international operations or what are the drivers and what should be EBITDAs look like in the international operations?
- Kamal Sarda:** There are too many questions into it. I would say some of the questions I would try to answer. On a standalone basis the top line has grown by about 16%. So, that is a good growth if we take net of excise duty, these are not comparable pre-GST and the post-GST, net of excise duty sales has grown by 20%.- EBITDA has grown by 30%. So, you can imagine there is slight improvement of EBITDA. You are right the growth in the erstwhile IFGL Export plant which is the Kandla plant has been quite good. So, margins in Kandla plant were good number one. Number two the product range which we make in Kandla there has been a significant growth in the top line. So, there the margins are slightly higher. Number three, obviously Euro has been favorable as compared to the last financial year. You must have seen Rupee has depreciated vis-à-vis Euro. So that also favored us in the first 9-months this financial year compared to the last 9-months which is in fact a comparable figure. On the international front, I would say there has been some small issues as I mentioned Hofmann in my previous questions, I do not want to repeat it again. EI Ceramics has slightly marginally dropped because the first two quarters in the last financial year were slightly comparatively better, to that there was a very less uptick. For now the company looks to be doing very well. For

Monocon, the margins go high when we sell some equipment. So, this year overall the equipment off take has been slightly lower because steel plant had withheld all CAPEX in the last 1-1.5 years. So, hopefully in the next financial year FY19 the equipment sale would be good, and we are also doing some restructuring in that company. So, the margins in that company should also good. Overall, the currency situation is getting better now. So, hopefully the currency effect in the first 9-months will be a positive sign in the first quarter and going forward. So, this in a nutshell, things look this way.

Pritesh Chheda: Sir, just to clarify your view foresees that international operation recovers the loss margin next year and international operations mirrors the volume growth of the respective territory?

Kamal Sarda: Yes.

Pritesh Chheda: My second question on the IFGL Export side what kind of traction do you see next year?

Kamal Sarda: There is no IFGL Exports now. It is IFGL Refractories Limited now. It is a merged company, so it is only one company, so we will not talk of two different. IFGL we see a reasonable growth in coming quarters also.

Pritesh Chheda: Similar to what you have seen in the first half?

Kamal Sarda: We honestly try to avoid giving any kind of forward-looking statements. But I would say that we should be doing better compared to quarter 3, we feel quarter 4 should be very good and hopefully we can continue with similar kind of growth of FY17 in FY18 also.

Pritesh Chheda: So, just one clarification the standalone operation how much of it is domestic business driven?

Kamal Sarda: The domestic will be anywhere around 45% and 55% will be exports. Anywhere between 43% to 45%.

Pritesh Chheda: And are there any margin levers in domestic operations?

Kamal Sarda: They are slightly different. Dynamics are different, but if we look at overall logistics cost of transferring the material from our warehouse to their warehouse plus the commission agents, the selling agents, selling cost there are slightly higher. So, margins would vary but definitely the international margins are slightly better than the domestic margins.

Pritesh Chheda: My question was can the margins rise are there any drivers to the current margin of 16% that you have reported, are there any more drivers to that margin?

Kamal Sarda: No, specific drivers.

Moderator: Thank you. The next question is from the line of Abhisar Jain from Centrum Broking. Please go ahead.

Abhisar Jain: Sir, the question is on the standalone business. So, I think Q3 has been a subdued quarter wherein we have seen sequentially quite a large dip in the absolute EBITDA number despite the similar amount of top line. So, almost Rs. 8 crores dip. You mentioned sir in your comment previously that there was some excess provisioning also which is sitting in the other expenses. Sir, can you quantify that amount and is there anything else also which is led to this drop and you expect this to improve now going forward?

Kamal Sarda: See, there are few things, there is not only one thing which is there, the last question was on higher provision. So provision, I think you are not wrong I think anyway between Rs. 2.5 crores to 3 crores is the excess provision which we have taken in the December quarter. And as I mentioned possibly we will have a reversal of some of these past provisions in quarter 4. But on top of it there was a very high raw material price increase in the last 6 months and the last quarter and of course this current quarter also we will see a very high raw material prices to be absorbed. Price increase takes time, so price increase did not happen so much in December quarter. Hopefully, there are few customers who have agreed for price increase, so we will see some positive sign in the quarter 4 and coming months. So, also there was some quality issues in our plants we had to go for some sort of rationalizing our manufacturing processes. So, 3-4 issues put the quarter profitability absolutely down. But I hope the quarter 4 we should be doing pretty good. Overall on the 9-month basis I think the profitability is much better than previous 9-months.

Abhisar Jain: And sir just on this point of the raw material price increase getting pass through, so is there a divergence in you be able to get the price pass through in domestic and export is one market better than the other by any chance?

Kamal Sarda: See, for us domestic market has a different ball game. Domestic market you are all talking in Rupee terms. When you import in Rupee you sell in Rupee, import in Dollar and you sell in Rupee. So, dynamics is different. So, passing through happens only if the customer gives you a price increase. But fortunately, and incidentally for us Rupee has weakened over the last few months and our major sales are in Euro. So, we got some benefit out of that partially the price increase is getting offset against the Rupee depreciation vis-à-vis Euro, I would say. So, basically Euro appreciating vis-à-vis Dollar that is the major thing which has happened. So, obviously if the margins is compared to domestic in the last few months and maybe in the current quarter also, things have gone better in overseas compared to domestic, which has improved due to the exchange rate fluctuations. But pass on is happening, as the steel plants are now in the process of giving the price increase to anyone because for them availability of refractory is more important than price increase.

Abhisar Jain: Yes, actually sir, I was just coming to this point because we have seen a slight divergence in the gross margin performance of your company and your competitor Orient Refractory which is also servicing largely the domestic mills to the extent of 70%-75% and that too smaller ones. So, they were also cautious on the raw material price increasing and the pass-through, but they were mentioning that the pass-through has been signaled. So, but in their results, there has

been a gross margin expansion in this quarter whereas, we have seen a slight dip, but I am not too concern about sequential movements in specific companies but from a directional point of view you feel that Q4 we should be in a better position in the gross margin front, right?

Kamal Sarda: Yes.

Abhisar Jain: And sir from the expansion point of view which we are doing in both Kandla and Odisha, when it will be completed, we expect the revenues to start flowing from those new lines.

Kamal Sarda: I think it would be next financial year.

Abhisar Jain: Sir but any rough idea of whether it will be more H2 FY19 or will it start in H1 FY19 also?

Kamal Sarda: It is a gradual process, some of the equipments in fact for Kandla expansion we are almost through. So, in this quarter we will complete the expansion there in Kandla. We will start looking at the expansion getting used from 1st quarter itself in fact we will see something in the current quarter also. Rourkela we will see in fact we start seeing in the H1 only. But how much the market takes it has to be looked into we believe. It all depends on the market scenario. So, I think we will see some better results in Q4 and also going forward.

Moderator: Thank you. Ladies and gentlemen, that was the last question, I now hand the conference over to Mr. Kamal Sarda for his closing comments.

Kamal Sarda: Thanks a lot. I think gentlemen and ladies, we have had a good question-answer session and I hope I have been able to answer most of your queries. We look forward to your participation in the subsequent quarters. If you have any further queries, you may contact our Investor Relation Advisors that is Strategic Growth Advisors. Thank you all have a nice day.

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