



Praj Industries Limited

Transcript of Q3 & 9MFY14 Earnings Conference Call February 07, 2014

- Moderator** Ladies and gentlemen good day and welcome to the Q3FY14 Earnings Conference Call of Praj Industries. As a reminder all participants' lines will be in the listen only mode. There will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during this 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 Ms. Vinati Moghe from Praj Industries. Thank you and over to you.
- Vinati Moghe** Good morning everyone. We welcome you to this conference call organized to discuss Praj Industries' operating performance and financial results for Q3FY14 which were announced on Wednesday. I have with me Mr. Gajanan Nabar – CEO and Managing Director with Mr. Surendra Khairnar – Assistant Vice President (Accounts).
- Before we begin I would like to mention that some of the statements made in today's discussion may be forward-looking in nature and may involve risks and uncertainties. Documents relating to our financial performance were e-mailed to all of you earlier, these documents have been posted onto our corporate website. I would now like to hand over to Mr. Nabar for his opening remarks.
- Gajanan Nabar** Good morning everybody and thank you for taking the time to join us on this conference call for Q3 results of fiscal 2014.
- This is the first call to all of you from our new head office in Hinjewadi in Pune and my extreme apologies for a little bit of delay, this is an aspect of moving office and changing phone numbers. So please accept my profound apologies for a little bit of delay. We are also pleased to share that we have now adorned a new identity which is translated into change in our logo as has been communicated to most of you. The change in the identity was in response to our expanded portfolio of businesses and changing customer landscape on a global basis. It was also on the basis of the feedback that we have received from many of you. The change also heralds new energy within the company in the face of challenging times.
- We have maintained in our earlier calls that our second half for fiscal 14 will be better than the first half and we are happy to share that our numbers of Q3FY14 are in the right direction. We have also focused on operational excellence which can be seen by overall improvement in EBITDA margins.

We will cover our numbers in a little bit but first let me share the highlights of Q3FY2014. The Indian investment climate showed some silver lining but the investment confidence is yet to show signs of improvement. This being an election year, we are mindful of the fact that investment would come in for reconsideration and we have taken adequate steps to increase our focus further on export markets, not only for Ethanol and Brewery but also for emerging business. We are seeing some results of that in the emerging segments with increase in the export component. US and EU have both seen improvement in the economic parameters. While in the US we have seen investments taking shape especially driven by Shale gas activities, we are yet to see the same level of interest in EU. Latin America, South East Asia and Africa remain our best performing regions and going forward, we expect these regions to perform well as far as demand creation is concerned. During the third quarter, emerging businesses consisting of water, wastewater treatment, process equipment & systems and high purity systems saw good movement.

On the domestic Ethanol business, you may be following the Indian Ethanol blending program keenly, the Maharashtra State government has agreed in principle to discuss a move to E10, to help boost the sugar industry whereas the state run oil companies have set benchmark price for procuring Ethanol for blending with petrol at Rs.44 per liter. Thus, OMCs and sugar mills need to come to a consensus as far as the Ethanol price is concerned. Additionally, the Empowered Group of Ministers have also recommended moving to 10% blending, but in our reading the 5% blending needs to be fully implemented before supply of 10% can be committed. The Ethanol blending program has resulted in higher alcohol prices, increased interest in new capacity creation, also distillers dried grains which forms a part of the animal feed inputs is also seeing an increased demand and the prices are hardening. Grain distilleries are seeing a better profitability due to this.

On the international ethanol front, there have been some mixed developments. Countries like Argentina and Colombia are talking of increasing ethanol blending mandates while South Africa starts blending in the year 2015. So they need to start the preparation for capacity creation. Argentina which is currently at E7 is already discussing to increase the blending mandate to E12. In the US, scaling down of RFS2 volumes will have an impact on the global Ethanol trade. We need to see and study in which direction the trade will move. Brazil continues to import ethanol from the US, the supply quantity remains inadequate to serve the 25% blending target of Brazil.

We have made progress on the 2G Ethanol commercial sized demo plant, we are now working on the 'bolt-on' model for second-generation ethanol plant in India. The technical evaluation for the same is completed and MoUs are signed with identified client. This will help to address the requirement of existing global clients who have shown an interest in 2G program. We have evaluated three different models for our 2G demonstration program; one is a 'bolt-on' model, a Greenfield model in India and another for the European markets.

Now, a briefing on our financial performance. The consolidated income from operations was Rs.269.1 crore in Q3FY14 as compared to Rs.194.2 crore in Q2FY14 and Rs. 233.93 crore in Q3FY13. The revenue numbers for cumulative three quarters for FY2014 is at Rs.636.4 crore, the detailed breakup of the same will be available in the presentation on our website. EBITDA was Rs. 35 crore in Q3FY14 as compared to Rs. 9.32 crore in Q2FY14 and Rs. 25.84 crore in Q3FY13, which is an improvement of 38% over the corresponding quarter. We have made specific efforts to improve the quality of the orders at intake stage as well as value engineering during the execution phase. PBT is at Rs.33.61 crore in Q3FY14 as compared to Rs. 7.85 crore in Q2FY14 and Rs.29.38 crore in Q3FY13. Profit after tax stands at Rs.24.27 crore in Q3FY14 as compared to Rs.6.47 crore

in Q2FY14 and Rs.24.22 crore in Q3FY13. PAT has remained constant largely on account of normal rate of tax for Neela Systems. Neela's PBT has gone up from Rs.3.9 crore in FY13 corresponding quarter to Rs. 6.2 crore for the first nine months. The revenue of Rs. 269.1 crore comprises of export of 52% and domestic business of 48%. Ethanol business forms 67%, brewery business 6% and emerging business of 27% of revenues. The order backlog as of December 2013 is at Rs.875 crore out of which domestic business stands at 52%, Ethanol business forms 67%, brewery at 12% and emerging businesses form 21%. In keeping with prudent practices, orders amounting to Rs.50 crore, which are showing inadequate movement, have been removed from the order book. They will be reinstated as and when there are signs of improvement. The order backlog of Neela System stood at Rs.63 crore. The order intake for Q3FY14 at Rs.203.2 crore has been consistent with a good mix of international orders. Out of the total order intake, 25% constitute of the international orders and 36% of the fresh orders received during the quarter are from emerging businesses. Thus, we are in line with the stated objective that emerging businesses will contribute to 30% of our top line. During the quarter, Praj has formed a wholly owned subsidiary namely Praj Industries Namibia Propriety Limited in Windhoek, Namibia to serve the company's business interests in the region. Mr. Pramod Chaudhari was conferred the prestigious "Bio Spectrum Leadership Award" for his contribution to the biofuel industry and his continuous focus on green and clean energy.

To commemorate 30 years of Praj, the Board has recommended an interim dividend of 30% that is Rs.0.6 per share and has fixed February 14, 2014 as the record date for the payment. With this, ladies and gentlemen we will now take the questions.

- Moderator** The first question is from the line of Bhalchandra Shinde from Batlivala & Karani Securities. Please go ahead.
- Bhalchandra Shinde** Sequentially, in the last few quarters there was a decline. However, in December quarter there is good growth but are we seeing improvement on the investment cycle or the customer deferments??
- Gajanan Nabar** We are a project company. Please do not judge us on a single quarter. We need to look at our performance on a longer period. Orders and projects keep moving in and out of the quarter. So, the entry point of some orders that we got in the last fiscal or the last six months has resulted in a better performance in Q3FY14.
- Bhalchandra Shinde** What is the overall execution cycle for your consolidated order book?
- Gajanan Nabar** Since we are now into multiple businesses, every individual business runs on a different time cycle. for Ethanol and Beer is in the range of 12 to 15 months, CEPS is between 8 to 9 months, wastewater varies from 6 to 9 months and high purity water which is Neela is from 3 to 5 months. So, it is very different and they all run on different project life-cycles.
- Bhalchandra Shinde** Can you give guidance on the order intake and order book for the next 12 to 18 months?
- Gajanan Nabar** In India, there has not been any dramatic change as everybody is waiting for elections, so the investment cycle remains the same. But we are now seeing some traction for new businesses. Also, international brewery business has caught on because we have two large orders from Heineken and SABMiller, some of those new things have happened for Praj but overall I think the climate still remains sketchy.

- Bhalchandra Shinde** Is it fair to assume that order intake may stay flattish or muted for the next 12 to 18 months?
- Gajanan Nabar** We are not only optimistic but we are also prepared to mitigate the situation in the market by bringing innovative options or solutions to the market and looking at different business models. But as per the practice, I do not want to give color to how we are seeing, we remain optimistic. All the indications are that we would have a good order book going forward but time to time we will inform all the investors and if we receive some specific large orders, we bring it to the investors' notice immediately.
- Bhalchandra Shinde** Out of the total order intake, 25% was international, that implies that the domestic orders were high. Are we seeing good traction on the alcohol and the beverage side or water and wastewater?
- Gajanan Nabar** We are seeing traction on the brewery side. In India for the last 15 months there was not much movement on the project execution. But, on the brewery side we are certainly seeing that movement happening. We are also seeing interest because of the blending program and due to the talk of higher blending, there is some bit of excitement in the Ethanol domestic market as well. We are also seeing similar excitement in the international market, it has always been sporadic. The good part of Praj is that we are able to cater to the requirements in any part of the world, it could be Sierra Leone in Africa or it could be Hull in UK and we can cater to those requirements. So, we remain very vigilant about the opportunities going around the world and water, wastewater and CEPS are showing good traction. So it is a mixed bag.
- Bhalchandra Shinde** Regarding the high return on blending, the government is planning to increase it to 10% but what is the current capacity of Ethanol overall in India and how much capacity addition do you see because of this program?
- Gajanan Nabar** With 5% blending, there is enough capacity available. If further blending happens then we have to see how much. It is not a contiguous market to say that so much of blending would lead to so much. It is not directly correlated. However, there will be substantial opportunity opened up if we go for 10% blending further.
- Moderator** The next question from this line of Mahesh Bendre from Quantum Securities, please go ahead.
- Mahesh Bendre** As you had indicated that the second half could be relatively better than the first half and we have seen that in these quarterly numbers, so do you think this momentum will also carry on to the fourth quarter?
- Gajanan Nabar** Yes, we are confident that the second half will be overall better than the first half.
- Mahesh Bendre** How have the enquiry flows been as compared to the last year, is there any growth or anything substantial that you have seen?
- Gajanan Nabar** No, we do not see any substantial difference except we are seeing some roots for some of our new businesses. The international brewery is also showing some signs of finding roots, but we do not see any substantial climatic change in the opportunities in the market.
- Mahesh Bendre** Is that true for international business as well?

- Gajanan Nabar** Yes.
- Mahesh Bendre** What is the progress on the second-generation plant? How are things moving up?
- Gajanan Nabar** Things are moving quite well. The team has got back to the drawing board to work on the 'bolt-on' model. Praj has 600 plants worldwide which is a huge reservoir of opportunity, where the customers can use both first generation and second generation options and the 'bolt-on' model, which we believe could make the difference in the second generation game. The team has gone back to the drawing board and come up with a 'bolt-on' model which would be lower on capex; it could use some of the assets of the existing plants and could be possibly implemented faster. We currently have three options and we will go with the best option out of those. The three options are the Greenfield site that we had announced earlier, the Greenfield project in Europe and the third one is the 'bolt-on'. Based on that, whatever could be implemented quicker, we will go with that option and that decision will be known to all the investors very shortly.
- Mahesh Bendre** The second generation commercial plant will start operating by December this year, so is there any change in the timeline?
- Gajanan Nabar** Yes, it is on account of looking at what is the best possible option for the market because it also amounts to a substantial investment on part of Praj. We are very confident that the investment is a prudent investment but at the same time we are looking at all the options to make sure that this investment finds a quick productive use. So, there is a little bit of delay on implementation of the project.
- Mahesh Bendre** What is the capital expenditure planned for this year and next year?
- Gajanan Nabar** This year it is about Rs.35 crore. We are still working on it for next year. We could probably share that information in the next call.
- Mahesh Bendre** Will there be a substantial jump because of the second-generation plant?
- Gajanan Nabar** We do not think so, we will have to come back on it.
- Moderator** The next question is from the line of Manish Goel of Enam Holdings, please go ahead.
- Manish Goyal** Can you give us the revenue and the PAT number for Q3 for Neela Systems?
- Gajanan Nabar** For Neela, we had a revenue topline of Rs.35 crore and the profit before tax was at Rs.6.2 crore for the quarter.
- Manish Goyal** And fully taxed PAT numbers for the quarter?
- Gajanan Nabar** It stood at Rs.4.2 crore.
- Manish Goyal** From your standalone and the consolidated numbers, if we also exclude Neela System numbers, then overseas subsidiary numbers in terms of revenue have come down significantly as compared to the last year and a loss of Rs.10 crore is seen in overseas subsidiaries, so if you can just highlight that?

- Gajanan Nabar** Overseas subsidiaries mainly are local execution arms. So it depends on the project, which phase of project is being executed and all that. This determines what kind of revenues we would recognize in our local execution. Secondly, we had some expenditure on our Tanzanian project which we have booked to the extent of about Rs.5.5 crore which is taken into account and there is a goodwill amortization because of Neela of Rs. 2 crore in that in consolidation
- Manish Goyal** Is that on account of Neela?
- Gajanan Nabar** Yes. Neela is on full tax and the profit contribution was higher, so the overall tax impact has gone up. The overall net tax impact is of incremental of Rs. 4 crore and the other income is less by Rs.5 crore because of investment cycle. Although the EBITDA is up by 38%, the overall impact on PAT is of Rs.9 crore, so if you normalize all that you probably are better off.
- Manish Goyal** Coming back to the overseas subsidiaries, Rs. 10 crore is due to the expenses on Tanzania's subsidiary which you have put up and you have incurred Rs.5.5 crore loss or are you doing project execution?
- Gajanan Nabar** We are doing a project there and we have booked an expenditure of Rs.5.5 crore.
- Manish Goyal** So is it project related? Once the project gets completed, is there a possibility of it getting reversed?
- Gajanan Nabar** We will have to wait till the project is completely closed, the project is still open. So we will give you a more qualified answer probably in next two calls.
- Manish Goyal** Is it AS-7 accounting where you believe that the cost overruns would have happened?
- Gajanan Nabar** I think we will either talk about this separately or will come back to you once we complete the project.
- Manish Goyal** That is the whole idea why your other expenses are also looking up in the Q3 numbers?
- Gajanan Nabar** Yes.
- Manish Goyal** And probably this may not repeat in Q4?
- Gajanan Nabar** Yes, we believe so..
- Manish Goyal** That means the margins can probably look better than Q3?
- Gajanan Nabar** You are saying it.
- Manish Goyal** We should congratulate you that after a long time we are seeing the margins improvement. So is it also a function of the emerging businesses now growing strongly and they are crossing the threshold level of debt, minimum revenue and fixed cost getting covered and the profitability is now getting reflected from that part of the business also?

- Gajanan Nabar** It is a mix of few things, one is that the export business is better this quarter, second is the quality of orders which we executed in this quarter are better. Emerging business, Neela has increased and so have the other emerging businesses. This traction and the focus on the base business on operational expense side have helped. So, it is a mixed bag of contribution by variety of factors and we want to continue to hold that.
- Manish Goyal** Two more questions on the order inflow number, can you please give the breakup of Ethanol, non-Ethanol and Brewery?.
- Gajanan Nabar** We can give you that but soon we're going to put the complete detailed presentation and you can get all the information.
- Manish Goyal** On the emerging business, do you believe that this 30% revenue share what you have will go up in the next year because of increased business momentum?
- Gajanan Nabar** Yes, our objective is to reach 50%-50%, 50% for the base business and 50% for the emerging business in the next couple of years. In this year, we will meet the objective of 30% from emerging business and it will definitely show upward traction to take us to 50% share on growing base business.
- Manish Goyal** For this 50%, what should be the timeframe?
- Gajanan Nabar** we have set for ourselves a three years' timeframe
- Manish Goyal** We get a lot of orders on fuel ethanol related business from international market and from domestic market we get a lot of beverage alcohol business from all the spirit companies. So how are these two segments of business behaving?
- Gajanan Nabar** The domestic is a steady pot because it is linked to the consumption beverage grade and there is an additional spice because of the blending. There is some interest of creating some capacities and everything has not translated into the order book yet but we're hopeful that some of that will trickle into our order book. International is broadly linked to fuel, we have done many beverage grade plants outside India but it is linked to the mandates.
- Manish Goyal** What kinds of enquiries are you seeing, is the enquiry momentum picking up or slowing down, internationally?
- Gajanan Nabar** In February, there is a big decision on RFS. So, we are waiting to understand, what would be the impact of that. But in the last five years, after 2008 there has been no big international order from United States or North America. Our focus areas have always remained South Central America, South-East Asia and Africa and some part of Europe, sometimes in the eastern part of Europe. We see that there are a lot of countries which are pushing for higher mandates, for example, Thailand and Philippines. Both these countries, for temporary basis, are hit, Philippines by Typhoon and Thailand by a little bit of political instability. In Africa things are moving relatively slowly than our expectation and we can see some movement already happening in few parts of Africa wherein at least 15 countries are committing to mandates which is good news. Also, the feedstock is not a challenge in some parts of Africa. In South America again has the same story but really Europe and US is what we need to really wait and watch how it moves.

- Manish Goyal** The RFS decision in February, is it related to increasing the conventional fuel ethanol mandate or what is it pertaining to?
- Gajanan Nabar** Overall, it is the view on the mandate and how the blending program will move forward. Right now there is support in the US which will continue and how it will continue some of that clarification will happen on both sides on conventional as well as advanced biofuels.
- Manish Goyal** The last question on this 'bolt-on' model which now looks fairly interesting in terms of attaching the equipments with the existing plants, so when do we probably finalize this and move forward and when can we probably see the commercial demo plant start?
- Gajanan Nabar** You should hear something from us within this quarter or at about the time of next quarter results you should see an announcement from us.
- Manish Goyal** Do you continue to look for financial and strategic partners?
- Gajanan Nabar** We continue to look, but looking at the financial climate we are not really dependent on that, that decision is not linked to the financial partner but at the same time we want to be prudent. We want to make sure that we are not over investing or under investing and we are doing the right investment decision. We are very hopeful that the 'bolt-on' model will take off and it could probably be on a faster track as well but we will give you a little more detail on our next call.
- Moderator** The next question is from the line of Sunil Jain from Nirmal Bang Securities, please go ahead.
- Sunil Jain** You are building up your demo plant, in last quarter you talked about a tie-up in Europe and now the third one is the 'bolt-on' model. So in all three aspects, how will the revenues emerge for Praj in the future?
- Gajanan Nabar** We had made a 30 KLPD plant which would make 30,000 liters of Ethanol which is for commercial sales, so that is the revenue model. Like any other Biofuel Ethanol plant, the revenue model is predominantly the same. we want to establish, out of this plant, continuous operations 24X7 on variety of biomass based feedstock and creating confidence in our project investors' mind that this is a possibility and they can viably and commercially convert biomass into Ethanol. This is the objective of the plant but the revenue model remains similar to any other biofuels plant.
- Sunil Jain** what about the 'bolt-on' model, will you be getting engineering revenue and all that?
- Gajanan Nabar** the only change in the 'bolt-on' model is that it will be using some assets of the existing plant. It is not going Greenfield, we are not building the whole thing and we are not building the utilities back-up and all those things. So we save on cost but the model remains similar. There is no change in the model and it is Praj's plant so there is no other revenue like engineering revenues, it is for the future of second generation, so it is like an investment for us.
- Sunil Jain** Are these two separate things, 'bolt-on' plant is one plant and the demo plant is separate?

- Gajanan Nabar** Yes, 'bolt-on' also is a demo plant and we have three options and we will pick the best or the fastest one and then pursue the next ones also.
- Sunil Jain** Can this exercise force you to invest a lot of money in this 'bolt-on' plant and then demo plant?
- Gajanan Nabar** it is not that if we do 'bolt-on', then we will do demo. 'Bolt-on' is a demo plant, it is an option so either you go Greenfield option or you go a 'bolt-on' option. Now if you go by the 'bolt-on' option, we do not have to go with the Greenfield option, so it is not a sequential option. We will pick one of the three and go ahead in the race.
- Sunil Jain** What about this European plant which you were talking about?
- Gajanan Nabar** European plant is largely dependent on funding from EU. We have already announced that we are not going to put any money there, we will bring our soft skills, our technology and all that but the funding has to happen and right now the efforts are on to close the funding. If the funding closes, then we are in with the game on moving on with that as well. Infrastructurally or with amount of engineering efforts, we are prepared but it all depends on whether the Europe plants gets funding or not.
- Sunil Jain** In Europe, will the revenue model be of selling Ethanol?
- Gajanan Nabar** Yes, we call it commercial demo plant because it is not an R&D plant because we already have a pilot plant which does all kinds of permutations and combinations that we need to do for development of technology. This is a commercial plant where it is going to generate revenues out of creating ethanol out of biomass.
- Sunil Jain** In Europe, will the size will be near about to the demo plant which we are setting up here?
- Gajanan Nabar** We are working on it, it is not finalized.
- Sunil Jain** The Rs.44 price for Ethanol which oil marketing companies are willing to pay, how does second-generation fit into that? Do we become viable at Rs.44 and which all feedstock's become viable in that?
- Gajanan Nabar** It depends upon many factors. We certainly know that the technology is viable, but it depends upon how the feedstock is collected, from where it is collected, all the utility cost and the enzyme costs. So it is not prudent to give a straight yes or no. One has to look at it from case-to-case basis, but definitely the viability has improved. It was Rs.27, now it is Rs.44. It has substantially improved the viability of any project linked to biofuel whether it is second-generation or first-generation.
- Sunil Jain** When you were setting up a plant, you must have seen that?
- Gajanan Nabar** Yes, that helps the decision.
- Moderator** Thank you. Ladies and gentlemen due to time constraints that was the last question. I would now hand the floor over to the senior management for their closing comments.

Vinati Moghe

Thanks everybody for joining us today, you will find that we have put up a detailed presentation on the results on our website if you do not find answers to some queries that you may have please send us an e-mail and we will try and respond to it as early as possible. Secondly, we have also got our standalone results on our website you may please access that as well. Thank you and have a good day.

Moderator

Thank you very much, members of the management. Ladies and gentlemen on behalf of Praj Industries that concludes this conference. Thank you for joining us and you may now disconnect your lines.