“Aarti Industries Limited Conference Call”

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MANAGEMENT: **MR. RAJENDRA GOGRI – CHAIRMAN & MANAGING DIRECTOR**
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MR. CHETAN GANDHI – FINANCE HEAD

Moderator: Ladies and gentlemen, good day and welcome to the Aarti Industries Limited, Q1 FY'14 Earnings Conference Call. As a reminder for the duration of this conference, all participant lines will be in the listen-only mode and there will be an opportunity for you to ask questions at the end of today's presentation. Should you need assistance during this conference, please signal an operator by pressing "*" and then "0" on your touchtone phone. Please note that this conference is being recorded. At this time I would like to hand the conference over to Mr. Dheeraj Rajpal. Thank you and over to you Sir!

Dheeraj Rajpal: Thank you and good evening everyone. We welcome all of you. Thanks for taking out time for Aarti Industries Limited analyst and investor conference call for Q1 FY'14. To discuss on the performance and financial highlights of Q1 FY'14 we have with us today Mr. Rajendra Gogri – Chairman and Managing Director, Mr. Rasesh Gogri – Vice Chairman and Managing Director and Mr. Chetan Gandhi – Financial Head. We will begin this call with opening remarks from the management team following which we will open the floor for an interactive Q&A session. Before we begin I would like to mention that certain statements in this call may be forward-looking in nature and disclaimer to this effect included in the Investor release and concall invite, which was sent to you earlier. I would now like to handover the floor to Mr. Rajendra Gogri. Thank you and over to you sir.

Rajendra Gogri: Good afternoon everybody. Thank you for joining us on this call. We shall run you through the operational performance and key highlights for the quarter ended June 30, 2013. Before we go into the details of performance for Q1 FY14, we wish to highlight that the figures for the quarter ended June 30, 2012 does not include figures of demerged activities of Anushakti Chemicals & Drugs Ltd. (Manufacturing Division) merged into Aarti Industries Limited w.e.f. April 1, 2012. Hence to this extent these figures are not comparable. It may further be noted that the operations for Anushakti Chemicals & Drugs Limited (Manufacturing Division) was primarily into Performance Chemicals. Hence as a result of the above restructuring the financials of Performance Chemicals Segment are not comparable with Q1 FY13.

Now coming to the current performance we are glad to announce yet another export led performance. Total revenue of Q1 FY14 stood at Rs.594 crore of this export constitutes about Rs.309 crore i.e. about 52% of the total revenues. EBITDA for Q1 FY14 was Rs.76 crore while the net profit was at Rs.32 crore. We had witnessed a sharp depreciation of the Indian Rupee vis-à-vis the US $ in the month of June 2013. The average monthly rate of $/Re increased from Rs.54.60 for May 2013 to Rs.58.90 for June 2013 and finally was at Rs.59.38 as at end of Q1 FY14.

It may be noted that the company does not take any speculative or long-term position on the currency and follows a policy for hedging the orders accepted by the company, which is generally in the range of next 45 to 60 days of exports on a regular basis. The steep depreciation of Indian Rupees in the month of June has resulted for revaluation and mark-to- market losses in respect of those hedges. However on an overall basis the company stands to gain in medium-to-long term from the depreciation of Indian Rupee.

As you would recall, last year the company had scaled up the hydrogenation capacities to 3,000 tpm from 1500 tpm in Q3FY13. The company had also simultaneously, commissioned the backward integrated hydrogen gas generation plant. The expanded additional hydrogenation capacity will help the company to cater to the growing high margin and niche demand in the segment of polymers, agrochemicals etc., in the global market. This will also facilitate introduction of export-oriented further value added range of products.

As Phase-I unit was commissioned in Q3 FY13, in the last quarter we had carried out 2nd Phase of our expansion, wherein the shutdown was taken for 12 days & test the production at rated (maximum) capacity. As a result the production for Hydrogenated products was affected. The company has recorded the production of about 1,638 tonnes per month of hydrogenated product in the quarter ended June 30, 2013 as against the production of 1,550 tpm achieved for quarter ended March 31, 2013 and 1,390 tpm being the annual average production for FY13.

With the teething issues majorly resolved, we expect the volumes to progressively increase resulting to growth in revenues and margins in the coming period. Now I would like to give you key highlights of our segmental performance during the quarter ended June 2013.

Before going into financials let me update you that during the last financial year a major German Manufacturer had closed down and discontinued the manufacturer of Nitro Chloro Benzenes due to lower captive demand. This has opened up a large market (as captive usage for downstream products, domestic and exports customers) for Nitro Chloro Benzenes. Considering this your company has taken up the expansion of its Nitro Chloro Benzenes capacity on fast track. Against the present capacity of about 57,000 MT, the production achieved in FY2012-13 was about 48,072 MT (42696 MT for FY2011-12).

The company now proposes to expand the existing capacity of 57,000 MT to about 80,000 MT with an estimated capital outlay of about Rs.25 to Rs.30 crore and expects to commission by end of this financial year. The expansion for the above sale happened in two phases, first proposed to be taken up in Q4 FY14 and the second proposed in first half of FY15.

Now coming to the financials, the revenues from Performance Chemicals was at Rs.403 crore. We have taken some set down at Vapi & Tarapur unit for debottlenecking and maintenance purposes. Further during the quarter, the volumes for some of the value added performance chemicals were also affected due to global and domestic slowdown. However, the diversity in product mix and end-user applications have helped to a major extent to dilute this impact. Hence on account of above factors, the EBIT for Performance chemicals had reduced from Rs.55.86 crore for Q4FY13 to Rs.47.86 crore for Q1 FY14 and the EBIT as a percentage also had gone down to 12% mainly because of the forex effect.

As you would recall in Q1 FY13 we had appraised you that the Japanese Company had officially closed down its production as a result an opportunity had opened up for increasing our presence in the pigment application. We wish to update that our expanded capacity for this product has been commissioned and we expect the volumes to progressively increase from Q2 FY14.

In Agri Intermediates and Fertilizer segment, the total revenue for the quarter declined to Rs.90.15 crore as compared to Rs.128.15 crore for Q4FY13 and Rs.104.66 crore for Q4 FY13. Of the above total revenues, the component for fertilizer and nutrient based products (SSP and DCP) for Q1FY14 were at Rs.7.9 crore as compared to Rs.17.56 crore for Q4 FY13. It may be noted that on account of seasonality, the demand of SSP is generally higher as compared to the other quarters. Further during the Q1, there had been no sales for SSP in the month of April on account of non-release of government policy for distribution of subsidy at that time. Hence, as a result the sales of the SSP in Q1FY14 was 1,154 MT as compared to 22,926 tonnes for Q4 FY13 and 13,735 MT for Q1 FY13. In spite of lower sales in Q1, we were able to record and around 30% to 40% growth on annualized basis.

In respect of the other component constituting of products going into various Agrochemicals, herbicides, insecticides etc. across wider geographies, the volumes were lower this quarter on account of the shutdown taken by our global key customers for expansion purposes. Hence the demand for the key products in this quarter were lower. We consider this fall as a short term phenomenon and are hopeful to be able to achieve about 25% growth in this segment.

As discussed last time, the growth in Pharma segment by way of incremental volumes have helped the margins from this segment to increase significantly. The same is evidenced from increasing revenue from Rs.48.03 crore for Q1 FY13 to Rs.63.3 crore for Q1 FY14 and (Rs.52.1 crore for Q4 FY13), thereby posting over 20% growth as compared to Q4 FY13 and over 30% when compared to the Q1 FY13. Similarly the EBIT has also increased to Rs.7.3 crore for Q1 FY14 v/s annual EBIT of Rs.9.5 crore for FY13 (EBIT for Q4 FY13 was Rs.4.1 crore and that of Q1FY13 of Rs.2.1 crore). Thus as explained earlier also, the incremental growth in revenues result a significant improvement in EBIT. Exports now account for more than 50% of the total segmental revenue. We expect to continue on this growth momentum and target this segment to grow at about 30% to 35% on annualized basis.

Coming to the last segment that is Home & Personal Care Segment, we are in the process of reshuffling of product mix. The operation for this quarter was affected due to power disruption caused on account of heavy rains. The revenue for Q1 FY14 was Rs.37.5 crore and resulted into a loss of about Rs. 22 lakhs on account of these disruption and lower volumes. The spray dryer installed in Q4 FY13 is yet to be fully stabilized. With resolution to problems related to spray dyer and other related products reshuffling exercise being undertaken, we expect to improve the performance going forward.

Thus summarizing the quarter's performance, the volatility in exchange rates and lower volumes has been the major reason for lower profitability. Progressive growth in volumes from Q2 FY14 onwards, faster phase of growth in pharmaceuticals segment, higher production volumes in agrochemical range of products for sustained growth in performance, shall help the performance to improve going forward. Further to this the depreciation of Indian Rupee would not only help increase the volumes and margins in exports, but have also increase the demand from domestic industries as substitute for imports, which are now costing more. With these aspects, we expect to have better quarters going forward and also in the future years. Thank you.

Moderator: Thank you very much Sir. Participants we will now begin the question-and-answer session. We have a question from Yash Ved from India Infoline. Please go ahead.

Yash Ved: What is your outlook going forward over the next six to nine months and your expansion plans?

Rajendra Gogri: As mentioned earlier, we expect growth in volumes for the pigment intermediate as well as the hydrogenated product. We expect the performance to improve in coming quarters. As you can see from our last year, the agrochemical sales and EBIT is more in the Q4 as compared to the first three quarters, so that impact will also come in Q4FY13.

Yash Ved: What are your investment plans / fund raising plans or capex?

Rajendra Gogri: No we do not have any specific fund raising plans for in the equity market. Our capex generally will be funded from internal accruals and loans.

Yash Ved: What is your revenue mix - domestic and international operations?

Rajendra Gogri: This quarter we had 52% exports and 48% domestic.

Yash Ved: Thank you very much.

Moderator: Thank you. We have a question from Avdhut Raut from SBI Caps. Please go ahead.

Avdhut Raut: Good evening Sir. Congratulations on a very good set of numbers. My question is if you look at your depreciation amount for this quarter, there is an increase of almost 30% as compared to the previous quarter, can you please elaborate on how does the 30% increase that is question number one? My second question is as far as your segmental revenue is concerned your agri intermediates and fertilizer revenue is actually dropping on a quarterly basis so what is your future outlook for the coming quarters especially as far as this segment is concerned?

Rajendra Gogri: As I mentioned earlier, last year quarter ending June 30, 2012 is not comparable to this year, our merger of Anushakti Manufacturing division took place and the numbers are not comparable, but if you see the Q4, our depreciation was of Rs. 21.8 crore and actually it has reduced because some of the amortization expenses are over that got completed in the last year. Regarding the agri segment, there were low sales of single super phosphate in this quarter as compared to the previous year because the government had not announced their subsidy so there was no sale in the month of April and our export customers had taken shutdown for the expansion so that was the main reason but overall we are expecting the segment to close at the higher rate.

Avdhut Raut: Any capex that you are planning for the coming few quarters?

Rajendra Gogri: We have expanded our pharmaceutical plants so that would be one capex. The other things is our nitrochlorobenzene capacity is also being expanded and certain automation and infrastructure expansion will be done this year.

Avdhut Raut: So all this will be happening probably by the second or third quarter?

Rajendra Gogri: This is ongoing basically.

Avdhut Raut Thank you very much Sir. If there are any further questions I will come back in the queue.

Moderator Thank you. The next question is from Jasdeep Bedi an Individual investor. Please go ahead.

Jasdeep Bedi: Hi Sir, a quick question on the Rupee depreciation, the Rupee has depreciated a lot so how does it impact your business in the coming few quarters?

Rajendra Gogri: As we mentioned in this quarter there is an impact of mark-to-market because the depreciation took place sharply in the month of June but we being the exporters, 15% to 20% of our exports are connected to the exchange rate and about 50% of our top line constitutes the exports, so this will help us in general going further.

Jasdeep Bedi: Thank you. What about the domestic market? How are you seeing the growth prospects in the coming quarter?

Rajendra Gogri: In general the economy is slow so the impact we are able to see in domestic demand is a little slower especially on the performance chemical side.

Jasdeep Bedi: Thank you Sir.

Moderator: Thank you. We have a question from Ritu Sharma, an Individual Investor. Please go ahead.

Ritu Sharma: Sir, the government has proposal of cess on chemicals relating to the technological upgradation and innovation front so sir what is your view on the same?

Rajendra Gogri: I did not understand which cess the government has put?

Ritu Sharma: Chemical cess, which is proposed by the Ministry of Chemicals and the funds, which will be collected, will be used for technological upgradation and innovation fund for the industry so how do you see this impacting the industry?

Rajendra Gogri: As such I am not aware because generally as far as company like ours we have been developing our own technology and also importing certain key technologies so as an individual company we do not see much impact, but if they are changing something you know then obviously it will affect the profitability. But in the R&D they are giving good incentives so any R&D part for both revenue as well as capex, Government is already giving lot of encouragement.

Ritu Sharma: That is all from my side. Thank you.

Moderator: Thank you. We have a question from Nisha Harchekar from Way2Wealth. Please go ahead.

Nisha Harchekar: Can you brief us on the raw material prices scenario of benzene.?

Rajendra Gogri: The raw material prices are right now stable in the Dollar terms around $1200 to $1300 of benzene prices and other raw materials also fairly stable as such.

Nisha Harchekar: Chlorine is still quite low?

Rajendra Gogri: Yes chlorine is still low but now because of starting of agrochemical now it is coming little bit on the higher side but otherwise it is in the range about Rs.2 to Rs.3 and I think it will go up a little bit more towards Rs.4 to Rs.5 in coming month.

Nisha Harchekar: Thank you.

Moderator: Thank you. We have a followup question from Avdhut Raut from SBI Caps. Please go ahead.

Avdhut Raut: What has been your debt in the last financial year that is till March 2013?

Rajendra Gogri: Yes, it was about Rs.820 crore.

Avdhut Raut: Okay and Sir what is your roadmap to get it down in the coming years?

Rajendra Gogri: Basically you know our business is highly working capital intensive so actually more than half of this debt is for funding working capital, so down the line we expect our debt equity to go down in the coming years but being a working capital intensive we do not expect it to go down very sharply.

Avdhut Raut: Sir I asked this question because your debt is far more than your actual market cap so I was just wondering what is your target probably getting it down this year or do you have any specific?

Rajendra Gogri: We do not see any increase in debt in this year. Actually this number should start coming down. That is what we expect.

Avdhut Raut: Sir, any specific targets you have per se, like now it is 800 do you expect it to come down to say 600 or 500?

Rajendra Gogri: Basically, the debt equity, we will be targeting slowly to go below and more towards 0.9 over the next few years.

Avdhut Raut: Thank you.

Moderator: Thank you. Currently there are no further questions. I would now like to hand the floor back to Mr. Dhiraj Rajpal for closing comments.

Dhiraj Rajpal: Thank you for taking out the time for today's conference call. In case if you have any further questions you can get in touch and we would be more than happy to respond. Thank you.

Moderator: Thank you Sir. On behalf of Aarti Industries Limited that concludes this conference. Thank you for joining us. You may now disconnect your lines.