



TATA CHEMICALS LIMITED

Q3 FY2012 – Earnings Conference Call Transcript February 13, 2012 at 11:00 am IST

Moderator: Ladies and gentlemen, good morning and welcome to the Q3 FY12 results conference call of Tata Chemicals Limited, hosted by Prabhudas Lilladher Private Limited. As a reminder, for the duration of this conference, all participant lines will be in the listen-only mode. There will be an opportunity for you to ask questions at the end of today's presentation. Please note that this conference is being recorded. At this time, I would like to hand the conference over to Manish Mahawar from Prabhudas Lilladher Private Limited. Thank you and over to you sir.

Manish Mahawar: Good morning everyone. I would like to welcome all the participants in the earning call of Tata Chemicals. We have from the management, Mr. R. Mukundan, Managing Director and Mr. P. K. Ghose, Executive Director and CFO of the Company. We will begin this call with opening remarks from the management, followed by an interactive Q&A session. I would like to hand the call over to Mr. Mukundan to make his opening remarks. Over to you, sir.

R Mukundan: Thanks Manish. I welcome all of you and my colleague Mr. Ghose on this call. I will take this opportunity to quickly run through some of the perspectives on strategic front as well as on the operating performance for the nine months. The overall operating and financial performance for nine months FY2012 has been excellent in a challenging environment. There has been growth across domestic and international operations and the financial performance has improved across several parts of the businesses that underperformed last year. During the quarter, we also implemented the debottlenecking of soda ash capacity by 100,000 tonnes and it is undergoing stabilization currently. We also debottlenecked 50,000 tonnes per annum SSP capacity in Haldia. The full impact of these will be seen in the next year. We should also be adding up 200,000 tonnes of salt capacity, which should be hooked up in the fourth quarter of the financial year 2012. We have also made some strategic moves in current quarter. Khet-Se operations are now suspended and no further expenditure is being incurred on the operational front. We will take a call on that business only once we have clarity with respect to development of the way the back-end supply chain themes will evolve in India. Secondly, we have also decided to part with our operations in Biofuels in India with clear direction to either lease or sell our plant in Nanded and in that business we will also look at reallocation as an option where we have land available. We will take a call on whether we should continue with this business on our own or we should have a partnership or take a complete exit going forward. The overall approach is to refocus on the company's core strengths. These are in the chemical products i.e. the consumer chemical products as well as industrial chemical products and farm chemical products.

In our Consumer Product business, i-Shakti pulses continues to grow now, it is now available in 18 states. We are making strong promotional efforts to push i-Shakti pulse product sales. Our approach in the branded products will be to keep the investment levels low, but at the same time have a stable increase in the turnover.

Let me now provide some light on the chemical business. The demand for the soda ash in the domestic market has been healthy. The energy costs have been increasing. We have also been impacted by an increase in both logistics and energy costs i.e. coke and limestone. Rupee depreciation also had a very severe impact for a couple of months, which is now moderating. However, the severe cost-push has made us take some corrective action on pricing, to protect the margin to some extent and help us to maintain our profitability. Market demand within India remains firm and there is some turbulence in sectors, but more or less, the demand trend seems to be robust. In Europe, our plants are working at optimum utilization. There was a delay in onset of winter. At Tata Chemicals Magadi, we have seen a steady improvement in performance and in North America; we have finished our debottlenecking by 100,000 tonnes capacity per annum. In addition to that, we are seeing the demand from North American holding very steady and extremely robust.

On the fertilizer segment, we have had a stable production at our urea facility. There has been a substantial improvement in the customized fertilizer because of the customer acceptance as well as our plant operations. We are also encouraged by the growth of non-bulk products, which includes specialty fertilizers, seeds and pesticides. Our plan is to aggressively grow this. In addition, the sales volumes from IMACID up to the third quarter have been at the levels that we had projected, and the benefit of firm pricing on the phosphatic side has benefited the entire chain right up to Haldia. The environment in the fertilizer space has been challenging with international prices coming off the peaks and for the management it will be one of the key tasks in the fourth quarter and first quarter of next year to manage the fall in pricing which will certainly impact the profitability of these businesses.

The consumer product business continues to progress as per plan and our market share in the branded salt segment remains in excess of 60%. Both, the water purifier and branded pulses business are being nurtured during the early phase of their growth. Performance of Rallis was broadly impacted by erratic monsoon. Also, during the quarter, they had taken a strategic decision to shut down their Turbhe plant and in this regard a VRS was done. All the production which was to happen in Turbhe has now moved to the Dahej facility, which was commissioned and both the lines are working at 75% utilization. We expect to be adding further orders to take the up to the utilization levels to 100%.

To conclude, I want to say that we remained focused on our core businesses and on efficient operations. We have access to low cost resources as well as building our essential, extensive distribution network. With this, I will request Mr. P. K Ghose to take you through the insights on the financial performance.

P. K. Ghose: Thanks Mukund. Let me begin by giving you a quick recap on the financials for the quarter and the nine months. For the quarter net sales were higher by approximately 32% at Rs. 3,810 crore. Profit

from operations grew from Rs. 441 crore to Rs. 556 crore. Profit before tax grew by approximately 11% to Rs. 320 crore, while net profit increased by 36% to Rs. 224 crore. Profits include exceptional items of, Rs. 21 crore from partial sale of stake in Tata Steel to Tata Sons, and an unrealized loss of Rs.7 crore on revaluation of un-hedged ECB compared to a gain of Rs. 6 crore last year. Additionally there was a provision made in respect of impairment of the Biofuels and Rallis' Turbhe facility assets, which amounted to Rs. 23 crore, diminution in value of investment in Khet-Se, due to suspension of operations amounting to Rs. 12 crore and costs towards a VRS in Rallis to the tune of Rs. 17 crore.

For the nine-month period ended 31 December 2011, net sales increased by 23% to Rs. 10,335 crore. Profit from operations was higher at Rs. 1,757 crore translating to EBITDA margin of 17%. Profit before tax improved by 31% to Rs. 1,121 crore while PAT stood at Rs. 699 crore, up 38%.

Moving on to the balance sheet, the Company's consolidated debt as on 31 December 2011 stood at Rs. 6,243 crore, v/s Rs. 4,887 crore in December 2010. The increase in loans is primarily on account of funding for British Salt acquisition, repayment of shareholder loans at Magadi, EPM financing, EPM is the phosphate products in the States. EPM financing besides devaluation consequent to the movement in foreign exchange rate. Net debt to equity stood at 0.71 and the total cash and cash equivalents amounted to Rs. 1,350 crore as on 31st of December.

In conclusion, I would say that the overall performance in the quarter has been strong, but we continue to move forward with cautious optimism. Interest rates appear to be peaking out and the strengthening of the Indian rupee over the last month has been particularly positive. The U.S. economy is showing signs of improvement. However, Europe continues to have its share of challenges. We continue to live in fluid and volatile times, and being a global company, we are monitoring both international and domestic developments. This brings me to the end of my discussion and I would now throw the floor open for any Q&A.

Moderator: Thank you sir. We will now begin with the question-and-answer session. Participants, please restrict questions to only two per participant. Thank you. We have first question from the line of Prakash Goel from ICICI Securities. Please go ahead.

Prakash Goel: In the last 3-4 years, we have seen TCL getting into too many other businesses. I would like to urge you to define what the core areas of operations are. Do you consider water as also part of the core business?

R Mukundan: We have defined the areas in which we are and we have tremendous differentiators. These are areas where we have access to some upstream raw material assets, or assets which create value due to our distribution network in India. In addition, in terms of products, we have specialty products and bulk products. If you look at specialty products, there is specialty fertilizer, customized fertilizer and salt which tend to be amendable to some kind of branding or differentiation at the consumer level. The bulk products generally are industrial products and they all may move in bulk bags where one product cannot be

differentiated from the other at all by any nature source. There is a product level differentiation and a market level or let's say value level differentiation. Generally, in the bulk products, we would want to ensure that our value is created through upstream asset ownership and in a specialty product it has to be distribution or technology. As far as water is concerned, we are not getting into water as a business. We are fundamentally using our Innovation Center to provide water solutions. Our goal is that at some point we should be supplying the material, which goes into the purifier, which is then encapsulated. But we had to get into the durable space because the concept had to be fundamentally demonstrated to the market and shown to be doable. Having done that we remain excited about the specialty chemicals which can enter water space and we would look at that as a space. Beyond Swach, we are not planning to get into several types of water purifier and are not looking at those options. We would be keen on supplying ingredients to people who are in water purification, rather than we directly entering in the water business.

Prakash Goel: What is the investment that has gone so far in Swach and what is the likely investment over the next two years?

R Mukundan: In terms of capital it would be very low, It would be at Rs. 10 odd crore, but I really can't clarify that here in terms of capital because it is in our shed which already existed in Haldia and we have just bought some minor assemble equipment's. In terms of marketing, we have not done any major advertisement, in fact we've kept it mostly PR. Interest generation at the initial stage was focused around PR and we have been very tight on this approach and are continuing with the same approach even in the area of I-Shakti pulses. You would not be seeing too much of advertising activity in that area at all. We remain very focused on steady but a stable growth with very minimal spends from our side to build those products. We fully recognize the risks of overspending in these categories.

Prakash Goel: How do you see the situation panning out globally for Soda Ash?

R Mukundan: We are not seeing any issues in the U.S. There is no impact and the sales are robust. In Europe, the sales have been impacted in UK but in Northern Europe, they have not been not impacted. We are also not seeing pressure coming in from Turkey anymore in terms of the market pressure. In India, again, we are seeing the market grow at a much rapid pace and hence the imports continue to increase and we do not see any pressure in the Indian market. Where we see some softness is in China where we believe that there seems to be reduction in operating levels and these are early signs. There is large availability of material, which has a bit of pricing pressure on some of the domestic quotes we are hearing. We have not seen the load in international market, but these are early signs. The main impact would be felt in the markets, which are in the immediate vicinity of China either in Southeast Asia or in Japan and South Korea in addition to China where we continue to watch the space very carefully. The main issue is, if Chinese producers are ramping up the export quantities, we could very quickly end up with surplus entering the market, which will impact pricing. Hence, we would continue to watch that space very closely.

Prakash Goel: What do you see coming out of this meeting on the Urea investment policy? Do you think it will be useful?

R Mukundan: We have not made a public disclosure on the urea investment policy; we have our bids - under sealed condition. We are opening our price bids in anticipation of the policy. So, we will keep our process ready and if the policy framework seems suitable, then we would go ahead with the next few steps, which we will announce at the appropriate time. We are going to take our process to the completion of Phase I, which was to get all the commercial bids for the key equipments, which we have not proceeded on for about three to four months. Now we are going ahead with the opening of these bids.

Prakash Goel: How does the investment policy address the gas availability?

R Mukundan: The gas allocation to fertilizer industry has been accorded first priority and that will not change. In our view, it is the combination of both domestic and international gas, which is in proportion and is being defined. Now whether it finally comes out at 75-25, 75 being from the government side and 25 being allowed by each player, we will have to wait for the policy to come. But the draft policy clearly defines the input cost will be a pass through up to an upper limit which is quite comfortable.

Moderator: Thank you. Our next question is from the line of Atul Rastogi from RBS.

Atul Rastogi: Could you give us an update on the new projects that will come through in Q4 FY2012. TCNA expansion will be at 100,000 tonnes or 200,000 tonnes.

R Mukundan: 100,000 at TCNA it is been hooked up already.

Atul Rastogi: So the full production will start in Q4 FY2012?

R Mukundan: They are trying to stabilize it, which I think will happen in the next couple of weeks.

Atul Rastogi: Any more investment in the Gabon project so far?

R Mukundan: No. It is still at the stage that it was before. Hence, we have not highlighted anything. The technical work is going on and we will be able to provide you with some update on that in the next quarter.

Atul Rastogi: UK and Africa volumes have been down this quarter compared to the last quarter. Could you throw some light on that?

P. K. Ghose: There was a long shut down taken at our SAM plant, which has impacted a bit of production. The pure ash production is more or less the same.. As far as UK is concerned, production is nominally lower from 203,000 to 196,000 tonnes. SAM volumes were down from 85,000 to 73,000 tonnes and PAM from 44,000 to 37,000 tonnes. This is marginal and more likely inventories lying in the system at the end of the quarter.

Moderator: Thank you. Our next question is from the line of Devang Mehta from Canara Robecco. Please go ahead.

Devang Mehta: What is the outstanding pension liability gap for UK & US as on December 2011?

P. K. Ghose: Outstanding pension liability gap for UK is about £ 70 million and for US it is approx. US \$ 48 million.

Devang Mehta: Would you be able to get some breakup of the asset?

P. K. Ghose: There is a standard. In UK, we have brought this down to more debt, so it is now about 60:40 and in USA, it is about 50:50 now.

Devang Mehta: The tax rate for the quarter has been around 20% for the quarter. What is the reason for that?

P K Ghose: That is because there has been a substantial sale of investments, the amount of which is not taxable

Devang Mehta: There has been a continuous income from long-term sale of investments also some other income that is quite volatile in nature. So, I would like to understand both of it, how long will this continue the profit on long term investment and the constituents of other income?

R Mukundan: As far as the sale of shares to the Group is concerned, it was our plan to finance our Babrala project. Subsequently as you know this was postponed. The funds are now been used towards our investment in Gabon. Sale will be done only in a phased manner in the range of Rs. 50 crore to Rs. 100 crore a year.

P. K. Ghose: Other income comprises largely dividend income.

Moderator: Thank you. The next question is from the line of Abhijit Akella from IIFL. Please go ahead.

Abhijit Akella: Sir just wanted an understanding behind the decline in margins in TCNA this quarter. Were there some temporary expenses related to the plant expansion there?

R Mukundan: In TCNA there is a higher fixed cost allocation over lower sale because we had taken a planned shut down and we also incurred a high maintenance expenditure for the super outages we had done which is related to both, hook up and all other modifications in the plant.

Abhijit Akella: So can we expect margins to come back at the levels of Q1 or Q2 FY2012 levels going forward?

R Mukundan: It should normalize at around those levels.

Abhijit Akella: In the last quarter at BMGL, we had reported an improvement in profitability and this quarter again the margins have come off. So what could be the reason for that?

R Mukundan: Up to September, there has been a drop in margins, mainly because of the pickup, which was required in production since we had returned from a severe winter in December 2011, and then there is an increase in the cost of raw materials.

Abhijit Akella: So 3Q kind of levels is more sustainable going forward?

R Mukundan: Yes.

Abhijit Akella: Also, in specialty products rather the non-subsidy products growth guidance that I believe you have given is somewhere around 30% to 40% going forward. First, could you talk about how much of these customized fertilizer sales are within the fertilizer line? Does the growth guidance include Rallis and how exactly is each of these components growing?

R Mukundan: Rallis growth is separate and we do not mix that up, because Rallis is reported as part of a separate segment. It includes components of specialty fertilizers, customized fertilizers and seeds.

Moderator: Thank you. Our next question is from the line of Luv Jain from UTS. Please go ahead.

Luv Jain: Firstly, the industry volumes in complex fertilizers are declining and TCL volumes are improving, could you throw some light on that?

R Mukundan: Broadly, our urea numbers would be exactly as per what our production numbers is. The trading volume is slightly higher this year. There are some minimal stocks in the pipeline as we were very apprehensive of the price coming under pressure and that has come true. It was a commercial decision that we took of not carrying inventories into the fourth quarter. This will come out to be a positive relative for the rest of the industry.

Luv Jain: How is the availability and pricing of the natural gas for urea expected to be for Q4 FY2012?

P. K. Ghose: We are continuing to get full supplies of gas and our production is not impacted. Our plant is running at a steady rate of 3,450 tonnes per day approximately.

Luv Jain: Have you started selling urea on prices beyond cut off yet? Is the US plant operating in full capacity?

R Mukundan: The sales in this quarter will be mostly above cut off.

P. K. Ghose: The plant is being stabilized. We are at 90% to 95% utilization levels as of now. We have to ramp up the capacity further. We are just going through some equipment issues which would get sorted out.

Luv Jain: The natural gas prices are very low in USA, are you benefiting from it or you are passing it to customers as well?

P. K. Ghose: We do not have that concept anymore. The low energy prices would continue to benefit our operations. The margin capture is already happening there.

Luv Jain: Have there been some soda ash price increases in the recent times?

P. K. Ghose: In Q4 FY2012, there will be an increase because our prices are negotiated on calendar year basis. But prices are different for different regions. Across Kenya, UK, USA and India it will approximately be at about US \$15/MT or so. The price rise is as on 1st Jan.

Moderator: Next question is from the line of Ram Hegde from Investment Advisers. Please go ahead.

Ram Hegde: Sir you mentioned that in Rallis there was a VRS expenditure of Rs 17 crore and an impairment of Rs. 23 crore. So does the Rs. 23 crore include VRS also?

R Mukundan: Both are separate. One is an impairment taken at of about Rs. 12 crore for Khet-Se and other was for the Turbhe plant. In addition, there is VRS expenditure of Rs. 17 crore. Also, we had Rs. 3 crore for VRS at Mithapur, which has made it Rs. 20 crore.

Ram Hegde: How is the input side shaping up on phosphate?

R Mukundan: We have no imports happening in Q4 as of now.

Ram Hegde: But in terms of signing of contracts on negotiations?

R Mukundan: There is no clarity because the indicated prices by suppliers are too high to justify profitable operations in India.

Ram Hegde: Also, there was stock of inventory lying in the system especially. Is that right and would that create a problem?

R Mukundan: Our inventory levels are at very manageable levels but it will negatively impact our Q4 numbers and if you need a broad indication it will be may be in the region of Rs. 15 odd crore of a negative hit.

Moderator: Thank you. We have a last and final question from the line of Gauri Anand from the MF Global. Please go ahead.

Gauri Anand: Could you just elaborate on your initiative on the pulses segment, what is the current throughput and guidance going forward and if you could break it into FY13 and FY14? Also, did we take any price hikes in Q3 FY2012 for Soda ash?

R Mukundan: There was a minor price increase taken in India in the range of Rs. 500 to Rs. 600. Other than that, all the price increases in the rest of the world have been done in the month of Jan. With respect to pulses, as I said that we will finish close to about 10,000 to 11,000 tonnes this year and our target for next year is anywhere between 20,000 tonnes to 24,000 tonnes.

Gauri Anand: Would we be break even at this point of time?

R Mukundan: On pulses, the products which we continue to market are breaking even and we are making at least some bit of contribution. So, that has been our approach. We have exited those businesses where we had pressure of contribution being positive.

Gauri Anand: Why did we close Khet Se, if you could elaborate on this?

R Mukundan: I had mentioned that we are not going to expand beyond one center until we prove profitability and we had spent good amount of two to three years, trying to bring various options to make it profitable. We were very bullish till the point when the retail policy was coming, because we were very confident that once it came in, there will be a pressure to work with companies like ours. However, with that policy being put on the back burner, we do not see any clarity that there will be political will to bring in multi-brand and food stores under the modern store format. We believe now that the development of those formats will take a long time in India or at least will need political courage and we have said that we will put this entire relationship into suspension and take a fresh call when the country needs it.

Moderator: Thank you. I would now like to hand the call to Mr. Manish Mahawar from Prabhudas Lilladher Private Limited for closing comments. Please go ahead sir.

Manish Mahawar: I would like to thank all the participants to login for the call. In addition, I would like to thank the management for taking out time for the call. I would now like to handover the call to Mr. Mukundan for closing comments.

R Mukundan: We will continue to remain focused on ensuring a stable financial growth for the company and we are taking both defensive as well as growth steps to move in the direction. Going forward our immediate concern is on the fertilizer side where we believe that the falling prices will impact the profitability and margins which is known to most of the analyst & investors. In addition to that, we are keeping a close watch on the Chinese situation as it folds in the area of soda ash because China is slowing down and that

impact can put pressure. But as of now that is on the watch list. On the fertilizer side, we are seeing pressure coming in. In general, we have benefited from improved operations across all our businesses and this continues to remain our focus. In terms of the urea operations, the converter is lined about 150 kilometers away from our plant, awaiting crossing of river Jamuna, once it crosses it will then hit the plant and we would be taking a shut down as we had mentioned towards the end of month of March or during the second week of April to hook up the new converter. Once the new converter is hooked up, we would then start to get the benefit of debottlenecking which was done in Babrala, which had never really flowed down to the bottom line up until now. FY 2013 and FY 2014 will be the first two years of getting the benefit of that debottlenecking.

Moderator: Thank you so much. On behalf of Prabhudas Lilladher Private Limited, that concludes this conference. Thank you for joining us. You may now disconnect your lines. Thank you.

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