



Tata Chemicals Limited

Q1 FY '21 Earnings Conference Call

August 03, 2020

Moderator: Ladies and gentlemen, good day. And welcome to the Tata Chemicals Limited Q1 FY '21 Earnings Conference Call. Please note that this conference is being recorded. I would now like to hand the conference over to Mr. Gavin Desa from CDR India. Thank you and over to you, Mr. Desa.

Gavin Desa: Thank you. Good day, everyone and thank you for joining us on Tata Chemicals Q1 FY '21 Earnings Conference Call. We have with us today Mr. R. Mukundan – Managing Director; Mr. Zarir Langrana – Executive Director; and Mr. John Mulhall – Chief Financial Officer.

Before we begin, I would like to mention that some of the statements made in today's discussions may be forward-looking in nature and may involve risks and uncertainties. I now invite Mr. Mukundan to begin proceedings of the call. Over to you, Mukund.

R. Mukundan: Thank you, Gavin. Good morning, and thank you, everyone, for joining us for the Q1 Earnings Call. I am joined by, as Gavin has already highlighted, Zarir; my colleague and Executive Director on the Board and John Mulhall; our CFO, and they will walk through some of the details as we move forward.

I would like to start with highlighting couple of issues, a couple of points before I get into details of several of the elements as they have played out during the course of the current quarter.

As you know, we have four verticals in this company.

The first is the Performance Materials vertical which comprises of soda ash and other Alkali products as the key products in the segment. It also has a small emerging business which is our silica business.

The second vertical we have is Nutrition Science which has the iodized salt; which we sell to Tata Consumer and which was demerged last year and we have sodium bicarbonate business along with FOS and GOS, i.e. probiotics and prebiotics products which we are selling to other food companies. And there are many more products to come in this space.

The third vertical is Agri Science, through our subsidiary Rallis India.



The last business which we have, is Energy Science, which is a nascent business, yet to be seeded fully. We are still figuring out with customer's wants and what needs for the business.

In terms of the overall performance, let me start with the Performance Materials business.

The soda ash business, as you know, has exposure to various sectors. And the performance has been in line with the way the sectors have performed during this lockdown period and extreme turbulence around the world. Sectors like detergents, personal care and other chemicals have done well. Whereas sectors like flat glass, which goes mainly into automotive and real-estate, have had a difficult quarter. But these are behind us, and these factories are opening slowly. We hope as time passes by, the softness would start to reduce, and the demand would start to pick up and would again see traction from these sectors.

Overall, if you look at the performance, while U.K. and Kenya have very limited exposure to flat glass, and hence their numbers have been more or less steady, and have run as planned. There were some disturbances with respect to logistics because of port closures. Beyond that, I think there is no customer demand issue, as you know the bulk of the sales of Magadi goes to container glass and bulk of the sales in U.K. have almost zero exposure to flat glass. The flat glass exposure is in India and U.S. In India, it is fairly limited. To that extent, Indian demand was okay. In U.S., the exposure is slightly more, and especially the exposure to the exports is almost 50% to flat glass and that tended to feel the pressure of the activity. Hope as countries reopen, as the pressure of the pandemic reduces, these markets will open and will come back on stream.

As far as our silica business is concerned, they resumed operations during mid-May. And since then, they have had a very good traction in terms of demand and would continue to do well. We are also happy to say that the Tamil Nadu government has actually allocated additional land to us for expansion and growth of this business. And we will continue to build this business going forward.

In terms of the Nutrition Science, the salt did very well because of consumer demand. I think there was a stocking by everyone because of the fears of shutdown. And bicarbonate, both food and pharma grade, also did very well. And the Nutraceuticals business also performed well post reopening of the Mambattu plant, which reopened around middle of May. In fact, both these new plants have done better than previous year in terms of turnover despite the lockdown. British Salt in U.K, has done well. Also UK Bicarb business i.e. food and pharma grade bicarb business has done well during this period and continue to post strong sales.

In Agri Science, Rallis India has done commendable work in terms of the sales as well as the operations, despite difficulties in terms of running those operations which we have faced across the board with respect to labor and workforce mobilization, workforce safety, which were our primary concern, and have continued to perform well. And we hope that with good monsoon that would continue to happen and move forward.

With respect to Energy Science, I think our prioritization has been to calibrate our capital spend in this business, which is a new business, in sync with our customers. And as you know that the auto sector is under serious pressure, we are watching and waiting. We are not in a rush to sort of spend money. At the same time, we are also continuing our efforts to develop products which are the next

generation, which is beyond lithium. That work continues. As far as lithium battery cell is concerned, we have tapered down our investment plan in sync with our customers' situation in the auto sector.

So to conclude: Our focus during this period has been to produce as per demand, which means we have been having a tight control on inventory, except to raw materials where it has been secured for strategic reasons. We have continued to make sure that we collect from our customers well in time so that our overdues are kept in check. And we continue to focus on cash, run all the units for cash. And happy to say that, that has been delivered by the team.

We have also calibrated our fixed cost buildup, and have also conserved, wherever the customer demand, as we know, is going to be slightly slower to pick up, we have postponed those CAPEX. And accelerated the CAPEX where we know the demand is going to be high, especially in Nutrition and Agri segment.

As I want to conclude, I just wanted to say that our long-term strategy is intact. We will be continuing our focus to move the Performance Materials business towards more value-added products, even as we debottleneck some of the areas. So while we will debottleneck our Mithapur plant and those plans are afoot in the soda ash area, our investments will continue to expand the value-added products segment, both in terms of bicarbonate, which is a value-added product of soda ash, as well as investments in various other solutions we give to customer in terms of speckles for detergent business.

In terms of Nutrition Science, we will continue to focus on our investment plan, our growth plan in terms of expanding from 1 million tonnes to 1.5 million tonnes of salt is on track. And despite the issues with respect to project execution, we don't anticipate delays. In Agri Science again, I think we are focused completely on executing our expansion plan to support both domestic and international market.

On Energy Science, as I said, we have tapered down our ambition. But at the same time, this remains one of the pillars we will continue to focus.

So all in all, I would say the company is well positioned through these four verticals to deliver to market: Performance material, Nutrition Science, Agri Science and Energy Science. And we are very confident of navigating through the difficult time in terms of this pandemic. And we are very confident, as we emerge out of this sometime around the first quarter of next calendar year, we would be in a much, much better shape as a company, which has reengineered itself and is reprogrammed itself to serve its customers well.

With that, I will hand this over to John to explain the financial numbers. And then we will open this up for Q&A. Thank you.

John Mulhall:

Thanks, Mukund. And good morning, everyone. I expect there is going to be a lot of interest in the company's view of the coming quarters. But before that, I would just like to add some colour to the financial results for the quarter, which we published on Friday night.

While the profit before tax in the standalone results was down Rs. 149 crore, of this around Rs. 120 crore is actually related to reduction in other income at line 1B. Within there, you have a timing of a dividend receipt; we didn't receive any dividends from IMACID or Rallis this quarter. We have got Rs. 98 crore last year.

The massive dividend last year of Rs. 72 crores, including a one-off element that we did adjust to adjust the cash build up in Morocco and this year, when we get it in quarter two, I would expect it to be around Rs. 25 crore. We all saw the Rallis dividend of Rs. 26 crore, we will now get to quarter two. We also had reduced bank interest, mutual fund and fixed deposit income of about down Rs. 32 crores compared to last year. This is really a result of a slightly reduced cash balance, but also just the reduced rates we are seeing in the marketplace today, and that is also the reason why you all see a reduction in the unallocated income in the segment analysis of the SEBI sheet in Page 2.

From the operations side, while revenue is down around Rs. 91 crores, the gross margin itself actually held up quite well, this is in TCL standalone. The gross margin came in about 62.6% against 63.1% last year, so 0.5% reduction compared to last year. The revenue reduction itself was seen mostly in soda ash and sodium bicarbonate volumes, but this is offset by a strong salt performance. Prices did come under pressure but mix and some variable cost savings did limit the non-salt adverse price mix variance to around Rs. 10 crores to last quarter last year.

Our finance costs in India were down Rs. 15 crores on last year, really reflecting the repayment of the ECB loan in October and NCDs in July 2019. Our India cash position; of cash, mutual fund deposits and bank deposits moved to Rs. 1,999 crores in June compared to Rs. 2,162 crores in March, a reduction of Rs. 163 crores. Capital spending in the quarter in India was Rs. 105 crores against Rs. 175 crores last year.

Looking at international operations. And as Mukund mentioned, the steepest decline we saw was in North America. Sales volumes were 152,000 metric tonnes below last year, and nearly all of this was export related; no doubt, will be discussed later on in the Q&A. Profit before tax in the U.S. operation has reduced by Rs. 210 crores from last year. Two-thirds of that is actually volume related, Rs. 140 crores is volume related. And adverse price impact of export sales is around Rs. 30 crore.

And while good cost savings were actually offset by a deliberate reduction in mine output and surface and production output to control cost and also limited the inventory build-out. We did complete the \$375 million refinance in North America in some quite challenging market conditions and we had some additional costs as we changed the financing structure. The new arrangements will still be cheaper this year compared to anticipated costs of the previously contemplated finance facility.

For Magadi, they did record a marginal loss before tax of Rs. 2 crore, and while sales were down 6,000 tonnes at 62,000 tonnes in the quarter, the larger impact was seen in pricing and destination mix; these adverse results were partially offset by some rail and fixed cost compression.

The underlying U.K. performance itself was actually better than last year as we had a Rs. 12 crore exceptional gain last year. And this year, it was actually only Rs. 3 crores. For Tata Chemicals Europe, our soda ash sales were down 6,000 tonnes, 4,300 tonnes of that was actually PFR sales last year, which had minimal margin. So, this mix improvement, along with lower input cost on coke, and better manufacturing efficiency, alongside good bicarbonate sales, produced better contribution margins for both business units, the soda ash and the sodium bicarbonate business units.

U.K. salt operations were impacted slightly by our sales mix as a result of the pandemic restrictions, but lower input cost, mainly gas, which contributed slightly better performance than last year. And overall, our consolidated cash finished the quarter at Rs. 3,258 crore and net debt was Rs. 3,760 crore.

And with that, I will hand back to Gavin, and then we will open the lines for questions.

Moderator: Thank you very much. We take the first question from the line of Madhav Marda from Fidelity Investments.

Madhav Marda: My question was specifically on the U.S. operations. So, our EBITDA per tonne in this market has been about \$45 to \$50 for the longest time. And obviously, this quarter because of the lower volumes, it has been impacted. But I am just trying to reconcile why the EBITDA per tonne has come down to about \$12, \$13 per tonne versus \$45? What has been the reason for the decline, I mean, is it like product mix or operating leverage, what has impacted us there?

John Mulhall: Yes, like I said, I mean, a relatively high fixed cost base in North America has a disproportionate impact when you reduce the volume. And the price reduction on our export sales as well. So, two things; one, significant volume reduction which does impact your overhead recovery rates. Second piece is the price reduction. The third one is, we took the mine and then we curtailed production to meet demand. So we aren't building up stock and wasting cash that way, that's really why which has driven the reduction in EBITDA per tonne.

Madhav Marda: Okay. I am not sure if I am doing it right, but if I look at your ASP per tonne, which is just dividing the revenues by the volumes, ASP seems flat or little higher actually Y-o-Y. I am not sure, what am I missing here.

John Mulhall: No, the price is down against last year.

Madhav Marda: Okay. All right. I will just check, maybe. And maybe one other question, how soon do we think the U.S. operations, the volumes come back to more normalized levels? How many quarters do you think your anticipation is, it could take?

R. Mukundan: So, I think let me comment here, and maybe Zarir can add more colour to this. Broadly speaking, if you look at the U.S. operation, I think the market mix will keep changing the realization because the domestic market realizations are higher than the international market. As international markets go down, the volume goes down, the pricing mix will keep changing. But broadly, I think their contribution margin has been in line with what we usually do. And if I take a broad range, I mean, contribution margins should hover around about 55% broadly. So if you look at the compression, which the sales have gone, I think that would broadly explain the compression at the EBITDA level. And if at all, it will also tell you that there is a bit of a gain which has come in because of certain fixed cost effort the team has put in play. So that's really the way I would sort of look at it, because if you look at the loss of revenue itself and you look at the loss of contribution arising out of that revenue at 55%, it's about Rs. 125-odd crore broadly.

On an EBITDA of Rs. 189 crore, that Rs. 125 crore compression should have led to EBITDA which should be close to about Rs. 60 crore to Rs. 70 crore. I think the fixed cost absorption, as John has highlighted, has led to a bit of a pressure on the EBITDA a little bit more than what one would normally anticipate. So at the

contribution margin level, we don't see any big difference. It is basically the volume pickup, which will address most of the issues there. As far as the PBT level is concerned from EBITDA to PBT when you go, there is a \$5 million additional cost, which has happened this quarter, which will not repeat, which John has highlighted, because that was a part of the refinancing net take out cost because we wanted to move to a different structure. And that structure actually is cheaper than the current arrangement. So overall, the company benefits, but we had to take the entire takeout cost this quarter itself rather than amortize because of the accounting standards.

So that explains away at the PBT level about Rs. 35-odd crore of cost. That's approximately \$5 million. John, am I right about that?

John Mulhall: Yes. Just under \$4 million for this quarter.

R. Mukundan: Yes. So, I think the real issue is, which you raised as a question, when would the volumes come back? If that question has to be answered, fundamentally, the domestic market, really the slowdown in the domestic market in U.S. was not as severe. In fact, the Indian domestic market was more severe in terms of slowdown than the U.S. market. The real issue for U.S. is the export market, when will they come back? And our own understanding is it is going to start trending up slowly. Quarter two would see slightly better than quarter one.

But quarter three would see it more. But when would it return back to normal? I think maybe by the last quarter of this year or the first quarter of the next calendar year is when we believe the thing would return to a normal. If you look at two of their export markets, the large export markets are Southeast Asia and South America. South America is especially going through a real difficult time in terms of pandemic and Southeast Asia, hopefully, will recover earlier than South America. We expect South America also to swing back closer to the last quarter of this calendar year, which is somewhere around January, March or around that time.

Madhav Marda: Okay. And maybe just one follow-up from my side. On the pricing side, in our key markets in U.S. and India, can we see more pricing pressure going ahead, given capacity utilizations are a bit lower in the global soda ash market? Or it could be more resilient?

R. Mukundan: See, in the quarter one, in my view the pricing pressure was there, but I think the pricing pressure did not translate into what I would call margin pressure, because the input costs also came down in terms of energy costs. Only one place where the input cost did not come down was Magadi because they had certain oil hedges in place. And those hedges meant that they could not get the benefit of the low oil price during the first quarter, which they will get in the second quarter. So clearly, the rest of the units will get certain benefit coming in because of the low energy cost, which protected them in the first quarter. Going into second quarter, I think even if there is a pricing pressure, our assessment of the pricing issues, especially in Southeast Asia, they probably are reaching the bottom. Zarir, you may want to add exactly what is your understanding of whether they are at bottom or maybe another \$1 or \$2 down?

Zarir Langrana: Sure. So just once again, just going back to pricing for our North American unit. Once again, it would be useful to break it down into domestic and export. Domestic is primarily contracted and we are seeing customers honoring their contracts. So the pressure on pricing in North America, at least till the end of the year is likely to be minimal. In the export markets, as Mukund mentioned, yes, there has been

some contraction in pricing. Our view is that in Southeast Asia, this has possibly reached the bottom as far as Chinese pricing into that market is concerned. Most of the Chinese producers today, we believe, are trying to move pricing up, given the fact that their margins and their cash contributions are really at rock bottom today. We might see a little more aggression from the Turkish player in that market. The market today is at a level of about \$185 to \$200 CFR. At best, we believe it might slip down another few dollars to maybe \$180, \$181. But I think that should be the bottom of the market. And certainly, not with all customers, with selected spot offers into that market. But that being said, yes, the export markets will continue to be under a bit of stress, at least till the first quarter of next year or the last quarter of our financial year.

R. Mukundan:

Yes. And to further add to what Zarir has said, I think you need to watch out for few sectors in this. I think watch out for how the sectoral demand, especially the auto sector around the world gets back in shape. As it bounces back, especially the passenger vehicle demand comes back, whether it is in small or large vehicle, it really does not matter. For us, the small vehicles are much better because you sell more glass per dollar value of the car. I think the market demand direction will be outlined by that very specific segment. The issue is fundamentally going to be driven by that. And that will be driven by how well the pandemic has been controlled. So our view still is that Southeast Asia, it has been controlled better. South America is still not clear, I think they are under deeper pressure now. They will probably take another four to six months to get it underway, which is why we are saying by the fourth quarter of this year they could see better turn of light. This is under the assumption that India continues to do a good job. If we take the turn for worse, I think we are then for a bit of a rude shock.

Moderator:

We take the next question from the line of Abhijit Akella from IIFL.

Abhijit Akella:

Sir, just a couple of questions from my side. One is just a follow-up on the North American market. How much of the decline in volume in 1Q was because of logistics and by plant closures just because of operational or rather lockdown issues in the export markets for North America? Versus how much of it was because of just weakness in end-user demand? And therefore, what kind of recovery could we possibly expect in 2Q?

And then corollary to that, just on the EBITDA per tonne, I know that this quarter there were some unabsorbed fixed cost, but what would be a more normalized kind of number looking ahead from 2Q onwards?

R. Mukundan:

So, in terms of the U.S. exports, there were no port closures in U.S. itself. And if you really look at where there are port closures in Southeast Asia, there were some, but I think they are not the main driver of this. And so I would just simply say that as far as the U.S. market movement is concerned, it is primarily driven by the demand at the customer end, but this is not related to any port-related issue. The port-related issues mostly were concentrated only in one of our units, which is in Kenya, where Mombasa had some issues when they were trying to export, but that is also behind them. So really, these were not operational hiccups at all. Bulk of it, and I would say 90%, 95% of this is just the sheer demand not being there. Zarir, do you want to add?

Zarir Langrana:

Absolutely correct. I think port closures in some markets in Southeast Asia, maybe in the first half of April, but insignificant. I think most of the ports are now opened up. It's really pipeline stocks and lack of demand from end users. And primarily in the export market that translates into lack of demand from float glass producers.

The others are slowly coming back in line, but the path to recovery for the float manufacturers in the key export markets is likely to take longer. We are seeing very encouraging signs out of China in terms of both vehicle and infrastructure demand. And maybe we see some spillover of that into the Southeast Asian markets as well. But it is a wait-and-watch situation. Q2, as Mukund mentioned, will be marginally better than Q1. Q3 might see a further uptick, but really to see any significant movement we might have to wait till Q4.

R. Mukundan:

Yes. And I think just to add a color, I think if you look at the segment of container glass, flat glass and detergents and other chemicals, if you put it there; detergents and other chemicals, I think we continue to see steady demand. As far as container glass is concerned, there was a bit of a dip and then it picked up, in fact, it moved up beyond the current year in most markets, except India. And I will come to India, why India behaved differently. Around the world, the in-house consumption of beer and liquor actually increased, which meant that people were buying more bottles. The demand for bottles did go up. Whereas in India, I think the entire liquor consumption had been shut down, so that sector suffered only in India, container glass sector. Container glass also feeds in into pharmaceutical glass. I think those sectors are seeing good demand strength.

So that leaves us with flat glass and flat glass fundamentally is driven off in large numbers by auto sector in Southeast Asia. And in Latin America, it is driven off the housing starts and housing constructions. And as far as our understanding is concerned, this is going to be clearly a direction which we need to get from our customers. Auto sector customers believe that personal transportation will receive a boost, but that is only an expectation, we don't know for real. So as the float glass demand comes back, you could then start to predict the soda ash demand. The good news is, Southeast Asia and South America don't have any domestic production of soda ash, it is all international suppliers who are there. And if that demand comes back, everybody will have room to play. If the demand is slow to come back beyond, let us say, fourth quarter of this year, then I think we need to then look at what are the avenues to shift the marketing place.

So I think this is a, let's say, short-term issue which we are concerned with. As far as the medium-term is concerned, the Tata Chemicals, in terms of exposure to flat glass sector, our exposure is less than the industry. In India, it is less than the industry. Internationally, also, it is less than the industry. In fact, in U.K. and in Kenya we are not exposed to flat glass. And what we are trying to do, especially in India in the short-term, is to also switch our production and product mix away from the sectors which are vulnerable. In U.S., it will take a bit longer time. But there, again, the plans are afoot to sort of make sure that market mix which changes over a period of time. So our medium-term attempt is going to be fundamentally switch the product mix to the more resilient sectors and continue to focus on them. There's hardly any realization difference between all the sectors, so it is really who is serving which sector and that creates an impact on the P&L and bottom-line.

Abhijit Akella:

Thank you. That's really helpful. And then my second question was just with regard to the CAPEX plans for this year. You talked about dialing down your investments in sectors that are not seeing very clear demand going forward. So, on a consolidated basis, what kind of CAPEX should we expect for fiscal 2021? And then in case it yields any surplus cash, would you prefer to use that cash to pay down debt or are there any other plans in mind? Thank you so much.

R. Mukundan:

So clearly, if you look at the one which we have dialed down, even as we speak, and I think it's part of the strategy, is the storage battery business. Because we

think we will see demand robustness, not from the mobility solution in the short-term at least when I say 12 to 18 to 24 months, because the vehicle companies will be under serious stress in terms of putting out new, what I call, new vehicles in the market because they will tend to depend on what is already on the drawing board not to do something new. And I think the government support in terms of electrification also will be under pressure because there would be financial pressures in terms of giving fiscal benefits for boosting the domestic EV shift in the short-term.

In the long-term, that still is a vertical which we must play in. Also in the short-term, I think the solutions for Energy Science will switch to stationary solutions. And for that, we don't need to actually invest in a factory, there is enough surplus capacity around the world, we can assemble and give solutions to our customers. So we are engaging with customers, but that necessarily need not mean a factory build-out, because there are solutions available which are available from the current manufacturers around the world, which we can assemble and ship any orders which may win. And so, we have dialed down completely the Energy Science business, that is a fact, which I also highlighted in my opening remarks.

As far as the Agro Science is concerned, there is no change in our plan. In fact, we are accelerating some of the startups. We are taking additional capital spend there to push the production of both our formulation and our technical products. And this is happening in Dahej as well as in Ankleshwar, both plants are being pushed up to give the solution. Also, if you look at our Nutraceutical and our silica plant, I mentioned as far as the Nutraceutical is concerned, our factory can expand 4x the current size. And we are seeing a very good customer demand, so we hope to come back and continue to report strong numbers there. And hopefully, by the year-end you would see then the growth in that sector is happening.

As far as the silica is concerned, our solutions to tire industry was constrained by the current capacity and also the land which was available for expansion, which Tamil Nadu government has allotted additional land to us only, I think, last month, even during the pandemic. So we are going to go ahead with investing in that. As far as the salt is concerned in Mithapur itself, as well as in U.K., the investment shift to bicarb and salt in U.K. continues as planned. As far as India is concerned, the expansion of salt from 1 million tonne to 1.5 million tonne, in fact, is getting accelerated. There is a slowing down in terms of some of the investments we were making, especially in terms of the capital spends in U.S. as well as in India, especially with respect to some of the commoditized chemicals. But that slowdown also is not very dramatic to write about, but it's just extension of the phase.

So I think in terms of CAPEX spend, it is not going to be such a sharp dip, but it's going to be a slight dip. John, do you want to add some number to this? At least in the first quarter, you have seen a dip, I think that shift will continue even during the next couple of quarters.

The big issue, let me just highlight, is not coming from our intent to grow, it is actually coming from constraints in terms of project execution; we are not able to get the equipment on time, we are not able to get the workforce on time, which is leading to delay, which is leading to prioritization of what we put up. So, in the order of priority, anything which goes to Nutrition and Agriculture sector will get faster attention from us, the rest of the sectors will be reprioritized. And the constraint is not cash, the constraint is not the strategic intent because our strategy is very well crafted in terms of delivery to market. But our issue is more coming from the workforce and availability of project teams to execute these. So that's

where the prioritization is happening. So we could see a shortfall by Rs. 150 crore to Rs. 100-odd crore from our normal spend. But I don't see a dramatic dip below that. John, over to you.

John Mulhall: Thanks, Mukund. Yes, I would agree with that. We probably could end up being about 5% to 10% down on last year's spending. But when it comes to important strategic investments like in Rallis, where they do some development expansion work or in the U.K. where we are building out the carbon capture facility and spending some more money on developing bicarb facility, we will continue spending money in these areas, because these are margin accretive strategic investments. But where the return is, it could potentially be uncertain or we are just not sure what's going to happen in the next one or two years, then we will dial back. At this stage, today, I would probably say we are about 5% to 10% down on last year. But that might change a little bit.

R. Mukundan: Yes. Also, when your question about debt reduction, I think allow us time till the second quarter to come back to you. There is definitely work going on and I think we do think it's one of the things we must do going forward. So we will get that also as a plan and present back to you. Right now I don't want to comment where the work is going to review exactly how we need to move in that direction. But we are clearly focused to take even the international debt out so that we become as prudent in terms of debt overhang in the company, even internationally. Even though domestic business is in good shape, but we are also trying to move that also out in the same direction.

Moderator: We take the next question from the line of Tarang Agrawal from Old Bridge Capital.

Tarang Agrawal: My question is with respect to your international soda ash business. In a medium-term basis, what is the return on capital employed that the management envisages to achieve on its international soda ash ops, that is U.S., U.K. and Magadi? And the second is, what are the levers in the current business to move it to those levels?

R. Mukundan: See, I think if you look at ROCE typical calculations, I think in terms of U.K. and Magadi, the capital there, broadly if you look at the books, it is hardly minor capital, it's been mostly written down. So, any profits we make there is going to yield good returns, it will be upwards of 12% to 15% return. I think John can share the more accurate figures with you.

As far as the U.S. is concerned, there, the return on capital employed in the dollar terms is between 6% to 7%, broadly. And I think as we move the product mix to value-added products, we want to take it at least to certain decent double-digit figures, I think that's the plan. Right now we don't want to make any comment on exactly where we land the U.S. business with the value-added product move, which we want to make. So we will come back to you with specifics as and when those plans are cleared. But clearly, our approach to U.S. is to move that entire business to more value-added products.

Moderator: We take the next question from the line of Sumant Kumar from Motilal Oswal.

Sumant Kumar: My question is regarding U.S. business. So we have seen the trend of quarterly total expenditure of Rs. 650 crore to Rs. 700 crore. So can you quantify what is the fixed and variable mix the net of Rs. 650 crore to Rs. 700 crore per quarter?

- John Mulhall:** What I said at the start is that it's a fairly high fixed cost business, for very simple reasons. It's an extractive process where we basically buy the rights to mine the area. And then there is no real input cost other than the gas and coal. So the rest of the cost is going to be fairly fixed, labor, if you like, depreciation, some of the production consumables, maintenance expenditure. That's the thing that's generally open to be fixed. If I had to put it down, I would probably say that it's variable, but that could change.
- Sumant Kumar:** Any broader range of fixed and variable cost mix, in broader range?
- R. Mukundan:** John, let me intervene. I think I had already indicated when the first question came, that broadly it should be around 55% contribution business, broadly, give or take 1 percentage here or there. And I think the reason I am saying broadly is, the quarter one, any pressure on price was taken out by the reduction in the energy cost and other cost, variable cost, which held that percentage up. So if you take 55% broadly, I think that would give you an indicator of what the contribution number is. Then post that is all fixed, so that should help you between EBITDA and contribution you would find more or less, it is either semi-variable or fixed.
- We can't add color beyond this, because quarter-on-quarter this 55% may move because of product mix. If there is a higher export business then this may shrink; if there is a higher domestic percentage, this may increase. And it also moves broadly in sync with the issues related to how the energy prices and gas prices move. But I think if you want a thumb rule, I think that should give you a good fix in terms of the U.S. number.
- Sumant Kumar:** And you said the contribution margin for U.S. is same compared to previous year. So then why gross margin has declined in Q1 FY '21 at consol level? Which subsidiary is dragging gross margin?
- R. Mukundan:** I think broadly the margin levels in U.S., we have given you on the Slide 15. If you go to Slide 15 which we have shared with you. And in terms of the other ones, we can get specific about each item. And John has already highlighted the margin levels in India being stable. I don't think any place has had a margin issue in terms of contribution margin. The issue fundamentally is that more or less every one of these units has held well as far as the contribution margin is concerned. John, has there been any sharp erosion in any of the other units? Because I did not see that, it's basically volume effect, right?
- John Mulhall:** That's right. It's volume mix effect. So that is the higher contribution of the North America, and their sharp reduction in going to have a higher level on the consolidated basis. I mean, we talked about the reduction in India and North America.
- Sumant Kumar:** Just because of Rallis India, gross margin contraction at consol level, no?
- R. Mukundan:** I don't know. As I shared with you on Slide 15 entity level numbers. And I have also highlighted to you the gross margin in U.S., I think this should give you a very clear picture.
- John Mulhall:** No, you are missing the disproportionate size of the U.S. operation, and its reduction has a bigger impact on the consolidated gross margin. If I look at the

gross margins across the each of the entities, they are down slightly and in U.K., it's up a little bit, but they are down. But the bigger element is the size of the U.S. operation and its reduction on the consolidated piece, yes? So some mix element of the U.S. compared to the rest of the business.

Sumant Kumar: Okay. And talking about the export and domestic mix, what we have seen in Q1 '21, export is 55% of total business. So I think the annual level, it is lower, right?

Zarir Langrana: No, it's about the same actually, if you add it up. Export volumes hover between 45% - 48% for North America.

Sumant Kumar: Annual basis?

Zarir Langrana: That's right.

Moderator: We take the next question from the line of Dheeresh Pathak from Goldman Sachs.

Dheeresh Pathak: Just one basic understanding, the standalone segmental data where you mentioned the specialty products revenue. The underlying business in that is Nutraceuticals and the silica business, or that is part of consol? Can you just help me understand what is the underlying business in the standalone specialty products of Rs. 15.89 crores for the quarter?

R. Mukundan: Yes. I think, so the underlying specialty is basically the FOS, the Nutraceutical and the silica business. And clearly, I think these segments are not the way I explained it, I think we will move to that the way the businesses are structured.

Dheeresh Pathak: Okay. So in the standalone segment assets, I see specialty at Rs. 578 crore, that probably represents the CAPEX that you did in the silica and the Nutraceuticals business, right, that Rs. 600 crore, Rs. 300 crore each?

R. Mukundan: It would also include about Rs. 75-odd crore we have invested in land, in Energy Science in buying land. It has not been put to use, so I think that probably also is added there.

Dheeresh Pathak: Okay. And there used to be an underfunded pension liability at, I think, the U.K. operations. Has that materially changed anything there, if you can just mention?

John Mulhall: Yes. We have unfunded liabilities rather, in the U.S. and the U.K.

Dheeresh Pathak: We have seen sharp massive movements, if there is any number you can just quantify, has that improved or deteriorated?

John Mulhall: It will have deteriorated since March, because the discount rates have fallen off in in both areas since March.

Dheeresh Pathak: Okay. And just one last question, sir. Earlier my understanding was that India soda ash expansion is going to spend some Rs. 1,600 crore to expand at the Mithapur site. So of that Rs. 1,600 crore, how much has been spent so far?

R. Mukundan: No, Rs. 1,600 crore is not just for soda ash. You see, the number we have spoken about in Mithapur is split between the salt and soda ash along with common utility which are there. In terms of CAPEX spend, I think, overall number was Rs. 2,400

crore, and I think Rs. 600 crore may have gone in and about Rs. 1,800 crore is still to go. John, you have got more accurate figures?

John Mulhall: Yes. I wouldn't get too much further than that. I think that that's reasonable.

Dheeresh Pathak: Of the Rs. 2,400 crore, the balance Rs. 1,800 crore would be spent in the next what, how many months?

R. Mukundan: I think it would take about 2.5 years broadly, it could take us right into 2022 and 2023, somewhere in the middle, I think.

Moderator: We take the next question from the line of Ramesh S. from Nirmal Bang. Please go ahead.

Ramesh S: The first question I have is, in terms of the global soda ash industry, do you see any capacity closures that we can see, given that the capacity utilization is already at 80%? And what is the cash margin you see at which the capacity closure will happen?

R. Mukundan: I don't think we will see capacity closures, except maybe in China and in Europe, these are the two places. In China, I think the way they are dealing with it is, they are taking extended maintenance shutdown and whether they will come back on stream after this extended maintenance shutdown happens, is open to interpretation. So, one has to constantly keep watching. So, I think our assessment is, some capacity will go out, but more accurately to see this we need to watch this whether they go for completely extended maintenance closure, which runs into 9, 12 months or so, then I think the units will move towards decommissioning completely. As of now, they are taking a pretty much rolling maintenance closures during this period. Zarir, do you want to add anything specific beyond this?

Zarir Langrana: No, I think you are right, Mukund. I think there is some risk of capacity closures in China on a permanent basis. Currently, many of those plants have taken extended shutdowns. We have seen in the past in China when somebody takes an extended shutdown of, let's say, more than 12 months, typically that capacity goes off-line permanently. That number could be anywhere between 2 million tonnes to 5 million tonnes, 5 million tonnes on the upper end, 2 million tonnes on the lower end. I think the other thing that's happening certainly is that planned capacity expansions, primarily in North America and China, are likely to be delayed by at least 15 to 24 months.

Ramesh S: Okay. And if you look at the current share of the end-use market pie for soda ash, what is the share of the flat glass market globally and in the U.S.?

Zarir Langrana: So flat glass, I think last year if you look at the number, it was close to about 32%. Given the contraction in the market, in 2020 we expect that to probably drop to about 28%.

Ramesh S: This is for the U.S. market or global market?

Zarir Langrana: No, this is global.

Ramesh S: Okay. Just one last thought sir. If you look at the losses in U.S. and U.K. for the quarter, and supposing assuming that this kind of pressure on volume persists,

how are you placed in terms of cash flows to finance your working capital and your CAPEX?

R. Mukundan: So, I think as far as we are concerned, we have no issues in terms of financial figures at all. The first half and first quarter when you look at it, the losses were actually accentuated at the PAT level by almost Rs. 35 crore, Rs. 40-odd crore, which was a one-off, it is not going to repeat itself again. But if you take a PAT figure of about Rs. 110 crore and Rs. 120-odd crore, we are looking at about Rs. 80 crore claw back which we need to do. And I think on a cash profit basis these units should be fine from the second quarter onwards. It is just that our capital spend is in tune with the cash profits which we are earning, especially in U.S. So we don't anticipate any major issues as far as our ability to service any of our costs are concerned. In fact, as I mentioned, we believe that we could use some of our cash to repay the debt, which we have internationally, which we will work and come back to you by second quarter results are done.

Moderator: Next question is from the line of Saket Kapoor from Kapoor & Company.

Saket Kapoor: Sir, firstly, you spoke about this value addition part in U.S.A. Sir, if you could dwell more, what will be the product line for which you are harping on to?

R. Mukundan: We are examining two, three options there. Let us come back to you. And that will certainly cut back the pressure on volume, which is going in the export market, but we will come back to you. I think during the course of the year, we will have more details and more color to add. But we have done this in U.K., for example, we moved from being a pure soda ash company, now almost we are saying that we will have a large proportion of the business as bicarbonate. We have done this in India also. We have continued to add bicarb capacity and also adding multiple product lines within Mithapur to make that more robust. So we think there is an opportunity to do a similar job in Magadi and in U.S. But we will come back to you specifically during the course. Our teams are working on it, it's essentially our plan. Our plan is not to add substantial volumes in soda ash, but to add value in soda ash, that's really the way we are going. And to add volumes in the specialty businesses because that's where the value creation will happen.

Saket Kapoor: Right, sir. And in terms of U.K., sir, is the transition period over? And now the results will start yielding because, sir, the EBITDA has moved up from Rs. 18 crore to Rs. 28 crore, but the PBT and PAT has remained negative by Rs. 15 crore. So if you could explain that?

John Mulhall: The first part on the **carbon capture** facility, we are hoping to get that really towards the end of this fiscal year, is where we would expect to see that starting to produce. So that's one piece. In the U.K., you have a couple of other things going on in there. There is also the, of course, an SPV debt within the U.K. operations, \$75 million, so there is an interest line to that. And then we also have about £150 million of bank debt in there. So you do see a big drop in EBITDA and PBT coming from that. Our target going forward is also, as Mukund said, is to move up the margin chain, which is concentrated more on bicarbonate and the soda ash, and the soda ash is the feed for our sales of bicarbonate, and generate more cash and use that then to, as far as satisfying the debt items we have in the U.K.

Saket Kapoor: So sir, this PAT loss and PBT loss was attributed for what?

John Mulhall: There are only two things for below EBITDA, and that's bank interest and depreciation.

- Saket Kapoor:** Right, sir. And sir, one very small understanding, when we present our segment, there is a bit of confusion, as earlier also a speaker has told about this the specialty product part, if we could come with more granular split, since it has not reached the critical mass but still the Nutraceutical line, silica and getting differentiated with the agro one would give a clear picture then being jumbled up inward. So that would give more clarity, sir.
- John Mulhall:** Yes, we can certainly do that. But the thing to bear in mind here is, just now the agro is purely Rallis, and you can see those Rallis results separately, yes? Standalone specialty is only FOS and silica, but we will take your point and we will look at it.
- Saket Kapoor:** Right, sir. And the very small point about this Rs. 38 crore, which you explained about the refinancing cost part, could you dwell more? And sir, where it is clubbed in the line item?
- John Mulhall:** It's in finance expenses in consolidation.
- Saket Kapoor:** And what has this translated this refinancing cost to? What has led to this Rs. 38 crore cost?
- John Mulhall:** We had a \$225 million facility in North America as a Term B, and that was due to mature in August 2020. And December '19 we took out a further \$175 million bridge loan, which basically funded the acquisition up to 25% in TCSAP from the Andover Group. At the time we were considering another Term B refinance of \$400 million. But the market, as you can imagine, in March and April was not conducive to a Term B transaction, so we switched away from that into a Term A transaction. And there were a set amount of cost fees, legal fees, things like that, that we ought to have relating to the Term B transaction, that's all.
- Moderator:** We take the last question from the line of Rohit Nagraj from Sunidhi Securities.
- Rohit Nagraj:** Sir, in terms of inventory, what is the current situation of soda ash inventories, both in Indian market and globally?
- Zarir Langrana:** Yes. So our estimate of inventory in India, if you look at what's sitting with producers, it's probably about today in the region of 150,000 tonnes to 200,000 tonnes. Global is a tough number for me to give you, but I would estimate that if you take China, Europe, Turkey, North America and, of course, the Indian numbers all put together, that could be somewhere in the region maybe of 900,000 million tonnes to 1 million tonne at best. But that is a number that's constantly winding down as producers dial back on production, take extended maintenance shutdowns.
- Rohit Nagraj:** Right. Thanks for that. Sir, and last question. In terms of soda ash pricing, are the benefit of all the input cost in terms of, say, raw material or energy cost are currently priced in? And if so, when the capacity utilization is going down, what will be the level at which producers will be able to increase the prices because the fixed cost absorption will be untenable?
- Zarir Langrana:** So I think as far as soda ash pricing is concerned, it's probably more a function of supply-demand dynamics than it is of cost. And that's really what we are seeing in the market presently, in most of the markets where we operate.

Rohit Nagraj: All right. So all the input cost benefits are currently being factored in and incrementally we don't foresee any kind of reduction in input cost as far as the raw materials or energy costs are concerned, right?

Zarir Langrana: I believe that.

Moderator: Well, ladies and gentlemen, that was the last question for today. I would now like to hand the conference back to the management for their closing comments.

R. Mukundan: Thank you. And thank you, everyone. I think this has been a tough quarter for all our units, and they have performed to the extent the market demand has permitted them to move the material in as aggressively as they could. The good news is, some of the demand held up, especially the Nutrition as well as the Agri products. The softness we saw in the Performance Materials has been primarily driven out of the flat glass demand, which we hope that the markets would begin to stabilize maybe by the fourth quarter of this fiscal year, that is the first quarter of the calendar year next.

And this has primarily driven off the softness we have seen in Southeast Asia and in South America. We believe that the Southeast Asian demand would be first one to get off the block and South America would follow soon thereafter. Those are the indicative numbers we can give you in terms of the way we see the color of the market.

In parallel, I think our strategy is intact. We are going to value-add in the Performance Materials, grow the Nutrition Science, grow the Agri Science and wait and watch the situation with our customers in the Energy Science business. And the company will continue to explore as we move forward. Also to look at what we can do with respect to the debt position of the company, especially overseas debt. And we will address these questions as we move forward in the coming quarters as we interact with you.

Very thankful that all of you have been able to engage with the company and our employees have been able to stay safe through this period. Thank you all and look forward to seeing and meeting you in the next call. We will come with more details on the plans forward. Thank you.