“Apar Industries Limited Q3 FY17 Results Conference Call”

February 03, 2017

Moderator: Thank you. Good evening everyone on behalf of Four-S Services, I welcome all the participants to Apar Industries Limited Q3 FY17 Results Conference Call. Today on the conference call we have Mr. Kushal Desai – Chairman and Managing Director; Mr. Chaitanya Desai - Managing Director and Mr. V. C. Diwadkar - CFO, Apar Industries. I would now like to hand over the call to Mr. Desai for his opening comments.

Kushal Desai: Thank you, Nisha. Good afternoon everyone and a warm welcome to the Q3 FY17 earnings conference call of Apar Industries. I would first like to outline the key operational and financial highlights of the quarter and then deliberate a little bit on our growth strategy and then open up the floor for questions.

In the last quarter, we are happy to report that there is a growth in profits for the 6 consecutive quarters in a row. Profitability has increased which is largely been driven by contribution from our conductor business, where there have been some additional value added products with good traction and a high efficiency conductors as well as from our cable business where our Elastomeric cables sales have further increased. EBITDA in the quarter grew by about 24%, so that has increased from Rs. 87 crores, a year ago to Rs. 107 crores and profit after tax for the quarter has grown by approximately 50% to Rs. 43 crores from the previous year’s Rs. 29 crores. If you look at the EBITDA and PAT margins, the EBITDA margins have increased to 9.3% and the PAT margins have increased to 3.8% compared to 7.2% and 2.4% in the corresponding period previous years respectively.

Revenue, however has been marginally impacted largely due to lower input prices compared to a year ago and in some segments like conductors, the volumes have been slightly smaller as we have produced more of the high temperature conductors which carry a larger value per unit of volume. In the 9-months’ period, we have witnessed a similar uptrend in the EBITDA, so that has grown by about 21% and our EBITDA for these 9-months has come in at about Rs. 270 crores a year ago and this year it is at Rs. 326 crores. And if you take profit after tax for the 9-months’ period that has grown by 65% to Rs. 136 crores from Rs. 82 crores. The EBITDA margin has reached 9.2% and the profit after tax margin has come in at 3.9%. So, revenues saw a marginal decline of about 5% for the 9-months and it has come in at about Rs. 3,533 crores.

This improvement in profitability is actually a testimony to the efforts that we have put in of really bringing in more higher value added products, which are now picking a momentum in terms of total volume and having some impact on the bottom line. Additionally, there are some discussions going on for the 13th plan and even though it will come out in a different form. The draft plan seems to indicate that the total investment involved will be about Rs. 260,000 crores which include about a 100,000 circuit kilometers of transmission lines and 300,000 MVA of transformation capacity at 220 KV voltages and above.

Even in this quarter gone by there has been some positive developments particularly on the high end technology front in the transmission & distribution side and $840 million mega project has been awarded to ABB of 800 KV, ultra-high voltage DC transmission line. So this is 1,830 kilometer line connecting Raigarh to Pugalur which will be amongst the longest such lines in the world, bringing electricity to approximately 80 million people. So ABB and BHEL have teamed up and this order has been awarded by Power Grid. On another note there has been further progress in signing different states under UDAY. So, 4 new states in the quarter has signed up which include, Tamil Nadu, Himachal Pradesh, Telangana and Assam. So, now 92% of the country's DISCOM debts have been covered under the UDAY scheme. However, there are still execution issues and some delay continue to be there in on the ground implementation. Honestly we have not really seen a big surge in orders coming in from the UDAY cycle, both in transformer oils and in the conductors segment. But it is eminent that it is likely to happen. We are also confident that given the above developments in the sector, it is a matter of a quarter or two before which we will start seeing the positive effects of UDAY and some of this TBCB bidding that has happened. In the mean time we continue to increase our focus on some of the export markets and as is reflected in the conductor order book from the last quarter, we have received some significant export orders, as well as our intake of high efficiency and high temperature conductor has also increased.

I would now like to spend a few minutes and discuss each of the business segments in more details. If you look at our conductor segment, the revenues came in at about Rs. 510 crores compared to Rs. 540 crores from a year ago. Exports contributed 44% of the segmental revenues. The decline goes on account of slightly lower commodity prices but also because of the change in the nature in which we have executed some of the business for a few large customers. In these contracts, we have taken on processing contract as opposed to buying the metal ourselves and this has really only impacted the revenue but then once you get down to added value, contribution margin and the EBITDA per ton, this is really agnostic in terms of those measurements. High efficiency conductor's contribution came in at 8% of the overall conductor's revenue compared to 3% from a year ago, indicating that there is a steady growth that is taking place. If you look at the EBITDA per metric ton post forex adjustment, it has increased to Rs. 13,912 per ton compared to Rs. 7,738 from a year ago.

A word on our order booking, which has actually come in at Rs. 1,611 crores as of 31st December, which is 6% higher than what it was at the end of the previous quarter. Export orders comprise about 46% of this order book and as I mentioned the company has witnessed better traction on the export front compared to the domestic side in the last quarter particularly. We have won orders in new geographies and also received our first large export order for high temperature conductors.

Our new plant at Jharsuguda, which commenced production in September is now ramping up, we have completed getting the most important approval of Power Grid and post that have started bidding on fresh business with Jharsuguda as a source of supply. If you look at the 9-months' period, the revenue for conductors has declined by 10% for the same reasons as I mentioned before. However, EBITDA per metric ton post FOREX adjustment is up 83% year-on-year at Rs. 12,053. So just to recap, what has contributed to this EBITDA increase, it can be attributed to a higher percentage of profitable orders some of which have actually been preponed and some less profitable orders which have actually been postponed for the last quarter. There has also been a fundamental growth in the high temperature conductor execution which has had a positive impact on the bottom line.

As mentioned on the downside the domestic demand has been a little bit slow, some of the tariff based competitive bidding projects awarded have not yet resulted in orders for conductors. We had anticipated that in end of the 3rd quarter we would start receiving orders from them, but the ordering cycle seems to have got delayed to some extent from the companies that have won these TBCB projects. This has resulted in the competitive intensity in the domestic segment having increased in the last few months. There are also a few TBCB projects which have been bid upon by various parties but the concerned nodal agencies have not yet opened those bids. So that has also resulted in addition to some of this awarded projects not been converted into orders, resulting in a temporary slowdown in demand in the short term in the domestic market. However, as we have always used as part of our risk mitigation strategy to go down on a global basis. We have turned on stronger focus for the export business and that has actually helped us counter the effect in the short term.

Coming to our next segment, which is the transformer and specialty oil, Revenues for the quarter came in at Rs. 423 crores which is about 6% lower compared to the previous period mainly on account of lower raw material prices. However, volumes have posted a growth of 6% and that have been driven primarily by increased demand from domestic transformer oil, white oil exports and our rubber process oil shipments. If you look at it on a global basis, shipments for the quarter came in at 90,789 KL compared to 85,606 KL from a year ago. And this actually is the highest volumes sales that we have had for a third quarter of any year thus far.

EBITDA per KL after FOREX adjustments actually declined to Rs. 3,851 from Rs. 4,871, so approximately, Rs. 1,000 per KL was the fall. This can be really attributed to the base oil prices having increased in the short term, which have impacted the profitability especially in the price sensitive segments like, white oils and process oils. A higher percentage sale of distribution transformer oils, which again carry a slightly lower margin and the sales of Industrial and automotive products has been lower which normally result in significant weighted average improvements that takes place in the bottom line and some of this has primarily come from reduced sales in the month of December post the demonetization.

We expect that volumes will start picking up from the month of February onwards as normalcy seems to have started creeping in especially into the retail distribution segment which is the most profitable segment that we have. If you look at revenues for the 9-month period they are down by about 8% from Rs. 1,263 crores on account largely of lower raw material prices. The volumes are up by 6% on a 9-months' basis, again with contributions coming in from the domestic transformer oil side, white oil export and rubber process oil. Also on a 9-months' period the auto lubricant business has still continued to show a 10% growth in volumes. So, considering this the EBITDA per KL post FOREX has come in at Rs. 5,108 per KL which is pretty much in line with the guidance which we have provided for the year.

Our sense is that the EBITDA per KL which is being declining from Q1 through Q3 should now show some signs of picking up in the fourth quarter as price adjustments takes place to compensate for some of the cost pressures that we have witnessed in the business. An important additional piece of information is that our plant in the Hamriyah Port which is part of the Sharjah Emirate has now commenced commercial production towards the end of January and we are in the process of picking up orders and gradually ramping up the production from that site.

Coming back to the auto lube segment, we have delivered a sales volume of about 5,741 KL for the 3rd quarter, which is a little lower than what we had same period previous year. But as I mentioned the sales numbers of the quarter were comparatively good considering the demonetization impact which hit both the aftermarket segment as well as the OEM sales in the month of December. If you look at the 9-month period the sales are up by almost 10%.

Now, coming to the cable business, the cable business has delivered a marginal improvement in revenues of about 3% in the quarter. So, revenues came in at about Rs. 211 crores versus Rs. 205 crores from a year ago. However, the EBITDA margin post FOREX increased significantly by almost 189 basis points to reach 9.7% and this is primarily lead from a very good product mix that we were able to put together in the last quarter.

Our Order book also stands at around Rs. 268 crores compared to Rs. 252 crores from the previous quarter and all the increase has actually come from our Elastomeric cable. We have continued to see further growth in the non-conventional energy side for us, which is the wind mill and the solar side of the business. We clearly are the largest supplier of specialty cable now in this segment as far as India is concerned and we have also started seeing more traction from business being awarded to us from the defense. We expect the solar segment to continue to improve in Q4 FY17. The power cable side has also witnessed increased demand, the margins have remained stagnant because of competitive pressures but we are clearly seeing an increase in the volume that we are able to address. Due to various cost control measures and the strategic focus on the specialty cable segment, we have been able to come in with this 9.7% versus the guidance which we are given of 8.5%.

If you now look at the 9-month revenue, we have seen a fairly robust 22% year-on-year growth, sales is at about Rs. 584 crores. The EBITDA margin post FOREX has increased 75% compared to a year ago to reach Rs. 51 crores for this business segment and the EBITDA margin for 9-months has come in at 8.7% versus our annual guidance of 8.5%. Our expansion in this segment is going as per schedule in terms of all the CAPEX that we are incurring. Most of it is focused around debottlenecking the Elastomeric side of the business, which we expect to grow by a further 15% to 20% next year and the power cable side where we are putting in some significant new machinery.

If you look at the general outlook, it remains positive. We expect all the planned CAPEX in the domestic T&D segment to start getting converted into new orders and this should likely happen in FY18. Post our recently commenced capacities, we are very well placed to monetize this growth opportunity. Our optimism remains that the effects of this demonetization in the short-term slowdown from this TBCB projects and execution issues in UDAY will quickly pass and within a couple of quarters we will start returning to seeing business flow improving. In fact these numbers have been delivered without really any impact coming in from some of the schemes like UDAY.

So with this, I would like to come to the end of my comments. Thank all of you for joining this call and at this stage we would be happy to take questions.

Moderator: Thank you very much. Ladies and gentlemen, we will now begin with the question and answer session. We have the first question from the line of Pawan Nahar from Religare Capital Markets. Please go ahead.

Pawan Nahar: After I think about 3 years, we will be hopefully making 19%-20% ROE, which is in line with our long-term average, so that was one. Second was if I were to then look at next year FY18, okay this year you say, we have not benefitted from UDAY and we have had very good profitability because of good product mix. What would you like to guide for FY18, both in terms of volumes and spreads for these segments?

Kushal Desai: We have earlier given a guidance where we are expecting in our cable business growth in the vicinity of 20% in terms of topline as well much volume growth. Profitability should also grow by between 20% and 25% because we expect some of the orders which have come in that are profitable like defense, etc., larger part of that execution will happen next year. The conductor business, we expecting may be a growth of about 5% to 6% in volume terms, there will definitely be improvement in terms of value because as we had mentioned even in some of our earlier calls, there is a lot of activity happening on the ground on the high temperature conductor side. It is slowly resulting in orders but the 2 signs that we look for is ticket size of our project as well as the breadth in terms of the number of states which are actively looking at participating in these sort of conductor opportunities. So, both of those metrics are positive, so our guidance actually for high temperature conductor is to probably target about 20% revenues of the business coming by 2020. In the next 3 years, if this picks up the way, it seems like it should, we should get somewhere in that vicinity of 20%. Additionally we are started seeing this high temperature conductor phenomena starting to also take route in some of the export market that we participate in.

Pawan Nahar: Oh yes, that was a question in fact, which market?

Kushal Desai: So, if you are seeing that in some of the South Asian markets, South East Asia also in North America where it is a standard. We received our first large order after a while from North America which is almost Rs. 100 crores in the last quarter. This is from an EPC contractor in Canada and Mr. Trump's infrastructure spend is something that should hopefully start showing some signs of coming in. So we are not targeting a big volume growth on the conductor side but looking at a better mix in terms of not only product mix but also hopefully client mix. On the bottom line the profitability will depend on the actual implementation of GST because as a company other than our conductor division we are paying a significant amount of central sales tax which our competitors are not paying, both in the oil business as well as in the cable business. So, that could affect to the tune of almost Rs. 30 crores at today's level. On the specialty oil side our guidance would be again something in the range of about 7% to 10% growth in overall volumes. Especially if UDAY starts picking up, we will see a significant uptick in distribution transformer volumes as well as some of the HVDC projects, we have large takes in terms of winning business in these segments. So, if that execution starts going on well, then we should see some uptick on that side also.

Pawan Nahar: And in terms of spreads like 9-months this year for oil you got Rs. 5,100 per KL, right? So what could you like to say for next year, should be higher right?

Kushal Desai: Yes, so our idea would be, our target is to look at about 10% higher spreads in the next financial year. So, from about Rs 5,100 per KL looking at something in the range of about Rs. 5,600 per KL.

Pawan Nahar: And for conductors overall for next year? Like this year hopefully you will be like more than Rs. 11,000 per MT it seems.

Kushal Desai: So, this year 9-months we are little over Rs. 12,000 per MT. It is a better run than we had originally planned or guided for. So, our immediate objective would be to kind of sustain that level through the entire next year. Because we do have a few orders which are actually not profitable and which were expected to the executed this year but for whatever projects related reasons, they have been pushed out and are likely to happen in the first half of next year. But we are trying to hopefully iron that out against some of the more value added business that we get in. So, competitive intensity of the domestic side in the last few months has been a bit stronger. Because as I mentioned in my earlier remarks, the order flow from TBCB that has already been awarded as well as some of these new bids which have not been opened, they have not actually flown into the industry yet. So, I think when they start flowing and then again you will start seeing just better business flow taking place and less pricing pressure. But at this stage we are factoring all that in and for the next year are looking at something which is relatively at the same level this year.

Moderator: Thank you. We have the next question from the line of Aditya Wagle from Equitas. Please go ahead.

Aditya Wagle: I wanted to ask like following up with the previous question, you are guiding that Rs. 12,000 EBITDA per metric ton guidance in conductors going ahead, approximately in that range.

V. C. Diwadkar: Yes, Rs 12,000 per ton.

Aditya Wagle: Similarly so, what could be our guidance for transformers and specialty oils?

V. C. Diwadkar: Around Rs. 5,600 per KL.

Aditya Wagle: In this ABB order out of $840 million what you think would be the percentage of conductors or something.

Kushal Desai: So actually what ABB has received is an order for transformers and so as a consequence some specialized types of transformer oil will also go into that.

Aditya Wagle: But what could be the percentage?

Kushal Desai: So we are one of the sort of key business it has still not been awarded because they have just very recently received that award from Power Grid. So the execution of that will certainly come up after several months, but it is just giving signs that this class of business is starting to grow substantially and the sizes of orders also have been very large. This gives a better trend for people like us to participate in these types of businesses. So, it is a little early for us to be able to say anything, we do not want to count our chicken before the eggs are hatched. The signs are clearly that we have some good tailwinds which are helping us.

Aditya Wagle: Sir and what would be the volumes we did it in conductors in Q3?

V.C. Diwadkar: Q3 volumes are around 38,000 tons.

Aditya Wagle: And by when is Hamriyah expected to achieve full ramp up?

Kushal Desai: We have already started the process, the plant actually received the clearances for actually commencing production just a few days ago. So, our target is to actually reach 5,000 tons per month from that facility. We expect to reach that volume may in about 4 to 5 months that seems to the target that we have. There are approvals to be received even though it is really the same product, with the same recipes, utilities need to reapprove the plant. So, if there are no major delays, then in about 4 to 5 months, we will start seeing the ramp up. But hopefully no, later is around than 6.

Aditya Wagle: All right 5000 kiloliters per month.

Kushal Desai: 5000 tons per month is equivalent to almost 6,000 KL.

Moderator: Thank you. We have the next question from the line of Maulik Patel from Equirus Securities. Please go ahead.

Maulik Patel: Couple of questions and I have asked this question in the previous call also. What could be the long-term EBITDA per ton in conductor business, because it seems that every quarter we have been doing better than the previous quarter and the expectations during the last concall you said that probably EBITDA per ton will come down, but it does not come down. That is number one. You mentioned that 8% of your conductor revenues is from the HEC. What could be this optimal mix in next 2 to 3 quarters which is again going to guide something related to the EBITDA per ton?

Kushal Desai: This is to answer you first question Maulik, our numbers have come in better than what we had planned partly from the luck of the more profitable order book getting preponed and some of the lower profitable orders, getting pushed out into FY18, , actually those projects getting stuck. So, some of it is actually just a short term tactical benefit that we have seen. From a structural stand point, the high efficiency conductor business has grown to 8%. We will start seeing it gradually going up, it is difficult to track in necessarily quarter-by-quarter but in a long-term strategy is to get it upto about 20% by 2020. So, that is about 3 years from today. So, approximately about 3% to 4% increase every year in terms of that volume of business and we attribute that to increase business domestically as well as some of the export markets also now starting to show signs. We have reached certain critical mass to be able to bid on these projects overseas. Because without having a certain volumes and lines which have been commissioned for certain durations of time you do not end up meeting the minimum criteria that is required to participate in these tenders. So, in most of the range of the high temperature conductors today, with the work which we have done over the last 3-4 years, we have garnered enough volumes to be able to now start bidding on some of these projects even overseas. So, that is a good development from that stand point.

Maulik Patel: What is the current volume as percentage from the HEC, around 5%-6%?

Kushal Desai: It is at 8%.

V. C. Diwadkar: 8% for the quarter and 11% for 9-months.

Kushal Desai: And in fact there are number of tenders which have been bid and open and they are in the stages of actually negotiation and business being awarded. So, I would see the opening order book for FY18 having some reasonable high temperature conductor.

Maulik Patel: Second question is on the working capital side, Because of commodity prices both aluminum and the base oil has gone up. We got significant benefit of commodity price going down last year in terms of our working capital, which was very low last year and this year the prices have gone up. So, what kind of working capital right now we are sitting on, if you can give us an absolute number that could be very helpful?

V. C. Diwadkar: Transformer Oil, capital employed is close to around Rs. 300 crores and cable is Rs. 328 crores and conductor is around Rs. 500 crores and the oil fixed assets are Rs. 86 crores, conductor net fixed asset is Rs. 197 crores cable is Rs. 178 crores.

Maulik Patel: What will be the CAPEX guidance for this year and the next year?

Kushal Desai: So, actually Maulik just to recap, you got the specialty oil side having working capital and involvement of a little over Rs. 200 crores about Rs. 215. The Rs. 150 crores in the cable side and about Rs. 300 crores on the conductor side, so that is around Rs. 650 crores to Rs. 670 crores. There is no control, if commodity prices goes up but the company's balance sheet and working capital limits in place will post no problems in terms of being able to accommodate the higher commodity prices as well as the volume growth which we are expecting.

Maulik Patel: Sir, I know our balance sheet is one of the best in the industry and I am also looking from the operating cash flow perspective that this year will be significantly lower because our overall working capital will go up.

Kushal Desai: Yes, there will be some impact because of interest not only from the higher commodity prices, however interest rates in India are coming down but all the Dollar rates have already started hardening. So, our expectation is there will be some creep in terms of finance cost but this is going to affect the whole industry and so, I do not think on a relative basis we have any disadvantage. The good news is that our balance sheet can accommodate this without having to go to the banks for any increased limits or anything of that sort. So, we should not have any operational issues coming out of this.

Maulik Patel: That I am pretty much clear sir on that side. I was just asking the CAPEX for this year and the next year?

Kushal Desai: So, the CAPEX for this year we got only one major project.

V. C. Diwadkar: Already in 9-months we have incurred up to Rs. 105 crores on the consolidated levels, including the Sharjah plant and next year CAPEX will be mainly in conductor.

Kushal Desai: So, we are looking at approximately Rs. 60 crores in terms of CAPEX for FY18 versus Rs. 105 crores we had in the 9-months plus about another Rs. 25 crores which we will have in the last quarter to complete the major cable expansion.

Maulik Patel: And out of that what is the CAPEX for the Sharjah plant?

V. C. Diwadkar: Sharjah total is around Rs. 105 crores. That is completed, entire capital is completed.

Kushal Desai: Spread between something that was incurred last year and this year.

V. C. Diwadkar: Correct.

Moderator: Thank you. We have the next question from the line of Saurabh Patwa from HDFC Mutual Fund. Please go ahead.

Saurabh Patwa: Sir, just as you mentioned in the opening remarks that since you believe that part of revenue was slower because the raw material was outsourced or as in like we did only a processing job, so just wanted to understand the impact on EBITDA. So, the EBITDA per ton, is it higher because that the volumes taken as a denominator would be lower?

V. C. Diwadkar: No, it is not like that actually. It does not affect the EBITDA but it affects the topline because the sales value, it does not capture the sales value only processing charges are captured and that gets into the EBITDA. And the tonnage is considered for EBITDA.

Saurabh Patwa: That is what I am asking sir. So, the benefit is taken in EBITDA?

V. C. Diwadkar: And the quantity is also considered for

Saurabh Patwa: So, the quantity itself is also considered.

Kushal Desai: So, what happens in this instance is that instead of Apar buying the metal some of these larger TBCB type projects, clients can actually get extended credit for metal, particularly for aluminum. It is not a very difficult thing to do, at the same time what it does for Apar is that it limits our exposure to a particular project and particular client. So, it also fits into our risk assessment metrics. So, it is like a win-win situation for both parties. You are agnostic from the value addition onwards, so all the metric that we reported will not get affected other than the sales value. The topline does not have actually the component of raw materials in it.

Saurabh Patwa: So, just from a technical point of view, now we will have a maybe in the quarter or two, since when Hamriyah will also start generating a good amount of revenue. So, we will be given the consolidated numbers going forward or will we still continue to give the standalone numbers as they are right now because otherwise after in the fourth quarter when you will declare consolidated from a next year point of view then the diversion would be higher as compared to what it is now.

V. C. Diwadkar: Yes, I agree with you actually. We are considering to give consolidated number from quarter one FY18.

Saurabh Patwa: And just this one last question, what would be total amount of debt right now?

V. C. Diwadkar: Debt is around Rs. 394 crores, Rs. 125 is the long-term debt and Rs. 269 is the short term debt.

Moderator: Thank you. We have the next question from the line of Prithviraj from Unifi Capital. Please go ahead.

Prithviraj: My question is regarding your cable segment. Can I have a breakup of solar and wind cables and Elastomeric cables as a percentage of the cable revenue?

Kushal Desai: So the solar cable, etc. actually get embedded within, the specialty solar cables, which get embedded within the Elastomeric segment. So, if you see that approximately in the 9-months' period Elastomeric cables for us has been approximately 40% of revenues and the power cables have been approximately 50% of revenues.

Prithviraj: And in the previous con call you mentioned that spot oil price is lesser than your contract oil price, so has it increased now?

Kushal Desai: So in Q3 what we witnessed was that there was a big oversupply situation with the Adnoc base oil refinery coming on stream and as you know any big refinery actually takes some time particularly in base oils to find an equilibrium on their clients. So, large parcels were offered to the Indian market on spot. So the spot prices actually came down very sharply because of that. So, the gap between our contract prices, spot prices actually became negative where this spot prices were lower than our contract price and normally contract prices are relatively quite competitive. So, this actually put a pressure on that, as you move into the fourth quarter we pretty much see that phenomenon is been pulled off because in fact Adnoc refinery had a fire in the first week of early January. So, their production is down which has actually resulted in a base oil scenario becoming pretty tight because there has been a few other refineries too, that had outages. So, we do not see that problem in the fourth quarter and that is why in my opening remark, we have mentioned that the decline which we have been seeing in the oil EBITDA by almost the Rs. 1000 per quarter from Q1 to Q2 and then Q2 to Q3, we expect that to now sort of reverse in Q4 because we are not only having a more stable base oil supply scenario but also some of the price increases which we had to eat towards the end with all these demonetization and all these things, we should be able to pass them through in the fourth quarter.

Prithviraj: And one final question from my side sir, so in your conductor business, you have said that most of the high efficiency conductor has been preponed. So, do we see any drop in Q4 margin?

Kushal Desai: Well, preponement is not necessarily of high efficiency conductors but it is been of the more profitable orders even of conventional conductors that we had. So, there will be a fall in the profitability in the fourth quarter compared to the first 3 quarters but it will be still higher than the guidance which we were offering for the year. However, as we get into the next financial year, we would pretty much try to maintain the same level of EBITDA per metric ton. The sooner GST gets implemented, if it really gets implemented on 1st July then our Jharsuguda facility actually will start reaping some benefits. Because there are some anomalies in the sales tax structure in the state of Odisha, where we are not able to get the full VAT credit. So, when you are buying from a smelter in Odisha you are not able to take the full benefit of the VAT credit and with GST coming in all those rules get rewritten and uniform across the country. So, the benefits which are there or actually being located near this smelter and being located near the customer will transparently fall to the bottom-line, because this offset of losing value added taxes credit that will actually disappear. So, GST implementation for us is a very crucial across all the 3 divisions.

Moderator: Thank you. We have the next question from the line of Ankit Soni, from Karvy Stock Broking. Please go ahead.

Ankit Soni: Sir, actually EBITDA numbers in conductor segment is showing a good growth. So, what is considered as a driving factors for that?

V. C. Diwadkar: Yes, as I said earlier, it is because of the more profitable conventional orders and increased high efficiency conductor execution. So, we have executed close to about 11% of high efficiency business as against last year 6%. Last year first 9-month was only 4%. So comparing YTD year on year, actually it is 11% high efficiency this time against 4% last year, plus the conventional orders that were executed are also more profitable orders.

Ankit Soni: On that front do we stand on the same lines of 15% HEC revenues to be contributing from total segment revenue?

V. C. Diwadkar: At present it is 11%, we are hoping that this year we will close to around 11% only, next year we can target around 3%-4% more HEC revenue.

Ankit Soni: Just on a clarification point sir, like you said Jharsuguda plant will be manufacturing around 5,000 metric tonnes per month. So, the total capacity comes off to 60,000 tons, so can you just clarify?

V. C. Diwadkar: Jharsuguda plant will manufacture only 3000 metric tonnes. It is 35,000 metric tonnes plant.

Ankit Soni: Sir, just before somebody said that 5,000 per month metric tonnes will be manufactured?

V. C. Diwadkar: That was Hamriyah actually. That is the specialty oils Hamriyah, Sharjah plants.

Moderator: Thank you. We have the next question from the line of HR Gala from Pranav Advisors. Please go ahead.

HR Gala: Two clarifications, one you already said that you do not know what kind of value this ABB contract can fetch you. Sir, my question pertains to this one slide number 19 where we have said that strategic investment of over Rs. 550 crores, so out of that how much has been spent till say, FY17 end?

V. C. Diwadkar: Almost everything has been spent now actually.

HR Gala: So, nothing is pending, these are all the projects which are over.

V. C. Diwadkar: Yes.

Kushal Desai: On the CAPEX front, Mr. Diwadkar earlier had mentioned that our 9-months spent has been Rs. 105 crores. We have approximately Rs. 25 crores which will come on stream in the fourth quarter to complete some of the cable projects which are still in CWIP and our next year's plan is to do about Rs. 60 crores of Capex. So, hopefully next year actually the increased free cash flow will also increase.

Moderator: Thank you. We have the next question from the line of Vikrant Kashyap from Kedia Securities Private Limited. Please go ahead.

Vikrant Kashyap: Sir, my question pertains to conductor order book. It is Rs. 1,611 crores and what is the execution period?

V. C. Diwadkar: It is about 125,000 metric tonnes. So, execution period you can say around 8 months or so.

Vikrant Kashyap: And sir just for a clarification sir, when a new tender comes in, how long it takes to convert into final order for the company usefully on and average basis?

Chaitanya Desai: It depends, sometimes the client has a deadline to meet, so they will go for a very fast delivery and at times they do have sufficient period but generally we are seeing the trend that it is getting compressed compared to earlier days when Power Grid used to be the monopoly that time, it used to be between 18 and 24 months. Now we are seeing within 6 to 12 months generally we get the business to execute.

Vikrant Kashyap: Sir, on your guidance for 2020 you have said HVDC should be 20% of a Conductors revenue that you were targeting, may I know what is it contributing right now?

V. C. Diwadkar: Right now, it is 11%.

Vikrant Kashyap: And sir, one more question. Do you have any plan of demerger of any of your vertical in these 2-3 years?

Kushal Desai: Not really. Actually we do not have anything immediately planned, if you see the composition of these 3 businesses in a period, where there is a lot of expenditure happening in the T&D segment. The composition of these 3 businesses actually it put us in a very strong position to participate across all the sub segments of the transmission & distribution side and we have been for while maintaining that we were not getting into a phase, where all the 3 businesses were able to kick in and start delivering positive numbers above par. But in this financial year quarter-on-quarter we have been able to see that happening and so, the big jump which has happened compared to the previous year really is with all 3 business segments actually starting to positively contribute. And in FY18 it seems pretty likely that the same should continue and thereafter because as the cable business was sort of dragging the rest of the profitability down that has clearly turned the corner with not only volume but also with fairly rich product mix.

Vikrant Kashyap: Sir, we are also increasing our cable capacity. So, what is our target capacity and what is it currently?

Kushal Desai: So cables capacity is very difficult to measure because of the large variety of products that we have, but we are looking at approximately increase in revenues next year of (+20%). So, this year also the 9-months we have grown revenue 22% and so on that higher base next year also we planned to repeat similar growth in revenue.

Vikrant Kashyap: Sir, on buy back, if may ask how successful has been the buy back and did promoter or promoter group also participated in that?

V. C. Diwadkar: We just got the SEBI approval. So, further process is on now actually and buy back will be completed by mid-March.

Moderator: Thank you. We have the next question from the line of Varun Agarwal from BOI AXA Mutual Fund. Please go ahead.

Varun Agarwal: Sir, just I missed initial part of the call. So, I had just few questions about certain segments; first of all cable segment. We had done really well in cable segment, so is this 10% margin sustainable for us?

Kushal Desai: Yeah, actually the sustainability of the margins are pretty much there. I would look more at the 9-month margin profile which is 8.7% and so, as we had mentioned even in your earlier call our FY18 target is to start looking at getting into double digit for EBITDA Margin. From that stand point yes, it should be sustainable.

Varun Agarwal: That will be more due to the overall mix change or operating leverage?

Kushal Desai: It is actually both, because see if you look at last 5 years this business has grown at about a 16% CAGR. Last year in 9-month growth is 22% we expect (+20%) as we go from FY17 to FY18. So, clearly scales and operating leverages is one of the factor but that alone cannot contribute to 200 basis points change, this is also coming from the mix of product that we are targeting. If GST comes in then we should have some more upside coming from the contribution on the GST implementation because some of our biggest competitors are actually not paying 2% tax because either they are in tax free jurisdiction or they are paying a tax which is 0.5%, 0.75%, etc. So, I think to answer your question sustainability seems quite possible.

Varun Agarwal: Sir, in specialty oil business, you said the overall there was a little slowdown but going forward you said there is certain orders which can help us in improving the scenarios, so how is our overall outlook in specialty oils, specifically about transformers oil business?

Kushal Desai: See, on the transformer oil side domestically after a while we have seen double digit growth. So, the volume has not been the issue, the problem has been on the profitability front which as we had explained, there was some reductions that took place in spot versus contract which is the replay, also there was some increases that happen towards the end of the quarter given that general crude and gas oil started moving up. So, combination of these 2 things put some effect, also there was a reduction that happened in the weighted average EBITDA because sales of industrial oils through our distribution channel as well as automotive oil across the board fell and these are the 2 most profitable segments. This was a fall out of the demonetization effect that happened particularly in the month of December. So, we see the reversal of the EBITDA per KL happening in the fourth quarter.

Varun Agarwal: Because of oil prices going up, so do we see some impact on our inventory losses?

Kushal Desai: No, in fact on the contrary there could be some upside only in the inventories that we hold. So, in our case because we have fair amount of ratable business that happens from clients, I do not think we are going to really see a lot of inventory gain. Whatever improvements happen should to a larger extent happened from just fundamentally booking orders at the right price levels going forward, catching up for the increases that are happened on the cost side.

Varun Agarwal: 2 more questions. One on this auto lubes business, how is the outlook for that, second can we improve margins there?

V. C. Diwadkar: On the auto lubes side, the EBITDA for KL for us is much higher than in any of the other segments. We are very bullish on growth in the automotive lubes segment because not only is the company itself gaining traction on its distribution and the new products which have been launched are receiving higher sales volume but generally we expect that the auto market itself should show positive sign of growth. The Rabi crops has been pretty good, it will have an impact finally in terms of tractor sales. Similarly, you got two wheeler demand expected to go up, passenger car likely to go up, even commercial vehicles indications are from various industry bodies and that also is likely to go up. So, putting all that together, I think auto sales is an area where we would target double digit growth at least for the next few years.

Varun Agarwal: So, here in Auto Lube segment do we pass on the price increase / decrease on regular basis or it is something where which is like market driven?

Kushal Desai: The prices increase, there is a latency factor for passing on the prices. Usually the call is taken by some of the largest players like Castrol, who make the first move on prices and then the whole industry has room to basically correct, but essentially you have almost 2 to 3 months lag for that effect to finally take place. So, generally if the increase is not very sharp then within a couple of months it gets recovered.

Varun Agarwal: So, one last question on conductor business, so you said in your initial remark that due to TBCB, some of the orders getting delayed. So, there was some delay in ordering, so how soon do you think that can pick up and how much impact that can have on our overall order book?

Kushal Desai: So, there are 2 parts to what I mentioned. There are certain tariff based competitive bidding projects that have already been awarded and then you have an ordering cycle taking place by the winner of that bid. So, we have not seen conductor getting ordered yet, it has taken a little bit longer than typically we would have liked. So, that is one part of the problem. The second part of the problem is that there are several bids which various parties have bid on for projects but those bids have not been opened and finalized within the time frame that the nodal agencies had indicated. I would say that within 3 to 6 months you should start seeing, it could even happen as early as this quarter especially for those projects which have already been awarded because with aluminum also strengthening to some extent, I am sure these companies will have to, because their bidding is not a fixed basis. So, they need to form up their aluminum procurement strategy, an ordering strategy and there is no sign of commodities coming down. So, I would imagine that they would probably now being looking more seriously at starting to place these orders out.

Varun Agarwal: So, will that have any impact on our overall margins in the conductor business because of as you said in the commodity prices have moved up and if there is any delay so, does that impact our margins ?

Kushal Desai: No, our margins should not get impacted because we do not speculate on metal we do everything back to back, where actually we see a short-term problem in terms of conductor margins is only because a lack of activity in this TBCB area in general has resulted in less order booking taking place by the industry. So, competitive pressures have been a bit high, but we see this as being a temporary phenomenon and once the ordering cycle starts, we should start seeing again normalcy coming in. So, from that stand point we do not really see that as a very long term thing.

Varun Agarwal: So, my question was with respect to the earlier thing, earlier method versus TBCB, so has any difference in margins or do you think margins are at par in TBCB also?

Kushal Desai: Well it is difficult to just predict generally, because these are all negotiated deals with the winners of the project. So, there is no appreciable improvement or reduction compared to what we have been doing in the last few months in terms of that order booking.

Varun Agarwal: Basically you will maintain our margin?

Kushal Desai: Yeah, that is why guidance for next year also is that we would like to try to keep and achieve these sorts of numbers through FY18?

Moderator: Thank you. We have the next question from the line of Alok Deora from IIFL Please go ahead.

Alok Deora: I just had couple of question. One was in your presentation you have mentioned about taking price increase in the specialty oil segment in Q4. So are you seeing that kind of demand where you would be able to take this price increase or would it be like very marginal increase which we would be able to take?

Kushal Desai: The increases have already started, we have already started quoting from January itself higher prices, some of them have already fructified and as you move into February we are seeing, the next phase of it getting implemented. So, I would say largely that by March we would have recovered pretty much most of the impact of the higher raw material prices. See, you do have a lag, because generally the client base is quite large and in the case of the automotive and industrial side you cannot change prices every month but because the increases have been reasonably significant you see crude from the mid-40s now in the mid-50s. So, that $10 is large enough to sort of create industry wise and globally prices have started going up of finished lubricants. So, it is really just a matter of couple of months before which it catches out.

Alok Deora: And one thing in this cable segment you also manufacturer this optic fiber cables. So, just wanted to know that in this budget we had this news on Bharat Net program or increased allocation, so does that impact our business positively in any way?

Kushal Desai: Yes, it does in the sense that after an initial spurt of ordering that happened by actually the UPA government before the Narendra Modi government came in, very large orders were placed for this fiber optic cables, there is been actually a big lull from both BSNL and BBNL. The number of tenders have been few and the values also haven't been very large. They have now started picking up and with the increased allocation in the budget hopefully we should start seeing larger tenders on the optical fiber cable side. However, the dampener in that particular segment is that there is a big shortage of optical fiber because China has ordered what is more than 10 times what India is looking at ordering in the same timeframe. So it is kind of sucking up the worlds excess fiber supply, so there is going to be a pressure in terms of margins for any companies that buy its fiber in the market and then makes optical fiber but in our case it is about 10% of our business and hopefully with the tendering and the volume increasing the higher fiber prices will any way be factored into new pricing of projects. So, we do not have a big back log. We will be in a position to participate in most of these new tenders.

Alok Deora: So, we procure the fiber from local player like Sterlite or the imported?

Kushal Desai: Both.

Alok Deora: But it is not that profitable, so any way

Kushal Desai: At the moment, there is a lot of cost pressure coming from the optical fiber in the manufacture of an optical fiber cable. So, fiber manufacturers are actually today in a very strong position globally because of their profitability. Given that there is a shortage of fiber especially as I said just now is driven really by a very huge program that China has launched.

Moderator: Thank you. We have the next question from the line of Dhiral Shah from GEPL Capital. Please go ahead.

Dhiral Shah: Sir apart from this Bharat Net addition which has been announced in the Union budget, any other key positive take away?

Kushal Desai: Well, from the budget actually there is no negative surprises, there have been larger allocations in most infrastructure segment. We expect non-conventional energy particularly, the solar side to pick up fairly strongly. It is a big increase compared to this year, 50% more actually in financial year FY18 over FY17. So, solar side obviously will be a positive, additionally increased allocation in terms of railways CAPEX, which have been a laggard, the defense and the increased spending considerably on the type of cable we made, Railways we have not nearly seen much improvement. With the increased allocations which are there in the segments that we participate in, we would expect that railway procurement over the next 2 years will substantially go up. So, in that sense it is all general positives, there is no negatives that have really come out of the budget for any of our businesses.

Dhiral Shah: And also this rural electrification by May 2018, so this is going to benefit us, 100% rural electrification and there has been incremental allocation to Deendayal Upadhyaya integrated power development scheme?

Kushal Desai: So, these are two older schemes which are there that fall under UDAY which is, Deendayal Upadhyaya and IPDS. So, the increased allocations means that there will be more spending happening, so it is a direct impact in terms of our conductor and cable business as well as in the case of oil, Deendayal Upadhyaya and IPDS actually benefits the distribution transformer segment to a much larger extent. Having said that even the draft plan for the 13th Five-year period sort of which is the next five-year projection from Central Electricity Authority has a pretty healthy procurement of transmission lines as well as transformation capacity. So, power transformer as well as conductor should both see sustained demand taking place over the next 5 years, as this next five-year plan is actually implemented. Outlook looks quite comfortable at this stage.

Dhiral Shah: Sir how much you may have gained from this 12th Five-year plan then?

Kushal Desai: Well 12th Five-year plan was a huge increase over whatever had ever been executed before and as you would see, the biggest gains are usually in the last year of the plan. So, it is actually apparent from even our numbers that this FY17 has been better that FY16 and FY15, etc. So, our company will clearly benefit from any tailwinds which are there and any increased spending that happens anywhere in the T&D segment. Any of the sub segments grow we should start seeing some traction or the other happening in some part of our business.

Dhiral Shah: And sir, in last concall you have stated that Rs. 50,000 crores worth of order to be announced in the system. So Q3 was like a lull period. So do you expect same amount of order to announce in Q4?

Chaitanya Desai: Yeah, it is not very clear as to what ultimately PFC and REC do because we have discussed earlier there have been some delays in various bids. But at some point those projects will get implemented.

Dhiral Shah: By March you expect, a big bang announcements something like that?

Chaitanya Desai: No, I think there will be more implementation happening at some point on the UDAY front. So, I think right now that will be the main concentration of the government and as you mentioned the electrification to be completed at the earliest, in fact they are talking about bringing it 2 years in advance of their initial plans. So, there will be a lot of implementation happening right now. Also we have mentioned earlier with the IPDS scheme, there will be a more this semi urban work happening and our reconductoring work also may improve, more cables being used. At the moment if you see there is no lack of announcements, there is no lack of allocation it is really certain implementation related issues whether it is politics between center and state of placing of orders and then further components of those orders going into the system. So, I think after the lull that has been there for the last few months that catch up should happen. You started seeing like for example ABB thing it was hanging for almost 8-9-months and it has come through. So, there is a lot of pressure coming from the government to deliver action, we are just patiently waiting and we have the capacity, we have everything in place. So, as the business start getting awarded we are pretty much there in terms of picking it up.

Dhiral Shah: And sir, what will be the scope of business for us in that $840 million announcement?

Kushal Desai: Well the scope is only supply of transformer oil, so transformer oil is typically about 5% of the value and provided we get a substantial portion of it. The execution strategy, ABB is still evaluating that because it has just got the order very recently. But the point I was trying to make in the opening remarks is that the CEA and the various utilities are now getting much more comfortable in executing complex projects of high voltage of transformers and that augers very well for Apar as a group and for our transformer oil business. As this business grows, we should start seeing obviously higher end products getting executed.

Dhiral Shah: And sir lastly sir, what is the percentage of value added revenue contribution to the overall business, combining the 3 segments?

Kushal Desai: It is difficult to pick up, because each of the sub segments also has pieces which we try to focus on the upper end of the market.

Dhiral Shah: Sir, what will be the contribution in 3 segments, let say 20%-30% something like that and you said in conductor it is 11%.

Kushal Desai: That is high efficiency conductor

V. C. Diwadkar: Cable is around 40%.

Kushal Desai: 40% is the Elastomeric cables which has a more profitable cable for us.

V. C. Diwadkar: And oil side the high KVA transformer is around 35%.

Dhiral Shah: When you combine all this thing, what will be the proportion then in overall revenue?

V. C. Diwadkar: Close to 35%.

Dhiral Shah: And sir what is the export revenue?

V. C. Diwadkar: On an average export revenue is around 35% to 40%, this time conductor has done more actually 44% this time, this quarter actually. But overall it is around 35% to 40% is export revenue, the company as a whole.

Moderator: Thank you. We have the next question from the line of Anand Gurnani from Sameeksha Capital. Please go ahead.

Anand Gurnani: Most of my questions are answered, just one clarification needed, in early part of concall you mentioned that due to central sales tax and GST coming in Rs 30 crores kind of impact could be there post-GST comes in for oil and conductor business. Sir, can you elaborate on that?

V. C. Diwadkar: For oil and cable business, basically we are paying central sale tax but our competitors are in a location where they are not paying the central sales tax. So, at present there is competitive disadvantage to us. Once the GST comes in everybody will be on par.

Anand Gurnani: So, Rs. 30 crores odd benefit, do we directly expect it to flow to the bottom line?

V. C. Diwadkar: Not necessarily actually. But it helps us in the competitive scenario.

Kushal Desai: See today this money, this 2% is actually being absorbed by Apar in its pricing. So, as a consequence when GST comes in it become a level playing field there will be no longer a need for Apar to actually absorb the 2%. As a consequence it is the chances of it then, the margins getting expanded by that are very high. Because competition is already not paying any taxes or paying very marginal taxes compared what we are paying. It is a combination of central sales tax and local body tax which we pay here in our oil plant in Rabale. Put together it is little over Rs. 30 crores based on FY17 expected numbers in the 4 quarters.

Moderator: Thank you. We have the next question from the line of Sachin Mehta from Centrum Broking. Please go ahead.

Sachin Mehta: Sir, most of my questions have been answered, I missed out few more questions, this is regarding conductor business. So, if you could give some color about the order book of Rs. 1,611 crores that we have. What is the quantum of low margin orders which are pending to be executed now that we see getting executed in FY18?

V. C. Diwadkar: We do not give this details actually.

Sachin Mehta: And sir the low margin as we see is in the range of Rs 8,000 to 9,000 per MT?

V. C. Diwadkar: See, there will be orders with several EBITDA margins actually it can start from Rs 5,000 it can go up as I said.

Sachin Mehta: And in the next year when we will look to achieve the similar kind of a run rate on the conductor side, one of the contributors will be the HEC revenue and margins growing from what we see as 11% growing to 14%-15% next year and at the same time you see some kind of pick up on the competitive intensity as well in the domestic side. So then when you are looking at, we will have some part of the lower end orders also getting executed next year. So to offset it, is cost efficiency the only major driver apart from probably some additional exports that will kick in on the HEC side?

V. C. Diwadkar: No, actually what has happened, the low margin order now it has got spread out actually. Because right in the beginning of the year we were having good amount of low margin orders. But because some of these projects got delayed actually, they got spread out, so that impact will not be felt now that much. That is why we are saying that next year we will be able to maintain the Rs. 12,000 per ton EBITDA margin. Plus of course there will be some gains coming out of the GST, some gains coming out of the Jharsuguda plants

Sachin Mehta: Some cost efficiencies.

V. C. Diwadkar: Cost efficiencies will be there, correct.

Sachin Mehta: And sir just coming back to what Saurabh has asked earlier we had some kind of outsourcing done on the conductor side, which is why you look at the EBITDA per ton, it looks stronger but when you look at the revenue per ton, it looks declining sequentially. If I look at your revenue cut and it has come of sequentially on the conductor sides of about 14% whereas in the same period, if I just have to compare the falling price of aluminum which is the major component of RM and having a reflection in the topline as well, it has moved up about 5%. So, that anomaly only because of the reason earlier specified.

V. C. Diwadkar: Yes, that anomaly is only because when you do processing, the sales price is not captured in that.

Kushal Desai: So, to evaluate this business, the 2 metrics that we would recommend for any analyst to look at is the volume sales, the volume execution that is happening and EBITDA per metric ton. If you look at these 2 measures then it is agnostic of this other sort of thing and it gives you really the crux of how well the business has run without any confusion taking place. So, I would recommend that these 2 metrics and that is why we actually focus on these 2 metrics, which is the total volume and the EBITDA for metric ton post the FOREX adjustments. So there you get an apple to apple comparison across each quarter.

Moderator: Thank you. Ladies and gentlemen, that was the last question. I would now like to hand the conference over to Miss. Nisha Kakran for closing comments. Thank you and over to you, ma'am.

Nisha Kakran: I would like to take this moment to thank the management for giving us the opportunity to organize the call and all the participants to join in the call. Thank you.

Kushal Desai: Thank you very much for your patient listening and participation. Thank you.

Moderator: Thank you. Ladies and gentlemen on behalf of Apar Industries Limited that does conclude the conference call. Thank you for joining us and you may now disconnect your lines.