Apar Industries Limited
Q3 FY18 Earnings Conference Call
January 30, 2018

Moderator: Good day, ladies and gentlemen and welcome to the Apar Industries Limited Q3 FY18 Earnings Conference Call hosted by Four-S Services. As a reminder, all participant lines will be in the listen-only mode and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during this conference call, you may signal an operator by pressing '*' then '0' on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Lokesh Bhati of Four-S Services. Thank you and over to you, sir.

Lokesh Bhati: Thank you. Good afternoon, everyone. On behalf of Four-S Services, I welcome all the participants to Apar Industries Q3 FY18 Results Conference Call. Today on the conference we have Mr. Kushal Desai – Chairman and Managing Director and Mr. V. C. Diwadkar – CFO Apar Industries. I would now handover the call to Mr. Desai for his opening remarks.

Kushal Desai: Thank you Lokesh. Good afternoon, everyone and a warm welcome to the Q3 FY18 Earnings Conference Call. I would like to begin the call with giving some industry highlights that have transpired during the last quarter and follow that up with financial analysis of this quarter's performance. Post that, we can open up the floor to questions.

So the last quarter has been relatively good for the transmission and distribution sector which has seen significant increase in the primary order flow that has come in. Key players participating in T&D infrastructure both domestically in India and Indian players who are bidding for jobs overseas have received orders of almost Rs 12,773 crores compared to about Rs 4,500 crores in the previous quarter. A large portion of this actually has come in from business that has been won from overseas. The domestic market is also reasonably poised and there are some strong drivers in place such as the integration of renewable energy, shift towards higher voltage level systems and also an up gradation of the existing infrastructure. There is continued positive progress in some other policy initiatives which is also adding to the momentum.

The Saubhagya scheme which was announced in Q2 FY18, has been launched in Assam, Madhya Pradesh, Jharkhand and Mizoram. Also as far as UDAY is concerned states like Nagaland, Andaman & Nicobar, Dadra & Nagar Haveli, Daman and Diu have also signed the MOU with the government. So, today we have 27 states and 4 union territories which are part of UDAY. There has been some progress in terms of the effectiveness of UDAY as the losses for DISCOMs participating in the UDAY scheme have come down from Rs 51,590 crores to about Rs 36,905 crores. So, these have been some positive developments, on a slightly more somber note we have to take cognizance of the fact that prices of commodities including aluminum have risen quite sharply in the last 6 months particularly.

Given the fact that tariff based competitive bidding is ultimately on a fixed price basis as quoted by the developer. There is a cost escalation which will have happen relative to budgetary costing for CAPEX of these projects not only from aluminum but also in terms of steel and some of the other commodity ingredients that go into any such project. So, this will put a strain on the profitability and even timing in terms of implementation throughout the entire supply chain. There has been delay in ordering particularly in the domestic market. However, these projects will get executed in the near future as they are finally time bound, what may likely happen is there will be reduced margins through the entire supply chain. However, we see the industry order book growing sharply as we move into FY19 through the awarding of these projects as well as the numbers of substations which have been given out. Other segments of the business including auto segment, defense segment, railways, etc. which have an effect in terms of our cable business, conductor business and transformer oil business have all been seeing substantial growth taking place.

We do feel that managing commodity prices and commodity price risk will be a major priority from now through till FY19. Also, the government is expected to introduce the electricity amendment bill that provides 24x7 power and direct benefit transfers in the budget session. The new law will impose hefty fines on DISCOMs for outages. So if this plan actually does get implemented it will do away with cross-subsidy in the national tariff policy which would provide a big relief to industrial consumers. But the spending in infrastructure that DISCOMs will have to do to ensure this 24x7 power without outages will actually further drive demand for product that company like Apar have to offer.

Coming to more specific financial results in the quarter Apar saw strong revenue growth on a year-on-year basis. Margins were impacted on account of some of the cost escalation from the commodity price increases in particularly the conductor segment. However, the profitability in both the oil business and the cable business has been better. The performance has also improved compared to Q2 FY18 as some of the effects of the GST has started stabilizing. As I mentioned earlier there are further increased indications of CAPEX spending from not only transmission and distribution but also railways and the defense sectors. If you look at our consolidated revenue it came in at about Rs 1,500 crores for the quarter which is up 31% from Q3 FY17.

The EBITDA for the quarter actually declined from Rs 107 crores to Rs 99 crores resulting in an EBITDA margin of about 6.6%. Profit after tax for the quarter came in at Rs 40 crores versus Rs 43 crores. Part of this was also affected due to a much higher provision of depreciation as the company has invested substantially in CAPEX for new capacities as well as for production of new products. So the profit after tax margin actually came in at about 2.6%. Depreciation for the quarter is up 23% at about Rs 14 crores. As I mentioned, profitability improved both in the oil lubricants business as well as the cable business compared to Q2 FY18. Looking at YTD 9 month's picture revenue is up 15% at around Rs 4,054 crores. The EBITDA was down 13% at Rs. 285 crores and the EBITDA margin has come in at about 7%. EBITDA has been impacted on account of some of the more competitive pricing particularly in the conductor business, higher raw material price from the commodity increases and some of the GST implementation effects that really showed up in basically Q2 FY18.

Profit after tax for this 9 months period came in at Rs 105 crores which is about 23% lower than the same period previous year. The new manufacturing assets that we have put in place have been commissioned in Jharsuguda and Lapanga in Orissa. The power cable plant in Umbergaon is also now producing at close to full capacity and the new plant in Hamriyah also had its highest production in the last quarter. The commissioning of these facilities with the movement of plant and machinery in some of the cases have weighed on the bottom line. We have also further planned more movement of machinery and today the capacity in the Orissa belt which is at Jharsuguda stands at about 80,000 metric tonnes, 50,000 tonnes higher than what was originally planned. This movement has been done primarily keeping in mind all the benefits accruing from GST with the locational advantage coming out of the Orissa location.

If we now look at each of the business segments, our conductor revenue was up 25% at Rs 638 crores compared to Rs 510 crores in Q3 FY17. Export contribution came in at 47% of the segmental revenues. The segments order book today stands at Rs 1,531 crores which is higher than Rs 1,406 at the end of September. So, orders came into the extent of about Rs 125 crores more. Export orders contributed about 50% of the pending orders. We are seeing that distribution conductors are also growing very strongly in fact much faster than we had originally envisaged even though they are lower in tonnage. But this is indicative of all the efforts that are happening in the distribution sector as well, where the money is flowing in from UDAY scheme. We have received substantial orders in the domestic segment in the last few months about Rs 109 crores which is expected to increase capacity utilization primarily of our Jharsuguda plant. Our expectation is that in Q4 we will be running the Jharsuguda plant with the increase capacity at 100% level.

High efficiency conductor contribution to the segmental revenue stands at around 13% for the quarter. There is a very strong pipeline of prospects of these HEC tenders as we enter into Q4 both domestically as well as in the export markets of South Asia. However, the actual awarding of these tenders is getting postponed and our expectation is that in Q4 we should see a substantial jump in the order book coming in from the high efficiency conductor tenders. A large portion of that execution will happen actually in FY19. So the increase in order book which we are likely to see in Q4 should get executed in the next financial year itself. The domestic markets have been quite competitive due to the sluggish demand from the new interstate transmission lines. Also I had mentioned earlier that postponement of ordering has taken place by many of the developers in the hope of lower commodity prices either by the original developer or by the EPC Company.

Finally, if you see EBITDA post Forex per metric tonnes decline to about Rs 7,000 from Rs 13,900 in Q3 FY17. This is primarily due to the higher competition in the conductor segment as well as the lower contribution from some of the high efficiency conductors. We are also happy to announce that our new aluminum rod making and melting facility in Lapanga has commenced production based on ingots. We have signed a binding MOU with Hindalco for delivery of molten metal and this plant is actually co-located right next to the Hindalco's facility at Lapanga and we are awaiting clearances to receive molten metal which we hope to expect before 31st March 2018. This will result in a more competitive position for our conductor business. It is a 10 year molten metal purchase contract which is being finalized. If you look at the 9-month FY18 revenue, it came in stable at about Rs 1,674 crores with exports contributing to about 48%. The high efficiency conductor revenue for the 9-month period came in at 15%. So EBITDA per metric tonnes post Forex adjustment came in at about Rs. 8,900 per metric tonnes.

Coming to our transformer and specialty oil business the revenue for the quarter actually grew strongly by about 34% to reach Rs 567 crores compared to Rs 423 crores a year ago. We saw substantial growth in industrial process oils, rubber process oils, exports for white oils and industrial and automotive lubricants. Transformer oil business in the last quarter was a little bit subdued but we expect a pickup to happen in the fourth quarter. If you look at global shipments for the quarter, it increased by 16% in volume terms to reach almost a 106,000 KL compared to about 91,000 KL a year ago. So this has been by far the highest historical sales that we have achieved in a quarter and the Hamriyah plant also has contributed towards the highest sale that it has achieved.

Also in this quarter we did witness a sharp increase in crude oil prices coupled with lower base oil supply position resulting in cost increase across all products. This increase has essentially been passed through during the quarter in most categories. There is some lag in the industrial and automotive side but price increases has been announced and within this quarter we should see higher prices materializing. The rise in the crude prices however is continued through December into January. So there is expectation for further increases of base oil prices likely to happen in this quarter. If you see the EBITDA per KL after Forex adjustment for the quarter that increased by 17% to Rs 4,522 per KL. So the declining trend in the EBITDA margin which we saw over the last 3 quarters has been reversed in Q3FY18 and we expect a similar sort of result to come in Q4 FY18.

In terms of our auto lubes segment, we delivered the highest historical volumes which amounted to about 8,716 KL 52% higher than the same period previous year. This was largely led by growth in the OEM segment and also a 10% increase in our retail sales. Profitability in the segment had some temporary impact due to the raw material price increases but as I mentioned earlier this has been pretty much offset by the higher volumes that we achieved. So if you look at the 9 months period the revenue grew 24% to reach Rs 1,572 crores. Global shipments for this 9 month period is 14% higher coming at about 298,000 KL, which is once again a historical high for a 9 months period for us. The EBITDA per KL after Forex came in at Rs 4,130.

Coming to our cable business, the cable business delivered a good revenue growth of about 36% and revenue for the quarter came in at about Rs 285 crores compared to Rs 211 crores from a year ago. A large portion of this growth has come in power cable which is up actually 97% over the same period previous year as well as some increase has taken place in the optical fiber cables and elastomeric cables that have gone into particularly the defense sector. There has been a substantial reduction that is happened in wind mill demand, so that has actually reduced some of our business on the elastomeric cable side. The EBITDA post Forex adjustments increased to 10.8% from 9.7% in the period a year ago. So if you look at the 9 months period for the cable division revenue is up 34% to reach Rs 780 crores and it kind of puts us in a position to hit sales number of approximately Rs 1,100 crores for the year.

So in 9 year period that Apar has been running the business. The sales revenue were increased about Rs 120 crores to Rs 1,100 crores for this division. EBITDA post Forex adjustment has come in at about 9.2%. The optical fiber business has witnessed higher volume demand. We have received some new orders from BBNL. However, the fiber prices have increased very substantially and fiber availability is very tight which is likely to limit the new opportunities that we can bid on in the foreseeable future. Simultaneously though we are seeing good traction in the export markets not only for our power cables but we continue to see a good demand for some of the other categories of products also domestically. The elastomeric business as I mentioned has been a little bit subdued due to the slowdown in the wind mill segment. However, within the elastomeric segment we have seen a substantial increase in ordering from the Indian railways as well as on the defense side compared to a few years ago. So, even though the elastomeric volume has fallen the profitability has increased within that segment.

We have been exploring opportunities in 3 major areas on the cable side. The first one is in medium voltage covered conductors which actually result in significantly higher safety for cables in the distribution segment especially when we are running through forests largely wooded areas and wherever there are game parks and game reserves both for animals and birds which would prevent any short circuiting happening for them. We have also looked at entering the auto cables business with our E-beam cables and we are looking at increasing business to the Indian railways by entering the railway harness segment given the fact that our E-beam cables forms a very large percentage of the product which is being delivered. So, all these initiatives will really not have any impact on the financials for this year but will start contributing from FY19.

As some concluding remarks, we expect that conductor volumes to grow backed by a higher order book with increasing demand not only for distribution conductors but also for high efficiency conductor. This trend of reducing margin should reverse in FY19. In speciality oils, where we have delivered good volume growth our focus continues to be on margin improvement. We have already achieved that in the last quarter and expect similar result in the coming quarter. Our cable business is positioned to continue to perform well in terms of both guided revenue and EBITDA.

So, with this I come to the end of my comments. I would like to thank everyone for joining this call and would like to open up the floor for questions that may be there at this stage.

Moderator: Thank you very much, sir. Ladies and gentlemen, we will now begin the question and answer session. We have the first question from the line of Adit Makhijani from B&K Securities. Please go ahead.

Adit Makhijani: I wanted to understand two things from you. One is your outlook on EBITDA margins going forward in each segment and secondly your outlook on the end market demand. Are the DISCOMs spending on CAPEX and things like this?

Kushal Desai: So, let me address the second question first. As I mentioned in the call we see actually accelerating demand across various segments, certainly there is a lot of demand on the distribution side. So our Power cable business actually is up, we are basically just limited by capacity at the moment. Whatever new CAPEX we have put in, we will run it flat out in the fourth quarter. Similarly, in the distribution conductors the demand has surprised us on the upside. So, and the transformer oil side actually has been a little bit slower in terms of business for us because we have been a little tough in terms of outstanding's we have had to keep that under check. But the order inflow of transformers in both power and distribution transformers is also at a fairly strong levels. So, the CAPEX spending in fact we see much stronger visibility in FY19 than we had in FY18 and there is no likelihood of the two major events that happened in the last financial year which is the demonetization and the GST particularly. So, FY19 seems actually a fairly good year for us to look at. The first question you had in terms of margin guidance, the business which has had difficulty in the last few months is the conductor business and as I mentioned there were two primary reasons for it. One is the percentage of high efficiency conductor orders, new order inflow and execution has been a bit slower than what we had anticipated. Having said that as we enter Q4 and FY19 we will see a big surge in terms of these orders. So, in the fourth quarter itself we are expecting number of these jobs to actually close and FY19 has a very large set, very big pipeline coming not only from India but also from South Asia which includes Nepal and Bangladesh. So, we see actually the margin improvement taking place on the conductor's side as a consequence of both of these. In terms of our Oil business, the structural thing that is happening is the automotive business and industrial business are both growing and they add to a higher level of profitability. The White Oil business which actually had a big jump in volume carries a lower profitability on a per KL basis. However, if you take the absolute number the oil business has actually performed much better in the third quarter compared to the second quarter and we expect something similar in the fourth quarter also. On the Cable side, the EBITDA's have gone up from 8.3% which we had guided for the year to over 9% for the 9 months period. We would expect at least a 20% plus growth happening in FY19 and even though some of these growths will come on account of power cables which carries a lower margin, to some extent it should get off set by the railways and defense and some of the other segments where we sell speciality products. So, the percentage EBITDA may not increase but you will see a growth of Rs 200 plus crores on the topline.

Moderator: Thank you. The next question is from the line of Aditya Wagle from Aequitas Investment Consultancy. Please go ahead.

Aditya Wagle: My first question is regarding the conductor segment. Sir, can you just elaborate on the 10 year purchase contract which we are entering with Hindalco in terms of what will be the price revisions or any other terms?

Kushal Desai: So, actually it is a molten metal contract and it is basically linked into a combination of the LME and the domestic price index which will be there. So, in that sense the prices will keep adjusting based on the movement that happens on the metal. So, it is no different than what we would have bought in terms of ingots and the movement that is there. The benefit really is on account of receiving the molten metal and converting it into rods at a lower cost. The other major benefit is that this enables us to be fully self-sufficient in the Orissa area and with the smelting capacity all coming in there, you may have also recently read about new mines being allocated to Vedanta in that area. So, aluminum production is all going to be concentrated in that Jharsuguda area which enables both incoming and outgoing logistics to be cheaper for domestic sales to a very large extent. So that is why we see this as a very significant move.

Aditya Wagle: And sir, what would have volumes been at the Hamriyah plant this quarter?

Kushal Desai: So, the Hamriyah plant has actually delivered about 43,000 KL in the 9 months period.

Aditya Wagle: In 9 months, okay.

Kushal Desai: Yes, because we really started production sometime in March.

Aditya Wagle: And sir, the last thing with cables I think you answered in the previous question. How do you expect your newer initiatives to deliver in terms of top-line.

Kushal Desai: The power cables, business is growing and the profitability within power cables is also improving relative to what it was in the past. But as a category, in power cables there is no scope for differentiation with much higher level of competition compared to some of the most specialized cables. So, the percentage EBITDA may not increase but it will be on a larger base.

Aditya Wagle: And newer initiatives which you all are planned in terms of railways and auto cables. How do you see them contributing?

Kushal Desai: So, it is difficult to just peg a number in there because next year all of these are undergoing various levels of client testing and approval but our expectation is that by the end of the first quarter we should have all of these three areas starting to have commercial revenues coming in.

Moderator: Thank you. The next question is from the line of Rajnath from Choice Equity Broking. Please go ahead.

Rajnath: Sir, I have couple of questions. First question what was the reason for your decline in the conductor margin? Was this related to TBCB projects, just wanted to know?

Kushal Desai: Well, there were basically two reasons as I have mentioned earlier. One is that at domestic site there has been fairly high level of competition, the competitive intensity has been high especially given the fact that some of the ordering has got postponed in light of the risen commodity prices. So that has been one reason and the second one is the high efficiency conductor also have come in lower in terms of execution than we would have like and that is primarily from the fact that for the last couple of quarters some of these tenders which should have got finalize have got postponed. But our sense is that in Q4 a lot of that should actually come through and we will be sitting on a much higher high efficiency conductor order book by the end of Q4.

Rajnath: My second question is what would be the conductor order book in terms of volume terms and what will be the export contribution?

Kushal Desai: So, it is about Rs 1,500 crores. Metric tonnes is 97,000

Diwadkar: It is 50-50, export.

Kushal Desai: Yes, the break up is around 50% export and 50% domestic.

Rajnath: Sir, I have missed the answer explanation which you have given for conductor EBITDA. Just can you explain, what is the expected conductor EBITDA per ton for FY18 and FY 19?

Kushal Desai: So, well EBITDA per MT had come in at about Rs. 8,900 that is the actual performance versus the Rs 10,000 per MT that we had guided for the year. We are about at Rs 1,000 - Rs 1,100 lower. In primarily it's come from whatever happened in Q3 as we move into Q4 we expect that to have some signs of improvement but FY19 we see a much clearer path for it to get back up to Rs 10,000 plus, especially from the contribution from the high efficiency conductors.

Rajnath: And sir last question is the concerns related to GST for renewable and defense sector resolved?

Kushal Desai: So, the defense sector actually was just paper work because the sector is actually finally to be exempt. So, there was paper work in terms of how the purchase order has to be prepared, etc. As far the renewable sector is concerned the problems are not fully resolved, simply because the mechanism for actually getting the reduced GST of 5% is not yet firmly in place. Secondly, there have been some other effects coming in with some safeguard duty and things like that on panel. So, there is still some level of uncertainty but the business on the wind mill side has been badly affected. We see the wind mill side improving because part of it was due to DISCOMs not wanting to honor the various PPAs which were agreed upon in the past. The government has now taken a firm stand that those PPAs need to be honored also wherever the generation is beyond whatever was signed, the DISCOMs are not taking any additional energy. Whereas, now the power is being taken at a 25% discount. So, there are a few things that the government has actually put in place on the wind side which should help enable an improvement on the wind side because it is really fallen of the cliff in the medium term. The solar side has actually not been as strong as prior to GST. Our expectation is that it should start picking up.

Moderator: Thank you. The next question is from the line of Ashish Poddar from Anand Rathi. Please go ahead.

Ashish Poddar: My question is basically your guidance. So, if you can explain your guidance for FY18 and FY19 across all the three segments?

Kushal Desai: So in terms of FY18, our conductor guidance which we had given at the beginning of the year was close to Rs 10,500 per metric ton. 9 months we have come in at Rs 8,900 and our expectation for the fourth quarter is we will do something in that same range. However, as we get into FY19 depending on finally the amount of high efficiency conductor orders that come in, our expectation is to go back above Rs 10,000 per metric ton in the next financial year. In terms of our oil business we have come in at about Rs 4,100 per KL. We expect the fourth quarter to be in line with that and expect FY19 to actually be a bit higher coming in from the additional volumes from our automotive and the industrial side of the business. There is a lot of flux going on right now because of the sharp increases happening on crude and base oils. So, it is difficult to just peg a number but in terms of the mix, the mix is likely to get richer as you get into the next financial year. On the cable side we expect that the EBITDA percentages will remain, 9.2% for the 9 months period. We expected to come at this level through the rest of the year and next year should remain at the same level but on a 20% plus higher sales base.

Ashish Poddar: This was helpful in terms of margin side but what is the guidance on the volume front?

Kushal Desai: So on the volume front, our expectation is that we will come closer to about 160,000 tonnes to 170,000 tonnes on the conductor side. Our speciality oil business, we are expecting to have at least a 7% to 8% growth over and above the 14% which we have seen this year and on the cable business we are expecting about a 20% growth.

Ashish Poddar: Yes, so what is the Conductors volume number for FY18?

Kushal Desai: So, we are expecting FY18 to come in between 150,000 tonnes and 155,000 tonnes.

Ashish Poddar: So, not much volume growth you are expecting there?

Kushal Desai: But there is a big change in the mix which we are expecting next year. Because the high efficiency conductors, the tonnage is lower but the value per ton is significantly higher.

Ashish Poddar: Yes, that is true and what for the oil and cable?

Kushal Desai: So in the oil, the guidance which we have for this year is of about a 375,000 KL. We have done around 297,000 KL so far and for the cable business we expected to close at about Rs 1,100 crores.

Moderator: Thank you. The next question is from the line of Varun Aggarwal from BOI AXA Mutual Fund. Please go ahead.

Varun Aggarwal: Primarily question on your conductor business. You have explained the reasons for the decline in the EBITDA for the current quarter. But I just want to understand in terms of exports, were exports at lower margins this year due to some reason, I mean it is not showing in EBITDA just wanted to understand a bit more on the export side.

Kushal Desai: So, well Domestic margins are always little bit higher because of the freight and logistics benefits that one gets. The export margins in some instances have been lower because of pricing which we got. As we spoke about, it depends on sometimes the Chinese competition that comes in and the relative difference between LME and Shanghai Metal Exchange. So, we had two quarters that was unfavorable and last quarter actually one the two quarter. So, some of the export margins were under a little bit of pressure as we mentioned in the previous calls. Having said that, the exports margins are pretty much at this level of around Rs 9,000 a ton.

Varun Aggarwal: So, going forward do you think they will remain at same level primarily the incremental improvement should come from the domestic business?

Kushal Desai: So, as we have mentioned even in the past in several interactions and call we do not expect a significant growth to take place in margins per unit. However, we expect a substantial improvement to happen coming from the mix of the product. So, the trajectory that we were growing if you see the way high efficiency conductors have grown they have grown very substantially over the last two years from below 5% to as high as 18% in a particular quarter. Our expectation in FY19 is that factor is going to kick in because there is a lot of pending tenders which are there and the pipeline is also very strong. So, that will be the primary driver as opposed to how much more margins you are going to make in a standard aluminum conductor.

Varun Aggarwal: So, basically considering all the benefits now we will have in place for the new plant in Odisha plus the molten metal. So is the Rs 10,000 per MT right number to look at, I mean are you basically building all the improvements in the cost benefit.

Kushal Desai: Yes, at the moment that is the guidance which we can give that we will exceed Rs 10,000 per metric ton because a lot of these HEC conductors we still need the tenders to come into our order book. So, as it comes into the order book we would be in a position to give you a better guidance. But the one thing that is clear is that as you have the order book showing up at the end of Q4 and at the end of Q1 FY19 the percentage of HEC conductors is likely to be much higher than it is in today's scenario.

Varun Aggarwal: What about new opportunities you are exploring in the cable segment. Can you elaborate a bit on that auto cable, railways and what exactly is this? How big is the opportunity for us?

Kushal Desai: So, the auto cable market is very large. The auto cable however, we are seeing a trend where for increase safety battery wiring and some of the other auto wiring in the harnesses likelihood of electron beam cables is likely to increase. So, as a consequence we have actually submitted samples to the key harness manufacturers and some of the auto companies and the testing for these cables is on. So our expectation is that by the end of the first quarter of FY19 we should receive approvals and then depending on the plans that these companies have for bringing in these sort of products especially at the higher end of their model. It is difficult to predict what the growth will be, but it is definitely a trend which is that safety is going to play a bigger and bigger role and as you have more electronics going into the vehicle the density of cable population in a car is increasing which means that considerations of heat generation and all these things start coming into effect. So, the market is moving in the direction of these E-beam cables. So, difficult to just pluck a number, total addressable market is over Rs 10,000 crores. Now what percentage of that comes to E-beam cables that still a question but it is definitely taking that trend. In terms of the railway harness business today the railways are actually buying the cables separately and giving a contract for doing the harnessing to two different parties. Whereas, going forward they want the turnkey job and they want delivery of the railway harness to be delivered to them. So, the incremental business will come only from the growth of harness that is going into the railways as they expand. But the opportunity for us opens up dramatically because today we are supplying cables to people who are putting harness together from FY19 onwards we want to start bidding directly on the harness contracts.

Varun Aggarwal: Sir, just to understand a bit on the cables part of the business. Does it require a little more CAPEX going forward in next couple of years considering the new initiative which we are going to go?

Kushal Desai: So, we expect to continue to have to invest in CAPEX but it will not be substantially more than the depreciation that we are taking on, so in the cable business. So, the CAPEX is going to be in between Rs 20 crores-Rs 25 crores in FY19. Because a lot of the base has already come into effect, like for example setting up a harness manufacturing facility is not a capital-intensive investment. To manufacture MVCC which is this medium voltage covered conductors there is not a huge amount of CAPEX involved. It is mostly technology that we developed at our end to be able to make those types of products. So, it is really a mix that is improving and so the CAPEX is not going to be very significant.

Varun Aggarwal: Sir, one last question on the conductor business again coming back to that question. We have given a guidance of around Rs 10,000 metric tonnes with the volume growth of 160,000-170,000 you gave. So, do you think overall pent up demand in domestic as you mentioned, most of that has in built in and the new projects are going to come at a relatively better rate or something?

Kushal Desai: So, the business model has changed here, in the last call we spend some time explaining how the tariff base competitive bidding model is different where everything is on a fixed price as far as developer is concerned. So, I guess with time passing by the model actually, will improve in terms of the way risk is being managed particularly commodity wise. So, going forward I think people as they bid will be factoring these things into account. It is really not something which we can push because the tail cannot wag the dog in terms of the way in which the business model is being bid by the developer. But I think going forward the risk management will become a much more comprehensive exercise being done at the time of bidding.

Varun Aggarwal: So, what I am basically trying to understand is, is it a new normal as you said there is a change in the business model. So, is this a new normal which we are looking at because, I mean after the TBCB norms so everyone is looking to basically predict the margins.

Kushal Desai: So, the model is evolving, the ordering which will happen now on the CAPEX cycle is more than the bids which went in FY17 and FY18. So, when the new bids come up, I am sure that cognizance will be taken off commodity risk to a much greater extent than was taken before. Currently there is a problem because the cost escalation which has happened, someone along that supply chain has to pick up. So, it is between the developer and the EPC contractor and to some extend the margins of even the conductor suppliers will come under pressure, it has already start coming under pressure because the bill has to be paid finally.

Moderator: Thank you. Next question is from the line of Maulik Patel from Equirus Securities. Please go ahead.

Maulik Patel: On lubricant side you mentioned that auto lubricant has a growth in excess to around 40%?

Kushal Desai: Well, last quarter the automotive lubricants grew in volume terms by 52%.

Moulik Patel: I understand the base was quite weak because of the demonetization but are we confident that business can grow 20% given that our market share is in low single digit?

Kushal Desai: The auto lube segment our plan for next year would be to grow at least at 15%.

Moulik Patel: And that is the high margin business right?

Kushal Desai: It is definitely much higher margin than white oils and processed oil.

Moulik Patel: Is this margin comparable to the some of these large players who are only in auto lubricant segment like Gulf Oil or Castrol?

Kushal Desai: Well, the margin profile in the automotive side if you take the retail side which is done in the ENI brand those margins are not very far off from what Gulf Oils margins are. The OEM side of the business, the margins are lower. Gulf Oil does have a benefit being the sole supplier to Ashok Leyland where they end up actually getting significantly better prices and we do not have that sort of privilege in that line of our business. But if you look at the auto lube side the margins on a per KL basis are almost double that of the white oil and process oils, etc.

Moulik Patel: Within the transformer oil category how has been the growth over in this quarter or probably in the 9 months. Have the SEBs started spending more or still they are in that dilly-dallying what have been there since last many years. Is there any improvement you have seen?

Kushal Desai: So from whatever we have seen of the order intake that is coming into our customers which is the transformer manufacturers and the flow of tenders which are coming up for transformers both of them are at relative historical highs. So, if you see the domestic sale for the 9 months, transformer oil domestic sales is up but it is not up by a very big number. Some of it we have limited because of fiscal discipline that we need to implement as all these collections are still a little bit slow from some of the players. But the demand actually is very strong. So, our expectation is that the fourth quarter will be quite strong in terms of demand

and in FY19 a lot of power transformer business is actually being tendered which will result in execution.

Moulik Patel: Sir, coming to this conductor segment last year the same time the margins were highest ever margin and this year we have probably the lowest ever margin on just a quarterly basis. But you have been guiding always that the range will be around Rs 9,000 to Rs 10,000 per tonnes something like on that range. HEC segment where the contracts are basically on the fixed price basis. Do you think that the margin actually will be better once this commodity inflation probably stabilized?

Kushal Desai: So, as the commodity inflation stabilizes there will certainly be some improvement because the fluctuation from commodity will be lower. Now that does not affect to a very large extent just the normal because there are price variations that are in place for some of the business and some of the fixed price business which we bid on we actually hedge the metal. When the volatility is high the hedging cost are a bit higher. The main kicker for the conductor business is going to come from actually the increase in sale of the high efficiency conductors. And we saw actually a lower percentage of that in this quarter and lower margins on the contracts of the HEC which we executed in this quarter. But going forward there is a very strong pipeline which is in place. So, you will see a big change in the order booking that will happen of high efficiency conductors as we complete Q4 and get into FY19. And the thing is that lot of execution cycles for that are relatively short. So, our expectation is that whatever orders come to us by the end of Q1 of FY19 we should see execution happening in FY19.

Moulik Patel: And the last question is on this cable segment and it has done really well and now we are almost touching on an Rs 1,000 crores run rate on annualized basis. What we understand is that government is also coming out with a big tender for the Bharat broadband that is another phase which is going on and that we have done very good in this electric and cable category. But any signs that this business can become a substantially large over, so the growth rate can sustain, we have doubled in the last two years also in terms of revenue.

Kushal Desai: Are you specifically referring to the optical fiber cable?

Moulik Patel: I am referring to overall cable segment where the revenue this year will be around Rs 1,000 crores.

Kushal Desai: Yes, so next year we are definitely targeting a 20% growth over this year based on the pipeline that we see and the kind of order flow which is expected to come in. It is being largely driven by the government’s initiatives on improving power availability in terms of power cable and the elastomeric cables business is being driven by the railways where the spending has now started taking place like railway orders this year are 50% higher than the same period 9 months of the previous year. Defense also has shown a big increase over the same period previous year. We will see some of this non-conventional energy also starting to pick up because there has been policy related issues on various fronts as we discussed earlier in the call. As those start stabilizing the solar side will pick up and wind also expectation is that it will not go back to hey days but it will certainly be better than what has happened in the last 3 months to 4 months. So, the cable side we see multiple growth drivers in each of the sub-segments. The place where we have a little bit more difficultly to take care of all the opportunities that are coming by is on the optical fiber side. So, in the case of optical fiber cable we are being limited essentially by the fiber availability. That is in tremendous short supply, so even at higher prices the availability is very tight. So, we have to bid carefully for business based on the amount of fiber supply that we have available to us. But still the fiber business, OFC business is also expected to do better than it has done in the last financial year.

Maulik Patel: So, I am just looking in the totality as in all the three business. The last year the performance was largely driven by the conductor. This year the conductor has not that done well and the speciality oil as a segment has done well while the cable continues to doing well. But overall earnings growth is not there in this financial year. Next year assuming all the three do well, we again can have significant growth in coming year, right.

Kushal Desai: Yes, that is what we have been expecting and guiding that compared to per metric tonnes / per KL / percentage, the amounts will remain at reasonable levels, at good levels and the volume will grow across all the three segments. So the clarity that we have seen FY19 actually is much higher than we have seen in FY18.

Moderator: Thank you. Next question is from the line of Divyata Dalal from Systematic Shares & Securities. Please go ahead.

Divyata Dalal: Sir, I missed your comment on the Jharsuguda plant at the start of the conversation. Has there been an increase in capacity there?

Kushal Desai: So, when we originally envisaged the facility, we had planned capacity of 30,000 metric tonnes. Now given that the GST is been implemented and the cost dynamics are now very clear in terms of operating from Jharsuguda versus Silvassa we have actually moved significantly more amount of plant and machinery from Silvassa to Jharsuguda. So, the capacity that we will have to produce in Jharsuguda will be closer to 80,000 tonnes. So, out of the 180,000 tonnes the original plan was 150,000 in the Silvassa area and 30,000 in Jharsuguda as we will end up with 80,000 in Jharsuguda and 100,000 in Silvassa. So, there is a big change and all that is happened during this year. So, whatever financials you see have actually picked up the pain of all the moving cost, etc. also that are associated with transferring machinery from one location to the other.

Divyata Dalal: In terms of you are saying overheads for the conductor business?

Kushal Desai: In terms of overheads, disruption of production, commissioning costs all that has been pretty much expensed.

Divyata Dalal: Yes but on the volume side, I think we have really caught up very well because till last quarter we were guiding a 12% de-growth but we are already at (-5%) growth. So, definitely volumes are picking up in a very good way and the conductor side

Kushal Desai: So, we were actually constraint in terms of the tenders which we were filing in the first few months of the year in the absence of clarity on GST. So, once that GST clarity came in place then we started bidding on all the business with Jharsuguda being the location of manufacture. And so that is how the production started ramping up there and in this fourth quarter we will be running pretty much flat out. In addition to that next year we will end up getting molten metal capability also. So, that will make a difference of almost little over Rs 1,000 per tonnes in terms of just the cost of metal.

Divyata Dalal: So, this particular saving is what we will be using for bidding for better projects, it will result into cost savings per say?

Kushal Desai: So, there will certainly be the cost savings coming in. We have taken conservative level in terms of the conventional conductor bidding. So, our main drivers is that, we will be the lowest cost producer in the country and the mix of product is where really we are hanging a hat in terms of the margin improvement.

Divyata Dalal: So, currently out of our total order book how much will be HEC?

V. C. Diwadkar: HEC is around 14%.

Divyata Dalal: 14% of order book?

V. C. Diwadkar: Order book, yes.

Divyata Dalal: Which we are expecting in Q4 and Q1 this number should go up as a percentage of order book?

Kushal Desai: It should substantially go up.

Divyata Dalal: And this will be driven by the interstate CAPEX?

Kushal Desai: Well, I mean if you look at the pipeline of tenders there has been awarded and the likely tenders that are coming up. Most of it is within the state as far as domestic is concerned there are some fresh lines coming in from power grid and couple of transmission companies which are interstate and then there is a whole lot of business which is being bid in

Bangladesh and Nepal. Both of which have adopted high efficiency conductors much faster than India has adopted.

Divyata Dalal: So, Bangladesh and Nepal also will we do the EPC or we will just do that our conductor?

Kushal Desai: For new lines we have actually tied up with EPC contractors. So, we have done joint bidding on the line so that when the business comes to that particular EPC contractor the automatic conductor comes to us. We have done similar arrangements also in Nepal. So, some of these tenders have opened and some other tenders are due to open. So based on that our feeling is that over the next two quarters which is Q4 of this year and Q1 of next year we should see a big jump in the order booking of high efficiency conductor.

Divyata Dalal: And which will come for execution in FY19?

Kushal Desai: We expect to get completed in FY19.

Divyata Dalal: And in terms of CAPEX in this moving of capacity from Silvassa to Orrisa any substantial CAPEX that we did there?

Kushal Desai: The CAPEX was largely involved in terms of putting up new land building and electrical connections, etc. but the cost of shifting a lot of it has actually just been written off. So, that has had also some impact on the conductor business margins.

Divyata Dalal: And in terms of oil segment since we are saying the mix will be richer which will be more towards the industrial oil or may be power transformer oil or auto oil. So, how can this swing the EBITDA per KL. If you can give some direction in terms of how this can move can we go to the past levels of Rs 5,000 per KL.

Kushal Desai: So, our target is to get to those higher levels. We are hesitant in terms of picking a number at this stage simply because crude has been moving up so sharply in the last few months. In fact in the last one month in December and early January that there is a whole cycle of increases taking place, for all hydro carbon, which is our base oils, additives. So, it is a little unclear in terms of when we will be able to pass through all of these increase, if you just gone through one round of revision and there has been another increase that has been seen. So, if this sustains then we will start seeing increases in everything right from packing material to additives and all that. But the trend is that if we do end up achieving the mix which we are talking about where there will be a 15 plus percent growth in our automotive industrial segment. Then the mix would have really changed because the margin is almost double in those segments compared to the white oils, process oils and even the distribution transformer oils. So, we are more focused on the mix because whatever transitions are there in terms of base oil pricing, etc. it will take a few months but it will just settle. You have got to keep in mind that in the last few months crude has gone up from $ 44 to now $70 plus. So, it is a big jump.

Divyata Dalal: Despite that we have been able to take some price increases. So that is encouraging actually.

Kushal Desai: Yes.

Moderator: Thank you. Ladies and gentlemen, that was the last question. I would now like to hand the conference over to Mr. Lokesh Bhati of Four-S Services for his closing comments.

Lokesh Bhati: I would like to thank the management for giving us this opportunity to organize the call and all the participants to join in. We look forward to connect with you on the next call. Thank you everyone.

Moderator: Thank you very much, members of the management. Ladies and gentlemen with this we conclude the conference Apar Industries Limited, thank you for joining us and you may now disconnect your lines.