Apar Industries Limited
Apar Industries Limited Q4 & FY16 Earnings Conference Call
May 26, 2016

Moderator: Ladies and Gentlemen, Good Day and Welcome to Apar Industries Limited Q4 & FY16 Earnings Conference Call hosted by Four-S Services. As a reminder for the duration of this conference all participant lines will be in the listen-only mode and there will be an opportunity for you to ask questions at the end of today's presentation. If you need assistance during this conference call, please signal an operator by pressing '*' and then '0' on your touchtone phone. Please note that this conference is being recorded. At this time, I would now like to hand the conference over to Ms. Nisha Kakran of Four-S Services. Thank you and over to you, ma'am.

Nisha Kakran: Thank you. Good afternoon everyone on behalf of Four-S Services I welcome all the participant to Apar Industries Q4 and FY16 Results Conference Call. Today, on the conference call we have Mr. Kushal Desai 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. Over to you, sir.

Kushal Desai: Thank you Nisha. Good day everyone and a warm welcome to a Q4 and FY16 Earnings Conference Call. I would like to begin with some of the key operational and financial highlights for the year and then talk a little bit about our growth strategy and post that we can throw the floor open for questions. Through this financial year 2016, we still saw quite a few challenges on the ground in the power sector and even some of the other businesses including our auto lubricants etc. However, it has been a very important year with some path breaking initiatives that were announced by the central government and this should certainly provide a boost to the demand in the power sector. Especially the most transformative Uday scheme, has already garnered a response from 10 states and bonds worth Rs 98,960 crores has already been raised. We also expect some more actions to come further in the year. Given the fact that the power ministry has floated a cabinet note to extend the deadline for the scheme. So couple of states which should have actually come on to Uday but haven't, now have the opportunity to actually sign up. Power Grid Corporation of India has also indicated that its normal CAPEX which is Rs 22,500 crores a year may be increased. We have also seen the operationalization of the ultra-high voltage 1200KV national test station at Bina in Madhya Pradesh and a couple of transformer companies whose transformer have been used actually carry our transformer oil in it. There is also positive indicator in terms of the coal production from coal India and a growth rate in production of coal which is at about 536 million tons, which augurs well finally for the availability to power plants and major users.

Our sense is that the future augurs well and the year witnessed slow progress on the ground, but there is a lot of pent up demand that is likely to come through the implementation of these schemes and we are already starting to see some movement on the ground in terms of tenders actually being floated. It is still open to the jury in terms of which quarter we will see the revenues actually coming in to our business, but as you look into the future, the future definitely looks brighter than it has been so far. Despite some of these challenges which were on the ground, our financial numbers have been reasonably strong for the year. We have achieved the highest volume ever in all our three businesses i.e. maximum sale of specialty oil products, highest shipment of conductors and also the highest volumes of cables that the company has ever done. In FY16, the company posted a consolidated revenue of about Rs 5,080 crores compared to about Rs 5,122 crores in FY15. The marginal decline is essentially from the specialty oils side in terms of value, given the fact that crude prices have fallen so significantly. This was partially offset because the cable segment grew by about 20% and there was a strong growth even on the conductor side. Further there has been improvement in a margin profile where the EBITDA margin has increased by 226 basis points to reach about 7.2% in the financial year from 5% in the previous year.

Profit after tax excluding the treasury gains that we had on the sale of treasury share of Rs 43 crores is at Rs 120 crores, so that is up by about 142% over the period previous year. In Q4 FY16 our consolidated revenue that we delivered was Rs 1,347 crores compared to Rs 1,354 crores in the same period last year. The EBITDA grew by 111% and the profit after tax for the quarter grew by 332%. This growth in EBITDA and profit after tax needs to be seen in the context of some of the inventory losses which we picked up in the oil business in FY15 that subdued the number in that period. Whereas fortunately through FY16, we were able to manage the fluctuation in oil prices and currencies fairly well through the year. The EBITDA Margin came in at about 7% for the quarter and the profit after tax was at almost 3%. I would now like to actually run through some of the segments wise performance. In our conductor business, we reported a revenue of Rs 2,550 crores in FY16 which is up 10% from the previous year even though the prices of aluminum and steel have fallen substantially. Exports contributed 40% of our revenues, despite challenges in many parts of the world especially from commodity driven economies. Volume through the year grew by 13% to reach a 170,000 metric tons compared to about a 150,000 metric tons in the previous year. The EBITDA for metric ton post forex adjustments came in at Rs 7,600 per ton. This is in spite of the first half having legacy orders which were at relatively lower margins. So you will see a gradual increase in the EBITDA per ton in the conductor business as we had provided in our guidance.

Volumes for the quarter grew by 18% to reach about 50,165 tons for the quarter and this is the highest sales that we ever had in a quarter. The EBITDA per metric ton post forex adjustment for the quarter grew to about Rs 9,700 per ton compared to Rs 4,700 in the same period in the previous year. This was actually helped by the preponement of some of the profitable orders that we had from Power Grid, which not only helped us with higher sales volume, but also with better profitability for the quarter. The segments order book stands at about Rs 1,751 crores which translates to about 140,000 metric ton worth of conductors and of this the export contribution is approximately 30%.

One of the highlights is been that the company has been actively growing its presence in the high efficiency conductor segment and the revenues for this segment came in at about 6.2% of the overall conductor revenues compared to 1.1% in the previous year. We have received orders worth little under Rs 300 crores for this conductors during the year and we have also successfully completed the longest transmission line with re-conductoring work till date of ACCC which is gold standard in terms of high efficiency conductors for the Orissa power transmission company, that project was completed in FY16. Several other significant installation work of ACCC for Torrent power in Gujarat and many other projects are also completed in the year. If we now move to the transformer oil side, the revenues for the year came in at Rs 1,841 crores which was lower than the previous year because of the falling crude prices. However, we posted a 2.6% growth in aggregate volume and this volume is the highest sales volume that we had till date. Growth has actually come really from our automotive lubricants, rubber process oil and industrial oils. The EBITDA for KL after forex adjustment for the year increased quite significantly from Rs 2,700 to Rs 5,400, so it is almost doubling of the EBITDA and this can be attributed to a sale of richer mix of products and primarily from lower raw material cost, particularly our industrial and automotive businesses delivered the highest EBITDA that they have for a long time. Given the fact that we were able to hold on to some of the selling prices, even though raw material cost were lower. If we now look at the Q4 FY16, the revenue came at Rs 437 crores versus Rs 505 crores. However, we posted a 3% growth in aggregate volume period-on-period reaching approximately 89,000 KL in the quarter compared to 86,000 KL in the previous period. The EBITDA for KL post forex adjustment came in at about Rs 4,561 per KL compared to Rs 3,048 per KL a year ago.

During this year, as I mentioned we also made the first set of supplies to HVDC transmission projects of 800 KV executed by Power Grid. This oil has gone into transformers delivered by Alstom in the Champa Kurukshetra line and our oil as I mentioned earlier has been used in transformers of couple of manufactures, where the commissioning has happened of the 1200 KV AC Transformers in the test station setup by Power Grid in Bina. We have also completed successfully supplying over 20 million liters of transformer oil into the 765 KV AC segment and also been able to now present data to power grid and other users of over 3 years of performance in actual live transformers which puts us in a fairly advantageous position in terms of being able to present our credentials.

If we look at the automotive lube segment, volumes were up by only 2.9% which was essentially due to a sharp drop in the rural sector and rural demands, particularly from the agricultural portion of the business, but as we launch new products and increased distribution we still ended up having a positive volume sales number. As I mentioned earlier, the profitability in the segment was higher due to an improved product mix and lower raw material cost. We were fairly disciplined in terms of our pricing that enabled us to hold on to pricing relative to raw material cost situation. The company continues to implement its strategy of expanding distribution. Based on data from the Society of Indian Automotive Manufacturers there is a positive forecast for this year in terms of growth where passenger vehicle sales is expected to grow between 6% and 8%. This of course is contingent on a good monsoon taking place which hopefully the law of averages should catch up and if that monsoon does takes place then well the expectation of the auto segment growth will be relatively good and will also have a rub off effect on our industrial oil sales as well as rubber process oil sales.

If we now come to the cable business, the cable business has delivered a reasonably good growth where we have grown by 20% in value terms please keep in mind that aluminum, copper and polymer prices were sharply down in FY16 over FY15. So the amount of tonnage which we processed is far more than a 20% growth. The revenue has really come from elastomeric and E-Beam cables which delivered a growth of about 68% and the power cable segment which delivered a growth of about 24%. The EBITDA margin post forex adjustment increased by 20 basis points from 5.5% to about 5.7%. This is after actually taking advantage of cleaning up a lot of the old issues that we had in terms of various contract and project executions in the cables segment over the year. A few of which were legacy issues that we inherited when we took over the business 5 years ago. All these provisions put together come to approximately Rs 5 crores, which have been factored into the cable business numbers and affected the EBITDA Margin by almost 0.8%. If you factor that in EBITDA Margin would have been actually 6.5% for FY16. The outlook that we have remains positive as we expect the domestic scenario to improve for all our businesses. There are clear signs of eminent improvement in demands if these schemes announced by the government actually result in the tenders of the sizes that are being indicated.

Our sense is that by the time these tenders are really awarded and business flow comes into our products which are little bit later than the CAPEX cycle it will happen only in the second half of this year. On the export side, we are seeing more challenges relative to domestic sides since many of our target countries for export are actually cash strapped due to the lower commodity prices. So clearly, the strategy is to focus more on the domestic market across all the product line, though we will maintain our presence on the export side. Anticipating these increased demand, we have further embarked upon a capacity expansion plan. The plant which is being set up in Jharsuguda with a capacity of 30,000 metric tons per annum of conductors is likely to be commissioned – in the Q3FY17 we are targeting a timeframe of October, 2017 if everything goes well. The specialty oil plant which is being built in Sharjah, UAE through our subsidiary of a 100,000 KL is also expected to be commissioned in the August, September time frame, subject to all the local approvals being obtained. We are also increasing our power cable capacity where we will be able to increase not only the volumes, but also be able to take the range up to 66 KV towards the end of this financial year. If you add the CAPEX number over here then a total of about Rs 140 crores of CAPEX will be spend between FY16 and FY18 on these projects domestically and approximately a Rs 100 crores which is $15.5 million on the plant which is being built in Sharjah. All in all even though things look at the moment little bit slowly on the ground there seems clearly eminent improvement in demand likely to come and we are quite optimistic that if these demands does come through then Apar as a company is very well positioned to take advantage of this scenario. With this I come to the end of my comments I would like to thank all of you for taking out time to attend this Earnings Call of us and we would be happy to take any questions if there are any at this stage.

Moderator: The first question is from the line of Aditya Wagle from Aequitas, please go ahead.

Aditya: Could you just repeat volumes for Q4 in conductors?

Kushal Desai: In conductors we did approximately 50,000 metric tons.

Aditya: In conductors and specialty, do you see the margin sustainable going forward, the margins which you did, the EBITDA for metric ton and EBITDA per Kiloliter which you did in Q4.

Kushal Desai: On the conductor side, the guidance which we have is to do between Rs 8,000 and Rs 8,500 per ton. So the Q4 margins were little bit higher it came at almost Rs 9,700 per ton, some of that was from more profitable orders that got actually preponed, but we have a reasonably strong confidence that we should be between this Rs 8,000 and Rs 8,500 per ton basis. As far as our oil is concerned, the Q4 numbers and our guidance for the next year are almost similar where we are guiding an EBITDA between Rs 4,000 and Rs 4,500 per KL but on a higher sales number. Our target is to do about 9% to 10% increased sales volume.

Aditya: The legacy orders in the cable segment the provisioning, has it all been done or will it continue?

Kushal Desai: Yeah, we have actually provided for almost pretty much everything that is there. So the slate is relatively clean. Some of these were actually also pertaining to commitments which had to fulfilled on export obligations and things which were not done by the erstwhile management. All those things have been sort of factored in and then cleaned up in this period.

Aditya: What is the current order book in the conductor segment?

Kushal Desai: Approximately it comes to 140,000 metric tons which is at Rs 1,751 crores of order book, approximately is that much in quantity.

Aditya: Fine sir. That is it.

Moderator: We have the next question is from the line of Sandeep Baid from Quest Investment, please go ahead.

Sandeep: Congratulation on a very good set of numbers. The last call you had mentioned that the oil business we may take some inventory hit, so that has not come and, we have been able to manage that?

Kushal Desai: The bulk of inventory hit was taken in Q3 and Q4 of the last financial year and then whatever little residue was left over was compensated by lower raw material cost and a few orders that slipped in from the previous year into this financial year. So as a consequence, you will see the EBITDA per KL being higher for the first half because of the spillover of higher price order into the financial year, but everything has been factored into these numbers. We are not really carrying forward anything.

Sandeep: So the numbers we delivered in Q4 is what we think will sustain going forward.

Kushal Desai: Yeah, that is pretty much what we feel.

Sandeep: On the conductor side, we have delivered 1,70,000 tons while our capacity is about 1,50,000 ton. Has there been some outsourcing also involved in?

Kushal Desai: There has been some outsourcing involved and in some cases even the mix of conductor that were there which were favorable. It allowed higher output because the capacity is taken actually for the certain standard weighted average combination of conductors that are manufactured. However there was a component of outsourcing involved where the contract allowed us to some amount of outsourcing and this was primarily done because certain clients suddenly wanted faster delivery especially when power grid needed to do faster deliveries in the Q4, some of the other client's conductors were then outsourced.

Sandeep: I assumed that your margins on the outsourcing will be slightly lower

Kushal Desai: The margins on outsourcing are substantially lower, so actually that drags the total number down.

Sandeep: My last question is on your Rs 9,700 margin on conductor side in Q4, what was the share of high efficiency conductor that got executed in Q4?

Kushal Desai: In that particular quarter, it was over 10%. For the whole year, the number came in at 6.2%, but in the Q4, it was over 10% and that has actually yielded a higher EBITDA per ton for that particular quarter whereas the guidance which we have for the next year takes more even loading of these high temperature conductors.

Sandeep: I think of your order book about 6.5% or 7% you are saying is high efficiency conductor.

Kushal Desai: At the moment, the high efficiency conductor order book is about Rs 300 crores out of a total order book of about Rs 1,750 crores.

Sandeep: Total that is about closer to 17% or 18%.

Kushal Desai: Sorry, it is Rs 225 crores on a segment order book of about Rs 1,750 crores.

Sandeep; That is about 12%.

Kushal Desai: Yeah.

Sandeep: Till 13%.

Kushal Desai: Guidance is that we should be able to do about 10% of high efficiency conductor next year given whatever the delivery schedules are for these orders.

Sandeep: Similar to what you did in Q4.

Kushal Desai: Similar to what we did in Q4.

Sandeep: Thank you.

Moderator: The next question is from the line of Divyata Dalal from Systematix Shares, please go ahead.

Divyata Dalal: Good afternoon sir congratulations on a very good set of number. We wanted your view on the volumes in the conductor business, how will it sustain going ahead for next 2 years, what is our view on the volume growth?

Kushal Desai: During FY17, we expect the volume to be approximately between 150,000 to 170,000 tons and there are two major factors for that. One is that when this Jharsuguda plants comes up which is around the October timeframe, certain equipments will be moved into that location, so there will be a short-term disruption for a couple of months that takes place due to the and then the usual commissioning issues. However, as a high temperature conductor business goes up, the total amount of conductor that we can run on the same sort of equipments goes down because of the significantly larger amount of processing time, but then the mix of the product changes much more favorably. Our focus for FY17 really is to look at delivering a similar volume number as a previous year may be marginally less, but with a much better product mix as we expect the high temperature conductor demand to be at about 10% to even may be 12% depending on if any new tenders get finalized in the year, a 30,000-ton capacity increase you will see which will be fully effective in FY18. So the FY18 name plate capacity will go to 180,000 ton.

Divyata Dalal: In the presentation, we have mentioned that we are facing some competition in conventional conductors?

Kushal Desai: In the conventional conductors side as the tenders are coming up and all of it comes really on a reverse auction basis, there is a lot of pressure the whole system is actually margin deflating because everything is on reverse auction basis including EPC contract which are awarded after this, many companies are following on a reverse auction basis. So as a consequence, we see that there is a certain amount of pressure which will come on conventional conductors which can be delivered by a larger numbers of players and the overall weighted average mix will improve with us growing the high temperature or the high efficiency conductor business. This seems like the way the market is going to operate in a next couple of years, the only trigger point that may change this is when everybody order books start getting filled up and sense is that as the demand increases in the second half of this year and into FY18 even the regular conductors may see a general improvement taking place in the EBITDA per ton basis.

Divyata Dalal: In terms of volume and the cables business what is the contribution of elastomeric and OFC cables to total sales for the full year?

Kushal Desai: The elastomeric and optical fiber business was approximately about Rs 350 crores out of the Rs 672 crore, so it is about 55% of the revenues. That mix will partially change the next year because we do expect the elastomeric business to grow, but on the other hand the fiber optic side there is nothing happening on that front and our expectation is to grow the power cable side of the business. All these IPDS and the Uday scheme already the company has received about Rs 50 crores worth of orders from the first set of tenders that have come up under Deen Dayal Yojna. Cable side actually you should see also some amount of increased activity from the Deen Dayal Yojna as well as the IPDS. The IPDS is more for the 33kv and higher voltage and Deen Dayal is actually focused around distribution transformers and the lower voltage cables and conductors.

Divyata Dalal: In terms of growth numbers for cables for next 2 years or 3 years our focus will clearly be on elastomeric and power cables.

Kushal Desai: The elastomeric cable growth is driven by three segments. One is growth in the business from the Indian railway, second one is projects coming up from defense where we are seeing a there is increased number of tenders which will be floated and then the non-conventional energy side which is wind and solar. So all of these segment we see growth taking place. So the elastomeric side will definitely grow over the next 2 years, clear visibility on that and the power cable side is essentially as I mentioned earlier coming through the Uday related schemes.

Divyata Dalal: We can assume 15% to 20% growth similar to what we did in FY16?

Kushal Desai: Our next year target is basically a 15% growth in the cable business. Our budget is at about less than Rs 800 crores.

Divyata Dalal: Lastly, in terms of CAPEX, you mentioned Rs 140 crores in the domestic market, so this around Rs 35 crores or 40 crores would be for the Jharsuguda plant I assume.

Kushal Desai: The breakup of that actually is, about Rs 30 odd crores in the Jharsuguda Plant and there is also certain CAPEX which we are incurring in our conductor facility at Silvassa. In addition to that about Rs 45 crores will go into the cable side for expanding or debottlenecking some of the elastomeric cables as well as putting all these new manufacturing capacity in place for the power cable side. The oil business on a domestic is below Rs 20 crores.

V C Diwadkar: Out of this Rs 140 crores, Rs 32 crores is already incurred actually. It is sitting in CWIP, but you will see assets equivalent to Rs 140 crores getting commissioned.

Divyata Dalal: This will be over a period of next 2 years.

Kushal Desai: FY17 and may be a slight spillover into the early part of FY18. This is all being timed in line with bigger increase in demand which we expect in FY18 which will emanate from all these schemes actually start getting operational.

Divyata Dalal: And the funding for these would be through internal accruals and may be some?

Kushal Desai: Through internal accruals and then of course there were some Rs 71 crores raised last year through the placement of treasury stock. So between those two we should be able to fund these expansions.

Divyata Dalal: What would be the average cost of debt?

V C Diwadkar Average cost of debt will be basically close to around 7.5% something.

Divyata Dalal: All right. That is it from my side. All the best. Thank you.

Moderator: We have the next question from the line of Girish Raj from Quest Investment, please go ahead.

Girish Raj: Thank you for the opportunity. I just wanted to understand at what point of time we will have to communicate to the customers in the conductor segment that we would be supplying an outsourced product?

Chaitanya Desai: Most of the times we don’t need to do the outsourcing, but at times when the client is asking for preponement especially on the export business at that time we told the party that we would be able to supply after a couple of months, but since the party wanted the earlier supply, we told them the other alternatives to get it outsourced which they agreed and there were some cost consideration towards that also. Generally, most of these tenders are EPC related contract, so there is nothing that debar outsourcing as long as you stick to the quality and the specification of the product. However, in most cases our policies is to be very transparent and so we carry the customers and keep them in the loop in terms of every stage of what is going on. Our preference is not to do any outsourcing for two reasons one is that it preserves the better margin in the company and secondly obviously we believe that we make the best conductors in the country and we have more control over the quality if it is made in-house. So that route is not really taken by us unless we are pushed against the wall or the client really desperately needs it to meet certain delivery commitment.

Girish Raj: If there was order book for FY17, why can't we source the conductors since we are keeping the volume?

Kushal Desai: Our preference is not to do that because as we stated earlier it is really marginal dilutive and if we are able to time it such that we can accommodate the manufacture within Apar itself then we deliver not only a better margin to ourselves, but our clients are also happier with a better quality product going out to them. Our strategy that we get into FY17 is to actually avoid that.

Girish Raj: Got your point, sir. Thanks for the explanation.

Moderator: The next question is from the line of Pawan Nahar from Religare, please go ahead.

Pawan Nahar: Good afternoon gentlemen and congratulations for good results. I am sorry I missed the first part, so I just wanted to ask you volume in EBITDA guidance for the two segments mainly oil and conductors?

V C Diwadkar: As far as conductor is concerned we are targeting volume close to last year, something less than 170,000 actually. We have done 170,000 and the EBITDA guidance between Rs 8,000 and 8,500 per ton. As far as oil is concerned we are targeting close to 9% to 9.5% growth in volume and EBITDA guidance, is Rs 4,000 to 4,500 per KL.

Pawan Nahar: This seems to be lower than what we have done in the past and what we think is normal. If I would look at 7 year average I am looking at sheets your EBITDA per KL is more like Rs 4,500 and in the past you have told us the band is more like it can go to Rs 5,500 to 6,000 any big change that has happened.

Kushal Desai: No, there is no big change Pawan. If you basically look at the last financial year, we did have better margins in the first half of the financial year and that really came from lower raw material cost versus orders that are actually spilled over from the previous period and particularly in the case of our industrial and automotive products some of the lower raw material cost we were able to hold on to in the form of increased margins by holding on to prices. Given the fact that the scenario this year is reversed where you know you are seeing steady increase in the price of crude and as a consequence the steady increase in the price of base oils you will not have that additional kicker coming in. We expect that the margins will go more to a normal situation and there are bound to be some price leakages as you have to keep increasing prices, so considering all that on a weighted average basis guidance should be in between Rs 4,000 and 4,500 KL. Also we are keeping in mind that you know there is growth of about 9% to 9.5% which Mr. Diwadkar just mentioned. A portion of that is going to be led from the transformers oil side and we expect that demands for transformers oil will be higher in the distribution segment where you have particularly the spending under the Deen Dayal Yojna taking place with rural electrification and the kind of products that go into that are much lower in terms of margin for us relative to some of the power transformer side. Considering all that this is the sort of the guidance that we see looking at where we stand today.

Pawan Nahar: In FY16 again pardon me if this question is being asked in cables side you have made some provisions relating the past order, but if you can quantify how much was that

Kushal Desai: The provision is of approximately Rs 5 crores on a various contract related issues meaning all the legacy issues which were there as well as certain export obligations which we cleared off.

Pawan Nahar: So your EBITDA margin was more like little over than 7%.

Kushal Desai: If you actually take the EBITDA for the operations for the year they were higher by about 0.8% because it Rs 5 crores over sales of Rs 675 crores. Correspondingly, all of that provision was made in the Q4. So the adjustment in the EBITDA in the Q4 also can be then computed.

Pawan Nahar: What about your margin expectation for FY17 on this ballpark Rs 800 crores turnover.

Kushal Desai: On margin expectation for that is to be at between 7.5% and 8.5% on the cable side.

Pawan Nahar: Okay for now. Thank you so much.

Moderator: Thank you. We've the next question from the line of Nidhi Singhania from Kotak Mahindra Bank. Please go ahead.

Nidhi Singhania: Yeah, I just wanted to check that what would be the total amount of acceptances out of the total creditors as on FY16.

V C Diwadkar: Acceptances will be close to around Rs 900 and Rs 950 crores.

Nidhi Singhania: Okay. And sir how much would be the loans repayable within a year out of the current liabilities.

V C Diwadkar: Loans repayable within a year is around Rs 37 crores i.e. long term loans repayable within a year.

Nidhi Singhania: Sir, at consolidated what level?

V C Diwadkar: I'm talking at consolidated level only.

Nidhi Singhania: Okay, both these numbers are at consolidated level.

V C Diwadkar: Correct, correct.

Nidhi Singhania: Okay. Thank you sir.

Moderator: Thank you. The next question is from line of Bharat Sheth from Quest Investment, please go ahead.

Bharat Sheth: we have started talking of HVDC line, tender floating and some of the lines are also commissioning. So can you give something going ahead?

Kushal Desai: Well at the moment, you know, we're the only Indian transformer oil manufacturer that, has experience of supplying into the HVDC transformers and we have approval in place, from Alstom to whom we've actually supplied quite a lot of products as well as from ABB, Sweden and Siemens in Germany, so our sense is that, India is looking at increasing the footprint on HVDC because there are inherent advantages of HVDC over the AC systems. So as business grows, you know, we stand to gain from it. The first HVDC line of Alstom, you know, almost 70% of that quantity is still left for us to supply and we expect it to happen in this financial year. As I mentioned earlier, the 1200 kV test station in Bina of Power Grid has also commissioned, transformers of a couple of manufacturers have gone live and they contain actually our power oil, which we specifically design for the 1200 kV product so from product stand point we still sit, you know, at a top of the chain.

Bharat Sheth: Okay. I mean how big is this opportunity that we've seen and how is the profitability vis-à-vis normal transformer oil for us.

Kushal Desai: The general profitability is a bit higher because the expectations, of the product are significantly more than the general transformer, but you know when you look at next year's number, we will see increased profitability in FY17 from sale of these products. But on a weighted average basis, it may get mitigated to some extent because we have seen big growth happening on the distribution transformer side where you know the product that goes in is relatively at the low end of the spectrum and the competition levels are also more intense compared to, on the power transformer side where the specifications are tighter and the advantages that people like us have are much greater. Uday Yojna which is there is all entirely small distribution transformers and that's where a very large allocation of the money is taking place.

Bharat Sheth: Okay on transformers oil in the replacement side, can you give some sense how Uday can improve things for ourselves.

Kushal Desai: Well, I think these are two separate issues, replacement of transformer oil, you know, there is a certain replacement demand, which is there, as we maintained in the past, it is may be between 5% and 7% of the installed base. We focus more on the power transformer side as oppose to the distribution transformer side in terms of these tenders. As far as Uday is concerned, we see a big uptick in demand once, you know, these tenders started getting finalized, but most of it is going to be on a distribution transformer side, but the number of transformers, just the physical quantity is going to be very high and our sense is that the orders will started getting placed in the second half of this year and you will see some demand in second half of FY17, but a big jump in FY18 as you know the actual deliveries of the transformers take place.

Bharat Sheth: Going ahead with the commissioning of this Sharjah facility, how it will change our overall oil effect?

Kushal Desai: We expect about 50,000 kiloliters of products, which we're currently exporting out of India to be shifted, for manufacture and sale out of the Hamriyah facility. And then of course, we obviously intend to grow the business from Hamriyah because the nameplate capacity there is for 100,000 KL. And given the proximity that we would have to growing market in the Middle East especially these oil prices stabilize, then you know we would stand an advantage compared to any of our competitors, none of whom have a manufacturing facility in the Middle East.

Bharat Sheth: How in terms of profitability, it can work for us?

Kushal Desai: You know there is no immediate impact that we see in terms of, dramatic improvement in profitability if we move, to the Hamriyah facility. So our objective is to kind of maintain the profitability that we have out of India, given the fact that, you know the scale that we'll be operating there initially will be less, but the superior service level should help us, you know, gain more market share in that particular region. So it's part of a growing the volume strategy as well as these schemes, are production basis because all our raw material incoming and outgoing, all goes through the ports around Mumbai, so it's a very concentrated position. When you do the risk assessment for the company, our Board of Directors have been constantly looking at de-risking for our operation. And this was the integral part of, the decision that we took to look at an outside location. Our exports actually if you see in terms of turnover is approximately for the oil business is about 35% of the volume that happens of the business. So that's how this de-risking should take place, so I won't really see that as incremental increase in profit as much as volume growth through proximity to clients as well as in the long term, de-risking that the company will have advantage of that.

Moderator: Thank you. Our next question is from the line of Shraddha Sheth from Edelweiss, please go ahead.

Shraddha Sheth: Hello Kushal, Congrats on a good set of numbers. Just follow up from the previous question, I just wanted to understand this value-added in the overall oil portfolio would be how much percent of sales? In the sense about 220 kV would be how much percent of sales?

Kushal Desai: Yeah, so if you take the transformer oil side, about 25% of our volume actually comes from products that are going in at 400 kV and other special type of transformers where, the specifications of the oils are different like for example you have certain special type of instrument transformers, furnace transformers, all requiring special type of products. So last year we delivered approximately 25% of products coming from that. If you take 220 kV and above, Mr. Diwadkar has just thrown up a number here, which is about 34%, so 34% of our transformer oil sales has come from product that goes into 220 kV and above and has some special requirements.

Shraddha Sheth: So from your commentary as I understand what we're guiding is because of the demand in the, lower value-added oils in Deen Dayal Distribution Transformers, should we expect the net to deteriorate in this year?

Kushal Desai: You know if you look at the special products that we have, the percentage volume may fall a little bit because we're expecting that the standard products that go into distribution will just grow at a faster pace in the short term. The demand for power transformers, we see it to be steady for not just 1 or 2 years, but a period much longer than that. So the absolute number will continue to increase, but you know we see this big short term fill-up happening because of this Deen Dayal Yojna, you know, on the distribution transformers.

Shraddha Sheth: Sure. So let me put it this way. As you said, you know, towards FY18 we really see the pickup happening in the power transformer side, so can we expect better EBIT margins or EBITDA for KL go into FY18 with the changing mix.

Kushal Desai: Well, actually, you know, it's really difficult to predict, you know, beyond a period, so the strategy, which have been following for our transformer oil segment is, you know, we have about 45%, 46% market share and we want to maintain that share across the different segments. So depending on which segment grows, we will offer the product, which is relevant to that segment and that will dictate the sort of margins based on the competition that is there. So it's little difficult to see if automatically the margins will grows in just transformer oil, however, if you see weighted average margins for the business as a whole as our automotive and industrial business picks up, certainly those are higher margins than the transformer oil side. And you know just to give you an example we do approximately 11% of volume in the high end industrial and the automotive but that contributes about 18% of revenue, so you know automatically as that segment grows and we are expecting those two segments to grow faster than the rest of the base business, that will then end up actually yielding a better weighted average mix, you know, into FY18 and beyond.

Moderator: Thank you. Our next question is from the line of Chirag Muchhala from Nirmal Bang, please go ahead.

Chirag Muchhala: Yeah, thank you sir. Sir, the question is on our interest cost, I mean normal bank and finance charges as well as the Forex element, so basically for these couple of years, it has been at around Rs 150 crores, so I mean sir any outlook on that sir.

V C Diwadkar: Out of Rs 150 crores, we're picking up close to Rs 40 crores of the open period exchange in the EBITDA. If you see our investor presentation, we knock off the open period FOREX while taking out the EBITDA per KL.

Chirag Muchhala: Correct.

V C Diwadkar: Rs 40 crores goes actually, then after that what remains is Rs 27 crores of the Forex and Rs 84 crores of the interest actually. More or less the interest cost will remain same actually.

Chirag Muchhala: Even though, you know, we have seen a significant reduction in debt also, but even though interest and borrowing cost, I mean, if I see excluding this FOREX element.

V C Diwadkar: It depends upon the financing actually. In case of conductors, we have done more of the domestic financing actually. When you take more of domestic products, it depends on the how you do the sourcing actually. Sometime the imported products are cheaper, so you bring imported products, then the imported financing will be there. The imported interest along with the forward cover cost will be lower actually whereas this year as compared to last year, we have done more of the domestic financing, so that is why you must have seen increase in the interest cost.

Chirag Muchhala: Yeah, right, but basically you're saying that both put together, this Rs 150 crores is not a mix…

V C Diwadkar: Remaining to 120 crores actually, after removing the portion, which is adjusted against EBITDA.

Chirag Muchhala: Sir, in our conductor revenue, is it possible to get a split of the domestic market, the split between how much comes from Power Grid, state electricity boards and other private BOOT projects.

V C Diwadkar: See Power Grid portion was close to around 20% in this year.

Chirag Muchhala: That is a total or conductors revenue

V C Diwadkar: Of the total conductor revenue, Power Grid was 20%.

Chirag Muchhala: Okay.

V C Diwadkar: 40% was exports.

Chirag Muchhala: Correct.

V C Diwadkar: And the balance split, right now I'm not having actually. It will be some EPC contractor will be here, Kalpataru, KEC, etc. plus there will be some transmission companies.

Chirag Muchhala: Correct. So sir, how are you I mean witnessing the current, competitive scenario in terms of, pricing in the Power Grid tenders?

Chaitanya Desai: Power Grid is nowadays also buying the conductor through some of the EPC for this through the reverse auction method, so basically there is a competition and it is not anything different from what we've seen in the past as far as Power Grid. It was already competitive, so it will continue to be competitive.

Chirag Muchhala: Okay. In this HEC conductor, I mean now it becomes approximately 6% of revenue, so that primarily goes to Power Grid or it is again evenly spread among all other parties also, SEBs, exports or I mean private BOOT projects.

Chaitanya Desai: It is mainly from the state companies, state transmission companies. Power Grid is also there, but they are not doing on the EPC model they are outright buying the conductors while the state transmissions are buying the conductors as well as asking us to do the turnkey job.

Chirag Muchhala: Okay.

V C Diwadkar: At present, there are no exports.

Chaitanya Desai: Yeah, as of now no.

Chirag Muchhala: Sir, any specific reason for that sir?

Chaitanya Desai: So some of the export markets, they have very difficult qualification requirements. So as we build up our QR in India, we will be eligible to bid for the export jobs in times to come.

Chirag Muchhala: Okay. And sir, last question again on the bookkeeping part, the tax rate for full year in FY16 was approximately around 26%, you know, compare to 30% last year, so what should be ideally the steady state tax rate for 17?

V C Diwadkar: Tax rate for FY16, you said?

Chirag Muchhala: Yeah.

V C Diwadkar: That was mainly because of that Rs 43 crores profit on the treasury shares, it was not having any tax impact, but otherwise we're almost in full tax actually.

Chirag Muchhala: correct.

V C Diwadkar: Once our Sharjah Subsidiary starts there will be no tax for Sharjah Subsidiary.

Chirag Muchhala: Okay sir.

Moderator: Thank you. Ladies and gentlemen as there are no further questions, I now hand the floor over to Ms. Nisha Kakran for closing comments. Thank you and over to you, ma'am.

Nisha Kakran: I would like to take this opportunity and thank the management for giving us the opportunity to host the call and the participants for joining the call. Thank you everyone.

Moderator: Thank you very much. Ladies and gentlemen on behalf of Four-S Services, that concludes this conference. Thank you for joining us and you may now disconnect your lines.