



“APL Apollo Tubes Q1 FY15 Earnings Conference Call”

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MANAGEMENT: MR. ASHOK GUPTA – MANAGING DIRECTOR

MR. PANKAJ GUPTA – CFO

MODERATOR: MR. GAURAV SUD – ANALYST, KANAV CAPITAL ADVISORS

Moderator: Ladies and gentlemen good day and welcome to the APL Apollo Tubes Q1 FY15 Earnings Conference Call. As a reminder, all participant lines will be in the listen-only mode. There will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please 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. Gaurav Sud. Thank you and over to you sir.

Gaurav Sud Good evening everyone and this is Gaurav from Kanav Capital Advisors. On behalf of Christensen IR and Kanav Capital Advisors it is my pleasure to welcome you all to the APL Apollo Tubes Q1 FY15 Investors Conference Call. The call is being held to discuss the performance of APL Apollo for this quarter and to answer any questions that you may have. I hope that all of you have had a chance to go through the quarterly results and the press release. Today on the call we have Mr. Ashok Gupta – Managing Director and Mr. Pankaj Gupta – CFO from APL Apollo Tubes. I would now like to hand over to Mr. Pankaj Gupta of APL Apollo Tubes for his opening remarks.

Pankaj Gupta Good afternoon ladies and gentlemen and a very warm welcome to our Q1 FY15 earnings conference call. For the first quarter ended 30th June, 2014 we are happy to report that our consolidated gross turnover is Rs. 838.69 crores. This represent almost 20% year on year increase driven mostly by similar increase in volume. The volumes reached 1.69 lakh metric tons for the first three months as compared to 1.45 lakh metric tons in the corresponding period. Net sales for the period is Rs. 745 crores, an increase of 18.37% year on year. Our EBITDA for Q1 FY15 is 50.15 crores and PAT is Rs. 19.86 crores, registering almost 40% growth from the previous quarter that is Q4 FY14. The non-annualized EPS is Rs.8.47 for the quarter . We are well on track to achieve 1 million tons capacity and have recently commissioned our third sheet galvanizing plant. Work for installation of fourth sheet galvanizing plant is in advanced stage which further extends our leadership in pre-galvanized space of the ERW tube category. Our capacity utilization remains high at +85%. In the current subdued economic scenario, the company is focusing its efforts to be as close as possible to consumption centers and hence penetrating deeper into Tier-2 and Tier-3 cities through strong brand promotions, exercises, alliances and fabricator's conferences etc. This, coupled with other operational and marketing initiatives helped us improve our margins in the reported quarter. Our EBITDA is over Rs. 50 crores with EBITDA margin of 6.7% registering almost 45 to 50 BPS improvement than the immediately preceding quarter. To improve professionalism and strengthen the corporate practices as we grow in scale and size the board has appointed Mr. Anil Kumar Bansal as independent director who has been Executive Director of Indian Overseas Bank with almost four decades of rich experience in banking industry. Presently he is serving as Chairman and Director of Care Limited, an independent rating agency and Director of Canara HSBC Oriental Bank of Commerce Life Insurance Company Limited. With this I would like to hand over to Mr. Ashok Gupta, Managing Director of the company.

Ashok Gupta

Thank you Pankaj. Good afternoon everyone. I am once again with you and on a relatively better note. Q1 FY15 was definitely a slightly better quarter than what we have seen in the last year. There have been some resurgence in demand and because of that you would have seen EBITDA margins have started going North. There is some improvement now, something which we were looking forward to for quite sometime. We are continuing focus on further improving the EBITDA margins. The top-line is already growing. I think in the first quarter top-line grew by over 20% and we are trying that it should grow on a year as a whole by more than 20%. There are a lot of activities being done to improve the margins including branding new products, most of the things we have already talked about in our previous conference calls and in case there is anything else then during the question hour I will try to bring in those highlights as well. So without further ado let us start the question-answer. So I invite all of you to please put up your queries and we will try to answer them to the extent we can. Thank you.

Moderator:

Thank you very much sir. Participants we will now begin with the question and answer session. We have the first question from the line of Agastya Dave from CAO Capital. Please go ahead.

Agastya Dave

You mentioned that this was a better quarter than what the previous quarter that we saw – and you are seeing better demand. I was just wondering we had spoken earlier and as you were suggesting that there is a little bit of restocking there. So can you elaborate whether this is restocking or there is genuine end-user demand which is happening? And also on the demand side if you can just tell us what you are seeing across different segments of pipes and how different products are behaving? Where the demand has started picking up and what are your thoughts over the next 2 or 3 years, where do you see demand genuinely picking the fastest and hence because of demand how the product mix will change and how your EBITDA margins going forward will look like? And my last question is on the capacity side, you said we are on our way to meet 1 million tons this year. Did you mean by volumes of sales or just installed capacity?

Ashok Gupta

Thank you very much. Actually you are right. There has been resurgence in demand but it is possible that the real demand may still take some more time to pick up. The Modi effect may still take time to come. Some of it may be restocking but then it may be down the line, which means that while the stockists, the retailers, the dealers maybe restocking plus companies which are trying to complete their projects now with the hope that things could look better. You know when sentiment improves, it improves all through the line. So in my own understanding there has been improvement marginally in the demand from the consumer front but significantly by restocking. And as days pass by, the consumer demand should further improve because the sentiment is improving particularly among projects. People are trying to put up projects for manufacturing of things. People feel that industry revival is on the go. Today only I was reading that the salary level of engineers from IIT and non-IIT are increasing which again show that there is some appetite for expenditure. I feel that though there has been a marginal improvement in real demand, it will further go up in the days to come. And secondly about EBITDA margins, you see EBITDA margins are limited to couple

of things. One is of course the real demand. As the real demand improves then EBITDA margins are expected to improve and there is another connection to it. As the governance improves and better practices are followed, then again the players who are not so serious get marginalized and so again EBITDA margins improve. Last but not the least, it also is affected by the management actions. We are taking series of actions to improve our EBITDA margins. One big thing we are trying to do is to create our own significant brand so that people can really feel the difference between a good brand and a bad one. Here we are trying our best that there should be a pull factor from the consumers. To some extent this has already started. Despite the rainy seasons, our sales in the month of July were pretty good. This is because of the pull factor from the consumers. We are trying to further focus on that and also we are working on new products. Recently we have designed a totally new product, which is neither a square, nor a rectangle, nor a round shape. It is a very odd shape. Something that could be used for door frame and we have also got the design patented. We are working on some new products so that when the new products are there and we are the only manufacturer again we will have some better margins possibility. We are taking a lot of steps to ensure that the EBITDA margins improve. Our focus is that sometime back this used to be around 8% and last year it had fallen to around 6.5% or even below that. Now we are trying to recover that and it should again come back to the level it used to be. I am hoping that with the steps we are taking there will be some improvement. So far as capacity is concerned our current capacity is around 8 lakh and we are hoping that within next 18 months or so we should be able to cross 10 lakh. That is the capacity which we have planned for, the goal we have kept for ourselves. And our capacity, utilization level continues to be around 80-85% so this year we are expecting that we should be able to produce anywhere between 7 to 7.5 lakh ton, our target being 7.2 lakh tons. We hope that slowly and gradually we are on the way to that. If we achieve 7.2 lakh that will mean 30% improvement over last year. In the first quarter our sales was around 20% higher as compared to the first quarter over last year. Now we have to work much more than that. 20% will not do, 30% is required. So this is the story. So far things have been alright. Things have been in our favor. We hope things will further improve and we are working on it.

Moderator

Our next question is from the line of Giriraj Daga from Nirmal Bang. Please go ahead.

Giriraj Daga

Sir my question is that you said you did a volume of 169. If I normally look at it from a realization perspective it has dropped slightly on a sequential basis, on a blended basis. So any particular thought for that, like prices have come off because what we had said in terms of pricing that we are holding on the prices but when you look at the prices on a blended basis they have slightly come down. So any particular thought and how the pricing currently is, currently in the sense like how the raw material cost in particular HRC prices have moved and have we passed down any benefit or have we taken any calls for the prices increase on that side?

Ashok Gupta

You see there will be some minor adjustment which will be there because of two factors. One is that you always have some movements of raw material prices up and down and that is a

continuous phenomenon. Also the mix may be different. The price is not uniform across all the products. Our price varies from around a level of 41,000 to 61,000. There could be some variation in the product mix, that is why average pricing could be up or down. So relatively pricing has not changed much. The pricing has slightly in fact improved but on average price front you may see some minor variation. That is not affecting the overall pricing level. So pricing has not reduced. There is some improvement only in April-June as compared to the previous quarter.

Giriraj Daga

If I look at the GI pipe, the proportion is increasing which is actually a good thing but right now simultaneously zinc cost is also increasing. So are you going to pass on that cost increase to our customer or we are going to do it only through the volume increases, they have got it outside that?

Ashok Gupta

No, increase in the zinc price is marginal. As it is the zinc cost and the overall cost is less than 10%. It is around 6% to 8%. And the zinc price increase may be another 5% to 10%, so overall effect is less than half a percent. And even that we try to pass on the increase, sometimes you are able to do that, some sizing you are able to do it. In the first quarter we were able to pass on almost the entire increase to the customer. But again it depends on the branch or state to state. While in the State of Kerala we were able to do it. in the state of UP and Gujarat we were not able to do it. So overall I should say this is not having any major impact because the proportion of consumption of zinc as a whole is pretty less but let me again tell you that even though we may not be able to pass on the increase in a particular month because the EBITDA margin in these two cases is so good that on an overall basis it does not matter much.

Giriraj Daga

And sir my last question is what is the gross debt and net debt for the quarter?

Ashok Gupta

Gross debt today is around I think 475 or 500 crores.

Giriraj Daga

And net debt should be similar?

Ashok Gupta

No, we do not have cash.

Ashok Gupta

We are cashless people.

Moderator

We have the next follow-up question from the line of Agastya Dave from CAO Capital.. Please go ahead.

Agastya Dave

Sir you just mentioned on realization and I had similar questions on the cost side. What do you see happening to steel prices domestically, there is some excitement amongst the steel players that now prices will increase. Even though it does not look like there is a supply constraint as of now but with the currency also depreciating do you think in rupee terms the steel prices will go up? And second how do you see the steel scenario playing out? To me it seems some time or other the sales capacity will come in and your raw material should not go out of control. And on a similar front if the demand improves will we get any pricing power this time?

Ashok Gupta

Fine, let me just give you some idea. You see international price of HR coil are hovering around \$550-560 for quite some time. So there has not been any major change, sometimes it goes up by \$10, it comes down by \$10 and the iron ore prices and coal prices have also been under pressure. They have not been increasing. I must say that international prices may not change much. Indian prices may go up by the extent of dollar because Indian pricing is done based on the landed price – imported into duty plus freight. So hopefully only to the extent of dollar parity goes out that means 1% or 2% for example, dollar aside rupee has weakened by 2%. So they may try to pass on the 2% increase. But again it depends on the domestic market. Domestic market today is not having any shortage of HR coil. That being the case they may postpone the decision to increase it and by the time they decide to increase it again the dollar may come back to 60. Hopefully prices will not change much except to the extent of 1% to 2% depending on dollar parity. So far we are concerned that we are not able to make use of any such shortages in general. Because there is sufficient capacity of steel as well as pipes. So we are not looking for any shortage per se but what we are trying to look for is a loyalty or the consumer loyalty of the retailers, loyalty of our dealer network. So we are working on that. So we are not looking forward that in case there is a shortage our price may go up. Our price may or may not go up because of shortage. First of all I do not think there will be any shortage at all. And secondly even the shortage is there I do not think there will be much of a pricing power which will come in. Rather what we are trying to do is we are trying to tell the consumers and the dealers that we are increasing the value of our products. So when I increase the value of my product then I expect to get a better price because of the value I am giving. This is the premises we are working on.

Agastya Dave

Second part of my question is again on the capacity side, do you mean the cycle will now begin? I am sharing with respect to the demand side, assuming that the demand now picks up and probably within 18 months to 2 years you will be running out of your existing capacity or at least should be reaching 90-95% capacity utilization. So when will you take the next capacity expansion? What are your thought processes with respect to debt? Earlier interactions with you guys have led me to believe that you are fairly conservative in terms of loading up of debt and one of your stated purposes was that I want to be a debt free company at least for some time. So do you stick by that and how are you thinking about CAPEX and debt going forward?

Ashok Gupta

So far as capacity is concerned it has been our practice that all along we are trying to increase this step by step. We have already crossed 8 lakh. This year we are somehow trying to cross 9 lakh and there is no CAPEX we take especially for that. We already have the infrastructure, the land, and the approvals all in place so we go over adding 1 mill in a quarter or so. So hopefully we will be able to add 3 mills in this year and take our capacity to around 9 lakh tons and next year we will try to jump to the 10 lakh or 1 million ton level. And this does not require much of a funding. Our total plan for this year is only around 40-45 crores for the CAPEX of which 15 crores has already been spent, another 20 crores may be required which will come out of our own profits. So we do not see that we will be taking any debt. In fact on the other hand our target this year is to reduce debt even by small amount. So we are working

on reducing debt this year. How much we are able to do it will depend on the profits we make and also how much of further debtor controls we can do. But definitely there will not be an increase of debt. Our stated purpose of always controlling debt will continue. I am not really sure whether we could become debt free but that is a more of a dream for me, not exactly a goal. But definitely we will work for not increasing debt and we will try to ensure that debt comes down.

Moderator

Our next question is from the line of Bhavin Chheda from Enam Holdings. Please go ahead.

Bhavin Chheda

Few questions. One, what would be the geographical sales mix during the quarter on how much was exports and second if you can provide me what would be the plant wise production? How much the Bangalore plant is operating, Maharashtra plant is operating and UP plant is operating at?

Ashok Gupta

First of all let me share with you a good news, which I forgot to mention earlier, in the month of June for the first time in our history we crossed a level of 60,000 tons. Earlier our highest was 50,000. Now this is a very big step. We consider it a big achievement in this context that no other manufacturer has been able to cross a limit of 35,000 tons in a month. So I think it is a big thing for us and out of this 60,000 around 21,000 has come from our Hosur plant and 7,000 has come from our Lakshmi plant and 14,000 has come from Murbad plant and balance of around 18,000 has come from our North Indian plants. So basically all our plants have been working at around 85-90% capacity now in this quarter, first quarter particularly in the month of June and July. And exports have not increased much. I think there has been some pressure on exports. Our European market is also under pressure so our exports contingency will be between 7% to 8%. They are not increased at all I should say. Their percentage is almost same and we are now focusing on Australian market. We are talking to them. I am expecting some breakthrough in this month. I am expecting that first big order from Australia should come now. USA is steady. I am trying there also to open some kind of a warehouse or some arrangement in USA. Perhaps that also will be through by September. So these two developments can take our exports in the coming months. Otherwise at this moment there is no surge in exports. It continues to be around 7% to 8% only.

Bhavin Chheda

What would be the all India sales mix like?

Ashok Gupta

See we sold 60,000 tons. Out of 60,000 tons around 28,000 has come from South, almost 50% has come from South.

Bhavin Chheda

This is the June month.

Ashok Gupta

Yeah, because June was highest so that is what is reflecting the future trend and around 13,000 has come from West and around 16,000 has come from North and balance is exports.

Bhavin Chheda

And sir other question how is the working capital needs or working capital cycle is moving on since now you are achieving critical size and now you being a large volume player are you

able to command your terms because we have spoken in the past also it is very important that you tighten your working capital at this size. So are we able to establish the brand and turn into more B2C type of business and squeeze on the working capital side?

Ashok Gupta

I am sure that things on the credit side are pretty challenging because fund flows or credit squeeze continues to be there. We on our side are trying to maintain that our debtors should despite increase in our sales should not be exceeding 30-32 days which have been traditionally there. In the first quarter also there were 30-32 days only so there is no increase per se. Similarly on inventory front also it continues to be between 30 and 32 days. There is no increase on that side as well. Now further squeezing is slightly difficult. What happens when you are trying to get new customers or you increase your volume to the existing customers, those people they want liberalized conditions because they are shifting from one supplier to another supplier and expecting better. So it becomes a challenge and nobody is used to this tight condition of 30 days. People are used to much better conditions. So we on one hand try to accommodate them. Recently we have increased our sales in South and there I think the normal industry cycle is much more than 30 days. So we had to of course fall in line and give more than 30 days but thereby decreasing somewhere else, so average continues to be around that. I would put it this way that we are trying and we have been successful in controlling debt to a large extent. And we are trying that it should go below 30 days but I do not think we will be able to reach anywhere between less than 20 days. So it will always be below 30 days but not much below 20 days.

Moderator

Thank you. We will take the next question from the line of Ritesh Baijal from Christensen.

Diwakar Pingle

Mr. Gupta I think in the initial part you did mention about APL doing a bit to build the brand and things like that. For the benefit of the investors just want to understand what are those efforts that you are taking to, kind of build the brand not only in India but across the globe?

Ashok Gupta

We have taken up a special campaign to improve our brand and make it as popular as the large brands like Tatas and Jindals are and for this we have taken up scheme of things. For example we are having hoardings and retailer boards all over India. We plan to put up around 5000 boards in the whole country and we are trying to have the plumbers and the architects and the fabricators meet. We are holding almost 6 such meeting every week. So with this we are expecting that each and every user of pipes whether it is for structure purpose or it is for transportation purpose he will be aware of our brand, he will understand the better benefits of our brand and obviously we will be able to convert himself from the existing brands through Apollo. That way we are taking a big exercise. In addition to that we are also working on other kind of advertisements like print advertisements and other format by which more and more people become aware of the Apollo name. And you know as our consumption is growing that obviously means more people are using our pipes by word of mouth itself many more people are coming to know of it. Hopefully we will have a very good brand image in days to come.

Diwakar Pingle

I think connected to that is apart from building a brand obviously you need to have products that will kind of give the credence to the brand. So you did mention again in your initial talk

about new products being launched and things like that. So some color on what are the kind of product pipeline as far as new launches are concerned and what you kind of launched in the recent past?

Ashok Gupta

We have been launching special profile and special sizes for the last couple of months. Now we are working on a couple of new products. For example we are working on pre-painted pipes. We are working on color coated pipes. Till now all the pipes sold in the market were black pipes, ordinary pipes, and steel colored pipes. But in many advanced countries particularly Australia all the pipes sold are blue colored. The reason being that such colored pipes do not get rusty and they look nice as well. We have also ordered for the equipment and within next 3 to 6 months we will be launching those pipes in the country. Once you launch those pipes it will be big thing. Also we are working on designer pipes. Currently the pipes are all round and plane but we are working on pipes which will be different shapes so that aesthetically they will look very nice. With this we expect that there will be very significant increase in the brand image as well as the acceptability of our products.

Diwakar Pingle

And my last question is on margin. You did talk about and obviously this quarter has been a better quarter in terms of margins. You also talked about the margins moving back to kind of 8% levels which was there before. You did talk about margins moving up once the demand picks up. But from an operational standpoint are there any specific exercises taken by the company more from cost efficiencies and things like that that the company is doing that can give us some kind of leverage to this margin build up exercise sir?

Ashok Gupta

Yeah, apart from marketing effort you would have observed that despite increase in operation our cost continues to be under control. In fact our labor cost, our power cost, manufacturing cost all have been slightly inching downwards. So I think in days to come we will be further making efforts. One of the main factors of our cost was power and we are shifting more and more to state utility power. That should further reduce the cost. So we are expecting overall cost levels to be better than what they are currently. Currently already we are the best in the country. Our costs are lowest and we are further inching downwards.

Moderator

As there are no further questions from the participants I now hand the floor back to Mr. Gaurav Sud for closing comments. Thank you and over to you sir.

Gaurav Sud

Thanks Shyma. Thanks everyone for being on the call and we look forward to your patronage and if you have any specific questions you can always mail back to us. Our details are on the invite and we look forward to having a call again after the next quarter. Thanks everyone.

Moderator

Thank you sir. Ladies & gentlemen on behalf of APL Apollo Tubes that concludes this conference call. Thank you for joining us. You may now disconnect your lines. Thank you.