"Oriental Carbon & Chemicals Limited Q3 FY18 Earnings Conference Call"

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MANAGEMENT: **MR. AKSHAT GOENKA – PROMOTER AND JOINT MANAGING DIRECTOR, ORIENTAL CARBON & CHEMICALS LIMITED**
MR. ANURAG JAIN - CHIEF FINANCIAL OFFICER, ORIENTAL CARBON & CHEMICALS LIMITED

Moderator: Ladies and gentlemen, good day and welcome to the Q3 FY18 Earnings Conference Call of Oriental Carbon and Chemicals Limited. This conference call may contain forward-looking statements about the company which are based on beliefs, opinions and expectations of the company as on the date of this call. These statements are not the guarantee of future performance and involve risks and uncertainties that are difficult to predict.

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 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. Akshat Goenka – Promoter and Joint Managing Director of OCCL Limited. Thank you and over to you, Mr. Goenka.

Akshat Goenka: Good afternoon and a very warm welcome to everyone. Along with me, I have Mr. Anurag Jain – our CFO and SGA, our Investor Relations Adviser. I hope you have received our results and investor presentation by now, for those who have not, you can view them on our website. During the last quarter, we witnessed volume growth especially in domestic demand. Auto companies have also done well in the last quarter. All auto OEMs have registered growth of around 11% in 9MFY18 compared to the corresponding period last year. Commercial vehicles have witnessed a robust growth led by the high demand of medium and heavy commercial vehicles. This has led to the growth in the domestic tyre industry which has led to increased sale of insoluble Sulphur which is our product. Post the imposition of antidumping duty on Chinese tyres, there has been a significant drop in imports. The imports of truck and bus radials from China has approximately halved thus enhancing the demand of domestic tyres further. The global tyre companies are also investing in India which augurs well for the future growth of the tyre industry here.

We have started doing well in the new geographies of China and North America and we expect these markets to be major markets for us going forward. We have been continuously strengthening our ties with all our customers. With regards to the second phase of expansion, the work is progressing well and is in line with our schedule and budget. Now, I would like to hand over the line to Mr. Anurag Jain to update you on the operational performance for the company. Thank you.

Anurag Jain: Thank you, Akshat. I will take you all through the financials of the company. The revenue for Q3 FY18 is Rs. 88 crores compared to Rs. 77 crores in Q3 FY17, a growth of 21%. Revenue for 9MFY18 is Rs. 242 crores compared to Rs. 221 crores in 9MFY17, a growth of 10%. For Q3 FY18, EBITDA stood at Rs. 27.5 crores, a growth of 28% from last year. For 9 months, it stood at Rs. 78 crores, a growth of 15% from last year. EBITDA margins for the quarter stood at 31.3% and for 9 months at 32.2%. Our interest cost has increased in this year on account of additional interest expense on new launch which were capitalized till start of commercial production last year.

Profit after tax for Q3 FY18 was up 3% to Rs. 15 crores. Profit after tax for 9MFY18 was down by 5% to Rs. 42 crores. This is due to the higher taxes paid on account of increase in deferred tax provisions attributable to the new capacity added and impact of investment allowance last year. PAT margins for the quarter at 9 months stood at 17.4%. With this, I would like to open the floor for questions and answers.

Moderator: Thank you. Ladies and gentlemen, we will now begin with the question and answer session. We will take the first question from the line of Shashank Kanodia from ICICI Securities. Please go ahead.

Shashank Kanodia: We have already guided for Q2 FY19 as a probable commissioning date for second phase of expansion. So are there any chances of advancement of the commissioning?

Anurag Jain: At this stage, we are still looking at Q2 FY19 as a probable commissioning date for second phase of expansion.

Shashank Kanodia: Any guidance on the next leg of growth for us, any concrete plans or any other expansion plans related to the business ??

Anurag Jain: Currently we are evaluating various options, but there is nothing concrete which we can report.

Shashank Kanodia: On the yearly contracts, how has been the pricing trend. I think we were to negotiate some yearly contracts at the end of December. So any favorable outcomes for us?

Anurag Jain: They have been stable.

Moderator: Thank you. The next question is from the line of Rahul Veera from Elara Capital.

Rahul Veera: In terms of our contracts with the tyre companies, , do we work on cost plus basis or are we able to pass on the higher input cost?

Anurag Jain: We do not work on cost plus basis; however, we have two kinds of contracts. One is where we negotiate the prices on every renewal of the contract (every quarter, 6 months/ or annually) and in some cases, we have a formula based contract which moves the price. So we have both the arrangements with tyre companies.

Rahul Veera: What proportion of our business comes from contractual agreements with the tyre companies?

Anurag Jain: The way insoluble Sulphur sells is that you have to first have it approved and then sell it to the tyre companies. So, most of the quantity would be contractual because there is hardly any spot business in insoluble Sulphur. The natures of contract could vary, but most of it would be contractual.

Rahul Veera: On our competitors, how is it behaving on the domestic side like Eastman is there in India right? and how does the prices move for them ?

Anurag Jain: There are no domestic competitors. Eastman is there, but they are not in India. So there are some tyre companies which import material from Eastman, but they are not present in India

Moderator: Thank you. The next question is from the line of Rahul Jain, an individual investor.

Rahul Jain: There have been curtailment in production of certain chemicals for pollution related issues in China. So are we seeing any benefit out of such global events?

Anurag Jain: , There is a curtailment in production of Chinese material of insoluble Sulphur , but it is an entirely different market and not the same market that we cater to. So there is no direct correlation with our market; however, we are seeing some buoyancy in demand.

Rahul Jain: On your next phase of expansion plans, are you fully tied up in terms of your customers or when will they purchase the additional quantity that you will manufacture?

Anurag Jain: That is going as per plan. Our selling time line is on schedule. So it would tally with the projected ramp up of the capacities.

Moderator: Thank you. The next question is from the line of Shashank Kanodia from ICICI Securities.

Shashank Kanodia: If you can just explain the scenario in China regarding the rubber chemicals because a lot of your competitors are expanding this domain, not necessarily insoluble Sulphur, but other rubber chemicals. What is driving that demand and how are we placed?

Anurag Jain: As far as rubber chemicals are concerned, we hear that there has been a cut back in production in China. It is mainly on account of the fact that the Chinese government has become more stringent in terms of EHS (Environmental, Health, Safety) which is forcing the Chinese companies either to close down or cut back production till they ramp up their EHS capabilities which has created a shortage globally and therefore there are many people who are expanding in the rubber chemicals area.

Shashank Kanodia: Do you see this as a structural change or just a temporary blip?

Anurag Jain: No, it would be a structural change to the extent that the Chinese manufacturers will not be able to command the same kind of price benefits or dominant position as they used to do earlier because if they come to the global standards of manufacturing, then their prices of manufacturing rubber chemicals would also go up. So it is going to be a structural change to that extent that then it will be more of an even playing field as far as pricing is concerned.

Shashank Kanodia: So doesn't this opportunity excite Oriental Carbon & chemicals given that your competitors are aggressively expanding in this space generating 30% ROCE and EBITDA margins in 2x of turnovers. Not exactly in the insoluble Sulphur space, but other rubber chemicals.

Anurag Jain: Yes, they are expanding and as Akshat discussed earlier, we are also evaluating certain proposals in different fields.

Shashank Kanodia: Hasn't the process been a little bit slow because it has been almost 6 quarters we have been evaluating projects ? i

Anurag Jain: I agree it has been a little slow. We have pursued certain areas. However, it was not found suitable and sometimes it happens you spend some time on a certain proposal and then it eventually does not work out.

Akshat Goenka: The process will be slow because we are not going to make any kind of hasty decision. Only when something matches all the criteria, are we going to go ahead and we are not going to go ahead just because there is some sort of a deadline that we have to move.

Shashank Kanodia: You initially had some experience for manufacturing carbon black in the past. So is it something which we are looking into again, given that now it has become a remunerative process?

Akshat Goenka: No, carbon black is not in our horizon.

Shashank Kanodia: On the DTL(deferred tax liability) front , can you please help us understand the logic for creating this? But why there is a need to create this given that we are a MAT paying company? **Shashank Kanodia:**

Anurag Jain: The provision of deferred tax (DTL) has nothing to do with MAT. It is a requirement of the accounting standards. So whether we are MAT or not, our deferred tax provision has to be made.

Shashank Kanodia: But we never used to make it before right?

Anurag Jain: No, it was always there. The amount will always be more when there is a capitalization happening. So what has happened is that there was a capitalization last year and for which, deferred tax provision for the investment allowance and whatever the additional depreciation we got was made in the end of the year. So for the 9 months the deferred tax provision was around Rs 1.5 crores, for the whole of the year it was about Rs 8 crores. So that is what we are saying that by the time the year ends, if you look at the deferred tax provision, it would be less than the last year, though obviously the current tax would go up, but deferred tax provision would come down from Rs 8 crores last year to Rs 6.5-7 crores by March'18.

Shashank Kanodia: So are we still remaining a MAT being company on cash out basis right?

Anurag Jain: On cash out basis, we are MAT paying company**.**

Moderator: Thank you. We will take the next question from the line of Brij Shah, an Individual Investor.

Brij Shah: Just couple of questions. We saw good growth of around 21% in terms of revenue this quarter. So was it due to the volumes or due to the price hike?

Anurag Jain: Mainly due to volumes.

Brij Shah: And what is our volume growth in domestic industry and export industry?

Anurag Jain: We have got good growth in both domestic and export, but in quantitative terms, the growth is more in export, but in percentage terms, it is more in domestic.

Brij Shah: On our contracts side, in terms of volume as well as in terms of price whether they are renewed annually or quarterly?

Anurag Jain: So contracts are long-term, but price revision would happen. So for example, quantities are done normally on an annual basis and price revision would happen either on a quarterly or a 6-monthly basis depending on the contracts that we have on different parties.

Brij Shah: What would be the capacity utilization currently for the new plant in terms of percentage

Anurag Jain: It is running on optimum capacity now. The demand is there. We do not give percentages. When we say optimum, that means that whatever is the best way to run the plant, it is running on that. We are not running low on capacities for want of orders

Brij Shah: ?

Anurag Jain: ,

Brij Shah: What percentage of our sales goes to North America and China?

Anurag Jain: No, sorry I cannot disclose that percentage.

Moderator: Thank you. The next question is from the line of Kashyap Javeri from Emkay Global.

Kashyap Javeri: When is the Phase-II of capacity expansion 5,500 MTPA, supposed to come on stream ?

Anurag Jain: It is supposed to come on stream in Q2 of 2018-19.

Kashyap Javeri: Earlier we had a discussion on savings on fuel and power costs because of steam utilization. So any more benefits yet to come out of that even if I look at this quarter seemingly or despite growth in volume, power cost seems to remain more or less flattish. So any more benefits coming out of that?

Anurag Jain: No, so there are two things. As far as quantity is concerned, we do not see any benefits coming out further except for the fact that there would be a slight benefit in terms of efficiencies when Phase-IV comes up, but otherwise no, we do not see any benefit as such.

Moderator: Thank you. The next question is from the line of Sachin B, an individual investor.

Sachin B: , In the last quarter we had turned positive on the Duncan Engineering business nd as per the last call, we did discuss about an opportunity to sell off this business. So any plan around that,?

And what is the trend of the Raw Material cost ?where were exactly it is moving since crude prices are moving in upward direction, do we have any impact on that and do we have a pricing power to pass on that price to our customer?

Anurag Jain: As far as RM cost is concerned, the Sulphur prices moved up quite appreciably in the last quarter, but they have started cooling down now. As far as coating oil prices are concerned, those were stable, but in current quarter we are seeing some firming in the coating oil prices. So overall per metric tonne cost of raw material should roughly be in the same region as they were in the last quarter until and unless coating oil hots up a little more further in Q1 of 2018-19.

Akshat Goenka: And as far as Duncan Engineering is concerned, as I have said multiple times, the target this year is to have a breakeven and be positive as far as cash flow is concerned and we are on track for that. And once this stabilizes, we will move forward with next steps.

Sachin B: So again, the question is regarding the Raw Materials. Do we have any clause included in contracts if RM cost increases, do we have pricing power to pass on this customer or contract prices are fixed when we entering to the contract?

Ankur Jain: The pricing is on a quarterly or 6-monthly basis. And if there is any appreciable sustainable movement of raw material, then the prices are renegotiated. Or there are some contracts where the pricing of raw material is included as a component of the contract. So we have both the kind of contracts where we will get it automatically and another if there is appreciable sustainable movement in prices, then we do change the price from the next date.

Moderator: Thank you. The next question is from the line of Yogash J, an Individual Investor.

Yogash J: How are we placed in the China and US market. As you mentioned in your opening comments as well that it is doing well. So could you help throw some more light on that front ?

Anurag Jain: So China and US are the two biggest markets for insoluble Sulphur and we are now placed well there. We have already started dispatching good quantities in China and also in US. And I think by the time our fourth phase comes, appreciable amount of the new quantities would go to these two areas.

Yogash J: So is it safe to assume that this quarter's volume growth that we see is more from the export to China and US than domestic? e. Is that understanding o correct?

Anurag Jain: This quarter, there is a growth and it includes growth on account of domestic where we have done very well as well as China. China and America if you put both together, then growth has been there also.

Yogash J: And on more of qualitative basis since we do not share quantitative numbers, so are we satisfied with the kind of traction that we are seeing in US and China and what is your outlook on that. Are we satisfied with what we have achieved so far and are we confident of achieving it further going forward with Phase-II coming in?

Anurag Jain: Yes, we are satisfied with the traction that we have received till now. And as I mentioned earlier, we are quite confident that when the fourth phase comes on line, we will sell off the fourth Phase-In line with the projected ramp up of the capacities.

Yogash J: On the tax front, I think this year overall we have posted a higher effective tax rate. So what kind of number should we work around going forward?

Anurag Jain: So, you have the quarterly number with you as well as the 9-month number with you?

Yogash J: Yes

Anurag Jain: That is a very good indication I would not like to comment on what is going to be the profit at the end of the year.

Yogash J: It is a fair assumption that we can work around these numbers going forward right now because it is moved up if I compare with FY17?

Anurag Jain: Yes, but as I pointed out earlier, there are two components of tax. One is the deferred tax. Deferred tax in fact for the whole year is going to be less than last year. It is only in the 9 months that it is showing excess deferred tax because last year for the whole year, the deferred tax figure was nearly Rs.8 crores and this time it should be about Rs 6.5 - 7 crores.

Anurag Jain: So by the end of the year, deferred tax provision should be less than last year a little bit. As far as current tax is concerned, yes, the current tax is going to be higher than last year because of two reasons. One is profitability and the other is that this year the provisioning of tax would be at a rate which is higher than MAT. Though the cash outflow will be on MAT basis**..**

Moderator: Thank you. The next question is from the line of Amod Joshi from SPA Securities..

Amod Joshi: Sir, as we can see this situation in China regarding this pollution norms, it is now becoming strict. So just wanted to understand how the scenario in India is for the chemical industry. Are we as strict as them or are we better than them in this scenario or are we still lagging behind them?

Anurag Jain: So if I talk about the organized industry, we are much ahead of China as of present and for an industry like Oriental Carbon, I think we are on global standards. Our plants are approved by major tyre companies in the world on the parameters of EHS as well and we have got ISO 14,000 and OSHA Certification. So we are on a global standard.

Amod Joshi: And with this increasing capacity, are we also increasing the capacity to treat the effluents or the pollution creating chemicals which are coming out from the plant or how does it work ?

Anurag Jain: There is no substantial effluent that we have in the plant and we do not have any pollution creating chemicals.

Moderator: Thank you. We take the next question from the line of Bobby Jayram from Falcon Investments.

Bobby Jayram: The crude has been on a continual upfront, have you seen any upfront in insoluble Sulphur prices?

Anurag Jain: So as far as crude is concerned, I commented a little while back, though crude is up, Sulphur is going down. It had gone up quite a lot in the months of November and October. It is coming down; however, the coating oil prices have started firming up now. So the impact as far as my cost is concerned will be on two areas. One is the coating oil and other on fuel.

Bobby Jayram: My question is on insoluble Sulphur, your final product?

Anurag Jain: So insoluble Sulphur if this thing remains, so whenever we renegotiate the prices, we will take all this into account.

Bobby Jayram: Internationally are the prices adjusted to the crude oil increase or are they pretty much the same they were on an average?

Anurag Jain: The prices do not move on a daily basis for all of us whether it is Eastman or us. The pricing would adjust on a quarterly or a 6-monthly basis. So the first indication would be in the first of April or the first of July.

Bobby Jayram: Right, so there is no internationally quoted price for this as such?

Anurag Jain: No, there is no international quoted price at all because there are two manufacturers. It is not a thing which is quoted or even reported anywhere.

Moderator: Thank you. Ladies and gentlemen, that was the last question. I now hand the conference over to the management for his closing comments.

Akshat Goenka: Thank you everyone for joining on the call. I hope we have been able to address all your queries. For any further information, kindly get in touch with Strategic Growth Advisors, IR Investor Relations Advisor or with any of the official team. Thank you once again.

Moderator: Thank you. Ladies and gentlemen, with that we conclude today's conference. Thank you for joining us and you may now disconnect your lines. Thank you.