



“Oriental Carbon & Chemicals Q4 FY17 Earnings Conference Call”

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Moderator:

Ladies and gentlemen good day and welcome to the FY17 Earnings Conference Call of Oriental Carbon & Chemicals Limited. This conference call may contain forward-looking statements about the company which are based on the beliefs, opinions and expectations of the company as on date of this call. These statements are not the guarantees 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 to Mr. Akshat Goenka-Promoter and Joint Managing Director of OCC Limited. Thank you and over to you sir.

Akshat Goenka:

Good morning and a very warm welcome to everyone. Along with me I have Mr. Anurag Jain-CFO and SGA, our Investor Relations Advisor. I hope you have received the result and investor presentation by now, so those who have not you can view them on our website.

FY17 was a good year for our company. As mentioned in the last earnings call, we are delighted that we commenced the production of our first phase of capacity expansion of 5500 metric tons per annum ahead of its scheduled in Mundra. We have started dispatches from the new plant as well, which has helped us increase our volumes for the year and this last quarter. Having had a successful year, we are happy to announce that our company declared a total dividend of Rs. 10 per equity share for FY17 that is 100% of the face value. The work on second phase of expansion at Mundra has started and the plant is expected to be commissioned in Q2 FY19.

The growth trajectory post demonetization in auto sales has normalized as can be seen in the numbers of April '17. We feel that all the new regulations and new emission norms that are coming up shall have no impact on the longer run as far as the consumption of insoluble sulphur and tyres is concerned. The demand of insoluble sulphur in India has increased but is still lower as compared to other significant economies and has headroom and opportunity for growth. We expect the demand pick up in both medium and heavy commercial vehicle segment driven by better tyre quality, expenditure on infrastructure and manufacturing and an overall economic upturn.

The company is expected to grow in all markets especially in China and North America. Going forward we have been continuously strengthening our ties with all our customers. Now I would like to hand over the line to Mr. Anurag Jain to update you on the operational performance of the company.

Anurag Jain:

Thanks Akshat. I will take you all through the financials of the company. Net revenue for the Q4 FY17 is Rs. 82 crores compared to Rs. 69 crores in Q3 FY16. Net revenue for the year was at Rs. 297 crores vis-à-vis Rs. 275 crores for the same period last year. We have seen increase in volumes which has helped us increase our top line by 18% this quarter on account of commissioning of new line and 8% for the full-year. For Q4 FY17 EBITDA stood at Rs. 26 crores which includes other income, EBITDA for the full-year stood at Rs. 94 crores. EBITDA margins for the quarter was 31.7% and for the full year were 31.6%. Profit after tax for Q4 was Rs. 9.3 crores, for the full year PAT improved marginally to Rs. 53.4 crores. This was mainly because of additional provision of deferred tax of about Rs. 7.8 crores on account of



commissioning of the new capacities. PAT margins for the year stood at 18%. With this I would like to open the floor for question and answers.

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

Shashank Kanodia: If you can throw some light on the GST rate, so our product has been classified at an 18% category, so how does it affect us and what was the tax incidence prior?

Anurag Jain: As far as GST is concerned there will not be any negative effect on us because we are basically a B2B company and everything would be VATable. Earlier the tax incidence for interstate sales was 2% CST and 12.5% excise while selling and the same while purchasing, so there would be an increase of 4% on tax on our domestic sales but that will also be VATable, so in fact CST which was not VATable earlier would now become VATable.

Shashank Kanodia: But effective excise duty paid by you is just close to 4.5%-5% which I believe is because of high amount of exports, right?

Anurag Jain: That is right.

Shashank Kanodia: So net effect would be neutral towards whatever increase in tax rate is going to be passable to our customers?

Anurag Jain: It will be passable because it will be VATable. So it will be VATable when I'm selling and also when I am buying. So whatever tax rate is there it will become fully VATable at my end also. There will be a complete pass through.

Shashank Kanodia: The capacity utilization levels of the Phase-1 for Q4 FY17 so have we cross 60%-65% utilization levels on the Phase-1 in Q4?

Anurag Jain: The new capacities have been utilized at a good level for the last quarter. We do not however disclose the exact numbers.

Shashank Kanodia: Just for the new phase, if you can throw some light?

Anurag Jain: That is what I'm saying; they have been utilized at a very good level.

Shashank Kanodia: This quarterly you have reported some deferred tax, right, so can you just explain us what's the logic behind that?

Anurag Jain: There is no logic, but a provision of law. This year there was a massive capitalization on account of the new line and obviously there is a difference between the income tax rate of depreciation and the company's act rate of depreciation. And whatever that difference is that has to be provided as deferred tax.

Shashank Kanodia: But normally company don't report this deferred tax every time they commission new facility.

Anurag Jain: No, it is a choice. Whether you report it separately or you club it with the overall tax. We choose to report it separately, so that you can get an idea that this is not an actual expenditure. It's a provision on account of expansion and since it was a significant amount, we have chosen to disclose it separately.

Shashank Kanodia: Will that incidence repeat itself in next financial year?

Anurag Jain: Yes, it should repeat. Not to this extent but it would repeat itself because the income tax depreciation was applicable only for six months in the current year and not for the whole year.

Shashank Kanodia: So for FY18 what is the tax rate that you're guiding to us?



- Anurag Jain:** The exact tax rate I cannot comment. But as we have been saying, the actual payout of tax would remain on MAT.
- Shashank Kanodia:** We have been always guided that there are three players in the global market, Eastern Chemicals, Shikoku and us. So what about this new player called Sunshine Chemicals, is it serious competition to us which is close to 20,000 tonnes per annum?
- Anurag Jain:** There is not only one player, there are many players in China, so Sunshine is one of them.
- Shashank Kanodia:** Is it the quality that the manufacturer is comparable to what we manufacture?
- Anurag Jain:** What we have been saying is that there are three manufacturers, who have a quality which is acceptable worldwide. Others have not yet reached that stage.
- Moderator:** We will take the next question from the line of Abhisar Jain from Centrum Broking. Please go ahead
- Abhisar Jain:** My question is related to the other two global competitors because their expansions are also supposedly coming on stream in CY17, so just want to know from you whether those expansions have also hit the market and if yes, is there the demand supply still quite balanced or are you seeing some chances of oversupply in the market because all the three new capacities are supposedly coming at once effectively?
- Anurag Jain:** I think Abhisar this was discussed earlier also in con-call. Even with the new capacities the gap between demand and supply is not very huge, so we may be talking about demand in the 80% -85% vis-à-vis capacity. As far as whether they have actually come online or not we have no way of confirming that positively because these events are not announced by these companies.
- Abhisar Jain:** If you could also throw some light on your subsidiary Duncan Engineering. I have looked that the Q4 financials and obviously now it's a downsized operation but what do we expect for FY 18? As of now it seems that still we are not able to clock positive EBITDA and PAT there as of Q4.
- Akshat Goenka:** Abhisar you have to look at the Q4 numbers in two ways. There are lot of one-time provisionings that have also been taken in the Q4 numbers. But if you want to see some signs of improvement if you look at the turnover in Q4 vis-à-vis Q3 and you see the turnover has gone up. So basically the reason the employee benefit costs are up and the reason other expenses are up is more because of certain one-time cleanups that were required to be done. But on a standalone Q4 basis we did okay comparatively speaking. In my opinion this company has hit its rock bottom and is now climbing its way up.
- Abhisar Jain:** So if I were to understand this correctly that obviously in the top line we would have stability or some improvement from the current exit levels of Q4 and some one-offs which were there in staff and other expenses would now go away in FY 18?
- Akshat Goenka:** Let me put it in another way that we have hit the bottom, now we are on the way up. Q4 was also on the way up; Q4 was not at the bottom because if you look at the top line it's significantly higher than the average of the other three quarters. And this year we definitely expect to make positive EBITDA and positive cash flow.
- Abhisar Jain:** Could you quantify the one-off if possible in other expense and staff cost combined?
- Akshat Goenka:** As far as employee benefits expenses are concerned, there were certain capitalizations that were happening which we realized should be more revenue in nature so those things were added there. And other expenses pertain to old liabilities or things like C-forms bad debts and inventories - and obviously some legal expenses that are due to the ongoing legal affair



Abhisar Jain: Any number you can put all this?

Akshat Goenka: No I don't want to put numbers. I will give you one clue; you can take the costs of Q3 and the turnover of Q4 to get an idea.

Abhisar Jain: On the debtor side just lastly I understand the volume pickup in Q4 from the new line which might still be as such not received in terms of payment but as such just want to be sure that there is no trend of some sustainable increase in debtor days, right. We will be more towards a long-term average even for the new capacity that we are selling.

Anurag Jain: That is right; it should be on that basis only.

Abhisar Jain: So the spike up of almost 20 days which we are seeing on just a margin number is more or less temporary in nature, right?

Anurag Jain: Yes.

Moderator: We will take the next question from the line of Bobby Jayram from Falcon Investments. Please go ahead.

Bobby Jayram: What's percent of your new capacity is used to service your Indian customers?

Anurag Jain: The Indian customers constitute about one third of our total capacity earlier without the new capacity. And with the new capacity coming in about maybe 25%, so that can be serviced by our existing capacities only. In other words, the new capacities being added are basically helping us to increase our export sales.

Bobby Jayram: We are still hearing from some of the tyre manufacturers in India about the Chinese TBR imports, how is that impacting your demand scenario?

Anurag Jain: We are still meeting our projected demand as we have been saying that we should grow in double digits in India and we are seeing that growth. We have seen it last year and we are seeing it currently also. So as far as insoluble sulphur is concerned we cannot see any impact on that.

Bobby Jayram: Would your Phase-2 expansion program on track for FY 18?

Anurag Jain: Yes it is on track.

Akshat Goenka: It's not supposed to come on FY18; it will come in FY 19.

Bobby Jayram: So what month can you pin point or is it early?

Akshat Goenka: Quarter 2 FY19.

Bobby Jayram: This is the same forecast you had issued last quarter?

Anurag Jain: Yes it's the same forecast and we are on time for that.

Moderator: We will take the next question from the line of Ayush Mittal from Mittal & Co. Please go ahead.

Ayush Mittal: Just a bit on the inventory side I think there has been some improvement on that is that one-off or sustainable?

Anurag Jain: The improvement in inventory is sustainable maybe not to the extent that it's come down, but obviously, it will not go back to the levels it was earlier hopefully.

Ayush Mittal: And as you have done the expansion and now it is operational, what kind of benefit you must be seeing on the savings of logistic cost and all those things that you have mentioned, anything you like to pinpoint or mention?

Anurag Jain: Obviously there would be saving as far as fixed expenditure per metric ton is concerned. We would see savings there. There would be certain savings on some semi-variable costs so



variable costs like power and fuel. And logistics obviously there is not going to be any perceptible saving because whatever has to be exported has to be exported irrespective of whether it is two lines or three lines. So we do not see any saving in logistics per se because of expansion. But on fixed cost and variable cost in terms of power and fuel yes we should see some saving.

Ayush Mittal: On this tax rate I'm still not very clear like at Mundra you would still be getting the tax benefit wherein we would be paying I think 50% tax?

Anurag Jain: That is right; there is the 50% tax rebate.

Ayush Mittal: As that has to continue for a few more years, shouldn't our overall tax rate be lesser closer to 23%-25%?

Anurag Jain: It is, I think that is what we are looking at.

Akshat Goenka: Our overall tax rate is actually less than 20%.

Anurag Jain: You take the deferred tax separately.

Ayush Mittal: That is what if we see the overall tax that has been provided that is coming around 29% or 30% I think.

Anurag Jain: But that is because you are looking at deferred tax provision. That is what we are saying that look at deferred tax provision separately and then look at tax. Deferred tax provision is a provision in the balance sheet. So if you look at two figures, one is tax provision and one is deferred tax provision. So the tax provision is Rs. 12.23 crores whereas deferred tax provision is Rs. 7.91 crores

Akshat Goenka: Let me clarify for everybody, this is not something that we are doing willingly or this is not something that is our interpretation. This is something that is statutorily required and that's what we are following. It's not optional for us to do this provision. And all companies would be doing it across the board whoever has expanded.

Ayush Mittal: If we see the tax rate last year, overall provision, it used to be 20% or maybe a bit more around that number.

Anurag Jain: Ayush the tax last year was 12.63 crores out of which actual tax was 12.61 crores, right. And that was on the PBT of 59.6 crores. This year on a PBT of 70 crores, it is 12.23 crores.

Ayush Mittal: I'm talking about overall tax which has been provided.

Anurag Jain: We have told you that the 7.91 crores is a deferred tax provision. That is why we have shown it separately so that you can make sense out of the numbers.

Moderator: We will take the next question is from the line of Srinath Sridhar from ICICI Securities. Please go ahead.

Srinath Sridhar: On the CAPEX front we have spent close to 100 crores this year, so for Phase-2 how much are we expecting?

Anurag Jain: Phase-2 should be around 62 crores.

Srinath Sridhar: And apart from this our usual maintenance CAPEX?

Anurag Jain: Yes.

Moderator: We will take the next question from the line of Ashish Parekh, an individual investor. Please go ahead.

Ashish Parekh: During this quarter we saw revenue growth of around 18%, so this will be primarily due to increase in volumes because of our new capacities or there has been any price hike?



Anurag Jain: No, it's primarily because of the new capacities and our ability to get more volumes to sell.

Ashish Parekh: So these new volumes, we have been able to sell them to our existing customers or have we increased our customer base?

Anurag Jain: Mix of both.

Ashish Parekh: GP margins are 80% for this quarter. Will we be able to maintain this going forward?

Anurag Jain: That is a very difficult thing to say because when you are looking at GP margin then you have to also look at change in inventories of finished goods, purchase of stock in trade and all. So when you say GP margin I'm assuming that you're talking about after cost of raw material which has been around 24%-25% earlier. If you look at last year it was 25% and even here when you add all this it will come to around that 23%-25%.

Moderator: We will take the next question from the line of Jigar Jani from Edelweiss. Please go ahead.

Jigar Jani: Would it be possible to share the sales in metric ton of insoluble sulphur for FY16 and 17?

Anurag Jain: No, we don't share the volume numbers due to certain competition

Jigar Jani: What would be generally the price realizations that you would be selling the product at?

Anurag Jain: No, we don't disclose that either. You will have to appreciate that none of our competitors do that and we don't want to be at a disadvantageous position with them by disclosing sensitive information.

Jigar Jani: What is the volume expectations do we expect the Phase-I ramp up to hit like 80% utilization in FY18?

Anurag Jain: FY18 should see optimum utilization of capacities from the expansion also.

Jigar Jani: So by optimum about 80% approximately?

Anurag Jain: Yeah, so 80% to 85%.

Moderator: We will take the next question from the line of Abhisar Jain from Centrum Broking. Please go ahead.

Abhisar Jain: Just wanted to get a sense on the raw material price movements, are you seeing any change in those movements in both the raw materials for us - sulfur as well as naphthenic oil in a major way?

Anurag Jain: They have been stable for the last six odd months with slight movements. I would say that they fell dramatically last year in the last quarter and then they fell a little more but now they are stable.

Abhisar Jain: So that portion is largely stable, right?

Anurag Jain: Yeah.

Abhisar Jain: Also the new volumes are going in both the geographies, US and China or is it that it's largely been the North American markets?

Anurag Jain: No, it's going everywhere. We cannot disclose the exact quantities, but the new volumes are servicing the increased demand of our existing customers as well as new geographies.

Moderator: We will take the next question is from the line of Shashank Kanodia from ICICI Securities. Please go ahead.

Shashank Kanodia: Can you share the power and fuel cost for this quarter, Q4 FY17? You used to provide this number previously I think it has been clubbed under the other expenses for his quarter.

Anurag Jain: The power and fuel cost for the whole year has been Rs. 36 crores

Shashank Kanodia: So roughly 11 crores for this quarter, right?



- Anurag Jain:** 36 crores for the whole year and about 10.2 crores for the quarter.
- Shashank Kanodia:** You have been guiding us there would be savings in terms of fixed cost as well as semi-variable cost given it's a Brownfield expansion for us. So would like to put any number in terms of basis points improvement in EBITDA margins like 150 or 200 basis points?
- Anurag Jain:** No, we don't like to give. We have been maintaining that EBITDA margins guideline has been in the late 20s and one or two basis points can always change in terms of exchange rate fluctuation or so many other variables, so we can not give more exact number.
- Shashank Kanodia:** This year our payout is roughly around 20%-odd, dividend of Rs. 10 on an EPS of Rs. 50. So we will maintain that same payout going forward?
- Anurag Jain:** We had stated earlier also that our intention is to maintain our payout of about 20%.
- Moderator:** We will take the next question from the line of Ashish Parekh, an individual investor. Please go ahead.
- Ashish Parekh:** I had a couple of back up questions. First one being while entering newer geographies have we been subject to any pricing pressure from China?
- Anurag Jain:** No.
- Ashish Parekh:** So we have been able to sell at the normal prices only?
- Anurag Jain:** Obviously. So when we enter newer geographies obviously we have to keep in mind what are the prevailing prices there and accordingly we enter there. So there is no other external pressure
- Ashish Parekh:** Another question being we have increased our global market share in last two years, so what would be our strategy to increase this in the coming years?
- Anurag Jain:** The same strategy that we have been following for the last 10 years. What we do is we will take a little bit more of the growth than our market share and we will keep growing accordingly.
- Ashish Parekh:** How much can we reach in the next two years?
- Akshat Goenka:** In the next two years we will basically be selling out all the capacities that has just come on stream, so that is what will give the growth.
- Moderator:** We have the next question from the line of Jigar Jani from Edelweiss. Please go ahead.
- Jigar Jani:** Regarding our new CAPEX of 63 crores for Phase-2, we are expecting 2:1 debt-to-equity funding for that CAPEX, so have we tied up debt and what is the rate at which we have tied up that debt?
- Anurag Jain:** We are still in the process of tying up. You would appreciate that once the year ends all the banks want to have the numbers for the year before finalizing the debt tie-up. We have informally tied it up but it needs to be formalized and that should happen in the month of June.
- Jigar Jani:** You just highlighted that over the next two years your plan would be just to utilize your existing Phase-1 and Phase-2 capacities and sell those. But you would be generating significant operating cash flows over the next two years considering all the capacities you would be ramping up, so any plans of doing more distribution for increasing the dividend payout?
- Anurag Jain:** Currently we are distributing dividend at 20% and we have cash and we are looking for opportunities and let us see how it unfolds.
- Jigar Jani:** So you are looking at inorganic opportunities?



Anurag Jain: We are looking at all the opportunities which are similar to the kind of business that we have today, in terms of specialization, margins and other things and maybe some synergic opportunities also.

Akshat Goenka: Till now this has been done in a very informal way; nothing is imminent as such. And whenever there is any concrete information we will definitely be sharing it. Secondly if we go into anything rest assured that it will be along the same financial lines as our current business model. We will not be compromising on those principles.

Jigar Jani: There are no plans to divest of your other subsidiary which is the pneumatic valves subsidiary?

Akshat Goenka: Who will buy a loss making company; we have to first make it profitable. Let us turn it around and then we will see how it goes from there.

Moderator: We will take the next question from the line of Mrunal Savla from Anand Rathi. Please go ahead.

Mrunal Savla: This onetime provisioning you have mentioned about the employee expense and other expense

Anurag Jain: It is in the subsidiary, not in the main company.

Mrunal Savla: Going forward EBITDA margin if this one-time expense is not there, so what is the company's vision of looking at EBITDA?

Akshat Goenka: Which company you are talking about right now?

Anurag Jain: Onetime provision when it was being discussed it was for Duncan Engineering and not for Oriental Carbon.

Mrunal Savla: So 30% EBITDA margin can we take that to 32%?

Anurag Jain: We have always been given the guidance that it should be in the late 20's and we will never commit to something more than this though as you can see that we have been able to maintain the margins around 30% for the last three years. But if you are asking for a guidance we can't give you.

Moderator: We will take the next question from the line of Kamalkant Sahu from IndiaNivesh. Please go ahead.

Kamalkant Sahu: I would like to know about the Phase-2 expansion plan in more detail like I want to know about the CAPEX and the capacity.

Anurag Jain: The CAPEX is going to be 62 crores and the capacity is going to be 5500 metric tons per annum.

Kamalkant Sahu: In Phase-1 also it was 5500, right?

Anurag Jain: Yes.

Moderator: Thank you. Ladies and gentlemen as there are no further questions from the participants I would now like to hand the conference over to the management for closing comments.

Akshat Goenka: I would like to thank everybody 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 our Investor Relations Advisors, SGA or with anybody from the OCCL team. Thank you once again.

Moderator: Thank you very much. Ladies and gentlemen on behalf of Oriental Carbon & Chemicals Limited that concludes this conference. Thank you for joining us and you may now disconnect your lines.