"Oriental Carbon & Chemicals Limited Q4 FY'18 Earnings Conference Call"

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MANAGEMENT: **MR. AKSHAT GOENKA- PROMOTER AND JOINT MANAGING DIRECTOR, OCCL**
MR. ANURAG JAIN – CFO, OCCL

Moderator: Ladies and Gentlemen, Good day and welcome to Oriental Carbon & Chemicals Limited Q4 FY18 Earnings Conference Call. 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 risk and uncertainties that are difficult to predict.

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 the operator by pressing "*" then "0" on your touchtone phone. Please note that this conference is being recorded.

I now hand the conference over Mr. Akshat Goenka Promoter and Joint Managing Director of OCCL Limited. Thank you and over to you sir.

Akshat Goenka: Good afternoon and a very warm welcome to everyone. Along with me I have Mr. Anurag Jain a CFO and SGA our Investor Relation Advisors. I hope you have received our results and investor presentation by now. Those who are not you can use them on our website. FY18 has been a year of consolidation at OCCL. We were able to operationalize our new capacity through which we have been able to cater to new markets globally. We have also been able to cater to the increased domestic demand. I am especially pleased to announce that our new line at Mundra has already started trial runs. The commissioning is expected soon, and we shall inform the stock exchanges once that happens.

We are also expecting decent saving in our total project cost. The Indian auto industry on the cusp of transformation moving from BS4 to BS6 regulations and later on to electric vehicles. The CV segment recorded a milestone year with the growth of 20% from last year with medium and heavy vehicles eclipsing in the previous peak posted in FY12. The strong performance was on the back of the introduction of GST which resulted in free movements of goods, government push towards infrastructure development and stricter implementation of the ban on overloading of trucks.

Braving out the adverse effect of growing tyre imports from China, the tyre majors have embarked on a massive capacity expansion in India as well as abroad to meet the growing demand. Having reached more than 80% capacity utilization marks, tyre makers are investing approximately Rs. 35,000 crores in Greenfield and Brownfield project to expand capacity. They also anticipate double-digit growth from FY19. All these factors have led to the growth in the tyre industry which has led to increase sale of insoluble Sulphur. Another driver is the new compound being designed for the ultra-high performance tyres where requirement of insoluble Sulphur will be higher.

We continue to make inroads in China and North America and we expect these markets to propel us going forward. We have been continuously strengthening our ties with all our customers. I am also very pleased to inform that our subsidiary Duncan Engineering has declared a positive PAT for the first time since we took it over. Cash flows have also improved tremendously and our subsidiary has actually repaid one and half crore rupees loan back to OCCL. We expect the subsidiary to improve further this year.

Now I would like to hand the line over to Mr. Anurag Jain to update you on the operational performance of the company.

Anurag Jain: Thank you Akshat I will take you all through the financials of the company. The company has adopted IndAS from FY18 and accordingly the results of FY18 and previous year FY17 as well as FY16 has been prepared as per laid down principles in IndAS. Revenues for Q4 FY18 is Rs. 91 crores compared to Rs. 84 crores in Q4 FY17 a growth of 9%. Revenue for FY`18 is Rs. 334 crores compared to Rs. 304 crores in FY17 a growth of 10%. Consolidated revenue for FY18 is Rs. 374 crores compared to Rs. 338 crores in FY17 a growth of 10%.

During the year we have seen volumes increase as we have been able to cater to newer geographies. For Q4 FY18 EBITDA stood at Rs. 26 crores for FY18 EBITDA stood at Rs. 104 crores a growth of 10% from previous year. EBITDA margins for FY18 stood at 31.2%. Consolidated EBITDA for FY18 is Rs. 106.7 crores as compared to Rs. 94.59 crores a growth of 10,000. Interest cost was higher in this year due to commissioning of the new capacity last year as the interest cost till then was capitalized and now transfer to P&L. Profit after tax of Q4 FY18 was up 47% to Rs. 15 crores and for FY18 up 5% to Rs. 57 crores. PAT margins for the quarter and FY18 stood at 16% and 17% respectively. With this, I would like to open the floor for question and answers.

Moderator: Thank you, Ladies and Gentlemen we will now begin the question and answer session. The first question is from the line of Abhisar Jain from Centrum Broking. Please go ahead.

Abhisar Jain: Sir, my question is related to the standalone operations, so just wanted to know that the Mundra first line is now running at full optimum utilizations and there was a minor hiccups in the early part of this year, so have you fully recovered from that?

Anurag Jain: We are on the way to recovering from that. We have not fully recovered from that and as a result we are not at 100% utilization. We are gradually ramping it back up to that level. Whatever hiccups we had suffered those have been overcome, but when the ramp ups take a little bit of time back.

Abhisar Jain: Is it possible for you to throw some more light on the exact nature of that hiccups if you can please?

Anurag Jain: As we had outlined in the previous call as well, this was more related to teething problems from some of the new customers.

Abhisar Jain: In terms of the again on the standalone top line growth which was around 10% for FY18, is it safe to assume that it was largely through volumes and realization would have been marginally negative only on a year-on-year basis?

Anurag Jain: So the growth is mainly on volumes. Realization has been very marginally negative because of the exchange unit otherwise it has been nearly the same.

Abhisar Jain: Effectively realization also in dollars terms would have been flattish of sorts?

Anurag Jain: Yes, it has been nearly the same.

Abhisar Jain: In terms of the volumes again the breakup between domestic and exports we would have realized more percentage growth in terms of volume in domestic right?

Anurag Jain: That is right because as we have been pointing out every time that there is a domestic growth in two digits. So therefore, more growth comes from the domestic markets in terms of percentages individually.

Abhisar Jain: And export growth again obviously dominated largely by the new geography penetration of North America and China?

Akshat Goenka: Also due to increased allocation from the existing customer both has played a role.

Abhisar Jain: But exports growth overall would have been single digit somewhere not the double digit?

Anurag Jain: Yes, it has to be single digit it cannot be double digit.

Abhisar Jain: Just one more point on the overall other expenses and the benefit of operating leverage that we have been forecasting from the new line I understand sir as we have the other line coming in and we start running at more volumes and the actual benefits would be seen, but in FY18 we were not able to see much of those benefits because our other expenses went up on year-on-year basis more than our top line growth, so could you give some more color there exactly how the cost are shaping up and where can be see the benefits going forward?

Anurag Jain: There has been benefits in operational costs in terms of power and fuel once this line has been commissioned. The major reason why the cost in the balance sheet is more for FY18 is because of reinstatement of forward covers on 31st March as you would know that we take 6 months forward covers and by 31st March Rupee had started appreciating so we had to book a loss on mark-to-market valuation of the open covers which was around Rs. 2 crores

Abhisar Jain: Rs. 2 crores okay.

Anurag Jain: So this is a provision obviously it is only a provision which has to be provided. So that is one of the major reasons why you see a bump up in the overall expenses.

Abhisar Jain: Any other cost would have also seen sir some more inflation and not allowed the other expense to come down as such because power and fuel you are saying was lower as such. Any other head sir also where in you would like to.

Anurag Jain: Little bit of freight outward.

Abhisar Jain: Just one last one from my end Akshat sir mentioned in the opening remarks that we would be saving on the project cost also, so can we indicate sir what could be that saving in the CAPEX number and then your CAPEX outlay for FY19?

Akshat Goenka: We will indicate the saving very soon once it gets crystallized, but if I am mentioning that you should assume it will be a good saving.

Abhisar Jain: The CAPEX number for FY19 Anurag sir if you can mention that approximate what could be the CAPEX now because since expansions will be through so where CAPEX should be falling.

Anurag Jain: Other than expansion it will be mostly normal CAPEX or the maintenance capex

Abhisar Jain: Which is sir close to Rs. 20 crore range.

Anurag Jain: No it will be much less, in single digit.

Abhisar Jain: Sir both plants together.

Anurag Jain: Yes, everything together.

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

Shashank Kanodia: Sir you mentioned in the opening remark that this robust tyre demand growth which is resulting to good demand growth for insoluble Sulphur as well? Has that is not been increasing premium for a product or better credit term with our customer?

Anurag Jain: It is not impacted the prices of the terms and I do not see the terms being impacted by demand supply situation either. If demand supply situation changes then it is the prices that moves up and down credit terms generally do not fluctuate.

Shashank Kanodia: Secondly in the recent past the crude prices has shot up right, so does it impact in terms of Sulphur prices increase and how are we mitigating that risk?

Anurag Jain: Sulphur prices has no correlation with crude prices first of all because it a by product of the refinery. So it has its own life. Sulphur prices did increase in the first quarter, but now they have stabilized. So there was a point in time when the crude prices were going on and Sulphur prices actually went down by Rs 500 when they increase but now they are stabilized. We do not see much impact in Sulphur prices in correlation with the crude prices if that is your question.

Shashank Kanodia: Secondly, but are we hedged in terms of our pricing contracts include the pass on for Sulphur price volatility or we have to observe the impact as a positive or negative way?

Anurag Jain: See the Sulphur prices as a percentage of overall sale is quite less and we have been stating that in some cases we have formula-based pricing where it will be passed on whenever the next formula price revision land mark comes and in other cases the passing on happens only when there is a substantial increase in prices for a sustained term then we pass it.

Shashank Kanodia: Thirdly on the macroeconomic front you may mentioned that tyre companies are growing double digit, so do you see this mode of structural play the revival in MSEB segment or it is going to be a short-term play?

Anurag Jain: It is a structural play as far as tyre company is concerned it is not about MSME segment. It is about the overall position of India in the tyre story of the world so there are two aspects because of which the production of tyre in India would increase. One is because of the consumption in India which is quite healthy. Second, because the imports from China are decreasing and the third is because India is now becoming a hub for exports also worldwide. So these are the three major driving factors which would drive the demand in India for tyres.

Shashank Kanodia: So given all the three triggers are we planning for further expansion or any strategic play post FY21 for us. when we probably will exhaust the phase two of Mundra?

Akshat Goenka: No that is correct. We have started going on the drawing board to chart out our future plans and over the next two to three months we will crystallize exactly how we are going to move ahead.

Shashank Kanodia: It is going to be same product or something different sir?

Akshat Goenka: I thought your question was regarding the same product, so I was answering in that context. As far as different product is concerned that journey is on as it has been on for the last year, year and half and soon as something crystallizes on that front we will inform you.

Moderator: The next question is from the line of Alok Kapadia an Individual Investors. Please go ahead.

Alok Kapadia: I just had two questions one is that what is the kind of capacity which is likely to come on stream globally over the next two years and second related question is that there is a company in China called China Sunsine which is also expanded its capacity for insoluble Sulphur significantly. So besides the top three players that is us, Eastman and there is one more company in Japan does China Sunsine figure in terms of competition?

Akshat Goenka: Let me answer this question in two parts. I will tackle the China Sunsine part second. Firstly, on the basis of the published information we believe Eastman has already or is going to by end of the year come out with 20,000 to 25000 tons in its Malaysian plant. Apart from that we do not have any announced capacity expansion plan from either of our competitors. As far as China Sunsine is concerned we have been in the market making insoluble Sulphur for quite some time. They are from our understanding basically serving the Chinese market. Now recently we have been hearing news as other rubber chemical manufacturer even the small, small insoluble Sulphur manufacturer in China has started shutting down. So China Sunsine expansion could possibly be catered to replace that capacity as China Sunsine is supposed to be an organized player in the Chinese market and not like the other ones who have been forced to shut down.

Alok Kapadia: Sir globally do they compete with us in any significant way then?

Akshat Goenka: No, not to the best of our knowledge.

Moderator: The next question is from the line of Rahul Veera from Elara Capital. Please go ahead.

Rahul Veera: Sir I just wanted to understand in terms of the process, what would the conversion ratio from insoluble Sulphur and from raw material to the final product for us.

Akshat Goenka No we do not answer question on the process please sorry.

Moderator: The next question is from the line of Ankit Kanodia from Smart Sync Services. Please go ahead.

Ankit Kanodia: Most of my questions are answered I just had one query regarding the forward cover, you mentioned that you have to make a provision on 31st March regarding the dollar appreciated against the rupee, so do you make that provision every quarter or on yearly basis?

Anurag Jain: On every quarter it is made depending on the outstanding position on that particular day.

Ankit Kanodia: So is my understanding correct that in the current quarter also since the rupee has depreciated sharply from April till today, so there should be some provision again made in June?

Anurag Jain: It will depend on the rate prevailing on the 30th of June, so we cannot comment now because it is coming back to 67.50 around that way time.

Ankit Kanodia: So every quarter you have to book?

Anurag Jain: You have to provide either an income or an expense depending whether mark-to-market is positive or negative as on the date of the closing of the call.

Ankit Kanodia: Generally, what is your policy of forward cover you take a 6 months cover?

Anurag Jain: Generally, the policy is that we take 75% of our net exposure as 6 months cover

Moderator: The next question is from the line of Ritesh from RB Securities. Please go ahead.

Ritesh: So my question is related to our raw materials, so as we are aware the oil prices basically are on an uptick, so I just wanted to understand how does this oil price rise has impacted us and and are we able to pass it on and if yes then what is the time lag between the pass on. So what is your outlook on the raw material prices will they go up or down or how will they will be?

Anurag Jain: So our two raw material are coating oil and Sulphur. Sulphur though is a refinery by product it has no correlation with the crude prices. The other one is coating oil which again is a refinery product. It does have a correlation though not very direct is a loose correlation it does have a correlation and it tends to go up little bit if the refinery prices remain firm for a significant period of time. Now as far as Sulphur is concerned we think that it is stabilized and as far as coating oil is concerned, looking at the stabilized position of crude prices which appears to have stabilized, we feel that even the coating oil prices should also stabilize.

Ritesh: Suppose if they rise, so are we able to pass it on?

Anurag Jain: As I just said a while back that in some cases it is passed on where we have a formula-based pricing. So it is passed on either ways and in other cases only if there is a significant impact on cost on a sustainable basis then the competitor and all would ask for a price increase.

Ritesh: What is the time lag for that pass on?

Anurag Jain: Normally the price contracts are on a quarterly or a six monthly basis.

Ritesh: So that answers my raw material related questions. Now another one more book keeping questions that is related to our debtor's days, so just wanted to understand what is the debtors' days for domestic and international clients and also is there any pricing difference between domestic and international clients?

Anurag Jain: So there is no significant difference between domestic and international clients and our average debtors days are of 75 days.

Ritesh: 75 days so it is similar for both domestic maintenance?

Anurag Jain: There is no significant difference.

Ritesh: As you said there is no differentiation as such. So next question is related to this are Mundra on a capacity that we expanded, so from when we expect to commercialize and expect to earn revenues out of that a new capacity of 5,500 mt.

Anurag Jain: As Akshat has pointed out that we expect to commercialize it soon and the moment we commercialize it we will inform the stock exchanges and we will inform our investors.

Ritesh: Any ballpark figures for that?

Anurag Jain: What kind of figures are you looking at?

Ritesh: Basically, the time line let say next 3 months, 6 months or something like that?

Anurag Jain: No, we will appreciate that this is an information we don't want to share.

Ritesh: Last two questions from my side? Basically, the situations in China so just wanted to understand are we benefitting from that situations and like what is the outlook from that, do we see any uptick in demand?

Anurag Jain: In China there has been certain insoluble Sulphur manufacturers who are facing the heat in terms of environmental issues and have been forced to close down or to curtail production, so therefore definitely we see that the demand in China should be better in the coming period.

Ritesh: Again, on that Mundra plant are we looking to expand further from the existing 5500 mt capacity or enter any new products or something?

Anurag Jain: The current facility that we have in Mundra is now full with this expansion, and as Akshat has pointed out we are considering what to do after this expansion as far as our current product is concerned and once the plan is crystallized, we will get back to you on that.

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

Shashank Kanodia: Sir what was the cash flow which generated from operations for this year FY18 close to 90-odd crores?

Anurag Jain: Do you have any other question in the meantime.

Shashank Kanodia: We are still a MAT paying company right on a cash basis tax rate for us is 22%?

Anurag Jain: Yes.

Shashank Kanodia: And this is going to be remaining for how many years?

Anurag Jain: For 4, 5 years at least.

Shashank Kanodia: Since we are majorly done with the CAPEX program, so how do you see the debt reduction going forward in the next two years can we see some 50, 60 odd crores of debt repayment given that we have strong cash flow from operations?

Anurag Jain: We will be paying that as per the schedule and if we keep doing, that would not be a significant reduction in debt until and unless we embark on another extension or diversification.

Shashank Kanodia: Sir on a broader sense our presentation mentions that global demand for insoluble Sulphur around 2,64,000 MT as of FY16 and it is going to be 3,40,000 MT by CY 20, so this creates a further room for 76,000 MT. So Eastman you mentioned is expanding 20,000-25,000 MT we are already done with a 11,000 MT. So for the rest of the demand, how do you see the mechanics going?

Anurag Jain: You can very well imagine we will not be sitting quietly and nor will be Eastman.

Shashank Kanodia: What about Shikoku, are they Shikoku are they expanding anything?

Anurag Jain: Yes, they have expanded recently, but they have not announced any expansion plan as of date. So there is no expansion plan which has been announced.

Shashank Kanodia: How much did they expand recently you mentioned?

Anurag Jain: I do not have that figure how much they expanded but their capacity is somewhere around 35,000 metric tons.

Shashank Kanodia: You mentioned in your opening remark there will be some operating leverage benefits right given that they are going to approaching a fixed cost of a high base so if you can quantum what kind of basis improvement in margin can be foresee for us over next two years?

Anurag Jain: As far as margin is concerned we always maintained that EBITDA level should be in their high-20s so we do not want to revise that.

Shashank Kanodia: Sir just give us some ballpark number about the improvement that you expect so high-20s have been your general statement over a quite a period of time.

Anurag Jain: If we operate in a market where there are so many variables, so I would not like to venture and I cannot say that my margins will improve by so much. What we can say is that all these benefits give us the confidence to maintain the margins.

Shashank Kanodia: What are the administration head expenses for a full year basis if you can share?

Anurag Jain: And what do you mean by administration expenses?

Shashank Kanodia: Corporate office, senior management salary.

Anurag Jain: You mean salary and wages.

Shashank Kanodia: Yes, senior management salary and wages plus overhead expenses.

Anurag Jain: Senior management salary and maybe disclosed in the balance sheet, last year you have seen that. So you have GMPs, you have the top 10 people how much they are drawing, it is always there in the balance sheet. As far as the employee cost is concerned that is Rs. 39 crores this year against 37 crore last year.

Shashank Kanodia: Lastly is it safe to assume that on a combined basis as of FY18 and on a capacity of 28,500 tons we have crossed 90% nutritional level?

Anurag Jain: Sorry we would not like to answer that in terms of quantities or percentages.

Shashank Kanodia: So if you can help me with cash flow from operations for this year?

Anurag Jain: If you look on the basis of the cash flows which get published on a standalone basis the cash flow from operational activities was Rs.85 crore.

Shashank Kanodia: For Duncan Engineering we have been PAT positive this year so we have witnessed some turnaround, so how do you see things going forward in that subsidiary?

Akshat Goenka: I think we have crossed the first hurdle by declaring a positive PAT for the first time and things should only improve from here. We still have some legacy issues to sort out which has not been all sorted out so some of that will hopefully get sorted out this year which we may have an impact but in spite of everything I expect another positive PAT this year as well.

Moderator: Thank you. As there are no further questions. I now hand the conference over to the management for their closing comments.

Akshat Goenka: Thank you everybody for joining on the call. I hope you have been able to address all your queries. So, any further information, please get in touch with our team or our investor relation advisors and they will help you out. Thank you once again.

Moderator: Ladies and Gentlemen on behalf of Oriental Carbon & Chemicals Limited. That concludes today conference. Thank you for joining us and you may now disconnect your lines. Thank you.