



DCM Shriram Ltd.

Q3 FY16 Earnings Conference Call Transcript

February 8, 2016 (12.00 noon)

Moderator: Ladies and Gentlemen, Good Day and Welcome to the DCM Shriram Limited Q3 & Nine Months FY16 Earnings Conference Call. As a reminder, all participants' 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, please signal an operator by pressing '*' and then '0' on your touchtone telephone. Please note that this conference is being recorded. I now hand the conference over to Mr. Siddharth Rangnekar of CDR India. Thank you and over to you, Sir.

Siddharth Rangnekar: Good Afternoon and Thank You for joining us on DCM Shriram Limited's Q3 & 9M FY16 Earnings Conference Call. Today we have with us Mr. Ajay Shriram - Chairman and Senior Managing Director; Mr. Ajit Shriram - Joint Managing Director; and Mr. J.K. Jain - CFO of the Company. We will begin the call with opening remarks from Mr. Ajay Shriram and Mr. Ajit Shriram, following which we shall have an interactive Question-and-Answer Session.

Before we begin please note that some the statements made during this call may be forward-looking in nature and a note to that effect has been included in the 'Conference Call Invite', which was sent to you earlier.

I would now like to call Mr. Ajay Shriram to give us an overview on the Company's operations for the Quarter and Nine Months ended December 31st 2015 and the opportunities going forward.

Over to you, Sir.

Ajay Shriram: Thank you, Siddharth. Good afternoon, Ladies and Gentlemen and a very warm welcome to DCM Shriram Limited's earnings conference call for the quarter and period ended December 31st 2015.

I will take this opportunity to share insights into major developments in our sector and our plans going forward, following which Ajit will take you through the Financial Highlights of the Company for the Quarter and Nine Months ended 31st December 2015.

We are glad to report stable performance in Q3FY16 amidst weak commodity prices, adverse weather conditions and improving operating environment in the Sugar business. Let me now take you through the business wise developments:

Sugar business: We have seen a more rational cane pricing policy by UP state government and that has been implemented with the cane price subsidy scheme linked to the product price. The central government has followed a comprehensive policy to push use of ethanol which has resulted in production of ethanol becoming a viable activity for Sugar companies and third, the central government is pursuing policies to ensure that the surplus Sugar is exported out of the country and imports do not disturb the domestic market. All these measures are in the right direction and need to be strengthened over the next few years to restore the financial health of this industry.

Industry expects Sugar production in the current season to be lower than last year. This has given a much needed push to Sugar prices which have touched about Rs.29-30/Kg from a low of Rs.21-22/Kg. The prices need to go up by at least 10% more so that industry can earn small profits. The crushing operations in our factories are satisfactory with higher recoveries. We expect better performance going forward if Sugar prices remain firm.

Chloro-Vinyl Business: The product prices are vulnerable to cheaper imports with low custom duty protection. The global prices in the current year have been trending downwards. International PVC prices in the current year have declined by about 20% from the peak witnessed in April '15 whereas Caustic Soda prices are also lower by 8%. The rupee depreciation has provided some support to prices. Input cost of key raw materials such as salt, limestone, carbon material have declined slowly over this period, providing part mitigation to the impact of falling prices. The new taxes and levies on coal based are putting an additional burden. In this scenario, our investment in cost optimization initiatives and capacity expansion will help to improve our cost structure and volumes from financial year '17 onwards.

Shriram Farm Solutions: The Agri scenario in the current quarter continue to be challenging on account of adverse weather conditions, low water reservoir levels, delayed sowing in Rabi season and weak farmer sentiment. These have led to a lower paying capacity of the farmer, leading to low volumes and margins of Agri Inputs. There is high inventory at trader level, which in turn is leading to higher working capital. Added to this the subsidy outstanding with the government has increased. The business on its part has intensified its marketing activities, is realigning its product portfolio of Bulk Fertilizers and increasing geographical footprint to drive growth over the medium-term.

Bioseed Business: This business is facing similar challenges in terms of adverse weather and weak farmer sentiments as our Farm Solutions business. Added to that the central government has promulgated the cotton seed price control order, the decision under which will affect the performance of this business. El Nino effects impacted the growth in our international operations and now there is a risk of La Nina. Given normal weather conditions, the business is poised to witness growth in the medium-term especially due to the strength of our product offerings, a result of sustained high focus on R&D activities.

Fertilizer Business: This business is facing two challenges – One, on account of tightening in energy norms under the new urea policy and second, on account of higher subsidy outstanding. We continue to reduce our energy consumption and work with government to have a rational pricing mechanism for older plants to ensure viability of this business. We expect business to be stable for the next 2-3 years.

Fenesta Window Systems: The business is witnessing high growth in the order booking from the Project vertical. The billing and execution however continues to lag due to cash flow constraints of the real estate sector. Retail segment continues to record moderate but steady growth. Volumes were impacted by floods in Chennai. However, this should be made up in Q4. We continue to work on development of new products to suit the varied customer needs.

At the Company level, our balance sheet continues to be strong and is expected to remain strong though we expect increase in borrowings in Q4 FY16 due to higher Sugar inventory and higher subsidy outstanding. It would, however, come down as soon as fertilizer subsidy payments are released by the central government. Our Chlor-Alkali capacity expansion plan at Bharuch is progressing well with Caustic Soda expansion expected to come onstream in Q1 FY17. The new power plant at Bharuch plant is expected to be commissioned by September 2016. The Cogen capacity expansion of Sugar is expected to be commissioned in Q3 FY17. These will add to the Company's performance from FY 17 onwards. We are focussed on growing our Bioseed, Farm Solutions and Fenesta businesses and improving our cost profile across all our other businesses.

I will now request Ajit to take you through the Financial Highlights.

Ajit Shriram: Thank you. Good Afternoon, Ladies and Gentlemen. I will now summarize the Financial Performance of the Company:

Total revenues for the quarter stood higher by 6% year-on-year to Rs. 1,263 crore primarily due to higher volumes of Bulk Fertilizers.

PBDIT increased to Rs.101 crore during the quarter, up 85% year-on-year. Increase in earnings during the quarter was on account of stable earnings of Chlor-Vinyl business and lower losses in the Sugar and Bioseed businesses. The financial charges for the quarter and year-to-date are lower due to lower debt and lower cost of borrowing.

Let me now take you through Business wise Financial Performance:

Sugar business' revenues in Q3 stood lower as volumes declined to 3.0 lakh quintals from 4.8 lakh quintals last year, a result of lower opening inventory this quarter. Realizations stood at Rs.2635/Qtl., down 7% year-on-year, although sequentially we are up 14% and currently at about Rs.3,000/Qtl. Losses stood lower in Q3 versus last year due to lower inventory write-down as cost of production improved due to improvement in recovery till December 31st from 9.97% last year to 10.67% in the current year and the Sugar price outlook improved. Inventory write-off declined to Rs. 10 crore from Rs.27 crore last year.

The trend of higher recovery has continued in January and February so far. UP government has announced the SAP for 2015-16 along with cane support price of Rs.35/Qtl.. However, we have taken credit of only purchase tax concession of Rs.2/Qtl. of Cane after the same was notified. The other cane support elements will be recognized as and when they are notified.

The Chloro-Vinyl segment revenues in Q3 increased marginally vis-à-vis last year. Vinyl had lower volumes whereas Chlor-Alkali had higher volumes and realizations. Carbide's realization stood steady during the quarter and the Company is trying to optimize its volumes. Segment PBIT

increased 39% in Q3FY16. This increase in earnings is attributable to stable Chlor-Alkali prices in the current year whereas there was a sharp drop in prices in Q3 FY15. The cost of production has also come down due to improvement in efficiencies as well as lower input prices. The business has planned maintenance shut down in the fourth quarter, which will impact volumes during the quarter.

Shriram Farm Solutions - Q3 revenues stood higher by 35% due to higher volumes of Bulk Fertilizers. Revenue of Value Added vertical stood lower by 5% due to lower offtake of Crop Care Chemicals and Micronutrients. Earnings stood lower primarily due to low margins in the Bulk business. Earnings were also impacted by higher subsidy outstanding of Rs.260 crore Vs Rs.167 crore as on December 31, 2014. The segment's capital employed increased to Rs. 322 crore due to higher subsidy outstanding and inventory of Bulk Fertilizers.

For Bioseed Q3 is an off-season. Revenue increased to Rs.46 crore, up from Rs.30 crore last year due to higher sales of Corn Seeds in the international business and Vegetable and Corn Seeds in the domestic business. Bioseeds business' Q3 losses moderated primarily due to one-time inventory write-off of Rs. 8.7 crore in Q3 FY15.

Fertilizer business' revenue increased 8% year-on-year primarily due to increase in volumes. Tightening in energy norms under the new urea policy has impacted the performance. Energy efficiency continues to improve and stood better both sequentially and vis-à-vis last year. Subsidy outstanding as on 31st December 2015 stood at Rs. 324 crore, up 19% year-on-year leading to higher working capital requirements impacting return.

The 'Others' segment earnings improvement was due to better performance of the Fenesta business. Fenesta business's revenues increased by 9% year-on-year to Rs.52 crore on account of increase in volumes in the Project and Retail segment by 53% and 6% respectively. Retail business's contribution to revenue in Q3 and nine months FY16 stood at 68% and 74% respectively. Order booking in the business has also been robust in Q3 and Nine Months FY16. The Company's net debt as on 31st December 2015 stood at Rs.435 crore as compared to Rs.491 crore as on December 31, 2014. The Company's cash profit in nine months FY16 increased to Rs.330 crore, up from Rs.317 crore last year.

That concludes my financial overview. We would be glad to take any questions that you may have.

Moderator: Thank you very much. Ladies and Gentlemen, we will now begin the Question-and-Answer Session. The first question is from the line of Abhijit Dey of BNP Paribas Mutual Fund. Please go ahead.

Abhijit Dey: What is the current recovery in the Sugar business in the current quarter?

J.K. Jain: To-date recovery for this season is about 10.8 vis-à-vis last year when recovery stood at 9.9 for the full season.

Abhijit Dey: In your Sugar business, how much growth in production are you expecting this year vs. last year?

Ajit Shriram: That is a bit difficult to say right now, Abhijit. There has been a slight decline in yields because of poor weather conditions and we have seen a higher recovery. So we feel both will offset each other and our volumes would be similar to last year, as of now.

Abhijit Dey: What is the progress on the capacity expansion in the Chemicals business right now?

Ajay Shriram: It is moving satisfactorily as I mentioned. We expect our Electrolyzer and the Chlor-Alkali manufacturing site to be commissioned in the first quarter of financial year '17 and our power plant we expect to commission by about September this year. In the interim, before the incremental power capacity comes onstream, we plan to use our 22 MW of furnace-oil based power plants to start production of newly added caustic soda capacity. Post September 2016, once our additional coal based power plant comes onstream we will shift production to the new power plant from the DG sets.

Abhijit Dey: How long will be the maintenance shutdown in the Chloro-Vinyl business in Q4 FY 16?

J.K. Jain: 5 to 10-days each in both the plants at Bharuch and Kota.

Abhijit Dey: Did you have a similar shutdown in Q4 of last fiscal also?

J.K. Jain: Not in Q4 last year, last time we had taken in Q2, this time it is being taken in Q4.

Abhijit Dey: To what extent will it impact performance?

J.K. Jain: Production will be impacted to this extent and there will be some maintenance expenditure, which will not be very significant.

Moderator: Thank you. The next question is from the line of Aman Sonthalia from Suvridhi Capital. Please go ahead.

Aman Sonthalia: What was the closing valuation of Sugar?

J.K. Jain: Rs. 2,880/Qtl as on 31st December 2015 .

Aman Sonthalia: Did you have to book inventory losses on the closing stock?

J.K. Jain: As we indicated we had taken an inventory loss of about Rs.10 crore in Q3 FY 16.

Aman Sonthalia: Can you please explain the conditions under which the subsidy will be payable under the new UP Cane Policy?

J.K. Jain: As per the incentive policy, the incentives are linked to the product prices and the recovery, both and that will be decided based on the actual prices between November to May. If the product prices move favorably, one will not get incentive, but then we will have higher profits from product prices. So I do not think it has effect on the financial profitability of the mills either way, either through subsidy or through product prices the profitability will happen.

Aman Sonthalia: Suppose if the average price is below Rs. 3,174/Qtl., then will the industry get the subsidy?

J.K. Jain: As I said there are two things -- one is the recovery which is base recovery at 9.5 and there are product prices which is not only Sugar prices, it is the prices of all the products, Bagasse, Molasses, Press Mud. So depending upon the movement of all the prices, government works out the price of the overall package and then decides the subsidy is payable or not payable.

Aman Sonthalia: How much exports have happened from India till date?

Ajit Shriram: From the industry the total physical export which has happened is about 750,000 tonnes and we anticipate that at least a million tonne more gets exported.

Aman Sonthalia: Since international price have come down, even in that scenario also, this much will be exported?

Ajit Shriram: We do hope so that from the coastal factories exports do take place. Landlocked factories like those in UP they are contracting with trade houses and with coastal companies, to export on their behalf.

Aman Sonthalia: Have we sold our total quota?

Ajit Shriram: We have sold about 75% of our quota, so far.

Aman Sonthalia: On production, ISMA has come out with a figure of around 26 million tonne , but as per industry estimates production will be less by 30% in Maharashtra and around 20-25% less in Karnataka and in UP also the yield in some of the places is very-very low, so even we take this higher recovery into account, the production may fall by 3-4% in UP also. If I take all this into account, the production figure look to be around 23.5-24.0 million tonne. So can you give some light on this?

Ajit Shriram: Last year the Sugar production was 28.3 million tonnes, Maharashtra produced 10.3 or 10.5 million tonnes, this year we are looking at Maharashtra producing about 8.5 to 9 million tonnes. UP produced 7.5 million tonnes last year and it will be somewhat similar this year. There is higher recovery but as you rightly said there is lower yield as well. On the whole, the production estimates of both the government and ISMA at 26 million tonnes holds.

Aman Sonthalia: But there are estimates that production in Maharashtra might come down to 70-75 lakh tonnes as the yield is very low there?

Ajit Shriram: We are currently in the early parts of February, we will get a clearer picture around the middle or end of March when the Sugar factories begin closing down, then that will give us a more accurate picture.

Moderator: Thank you. The next question is from the line of Falguni Dutta of Jet Age Securities. Please go ahead.

Falguni Dutta: A basic question on the Sugarcane price. So SAP has been retained at Rs. 280/Qtl. Can you just give the breakup what will be the landed cost if we get subsidy and what if we do not and what are the levels broadly at which we will be getting subsidy?

J.K. Jain: Rs. 280/Qtl. is SAP and Rs.35/Qtl. is subsidy for the industry. If we do not get subsidy, then the price will remain Rs. 280/Qtl., if we get subsidy it will be lower by Rs. 35/Qtl..

Falguni Dutta: There will be some transport cost added to this obviously?

J.K. Jain: About Rs.11-12/Qtl. is the transportation cost and that remains constant.

Falguni Dutta: This Rs.11-12/Qtl. is net transportation cost, right?

J.K. Jain: Yes.

Falguni Dutta: **Would we get** this subsidy Rs. 35/Qtl. If Sugar prices remain above Rs 31.74/Kg?

J.K. Jain: As I just explained it is linked not only to Sugar prices it is linked to Sugar, Molasses, Bagasse and Press Mud prices and also with the recoveries. Based on 9.5% recovery and the prices that they have specified if it remains below that then we will get the full subsidy, otherwise they will work out some pro-rata.

Falguni Dutta: But for Sugar particular they have kept Rs. 31.74/Kg.?

J.K. Jain: Rs.31.78/Kg., yes.

Falguni Dutta: There is no central subsidy to this?

J.K. Jain: There is a central subsidy in FRP which is Rs. 4.50/Qtl. of Sugarcane provided we meet all the export obligations.

Falguni Dutta: So which means that this will be in addition to the Rs.35/Qtl. deduction that we might get?

J.K. Jain: Yes, but it enables us to contract out export and pay some premium. So chances are the premium that we will pay on export and the subsidy that we will get from central government will balance out and will not add to the profit of the Company.

Ajit Shriram: The main benefit is that by giving this export subsidy physically Sugar will go out of the country and the inventory stocks from the country will reduce.

Falguni Dutta: Yes, so it will benefit in terms of pricing?

Ajit Shriram: Domestic pricing.

Moderator: Thank you. The next question is from the line of Rohan Gupta of Emkay Global. Please go ahead.

Rohan Gupta: Sir, first question is on Bioseed. You mentioned that roughly Rs.8 crore was write-down in current quarter, right?

J.K. Jain: We mentioned that last year same quarter.

Rohan Gupta: Current year there has been no write-down?

J.K. Jain: This is the difference, there has been some write-down, we are saying last year we had to write-down this Rs.8.5 crore extra. As a part of normal practice, there is always some write-off which we do on old stock which continues every quarter.

Rohan Gupta: What is the total write-down we have taken in current year in Bioseeds?

J.K. Jain: It is Rs.12 crore for both India and international combined to-date in nine months.

Rohan Gupta: Last year Sugar business EBIT was at Rs.68 crore loss. Out of that almost Rs.75 crore subsidies you have received this year which was actually related to previous year?

J.K. Jain: Yes.

Rohan Gupta: So Rs.75 crore if I add it back, it means last year there was a positive EBIT of close to Rs.7-8 crore, that was given a weak industry environment last year. Now, in current year we have seen that Sugar prices have gone up and even your better realization in other by-products also. So, do you see that there should be significant improvement in Sugar business in the current scenario? What is the per Kg minimum EBIT we can expect even if the government take the subsidy of Rs.31.75/Kg. if we achieve the Sugar prices assuming that subsidy in that level also?

J.K. Jain: Just wanted to correct the last year's number. You are right that if you just take the March number and add the subsidy you will reach a positive EBITDA, but then there was a big loss during June quarter and September quarter also, because the prices had dropped after March, further.

Rohan Gupta: That is on the Sugar inventory, mark down losses which we have...?

J.K. Jain: The Sugar inventory which we had in March we had valued at Rs. 2,700/Qtl., but we realized much less when we sold during this particular year. So the subsidy should be set off against full season basis and on full season basis even after subsidy Sugar had negative EBITDA last season. In that sense you are right that this year if the prices move up it should create positive EBITDA, but as of now the prices are just equivalent to the cost of production after factoring in subsidies. So we do not expect positive profit unless the prices move up above this.

Rohan Gupta: On Fertilizer business, what was the subsidy pending?

J.K. Jain: As on 31st December for Urea it was Rs.324 crore and on DAP MOP Rs.260 crore, so total was Rs.584 crore.

Rohan Gupta: Given the high inventory in Fertilizer business as you also mentioned in your opening remark, what is the industry sense and what is your estimate that when we entered next year Kharif crop how much inventory we will start with the season and what will be your take on the trading of DAP and MOP?

Ajay Shriram: It is an estimate which people are still trying to understand because a lot depends on how the monsoon is going to be like in this current Kharif season. So people are cautious across the board. It is difficult to give a figure. But there is a sense of apprehension that in case the monsoon is not good, then it would not be a good situation but if the monsoon is good and as per indication is that we should have a satisfactory monsoon or maybe little extra rainfall. If that situation comes it should be all right.

Rohan Gupta: Sir, in your Fenesta business, you gave some number that Retail contribution is 68% for Q3 and 74% for nine months or it is other way round?

J.K. Jain: You are right.

Rohan Gupta: Sir, with focus on 'Retail' segment, how did we do higher business in the 'Projects' segment ?

J.K. Jain: The billing part can keep fluctuating depending upon how the Projects progress, sometimes a Project just takes off and therefore you need to meet the delivery obligation which does not mean a change in focus. I think we continue to focus on both the parts of the business. Right now 'Retail' is doing better than 'Project' in terms of overall execution. That is why 'Retail' segment's share is high. But it does not mean any change in focus of the company.

Rohan Gupta: But overall this Fenesta business compared to like last year nine-months I think we have done close to Rs.200 crore turnover and this year also close to Rs.195 crore. So there has not been any significant growth. So it is because you are continuously reducing your sales to Project and focusing more on Retail or there is overall impact of slowdown in real estate which we see?

J.K. Jain: I do not think your numbers are right. You are reading the other segments which includes besides Fenesta, our Polytech business and last year it included Textiles business also for part of the year, which we exited. For Fenesta business per se we had a growth in turnover of about 15% for nine-months, revenue is about Rs.154 crore Vs Rs.133 crore last year and the growth has been sharper in the Retail segment and slower in Project segment.

Rohan Gupta: In Retail, growth has been higher?

J.K. Jain: Correct.

Rohan Gupta: Out of the EBIT, if you can just give us the number what was the EBIT from Fenesta business, is it positive or negative?

J.K. Jain: Fenesta is now PBT positive. So there is no negative EBIT.

Rohan Gupta: In 9M FY 16, 'Others' segment's EBIT is roughly Rs.5 crore. So can we assume all is coming from Fenesta?

J.K. Jain: It will be largely Fenesta EBIT.

Moderator: Thank you. As there are no further questions from the participants, I now hand the floor back to the management for closing comments.

Ajay Shriram: Thank you, Ladies and Gentlemen. As we mentioned, the Company has reported satisfactory and reasonable performance in the current year despite a challenging global scenario and adverse weather conditions. A healthy balance sheet and reasonable cash flows enable us to comfortably fund our ongoing CAPEX programs. Our capacity expansion programs in Chemicals and Sugar businesses, efforts to grow our Farm Solutions, Bioseed and Fenesta businesses and sustained focus on cost optimization measures, places the Company well to witness steady growth in the medium-term. Thank you very much once again for joining us on this conference call. Good Bye.

Moderator: Thank you. Ladies and Gentlemen, on behalf of DCM Shriram Limited that concludes this conference. Thank you for joining us and you may now disconnect your lines.