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"Deepak Nitrite Limited Full Year FY2016 Earnings Conference Call"

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MANAGEMENT: **MR. UMESH ASAIKAR – CHIEF EXECUTIVE OFFICER, DEEPAK NITRITE LIMITED**
MR. SOMSEKHAR NANDA – GM - FINANCE, DEEPAK NITRITE LIMITED

MODERATOR: **MR. AMISH SHAH – ANTIQUE STOCK BROKING**

Moderator: Ladies and Gentlemen, Good Day and Welcome to Deepak Nitrite Limited's Q4 & FY16 Earnings Conference Call. 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. Amish Shah from Antique Stock Broking. Thank you and over to you.

Amish Shah: Thank you, Zaid. On behalf of Antique Stock Broking, I welcome you all to the Q4 & FY16 Results Conference call of Deepak Nitrite. I take this opportunity to thank the management of Deepak Nitrite for the call. On the call, we have Mr. Umesh Asaikar -- CEO and Mr. Somsekhar Nanda -- GM, Finance & Treasury. I now hand over the call to Mr. Asaikar for Opening Remarks. Thank you, and over to you sir.

Umesh Asaikar: Thank you very much. Good Afternoon everybody. I welcome you to Deepak Nitrite's Q4 & FY-'16 Earnings Conference Call.

To begin with, let me share the Corporate Developments and then take you through the Results Highlights during the Quarter and Full Year ended March 31st 2016.

We delivered strong growth in profitability during the year with healthy improvement in EBITDA, Profit before tax and profit after tax. Our EBITDA margin also increased by over 200 basis points year-on-year. All this was a result of solid performance in Fine & Specialty Chemicals segment which benefited from favorable product mix towards higher contribution products. This was further aided by our efforts to improve the operating efficiency, de-bottlenecking of production lines, better working capital management and control on operating and finance cost.

In order to share the increased profitability with the investors, the Board of Directors has recommended a dividend of Rs. 1.2 per share on an enhanced capital base. We have recommended a higher dividend in FY16 compared to FY15, that too on a capital base that was enhanced by the QIP issue that we undertook in January 2016.

I trust all of you are aware that we raised Rs. 83.3 crore through QIP issue of 1.175 crore shares of a face value of Rs.2 each. These were issued to some credible international and domestic institutional investors. In April 2016, we sold a land parcel located at Sinhagad Road in Pune, Maharashtra for a total consideration of Rs. 69.6 crore. We also surrendered our lease hold right in respect of the adjoining land in Pune for a total consideration of Rs. 9.66 crore. The proceeds from the sale of about Rs. 80 crore combined with QIP proceeds of Rs. 83.3 crore will form a meaningful component of company's equity contribution towards funding the Greenfield project of Phenol and Acetone in Dahej.

With respect to this project, we have completed the basic engineering work while significant progress has been achieved on detailed engineering. The project management team is established and the project will be implemented as per schedule. As on March 31st, 2016, we have deployed a total of Rs. 67 crore towards this project. As highlighted in the past, we have started seed marketing of Phenol and the response so far has been encouraging. As you are all aware, India imports its Phenol requirements as demand surpasses the existing supplies. Thus, our objective would be to bridge this gap which will give Deepak Nitrite the market leadership position in India. We also expect the Phenol demand to increase in the years to come due to changing consumption trends of the end user industries.

During the year, we augmented our Fine & Specialty Chemicals segment with entry into high-potential segments of Pharma and Personal Care Intermediates. We started offering new intermediates in both Pharma and Personal Care space and the traction thus far has been promising. Going forward, we expect a larger contribution from the Fine & Specialty segment on the back of healthy contribution from all the three segments of Agro, Pharma and Personal Care Intermediates.

Let me now share some highlights on our Financial Results. I hope that all of you had the chance to go through the 'Result Documents' shared earlier. We recorded an overall volume growth of 9% during the year which was driven by solid volume growth of 24% in Fine & Specialty segment and 10% in Fluorescent Whitening Agent segment. Revenue growth in Bulk Chemicals and Commodity segment was sluggish due to decline in the prices of global crude oil and related Petrochemical Intermediates. We were however able to maintain the spreads. Our EBITDA increased by 21% to Rs. 138 crore with EBITDA margin of 12.6% which is higher by 200 basis points year-on-year. Revenue shift towards products which enjoy a favorable demand-supply and stable spreads led to better EBITDA performance. Profit after tax increased to Rs. 65 crore compared to Rs. 53 crore in FY15 representing a growth of 22%.

Domestic revenues came in at Rs. 795 crore in FY16 against Rs. 787 crore while the revenues from Exports increased to Rs. 526 crore.

Looking at performance by segments, the Fine & Specialty Chemicals and Fluorescent Whitening Agent segments delivered higher revenues, while revenues from Bulk Commodities and Chemicals segment were impacted due to reduction in prices of products. Volume growth was strong in the quarter in-line with higher demand in the end user industries. Both, the Fine & Specialty Chemicals and Fluorescent Whitening Agent segments reported volume growth of 25% and 13% respectively on year-on-year basis. EBITDA came in at Rs. 47 crore higher by 25% translating to EBITDA margin of 13.7%, an increase of 250 basis points year-on-year. This was a result of higher contribution from key products as well as changed product mix. Profit after tax stood at Rs. 21 crore compared to Rs. 15 crore in the same period last year, an increase of 35%.

The Fine & Specialty segment was a standout performer delivering a revenue growth of 21% with healthy volume growth of 24%. This was supported by higher traction in our Fluorescent Whitening Agent segment. Bulk Commodities of Chemicals segment reported subdued top line growth as a result of decline in global prices of crude oil, but the volume growth was positive. Fine & Specialty Chemicals and Fluorescent Whitening Agent segments will be the frontrunners in the times to come on account of better demand for our products in the end user industries as well as expansion in product categories. Despite stiff competition in the global landscape, our Optical Brightening Agents portfolio showcased solid volume growth in domestic as well as international markets.

The road ahead looks encouraging, as we continue to demonstrate value-led growth in all the three segments, namely Bulk Commodities, Fine & Specialty and Fluorescent Whitening Agent segments. Furthermore, some of the new product categories like Pharma and Personal Care Intermediates can be scaled up many times the present revenue allowing scope for further growth in established product lines. The Fluorescent Whitening Agent segment and the Phenol segment will be the key growth engines and help us to take the Company to better heights in the years ahead.

With that, I would now hand over the call to Mr. Nanda - our General Manager, Finance & Treasury for comments on the Financial Performance.

Somsekhar Nanda: Thank you, Mr. Asaikar. Good Afternoon everyone and Thank you for joining us on the call today. I will take you through the Financial Highlights for the Financial Year 2016.

Total revenues stood at Rs. 1,327 crore in FY16 compared to Rs. 1,336 crore in FY15 while EBITDA increased by 21% to Rs. 168 crore translating to EBITDA margin of 12.6%. Margins improved by around 200 basis points year-on-year led by favorable product mix across all the business segments.

PBT grew by 35% to Rs. 91 crore compared to Rs. 68 crore in FY15. Apart from higher contribution from Fine & Specialty and Fluorescent Whitening Agent segments, this growth was possible due to only moderate increase in depreciation and finance cost. PAT was higher by 22% to Rs. 65 crore compared to Rs. 53 crore in previous year.

The Employee cost during the year increased by 16% to Rs. 116 crore due to impact of annual increments and increase in the retirement benefits. Depreciation in FY16 stood at Rs. 39 crore, higher by 9% compared to Rs. 36 crore in FY15. Capitalization of the hydrogenation as well as MAHCL facilities which were fully commissioned during the year, resulted in higher depreciation during the year.

In FY16, the finance cost stood at Rs. 37 crore compared to Rs. 36 crore, while in Q4 FY16 the finance cost declined by 4% to Rs. 8 crore. The finance cost includes exchange loss for FY16 which is marginally higher due to sharp volatility in exchange rates as well as other related expenses. As a policy, DNL will continue to protect its foreign currency exposure through regular hedges.

During the year, revenues from Bulk, Chemicals and Commodities (BCC) segment came in at Rs. 675 crore compared to Rs. 750 crore in previous year FY15. Decline in crude oil prices and relative petrochemical intermediates impacted the top line of BCC segment. We were however able to maintain spreads. EBIT margins improved by 200 basis points to 11.8% against 9.8% in FY15.

Moving to Fine & Specialty Chemicals segment, revenues stood at Rs. 393 crore in FY16 compared to Rs. 326 crore in FY15, representing a strong growth of 21% year-on-year basis. Volume growth also stood healthy at 24% driven by higher traction in select products and contribution from newly introduced Pharma and Personal Care Intermediates. In FY16, revenues from Pharma and Personal Care Intermediates stood at Rs. 9 crore and Rs. 22 crore respectively. Fine & Specialty Chemicals segment contributed 29% to the total revenues with EBIT of Rs. 97 crore, higher by 57% against Rs. 62 crore in FY15. EBIT margin stood at 24.7% as compared to 19% in FY15.

Revenues from FWA segment came in at Rs. 274 crore compared to Rs. 266 crore last year. Strong traction in OBA-led product portfolio as well as better customer acceptance helped improve the overall performance in FWA segment. Volume growth stood at 10%. The contribution of FWA segment to revenues was 20%.

Coming to our Balance Sheet Position, our total debt declined to Rs. 495 crore in FY16 compared to Rs. 545 crore in FY15 translating into debt-equity ratio of 1.01x. This includes exchange fluctuations of around Rs. 43 crore, and if we remove this impact debt-to-equity ratio stands at 0.92x. As highlighted in the past, we would continue to maintain a strong balance sheet in the coming years even as we undertake significant investments in the Greenfield project for Phenol and Acetone.

With that, I would like to request the moderator to open the session for Question-and-Answers.

Moderator: Thank you very much, sir. Ladies and Gentlemen, we will now begin with the Question-and-Answer Session. The first question is from the line of Arun Malhotra from Santalum Capital. Please go ahead.

Arun Malhotra: You are setting up a new plant for Acetone and Phenol and in that process doubling the existing gross block, basically it will be twice the existing size. So your thoughts on how would we manage that and what makes us confident about these two products – Phenol and Acetone?

Umesh Asaikar: India is Phenol and Acetone deficient country. India's demand for Phenol is about 260,000 tonnes and our Phenol capacity is going to be 200,000 tonnes. India has about two companies;

one is Schenectady i.e. earlier Hardellia and Hindustan Organic Chemicals (HOC), between two of them, production of Phenol stands at about 40,000 to 50,000 tonnes. So India has to import more than 200,000 tonnes of Phenol every year. Now, Phenol is a building block and therefore its growth rate is normally connected to and has a very high coefficient of correlation with the country's GDP growth. You know that our country is expected to grow at a GDP growth rate of more than 7%. So you can just build this growth rate on the current consumption of India at 260,000 tonnes. So we have no doubt that our Phenol and Acetone project will be completely sold out from the day we start producing.

Arun Malhotra: But in these kind of chemicals, what would be our cost of production vis-à-vis the international majors and who are the international major players?

Umesh Asaikar: There are a whole lot of international players including US, Europe, China and across. We are not much worried about that, because the starting materials 'Benzene' and 'Propylene' for Phenol and Acetone are always bought at international parity. Propylene and Benzene, India has enough to give it to us. So there is no issue on that. So our cost of production to answer your question specifically will be having international parity, in fact, we might hold certain cost advantages over the others including China in terms of energy cost and in terms of manpower cost. This entails Rs. 1,200 crore of CAPEX. More than that, Phenol is a bulk item and the Indian Phenol consumption industry is a fragmented industry. Therefore, we will hold a clear cut logistics advantage over exporters of Phenol to India. Today, there is no alternative and that is why they are in a position to export, but here we are sitting in terms of logistics advantage also over the foreign players and we would be introducing as a part of our Phenol project, the latest in logistics technology too.

Arun Malhotra: Are there any existing players also in the process of expanding or any new player expanding?

Umesh Asaikar: No, there are not.

Arun Malhotra: On the margins and the profitability, do we expect the same kind of margins what we are making in the current Fine & Specialty Chemicals segment?

Somsekhar Nanda: Yes, we are hopeful and we are more or less sure that this kind of margin will be sustainable. In the last concall also we said we will be doing about 27% to 30% and probably we will be moving around in that range over the next few quarters.

Arun Malhotra: The same asset turnover, means on Rs. 1200 crore of CAPEX can we assume around Rs. 2,000 crore of turnover? When will this project be completed?

Somsekhar Nanda: The asset turn ratio on a normal crude price, crude price is subdued now, on a normal situation it will be about 2.25x:1. Commissioning time is December 2017, few months here and there, but the project is running as per schedule.

Arun Malhotra: Do we have the resources in terms of talent and manpower to manage the new size of the company?

Umesh Asaikar: We have put in excellent quality project team in place already. We have all the Government approvals in hand, we have tied up our technology and most of the important suppliers of plant and equipment, we have finished our detailed engineering also, we have done the ground breaking also and civil construction should be over in next 2 to 3 months of time, so everything is as per schedule. We have all the Government approvals including environment and all that in hand already. So there is no issue on that. As I mentioned, we have already started seed marketing of Phenol because we want to understand our customers and the various nitty-gritty's of the distribution channels before we commercially on a very large scale come to market in the early part of the calendar year 2018.

Moderator: Thank you. The next question is from the line of Janakiraman from Franklin Templeton. Please go ahead.

Janakiraman: Can you throw some light on the OBA business, it is a relatively young business, how it is scaling up in terms of customer acceptance, and in export markets where are you standing now?

Umesh Asaikar: We have improved the turnover of Optical Brightening Agent. Please note, sometimes we say Fluorescent Whitening Agent or FWA and sometimes we say Optical Whitening Agent or OBA, both is the same. We have improved the turnover from Rs. 121 crore in FY15 to Rs. 171 crore in this year. So that is a substantial improvement in turnover. In coming year FY17, we expect to get past with much of ease Rs. 250 to Rs. 275 crore. As we close this coming year, as we come to Q4, our annualized turnover would have been much more than Rs. 300 crore. So right now we are scaling it up from Q1 to Q4 and possibly we will touch around Rs. 275 crore, but if I multiply Q4 by 4x just to analyze it or second half by 2 just to analyze it, it would be getting past Rs. 300 crore very easily. So we would end this FY17 having achieved on annualized terms literally doubling the turnover from Rs. 171 crore to Rs. 325 crore in terms of annualized kind of things.

Janakiraman: So let us say our Rs. 250 crore or thereabouts, what kind of capacity utilization would you have hit this year?

Umesh Asaikar: We would have gone to about 60% to 65% capacity utilization at Rs. 325 crore.

Janakiraman: I gather that till last year which is let us say at Rs. 170 crores, OBA has not yet reached breakeven?

Umesh Asaikar: No, we have reached EBITDA breakeven in Q4. We have approximately 100-105 clients already added and customer acceptance is very good, customers are very happy with our products performance. You are aware, that this is an application performance chemical, it is not only chemistry and price, but our product has to perform in terms of its brightening quality performance at customers end, on customer's cloth, on customer's detergent, and on customer's paper. So these are very tough standards and we compete against internationally reputed companies and we are doing pretty well in terms of customer acceptance.

Janakiraman: Among the three end user industries, Cloth, Detergents and Paper, in terms of the size of the requirement, how will it look like?

Umesh Asaikar: Globally about 120,000-125,000 Optical Whitening Agent demand is there at active level, out of that approximately 60% to 64% would go into Paper and rest of it I would say evenly distributed over Detergents and Textiles.

Janakiraman: On the Fine & Speciality Chemicals business, over the next three years, how does the business look in terms of expansion of your product portfolio, expansion of end user industries, etc.?

Umesh Asaikar: We have at least four current products where we are doing capacity expansion in Fine & Specialty segment, this is point no. 1. Point no. 2, we have said last year that we will pick up Pharmaceuticals and Personal Care Products as one more segment to be nurtured over the years and we achieved turnover of approximate some Rs. 30-40 crore last year in this segment of Pharmaceutical Intermediates and Personal Care Products. We have done detailed plans to reach and take this segment to beyond Rs. 300 crore in next three years of time. We have done some CAPEX investments also in this segment which will bear fruit this year. So I expect Pharmaceuticals and Personal Care segment as part of Fine & Specialty strategic business unit to grow to about Rs. 300 crore in the next 3 to 4 years, while growing the other Fine & Specialty segment substantially.

Janakiraman: Just to get the numbers right, the Pharma and Personal Care Products segment stood at about Rs. 40 crore in FY16?

Umesh Asaikar: This segment we will take it to more than Rs. 300 crore in 3 to 4 years' time.

Somsekhar Nanda: If the turnover is Rs. 400 crore for the entire Fine & Specialty, out of which if we say about Rs. 30 to 40 crore is Pharma and Personal Care, now if we subdivide this between Rs. 360 crore and Rs. 40 crore, this Rs. 40 crore on standalone basis will go up to Rs. 300 crore and the rest Rs. 360 crore will continue growing the way it is growing now.

Janakiraman: So that is an extremely bright view, probably you have enough reasons for that kind of optimism. So can you share one or two key reasons why you are thinking that this will scale up from Rs. 40 crore to Rs. 300 crore in about three-four years?

Umesh Asaikar: Fine & Specialty Chemicals requires outstandingly close intimate relationship with customers. You need to engage customers on the technology and technical front, you need to design the products to attain to customers requirement of the intermediate, and you should be process strong chemical process to be able to win the customer's confidence, this is point no. 1. Point no. 2 is, all these customers are basically in Agro and Pharmaceutical field. So they come and do very severely strong audit of our manufacturing facilities. Based on this, we are very hopeful of building up Fine & Specialty Chemicals segment to more than double what it is there today in 3-4-years time. It will not be appropriate, Mr. Janakiraman, I think you will pardon me for this to disclose what kind of product intermediates we are working on.

Moderator: Thank you. The next question is from the line of Abhijit Akella from IIFL**.** Please go ahead.

Abhijit Akella: For this Pharma and Personal Care Intermediates, have we put in place CGMP manufacturing facilities? What is the exact competitive advantage that Deepak Nitrite has over other companies that might be targeting the same customers?

Umesh Asaikar: CGMP grade facilities are required for pharmaceutical formulations and to some extent they are required for chemical FDA approval at active stage. We do not manufacture Agrochemical or Pharmaceutical Actives. So that is the API game. We are not in API game; we are N-1 or N-2, we supply Intermediates which the customer buys from us and will convert that into an API. For example, we would have a product which we give even to Chinese customers and Indian customers, from there they would manufacture an analgesic anti-inflammatory kind of API active called Methanoic Acid for example, so for Methanoic Acid and its formulations you require CGMP facilities, not for N-1 or N-2 of Methanoic Acid. We all heard about Crocin. It is basically Paracetamol (P-Acetyl-Aminophenol) That is the active name. We do not manufacture Paracetamol, but we would give N-1 or N-2 of Paracetamol, we sell Intermediates.

Abhijit Akella: So just to clarify, the competitive edge that Deepak Nitrite has in this segment, is it our expertise in Nitration or is it something else?

Umesh Asaikar: So there are a lot of processes, kindly go on the website also, we are very good at many processes – Nitration, Hydrogenation, Concremation and Dyzation, there are few which I can mention quickly. So it is not only about having competency in these kind of chemical processes and many of them not only one or two, but it is also about the R&D capability to go quickly to the market. We need to design the product in R&D on paper, we need to conduct what we call kilo lab experiments, we need to scale it up to 5 Kgs to 25 Kgs that size and then we need to pilot it to a tonne-kind of a bag size and then we take it up finally to commercial scale by building a chemical plant around our processes based on the kilo lab and pilot plant experiences.

So this is a very long process of a new product development and you need to be quick at it, customers are not going to wait for you for months and years. So that is what we bring to the table as some kind of a competency from customers point of view. Of course, customer requires quality, customer requires delivery, performance and assurance, customer requires delivery promise.

Abhijit Akella: Are these products with limited life cycle in the sense that they might be phased out or not be required by customers in three-four-years or do they have long life?

Umesh Asaikar: Normally APIs have very-very long life, I have not heard of an API which dies within 20 years, but I must tell you as a matter of dilation, the longest surviving API is Aspirin, which is more than 125 years old and what was to be taken for headache is now a cardiology product, all cardiologist now give you dispersible Aspirin to dilate your blood vessels and keep the blood in a thin condition, so aspirin is longest surviving and doing very well.

Abhijit Akella: Here we are targeting the Export market also or is it mainly for the Domestic market?

Umesh Asaikar: No, our Fine & Specialty game is more Export-oriented than Domestic-oriented.

Abhijit Akella: We have started seeing crude prices moving up. So now how does that impact FY2017 financials or margin profile? First of all, do you think there is a possibility of some inventory gains for us? Second, can the prices move up and therefore can margins in percentage terms come down a little bit?

Umesh Asaikar: This takes me to remark on the last year's performance. Over the last 15 to 17 months, crude prices crashed from $108, they have crossed the other side of $30 also, and it was a recessionary year because of second drought across the globe in succession, etc. The price lines fail because most of these chemicals are petrochemical-based. But, we maintained the margin of our products if not improved them. We improved our margins substantially in Fine & Specialty Chemicals. So when the crude price goes back to $75+ or maybe $100+, we would be riding on that wave to our benefit.

Abhijit Akella: Are you seeing that already in the current price trends?

Umesh Asaikar: Yes, there is some firming up of crude prices, but this is a personal view, this is not Deepak Nitrite's view in that sense because we know no experts in forecasting. Personally, the point is that I do not expect it to cross $70 in near future.

Moderator: Thank you. The next question is from the line of Chirag Dagli from HDFC Mutual Fund. Please go ahead.

Chirag Dagli: What was the Pharma and Personal Care sales in FY15?

Somsekhar Nanda: We had said that it will be around Rs. 25 crore in December concall, but actually it went up to about Rs. 31-32 crore**.**

Chirag Dagli: So it is flat YoY for the full year, is it?

Somsekhar Nanda: It was nil in previous year, FY15.

Chirag Dagli: FWA as a segment has done an EBIT loss of Rs. 8.7 crore for the full year. Out of that, how much was for OBA, because that is sub-optimal operation, right?

Somsekhar Nanda: I have FWA segment number, OBA we will take it separately.

Chirag Dagli: You alluded to significant growth in Pharma, now when I look at our Fine & Specialty Chemicals segment, the EBIT margins were about 25% and the EBITDA level would maybe 28%, we do not see API companies actually making this kind of high margins, then your comment on the sustainability of these margins when you scale up the Pharma Intermediates business?

Umesh Asaikar: As I explained to you, our model is based on our relationships with our customers and we are just not making it for stock and sell, we make it useful for the customers against Memorandum of Understanding against quantity contract system. Therefore, I think we should not be generally compared with others as far as margins are concerned. These are specific customer needs, customer pinpoints being addressed.

Chirag Dagli: So these are innovator pharma companies or are these generic pharma companies?

Umesh Asaikar: Both.

Chirag Dagli: But in general you think these kind of margins in Fine & Speciality segment are sustainable?

Umesh Asaikar: Yes, they are sustainable.

Moderator: Thank you. The next question is from the line of Dhawal Shah from Oppenheimer. Please go ahead.

Dhawal Shah: In terms of CAPEX, what is the future guidance? Do we have more CAPEX coming in?

Somsekhar Nanda: Our regular CAPEX including growth CAPEX and maintenance CAPEX in the range of Rs. 40 to 50 crore a year which we shall be doing ever year for next two years. Apart from that, we are having a CAPEX for our Phenol business, of Rs. 1,200 crore. We have undertaken a project to manufacture 200,000 tons of Phenol and 120,000 tons of Acetone in a wholly owned subsidiary called Deepak Phenolics Limited, with a total estimated cost of Rs. 1,200 crore.

Dhawal Shah: The rights issue was issued for the same reason if I am not wrong?

Somsekhar Nanda: There was no rights issue, rights issue was done many-many years back. Close to 4-5 months back, we did a QIP at Rs. 70.9 per share.

Dhawal Shah: We recently sold a land in Pune. Was this land not viable for this particular option which we are trying to do?

Somsekhar Nanda: This land was not being used for some time and since this project is coming in Dahej, Gujarat, our management took a call and sold that parcel of land, the proceeds out of the sale will be used as an equity towards the project.

Dhawal Shah: How we are planning to do this CAPEX in terms of debt-and-equity ratio?

Somsekhar Nanda: The contemplated debt-equity ratio is about Rs. 480 crore of equity and Rs. 720 crore of debt.

Moderator: Thank you. The next question is from the line of Hardik Bora from Union KBC Mutual Fund. Please go ahead.

Hardik Bora: With respect to the phenol project, we will be substituting the import requirement. My question is that what are the chances that once you commence production, the competition right now which is currently the importers, they reduce the prices and make it slightly more unviable than what you would have envisaged earlier, do you perceive that as a risk?

Umesh Asaikar: I must say with a matter of pride that we have a very proactive and responsible Government in place and we have a very sympathetic Ministry of Commerce working with a lot of agility. So if such a thing happens, then you will immediately move for increase in anti-dumping duty. There is anti-dumping duty already in place which Hardellia now Schenectady Industries and Hindustan Organic Chemicals put together has brought in and that currently is there, it is in the book and therefore if further dumping is there beyond that, than we will go for enhancement of that anti-dumping duty and we will have Hindustan Organic Chemicals on our side and we will have SI industry on our side, and let us not forget that Hindustan Organic Chemicals is a Government of India Undertaking, it is a public sector company. To direct, just imagine how fast Commerce Ministry will act because they need to protect their investments and public sector profitabilities.

Hardik Bora: On the Phenol project, the CAPEX is Rs. 1,200 crore, how much of it will be funded through debt?

Somsekhar Nanda: Debt is 60% i.e. Rs. 720 crore.

Hardik Bora: If I work my numbers correctly, this CAPEX is going to be done over the next two years, right, by FY18?

Somsekhar Nanda: Residual is little less than two years, yes.

Hardik Bora: My calculation indicates that you probably will be making about Rs. 350 crore of cash flow from operations over the next two years. Are there some more non-core assets that you are looking to sell because if not then it seems to indicate that you might need to raise more debt than what you are right now calculating?

Somsekhar Nanda: The plan is that we will be working out 40% of the equity which translates to Rs. 480 crore of equity. This will be a mix of internal accruals. Secondly, the project land that Deepak Nitrite has given to the project company for cost of project, the land sale that we have just done in Pune and the first tranche of equity that we have done. So, this translates into about Rs. 280 crore out of Rs. 480 crore of equity. For the balance Rs. 200 crore, we will augment another fund raise program and calculate anything and everything, depending on the then market situation, the quality of investors and management's appetite. We can go for the possible option as per our board directors and shareholders' approval, and also having required to the capital structure of the company, what kind of instruments we can bring in and what kind of prices will be coming for.

Hardik Bora: I know it is difficult for you to give a guidance on the margins because it is based on how the realization moves, your sales growth can also be different from what you would guide right now. But assuming the crude price remain where they are, your 11.5% EBITDA margin for FY16 where can it go with the product mix improving, Fine & Specialty going up, what kind of guidance you can give on the EBITDA margins?

Umesh Asaikar: In the next two to three years, we would be adding 1 percentage point to our EBITDA margin every year.

Moderator: Thank you. The next question is from the line of Kashyap Jhaveri from Capital 72 Advisors. Please go ahead.

Kashyap Jhaveri: With respect to revenue breakup for FSC, FWA & BCC, could you give the same number for FY14 also?

Somsekhar Nanda: Kashyap, we have to send that separately, as we do not have that readily available.

Kashyap Jhaveri: The second question is on your return on capital employed both standalone and consolidated. Over the years, the margins have expanded, cash flows have been pretty strong, we are doing new CAPEX, but if I look at our return on capital employed that has been hovering in the range of about 10 to 12% with ROEs between 10-14%, so what has exactly kept this sort of low probably near the cost of capital or what could drive that number in late teens or probably in 20s?

Somsekhar Nanda: On a consolidated basis, we have the Phenol business, so I am taking that out, excluding the Phenol business, our capital employed would be around Rs. 850 to Rs. 900 crore. Out of this Rs. 900 crore of total capital employed, the capital employed for the Optical Brightening Agents Business is about Rs. 370 crore and this Rs. 370 crore has not started giving us cash or for that matter profits to the balance sheet. So that is one of the reason as OBA performance is still at sub-optimal level and we are hence falling short in the ROCE number. Once we start getting more revenues from OBA hopefully from this year, than this will significantly turn up.

Kashyap Jhaveri: So, OBA this year was roughly about Rs. 170 crore?

Somsekhar Nanda: Yes. You are right.

Kashyap Jhaveri: OBA at peak utilization at whatever assumptions that you have on raw material prices, what could be the turnover that this could give you?

Somsekhar Nanda: OBA should be between Rs. 550 to Rs.575 crore.

Kashyap Jhaveri: This is based on what raw material number?

Somsekhar Nanda: There are about 7 or 8 raw materials, right now we are operating at about 34-35% capacity utilization, 90% which is supposed to be the maximum capacity utilization if we do not say 100% will be close to Rs. 575 crore or Rs. 580 crore.

Kashyap Jhaveri: EBIT margins in OBA segment, let us say standalone are roughly about 9-9.5%, Is that correct?

Somsekhar Nanda: I would not be able to tell you the EBIT number, but EBITDA margin in a normal situation for OBA business would be around 14%. To answer your previous question on the raw material front, all our businesses in OBA is B2B and these are all between us and top notch companies across the world. So any movement adverse or positive movement in the raw material prices is shared. So to that extent risk of price movement is insulated.

Kashyap Jhaveri: In your FSC and FWA segment, normally how does the pricing work? So let us say for example your raw material is quoting at Rs. 100/ton, would you charge Rs. 100 plus Rs. X per ton to the client and when the raw material comes down to Rs. 50, you would again charge Rs. 50 plus the same Rs. X per ton as your conversion charges and accordingly quote?

Umesh Asaikar: Pardon me, certain things like pricing strategies and all that are matters which are extremely confidential between our customers and us, but I can assure you that our customers are our long standing partners, so there will be so much of mutual faith and trust that there will always be a win-win situation created between the customer and us and that is my company's philosophy.

Moderator: Thank you. The next question is from the line of Pawan Nahar from Religare. Please proceed.

Pawan Nahar: You have mentioned OBA has Rs. 370 crore capital employed. Can you please tell me the gross block or the fixed assets in that business, how much did you invest?

Somsekhar Nanda: Gross block would be close to Rs. 270-280 crore.

Pawan Nahar: Right now, excluding the Phenol project, our gross block would be close to Rs. 900 crore?

Somsekhar Nanda: Yes, you are right.

Pawan Nahar: I have a simple request or a suggestion if you like. Do you think it is better to look at your business in terms of absolute spreads per ton of unit rather than looking at percentage margins because as you said in OBA segment, the raw material is more or less the pass-through, we need to look at the spreads, so do you think it is possible for you to in your communication with us talk about spreads?

Somsekhar Nanda: That is a good suggestion. Can we touchbase on this on a one-on-one basis.

Pawan Nahar: Sure. Because a lot of companies which do volume-based business like a refinery, most chemical companies would look at pay back. So the reason I asked you, your gross block on OBA was just to understand, literally 1/3rd of your gross block right now invested is not yielding, you are still scaling up, the balance is generating more like Rs. 170-180 crore in terms of EBITDA on a gross block of Rs. 600 crore, that is a phenomenal pay back and my understanding would be that any new project that you would set up would typically aim for a payback of 5-years. So that is why I wanted to know one is the spread number if you can talk about that at a later point. The other thing I would like to always look at is your yield on gross blocks.

Somsekhar Nanda: That is a good idea, we will try if this is possible and I will call you separately. Having said that, OBA business actually is not a bulk business, it is a specialized performance chemical and very-very specialized, it has to perform its quality. For getting a nod at the customers place we will have to work with the chemical at their plant, if chemical is not working as per their satisfaction or as per their chemical perception they might lose a million meters of cloth or million tons of paper. So very-very difficult. Anyway I will keep this in mind and let us work on this.

Pawan Nahar: The third thing was I wanted to ask you was that clearly your Fine & Specialty Chemicals have done extremely well in terms of your absolute increase in EBITDA or EBIT. So I can see that you do very well in Nitration. Nitration is the prime chemistry for you if my understanding is right and Toluene Derivatives. So is it like volume growth or is it like some category that have just expanded meaningfully because this is like 50% growth in EBITDA or it could be new products like the pharma thing?

Somsekhar Nanda: In Fine & Specialty products, the manufacturing process might have Nitration, might have consolation, might also have diazotization. There are few processes of chemistry. So that involves a lot of expertise of chemistry. Now if we say Nitro Toluidine, it is not a part of Fine & Specialty segment, it is a part of BCC segment. So after all many other chemical process also. The reason of sharp increase in the absolute number is the change in product mix, that would be the primary reason and other reason is that we have taken a few steps in the recent past which has increased our operational efficiencies significantly.

Pawan Nahar: Product mix would mean pharma or something else within the existing segment?

Somsekhar Nanda: Not very significant in Pharma and Personal Care segment as I said it is about Rs. 32-33 crore, but it is largely in Agro segment.

Pawan Nahar: Generally in chemistry one would talk about say like your Phenol and Acetone plant would be a continuous process plant, right, it will run for 24-hours. I would imagine the same for DASDA and FWA, it is a dedicated plant?

Somsekhar Nanda: DASAD is a fully dedicated plant, FWA is not a dedicated plant, it has got four streams, and it can manufacture something else also in one of the streams.

Pawan Nahar: So the balance part of the business, Bulk Chemicals or Fine & Specialty Chemicals, would that be more like you can move in batches, how does it work? Hope I will be able to visit your plant soon so that I will have a better understanding.

Somsekhar Nanda: Fine, we will invite you and we will organize this visit.

Pawan Nahar: But most of your past CAPEX would be what, can move between products barring the DASDA and FWA segment?

Somsekhar Nanda: Yes, largely in Bulk Chemicals, Fine & Specialty and some in FWA also, but very minor.

Moderator: Thank you. The next question is from the line of Sandeep Baid from Quest Investments. Please proceed.

Sandeep Baid: You mentioned that OBA sales have gone up to Rs.170 crore. So that would mean that your DASDA sales have come down a bit in FY16?

Umesh Asaikar: I would agree with that, yes.

Sandeep Baid: So going forward would we assume that DASDA sales will be more or less the same as FY16 or do you think that it can go down further because you will use it for OBA?

Umesh Asaikar: The Company is taking very active steps to de-bottleneck the DASDA capacity and therefore to absorb this OBA effect partially. Incidentally, the company achieved the highest DASDA production in the year that passed by and we have plans to increase it in the near future by de-bottling it by 8-9% further.

Sandeep Baid: You mentioned that for OBA by end of FY17 you would hit a run rate of about Rs. 300 to 325 crore which would mean capacity utilization of about 60-65%. So can we assume with that capacity utilization, your EBITDA margins for the OBA business will be about 10%?

Somsekhar Nanda: EBITDA would be about 6%.

Sandeep Baid: On the Phenol project, given the fall in the commodity prices like steel and all, will there be some savings on the total project cost of Rs. 1,200 crore or we will still incur Rs. 1,200 crore?

Umesh Asaikar: Yes, we expect to save a few crores here and there as two things have happened; material prices of crucial elements are down like steel and cement but more than that normally the equipments are not measured in terms of tons of steel that it uses, because there is something called technology and knowledge cost, which we need to pay to the supplier of a particular process equipment. So more than the material prices coming down, there is a slight glut across the globe in capital goods industry and possibly we will take advantage on that basis and it will be beneficial to us, yes, you are right.

Sandeep Baid: So how much savings can we assume here on the total project cost?

Umesh Asaikar: When we come to it, we will tell because every 6 months to 1 year you would be asking questions now then out of Rs. 1200 crore of capital cost how much you have incurred and at what stage the project is because we have just done the ground breaking on first day of the Chaitra Gudi Padwa. So, we have just done the ground breaking and we are starting our civil construction. We have tied up all our technology partners, we have done the detailed engineering drawings and we are laying down on the systems and all that. So the real money will be spent in the last 9 months of the gestation period. So we are little bit far away from spending all the Rs. 1,200 crore as of now.

I feel tempted to give this information; we are not only a nitration company, we are good at more than 10 or 11 chemical processes, we are damn good at, so we possibly started as a Sodium Nitrate company which is incidentally Ammonia Oxidation and then we put up our Aromatic plant in 1992 or so when we started with Nitration technology source from BRG but lot of water has passed through Ganges since then and we are good at so many processes. That is what I was trying to explain is our competencies. We are not only a nitration company anymore.

Sandeep Baid: At current prices of Phenol and given the cost of production that you are looking at for your project, the EBITDA margins assuming the current prices can be in the region of about 25%, is my understanding correct for Phenol project?

Somsekhar Nanda: EBITDA margin is not 25%, it should be about 19-20%.

Umesh Asaikar: One more explanation; Because somebody had asked to talk more about margins and all that. The large petrochemicals which are made on the basis of 2 lakh tons, 3 lakh tons Phenol and Acetone project which is totally 3.2 lakh tons if I add ton on ton, these are actually spread-sensitive, they are not sensitive to price lines, they are sensitive to spread, so the Phenol price minus combination of Propylene and Benzene will be typically defined as a spread in this case. Am I managing this spread very well? Am I trying to maximize this spread beyond what I have got at project stage, will decide the success and better success of the project. So we as a company are acquiring all the competencies required in terms of buying of efficiency, in terms of negotiating skills, in terms of various kinds of relationship managements and logistic cost minimization, all that, because they are necessary for managing projects of such lakh ton capacity. So that is where the success is and we are acquiring all the human skill and balance and experiences in the fields to make us successful by doing these things.

Moderator: Thank you. We will take our next question from the line of Dheeresh Pathak from Goldman Sachs. Please proceed.

Dheeresh Pathak: I just want to clarify, of Rs. 270 crore of revenues in FWA, Rs. 170 crore was OBA. How much was DASDA and what were the other elements if any?

Somsekhar Nanda: Dheeresh, there are only two elements - DASDA was Rs. 100 crore and OBA was Rs. 170 crore.

Dheeresh Pathak: How much was OBA last year?

Somsekhar Nanda: OBA, was close to Rs.122 crore.

Dheeresh Pathak: When you said on 90% utilization you will do Rs. 550 crore, at that utilization what EBITA margins do you expect to have?

Somsekhar Nanda: EBITDA would be around 14%.

Dheeresh Pathak: Also you said that Rs. 270 crore of capital you have deployed in OBA, is it right?

Somsekhar Nanda: No OBA's capital employed should be Rs. 370 crore.

Dheeresh Pathak: That is in the whole of FWA segment?

Somsekhar Nanda: No, OBA standalone, as on 31st March 2016, the capital employed would have been Rs. 370 crore.

Dheeresh Pathak: But in your exhibit, it says that it is for FWA segment. So something must be in for DASDA also right, out of Rs. 370 crore?

Somsekhar Nanda: It is very low amount because DASDA is a 10 year old plant now.

Dheeresh Pathak: So what was that number, you said Rs.270 crore?

Somsekhar Nanda: Around Rs. 280 crore was our capital cost and other elements like working capital.

Moderator: Thank you. The next question is from the line of Bhavesh Jain from Envision Capital. Please proceed.

Bhavesh Jain: Can you give us some sense on the Chinese competition because we are hearing as well as reading a lot that there are plants shutting down in China, so your take on Chinese competition?

Umesh Asaikar: Chinese competition is a detailed subject and possibly we will engage many people for doing the detailed studies. Yes, China is going through lot of environmental related problems. Their water tables have been contaminated in many places. The Chinese Government at the behest of United Nations Organization's pressure from international community, etc., are coming very heavily down on industries which are polluting. It has two effects - the very bad effect on them is the closure of these particular units, and if that happens, which you must have seen during Beijing Olympics days then there is some kind of a shortage created and prices will shoot. We will benefit out of that if it happens.

Point no. 2 is that Chinese Government then typically next to the closure action give them time to put in the affluent treatment equipments in place and this entails heavy CAPEX for the Chinese companies as well as environment related processing cost which is part of variable expenses, therefore product cost go up. So sum and substance, I expect that the Chinese environment crisis will ultimately end up in firming up of all the products where China is dominating. However, when we give guidance on the future as a company, we do not depend on these kind of optimism, we give the guidance on the basis of our own strengths. If these things happen, good enough, our profitability will improve and we will give much better results. But we do not give guidance on the basis of these kind of extremely optimistic assumptions on let enemy get into problem, then we will benefit, we do not believe in these kind of things. So I would not give much credence to that. When it happens it happens, we will benefit.

Moderator: Thank you. The next question is a follow up question from the line of Abhijit Akella from IIFL. Please proceed.

Abhijit Akella: Just to clarify on Phenol, you mentioned that the margins at peak utilization is 19-20%, is it?

Somsekhar Nanda: No, the depressed prices of crude hence the Phenol Prices and Acetone prices came down what would be the top line and hence optically there has been increase in the EBITDA margin. To answer that question, I think it is around 19%, but if crude prices were about $80 or $85 in a normal situation this would have been around 12% to 13%. What is important is as you know the importance is of crack, the spreads which I was mentioning, if my crack was this $600, now also $600 I am devoid of any other averse movement in the market.

Abhijit Akella: So at peak utilization, would it be fair to assume an EBITDA in absolute rupees of around Rs. 350 crore from Phenol plus Acetone?

Umesh Asaikar:1 Around Rs. 400 crore I would say.

Abhijit Akella: Just on this whole 'Seed Marketing' initiative that we have been taking, obviously, it is important for us to seed the market in a substantial way as we head into full production 2 years out. So what exactly is the ramp up you are planning in terms of the Seed Marketing sales, and is there any profit that you would expect to make from it or should it be just breakeven?

Somsekhar Nanda: We will be having about 150 to 200 customers by the end of this year and we will be doing turnover of about Rs. 250 crore to Rs. 300 crore in FY17. We are seeing this as a special campaign to get into the market, not that we are targeting this for a profit or a loss, if profit or loss happens, that will be a derivative for our main agenda, the agenda is to reach the customer, agenda is to understand the requirement, be with them and the day we come up with the commissioned plant of Phenol and Acetone, same day we will start supplying to them, so they do not go to the importers.

Abhijit Akella: Probably close to breakeven level, that is the plan?

Somsekhar Nanda: I do not say break even, the plan is that, yes. If there is a loss so I would say that this is a cost of understanding the market or seeding the market, penetrating the market, if there is a profit we would say it is fine.

Abhijit Akella: Just to understand the Rs. 720 crore Phenol debt that will come on the subsidiary 'Deepak Phenolics' books entirely or will there be some portion which will be on Deepak Nitrite's standalone books as well?

Somsekhar Nanda: No, it will be 100% on the subsidiary's books and this loan does not have any recourse on Deepak Nitrite.

Abhijit Akella: You have mentioned previously it is a 13 year loan with a ballooning repayment schedule. What is the cost of debt that you have for this?

Somsekhar Nanda: Cost of debt as of now would be about 10.75%.

Abhijit Akella: Are we adopting Ind-AS in FY17, and if so, any impact from that?

Somsekhar Nanda: Not FY17, it is applicable to us next year onwards.

Moderator: Thank you. The next question is a follow up question from the line of Dheeresh Pathak from Goldman Sachs. Please proceed.

Dheeresh Pathak: Rs. 480 crore of equity requirement for the Phenol project and you said we have Rs. 80 crore from QIP and Rs. 70 crore from land sale, so that is Rs. 150 crore and you said we have got Rs. 280 crore, now Rs. 280 crore minus Rs. 150 crore, the balance Rs. 130 crore is internal accruals, is it?

Somsekhar Nanda: There are two other elements - one is the project land which is about Rs. 20 crore and another is Rs. 120 crore which comes out of Deepak Nitrite's internal accrual over the period implementation which is 3 years, so over 3 years Deepak Nitrite will give about Rs. 120 crore plus the project land cost which comes at about Rs. 20 crore as per GIDC valuation and this QIP plus the land.

Moderator: Thank you. Ladies and Gentlemen, we will take our last question now which is from the line of Kashyap Jhaveri from Capital 72 Advisors. Please proceed.

Kashyap Jhaveri: Could you let me know FY16 gross total debt number?

Somsekhar Nanda: Rs. 495 crore.

Kashyap Jhaveri: This Phenol CAPEX, you said total is Rs. 480 crore?

Somsekhar Nanda: No, total CAPEX is around Rs. 1,200 crore at debt-equity mix of 60 to 40. So, Rs. 480 crore is an equity number.

Kashyap Jhaveri: This will be over a period of how many years?

Somsekhar Nanda: 3-years, out of which 2-3-months have already gone, so 1-year 9-months or 1-year 10-months.

Moderator: Thank you. Ladies and Gentlemen that was the last question. I now hand the conference over to the management of Deepak Nitrite Limited for closing comments. Over to you.

Umesh Asaikar: Thank you very much everybody for joining us on the call. Should you have any further questions, please feel free to contact Mr. Somasekhar Nanda or our Investor Relations Team. We look forward to connecting with all of you next quarter. Thank you very much. Have a great day ahead.

Moderator: Thank you very much, members of the management. Ladies and Gentlemen, on behalf of Antique Stock Broking that concludes today's conference call. Thank you for joining us and you may now disconnect your lines.