"Carborundum Universal Limited Q3 Financial year 2014 Conference Call"

February 03, 2014

ANALYST: MR. JASDEEP WALIA

MANAGEMENT: MR. K. SRINIVASAN
MR. SRIDHARAN RANGARAJAN

Moderator: Ladies and gentlemen, good day and welcome to the Carborundum Universal Q3 FY 2014 earnings conference call, hosted by Kotak Securities Limited. 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 this conference call, please signal an operator by pressing "*" and then "0" on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Jasdeep Walia from Kotak Securities. Thank you and over to you Sir!

Jasdeep Walia: On behalf of Kotak Institutional Equities, I welcome all the participants to Q3 FY 2014 results conference call of Carborundum Universal. We have with us on the call, Mr. K. Srinivasan, the Managing Director, Mr. Sridharan Rangarajan, the Chief Financial Officer, and Mr. Raja Mukherjee, DGM Internal Audit & Strategy. I will hand over the call to Mr. Srinivasan for his opening comments.

K. Srinivasan: Good afternoon to all of you and wishing you all a very happy New Year though a little belated. I know we could have come up with better numbers, but I think I must say that looking at the business from close quarters we are not feeling probably and let us say let put it mildly as negative about it, as others would, because we think that we have done quite a bit of good work which are not probably showing up in the numbers.

On a consolidated basis, I can say the sales grew by about 16.3% on a quarter-on-quarter basis, a little bit flattering because you know that we had a bad Q3 last year, but sequentially there was a drop of 6.6%. Now this is pretty normal because we have to consider that Q3 always is a much smaller quarter compared to Q2 and Q4. It is a two-and-half month quarter for most parts of the world even in India we do have the poojas and Diwali holidays, so to that extent this has sort of accept in years of continuous 20% growth, we always have this mild drop in Q3, so that was not unexpected, but the margin falls in some of these business definitely was not what we expected.

Let me straight away jump to the performance of the three verticals, abrasives, electro minerals, refractories in ceramics, and then I will ask Sridhar to sort of help me out with numbers.

Abrasives Q3 at 213 Crores versus 197 of the corresponding quarter with an 8% growth, but sequentially there was a 6% fall, but the bigger problem really was the lower margins that we had in abrasives largely coming out of the fact that we had an unfavorable product mix with all the project orders drying up, all the auto, auto components, specialities going slow most of the major companies taking longer shutdowns in the last quarter, we had to live with the commodity products, primarily products in which we compete against the lower end imports and Chinese products, so consequently an unfavorable product mix really pushed it down, but the good side of the abrasives I must say is that we have refocused our business tremendously on exports and exports I must say is still doing very well.

We are going more than 50% on a small base compared to the last year in exports. Significant amount of work has been done in terms of accessing new markets, putting out trial or test wheels, we have taken a lot of these costs in terms of addressing new markets putting out test wheels getting our first set of things accepted etc., and this I am sure we will bear fruit not only for Q4 but even going forward. So this is a move that we made though it cost us some money and time, I think it is something which will help us going forward in abrasives.

In the Electro Mineral business, I think the consolidation and improvement is happening in a planned manner. Considering it is a smaller quarter, we were 204 Crores versus 132 of the corresponding period last year. This 50% plus growth is a little flattering, but on a sequential basis it is still 5% lower than the pervious quarter. Again, like I said, smaller quarter in terms of number of days available for production, so it is sort of running steady, we are not seeing any dramatic upturn, but there is a steady claw back in our position, the stronger entities are clearly consolidating and doing well and so we quite happy with our progress in the Electro Mineral business. Zirconia products are getting better. We are stabilizing our bubble business. We are having a cross flow of moving some of the Zirconia back to India for making Alumina Zirconia, so overall quite pleased with what is happening in Electro Minerals.

The only point of continued challenge is really is refractory business, we still not able to pickup volumes as quickly as we would like to and consequently we are paying a fairly high power cost since we are not running volumes. We hope this would play out in the next two quarters and we would be in a better shape.

So overall on the Electro Mineral business I would say steady progress, getting better quarter-on-quarter. Ceramic business is probably the most stressed business at this stage, simply because of the fact that the two pieces, alumina ceramic and wear ceramic is deeply impacted by what is happening in the power plants, in the coal washeries, etc., so we are running with one tunnel sitting idle and the other tunnel running at part capacity.

Coal production in Australia last year 2013 was 2% up on volumes, but in terms of price there is almost a 30% to 50% fall in the price. Consequently most of the maintenance activities are being largely cutback, huge fall in spends in terms of new lining, etc., so this is really pushing our ceramic business back both in Australia as well as in India. We have done reasonably well in the metz cylinder part and got new customers broad basing our business; however, the big fall in the group 1, which is really the wear ceramic just could not be made up and the efficiencies have taken a big beating with volume suffering. If you look at practically there has been no power plant orders in India, so we are really suffering in terms of under utilization of capacities in terms of the alumina ceramic business.

In the refractory business again we are running through a similar situation of poor consumption, our customers are not doing well; however, the investments in two new projects that we did in the last year, which is the Sheffield refractory project as well as anderman ceramic have ensured that we do not suffer as badly as others seem to have in the refractory business. These are helping us to at least remain reasonably flat compared to the others. So on the ceramic our Q3 sales consolidated 112 Crores versus 124 Crores sequential and 119 of the last quarter is sort of 10% drop on a sequential and 6% on a quarter-on-quarter basis.

At this environment that we are I think is not as bad as it sounds. We have significantly cutback on a capex spends except in case of capability creation like you know most places we still have significant capacities, so consequently our planned 100 Crores capex would probably not get fully spent this year. First nine months we have spent roughly about 68 Crores; we are likely to end about 80 to 85. Since we have planned for the kind of capex we thought it is reasonable to payout an additional dividend so the cash generation is still very strong. So we paid an interim dividend higher than last year. Last year was 0.50 paisa to a rupee and this time it is 0.75 paisa to a rupee as an interim dividend.

Clearly sort of indicate that our balance sheet is very strong. We have kept to our usual policies, provisioning in a stressed market condition, simply whatever material has not moved out of our factory in a particular time, whatever receivables have not come in a particular time we are making strong provisioning consequently balance sheet remains very, strong and robust. So overall I would say this quarter the environment is still much stressed, but there a lot of green shoots particularly in exports and that is probably going to be the way things are going to move up.

I am clearly seeing that there is no more going down in most of our businesses or all the businesses, it is only going to be getting better from here. So that is broadly what it is on the four verticals. To explain the numbers more I am going to request Sridhar to take it forward from here.

Sridharan Rangarajan: Good afternoon to all of you and wish you a very happy New Year. Before we start I just want to set few things to help us lead the further discussion. Q2 of last quarter that is 552 Crores sales that we did is the highest ever sales, even compared to the 2011-2012 best quarters that we had and the sales that we have on a standalone basis last quarter was about 299 Crores, which is again the highest ever sales on a standalone basis.

Second point is that in the last four years if you really look at Q2 versus Q3 either they were flat or they were going down. If you look at the last year we went down by 15% compared to Q2 to Q3 and now we are going down by about 6% and this was a similar observation you will see in the prior years as well. I thought that we should leave these two frameworks so that we are able to appreciate the numbers.

So with that, I would start by saying that on a quarter-on-quarter basis sales grew by 72 Crores, which is about 16.3% growth and the PBT increased by about 7 Crores. So out the incremental sales of 72 Crores and the gain of 7 Crores operating PBT, standalone sales increase was at about 12 Crores, but the PBT drop was at 4.2 Crores this means the subsidiaries and JVs contributed to a 60 Crores increase in sales and increase of about 11 Crores in the PBT. That is because few of these subsidiaries losses have come down particularly Foskor.

On a sequential basis sales drop by about 36 Crores, which is a drop of 6.6%; however, PBT dropped by about 26 Crores. Out the incremental sales of 36 Crores and a drop of 26 Crores in PBT, standalone sales drop was 32 Crores and the PBT drop was at 20 Crores. This means the subsidiaries and JV's contributed to 4 Crores of drop in sales and a 6 Crores drop in PBT and I will cover that in a minute later.

On a YOY basis sales increased by 105 Crores which is about 7.2% increase; however, the PBT there was a drop of about 11%. So out of incremental sales of 105 Crores and a 11 Crores drop in PBT standalone sales increased by 26 Crores and the PBT drop was 5 Crores out of this 11 Crores. This means the subsidiaries in JVs went up in sales by about 79 Crores and they contributed to 6 Crores drop in PBT.

CUMI standalone on a sequential basis there was a drop of 19.8 Crores in the PBT margin which is a substantial decrease. The broad reasons are the volume drop was about 32 Crores leading to a margin drop of about 8.8 Crores. Power and fuel cost has gone up by about 4.2 Crores. That is actually due to benefit from Maniyar Power Project that we have in Cochin, in Kerala we had the best rainfall in Q2 and normally the Q3 rainfall is lower than Q2 which is the seasonality issue. The fuel rate however went up by about 0.70 paisa per liter between these two periods, but the biggest contributing factor is the lower power generation for Maniyar. Third reason is the lower other income and lower exchange gain compared to the Q2 about 3.7 Crores and we also have an increase in other expenses. We just stressed on that increase in higher provisioning and also higher repairs, some of the repairs that we kept on postponing we will have to do that and that also contributed to the decrease in profit. There was a little bit of offset from the personal cost to the extent of about 1.3 Crores.

Now CUMI standalone operating PBT drop of Rs. 4.2 Crores on a quarter-on-quarter basis. Volume gain of 12 Crores leading to a margin gain of 10 Crores due to the better product mix, lower other income on account of lower dividend is again a timing issue and lower scrap sales and lower exchange gain, all three contributed about 2.6 Crores. Employee addition and increase in salary because we are talking two different years about 3 Crores and increase in provisioning and other related cost is about 8 Crores. Power and fuel higher spend by about 1.6 Crores and we also have about lower finance cost of about 1.5 Crores for the same period.

CUMI standalone operating PBT drop of about 5 Crores on year-on-year basis is due to volume gain of 26 Crores leading to a margin gain of 4.6 Crores. Employee additions and increase in salary and also due to some other changes in the provisioning as far as the Gratuities and Provident Fund Act about 10 Crores, higher other cost by about 5 Crores. Power and fuel lower spend by about 2 Crores. If you really see on an YTD basis the Maniyar power generation was far higher compared to the last year and that is why you are seeing on YTD basis you have a gain in the power and fuel cost. Though the real power cost and the fuel cost are substantially gone up, this is masked by the gain that we had from Maniyar power generation and a lower finance cost of 3 Crores reflecting a better cash generation.

Now going to consolidated numbers, on a sequential basis the drop of 25.8 Crores of PBT is due to the following: CUMI drop, which we just covered about 19.8 Crores. The drop in VAW about 3.5 Crores due to the lower sales as well as it is end year so they have few of the accruals coming up. Normally they will have their Q4 which is our Q3. Drop in volumes in Sedco, which is our gas-based power generation plant. They had some challenges in supply of gas from ONGC and Wendt and China put together about 2 Crores.

On a quarter-on-quarter basis, PBT consolidated margin improved from 3.1% to 4%, increase of 7 Crores by way of the following: Increase in Foskor's profits by about 11

Crores. The situation in Foskor because of the high cost of inventory, market-related situation, intensified from Q3 of the last year bottomed out by March and we have better sales at this point in time compared to the last year. The input prices are more or less stabilized and we have a better leadership team in place and we are seeing things are getting better at this point in time. Increase in VAW profit by about 5 Crores. This is compared to the last year. This is again due to better product mix and they also have higher volumes than the last year. This has been offset by the swing in profit in CUMI about 4.2 Crores, which we just covered. Losses in Sedco, losses in CAPL and we also had similar challenges in Australia, which Mr. Srinivasan just covered as far as the coal business is concerned.

For the YOY PBT consolidated margin dropped from 8.6% to 7.3% about 11 Crores largely by way of the gain of 11 Crores from Foskor and gain from VAW about 10 Crores and standalone drop of about 5 Crores and CAPL drop, Sedco, Thukela drop accounting for the balance.

No we will get into the details by segment. PBIT margin in abrasives at a consolidated level dropped from 9.8% in Q2 to 4.2% in Q3, which is probably the lowest ever. This drop is due to the following: CUMI abrasives 6 Crores due to the lower sales of 11 Crores and also we have some lower scrap sales of about 1 Crores. Wendt India similar reasons as far as abrasives business. Volumes are down about 1 Crore, China and Middle East contributing to about 3 Crores in that and VAW about 3 Crores due to lower sales, lower price realization and also the product mix that they have.

On a quarter-on-quarter basis on a consolidated level the margin dropped by about 10 Crores due to the following: Abrasives India margin dropped by 7 Crores despite the pickup in volume due to cost increase on account of exchange rate pickup from 52 on an average to 63 and power and fuel about 1.6 Crores and again same reason for China and Wendt about 3 Crores. On a YOY basis on a consolidated level the margin dropped by about 12 Crores. Abrasives India margin dropped by about 10 Crores, largely due to the exchange rate movement, adverse product mix, tight user market condition and not allowing us to put up prices there and Sterling gave lower profit on the similar industry so they also have a lower profit of about 1 Crore and the rest of the entities contributing to 1 Crore.

On EMD PBIT margin on a consolidated basis moved from 10.4% to 7.7%, a drop of 6.6 Crores. A drop of 3.6 Crores coming from CUMI India, largely due to lower Maniyar and lower offset in power cost, which is the result of Maniyar and the lower alumina sales. Then drop in Thukela refractories 1.6 Crores and drop in VAW about 1.3 Crores. On a quarter-on-quarter basis on a consolidated level the profits have improved by 24 Crores, largely due to EMD's profit went up by about 6.4 Crores, better Maniyar compared to the last year, better alumina's compared to the last year and increase in Foskor's profit by 12 Crores, increase in VAW by about 6.8 Crores and higher losses in Thukela about 1.2 Crores.

On a year-on-year basis Electro Mineral consolidated level the profits have improved by about 33 Crores, CUMI standalone contributed a 15 Crores, in Foskor the swing in profit is about 13 Crores, VAW is about 12 Crores and higher losses in Thukela is about 6.6 Crores, offsetting the gain that I talked about because we had nine months of operation this year versus five months of operation last year.

Going to ceramics, PBIT margin of ceramics moved from 11.2% in Q3 to 11.9% in Q2, then dropping to 10.4% in the current quarter which is an all time low. The drop is about 1.8 Crores on quarter-on-quarter basis and 3.1 Crores on a sequential basis. On a sequential basis 8.7 Crores drop is on account of ceramic standalone business itself mainly happening out of 16 Crores sales drop in ceramics business largely out of low project business that is what Mr. Srinivasan was just explaining and highly sensitive to volume business so since the volume is dropping and it has an impact consequently on the profit. This drop was offset by profits improvement in CUMI Australia about 2 Crores though sequentially there going down, overall they are below last year and our JVs MMTCL and Ciria has also done a better performance compared to last year. On a quarter-on-quarter basis EMD drop is entirely due to standalone business.

PBIT margin of ceramics moved from 16.9% on YTD 2012-13 basis to 12% YTD 2013-14, a drop of 21 Crores is due to the following: 7 Crores on account of ceramic standalone business, largely out of the sales drop of 21 Crores and CAPL business contributed to a 12 Crores and Ciria drop contributed about 2 Crores.

As far as capex, we just covered that earlier 68 Crores is what is the spent up till now. We expect this could go to the level of 80 to 85 Crores. On debt equity information on a standalone basis, we improved the debt equity from 0.19 as of September to 0.17 as of December and on a standalone basis the debt stood at about 128 Crores as of December 2013. On the consolidated basis the debt improved from 0.43 to 0.40 again probably the lowest ever at this point in time and overall debt remained at about 265 Crores.

By and large I would say better cash management has resulted in one you could see that finance cost is going down and second is that we have been very prudent as far as the provisioning of receivable and inventory is concerned. The receivable stress in all around has witnessed so we have been cautious in taking provision on a consistent basis. We have not relaxed on account of current pressure.

So by and large I would say the balance sheet looks far better cleaner and continue the same line at this point in time. So this is how we are looking at this point in time.

With that we will open up for question and answer.

Moderator: Thank you very much. Ladies and gentlemen, we will now begin with the question and answer session. The first question is from the line of Balachandra Shinde from Batlivala & Karani Securities. Please go ahead.

Balachandra Shinde: Good afternoon Sir. Sir regarding power and fuel cost, I would like to know both on standalone basis and consolidated basis if you see as a percentage of sales, sequentially it has increased substantially. What normal percentage of sales we can consider as a power and fuel cost that will be maintained or do we see any abnormal thing in this right now?

K. Srinivasan: See I think Sridhar explained to you in Q2 there is netting off effect of power we generate from a hydroelectric power station at Maniyar. The Maniyar is a hydroelectric station. Bulk of the power is generated during the monsoon time. Kerala monsoon is roughly between let us say July, August and September, so key power generation happens in the first half and second quarter and so consequently you are not comparing like-to-like when you look at Q2 to Q3. The power rate itself has not moved up in any of the domestic territories that we operate, Kerala, Tamil Nadu and other places, but we have used significant amount of diesel generated power in Tamil Nadu in Q3 compared to Q2 because of the fact that power cut has again come back. The rate of furnace oil or SKO which we used in furnaces for our firing has also gone up by about 0.70 paisa between the two quarters. So overall if you look at it there are two pieces. Our efficiency in terms of units of power per tonne has probably improved marginally. The fuel used per tonne of fired product again as remained by and large the same, so the efficiency parameters are in place, the rate parameters have marginally moved upwards but the big change is the hydroelectric power that gets netted off in our power consumption because it is a captive plant, so Q3 the big change is coming out of this.

Balachandra Shinde: So on subsidiary level, the higher power cost as a percentage of sales is due to this Maniyar subsidiary?

Sridharan Rangarajan: Maniyar is a part of the company. It is a part in our standalone. It is not in our subsidiary.

Balachandra Shinde: So at the subsidiary level why the power cost was high comparatively if you see Q1 overall our percentage of sales in the standalone was 10% of sales and on the consolidated basis also it was at around 15%, but if you see there is a deterioration of around 2% in the power cost?

K. Srinivasan: See if you really see the power cost in VAW went up compared to the last year. This is one reason. Second is the production levels in Foskor has gone up and Thukela has gone up. So the one is rate related, the other one is volume related. Include VAW our volumes have gone up that is the reason it is going up.

Balachandra Shinde: Can we assume that the power cost will be at these current levels as a percentage of sales for the coming quarters?

Sridharan Rangarajan: I think the range should be somewhere 15% to 18%. It can fluctuate in that range.

K. Srinivasan: About 16% you take it as an average I think it is a fair thing because in months when we have hydroelectric power it comes down to about 15% and in worst case can go up to 16% to 17%. So I think 16 on an average is a good number to work with.

Balachandra Shinde: Sir regarding the other expenses where you said the provisioning what we have done, is this is the only quarter where we did because again in that also we did see a good jump?

K. Srinivasan: See I think we have explained this. Provisioning is done as per policy every quarter, every year. What normally happens is there is a clear written policy which says that let us say receivables about one year is fully provided, non moving inventory beyond a particular period is fully provided, if it is slow moving it is half provided etc., this is the standard policy. In a stressed business condition even very, good customers who have retained some money and not paid it saying that we will pay after sometime etc., even there we have gone ahead and stepped to our policy and made those provision, which normally does not happen. I do not want to give names of big customers, but a lot of the big customers who eventually will pay they have not paid the full amount in the 365 days, so we have gone ahead and made provisions.

Sridharan Rangarajan: Another reason is that what we mean by higher provisioning is because our collections have stressed at this point the old dues have increased, so as the old due increases the provisioning also goes up, so that is how what we are telling as the provisioning is going up.

Balachandra Shinde: What kind of normalized margins we can see comparatively if we have to see because there has been a lot fluctuation happening in our margins for last four to five quarters?

K. Srinivasan: See the few things that we need to look at it definitely is that, one is volume related, largely in the ceramics and in abrasives this quarter again volumes have come down. By and large, I think we still maintain that abrasives on a long term basis, we should have somewhere about 10% to 12% we should have going up to about 14% which is our normal margin that we should have. Ceramics at this point in time has come probably the lowest at this point in time can come back to about 14% to 15%. So this is I would say it will take some short term to medium term it will take sometime to correct.

Balachandra Shinde: Last I would like to know like regarding each division wise what is your view in next 12 to 18 months both on our subsidiary levels and our domestic markets also, both international and domestic market?

K. Srinivasan: Abrasives is roughly about 75% India specific, but we are trying to sell more and more in export because Indian market we believe will continue to remain muted flat. We are not seeing any significant recovery that is likely to happen on a short term, so abrasives short term is scrappy volume growth, volume growth will come because we are fighting to take the lower end of the market. We also trying to take export market and I think the volume growth we will try and keep going, so I think that is basically what abrasives will be, but volume growth is reasonable to expect at least on the full year basis to at least 6% plus kind of a thing and going forward should be even a better volume growth. So that is as far as the sales top number is concerned. Rest of the abrasive sales in China, in Russia, etc., is all the fairly small part of it. It will continue to remain flat or grow marginally. So abrasives overall I would say about 6% plus growth on the topline, fight to get back to margins. Ceramic business and refractory business are going to be the two difficult businesses till project starts coming back. Ceramic particularly the group 1 which is the wear ceramic, which is largely dependent on coal washeries, power stations in India, in Australia, in US, etc., is going to remain a tough battle for the next at least two years. I do not think it is going to go way in hurry, because the coal prices are really low. So consequently there is a big push from the mining companies, not to spend money on maintenance etc. So there is going to be a battle, but it is also going to force us to do more of the value added ceramics, which is the high margin business, significant amount of effort is going there. So hopefully we should again get back there, but to get back to last years' sales numbers is our initial target because we are still below last year's number as far as topline is concerned. Here it is a very volume driven margin if I run my plant full I make better margin because the efficiencies go up tremendously.. The refractory business is about status quo kind of a thing at last year's level. There is no big piece outside India. The pieces outside India in the Russian part are largely selling into the aluminium industry. Aluminium industry is at its worst. We have never seen aluminium prices below this level for many years, 1750 per tonne is some of the lowest aluminium prices, so there again pressure on not spending money on maintenance etc. So refractory is going to remain a little flattish compared to last year. The Electro Mineral business is clearly where we think things have bottomed out. We are running reasonably flat in silicon carbide in Russia. The newer initiatives in India is catching up one-by- one though the industry to which they are selling is all under stressed condition. We have come out of the bottom effect of Electro Minerals because we came out of the downturn in the photovoltaic and other things. We have repositioned our business, so I think Electro Minerals would probably see volume growth as well as margin pickup. So that is broadly what we look at.

Sridharan Rangarajan: Besides this I think Foskor definitely is gaining strength.

K. Srinivasan: Yes because that is the new Zirconia business. There is value chain integration so clearly the Electro Mineral business will start coming back strongly.

Balachandra Shinde: So overall we can say that in FY 2015 there might be a growth of around 7% to 8% on the topline?

K. Srinivasan: That is a reasonable expectation.

Balachandra Shinde: Margins do you see any margin improvement from current means it will be at around 11.5% to 12% in FY 2014, so do we see any kind of margin improvement?

Sridharan Rangarajan: That is going to be the most difficult question. Hopefully we should see, because we believe overall I think we have seen bottoming out and hopefully things should get better.

Balachandra Shinde: Thank you very much Sir.

Moderator: Thank you. The next question is from the line of Kashyap Pujara from Axis Capital. Please go ahead.

Kashyap Pujara: Good evening to Mr. Srinivasan and Sridharan, and Raja Mukherjee. Just a couple of questions, firstly just to pickup where the previous gentleman left I think if you look at your overall revenues while you are down 40 or 50 Crores on quarter-on-quarter, your EBITDA is down 25 Crores and more or less you are seeing gross margins which you have expanded on a QOQ basis, so it is largely the fixed cost which are stubbornly sticky and whatever provisioning that you have done that is actually let to steep disappointment in your operating profits. So my question is that what is the normalized level of other expenses or cost that you see playing out going forward or do you see that the current levels are sticky and you do not see much change there and it is largely going to be if your revenues grow because that is where the operating leverage will deliver?

K. Srinivasan: See a couple of things we are doing. We are also using this downturn to go after fixed cost. We are not using any kind of a horizontal gelatin taking out cost ruthlessly because we still believe it is a growth business, we can do much better going forward, but we are definitely using the downturn to take out cost. I think costs are being taken out structurally, moving out people, reducing structure etc., are being ruled out. this will sort of at least ensure that the cost does not grow from here so that is one thing definitely that will happen and there will be a slight reduction in fact going forward in terms of fixed cost. But a part to this fixed cost like you said is also coming out of operations, which is really the provisioning and those kinds of thing, those are things which is very, very dependent on what is happening out there in the market. That is something which we hope things will get better.

Sridharan Rangarajan: The normalized I would say the cost should be in the range of about 25% to 26%, the other cost.

Kashyap Pujara: Now coming to your abrasive segment while on a consolidated basis the way it appears at a 13 Crores drop in sequential revenue and exactly similar drop in operating profit has shaped out as a consolidated level, but if I dissect it I think Russia which is the international piece has gone from a positive probably 4 Crores in the last quarter to a negative 3 Crores on a similar revenue. So that is a reasonable swing that you had and I think on a standalone basis probably I have not seen Carborundum report these low margins on a standalone abrasive front since I do not remember when I last saw these margins. I am trying to understand what is it that is the price volume being managed well or is that we are trying to focus on volumes and probably ignoring or slightly being circumspect on the pricing front? Is it possible to rather focus on pricing and retain trying to give up some volumes because the lower end of the markets anyway will come back to you when the industry swings? There is no point competing at the lowest spectrum, so trying to understand what is your thoughts on this front?

K. Srinivasan: You made a valid point when you said you are seeing the lowest margin on a standalone in abrasives and I accept it. I have not seen such a low margin. There are two to three things which are adding up to this low margin. One is like I said that there is some amount of conscious effort to focus on volumes to keep the lower end of the market. The volumes have really not come in the customer end. There has been a tremendous cutback on buying from the automotive, the project people. A big part of the bonded business largely goes on the project, which is the fabrication industries, project industries and selling to them is actually giving away money because they are not paying in time. So to keep the plants operational we have consciously gone into lower end of the market and there we have picked up volumes, and at many cases we have picked up volumes at very low prices, amazingly low prices, so you are seeing that effect actually playing out this is one part. So that is what we said unfavorable product mix. The second thing we also seeing certain level of provisioning that we have gone ahead and done. Things those are not moving for payments that have not come beyond particular points we have gone ahead and made this provisioning. The third thing we have also seen playing out is there is an upfront cost that we have invested on trying to get into export market. Like you rightly said we cannot keep doing only this low end business because this plant and all our investment in towards addressing premium markets. So a lot of investments towards addressing the premium market in terms of putting out people, giving out samples, a lot of it is already there as cost into the system already. Like I mentioned our exports on a nine month basis has grown at more than 50% this is highest growth in export that we have seen in abrasives ever. Now a lot of it is upfront cost because these trials are giving out, samples are sent out and everything these are all fast, but I am hopeful that this will get converted into business opportunities at least in the next two to three quarters. So we do not think the Indian market is going to come back in any hurry. We think this is the longish term of downturn. It is not going to come back in any quick term. So in this context, the overall global market abrasive has not declined. Last year 2013 was the highest sale of automobile in the world. China hit almost 20 million pieces, US hit more than 14 million, and there was more than 68 million piece of car sold. So the grinding business per se has done very well. We have repositioned lot of our effort, handing out samples, putting out people, trying to address this big opportunities outside. Unfortunately our biggest market is the one which has performed the worst which is really for India, so that is why we are seeing one upfront cost of India trying to keep things going by addressing the lower end market on that shorter term basis, taking those market stresses in terms of provisioning all this happened in one quarter. Like you rightly said, this is the lowest margin we have seen in abrasive standalone and I hope that we never see this again.

Kashyap Pujara: Another thing is that the Russian front you had a swing on the same level of revenue. I mean obviously I am clubbing the other pieces of abrasive at the consol level along with Russia, so I am saying the balance the difference between consol minus standalone the same level of revenues I have seen a 7 Crores swing on a sequential basis?

K. Srinivasan: Abrasive we have two large distributors; one out of Ukraine and the other out of CIS country. I am quickly not able to say whether it is Belarus or the other one and there we have taken 100% provisioning considering the market condition this quarter. We do not think we will write off the whole thing, but since there is a stress business in those markets where we have made big dispatches in the last one year, we have taken the provisioning upfront. I hope to see how it works out.

Kashyap Pujara: Finally I mean you were also mentioning about your ceramics business, wherein you said that there is a lot pain in the wear related parts which are typically supplied to the Australia that is where the large market is for coal, but if I look at again the difference if your standalone business which is obviously 4% and the international business is yet at 19% margins?

K. Srinivasan: This is really where the volume kicks in. One tunnel is standing idle. One tunnel is running at miser mode that means I burn fuel to keep it running even if there is no production at 860 degrees temperature. Unless I ship my ceramics out to the coal business, be it in Australia, be it in US, be it in South Africa and others or to our own power plants and coal washeries in India the tunnel zones run, so I produce nothing and burn fuel.

Kashyap Pujara: When do you see these things obviously part is related to the market, but say some part especially in abrasives like you mentioned it will take two to three quarters, so can you expect a better product mix from the coming quarters because that itself will give you lesser provisioning also the low end of the market will typically be more time consuming to recover from as well, so will you in the next three quarters or so will be able to see a calibrated move towards the higher margin outlook in the segments?

K. Srinivasan: I believe Q4 onwards things will get better and you should see it getting better and like you said we should come back to the 14%.

Kashyap Pujara: I will just take one last question, where do you expect your normalized tax rate to settle down over this year end next year if you can give a two to three year outlook as to how your tax rate is likely to shape up?

Sridharan Rangarajan: Since you are talking normalized and long way outlook a three year timeframe is probably reasonable to assume because we are looking at few entities which will take sometime for us to get back to normalcy and coming back to the profit level, so on a three–year timeframe it will become normalized. Our effective tax today is around 40%.

Kashyap Pujara: That is all. Thank you so much and all the best.

Moderator: Thank you. The next question is from the line of Jasdeep Walia from Kotak. Please go ahead.

Jasdeep Walia: Could you briefly touch upon what is happening in your various international subsidiaries starting VAW, RHI and Foskor? Sir just I need your perspective on volumes how has been the sequential movement in volumes and how do you see the volumes in margins going forward in the subsidiaries?

K. Srinivasan: I will start with Volzhsky. Volzhsky did highest tonnage last year. We did approximately almost about 72000 tonnes probably the highest tonnage wise we ran it flat. We produced again the highest metallurgical grade silicon carbide, shrunk dramatically on crystalline. There is a small increase in the prices of all the products, which means clearly things have bottomed out. We are approximately on an average price basis coming back to a one year old price after going down very steeply, but that alone does not give any kind of a comfort because the power cost one year back was approximately for us 1.5 Ruble today even at lower price is about 1.8 Ruble, so there is a big power cost increase largely compensated by a lower price of pet coke again the competing industry being aluminum industry not doing well. Pet coke is available at record low prices, reasonably low prices of other input materials, so consequently I think it is a bad story in the sense the margins are okay, volumes are running flat, we are still not going ahead and making a big investment simply because that the premium products are still not coming back. We are running it flat, but the overall tonnage of silicon carbide produced in the globe has not gone up, still significant idle capacities exist in China and others, so consequently we are keeping it flat, now that is as far as Russia is concerned.

Jasdeep Walia: So what have been the margins this quarter let us say versus Q2 FY 2014 and how is the trend going forward?

K. Srinivasan: I will quickly cover the overall business and then I will come to the margins. Foskor Zirconia again volumes are coming back. We almost did 900 tonnes this quarter, which is again coming back almost a four, three or five quarter high. We were not at 900 for many, many quarters back and out of this 900 about a 150 odd tonnes of bubble is there as well. So it is really a good sign. Going forward if we start hitting 1200, 1500 and then higher than that it will be a big boom, because we start making money. The plant is stabilizing, the bubble is getting integrated into the next line customers which is both EMD at India as well as Thukela who do further value added products so to that extent Foskor is coming back, the new leadership thing is settled, technical problems are being ironed out, so hopefully they should come to profit as soon as they start looking 1200 tonnes quarter onwards.

Orders are there. Customers are picking up, price is stable, sand prices are reasonably low, so again the business has bottomed out and I would think only positive about what is happening in Foskor Zirconia. Thukela refractory have got orders for RHI, tonnages are available. The team is now settling down to a new rhythm. Hopefully Q4 should get better. We should start hitting at least about 2000 tonnes plus from this quarter onwards. So that will really take us to at least lower losses, but the old depreciation and the inventory write down would take another two quarters to come back to normalcy. But otherwise I think operationally we should get better in Q4. That is as far as three mineral businesses are concerned. Margin wise overall Electro Minerals I think we have been that we will get back to about 15% once the volumes start picking up and I think we are working towards it on an average basis because it all moves between companies.

Jasdeep Walia: Also these days we read in the media that Europe is improving considerably so PMI indicators in Europe are up to I think around 53 to 54, so could you just take us through your first of all what is your overall exposure in Europe in what all segments and do you see an opportunity to scale your revenues in Europe and let us say in the coming one or two years?

K. Srinivasan: This year roughly about 46% of our revenue will be India, about 24% to 26% will be Europe including Russia and the rest would be the other places, US, Australia and other things. As we see in our business, things are getting better, but getting better slowly. A couple of reasons why I am saying slowly is for us to access Europe in each one of product group there are separate efforts, so example to sell silicon carbide, to sell grinding wheels, I have OSA registration and other things and the scale up is going to be slow. We are through most of it so for me Europe being important scaling up also is going to be that much more time consuming.

Jasdeep Walia: Sir also could you talk about your exposure in various segments to Europe?

K. Srinivasan: The big part of what we sell in Europe is really the mineral business.

Jasdeep Walia: Let us say Europe revenues are 100, so could you break it up into minerals, abrasive and ceramics?

K. Srinivasan: Our overall sales 25% to 26% is Europe and out of it almost 80% will be mineral. Only in ceramics we sell a little bit, ABB and abrasives, about 80% of mineral is a fair number.

Jasdeep Walia: That is all from my side. Thank you.

Moderator: Thank you. The next question is from the line of Ram Hegde from Primus Investment Advisor. Please go ahead.

Ram Hegde: Two questions, one is could you quantify the provisioning that you have done in the first nine month period and how is it Y-o-Y?

Sridharan Rangarajan: Ram generally we do not share specific information as to provision. This is not a big number.

Ram Hegde: Second was could you give a sense of the utilization levels across your each division on a consol basis?

Sridharan Rangarajan: I think in the ceramics it will be around 50% to 60%, both refractory as well as industrial ceramics; abrasive would be about 75%, electro minerals will be 85 plus.

K. Srinivasan: If you take Foskor now less than 50?

Sridharan Rangarajan: Foskor, TRI and all less than 50.

Ram Hegde: The other was the you hinted that abrasive the mix change has really impacted your in the margins again any sense in terms of the commoditized end of it what typically was the percentage of the abrasives and what it has gone up? How has that moved?

K. Srinivasan: We explained a little bit like this. We have supplied out of trade or out of China that is the market that we have taken and we have taken at very, very low margins at this price, not that that market is growing, but at some market we are forced to take because the other end where we sell to the automative manufacturers and others actually that has shrunk in the last one year.

Ram Hegde: Lastly on the bubble scale up really, if I recollect Q2 was around 100 tonnes this quarter you said is 150?

K. Srinivasan: 150 plus, I think we really did about something about little more than 150.

Ram Hegde: Just in terms of scale up is this as per plan?

K. Srinivasan: We are way behind plan. We should have hit almost about 100 tonnes a month. We had quite a few technical glitches. We had acceptance issues etc., but I think little bit though quite a few things came as surprise we have seemed to solve everything so I am hopeful that we do better in Q4.

Ram Hegde: This month you have seen a lot of currency movement especially in the emerging market anything that you think would impact you all getting into this quarter?

Raja Mukherjee: Forex is the specific line you can see for yourself which is not a big number, but on a translation basis I am talking the topline roughly about 1.9% on YTD basis at a consolidated level is the benefit that we got.

Ram Hegde: That is it from my side. Thank you.

Moderator: Thank you. The next question is from the line of Ravi Purohit from Securities Investment Management. Please go ahead.

Ravi Purohit: Thanks for taking my questions. Just two of them, one was if you could elaborate a little bit on the abrasive market in India, in the sense you mentioned that we have focused on the low end of the market because the high end of the market has shrunk, but can you just throw us some more light on the high end of the market? Has there been increased competition from let say 3M which hitherto was probably present in certain niche areas? Are they coming in or they have been newer players getting into that segment because virtually all along this has been like a two player market so far, so is it that competitive intensity in the high end of market has increased?

K. Srinivasan: Let me explain it like this rather than using the word high end I would say like this there are some segments of market, which have not grown at all in fact they have shrunk. For example the industry, which consumes a lot of this thin wheel, is the fabrication industry going connected to the projects and other things. Now this has seen one of the lowest sales this year primarily because most of the projects are either are under standstill and not being completed. So this is largely using what is called a flexible disk, DCs and thin wheels, it is not a high end in that sense but this is a project business and that market has seen actually degrowth after many years. So that is the volume that is disappeared. On the other high end as you would call it as the automative nonstandard customers who take specialized product, this has seen degrowth again. Degrowth between 10% and 25% in different products. All this combined means and all these products are valuable products, they make decent margins on these products. This is being compensated by what is called as trade product, sheets, papers, things which run on the paint counters, on the hardware stores and other counters as well as for smaller customers etc., those are products, which are traditionally not which makes good margin and these are not our core products. We participate in a premium end of these product but today we have gone ahead and taken every thing that we can in this markets simply we see that we do not loose volumes our plant keep running, because a part of the plant cost is semi fixed. The furnaces run they run, whether you fill it up with your product or you do not fill it up with your product, they still consume fuel. So we have just filled up these furnaces and other things which means the overall average margin has gone down relative to sales, but hopefully things should get back once the product mix shifts to a more favorable mix.

Ravi Purohit: Actually, I was coming from the point that in many industries in India in the fast moving industrial good space is where they have got two or three players and there are couple MNCs who entered at a later date, so the market to adjust these new players the broader margin of the overall industry tends to shift downwards, so I just want to kind of understand is that something that you are seeing?

K. Srinivasan: There was no competitive pressure from 3M on the contrary they seem to have actually withdrawn in some areas. So no competitive pressure coming in from any of the name that you have mentioned

Ravi Purohit: Sir the second question is on the refractory business. I think in the previous call you had given a fair bit of insight into your entry into refractory business. I just wanted to get a little bit more insight in terms of what specifically are you looking at in the refractory business? Is it are you targeting the steel industry, are you targeting the glass industry, are you targeting cement, also within refractories there are whole host of refractories like flow control, monolithic, so if you could just throw some light of what exactly are we looking at in the refractory space?

K. Srinivasan: See basically 70% of the refractory is consumed by the steel industries and our new two tie ups that we mentioned are primarily to address this industry. The steel industry itself is not doing as well as it used to, but still consumptions are reasonably robust though the margins are drying up because they in turn are also under pressure. We addressed all the industries that you mentioned. We have again all the products with these new types we make fire refractories, we make flow control with the tie up that we have with TRI investment, we make fiber refractories in the joint venture with thermal ceramics, which is Murugappa Morgan Thermal Ceramics. We make castable refractory in the Jabalpur factory as well as Ranipet, so we have a complete range of refractories. We also address glass and cement and in each of these industries we have unique advantage compared to the others thus each of them have a first part which is the coal part, which is wear systems which uses ceramic, then in the hot part to use the refractories, so we are into both of them. So we have a package for these industries, we work with these industries and we are hoping that each of these industries today are not spending enough money because they are going through their own downturns and cycles, but things will come back.

Ravi Purohit: Thanks for you time and so much insight in all the calls. Thank you Sir.

Moderator: Thank you. Next question is from the line of Kashyap Pujara from Axis Capital. Please go ahead.

Kashyap Pujara: I just have a followup question. Regarding the EMD division again I think the standalone margins were in the range of 11% for the quarter, so there is significant improvement on a YOY basis when you actually hit the bottom in the EMD business in the same period last year. Now having said that okay on a sequential basis though it is low but what I wanting to understand is if I look at your consolidated difference then the margins in EMD are in the range of 6% it is more or less similar to last quarter? Now wanted to understand, if we could give a breakup just to what is the margins currently that are playing out in Foskor, and how are you in so that we get some granularity as to where the pain area is?

K. Srinivasan: Largely if you see I think your question is more in terms of the consolidated while standalone seems to be better and the consolidated numbers are not that side. That is where you are coming from?

Kashyap Pujara: I was trying to understand if we have to go towards say 15% what really needs to be done because in India there was a structural change and you are trying to resolve that by doing a new facility in Kochi and you are still at 11% there, but your international to move from 6% to say double from there or say 14% to 15% we needed to understand where is your different segments at and we can then critically look at which basis we need to move?

K. Srinivasan: The biggest piece that need to move is at this point in time is Thukela refractories and the second one is Foskor. The Foskor we feel that we are on track. We see signs of improvement, quarter-after-quarter we see signs of improvement, if we have the numbers that we are looking at Q4 we may have better numbers coming from Foskor that is one portion of it. The second portion is the Thukela portion, but for these two on the Electro Mineral outside of India we are in good shape. There is no challenge and continues to be in good shape and Thukela will give or take about one to two year timeframe by the time we have the volumes coming from RHI business as well as repositioning to some of the outside customers. So that work is still in progress, so once we have that that is how we said that we will have two ranges, the mid term is about 15% and then we can get back to about 18% to 19% in about three to four years' timeframe so that is how we are looking at, both Foskor as well as Thukela losing money at this stage that is the reason why you are seeing this kind of negative effects.

Kashyap Pujara: Absolutely I understand. Now the point is that in Thukela the RHI had a certain level of minimum volumes which they had committed.

K. Srinivasan: They have given the orders. They have gone back and started giving the orders. They are coming out like you said Europe is getting better, they have started feeding orders so orders are coming in now. So hopefully Q4 onwards thing should get little better, but like Sridhar explained it will not like it, it will not switch on to immediate profit, it will go through as far as we still have a high depreciation that has to go out of the system and then will start coming into process.

Kashyap Pujara: But as a trajectory it will be on an improving trend?

K. Srinivasan: Absolutely, absolutely we still have at a good run. South Africa delivers power at 0.6 Rands. Rs.3.60 I do not have to have a generator, other than Russia that would be still a good place to put power dependent projects. From Russia it have to get a mineral out to any part of the world it is a $140 per tonne. I can get material out of South Africa into any parts of Europe at $60 to $70 a tonne. It is structurally a very good market to be in. We are fighting it out because we are going through. We went into it at a time and everything went down, so we have to have the patience to build it back but it is a good place to build the business back again.

Kashyap Pujara: Fair enough, and in terms of Foskor again to some extent, the improvement would be intertwined to your domestic bubble Zirconia plant as well right?

K. Srinivasan: Value chain integration, a part of it moves into micronizing and to our alumina Zirconia, a significant part to move into Europe for other applications which is also tested out and we are getting orders from there as well.

Kashyap Pujara: So there you do not see much of the challenge internally like say Thukela to that extent dependent on external RHI taking the order, but here Foskor is more internal focus wherein you can improve, so how fast can we get our act there?

K. Srinivasan: Hopefully we should start seeing better numbers from Q4.

Kashyap Pujara: Lastly was about the currency like if I were to look at it I think your production across most countries are typically in the emerging markets and most of them would have devalued against the dollar and the Euro in that sense, so what is the kind of are you typically seeing more traction on business front considering that you are a net exporter from all these regions that is one?

K. Srinivasan: We are finding ourselves being more competitive than we were a year back, be it out of Russia, be it out of South Africa, or be it out of India.

Kashyap Pujara: Thanks. That is all from my side.

Moderator: Thank you. That was the last question I now hand the conference over to Mr. Jasdeep Walia for his closing comments.

Jasdeep Walia: Thank you everybody for participating in the call. Have a good day ahead.

Moderator: Thank you. Ladies and gentlemen on behalf of Kotak Securities Limited that concludes this conference call. Thank you for joining us and you may now disconnect your lines.