"Carborundum Universal Limited Q2 FY18 Earnings Conference Call"

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MODERATOR: **MS. BHOOMIKA NAIR – IDFC SECURITIES**

Moderator: Ladies and Gentlemen, Good Day and Welcome to the Carborundum Universal Q2 FY18 Earnings Conference Call, hosted by IDFC Securities. 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 telephone. Please note that this conference is being recorded. I would now like to hand the conference over to Ms. Bhoomika Nair from IDFC Securities. Thank you and over to you, ma'am.

Bhoomika Nair: Good morning, everyone. On behalf of IDFC Securities, we are hosting the Carborundum Universal Q2 FY18 Earnings Call. The management today is being represented by Mr. K. Srinivasan – Managing Director; Mr. Sridharan Rangarajan – Chief Financial Officer, Mr. Raja Mukherjee – Senior General Manger, Internal Audit and Strategy.

I will now hand over the call to Mr. Srinivasan for his initial remarks. Post which we will open up the floor for Q&A. Over to you, sir.

K. Srinivasan: Good morning, Bhoomika. And good morning to all of you. Thanks for joining us on this call.

Let me start by saying that we had after a quite a few quarters, an eventless quarter where things were all back to normal. Consolidated sales grew to nearly Rs. 579 crores, which was up 13%. Standalone sales grew Rs. 385 crores, again up 10%. Post tax profit on consolidated grew to Rs. 55 crores, which is up 38% compared to sequential quarter, and post tax profit on standalone grew to Rs. 32 crores, which is up 24% compared to last year quarter. It was a good quarter where things are all coming back to normal. Business across all major geographies was good, there was a pickup in Europe, pickup in the American markets, pickup in India as well. So it was a good normal quarter after a long time.

If I go to the segments, Abrasives had a consolidated sales of Rs. 259 crores, up 12%. Electro Minerals had a consolidated sale of Rs. 217 crores, up 20%, this largely comes with a higher volume in Russia. Ceramic, Rs. 121 crores, up 5%. All the three segments did well.

The Abrasives segment is notable for the fact that it did particularly well in the domestic market, because we had, as you know, in Q1 the GST impact, so the channel had a significant amount of destocking. So, the channel has started to restart, it is still not at a level it was traditionally used to be. So, if I have to evaluate the stock in the channel, it is still below the normal average. So we should expect further stocking to happen during Q3, Q4.

On the Electro Mineral, the significant part of the growth really came out of volume growth in Russia where we did approximately about 7,000 tons more. This, as you would know, was largely because we did less production in the previous year out of a power outage in the main grids. There was also volume pickup in the domestic segment in the Electro Minerals.

The Ceramics business was muted, both in domestic, in exports and in the international market because it is project driven and these are still to pick up.

So, that is broadly what the businesses did. We spent a CAPEX for first half year of about Rs. 35 crores on the standalone and Rs. 52 crores on consolidated basis. We seem to be in-line to do about Rs. 75 crores to Rs. 100 crores that we have been talking about. Debt equity is almost at the lowest ever.

And now I will hand over to Sridhar to take you through with the numbers. Sridhar?

Sridharan Rangarajan: Thank you, sir. Good morning to all of you. I think we have good set of numbers, we will quickly walk through that. On a quarter-on-quarter basis at consolidated level we registered a net sales growth of 66 crores, this is after eliminating the excise, both the periods, with the operating PBT growth of Rs. 18 crores. The PBT growth came due to lower interest cost of Rs. 3 crores, lower foreign exchange loss of about Rs. 3 crores and we also had offset by lower other income of Rs. 6 crores. The entire PBT growth of Rs. 18 crores is then coming by way of higher volumes. If one looks by entity, then Standalone PBT were up by Rs. 8 crores due to higher sales of Rs. 35 crores. Subsidiaries PBT increased by Rs. 13 crores due to higher sales of Rs. 32 crores, largely coming from VAW's top-line growth and Sterling Abrasives as well as CUMI Australia doing well. JVs and associates profits were lower by Rs. 3 crores.

On on a sequential basis at consolidated level we registered a sales gain of Rs. 67 crores and a PBT gain of Rs. 26 crores. The movement in interest cost and foreign exchange loss was almost nil. Power and fuel cost was lower by Rs. 1 crores, despite higher volumes. So the entire PBT growth of Rs. 26 crores came by way of higher volume and better leverage. The entire gain came from better performance of CUMI's standalone business.

On an YTD basis at consolidated level we registered sales gain of Rs. 80 crores which is 8% growth and the PBT gain of Rs. 15 crores. Increase in power cost, which is one of the substantial number if you look at YTD basis, largely coming from higher volume in VAW by about 7,000 tons. And then the local power tariff, 25 paisa, it has gone up, so that is one reason. As far as Maniyar power generation is concerned, it is almost same comparable to last year, which was almost 30% lower than the prior year.

So, entity wise the entire gain came from the better performance of VAW. And as Mr. Srinivasan said, last year we had due to power outage a lower volume, and that is offset and we have also gained there some more volume and that is how we are doing better.

By segment, Abrasives PBIT margin Abrasives increased from 12.9% in Q2 last year to 10% in Q1 to 14.1% in the current year Q2. Now, whatever margin I am talking about is all net sales basis, that is after removing the excise on comparable periods. The margins have improved on the back of higher sales in standalone. Rs. 6 crores profit expansion on quarter-over-quarter and Rs. 14 crores on sequential basis is all coming purely from standalone.

As far as the Electro Mineral business the consolidated PBIT margin of EMD went up from 13.4% in Q2 last year to 13.8% in Q1 of the current year, to the current quarter of about 17.2%. Again the better performance is purely coming from VAW's better business, 7,000 ton higher volume.

As I said that the power cost going up is a factor of three things, one is higher volume in VAW, KSEB power cost going up by 25 paisa and higher volume production here in standalone business. Sequential growth of PBIT of Rs. 8 crores came by way of Rs. 7 crores from CUMI and rest from VAW and Foskar in South Africa.

For Ceramics, the consolidated PBIT margin of ceramic was at 13.9% compared to 14.8% in Q2 last year and 14.1% in Q1 current year. Industrial ceramics business had a very good growth in the current quarter, however the refractory business we expect a better performance in the second half because of the postponement of few projects.

CAPEX, so far we have done about Rs. 52 crores and we will be in the range of about Rs. 75 crores to Rs. 100 crores as of full year. And as far as debt-to-equity ratio, we are at about 0.1 at consolidated basis and net of cash and cash equivalence, probably we are almost debt free at this point in time.

So, that is a broad summary of our results. We expect broadly in trajectory to so far whatever we have communicated for the full year. We will now open up for question-and-answer session.

Moderator: Thank you. Ladies and Gentlemen, we will now begin with the question-and-answer session. We take the first question from the line of Balchandra Shinde from Anand Rathi. Please go ahead.

Balchandra Shinde: Sir, regarding Abrasives as you said most of the growth was due to destocking. If we want to bifurcate in the growth prospect wise that how much was because of restocking and how much was because of demand improvement? Because after few quarters that restocking scenario will go away, so would like to know how you see the demand improvement side.

K. Srinivasan: I can give you a very broad idea that we have about 30% of Abrasive sales going to direct customer. And this has also grown by at least about 10% to 12%. So, with that action I would take it that a lot of it is also by demand improvement. Restocking practically happens only in one month out of three months, that is why I said you will see restocking go up during the next two quarters as well.

Balchandra Shinde: Okay. And sir, on the channel side, how are you seeing the GST implementation being going? Because I have heard that most of the distributors are facing problem because of slightly stretch on their working capital side or credit. So, are we giving any discounts or relief to the distributors to that end?

K. Srinivasan: We mentioned even in the last quarter that we were not giving any kind of a discount or doing anything to help the channel in terms of handling GST because this is a normal process that they would have to find their way to do. We did provide them technical assistance and support in terms of understanding and implementing GST at their end in terms of registration, in terms of trying to understand how the whole thing can be organized. Beyond that financially we did not support them. We will stay with that principle as well. To your first question, in terms of how the channel is handling the GST, I think there are two tiers all these channels. The part of the business that handles the formal goods, all our products, they have been able to adapt it pretty quickly. But one tier below and in parallel in most of the cases there is a informal channel of sales that has always been there and that part of the business has still not found a way to handle the whole thing. And this is not going to happen easily, it will take its time, we will have to find a way to manage the whole thing.

Balchandra Shinde: Okay. And sir, in Electro Minerals just would like to know that as the commodity prices are going up in most of the commodities, so how the silicon carbide prices have moved up? And if we see in our growth, how much will be because of price increase and because of volume increase?

K. Srinivasan: In Q2 practically there has been no price increase in silicon carbide part of it. We are not seeing a significant price growth in silicon carbide, this is pretty unusual, I expect this to correct in the next couple of quarters. Every other Electro Mineral input as well as Electro Mineral product, like you said all commodity materials, prices have gone up significantly. To give you an idea, all the input materials biggest growth has been in the carbon based products like graphite where the prices have gone up seven times, or more in this case. And all the input raw materials like zircon sand and bauxite everything is up anyway between 10% to 30%. So there is a significant input increase, partly translated into prices increases, most of it is yet to be seen in terms of hitting the sales and margins. So you will see that happening in Q3, Q4.

Balchandra Shinde: But are we passing through this input increase or it is…

K. Srinivasan: Yes, we are desperately trying to pass as much as we can. And like you know there is always a lag, so Q2 did not see too much of a pass through, we expect a bigger pass through to happen in Q3 and Q4. Because our cost increase has also been calibrated because we did have some amount of old inventories.

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

Kashyap Pujara: Just couple of questions. Firstly, I have seen 14% margins at the EBITDA level, segment margins for Abrasives after a stretch of five years. So, really encouraging to see that number, the last time we clocked this was somewhere around 2011-2012. So, are these margins here for good and are they sustainable, I reckon that there would have been price increases also which we would have taken up, so do we assume that markets are willing to absorb the price increases which were pretty illusive last couple of years?

K. Srinivasan: First is, I think these margins are sustainable and hopefully should improve. A couple of points, one is, so far there has not been any major price increase, there have been minor price increases. But I think in the next two quarters we will have to put up prices further and this price increase has to be absorbed by the market because this is based on a strong input cost increase that is happening from the Electro Mineral side. And the buyer of Electro Minerals are not only our internal customer Abrasives, but also our competitors. So, to that extent it is secular, everybody is going to have higher cost, and everybody has to correct prices. It is also impacting imports, both the high and low end products, far more significantly because Euro is strong, and also significantly impacting the low end products coming from China. So, this price increase is here to stay, there is going to be a massive increase we push on Abrasive pricing in India.

Kashyap Pujara: So, essentially since FY10 if I were to have a look, the peak margins for the full year that Abrasives division as a whole has clocked has been 15% at the consolidated level. So, obviously, we have seen 16% margins also but that has not been sustainable throughout all the quarters. And obviously this 15% would include the drag from Russia back then, so to that extent the domestic margins should have been better than 15. So, in all probability now is it fair to assume that Abrasive margins can move north of 15% - 16% over time?

Sridharan Rangarajan: Kashyap, I think let us split this into two parts. The first portion is relating to standalone which is the biggest driver of the margins. Now on an YTD basis the standalone margin for us is 13.5%, the reason I told YTD is because we had a Q1 lower and we have pickup in Q2. And I am doing this margin calculation on net sales basis, without excise duty for simplicity, apple-to-apple comparison. Now, this 13.5% we expect could be in the range of 14% to 14.5% at the year end on a full year basis at the year end. So, this is what is on the standalone basis. But on a consolidated basis for the full year which is predominantly a portion coming from rest of the businesses, I feel that we can be in the range of broadly, I am giving you a broad stroke number, should be in the range of about 12%.

Kashyap Pujara: 12% for international piece or for the consolidated piece?

Sridharan Rangarajan: Consolidated piece, it should be in the range of about 13%.

Kashyap Pujara: Okay. And secondly, if you look at the Ceramics side, that is the segment where we have maximum operating leverage from. And obviously due to the poor investment cycle the country has been in we have not seen any pickup here. So, what is your sense on overall demand, are we seeing demand coming back, are enquiries picking up, what is your sense? And this is one segment which can actually go back to 18%, 20% margins if we get the growth, so any thoughts on that?

K. Srinivasan: Yes, I will split this into two parts. In the Ceramics, the industrial ceramic part of it we would see pickup as we scale up our Metz II Plant and we get the volumes up. And you will see this happening in Q3, Q4. On the Refractory side, while we say that it will definitely be better than what we have done in Q2, major projects are still illusive. However, there has been certain amount of maintenance driven project happening largely around glass and carbon black industries, this is going to drive volume for us because these are critical areas for us in the refractory side, we have a good market presence, market share in this. And these people are doing well compared to the previous years, so they also are in the cycle where they need to redo their furnaces. So the glass and carbon black industry would drive growth for us in the next two quarters on the refractory business.

Kashyap Pujara: Okay. So, here what is the kind of growth outlook which one could paint in the segment?

Sridharan Rangarajan: So, in the segment at the full year, Ceramics, by and large we are looking at a growth of about say give or take about 18% to 20% growth we can look at it.

Kashyap Pujara: And that would definitely change the margin trajectory with that kind of growth?

Sridharan Rangarajan: Yes.

Kashyap Pujara: I have just one last question, and that is about the Electro Mineral side. Just some thoughts about how has the ramp-up in India for the plants that have moved here, how is that picking up, some update on that? And also, in between we were seeing a situation where semi-friable in the world were getting in to shortage and we were getting some pricing benefits there. So, what are your thoughts on what are the trends that are shaping up in the EMD front?

K. Srinivasan: Yes, in terms of the two plants that we moved, the bubble plant is yet to really get volumes, we have unusual challenges in terms of securing sand, securing electrodes, etc, but our product has been accepted, we are probably doing about 100 tons a month on an average where the plant should be able to do at least about 450 tons plus, 400 tons plus at least. So there we will probably see a full scale up and running flat out somewhere in Q1 of next year on running it flat. But the acceptance of the product is pretty good, we must also keep in mind the fact that the price of this product is simply galloping, the final product is already up by almost 30%, so it is really a market where the costs are going up, price is going up. The other plant really was to address the alumina, both white, brown, semi-friable, etc, there the scale up has been pretty good, we are almost running it now 60% plus and we expect that we will be running it flat out in Q3, Q4. So, volumes in EMD would go up and that would also mean better margins coming up.

Now to answer your question in terms of global positioning and pricing, this is now on the uphill, all the inputs are going up, including power costs, as Sridharan mentioned, it is going up in Russia, it is going up in India, the raw material is going up. So, we will see a massive uptick in the final product price. Would the market be able to give it? It will give it because everybody has got the same cost position, everybody's price is going up. Do they like to give it? They surely do not like to give it and they are not used to giving 20% - 30% price corrections to buyer being at the Refractory or Abrasives, they themselves are not used to giving these kind of corrections. So, it is a battle but it is happening and it is happening every day, every account.

Moderator: Thank you. We have the next question from the line of Nirav Vasa from B&K Securities. Please go ahead.

Nirav Vasa: Thank you very much, sir. My queries have been answered.

Moderator: Thank you. We take the next question from the line of Ujwal Shah from Quest Investment Please go ahead.

Ujwal Shah: Shridhar sir, just needed clarification on the results. In the consolidated results there is this item that may be reclassified to P&L in which we have exchanged differences and the amounts are there, this never used to be before. Can you just throw light what is this about and can it impact the P&L?

Sridharan Rangarajan: So, in the consolidated results we have put here items that may be reclassified to profit & loss, which is you are talking basically on the other comprehensive income. And then there are other items which are items that will not be reclassified. So, these are basically relating to the exchange differences in translation of our foreign currency operations, when you consolidate and hedges that we take. Now, once you realize this it can get back to the profit and loss account once, but I am saying the predominant portion of this is on the translation which will take long, long time unless you close down the operation it will not get into the P&L. So, for practical purpose you can assume that this will remain in OCI only.

Ujwal Shah: Okay. So, is it under the new regulation?

Sridharan Rangarajan: Yes, this is because of IndAS.

Ujwal Shah: Okay, fine sir. Coming to the business part, Ceramic growth in the first half has been quite sluggish and we are expecting around 18% to 20% kind of growth for the full year. Do you think second half would be that good for this division? And if yes, what is the margin guidance for the full year for the Ceramic part?

Sridharan Rangarajan: So, the Ceramics, actually you are right, the first half is muted. But what you do not see is that the industrial ceramics side of the first half has grown really double-digit growth. And refractory portion, we are in the negative and that is why you are seeing a muted performance there. So, with the new metalized cylinders line coming in and then we will start utilizing it, so we expect the second half of industrial ceramics to be better. And refractory, with orders pushed to the second half also will be better. And the Australia business continuing to do the way they are doing so far in H1, we expect the trajectory what we have shared with you.

Ujwal Shah: Right, sir. So, in that case what is the margin guidance from this division?

Sridharan Rangarajan: Ceramics, I expect it could be in the range of about 14.5% to kind of 15.5%, 16% that range it would be, depending on the volume it picks up.

Ujwal Shah: Right. Sir, on the EMD portion, at VAW we have achieved these higher volumes, are we running flat out over there and we were planning to debottleneck some volumes over there, so has that been undertaken already and can we see some more volumes kicking in from there?

K. Srinivasan: See, we are running it flat out as we speak, and this would take us to about 80,000 plus this year. There is an ongoing work, like we mentioned, to take it up to 90,000, that is a 10,000 extra over an 18-month project, because we actually are trying to increase output in existing operating furnaces, so it is a pretty complicated process both by looking from moving to DC power and all kinds of things. So there is a lot of technology that is going into it. This is ongoing, so this will gradually creep in. We said 18 months, we are already three months down this journey. This will gradually start creeping in quarter-on-quarter, so we will see that we realize this 90,000 ton existing location, existing place with the existing investment with only incremental things in terms of controls and other things. So, that is in process, we will have it in the next 15 months.

Ujwal Shah: And lastly sir, on the Abrasives side, if we look at the first half numbers for the standalone business, considering 1Q was the GST impact and 2Q has seen a recovery, based on our 1Q assumptions what is now our target for the full year for abrasives on the standalone side?

Sridharan Rangarajan: 8% to 10% volume plus price growth, put together 8% to 10% for the full year.

Ujwal Shah: On the standalone side you are saying?

Sridharan Rangarajan: Yes, on the standalone.

Ujwal Shah: And sir, on the consolidated if you can give us?

Sridharan Rangarajan: Consol, my guess is about 2% to 3% at best, because standalone is the biggest volume. And on the rest of the consol we do not have any, I mean it is a flat number, so that is how it will turn out to be in that range.

Moderator: Thank you. We have the next question from the line of Jasdeep Walia from Infina Finance. Please go ahead.

Jasdeep Walia: Sir, my question is on this Electro Mineral segment, why are the prices going up and what is your view on the sustainability of these price increases?

K. Srinivasan: Prices are going up largely on the back of increased input cost. Like I mentioned, all key inputs have gone up, including graphite which has gone up the highest. Is it sustainable? I believe this is a cycle, it will continue to go up, a lot of it will not come back, we have still not seen the peak prices, it will probably peak during the third or the last quarter of next calendar year, 2018. So you will really see pries continuing to go up. Some amount of trend is visible only after we finish the spring festival and the Chinese come back to work somewhere in March, April. Till the time we cannot say where it will go and settle. But these low, low prices are over, I think it is coming back to something which is realistic. Why it is going up? Multiple things, one, there has been an environmental clamp down, cleaning up of operations in China, I think that is one part of the story. A lot of these smaller ones were driving down prices are not going to come back ever, so in that sense some of this price increase is going to be a reality. The second part of it is also coming from newer applications which is taking up some of these key input material, for example carbon is the source for practically, in different forms it required for the battery manufacturer and that is a big business that is driving up volumes across the EV powertrain. So there some of them are events, some of them are trends, we would be able to separate out events from trends only as it evolves over the next two quarters.

Jasdeep Walia: Alright. And sir, you said that as of now Electro Mineral prices have been going up because of this increase in RM prices, but your margin seems to have improved significantly?

K. Srinivasan: The margin improvement comes from the Volzhsky's volume going up, so I think that we explained in the beginning, we have got a 7,000 tons of extra volumes coming in. So that actually significantly helped on the consolidated margins.

Jasdeep Walia: And you have been able to take price increases in the Electro Mineral segment to pass on this higher?

K. Srinivasan: Silicon carbide price increase is not happening, usually silicon price is flattish, it is going up but very, very small. So we probably think that will also go up after a couple of quarters, this is largely because there is significant amount of channel capacity available, channel stock available, but even this will play out.

Moderator: Thank you. We have the next question from the line of Rajesh Kothari from Alpha Accurate Advisors. Please go ahead.

Rajesh Kothari: In terms of margins on Abrasives side, as the domestic side of volume keeps growing at around 8% to 10%, do you think the margins on Abrasives side can improve significantly on a full year basis on a consol level?

Sridharan Rangarajan: That is what I just shared, standalone basis we could be in the range of 14% to 14.5%. On a YTD basis we are at about 13.5%. And that is why the movement from 13.5% to 14% - 14.5% is the reflection of that. So, on a consolidated basis we would be in the range of about 13.5% at best.

Rajesh Kothari: So, full year you are saying 13% - 13.5%, fine. And on Ceramic side, as your volume growth becomes 18% - 20% on full year basis why you are saying the margins will remain at 14% - 15% because that was even your last year margins, so is there any operating leverage which can improve your margins here?

Sridharan Rangarajan: Currently, if you look at our YTD margins we are operating in the range of about 14% and Q2 is about 13.9%. I am just talking about 14.5% to 15% range which reflects the volume growth whatever we are projecting in the second half.

Rajesh Kothari: And on Electro Mineral side, can you tell us what is the total, as on current basis as your old inventory gets over, what is the total raw material price increase?

K. Srinivasan: You are asking price increase for what we buy or price increase for what we sell?

Rajesh Kothari: Right now first for what you buy, on the raw material side.

K. Srinivasan: Okay. So this is different for different products, see the electrode prices have gone up from something like $2,000 a ton to $14,000 a ton on an average, so that is a different price. If you are talking about Zircon sand, it has gone up almost 30%. If you are looking at bauxite, though we do not buy a lot, we have to look at bauxite and alumina where price is up by 10% to 15%. So, I think different products inputs have taken different price. Power, like Sridhar mentioned, we have 25 paisa increase in Cochin where we consume about 120 million units, in Russia we have had another 18 kopeck increase where we consume about 650 million units. So, increases have been across the board on practically all inputs to different degrees.

Rajesh Kothari: Sir, on basket basis is it possible to get the weighted average inflation on RM side in Electro Mineral division?

K. Srinivasan: It will not make sense because different products consume very different kind of inputs. See, the Zircon, if you look at the biggest impact would be on the Bubble Zirconia where the sand has gone up 30%, electrode has gone up six times. So there you can say the input cost has gone up by almost 25%.

Rajesh Kothari: So you think that that kind of a price increase is now required to make sure that your margins remain at current levels?

K. Srinivasan: Yes, everybody has to do it and everybody is doing it.

Rajesh Kothari: So you do not see any risk to your current margins?

K. Srinivasan: There would always be this catch up, immediately the price increase takes time to get it through your customers. I mean, in between if you want to continue the supply you will have a margin decrease during the period, and we are going through that.

Rajesh Kothari: Okay. And last question is on FY19, would you like to give some outlook on FY19 on overall revenue as well as on overall margin perspective?

K. Srinivasan: Like we said in the beginning, I think we have had a couple of quarters which are largely driven by events. We still need to come to a point where we will start seeing trends, we are still moving quarter-on-quarter driven by big events. Let the F18 go through, F19 like we always give a long-term projection to get our capacity utilizations up. Inherently in all these businesses, I look at not only India but on a global basis, are all growing. Good sales up in US, Europe, US is up by almost 4.5% - 5% which is big, Europe is up by about 3% plus. So there has been overall significant growth happening in our space. We expect that we will do what we committed as Rs. 3,200 crores overall sales in the three-year projection that we will get there.

Rajesh Kothari: That is FY20 you mean?

K. Srinivasan: Yes, that is what we communicated before that.

Moderator: Thank you. We have the next question from the line of Bharat Sheth from Quest Investment. Please go ahead.

Bharat Sheth: Sir, in Abrasives we have seen this expansion in the margins and further we are looking on consol basis. So, can you give some sense to what exactly we are doing so that is helping, because one side we are saying that input cost is also going up still we are able to do. So, can you give some more color on it?

K. Srinivasan: Two things are happening, one, I think if you do not look at H1 but look at only Q2 on Q2, Q2 is I would say one of the quarters, like I said in the beginning, less event driven and more trend driven. And this is going to play out in Q3, Q4 and get better while margins will go up largely because we expect Q3, Q4 volumes also to go up. Second part of it, yes there is an input cost increase, but to that extent there will also be a price correction. So this is also being done and it is being done by the industry because this is secular, this cost increase is for everybody and across the globe.

Bharat Sheth: I mean, what exactly has helped, of course some more value-added product or that is helping us? Second thing, this unorganized sector, which is largely driven by the import, so because of GST they are down.

K. Srinivasan: I think, I have actually discounted both of this, I think, one is there is a significant amount of work going on new product, product improvement, etc, we continue to file patents, we continue to bring in new products, this continues to happen. But this growth that we have planned both in terms of top-line and bottom-line is routine standard growth and profit increase from volumes. As far as the imports from China and other things are concerned, this is continuing as usual, I mean nothing dramatic has really happened, people are finding their own ways to work with the new environment and I do not think the trade has given up on it, they are finding their own way. This has not stopped or nothing dramatic has happened in this so far.

Bharat Sheth: And sir on Ceramic side, how do we see in the next two, three-year time and how much would be really coming industrial ceramic vis-à-vis refractory business mix going ahead?

K. Srinivasan: See, the industrial ceramic part is gradually becoming two-thirds of the total and that will continue to get bigger with the metalized cylinder plant scaling up, they are getting new work on the engineered ceramic side. So this will remain two-third. The other one-third and that is reason why Sridhar has also talked in terms of not only volume growth but also margin growth as it picks up.

Bharat Sheth: And sir on the Electro Mineral side, how much can we read over next two, three years, I mean again from pure Electro Mineral commodity business to business mix in more value-added product?

K. Srinivasan: The only large capacity that we still would have to run flat out would happen in the next year first quarter would be the Bubble Zirconia plant. Otherwise most of our capacities by that time would be running flat. So, Electro Mineral, we would have to think through further growth projects and we will look at it in the next 12 months.

Bharat Sheth: And VAW side are we doing really some value-added products or it is a pure silicon carbide?

K. Srinivasan: In silicon carbide, VAW produces one of the finest silicon carbides in the world, it is the only plant of that scale and size in the world which offers water washed, carbon free, silica free product. It is a very unique product, so though we talk of it as if it is just the standard silicon carbide, the reason why they continue to run through capacities during good times, bad times, at all times is not just because they have a cost position, because the cost position only reflects in the margins, but the reason they sell out their capacities, the product that they offer is unique, differentiated and valuable to the market.

Moderator: Thank you. We take the next question from the line of Gunjan Kabra from Niveshaay. Please go ahead.

Gunjan Kabra: All my questions are already answered, but I wanted to ask, can you guide on this sector that contributes to significantly in the total revenue of Abrasive markets and Refractory?

K. Srinivasan: The biggest contributor to the Abrasives business would be the fabrication, construction kind of an industry which would be about 15% - 20%, I have included everything in that, including projects, construction. etc. Auto, auto component, bearing, all combined would be about the same, about 15%, rest are all significantly smaller.

Gunjan Kabra: And what about Refractory?

K. Srinivasan: In Refractory the single biggest piece for the industry is the steel making, 70% of all refractoriness goes to the steel making. But for Carborundum steel is not big, for us it is largely non-steel industries which I mentioned, glass, carbon black, petro chemical, etc, they are our biggest customers.

Gunjan Kabra: Okay. And sir, and in one of the articles you guided that you plan to venture into graphite and switches which would be used for electric vehicle, so is there any further development on that?

K. Srinivasan: I do not think we mentioned in terms of getting into graphite. But what we are working on is basically we work with different electrodes of carbon, we work with diamonds, we work with silicon carbide, we work with different forms of carbon. So, we are working, and we have a couple of patents coming up in this space. A part of these products would find itself into the power supply for the EV powertrain. We are working on this, this is still at a very nascent stage.

Gunjan Kabra: Okay. And sir, there are a lot of production factors in China in carbon and metal sector, so is there any production factor in Refractory and Abrasives also which can help us?

K. Srinivasan: The significant amount of production cut in China largely is in the polluting industries which is like we said in the beginning, the carbon electrode manufacturing has taken a significant cut, the bauxite industry has taken a cut, all of them are suppliers into the raw material side of our business. That is the reason why there is a price growth. It is also impacting Electro Mineral availability in the world, consequently there is also a price correction in the Electro Minerals that is happening.

Moderator: Thank you. We have the next question from the line of Ravi Swaminathan from Spark Capital. Please go ahead.

Ravi Swaminathan: Sir, on Abrasives segment you had guided for 8% to 10% growth in the standalone level, is it at a volume level or at a value growth?

Sridharan Rangarajan: I said that volume price put together.

Ravi Swaminathan: No, in the sense that prices there will be a significant increase in prices during the second half, even considering that we are getting 8% to 10% growth?

Sridharan Rangarajan: Yes.

Ravi Swaminathan: Okay. And at a consol level you are saying 3% growth?

Sridharan Rangarajan: Right.

Ravi Swaminathan: And in terms of power cost what are the initiatives that we would be taking to reduce the overall power cost?

Sridharan Rangarajan: One is that the hydel power project that we are looking at is one initiative that we are looking at. And the power cost increase of 25 paisa can probably be changed because as the power position in the India changes may be the government of Kerala could also take a relook at and think about it. But other than that we have very little leverage at this point.

Moderator: Thank you. We have the next question from the line of Ritwik Sheth from DU Finance. Please go ahead.

Ritwik Sheth: Sir, just a couple of questions. Sir, this Russia sales which we did, what amount would that be in the quarter?

Sridharan Rangarajan: Russia sales is about Rs. 135 crores.

Ritwik Sheth: No, just from this incremental 7,000 tons?

Sridharan Rangarajan: Including this is Rs. 135 crores, and 7,000 tons is for the half year and not the quarter.

Ritwik Sheth: Okay, so that would be around Rs. 10 crores - Rs. 12 crores?

Sridharan Rangarajan: We do not want to disclose like that.

Ritwik Sheth: Okay. Sir, and for Electro Minerals should we expect similar growth for H2 FY18 or it will be higher than H1?

Sridharan Rangarajan: So, the second half, see what will happen is broadly the seasonality of Russia business also will kick in, our Q3 is their Q4, they will be better; our Q4 is their Q1 is always lower because of winter, vacations and all that will kick in, so there will be some seasonality there. We have considered that and that is how we are talking about our numbers.

Ritwik Sheth: Okay, so it will be around H1 growth?

Sridharan Rangarajan: Growth wise I would say the standalone can be a better growth because we will have our alumina and Bubble Zirconia will do better in second half.

Ritwik Sheth: And just one last question, sorry for my ignorance on this, but the increases in price of our key raw material for Electro Mineral segment is neutral for us or positive or negative?

K. Srinivasan: No, I do not understand, neutral? I think we will have an effective input cost increase of all put together. And somebody else has also asked me, at least about 10% to 12%. So we will have to accordingly correct our prices.

Ritwik Sheth: Okay, so that we will be passing it on to the customer?

K. Srinivasan: Hopefully.

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

Farzan: Sir, this is Farzan over here. Would like to enquire about the hydel power plant which is coming up in Kerala, the 21 megawatt. So, what is the progress, are we on track?

K. Srinivasan: The hydel power plant is still stuck in the bureaucratic approval processes, we have not progressed. The allotment was done but that is being challenged by the KSEB saying that they have a right to get it and not the private sector, etc. So, this is stuck in bureaucracy and we are trying to navigate.

Farzan: Alright. My last question is on the capital employed from the segment of others, so why has that suddenly reduced, any specific?

Sridharan Rangarajan: Yes, I think you are looking at some Rs. 180 crores of drop, this represents the loan repayment from that period to this period. So that is how our debt has also come down significantly.

Moderator: Thank you. We have the next question from the line of Ashutosh Adsare from Sharekhan Limited. Please go ahead.

Ashutosh Adsare: Congratulations on good set of numbers. Sir, one question, sir could you share the Forex loss during the quarter?

Sridharan Rangarajan: Forex loss at consolidated level is about Rs. 4 crores to Rs. 5 crores, but let me reconfirm. If you have other question go ahead, I will reconfirm.

Ashutosh Adsare: Okay. And sir on this only, continuing with this, sir what is your hedging strategy going forward for FY18 or FY19, or broadly what is your hedging strategy?

Sridharan Rangarajan: See, our hedging strategy is on the net position, we take net cash flow position, minimum coverage is 50% of the net cash flow, that is how we always do that. So, that is our position and we continue to do that. The restatement what you are seeing in OCI is un-hedgable, that is why that is a translation difference hedging. So, that is beyond the hedging process. So our normal hedging happens is on the receivables payable position or say Capex position.

Ashutosh Adsare: Okay. And sir one more question on the China part, so could you just broadly tell how the Chinese subsidiaries currently now have turned from manufacturing to outsourcing one, so can you brief on that?

K. Srinivasan: Yes, they are doing well. They have got into the rhythm of selling more into the Chinese market and to Chinese customers. They are broadly in line to do about Rs. 40 crores in rupee sales for the year and they would get better going forward.

Ashutosh Adsare: Okay. So, sir had it been possible that if you had manufactured like Chinese subsidiaries there, we would have been getting more margins there right now?

K. Srinivasan: I think we were losing money trying to manufacture in China, I think I explained this in one of the earlier calls, the facilities that they have set up was predominantly to make low cost products for exports. And the product that we are currently selling into the Chinese market is premium product for the key industries, aerospace and automotive, etc, which we have no facility there to manufacture and they had to made and shipped out of India. So, it was a mismatch of what we were trying to do and what we had as investment there.

Ashutosh Adsare: Okay. Sir, could you just brief about the Abrasive sales between the bonded and the coated one, our sales mix broadly?

K. Srinivasan: It stays about the same, two-thirds is bonded, one-third is coated. Probably getting to more like 40% to coated now.

Moderator: Thank you. We have the next question from the line of Bharat Sheth from Quest Investment. Please go ahead.

Bharat Sheth: Sir, now coming back to three-year plan, earlier we were talking of Rs. 3200 crores to Rs. 3400 crores top-line, so with now new capacity addition and all, still we stand there or we are think we will be able to out pass the number that?

K. Srinivasan: We will get to that number, maybe we will get to that number a little earlier if these inflatory pressures continue. Like I said, Bharat bhai, what we need now is at least two quarters of trend to predict something more reasonable. We are being driven by a series of events that have either supported or derailed whatever has been happening in the last couple of quarters. Let us give it two quarters and then we will give you a very firm kind of prediction.

Bharat Sheth: And Sridhar, one more thing, I mean based on this current quarter EBIT number I believe that we are already hitting a 22% kind of ROCE. So where do we see ROCE in FY20?

Sridharan Rangarajan: Look, I think I would say on a consolidated basis we are not there at 22%, we still need to pickup that. But I think my guess is that in two years time we should be in the range of about 23% - 24% that is what I would look at it.

Bharat Sheth: And sir, can you elaborate a little more on impact of electric car on our company?

K. Srinivasan: See, it is a very difficult transition and I think we are all looking at things which potentially can happen. There are many, many schools of thought about electric car and the intensity at which this change can happen. Now what can this do, one, if we assume that half the total number of cars produced which is roughly about 85 million cars a year, if half of it were to change to electric cars the biggest impact would be on the auto and auto component industry which consumes abrasives. Like I mentioned in one of the early answers, roughly 16% of our sales is towards auto, auto component and this part of it would get impacted, that could be a reduction. Now, what is the redeeming, compensating factor. Significant amount, see for example to give you an idea, to compare an EV powertrain car to current IC engine powertrain car, the actual weight of the EV powertrain car today is about 20% higher, that means it has more material. We are basically a material science company, a lot of the material that goes into it, be it body parts, be it the battery component, etc, they all either need electro mineral inputs or a certain level of finishing. So to that extent we have done our numbers, we believe that net to net a transition to EV powertrain would be significantly beneficial to a material science company like Carborundum. Segmentally there could be a little more impact on bonded Abrasives, there could be positive impact on coated Abrasives, significantly positive on Electro Minerals, significantly positive impact on metalized ceramics part of Ceramics business, etc. So, overall, net-net positive for Carborundum.

Moderator: Thank you. We have the next question from the line of Manish Goyal from Enam Holding. Please go ahead.

Manish Goyal: Sir, on Electro Minerals, maybe I missed it, can you just guide for the full year what kind of revenue growth we can see on a standalone and consol basis?

Sridharan Rangarajan: Standalone I think should be in the range of about 20% in that range. Consol should be in the range of about broadly 18% and 20%.

Manish Goyal: And on margin side, sir?

Sridharan Rangarajan: Margin, I said consolidated margin about 13% in that range.

Manish Goyal: And standalone sir?

Sridharan Rangarajan: Standalone full year looks like around 7%.

Manish Goyal: Okay. And this can improve next year once Bubble Zirconia…

Sridharan Rangarajan: Standalone will improve year after next year, definitely it will improve. Once you have the capacity utilization going above 50% plus, it will definitely improve.

Manish Goyal: And sir on a consolidated basis for the full year last call we had guided for 15% top-line growth, in first half we are at roughly 8% growth on a net sales basis. So, we continue with that number?

Sridharan Rangarajan: Which segment you are talking about?

Manish Goyal: Overall growth for the company.

K. Srinivasan: Can I answer this like this, don't look at the first quarter because first quarter was event driven. If you look at the second quarter, the growth in the second quarter on a consolidated basis has been 13% at Rs. 580 crores roughly 13%. So, for me this is a more representative growth pattern, so I would expect that the growth consolidated for the company could be 10% and above, because we still have to have the legacy of the first quarter. So, as a consolidated basis for the year 10% and above.

Manish Goyal: And with better margins than last year of 150 bps?

K. Srinivasan: I am careful on the margin side, I am going to ask Sridhar to answer that.

Sridharan Rangarajan: By and large we should be in the range of PAT Rs. 215 crores to Rs. 220 crores, that range.

Manish Goyal: Okay. Sir, I am just wondering, because what we are basically seeing a price inflationary situation in second half, but that large part of the growth what we probably are talking about 10% is then probably volume growth share is looking to be muted in the times to come forward?

K. Srinivasan: At least in the next two quarters we have plugged in not any major volume growth either in Abrasives side or in the overall business, largely because we think that the India story is still to be understood. But we expect a marginal growth, 3% - 4% at least but price growth to power the rest.

Moderator: Thank you. We have the next question from the line of Balchandra Shinde from Anand Rathi. Please go ahead.

Balchandra Shinde: Sir, regarding Electro Minerals, as you said that we will increase our capacity by 10,000 tons over next one year. Don't you think that there is already a geopolitical risk for us because of trade sanctions in Russia, increasing the capacity there will create kind of a uncertainty for us more on that side?

K. Srinivasan: There is really no geopolitical risk per say in our business, this is a non-strategic area, there are no sanctions on this product. A significant part of what we make is exported to first world countries, it goes to Europe, it goes to America. So, I think that is not a big issue. Second is, we are not putting new Capex in to it, like I said this is an incremental improvement of existing operating plant to extract another 10,000 tons by modification in the electrical power systems, etc.

Balchandra Shinde: And sir, the carbon electrodes, means like the carbon components which you said related to lithium iron batteries which we may try over a period of time, what kind of Capex will be required?

K. Srinivasan: Too early, Bala. I will have to go through it a little more carefully, several patents have to be filed. And I would not even restrict myself to lithium ion batteries, it could be for various EV power sources. So, it is too early to talk of Capex. We at the moment at filing patents, we at the moment what I call is technology straight projects, right to play kind of bets that are being taken. So, we will come back when it is significant.

Balchandra Shinde: But do we have the products for that purpose or we have to develop new products?

K. Srinivasan: We have the basic competence to make carbon related products, because that is our area. We have been working in various electrodes of carbon and we are very strong in the way it is made. To give you a simple idea, synthetic carbon, graphite is made in the same process as you make silicon carbide furnaces. So, we are in this business, we have to see how to make a commercially and technically viable product.

Balchandra Shinde: But sir, as per the technological side, what I have seen is like if you get a normal coke or petroleum coke and if you want to prepare a synthetic graphite. Graphitization for synthetic graphite is much higher, means much higher requirement as compared to three, four months we require five, six months. So, your capacity gets reduced by that technology.

K. Srinivasan: Now we will have to appoint you as our technical advisor, that we have to do it offline now. Sorry, but I think really you have a lot of ideas and I think it is right, that is why I do not want to get into this discuss because there are other processes by which we will do it, we may not convert any of our silicon carbide furnace, that is why I want to be a little careful on what we talk about here.

Moderator: Thank you. Well, that was the last question. I now hand the floor over to Ms. Bhoomika Nair for her closing comments.

Bhoomika Nair: Thank you everyone for being on the call. Sir, thank you very much for taking time out and giving us an opportunity to host the call.

K. Srinivasan: Thank you. And thanks to all of you for patience.

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