DCM Shriram Consolidated Limited

Q1 FY14 – Earnings conference call Transcript
August 7, 2013 at 4:00 p.m. IST

Moderator: Ladies and gentlemen, good day and welcome to the DCM Shriram Consolidated Limited earnings Conference Call. As a reminder, all participants' 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 "*" followed by "0" on your touchtone telephone. Please note that this conference is being recorded. I will now hand the conference over to Mr. Ishan Selarka from CDR India. Thank you and over to you, sir.

Ishan Selarka: Good afternoon and thank you for joining us on DSCL's Q1 FY14 earnings conference call. Today we have with us Mr. Ajay Shriram, Chairman & Senior Managing Director; Mr. Vikram Shriram, Vice Chairman and Managing Director; Mr. Rajiv Sinha, Joint Managing Director; Mr. Ajit Shriram, Deputy Managing Director and Mr. JK Jain, CFO of the Company.

Before we begin, please note that some of the statements made in this conference call may be forward looking in nature and a note to that effect was included in the concall invite sent to you earlier. We will now begin the conference call with opening remarks from Mr. Ajay Shriram and Mr. Vikram Shriram following which we will have an interactive question and answer session. I would now like to invite Mr. Ajay Shriram to give us a brief overview on the Company's operations for the quarter ended June 30, 2013, and the opportunities going forward. Over to you, sir.

Ajay Shriram: Good afternoon ladies and gentlemen and a very warm welcome to DCM Shriram Consolidated Limited earnings conference call for the first quarter ended June 30, 2013. I will share with you our perspectives on business developments following which Vikram will take you through the financial highlights.

We are pleased to begin the year on a satisfactory note in terms of overall performance. We believe that this is a result of consistent efforts by the Company over the last two – three years to improve cost structures and operating efficiencies across all our businesses. Simultaneously, we have rationalized and restructured our operations to exit from segments that were not generating reasonable returns. The reduction in the overall debt has helped in reducing the financial charges also.

The Company recorded an EBITDA of Rs. 202 crore during the quarter, a growth of 20% over the last year. The PBT before exceptional items was Rs. 123 crore which was 41% higher than last year. Net profit for the quarter stood at Rs. 114 crore as compared to Rs. 31 crore in the corresponding period last year.

Let me now take you through the major developments in each business.

The Chloro-Vinyl vertical comprises of Caustic Soda & Chlorine in Chemical business and the Plastic businesses. As mentioned in the last call, the chemical business has been recording downward trend in prices. The ECU dropped by about 19% over last year and about 10% over the sequential quarter. However, there has been mild reversal in this trend in July supported by Rupee depreciation. The international prices are stable and thus we expect the price to be better going forward. The prices for Plastic were marginally higher and recorded further improvements in July this year. We have achieved substantial cost reduction in both, Chemicals and Plastic businesses with improvements in operating efficiencies and capacity utilization of all the plants including the power plants. The fuel and carbon material mix has been optimized to achieve cost efficiencies and economies. These efforts have helped in improving the margins for Plastics and mitigating into a large extent the adverse impact of drop in ECU prices of Chlor-Alkali. We aim at consolidating the gains of cost rationalization and take further steps to improve the cost structures in these businesses.

The Agri Input vertical for DSCL includes Bioseed, Shriram Farm Solutions and Urea (Fertilizers). With good monsoon in the country so far, the Agri Input businesses are recording positive demand movements except for some segments like cotton-seed, which is facing both market as well as regulatory pressures.

We expect Bioseed's business in India to deliver satisfactory performance during Kharif 2013. We expect satisfactory volume growth in all segments except cotton where the growth will be moderate due to shrinkage in overall markets. Our new cotton-seed hybrid launched in Central and South markets is showing good potential. We expect to register good growth in this market in the next few years. In the case of international businesses, we decided to take back all the unsold material lying with the trade in order to ensure delivery of high quality products to farmers at all times and strengthening the overall supply chain. This led to negative sales in the quarter; however, it will help in more sustained growth going forward. The profits are expected to be flat due to pressure on cotton-seeds and the negative sales in Philippines as explained earlier.

The Shriram Farm Solution business is growing in both, the value-added input as well as the bulk Fertilizers segment. The value added input segment grew by about 19% in the first quarter led primarily by growth in the seeds segment. The good monsoon should enable growth in other inputs during the second quarter. The Company has contracted for about 200,000 MT of DAP and MOP, which we plan to sell fully in Q2 FY14. This will be almost double of last year’s volumes. The business has seen delay in subsidy payment, which is adversely affecting the cash flow, growth and profits. We hope the situation improves going further given the criticality of timely availability of Fertilizers.

In the Urea business, the Company achieved satisfactory operating performance with higher capacity utilization and better efficiencies. This has enabled us to record moderate profits in this segment in spite of non-revision of the retention prices which are already delayed by over three years. The subsidy payments which were in arrears for long has been updated in July. We hope that the subsidy receivables will not go into arrears going forward.

The sugar business recorded negative margin of Rs. 171 per quintal for sugar season 2013 as compared to a positive margin of Rs. 211 per quintal last season. The industry is suffering from over supply due to higher domestic production and continuing imports at very low import duty. International prices are also low making the exports uneconomical. The sugar prices therefore, are likely to remain soft going forward in this season. The government is altering the regulatory framework in piece-meal rather than carrying out comprehensive reforms. The sales are decontrolled and are exposed to global competition with very low import duty. The cane price however continues to be set by the government primarily based on political considerations. It is however heartening to note that Karnataka had decided to rationalize the cane pricing system and Maharashtra is also moving in a similar direction. It is imperative that UP, which is the second largest producing state in the country, also takes similar steps at the earliest. The power generation and sales is also becoming less attractive with delays in payment from the UP State Electricity Board for the electricity supply. The Company therefore reduced the power generation and sold more bagasse during this period. Our focus continues to be on improving the cane availability and sugar recoveries so that we further improve the inherent strength of the business.

The restructuring and rationalization of Hariyali Kisaan Bazaar has been completed. We are now carrying out only fuel retail activities at 37 outlets, which are profit positive. Sale of surplus properties is in progress and we expect to make substantial progress in the next 18 to 24 months.

The Fenesta business has strengthened its presence in the retail segment over the last two years leading to satisfactory sales growth. It has also strengthened the order fulfillment process. These steps have resulted in better financial performance of this business.

Overall, we are confident in achieving good operating performance across all our businesses. The financial performance will depend on various markets and regulatory developments. We hope the UP government will follow a rational cane pricing system for the coming season and implement the recommendations of the Rangarajan Committee in this regard. As a policy, we will continue to conserve cash and control our debt levels going forward. I would now request Vikram to take you through the financial highlights.

Vikram Shriram: Good afternoon ladies and gentlemen. I will now summarize the financial highlights for Q1 FY14.

The total revenue for the quarter was higher by 8.5% at Rs. 1,549 crore. Revenues excluding Hariyali business grew by 18% to Rs. 1,427 crore. Hariyali revenues declined to Rs. 122 crore from Rs. 213 crore consequent to discontinuation of its loss making activities. Growth in revenues was driven by Shriram Farm Solutions, Bioseed and Sugar businesses. PBIT before exceptional items was up by 28% at Rs. 167 crore. Shriram Farm Solutions and Chloro-Vinyl registered good growth in PBIT. Breakeven in Hariyali business (as compared to a loss of Rs. 20 crore last year) also contributed in the profit growth. The financial charges for the period were flat at Rs. 44 crore. Net profits stood at Rs. 114 crore compared to Rs. 31 crore in the corresponding quarter last year.

Let me now take you through our business-wise performance.

Revenues from the Chloro-Vinyl business were up by 2% at Rs. 285 crore. The volumes were up by approximately 15% for Chemicals primarily due to maintenance shut down at one of our plants last year. However, a drop of 19% in the prices per ECU in Chemicals restricted the growth in the overall revenues. PBIT of this segment was higher by approximately Rs. 8 crore over last year at Rs. 81 crore. The drop in ECU prices had an adverse impact of Rs. 30 crore. The reduction in the operating cost in both, Chemicals and Plastic businesses and the increase in volumes helped in mitigating the adverse impact of the ECU drop.

Revenues and PBIT for the Fertilizer business stood at Rs. 144 crore and Rs. 7 crore respectively. The business registered volume growth of 4% and better operating efficiencies. This helped in partly mitigating the impact of rising cost and non-revision of retention prices. The subsidy outstanding remained high throughout the quarter but reduced to normal levels in July 13.

The revenues from the Shriram Farm Solutions business grew by 56% to Rs. 464 crore. This was driven by growth in value-added inputs up by 34% and bulk Fertilizers up by 110% driven by growth in the DAP business. PBIT from value-added inputs grew by 19%. The growth in profits was moderated due to drop in margins in cotton-seed business.

In the Bioseed business, revenues were higher by 14% at Rs. 289 crore driven by healthy growth in the Indian operations. However higher sales return in Philippines business moderated the growth in the revenues. PBIT at Rs. 66 crore was almost same as the last year due to pressure in cotton-seed segment and sales return in Philippines as explained earlier. Please note that in Q2 FY13, we had faced higher sales return in India, which had led to correspondingly higher losses. We do not expect similar sales return situation in the current year.

Revenues in the sugar business were higher by 21% at Rs. 338 crore driven by higher volumes. However, earnings continued to be under pressure in this business as the realizations at Rs. 3,160 per quintal were much lower than the cost of production of Rs. 3,331 per quintal. We had accounted for the inventory at the estimated NRV in March 2013, which limited the negative result for this segment in this quarter.

Revenues from Hariyali Kisaan Bazaar declined from Rs. 213 crore to Rs. 122 crore. Please note here that the current revenues include revenues from fuel sales only. The segment achieved breakeven as compared to a loss of Rs. 20 crore in the same quarter last year consequent to implementation of restructuring and rationalization plan which involved restricting activities only to the profitable line as mentioned earlier.

Revenues in the Cement business were lower by 21% at Rs. 30 crore driven by lower volumes, down by 18%, and lower realizations, down by 3%. PBIT was lower by 60% at ~Rs. 3 crore.

Revenues under 'Others' stood flat at Rs. 76 crore in the quarter under review. PBIT losses from this segment reduced from Rs. 7 crore to Rs. 30 lakhs due to better performance of the Fenesta business.

That concludes my financial review and we should be glad to take any questions that you may have.

Moderator: Thank you ladies and gentlemen. We will now begin with the question and answer session. We have the first question from the line of Rahul Bhangadia from Lucky Investment Managers. Please go ahead.

Rahul Bhangadia: Could you give us a sense on the cotton-seed business within India. In addition, how many packets did you sell in the northern and southern markets?

Rajiv Sinha: Our internal estimates suggest that currently the overall market in the country is probably lower by about 10% in terms of the total number of the packets. Last year, the country sold about 4.1 crore packet and the overall number for this year is estimated to be about 3.7 crore packets. In North, the market has shrunk by about 10% from about 60 – 62 lakh packets to about 58 - 60 lakh packets. As far as we are concerned, we have been able to maintain similar volumes in North as last year, if you take Kharif as a whole, and slightly higher volumes we expect through Kharif as far as south and central is concerned.

Rahul Bhangadia: I believe during last year, you had sold something like 19 lakh packets in the North and 3 lakh packets in the South. So what are these numbers looking like in the current year?

Rajiv Sinha: If you recollect, some part of the sale that were supposed to happen in March last year took place in Q1 FY14 due to delay in permissions. On a prevalent basis, we would be about the same level as last year as far as North is concerned. This means that we have retained our volumes even in a declining market and have thus improved our market share in the process and of course we still have the largest market share in the north at about 35-38% of the total volume. As far as the South and Central is concerned, we have made good progress. We sold about 7.7 lakh packets in the total Kharif season last year and for the current year; we should be at 9.5 lakh packets or so.

Rahul Bhangadia: Is 7.5 lakh packets net of returns?

Rajiv Sinha: All the numbers that I am giving you are all net of returns. These are all Kharif season basis and not on a quarter basis. I think the main difference is in the South is that we have introduced a new product which has gained good traction with time and this is really what we are looking for growth in the next couple of years.

Rahul Bhangadia: But from what I recall, South and Central markets were 3 lakh packets?

J. K. Jain: No. On a Kharif season basis it was 8 lakh packets.

Rajiv Sinha: We have given all the numbers based on the Kharif season and not on quarter.

Rahul Bhangadia: What is the kind of realization rise you have seen in July because of the rupee depreciation in the Chlor-Alkali segment?

Ajay Shriram: It has recovered some 7 to 8%.

Rahul Bhangadia: Would it be fair to assume that the 7-8% rise in realizations would flow straight to the bottom-line given that your costs are under control?

Ajay Shriram: Yes. The cost of production is a separate area of concern and action in any case. Therefore, any addition we get goes straight to the bottom-line.

Rahul Bhangadia: How long can sugar mills sustain these losses?

Ajit Shriram: As far as the Sugar business is concerned, particularly in UP, as have we mentioned in the opening remarks I think implementation of the Rangarajan Committee report on the cane side is very important. As we had mentioned, it is being implemented in Karnataka and Maharashtra. Now if over one-third of India is going to go by these recommendations, then it becomes very imminent for UP also to do the same; otherwise UP will be completely out priced. Now we really hope that there is rational cane price in the coming year and in an ideal case scenario, it should not increase from the current level.

Rahul Bhangadia: What would be the sugar cane arrears in UP?

Ajay Shriram: There was a statement made by Mr. Thomas yesterday that arrears in UP is about Rs. 4,200 crore.

Moderator: Thank you. The next question is from the line of Pratik Poddar from ICICI Prudential Asset Management. Please go ahead.

Pratik Poddar: Could you throw some light on the cane acreage in UP?

Ajit Shriram: To be frank, the farmers know that the cane price will be paid to them and there will be no default as such. In addition, Rs. 280 is a very good price if you compare it with the other crops like wheat and rice. So, even though there are arrears, the cane area has not really gone down and with good monsoon the yield should also be good.

Pratik Poddar: Any progress on the land sale in Hariyali Kisaan Bazaar?

J. K. Jain: We have already contracted for about 15 properties out of 100 properties. These will get transferred in next two quarters as per the contract terms. The balance is at various stages of discussion and negotiations.

Pratik Poddar: How many properties do we have on sale in total?

J. K. Jain: All the 100 are on sale.

Pratik Poddar: Are these at book value?

J. K. Jain: As we mentioned last time, we are carrying them at book value. It comprises land and building both and we expect that in totality we should be able to realize at least the book value.

Pratik Poddar: This time the PVC business more than compensated the decline in Chloro-Alkali business. So, can we expect similar kind of realizations in PVC business in Q1 as well or there has been some dip?

Ajay Shriram: PVC realizations are quite stable at the moment. While we do not see too much swing, but it being a commodity, a 5% move up or down is normal.

Pratik Poddar: You mentioned that you have taken a price hike. That was for the plastic business, right.

Ajay Shriram: No. That is for Caustic Soda and chlorine and that too just marginally.

J. K. Jain: I would just like to highlight that the entire drop in Chlor-Alkali price in the first quarter was not compensated by PVC price increase alone. It was also some cost optimization initiatives that we had undertaken as you would have noticed in the presentation.

Pratik Poddar: So the volumes have gone up by 21%.

J. K. Jain: The volumes of chemical went up and cost went down significantly.

Pratik Poddar: And will this continue for the whole year?

J. K. Jain: It is difficult to predict for the whole year, but the cost reduction is sustainable.

Pratik Poddar: Could share the number of packets that we have sold of Yuva?

Rajiv Sinha: As I mentioned, the Kharif season is still on. Hence, I will not be able to give you an exact number. We estimate the total number to be about 9.5 lakh packets, which includes significant quantity from Yuva.

Pratik Poddar: Could you share the gross and net debt figures?

J. K. Jain: There is no sharp difference between gross and net debt. Our net debt was at about Rs. 1,550 crore and gross may be about Rs. 100 crore more than that because that is the amount of transactional cash and bank balance that is there in the system.

Pratik Poddar: And this Rs. 1,550 crore would obviously include the working capital and the subsidy, right.

J. K. Jain: This includes the term loans and working capital loans. And the working capital loans includes subsidy.

Pratik Poddar: What would be the subsidy amount?

J. K. Jain: It was about Rs. 350 crore as on June 30, 2013.

Pratik Poddar: Was this for the first quarter only or anything from the March quarter or also that is being carried forward?

J. K. Jain: Yes, it includes last year's subsidy receivables.

Pratik Poddar: And we have still not received that?

J. K. Jain: There is difference product-wise. As far as Urea is concerned, we received all the old outstanding in July. In DAP and MOP we have received 85% of the subsidy relating to last year but 15% still continues as pending. For SSP, even the principal amount is still pending relating to the last year. Therefore, it is varying from product to product.

Pratik Poddar: One question on the strategy side. What I understand that since the Hariyali Kisaan Bazaar losses are over and the business seems stable, in fact growing, we would be a free cash flow generating Company and we would have some cash from sale of land as well. So what is your capital allocation policy and what kind of return ratio do we target?

Ajay Shriram: Our policy is very clear that we will continue spending money wherever we need to, be it either for the plant maintenance to keep it state-of-the-art or for cost reduction and we have spent money. That is getting reflected and if you see our power plant, costs have come down because of the various initiatives taken. Secondly, we will be implementing one more electrolyzer in our Caustic Soda plant in Gujarat and that would be about Rs. 30 odd crore in the next 8-10 month. Frankly if we look at it, our commodity business continues to need to be upgraded and marginal expansion will carry on over there. For the other businesses, we will keep investing as and when the need arise. We will spend on Fenesta because we already have good capacities and if there is a need to put up another plant somewhere, we will do that. Overall, we will invest wherever needed. But in today's environment, we are a little more cautious and we do not want to jump in with a very high cost sort of approach that within the next three years we are going to spend so much. So, I think one has to get a little better sense of what is happening in the world economy and the Indian economy before we jump in too much.

Pratik Poddar: Which businesses you expect to grow in the next three years?

Ajay Shriram: I think in the next three years, business that we believe will grow are Farm Solutions, Fenesta, Bioseed, Trading and Caustic Soda as we are putting up a new plant.

Pratik Poddar: What kind of revenue potential will the investments that are being made in caustic soda have?

J. K. Jain: It will add about 8,000-10,000 tons of additional production, which should be about Rs. 20 crore.

Moderator: Thank you. The next question is from the line of Nehalata Khare from Deutsche Bank. Please go ahead.

Nehalata Khare: What was the CAPEX amount for this quarter?

Ajay Shriram: We did not have any major CAPEX amount for this quarter.

Nehalata Khare: Are you planning for some?

Ajay Shriram: As I mentioned, we are putting up a caustic soda electrolyzer. It is about Rs. 30 crore. It will come about in the next 10 months.

Moderator: Thank you. The next question is a follow up from the line of Rahul Bhangadia from Lucky Investment Managers. Please go ahead.

Rahul Bhangadia: Now that we really do not have any significant CAPEX planned; and all the profits and depreciation would mostly be cash flow for the Company, so I was just wondering what would be the dividend payout policy that the Company will implement going ahead?

Ajay Shriram: Well that the board will decide on the year-to-year basis depending on the plans which we have at that time and depending on how the market is doing. Dividend is not only based on internal accruals; but it would also depend on what is the external environment and what are the plans for the Company. So the Board will take a view.

Rahul Bhangadia: But would there be something that would be there in your mind may be 20% of profits, anything that you can indicate.

Ajay Shriram: No. We have not looked at it that way.

Moderator: Thank you. We have the next question from the line of Amit Goela from Rare Enterprises. Please go ahead.

Amit Goela: The inherent profitability of the business is now coming out and the numbers have changed significantly since you have taken care of Hariyali over the last two years. So are you looking at some incremental value unlocking exercise?

J. K. Jain: If you are talking about any restructuring or hiving off, we have not addressed those issue at all; but in terms of cash, I think as our chairman mentioned, the prime focus continues to be conserving cash and reducing the borrowings and improving the cost structure. So that will continue.

Moderator: Thank you. As we have no further questions I would like to hand the floor back to the management for closing comments. Please go ahead sir.

Ajay Shriram: Ladies and gentlemen, thank you once again for attending our Company's Q1 FY14 earnings call. As mentioned during the call, we expect the Company to continue to record good performance in the coming year. While some businesses are experiencing softness in prices, improvement in the overall operating efficiencies and cost rationalizations are going to be a positive factor and a continuing process for us. Better performance of the Fenesta business and breakeven of Hariyali will also contribute to a better performance. Thank you once again.

Moderator: Thank you gentlemen of the management. Ladies and gentlemen on behalf of DCM Shriram Consolidate Limited that concludes this conference call. Thank you for joining us.
