TATA CHEMICALS LIMITED

"Tata Chemicals Limited Q4 FY16 Earnings Conference Call"

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TATA CHEMICALS LIMITED

CHORUS CALL®

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Moderator: Ladies and Gentlemen, Good Day and Welcome to the Tata Chemicals Limited Q4 FY16 Earnings Conference Call. As a reminder, all participant lines will be in the listen-only mode. And there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing '*' then '0' on your touchtone phone. Please note this conference is being recorded. I would now like to hand the conference over to Mr. Gavin. Thank you and over to you, sir

Gavin Desa: Thank you. Good afternoon, everyone and thank you for joining us on the Q4 and FY16 Earnings Call for Tata Chemicals. We have here with us today Mr. R. Mukundan – Managing Director, Mr. John Mulhall – Chief Financial Officer and Mr. Ranjeev Lodha – VP and Group Corporate Controller.

Before we begin, I would like to mention that some of the statements made in today's discussion may be forward-looking in nature and may involve risks and uncertainties. A detailed statement in this regard is available in the results presentation. I now invite Mr. R. Mukundan to begin proceedings of the call.

R. Mukundan: Thank you, Gavin. I would like to welcome at this point my colleague John and Ranjeev on the call and all of you as well.

We will start briefly by sharing with you some key highlights of our operating performance during the quarter financial year ended March 2016, following which, my colleague Mr. John Mulhall will share the key financial details. After this we would be happy to respond your queries.

The quarter under review saw consumer portfolio and Indian chemical business registering robust performance. The performance of Europe and Magadi has been positive. The US operations have shown signs of stability in terms of output. In India, the chemical business improved performance due to lower input cost, improved sales of the consumer business in terms of salt and pulses over last year contributed to increased turnover of that portfolio.

In the farm business, volumes of urea have been lower consequent to the annual turnaround, which we took in the later part of March, and also extended into April, so the same impact would be in the quarter one of the current year. Adverse climate and market conditions have impacted fertilizers and other agri input business. The performance of agri business was adversely impacted as a result of high working capital levels witnessed through the year, especially in fertilizer due to delay in subsidy payment. Improved sales of salt as well as pulses over the last year contributed to higher turnover of consumer portfolio, and this portfolio continues to grow with leadership position in edible salt.

Tata Sampann, our umbrella brand for all new and future product launches in food space registered an increase of 25% for the quarter, 71% for FY16 in pulses, which is in line with our focus on expanding this portfolio. The pan-India rollout of Tata Sampann range of spices continues in line with our business plan and this is likely to go beyond the north, which we have rolled out at the end of March into other parts of India during the course of the year to cover the entire India sub-continent.

In summary, while the consumer and chemicals businesses registered improved performance, adverse climatic and market conditions have impacted the farm facing business and we do look forward to the positive news on the timely arrival of monsoon especially for this business which is housed in our fertilizer business as well as in Rallis our subsidiary, and Metahelix which is subsidiary of Rallis. Going forward, we continue the journey of transformation to become a more consumer and specialty focused business.

At this point I would now request John to give us some insights into the financial performance. Thank you.

John Mulhall: Thanks Mukund. I would like to briefly recap on financials for 4Q FY16. On a consolidated basis our net income for the quarter stood at Rs.4,007 crores against Rs.3,743 crores in the same corresponding quarter for the previous financial year. Higher revenues recorded across all business units.

Profit from operations increased by 26% at Rs.520 crores compared to Rs.413 crores in the same quarter last year primarily through improved margins and chemicals and consumer business and portfolios. There is also a favourable impact due to the rephrasing of the accounting of urea production above “cut off” production that was discussed in previous earnings call of this year.

Profit after tax and minority share of interest is Rs.242 crores against the loss of Rs.74 crores reported last year. Results for quarter four 2015 included a onetime, non-cash charge, towards the write down in investment in overseas joint ventures aggregating to Rs.198 crores. On a standalone basis, the net income for the quarter was Rs. 2,268 crores, up by 154 crores from last year’s Rs. 2,114 crores. Profit from operations is up, at Rs.186 crores, against Rs.163 in the same period last year primarily due to lower input costs, specifically energy costs and improved performance of our consumer portfolio. Profit after tax was Rs.132 crores and is better than the Rs.92 crores last year.

The company's standalone net debt on 31st of March, 2016, was Rs. 2,442 crores compared to Rs. 2,142 crores on March 31st, 2015, the delay in subsidy resulted in higher working capital borrowings as well. On a consolidated basis, the net debt was Rs.7,324 crores against Rs.6,914 crores, this is after taking into account Rs.272 crores of foreign currency translations losses in the year.

The company holds cash and cash equivalents of Rs.1,371 crores on a consolidated basis and subsidy outstanding at 31st of March, 2016, was Rs.1,902 crores against Rs.1,976 crores last March and Rs.1,577 crores in December 2015.

And this brings me to end of my discussion and I would like to open the floor to any questions you may have.

Moderator: Thank you very much. We will now begin with the question and answer session. The first question is from the line of Abhijit Akella from India Infoline. Please go ahead.

Abhijit Akella: My first question is related to the consumer business in India excluding salt, which I believe is shown under the others segment in your standalone results. So there the revenues this quarter have fallen, I am just talking on a quarter-on-quarter basis they have fallen from Rs.119 crores to Rs.95 crores and two quarters ago they were Rs.145 crores and the EBIT loss has increased probably because of the fall in revenues. I believe this largely includes pulses, so if you can just help us understand what is happening here exactly?

Ranjeev Lodha: Abhijit, this is basically on account of the pulses business, which has seen an increased turnover compared to the previous year but not compared to the trailing quarter, but largely because of the ad spend that we had in the consumer portfolio.

R. Mukundan: I think let me add a bit more colour to this. In the last quarter of this year the pulse sales were marginally impacted due to availability issues, which we had to sort out in the market, but apart from that we do see this segment growing. And as rightly pointed out, we are still investing in the brand, a lot of these elements of negative run are all because of investment in brand, we see this investment to continue for couple of more years before it starts to trail down and whole equation moves in the positive zone where we can tone down the investment to what I would call is maintenance level. Today the entire effort is on creating the brand and our focus is likely to continue.

Abhijit Akella: So you would still expect this to continue to grow strongly in FY17 and probably bring down the operating losses as well?

R. Mukundan: I would not call them that, we would continue to grow strongly but we will also continue to invest, these are discretionary investments and effectively the value we are creating here is the brand and we have to invest to create that brand.

Abhijit Akella: And also your press release talks about the launch of FOS based formulations in 92 cities, so just to clarify is this Fructo-oligosaccharides we have been planning to launch?

R. Mukundan: Yes, we are today selling FOS which we manufacture and we are also bringing in formulations of Maltitol and other sugar, what I would call related substitutes which basically impact your dietary intake and this is in the initial phase and I think it is having a good demand in the market place.

Abhijit Akella: And on the fertilizer business, we have seen a lot of pressure on the margins this year, obviously part of it may have been because of the drought. Now given the outlook for a better monsoon next year do you think margins can somewhat revive closer back to historical levels or is the competitive situation and inventory overhang still too high to permit any uptick in margins?

R. Mukundan: I hold a consistent view and my view has not changed, number one, the subsidy situation for the industry continues as before, and this is across all players, so we are equally impacted. The second issue is, urea will remain as a stable cash generating business, and we see that business doing well, however the phosphoric fertilizer manufactured in India is having challenges, apart from the brand and distribution, we have no major competitive advantage in that business. So it is going to continue. In my view you will see blips because of inventory overhang but strategic view of the business is exactly what I said, urea will be a steady cash generating business and DAP has challenges due to strategic considerations because the factors of production do not exist in India.

Abhijit Akella: There are I believe some discussions or the Indian Government is studying the anti-dumping duty that is currently invoked in India, do you see a risk that the duty could be taken away in the next few months, and if so, what kind of impact can it have on the Indian businesses' margins?

R. Mukundan: As a company, are in favour of free market. If in the interim industry needs some kind of adjustment period, I think these duties come in handy and we are well prepared. As of now we do know that there review is going on, but in any case if the duties are going to go off, may be in the year 2017 end or towards 2018 beginning, either way, it does not really change the situation much, it only advances the period. The world market in this regard is fairly balanced as of now and this balanced position is likely to continue till end of 2018.

Abhijit Akella: So you would not expect a major impact on margins in India?

R. Mukundan: That is a bit of a speculative statement, we will see when it comes, but obviously these types of major dislocations leads to some adjustment, what we need to watch out for is whether the business is balanced between demand and supply. As far as we can see, till the end of 2018 this demand / supply situation is going to remain balanced.

Moderator: Thank you. Our next question is from the line of Manish Ostwal from Nirmal Bang. Please go ahead.

Manish Ostwal: My question on the consolidated financial, the interest expense declined QoQ so could you explain the reason for the same?

John Mulhall: We had a small MTM gain on the gas hedges in the UK of about Rs.8 crores which is really the reason why it dropped down against a quarter three charge of Rs.45 crores relating mark-to-market charges for UK gas hedges. So it is not cash, it is mark-to-market accounting for finance expenses, it is not interest.

Manish Ostwal: And secondly, when you look at the standalone performance and consolidated performance, the consolidated performance especially on the operating profit level is much better, so I believe the overseas subsidiaries are doing relatively better performance this time compared to the previous few quarters. So first question is, what are the things happening in those subsidiaries? And secondly, how sustainable the profitability of these subsidiaries is at current level?

John Mulhall In Q2 and Q3 in North America, we lost couple of hundred thousand tons over the year against last year. And what we saw in quarter four was a much more stable production and that is slightly ahead of production the same quarter last year. So, in a sense it is a recovery of a bad position in the quarter two and quarter three. Margins have improved across North America and India really due to lower input cost for energy: gas and, coal. And finally quarter four showed a reduced energy cost in the UK due to the operations of steam turbine, installed last year and in operation throughout the winter. We were able to generate electricity for sale onto the UK national grid from waste steam which generated £2.5 million over the previous quarter.

Manish Ostwal: And lastly for FY17, what is our CAPEX plan and do we have any major repayment of debt in FY17?

John Mulhall: For debt repayment we do have one piece which is Rs.325 crores ECB loan at the TCL level that will be repaid in October and we talked about this in the last meeting. As regarding CAPEX, we do not give guidance on CAPEX or profitability going forward.

Manish Ostwal: Sir I am asking CAPEX number; I am not asking any profitability guidance because I understand there are multiple variables affecting business.

John Mulhall: Yes, you are quite right, the CAPEX is part of that as well and we do not give CAPEX guidance either.

Moderator: Thank you. Our next question is from the line of Alok Deshpande from HSBC. Please go ahead.

Alok Deshpande: A couple of questions, first, on the US soda ash operations. So obviously Q4 saw very good recovery in terms of utilization as well as margins, just wanted to get your sense on what you see in terms of utilization over the next couple of quarters and your outlook on the margins based on the cost that you are forecasting?

R. Mukundan: So as far as US is concerned, you are absolutely right, the last quarter saw more stable production, we have taken a number of steps and we do expect going forward the stability will be there and we are working towards continued stability of the plant.

Alok Deshpande: And these margins what you saw in Q4, is that something which is sustainable as well if we continue at the same utilization levels?

R. Mukundan: If you look at US their contract period is from January to December, so Q4 of India actually is their first quarter of new contracts, so I think if at all any contracting issue needs to come up we will probably be able to tell you next January, that is when the contracts would be done, as of now there is nothing, at least till December current contracts are into that.

Alok Deshpande: And second question was on salt pricing, so if you can give us some colour: first of all, did we see any pricing gains this year in salt, and also, how is the market competition in salt currently? Whether it is conducive to taking pricing, hikes going forward and also the volume outlook, how does that look?

R. Mukundan: On salt, really there are two drivers; one is volume which certainly we would continue to grow along with the market to maintain our market share. Second, I would say is with respect to margins and it is largely running across salt and soda ash both, fundamentally on account of reduction in terms of the energy cost which benefits both the units. In fact, all the elements of our production and I do not see any big uptick in coal prices and because coal is the main driver of energy in India we should see stable energy costs.. And lastly, freight has also been fairly benign but there has been slight increase in rail freight but otherwise overall freight has been more benign than before.

Alok Deshpande: But sir, my question was, as per the market competition that is there in the market, is it based on the demand of your products, is it conducive to taking the normal price hike that you have been taking for many years over the five, seven years, will that trend continue?

R. Mukundan: I would not like to comment on pricing because it is fairly strategic business led decision, all I would say is that there is terrific brand franchise which we enjoy, Tata Salt was judged in Economic Times as number two most trusted brand and we will continue to invest in brand to continue to make good this franchise which we have with our customers, it is on the back of that franchise we are building our Tata Sampann brand and we are also seeing great affection and love from our customers for Tata Sampann brand as we launched spices in Punjab and Haryana. The initial offtake was better than our internal estimates of what we thought we would be doing in the initial months. The rollout in north also has given us a terrific response and we will continue to roll this out all over India for spices. Pulses, of course is already national and we are growing it in a manner that it gets a brand pull, we do not want to have a commodity-led growth, hence you would see that it is a very measured growth to ensure there is consistent pull from the customers.

Alok Deshpande: Sir just one last question, what was the CAPEX for the past year FY16?

John Mulhall: Rs.664 crores.

Moderator: Thank you. Our next question is from the line of Lokesh Manik from Vallum Capital. Please go ahead.

Lokesh Manik: My questions are mostly on the macro front, to just to get an idea going down the line next five years in which divisions do we expect majority of the CAPEX happening?

R. Mukundan: I would not like to guide in that manner, but all I would say is that, if you look at our growth engines they would continue to be in the **consumer and specialty** business, including the underlying subsidiary which we have in Rallis and its own subsidiary Metahelix, which is now its 100% subsidiary. And as far as CAPEX in the soda ash, which is where bulk of our focus would be, because it is capital intensive, largely it would be sustenance and maintenance-led CAPEX except for, when we press the pedal and that point we will come back to you exactly, when we are pressing the pedal in US and in India.

Lokesh Manik: Do we have any plans to exit the fertilizer business or the urea business for that matter?

R. Mukundan: We have clarified before that this is speculative news and for us the way we view the urea business as annuity business and Haldia has its own challenges, in fact DAP manufacturers face similar challenge, and we are facing it. And the rest of the news is speculative.

Lokesh Manik: Sir, on the soda ash front, just wanted to get an idea of the total global demand of close to 56 million metric ton, how much would be met by synthetic soda ash and how much would be natural soda?

R. Mukundan: It is, at a broad level, approx. 75% synthetic and 25% natural. And as far as the other point which I wanted to say is that the business we are deemphasizing which means no major capital going forward is fertilizer, so just wanted to make that point clear.

Lokesh Manik: And sir in the last few years emerging economies has been a driver of growth for soda ash, now that we have seen a slowdown even in these economies where do we see demand coming in from going ahead?

R. Mukundan: I think the demand drivers would continue to be India and Southeast Asia as well as parts of South America and US has grown positively in line with the economic growth, so we would see these as the growth pockets. And China, which was the engine of growth is certainly slowing down, but good news, at least for in terms of the of balance in the world market, is that Chinese capacity growth also is slowing down substantially on the back of tightening environment law and government's own approach to sort of tighten some of the industries which have had great capacity growth in the past.

Lokesh Manik: So any reduction in the energy cost in China would have an impact on India in terms of imports?

R. Mukundan: India is equally competitive on energy because bulk of our energy is coming from Indonesian coal, so it is not that we see any different, we track the cost structures, our Indian operation is as competitive as Chinese operations.

Lokesh Manik: So as I understand in your annual report you mentioned that we follow a strategy of distributed sourcing that increases the reliability of supplies, so just to get an idea, does transportation offset any of the benefits that we have with natural soda we have around 67% capacity in natural soda?

R. Mukundan: Sorry I did not get your question, what was the question about? Does freight impact natural soda ash?

Lokesh Manik: Right, the freight impact on the difference between natural soda ash and synthetic soda ash, does it get offset, does the freight cost offset the benefit?

R. Mukundan: Yes, lower freight regime benefits of natural soda ash because it can then travel longer.

Moderator: Thank you. Our next question is from the line of Girish Raj from Quest Investments. Please go ahead.

Girish Raj: I did not quite understand your commentary on phosphatic fertilizer and the competitive advantage, were you hinting on the DAP as a category or phosphatic as a category or it's our position in phosphatic?

R. Mukundan: I was not specific about our position because that will be forward-looking statement. It is about the general factors of production in India. If you look at rock phosphate it does not exist in India, ammonia does not exist in India, everything is imported. So I was saying in commodities, if you do not have security and control over your upstream, really any value addition only on the basis of downstream is very difficult, especially if it is a controlled business. So we have this situation where the fertilizer is controlled. It is subsidy driven so upstream value creation is difficult. Downstream, there is no factor of production in India henceit is a challenged industry. So I just wanted to highlight, broadly that is our view.

Girish Raj: In terms of demand going forward, today it is 16 million approximately, so in terms of demand do you see any issues or urea at 30 million?

R. Mukundan: No, I think demand is not an issue in India, I think India will remain an agrarian economy and fertiliser demand will be there. All I was saying is in both urea and phosphate the ratio will shift more and more towards balanced if the government starts to move in the right direction phosphate demand should grow as well as the demand for potash should grow. But effectively, all we are saying is in potash obviously we import everything. In the case of urea, we do have the conversion cost and efficiency wherein Indian manufacturers do well.

Moderator: Thank you. Our next question is from the line of Anil Shah from Birla Mutual Fund. Please go ahead.

Anil Shah: Sir, my question is on your stated objective for at least for the last six to eight quarters of investing in asset-light models going towards the customer in terms of basically the consumer part of the portfolio and hence generating free cash flow and reducing debt, are we still on that path?

John Mulhall: I think we are very clear it will be under control and we repay debt as and when compared to this time last year our on standalone basis our inventory is Rs. 1,000 crores lower this year. Sundry debtors where kept a very close watch. So where we can control we do control, where we cannot control obviously Rs.1,900 crores outstanding on subsidy bill and that is what is holding us back, though that money costs us around Rs. 75 crores - 80 crores a year in excess interest expense.

Girish Raj: I will just rephrase the question, in terms of reduction of debt is it only because, are you saying that we are only stuck up because of the subsidy amount getting stuck, is that being the case because the subsidy was flat on a year-over-year basis and the debt has also remained almost flat? Form a business operations perspective we have not been able to reduce debt.

John Mulhall: On a standalone basis?

Girish Raj: No I am looking at generally at a consol.

John Mulhall: On consol basis, our debt is pretty much termed out.

Girish Raj: Sorry, I could not understand, could you just be more specific, I am saying that debt is on a year-over-year basis flat, the receivable in terms of subsidy on a year-on-year basis is flat.

John Mulhall: That is right, you are absolutely correct, the debt has increased when we suffered Rs. 270 crores exchange difference. I would except our debt not to move that much this year, given the recovering performances in the UK and Magadi. The US, which suffered from production issues at the start of the year and, although it made a profit, our net debt has not moved that much. And taking up further Rs. 270 crores foreign exchange loss has not helped.

Girish Raj: And the CAPEX number that you have talked about which is 664 in terms of FY16, would it be possible to give us a split in terms of this CAPEX, how much of this is maintenance CAPEX and how much CAPEX you would have done as a one-time CAPEX or as a CAPEX which was expansionary in nature for any particular business and so on and so forth, because just trying to get a sense of how much do we really need given the fact that we are not going to be spending on fertilizer in terms of CAPEX, consumer is an asset-light business, we are not looking at any major expansions in soda ash right now. So I am just trying to get a sense of what is the maintenance CAPEX that we have from a yearly perspective?

John Mulhall: We had a couple of large projects last year in the US where we have installed a new shaft which was $25 million which we do once every eight, 10 years. In UK we have probably spent on the turbine so there is another Rs. 25 crores to 30 crores there. There are bigger one-offs with our ATR in Babrala which is another Rs. 35 crores this year that we have spent on a year-on-year basis. So there are some one-off numbers in there.

Girish Raj: Exactly, so you may not want to give a number but about Rs. 400 crores would be something that you would have in terms of maintenance CAPEX?

R. Mukundan: So let me just say this, I think it will move within the range of somewhere around Rs 350 to Rs 500, depending on when we take up these maintenance projects.

Moderator: Thank you. Our next question is from the line of Dewang Mehta from Canara Robeco AMC. Please go ahead.

Dewang Mehta: Just a couple of questions on the UK plant, we have been looking at what kind of capacity would be left with in the soda ash and also what kind of bi-carb capacities we will be having?

R. Mukundan: UK is about 330,000, broadly give or take 10,000 – 20,000 year-on-year..

Dewang Mehta: In terms of bi-carb?

R. Mukundan: Bi-carb is about 100,000 out of that.

Dewang Mehta: It is out of 330k combined?

R. Mukundan: No, the way to work that is, 360 is soda ash and 110 is bi-carb. And the soda ash goes into bi-carb, so for getting exact produce for sale, you need to reduce 0.6, i.e. 60,000 you need to knock off from the soda ash.

Dewang Mehta: And what would be the current utilizations for soda ash and bi-carb?

R. Mukundan: Nearly fully sold.

Dewang Mehta: And one more question, are we facing any issues at Magadi for the Trona?

R. Mukundan: In terms of Trona, we do not have any issue, it is a perennial resource and at least technically as we understand it is self-regenerating resort.

Dewang Mehta: So last year there were some issues in terms of expecting the Trona from the river.

R. Mukundan: No, let me clarify this, upstream there is a river, which flows into the lake, which there was deforestation issue causing the soil to be washed into the lake, right now we have constructed dykes so the technical issue has been resolved, as of now.

Moderator: Thank you. Our next question is from the line of Abhijit Akella from India Infoline. Please go ahead.

Abhijit Akella: The gas hedges as they are running off, the cost of goods sold in the UK is that now at the hedged gas cost and therefore is that weighing on the profitability there? Just trying to get a sense for whether we should expect margins to improve in the UK once these gas hedges run off.

John Mulhall: You are right on your statement.

Abhijit Akella: And in Kenya we have had a nice bump up in profits this quarter, so is there any additional benefit maybe from the South African trading operations or anything like that?

R. Mukundan: No, it is just the Kenyan operation.

Abhijit Akella: In the presentation we gave soda ash production as well as sales volumes for India and the UK and the two of them are quite divergent, there is a gap there of around 100,000 or 150,000 tons.

Ranjeev Lodha: Abhijit, you are referring to the quarter number or the year number?

Abhijit Akella: The full year actually.

Ranjeev Lodha : So the full year in UK sales are higher than production that is for two reasons, one is, the sales are whatever goes out of the opening stock and any purchased for resale.

R. Mukundan: The UK does buy material from US to sell in the local market because, you will recall, we restructured UK Business and shut one plant down, but we kept the customers and those customers are being serviced from US.

Abhijit Akella: And in India what is the situation sir, India sales are lower than production.

Ranjeev Lodha: That is basically the consumption of soda ash for bi-carb manufacturing.

Abhijit Akella: And finally on the tax rate, it was quite low this year at 22% at the consol level, so is this the right number to trend off of going forward?

John Mulhall: Yes, the tax rate is actually around 27%. You need to deduct the minority interest to get to the taxable profit

Abhijit Akella: 27% going forward?

John Mulhall: Well, no, that is what we have this year.

Ranjeev Lodha: Abhijit, what happens also that IMACID the tax rate changes depending on the profitability versus the revenues, it is equivalent to a MAT regime in India. So that would also have an impact based on their profitability.

R. Mukundan: And also the third element is, as Kenya and UK start contributing to profits they have got a tax shield which means they have zero tax.

Abhijit Akella: And finally just on IMACID we have seen a quarterly loss this quarter, is this just some seasonal phenomenon?

R. Mukundan: It will continue for some time, they had a breakdown of their turbine-generator which used to generate power from steam, so they are not able to sell excess power, I think it should last for about a couple of quarters in IMACID after which they would be back to normal.

Moderator: Thank you. Ladies and Gentlemen, that was the last question. I now hand the floor over to the management for closing comments. Thank you and over to you

R. Mukundan: Thank you, everyone, for this call and joining the call. And I would like to again end on the note that the Company is well on its way on its transformation journey to focus on consumer and specialty business. We will continue to maintain our market share in soda ash but at the same time be focused stable operations in fertilizer. We are committed to reducing our debt, we do hope that the monsoon is on time and well spread for our business to prosper which is going to lead to probably better sales for the farms business this year than the previous year and that would also lead to better consumer demand. So we are all entering the new year with even greater hopes. Thank you.

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