



Triveni Engineering & Industries Limited

Investor/Analyst Conference Call Transcript

July 22, 2010

- Moderator** Ladies and gentlemen good afternoon and welcome to the Triveni Engineering Q3 and nine months FY 2010 Earnings Conference Call. As a reminder, for the duration of this conference all participants' lines will be in the listen-only mode and there will be an opportunity for you to ask questions at the end of today's presentation. If you should need assistance during this conference call please signal an operator by pressing * and then 0 on your touchtone phone. Please note that this conference is being recorded. I would now like to hand the conference over to Mr. Rishab Barar of Citigate Dewe Rogerson. Thank you and over to you Mr. Barar.
- Rishab Barar** Thank you Rochelle. Good day everyone and a warm welcome to all of you participating in the Q3 and nine month FY 2010 conference call of Triveni Engineering and Industries Ltd. We have with us on this call Mr. Dhruv Sawhney, Chairman and Managing Director of the company along with other members of the senior management team. I would like to mention before we begin that some statements made in today's discussion maybe forward looking in nature and a statement to that effect has been included in the conference call invite, which was mailed to everybody earlier. Also I would like to emphasize that while this call is open to all invitees; it may not be broadcasted or reproduced in any form or manner. We would start this conference with opening remarks from the management followed by an interactive Q&A session where you can discuss your views and key issues. I would now like to hand over to Mr. Dhruv Sawhney to share some perspectives with you with regards to the company's operations and the results for the quarter under review. Over to you Mr. Sawhney.
- Dhruv Sawhney** Thank you very much. Good afternoon ladies and gentlemen and welcome to our Q3 conference call. The nine-month period for Triveni Engineering and Industries ended with sales of Rs. 16.7 billion, which is a 25% increase. Our EBITDA went up to slightly over Rs. 2 billion, which would give us a margin of 12% and with the PBIT of Rs. 1.37 billion. The PAT has come in at Rs. 736 million, or Rs. 73.6 crore. The engineering business has shown a good growth of turnover of 29% with a 19% improvement in PBIT. Sugar in inventories as on June 30, 2010 have been written down by Rs. 805 Million, which is Rs. 80.5 crore and this is the real reason for the results of the third quarter and the nine-month period versus similar period last year and this has been owing to the lower sugar prices, lower compared to our cost of production and also owing to the higher levy obligation, which is at a loss and is at a fixed price. Before I get into our Q3 figures in sugar I thought I might just mention a little bit about the situation in the country for the sugar year that is going to end in September and what our thoughts are for the next year and then put this to our sugar group. As you are all aware, it is pretty sure that the production in the country will end at around 19 Million tonnes and we are going to end with a closing stock of around 5.9 million tonnes, which is about two months of next year's consumption. This is a fairly good closing stock with respect to the stabilization of sugar prices and while it is likely more than last year it is at a very decent level compared to consumption to when it was when the prices had dipped very steeply. We are

forecasting the production for next year to be at around 24 to 25 Million tonnes and that is fairly uniform in the industry. Of course it will depend on the monsoon as well as on the Government Policy, which I will come to in a few minutes. We ended June 30, 2010 with an inventory of 25.25 Lakh quintals, which was 20.2 Lakhs of free sale sugar and 5.06 Lakhs of levy sugar; this is in stock on July 1, 2010. We valued it, the free at market and the levy at the revised levy price, so there would not be any further losses on the levy when it is sold in the fourth quarter. As far as our sugar fundamentals are concerned we believe they are good going forward both into the fourth quarter and into FY 2010-2011 as well. And this is really because, one, we do feel that even in the fourth quarter there should be a levy change from the 20%, this paper was put up to the ministers and while it had been deferred, it is being looked at favorably. What that percentage will come to is not sure but it should be in the range of 16% to 17%. This will help our year closing in sugar and next year. I think the time is very opportune for decontrol, the mood of both the state and the central government is good. We have seen decontrol in government polices in petroleum and the various ministries are looking at this in a very positive manner, they are really waiting to see that the monsoon is clear and they have some idea of next year's production so that there will not be any spurt in sugar prices, which we do not think will happen with this possibility, but a decontrol of sugar really means that we will have no further levy obligation and there will be no control on releases. This is really a major step for the industry going forward and will affect our group very positively in the next year and the years to come. We also expect much less diversion next year not only because of the higher production but also because of the fact that with this decontrol policy the cane price paying capacity of the gur units will be affected. At the moment they are not doing very well and the traders have lost substantial amounts similar to the sugar industry. The international market is really governed by Brazil, it is the single country that really governs the market and the cost of production there is around 17-18 cents a pound, so their industry has also been hurting compared to what it was doing in the first half of their sugar year, so the prices, which have declined very precipitously since January 2010 has affected not just the Indian sugar industry but also the Brazilian sugar industry, which is the most efficient in the world today, in a negative manner, but going forward they are also looking at FY 2010-2011 in a very positive manner, so the comments, which we are stating are not just for UP or India but for the global sugar scenario as well. We feel that the possibility of the government moving on this, once the monsoon are clear. At the moment in our area the monsoon have been good, the cane areas are up by about 14% to 15%, there are no disease and/or pest and the rainfall in July particularly has been quite adequate. We are looking at a good crop and with that a better recovery than last year and that will help our viability to a major extent.

To move on to our engineering group the crux is the increase in order book, we have a 22% increase in our engineering order book upwards compared to the last year, as on July 1, 2010 and we expect this actually to be continued in the next few months and quarters in FY10-11. The inquiries on hand are extremely good probably one of the best that we have seen in all the three engineering businesses and that is extremely encouraging. To take our steam turbines first, we have almost 1000 megawatts of orders on hand, which is about 21% higher than the corresponding period last year and we have an increase in sales of about 20%. Normally one does not give statements for the future but we are well into our fourth quarter so I can say that in our fourth quarter we believe the engineering PBIT will be some 40% to 50% higher than what it was in Q3 and that is because we are executing everything right now. In our steam turbine business in FY10-11 we expect sales to rise by over 25%, similar if not more increases in gears and of course much larger in our water business. In gears we have a PBIT margin of 34% for nine months, which is quite extraordinary as looking at the global situation, it is one of the highest we have. Quarter-to-quarter in all our engineering businesses it is difficult to compare exactly because of the type of orders and the type of customers and really what matters is the cumulative figures, and the orders going forward. In gears the team is evaluating strategic opportunities, which are in the best interest of expanding the gear business and that is currently underway now, which will carry on for the next three to six months. Water has grown 73% in the last nine months, an extraordinary increase in turnover. Orders on hand right now

are Rs. 2.57 billion and this does not include, where we are L1 in a bid, where the order will be about Rs. 2,000 million or Rs. 200 Crore, so that one order itself will be more than the turnover for the current year. Both the lines of our business, both the municipal line and the industrial line are doing well. We feel that this business in FY10-11 will continue the ambitious sales growth that we have and while margins are going to be industry best at 10% to 12% slightly lower than the 14% we had earlier, but this rapid increase in sales growth augurs very well for the fortunes of this group.

I would like to just cover a few other items. The first is our demerger. Stock exchange took about two months to respond to our application and we received a letter from them just two days ago. They are asking for some clarifications, which we are going to sort out and we expect to apply to the court in the next two to three weeks. The demerger is still on track and we hope that the new company would be functioning as we had earlier stated by the end of this calendar year. As far as GE Triveni is concerned the company has been formed and the closing formalities are in progress. The integration teams have been meeting on a number of occasions in India and overseas and the engineering at both sides is on. I would like to end by saying that we in both the sugar and engineering groups are concentrating a lot on development. In sugar, while it is a very cyclical industry the company's view on technology is also in sugar and our efforts on cane development has started showing extremely good promises right now. This of course needs multiplication so it will take a few years. Similar is our case in turbines. Our development efforts have been extremely successful. Our market share that we have got in the 30-megawatt range where we are now at 60% market share of steam turbines up to 30 megawatt, has from our R&D and development efforts and similar is our technology in gears and water. So, with an increased market in FY10-11 and good development efforts I think this side of the business looks very good. As far as sugar is concerned it will to a large extent depends on the sugar policy announcement but the sugar fundamentals are good both nationally and on an international level. Thank you very much and I would like to now open the floor to questions.

- Moderator** Thank you very much. Our first question is from the line of Sanjay Satpathy of Merrill Lynch. Please go ahead.
- Sanjay Satpathy** At the end of this quarter i.e., June quarter, what is the size of the inventory of the free sale sugar?
- Dhruv Sawhney** The free sale price in our evaluation is Rs. 27.75.
- Sanjay Satpathy** How much has levy sugar obviously has been valued at?
- Suresh Taneja** Rs.17.75 for us.
- Sanjay Satpathy** What has been the cost of production?
- Dhruv Sawhney** The cost of production has been approximately about Rs. 2,896 / quintal for the season.
- Sanjay Satpathy** We were looking at the reversal of the losses that you had booked in the March quarter because of the increase in levy sugar price, so just wanted to understand how the math have been now that we reported a Rs. 80 crore loss in the inventory?
- Suresh Taneja** As of June 30, 2010 whatever inventory was there whether it was levy or free sugar, levy was priced at revised levy price and free sugar was at the estimated realizable value and accordingly we have taken an inventory write down of about Rs. 80 crore.
- Sanjay Satpathy** But you had already had taken a hit of Rs. 50 crore at the end of March quarter.

Suresh Taneja No, this is inclusive of that. In other words what you can say is the difference between 80 crore and 51 crore was the incremental hit we have taken. Now, this is mainly also because of two factors, one, there was production during the quarter in the month of April at a high cost of production on which there was some inventory write down and number two because of the decline in the free sugar prices there was another hit coming in.

Sanjay Satpathy So you are saying that for the quarter the amount of inventory loss is actually 30 crore?

Suresh Taneja Rs. 29 crore

Sanjay Satpathy Okay, so these Rs. 80 Crore is the cumulative inventory loss?

Dhruv Sawhney Yes.

Sanjay Satpathy In this quarter your revenue from the engineering business was affected because you could not supply certain turbines. So just wanted to understand what exactly happened and how is it going to be made up for in the last quarter?

Dhruv Sawhney No, as I mentioned to you customer who takes the delivery in the first week of July instead of the last week of June can make a difference for that particular quarter, so this is absolutely of no consequence when you look at the full year results. As I mentioned almost 30% of the sale happen in the last quarter and that is why we are expecting 40% to 50% rise in PBIT in the fourth quarter, also as you see-to give you an example of engineering in quarter two in gears we had an enormous jump in sales, which was quite extraordinary and that is because the clients wanted the gear boxes much earlier than they had contracted the delivery so you had a 100% increase in profitability. Now this is not something that is sustainable, so we are taking about the nine-month period in which we have got 37% increase in gears and if you look at the turbine sales increase we have 20%, which we fully expect to continue in the fourth quarter rising to at least 25% in 2010-2011. Steam turbines is about 10 to 12 months or sometimes longer delivery so we have come out of the slight recessionary situation in 2008-2009. Now for the future in both the inquiries and the orders on hand are giving us this confidence of 20% in the fourth quarter and over 25% increase in turnover in FY 2010-2011.

Sanjay Satpathy Lastly, relating to the JV that you have formed up with GE. Can you give us some guidance about the kind of business that you are looking at from this in two to three years time?

Dhruv Sawhney I cannot really talk till we have had the closing but I want to tell you that we are looking at the 30-100 megawatt range and you know the range of demand in India, but the global demand which we are going to be catering for is three to four times the Indian demand and we are expecting to gear up both sales domestically and internationally from the first to second year onwards, so you have a very high potential of market access. I cannot give you figures on that.

Sanjay Satpathy Thank you.

Moderator Thank you Mr. Satpathy. Our next question is from the line of Achal Lohade of JM Financial. Please go ahead.

Achal Lohade On the cane price, recently Tamil Nadu Government announced the SAP at Rs.190 per quintal, how are we looking at the cane price for the next season, obviously it all depends on whether the actual decontrol of cane price happens or not. I just want to get a sense on how we will be looking at the cane price scenario for the next year?

Dhruv Sawhney Good question. I am really not aware or clear of the drivers of what exactly has happened in Tamil Nadu but I want to tell you on UP which is where we are. UP

has been in a situation where there have been cane price dues. We have just cleared our cane price dues, all of them, but there have been substantial cane price dues after the end of the season, so the government of UP is as conscious on cane price being actually distributed to the farmer than on merely announcing a high cane price. We do not have expectations of a high cane price in the coming season. There are no political elections around the corner and I think the cost of production of cane at a figure of around Rs. 170-175 per quintal is good for the farmer, the SAP last year was Rs. 160 per quintal, so we are expecting a reasonable SAP which will be substantially less than what was actually paid by the UP factories including your own factory.

- Achal Lohade** When do we expect announcement relating to the SAP to come in? Will it be as late as October or we may look at SAP announcement anywhere in July or August?
- Dhruv Sawhney** October at the earliest.
- Achal Lohade** The other question was relating to the ethanol program. What is the current status and how are we looking at it going forward?
- Sameer Sinha** Well, the ethanol program is before the union cabinet and the government is expected to take a view on that and the earliest I believe that this program will take off will be the next quarter which is the last quarter of this calendar year.
- Achal Lohade** Some industry players are talking about the growth in Brazilian cane production to slow down compared to what we have seen in the past four to five years, just wanted to get your sense on the Brazilian growth in the cane acreage or the Capex cycle?
- Tarun Sawhney** Our expectation is very similar that the massive growth that we have seen in cane production in Brazil will taper down over the coming years, what is becoming clear is that the fresh acreage on cane has reduced this year compared to last few years, so our company's opinion is very much the same as the comments that you just made.
- Achal Lohade** Thank you.
- Moderator** Our next question is from the line of Shipra Pandey of HSBC. Please go ahead.
- Shipra Pandey** Sir, you have taken an inventory write down of Rs. 80 odd crore. This is the cumulative write down in nine months. Out of this you had taken a provision of Rs. 50 crore in the last quarter and the remaining Rs. 30 crore have been booked in this quarter, so the EBITDA whatever is getting reported, is coming out to be some Rs. 82 odd million, would that actually be Rs. 382 million.
- Suresh Taneja** Yes.
- Shipra Pandey** Thanks a lot for this clarification, my second question is regarding the distillery sales guidance as well as the price, the prices have been coming off of late, so what is your view about the distillery price?
- Sameer Sinha** Well, the prices are coming down because there is an oversupply situation of alcohol, this will correct once the ethanol program takes off. The prices are in decline and they would come down by about a rupee or a number like that going forward.
- Sameer Sinha** It is really determinant on this ethanol program and then the pricing of that, so that is the uncertainty for the next few months only.
- Shipra Pandey** Are the ethanol prices expected to start in October?

Sameer Sinha With the new production, yes.

Shipra Pandey And the price right now which everyone is still expecting it to be is close to Rs.27 for ethanol.

Sameer Sinha Some people are even talking about Rs. 25.

Shipra Pandey All right, regarding your cogen business, in fact in this quarter the distillery and cogen volumes were very high and the cogen realizations was also quite high, just wanted to know what was the average cogen realization for this quarter?

Sameer Sinha Well, the average cogen realization has been at the regulated prices, which would be approximately about Rs.3.89 / unit, so that is the regulated price at which we were operating.

Shipra Pandey What about the power that was produced using coal?

Dhruv Sawhney That will be in the fourth quarter.

Shipra Pandey If I say that right now you have produced close to 133 million units in nine months, what would be the guidance for the entire year?

Dhruv Sawhney We do not give guidance but we are expecting some production through coal in this quarter and that will add to the fourth quarter.

Shipra Pandey How many days of production approximately in the entire quarter?

Dhruv Sawhney Well, it is only one unit, so it will be about 45 days.

Shipra Pandey The CER sale of some Rs. 61 odd million, has been recognized in the cogen segment only?

Dhruv Sawhney This carbon credit is for the year 2007-2008. We have an application which is being processed for two years simultaneously now because there was a lot of problem in getting this through because of the bureaucracy and also many other companies have not got through, but it is very good that we get it and actually got the carbon credits, so now we will be getting 2008-2009 and 2009-2010 processed in one go and this we expect by third quarter FY 2010-2011. This is two years' earlier, the one that we got now.

Shipra Pandey So, this Rs. 61 million has been recognized in this quarter's revenue and EBIT for cogen segment. That has been kind of inflated and that is why I was just trying to fit in. Okay, thanks a lot.

Moderator Our next question is from the line of Sangam Iyer of Alpha Accurate Advisors. Please go ahead.

Sangam Iyer My question is pertaining to your engineering segment. We had earlier guided for around 40% growth in this particular segment for the whole year and as of now in the nine months we have done around 29%, Does this guidance still stand with respect to the overall growth on YOY basis or is there any change because of the delay in client off take?

Dhruv Sawhney We do expect about 30-35% growth by the end of the year, if you look at all the three businesses. And as I said turbines is about 20-22%, water will be almost 70% and gears is around 35%, so by and large we are looking at figures of 30-35% or so and we are expecting a similar growth rate next year.

Sangam Iyer Could you just give an idea on the margin profile for the steam turbine segment? We are currently clocking at around 23% kind of level at the EBIT, so is there any

chance of expanding that going forward or is this a more sustainable kind of a level in the long term basis that one should be looking at?

Dhruv Sawhney Our EBIT level is probably one of the highest in the world, it is an extraordinarily high level, now as we expand rapidly the EBIT for the nine months is 22%, we are looking at maybe a percent or so in the long-term coming down, but we will still be over 20 to 21% and sometime going to 22%, so it is a flat EBIT going up and down by 1 or 2% in quarters but it is really the volume growth that we are looking at which is there as an opportunity. We are also expanding quite rapidly in 2010-2011 in exports and in our customer care segment. We are not expecting any growth in margins but we are not expecting any rapid decline either.

Sangam Iyer For the water segment, how should one be looking at the EBIT level, with more and more larger projects coming in, we are currently at around 12% for the first nine months, is that the level one should be looking at? I think during the call you had mentioned around 10-12% or something like that if I am not wrong?

Nikhil Sawhney Yes, I believe the margins for this business should maintain at around 12% up or down 1 or 2 odd percent from quarter to quarter basis, this is partly driven by the fact that the business is growing very rapidly, there is provisioning that is taken in each project which would be reversed only at a point in time once we have closed it, so those will lead to certain spurts in margin, but I think on a conservative viewpoint, it is good enough for us to take.

Sangam Iyer For the gear segment, 30% plus is the level that we have been sustaining for quite some time that. Is the long term number that one should be looking at.

Dhruv Sawhney I think 30% is a fair number on a long-term basis.

Sangam Iyer Could you recap on the outlook that you have been in for FY 2011 for this particular segment, engineering segment, how should one be looking at that?

Dhruv Sawhney As I said we are looking at growth of over 25% in turbines, which is more than the growth in FY 2010. In water, we are looking at over 50% growth, maybe even 60% if we get this one where we are L1 it will be even higher, Rs. 200 crore on just one order, but of course these things till come, we cannot put them in to planning, as I said not only are we looking at growth of over 30% we are evaluating these strategic opportunities for the group which is also quite exciting because this is increasing our geographical and product spread.

Sangam Iyer Just a clarification, the 50% to 60% in water segment is excluding this Rs. 200 crore order.

Dhruv Sawhney Yes.

Moderator Our next question is from the line of Anup Ranadive of Tower Capital. Please go ahead

Anup Ranadive Regarding the closing stock situation, you mentioned that according to ISMA and you mentioned about 5.9 million tonnes expected at the end of September whereas according to some press reports and according to the government the number is expected to be in the range of about 2 to 2.5 million tonnes. First question regarding such a huge discrepancy in both the estimates and second the government is estimating about 2-2.5 million tonnes of closing inventory, would it really go for decontrol at this size specially on levying import tax on sugar?

Dhruv Sawhney Let me clarify, while I would not like to comment on any report that you are saying from a government figure, it depends when you got it, but the first thing is that production now is pretty certain at 18.8-19 million, because these figures are very recent and so if you go on a little earlier you may not have had the same figure, so if you have 19 million as production, that is the first, the next is that the imports that

have come in up to the end of June are fairly accurate, so people also know the contracts of sugar that are outstanding and what may come until September, so we have that. Then third is the consumption, consumption is pretty easy because you have the government releases, so when you have releases up to the month of July and so you got only two months more of releases, so one can be slightly off here or there, and the opening stock figure is as per the excise data. The main point is if there was forecast were such low opening stock for next year, the sugar prices will remain much higher today.

Anup Ranadive Actually I read the report in today's newspaper.

Dhruv Sawhney I hope you are right then I will be getting Rs.3 more today.

Anup Ranadive Second question is regarding the SAP, you expect the SAP in UP to be about Rs.170-175, however just a hypothetical question here, if the SAP is round about Rs.200 and you actually have to pay 200 rupees per quintal and assuming you have an increase in sugarcane production of about 20-25% what would be your tentative cost of production for the next year?

Dhruv Sawhney Let us not go in to these hypothetical things, we do not have long to wait but I did not say I expect the sugarcane price, I said the cost of production to the farmer is around that figure. He gets an adequate return at around Rs. 170-175, the return to the farmer, so that he does not switch to another crop and with the yields of today is, he going to be fine at that price. So from a farmer point of view I really would not be wanting to speculate on what is in the jurisdiction of the state government.

Anup Ranadive Let me rephrase, if you pay like Rs. 170-175, and assuming a 20-25% increase in sugarcane production, then can you provide with a tentative cost of production, This year it was about RS. 28.5, assuming you do? Ballpark number is perfectly fine.

Suresh Taneja If your basic cane price is about Rs. X, I think you will spend about Rs. 10-12 more in order to get the cane landed at factory and then one of the variable is the recovery, so whatever is the recovery it has got a great implication for total cane cost per bag of sugar and then conversion cost roughly is between Rs. 250-300 per quintal.

Anup Ranadive Thank you.

Moderator Mr. Sunny Agarwal from Aditya Birla Money, please go ahead.

Sunny Agarwal What is the transfer price of molasses and bagasse?

Suresh Taneja Are you talking about transfer prices of molasses to distillery and to cogen?

Sunny Agarwal Yes.

Suresh Taneja We do it on a market related basis completely.

Sunny Agarwal Can you help me with the market price? What is the current ruling price of molasses and bagasse?

Suresh Taneja The current molasses price would be in the region of about 180 to 200 rupees as far as the unreserved molasses is concerned. For bagasse, there is hardly any transaction of bagasse at this particular point of time; bagasse has been between 175 rupees to 210 rupees during the season.

Moderator We have one more question it is from the line of Abhishek Soni of Canara Robeco Mutual Fund. Please go ahead.

Abhishek Soni Just wanted to check on the overall borrowing figure and breakup in to the short-term borrowing as well as long-term borrowing?

Suresh Taneja Our total debts have been approximately about Rs. 1, 180 Crore comprising of Rs. 540 crore of working capital loans and Rs. 640 Crore of term loans.

Dhruv Sawhney We have some sugar development fund loans which is about Rs. 80 crore.

Abhishek Soni Thank you.

Dhruv Sawhney Thank you very much everybody and thank you for joining our call. We look forward to talking with you again after our annual result in November.

Moderator Thank you Mr. Sawhney, thank you gentlemen of the management team. Ladies and gentlemen, on behalf of Triveni Engineering that concludes this conference call. Thank you for joining us on the Chorus call conferencing service and you may now disconnect your lines. Thank you.