



Triveni Engineering & Industries Limited Q3 & 9MFY13 Earnings Conference Call August 2, 2013

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- Moderator** Ladies and gentlemen good day and welcome to the Q3 & 9 months FY13 earnings conference call of Triveni Engineering & Industries Limited. 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 this conference call, please signal an operator by pressing * followed by 0 on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Rishab Barar of CDR India. Thank you and over to you sir.
- Rishab Barar** A warm welcome to all of you participating in the Q3 & 9 months FY13 results conference call of Triveni Engineering & Industries Limited. We have with us today on the call Mr. Tarun Sawhney – Joint Managing Director; Mr. Suresh Taneja – CFO and Mr. Sameer Sinha – President 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 may be forward looking in nature and a statement to this effect has been included in the conference call invite which was mailed to everybody earlier. 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 like to start this conference with opening remarks from the management followed by an interactive question and answer session where you can discuss your views and key issues. I would now like to hand over to Mr. Tarun Sawhney to share some perspectives with you with regards to the company's operations and results for the quarter under review. Over to you Mr. Sawhney.
- Tarun Sawhney** Thank you Rishab. Good afternoon ladies and gentlemen and welcome to the 9 months Q3FY13 financial results review.
- Let me start off by taking you through the financial results and then focusing on our individual businesses coupled with a quick perspective on the industry. Our net sales for the 9 months stood at 11% higher at ₹ 1,541.05 crore and our EBITDA was also higher at approximately ₹ 100 crore for the 9 months period. However, we have due to market conditions, had a loss in the three months of about ₹ 24.25 crore for the quarter and ₹ 55 crore for the 9 months and our profit after tax for the same period is ₹ (19.3) crore for the quarter and ₹ (38.8) crore for the 9 months. The profitability for the quarter and 9 months has been impacted by lower profitability in both the sugar and engineering businesses and specifically in the sugar business because of a significant inventory write-down that we have taken in the last quarter.
- Let me move towards the sugar industry and give you a small perspective of the industry before focusing on the company's results. Contrary to an initial estimate and even as far as our last call, the production for the country has ended up at an estimated 25.2 million tonnes. This is much higher than what we had expected in January and also a little bit higher than what we had expected in early April. This increase is primarily due to a higher production in the state of Maharashtra and it is already tantamount to a small

decline from the previous year. According to our estimates, and we have done some substantial review for the next year's crop, and we estimate the production somewhere around 23.5 million tonnes. We would like to be conservative in our approach, so we have been conservative despite the forecasted decrease in production in the state of Maharashtra and in the state of Northern Karnataka coupled with a small increase in the state of UP. It will lead to an overall reduction, to about 23.5 million tonnes; however, this estimate again can be revised downwards and that downward revision would primarily depend on the state of Uttar Pradesh. Our forecast indicates that Uttar Pradesh would produce 8.2 million tonnes which is about a half a million tonnes higher than this current year. That is a substantial increase and that increase has predicated on higher recoveries simply because of timely rainfall and also because of timely sowing. Having said that, this is very early in the planting season. We are the middle of the growth period and frankly speaking the weather and the persistence of any pests and disease over the next few months can have an impact on the crop. However as of now, across the state the crop looks fairly healthy. As you all know Dr. Rangarajan Committee had recommended a revenue sharing formula for sugarcane pricing. The Karnataka government has passed an act in accordance with this recommended policy and we believe that the state of Maharashtra is also considering a similar move prior to the start of the next season. This is a remarkable initiative taken by these two State Governments and we hope that this will have a positive influence on the Government of UP. We all know that next year is an election year and frankly speaking if the State Governments of Karnataka and Maharashtra feel that there is no real need to move towards an SAP or to an arbitrary price mechanism, I think that is a very plausible argument for the State Government of Uttar Pradesh as well. One hopes that the State Government will also view this favorably. The events over the next 3 months will be very important in this decision making and of course the decision of setting a SAP if that case may be. The central government has increased the fair and remunerative price by 24% to ₹ 210 per quintal of cane and this FRP is of course linked to a recovery of 9.5%. Over the last few quarters, there have been steady imports of sugar into the country. This is one of the reasons amongst other factors that have resulted in a downward pressure on sugar pricing. We have estimated sugar imports of approximately 6,50,000 tonnes has happened over the last 7-9 months. It is a very substantial amount. The combination has been between raw and white sugar and this is part of the reason for the decline in prices. However, the Central Government in the last few weeks has increased the import duty from 10% to 15%. In addition to that, the depreciation of the Indian rupee to ₹ 61 levels has also curbed the inflow of sugar. I would like to point out that given international prices at this point in time, and given the rupee and rupee forwards at this point in time, it is extremely favorable for export from costal millers. In fact, over the last few days, we believe that certain contracts have been entered into for exports. Of course they are small in quantum and we are still ascertaining the total quantum. Having said that if this is to actually move forward and sugar is to exit India that is a very positive news for the month and quarters ahead and especially considering the fact that we have got 23-23.5 million tonnes of sugar being produced in the next year.

On the international front of course it is estimated that the global production will record 10 million tonnes more than consumption in 2012-13 and further impacting global sugar prices and according to a recent industry report, preliminary projections for the season 13-14 indicates a fourth year global surplus of around 3.7 million tonnes of sugar.

Returning to our business, from an operating perspective, we had a very good year in sugar. Our cane crush was 10% higher, our recovery was 0.19% higher to 9.28% season average from 9.09% in season 11-12 which is a substantial increase and one that I feel we can sustainably increase over the coming few seasons. That culminated in a 12% increase in sugar production and very close to the estimates that I had shared with you on the last earnings conference call. Over the quarter, we have had a net sales of about ₹ 320 crore and PBIT, a loss of ₹ 7.58 crore. The loss in sugar I would like to delve on for a couple of minutes. Over the quarter, we have seen a rupee per kg fall in average sugar pricing. That of course is because of higher production in the country amongst

other factors, including imports, of course higher production in Maharashtra is as I had mentioned. The other important factor from the demand side is weaker demand during the month of June and this has been precipitated by early and sustained rainfall across the country and that of course can be seen in discussions that we have noticed from the institutional buyers from their perspective. We supply to the large beverage manufacturers and FMCG companies, etc., and we have seen their demand petered off and not meet the expectations that they had mentioned to us in our discussions with them 5-6 months ago.

Looking at the company's initiatives within the sugar business, as you all know we have converted our plant in Sabitgarh into a refinery. That conversion has been very successful and I am happy to report the quality of sugar being produced at the unit is of very good and global quality. The unit in this season made approximately 7 lakh bags of sugar. In addition to that, we had initiated incidental co-gen projects at two of our units. Those units ran for part of the season and ran very well. We expect that going forward these units will run for full seasons and will be able to generate profits for the company. Over the next few months, we are embarking on some small capital expenditure. The most significant part of that is that we are converting our largest sugar unit Khatauli into a refinery producing European grade sugar of a very high quality. What this means is that from the start of the next season, ~40% of the sugar produced by Triveni will be refined sugar and it means that commensurately we are the significant delta between plantation white and the refined sugar, we would be beneficiaries of that. In addition to that, we are also doing some marginal balancing at three of our other units to reduce steam consumption and to improve crushing very marginally. This entire balancing would allow these three units to perform at a much higher standard going forward and these are three of the other units where we have not done very much work in the last year and we feel that there is tremendous promise for the following year.

Our push on institutional sales has been showing great promise and over the last 6 months, a larger portion of our sugar is moving towards institutional side through direct sales. This is an initiative where I feel that we will continue to push considering that 70% of the consumption of the country is with institutional buyers. That 70% usually goes through the trade. We believe that going directly to manufacturers has benefits for the company.

Moving towards the co-generation business – The quarter's performance was also fairly reasonable because that is on the previous quarter of the corresponding year. Let me suffice to say that both the co-generation units have run in the month of July and so we will be seeing some performance in our Q4 results going forward. The operations of the co-generation unit have remained steadfast and at a very high level.

Moving to our distillery business – The performance of course is in front of you in the note that we shared, but let me talk a little bit more about the business. It is a business that has delivered extremely well not just in Q3 of the year, but across the year and this has been due to sustained performance, uninterrupted manufacturing and maximum capacity utilization. We have achieved levels we have never had in the past and result of that has been greater profitability. In Q3, 66% of our dispatches were ENA and the ENA price has already risen in Q4. As we entered the month of July, we have seen an increase in ENA pricing and we believe that moving into August or September, the pricing levels look even better. We are holding fairly significant stocks of about 83 lakh liters as on 1st July. This is very substantial and we believe that this will assist us in delivering better profits in this quarter and of course moving forward. We are exploring further opportunities in the distillery business because we believe this is one of our core-strengths especially within our sugar business.

Looking very quickly at our high speed gear and gearbox business – The quarter was slightly disappointing and that is because some orders were pushed into Q4; however, let me share with you that I expect both record revenues and record profitability in Q4

which will compensate for any shortfall from our budget for the 9 months and I believe that we would have a very robust year both in topline and especially on the bottom-line. It is an exciting journey that we have embarked on this business. The focus area of exploring international marketing has borne tremendous fruit. 17% of our products, dispatched products are now exported from 5% in the previous year. We see this percentage going up very substantially going forward. In addition, our R&D efforts are also bearing fruit. We have looked at bearing design as an important part of our philosophy and that efforts have also been bearing fruit very nicely. In addition to that, we have also looked at designs of planetary gearboxes and those designs will be marketed starting October of this year.

Our water business has also had a disappointing quarter; however, I would like to mention that in July, we have received ~₹ 210 crore worth of orders, three particular sites which are executable in the next 18 to 24 months and we believe that with this kind of a trend, we are poised to have a good fiscal 2014 in the water business and of course looking forward with more expenditure done by municipalities and by corporates. We continue to believe that this business has a very robust model. Thank you very much. I would like to open the floor for some questions.

- Moderator** Thank you very much sir. Participants we will now begin with the question and answer session. We have the first question from the line of Baidik Sarkar from Unify Capital. Please go ahead.
- Baidik Sarkar** Could you throw some more light on how exactly you believe Q4 is going to make up for the depressed numbers for first 9 months?
- Tarun Sawhney** I assume gears?
- Baidik Sarkar** That is right.
- Tarun Sawhney** Some of our customers with the vacillation especially in the currency market decided that they would accept products that they had already ordered just a month or two later. So our dispatches just moved forward by a few weeks from Q3 to Q4. In addition to that, we have also booked some refurbishment orders which are shorter duration orders, sometimes even there are two month orders in terms of booking to dispatch and those orders will also fall into this quarter.
- Baidik Sarkar** Did you mean that the earnings momentum in Q4 from just the gear business is good enough to make up for the entire losses at the consolidated level?
- Tarun Sawhney** No, I am talking about the business at standalone.
- Baidik Sarkar** Just from a standalone perspective?
- Tarun Sawhney** Right.
- Baidik Sarkar** Secondly, what is the inventory level in the industry as we talk?
- Tarun Sawhney** In the industry, I believe the inventory levels are in the high 50s, early 60s percentage point at the beginning of this quarter.
- Baidik Sarkar** Could you please give me a number in actual fiscal units?
- Tarun Sawhney** I do not have that number with me. If you call us offline, we will be able to share it with you, work it out and give it to you.

Baidik Sarkar So which means unless and until your estimate of 23.5 million tonnes of production actually hits the shelves next year, is it realistic to assume that at a standalone EBITDA level, the sugar industry will struggle to be breakeven positive?

Tarun Sawhney No, I think at the EBITDA level, everything is absolutely fine. A lot of things are predicated on the assumption of cane price and that is a big black box. Without knowing exactly what that cane price are going to be especially for the state of Uttar Pradesh, it is impossible to be able to look through financials. However, let us look at the estimated production, 23.5 million is a little bit higher than consumption in the country which is about 22.5 to 23 million and therefore what I am indicating is half a million tonne addition to stocks. Having said that given what international prices are at this point and given the weak rupee, there is an opportunity for export. We are seeing that interest is generating and gaining momentum amongst the southern and coastal millers, export contracts have been entered too. If this gains momentum, frankly speaking we could be in balance position and the year end stocks could improve and that will result in better sugar pricing.

Baidik Sarkar And what are your ENA realizations right now?

Sameer Sinha ENA realizations in July were in the region of about ₹ 34-35 which have already jumped for August orders to about ₹ 36.50- ₹37- 37.50 range.

Baidik Sarkar What is the realization of ethanol?

Sameer Sinha The weighted average pricing for the orders that we have received is just a shade under ₹ 36.

Baidik Sarkar For ethanol?

Sameer Sinha Yes.

Baidik Sarkar And the sales mix is still 20-80 right, how does it work between just ethanol and ENA?

Sameer Sinha For ethanol, we have orders of about 130 lakh liters and the rest will be ENA with a very little quantity of RS or SDS thrown in. Let us say percentage would be about 30% for ethanol and let us say 65% for ENA, 5% would be the others.

Moderator Thank you. We have the next question from the line of Tanuj Makhija from Ambit Capital. Please go ahead.

Tanuj Makhija Can you provide some more color on your outlook for water treatment industry in India and can you elaborate please which are the three orders that you have won, are they in municipal or industrial segment?

Tarun Sawhney All three orders are in the industrial segment and in terms of looking forward, we have seen the interest for municipalities to look at orders. The interest is certainly there for the industry as well as for the government in terms of moving to a better and more sophisticated water platform across the country. Having said that, we have had a sluggish industrial growth. We had challenges that the industry has faced which has caused postponement of projects, postponement of power plants etc. These plants are necessary for the country. They will come up. The fact that they have been delayed by a year may be a little bit longer is terribly unfortunate, but we do believe that this is central for the country to move forward. When they do come up, they have a demand for water and we hope to participate aggressively in that particular business. As far as the municipalities are concerned, we have seen some interest generation starting to pick up and we are participating in several orders. Our concern at the moment is quick order

finalization. Again, this is not in our hand, but these are initiatives that municipality and State Government needs to take up aggressively and again it is need of the hour. If it does not happen this month, it will probably happen next year. If not this year, it might happen year after that. Our hope is to provide knowledge to our stakeholders, to our customers to help them facilitate their decision and bring that decision forward.

Tanuj Makhija We have seen that the order inflow has slowed down. So do you see competition increasing and players aggressively bidding for orders?

Tarun Sawhney I do not think so. I think we participate very aggressively in orders and just to give you an example over the last 31 days, we have received ₹ 210 crore of orders and with the possibility of going up to ₹ 255 crore. So that is very substantial. This is a timing issue and we of course recognized the orders at the moment we get them.

Moderator Thank you. We have the next question from the line of Achal Lohade from JM Financial. Please go ahead.

Achal Lohade Just a couple of questions. One on the production front and the expectations.. Just wanted to get a sense as to how is the acreage in key states, UP, Maharashtra, Karnataka according to you. The latest data point and how do you see when will the clarity emerge through satellite mapping and other means?

Tarun Sawhney If you want specific numbers, we will be happy to share that with you offline, but let me provide a broad answer to you. The poor rains in the previous year in Karnataka and Maharashtra has had an impact on the next season's crop. As you know the crop in Maharashtra is a 12-15 months crop and the consequent result of that is a 12.5% shortfall into a cane acreage year-on-year in Maharashtra. Now in Karnataka that number is about 8% lower compared to last year.

Achal Lohade And in terms of the cane pricing, Karnataka has passed a law. What is the modality actually? Will it be done by any committee or straight linkage of formula or they are just yet to give out any formula?

Tarun Sawhney No, there is a board that has been formed. The board will deliberate and contemplate and then revert with a suitable number, but the parameters of that are part of the act which is that sugarcane pricing must be linked to eventual sugar price. The mechanics and modality will be worked up by the board. Similarly, I believe in Maharashtra a broadly similar model is expected to be adopted and frankly speaking that is in accordance with what Dr. Rangarajan has already expressed in his views to the Prime Minister and in his report. This kind of a pricing formula is very important for UP. If you go back for a few years, for the last 4 years we have seen a 70% increase in the SAP in UP whereas the price of sugar has only gone up by about 20 plus percent. So there has been great pressure on improving efficiencies, but with such a substantial increase in your cost of production, the net result is losses and that has been there for all of you to see from the industry in UP over the last several quarters and years. Now going forward for a healthy cane industry in UP and the sugar industry in UP and for the benefit of the farmers, such a formula is very important. The association has written to the Chief Minister requesting him to implement such schemes and we believe that there is promise. One has to work with the industry and with the farming body to find a solution that will work uniquely for the state of Uttar Pradesh.

Achal Lohade Can you highlight what are the cane arrears right now in UP and what are the arrears for Triveni?

Tarun Sawhney The cane arrears in UP are now under ₹ 3,000 crore and our arrears are about ₹200 crore.

- Achal Lohade** Do you see these cane arrears for the industry becoming zero by the end of this sugar year?
- Tarun Sawhney** I think it is going to be a challenge for the total ₹ 3,000 crore to be paid. There are some companies that are already by far facing a tremendous difficulty and this has been perpetuated not because of the millers frankly speaking and those mills will have great difficulty in paying the entire amount.
- Achal Lohade** Just wanted to get a sense as to how much of the total industry in UP would be under stress according to you, will it be 70-80%, will it be 40-50% depending on the ownership?
- Tarun Sawhney** Well this is very much on the record, but it is very difficult to give an estimate. I must say I do not track the financial performance of other companies; however, we are very active in the association. We do spend a lot of time speaking to our peers in the industry and there is tremendous stress and stress across the board. I would say that there is nobody in the industry that is not feeling the stress.
- Achal Lohade** Couple of companies, the listed ones, they are talking about restructuring or going into BIFR. I was just wondering about the private sugar mills, how are they coping up with the stress actually?
- Tarun Sawhney** Very poorly. The stress is across the board. Frankly speaking despite how efficient you are with such a high cane price that we have to pay and a massive reduction. Let me take you back about 9 months. When the cane price was set at ₹ 280 which is a ₹ 40 increase over the previous year's price, the prevailing sugar price was ₹ 35-36 a kg. Now from ₹ 36 a kg, we have seen a massive slump of just under ₹ 5 a kg. It is very substantial. That is a huge drop and that pain has to be felt by one and all regardless of how efficient you are.
- Achal Lohade** Just last question if I can about the power. Have you seen the payments from government been made timely or do you think it is getting delayed?
- Tarun Sawhney** It has been delayed. The State Government released the payments for January a few days ago and there was some more payment that was released yesterday. The details of which will be out today and that will be towards the month of February. So we are running 5 months behind.
- Achal Lohade** What is the status on the UP sugar promotion policy, have you heard any development from that or any other fiscal incentive from the State Government given the stress?
- Tarun Sawhney** Purchase tax revision has been given. The quantum of benefit to the industry is under ₹ 2 a quintal. So it is less than 1%, it is really insignificant.
- Achal Lohade** And about the promotion policy, there is no development yet?
- Tarun Sawhney** The promotion policy is sub judice at this time, I wish I had better news to share with you. I think the matter is in the court. It is being fought aggressively, but there is no news either positive or negative to report.
- Moderator** Thank you. We have the next question from the line of Ashwani Agarwal from Ashmore India. Please go ahead.
- Ashwani Agarwal** One was on ethanol tenders that were floated. I wanted to find out did you participate in the first tender that was closed couple of months ago and do you have any plans to start producing ethanol at your refineries?

Sameer Sinha We have participated in the ethanol tenders. We have got orders, LOI of approximately 1 crore 30 lakhs liters and we have started production of ethanol, supplies have also commenced. They are skeletal in nature as of now, but we believe they will pick up in the coming months.

Ashwani Agarwal And the price I am given to understand was about ₹ 34-35 a liter is that?

Sameer Sinha Our basic price which we have got is just a shade under ₹ 36.

Ashwani Agarwal And this is your price realized by you or this is the ex-depot price so you have to incur the transportation?

Sameer Sinha No, that is on top of it. This is the basic price.

Ashwani Agarwal You did speak about the water business and you received a few orders during the quarter. What is the size of the order book as of 30th June in water?

Tarun Sawhney ₹ 424 crore was the order book on the 1st of July.

Ashwani Agarwal And would you be able to break that up for me in terms of municipality and industry?

Tarun Sawhney It is approximately 50-50%.

Ashwani Agarwal And in terms of the outlook, how do you see this business growing for you over the next 3-5 years?

Tarun Sawhney We are tremendously bullish on this business. We believe that if you go back maybe 2 years and we have had this conversation 2 years back, we actually believe that there would be large amount of order finalizations that would have happened; however, the market went very slow. I think next year will also be slow, but there will be movement. We have just received ₹ 210 crore of orders and just like this we will keep picking up orders, but over a 3-year horizon, we believe that there is tremendous potential. There is a lot of work that has to be done across the country. We have had surveys done, we have people that are in various parts of the country who are working with municipalities, working with industrial customers. There is a very significant potential. As the economy bounces back, the water business will be a significant beneficiary of that industrial growth.

Ashwani Agarwal And this ₹ 210 crore is over and above the ₹ 424 crore at the end of June?

Tarun Sawhney Correct.

Ashwani Agarwal And this is all industrial?

Tarun Sawhney Correct.

Ashwani Agarwal What kind of EBIT margins do you target when you bid for industrial projects or municipal projects, how do you go about it, what kind of profitability should one model on a sustainable basis?

Tarun Sawhney This is competitive information and this is very difficult for us to share.

Ashwani Agarwal What is the reported EBIT for the water business for 30th June quarter?

- Tarun Sawhney** The expenses were little high. But I will just give you the number. The PBIT number was ₹ -3.19 crore for 9M FY13.
- Ashwani Agarwal** But you were saying that your overheads were high presumably because the scale of the business is still small than it's potential?
- Tarun Sawhney** Correct. Lot of it was about the overheads recovery.
- Moderator** Thank you. As there are no further questions from the participants, I would now like to hand the floor back to the management of Triveni Engineering & Industries Limited. Over to you sir.
- Tarun Sawhney** Thank you very much. I would like to thank all of you for joining us for Q3 & 9 months' fiscal results for the '12-13. I look forward to speaking to you in about 3 months' time and I expect that I will return with better news and that is our endeavor. We have been focusing on improving our efficiencies, significant improvement in cane management, etc., in our sugar business, in our engineering businesses of course we got the orders. It is now our time for us to execute and next time when we will speak I will be post that and I look forward to sharing much better news with you at that point in time.
- Moderator** Thank you sir. Ladies and gentlemen on behalf of Triveni Engineering & Industries Limited that concludes this conference call.