Camlin Fine Sciences Q4FY19 Concall transcript

Standalone net revenue increased by 34% YoY to INR 172cr. Operational EBITDA (after adjusting forex gains/losses) grew 10% to 12cr vs 11cr YoY. Operational EBITDA margin 17.2% vs 8.64% YoY. Net profit 3cr vs 1cr YoY. On the operational front, topline grew but operational EBITDA margins was impacted due to rupee appreciation affecting raw material costs.
Consolidated: Net revenue increased 16% YoY to 268cr. Operational EBITDA grew > 100% to 21cr YoY. Oper EBITDA was 7.97% vs 4.58% YoY. NP 6cr vs -4cr YoY. Turned profitable on consolidated basis.

US subsidiary was driving factor by increased traction from new clients. Italian subsidiary running at optimum capa utilization. Vanillin business ramping up. China plant where it is produced is running at 55% cap utilization. Will increase further. Net revenue increased 23% to 892cr. Operational EBITDA grew to 69cr vs 16cr in 2018. Operational EBITDA margin was 7.7% vs 2.1 in 2018. NP was 3cr vs -24cr in 2018.

Subsidiaries:
CFS N.America grew significantly. Revenue 24cr vs 18cr in 2018.
CFS Brazil 41cr vs 25cr in FY18.
CFS Europe (Italian subsidiary) 329cr vs 277cr in FY18.
CFS Mexico 217cr vs 164cr in 18. Turnover doubled since we took over.
CFS Argentina and CFS Chile have commenced in 3rd Q.
CFS Pahang (South-East Asian market) is registering products in Malaysia. Should start operating by end of this year.

Dahej plant- expect commercial production to start in second half of FY19.

Q&A:

Q: Guidance of 1500cr revenue without Lockheed Martin in FY21. How will it be achieved?
A: In FY21, Indian operations will be >1000cr. Italian will operate at curent levels that is 325cr. Mexico will grow at 20% to 250cr. US and Brazil will grow to 75cr each. Together, expecting 1500cr.

Q: In this Q, China revenue down. Why?
A: Seasonal business. Q2 and Q3 are significantly higher in business than Q1 and Q4.

Q: Invested 60cr in Brazil and N.America. When have we invested this and break-up?
A: Over last 5 years. Don't have info of breakup.

Q:Cash and bank balance of 100cr. Debt is now at 74cr. How will we use this money?
A: The main cash is on account of money from IFC loan for Dahej plant. 70Cr is the funds drawn from IFC. To be utilized entirely for Dahej plant in the next 6 months. Rest of the cash is operational.

Q: Dahej plant timeline?
A: Construction going on in full swing. By mid-July plant should be ready for water tirals. By Sep end, will be complete. So commercial production should start in October. So part Q3 and full Q4.

Q: What is the captive consumption of Catechol and HQ in FY19?
A: In FY19, almost all of Catechol from Italy was consumed. Very little was sold. Similar for HQ.

Q: Quantity wise any numbers? Level of consumpton of HQ and Catechol?
A: Right now consuming 90%. In next 2 years, we should consume 90% of both captively. In the interim, we will sell HQ in the open market. De-bottlenecking and expanding capacity in the meanwhile.

Q: Ramp-up of Dahej?
A: Ramp-up will start in Q3 from 50%. By Q4 end, we should be at 90%.

Q: Cost saving due to Dahej?
A: Process in Dahej is better than that in Italy. HQ is more profitable than Catechol. In Italy, it is 45% Catechol and 55% HQ. In Dahej, 60% HQ and 40% Catechol. Big kicker for margins. HQ CMP is $6 whle Catechol is $2.5. Due to improved process, yield in manufacuring should improve by 10%. Significant cost saving.
Steam cost in Italy is expensive (gas based) $40/1T of steam. Dahej is coal based $15/T. Significant savings.
Waste disposal significant in Italy. In India we have approval from environmental clearance to dispose to cement units who use it as fuel.
Establishment cost in Italy (labor, electricity etc) is higher. WC cycle will save 60days.
As for forex, today also we buy from Europe. So it won't be significantly different.
On consolidated basis, there would be benefit. Right now we are making in Euro and selling in Dollar. In Dahej, both will be in Dollars. Risk of fluctuation reduces considerably.
So we should have savings of cost of $1.5 to $2.

Q: Dahej in terms of revenue? We will be using internally with interim selling?
A: Dahej is 10000T where 6000T is HQ (annually). 1500-2000T of HQ should be consumed internally and rest sold in the market. In 2 years, it will reverse- we will consume 4000T and sell only 1500T. The additional revenue from HQ at $6 for 4000T would be 240million dollars.

Q: Would so much additional capacity affect prices?
A: Yes. When 6000T HQ capacity comes online, price correction should happen from $6 to $5. This will impact the 4500T manufacutring in Italy. However, much higher delta we will get from Dahej. On consolidated basis, we should be a dollar up from Dahej.

Q: Can Dahej help you penetrate blend business?

A: Blend business correlation with Dahej: Some of our blends (30%) is TBHQ and BHA based products. Significant advantage will be there due to veritical integration. Will give us access to much higher volumes in this competitive market.

Q: Share of blends in revenue and forecast for next 2 years? US has turned positive this Q?
A: In FY19, we did 263cr out of 890cr. This 263 should go to 350-375cr in the next 2 years.

Q: Rampup in US?
A: 13cr runrate in US last Q. By end of this year, we should be at least 20-22cr on a quarterly basis. This is the first Q where we are profitable.

Q: Current performance sustainable regardless of seasonality?
A: Yes. Sustainable. We should be profitable going forward.

Q: Do we foresee any challenges in Dahej with the timeline? Already delayed?
A: Dahej was delayed due to financial closure. Not due to execution. IFC funding closed in Sep. And then we started construction. On track right now for mid-July for completion. In Q3 we will be in commercial production.

Q: Post setting up of the Dahej plant, do we see any issues on the operational side since the compound is bit difficult to make?
A: We have enough experience manufacturing this product in Italy. No issues should be there.

Q: US guidance. 20-24cr range for run-rate is given. What kind of visibility do we have? Is business already in?
A: Some business are already in. Some are in advanced stage of negotiation. What we gave is an estimate.

Q: Progress in Negolyte with Lockheed martin?
A: Currently working on 3 fronts.
One, we have given contracts for basic engineering which should be over by October. This will give us an estimate of the investment required for that plant. Then we can get into an agreement with LM for setting up the plant.
Second, we have to produce some material this year- first is for their gamma facility and the other for their 1MW battery. In current year we have to supply some material for which we had to make some investments which LM is paying for since this is exclusively for them.
Third, the scope of work we have with LM is also expanding. Some of the chemicals we were planning to buy we will produce internally. So new opportunities opening up.

Q: Quantum that is being supplied to LM? What is the investment done?
A: 15cr funded by LM for this particular quantum. Till engineering is done and cost estimate is made, difficult to give timeline. Afterwards, part financing will come fromLM. Balance we will have to do.

Q: China subsidiary. Why is topline so volatile?
A: Challenge is in the market, not production. We are in the process of registering with all the large flavor & fragrance companies (top 10 companies globally). Once done, we can sell directly to them instead of through distributors which constitues 80% as of now. By end of current calendar year, we should be done with all registrations and should be ready for their next year contracts. This year we will be at breakeven level. Next year onwards, it should start contributing.

Q: Vannillin question. We will be breakeven this year, right? Will it be due to utilization levels improving or guaiacol issue discussed last quarter?
A: The RM situation is same. We don't expect prices to come down soon. So it is mainly capacity utilization. Our supply of guaiacol to the JV in China, is positive on consolidated basis. Only China is losing money.

Q: Are peers increasing price which you are not able to do?
A: We have two competitors- Solvay is the main one for F&F customers. They always sell at a premium to F&F guys. The other competitor is China. Capacity as large as Solvay. At the trader-distributor level, we compete with Chinese supplier and with Solvay at F&F level. Chinese company is vertically integrated for this product. Solvay is not vertically integrated since they have to buy Glycilic acid. So when we move to F&F, we will be competing with Solvay and hence a level playing field.

Q: Poor gross margins on consolidated basis in Q4?
A: Around 45-46%. Should be stable going forward.
Q: Q4 had low Vanillin sales. So overall FY20 can we do more than 1100cr topline?
A: Yes. Margins would also improve. Should grow topline by 20%.

Q: Vanillin side. How competitive are we currently? And with Dahej plant will situation improve?
A: With Dahej our cost of production of Catechol will decrease substantially compared to Italy. So Vanillin business will become profitable. Presently it is profitable at the Guaiacol level, On the Vanillin level it is just breakeven. When Catechol cost comes down, our margins would improve significantly at the Guaiacol level.
Q: Are our prices similar to Solvay?
A: No. Right now we are competing with Chinese producer. Once we get to F&F, where the pricing is better, then we would be competing with Solvay, not Chinese.
Q: How long will it take?
A: Sampling is over. We are getting registered with the big companies. Expecting by Oct-Nov, we will be in time for their annual contracts next year. Already won some small contracts for this year.
Q: Volumes through distribution in Vanillin currently?
A: Total capacity is 4000T. Currently doing 2200T. Doing 85-90% through distributors. Will change significantly next year. China capacity should be profitable by 70-73% cap utilization. Expected by this year.
Q: Till the time Dahej comes up, what can improve our profitability?
A: We are seeing traction for the blend business in most of the markets. Blend business is growing. Second, process improvement- we are focussing on manufacturing process which can improve margins by couple of percent in the next quarters. Right now team is looking

into it. So we should see sequential improvement in margins till the time Dahej comes online.
Q: With the cost effective process we have already developed for Guaiacol (part of chemical business), that operation is also getting supported by cost-effective Catechol. Keeping this in the mind, what is the kind of progress on the performance chemical one should look at for the current year and margins?
A: Guaiacol is running at capacity (our own consumption). We need to expand the capacity. Probably towards the end of this year. Current capacity with the vapor phase (new process), we produce 300T/month. BY the end of this year, we want to take it to 450T/month. This should give us significant cost savings. Also some product will be sold in the pharma market.

The other products like TBC.. we are growing TBC at good pace. On a yearly basis we should do 30% higher volume compared to last year. Currently we are at full capacity. Expanded now to 220-230T/month. For all of last year we produced 1700T. So there is an uptick.

Similarly MEHQ and CME. Due to high cost of HQ, we are not significantly profitable in MEHQ. With Dahej, we will have great opportunity to gain market share in MEHQ. It will become an important product of our portfolio. Last year we did 500T. This year we are doing 70T/month till Dahej. After Dahej, it should be 150-200T/month of MEHQ.

We have also launched another product called HQE which is HQ based. We should see a ramp up this FY. We started the small business in March at 10T. Now ramping up to 30T/month. By end of this year we hope to take it to 50T/month. It is a $10 product and have reasonable margins in that.

Q: So for performance chemicals volume wise 20-30% growth. So can we have 20% kind visibility?
A: Right now we have more capacity than the market. So lets get Dahej ready and then we will work on capacity expansion for the downstream products.
Q: How will US-China trade war affect Vanillin business?
A: *High Vanillin (??)* is added in Schedule-3 which is under 30% tariff. Vanillin is not in Sch-3. Most likely it will come in June around 20% range. If it does come, we will have the opportunity to bring the material to India, purify and sell in US market. But overall, if tariffs are high, Chinese producers will try to sell in the other markets and there will be pricing pressue in those markets. So overall there shouldn't be much impact.

Q: US business was breakeven this Q. Despite that, quarterly EBITDA was 16-17cr. Assuming that the loss at EBITDA level in US was ~3cr. Why hasn't that been populated into the EBITDA?
A: We have taken a writeoff from a customer in Italy of around 4cr. It is an old outstanding for the last 8 years, not cash. It is booked in other expenditure.
Q: Future performance. You said EBITDA for US will be breakeven. For the last 3 quarters, it has been 3cr loss per Q. Will this 9cr be added next year?
A: Yes. To the 75cr EBITDA, an additional 10cr will come and one-offs. So the trajectory will be on the increasing trend from where we are. Dahej will have additional benefits from Day-1.
Q: Any particular geography which can affect profitability? Like Mexico?
A: Not really. As for Mexico, fishing season gets over by Nov-Dec. So Q4 will be weaker than Q3 due to cyclicality. Similarly in Peru. On an overall basis we are on target to grow by 25%. Only risk is dollar.

Q: In other intangible assets, it is down from 23.5cr to 17.5cr YoY. Why?
A: Existing intangible assets have been amortizing. No impairment of any technological assets. Since we had subdued performance in CFS Europe, N.A and Brazil, all investments are tested for impairment at year end. No impairment since future profits will justify the investments.
Q: When is conversion of warrants due?
A: It was issued in Feb 2018. Due in August 2019.
Q: What is the intent of the promoter? There could be a mismatch in capital allocation or sourcing of capital?
A: We are working on it. We are looking at all options.