



CHAMBAL FERTILISERS AND CHEMICALS LIMITED

Q3 FY 2014-15 Results

Investor/Analyst Conference Call Transcript

February 9, 2015

Raghavendra Jaipuria Good afternoon and thank you for joining us on Chambal Fertilisers and Chemicals Limited Q3 FY15 Earnings call.

Today we have with us the senior management represented by Mr. Anil Kapoor (Managing Director), Mr. Abhay Baijal (CFO), Mr. M. S. Rathore (Vice President - Legal, Corp Com & CS), Mr. V. K. Gupta (Vice President-Marketing), Mr. Anuj Jain (General Manager-Finance) and Mr. Rajveer Singh (General Manager-Legal & Secretarial). I would now request Mr. Kapoor to make his opening remarks. Thank you.

Anil Kapoor

Thank you. Good afternoon ladies and gentlemen. Welcome to our earnings call post declaration of third quarter results for FY14-15. Before we go further I would like to mention that we have sent today a letter to stock exchanges making the following announcement. I will read out the para.

“This is to inform you that one of our urea plants at Gadepan, District Kota, Rajasthan has been shut down from February 8, 2015. The shutdown of the plant is necessitated due to unfavorable policy of Government of India for production beyond 100% capacity of the plant for the financial year 2014-15. The company shall carry out routine maintenance activity during the shutdown period and the plant is expected to resume operation during last week of March or first week of April 2015.”

Now, I would like to share with you some of the financial highlights for the period ended 31st December 2014. In the first nine months of 2014-15, our revenue increased by 12% to Rs. 7,329 crore against Rs. 6,540 crore and Profit Before Tax increased by 48% to Rs. 506 crore from Rs. 341 crore as compared to the corresponding period of last year. In the nine months ended 31st December 2014 the revenue of our fertilizer and agri input segment increased by 12% to Rs. 6,503 crore against Rs. 5,812 crore in the corresponding period of last year. The revenue of shipping was up by 22% to Rs. 520 crores however textile remained at the same levels as last year.

I will now request all the participants to ask questions you may have with regards to our results. Thank you.

Moderator

Thank you very much, sir. Ladies and gentleman, we will now begin the question and answer session. The first question is from the line of Balwinder Singh from B&K Securities. Please go ahead.

Balwinder Singh

My question is more on the regulatory side. Firstly on the IPP linked policy. We have been hearing for last six months that it will come but nobody knows when it will come. Then I think there is a clause about the fixed profit which

will save us in terms of lower IPP prices but again there will be no upside from that. So how is the industry reacting to that? And second question is about farm-gate urea price increase?

Anil Kapoor Balwinder, as of right now there is no policy indication. The government has assured the Industry that some policy change with respect to NIP 2008 will happen. However, even if that policy were to change, Gadepan-II would not have made money. We took a conservative call and shutdown the plant. As far as the policy is concerned we have only the assurance of Department of Fertilizer that change in policy will happen. If it will not happen I really do not know what the repercussion on the industry would be.

As far as your second question of farm-gate pricing or increase in farm-gate pricing, there is no indication from Government of India on this subject.

Balwinder Singh I just want to understand if anything is moving from the Government side on the regulatory issues post the new government coming in or it is still status quo?

Anil Kapoor If anything is happening we are not aware.

Balwinder Singh And sir, earlier we had constituted a committee for evaluating opportunities in the non-core business, any further update on that if you can share?

Anil Kapoor Balwinder, we are working on all the other segments of our business - whether we want to continue with them or not. As and when anything fructifies, we will definitely inform the investor community.

Balwinder Singh Sir, are we looking at restructuring the business or divesting. I just mean to understand what is the direction?

Anil Kapoor The direction will be more towards divesting.

Balwinder Singh Probably it will take some time before you inform the stock exchange?

Anil Kapoor Whenever there is a serious proposal and the board approves it, we will inform stock exchange immediately.

Moderator Thank you. The next question is from the line of Falguni Dutta from Jet Age Securities. Please go ahead.

Falguni Dutta Sir, I did not understand your point that even if there is some change in policy, Gadepan-II will still not make sense to run and hence you have taken a shutdown. Could you just explain that a bit?

Anil Kapoor The proposal which is going around and has not yet been sent to cabinet is that they are going to give IPP plus USD 25 i.e. Rs. 1,500. Even if that policy were to go through, since our average cost of energy is higher at Gadepan-II because we use predominately LNG, we were still not be able to meet this criteria. Even though Gadepan-II is one of the most efficient plants in the country.

Falguni Dutta Will it possible for you to quantify the impact of this in Q4?

Anil Kapoor As far as Q4 is concerned we are not looking at too much upside on profitability in Q4.

Falguni Dutta But what I wanted to understand that this would not result in a loss quarter?

Anil Kapoor I do not think so.

Falguni Dutta What is the manufactured urea and sales volume for Q3?

Abhay Baijal In Q3, our production was about 530,000 tons and our sales was about 520,000 tons.

Falguni Dutta Can you tell something about our software subsidiary?

Anil Kapoor See, we are actively looking at software business being restructured. We are looking at appointing some merchant bankers and either we bring in a partner in that business or we can even look at a divestment if the price is right.

Falguni Dutta How has been the performance of that till date if you can share a number?

Abhay Baijal At the PAT level the loss is about \$9.3 million. This is for the complete year January to December 2014 and the EBITDA level loss is about \$ 1.05 million.

Moderator Thank you. The next question is from the line of Badrinath Srinivasan from Credit Suisse. Please go ahead.

Badrinath Srinivasan Sir, if my understanding is right you have roughly 45% of your gas used to be long term LNG. Given that I would think it is long term take or pay contract, how much leeway do you have in terms of taking less or basically how tight is this contract?

Anil Kapoor we have leeway of about 5% at the beginning of the year. We can contract lower volume beyond which we will have to take or pay. However, since the contract is for 25 years, we have no opportunity for backing out. However, there is a rolling 5 year average for RLNG Price. So if the crude price continues approx. at \$65, we expect the gas prices to come down gradually. Next year, we should expect a gas cost reduction of about 5% to 6%.

Badrinath Srinivasan Is it currently cheaper to import urea than to produce in India using RasGas LNG?

Anil Kapoor If you take RasGas, yes it is cheaper to import urea. But if you look at the blended cost of gas to the industry, domestic production will be cheaper than imports.

Badrinath Srinivasan The spot LNG prices are almost about 60% of RasGas. So is it possible to replace some of this term contract with spot LNG. Is that flexibility being given to us by our suppliers?

Anil Kapoor No, supplier will let go a higher gas availability when the spot prices have fallen to \$12 to \$13 per million BTU. So that will not be possible. But we have been requesting the Government to either pool the gas or may be change the formulation to a small extent in the policy. Let us see how the government moves. Going forward next year there may be an opportunity for both our plants to continue where IPP were to remain at the same level and spot gas were to remain at the same level at present. Then we should be able to produce from both the plants next year.

Moderator Thank you. The next question is from the line of Prakash Goel from ICICI Securities. Please go ahead.

Prakash Goel I want to understand - how would the profitability pan out that is your take or pay contract is applicable or not in the fourth quarter in the urea segment? Because we just heard from your competition that they will have to produce

because the take or pay would lead them to make more losses and hence they will be producing even at marginal loss?

Anil Kapoor We will have no take or pay issue as we have taken care of that. As far as the fourth quarter is concerned, we are not expecting any loss in this quarter.

Prakash Goel No, I am just talking about the urea segment not on the overall basis?

Anil Kapoor I do not have the calculation here but I am giving you the overall profitability.

Prakash Goel What is the policy now for urea between reassessed capacity and cut off and beyond cut off? Is there any change compared to the policy earlier?

Anil Kapoor Yes, the policy being proposed is that they will give IPP plus Rs. 1,500.

Prakash Goel That is for beyond cut off?

Anil Kapoor Yes, that is beyond 100%. You can use APM gas upto cut-off in your formulation and beyond cut-off the APM gas is not available.

Prakash Goel So it would not be viable beyond cut-off, that is what you are trying to highlight for unit 2?

Anil Kapoor In Gadepan-II we do not get APM at all. So it really does not matter for us if we get IPP plus Rs. 1,500 as there is no issue of cut off there.

Prakash Goel Sir, I want to know your views. Some of the South based capacity were allowed to operate on Naphtha because Government says there is paucity of urea stock. You have taken shut down, would it not change the equation in government doing something to make sure that volume is also viable?

Anil Kapoor I think you should talk to Government of India on that subject.

Prakash Goel But is it not logical?

Anil Kapoor As I have said earlier, we are one of the most efficient fertilizer plant in the country and we have shutdown.

Prakash Goel And Naphtha based players are being allowed to operate on a temporary basis?

Anil Kapoor I will not be able to comment on that Prakash, you will appreciate.

Prakash Goel So the policy response has been like in the earlier regime, we could understand. Even in the current regime, these logical things are being ignored?

Anil Kapoor Prakash, the fact is that we have shutdown answers all your questions.

Prakash Goel So I would move to the next point. On the software side. What is the EBITDA loss you have so far?

Abhay Baijal It is \$1.05 million at EBITDA level for the calendar year 2014.

Prakash Goel What will be the EBIT loss reported on the basis of \$1.05 million EBITDA loss?

Abhay Baijal The EBIT loss I had mentioned a number at PAT level of USD 9.3 Million and at PBT level it is about USD 8.3 Million.

Prakash Goel So PBT is 8.3 and PAT is 9.3 million?

Abhay Baijal Yes.

Prakash Goel Sir, any thought process on the shipping segment because it is doing relatively better now? I know the global prices of ships have gone down significantly and any chances of separation plan in the coming year?

Anil Kapoor Prakash, we have appointed a committee as I had mentioned in the beginning itself. We will look at options for all three non-fertilizer businesses.

Prakash Goel The last thing that I want to know is about the restructuring of the software segment business. So what is it exactly that we are trying to do?

Anil Kapoor We are trying to look for a new partner or if the conditions are favorable we can even look at complete divestment.

Moderator Thank you. The next question is from the line of Rohan Gupta from Emkay Global. Please go ahead.

Rohan Gupta Sir, just I wanted to have a volume for your sale for complex fertilisers? I mean trading volume?

Anil Kapoor Rohan, those are slightly confidential numbers at this moment.

Rohan Gupta But sir, the government is anyhow keeping a track of them?

Anil Kapoor Put it this way, fourth quarter the sales anyway come down substantially. However, if you can keep a track of our stock we can assure you that most of our stocks will be sold out.

Rohan Gupta Okay, that would be quite complex exercise to do from our side but I understand.

Anil Kapoor You should be able to get our stocks from government sites. I can tell you that even our competition will look at how much quantity of DAP and MOP we are going to sell in this quarter. It will not be fair for me to share that number on a public platform.

Rohan Gupta Sir, in complex fertilizer or in trading businesses have you seen a better margins in the current quarter versus previous quarter. I mean verses Q2?

Anil Kapoor Q3 margins have definitely come down from Q2.

Rohan Gupta But it would be possible to share in terms of per ton what would have been the average margin on trading?

Anil Kapoor I will give you approximately - this has come down by 30% to 40%.

Rohan Gupta So it is mainly come down because the realization have been dropped in the market or because of the raw material price. I do not think that finished product prices in the international market has gone up?

Anil Kapoor No, product prices in the international market has gone up from second quarter.

Rohan Gupta So we have not dropped the realization in the domestic market. It is basically from the cost increases?

Anil Kapoor Gross realization has improved in fact. The margins in to the distribution channels are substantially reduced in Q3.

Rohan Gupta So are we trying to give a higher credit or discounts to the dealers?

Anil Kapoor The discounts were reduced substantially but the product price has increased. What we are buying at \$450-455 per ton or even at \$460, is now available at \$485-490.

Rohan Gupta So the running contract which we are doing for DAP is \$480?

Anil Kapoor Running contracts in Q3 were approximately at \$490. Chambal has taken a price increase in Q4.

Rohan Gupta What is the extent of the price increase, sir?

Anil Kapoor We have increased our DAP from Rs. 22,700 to Rs. 23,300 a ton.

Rohan Gupta Can you also give us the debt number for the current quarter?

Abhay Baijal Our debt number for the current quarter is Rs. 3,884 crores - that the total borrowing.

Rohan Gupta Sir, what would be cash right now?

Abhay Baijal There is hardly any cash.

Rohan Gupta Sir, what would be the subsidy pending right now from the government?

Anil Kapoor Approximately Rs. 2,800 crores. We got complete subsidy for production up to July and only 35% of the production for the month of August. Post that, urea segment has not received any subsidy.

Rohan Gupta Sir, on the policy front you mentioned that government is still proposing that IPP plus Rs. 1,500. They are still not following that, right?

Anil Kapoor I agree, they are not following that but they have assured the industry that they will get these policies through.

Rohan Gupta So earlier it was 85% of IPP which the industry used to get so now it is 100% IPP plus Rs. 1,500; am I right sir?

Anil Kapoor That is right.

Rohan Gupta If at that cost also it is not working for one of the most efficient plant in the country, then sir, on what ground we should be expecting higher subsidies from the government? I mean then it make sense for the government to keep importing, isn't it?

Anil Kapoor No, but you look at this way as an analyst. Is Rs. 1,500 adequate? You see India's import price is approximately \$300. We have got 6% duty which makes \$18. There are port handling charges of approximately \$17 to \$18 per ton. So that makes it \$35. Government pays us whenever they can and payable when able. The Govt pays to importers through Letter of credit whereas our interest cost is approximately \$10 a ton. So that makes it \$45. Then there is a differential freight. According to our calculation, the right formulation should have been IPP plus \$60 instead the government has given us IPP plus \$25. Tomorrow if it is a free market, we will be able to produce and compete with imports even at \$300.

Rohan Gupta Produce and import even at \$300?

Anil Kapoor No, if you were to import at \$300 we will be able to produce with our gas mix available today and compete with imports.

Rohan Gupta So what is the underlying assumption for the gas prices when you are saying that you will be able to compete with imports at \$300?

Anil Kapoor At the existing prices available today.

Rohan Gupta At \$10?

Anil Kapoor No, I did not say \$10. I have got a mix of products 45% LNG and even with that mix I will be able to produce and make decent profits.

Rohan Gupta But sir, assuming going forward if the government completely decontrol it, so then if you have to make entirely on LNG (not even just 45% but 100%) then will we be competitive?

Anil Kapoor No, that is not the case. The fertilizer industry has been assured 31.5 million standard cubic meter of domestic gas, and we have been allocated non-APM gas in January.

Rohan Gupta So it is additional \$60 which will solve the problem of the industry?

Anil Kapoor I am not saying about the industry. I am saying about Chambal Fertilisers. We are not saying \$60 but additional \$35 i.e. IPP plus \$60.

Rohan Gupta Sir, just on a strategy question, you have mentioned that you are looking for divesting. You are definitely looking at the measures for the restructuring and divestment. Sir, which will be the area where you will be most comfortable putting your investment because as of now your company has a Rs. 3,800 crores debt but a large portion of that is coming from subsidy debt. So virtually you are almost a debt-free company except that shipping business debt. So with a huge cash flow generation in next two to three years or maybe even a slightly longer period where the company's cash flow will be deployed?

Anil Kapoor Chambal has made a commitment that we will be making investment for the third urea plant at Gadepan.

Rohan Gupta But for that you will be seeking the clarification from the government on policies front, right?

Anil Kapoor No. The policy is announced and it is favorable.

Rohan Gupta Okay, so with the current policy on the new urea projects, you will be going ahead with the Gadepan Plant-3?

Anil Kapoor As of right now, yes.

Rohan Gupta So when can we expect the final announcement from your side? Are you still talking with the gas suppliers for the longer term contract, that is only pending issue or something else is there?

Anil Kapoor We are talking to both gas suppliers. Due to the delay in government announcing the policy, EPCM contractors have asked for a substantial increase in prices which are under negotiations at this moment.

Rohan Gupta So what is the total cost coming down for 1.35 million tons project. I believe that will be a standard size of the plant now?

Anil Kapoor The cost will be say Rs. 5,000 crores plus or minus 10%.

Moderator Thank you. The next question is from the line of Gauri Anand from Phillip Capital. Please go ahead.

Gauri Anand Sir, I believe this is second shut down in this Fiscal and this is slightly longer. So does it mean you are bound by the take or pay. Does it mean that you will draw down more gas next year, you start the arrangement with the gas suppliers?

Anil Kapoor Yes, you are right. In order to protect the take or pay, we will draw a little bit more gas in the next year. However we will also use our contractual obligation next year to reduce our requirement.

Gauri Anand You will reduce your contractual obligation which means?

Anil Kapoor We will use the downward flexibility.

Gauri Anand Okay 5% flexibility that you have indicated at the start?

Anil Kapoor That is right.

Gauri Anand And sir, how confident are you that this IPP plus Rs. 1,500 will be more like a IPP plus Rs. 2,400?

Anil Kapoor Rs. 2,300 and Rs. 1,500 is not going to change. The government has committed to IPP plus \$25. I think your confusion is whether the industry can at best make Rs. 2,300 a ton which does not include bag cost. If you are where to take out the bag cost, which is approximately Rs. 300 and Rs. 100 is other miscellaneous costs like handling at railheads, etc. the net realization to the industry will be Rs. 1,900 and if you were to take out interest cost from that, because typical interest cost of the industry is Rs. 500 to Rs. 600 a ton, the net-net realization before tax would be Rs. 1,400 to Rs. 1,500 a ton.

Gauri Anand I am saying you have multiple gas sources so can you give us the delivered gas cost for at least the three mains like the contracted LNG, the spot LNG and the domestic for the month of February?

Anil Kapoor Average delivered cost of APM right now is around \$7 per MMBTU. RIL and non-APM would be approximately \$7.5 per MMBTU and LNG at this moment would be approximately \$19.

Gauri Anand This is contracted?

Anil Kapoor LNG is contracted and spot is \$13.

Moderator Thank you. The next question is from the line of Mayur Bhutani from India Ratings. Please go ahead.

Mayur Bhutani Sir, what I want to understand is - you said that at \$300 of IPP and considering the other charges like duty and port handling it cost around \$345, right?

Anil Kapoor \$360.

Mayur Bhutani Sir, given that the domestic gas prices also increased from 4.2 to 5.6 and you have mentioned that your gas price is \$7. So is it correct to say that if the gas price increases then or even at the existing gas prices the Gadepan-I unit will also not be operating post cut off or at this point it is conducive for you to operate?

Anil Kapoor Gadepan-I is conducive. We are not shutting down Gadepan-I.

Mayur Bhutani Okay, so at this price Gadepan -I will be conducive beyond cut off level also?

Anil Kapoor Gadepan-I will continue to operate, it is only Gadepan-II which was not viable.

Mayur Bhutani No sir, what I am saying is - it may be because the gas mix at Gadepan-I has more of domestic gas, right?

Anil Kapoor That is right.

Mayur Bhutani So given the fact that gas prices can also move upwards every six months, what will be the cut off levels of gas prices at which Gadepan-I can also become non-conductive?

Anil Kapoor It will all depend on multiple parameters.

Mayur Bhutani So I am saying considering the IPP pressure to be the same, what is the leverage that we still have in Gadepan-I as far as the gas prices are concerned?

Anil Kapoor See Mayur that is a hypothetical question. Why are the gas prices going to reduce? Our expectation is that from April onwards there will be a reduction in domestic gases because they have to follow also an averaging of international domestic gas pricing. So we are expecting gas prices to reduce.

Moderator Thank you. The next question is from the line of Rohan Gupta from Emkay Global. Please go ahead.

Rohan Gupta Sir, just quickly one clarification. You mentioned that 45% roughly is LNG in total gas that is for Gadepan-I or 2?

Anil Kapoor That is the average for both the plants.

Rohan Gupta Sir, can you just bifurcate what is for 1 and 2?

Anil Kapoor See domestic gas in Gadepan-II would hardly be 20% to 25%.

Rohan Gupta Domestic gas 20%?

Anil Kapoor Domestic gas and balance would be LNG and in Gadepan-I it is the reverse.

Rohan Gupta 80% is domestic?

Anil Kapoor Say about 70% to 75%.

Moderator Thank you. With this we conclude the conference call. Thank you for joining us and you may now disconnect your lines.