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Dear Sir,

We are submitting herewith Concall transcript of Apar Industries Ltd. for Q2 FY 2020-21 Earnings Conference Call made on November 06, 2020.

Kindly take note of this.

Thanking you,

Yours faithfully,

For Apar Industries Ltd.

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Apar Industries Limited
Q2 FY21 Earnings Conference Call
November 06, 2020

Moderator: Ladies and gentlemen, good day and welcome to Apar Industries Limited Q2 FY21 earnings conference call hosted by Four-S Services. As a reminder, 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. Should you need assistance during the call, please signal an operator by pressing '*' and '0' on their touchtone phone. Please note that this conference is being recorded. I would now like to hand the conference over to Mr. Samayak Jain of Four-S Services. Thank you and over to you, sir.

Samayak Jain: Thank you. Good afternoon everyone. On behalf of Four-S Services, I welcome all the participants to the Apar Industries Q2 FY21 earnings conference call. Today, on the conference, we have Mr. Kushal Desai - Chairman and Managing Director; Mr. Chaitanya Desai - Managing Director and Mr. V. C. Diwadkar - CFO, Apar Industries. I will now like to hand over the call to Mr. Desai for his opening remarks. Over to you, sir.

Kushal Desai: Thank you, Samayak. Good afternoon everyone and a very warm welcome to our Q2 FY21 earnings call for Apar Industries. At the outset, I hope all of you are healthy and safe. Let me start the call with a quick update and then I will go into details of the segmental performance of the three businesses.

So Q2 FY21 saw some amount of continued challenges of COVID-19, especially in the execution for domestic market. There has been a lower activity across domestic project sites in the second quarter and that of course is combined with what is the slower period due to the monsoon. There was minimal production in the railways and defense manufacturing facilities and a lot of tenders were deferred either from the lack of budgetary support at that point in time or the lack of meetings taking place for finalization between various central government and state government bodies. Transmission and railway tenders also has been postponed, many of them from April 2020 to sometime in the third quarter of 2021 which you hopefully see them coming to light, so putting these factors together, it has resulted in a lower domestic revenue and order booking, however, since we had already set our focus on increasing export revenues and especially for our specialty oil business with the location of Hamriyah plant it has actually helped us to counter some of the headwinds. We hope that in the second half, we will see tender activity pickup and some of it will clear the pent-up demand that is in place plus the government should hopefully, both central and state government, be able to allocate more money given that the GST collection has now come in reasonably well for the last 4 months.

Now, coming more specifically to numbers in terms of our performance, in the second quarter of FY21, Apar posted consolidated revenues of Rs 1,482 crores which is 19% decline year-on-year and this was largely contributed by 29% decline on the domestic revenue side. Our export revenues were stable and actually grew as a percentage of the total sales contribution contributing to 42% of our total revenues compared to 34% from a year ago. There was a smart recovery in our specialty oil and lubricants volumes due to a strong demand as well as very large client base that we have developed over the years and EBITDA post FOREX adjustment came in at Rs 118 crores which is 8% higher than the same period previous year and the EBITDA margin is at 8% which is up 201 basis points compared to the same period previous year.

Both the specialty oils and lubricant segment and the Conductor segment posted a higher profitability compared to the previous period in Q2. So profit after tax was at Rs 53 crores for the quarter which is up 58% year-on-year and one of the features that I could highlight in this is there has been a 56% decline in finance cost as the quarter saw lower rate and also some amount of improved working capital cycle. Some of it of course was contributed due to a lower topline, but a larger portion came from these other two factors.

Looking at the first half H1 FY21, Apar posted a consolidated revenue of Rs 2,775 crores with an EBITDA of Rs 153 crores and a positive PAT of Rs 30 crores. The management reduced receivables and inventory in absolute terms by about Rs 609 crores across the divisions as you look at the closure of 30th September and we have also completely repaid all the moratorium and short-term funding that had been taken to tied over the initial months of the lockdown, so for all practical purposes by the end of September, our cash flows were absolutely back on course.

In terms of couple of highlights in the Transmission and Distribution sector as such, so T&D companies won orders of approximately Rs 7000 crores in this quarter which is a marked reduction over the same period previous year. 22 TBCB based transmission projects are currently under construction as on September 2020 and we would imagine that activities would pick up pace in the second half for completing their execution. Most of these are for evacuation from infrastructure projects which are essentially renewable energy projects. Rs 1.08 lakh crores of loans have been sanctioned under the liquidity package for the stressed DISCOMs of which Rs 30,000 crores has been so far disbursed. So the government is also working on some other systemic reforms like new draft electricity amendment bill 2020 that will recast the cost which are reflected and tariffs bring in compulsory smart metering, DBT, DISCOM privatization, financial discipline for DISCOMs etc., and if this happens, then it will be a huge step in the right direction using legislation. Also the government plan for the Indian railway electrification still stands at completion by the financial year 2024 and 23,765 railway kilometers are still required to be converted.

Coming onto the more specific segment wise performances, our Conductor revenue declined 30% year-on-year and came in at Rs 628 crores in Q2 FY21. This was mainly due to the 48% decline in the domestic revenues and largely coming in from the COVID-19 related issues as I have explained earlier in terms of project sites and the work going on project sites which only started normalizing a little bit closer to the end of quarter. Exports declined marginally by 3% year-on-year, but still contributed to 56% of the revenues up from 40% in Q2 FY20. So overall volumes fell by 22% year-on-year to 33,797 metric tons. There was an improved demand for the copper transposed conductors used in the transformer industry and OPGW based on new approvals which we have obtained. EBITDA per metric ton post FOREX adjustment came in at Rs. 11,791 per metric ton compared to Rs. 7,789 per metric ton a year ago. If you look at the new order inflow, we had inflow of orders of about Rs 805 crores in the quarter which is 9% lower than same period previous year. The order book at 30th September 2020 was Rs 1698 crores, 1700 crores for all practical purposes and orders in the pipeline are Rs 380 crores and these orders are basically where we are L1 and the formal order process or financial arrangements are still in the pipeline.

When you look at the first half FY21, the conductor's revenues came in at Rs 1,337 crores down 30% year-on-year. EBITDA post FOREX adjustment came in at Rs. 9,071 per metric ton. The new order inflow in the first half was Rs 1,122 crores, so that is about 24% lower in the same period previous year. In the Conductor segment, we were able to reduce receivables and inventory to the tune of Rs 294 crores.

Specialty oil revenue increased 5% year-on-year to Rs 599 crores driven by about 20% increase in our export revenues. We have achieved the highest Q2 sales volume over the last decade which came in at 1,13,897 kL which is 16% higher than the same period previous year. Exports contributed to 42% of the revenues compared to 36% a year ago. Our Hamriyah plant which I had mentioned earlier paid off in terms of strategy of having multiple locations in multiple countries was able to run at a capacity utilization of 98% for the quarter versus 65% in Q2 FY20 and we were also able to add several new customers to that site who wanted to de-risk their supply chain given that the COVID-19 numbers from India were kind of peaking towards the end of August, beginning of September. So white oil sales both in the domestic and export market was up by almost 50% year-on-year whereas transformer oil declined due to poor demand from the utilities and transformer OEMs for the same reasons as I had mentioned earlier in my opening remarks as well as with Conductor division.

The auto lube side of the business and industrial lubricants have done quite well while the revenues are up 15% year-on-year. Our focus on the agriculture segment on the lubricant side where we supply to Eicher, Sonalika and Escorts; contributed to approximately 25% on the oil revenues versus 23% a year ago. We also gained from reasonably good recovery in the retail side led by increase in the volumes of tractors as well as two-wheelers. So if you look at the EBITDA per kL after FOREX adjustment, so that has increased by 130% over the previous year same quarter, so that came in at Rs. 6,538 per kL. Q1FY21 lockdown also created obviously ordering and supply disruptions and that caused a negative reflect in Q1 with higher price inventory, but the benefit of it came in Q2 as the orders got executed, but with a cheaper inventory level, so to that extent there has been some amount of an exceptional occurrence taking place due to this.

If you look at the overall first half, the oil business posted a revenue of Rs 950 crores which is down 20% year-on-year. The EBITDA per kL post FOREX came in at Rs. 4,500 per kL which is still 32% higher than the same period previous year. When you look at reduction in terms of receivables and inventory, it came in at approximately Rs 94 crores.

And finally if we look at the cable segment, so cable revenues declined by 31% and came in at Rs 254 crores. This was due to an overall low market demand. We did have a lot of delayed payments from EPC customers and some of the utilities and the competitive pricing resulted in quite a few unremunerative margins in particularly the commodity lower end of the power cable segment. The export revenues contributed to 12% of revenues. Power cables continued as I mentioned to be highly competitive. The elasto and e-beam cable also was affected due to the lack of production as the factories of railways and defense were in the first half, they have run at less than 10% capacity. Our expectation is that in the second half, we will start picking up, but some of the orders have been pushed back to the first quarter of next year, which is from April onwards.

The Solar sector projects were low in the first half, but towards the end, that means from September month onwards they have started picking up. So we expect a much better order flow and it has already started from the month of October for the solar DC cables. The optical fiber and telecom side also saw relatively lower offtake. There has been a deferment of deliveries in a few cases. The EBITDA margin post FOREX came in at about 4.4% versus 11.2% in the previous year. The export order booking for the second half however is a lot better on the cable side.

In the first half, FY21, cables posted a total revenue of Rs 504 crores which is 34% down compared to the previous year and the EBITDA margin posted was 3.7%. There has been a reduction of Rs 221 crores in receivables and inventories.

So just to summarize, going ahead in the second half FY21, we expect definitely better tendering to be in place compared to the first half. We are also expecting a higher utilization in the railways and defense facilities. Revival in demand has already showing signs of picking up in the mining sector, the wind power as well as the solar segments. Our execution of export orders will also improve in the second half, especially in the cable business as I mentioned earlier. So with this, I come to the end of my comments. I would like to thank all of you for joining our call and wish you good health. We would like to just open up the floor for questions if any. Thank you very much.

Moderator: Thank you very much. We will now begin the question and answer session. The first question is from the line of Pratiksha Daftari from Aequitas. Please go ahead.

Pratiksha Daftari: So my first question is with respect to Conductor segment, so now that order inflow is more tilted towards export, I wanted to know how is the margin profile for these export order and how does it compare to our existing business and whether the working capital requirement or the days for this business would be higher as compared to our existing?

Chaitanya Desai: Generally, our export business has been giving us better margins than the domestic business on the Conductor side. The only problem we see is that the government of India is undergoing a transition with regard to the export refund scheme for certain taxes. Earlier, it was in the form of MEIS scheme. Now, they have said they will have a sunset for that and they will introduce a new scheme, so we are not clear as to what the new scheme in terms of the numbers will be compared to the existing scheme, so there is a possibility that there could be some different kind of rate that they have fixed up, so that we will know in a due course of time and with regard to working capital cycle, generally for the export is a little higher, but the rate of interest cost is lower compared to the domestic side. So overall finance cost per say is actually reduced and also we don't have to hedge in terms of the export because of the natural hedge we are buying raw materials in dollars and selling also in dollar terms. So the hedging cost is somewhat reduced in the export compared to the domestic whether we buy from Indian producers or we buy from the duty paid imports, they have all back to the LME rate which is in dollars, so we have to take up forward cover also for that and we have to incur the cost of the rupee, dollar as it fluctuates.

Pratiksha Daftari: And like good margins has been better this quarter for Conductor segment, our EBITDA margins have been about 6%, do we think that this margins are sustainable considering that our metal prices in general are going up, the key raw material prices are going up and would we be able to like sustain these margins in H2?

Chaitanya Desai: Basically, we have hedging mechanism for the raw materials and our entire business model is based on the value addition on the raw material, so we typically take back to back hedging position against the orders that we take, so as such even if the metal prices are high or low, it does not really make a difference for us.

Pratiksha Daftari: So those margin improvements would be like because of cost optimization?

Chaitanya Desai: Yes, one part is of course to do with the order mix because now in the Conductor businesswe have not just the conventional conductors, but we also have other types of products that we have introduced over a period of time, so that has contributed to some extent and also certain cost we had to reduce with COVID situation and the lockdown, so we have taken certain steps to reduce our operating cost.

Pratiksha Daftari: And with respect to volumes, what I have, last year we have done average quarterly volumes of 40,000 tons, so do we expect to get something close by say Q4 or this year volumes will be substantially lower?

Chaitanya Desai: As things stand they look like they will be lower, because in India lot of the tendering has got postponed, so we will be taking somewhat of a reduction in volume on the local business. We are trying our best to try and make up on the export side, but probably net-net, we may still see a reduction in the volume and also some of the other businesses where railways are involved and all, there has also been slowdown basically, so a lot will depend on how quickly people want to catch up on the 6 months which are practically been lost.

Kushal Desai: So if you see the plan, we are approximately 140,000 tons we had planned for the year and if you see the first half, it has come in at around 66,000 tons. Pro rata basis, it is a little bit lower. As Chaitanya said here, there is just some uncertainty in terms of exactly the call of that will happen. Our sense is that second half activity will pick up because the corona virus situation has improved to some extent and I think the arbitrariness in the way in which project size would be handled pre-September, I think that also had settled down, so hopefully we don't have a huge spike after Diwali, which disrupts things, but otherwise I think the second half should look a bit better. It is difficult to take exactly what it would look like, but the general trend looks like it should be a bit better.

Pratiksha Daftari: That is great to know. So on the interest, but I think it is commendable reduction and cost of 40 crores over the quarter was great number, but I just wanted to know that now that we are expecting that in general the activity will improve in H2 and the business in general will pick up, how much of this interest reduction is going to be sustainable?

V. C. Diwadkar: This interest is sustainable actually, but if we do more business, then more working capital will be required, that is true.

Kushal Desai: If you just look at the whole first half situation, the revenues had been down by about 20%, whereas the interest cost has been significantly reduced, so it is some on account of 2 fronts, one is lower interest rate itself and secondly more discipline in terms of the whole working capital cycle, so being more selective in terms of who we do business with, what are the payment terms, inventory optimization, all that sort of stuff. So there is a certain portion as Mr. Diwadkar said which is sustainable. Only 20% of it has come down on account of the volume which was lower or rather the value which was lower.

Pratiksha Daftari: And sir, if you could just give us the non-fund based limit number along with the breakup?

V. C. Diwadkar: I will just give you. The total non-funded number, interest bearing is Rs 916 crores, out of that Rs 578 crores is LIBOR based and Rs 338 crores is domestic.

Pratiksha Daftari: And sir, now this year, this 6-month period, our balance sheet shows that there has been increase in short-term debt, so are we moving onto a model where we will be taking more of fund based limits and maybe we are reducing non-fund based limits or is there…?

V. C. Diwadkar: No, it is not like that actually, it was before for the initial COVID period, we had moratorium finance and that moratorium finance later on, because it was costly. The moratorium finance the bank gave, but that was costing 10.8%, so we did a buyers' credit of 5.4% actually and repaid the moratorium finally, but our model will remain same as the suppliers credit what we have been doing actually, the same model will continue more or less.

Pratiksha Daftari: Sir, with respect to oil segment, so how much was the decline in transformer oil revenues?

Kushal Desai: Decline in transformer oil volume was mainly in domestic. Domestic was down a little over 16% in the second quarter compared to the same period previous year, but it was more than made up by whatever happened, the applications where white oils and pharmaceutical oils go into, even they go into medical formulations, food packaging, all these areas we saw substantial increase.

Pratiksha Daftari: And sir, this margins now you said that Q1 we have high priced inventory in the raw material cost and Q2 we had lower priced and there is an exceptional gain here, so how do you see this margins normalizing?

Kushal Desai: That is why I mentioned that the average that we see in the first half is what we pretty much are at that level even in Q3 now.

Pratiksha Daftari: So average margins of H1 is sustainable?

Kushal Desai: At least yes, so far the Q3 seems to be also pretty much in that line.

Pratiksha Daftari: And sir, what about our new client, I mean the volume that have come from the new clients and there is a sudden surge in utilization in Hamriyah, is this because the COVID disruption or we would be able to retain these client and these volumes?

Kushal Desai: Several of our existing clients also became new clients for that facility because people wanted to, our customers are always looking now at the supply chain risk. Also, there is an acute shortage of containers and the freight rates have substantially gone up and India has seen a relatively higher increase in freight rates compared to other locations. So when you look at the whole analysis of things, risk mitigation just in terms of location versus delivery etc., customers etc., we are one of the few who is able to provide out of India, two alternate locations which are unconnected to each other in terms of supply chain risk. So we have gained market share as well as the business has got split a little bit between India and Hamriyah, so the two effects have happened. So one is, we signed on new clients and this is an absolute increase with clients and secondly, there has been some movement out of India into Hamriyah as part of risk mitigation strategy that customers have had.

Pratiksha Daftari: And sir, with respect to working capital requirement, I think this segment has been the one which has the highest working capital requirement in terms of days, so how is that fairing?

V. C. Diwadkar: It has improved actually.

Pratiksha Daftari: What would be days like in this segment?

V. C. Diwadkar: 76 days, debtors and inventory, 51 days.

Pratiksha Daftari: And this would compare to earlier of?

V. C. Diwadkar: About 4-5 days improvement is there as far as debtors is concerned and further you will be able to see some actions have been taken, actually some decisions have been taken, the impact of that you will be able to see in Q3 and Q4.

Kushal Desai: The inventory also includes the inventory which is in transit, so what we have got on the ground actually is less than 30 days today and you have about 30 days of inventory on the high seas for goods in coming into the three manufacturing plants again.

Pratiksha Daftari: And sir, my last question, sir we know what we have understood is that the overall orders in T&D has gone down and the release package for DISCOMs, what we have understood is that the disbursement is really low, since most of our business is dependent on power sector, lot of our segments are dependent there, how do you feel is going to be the demand in medium term from this segment? Do we see any material change happening which could help us or adversely impact us?

Kushal Desai: Our exposure is much more to the transmission sector and distribution. The transmission sector still seems to be relatively in a better position. The state governments have actually gone in and kind of frozen any expenditure happening for some period of time because there was a huge allocation that they had to make for fighting the coronavirus related issues in the absence of the GST payments coming in from the central government. Now, with the central government, the GST collections having improved and they have already started releasing money to the state plus there is some discussion going on and the few states have already started borrowing from the GST window that has been created for funding, our sense is that the transmission projects will come back on track lot faster than the distribution. So on the distribution side, we really have only the cable business which has a direct impact and off that the bulk of our cable revenues come from 3 states as far as the distribution companies is concerned which is Gujarat, Maharashtra, Karnataka and to some extent Kerala. So these three states are relatively not in such a bad position as far as the DISCOM is concerned. Gujarat, the DISCOMs have traditionally been profitable and in Karnataka, lot of our work goes on between Bangalore with B and Mangalore with an M and those are fairly profitable hubs in Karnataka. So there will be some impact, but it is not going to result in derailing whatever business that we are seeing on that front. Our concern has been more on the cable side on two fronts, one is the general demand has been relatively affected and secondly, a very profitable portion of our business for supply to the railways and the defense sector and because no production has been happening over there, it is less than 10% for 6 months. Activities have started picking up, but you got a lot of deferment in supplies happening, so I think that is where we see a bigger red flag than any problem on the utility distribution side.

Pratiksha Daftari: So sir, how soon do we expect the transform activity to pick up and what would be our trigger point for railway and defense for their production to pick up, like you are saying that it is 10%, so?

Kushal Desai: I think the question on the defense and railways that is really anybody's gue ss. Private sector, our plants are running at the full capacity from middle of May, these guys are struggling to follow all the norms which the government has set for all the manufacturing companies in terms of the precautions to be taken etc., but having said that lot of the plants are located in the Eastern part of India and in the South, ICF for example is in Chennai, so there the coronavirus situation also has improved, so our sense is that it will start picking u p. Definitely, Q4 will have big impact and I am sure they will run on overtime and churn out a lot of stuff, but difficult to exactly predict. All I can say is that it will be much higher in second half than in the first half

Chaitanya Desai: And on the transmission part of it, what we see is that it has been more delayed due to procedure aspects with regard to opening tenders. It is not stuck up because of financing and typically these are tariff-based competitive bidding projects whereas the finance will be not from the central government, they will be again based on bank financing of people like Adani Grid, Sterlite Grid and Power Grid and some of their other boot operators. So to a large extent, it is just a procedure of also physical meeting and awarding and things like that.

Pratiksha Daftari: Sir, typically for us to benefit, I am assuming there will be some delay, like first the tendering has to begin and then order flowing to us and our execution…..

Kushal Desai: That is why we feel that the second half will be better than the first half, but we are continuing to concentrate more on some of the export projects where the part seems to be clear and the orders have already come into the system.

Moderator: Thank you. The next question is from Maulik Patel from Equirus Securities . Please go ahead.

Maulik Patel: Just a few book keeping questions, lot of questions are already answered, so what are the CAPEX we are looking for this year and the next year?

V. C. Diwadkar: Maulik, we have already incurred about Rs 17 crores CAPEX and not much CAPEX is now planned actually at the most another Rs 15 crores, I will say.

Maulik Patel: So this is for this financial year, anything you have planned for the next financial year?

Kushal Desai: Maulik, there are no major projects which are there. If you take maintenance CAPEX and everything put together, it would probably be in the range of around Rs 40 odd crores.

Maulik Patel: Sir, the question is in the context of the last two years, not this year, but the previous two years we invested a lot into the creation of the facilities and others and now given, so are we looking to reduce our long-term debt in next two years significantly from the current level?

Kushal Desai: Whatever long-term debt we have, in the next couple of years, it will be largely paid off. There is one ECB that we have is a little bit longer term, but as due days come for this, we intend to pay it off and then not likely to have to take any more debt on. So we are on a debt reduction mission as opposed to needing any further long-term borrowing as such.

Maulik Patel: My second question is that, given this all pandemic and the way the things are working, have you seen any of your business particularly from the export that the competition from the China is lower or the buyers are preferring more about non-Chinese players, something that you have observed?

Kushal Desai: So If I just run through both the conductors and cable business, are the ones which have been facing competition from China as such. One thing on the cable side is that the inquiry levels have substantially gone up and it has translated in some amount of business coming and we believe that it is as the expense of diversifying the supply chain related to China, but I think the bigger kicker will come in when customers are at a position to travel here and complete doing all their diligence because we have done whatever due diligence has been done with customers, have been done all online where with cameras moving around and equipment and things like that. So the work has already started and there is a definite interest in terms of diversifying supply chains away from China, but customers need to establish that not only quality, but even delivery and things like that are all falling in place, so we see a longer-term trend for sure.

Maulik Patel: So that is more prevalent under the cable business, right?

Kushal Desai: Yes, in our oil business, we don't compete with the Chinese at all. The Chinese are very internally focused. The conductor side, there is competition in certain markets outside India while the Chinese have been active, but the sense we get is that the clients are, if other things be equal, they would prefer to buy from may be an India party compared to a Chinese. That is from trust point of view. One of the markets where you will see the clear benefit and our tenders, quotation, discussions have reached significantly more serious levels, has been in Australia. You see the Australian business on the cable side substantially increasing in FY21 compared to FY20 in spite of all the other limitations that I mentioned and in some of the other places also I would imagine that this will take place. So I wouldn't bank on some huge numbers changing in Q3 and Q4, but this trend is a trend which is definitely going to be in our favor and we are working as hard as we can in terms of putting more and more resources under the export side to build that part of the business and in the longer term I am sure that business will shift in our businesses from China to Indian companies.

Moderator: Thank you. The next question is from the line of Saurabh Patwa from HDFC Mutual Fund. Please go ahead.

Saurabh Patwa: Sir, I wanted some book keeping numbers, what would be the amount of LC and guarantees?

V. C. Diwadkar: The total LCs are 916 crores. Out of that 578 crores is LIBOR base and 338 crores is domestic. These are interest bearing LCs, correct.

Saurabh Patwa: So this has come down sharply, sir?

V. C. Diwadkar: Yes, it has come down.

Kushal Desai: Saurabh, 30% of it has come down only because of the volume which is lower, but in some of the cases, as the cash flow has improved domestic purchases and even from the export purchases, smaller purchases we are just taking on a direct basis without opening letters of credit.

Saurabh Patwa: So historically last 3-4 years, what has happened is I think we have seen improvement in Conductor business, especially in terms of EBITDA per ton, but our incremental financial charges are actually negated that positive impact, so I think in this quarters, financial charges were I think less but least in last 3 years or may be actually, so what is the kind of trend you are seeing or there is any change in strategy or in terms of market conditions?

V. C. Diwadkar: We have tightened our working capital, overall actually as far as debtors are concerned, inventory which earlier also Kushalbhai mentioned actually, so you will see this trend actually, whatever you have seen in this quarter and the last quarter also, we will see this trend going forward actually. We also said that we are having more focus on the working capital.

Saurabh Patwa: Because our debt has been coming down, but this LC based part has actually negative almost positive thing. I am not saying about this quarter, something in last 3 years or so, the trend has?

V. C. Diwadkar: I agree with you actually. Earlier that trend was there actually, whereas finance cost has increased actually, so now you will see that the finance cost is going down.

Kushal Desai: One of the things Saurabh that you may have even picked up from the last call that we had in the call before that, this was before the pandemic even hit that, we had already put a plan in place to make sure that our finance cost came down and the total working capital cycle became more efficient and we were prepared to drop the bottom end of the business if that was required in order to achieve this particular objective. So we have actually gone in and executed it, so you will see that to some extent the business volumes also have suffered. On the cable side itself, if you take some of the customers where the orders were relatively large for 200 crore of business, we have not pursued, even though we were at the final stage and customer wanted to place the order on us because we couldn't agree on the right commercial terms, etc. I think slowly larger players who will also burn themselves if they don't follow this discipline will start falling in line because the banks have become very tight in terms of extending credit for dues which are beyond 90 days etc. This discipline is something which we had already started. That is why the benefits of it have shown up in the first half of this year, but if something which we want to go forward with that. In fact, in the previous question also I had mentioned that the reduction in the interest cost is much more than 30% which is the reduction in the sales value that we have had.

Saurabh Patwa: Sir, I also wanted to understand our strategy on the cable part, so the drop has been sharp, but many of these projects now there is a competition increasing which from other e-beam cables, plant being added in the country, so may be some 3-4 years down the line, how do you think the competitor scenario and how do we see ourselves?

Kushal Desai: Yes, the competition has increased on that front, but we have done two things to secure our own volume. One is that we have started expanding our footprint outside India for the same sets of cable including solar cables and other e-beam cables. The second thing is we have forward integrated into doing railway harnesses, so that gives us much bigger leverage because you are using our own cables to then provide value added service to the various locomotive companies as well as the coach companies. So the harness business also will help so that is another additional source of growth using the same e-beam cables, but the cables are cut and put together in a ready to use frame, just like how you have harness for cars, where company like Motherson Sumi being leaders in that space. We are the first guys to get approval from JBM for the electric vehicles, the buses, so we got the first order of 99 buses and that is to be followed by another 140, so that also we are supplying an electric harness, the cable in the harness form to JBM.

Saurabh Patwa: Sir, if I can just last one more question if I can just add on, sir, in this Hamriyah, now we are reaching our utilization level which we were always targeting and I think our presentation also mentioned that large part of it is also due to new customer addition, so would it be fair to assume that going forward, so are the initial target when we were setting up the plant was that we were moving the export demand to Hamriyah and we will focus more on the domestic market, are we nearing that thought process?

Kushal Desai: Not entirely Saurabh in the sense, our idea is to utilize our Indian capacities and then Hamriyah capacities incremental. Some of the cannibalization has taken place to win overall share of business from customers by providing de-risked supply chain which none of the other Indian competitors of ours has been able to provide. If you see the Hamriyah capacity for the quarter was 98%, for the half year it is 76% and we can actually look at debottlenecking and produce more over there with minimal investments in piping and other things, so we will do that as and when it comes up. The other thing that we revolve to is that certain product lines which we are executing now out of India where the products are of higher value and more specialized and we moved some of the more commodity products of white oil etc., to Hamriyah which they can execute reasonably efficiently. So one of the things that has been demonstrated in this quarter is, if we look at the fixed cost structure of Hamriyah, even though they ran at about 98% capacity compared to the previous quarter which was in the mid 50s, the cost structure hasn't changed very much because the plant is highly automated whereas in our Indian plants if we were to step up that kind of production, there is almost a linear increase that happens on the variable cost front. So we expect to continue to push as much of the commodity business of white oils and certain geographic spread to the Hamriyah plant and we are using the most specialized infrastructure here to do more specialty grades out of India. So you still see both the plants export happening from both locations.

Saurabh Patwa: But then this will increase our blended margins compared to our historical say like what we used to make between like 4500-5500 what was generally the average, so does this make a longer term, medium term change to this, so obviously last two years have been weak, but?

Kushal Desai: It absolutely should. In the last two years, we have had finance cost and FOREX changes affecting this. More and more volume we do out of Hamriyah, they are also immune to any of the FOREX recognition related things because the whole business is a dollar run business.

Saurabh Patwa: And also as you mentioned that the fixed cost of Hamriyah was same even 2 years?

Kushal Desai: Yes, because the plant was extremely automated. It is significantly more automated than the transformer oil, white oil facility we have here in India.

Saurabh Patwa: So the more we do, more beneficial it is and vice versa?

Kushal Desai: Hardly, when you increase your production from the mid-50s to 98, it gives an addition of around 10-12 people in total at the lowest level. We had added some forklift operators, things like that. The rest of it, the management staff remains exactly the same, because he is just sitting in front of computer terminals and just processing more volume.

Moderator: Thank you. The next question is from the line of Anuj Upadhyay from Emkay Global. Please go ahead.

Anuj Upadhyay: Sir, if I go by your presentation, then HEC revenue share during the quarter has fallen to 13% compared to 15% year-on-year, even our copper conductor for the railways have contributed only 5% vis-à-vis 22. Broadly, if I see there is a higher margin contributing product composition has come down during the year, but instead of this the EBITDA per metric ton has gone up, could you throw some light on this part sir, which are the things which are missing out here?

V. C. Diwadkar: This is because of the per order profitability. See, we have cut down some customers where the margins were lower actually, but we said that we will go away with this business, but we will not take the lower margin business. So you are right actually, the conventional conductor and rod business, profitability has improved, also it has to do something with the cost reduction actually. Lot of cost reduction initiatives were taken, actually pre-COVID and after COVID also obviously during that period, so that has also helped this.

Anuj Upadhyay: Second sir, in the outlook on the domestic transmission oil, because what has been yes, I am like we have been suffering in terms of gaining margin in this segment and even in the current quarter, if the exports business which has done extremely well, but the transformer oil within the domestic is something which is suffering. On the other hand, we are seeing much better traction across the white oil and the lubricant segment, so any long-term business decision which we are planning to have so that to shift our focus more towards the non-transformer oil segment or will continue to have our strategy 50-50 across the transformer and non-transformer?

Kushal Desai: So to tell you honestly, the volume which is coming out of the different segments, they are not interdependent. We can follow an independent volume on transformer oil versus on white oil and lubricants, so we have consciously been trying to grow our lubricant volumes and we have been succeeding in doing that. In terms of transformer oil, the domestic demand itself has been soft and then as you may have heard earlier, we put a lot of more discipline in place in terms of financials and even profitability that we would want a minimum profitability, so customers, who we are not able to get that from, we have decided to just allow that business to just fall off. So in the half year, the profitability of our transformer oil business also has gone up commensurately. That is how, because it is still a chunk of the total amount of volume that we do. It is around 34% of the total oil business that we have. So the profitability on that also has gone up and we will continue to follow this because as we mentioned before this year started that if some volumes have to fall, we are okay with it, but we have to concentrate on a profitability and return on equity, equity return on capital employed. We are following through on that.

Anuj Upadhyay: So one-off benefit which we had this year was it applicable across oil segment for both the lubricants and industrial as well?

Kushal Desai: No, actually the lubricant doesn't have that. It happened more in the case of transformer oil and to some extent the white oil. It is actually pretty simple in the sense that you had orders which you were suppose to execute in the first quarter, but customers were not able to take the product because of lockdowns and various other related issues. So they deferred the schedule into the second quarter. In the mean time, we booked new business in the first quarter, which obviously had to carry prices that were more competitive and prevailing in that period, so we used more expensive raw material to service the cheaper price order and then when these got deferred into the next quarter, we used the lower price raw material which came from the lower crude prices, etc., and executed those deferred orders, so as the consequence to be fair we have been saying that we want to evaluate the profitability of the business, it is better to look at it for the half year, but this impact is actually something where you can ignore when you look at the half year and whatever we have done in the half year, we are seeing the similar kind of profitability in the Q3 as we speak today. Q4 is again a little open here where new US president is going to come in, we don't know what the impact will be of these lockdowns and things in overseas countries because all of these has fairly sensitive bearing on prices of crude and crude production and things like that.

Anuj Upadhyay: And sir, on your order book within the conductor segment, can you just give us a breakup, how much would be the high margins and how much would be the conventional one or as Mr. Diwadkar said, see now because of this change in the business metric, even the rod business have now better margin, so we should assume that this entire order now comes under the high margin segment?

V. C. Diwadkar: Yes, but still if you want actually, the HTLS conductor order for Rs 329 crores and copper railway conductor orders is about Rs 95 crores out of the total order book of about Rs 1700 crores.

Anuj Upadhyay: 329 for?

V. C. Diwadkar: 1700 crores total order book.

Anuj Upadhyay: 329 was for?

V. C. Diwadkar: HTLS.

Kushal Desai: It is same as HEC.

V. C. Diwadkar: And copper railway is 95 crores because the railway tenders have got postponed as we said earlier, they are not able to work virtual, they require personal meetings and all the things, so for us it will start in this Q3.

Anuj Updhyay: Lastly sir, in your slide where you have mentioned about the capital employed across various segment, it is showing that the capital employed across the conductor segment has almost gone up by 2.5x from 200 odd crores in June 22, it is like 490 crores?

V. C. Diwadkar: Actually, see there, whatever we show as current liabilities, they are interest bearing liability, so we do not look too much. What has happened actually, we have paid out the current liability. Lot of current liabilities we have paid out during this period and further you will see during this October, November, December also we will be paying off some of the liabilities. As you are seeing, the LC number also has come down.

Anuj Upadhyay: Yes sir, that have come down significantly and if I can add one more sir, lastly on the renewal space, are we seeing any traction sir, across the solar and wind for our e-beam segment?

Kushal Desai: As I mentioned, yes we are seeing more traction now starting to come on both the segments, from September onwards we started getting increased orders on the solar DC cables. They are the cables which are used for the panel wiring. It wires the panels of the, where we are the largest producers in the country of that. So that business has started kicking in and our expectation is that it will do very well compared to the first half in the second half. The project size are pretty clear today for execution and most solar size don't require more than 6 months in terms of execution cycle from start to finish. So you will see a lot of activity happening in solar in the second half and the activity in wind also has started picking up where order inflow from Suzlon, Gamesa all these guys have started increasing, so both those segments will do lot better in the second half compared to the first half.

Moderator: Thank you. The next question is from the line of Adit Shah from Vibrant Securities. Please go ahead.

Adit Shah: My first question is that Rs 53 crores is perhaps the highest ever quarterly profits which we have reported as a company and it is commendable considering that the revenues are much below our highest ever also in terms of the volumes and one of the biggest reasons has been the significant reduction in the interest cost. So what I understand is that there is no change in the way the business in terms of the dynamics. It is just that we are being more cognizant in terms of the kind of orders which we take in terms of the creditors and basically low receivables days, is my understanding correct?

V. C. Diwadkar: Correct. Two three other impacts are there, rate impact is also there, commodity price impact is also there plus what specific actions which we have taken which earlier we have discussed that we have done away with some marginal customers actually where the final cost was higher and the margins were lower.

Adit Shah: So effectively, LIBOR movement is not in our hand neither commodity prices, so that impact may get negated, but the one which we are doing from our end would be sustainable, that is what I am saying, I get that. Sir, do you have any guess on whatever interest cost could be on a quarterly basis around 40 crores less than that or it is very difficult to say that?

V. C. Diwadkar: Again, this is driven by the interest cost. As you rightly said, nobody can predict what will be interest cost actually, but if this remains like this only, it should be below Rs 40 crores.

Adit Shah: Sir, one question is that we had released a lot of capital, most than 600 crores to reduction in the inventory and receivables, however, we actually repaid more than that and actually took up borrowing on the balance sheet in terms of short-term borrowing. So what the idea because of just arbitrage, the short term borrowing was at a lower cost, so it is better to repay the creditors?

V. C. Diwadkar: See, some of these liabilities when they become due, you have to pay, so we have paid those and the LC liabilities have gone down actually.

Adit Shah: Sir, my second question would be in terms of segments, you have mentioned for the conductors you are budgeting for 1,40,000 tons for the year which we should be on track, can you sort of suggest similar guidance for may be oil what we expect in the second half and also cables, is it possible or no?

Kushal Desai: Our original plan was to do 1,40,000 for conductor, we don't know exactly where we will end up. We have ended up doing 66,000 in the first half, so we believe that the second half should be better, but at this stage to give a guidance it will be a little bit difficult. The only trend which we can give probably is that is the second half looks to be better than the first half in terms of volumes as things are done of settling down and obviously the first two months was a big drag. Things picked up in the next couple of months where some of the backlog was cleared, but generally we see second half being better than the first half.

Adit Shah: Sir, my second question would be that if I look at your business segment wise, we see that the cable as a relatively weak export franchisee in terms of the share. Is there any particular reason for that in terms of the kind of products which we are making? Are they not suitable for international standards or is it that we have not focused on international market? Do you want to add any comments there?

Kushal Desai: Traditionally, our exports in the cable business were happening more into Africa and we had ridden on the back of our Conductor business and approvals which we had in Africa, lot of world bank and African development bank aided projects and things, so today we are actually expanding our cable footprint to cover countries like Australia, the United States and other places whereas specially we see that predominantly in the past, Chinese companies have been primary suppliers and where there is an opportunity, there has opened up. So we started focusing on our cable export business from the December ending quarter of last year. This is September-December quarter where we have two new sales people added just before the lockdown started, so there is a significantly increased focus on the export business. It is just that difficult for customers to come and do inspections etc., business has started, but I think it will accelerate as the quarters go by and especially once travel opens up because if you want to buy high value critical type of products, you obviously want to have a much better look and feel in terms of the manufacturing facilities and the infrastructure which we have and things like that. So in fact to some extent, China is benefiting because of the lack of people being able to do all the diligence properly. Once the diligence starts, I think companies like us and countries like us will be able to accelerate this transition.

Adit Shah: And sir, do you think that export business within cables would be in terms of profitability at par with the domestic business or better?

Kushal Desai: Yes, it should be in the same range, if not better for, may be even better in terms of working capital for sure because many of these are all LC based sort of transactions and the customers are dealing with many of them are big EPC players and also utility. So that is the reason why profitability in the export markets should be lower than like-to-like products in the domestic.

Adit Shah: I get that sir and is there any opportunity with niche sectors in cables like defense what you do in India or that is too far away?

Kushal Desai: No, I think that would be a bit utopian for us to think that would come about because the big defense providers come from the United States, Russia, France, these sort of places, so the defense is going to be largely an Indian thing. Of course, we are going to see increased business there because this make in India has been actually accelerating and then we have done many more than 50 prototypes for the various armed forces, that is navy and even the army of different types of cables and things, so they are all under testing at various stages because defense is a long cycle business. We will pick up, but that business will be domestic, our e-beam cables and the other power cables we expect are larger share to come from over the next couple of years.

Adit Shah: Do you want to comment on the new products which we have launched over the last 12 to 18 months like the one for transformer?

Kushal Desai: It is also CTC copper transpose conductors. In my opening remarks, I had mentioned that these are getting more and more approvals from the transformer manufacturers and the utilities. In fact, that effort has been significantly slowed down because of the lack of being able to travel and meet, but in spite of all that we have got more and more people approving where the process was started prior to the lockdown. We are following through on it, approvals are coming through, so you will see a jump in the business of the copper transpose conductors. Similarly, we will benefit from the OPGW product line because significant competition was coming from Chinese manufacturers in that and with the new rules which are in place, we have almost excluded from being able to quote on the business. As the tenders are coming up, the share of business which we will gain will be much higher.

Adit Shah: And sir, the rod thing is like intermediate product in the conductor value chain, is that what it is?

Chaitanya Desai: Part of it is and part of it is actually going into other applications which are not through the electrical field, more the mechanical products.

Adit Shah: Sir, is there any opportunity there to focus there also or is it like more tactical and optimistic in terms of rod business?

Chaitanya Desai: We have been doing this business, but it has been gradually increasing over the years, so that is more sustainable business with better margins also, so we would be concentrating on it, but it is a relatively more niche product.

Adit Shah: Sir, on the oil business, you had mentioned that the India facilities are not as mechanized versus the Hamriyah and there is much more operating leverage there, so we don't plan to do that investments in India and make it at par? Is it not feasible?

Kushal Desai: It is not that this is not feasible, it is just that the CAPEX involved is fairly huge, so we look at the cost benefits, it make sense to continue to operate in India the way we are and move to more specialized products where the volume runs are little smaller, more SKUs, those sort of things whereas in Hamriyah you get a very good operating leverage because the plant is very automated. When you go from 50 to 100% capacity, then cost is only very incremental. Here it would be more linear, so we are trying to utilize that. The specific question was that how are we going to operate between the two plants in terms of export, customers, etc., so you can use the two plants on a complimentary basis.

Adit Shah: Sir, one more thing which I just noticed on the linked in page is that we have something on Arkos-based branded two-wheeler batteries and lubricants, do you want to sort of, what exactly is that business? Are we tying up with the Singapore based company because you already have relationship with Eni do you want to comment on this?

Kushal Desai: The Arcos-based products are those, we have brand leverage on that brand which we are bringing in, so we used to do some amount of retail in the case of power oil and the power oil brand has a connotation of basically an oil and largely a transformer oil where we are very famous for that brand and we wanted to look at extending products across different car care segments etc., so the first product that we have actually brought on and experimented with is two-wheeler batteries and we will be talking much more about it in the coming quarters because we just launched and it got launched just pre-COVID, so now the business is trying to pick up, supply chain getting settled, but the Arcos brand is a brand that we want to use across product categories, not just lubricants but also looking at batteries and then other allied products. We will become significant enough when it make sense to talk about that business, so it is a very infancy stage right now.

Adit Shah: Sir, one final question, based on the management's estimate, the capacities which we have across India and even the Middle East cultural products, you also talk about in terms of return on equity of 20%, so what I understand is that you believe that this company has an earnings power from 200 to 250 crores, is that the right number which you feel, or can it be significantly higher than that also? Just to understand what do you think is potential sort of profit-generating power of this business because I think for the last quarter, it has been underperforming in terms of its true potential, you want to comment that?

Kushal Desai: The capability is to definitely get to the 250 crores and then the product mix will drive profitability that goes higher than that and that is what we are focused on trying to deliver. Unless you start sharing some of the commodity business, there is a crutch that everybody actually uses, so we have taken a much harder call now, saying that we are dropping some of the business that doesn't make sense and focusing on higher value business. So as these things start picking up traction, whether it is CTC for transformers, whether it is OPGW, all of this is starting to show some signs, it will deliver then higher EBITDA margins on a blended basis per ton or kL etc. If you see our lubricant business also has been regularly growing up and the performance of that was getting a bit hampered just because of fluctuation in prices which happened particularly in the previous 18 months. That having leveled off, the results are now much more evident to be seen. The operating leverage really comes from the mix.

Moderator: Thank you. The next question is from Dhiral Shah from Phillip Capital. Please go ahead.

Dhiral Shah: Sir, my question is again pertaining to the finance cost, maybe we have seen a lower commodity prices in H1 and now commodity prices have moved up, so do you feel we will stick to our guidance of, let us say, less than 40 crores per quarter of finance cost in spite of commodity prices moving up?

V. C. Diwadkar: 40 crores should be possible actually with the lower interest cost which is there, plus what actions we have already taken as far as the financial discipline is concerned across all the businesses.

Dhiral Shah: So you don't see much deterioration in working capital because of this commodity prices moving up, right?

Kushal Desai: The commodity prices have moved up, but they haven't spectacularly moved up, it is still, oil has moved a little bit down, copper and aluminum have moved up, but they are not at all time highs or any such thing.

Dhiral Shah: My question is again, let us say, may be in coming quarters, let us say moved up to all time high, do you feel you can maintain this kind of quarterly run rate of finance cost?

V. C. Diwadkar: If it moves up by 100%, then obviously we will not be able to manage. We should be able to manage actually because of all the actions which we have already taken.

Dhiral Shah: And sir, now we are more focusing on the value addition part, so what kind of EBITDA margin we are likely growing to sustain in coming quarters?

Kushal Desai: We will go by metric tons, so in the conductor business our target at this time is to get to Rs. 12,000 per ton on a sustainable basis, so all the actions are targeted towards getting there and our oil business sustainability has gone across 4500 per kL and in the case of cables we want to be double digit EBITDA per metric ton, but cable will take a little bit longer because of all these other issues that have happened with defense and things like that, so until that normalizes because that is quite a profitable part, but on the conductor and oil side, we are pretty much already there and if you take the second quarter and for oil the entire first half of the year, so it is the cable side that we need to focus in order to bring it up into that double digit back again.

Dhiral Shah: And sir lastly, with the kind of current gross block which we have, what kind of potential revenue we can generate sir on that?

Kushal Desai: See, our current utilization across the facilities is only in the mid 70s, if you exclude the Hamriyah plant which produce 98% in the quarter, so we can easily produce 33 to 40% more than what we have seen in the last quarter and then we have crossed the bridge when we come to it. Our whole focus is really that if we lined up with the capacity constraint, we will see whether it make sense to put more money to expand capacity or to drop product lines which are more commodity and not paying us enough and focus more on value added products because we don't want to play a volume game anymore, we are concentrating on getting our metrics in place.

Moderator: Thank you very much. That was the last question in queue. I would now like to hand the conference back to the management team for closing comments.

Kushal Desai: Thank you. Thank you everybody for patiently being on the call. I will also like to take this opportunity to wish everybody a happy Diwali and a prosperous New Year and certainly we see as I had mentioned in my closing remarks of my initial talk that we see a better second half with increased tendering and higher utilization from the railways and defense facilities, a revival in mining, wind and solar segment which already seems to be underway and our export execution will only increase as time goes on and we are also able to leverage supply chains, de-risking from China into India as such. So with that I would like to thank everybody and wish you all good health. Thank you very much.

Moderator: Thank you very much. On behalf of Apar Industries Limited, that concludes the conference. Thank you for joining us. Ladies and gentlemen, you may now disconnect your lines.