

Transcript

Conference Call of Omkar Speciality Limited

Event Date / Time : 3rd February 2015, 11 AM IST

Event Duration : 40 min 58 sec

Presentation Session

Moderator: Good morning ladies and gentlemen, I am Beulah, moderator for this conference. Welcome to Omkar Speciality Chemicals 3QFY15 results conference call. We have with us today Mr. Satish Mishra from HDFC Securities and the management team from Omkar. At this moment, all participants are in listen-only mode. Later, we will conduct a question and answer session. At that time, if you have a question, please press * and 1 on your telephone keypad. Please note, this conference is recorded. I would now like to hand over the floor to Mr. Satish Mishra from HDFC Securities. Thank you and over to you sir.

Satish Mishra: Thank you Beulah. Very good morning to all of you. On behalf of HDFC Securities I would like to welcome all the participants to the earnings call of Omkar Speciality Chemicals. Today, we have with us Mr. Pravin Herlekar, the Chairman and Managing Director of Omkar, Mr. Siddharth Sinkar, Director, Mr. Ameya Deshpande from Chairman's office, and Mr. Nirav Momaya, Company Secretary. We will start with the opening remarks from the management's side and post that the floor will be open for questions and answers. Over to you Mr. Nirav.

Nirav Momaya: Thank you very much sir. This is Nirav Momaya. Good morning all the participants. I would like to welcome you on behalf of Omkar Speciality Chemicals Limited to this Q3 financial year '15 earnings call hosted by HDFC Securities Limited. I would like to hand it over to Mr. Pravin Herlekar, CMD of Omkar to give a brief on the performance of the company during the quarter. Over to you sir.

Pravin Herlekar: Thank you Nirav. Thanks to you for joining us on this call to discuss the Q3FY15 and nine months FY15 of Omkar Speciality Chemicals. At the outset I would like to inform you that the company on a consolidated basis has clocked a turnover from October, INR 71 crores, which is 6.2% growth quarter-on-quarter that is compared to the previous quarter and a 31.9% growth year-on-year that is compared to the third quarter of FY14. With this the nine month revenue for FY15 stands at more than INR 190 crores. The business has achieved an EBITDA of 22.7% for the quarter compared to 19.9% in the previous quarter and 19.5% in the third quarter of FY14. Growth in EBITDA is primarily due to the growth in the contribution coming in from revenues from our API division, which has increased to 24% for Q3FY15 as well as the growth in the revenues coming in from sale of our niche molecules recently launched. Exports as a percentage of revenues have increased to 33.7% and will stand at 31.4% of our revenues for the period of nine months FY15. Our API business revenues for the quarter ended were at INR 17 crores and have now crossed INR 44 crores for the period of nine months FY15. Iodine derivatives, which happens to be our major business operation remains our major revenue contributor with a contribution of 58.3% for Q3FY15. Iodine prices have now more or less stabilized and you don't expect much of a

decline in the price. It was happening during last year and in the first few quarters of this year. The price margin has increased 10.5% for the quarter from 9.5% in the previous quarter. Working capital cycle, which we are in discussion in our earlier discussions also, was stretched and the working capital cycle has been addressed by us and the net working capital as of December '14 is 192 days compared to 207 days as of September '14 on an annualized basis considering last four quarters of revenues. This is expected to reduce further owing to increase in exports where the payments arrive much faster as well as other strategic business initiatives. We would also like to inform you that the board in its meeting yesterday has agreed in principle to set up an overseas wholly owned subsidiary having warehousing facilities to cater to our growing exports more effectively and efficiently. We will definitely provide an update on the status of the same at an appropriate time. To sum up about the business outlook, I would like to state that our API business is quite promising as we benefit from the revenues growing year-on-year. We had revenues of 9 crores in FY13, 30 crores in FY14, and in FY15 so far we have crossed 44 crores. Better margins, coming in, in this particular segment, which was made possible by our backward integration strategies are contributing to our EBITDA and PAT. Secondly, the launch of recently developed niche products has also been contributing to the margins and this picture will improve further in coming quarters. Lastly, our exports are growing and exports are strategically important to us in terms of better margins plus faster payment cycles, it will help us in bringing down our working capital. I would now like to throw open the floor for Q&A and I request you to come up with your queries, which we will try to address. Thank you so much.

Question and Answer Session

Moderator: Thank you, sir. Ladies and gentlemen, we will now begin the question and answer session. If you have a question, please press * and 1 on your telephone keypad and wait for your turn to ask the question. If you would like to withdraw your request you may do so by pressing * and 1 again. Our first question is from Mr. Sivaram from Crisil. Please go ahead.

Sivaram: A very good morning sir. Thanks for taking my question. Sir, to begin with, I wanted to ask you we have seen a new plant going live in the previous quarter, the unit Six, so can you tell us what is the contribution from this particular plant?

Pravin Herlekar: We have lot of integrations happening in the various units, so it is not that the sales, which are happening, may not be coming from a particular unit. There are lots of intermediates, which are made at different levels in different units. So, as of now, it may be difficult because that plant will be again making something and giving it to our other units, maybe it is our API division and from there the sale is happening. So, it is very difficult to define actual contributions, but then I can make a statement that whatever increase in revenue have been noticed, they are mostly from this particular plant.

Sivaram: Okay sir. And secondly sir, in terms of speciality chemicals, what is the number that the revenue contribution in terms of actual numbers?

Pravin Herlekar: Speciality Chemicals, as we all know, we have three major segments, one is the iodine derivatives, another one is API, and third one is the speciality niche products. So, may be Ameyan can talk about this.

Ameya Deshpande: Yeah. So, basically with regards to the revenue contribution that the company has made via the various segments, we are looking at iodine compounds, which have contributed around 58% of the total revenues, APIs have contributed around 24% of the total revenues and thereby the remaining pie would be the 18% that we are referring to.

Sivaram: Okay sir, okay. Thank you for that. That's it sir, thank you very much.

Moderator: Thank you. Ladies and gentlemen, if you have any questions, please press * and 1. Our next question is from Mr. Chintan Seth from SKS Capital. Please go ahead.

Chintan Seth: Sir, just wanted to know the few data points, like, what is the gross debt including the current maturities as on December?

Pravin Herlekar: Siddharth?

Siddharth Sinkar: Total debt outstanding as of December is 210 crores on a consolidated basis.

Chintan Seth: Okay, out of which short term debt would be around?

Siddharth Sinkar: Short term debt will be about 130.

Chintan Seth: Which includes 25 crores of current maturity loans, right?

Siddharth Sinkar: Yeah, that includes, correct.

Chintan Seth: Okay, and sir, what is the current capacity utilization at all the plants on an average?

Pravin Herlekar: On an average, it is about 80% to 85%.

Chintan Seth: How is the market going around like, what kind of utilization can be sustainable over the next two, three years?

Pravin Herlekar: We already have a capacity of 4500 metric tons, which is in operation. Now this is being utilized at about 80% to 85%. Now additional 4500 metric tons is in the pipeline, which would partly happen in this calendar year FY15 and remaining by FY17. Now, to be honest, all our capacities are reasonably occupied. In any typical chemical industry, the normal level of operations should be around 80% to 85%, you cannot go beyond that. And today we already have many new products, which are already developed and ready for launch. Customers have also been identified and we have executed trial orders with them, but then capacity is still a handicap. So whatever new capacities will keep coming in next few quarters that will again get loaded adequately at appropriate time. So, we don't see any issue of capacity utilization since we have many products, which are ready with us. In fact the customers have been demanding from us that we should be able to deliver at the earliest.

Chintan Seth: Okay, so as I understand correctly, 4500 is the current capacity and you will ramp up doubling it by CY17, right?

Pravin Herlekar: Yes.

Chintan Seth: Okay. And if I come again on the margin side, this quarter has given a strong margin on EBITDA front, how can we be sure about the sustainability of those kind of margins? Are there any benefits we are getting on any of the APIs or any derivatives we use we shall.....?

Pravin Herlekar: There is no benefit as such, but then it is because of the product nature, the lesser competition, and whatever integrations we are having, backward as well as forward, which is adding to the margin, plus we have already launched the niche molecules, which we have recently developed. Some of them are also patented from our side. So, going forward, we don't see any reason why margins should decline. We should, on the contrary, perform better for time to come.

Chintan Seth: Okay and how many patented molecules we have currently?

Pravin Herlekar: We have already, two patents we have received and then there are 14 items for which our applications are pending, which we are sure we should get in coming months.

Chintan Seth: Okay, so in total two patents we already have and 14 patents we have applied for it.

Pravin Herlekar: Yes.

Chintan Seth: Okay, and...

Pravin Herlekar: Normally it takes about 2-1/2 years.

Chintan Seth: Oh yeah, that is quite understood, that patents take some time. Basically can you just explain the broad idea about the business, how it is basically run because I was just looking at the company and from your statement the concern is more towards the working capital cycle itself, where quantity is the norm with this kind of business, so how are you addressing? Is this the domestic business in India is taking much time to get converted into cash, is it the norm of the industry or is it what we are facing unusually?

Pravin Herlekar: This is normally the norm in the domestic industry, so major pharma companies in India, they pay after 90 to 120 days, that stretches our working capital, another issue is for the raw material, which is imported from Chile, it takes about two months for the material to come here after we open LC and all that, so transit period is two months, so this, on one side the raw materials, the second say on the sales side that delays payment by domestic customers, this stretches our working capital and that is why number of days in working capital are stretched. However, we are addressing it. Firstly by sounding all our local customers that we will not be afford such a delay and many of them are coming forward for addressing because for most of the products they are dependent on us, so they will accommodate us on this and it has started yielding results. Secondly as far as the imported material is concerned, which takes two months

for us to get it, now our major supplier in Chile, they have opened a warehouse in Mumbai near JNPT, so we will be getting delivery ex-house from the Mumbai warehouse. So that will cut down on our working capital cycle again.

Chintan Seth: Okay, when is this going on-stream?

Pravin Herlekar: It has already started. So going forward I can very well tell confidently that this issue will be addressed. Secondly we are embarking on the increase of our exports where the payments are coming out quite fast that is locally against the orders or against shipment documents, so basically exports will also be cutting down on our working capital days.

Chintan Seth: Can I get the name of the supplier, Chilean supplier you mentioned?

Pravin Herlekar: SQM is the company; they have already opened a warehouse in Mumbai.

Chintan Seth: And how is the relation with these guys, in terms of payment, is it in cash or is it in...

Pravin Herlekar: Normally we work on LC, we have to open an LC and if the material has to come from Chile, then after opening of LC, it takes normally about 10, 15 days for the shipment to happen and then the transit time of about 1-1/2 months.

Chintan Seth: Okay, so total two months.

Pravin Herlekar: So about two months or a little more; but now that time will be cut down.

Chintan Seth: If there is any supply abruption or any kind of, is it near (not clear) and you can get any supplier revision from there and we can get it in the first hand information that see this plan will get abrupted because of some certain reasons and we can...

Pravin Herlekar: SQM is our major supplier and we have relations with them for the last 20 years and they have been accommodating us in every respect, not only in quantity, but even price as well, and once when there was a crisis in iodine availability during FY11 and 12 we did get our supplies without any issues. So we have really good relationship with them and now with this warehouse being opened, we are quite comfortable to address this working capital days.

Chintan Seth: How much on a broad level, how much benefit of this warehouse will be in our working capital cycle, if you can just.....?

Pravin Herlekar: As I said, it will cut down on the transit time of two months. So, we don't have to block our LC for two months. See, I can explain to you in very short time, that is, LC of 90 days we are opening and out of that say few months are post LC transit. So, after the material comes to us we get only max to max one month for making the payment, okay. But then now, we can get the material, the stock from

Mumbai godown so that we can start processing the material we get credit of another 90 days after getting the material.

Chintan Seth: Okay, we will get the 90 days credit post the receipt of the material.

Pravin Herlekar: So, this is going to be very helpful to us.

Chintan Seth: Okay sir, let me check on numbers again and if any questions. Okay, one more question on the pledge history, how are you going to bring down the promoter pledge in terms of any broad, basically I can understand given the high working capital and short term money you require you have resorted for that kind of thing and any timeline or any broad mindset about how are you going to release it or what is the thought process of the commerce if you reduce the complaints?

Pravin Herlekar: See, I would like to share with you that the pledging has been done primarily for two accounts; one is for creeping acquisition which I did last year then secondly for subscription of warrant during this year and lastly as you said for the liquidity for working capital. Since our proposal for enhancement with Bank of Baroda was delayed to some extent, so we had to borrow against my shares, but then now the Bank of Baroda proposal is almost through and we should be getting the funds from BOB maybe in the next 15 days, so I am sure that by end of March the pledge level will come down sizably.

Chintan Seth: Okay, but on a sequential basis it has inched up, right?

Pravin Herlekar: Pardon me?

Chintan Seth: On a sequential basis last quarter to this quarter it has inched up little bit?

Pravin Herlekar: Yes, that is as I said we have taken funding for working capital and that will be eased out.

Chintan Seth: Okay, so you are looking at reducing it over a period, as of end of March you will...

Pravin Herlekar: Next couple of months it will be done.

Chintan Seth: Okay sir, thanks, all the best.

Moderator: Thank you, sir. Ladies and gentlemen, if you have any questions please press * and 1. Our next question is from Mr. Satish Mishra from HDFC Securities, please go ahead sir.

Satish Mishra: Yeah, hello sir. Sir, just to understand on the raw material side, I believe Iodine is one of your key raw materials, can you give us what proportion of total raw material is iodine and what are the other key raw materials and also with the recent commodity fall how these prices are behaving?

Pravin Herlekar: Well, iodine derivatives is the major segment in which we are catering to and iodine element in the raw material, that constitutes about anywhere from say 40% to 60% in the consumption of iodine derivative. It varies from product to product, that is one. Another important raw material what we require is Selenium metal, this is again imported from Europe and it is consumed for making lot of derivatives which are niche in nature. Apart from that we require Tartaric Acid which is also imported from China because India doesn't have any source for these raw materials, but major consumption which is iodine that will continue for the time being because iodine nevertheless is our major business and it gives us a very consistent business, so iodine business will keep going with whatever new additions of molecules we are doing in that iodine business. We have some niche molecules in iodine which are being recently patented also. So, iodine we will definitely keep going, though as a part of overall business, iodine business may get diluted to some extent as our API business is growing and another intermediate business is also growing. So currently last quarter it was 58% for the iodine business which may come down in coming quarters with the growth in APIs and other areas, but iodine will still continue to be our major business and we have a name in iodine business, we are considered as leaders in iodine derivatives especially in the niche iodine molecules particularly organic iodine molecules.

Satish Mishra: Okay, sir and how these prices have behaved over the last one year?

Pravin Herlekar: Iodine prices, they are declining during FY14 and in the first two quarters of FY15 also there was a decline, but now it has reached the level of around \$30 which is the rock bottom price for iodine and nobody expects the price to go down further and it is more or less stable at this level.

Satish Mishra: Okay and even other raw materials are also stable, there is no...

Pravin Herlekar: Other raw materials are more or less stable, I mean, there is not much movement.

Satish Mishra: Okay and sir, the new expanded capacities, you talked about doubling your capacity, so what kind of export proportion you are looking at in your total revenues in FY17?

Pravin Herlekar: Last year we had 30% exports, this year there will be a marginal increase in that and next year FY16 this may further improve and we are very confident because number of overseas customers have been added, particularly MNCs and the business is quite promising. At the same time as I had mentioned earlier we are now seriously thinking of opening up a subsidiary for taking warehouse space so that we can maintain stocks over there because there is a constant demand from most of our overseas customers particularly in Europe that we should maintain stocks there so that, they are ready to pay a premium also on our price if we have stocks, because they will get just in time of delivery. Like we are expecting our iodine suppliers to have a warehouse here similarly our customers over there, they are expecting us to maintain stocks there. So that will be a win-win situation for both and definitely the exports will also add to our margins plus more importantly relieving us from our working capital stress.

Satish Mishra: Fine, sir. Thank you, sir.

Moderator: Thank you. Next question is from Mr. Saurabh Ginodia from Steward and Mackertich, please go ahead.

Saurabh Ginodia: Hello?

Pravin Herlekar: Hello.

Saurabh Ginodia: Hi, sir. Can you give me some color on the competition scenario in your different product categories?

Pravin Herlekar: Yes, we have three major segments that are iodine derivatives, APIs and intermediates. Now, in iodine derivatives we have couple of players in India who are in this line for the last say 3 years, but the only distinction between them and us is the product profile. These competitors are mostly into commodity segments which is a low margin business whereas we are into specialty iodine derivatives with much better margins, this is one thing and then as far as these iodine derivatives are concerned, it is not only the domestic players which I just talked about, but even in the international level there are about 2 to 3 players who make iodine derivatives, but there again they are only focusing on commodity space mostly required for salt industry and animal feed industry, whereas we are one of the leading players for pharma industry and that gives us the strength in iodine business and we are able to maintain our positions. So, today whenever any consumer in the international market, use of any new iodine molecules we will certainly get an enquiry whether we can supply this that is our strength. Similarly Selenium, again the same logic applies, we are maintaining our position as a niche player and not a commodity player which gives us the strength to again maintain our norms. Selenium there is only one major manufacturer in Germany by the name Hicot and they also make commodity products for mostly the feed industry, animal feed and then glass industry, whereas we have Selenium derivatives which are consumed not only in these areas but even in micro nutrients, cosmetics and pharmaceuticals and these are very very niche molecules which nobody makes in the European market also. Similarly we have other categories of products like resolving agents which is again a very very specialized category for pharma, so there again we are pioneers and market leaders. So, we are maintaining our position as pioneers based on our R&D and the technology what we have and that gives us a comfortable position to remain leaders in the market.

Saurabh Ginodia: Sir, but if you can just name the two domestic players which you have just...

Pravin Herlekar: Well, it may not be appropriate on my part to name anybody, but then for the sake of sharing information I can say there is one company by the name Caliber Chemicals and one more company called Samrat Pharmachem. You can go to their websites and see their products and vis-à-vis our products.

Saurabh Ginodia: Okay and sir, how does this pricing mechanism work in your industry as you were just mentioning that iodine prices have gone down?

Pravin Herlekar: Correct, it is normally done on cost plus basis, that is based on iodine pricing with that we work on cost plus and normally this costing is done every

quarter, the prices for the material, that is iodine, they are decided on quarter to quarter basis and then we pass it on to our customers.

Saurabh Ginodia: And sir, lastly if you can help me with what kind of a revenue growth we are targeting for next two years and how do you see margins going forward?

Pravin Herlekar: Well, broadly what I can confidently say that the revenues will keep growing at pace of about say 25% year on year and margins as we have noticed, they will be improving because lot of niche products are getting added. API business is also growing which are the specialty intermediaries as well as API, they are our higher margin segments, so margins definitely will improve.

Saurabh Ginodia: Okay and sir, with respect to your process patents specifically for methylbenzoic acid.

Pravin Herlekar: I think you might be referring to 5-iodo-2-methylbenzoic acid.

Saurabh Ginodia: Yeah.

Pravin Herlekar: Correct, okay. So, that is a very new development and this product is used for anti-diabetic applications, this is a new drug developed by Nuveta and we supply to them. So, we are holding a patent and if we see a promising business out of this because just to share with you when we developed this and supplied to the customers on a trial basis they had taken quantities of roughly about 40 tons amounting to more than 24 crores worth. So, they were trial orders, so now when the product is already launched and we have started supplying so we expect to do much, much better than this.

Saurabh Ginodia: That's all from my side, thank you.

Moderator: Thank you. Next question is from Mr. Chintan Seth from SKS Capital, please go ahead.

Chintan Seth: Yeah sir, thanks for taking my question again, what kind of CAPEX we are looking for that expansion of capacity to 4500 MT?

Pravin Herlekar: Mr. Ameya will answer this question.

Ameya Deshpande: Yeah, so with regards to the expansions that we are looking at, we have already expended around 75% to 80% of the total requirement for the expansions that have taken place across the lasa unit at Mahad, Unit 5 and Unit 6. Unit 5 is going to be the 4,500 metric ton unit and we are looking at approximately 65 crores which have already been expended on this one and maybe another 14 to 16 crores to be expended over the next year.

Chintan Seth: 65 crores you have already spent?

Ameya Deshpande: Yes.

Chintan Seth: Okay and that is all we need as of now for doubling of the capacities?

Ameya Deshpande: Yes, so basically the capacity is expanding across four units, you have got Unit 5, which currently does not exist; basically it is a new project which will increase to 4,500 metric tons by FY17. 3,000 will come up stream by FY16 and another 1500 will come up in FY17. We are looking at Unit 6 which is again at Chiplun which is a 750 metric ton per annum plant, 300 of which is commissioned or is about to be commissioned in this last quarter of this financial year and the remaining 450 will come up by FY16. Then the Lasa plant which is the API plant at Mahad which is a 120 metric ton per annum plant currently; we are looking to expand this from 120 to 600 MTPA, this will again come up by FY16 and we are looking at Unit 1 which is the parent company at Badlapur, this is a 600 MTPA plant currently, this will increase to 900 MTPA basically an addition of 300 MTPA again to come up by FY16.

Chintan Seth: So, we are upgrading the 4 plants Unit 1, Units 5 & 6 and API 1?

Ameya Deshpande: Yes, exactly and the Urdhwa plant at Chiplun is being upgraded for FDA compliance.

Chintan Seth: Okay, so all in all we have spent 65 as of now and 14 to 16 crores by next year, so...

Ameya Deshpande: No, let me just clarify that. Across all units we have spent something around 120 crores as of now, across all units and we will require an addition over the next two full financial years plus this quarter we are looking at somewhere around 55 to 65 crores.

Chintan Seth: 55 to 65 crores we will be needing for next two years?

Ameya Deshpande: Yes, exactly.

Chintan Seth: Okay, so we can see post FY17 at 80% to 85% utilization we can see our revenue to double from current levels that is the correct expectation?

Ameya Deshpande: Yes, you are right in that.

Chintan Seth: Post FY17, post stabilization all the plants we have?

Ameya Deshpande: I would say that by FY17 we will be doubling our revenues.

Chintan Seth: Okay sir, thanks for taking my call and all the best sir.

Ameya Deshpande: Thank you.

Moderator: Thank you, sir. Ladies and gentlemen, please press * and 1 for your questions. Sir, there are no further questions; now I handover the floor to Mr. Satish Mishra for closing comments.

Satish Mishra: Yeah, thank you Madam. Thank you everyone for participation in the call. Thank you, Omkar Management for giving us the opportunity and your valuable time. Sir, would you like to make any closing comment.

Pravin Herlekar: Well, I would only like to say that apart from whatever we have discussed if anybody has any further queries they can drop a mail to you and then probably you can forward it to us or they can write to us directly.

Satish Mishra: Sure sir, thank you sir.

Moderator: Thank you, sir. Ladies and gentlemen, this concludes your conference for today. Thank you for your participation and for using Door Sabha's Conference Call Service. You may disconnect your lines now, thank you and have a pleasant day.

Note:

- 1.This document has been edited to improve readability.
2. Blanks in this transcript represent inaudible or incomprehensible words.