"Deepak Nitrite Limited's Q3 & 9M FY23 Earnings Conference Call"

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Moderator: Ladies and gentlemen, good day and welcome to the Q3 & 9M FY23 Earnings Conference Call of Deepak Nitrite Limited hosted by IIFL Securities Limited.

As a reminder, all participant lines will be in the listen only mode and there will be an opportunity for you to ask questions after the presentation concludes.

I now hand the conference over to Mr. Ranjit Cirumalla from IIFL Securities Limited. Thank you and over to you, sir.

Ranjit Cirumalla: Thank you Rutuja. Good afternoon, everyone and thank you for joining us on Deepak Nitrite's Q3 & 9M FY23 Earnings Conference Call. Today, we have with us Mr. Maulik Mehta – Executive Director and CEO; Mr. Sanjay Upadhyay – Director, Finance & Group CFO and Mr. Somsekhar Nanda – CFO.

We will begin the call with opening remarks from the management team followed by an interactive Q&A session.

To begin with, Mr. Maulik Mehta will share his views on the operating performance and the growth plans of the company followed by Mr. Sanjay Upadhyay who shall take us through the financial and segmental performance.

I now invite Mr. Mehta to share his opening comments. Thank you and over to you.

Maulik Mehta: Good morning, everybody, and a warm welcome to you on Deepak Nitrite's Q3 & 9M FY23 Earnings Conference Call. I trust you had an opportunity to go through our results documents that was shared earlier. I will begin by taking you through the key financial highlights and operational highlights for the period ended December 31st, 2022, and some key developments and strategic approaches for the coming year. Mr. Upadhyay will then present you with the financial overview about the period under review.

The operating environment continues to be highly dynamic. The recalibration of global supply chains over the last year due to various points like the sanctions on Russia continues to play out. Further, we have the Chinese economy reopening after loosening of very strict COVID protocols. it will continue to remain dynamic at least for the next couple of months as the situation gets normalized. Of course, these developments have certainly affected the supply and demand of key intermediates.

Within this backdrop, we are pleased to share that DNL has demonstrated remarkable agility in capitalizing on pockets of opportunity during the third quarter. Our global competitiveness and strong customer relationship ensured that we are called upon by customer for the requirement while our focus on operational efficiency ensured that plants can be consistently operated at high utilization levels. This quarter, we have set new benchmarks in production and sales volumes for several key products such as DASDA, OBA and Phenol.

Consolidated revenue for Q3 was Rs. 2,004 crores, higher by 15% on a year-on-year basis. Now, despite the recent cooling off in price on certain inputs and by recent, I mean the last couple of weeks, they do remain elevated as compared to the same time last year. We had indicated that higher cost would be passed onto customers with some lag and the ongoing passthroughs. Q3 EBITDA of Rs. 328 crores were higher on a sequential basis from the previous quarter of Rs. 283 crores by 16%. Consequently, the EBITDA margin too has risen over the previous quarter, though it remains below the elevated level of last year. Certain product margins were high last year but have normalized this year causing margin compression compared to the base period. We are taking further measures to pass on increased input cost while also driving cost optimization to protect profitability, but I would also want to mention one important point that this is the base effect. From a standalone basis, every single kilo that the company manufactures have been able to maintain or grow its gross EBITDA per kilo. Naturally, with higher raw material price and higher finished good price, the percentage looks squeezed.

Anyways, going onto the performance of the Strategic Business Units - The Advanced Intermediates business delivered strong revenue despite inflationary pressures in the backdrop of strong demand. We have aggressively pursued opportunities both domestically and with international customers. There was a sharp rise in exports by nearly Rs. 100 crores in the same quarter when compared to the previous quarter. The segment is expected to continue to perform well due to the shift of global supply chains and positive demand trends. Further performance will be driven by new multiyear contracts, strong demand and the ability to pass on cost increases to customers as prices of product and raw materials stay at elevated levels per kilo margins as I mentioned earlier are better even though the percentage looks deceptive. I would remind you that out of 9 months, our Nandesari unit is operated for 8 months, little bit less than 8 months as the month of June was lost owing to fire incident that took place.

The Phenolics business has demonstrated encouraging results with an average capacity utilization more than 117%. I would like to say here that while demand in India remained stable, weakness in global demand was observed. Many Asian Phenol plants were operating at 60%-65% capacity and nonetheless, we were able to manufacture and sell more than 117% of our production capacity. We saw an EBITDA margin improvement compared to the previous quarter owing partially to moderation of raw material prices and partially due to the Indian demand remaining a price spot in Asia.

Deepak Nitrite's standalone basis achieved first 13 consecutive quarters an ROCE of more than 30% including the current quarter. The results should be seen in light of the unusually high base of higher margin in Phenolics and recent supply side challenges for critical raw materials like Nitric Acid. Now, while the world has witnessed volatility, Deepak's customers have not. The Company has maintained or grown wallet share in nearly all its products and its relationships with key accounts remain buoyant. As domestic consumption in some segments has been subject to sluggish demand in the recent few quarters, the Company has prioritized export market and ensured that both production and inventory remained very much in control. We are also progressing well with our expansion plans with multiple projects in progress.

The installation of capacity for our SAC plant is set to be commissioned this quarter. Our project for MIBK and MIBC which are derivatives of Acetone are progressing well and should be on stream as planned. Just to highlight that between these products and IPA, the Company will consume 80% of the Acetone that it manufactures. We are constructing a facility for complex fluorination and photo chlorination that will go on stream starting early age 2.

Our project to internally manufacture key raw materials is progressing well and towards commissioning as planned. In addition, our Board has approved a capital investment of approximately Rs. 1,000 crores which will help the company's growth plans. Out of this, we have approved the project for manufacturing Polycarbonate compounding at a world scale which will add impetus to our move towards the Polycarbonate business and this will help us in understanding the key market place, the niche players, the large players and we will be manufacturing compounding products which will be used by growing demand in India in applications like 5G boxes, EV batteries, medical devices and much more.

With the Nandesari plant back into full operations and other plants running at high utilization, we are operating with good momentum. Our captive power supply enables us to do so consistently, and steps have been taken to create assured supply of critical raw materials while we further de-risk the business. With multiple plants set for commissioning in the ensuing quarters, we are very well placed to continue to deliver on our growth aspirations.

One point that I forgot to mention also is that we continue to progress as per plan with regards to our plant in Oman that will manufacture Sodium Nitrite as Phase-1.

Thank you and I would now like to hand the call over to our Director, Finance and Group CFO, Mr. Sanjay Upadhyay to address this forum and take you through the financial performance. Thank you.

Sanjay Upadhyay: Deepak Nitrite reported an encouraging performance during the period under review. Despite the ongoing macro challenges, solid improvement was demonstrated in both our business segments aiding DNL's continued strong revenue growth. I may like to mention here that around this time, the macroeconomic situation for chemical industry as regard prices of raw material were not very supportive, however, in spite of its steep challenges, we could bring in a resilient performance owing to diversity in our product basket reaching out to the customers not only at the time of their need, but always hence increasing the wallet share. Constant negotiation of price of major raw materials, making raw materials available at all times to see that we excel in our operations. All of these steps helped us to deliver better and sustainable performance.

While I take you through the numbers, there was one key development during the period, the Company was awarded for Excellence in financial reporting for its annual report 2021-22 by The Institute of Chartered Accountants of India. We take pride in announcing this and these is a milestone achievement for us.

On the operating front, the domestic business revenue stood at Rs. 1,574 crores in Q3, higher by 11% and on a cumulative basis, Rs. 4,898 crores higher by 30%. Export revenue was at Rs. 417 crores in Q3 and Rs. 1,113 crores in 9M FY23. On a consolidated level, domestic to export mix stood at 79:21 for Q3 FY23 while standalone DNL's export revenue was 45% of the total turnover.

In 9M FY23, on a consolidated basis, revenues were up by 22% at Rs. 6,046 crores compared to Rs. 4,969 crores in 9M FY22. Robust revenue growth was achieved through increased volume across segments and especially in Phenolic segment. Utilization level remained high with ongoing improvement throughout the year to that period. EBITDA stood at Rs. 976 crores in 9M FY23 compared to Rs. 1,232 crores in 9M FY22. PAT stood at Rs. 618 crores versus Rs. 799 crores in FY23.

In Q3 FY23, on a consolidated basis, revenues grew by 15% at Rs. 2,004 crores as compared to Rs. 1,748 crores in Q3 FY22. The impressive topline performance was fueled by higher production volumes in several key products. EBITDA came in at Rs. 328 crores compared to Rs. 378 crores in Q3 FY22 and PAT stood at Rs. 209 crores. Profitability is lower on a Y-o-Y basis due to high base in the previous year, but the Company has improved profitability quarter-on-quarter in line with its operational performance.

Now, moving to our segmental performance, in our Advanced Intermediates segment, revenue was higher by 19% to Rs. 829 crores in Q3 FY23 versus Rs. 699 crores in Q3 FY22. The growth is owing to sustained healthy demand from key customers while the rise in EBITDA was 2% to Rs. 172 crores during the quarter under review. As Maulik mentioned, growth in EBITDA has not kept pace with revenue growth due to significant increase in input cost compared to the previous year. Although input price has moderated recently and the Company is working to transfer the elevated cost to its customers. By and large, we are successful in achieving this. If you see on per ton basis, we have achieved higher contribution, but in terms of percentage because the total revenue is also going up, you are seeing marginal impact on the percentage.

In 9M FY23, the revenue grew at 27% to Rs. 2,263 crores and EBITDA came in at Rs. 470 crores translating into margin of 21% despite the current environment and challenging circumstances.

Deepak Phenolics has delivered an encouraging performance with revenue growth of 13% to Rs. 1,187 crores in Q3 FY23 versus Rs. 1,050 crores in Q3 FY22. The Company has operated all plants at high utilization rate. The Phenol plant has clocked an average utilization of 117%

for the quarter and achieved highest ever quarterly domestic sale and highest production per day of Phenol. In spite of achieving 117% we are debottlenecking the Phenol capacity further and you can expect some further growth in the volumes. EBITDA stood at Rs. 157 crores and EBITDA margin came in at 13% in the quarter.

In 9M FY23, the revenue stood at Rs. 3,812 crores and EBITDA came in at Rs. 508 crores translating into margin of 13%. During the quarter, DNL witnessed extreme volatility in exchange rates (USD to INR), which peaked at Rs. 83.03 and bottomed at Rs. 80.81 recording a volatility of 2.75%. For 9M FY23, the exchange rate moved between Rs. 75.30 to Rs. 83.03 recording a sharp volatility of 10.22%. The Company implemented dynamic hedging strategies to mitigate foreign exchange risks resulting in a gain of Rs. 3 crores in Q3 FY23 and Rs. 4.62 crores in 9M FY23. The Company continues to remain debt free with a networth of Rs. 3,860 crores thereby strengthening the balance sheet for future expansions.

I would now request the moderator to open the floor for question-and-answer session, please.

Moderator: Thank you very much. We will now begin the question-and-answer session. The first question is from the line of Nirav Jimudia from Anvil Research.

Nirav Jimudia: Sir, I have two questions to ask. First of all, great details on the expansion program, so I think we have got almost all the details of the Rs. 1,500 CAPEX which is currently undergoing. So, just wanted to ask here, you have mentioned one of the points in terms of the backward integration in Fluorination space and Acid plant, so if you can help us explain the rational over here like in terms of let us say first on the Fluorination side, so are we producing some of the products where entering into Fluorination would be a first step to assist our current product profile as well as the newer opportunity size which we will be addressing with this foray into the Complex Fluorination which you just mentioned in your opening remarks. So, this is on the Fluorination side and on the Acid plant, if you can just give some bit of understanding like what the size of the plant could be or let us say out of around Rs. 460-Rs. 470 crores of raw material cost which we have reported in the standalone business for Q3, how much would be the contribution of or the raw material composition of acid out of this Rs. 470 crores?

Maulik Mehta: I will answer the first question first. So you rightly pointed out our strategy when it comes to Photo Chlorination and Fluorination. About few years ago, this was imported 100% by us, not just the Fluorinated molecule, but downstream as well and then we used that as a feedstock for a few of our agrochemicals. Then, we started facing pricing pressure from China and hence about a year ago, we stopped using some of our existing assets and repurposed them to make the upstream ourselves partially and those steps required Nitration, they required reduction, distillation, purification, those things. So, those were processes which Deepak is intimately familiar with, so we shifted from manufacturing, other products and started using them here in order to de-risk our supply chain. We started with 50%, today we are manufacturing 100% of our internal requirement, but we were still at risk for the basic feedstock which again came from

China. Now, with this, what we aim to do is have a 100% de-risked model all the way from the petrochemical source to the final advanced intermediate. More than that, we recognize that these are competencies which we are adding to our portfolio. So, it was important that we start with products where we ourselves would be the anchor customers and it would essentially not require a market discovery process. While we would sell good amount of volume to strategic customers, we would also be our own customers. Nonetheless, this was never the end in tension, this was the beginning. So, all of the assets that we are putting up are up engineered in that sense to be able to do a lot more to be very flexible and fungible and with that we intent to get into more advanced processes which require the same chemistries. But as I mentioned the first step was to do something where we have a very high chance of success and as we are succeeding and as we have established the key infrastructure which is required, we are working with strategic customers in order to develop products that they want which would utilize some of these streams into supplying their requirements. So, it should be very different from the product that we are going to be making which we will self-consume. So, this gives you a good understanding of how we are looking at investments, first by either having an existing strong competency or building a competency by targeting strong customer in this case ourselves and then building up that competency horizontally by ensuring that the processed knowledge that we are able to gain allows us to make more complex molecules with niche applications.

So, that answers your question about Fluorination and Photo Chlorination. Both of these are built in multiple ways, so that there is a level of flexibility. We have purification towers along all of these, so that it allows us a greater sense of flexibility in making one set of product and another set in parallel, if we so choose or we can make higher volume of a smaller number of molecules. This choice will remain ours and the plants are engineered to be modular in that fashion even moving forward.

Similarly, as you asked about the backward integration, what I can just share rather than going into very specific numbers is that the capacities will address not only all of our requirements today, but all of our requirements over the next few years because once we have our own internal supply, we will naturally work towards expanding its consumption. But there will be ample supply for us even with the expanded capacities.

Nirav Jimudia: So, sir, if I understood your answer correctly, in the Fluorination space, some of the products what we are already producing, 100% of that product backward integration we are doing, but we are going one step ahead and building up the capacities to assist the 100% backward integrated product also and safe to understand that product or the capabilities what we are building can suffice newer number of addressable products which then we may approach to the markets for agrochemicals or may be pharma and a new stream of revenue could be opened up for us?

Maulik Mehta: Absolutely, we are already in active conversations with specific strategic customers to develop products for their niche application. They happened to be in the life sciences, the agro and pharma space. We are working with them, we cannot talk specifically about the products, but rest assured that these will be with a long-term focus in mind.

Nirav Jimudia: And this acid plant would also have NA plant for our CNA requirement, right?

Maulik Mehta: Again, not going into specifics, let me just tell you that we will be no longer subject to the vagaries of the market. The point is to de-risk and we have been working on this for a while and it is something that we expect to see very soon and it will allow us to be on very firm footing.

Nirav Jimudia: Sir, second question is on putting up the Sodium Nitrite plant in Oman, so I think we are substantial player here in India for Sodium Nitrite and our last quarter press release suggest that we will be increasing something around $15 million as the initial amount for that GV where we will be holding 51% stake. So if you can just help us through the rational of putting up a plant over there, why we have been putting up a plant in Oman? What could be the size of investments which could be happening and let us say if our current capacity is X, how much would be the addition happening to overall Deepak Nitrite portfolio so far as Sodium Nitrite is concerned from Oman?

Maulik Mehta: Basically, this is something that we have been working on for a while, but we were doing it in a soft manner. As we saw the situation all over the world with regards to the energy crisis, develop and become, in the beginning it was more of a short-term threat, but it turned out to become more of a systemic challenge. We activated and we started fast tracking a lot of the initiatives that we had been working on anyways in Oman and hence the reason that we have targeted it is clear. Oman is a country where the energy that is available is used both as a feedstock as a raw material in the form of ammonia as well as an energy source. It also has paid agreements with various countries of interest worldwide.

Now, one thing that happened over the last 2 quarters or 3 quarters that is while the Indian domestic demand was temporarily subdued because of XYZ reasons, we targeted more and more of the export demand which was earlier may be supported by European manufacturing because we saw the systemic shift. Today, I think we have more than doubled our export volumes compared to the same time last year and this will continue. But we are running our plants on full right now, so we cannot wait for this facility in Oman to come up. So, we really needed to come up very quickly, so that as we see the Indian market also recovering, we don't need to let go off the export market which we have been able to capture. So, that market will be serviced by our facility in Oman whereas the resurgent Indian demand will continue to be met by our plants in India.

Now, with regards to size, today Deepak is already a world scale manufacturer of Sodium Nitrite and what I can say is that the Oman facility to start off with, will be of reasonable size compared to the Indian plant. It will not be exactly as large, but it will have the capacity to ramp up production rather quickly depending on the demand, but we take a balanced approach, so we can say that the plant in Oman will be world scale, but to start up with Phase-1, it will be somewhat smaller than the plant in India. It will also have ample room to grow in terms of the infrastructure along with the opportunity to set up other products in phase 2 and phase 3 which may have something to do with Sodium Nitrite, may not necessarily but may follow similar philosophy where we are able to use the Omani advantage to our benefit.

Nirav Jimudia: Is there any timelines we have set internally for this project to start in the Phase-1?

Maulik Mehta: We are targeting to see how we can do it in 2 years or so, the early, the better for us.

Moderator: The next question is from the line of Vivek Rajamani from Morgan Stanley.

Vivek Rajamani: The first question was on the Advanced Intermediates performance and it is a bit of a two part question here. Obviously towards the end of last quarter you said that your Nandesari facility was now operating fully and I think even during the comment you mentioned that you have had high utilization rates, so the question was if I see this quarter, it is obviously still quite a bit lower than the peak that you saw in the fourth quarter of 2022. Would it be fair to say that this is purely based on the margin and price compression that you see since then and if you could just elaborate on which products are causing this that would be great? And the second part of the question was you obviously mentioned very high utilization rates across the board, would it be possible to give a bit more specifics for some of your bigger plants, that will be helpful?

Maulik Mehta: I did not understand the first part of your first question, are you comparing our quarter 3 performance to our quarter 4 performance, or you are talking about this particular quarter that we are speaking about meaning Jan to March 2023 because we barely know our internal numbers, I am surprised that you know that.

Vivek Rajamani: I was just referring to the December quarter performance and comparing to the March quarter of 2022 which was obviously the peak for that segment?

Maulik Mehta: Let me also point out that to a certain extent, last year some of our raw materials on formula link where it is not the case today. That is one of the factors. The other factor of course is that last year before the Ukraine war broke out, the price of several commodities like oil and therefore petrochemicals, BTX were lower. Along with that there was generally speaking an optimistic atmosphere where the domestic market, dyes and intermediate segment, all of these segments were quite buoyant in terms of their expectations and outlook through the year and also one thing that is always there is while Q4 is in that sense a relatively normal quarter in any year, the Jan and Feb months are normally affected by uncertainties owing to China's New Year and all of those things. Beyond that, what else are happening is that a lot of customers of ours are looking at the year a fresh, so they are done with their previous quarter which would be on the calendar basis, the non-Indian customers, they have finished and now they are looking at new volumes, new contracts, new this and new that and in most cases, it has allowed us also to have slightly higher prices and slightly improved margins as per the renegotiated contracts. So, these things happen and I would not read too much into this to be honest. What I can say is that quarter 4 has just begun. It began with some rays of optimism, but it is too early to call the quarter a normalized quarter. Nonetheless, it does point to greater consumer confidence in various countries across the world. So, we see how it goes, but I remain cautiously optimistic.

And about our plant utilization, our plant utilization is good across the board. In most of our plants, all our large volume or high value plants, we are doing well. I can give you one example in the month of November and December, when we commissioned facility that goes into manufacturing of an agrochemical intermediate, this was an expansion project. Now, once we commissioned it, we were able to ramp it up to 100% utilization within a few days and by the end of the month, we were able to ramp that up further to 120% of the designed capacity and we were able to do it with all due precautions in mind and let me also assure you that throughput, even the increased throughput is all spoken for several years to come as well because these are all tied up in volume contract and our customers have shown that there is a great degree of optimism with regards to the end application here.

Vivek Rajamani: And the second question was something you did also touch upon briefly in your answer, I just wanted to get a sense in the first month that we have seen, whether there has been any change in the trends in terms of the end segment demand or is it broadly similar or again like you said you are cautiously optimistic, so just wanted to get a sense if any segments show some signs of pick up or not?

Maulik Mehta: Generally speaking, we are seeing compared to the previous quarter slightly greater sense of optimism. Now, just to be very clear, optimism doesn't straight away translate into more orders. Optimism translates first into discussions with a longer outlook in mind rather than just a few weeks or a month. It talks more about how we see the situation and the resilience of the end application, whatever the end application is, it could be textile, it could be paper, it could be detergent, it could be agrochemical or pharmaceuticals. So, our customers are having a conversation which includes how they see the world improving in its buying sentiments over the next few months. And in some cases, this has resulted in our customers being more willing to buy larger volumes, run their plants at a higher capacity, holding onto more stocks of raw material because they see their order book selling up, but as I mentioned, cautious optimism because this is still early days, a lot of new factors have to be considered, for example, China's reopening, Europe going through milder winters than anticipated, various countries, central banks also sounding not dovish, but less hawkish, so it is going to be end to end about whether every single part of the global recovery trends in the same direction or not. Therefore, it is enough to start a conversation.

Moderator: The next question is from the line of Naushad Chaudhary from Aditya Birla.

Naushad Chaudhary: Firstly, on the power cost pressure sir, in last couple of quarters, it has almost doubled. Any outlook here, any sort of relief we are witnessing here or how do you see in next 2 to 3 quarters, how should it be?

Maulik Mehta: See when you are saying power cost, you mean power, coal, all utilities, correct?

Naushad Chaudhary: Yes, what we see in the P&L, sir, I don't know the split there?

Maulik Mehta: See, as volumes for example in Phenolics as the volume and the throughput of the plant increases, you can anticipate that so would the power and fuel cost. On per kilo of the final output basis, it remains consistent, but we are still exposed to the volatilities of the movement of prices of products like coal and natural gas, for example. So, as we stabilize over a period, you will see the gross value of these costs also stabilize. One thing I can tell you is that because of our Cogen power plant operating in Dahej, we were able to avoid any and every failure of the plant because of the grid being down. This allows us to maintain a consistently high level of production and allows us to avoid any negative impact with regards to the specifications in quality of our Phenol or Acetone because they are manufactured in a continuous basis. So, this gives us more confidence, more product, better quality.

Now, let us see how coal prices and the gas prices moderate over a period of time. Right now, it seems like in the last couple of weeks they have improved, but it is again as I mentioned very early.

Sanjay Upadhyay: There is a onetime intake also. Because of fire, our coal fired boiler was down in Nandesari and we had to run our plant because we wanted to get production yet to run on gas, which you know it was very costly then. So, these things do happen and these what you are saying is a total number, but the production volumes have also gone up in Phenolics and this. So this is also impacting, so we can't just compare the absolute number, but then yes, it is fairly under control.

Naushad Chaudhary: Sir, the one-off impact, can you quantify that and would it be there in the coming quarters as well?

Sanjay Upadhyay: No, but that was because of fire, now why should it be there.

Naushad Chaudhary: And would you be able to quantify that?

Sanjay Upadhyay: No, no need to quantify this particular figure, but I have just explained to you that this is also there because one month, we have to run the boiler on hot gas.

Maulik Mehta: We will quantify it when speaking with the insurance company.

Naushad Chaudhary: And sir, just, I have calculated it though, but just wanted to hear from you how you are saying the Phenol spread moving because I see the Benzene, Propylene, these prices are softening. But if you compare it with the Phenol prices, Phenol prices relatively are stable, so how you see the Phenol spread currently and any outlook if you would like to share?

Sanjay Upadhyay: What does your calculation say, I shall hear from you?

Naushad Chaudhary: Obviously, the secondary market data and you have been sharing that your way of doing things it slightly different, so it won't match, but directionally it is indicating that there is a positive improvement at least from the spread side, so would you validate that, sir?

Sanjay Upadhyay: May be in short term, not much, I don't know whether if you are saying but yes, in Phenol margin, I think by and large will remain in the same range as of Q3, maybe 1% or 1.5% here and there.

Naushad Chaudhary: And last question, in terms of the end user slowdown, earlier you had indicated textile is having some problem, apart from this any other end user which is giving us problem in terms of growth?

Sanjay Upadhyay: I think it is it is done but that is the reality, it is only textile and dyes and dye intermediates where also we are seeing the improvement now in the fourth quarter. That segment is really impacted, otherwise we don't see much of a problem in any of the other segments.

Maulik Mehta: I will add however, that the European paper industry is currently in quite a depressed state, but it has been low for the last 3 quarters, so any small improvement will also be a big improvement and that is significant power cost and water cost and energy cost that it has to contend with. So, as I mentioned earlier this is a structural thing, but our customers certainly are looking at Deepak as larger player rather than their other suppliers who are also based in Europe. So, this helps us because when we are manufacturing in India and supplying to European companies, suddenly they prefer Deepak rather than buying from other European companies which might be facing their own cost of power and energy and water.

Moderator: The next question is from the line of Chintan Modi from Haitong Securities.

Chintan Modi: Firstly, you have mentioned about new investment of about Rs. 1,000 odd crores, which will partly also go for Polycarbonate compounding business and furtherance to your Polycarbonate business, so if you could help us understand what exactly would this mean?

Maulik Mehta: It is now exactly that, as you rightly mentioned, so the compounding facility which would be a world scale facility will be able to make small batch and large batch, so made to order and made to stock and it will largely service India's very fast-growing demand of these compounds. Now, the compounds are manufactured based on certain properties that they are imbued with it. It could be the ability to withstand temperature or pressure or a particular shape, it could be on the base of precession, lot of different metrics depending on the end application and all of these therefore have Polycarbonate as their main ingredient with other additives which are able to support that particular application.

Now, in this case, what we are going to do is with this facility, we will engage with key partners and start building those relationship supplying and having our products approved at their end and as we are doing this we put up significant facilities that will manufacture Polycarbonate and its upstream all the way to Phenol over a period of time and then once that is done, it is essentially supplying to the compounding facility itself which is then making the application compounds as the customers require. Some amount may also be sold into the market and some amount will be moved via this compounding facility. So, it is our effort to occupy a space way downstream where we are talking more about applications and more about long-term value creation with customers who are based on Indian requirements.

Chintan Modi: So, basically, currently, you would be buying Polycarbonate, compounding it and sell it into the market and once you understand the market, you will be going more backward integration by setting up a Polycarbonate plant?

Maulik Mehta: Yes, so imagine building a bridge from both sides of the river.

Chintan Modi: And secondly, as you mentioned about your backward integration projects which are currently under implementation. Once you are done with that what level of self-sufficiency you will achieve in advanced intermediate business if you could give us some kind of a number?

Maulik Mehta: We should see an EBITDA improvement of at least about 2% across the Advanced Intermediate revenue. So whatever is the EBITDA percentage that we get, we will consistently be able to add at least 2% to that, more as we add more production and the debottleneck and add more capacities. So, that will be margin accretive, but in the meanwhile, it will be at least 2% on the current business.

Chintan Modi: And if we were to just see it from a revenue perspective like how much portion of that will be backward integrated to a large extent, how much would that be?

Maulik Mehta: Just to be clear, I don't think I have understood your question to be honest, but we will be internally consuming to start up with about two third or little bit more than two third of the capacity with plans over the next two years to expand that to about 90%-95%.

Sanjay Upadhyay: See, the idea here is we are setting up this facility with some extra capacity. We will expand parallelly in Nitrogen business, so that we consume entire production captively. It paves way very fast, may be 3 to 3.5 years and this is a step in right direction because not only the price advantage, but it was also causing interruptions in the operations which will stop now. So, it is helping us on both fronts, EBITDA improvement as well as running the plant smoothly.

Chintan Modi: Sorry to hammer on this, my question was a little different like, out of the Rs. 100 of revenue that you are deriving today, say in Advanced Intermediates, how much proportion of that revenues would you be fully backward integrated or say to a large extent backward integrated?

Sanjay Upadhyay: Advanced Intermediate a large product portfolio. We are talking of only Nitric Acid here, right and the fluorination. So, the combination would not be, I don't know how it matters to you in terms of percentage. That cannot be so large. There are usually two products what Maulik spoke about.

Maulik Mehta: I think there is confusion about your question. Look, we manufacture a lot of products which will use these feedstocks. They have their own revenue and margin profiles and because we are long in particular streams, it is very difficult to quantify because if I am making a product which has nitration as key step, I am selling that, but I am also internally consuming that to go downstream into other processes which may be Hydrogen Reduction or Sulphonation or Cyanuric Chloride reaction and things like that. So, it becomes very challenging for us to answer this question because everything that we are doing in the Advanced Intermediates business is part of one chain or another, so how do we go about answering this question. Most of them begin from the Basic Intermediate building blocks and the large part of Basic Intermediates as the building block require these few intermediates that we spoke about which we are backward integrating into. They are not only one, but they are key raw materials. So, as it supports the upstream cost and availability, so will it benefit all the way downstream as well, but the safer answer to tell you is that it will certainly help something in topline because we have not had the opportunity to manufacture consistently because of unavailability of some raw materials as I mentioned. So, when we do it on a regular basis, we will add to the topline, but the significant impact will be an improvement to the EBITDA percentage. This is what Mr. Upadhyay has also emphasized.

Moderator: The next question is from the line of Meet Vora from Axis Capital.

Meet Vora: I just wanted to understand on Phenol and Acetone derivatives, so while you have said that we will be doing MIBK and MIBC and including IPA the total Acetone consumption captive will be around 80%. So currently you will be selling the current Acetone in open market, so will we let that market go off or how we are planning on that one MIBK and MIBC come on stream?

Maulik Mehta: That is kind of left to us because we will see that we participate in the market depending on the value that we get, but it gives us that sense of flexibility because when we make Isopropyl Alcohol - IPA, it comes in a margin accretive manner compared to sale of just pure Acetone. Similarly, MIBK comes in the margin accretive manner, similarly MIBC is margin accretive to MIBK itself. So, all of these and in fact MIBK and MIBC will have margin profiles which would be similar to what you would expect from say the AI business. So, it is an effort to go downstream, now, if you are asking about the pure play Acetone market, we will need to figure out the strategy about how we can address that, but as Mr. Upadhyay also mentioned we are debottlenecking our Phenol and Acetone capacities anyways. When I refer to 80% of Acetone production, I was referring to the current production. We will be able to add some through debottlenecking exercises which are extremely short term. So, you should see the result of that coming in may be a couple of months from now to be honest, may be in Q1 of the next year and that will add capacities of both Phenol and Acetone. So, I think we will be well placed to have a significant market share of all the product including Acetone, even though we plan to internally consume higher and higher quantities and as required, when required, in the future we do anticipate that we will need to significantly expand our Phenol capacity far beyond what the current plant is capable of doing. So, we will have to put up new plants, some of those capacities will be consumed downstream as we move toward Polycarbonate and some of those will be available to the market as we intent to maintain a particular wallet share in India's growing story.

Meet Vora: And secondly, as you rightly said that in Polycarbonate we are building bridge from both sides of the river, so I just wanted to understand whether we have tracked the Phenol downstream products till we go up to Polycarbonate like this Phenol, entire have we tracked or till the time we market for Polycarbonate through just processing it and once you find the end consumers then we will start tracking or how is it going to go about and also if you can quantify that?

Maulik Mehta: Sorry, what do you mean by tracking, the technologies are widely available and well established. There are various different technologies, different groups, all of them are well established, all of them have different advantages as it pertains to the Indian ecosystem, now it is up to us to decide which road we want to take, but the destination is clear and we have started to invest in the destination as well.

Meet Vora: And sir, if you could quantify the debottlenecking exercise that we are doing on Phenol and Acetone plant that will be helpful?

Sanjay Upadhyay: We will add around 50,000 tons, we will touch around 3,00,000 ton, above 3,00,000 ton.

Moderator: The next question is from the line of Manish Jain from Moneylife Advisory Services.

Manish Jain: I wanted to understand the trend in raw material prices, in the past few quarters, prices had increased drastically due to various factors, so are you witnessing moderation in the prices especially for Nitric Acid, Ammonia and Caustic Soda?

Maulik Mehta: These prices are volatile now. They are at an elevated level if I am comparing to the last year the same time. There has been, I won't call it moderation certainly, but I would call it plateau compared to the previous quarter and as and when we do find small pockets of opportunity, we take them, we are large consumers and hence we are able to use that and leverage better product pricing, but beyond a point this is also challenging. So, in the short term, we do anticipate that even if prices moderate, they may not reach the prices that were turbulent last year. One of the reasons of course being that last year, we were engaged in contractual agreements with formula prices and this time we are addressing the situation on our own. I will just highlight that what you see as the performance of this quarter, the last quarter, and the quarters before that is despite having this as a challenge. So, this is not a challenge that began last week, it is not just going to be in quarter 4, it have been the challenge for the entirety of this financial year and as you can see while it is a challenge we take it as pride, we are up to the task and we work hard to maintain our margin profiles and while we are doing all of this, we do not lose wallet share.

Manish Jain: Secondly, wanted to understand are you looking to strengthen your employee base in the medium term for the upcoming projects and expansion and also, can you give us sense on the number of employees you will be looking to add in the R&D department as you foray into more downstream products?

Maulik Mehta: No, I won't go into numbers, but there will be significant addition, nonetheless, we also have internal programs where we target to prefer internal mobility. Now, of course in R&D it is difficult because our teams are generally occupied and normally for things like compounding and all, it requires a specialized skill set. So, we have been looking out and taking talent and we have some good people who have joined us with very clear vision in mind and they are already working on that. It is in that sense quite like what we did about 2 years ago when we decided to enter the Fluorination space. We announced it about 8 months to a year after we started recruiting, we started building R&D facilities, we started piloting, we ensured that we tied up our raw materials, we started hiring people who would be operating at the plant, those people were also deeply involved when we were doing the piloting, so that they would be confident that what they were getting when the plant is operational is something that they were confident running. Their input and guidance have been invaluable to us while we have done this. So, we recruit at the right time, not too early, but not only at a time where we need to operationalize. So, whether it is at R&D level or it is at plant level we start incorporating people and ensuring that the transition is smooth.

Moderator: The next question is from the line of Rohit Nagraj from Centrum Broking.

Rohit Nagraj: Congrats on the sequential growth in both segments. Sir, my first question pertains to the CAPEX, so Rs. 1,500 crores CAPEX is what we have planned for FY23 and FY24 and as I understand in previous calls, we had indicated about Rs. 700 crores of this will go to Phenolics, we have already invested close to about Rs. 400 crores in Clean Tech, so just wanted a broader bifurcation in terms of standalone Deepak Nitrite how much of this CAPEX will go, Phenolics and Clean Tech?

Sanjay Upadhyay: This is actually, Clean Tech is a vehicle, it is a 100% owned subsidiary, so all these expenses are through Clean Tech, so don't read too much into how much is going to Clean Tech and how much going here, it is all through Clean Tech only.

Rohit Nagraj: Let me rephrase the question, so out of Rs. 1,500 crores of total CAPEX, how much of CAPEX will go for backward integration and how much of it will go for capacity creation or growth?

Sanjay Upadhyay: 50-50, you can take.

Maulik Mehta: This of course does not incorporate the additional announcements that you would have seen in the presentation, which is approximately about Rs. 1,000 crores which would be over and above this and most of that would go into revenue generation.

Rohit Nagraj: And out of this Rs. 1,500 crores how much we expect to capitalize in FY23 and the rest will certainly in FY24?

Maulik Mehta: FY23 is over.

Sanjay Upadhyay: FY23 is hardly anything, I think around Rs. 70-Rs. 80 crores. Rest all will be next year.

Rohit Nagraj: So, probably some Rs. 100 crores this year and the rest of Rs. 1,400 crores will be capitalized in FY24?

Sanjay Upadhyay: Yes, FY 24 and may be beyond that also in the first quarter. Not everything is coming in FY24.

Rohit Nagraj: There could be spill over by quarter also?

Maulik Mehta: Yes, that is it.

Rohit Nagraj: And in terms of the PC compounding facility, so could you just give us a broader understanding in terms of capacities that we want to create here in the initial stage?

Maulik Mehta: As I mentioned earlier, it is world scale, so to startup within Phase-1, it will be about 35,000 tons and this will be broken up into small batch volumes and large batch volumes and all of those. So, there will be tremendous amount of flexibility from day one and as we need to grow, we do it in a phase manner.

Rohit Nagraj: And initially the PC will be imported?

Maulik Mehta: Yes.

Moderator: The next question is from the line of Tharun, an Individual Investor.

Tharun: So, regarding the recent fire, although minor which happened 3 days back for the second time in the past year, so wanted to understand what actions have been taken now to ensure that the chances of this happening reduced in the future?

Maulik Mehta: Believe me, I appreciate your concern, we are significantly concerned as well. Investigations are definitely on the way, and we are working on this. Unfortunately, at this very movement, on this call I cannot give you an answer, but we are working with an internal team, we have got an external team which is specialized in investigations, and we are working with statutory bodies on this. One thing is for certain, let us not get into whether it is minor or major, we take everything equally seriously. What I can assure you is that the actions that are around the corner will be decisive in nature and that will be the end of any such situation happening. That is the intention with which we are pursuing this.

Moderator: Thank you. Ladies and gentlemen, this was the last question for today. I would now like to hand the conference over to the management for closing comments.

Sanjay Upadhyay: Thank you all for joining this call. In case you need any further clarification, please do get in touch with our Investor Relations team. We will be happy to provide all the clarifications. Thank you once again.
