"NOCIL Limited

Q3 and 9M FY '23 Earnings Conference Call"

February 11, 2023

Disclaimer: E&OE - This transcript is edited for factual errors. In case of discrepancy, the audio recordings uploaded on the stock exchange on 11th February 2023 will prevail.

MANAGEMENT: **MR. S. R. DEO – MANAGING DIRECTOR – NOCIL LIMITED**
MR. ANAND – DEPUTY MANAGING DIRECTOR – NOCIL LIMITED
MR. P. SRINIVASAN – CHIEF FINANCIAL OFFICER – NOCIL LIMITED
SGA – INVESTOR RELATIONS ADVISOR

Moderator: Ladies and gentlemen, good day, and welcome to the NOCIL Limited Q3 and 9 months FY 2023 Earnings Conference Call. 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. Should you need assistance during the conference call, please signal an operator by pressing star then zero on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. S. R. Deo, Managing Director of NOCIL Limited. Thank you. And over to you, Mr. Deo.

S.R. Deo: Thank you. Good morning, and very warm welcome to everybody present on the call. Along with me here, I have Mr. Anand, our Deputy Managing Director; Mr. P. Srinivasan, our CFO; and SGA, our Investor Relations Advisor. Hope you all have received our Investor Presentation by now. For those who have not, you can view them on the stock exchange and company website. I hope you and your loved ones are safe and doing well.

We will begin with the business updates for Q3 FY '23. Our operating revenue was INR 326 crores for the quarter. As indicated during previous calls, the business experienced price pressures during Q3 along with volume degrowth. There is a decreasing volume in the domestic market. Our export volume remained flat despite global recessionary trends. During the quarter, our customers offtake decreased owing to the inventory accumulation at their end. However, based on 9-month performance, our domestic volume remained strong. We see that both domestic and export volume will grow in Q4 FY '23.

The Plus 1 strategy continues to be an important differentiator for NOCIL, when our customers look for security of supply chain from a medium to long-term timeframe. With strong appetite for growth, supported by robust R&D and spare manufacturing capacities, we can address our customers' needs to secure the supply chain. Based on the discussions with customers, we are quite confident that in the coming years, our export business will improve significantly from the current levels.

Now coming to the debottlenecking projects. Our debottlenecking initiatives for some of our key products is on track and will be completed during FY '24. The global economic scenario continues to be volatile, thereby impacting the ramp-up of existing capacity to optimal levels. Similarly, on the new capex front, we continue to evaluate the global economic scenario and at an appropriate time, we will take a final call on the capex. Now, I request our Deputy Managing Director, Mr. Anand, to provide an update on the industry outlook and our tyre customer end.

Anand: Thank you, Mr. Deo. A very good morning to you all. To start with, let me give you an overview of the industry. Our rubber applications, as most of you would know, is broadly classified into applications for tyre and non-tyre applications, with tyre applications taking the lion's share in most markets, including India. The non-tyre applications would include rubber applications for auto components, belts and hoses, cycle tyres and tubes, footwear, etcetera.

First, let me speak about the domestic market. NOCIL for many years continues to have a dominant position in both the tyre and non-tyre segments in India. The Indian tyre industry, by and large, has about 30% of sales going to OEMs and around 70% for the replacement market. In the last couple of quarters, while the OEM segment has been doing well, the replacement market has not shown a similar robustness leading to a mixed volume development at tyre majors, with a few showing growths in volumes and a few degrowth on quarterly basis year-on-year. There has also been some lowering of inventory levels at the domestic level. A combination of lower inventory levels and lower demand for replacement tyres has led to lower demand for rubber chemicals, thereby showing a negative volume development for the quarter on a sequential basis, but still positive growth on a YTD basis versus the previous year. As we work with our key customers on innovation, sustainability, and localization, we continue to secure our market share and are positive about increasing volumes in Q4 FY '23.

As far as international markets are concerned, as mentioned in the last quarter, we were witnessing destocking or lower stock levels in anticipation of a slowdown or the prevailing recessionary trends. This has led to some of our customers ordering less than before. The tyre market in Asia has shown better resilience compared to Europe or the Americas.

With the China Plus 1 strategy gaining further traction and to a certain extent, on account of the euro energy situation, NOCIL is in a good position to increase volumes in the export market. Our export volumes in Q3 have been at similar levels as Q2 in spite of the unfavourable market environment. We are approved at most of the key tyre plants with global customers. And as we speak, we continue to gain approval at more plants. We are positive of increasing our volumes in the coming quarters.

That is it from my side for now. I will hand over to Mr. P. Srinivasan: to give you an update on the financial performance.

P. Srinivasan: Good morning, everyone. Thank you, Mr. Deo, Mr. Anand. Hope all of you are safe and in good health. Now let me run through the financial highlights, some key parameters. The sales volume for Q3 FY '23 is 108 on index basis, taking base of Q1 FY '20 of 100. On a sequential quarterly basis, the volume registered a degrowth of 7.5%. As indicated earlier, domestic market impacted the sales volume on a sequential quarter basis.

On the revenue parameters, net revenues for Q3 FY '23 stood at INR 326 crores as compared to INR 389 crores in Q3 FY '22. Net revenue from operations for the 9 months April to December 2022 stood at INR 1,224 crores as compared to INR 1,109 crores in corresponding quarter of FY '22.

Coming to operating EBITDA parameters. Operating EBITDA for Q3 FY '23 stood at INR 37 crores as against INR 50 crores in Q3 FY '22. Operating EBITDA for 9 months FY '23 stood at INR 200 crores as against INR 172 crores in 9 months FY '22. EBITDA margin for Q3 FY '23 stood at 11.2%, a drop of 160 basis points as compared to 12.8% in Q3 FY '22.

Coming to profit before tax. PBT for Q3 FY '23 stood at INR 25 crores as compared to INR 40 crores in Q3 FY '22. PBT for 9 months December '22 stood at INR 162 crores as compared to INR 144 crores in 9 months December '21.

On profit after tax parameters, the PAT for Q3 FY '23 stood at INR 19 crores as compared to INR 30 crores in Q3 FY '22. For 9 months December '22, it stood at INR 120 crores PAT as compared to INR 107 crores for the corresponding period 9 months of previous year.

With this, we would like to open the floor for questions-and-answers.

Moderator: The first question is from the line of Damodaran from Acuitas Capital.

Damodaran: Yes. So the first question is, I mean, if I look at your PPT, you have mentioned that the rubber industry was essentially flat for calendar year '22. Whereas if I look at our volumes, they were sort of down 7%. And while the split is not available, but I'm presuming most of this decline is attributable to exports. So it seems we have lost market share, and this is sort of counterintuitive to the China Plus 1 narrative that we've been hearing. So especially given the challenges that China has faced in the last one year, I mean, with COVID and everything.

So just wanted to get your thoughts on that. I mean, how do you reconcile this? And a related question is, I mean, on the guidance front, can you give any guidance about growth relative to the industry's growth? I mean, if industry is growing at X percent, what typically do you internally look at to grow? I mean, is it X plus 2% or any such guidance that you can give? That's it. Yes, those two questions from my side.

Anand: Yes. So, let me first speak about the export markets and your comment about market share. So like we said already, when we look at the export markets, clearly, our volumes are more in relation to also where customer demand has gone down. We don't see an indication of loss of any market share in the export markets. Clearly, there's been destocking in the marketplace. And overall, there is a sentiment of lower demand expected in the coming quarters. But that's the kind of sentiment that's played out, but not any loss in market share in the export markets.

Another observation is that we are also present in the latex market, and that is a part of Southeast Asia and Malaysia, where there has been a significant drop in the rubber gloves market. And having presence in that market, that's also reflected in the export numbers. So if you really look at it, it's a combination of tyre destocking as well as the latex market taking a nosedive since the COVID abated. Your second -- your other part of the question, can you just repeat that, Mr. Damodaran?

Damodaran: Yes, sir. Sure. So with respect to any guidance you can give with respect to your growth relative to the industry's growth, how do you look at that? I mean, if industry were to grow at X, how would you look at your growth? I mean, should it be X plus 2% or X plus 5% or any such guidance that you can give?

Anand: Yes. So like we have stated in the past, again, it's a correlation to our market share in the market. So if you look at the domestic market, where we have a dominant share, we look to grow above market growth rates at least a couple of percentage points. Whereas international markets, I think that would not be the metric. We would look to grow significantly, like you said, X, but difficult to put a number to it because we have a low market share in the export market.

Damodaran: Sure. Sure. Okay. And just one last question from my side. If you can give out, I mean, what was the growth in export and domestic volumes over nine months?

Anand: So, I think if you look at the growth in the domestic market, we have 7% to 8% growth year-to-date, I mean the domestic market. The export markets, we have not seen growth. So, that's why we say -- YTD, there is no growth. It's only from a quarter-to-quarter that we see it's flat.

P. Srinivasan: Just to add a bit, this is Srinivasan here. In export market, as Mr. Anand just referred to, the latex market degrowing. If you see the latex market rubber consumption growth parameters, it's degrown by 25%. So, that is impacting the latex product. So therefore, our export has a latex share, and that share has significantly come down. That's where we have lost lots of business as compared to other traditional rubber chemicals market.

Anand: So I think, again, to clarify, that's more a market degrowth that's kind of playing out. Yes.

Damodaran: Sure. And any specific number that you can give? I mean, how much does latex account for in your overall exports?

Anand: 25%, yes.

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

Rohit Nagraj: Sir, first question is in terms of the tyre capacities which are getting added in the Indian context. So, I believe in the next two years, three years, there will be significant capacity addition which is happening. How are we placed in terms of product validations? Because I understand that we've been telling there are four different parameters in terms of product validation and that puts us competition at bay. So where are we for those newer tyre capacities in terms of our product qualifications or validations? Thank you.

Anand: So as far as the domestic markets are concerned, again, qualifications and this is also applicable for export markets. Where it's an expansion in an existing plant, there is no new qualification process. I think it's only when it's a new plant, where you really have a qualification process. But typically, like we have mentioned, which we are already present with the rubber plants, then this process is kind of fast tracked. So it's much lesser. It's not the usual six months to one year, but it's kind of well-timed with, as and when those capacities are coming on stream.

Rohit Nagraj: Right. Sir, second question is, Srini sir, if you can give the absolute number of exports during first nine months in terms of revenues and a similar number for last year?

Anand: Yes. Just a second, please. He is just getting it.

Rohit Nagraj: Sure, sure.

P. Srinivasan: The absolute number last year for nine months is about INR 400 crores exports. This year, we are at INR 350 crores.

Rohit Nagraj: Right. Got it, sir. Sir, one more question. In terms of sequentially, the costs have come down. So, this is primarily because of the variable cost regarding our volumes, the opex?

P. Srinivasan: It's a combination of some volume level of operations, as well as some price improvements in certain key raw materials.

Moderator: The next question is from the line of Dhwanil Desai from Turtle Capital.

Dhwanil Desai: Sir, I think in your presentation, you have mentioned that you expect volumes in Q4 to improve sequentially. So are we expecting that to reach Q2 level or surpass that level? Any quantification around that?

Anand: So, that would be -- we do see an improvement over quarter three, but difficult to put a finger to say whether it will be a Q2 or better. Yes. So, obviously, I think, definitely, there is an improvement that's expected there.

P. Srinivasan: I think if you are looking at 117, maybe we are nearing that or better than that.

Dhwanil Desai: Okay. Got it. Second question, sir, if you can comment on the realization side. I mean, you mentioned that it has been coming down. So how do you see this from here? And on the value addition part, do we expect that to reach 49%, 50% as we were targeting in couple of quarters, or do you think that's slightly far away?

P. Srinivasan: To answer this question, I think we have been trying to understand the price regime. So what we are looking is at the absolute value addition per kg or EBITDA per kg is what we are focusing on rather than getting into the percentage business, because ultimately, the base level, which we are comparing on a particular period, A and particular period B, the base level may change. So therefore, you have to look at an absolute EBITDA per kg is what we are focusing on.

What we have been giving guidance that always look at an average performance for a year rather than getting into quarterly performances. So by and large, we see for FY '23, the full year, around the same level for FY '22 average, just around that level adjusted for volumes.

Dhwanil Desai: Okay. And FY '24, do we expect to remain at FY '23 level or how do you look at it?

Anand: Yes. So, again, given the environment on how the prices have operated, I think we've kind of seen a good position in quarter one of this year and quarter four of the previous year. So difficult to put, but at least we would imagine that it should be at a stable level going into the next year at this point in time.

Dhwanil Desai: Okay. And sir, any take on the value addition part?

P. Srinivasan: I think we actually answered the question that we are focusing on more EBITDA per kg getting into specific value addition because, ultimately, we have to look at the total cost of operations rather than getting into segment wise. So, we prefer to look at EBITDA per kg as a driving point.

Anand: At the same time, we expect volumes to be better. Yes.

Moderator: Next question is from the line of Ravi Mehta: from Deep Financial.

Ravi Mehta: Yes. My question was more pertaining to the realization that you guided last quarter that you are seeing pressure and it's visible in the Q3 numbers. I just wanted to get some sense how is this scenario panning out with the whole China opening that we are hearing? What kind of a realization pressure or the dumping stress that you're anticipating? Is it playing out? It's better than what you thought or some color on that?

Anand: Yes. So when we look at this situation with China opening up, we do see the trading margins to be at similar levels. And also, I think there are lot of other variables playing out in terms of demand increase in the downstream industries for some of the chemicals, raw materials. So it's a pretty dynamic situation, but our expectation is at least the trade margins will hold here.

Ravi Mehta: And probably, the mix because of the latex market degrowing, that is impacting our realizations more in this quarter vis-a-vis a normal price pressure in the overall rubber market. Is that a fair understanding?

Anand: Yes. So the latex market is not the major contributor. It's overall price development that's moved downwards here.

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

Rohit Nagraj: Sir, any understanding on the new products, which are currently under development. So, we've been saying on this in the last couple of years. Any progress on that front and visibility in terms of when those products can be commercialized?

Anand: Yes. So the new products, we are talking about are some localization products, which are already at approval stages at most of our customers. We expect business to begin sometime in quarter one of the coming financial year quarters one, quarter two of the next financial year. While there is more work in the pipeline, but still in the testing phase, Mr. Nagraj.

Rohit Nagraj: And these would be apart from the auto segment, I mean, the catering segment would be different than autos, right?

Anand: See, largely, we still have critical volumes from the tyre. It will be largely in the tyre applications, which can then always be cross-pollinated into other rubber applications.

Ravi Mehta: Right. Right. Got it. And the recent volume in terms of the inventory destocking that we have experienced in the global market, so is it also a function of Chinese volumes being higher in the previous period and those now have been, the destocking is because of that sense? Or probably because of the supply chain issues due to war kind of situation, the tyre companies had stocked up significantly.

Anand: No. So we were talking about destocking in the international markets, and that was more on account of the overall sentiment of the recession. And that's what actually played also with the customer. So when you speak to them, they do tell you that they want to keep inventories low, foreseeing lesser demand. But I expect that, that's kind of flattening out now.

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

Chandragupta Acharya: Sir, I just have one question about the export market specifically and all this talk about China Plus 1 that has been going on almost for a couple of years now. So can you share some information on how many new customers or new plant locations we would have added in the last couple of years as a result of this shift to India China Plus 1 phenomena? Anything you can share?

Anand: Yes. Okay. Your voice broke a bit but let me try and respond in case I've not, please do kind of repeat your question in case I've not answered. Let me try. So basically, like we mentioned, as far as global customers are concerned, we are actually present with most of the customers, and we have approvals with most of the customers. It's about expanding from one plant to another.

And what we have seen is there is traction that's gaining traction about the intent on this China Plus 1, on the back of China Plus 1 to approvals at more plants. And that means that gives us the opportunity to start selling into those plants from one gate to another. So that's what is happening. So it's not necessarily, so since we're already present with most of the tyre companies, it's not that we are adding a new tyre company in the last few months. We are present with them. It's about now expanding into more number of plants. That's how it's working. Yes.

Chandragupta Acharya: Okay. But, I mean, is the number substantial? Or can you put some number or at least qualitatively, you can share, is it very high or very lower, something of that kind? And how do we know, I mean you mentioned that right now, there is a slowdown of demand in the European market and all. But assuming that the situation improves, then what gives you the confidence that our volumes will also improve correspondingly. So, I'm looking for something from that point of view actually.

Anand: So, we expect that with NOCIL's position, the increase in volumes will come from replacing current business of competition. So, that's potentially something that we expect. And while I am not able to give you a specific figure to this, but clearly, we are talking about large companies which are out in the international market.

Moderator: The next question is from the line of Iinder Ji Morya from Anvil Research.

Iinder Ji Morya: Sir, I have two questions to ask. So, one is on the conversion cost. So when we analyse the volumes and convert it into per kg basis, I think, on a sequential basis, we are on the similar levels to what we were in Q2. So if you can just help us, explain like in between the conversion costs, do we see some sort of benefits coming towards us predominantly in terms of, let's say, freight costs or power costs?

And from NOCIL's point of view, how do we see our conversion cost going forward? So one is the operating leverage benefit, which will come definitely when our volumes would improve. But from, internally, what we may be working on to reduce our conversion cost, if you can walk us through, that would be helpful, sir.

P. Srinivasan: Gentleman, if you see the other expenses of the financials, which we just published yesterday, released yesterday, there is a reduction of INR 10 crores thereabout in absolute terms. From Q2 INR 100 crores, it has come down to something like INR 91 crores. It consists of utilities and other fixed costs. Obviously, utilities, we will make an effort to improve further or optimize definitely as we go along. And as we improve the volumes, operating rates, definitely, some optimism, if it is definitely in the offering. I think generally, it goes with the inflationary trends. So once the volume increases significantly, I think those fixed costs despite being inflationary pressures within, but I think the optimization benefit definitely, you can get something out of it.

Iinder Ji Morya: Correct. But sir, when we see our power costs, so last year, predominantly the cost increases were significant when we compare the FY '21. And in the nine months also, those power costs were elevated. But have you seen some signs of improvement in Q3 where our per kg cost for power despite of lower volumes have seen some sort of improvement?

P. Srinivasan: The power rates have not seen any change. It is still flattish or marginal movement here and there. We are not seeing any breathing. What we are looking at is whether we can improve on efficiency as we ramp up the capacities.

Iinder Ji Morya: Correct. Sir, second question is on what Mr. Anand alluded in the previous remarks that we have been working on some new products where the volumes or some initial volumes would be start coming to us from Q1 and Q2 of FY '24. So if you can just help us, explain that what could be the opportunity size for those sorts of volumes in India? And is there a market for the export also for those new products, which we are currently working on? And are those products having more realization than our existing basket of products? So if you can just help us.

Anand: The products actually has scope, both in the domestic and in the international markets. They are part of our accelerator product line. And accelerators per se are much lower volumes in terms of consumption in the rubber compounding. So, we don't expect any significant jump in volumes, but the opportunity is there, both in the domestic and international markets. I would say from a margin point of view, similar to our existing portfolio. Yes.

Iinder Ji Morya: Correct. But let's say, out of our total rubber chemical size of, let's say, 11 lakh tons globally, how much this -- so let's say, 35%, 40% would be accelerators, if I'm right. So out of those accelerator basket of products, how much this would be? So could it be to an extent of 15,000 tons, 20,000 tons of volumes globally for these products, which we are currently under working stage?

Anand: Yes. It will be lesser than that. These are more niche accelerators. It would be much smaller.

Iinder Ji Morya: Okay. Okay. Sir, last question is on you touched upon on the export side also. So on your opening remarks, we mentioned that we expect a significant improvement in our export volumes. So if you can just slightly elaborate more like where we are currently? So those approvals which needed from all the tyre customers globally and from various plants of those tyre companies globally, have we gone through for most of our validations from the customers? Or we still have to receive some of the approvals before, which, those volumes should start seeing the improvement once the destocking and everything is over.

Anand: Yes. So it's not kind of start-stop kind of situation. It's all at different stages. So, we have already approved in the last four months to six months in additional number of plants. There are quite a few already in advanced stages. Some of them are in close to completion again. So it's all at different stages. And again, from customer to customer, depending on the number of plants and where they would like us to be present. That's where we are playing. So, I would say it's on a fast track but at different stages. Yes.

Iinder Ji Morya: Correct. And sir, just a last bit of understanding on the export volumes. So let's say, whenever we will exhaust our full volumes from now to whatever the timeline, which it could happen, what would be the mix of those export volumes? Let's say, if we are here to improve our volumes by, let's say, 30,000 tons, 40,000 tons hypothetically. So what could be the mix of those domestic volumes as well as the export volumes in terms of incremental volumes, which will be coming to NOCIL?

Anand: Yes. So when you look at incremental volumes, we do see that a major share will be coming in from the exports, like we had mentioned in the earlier address.

P. Srinivasan: Overall, we will be looking at exports 40% on the peak capacity levels of our overall revenue parameters. So the overall business.

Iinder Ji Morya: Okay. So, this you are talking on volume side, correct?

P. Srinivasan: Yes, volume and value.

Anand: 40%.

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

Rohit Nagraj: Yes. Sir, in terms of RM imports currently, how much is the percentage? And which and all are the key products that we import? Sorry, raw materials, not products. Sorry.

S.R. Deo: So, Rohit, I think we are changing our strategy in terms of raw material procurement. I will not be able to give you a percentage, but I think the objective is to shift more in terms of local purchasing. And I would say we have very successfully done it in key raw materials. And the endeavour will be to develop more and more local suppliers.

Rohit Nagraj: Right, right. Actually, Deo sir, I was going to come on that itself that whether the suppliers are actually going in for those import substitute products in terms of raising their volumes. So, we can be catered from the domestic market instead of relying on the imports incrementally. So, this is a good sign.

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

Chandragupta Acharya: Yes. One question. Can you share what is the cash position now as of 31st December? And given that we have no more major capex in the offing, is there any plan to increase the cash pay-out, sir?

P. Srinivasan: Gentlemen, we can give as of 30th September. The cash is about maybe INR 150 crores.

Chandragupta Acharya: That is 30th September, not December, right?

P. Srinivasan: December, we are not allowed to publish. So, we have given as of September, which is at INR 150 crores.

Chandragupta Acharya: Okay. Okay. And any plan to increase the pay out? What is the future plan for utilization?

P. Srinivasan: We are working on that. Some evaluation plans are being worked out. At a suitable time whenever we finalize, we'll get back to you on the capex front.

Moderator: As there are no further questions, I would now like to hand the conference over to Mr. Deo for closing comments.

S.R. Deo: Thank you. I take this opportunity to thank everyone for joining the call. I hope we have been able to address all your queries. For any further information, kindly get in touch with me or Strategic Growth Advisors, our Investor Relations Advisor. Request all of you to be safe under given circumstances. Thank you very much.

Moderator: Thank you. On behalf of NOCIL Limited, that concludes this conference. Thank you for joining us, and you may now disconnect your lines.