

# “Rain Industries Q4 FY14 Earnings Conference Call”

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**Moderator:** Ladies and gentlemen, good evening and welcome to Rain Industries Q4 FY14 Earnings Conference Call hosted by Prabhudas Lilladher Private 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. Should you need assistance during the conference call, please signal an operator by pressing “\*” then “0” on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Kamlesh Bagmar. Thank you and over to you sir.

**Kamlesh Bagmar:** Good Evening everyone. I welcome all the participants to the 4th Quarter 2014 Conference Call of Rain Industries Limited. We have with us Mr. Jagan Mohan Reddy, Managing Director of Rain Industries Limited, Mr. Srinivasa Rao, Chief Financial Officer of Rain Industries Limited, Mr. Gerard Sweeney, President and CEO of Rain CII Carbon LLC, USA and Mr. Henri Steinmetz, President and CEO of RÜTGERS Group.

We commence the call with opening remarks from Mr. Jagan Reddy providing an update on recent developments at Rain Group. He will then be followed by Mr. Srinivasa Rao providing you the highlights of the financial performance during Q4 2014. Mr. Sweeney will provide an outlook for the CPC business and Mr. Steinmetz will provide outlook for other Carbon products and Chemical businesses. This will be followed by question and answer session where the management will answer the questions from the participants.

Before we begin I would like to mention that some of the statements made in today’s discussion may be forward looking in nature that could be affected by certain risks and uncertainties. The Company’s actual results could differ materially from such forward-looking statements. I would now request Mr. Jagan Reddy to provide an update on the key developments in Rain Group.

**Jagan Mohan Reddy:** Thank you Kamlesh. Good evening everyone and welcome to our 2014 Fourth Quarter earnings call.

I would like to start my discussion with a brief update on the key developments of the Group.

- 2014 has been a challenging year and in specific the 4th quarter has been hugely impacted due to various macro-economic factors including prolonged weakness in primary Aluminum metal prices, falling commodity and oil prices, subdued end markets, falling interest rates in Europe and adverse currency movements that impacted the performance of the Company. For the Fourth quarter RAIN has achieved Consolidated Revenue of Rs. 25.90 Billion; Consolidated Operating Profit of Rs. 1.58 Billion; and Consolidated Net Loss of Rs. 2.00 Billion.
- The Consolidated Net Profit on a sequential basis decreased by 273% from Rs. 1.15 Billion in Q3 2014. Although we have seen some recovery in our Cement business, in the 4th quarter, the lower operating margins from Carbon and Chemical businesses has resulted in an operating loss during the quarter that has been further impacted by some exceptional

items. If we adjust the Net Loss with those exceptional items, the Adjusted Net Loss for the quarter will be Rs. 321 million.

- As expected, we have seen some recovery in Cement business during the current quarter in-line with the 3rd quarter. On a sequential basis, there is only a marginal decline of 1% in Cement sales volume in spite of normal seasonal factors. With Cement blended realization remaining stable at Rs. 227 per bag, operating profit of Cement business improved from Rs. 206 Million in Q3 2014 to Rs. 284 Million in Q4 2014 due to the reduction in operating costs. The EBITDA has increased from Rs. 402 per ton in Q3 2014 to 562 per ton in Q4 2014.
- With the formation of new States of Telangana and residual State of Andhra Pradesh, we expect the demand to pick up and utilization to improve on the back of fresh demand for housing, urban and infrastructure development from the new states.
- Due to the weaker market conditions and falling commodity prices, the performance was impacted in our Carbon and Chemicals business. My colleagues Gerry and Henri will take you through the factors that impacted our performance in Carbon and Chemical businesses.
- To give you an update on strategic developments, we have successfully completed the PA expansion project in Belgium on time and within the budget. The commercial production at this facility commenced on 6th October 2014 and the plant has achieved its rated capacity and quality.
- With regard to Russian project, detailed engineering has been finalized, all key equipment reached the construction site and construction is in progress. We still expect to commence operation in 2nd half of 2015. Due to 46% fall in Russian Ruble against US Dollar during the quarter ended December 31, 2014; the Company has incurred an aggregate loss of Rs. 521 million (including exchange loss of Rs. 181 million attributable to Joint Venture Partner) in restating loans and other liabilities denominated in US Dollar borrowed for incurring the Capital Expenditure for the Project. The long-term viability of the Russian Tar Distillation Plant was not impacted due to devaluation of Russian Ruble, as majority of the product would be sold in prices denominated either in US Dollars or in Euros.
- With regard to proposed new Solar Power Plant in Dharmavaram, Anantapur District, Andhra Pradesh, we executed Power Purchase Agreement with Southern Power Distribution Company of Andhra Pradesh Limited ("APSPDCL") to supply power generated from such Solar Power Plant for next 25 years at a fixed tariff of INR 5.89 per kWh plus an annual escalation of 3% for first ten years. RCL is in the process of acquiring land in Dharmavaram, finalizing the equipment suppliers and initiating other project construction activities. The Solar Power Plant is expected to commence operations in Second-half of CY 2015.
- As you may be aware, during October 2014, Hudhud cyclone had hit North coastal of Andhra Pradesh. However, due to the pre-emptive steps taken by the Company, Hudhud did not cause any material damage to the manufacturing facilities of Rain CII Carbon (Vizag) Limited ("RCCVL") (a Wholly Owned Subsidiary of the Company) situated at Visakhapatnam. The cyclone resulted in temporary stoppage of operations at this facility.

- Post completion of required repair activities and technical evaluation, RCCVL had restarted first Kiln on October 26, 2014 and second Kiln on November 5, 2014. RCCVL lodged claims against Insurance Companies for loss of property and inventories and such claims are partially settled during December 2014 quarter and the balance claims would be settled by end of March 2015.
- Our capex spending for the year 2014 was approximately US\$ 61 Million that is about \$33 below our budget due to the delay in the Russian project.
- Most importantly, I am happy with the Free Cash flow generation during the current year, with the normalization in working capital and delay in Russian joint venture, we have generated a strong free cash flow of US\$ 65 Million for the year ended December 31, 2014.

I would now request Srinivas to provide highlights of the financial performance during Q4 2014.

**Srinivasa Rao:**

Thank you and a warm welcome to all the participants.

To highlight some of the key performance indicators, on a consolidated basis:

- Consolidated Net Revenue is INR 25,899 million during the current quarter, a fall of 10% compared to INR 28,812 million during Q4 2013.
- Carbon product sales volume during the current quarter is 808 thousand tons, which is a marginal increase of 3% compared to 782 thousand tons in Q4 2013. Carbon sales volume increased during current quarter mainly due to higher Pitch sales and an increase in Pet Coke trading volume, which was partly offset by lower CPC sales in the United States. While carbon sales volume has increased by 3%, due to a fall in blended realization, lower Pet Coke trading sales (on CIF terms) and depreciation of Euro during the quarter, the Carbon division revenue has reduced by 12% in Q4 2014; as compared to Q4 2013.
- Chemicals sales volume during the current quarter is 83 thousand tons, an increase of 24% compared to 67 thousand tons in Q4 2013. While Chemical sale volumes have increased by 24%, due to fall in realization, change in product mix and depreciation of the Euro, Revenue from Chemical business has reduced by 13% in Q4 2014; as compared to Q4 2013.
- Cement sales volume during the current quarter is 506 thousand tons, an increase of 8% compared to 470 thousand tons in Q4 2013. With the combination of increase in sales volume by 8% and increase in average realization from INR 211 per bag in Q4 2013 to INR 227 per bag in Q4 2014, Cement revenues increased by 16% in Q4 2014; as compared to Q4 2013.
- Consolidated Adjusted Operating Profit for the current quarter is INR 1,577 million a decrease of 56% compared to INR 3,621 million achieved during Q4 2013. While the Cement division has delivered a strong recovery of 59% growth in operating profit and this was offset by lower operating performance in the Carbon and Chemical business as a result of change in product mix and lower margins in the Resins business. In addition the

operating profit of the Carbon and Chemical business in Q4 2013 was positively impacted by an environmental claim income of INR 1,007 million.

- Exceptional items during the quarter include:
  - o incremental pension liability from actuarial losses (due to significant fall in interest rates in Europe) of Rs. 1,820 Million,
  - o Inventory write down resulting from fall in net realizable value, due to abnormal decline in prices of inputs amounting to Rs. 237 Million,
  - o Russian ruble currency depreciation impact of Rs. 338 Million,
  - o Impairment loss in Carbon Business due to management's decision to shut-down CPC plant in China with effect from January 1, 2015 of Rs. 56 million;
  - o impairment of licenses in Chemical Business in Netherlands of Rs. 39 million; and
  - o net tax impact on all these items of Rs. 814 Million.
- During Q4 2014, the Company had a foreign exchange loss of INR 115 million, as compared to a foreign exchange loss of INR 135 million in Q4 2013. The loss in Q4 2014 is mainly due to loss on derivative contracts entered in Germany for hedging US dollar denominated receivables and due to depreciation of the Rupee against the US dollar.
- Finance cost during the current quarter is INR 1,482 million, a decrease of 4% compared to INR 1,551 million during Q4 2013. The fall in finance cost is mainly due to translation impact of foreign currency interest cost and marginal decline in debt.
- Considering the expected improvement in performance during subsequent periods, the Company recognized Deferred Tax Benefit of INR 950 Million on business losses eligible for carry-forward. Further, the Company has also recognized MAT Credit INR 25 Million, and reversed deferred tax liability of INR 223 Million, which is no longer required.
- Consolidated reported net loss during the current quarter is INR 1,997 million compared to consolidated reported net profit of INR 472 million during Q4 2013. However the adjusted net loss (after exceptional items) for the current quarter is INR 321 million. The Company achieved a consolidated negative EPS of INR 5.94 and adjusted negative EPS of INR 0.96 during the current quarter, as compared to consolidated EPS of INR 1.41 and adjusted EPS of INR 3.86 during Q4 2013 respectively.
- The Consolidated Free Cash Flows for the year ended December 31, 2014 is US\$ 65 million; after spending capital expenditure of US\$ 61 million and incurring cash interest cost of US\$ 113 million during the year.
- As at December 31, 2014, the Company has consolidated debt of US\$ 1,211 million (including working capital debt of US\$ 54 million) and Cash and Cash Equivalents of US\$ 145 million. The net debt as at the same date is US\$ 1,066 million.
- With the improvement in the liquidity coupled with undrawn revolver facilities of about US\$ 220 million, the Company is well placed to meet debt servicing obligations and capex projects in pipe line. The major debt repayments are scheduled to start only from CY 2018.

I would now like to hand over the call to Mr. Gerry Sweeney to provide outlook of carbon business... over to you Gerry.

**Gerard Sweeney:**

Thank you Srinivas, and good evening everyone. It's a pleasure to speak with you again.

Market Outlook:

- After a series of positive movements during November, which found LME primary aluminum prices rallying over \$2,100 per ton, the market has retreated toward \$1,800 MT on global instability fears due to precipitously falling crude oil prices and the resultant currency devaluations. Aluminum, like most commodities, has been hit hard by this instability in the markets.
- While the fundamentals of the industry remain in good form with orders and consumption up globally in every major end use category, the current economic concerns over Europe and China continue to hang over the market. Adding to the positive factors, regional premiums remain strong and LME global inventory levels have now dropped below 4 MM MT, a more than 1.5 MM, or roughly 27% drop from late 2013. Amid deficit metal production levels outside China, regional premiums are expected to remain relatively strong in 2015.
- In the short term, we do not foresee dramatic improvement for LME aluminum prices, until the world sorts out these looming energy, political and currency issues. Given the large scale premiums paid to producers, they appear to be netting a very reasonable return for their production. This has also played on in recent earnings reports of producers. Judging by the aforementioned industry fundamentals, we see little likelihood of further curtailments or delays to contemplated capacity additions, and have not had any such suggestions from producers to this point. The only concerns we have regarding the aluminum marketplace itself right now is the inventory surpluses we are seeing in China, and how they will deal with this if the country does not grow as expected going forward. We will be watching this closely going forward.
- Although disappointed with the aluminum market developments in the fourth quarter, we see the western aluminum production and inventories continue moving in a positive direction. Due to market sentiment, our prices remain under pressure for the first half 2015. We experienced a US\$ 20 per ton drop in our average CPC realization in second half 2014. This represented a combination of continued market pressure, and some price concession due to a loosening of specification with some key customers. We were mostly able to offset these price reductions through our raw material cost to sustain our average margin level. We expect margins to further improve starting second half 2015.
- The fall in crude prices will likely push refineries in the US to move from the Shale oil back toward indigenous light crudes, which would enhance the availability of high quality GPC in 2015. This would be a positive development for our US CPC business. Also, lower ocean freights due to lower fuel costs will have a positive impact on the US and Indian CPC businesses.

- From an operational perspective for the period, leaving the brief Hudhud outage aside, our Indian Calcining facility is operating at or near the maximum capacity and our US plants are running at approx. 80% utilization levels.
- Considering new environmental regulations which would require additional investment in the CPC plant in China; the Company was forced to shut-down its 20,000 tons capacity per annum plant during January 2015. The Company will continue to operate its representative offices in China which assists in the procurement of raw materials in country.
- As informed in the last call, we have resolved most issues in our Lake Charles energy project, this project has started contributing more fully from the month of August and we continue to optimize its operations. We are expecting a substantial improvement in energy revenue contribution from Lake Charles during 2015.
- Our commercial efforts to achieve flexibility in specifications from the smelters to control our input costs and to improve margins has greatly helped us protect margins during this prolonged downturn.

Now I would like to hand over the call to my colleague Mr. Henri Steinmetz to discuss the Ruetgers business... Henri....

**Henri Steinmetz:**

Thank you Gerry. It gives me immense pleasure to address you all once again.

First I would like to share with you recent market trends.

- In Q4 the market was facing a significant drop in commodity prices as well as a strengthening of the US Dollar against the EUR. The Fuel Oil price dropped from 554 USD/t to 317 USD/t, the benzene notations dropped from 1,322 USD/t to 745 USD/t by the end of December, while the USD appreciated against the EUR from 1.27 USD/EUR to 1.22 USD/EUR. The Ukraine crisis as well as the sanctions against Russia combined with the lower oil prices led to a significant drop of the Russian Ruble against the major currencies. Following the significant reduction of steel production we saw a significant reduction of coal tar and pitch supply coming from Ukraine which strengthened our market position with long term supply agreements for tar. Economical growth in Q4 in our major market the Atlantic region was good and so we saw also a good demand for our products.
- Given the strengthening of the USD against the EUR the competitiveness of our products especially compared to China and the USA will increase and should have a positive impact on demand and margins going forward.
- The economical trend was reflected in our business. In Q4 we saw an increase in production and sales volume for the Carbon business (Prod.: +36% Sales: +6,3%) as well as for the Chemical business (Prod: + 24%, Sales: 24%) YoY. While comparing Q4 2014 against Q3 2014 we have seen the typical seasonality with slightly lower production volumes for the chemical business while the volume for the Carbon business was flat.

- Driven by lower quotations – especially the lower oil and benzene quotations - revenue were despite the strong volume growth down for the Carbon business by 11% year on year while on sequential basis revenue declined by 20%. The active portfolio management towards higher valued products and the development of advanced applications compensated the price pressure on our other oil products.
- The Chemical business faced YoY lower revenue of 13% driven by lower quotations. On a sequential basis the revenue declined by 16% driven by seasonality and lower trading sales. The profitability of the Chemical business was down. Inventory revaluation, seasonality and an unfavorable product mix contributed to the declining profitability. As already mentioned in our last call we have seen in Europe following the summer shut downs a change in the feedstock of the crackers towards lighter fractions resulting in lower production yields which we are currently addressing by adjusting the supply and production processes. Positive results out of these measurements we expect already for the beginning of 2015.
- Further to add my views on the Oil prices, in addition to those shared by Mr. Sweeney, in long term we are having natural hedge on oil prices, as around 290 thousand tons of our sales are linked to the Oil prices and around 260 thousand tons of raw-materials (Coal Tar and other input materials) are directly linked to the Oil prices as well as our energy and logistics costs. The initiatives taken by the company to move product mix more towards sale of Creosote Oils, which is much less sensitive to oil prices, had helped to reduce the exposure to Oil prices. Overall the exposure of Group to Oil prices is limited and would not have material impact on performance in the long-term either way.
- As informed by Mr. Jagan, we have successfully commissioned our PA project on time and within the budget. The full benefit of the project can be seen in CY 2015.
- For the Russian project we had faced technical issues for some of the already existing structure causing a delay of the project to the second half of 2015. As already indicated by Mr. Jagan we do not expect any major cost overrun by this delay.

Thank you. I would like to open the meeting up for the Question and Answer session. Over to you Operator

**Moderator:** Thank you very much. We will now begin the question-and-answer session. Our first question is from the line of Uma Maheshwari from Centrum Wealth Management. Please go ahead.

**Uma Maheshwari:** How are we looking for the next quarters coming in, I think this quarter happens to be a very challenging quarter compared to the previous one, are we looking at a turnaround happening for the next one or two quarters with international markets stabilizing?

**Srinivasa Rao:** I think as Mr. Gerard Sweeney and Mr. Henri Steinmetz has mentioned to you, whatever impact we are seeing in last quarter of 2014 we do not expect them to repeat for long period, maybe from mid of 2015 onwards we should see an improvement in the performance.



- Uma Maheshwari:** Okay. So this would be almost for about two quarters the markets, the price of the share could still be in a subdued manner then?
- Jagan Mohan Reddy:** We expect the first half to be a little softer but it however it should be still better than the fourth quarter but it should be softer, we expect to see only a gradual rise from the second half 2015.
- Moderator:** Thank you. Our next question is from the line of Achal Lohade from JM Financial. Please go ahead.
- Achal Lohade:** If I look at the raw material to sales it is pretty stable at 58%, now there are issues of product mix, the pricing etc, the raw material side, can you help us understand how are you looking at the gross margins going forward which were like if I look at RM to sales it is about 58% so it means a gross margins of about 42% - 43% what we have seen for past three quarters as well as last year same time. How are we looking at going forward, would there be further compression in first and second quarter of 2015?
- Srinivasa Rao:** Achal actually as indicated in the press release the performance in December 2014 quarter is impacted by the fall in the commodity prices and we expect that there will be a recovery going forward even like Mr. Jagan mentioned first quarter of 2015 also we expect it to be better than what we have seen in December 2014 quarter.
- Achal Lohade:** Right. No, I was just checking about the gross margin side, one part I also wanted to ask is about the inventory write down, you have mentioned in the press release that the overall impact is about EUR8 million...
- Srinivasa Rao:** Yes, but the 5 million is already consumed during the last quarter and 3 million is what we carried forward from December 2014 to March 2015.
- Achal Lohade:** Right. Have the prices further reduced, would there be any revaluation of that inventory upward?
- Srinivasa Rao:** You see that there is some recovery happening in the commodity prices now, so that should ensure that our margins might improve.
- Achal Lohade:** Right. Specifically on the CPC business, are we looking at the similar volume, what was the volume if you could elaborate a little bit for the full year and how are you looking at the volume for current year?
- Gerard Sweeney:** Yes. Year-over-year 2014 to 2015 from the CPC business perspective we are looking at substantially same volume.
- Achal Lohade:** Right. And how about the margins, could you really talk a little bit about the CPC prices currently because it seems if I look at the realizations I mean it is a combination of the CTP as well as CPC but it seems to have dropped quite a bit actually, not only YoY but also sequentially by almost \$50. Can you please elaborate a little bit on the CPC part sir?

- Gerard Sweeney:** Yes, as far as Anode Grade CPC, the Anode grade CPC price remains under some pressure just because the market sentiment is rather negative with the repeated drop of the LME price. So we are getting some push on that although we are resisting on it, but I don't believe we will see substantial erosion in the price going forward and as I mentioned earlier we really do expect that it will be flat, slightly down in prices for the first half on CPC and then in the second half of the year we really do expect with the falling LME inventories and the general conditions in the marketplace from the demand perspective that we should have an opportunity to improve margin in the second half of the year. From 2014 that was absolutely a challenging year for us as far as battling a very depressed market and with no ability to really push back. However, that is on the pricing side, from a cost perspective we were able to push down our overall raw material price exposure through a combination of price reductions as well as specification change which allowed us to essentially protect our margins in a falling market. But I really do believe that for 2015 there is not a tremendous amount of momentum for further price reductions.
- Achal Lohade:** If I look at the oil price it has fallen quite substantially, haven't you seen a similar kind of call in the GPC price as well, how are the GPC prices flat or only slightly lower impacting our margins?
- Gerard Sweeney:** There is no correlation between GPC price and the price of oil, so when oil price was up they did not escalate in correlation with that and likewise with the crude oil price down they did not fall. Unlike our chemicals business we are not tied to that from the GPC perspective, it is strictly its own supply and demand economics. But going forward from the GPC side we are seeing in 2014 some of the difficulty in reducing our GPC costs more significantly was the fact that we were bumping up against the low level of pricing because of the few markets. The fuel coke markets were high enough in value where we could not continue to push our prices down for the sake of running into it. But those markets have now come off, they are moving off in the first quarter and that should provide more opportunity for us to push down our GPC cost as we go through the year that has really been something that has been coming off in January and February.
- Achal Lohade:** Any color on, sorry I am actually asking a little bit more in detail about this part, because of the fall in the crude has the availability of good quality GPC also reduced?
- Gerard Sweeney:** No, there has been no impact to the availability of GPC related to the fall in crude oil prices. To this point we have not seen any impact from the US to China on refining capacity and the production of any GPC. We are more likely to see an impact if the union strikes continue in the US we could see an impact on production, but nothing related to oil price.
- Achal Lohade:** Right. Just one more question on the basically the pension liability part, at the time of acquisition also were we like kept it unfunded, is there any immunization from the earlier owners with respect to this as well?
- Srinivasa Rao:** Actually whatever employees that are working in RUTGERS Group for them whatever pension liability is it is attributable to prior service as well as the future service. It is a change in the actuarial assumption, the discount rates we considered till December 2013 is 3.1%, the discount rate that we consider for December 2014 is 1.7%. So because of that the actuarial loss is about

€23.5 million and compared to the last financial year we have an actuarial gain of €3.5 million, it is only change in the actuarial assumption. If you look at IFRS and US GAAP such type of actuarial losses are not adjusted in the operating statement or P&L, we are allowed to take it to the balance sheet because this amount needs to be funded over a period of next 26 years, the average remaining service period of the employees in RUTGERS. So this is more of a non-cash and something specific to Indian GAAP.

**Achal Lohade:** Fair point. What I wanted to check is would not you create a reserve or create provisions to meet these obligations over a period of time and what is the actual cash outflow in terms of those pension payments on annual basis for let's say next two-three years?

**Srinivasa Rao:** It will be about €2 million to €3 million, not more than that and when we acquired the company RUTGERS all the outstanding pension liabilities is considered as equivalent of debt and reduced from the price offered to the Seller.

**Achal Lohade:** Right, okay. And in terms of the outlook on chemical business, if you could elaborate, are we looking at any improvement or it will be under pressure in coming quarters as well?

**Henri Steinmetz:** Yes, if we look to the chemical business we had very volatile 2014 specially in the fourth quarter with dramatic drop in adaptation by basically halving and going very low, oil went down to the level of \$47 at the lowest point, it has recovered today over \$60 again, so what we have seen in the chemical we got it by devaluations of our products but the margins we can keep. Secondly what we see is that due to the high dollar we see less pressure from imports for Asia and that is good for us, we are actually saying for this year regularly improvement of the situation, if the dollar stays high and if the notation is gradually up we will also improve the chemical business as we progress. We see at the moment good volumes, we are not other than that we see there is no loss in volumes at the moment, we are even seeing improvements there 5% to 6% this year but as the notations will go up we will also see the direct flowing into to the margins.

**Moderator:** Thank you. Next question is from the line of Kunal Banerjee from Brigade Capital Management. Please go ahead.

**Kunal Banerjee:** I just want to revisit that question on carbon products, I was actually pretty surprised to see the decline in carbon products I was expecting the decline in chemicals, some of your competitors have also recorded in the space service kind of telegraph ahead of time but the carbon product I just want to understand that a little better because Jerry I think you said that the CPC business was stable to maybe down a little bit in margins but you were able to offset most of the margins. So is it fair to assume that the majority of the decline then is on the CPC side and maybe you have some other products such as Creosote Oil and carbon black feedstock that's included in that segments. Could you just explain what part of RUTGERS is in carbon products and what is in chemicals?

**Henri Steinmetz:** Yes, it does the carbon products, if you look pitches only 50% of the tar and the others are benzene and oils. So from that perspective of course the oil part is linked to the oil drop and there

is 50% of the tar and I think here our big effort was really to start when the oil price was dropping we relatively were successful to move the mix of the oils which should show positive in this year and have a positive effect. The other part was the benzene impact, we have about 160,000 tons of benzene production, and that also was quite effected by the notations. We don't lose but the margin was half based on the products when you go from €1000 down to €500 for the product that has direct impact on the margins. And of course we have inventory impact as we have to do a revaluation on the impact on the values at the end of the quarter as we are required by the reporting rules. So if notations go up we also will get again a positive effect of the revaluation the other way round by the inventory. So, again as I said before its substantial part is linked to the oil in that product.

**Kunal Banerjee:** Okay. And so just following upon that, the coal tar that you buy you said you are kind of hedged on the raw materials and so I am assuming that the coal tar will reset lower, maybe if there was a lag effect here and that the coal tar didn't move down as quickly as your product prices did and if so would you see a reset lower in your coal tar acquisition cost going into Q1 and Q2?

**Henri Steinmetz:** Yes, we always the phasing of one quarter so the tar goes slower down than the oils and they come slower back than the oils, so that is always a delay of one quarter. So, exactly as you said we should also see if notation flow up again there continued increase in that business going forward as we are hedged by oil prices but there is a delay of one quarter.

**Kunal Banerjee:** So then I mean if that is the case if I look at Q1 we are going to basically get coal tar resetting down pretty substantially you are probably going to see a positive inventory revaluation because oil is at \$60 instead of \$47 or whatever it was averaging for Q4 and the volumes you said are pretty good so should not you start seeing a turnaround in the chemicals business and in the part of the carbon business that is RUTGERS legacy starting in Q1 and end of Q2?

**Henri Steinmetz:** We see a slight increase in impact in Q1 but I think the better impact will start in Q2.

**Kunal Banerjee:** Okay. And then Gerry just to confirm the CPC business itself the legacy CII carbon business sequentially was flat to maybe down a little bit, how would you characterize that?

**Gerard Sweeney:** By sequentially you mean by quarter?

**Kunal Banerjee:** Yes, Q3 to Q4.

**Gerard Sweeney:** No, we had less volumes but there was no radical impact on margin quarter-to-quarter.

**Kunal Banerjee:** Right. So basically it was seasonality but nothing more than that?

**Gerard Sweeney:** Yes, quarter-to-quarter there was no dramatic move in any way.

**Kunal Banerjee:** Okay. So I am just trying to reconcile the big decline in carbon products but it looks like the majority if not the entirety of it was then in the legacy RUTGERS carbon products, is that correct?

- Srinivasa Rao:** Yes, your understanding is correct Kunal.
- Kunal Banerjee:** Okay. And then just on the CAPEX this year, you are now talking about say Cogen facility in Kurnool, is that a must have, is that something that you need to do just given that there is a lot of uncertainty around how this year is going to shape up and your base earnings has just taken a leg down, so how are you comfortable about allocating capital versus keeping cash on the balance sheet or how do you see this year developing in terms of CAPEX? And you also have that solar project that you are going to have to spend on.
- Srinivasa Rao:** Couple of issues, one is the cement company is a debt-free company and there is no debt so we are actually a full tax paying company in the cement company. And the next thing is that cogeneration plant will help us because the cost of power today when we buy from Utilities is almost about Rs.6 a kilowatt hour but when we have a cogeneration plant we will actually get it just variable cost will be about Rs.1.5, so based on that we will be saving almost about Rs.2.5 to Rs.3 per kilowatt hour from this cogeneration project. And also the other advantage is we will get 80% depreciation very first year so we will not have any taxes. Similarly even for the solar power plant we will have 80% depreciation and we are using our existing lands and other things so it should help us, that is the reason why we are doing this project, it helps us from a depreciation perspective, they will reduce our tax rate and any how we are a debt-free company so a majority of the full income we are offering for taxes today. So these were the reasons why we thought it will not only reduce the cost of production of cement but at least it will also provide some tax shelter for us.
- Kunal Banerjee:** Okay, I get that. But I don't know, if I am doing the math it just does not seem like you are going to be spending about 100 million on that project right?
- Srinivasa Rao:** No, it is \$10 million.
- Kunal Banerjee:** And then just lastly, what are your plans I mean you did prepaid some debt, what are your plans going forward are you going to be opportunistic and be able to do that on a go-forward basis because it looks like your more obvious path of deleveraging is really to reduce the amount of debt because your EBITDA seems to be lagging down so your leverage is actually going up. But one way to address that is to reduce the outstanding debt so is that something you are going to be doing more as we go through the year?
- Srinivasa Rao:** Our idea is to use the funds for reduction of debt to the extent possible.
- Moderator:** Thank you. Our next question is from the line of Sanjay Jain from Motilal Oswal Securities. Please go ahead.
- Sanjay Jain:** Want to get some sense on how the CPC prices have moved with respect to the average prices in the fourth quarter, are they down in the January February or how the contracts negotiations is, has it been concluded or like these things are moving, that's question number one. And secondly, we had this discussion in the previous question regarding the segmental results of carbon

products, there is a very sharp decline from 2.4 billion EBIT in the third quarter to INR761 million in the fourth quarter. So whereas I heard Sweeney talking that there is not a material compression in the margin but the volumes were lower, how do I reconcile, was there losses other than the US part of the carbon business or they were just neutral?

**Gerard Sweeney:** I will take the first part of your question. From the CPC negotiation perspective for 2015 and expectations, obviously we negotiate on a six month basis and as I mentioned in prior calls the negotiations really take a while to shake themselves out but the early indications obviously with the aluminum price retreating the global concern over commodities our consumers came out, the aluminum smelters came out asking for further price concessions. We do not see any reasoning for that based on the market fundamentals not market sentiment and we have been resisting them to this point but the negotiations have not played out in total at this point. And what we are projecting at this point is flat to slight reductions in CPC price, but again any CPC price reductions are expected to be matched with GPC cost reductions as well. Henri, I don't know, do you want to handle the second part?

**Sanjay Jain:** Yes, before we go to the second part just one continuation in the same question, is there a spot market of CPC, could you give some sense if there is a spot business going on in the CPC, how they have moved?

**Gerard Sweeney:** No, there is relatively no spot business of CPC, the closest thing you would get to a spot type of situation is perhaps which tends to happen towards the year end is an aluminum smelter may find that they need one more cargo and they may ask people to bid on one cargo because it is an extra cargo beyond their contractual commitment. But by and large the nature of the business and the importance and criticality of the availability of supply lends itself to these long-term relationships and the fact that they need to plan well in advance to be sure that they are going to have carbon in specification on time.

**Srinivasa Rao:** Sanjay one more thing is, like the Indian calcining business is partly affected in the fourth quarter because of the Hudhud cyclone, we lost production almost for three to four weeks.

**Sanjay Jain:** Okay. So I mean if you strip off the US part of the business were there losses in the other parts if you put all of them together?

**Srinivasa Rao:** No, actually the reason for significant fall in the carbon business is mostly the lower margins in the European business because of the fall in the commodity prices and loss of production in the Indian calcining business. US is broadly in line with what they have done in the previous quarter.

**Sanjay Jain:** Right. So my question is, I mean if you remove the US part like should we say that it contributed positively in third quarter and contributed negatively in fourth quarter?

**Srinivasa Rao:** Yes, this is the only negative contribution came from the European business because of the lag effect of the raw materials, because while the prices of finished products have fallen

considerably the raw material prices actually there is a lag effect and you will start as Henri was mentioning you will only see that effect partially in this quarter and fully in the second quarter.

**Sanjay Jain:** Yes, I understood the discussion. My only question is in the numbers, have they contributed negatively like in other words let me say, is the profit of the US business more than the 761 million segmental EBIT which has been reported? So is that correct assumption?

**Srinivasa Rao:** Actually it is difficult to analyze the region-by-region but what we can say is the fall in the carbon business is two reasons, one is loss of production in Indian calcining business and commodity prices fall in the Europe, these are the two major factors otherwise everything should be normal.

**Moderator:** Our next question is from the line of Achal Lohade from JM Financial. Please go ahead.

**Achal Lohade:** What I wanted to understand is how do we track the recovery, what are the key monetarables according to you which can indicate that we are on the mode of recovery because if I look at past several quarters we always hoped that things will improve six months later, six month later however given the volatile economies across the world what are the key things to track as a shareholder?

**Jagan Mohan Reddy:** I would say the first thing would be the recovery in the aluminum price because we are hoping that aluminum prices will improve faster but they are not happening. But actually if you have been in the call for the last three or four quarters were always were mentioning that the recovery will be in the second half of 2015 and we think we are still reasonably we feel that the second half 2015 will be stronger especially with the QE that is being proposed in the European Union should help us because that should improve the commodity prices, so that should have a positive impact on the aluminum prices. So it is important for our business that the aluminum price also improves to a certain extent. With that actually if some input support can come from the aluminum price hopefully we should be on the recovery path but, however, I would also like to say that the fourth quarter was an aberration, we do not expect that it is to be repeated because of the lag effect and anything should be on the positive going forward even with the things remaining stable because the raw material prices also will fall compared to the things but to see a real impact, real positive impact we will need to see the aluminum prices improving.

**Achal Lohade:** And for RUTGERS?

**Jagan Mohan Reddy:** For RUTGERS also surge in aluminum prices will help but one good thing on RUTGERS is our Severstal project should start in second half of this year so that should provide some income and also any improvement in oil prices should help us going forward.

**Achal Lohade:** Right. And in terms of the cash flows we have seen pretty strong free cash flow in this year partly to do with the delay in the spending in Russia how are we looking at utilization in terms of dividend and the buyback for the quarter?

- Jagan Mohan Reddy:** Yes, the cash flow whatever we generated basically hopefully after this year this is the year where we will have the maximum cash outflow for the Severstal project and for other we are also doing a sulfur-dioxide scrubber in Chalmette Plant so that will also be completed by about August of 2015. So with these two major projects done I think going forward the cash accruals in our, we would like to reduce our debt, we would like to use the cash flows for reduction of debt.
- Achal Lohade:** Right. In terms of the CAPEX what is the budgeted CAPEX for the current year CY2015 and CY2016?
- Jagan Mohan Reddy:** CY2016 excluding the cement operations it will be about US\$50 million and these expansion projects like solar power plant and thermal power plant will be about US\$30 million.
- Achal Lohade:** And that will be entirely spent in the current year itself?
- Jagan Mohan Reddy:** Yes, majority will be spend in current year.
- Achal Lohade:** And how about CY2016 in terms of maintenance CAPEX?
- Jagan Mohan Reddy:** About \$40-45 million.
- Achal Lohade:** Okay. This \$50 million includes this maintenance CAPEX, is that understanding right sir?
- Jagan Mohan Reddy:** No, \$50 million is like what we do in US and Europe and Severstal and \$30 million is in the cement business.
- Achal Lohade:** So this \$80 million plus \$40 million is maintenance CAPEX, is that right?
- Jagan Mohan Reddy:** Yes.
- Achal Lohade:** So about \$120 million for the current year CY2015?
- Jagan Mohan Reddy:** You can say that.
- Achal Lohade:** Right. And any thought process on the dividend or the buybacks opportunities?
- Jagan Mohan Reddy:** See, one thing is that we can declare dividends due to some tax reasons I cannot say the quantum of the timing but we will be looking at interim dividend because that is more ideal for us from a tax perspective. So we will be looking at more of interim dividend going forward. On the buyback the Board has to decide but probably in the second half of 2015.
- Achal Lohade:** Right. Just one small question, I was just wondering for a seven megawatt we are incurring a CAPEX of almost 70 crores for the cogen plant at cement facility, I am just wondering what is driving that significant delta compared to normal CAPEX?



- Jagan Mohan Reddy:** See normally basically this order has been actually given to Thermax and normally the cogeneration plants are expensive compared to because of the smaller size, they are more expensive than the regular power plant because they use the waste heat recovery and also because of the lack of water in that area we actually have to use the air cooled turbines. So these actually will result in higher cost compared to the normal turbine plants.
- Srinivasa Rao:** Achal the payback period for this project is about four years when the cement operation starts capacity utilization improves we should recover the entire 70 crores investment in about four years' time.
- Achal Lohade:** And just last question, again about the US listing part what are the thoughts now, how are we looking at the time line, etc.?
- Jagan Mohan Reddy:** We can actually say to that extent that once we see recovery in the two commodity markets that is aluminum and oil markets we will definitely consider listing because we want to do that during an upward trajectory, of course this is subject to a Board approval but we want to see some positive movement in the aluminum and the oil industry then we would like to consider a listing thing.
- Achal Lohade:** Which is probably second half of 2015 or early 2016?
- Jagan Mohan Reddy:** If you tell me when these are going to improve then I can tell you that.
- Moderator:** Thank you. Due to time constraints that was the last question. I now hand the floor over to Mr. Kamlesh Bagmar for closing comments.
- Sri Shankar:** Hi, this is Sri Shankar here. Let me thank all the participant and special thank for the management for giving us an opportunity and thank you all the participant for a very interesting Question-Answer Session.
- Moderator:** Thank you very much. On behalf of Prabhudas Lilladher Private Limited that concludes this conference call. Thank you for joining us and you may now disconnect your lines.