“Deepak Nitrite Limited’s Q1 FY2022 Earnings Conference Call”

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Moderator: Ladies and gentlemen, good day, and welcome to the Deepak Nitrite Limited's Q1 FY2022 Earnings Conference Call, 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. Should you need assistance during the conference call, please signal an operator by pressing "*" then "0" on your touch tone phone. Please note that this conference is being recorded.

I would now like to hand the confidence over to Mr. Abhijit Akella from IIFL Securities Limited. Thank you. And over to you, sir.

Abhijit Akella: Thank you. Ladies and gentlemen, good afternoon and thank you for joining us on the Q1 FY2022 Earnings Conference Call of Deepak Nitrite Limited. We are delighted to host the Company's senior management team who are here with us to discuss the results.

I would now like to hand the call over to Mr. Nishid Solanki from CDR India to take the proceedings forward. Thank you and over to you, Nishid.

Nishid Solanki: Thank you, Abhijit. Good afternoon, everyone and thank you for joining us on Deepak Nitrite's Q1 FY2022 Earnings Conference Call. Today, we have with us Mr. Maulik Mehta, Executive Director & CEO; Mr. Sanjay Upadhyay, Director, Finance & CFO; and Mr. Somsekhar Nanda, Deputy CFO. We will begin the call with opening remarks from the management team, followed by an interactive question and answer session.

At the outset, I would like to clarify that certain statements made or discussed on the conference call today may be forward-looking in nature and a disclaimer to this effect has been included in the investor communication shared with you earlier.

To begin, 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. The results documents have been shared with you earlier and have also been posted on the Company's website and also uploaded on the stock exchanges.

I would now invite Mr. Mehta to share his opening thoughts. Thank you. And over to you, sir.

Maulik Mehta: Good afternoon everybody and a warm welcome to you on Deepak Nitrite's Q1 FY2022 earnings conference call. I trust you, your families and colleagues are safe and in good health in these unprecedented and very trying times.

Given the second wave of COVID-19, the Company maintains a high level of production at all of its facilities, while complying to all regulatory mandates, rules, and safety requirements. Our employees and communities' health and well-being are of paramount significance to us. Despite the limitations, we have ensured that all facilities are operated with utmost care for the safety of people materials and processes. Additionally, the Company has undertaken to vaccinate all employees and spouses.

Moving on, as our results documents were shared with you earlier, I hope you have had an opportunity to glance through them. I will initiate by briefly taking you through our key financial and operational highlights for the first quarter, and how we are preparing ourselves for the coming year. Mr. Upadhyay will then present to you a more detailed and comprehensive financial overview during the period under review. Following that, we will open the forum for Q&A session.

Our teams have once again performed well in the midst of a challenging environment, enabling us to maintain our performance momentum from the second half of FY2021 into the first quarter. In addition to the instability caused by the second wave in India, the operating environment was characterized by soaring input and energy costs, volatility in foreign exchange rates, inbound and outbound logistic limitation, as well as relatively high logistics and utility expenses. To ensure an efficient performance, your Company has utilized its manufacturing competence, world-scale facilities and agile operations. This was supported by a healthy balance sheet. I am happy about our announcements of key investments to elevate our growth momentum moving forward.

Deepak Nitrite delivered a resilient performance amidst the second wave. On a consolidated basis, revenues came in at Rs. 1,534 crore, up 125% year-on-year and 4% quarter-on-quarter. Improved capacity utilization aided revenue growth as also, DPL substantially improved performance, largely on account of higher realization of its products. Even though certain end user segments are yet to recover to pre-COVID level of activity, Deepak Nitrite and Deepak Phenolics have proactively catered to both domestic and export markets to generate higher volumes and capitalize on favorable realizations. I should mention that we had lost a month of operations last year in the same quarter, so the audience may please consider this.

In Q1 FY2022, EBITDA stood at Rs. 460 crore, higher by 144% year-on-year. EBITDA margins increased by 200 basis points to 30%. EBITDA performance has been improved by operating leverage from revenue recovery, as well as advantages from higher realization on expense management initiatives.

PBT grew by 206% year-on-year and 4% quarter-on-quarter to Rs. 405 crore in Q1 FY2022, attributable in a good part to an outstanding performance by the phenolics business. Besides DPL’s solid performance, PBT improved as a consequence of increased net revenue, and reduced interest rates as a result of significant debt reduction over the previous year.

During the quarter, profit after tax came in at Rs. 303 crore, higher by 206% year-on-year and 4% quarter-on-quarter as a result of improved operational and financial efficiencies, supported by higher revenues. Even though the market is still recovering from the effects of the second wave, the Company was able to record an improvement in PAT due to an improvement in performance across all the segments.

Now on to the segmental performance. Revenues in Basic Chemicals increased by 70% to Rs. 249 crore in the first quarter. This is keeping in mind that there is certainly an impact in the MSME sector, which is a large customer base for the Basic Chemicals products. This is thanks to the resurgent second wave and various logistical challenges. A resilient performance was exhibited during this quarter. Gradual rise in input commodities have helped to reap better realizations during the quarter. However, future margin will depend on the pace of demand recovery. Revenues in Fine & Speciality Chemicals increased by 48% to Rs. 207 crore in Q1 FY2022. Volumes have been affected this quarter due to disruptions in export-bound logistics. Furthermore, increased commodity costs have certainly had an influence on profitability. Meanwhile, revenues in Performance Product segment increased by 55% to Rs. 93 crore in Q1 FY2022. The Performance Product segment has seen only partial recovery in volumes since key end user industries have yet to fully rebound to pre-COVID levels. That said, DASDA, which is a key raw material for the segment, has seen its prices and volumes return to what we consider is a normalized situation.

Deepak Phenolics delivered a remarkable quarter; with revenues soaring by 202% to just shy of Rs. 1,000 crore in quarter one. Despite limited personnel and material transportation during the peak of the second wave, the facility continued to operate at high utilization with quarterly average utilization at or above 110%. While EBITDA grew by 263% year-on-year to Rs. 313 crore in quarter one, the EBITDA margin improved to 31%. The Company has been able to leverage favorable price trends and demand for both phenol and acetone during the quarter.

Without doubt, our business model has been put to test by the ongoing global pandemic. But with increased capacity from brownfield expansions and sustained robust demand from end user industries, we believe will help drive growth through all of the strategic business divisions.

In key developments, I am glad to share with you that we are nearing completion of our land development in Dahej 2. Investments of Rs. 300 crore for new products in life sciences have been undertaken at the site. While Deepak Phenolics is in the process of expanding its IPA facility and continuing to improve its utility capabilities, the Company is planning to invest another Rs. 700 crore to add new solvents, which are downstream of phenol and acetone. These solvents which are primarily used in applications like life sciences, paints and coatings are seeing a healthy demand CAGR within the country and in target export markets. The Company aims to become a world-class supplier of solvents, which are well integrated with its wide product basket and process competencies.

During the quarter, Dun & Bradstreet recognized our Company as a winner in the best growth performance of chemicals division. Deepak Nitrite has also been ranked No. 2 on Fortune India's Top 100 Wealth Creators. We are confident that the Company is well equipped to assess emerging growth opportunities and end user segment, while expanding in the value chain and nimble footedness to adapt to an evolving market, all of these will contribute to its long-term success.

In conclusion, I would like to emphasize that DNL is well-positioned for expansion in a range of aspects. Apart from a noticeable change in the chemical supply chain from other countries to India, Deepak Nitrite has the ability to take advantage of the opportunity and accelerate in the near to medium term. Deepak Nitrite is an excellent candidate to lead the India chemical manufacturing trend, thanks to its unique product mix and decades of manufacturing experience. This, along with contributions from ongoing brownfield expansions and major greenfield projects containing value added forward integration, will improve our competitiveness and position us to grow market share, generating value for all stakeholders.

Thank you. And I would now like to hand the call over to our CFO, Mr. Sanjay Upadhyay, to address this forum and briefly take you through the financial performance of the period in review.

Sanjay Upadhyay: Thank you, Maulik. Good afternoon, everyone. And thank you for joining us today on Deepak Nitrite's Q1 FY22 earnings call. I will walk you through the highlights for the financial results for the quarter ended June 30, 2021.

In Q1 FY2022, DNL has performed impressively in a challenging quarter, given the disruptions induced by second wave in India during April and May 2021. Escalating expenditures and persistent volatility in foreign exchange rates defined the operational environment. On a consolidated basis, revenues grew by 125% to Rs. 1,534 core during the quarter under review. The revenue performance has been attributable to the normalization in standalone operations, particularly in the basic chemical and fine & specialty segments, supported by DPL's significantly enhanced performance by running its facility at high utilization levels, allowing it to take advantage of favorable demand and competitive pricing for its products.

EBITDA reported at Rs. 460 crore, higher by 144%. Despite cost pressures and logistical challenges, the margin performance has been commendable with the Company reporting EBITDA margin of 30% during the quarter. PBT and PAT expanded by 206% to Rs. 405 crore and Rs. 303 crore respectively. As Maulik mentioned earlier, growth rates are to be reviewed in backdrop of lower base of last year caused by nationwide lockdown and related restrictions.

Now, moving to our segmental performance.

Basic Chemicals (BC) reported revenues of Rs. 249 crore in Q1 FY22, up 70% from Rs. 147 crore in Q1 FY21. The segment did well by capitalizing on a favorable demand landscape. Despite a brief impact on MSME sector owing to rising caseloads and logistical issues, performance was resilient during the quarter. EBIT increased by 134% by Rs. 85 crore with an EBIT margin of 34% in basic chemicals segment.

Fine & Speciality chemical segment revenues grew by 48% to Rs. 207 crore in Q1 FY2022 as compared to Rs. 140 crore in Q1 FY2021. EBIT improved by 9% to Rs. 67 crore with EBIT margin of 33%. Challenges in export logistics as well as a significant increase in commodity input costs have had an influence on Fine & Speciality segment's revenue performance. Product demand on the other hand continues to be strong.

Performance products segment reported revenue growth of 55% to Rs. 93 crore during the quarter under review versus Rs. 60 crore in Q1 FY2021. DASDA prices have gradually started returning to normal and volumes are improving.

Deepak Phenolics reported a solid performance with revenues expanding by 202% to Rs. 999 crore, one crore short of thousand in Q1 FY2022. EBITDA soared by 263% year-on-year to Rs. 313 crore in Q1 FY2022. EBITDA margin stood at 31% in Q1 FY2022. Robust demand and high plant utilization (quarterly average utilisation of 110%) helped revenue realization for both phenol and acetone increase over year-on-year. The Company has been able to take advantage of favorable demand patterns and competitive pricing for both phenol and acetone.

Lastly, on balance sheet front, Company's financial position has significantly enhanced and is leveraged to gradually reduce debt. On a standalone basis, Deepak Nitrite is debt free, surplus of Rs. 270 crore in cash & bank balances and investments. While on considered basis the net debt-to-equity ratio is 0.07x, down from 0.43x in the first quarter of FY2021.

With that, I would now request the moderator to open the forum for question-and-answer session. Thank you.

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: I have two set of questions. First is, if I see your annual report from last 10, 11 years, on a standalone basis we have almost invested around Rs. 100 crore on the R&D. And if I see from 2016 to 2021, baring 2019-2020, excluding DASDA benefit, our EBITDA has gone up from roughly Rs. 160 crore to Rs. 540 crore on a standalone basis in 2021. So, is it fair to assume that majority part of this R&D expenditure of Rs. 100 crore in the initial years of this decade was more towards process innovation, the benefit of which we started seeing now in the numbers? And the benefit of product innovation in terms of launching new products would be subsequently felt from 2021 onwards? So, this is question number one.

And a related question would be, how do you see the next decade of R&D expenditure at Deepak Nitrite? Probably we are at 40, 42 products at this point of time, so next 10 years of R&D expenditure would be skewed more towards product innovation than in process innovation, because what normally you guide in most of the interactions is that process before product. So, can it be reversed for next 10 years that now process innovation is mostly being achieved and next decade would be more towards product innovation?

Sanjay Upadhyay: Nirav, I slightly disagree with you. It was never process versus product; it was always both together. The products are also there, in fact, we have introduced quite a few products in last seven, eight years, 10 years, particularly in Fine & Speciality segment, so it's not like that. We have a separate team of people for product development as well as process development, both are running, I mean, it's not one versus the other. But yes, EBITDA margins and whatever you said, we are setting up a premium R&D facility now, up till now it was in our premises, now it's a separate building in which we will be coming up which will be high-tech. So, focus would be on both. But yes, we have the ability to go ahead and spend more and more on R&D and our products, you can certainly expect quite a few products in coming years, no doubt on that.

Nirav Jimudia: So, can the product in terms of number of products, be doubled from here in terms of either doing backward integration? Because every backward integration comes also savings in freight cost, etc., because we are within the same complex itself, on our raw material. So, if you can guide in terms of how many new products can we expect over the next decade or let's say even a period of five years would be helpful.

Maulik Mehta: Actually, I would be wary about talking about number of products, because frankly speaking, number of products is not a helpful guide. If you look at Deepak Phenolics, they added two products, but it significantly changed the economic landscape of the Company. So, instead of that, I would say that our goal is to be able to add a basket of very high-quality products, which are fitting within our, "right-to-win" template, which I have alluded to before. One thing that I can mention, and I know this has been a point of chagrin for a lot of investors, why we are shy about mentioning the names of the products that we are getting into, and it is not because there is a some sort of a veil here or something like that. But what I can very simply say is that our efforts over the last two years, and our efforts moving forward is to invest in platforms. Now, that platform in jigsaw puzzles with other platforms that we already have good competency in, results in a very large number of good opportunities for us. In many cases, these are with customers who already have a good key account relationship with Deepak Nitrite. So, it further enhances our right-to-win. And this is how we foresee the near-term future. When we invest into a new product, it will be keeping in mind the platform competencies that we have been building, along with that the kind of relationship and the right-to-win that we have in the short, medium, and long term. So, we have never shied away from saying that we would not look at making investments which are fly by night, where there is an opportunity in the short term, but long term we don't know. So, we stay away from such opportunities and focus on ones where we believe that for the next 10 years, 15 years, there is a very good reason that Deepak Nitrite to be number one, two or three in the world in those products. This is what we will continue.

And as Mr. Upadhyay has mentioned, we do have two separate pillars, one is process intensification and one is product development. Process intensification is taking existing products and improving the process to unlock value. And product development is where we use existing processes to develop new products.

Nirav Jimudia: Got it. And my second question would be in terms of talent pool, we have seen recruitments by almost all major chemical companies, including ours also. So, how we at Deepak have been able to retain the key management team or the key personnel within the Company as well as strengthening the leadership team by recruiting new people? And if I can ask a related question to this would be, as Mr. Maulik Mehta, where & what do you spend most of your time on? Either most of the time is spent on looking after expansion or looking after the existing business or interacting with the core teams across the business verticals, or like mentoring new teams, if you can give your order of preference in terms of these four parameters would be helpful.

Maulik Mehta: See, I am only 38 years old and I don't come with decades of experience that a lot of our management has. So, for me, every single opportunity is an opportunity to learn. If you ask me where I spend the majority of my time, I can tell you that I spend the majority of my time just seeing what I can do to help the rest of the management achieve the goals that we have collaboratively set about together. So, frankly speaking, my entire day goes in seeing what I can do to help the goals that have already been set or are in the process of being set, what I can do to remove potential impediments.

Now, in terms of the talent aspect, what we find is that talent where the values of the individual are in line with the values of the Company and talent which finds that there is a good opportunity for professional growth within the Company, and also talent that believes that at the end of the day the Company itself is growing, this talent that is likely to stick around. We have our internal processes where we look at enhancing the value, both on a personal and on a professional level that our best talent is able to drive, whether it is L&D opportunities, whether it is courses in connection with various premier institutes, both in India and outside of India, and whether it is opportunities to develop good, well-functioning cross functional teams. The goal here is to enhance the environment for productivity. When that happens, the organization is growing, the person has a chance to grow professionally, I think it's a good recipe to retain good talent. And as the word spreads, it's also a good opportunity to attract new talent. We have already started with the disadvantage of being located in a place which is far away from the metropolis cities, so we have to see what we can do to ensure that working here is a pleasure, not a pain.

Nirav Jimudia: Thanks for answering the questions in detail. And lastly, I would like to congratulate the team again for providing the encyclopedia of information in the annual reports. Best of luck, and good luck for the future.

Moderator: The next question is from the line of Saurabh Kapadia from Asian Market Securities.

Saurabh Kapadia: My first question is on the new expansion on the downstream products, can you provide more color in terms of capacity we are looking to add under this project and also the timeline in terms of commencement of the project?

Maulik Mehta: On the capacity front, instead of giving a direct number, because if you look at Phenolics, we could have told you that the capacity is 2 lakh tons, which we did, but we realized that that's not the right number, the capacity is what you make out of it. But what I can say is that the products that we are investing in, certainly have an import substitute element. And you know, what we believe internally is, step one is Atmanirbhar Bharat; but step two is, Make in India for the world. So, if we really want to have the right mix of market access and of cost optimization, we have to focus on world-class capacities. So, the solvents that we are looking into manufacturing, which are downstream of phenol and acetone, will have world-class capacities, but with a clear preference on import substitution.

Saurabh Kapadia: And our timeline for commencement?

Maulik Mehta: So, the timeline would be, I think, about 20 to 26 months.

Saurabh Kapadia: So, are we also going to add phenol and acetone capacity along with the downstream products?

Maulik Mehta: So, this is something that I have had the pleasure of answering in past concalls. As a Company, we have been very good at going downstream and at the same time maintaining the market share. Now, phenol consumption in India has a healthy demand CAGR, and also most of the downstreams of phenol and acetone are actually imported. So, that gives this double opportunity. So, in short, we will be doing both, it's only a question of what we do first and what we do second. Right now, the immediate priority is to ensure that we have downstream products, which are good import substitute and good value drivers. And at the right time, hopefully in the near future, we will also be looking at ensuring that we retain our market share in a growing demand situation.

Sanjay Upadhyay: Actually, I will just add on to this. We are moving towards you know we had said earlier that we want to captively consume both acetone and phenol around 30%, 35% in-house. So, this is the step towards that. And once these new facilities are commissioned, we will be doing that. So, both phenol and acetone downstream are ready, with captive consumption of 30%, 35%.

Saurabh Kapadia: Okay. My second question is on Fine & Speciality Chemicals. So, over past two quarters, we have seen some pressure on the margin because of the higher commodity prices. So, what is the outlook in terms of margin going ahead?

Maulik Mehta: So, the thing is that margins have to be looked at in range, because there's a basket of products. Thank you also for pointing out about the raw material price increases which of course have been a factor, so has the reality that logistics have certainly spiraled out of control in the last couple of months. Now, this will of course also have an impact. However, what's important, let me emphasize is that our products are preferred by our customers. So, in most cases, we are L1, in a few rare occasions we are L2, but that might also be because of our inability to go beyond a particular volume. That said, the margins at least in Q1 have been slightly under pressure, simply because a lot of our higher margin products are actually export-bound. And there were a lot of export disruptions where ship berthing was not available, where you had the Suez Canal issue, where in most of the cases orders are in hand, the job is to get the product to the customer at the right time. So, in all of these situations, what has happened is that Q1 numbers look slightly deflated, because many of these products that we targeted towards the Indian marquee customers.

Now moving forward, once the situation with ship availability, I am not even concerned about cost of shipping, but ship availability once this normalizes, we will continue to see a healthy balance between export volumes and domestic key accounts. And at that time, you will see at least some improvement in terms of the EBITDA. But it is true that this should always be considered in a range-bound fashion.

Sanjay Upadhyay: I will just add one more point here. Maulik rightly mentioned about the availability of ships and container. So, you must have read and which is the fact that sea freights have gone up significantly, so it helps us in some segments, but particularly in basic it affects, also in Fine & Speciality where we have slightly longer-term contracts and the terms are of CIF and we are bearing a freight. So, there would be an impact to the extent we have signed contracts, and by the time we negotiate and arrive at a fresh price. So, shipping line issue still remains for particularly in export business.

Maulik Mehta: Actually, thank you for bringing this question, it allows me to talk about one of the two or three points that I had handwritten. But let me mention that when you are talking about Phenolics and when you talk about Basic Chemicals, the best situation is when you have a stable demand situation and volatile logistics. Because at that time, the customer gives you a greater premium because you are local, you are dependable, you are easy access for the customer. In Fine & Speciality, the only thing that we have to look at is logistic movement from India to that country, worse off than logistic movement from some other country to the target customer. If it is as bad or if it is better, then we are in a good place. But if it is worse, then the customer is highly dependent on those particular products. And if that is a challenge in getting the material, so for example, it's so difficult to find ship berthing to places like Canada or South America that even if the orders are there, even in places like Europe, even if the orders are there, delivery is being delayed by a month, two months etc., can really push customers' production schedules off track. So, we are exploring various options like vendor managed inventories and other things, hopefully the situation will normalize in the future. But this is just to give you an insight into what each of our business unit, what kind of environment they prefer.

Moderator: The next question is from the line of Rohit Nagraj from Emkay Global.

Rohit Nagraj: Congratulations on yet another good set of numbers, plus the new announcement of capex. The first question is in terms of the newer opportunities, so we have been growing organically over a period of time. And given that the debt levels have been very, very low now, and the cash flows have been coming in, we have earmarked another Rs. 1,000 crore of capex for the next couple of years. Beyond this, do we aspire to go in for any inorganic initiatives, maybe domestically or outside India to garner some new technology or some new product streams which will be complementing our business?

Sanjay Upadhyay: So, this is always there, I mean, again, it is quite same in products and process. Of course, we are growing, and we have announced capex, and if there is a good opportunity to grow inorganically. No doubt, we will certainly grab that, there is no question. But it has to be meet and fit our requirement, otherwise you acquire and then don't make money out of that for four, five, six years doesn't make any sense. But yes, we are open to that, no doubt.

Rohit Nagraj: Right. The next question is on Basic Chemicals front, so predominantly in nitric acid and derivatives, the margins have gone up significantly and there is a slight anomaly where we have been gaining market share from the smaller players. At the same time, there is an impact on the smaller players, as you have said that MSME shipment has been under pressure during the quarter. So, how is the performance so strong during the quarter? And is it in a transitionary phase that may be couple of quarters down the line, things will start normalizing and probably the margins will come back to more normal levels maybe 20% plus/ mines?

Maulik Mehta: So, first of all, when you said nitric acid, immediately I thought you might be referring, maybe I should connect you to Deepak Fertilizers, because they are one of the largest nitric acid manufacturers, we are consumers. But if I look at products manufactured from nitric acid, and other petrochemicals and these things, it is true that we do have actually in this business, so in the nitrites business there's a lot of dependency on MSME. But in the nitro business, it's actually a good mix, so there is also the large players, the world players and there's also the small niche players. But that said, in terms of the margins, what I can say is what I mentioned in the earlier question, as long as the demand is stable or at an uptrend, it's good business for us and it is better business for us if export logistics are a challenge, because that way the customers will prefer to give a premium to a domestic supplier. However, the nitro business definitely had some tailwind because of disruptions in China and because of a reluctance from a lot of European companies and countries to engage in expansion of nitration, which if not handled properly, can be a dangerous chemistry. So, this is a key competency that we have and it is the key competency that we are investing into. There will of course be some amount of brownfield but you will also see greenfield. So, I can safely say that nitration and nitro products, the margins are directly proportionate to the kind of growth that we are expecting from the consumption. And Deepak Nitrite will continue to remain and maybe even improve its world market share.

Moderator: The next question is from the line of Vriddhi D. from Raedan Securities.

Vriddhi D: My question is, as per your knowledge, are there new incremental capacities coming up across the globe for phenol and acetone? And how are the current prices of phenol and acetone trending?

Sanjay Upadhyay: Capacities of course, people announce every now and then, I don’t want to comment on that because there's a big gap between announcing and then actually going ahead and implementing. And in any case, if these capacities come, it will be three to four years away from today. The way demand is growing, I mean there is absolutely no issue on phenol today. I don't want to comment on prices, as they keep on fluctuating, we had commented that yes realizations are better in Q1 and continues to remain improved on phenol, acetone of course some up and down is there, but then we have IPA also consuming acetone. So, I mean, that is how we want to play the game between IPA and acetone, and similarly when we have phenol downstream ready, again it is the same case. So, no point in telling you the price because there is no pricing point as such today. Today if I say it is Rs. 1 lakh, tomorrow it will be Rs. 110,000, day after it may be 90,000. So, it doesn't make sense in giving the numbers.

Vriddhi D: Sure. Thank you for that. And my other question is, what is the capacity utilization for Fine & Speciality Chemicals?

Sanjay Upadhyay: We run our capacity around 90%, 95% on an average.

Moderator: The next question is from the line of Rikin Shah from Omkara Capital.

Rikin Shah: Congratulations on a fantastic set of numbers. I just wanted to understand the new capacity addition that we are doing in the solvent and downstream space, what kind of competitive landscape is this in these businesses?

Maulik Mehta: So, as we mentioned, these are import substitutes. So, yes, there are capacities the world over, no doubt about it, but the demand for these products is growing and it is growing at a very high CAGR. In fact, it is in the life sciences, paints and coatings end segments that we are finding the highest utilization for these solvents and also the highest demand CAGR. So, this is something that we believe is going to be a continuing trend in India.

Rikin Shah: So, domestically we would be number one in this space?

Maulik Mehta: Yes, hopefully.

Sanjay Upadhyay: From a market perspective, yes.

Moderator: The next question is from the line of Asmita, an individual investor.

Asmita: My question is regarding the Deepak Clean Tech. So, I just wanted to know, as already mentioned that phenol will be getting used around 30% to 35% in-house, and that will be used for the product portfolio which are coming from Clean Tech, right?

Maulik Mehta: No, products that Deepak Phenolics is going downstream into are downstreams of phenol and acetone. So, the raw material for these products are being manufactured already today. And I think sometimes I feel like we should change the name of Deepak Clean Tech to just saying Deepak Chemicals or Deepak other chemicals or something like this, because it's making a lot of people feel that there is only a particular small basket of products that will be made here, maybe some detergent chemicals or some cleaning chemicals, things like this. That's for the name, it just happens to be a name, don't put that much into the name. I will just say that the products that will come into this business are ones that have very tight synergy between Deepak Nitrite's competencies and Deepak Phenolics' competencies, so that in the future nobody has to bother with asking should this product come in Deepak Nitrite or Deepak Phenolics, it happens to come in a separate segment called Deepak Clean Tech.

Asmita: Okay. Thank you. And one more question, just wanted to know, Deepak Clean Tech will be adding product portfolio, so on a projection basis, what type of revenue and margin we can see once capacity comes online? And also, I wanted to know, is there any plan for additional borrowing for expansion that is already in pipeline?

Maulik Mehta: We have not even finished announcing our capital investment plans yet, we have only announced two trenches of capital investment. You are already asking us about revenue, you don't want us to announce more investment plans? And with regard to the question about debt, see, we have a very experienced finance team. So, we are very comfortable taking debt also, we have absolutely no problems with that, we have a very strong liquidity position also, so we are happy to look at that. So, it opens up a lot of opportunity for us and we will take a very judicious call. But, in fact, Mr. Sanjay Upadhyay has told us many times that, look, he is very tired of people asking him about zero debt, he is not interested in being a zero-debt Company. And therefore, moving forward, we will ensure that we have a healthy mix of both.

Moderator: The next question is from the line of Ramakrishnan V. from Equity Intelligence.

Ramakrishnan V: Congratulations for the best set of numbers. I was just looking at your quarterly numbers, especially on Deepak Phenolics, Q3 FY2020 we were doing around Rs. 535 crore turnover and we had a Rs. 40 crore segmental profit of around 8% margin, then gradually it went up to 12%, 21%, 22%, 23%, now we are at somewhere between 30%, 31% EBITDA segmental margin on the phenol and the acetone. We have a huge capacity, and our capacity utilization also has gone up to 110%, so what has driven this, is it demand driven pickup, could you elaborate on that?

Sanjay Upadhyay: Yes, your observation is right. But if you see the Q4 numbers in terms of profit & loss, we have done well. These numbers are on turnover side, yes, because as Maulik was mentioning, if there are issues on the logistics and other factors, then basic chemicals stand to gain. Demand is already there in the phenol business. And we are running at 110%, 115% capacities at times. So, this is a combination of higher volumes as well as better realizations, the realizations were really, really better in the last quarter in Q1. So, this is a result of that.

Ramakrishnan V: So, what is the trend like, is it further demand? Because price trend nobody can predict, but the demand trend, what you see, is it COVID related, what percentage is COVID related and otherwise normal?

Sanjay Upadhyay: No, it has nothing to do with COVID, first of all. See, it is on supply, if we are facing problems in shipments, other companies are also facing problems in shipments. So, the local player seems to gain so demand certainly we get, and we are able to supply because we are the only large player here. So, that's the main reason. So, it is nothing to do with COVID. But yes, I don't want to use that word, but the shipping industry is becoming a major bottleneck today. So, the supplies across are becoming an issue.

Ramakrishnan V: It is basically import substitution.

Sanjay Upadhyay: Phenol is largely import substitute.

Maulik Mehta: Last year we had some challenging months where the domestic demand consumption was much less. Now as a Company, we didn't have that sort of money where we could put up any sort of a capacity, any sort of storage and all that, so we had limitations everywhere. And therefore, there were periods of time last year where we had to export our volumes. So, it is not like there have been only a consistent growth, growth, growth in terms of demand, that is the trend, no doubt about it. But things like COVID play spoil sports especially to industries which are linked to infrastructure, housing, these things, keeping in mind the margins I would give a high degree of credit to the operating team. Because such kinds of products and processes, a significant chunk of the margin actually comes from operating them at a high degree of productivity, which the team has done, either because of their process competency or because of this Theory of Constraints, because there's no other choice.

Ramakrishnan V: So, the import substitution continues, you should see this kind of a demand for both phenol and acetone going forward also?

Maulik Mehta: Yes, when we envisaged the project with 2 lakh tonnes, we expected to be about 65% of the Indian consumption story, which we expected it to grow also at 6%, 7% CAGR. When we finally came into production, and today if I look at it, with significantly more than 2 lakh tonnes, I won't give you the exact number, but significantly more, we are now at 55% of the domestic consumption. So, that is how the market size has actually increased, having a domestic supplier encouraging a lot of other companies also to think about making investments, that has happened. And we believe that this is a moving trend in this direction. So, we don't expect, in a normalized environment if you keep COVID and all this aside, we expect demand for products like phenol, acetone and even many of the downstreams of phenol and acetone to have a good healthy base and demand CAGR in India.

Moderator: The next question is from the line of Dhruv Muchhal from HDFC Asset Management Company.

Dhruv Muchhal: Can you guide for capex for FY2022?

Maulik Mehta: So, at the moment, we have announced Rs. 300 crore from Deepak Nitrite in new products and Rs. 700 crore in Deepak Phenolics for also new products which are downstreams of its current product basket. We will announce more as and when we find that it is the right opportunity. And this does not take into account the brownfield expansions that we do of existing products. And IPA and the utility cost enhancement projects which are ongoing in Deepak Phenolics, we are looking forward to seeing value come out of them in terms of revenue, and value come out of them from around the third quarter onwards.

Sanjay Upadhyay: Last year we had announced certain projects which we are completing towards the end of second quarter and third quarter from phenolics, whereas some debottlenecking expansions in existing capacities in DNL is also in the pipeline. So, last year this phenol capex was around Rs. 200-250 crore and Deepak Nitrite was Rs. 100 crore, which you will see the results in Q3, maybe towards the end of Q3 onwards.

Moderator: The next question is from the line of Rohan Gupta from Edelweiss.

Rohan Gupta: Congratulations on pretty solid set of numbers. Only one question from my side, your Company is a cash machine and now with the current commodity prices benefiting, your cash flows are constantly rising. Though you have already announced almost Rs. 1,000 crore capex for the current year, I just wanted to understand that does the management have the bandwidth and the thought process over next two to three years of capex plan or are they entire cash flows or already there is an opportunity to top up on debt? Can we look at the Company getting into a mode where we can see some capex for next three to four years of Rs. 3,000 crore to Rs. 4,000 crore, just management's thought process around that?

Sanjay Upadhyay: Of course, why not? Today we have such a strong balance sheet and strong cash flows coming in, so if we feel there is a good project or great project, somebody said about acquisition, certainly we can do it, we have that horizon and we have that benefit also to look at that, no doubt on that.

Maulik Mehta: I would also like to add one point that one thing that the Company has done very well over the last several decades is that it has approached things with a frugal mindset. So, having good cash generation allows us to invest in winning project. We are not going to invest just for the hell of it, it has to pass our very stringent "right-to-win" criteria. So, therefore, the projects that you will see will be projects where there is a very high degree of certainty that it is going to improve the financial performance of the Company and has a high degree of confidence that Deepak is the best Company to make these investments. So, we will not be making investments without care and concern, because today the cash flows are good and tomorrow they may not be, no, that's not how it works.

Moderator: The next question is from the line of Tejas Sheth from Nippon India Asset Management Company.

Tejas Sheth: Two questions, one on the R&D side. The new center which you are investing in, if you can just give some magnitude towards that, what would be the size of investment? What kind of chemistry we are looking in there? And how many R&D personnel we are looking to hire there?

Maulik Mehta: See, the size of the investment, frankly, what is the point of talking about things like civil structure and buildings and all that. We have made good capital equipment investments in the last two years; we will be increasing that somewhat. But in any case, the focus, as I mentioned earlier, is on platform. So, we have identified some key platforms, two of them which we have already announced which will work in synergy with our other competencies. So, I think right now, we have about 70 or 80 employees in the R&D center, and we will gradually look at improving that as and when we see fit. What is important is ensuring that the right kind of value comes out of that. So, R&D is one of those areas where the right question is not how much we are spending into it or how many people we are employing in it if nothing of significant value comes out of it. Our first job is to ensure that the pipeline of new products that we are releasing are really high quality, high caliber value drivers. And as we ourselves find our own confidence improving, we will ensure that we supplement the capital investment and people investment with the right additional resources.

Moderator: The next question is from the line of Manish Aggarwal from North Bridge India.

Manish Aggarwal: Firstly, I want to say thank you to the team of Deepak Nitrite. I am investor since last five years, means 2017 December I invested, and this is the first concall which I am attending. So, I have seen the days when we were having Rs. 7, and today we are clocking a minimum of Rs. 55 EPS, so thank you so much for the efforts and great value creation for the shareholders.

Maulik Mehta: Thank you for believing in us.

Manish Aggarwal: Thank you so much. I have just one query regarding the fluorochem business which we are going to start, so I just want to know the revenue which the Company can generate from this particular project. And follow up question on that, where do we see the revenue of Deepak Nitrite in 2025. So, just want to know your vision where we are heading for in 2025.

Sanjay Upadhyay: See, the fluorochemical numbers, I can tell you, that in any project as Maulik was just mentioning, we have a benchmark that our asset to turnover ratio should be 2:1 and payback not more than four years. So, you can calculate based on this, whatever announcements made so far, unless it's a captive conservation of our CPP. Otherwise, these are the normal ratios within which we operate.

With regards to your second question, where do we see Deepak Nitrite from today, the kind of announcements and kind of projects we are making along with our balance sheet today, I can say we are very, very confident. There was a time when our MD had said I want to reach, maybe four years back, $1 billion turnover. And at that time nobody believed, of course, dollar was at that time Rs. 59, today it has gone up to Rs. 74, that is the different thing. But we have actually proved ourselves that yes, we can do it. And again, since you have invested in 2017, if I see five years back that you will see a completely different Deepak Nitrite after five years, and only long-term investors should invest in that, because that is what we had in mind then when we were announcing the fluoro project. Today, I can tell you once again, that yes, we will see a completely different Deepak Nitrite in five years' time than today, the kind of effort we are making, the kinds of investments we are making, the kind of team we are creating, it's a very, very focused approach, chemical industry is giving us a lot of opportunities, let me tell you. A good R&D team, a good management team and a strong balance sheet. And we have got everything which enables the Company to grow, and you will certainly see the results, believe in us, and have faith in us.

Maulik Mehta: I will just add one point to what Mr. Upadhyay said, that as a Company, the kind of values that we espouse are also values that our customers appreciate very highly. So, that makes us ideal partners for growth. So, hopefully, when we have this conversation after three or four years, when you tell us that you have been invested in it for the last 10 years, I think we will have a similar kind of story, but different numbers.

Moderator: The next question is a follow-up from the line of Dhruv Muchhal from HDFC Asset Management Company.

Dhruv Muchhal: What I was earlier looking was the capex number. So, I understand that you have announced few projects and that will continue, I was looking for the capex spend that you are targeting in FY2022, just for my financial purposes. And also the second related question was, this Rs. 350 crore capex that we have, what is the timeline for that, that you announced? As you mentioned for Rs. 500 crore, if you can give it also for the Rs. 350 crore when it could be executed? And if you are comfortable, what are the products that we are targeting?

Sanjay Upadhyay: Any capex that we have done, that's what we have said, from the date of commencement. And cash flow wise if you are asking me, then this year it would be in the range of say Rs. 300 crore to Rs. 400 crore, because not everything is paid upfront. So, that is the cash flow part of it. Otherwise, you know, the analysis what we have already made.

Dhruv Muchhal: The Rs. 350 crore capex for about two years, that could be a right assumption?

Sanjay Upadhyay: Yes.

Moderator: The next question is from the line of Nitin Raheja from Julius Baer.

Nitin Raheja: Maulik and team, congratulations, guys, you have done an incredible job in the last two, three years, which has been a real difficult time. One of the very key things we have noticed is that the entire product portfolio, the way it has been built, has seen over the last three years great sustainability where at the point of time when one business does not do well the other one actually picks up the slack, and vice versa, so on and so forth. So, in that sense, we have really seen how value creation has happened. Just wanted a few thoughts in terms of when one looks at the Company in the next few years going ahead, how do you see yourself sort of evolving from here on after this incredible last three years journey?

Maulik Mehta: See, there are certain things that we have done, which have helped us. We look at new opportunities from an integrated perspective. We target products where we have high degree of confidence in succeeding in, and we take a calibrated approach towards investment in both existing products and the new products. And in all of this, what we see over the next few years, one, as Chairman already mentioned, we see ourselves also adding a significant investment and a position in the solvent space. Other than that, we see a significant increase in the investments that we will make to cater to the life sciences segment. And the third is that products which target the dyes and pigments segments, and what we will ensure that we do is that we have a growing market share in a much faster growing demand CAGR. So, this is what we see as a Company over the next few years.

But if you look at culture of the Company, what we are doing is, we are working very hard towards what we call our "Depend on Deepak" initiative, where we try to map out and we are very honest with ourselves about where we stand on three major stakeholders. One is the employee, two is the customer and three is the investor, we try to understand what it is that is getting us to where we are and what we need to do to enhance their dependability on us, whether it is in terms of performance, in delivery, in values, in mutual growth, all of these things. So, we have internal benchmarks set for us, of what we want to be as a Company for our employees, for our customers, for our investors over the next three to four years. We have taken a target of four years. In the past, in financial performance, we were able to finish our four-year target in three years, hopefully, we will be able to do the same thing with "Depend on Deepak" initiative. But we are going to continue to remain a science driven Company. The investments that we make in R&D, the investments that we make in process intensification, technology, and the investments that we make into ESG, that will continue to drive our outward looking growth. Internally, we have a lot of work to do to be the kind of employer that we dream of being. A lot of companies out there in the space which are phenomenal companies, and we are happy that we are one amongst very esteemed group of them, our goal is, over a period of time to be the most sought-after chemical Company to work with. We are not there, and we are very aware of that, but we are targeting to be there over the next few years.

Moderator: The next question is from the line of Shalu, an individual investor.

Shalu: My question is regarding, what are the margins range we are expecting for the next two, three year?

Sanjay Upadhyay: You are talking about Company as a whole, segment wise?

Shalu: Segment wise.

Sanjay Upadhyay: Every year we improve on our margins, of course, as Maulik was explaining in I think first question itself is that you take a range, which we have been giving. I have said in Fine & Speciality Chemicals segment it would be 37% to 42%, I will still stick to that, no doubt in fine and specialty chemicals because there could be one or two hiccups here and there because of some logistical issues, but otherwise, that is the range. And in basic chemicals, it will be in the range of 30% to 34%. And performance segment in the range of 15% to 20%, though one quarter could be here and there, but that is the range. Phenol, of course, you can't expect this kind of EBITDA margins every quarter, so I cannot commit on that. But otherwise, this is the range you can consider.

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

Ravi Mehta: Just a small clarification, the segmental margins range that you shared, these are EBIT margins or EBITDA margins?

Sanjay Upadhyay: EBITDA margins.

Ravi Mehta: Okay. And one more question was, I am sorry if it's repetitive, the Rs. 300 crore capex for the new products in Deepak Nitrite, this would be commissioned in what timeframe?

Sanjay Upadhyay: As I already said, it takes minimum 18 to 24 months.

Maulik Mehta: I think that's what we should target. Keep in mind, we have announced the projects a couple of months ago but keep the target of timeline in mind.

Moderator: The next question is from the line of Bharat Gupta from Edelweiss Securities.

Bharat Gupta: Congratulations for a good set of results. My question pertains, you have mentioned in your opening remarks that our Company is primarily looking for China-plus-one kind of strategy going ahead. So, are we in talks, like we are present across pharma and agrochemical space, so are we looking out for any opportunity in the CRAMS space as such? Like in terms of intermediate development, like for any particular global innovator.

Maulik Mehta: See, what we do is, when you are talking about CRAMS, what I can tell you is that we are discussing a couple of opportunities where we are talking about a long-term partnership. But when it comes to CRAMS, what you are basically saying is that I will create the house, you come in, tell me which room you want to occupy, so it is almost like a hotel in that sense that, you are basically a tool manufacturer, but your CRAMS sounds like a more attractive word than tools manufacturing. And there are very, very good companies in that space. Deepak today, we are open to that, but today what I can tell you is that we are engaging with certain potential customers for a long-term arrangement. CRAMS, you will see but it is not in our immediate horizon.

Bharat Gupta: But, in terms of our process capabilities, so like we are going into niche chemistry, so is that a targeted area going ahead, like a vision of next three to four years from now?

Maulik Mehta: We have actually a very large number of products that we will be looking at making in the facilities that we are adding. So, it is not like the Deepak Nitrite of old where one plant only focused on making one product, we have learnt at a very high cost the need to be fungible and have the flexibility of product. This is why we have always, in the last few concalls, stressed that this is a platform investment and not a product investment. So, we have several products that we will be looking at producing, what permutation and combination, depends on market forces. So, right now, we don't feel that there is spare capacity to consider CRAMS opportunities. But as and when it comes, it will only be a modular increase in investment. So, we will not be averse to it, but it is not the Company's go-to strategy.

Moderator: The next question is from the line of Vivek Chadha, an individual investor.

Vivek Chadha: My question is on the capex plan which we have announced of Rs. 300 crore. So, what kind of products are we going to target?

Maulik Mehta: I feel like we have responded to this several times. Just for the sake of brevity, we are investing into products that go into life sciences as intermediates. The focus is on products that will target pharma and agro spaces. We are adding new platforms to our existing group of platforms, which are fluorination and photo chlorination. Our existing group of platforms is nitration, dyes rotation, reduction, coupling, etc. So, these are two processes that we are adding to that table. And this Rs.

300 odd crore of investment will be made at the new site that we have acquired in Dahej under the name Deepak Clean Tech, which is a wholly owned subsidiary. So, I hope this summarizes all of your questions in this regard.

Moderator: The next question is a follow-up from the line of Vriddhi D. from Raedan Securities.

Vriddhi D: My question is that 35% of our phenol production is captively used, and with the new investments coming in for phenol and acetone derivatives, are we looking to debottleneck the existing capacities or also building upon the base for phenol?

Maulik Mehta: The goal is to consume 35%. Today, we are not, all the phenol that we manufacture is sold in merchant sales. The goal moving forward is to have the internal capability to consume up to 35% of what we produce. That does not mean that we will not look at debottlenecking and adding as well, which we will. But as a priority, we have chosen to go downstream. Soon, hopefully, we will also take the opportunity to announce the debottlenecking initiatives.

Sanjay Upadhyay: And we are already running at a run rate, of 110% in Q1 FY22 and 115% for last year. So, that continues, in terms of additional production, additional volumes.

Moderator: Thank you. Ladies and gentlemen that 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 taking out time to join us on this earnings conference call. I hope we have adequately answered all your questions. In case you have any further questions, please connect with our IR team, Mr. Somsekhar Nanda. Stay safe and please follow COVID appropriate behavior. Thank you so much.

Maulik Mehta: Thank you. And once again appreciate investor confidence in Deepak Nitrite.

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