"Deepak Nitrite Limited's Q1 FY23 Earnings Conference Call Transcript"

August 10, 2022

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MODERATOR: **MR. RANJIT CIRUMALLA – IIFL SECURITIES LIMITED**

Moderator: Ladies and gentlemen, good day and welcome to the Q1 FY23 earnings conference call of Deepak Nitrite Limited hosted by IIFL Securities Limited. Please note that this conference is being recorded.

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

Ranjit Cirumalla: Thank you, Good afternoon, everyone, and thank you for joining us on Deepak Nitrite's Q1 FY23 earnings conference call. Today, we have with us Mr. Maulik Mehta, Executive Director, and CEO, Mr. Sanjay Upadhyay, Director – Finance and Group CFO and Mr. Somsekhar Nanda, CFO.

We will begin the call with opening remarks from the management team followed by an interactive Q&A session. To begin, Mr. Maulik Mehta, will share his views on the operating performance and the growth plans of the Company, followed by Mr. Sanjay Upadhyay, who shall take us through the financial and segmental performance.

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

Maulik Mehta: Good afternoon, everybody, and a warm welcome to all of you on Deepak Nitrite's Q1 FY23 earnings conference call.

At the outset, let me state that the Company continues to maintain a high level of production at all its facilities while complying to all regulatory mandates, rules, and safety requirements. The health and well-being of our employees and the communities within which we function continues to be of the utmost significance to us.

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

Our business model continues to be tested with various operational and macroeconomic challenges, and I am pleased to report that we have emerged stronger and more confident. Increased capacity from incremental investments and sustained demand from end user industries continue to drive growth, both topline and bottom-line through the Company. The heartening part is, we at DNL, almost 40% of our top line has been contracted and at Phenolics, 20% to 25% of the topline has been in contractual agreements.

Deepak Nitrite has delivered a resilient performance in Q1 to kickoff fiscal 2023 on a positive note. On a consolidated basis, revenues crossed Rs. 2,000 crore, specifically, it was Rs. 2,068 crore up by 35% year-on-year and 10% quarter-on-quarter. This was achieved despite the Nandesari unit of Deepak Nitrite being unavailable for a meaningful part of the quarter owing to fire at one of its warehouses. The Company exhibited sustained topline performance despite several other challenges, such as the considerable inflation in raw material prices and challenges to their availability as well as elevated utility and transport costs.

In Q1 FY23, EBITDA stood at Rs. 366 crore translating to an EBITDA margin of 18%. There was a one-off impact from the fire incident, it must be appreciated that we are functioning in a highly dynamic environment with fluctuating crude oil prices, shutdowns of plants in Europe and China, as well as sharp fluctuations in input prices, as well as forex rates.

Deepak remained highly competitive in the global and the domestic markets, we continue to take several initiatives to lower overall costs and improve manufacturing efficiencies in order to structurally elevate profitability. On the operational front, our domestic business revenues stood at Rs. 1,687 crore in Q1, higher by 46% year-on-year. Export revenues came in at Rs. 371 crore in Q1. On a consolidated level, domestic to export mix stood at 82:18. Our focus on domestic business has to be viewed in the light of high cost and constrained availability of shipping vessels/ containers, congestion at ports and some revisions in protocols at China and Europe due to surges in COVID cases.

With respect to segmental performance. Revenues in Advanced Intermediates segment increased by 39% to Rs. 739 crore. In addition to substantial inflation in key input prices, there was extreme exchange rate volatility. Amid global trade volatility, Deepak delivered robust growth for key products, profitability lagged below sales growth due to two factors, increased commodity prices and a lag in passing on price increases to customers as per contractual agreements. As this normalizes further, margins are expected to improve in the following quarters.

Deepak Phenolics delivered a remarkable quarter with revenue soaring by 33% to Rs. 1,338 crore in Q1. In a notable accomplishment, the plant recorded a high average plant utilization rate, both the commissioning of the CPP and its stabilization, we were able to avoid several incidences of potential plant stoppage, which would have occurred due to power failures in the edge industrial areas. In the backdrop of an unstable macroeconomic environment, DPL was able to provide a robust topline performance driven by volume growth and maintaining the customer's wallet across key products of phenol, acetone, and IPA. Margins were impacted due to normalizing realizations of joint product acetone in relation to the prior period, where pricing was exceptionally high with regards to margin over material. The demand trend continues to be strong in the Indian sub-context, and the Company is well positioned to realize incremental gains in the segment over a period of time through downstream integrations with phenol and acetone derivatives.

As we have already explained to you, we are at various stages of project implementation, out of the projects that we have announced of Rs. 1,500 crore, which we will start seeing coming in phased manner over the next 15 months. In addition, three products are in the engineering phase, which means they are past the piloting phase, which will be downstream products or something that DNL and DPL make. They will service the pharma segment; these import substitutes involve a challenging gas liquid reaction and are expected to yield 20% to 30% EBITDA with both Indian and non-Indian anchor customers.

These products are further expected to bring both topline and bottom-line. We will come back to you with more details about these products at an appropriate time. We must mention here in a key development, the Company is increasing its capacity for in-house waste treatment as being part of projects under implementation and is expected to result in a decrease in its footprint. It is also going to be increasing its ability to backward integrate, so that it is de-risking its own supply chain.

Looking forward, we foresee strong growth for India over the medium to long-term due to the rising market demand on a global scale. The business is well poised to capitalize on an increasing import substitution trend across the nation. We will be able to take advantage of this trend attributable to a promising pipeline of products, which also includes solvents like MIBK and MIBC amongst others, which have already been approved.

During the quarter, our teams once again performed splendidly in the midst of a challenging environment, enabling us to maintain our performance momentum. The combination of factors is probably as extreme as I had witnessed so far. And there is always this question about different engines of Deepak operating at any given time which boosts our bottom-line numbers.

But in Q1, we had none of our primary engines firing. So, this is what we would look at as a pretty challenging situation, which we expect to be very short-term. It has leveraged its manufacturing expertise, world-class facilities, and flexible operation to deliver an efficient performance. This was backed by a robust balance sheet, and I am proud to announce significant investments to accelerate our growing trajectory.

In conclusion, I would like to emphasize that DNL is well positioned for expansion in a range of aspects. Apart from a noticeable shift in the chemical supply chain from China to other countries including India. Deepak has the ability to take advantage of the opportunity and its long presence in value chain. The Company is an excellent candidate to be one of the leaders of the India chemical manufacturing trend, thanks to its unique product mix and decades of manufacturing experience. This along with contributions from our expansion plans will improve our competitiveness and position us to grow market share and generate value for all stakeholders.

Following the recent unfortunate incident of the fire at warehouse in Nandesari, one of our manufacturing sites, all the plants are running at capacity as per permission given by statutory bodies as of July 2022, except sodium nitrite and nitrate, which is currently operating at about 50% capacity. This will move up to 75% by mid-September and is expected to be back to full scale operations by October.

We have always adhered to stringent safety measures, and we regularly conduct audits at facilities. Despite these vigorous practices, these incidents clearly indicate the challenges prevalent in manufacturing and storing hazardous products and inputs, and also the high standards-of-care required in handling such materials. We pride ourselves on a commendable safety record, and we will work to further tighten our processes and protocols wherever possible.

Those of you who participated in our virtual AGM on the 3rd of August, 2022 would be aware of the new directors being appointed to guide us through the next wave of growth. In management changes, Mr. Sanjay Upadhyay, who served as CFO of DNL has now been elevated to Group CFO. Mr. Upadhyay will now address this forum and take you through the financial performance. Mr. Somsekhar Nanda, who is also on the call has been designated as Chief Financial Officer for Deepak Nitrite Limited.

Sanjay Upadhyay: Thank you, Maulik. Good afternoon, everyone, and thank you for joining us today on Deepak Nitrite's earnings call. I will walk you through the highlights of the financial results for the quarter ended June 30, 2022.

Before we start discussing the financial numbers, a key development to share with you is the reclassification of business segments, as the businesses have undergone a lot of changes over a period of time, thereby inter-dependence of processes and products has increased, hence due to the increasing number of facilities catering to multi-products, integrated production processes in similar economic characteristics of products and business scenario, the Company and the Chief Operating Decision Maker reviews our group performance in two business segments and distributes research based on the value generated by these segments. Due to this mergers of SBUs, the Group's operations are now reported as the two business segments, Advanced Intermediates and Phenolics in accordance with Ind AS 108.

Coming to the business performance. In Q1 FY23, Deepak performed impressively during the quarter despite a challenging macro environment, such as escalating expenditures and persistent volatility in prices of major feedstock. Foreign exchange rates, as that also was very volatile during the quarter. On a consolidated basis, revenues grew by 35% to Rs. 2,068 crore during the quarter under review. EBITDA was Rs. 366 crore, down by 20%. Given the normalizing spread across the key products combined with inflationary pressures, as well as some operational and logistical challenges, the margin has undoubtedly faced pressure with the Company reporting an EBITDA margin of 18% during the quarter. PBT and PAT decreased by 22% to Rs. 315 crore and Rs. 235 crore respectively. Key raw material prices continued to rise significantly, which had an influence on the profitability dynamics. For example, the operations were affected by an increase in toluene costs of 72% and rise in nitric acid of 142% totaling to Rs. 16 crore and Rs. 19 crore respectively. However, we have a formula-based pricing, and these costs are passed on, but there will be some lag somewhere.

Due to the fire at Nandesari facility, the Company has estimated and recognized an initial loss of Rs. 47 crore on account of damage to certain property, plant and equipment and inventory, and has conservatively recognized insurance claim receivable to the extent of our unfortunate losses. Further, the Company is in process of determining final payment of reinstatement of assets based on about an estimated cost. The aforementioned losses and corresponding credit arising from insurance claim receivables have been presented on net basis (Nil) under exceptional items with the results for the quarter ended June 30, 2022.

Moving to the segmental performance. As mentioned earlier, our strategic business units have been merged in accordance with Ind AS 108 due to this merger, the Group's operations are now reported in the two business segments, Advanced Intermediates and Phenolics.

In the Advanced Intermediates segment, revenue has increased by 39% to Rs. 739 crore in Q1 FY23 versus Rs. 532 crore in Q1 FY22, while EBITDA marginally grew by 2% to Rs. 149 crore during the quarter under review, despite the current environment and challenging circumstances.

Deepak Phenolics delivered a strong performance with revenue soaring by 33% to Rs. 1,338 crore in Q1 versus Rs. 1,003 crore in Q1 FY22. While EBITDA stood at Rs. 217 crore and EBITDA margin came in at 16%. Robust demand and high plant utilization helped revenue realization to both phenol and acetone to increase over the previous year. The Company has been able to take advantage of whatever demand pertains for both the products.

During the quarter, currency rate was highly volatile, fluctuating by 5.33% highest being 79 and lowest being 75. In order to lower the risk of foreign exchange volatility, the Company uses dynamic hedging measures, which resulted in exchanged gain of Rs. 2 crore. The Company invested the remainder of its capital in safe and secure instruments like liquid mutual funds and used its excess to advance payments to a few chosen suppliers, earning a cash discount in the process. This resulted in an intake of Rs. 5.09 crore during the quarter.

Lastly on the balance sheet front, the Company's financial position has significantly enhanced, and it remains a zero-debt Company. In addition, the Company achieved ROCE of 44% in Q1 FY23, its net worth stood at Rs. 3,573 crore. This sound value of net worth is expected to facilitate leveraging of balance sheet or further expansion in the future.

With that, I would now request the moderator to open the forum for questions-and-answers, please.

Moderator: The first question is from the line of Nirav Jimudia from Anvil Research.

Nirav Jimudia: I have two questions. So, one is the initial remarks, you have mentioned that we have been setting up the MIBK capacity, and I presume MIBC is a forward integration of MIBK. So, in the AGM you have reiterated that we are planning to put up something around 40,000 tons of MIBK capacity. But if you can share your views in terms of how much we are planning to put up the capacities of MIBC? And when these projects are going to get commissioned?

Along with it, if you can also share that since we have announced almost Rs. 700 crore of capex for Phenolics, how much these projects would take care of out of our total capex of Rs. 700 crore, because let us say if this consumes let us say 50% of our total announced capex, are there further products, which would be a part of this Rs. 700 crore or this would exhaust our Rs. 700 crore capex limit? So, this is question one.

Maulik Mehta: What is Rs. 700 crore?

Nirav Jimudia: You have mentioned in the annual report, that we are planning to invest Rs. 700 crore for the Phenolics, for the solvents.

Sanjay Upadhyay: So, we are investing Rs. 700 crore for solvents in Phenolics, MIBC out of this, to answer your question is 8,000 tons. Now the Rs. 700 crore comprising of the MIBK, MIBC and other solvents also, okay. Breakup would be difficult to give, because it is set up on the new site and it includes infrastructure also. When you see certain capex, it covers the infrastructure cost also. So, in totality, we are spending Rs. 700 crore for this.

Nirav Jimudia: Okay, got it. And when these projects would be commissioned? So, would it be next year we will get the benefits of this projects getting commissioned or would it be in the year after that?

Maulik Mehta: So, as I have mentioned in the opening remarks, all the capex is that we have already announced, that includes MIBK, MIBC. They will be commissioned in a phased manner between now and the next 15 months.

Nirav Jimudia: Okay. And a small clarification on this capacity. So, our press release also says that we have been investing almost Rs. 210 crore in Deepak Chem Tech, so is this for the hydrogenation facility which we were earlier talking about?

Sanjay Upadhyay: Actually, Deepak Chem Tech is a vehicle, it is SPV and a subsidiary of Deepak Nitrite, wherein the investments are done including all this. This is just the capital infusion by Deepak Nitrite for these projects.

Nirav Jimudia: Got it. My second question is, if we see last three years, we have invested close to Rs. 820 crore in the business from 2020 to 2022. So, some of them is already there, the benefits also, we have started getting in terms of the IPA and the captive power plant of 29 megawatts. But let us say, if you can share it, out of this Rs. 820 crore, if we exclude this IPA and CPP, we would have invested something for the Brownfield expansion for our standalone businesses. So, how much of this benefit of this balance capex where we have done for the Brownfield expansion has already accrued and how much it would be accrued over next one or two years, considering an asset turnover of 2x, which we have mentioned earlier in our calls for our Brownfield expansions?

Maulik Mehta: So, in Deepak Nitrite, the Brownfield expansions were not included in the total capex amount that we have shared. Those are done as a matter of process, and we do not get into a discussion about the capex amounts and the volumes. We retain our ability to be world-class supplier. So, as our demand grows, we maintain our wallet share and trying to see how we can get more wallet share. So, any brownfield expansion that Deepak Nitrite is doing is in addition to this.

Nirav Jimudia: Okay. So, but let us say, if we exclude the IPA and the captive power projects, where was this balance amount being spend into? If you can give some understanding. That would be very helpful.

Maulik Mehta: So, there was land that was about a Rs. 150 crore that was spent. As mentioned earlier, between the captive power plant and the IPA, we spent a total of about Rs. 300 crore. And there were other which were Brownfield which have been mostly in Deepak Nitrite, which have had something between about Rs. 80 crore to Rs. 100 crore. And there is always incremental capex that is in Deepak Phenolics to maintain a high degree of operational throughputs.

Nirav Jimudia: Okay. Last question, if you may allow me. We have also mentioned in the AGM, that we are going to increase our Phenolics capacity by 25% probably which will come up in next year. So, is it safe to assume that probably the cost of these debottlenecking would be equal to the depreciation, what we have been incurring on a yearly basis, or the cost could be slightly higher than that?

Sanjay Upadhyay: I mean, there is no correlation between depreciation and the investment.

Nirav Jimudia: Yes. What I was trying to gauge is, in terms of how much capex we are trying too, because our annual depreciation is anywhere between Rs. 180 crore to Rs. 200 crore. I was just trying to get an understanding about the amount.

Sanjay Upadhyay: Yes. It was lower near Rs. 180 crore to Rs. 200 crore. So, do not worry on that, okay.

Nirav Jimudia: So, is it safe to assume that the amount would be lesser than that?

Sanjay Upadhyay: Yes.

Moderator: The next question is from the line of Levin Shah from ValueQuest Investment Advisors.

Levin Shah: My question is, so we have put in the presentation as well that the input cost for a lot of our raw materials that have gone up substantially. And now how do we see this situation post Q1? And whatever the cost pass-through that we would have done, do we see that for rest of the year, the margins would improve from here on?

Maulik Mehta: So, the largest raw material purchases that we make as a group are into petrochemical, benzene, toluene, propylene, and those saw a significant spike in Q1. They have reached numbers, which I mean in recent memory, they have never reached. And they have already started to soften in line with prices of crude that we see. So, while there is a pass-through, we will start to see some benefits of that moving forward. But anyways, the margin hopefully will start to strengthen in the near to medium-term, because we are seeing a decrease in the price of raw materials.

In Deepak Nitrite on a standalone basis, we also consume a large amount of ammonia and nitric acid which is based on ammonia. This has just as much seen a significant spike along with caustic prices. And I think that this is not expected to be long-term situation. This is current mismatch between supply and demand, which is expected to normalize over a period of time.

Nonetheless, the Company is also taking various steps to ensure that over a period of time, it increases its ability to have some level of self-sufficiency, and customers has been very, very supportive in that sense. So, we have not really lost market share despite these high and temporary increases in raw materials. We continue to be key suppliers to all of our customers in these downstreams.

Levin Shah: My second question is on phenol. So, at the AGM, we had mentioned that our capacity now stands at around 250,000 tons, and we are planning to expand this capacity further, so what could be the quantum of expansion and the kind of capex that we would be spending on it?

Maulik Mehta: Right. So, this was already asked basically, while the capacity does stand at like what, 250,000, this is part of the process, our original capacity was less than that and taking it to 250,000 and then further on adding maybe about 15,000 to 20,000 over and above that will be done in short course. And maybe over the next quarter or two quarters, any further increase will be done over a period of the next year or so. You are right, so the target by perhaps the end of FY24 to be about 50% over the original plant capacity of 200,000.

Levin Shah: And the capex on this, since it is a brownfield expansion would be not that significant?

Maulik Mehta: Not a lot at all.

Moderator: The next question is from the line of Isha Agarwal from VT Capital.

Isha Agarwal: So, my question is since we are projecting that the prices of raw materials may soften from here on. So, do we see the risk of inventory loss? And also, how do we procure our inventory, like for how many days do we keep the inventory of raw materials?

Maulik Mehta: This is dependent on products and dependent on how we see the macroeconomic environment shaping up. For example, when the prices of raw materials were low, we targeted every external tanks that we could, in order to carry high levels of inventory of raw materials. In such an environment where the raw materials are high, but coming down, then the goal is to see how little expensive raw material you can carry, because you are expecting it to be much better.

Now, this is true, whether it is Deepak Nitrite or Deepak Phenolics, and what I can also share is that while prices for petrochemicals are coming down, ammonia, nitric acid, caustic lye, which are large consumptions, they remain at multi-year highs. I mean, before prices start to come down, you have to start seeing prices plateau. This is what we are starting to look at, we have to see how the environment develops.

Isha Agarwal: Do we see any possibilities of inventory losses from here on?

Sanjay Upadhyay: No, we do not see any losses.

Isha Agarwal: Okay. My third question is, can you please help me understand the industry for the solvents like particularly the products that we are entering into, the MIBK and MIBC, so what is the demand and what is the growth that we can project from here?

Maulik Mehta: The demand is significant, and it will continue to grow because the world over, phenol and acetone are largely consumed as feedstocks in solvents. In India, which is a unique situation, phenol and acetone are consumed in segments like things like pharma, laminates and construction and those things. And that also means that all of these solvents are currently imported into India. So, the import volumes are significant. What we are looking at putting up 40,000 odd tons capacity with 8,000 tons of MIBC will very easily be consumed by the Indian demand. And over a period of time, like we did with phenol, we would see how we can look at debottlenecking.

So, we genuinely see no problem in supporting the Indian customers also along with the fact that there are no other domestic manufacturers of the same. And this is for MIBK, MIBC, even the other solvents that we are looking into as downstreams of phenol and acetone are actually entirely imported today with, I think 5% to 10% growth CAGR expected in consumption.

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

Rohan Gupta: So, couple of questions. First is on our capex, which you have talked about a little bit in our AGM in polycarbonate that is a forward integration in phenol. So, just want to understand that how much you think that there is a further investment opportunity in polycarbonate or even some more phenol derivatives which we have been talking about. So, definitely, the advanced plant you have already announced. But what I want to understand that how much investment potential we see over next 4 quarters to 6 quarters or 8 quarters we can put in this phenol derivatives, including polycarbonate?

Maulik Mehta: See, polycarbonates today, there is currently an import of about 2 lakh tons into India. And this is expected to grow. As I mentioned, Rohan, world over, phenol and acetone are largely consumed into the polycarbonate segment, but India imports always polycarbonate. So, over a period of time, over the next few years, having a meaningful presence in India to cater to domestic demand would have, I think roughly about between Rs. 5,000 crore to Rs. 7,000 crore as a total expected investment over a few years.

And I think this kind of consumption, which is currently standing at about 2 lakh tons, we expect it to become stronger because of a lot of Government initiatives also that are taking place. And also, frankly, because polycarbonates are generally linked to growth in GDP of a country. So, as we go from developing to a middle-income country, we will see an increased consumption of this domestically anyways.

Rohan Gupta: How much capacity we are initially planning for polycarbonate?

Sanjay Upadhyay: 200,000 tonnes.

Maulik Mehta: We would not get into the capacity that I am just sharing with you what currently India's import is. See, this is something that is not going to happen as an investment and commissioning overnight. So, while we are speaking with technology providers, while we are working internally also to see what we can fine-tune, we will see how the growth trend is in India. So, we will right size our plants. And we made this mistake when we put up phenol, because when we put up the plant expecting a CAGR of 6%, 7%, 8%, which was what consultants told us, we estimated that at 2 lakh tons, we would be roughly about 65% of the domestic consumption.

Now today at 2.5 lakh tons, we have 55% of the domestic consumption. So, this, call it, ensuring that we take the right opportunity at the right time or call it good luck or bad planning or whatever. But we have learned not to go with an assumption of growth, especially when growth is picking up because of various interventions, in India and worldwide. So, we will ensure that we put up world-class facilities, looking at the current demand of 2 lakh tons moving forward, we see how this grows and then we have the right capacity.

Rohan Gupta: And, some clarification what you mentioned, the Rs. 5,000 crore to Rs. 7,000 crore kind of investment is only related to polycarbonate which can happen, or you are talking about complete downstream of phenol?

Sanjay Upadhyay: Rohan, that is what I was trying to explain, this should not be seen in isolation. So, that is a potential investment what we can have. Polycarbonate will again be a total downstream what we are talking. That has been our strategy, and we have been discussing about this for quite some time. So, phenol downstream going up to polycarbonate, this is how we will grow. So, then obviously all these things will require around Rs. 6,500 crore to Rs. 7,000 crore based on current estimation.

Maulik Mehta: Right. And also, I will just add to that, that Deepak looks at making as many of its sites working as possible. So, there will be plenty of avenues in this investment to start manufacturing products, which may be part of the chain, but may not necessarily go into polycarbonates at intermediate levels. This also does not include investments that

Deepak Nitrite will be making for its own products. So, there is a good pipeline of products and good opportunity for Nitrite, Phenolics, and other subsidiaries to grow.

Rohan Gupta: Okay. Also a little bit more about your MIBK and MIBC, you mentioned that actually you are planning 8,000 tons kind of capacity usually to start with. And if you can give some sense on the entire Indian market and also the industrial market?

Maulik Mehta: 8,000 tons of MIBC and 40,000 tons or so of MIBK.

Rohan Gupta: Okay. And this is only going to like if I am looking at the Indian market and what kind of size and potential and also are we looking at export opportunities in this?

Maulik Mehta: Yes. We look at all opportunities, but primarily, we are seeing a high degree of import substitution here now. So, this is the current Indian requirement. And as and when I mean, see, last 2 years, we have also taken opportunity to export phenol when we felt that there was value in doing that. So, it is not like we are averse to it, but we already see a local and present opportunity.

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

Saurabh Kapadia: In the initial remarks, you mentioned about 3 products. So, just can you give more color in terms of end user industry and whether those products will be manufactured in the existing setup or in the new setup?

Maulik Mehta: Yes. So, these are products which are downstreams of Deepak Nitrite's existing products and Deepak Phenolics' existing products. They will be manufactured in sites that we already have, including the newly acquired site Dahej. They are largely catering to the pharma segment. And they are I mean; they utilize this very technically challenging gas-liquid reaction as compared to the other standard processes that are there everywhere else in the world. So, they are highly efficient, very low footprint in terms of energy and water cost and very, very efficient in terms of any byproduct that is generated. Over and above this, as I mentioned, we are targeting something like between 20% to 30% EBITDA. And these are import substitute products.

Saurabh Kapadia: Okay. So, are this a contractual product and we are a second supplier, something like?

Maulik Mehta: These, we will have anchor customers. We would not get into discussions right now about contractual agreements and this, that, but we will have anchor customers.

Saurabh Kapadia: Okay. The second question is on our other expansion on the chlorination, photo chlorination side. So, if you can provide some more color in terms of the products and maybe at R&D stage and also on the plant commissioning timeline?

Maulik Mehta: Yes. Sure. So, to answer your last question first, the plant commissioning will be over the next 15 months. But it will be less than that. I think for these plants, it will be over the next 10 months or so. Nonetheless, with regards to products that we are getting out first, these are products where there is already an existing market, including Deepak Nitrite. So, part of it will be self-consumed and part of it will be sold outside. And this is actually, photochlorination, the way that we are doing it is an extremely tricky and challenging process, which requires a very high degree of technical competence.

Along with that, we have also the fluorination setups that we are putting in, these are what you would call up-engineered setups. So, while they can manufacture the base products that we are tying up immediately, they also have the capability to manufacture far more complex molecules, which require very different environment, whether it is in kind of pressure or temperature or material construction. So, between these and unit processes that we are putting up in Dahej, whether it is processes like diazotization or nitration or reduction, which we are already competent in, there are actually a range of molecules that we are getting into by considering these platform technologies.

So, we have made these plants relatively multipurpose. We are starting off by consuming partially the output as well as selling it in the market. And we are working with customers in order to supply them smaller, higher value of intermediates using these plant processes.

Saurabh Kapadia: Okay. Just last clarification on the insurance claims side. So, have we accounted anything, a loss of any amount in the current quarter?

Sanjay Upadhyay: No, we have not.

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

Rohit Nagraj: First question is in terms of the new segment, Advanced Intermediates, is it possible for us to give what were the volume growth on a year-on-year basis?

Sanjay Upadhyay: Actually, this is not a new segment. This all, we had 3 segments, but it was creating a lot of confusion because our products are such that it is fine. It is a lot of integrated products, and the chemistries are similar. So, over a period of time, the plants are also multi-product plants. So, it was creating all kinds of confusion, so we have merged all these segments into one segment, which is called Advanced Intermediates.

Rohit Nagraj: Right. Just wanted to know, out of this 33% year-on-year growth on the aggregated segment, what was the volume growth on a year-on-year basis, if possible?

Maulik Mehta: Volume growth would not have been substantial in Q1. Maybe.

Sanjay Upadhyay: Q1, there was an incident of fire. So, I mean our top line certainly has grown. But I mean, for this quarter, we were impacted because of the fire incident.

Maulik Mehta: Yes. So, one of our largest sites was not operational for pretty much the entirety of 1 month.

Sanjay Upadhyay: We have some impact of fire because Nitrite is not running at full capacity as Maulik explained in his speech.

Rohit Nagraj: Right, right. So, effectively, the entire growth has come because of the pricing, which has improved over the last 1 year?

Maulik Mehta: Pretty much.

Sanjay Upadhyay: Yes.

Rohit Nagraj: The second question is just again harping on the project. So, we have indicated Rs. 1,500 crore projects over FY23 and FY24, out of which you have already explained Rs. 700 crore in Deepak Phenolics for solvents, about Rs. 200 crore in Deepak Clean Tech, which has already been invested. And so out of the rest, say, Rs. 600 crore, where this will go? I mean, partly, it will go into brownfield expansion of Deepak Phenolics. And what will be the other part, which will go into other segments, sub-segments?

Sanjay Upadhyay: It has various capex in that. One is brownfield, of course, then debottlenecking of Deepak Phenolics. It is the backward integration of the Deepak Nitrite of the products. There are some debottlenecking capacity expansions. And as explained in our speech, we are getting value out of waste, there is a capex on that also. So, it compares several capex, which will be incurred from next quarter, so maybe quarter after that, you will start seeing the numbers and results of each one delivering on whatever we have said, the bottom line on this, you will see from Q3 onwards. Each quarter, we will have some project commissioned, they are out of this Rs. 1,500 crore.

Rohit Nagraj: Right. Got it. Just one clarification, in the initial remarks, you mentioned in Phenolics, 20%, 25% of volumes are contracted, and in other businesses, 40% of volumes are contracted. Is that right?

Sanjay Upadhyay: Right.

Maulik Mehta: In terms of Nitrite about 40%.

Sanjay Upadhyay: Because when you say volume, it comprises of several products. So, it is a value which has contracted top line.

Rohit Nagraj: So, it is on value basis?

Sanjay Upadhyay: Yes.

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

Meet Vora: So, just 2, 3 clarifications. One is, we are saying that we are proposing to add new capacities of our key raw materials. So, which raw materials are these and whether they will be in Phenolics or they will be in Nitrite?

Maulik Mehta: We do not go into those details. What I said is that we are ensuring that between upstream integration and downstream integration, we have investments, as I mentioned in both, where we will be looking at de-risking part of our supply. So, we continue to be present in the market as customers and we see what we can do to de-risk ourselves internally as well.

Meet Vora: Sure. And on the brownfield expansion of select products, these will be phenol, acetone, 25%, which we are saying, or they are also in our Nitrite section as well as in sodium nitrite, sodium nitrate?

Maulik Mehta: Yes, both.

Sanjay Upadhyay: It is in sodium nitrite also.

Meet Vora: Okay. And one last question since you are seeing that our sodium nitrite and nitrate capacities are operating at 50% capacity right now. I believe the downstream of this might be going in our fine & specialty or your classification. So, is that segment as well affected and that will also see a gradual ramp up in next 2 quarters, 3 quarters, how does this go?

Sanjay Upadhyay: So, that other segments will not be impacted, we will ensure that other segments run as per the requirement and as per the capacity. That would not be affected.

Moderator: The next question is from the line of Krishan Parwani from JM Financial.

Krishan Parwani: I have 2 questions. So, one is that you need roughly about 8,000 tons of MIBK for 8,000 tons of MIBC more or less. So, external, MIBK could be 30,000 tons. Is that right?

Maulik Mehta: MIBK is 40,000 tons, MIBC is 8,000 tons.

Krishan Parwani: So, these are all external sales you are saying?

Somsekhar Nanda: It is a capacity build up. And as Mr. Upadhyay and Mr. Maulik said, these are all import substitute products. So, they will be all merchant sales**.**

Krishan Parwani: No, I meant is that to make 8,000 tons of MIBC, you would need 8,000 tons of MIBK.

Sanjay Upadhyay: Yes, correct.

Krishan Parwani: Say if your capacity is 40,000 tons of MIBK, then external sales at, let us say, 100% utilization could be 32,000 tons for MIBK. Is that correct?

Maulik Mehta: Yes. Correct.

Krishan Parwani: Okay. Fair enough. And the second question is on the other products in that Phenolics chain. Are you also planning DA and Hexylene Glycol and what about BP and Cyclohexanone?

Maulik Mehta: So, until we tie everything up and we announce it, it would not be prudent for us to discuss specifics about products, which have not yet been announced.

Krishan Parwani: So, just to follow up on that. So, whatever Rs. 700 crore capex that you are mentioning would be coming over, let us say, next 15 months. So, the other products are not part of this capex or are they part of this Rs. 700 crore?

Sanjay Upadhyay: Beyond what we are saying is not a part of this capex because we have already said what our capex is already and it is lined up.

Moderator: The next question is from the line of Nikunj Somani from Fortune Capital.

Nikunj Somani: Yes. I have two, three questions. First, my question is about the market size of phenol and how it is growing?

Maulik Mehta: Okay. So, there is a separate answer to that with regards to India and a separate answer with that with regards to the world. So, in India, which is largely dictated by end segments like construction, infrastructure, pharma, auto, there is certainly the visibility of reasonable demand resurgence, because the last couple of years were more uncertain with things like COVID and global uncertainties, but in India, by and large, there is generally a slightly improved temperament.

That said, worldwide, there is because of what is happening in Europe, for example, intermittent COVID outbreaks in China, there is certainly a disturbance that is taking place. Now it cannot just be handled by what happens in India because there is a significant import as well. So, as there is a gap sometimes where the producer, the production capacity, the effective production capacity is more than the effective consumption, you will have prices that may be on a declining trend for a period of time. But if you see that there is a higher demand than production because of, again, a mismatch, then you will see an increase in price trend.

And one way or another, this will come to India. It is certainly a little bit mitigated because of things like the dollar-rupee hedge or the amount of time that it takes to travel from wherever in the world to India, all of those things. Those are the areas where Deepak, along with its operational expertise is able to take advantage of. Nonetheless, this is one of those points where we are seeing such volatility globally that whatever answer I give you right now may turn out to be absolutely not true just two weeks from now.

Nikunj Somani: My second question is about how you choose your new products? And what is your new product line up other than that you announced?

Maulik Mehta: Let us start with the ones that I announced.

Nikunj Somani: Yes.

Maulik Mehta: So, we are seeing from both Deepak Nitrite, Deepak Phenolics, an opportunity to go both upstream and downstream, which we are exercising. We have announced already Rs. 1,500 crore of ongoing projects. In addition, we have also today announced that we are on the engineering stage of molecules that will be consumed in the pharma space, import substitutes and which will have a 20% to 30% EBITDA. Any more on this, whether it is with regards to capex, topline and all of those things, it is slightly premature, but we will definitely get back to you at the right time.

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

Deepak Mehta: Congratulations on the great set of numbers. So, due to this European energy crisis, do you see any benefits for our Company in the short-term and long-term? And if there is any demand shift from Europe to India and it is getting benefited for our Company's production and demand.

Maulik Mehta: See, that is a very affirmative question. And if I am being very honest, while there are opportunities, there are certain things about Europe, which one has to appreciate that while energy costs are extremely high, they are also facing a severe drought situation, which is making it difficult to move products within Europe through its existing waterways. Over and above that, there is, generally speaking, an expectation that this will at least continue over the next 3 months to 5 months because of its own energy crisis.

So, while one can construe opportunity, a lot of this in the short-term, it is prudent to take advantage when advantage is there, but not expected that this means that tomorrow, the European chemical industry is down. No, it has its own challenges. It is doing its best to work through them. As and when there are opportunities, we certainly are seeing an increase in inquiries. And we will play our cards right from that perspective to ensure that we take the best value both for the existing markets that we have over and above that, if there is any additional demand coming from customers who would otherwise have consumed European feedstock.

But you also have to keep in mind that if European feedstock has affected so many European consumption. At the moment, we are continuing to see satisfactory commentary coming from our customers even in Europe, but it is a dynamic situation. As of right now, we will continue to feel encouraged, but it is a wait and watch.

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

Shubham Ajmera: Do we have any update on the QIP, like when we are planning to raise the money and in the segment in which we will be utilizing this money?

Maulik Mehta: QIP, we just have an enabling resolution, because of the market conditions, we will launch as and when required. Frankly, today it is not required. And today, I mean market conditions are also not very favorable. So, we will have to wait for some time.

Shubham Ajmera: Okay. And my second question is on the exceptional line items in our P&L during Q1. So, is my understanding right that we booked a loss due to fire of Rs. 47.20 crore in exceptional item and we also recognized the income with the same amount. So, our net impact is nil in the exceptional item?

Maulik Mehta: That is the right understanding you have.

Sanjay Upadhyay: We have booked to the extent what we have written off as a part of insurance claim. Our claim is on, reinstate that value, as well as we have got a LOP policy also, but that is not yet recognized. As and when claim progresses or is there any further development, we will see what to do.

Shubham Ajmera: So, I think the CorVel insurance Company is still ongoing. So, have you received any confirmation for this Rs. 47.20 crore as well like since we have recorded this an income as well?

Sanjay Upadhyay: Of course, I mean confirmation in the sense that there is a policy existing, it is a contractual business, survey is already going on. So, based on whatever information, LOPs we have, we have booked the income.

Moderator: We will take one last question, which is a follow up question from the line of Rohan Gupta from Edelweiss.

Rohan Gupta: Yes. Just a couple of varying questions. One is on the current spread, we have seen that the phenol prices have continued to come down while the benzene has not started correcting. I think that in June, there was a significant pressure on margins. Do you see that this may impact our phenol business profitability in Q2 and in the near-term?

Sanjay Upadhyay: Rohan, can I ask you to get in touch with Mr. Somsekhar Nanda, he will explain to you separately.

Rohan Gupta: Okay. Just second question.

Sanjay Upadhyay: For the second question, you can further ask Mr. Nanda, that would be better.

Rohan Gupta: Okay.

Somsekhar Nanda: Right, Rohan. Thanks. And I will be in touch with you.

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

Sanjay Upadhyay: Thank you all for joining this call. For any further questions on this, you can address this to our investor communications team or Mr. Somsekhar Nanda, they will be answering whatever questions you have and clarify. Thank you so much.
