



Deepak Nitrite Limited

Q3 & 9M FY22 Earnings Conference Call Transcript January 27, 2022

Moderator: Ladies and gentlemen good day and welcome to Deepak Nitrite Limited's Q3 & 9M FY22 Earnings Conference Call. As a reminder, all participants' 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 the operator by pressing '*' then '0' on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Nishid Solanki from CDR India. Thank you and over to you, sir.

Nishid Solanki: Thank you. Good afternoon, everyone and thank you for joining us on Deepak Nitrite's Q3 & 9M FY22 Earnings Conference Call. We have with us today 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 results presentation shared with you earlier.

To begin, Mr. Maulik Mehta will share his views on the operating performance and 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 on the stock exchanges.

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

Maulik Mehta: Good afternoon, everyone, and a warm welcome to you on Deepak Nitrite's Q3 & 9M FY22 Earnings Conference Call. I hope everybody is safe and are taking due precautions whether they are working from home or from their offices or in transit.

I trust you've had the opportunity to go through our results documents, that were shared earlier. I will begin by taking you through the key financial and operational highlights for the period ended December 31st, 2021, and key developments and strategic approach for the coming year. Mr. Upadhyay will then present you with financial overview during the period in review. Following that, we will be happy to answer any questions on the open forum.

We are currently witnessing the third wave of the pandemic in India, but fortunately the human impact of the same has not been as severe as the previous waves in terms of fatalities and casualties. Additionally, we continue to take precautions at our facilities and offices to ensure safety and wellbeing of all of our employees and contract workers. Some of the issues that played out in the second quarter had some amount of lingering effect in the third quarter as well, especially issues like soaring raw materials costs, logistics and supply chain challenges, high costs of fuels like gas, furnace oil, especially also coal. However, we see strong demand coming up across segments.

Despite this challenging backdrop, the Company achieved its highest ever quarterly top-line performance, both on standalone and on consolidated basis. Notwithstanding the tumultuous input material condition, particularly with regards to higher raw material costs, spiking utility costs and availability of key raw materials, the Company efficiently executed its operating schedule and fulfilled a large part of its supply commitments to ensure reliable and stable supplies to key customers. Deepak Nitrite has been able to pass on hikes on raw material prices to consumers wherever strategically feasible. Overall, we anticipate the demand to continue to stay robust given that several industries are getting back to pre-COVID production levels and fundamentally there is a shift in supply chain to countries including India. Deepak Nitrite's wallet share amongst all customers' strategic and non-strategic remains robust and on the growing trend.

Demonstrating the resilience in our business model, in 9M FY22, our revenue increased by 71% to almost Rs. 5,000 crore while PAT grew by 65% to almost Rs. 800 crore, all on a year-over-year basis. While in Q3 FY22 on a year-on-year basis, revenue grew by 41% at Rs. 1,748 crore and PAT expanded by 12% to Rs. 242 crore. EBITDA in Q3 improved by 11% to Rs. 378 crore despite the impact of temporary disruptions as I mentioned before. By leveraging our experience and competencies in chemicals and value chain, we have demonstrated nimbleness to grow without compromising on quality or safety. Our success is a result of our strategy to grow revenues in a balanced manner, by diversifying across products, end user segments, customers, and countries.

Moving on to the performance of strategic business units, Basic Intermediates (BI) profited from healthy realization gains as price hikes that were undertaken for key products given higher input costs. In 9M FY22, volumes grew by 10% partially because of brownfield expansions that we were able to achieve. We achieved positive outcomes in this segment, despite the temporary disruption. Despite the challenging macroeconomic situation, the Company continues to maintain its delivery commitments. Additionally, we expect the BI segment's performance to remain strong in the ensuing period as a result of sustained shift in the global supply chain to India, as well as encouraging domestic trends.

Fine and Specialty Chemicals (FSC) segment's performance must be evaluated in view of major logistical constraints. Along with this, the Company witnessed higher input costs and in a couple of cases, unavailability at a particular time because of which delivery schedules got shifted. Due to the nature of contracts, the prices are not always instantly passed on, but with some time lags. The future performance will be driven by our ability to pass on cost increases to our customers combined with our strong demand trajectory.

Performance products (PP) segment stands to benefit from demand-supply asymmetries. The acceleration in the key intermediate DASDA demand is noticeable leading to an increased realization gain, and OBAs was able to pass on this price increase. Along with this, our integrated approach of having the raw material also internally produced has allowed us to take significant increase in market share, which we hope to remain sustainable. Top-line and margins are mirroring this trend with

volume increase for 9M FY22 standing at a robust 44%. The momentum is expected to continue in the near future as well. DNL is well placed to capture incremental gains from major sectors such as textiles, paper, and detergent, all of which have in some way resumed production at close to pre-COVID levels.

Phenolics business has demonstrated encouraging results as well with an average capacity utilization of 117%, attributable to strong demand in India and other key export markets. EBITDA enhanced by 85% to Rs. 771 crore in the last nine months. I would like to share one key development here. As you know, we had announced our brownfield expansion of IPA. I am glad to share that this has been successfully completed as on December 19th, 2021. As a result, our new nameplate capacity for IPA has doubled to 60,000 tons MTPA.

In another key development, EcoVadis the world's largest and most trusted provider of business sustainability ratings has bestowed 'Silver' rating to Deepak Nitrite with a sustainability ranking of 83 percentile. This has increased from 39th percentile just a year earlier, reaffirming the group's strive towards greater sustainability.

To conclude I would like to highlight that Deepak Nitrite is well positioned for growth across a range of initiatives and our plans for the future are equally exciting. We focus on creating a significant Indian chemical conglomerate with strengths in a spectrum of chemistries and the ability to provide clients with customized solutions. All the while, we stay committed to our mission of large-scale import substitution to meet global demand and grow our market share. This will strengthen our competitiveness and equip us to enhance market share, resulting in value creation for all our stakeholders as opined by our depend on Deepak initiative.

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

Sanjay Upadhyay:

Thank you, Maulik. Good afternoon, everyone. Thank you for joining us today on this call. I will walk you through the highlights of the financial results for the quarter and nine months ended December 31st, 2021.

DNL reported encouraging performance during the period under review, despite the ongoing macro challenges. Solid improvement was demonstrated in the Phenolics business and BI and PP segments also. DNL continued with a strong revenue growth during the quarter. It's one of the best. This is attributed to increase in demand and realization of key products. In fact, the volatility in prices of commodities is certainly impacted but we were able to pass on to the customers to a large extent.

In 9M FY22, on a consolidated basis, revenues are up by 71% at Rs. 4,969 crore compared to Rs. 2,912 crore in 9M FY21. EBITDA stood at Rs. 1,232 crore in 9M FY22 compared to Rs. 808 crore in the 9M FY21, higher by 53%. PAT expanded by 65% to Rs. 799 crore, DNL achieved highest ever profitability, thanks to favourable contributions from BI, PP and Phenolics SBUs.

In Q3 FY22, on a consolidated basis revenues grew by 41% at Rs. 1,748 crore compared to Rs. 1,240 crore in Q3 FY21. On a year-on-year basis, EBITDA grew by 11% to Rs. 378 crore and Rs. 340 crore in Q3 FY21. Despite the overall increase in input and utility costs, the Company's EBITDA growth was strong on an absolute basis. PAT grew by 12% to Rs. 242 crore, PAT performance remained stable aided partly by significant reduction in the finance expenses due to the repayment of debt.

Moving towards segmental performance:

Basic Intermediate reported revenues of Rs. 862 crore in 9M FY22 up 67% from Rs. 515 crore in 9M FY21. EBIT increased by 74% to Rs. 216 crore with an EBIT margin of 25.1% in 9M FY22. The volumes have also improved by 10% in BI segment.

Fine and Specialty Chemical segment revenue increased by 9% to Rs. 611 crore in 9M FY22 as compared to Rs. 561 crore in 9M FY21. EBIT stood at 181 crore with EBIT margin of 29.6%, volumes has been improved by 20% in this segment.

PP segment reported revenue growth of 69% to Rs. 368 crore in 9M FY22 versus Rs. 218 crore in 9M FY21. EBIT expanded to Rs. 59 crore and EBIT margins of 16%, volume has been improved by 40%.

Deepak Phenolics reported a solid performance of revenue expanding by 95% to Rs. 3,169 crore in 9M FY22. EBIT came at Rs. 691 crore, higher by 89% translating to EBIT margin of 21.8%, volume has increased by 23%.

Lastly, on the balance sheet front, the Company's financial position has significantly improved, and cash flows are being leveraged to gradually invest into growth projects. Also, on releasing debts, the Company prepaid Rs. 100 crore of project loans during the quarter without any prepayment penalty.

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

Moderator:

Thank you, ladies, and gentlemen, we will now begin with the question-and-answer session. The first question from the line of Nirav Jimudia from Anvil Research.

Nirav Jimudia:

I had one question. I want to understand more on the chemistry part. How do we select a particular chemistry? Is it like we are already into some group of products and probably this new chemistry, which we have selected helps us in process intensification and a related question to this is when we identify a new chain of products, probably with the newer chemistry, what is the normal size of opportunity we normally evaluate?

Maulik Mehta:

Okay. I can try to answer this. First of all, what we do is when we look at adding another chemistry essentially, let me give you an example. If we have announced recently that we would get into, some level of fluorination and photo chlorination, the way that we look at this, we said, okay, our goal is not to target to replace somebody who is in the market but if there are products where, there are five steps, six steps in order to make the final product. Out of those, there are four or five steps where we are already in them. Like, nitration is something that we're very comfortable with. Reduction via hydrogenation is something we're comfortable with. Digitization is something that we're comfortable with. Now, there are products which require maybe fluorination as one step, which until now we had not taken up because we didn't have that expertise, but we had the other three and we were fine managing product portfolios which required only those. Today we are comfortable saying, okay, let's take even the products which require many of the ones that we have, as well as fluorination or as well as a photo chlorination, which is at the end of the day, just one particular kind of chlorination with advanced chemicals. So, this is how we have gone about choosing a new product.

The second reason that we take while deciding a product is, is this a process which we are missing on it right now and we add it, is this a process where it is going to be the significant bulk of the value generation, if fluorination is going to be by far and away the most critical step, if that so, then we de-prioritize it a little bit. If there is an opportunity for us to do it, where fluorination is one of the key steps, but not the step where the significant value is, it could be on nitration on by-product management of

nitration doing it in a safe manner, ensuring that, the reduction, hydrogenation, distillation, these things are done efficiently, then we take it up because we say that fluorination is then just one of the missing pieces, but it is not the most critical piece in the cost structure. Over a period of time, we are confident that we will build as much of a competency on fluorination as we have another. At that time, we will be fine picking a product where fluorination may be probably the major component, but today we will take it in a sensitive, calculated manner, adding it, and continue to focus on our other key competencies and over a period of time, fluorination will also become one of those. At that time, we will again, re-evaluate what else we can add to the basket, I think I have answered your second question as well.

Sanjay Upadhyay: Over and above what Maulik said is the chemistry part, but this has to meet our basic parameters on financial terms also, because otherwise, whatever chemistry or whatever integration we have, but if it is not making sense if there is a strong competition, if the payback is not within our norms or the growth is not as per the projects or whatever, then we will certainly not go ahead with those kinds of projects, though we may have strength and though there is a synergy. It depends one is the chemistry part of it. We know our chemistry. We know our R&D and those things, but commercial sense it must make and right to win as Maulik rightly mentioned has to be there otherwise, no point in going with any of the projects. As Maulik explained about nitrite, but I can tell you about phenolics also, maybe whatever we are doing now, in philosophy Company has a bulk chemical, and then it adds, fine and specialty chemical to the bulk, and it is a forward integration. This is the logic which we are following, meeting all these criteria. Then we will go ahead with those projects otherwise, no.

Nirav Jimudia: Once we decide on a particular chemistry to be a critical part of the value chain of products, along with the chemistries, and let's say that product is probably an import substitution product. At that point of time, do we access that data? Probably let's say the size of opportunity is Rs. 1,000 crore and beyond which we don't want to foray into it. So, is there any critical benchmarks?

Maulik Mehta: The critical benchmark essentially is one. There are various benchmarks, as Mr. Upadhyay mentioned, financial benchmark is one. With regards to volume, size and things like that, our priority is not so much with regards to size, although we expect a minimum size, but it is also more with regards to the demand CAGR, the growth that we're expecting. Most of the products that we look at getting into, we are seeing that there is a strong possibility towards a low to mid double digit, low to mid-teens as year-on-year growth CAGR. This means that even companies which are already, focused on exporting to India from abroad, there will always be much higher amount of volume demand over the next three years, four years than there is today. If you compound it, that creates a significant opportunity.

Nirav Jimudia: Correct. Lastly in the last investor call you mentioned that we got one order from a customer, which was supposed to start scheduling or getting commissioned from April 2022. Does this new product, which we are going to cater is with respect to inculcating these new chemistries, which we want to get into, or probably it is related to the older chemistries and new chemistries would take part in a later part of our growth capex?

Maulik Mehta: Correct. So, this is on the basis of existing chemistries. However, the new chemistries that we have spoken about will be added on a commercializable basis later on in the financial year.

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

- Chintan Modi:** I wanted your views on two things. One is at a global level, what kind of capacities are likely to get added in phenol? Say in 2022 and 2023, and which regions are likely to contribute this to largely and second is, with the benzene production globally. Do you see, there could be some restrictions on pinching production over the next three to five years because of various reasons, like I believe some of the capacity is also driven through coal? So, could there be a shortage in the capacity and likely increase in the prices of benzene over a period of time?
- Maulik Mehta:** We don't see any expectation of shortage of benzene because there is also new capacity that is coming online during the year. In the meanwhile, with regards to phenol and acetone, what we do is over a period of time, you gave a very short period of time, just FY2022 and FY2023, we'll start FY2023 just in a short bit. But point is that at this short period of time, we look at incremental de-bottlenecking wherever possible by intensifying the existing assets. This will be moderate, frankly speaking, but we're confident that decent amount is going to be, if you're talking about our phenol production, with regards to benzene it is same in India also, worldwide also.
- Chintan Modi:** No, I am talking on global capacity.
- Sanjay Upadhyay:** Global capacities, yes, there are capacities coming up in China, but it will be majorly for the captive use and in any case, we always believe that phenol is a regional play when we started also this situation was there, even today this situation is there. So, even if something comes, we are not too much worried, but yes it is coming up in China, but it will be captive purpose in China.
- Maulik Mehta:** It would be integrated with down streams. This is something that always happens. Phenol and acetone being the commodity play, is normally also considered while, integrating it upwards or downwards.
- Chintan Modi:** Is this capacity a significant one in their existing capacity? I believe China has about 3.3 million tons of capacity currently.
- Maulik Mehta:** Generally speaking, it is domestically consumed, for example, I'll tell you that China is the world's largest producer of Chlor-alkali caustic soda, but it really doesn't matter on the global scale because it is also the largest consumer of Chlor-alkali, similarly you have phenol and products like phenol and things like that. The domestic consumption and the domestic production are both some of the world's largest, if not the largest.
- Moderator:** The next question is from the line of Kumar Saumya from Ambit Capital.
- Kumar Saumya:** Sanjay sir mentioned that in Fine and Specialty Chemicals, the 9-month volume growth was around 20%, so I'm right or missed something?
- Sanjay Upadhyay:** Fine & Specialty Chemicals' volume for nine months is 20%.
- Kumar Saumya:** Lastly, on the phenol side, phenol gross margin compression we've seen in this quarter. If you could just highlight on that, what are the finer aspects of that? Because spreads are largely in line with the first quarter, but the utilisation was better and still we are seeing some gross margin compression?
- Sanjay Upadhyay:** No, no, actually phenol margins spread you are saying actually there is a bit of difference. Phenol compression, if you see phenol at this level, the capacity utilisation is high, the turnover is high it's only the equation of margin. We believe this is settling down, the margin, maybe there will be ups and downs, but yes, I mean,

there cannot be a continuously high margin of 30% in phenol. That is not the commodity.

Maulik Mehta: Can I just add one thing to what Mr. Upadhyay said that while we are looking at spreads, the other missing component in that is energy cost. Now phenol as a starting block intermediate, has a reasonably strong component there, which is also the power cost, energy cost, steam cost, essentially. In Q3, we saw prices of key utilities go through the roof. Coal prices have doubled, quadrupled at some period of time, then even over and above that, there was an issue with regards to availability of the right kinds of coal. So, whatever happens in raw materials, only take a certain amount of what you're looking at as a spread. The aspect there that you're not able to consider in spread is power cost, steam cost. And these were formidable.

Kumar Saumya: But I was talking more on the gross margin side.

Maulik Mehta: These will affect the gross margin. Because the gross margin includes utility overheads.

Kumar Soumya: It should settle down at 29% considering the last quarter prices, if the prices are at this level, so could we expect steady state of 29%?

Sanjay Upadhyay: 29% in phenol?

Kumar Soumya: Gross margins.

Sanjay Upadhyay: I would rather go with EBITDA percentage of say 20% to 23%.

Moderator: The next question is from the line of Madhav Marda from Fidelity International.

Madhav Marda: My question was similar to a question that was asked earlier. If I look at the global capacity addition for phenol and I hope I have the right data, as you said, China's expected to add something like 3-3.2 million tons of capacity in 2023 and in 2024. While I understand, you said that China uses a lot of that for its own captive use, but that's because Phenol is like a global credit price. Can that impact global prices for phenol as these capacities come through and are my capacity numbers totally right that China is adding about 3 million tons in 2023 and 2024 calendar year?

Maulik Mehta: Frankly it's a very nuance question that you're asking and difficult to answer, but see, at the end of the day, what will always matter is the speed at which phenol comes up, the speed at which the key raw materials come up and the speed at which the downstream for phenol come up. When you will see, unusually high or low margins, when there is a mismatch between the phenol capacity coming in and the downstream or the upstream capacity coming in, this will happen. This will happen for a period of time and then it normalizes again. I don't think that if you look at it on annualized basis, you should not be so concerned because generally speaking, as Mr. Upadhyay said, phenol is a regional play. If you look over the last 10 years, you will see that Chinese phenol has really not had a significant impact on the Indian consumption. Even though Deepak came in with its plant only a couple of years ago, it has never really been a big player here, even though it is a neighbor, and it has the largest capacity worldwide.

Madhav Marda: Okay. In this, phenol prices effectively are kind of delinked to Chinese prices.

Maulik Mehta: No, no, there's nothing like that, I mean, of course, this is what I always say that when China sneezes the world catches a cold, but I would not look at it in that worrisome a manner because there's also a lot of downstream production that is

coming in. Generally speaking, we expect that phenol and acetone will remain strong drivers for our profitability moving forward as well. What is more important is that the domestic demand that was there when there was less worry about COVID, hopefully that returns to that form. It's not that it was weak, but we hope that it also continues to build itself. We are also very keenly looking at the results of auto companies and things like that.

Moderator: The next question is from the line of Deepak Saha from Savart.

Deepak Saha: My first question is regarding the Basic Intermediate segment and for the nine-month basis, if we record 67% growth in the revenue front and when we look at the volume growth during the same period, it was around 10%. Broadly, the revenue is largely on account of the price hike that we have undertaken in the recent months and there are also some raw material challenges on the supply front. Once this supply side challenges on the raw material front normalizes, is it a right understanding that we would see volume growth also pick up from the current levels and it would also expand the margins on the current levels, which do you think? This is the first question.

Maulik Mehta: Okay. Thank you for compressing a long question in a short period of time, but what I can tell you is yes, we had underutilized capacity, both in Basic Intermediate and in specialty chemicals despite having a very strong order book. At critical times, there was unavailability of important raw materials because suppliers raised force majeure. Therefore, I can also agree that yes, as long as volumes of raw materials availability is streamlined, even if there is some modicum of price volatility in the cost of raw materials, we are able to pass it on. The demand remains strong. So, does the customer confidence on Deepak. If we're able to see a streamlining of volumes of raw materials, you will certainly see that there is a higher utilization. You're absolutely right in pointing out that the revenue growth was only partially linked to volume growth and the rest of it was where we were successful in passing on price increases. We expect that, as soon as the raw material situation is stabilized, we should be able to supply to the customers need more confidently.

Deepak Saha: Okay. My second question is regarding the FSC segment, during the last quarterly concall, we kind of alluded to the fact that going head, the underlying contracts and the new contracts that would be tying up with, we would have quarterly pass-through mechanism in order to mitigate the margin pressures or so that we can also pass on the price hikes that are taking place in the industry. So, is that any like material development, as far as passing through mechanism is concerned in the contracts or the new contracts that we are going ahead with?

Maulik Mehta: By and large what we have is a quarterly pass through because what's more important for the customer is we have to make sure that their confidence is in ensuring that the supply chain, the pipeline is filled up. They depend on companies like Deepak because they know that we're healthy, we are robust, we know what we are doing, and we will work to tie up our raw material so that they will not be affected. They are not averse to passing on cost increases. Let's be very clear. What they are averse to doing is wasting a lot of time nitpicking about, month on month price increase and decrease because they would prefer to focus on growing their end product, which is where we want them to focus as well. Now, in all of this, if there is an absurd amount of raw material price increase, then we do try to have those conversations, but that is left at the end of the day to the customer. However, what bothers everybody including Deepak is when there is unavailability of raw materials. I would say at the end of the day, yes, we have faced a margin compression because of the aforementioned reasons, but the demand is strong, the confidence of our customers on Deepak is strong and we continue to be bullish about being able to grow market share with pretty much all of our strategic customers. We will be signing

more such contracts, which will be essentially medium to long-term driven, multi-year contracts for key customers.

Deepak Saha: Just a last question if I can pitch in, in FSC segment on year-on-year basis, when we look at the revenue numbers, it has recorded a slight decline, I believe, it is because of the logistical challenges that is prevalent in the industry? There's no issue on the demand front.

Maulik Mehta: No issue on the demand front, of course, logistics they play a role, but now it has become high for such a long time that it is almost become normal at this height. But what you saw, revenue compression is actually also a volume compression while Mr. Upadhyay's point was right, that we had seen volume growth compared to the previous year. We also have to keep in mind that the previous year volume itself was lower because of our nationwide lockdown. Also, because after the lockdown, there was an insistence from various State and Central Government that we restrict manpower to 25% or less. At 25% or less, the priority is not on production, it will always be on safety. Keeping those things in mind, we prioritized higher margin products last year. Whereas now, we have been able to broad base our volume, which were even then be affected by raw material availability and to a certain extent by freight availability.

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

Rohit Nagaraj: First question is on Phenol. Post commissioning of the downstream products on Phenol how much of Phenol capacity will be utilized, I understand that at 117% utilization currently we're producing something like 241,000 MT, so out of that how much will be utilized captively and how much will be for external sales?

Sanjay Upadhyay: To answer your question, these projects whatever we have announced, we want to consume 30% to 35%. This currently what projects we have, it will not consume that high, but there are plans in pipeline and ultimately, we will consume around maybe it is more than 40%, 45%, 50% phenol in captive. Today if you ask me it will be around 20% to 25%.

Rohit Nagaraj: The second question is on Performance Products segment, DASDA and OBA we have done extremely well in Q3. Going into Q4, do we see any kind of margin, prices getting contracted, or we are seeing the same kind of momentum continuing in Q4.

Maulik Mehta: It will continue in Q4 because the last couple of quarters, we have been giving a guidance that volumes have started to recover, and we believe that prices will also follow, maybe a quarter or so later. So, we have started seeing that. And today there is a robust demand in all the three segments as compared to previous quarters. However, in Q3, there was a slowdown in the demand for textiles because of various reasons that are all well-known things like GST, things like in Gujarat there was an issue with the local pollution control board and the industry bodies there and things like that. These have all by and large been addressed to some way or another in December. So, we have to see how things shape up. However, if I'm comparing to the last few quarters where demand was depressed to a large extent, it has substantially improved from there. What is more over and above that I think, customers have, had a significant preference for Deepak because of its integrated approach. This is something that we see more in performance products, because most other, if not all other manufacturers are not as integrated and therefore customers had seen wild swings depending on other suppliers, including unavailability of product.

Moderator: The next question is from the line of Nitin Tiwari from Yes Securities.

Nitin Tiwari: My first question is regarding the capex. How much of capex have we incurred in nine months? Also, at the end of the second quarter in the call we have mentioned that we will be spending about Rs. 700 crore in our downstream phenol plant and a little bit more on brownfield expansions. So, is there a revision in that plan in light of the QIP approval that we announced in December 2021? So, that is the first question.

Sanjay Upadhyay: Whatever we have announced that stands. QIP, see, we have definite plans. I would not be able to tell you much about that because we are under that process, we cannot diverge much about the projects in future but yes, there are definite plans. Once we are through with our all processes then we will come up with the release. See, today when these questions are raised about these margins, there are every segment and every product. This is where the confusion begins because since all the products are integrated, now, if you have a higher margin in bulk chemical, you will have a lower margin in fine and specialty. If nobody notices the improvement in performance products, which is significantly high, where it consumes higher, this bulk chemical also.

So, ultimately what we are saying that yes, products are doing well. There could be one quarter here and there, but ultimately if you see now, again, Q4 you will have a better margin as compared to this. So, it happens. And phenol also there are downstream definite plans as I explained earlier also. Our whole endeavor is to consume phenol captively and acetone also. There are definite plans and that is why this QIP. What the plan is for phenol is well a part of planning. So, the resolution is for Rs. 2,000 crore. How much we raise is a different thing, but the total enabling resolution is for Rs. 2,000 crore. And we have significant cash generated also in the business. So, with all these, you can see Deepak Nitrite as it stands today will have a strongest balance sheet ever, and then that enables us to do whatever we want. And then it will be fundamentally a very-very strong Company which will go up to the next level. Answer to your pinpointed question will be difficult today because we are not supposed to disclose so much of information.

Nitin Tiwari: That's fair and that is very well answered. My second question was with respect to the downstream phenol capacity that we have already spoken about. As you had given us a sense around phenol market size and how much our capacity would be in terms of percentage. So, can you give us some sense around the downstream phenol market and how the market stands today in terms of size, how much is the import dependence over there and how much import replacement would our capacity bring in whenever the downstream capacity comes?

Sanjay Upadhyay: It is not one product only. There are several products. I cannot tell you about each and every product, but these are all import substitutes, that much I can tell you. But then there are several products. So, it will vary from product to product. So, it is very difficult to explain to you on this call how it will be.

Nitin Tiwari: For that reason, I will come down perhaps and meet you and understand.

Sanjay Upadhyay: Yes, of course, but not now because this is not the right period to do. Once we are through with our QIP announcement and through with the processes then.

Nitin Tiwari: Certainly. And lastly if I may push in one more. You did allude to basically a positive anomaly in the DASDA prices which have helped us in the OBA and Performance Product segment. So, is this anomaly similar to what we had seen earlier in this segment and how long do we foresee that this is going to continue?

Sanjay Upadhyay: It cannot be like last time what it was. But yes, it will continue for some time, but not for long, it cannot. But then PT segment per se is doing well. You see the volume

growth there. OBA is doing well, OBA is absorbing all the other increased price and then doing it. So, there are many positives in all the segments.

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

Levin Shah: Again, my question is on the phenol segment. What we have seen in last three quarters, actually the prices of phenol have been quite robust and that is what is visible in our top line as well. But our margins, like you explained have been slightly volatile. And this quarter we have had impact because of the power cost and even on the raw material side. So, now going forward with our capacities now operating at very good utilization levels, how do you see this sequentially the costs? Are they going down, and will we see better profitability going forward?

Sanjay Upadhyay: I won't say major, but next quarter you will have power plant of course running. So, that saves energy cost. But then for that coal also has to go down, but unfortunately coal is also up. But otherwise, that is also going to give you that benefit. So, that is the straight capex which will give the return. Rest all it is up to us to utilize our capacities and how further we can improve on the capacities. Because margin being margin it is not in our control, in the sense, we are not too much worried about this. Someone asked about China's capacities; such situations happen; it's all part of the business. They have product capacity and will be able to meet demand. So, margins will go up and up, but we will control our production cost, we will see that our volumes are there, and we are able to sell to the maximum. Unfortunately, today there is one more element which has come up that is freight element. So, the exporting of phenol is becoming costly. But that is helping us also because people are not able to import phenol also to that extent. So, these are all the gains which any commodity product will have. So, not too much worried about this. And I do not think this is a bad margin what we have. It will further go up because of the power plant. But the range of the margin you cannot take 29%-30%-35%, that will be too high for a commodity. So, it will be remaining maybe in the range, should be in the range of 20% to 23%, up to 24% maximum.

Levin Shah: On this also now that we are operating at 115%-120% kind of utilization and also our downstream products may take some time where we will utilize, let us say 35%-40% of our production. So, going forward on the revenue side or at least the volume side we may be flat for the next few quarters, is that understanding right?

Sanjay Upadhyay: No, that may not be right.

Levin Shah: So, there is a scope for the further volume growth.

Sanjay Upadhyay: Yes. There is always a scope. I mean, who thought we can produce up to 1500-1700.

Levin Shah: My last question is on this Fine and Specialty segment. Like you have been always talking about the margin last year it was obviously high and not sustainable. This time around we have seen different kind of headwinds. But now going forward from medium term perspective, with the kind of pass through that we are talking about, do we see that margin improving from here? And what kind of margins will be sustainable for this segment?

Sanjay Upadhyay: I have always maintained that the 35% to 40% range is a fair range for any specialty chemical. I still stick to it and this quarter it is low, maybe around 29% to 30%. But certainly that range is doable. You will see much better again improved Q4. So, I am not much worried. These quarterly gains, in our kind of products one cannot have these kind of fixed margin, that 29%-30%-32%, no, it's not possible because today

the market is so volatile and there are disruptions in the prices. We cannot let go market because raw material costs are high. We have to produce and continue and market share has to go up. That's the whole idea here. So, somewhere the disruption is also playing, but I still stick to my target that it will be somewhere around 35% to 37%.

Levin Shah: Understood. Yes, quarterly ups and downs, we understand and that is what is beyond our control to some extent.

Sanjay Upadhyay: But somewhere I feel our business model is such which should be appreciated by the market that we have three segments is our own creation. Otherwise, if you see the overall margin has gone down by 3% of EBITDA. It has not gone down significantly. Somewhere DASDA performance is doing well, finance ratio has gone down, but bulk is doing well. So, ultimately the whole idea is better to present a picture which is integrated, because each product flows into other segment and everywhere you will find that there is a margin element in that. So, to come up to that particularly like P&P prices, for example, is significantly high which is absorbed by your caustic price which is high which is a bulk commodity, which is absorbed by fine and specialty. Sodium nitrate is consumed in Fine and Specialty. So, those things it should be understood and appreciated in totality rather than getting into a segment, and overall impact is how much. This is our business model.

Levin Shah: I think that is well appreciated and that thing has kept us going and even our performances if we see, over medium to longer term we have gained from our fully integrated model. So, no denying of that.

Moderator: The next question is from the line of Tanvi Bhandari from Hem Securities.

Tanvi Bhandari: Just a few questions. First, I just wanted to know that, overall because everybody is talking so much about margins, just a general question that if we have an inter segment thing that because one segment margin are higher than the other margins are low, but still we had 5% dented margins if we talk about an integrated level. So, I wanted some clarity on an overall level that from 27% in Y-o-Y basis where 22% EBITDA margin roughly and also in phenol as we are talking about more of downstream products and still it will not be all our commodities play because we are planning to have more value-added downstream derivatives coming in. So, won't there be high margin products?

Maulik Mehta: I will answer the first question first. You are right that there has been a dent, but as I have alluded to before, that is largely because we are able to absorb raw material cost increases sometimes with a lag of a quarter and that's normal. That's fine. What is difficult to be able to absorb is unavailability of raw material from time to time. And that was exacerbated in the case of Q3 because we were unable to get the raw materials owing to force majeure ways by one of our suppliers. Now, as the situation normalizes as material movement is available, we remain confident. But what happens at the end of the day, when we are talking about a Company which has a significant amount of its value coming from high capex intensification of its existing plants. If they are not able to run the plants because of unavailability of a raw material, then that will affect the average margin. There's no question about it. Also, you will find in some cases that, when we talk about margins, we talk about margins on a normalized basis that we expect Fine and Specialty to have a 35% to 40% margin on a normalized basis. Now, in that interim period, if for whatever reason, things like energy costs suddenly shoot up and then they come down, they do affect the bottom line, but they affect the bottom line in a way where it is not a sensible thing to pass on. Because it went up, it came down, it got normalized. Situation is normal. And therefore, what is more important is keeping the strategic customer supplied with your key products that they require so that they can grow. Now, yes,

there was a dent, but you will see by and large that one should not look at a single quarter in its isolation. These have happened. You will find that most companies that were involved in the production of commodity chemicals, like chlor-alkali, they will do well in Q3. Is that going to be an expected situation round a year, No. Just the same for us also you will have a situation where there was a margin compression because of unbelievable volatility in key material and therefore an underutilization. This is something that we don't hope will continue. There's no reason to expect it to continue, but once in a while it happens, and we take it in stride.

Now with regards to the question about phenol. Yes, you are right. Not all of the downstream that we would get into will be commodities. There will be others which are 'advanced intermediates', and they will have higher margin. So, by and large, as a balance you will perhaps see a change in the flavor of the business moving forward in the phenolic side. But let's be clear that when Mr. Upadhyay is talking about the margins, it is the margins of the products that are currently being manufactured by us. So, moving forward we may see an improvement. The extent of the improvement we don't know because at the end of the day it will always remain a blend of high volume and low volume with higher margin.

Tanvi Bhandari: One last question, could you just give us a glimpse and a flavor of the market share in each of your segments.

Maulik Mehta: Each of the segment very difficult to answer, but I think by and large for all of our products, maybe with one or two exceptions here or there, we are the largest player for that product or in the top three largest players for that product by and large worldwide to our target audience. Now, for example, sodium nitrate, you will have capacities. I mean, China by itself is maybe, 5, 6, 7 times the size of Deepak, but that's not our target market. So, we don't sell to that market. The markets where we sell, we are dominant players in terms of wallet share and capacity. Correct Mr. Upadhyay, is there any products that we are not in this position?

Sanjay Upadhyay: Most of the products would be around 70%-75%, even nitrite would be 80% maybe. So, I think wherever we are we are having a high market share and we don't let go our market share, that's for sure.

Maulik Mehta: And one good thing that is happening is India as a market in terms of demand is growing very rapidly. So, the demand CAGR that you see in the domestic market has grown substantially in many of the segments that we are in. There will be occasional contractions because of unexpected events like COVID. But as a general trend, I think we should all be proud of the kind of investments that the segments across the board are making in India, international players as well as Indian players. Many of them have announced capex, many of them are in the process of commissioning their previously announced capex. So, India is the right place for growth especially for companies like Deepak.

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

Manish Jain: My only question is that what has been the volume growth across segments compared to the previous quarter?

Maulik Mehta: I think we have mentioned.

Sanjay Upadhyay: Previous quarter I think we will have to tell our investors that Mr. Somsekhar Nanda will get back to you on this, each product, because it varies from product to product.

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

- Rohan Gupta:** Question is on our phenolics business. We have seen that definitely there has been some pressure on spreads in phenol but on quarter-on-quarter basis, there has been sharp decline in EBIT from our phenol business. While we have been running our plant at maximum utilization, you mentioned almost more than 115% and also probably benefiting from the IPA. So, is there any one-off or a higher raw material cost probably which has impacted the phenol profitability in the current quarter? Because that's not getting reflected in the spreads which are available.
- Maulik Mehta:** Utilities, steam cost coming from high priced coal. That is one of the major one. You see it probably in price. This is also there, but this will anyway get reflected in some way or form. But most important at the end of the day has been the cost of utilities. And freight costs have been an ongoing perpetrator in many cases. Nowadays, even domestic material movement, look at the price of petrol and diesel.
- Sanjay Upadhyay:** There is an impact, there is no doubt on that because of higher utility rates and then even propylene, the input rates are also high. High in the sense that though we are aiming a decent margin, but yes, the raw material input cost was high for the quarter.
- Rohan Gupta:** So, this high utility cost definitely continues with the rising coal prices. So, do we see that this kind of pressure in terms of spread, in terms of lower profitability in phenol business will continue?
- Sanjay Upadhyay:** Of course not. Why should it continue. Because phenol prices are also going up. It's not going to remain same. Because ultimately, if coal prices remain at this level, at whatever price it is, then the market will have to absorb the price. So, it is a matter of time. And raw material prices because the LPG rates are high, it is going to remain, because crude has gone up, so some where it has impacted the propylene price also. So, phenol then we will have to go up. But again, I repeat that if you are expecting a margin of 20% to 30%, that is not going to tell you something which is not sustainable. But yes, reasonable margin certainly anybody can pass on and get.
- Rohan Gupta:** And finally in Fine and Specialty chemicals business, you were mentioning that in your presentation that definitely there has been some lag in terms of passing it on to the end customer. So, I understand that we are an integrated business model and that's pretty helpful that higher profitability from one segment compensates probably the lower profit from other business, but in fine and specialty chemicals in last two to three quarters we have also commercialized more products and the revenues have picked up significantly. And that with the higher operating leverage our specialty chemical margin should go up. So, is it that because of the lag in terms of passing on the raw material increase, that is taking some time in terms of margin expansion with our customer?
- Maulik Mehta:** There has been no new capacity in Fine and Specialty Chemicals that got commissioned in the last two quarters. We have announced that there is expansion, there is investment in all of the segments, there is no doubt about it. That said, in the last two quarters there has not been any new debottlenecking that has been commissioned. The increase that you see in volume is because last year the volume was low. And this year, we are right now seeing at least in Q3, we have seen somewhat lower volume than our capacity because we did not have those key raw materials in time. The situation has improved, and we do hope to recover good amount of the cost increase now moving forward, what happened in Q3. But you cannot ask for a recovery for production that you did not do and material you didn't dispatch. But nonetheless, we do anticipate that by Q4, the situation with raw material availability will be better than it was in Q3. Let us see how things unfold.
- Sanjay Upadhyay:** Q4 again, as I said earlier, Q4 will be better for these segments compared to Q3.

- Moderator:** The next question is from the line of Nitin Agarwal from DAM Capital.
- Nitin Agarwal:** Just a quick one on the Fine and Specialty chemicals. How many products are we looking to add over the next two years?
- Maulik Mehta:** Cannot answer that. It's not a small number, that is for sure. And one of the reasons why we have not announced the names of products that we are going to get into when we announced Fluorochemistry as well as photo-chlorination is because it provides us a platform for a larger permutation and combination of products. Many of these will actually be tied up with customers for the medium term. So, difficult to answer. But certainly, it is going to be an interesting number. Specialty Chemicals as a segment even for us, is turning out to be a very attractive play even in terms of the kinds of engagements that we are getting into with, existing customers for new molecules and new customers for new molecules.
- Nitin Agarwal:** If I can just push you a little bit on that, in terms of timelines by when do we see the impact of the substantial new product additions, platform additions coming through in our numbers?
- Maulik Mehta:** Commercializing at least many of these molecules, contribution will be at the later end of the next financial year. So, between December and February is when we will start to move material out and therefore, we will see some impact coming in Q4 of next year. That is when you will start seeing the value coming in. In the meanwhile, there are brownfield expansions which we have already announced and those are also with long-term agreements that are tied up, but those are for existing chemistries and products that we currently do manufacture.
- Moderator:** The next question is from the line of Saurabh Kapadia from Asian Market Securities.
- Saurabh Kapadia:** If I have inferred your comment correctly, we are looking at debottlenecking in our phenol plant as well?
- Maulik Mehta:** We always look at debottlenecking in the phenol plant.
- Saurabh Kapadia:** So, what kind of incremental volume we can add and by what timeline?
- Sanjay Upadhyay:** Yes, we are certainly working on this because in this plant itself when we said 2 lakh tonnes capacity, today we are producing 117%. It will go up with our further debottlenecking in this. But to give you exact number is not possible now.
- Maulik Mehta:** And something which we have mentioned before is for us, the plant is designed in such a way, because this is what we had, this is the money we had, this is the land we had, is that it has been developed and commissioned in an extremely tight and efficient manner. So, that means that it is not just the capacity of phenol that can be improved, it has to be every single piece of the jigsaw. Just to give you one example, the cost of diesel that we pay for in order to move our material to the customers that itself on a monthly basis is Rs. 15 crore. There is a cost of the diesel for the trucks and the tankers that we have that get our material to our customers. This is what you would look at on an annualized basis, the bottom line of a small chemical Company. This is just the diesel cost. So, at the end of the day, all of these things had to move lock step, and we have been able to demonstrate that very well in the last year, two years. No reason to believe that we will not continue to do that. We have very strong systems and processes in place. So, as we debottleneck, we will also debottleneck our supply chain and end-to-end, we will continue to see value coming in from every part of it.

- Moderator:** The next question is from the line of Rushabh Shah from Anubhuti Advisors.
- Rushabh Shah:** First question is basically on the substantial rise in other expenses during the quarter on a sequential basis. If I understand, is this because of higher freight cost or something if I am missing?
- Sanjay Upadhyay:** Other expenses we are comparing nine months? What are you comparing?
- Rushabh Shah:** Sequentially, so last quarter as per your BSE filing it was Rs. 72 crore and this quarter it is roughly Rs. 100 crore.
- Sanjay Upadhyay:** It must be with some element of expenses net of also against that, the income, I don't know. Rs. 72 crore and Rs. 100 crore you are saying. Somsekhar, can you elaborate on this?
- Somsekhar Nanda:** Can you please repeat the question?
- Rushabh Shah:** As of quarter ending September 2021, the other expenses were Rs. 72 crore. It has substantially gone up Rs. 101 crore this quarter around. So, any exceptional item it was or was it just reflecting the higher freight and energy cost?
- Somsekhar Nanda:** Yes, both domestic as well as ocean freight was largely higher.
- Sanjay Upadhyay:** It is all likely to be logistic only, sales and administration.
- Somsekhar Nanda:** It is largely logistics and because of the larger volume that you had currently, the impact of this also is in this number.
- Rushabh Shah:** So, we are reiterating our margin guidance for all the segments. We are not cutting anywhere that our margins may go down going ahead.
- Somsekhar Nanda:** No, we are not saying that.
- Moderator:** The next question is from the line of Julie Mehta from Mount Infra Finance.
- Julie Mehta:** I just wanted to get back to our plan of entering into photo chlorination and fluorination. So, these chemistries are really complex to crack, if I am not wrong. So, I just wanted to know, what is your expected target and by when do we think we will be making any development on this front? Also, if we have any specialized personnel for this segment?
- Maulik Mehta:** Mr. Upadhyay and I both have mentioned that the capacities will come online towards the end of the third or beginning of the fourth quarter of next year. Of course, we have people who have a high degree of competency. The chemistries themselves are complicated. There are several chemistries that we are currently already doing which are complicated. So, anything which is new is always we feel a little bit complicated. And I think there has been an environment created by a lot of people that these chemistries are more complicated than normal. What is important to keep in mind is material handling and safety. Now that is something that we of course are going to pay extra attention to. There is no doubt about it. Material handling and safety at the end of the day is important, but this is not something that is new to us. We have various products in our basket which require a lot of safety and material handling, and this is our bread and butter. We know this and we are responsible for ensuring that every single person in the Company is able to work in a safe and secure manner. That is our job. So, we continue to hold ourselves to a high standard in terms of safety and in terms of material handling. So, we have had a fair degree of

confidence internally. Otherwise, we would have announced these projects a long time ago. What we had to do first is, yes, we were successful at the lab and the pilot level. We were successful at ensuring that all of these things are clear to us, but over and above that we had to work to ensure that raw materials were secured, that we got the right people on board so that it was not just extending our current selves, but we got people on board who had a good degree of experience in handling these kinds of chemicals. And then once we had these things tied up that is when we made the announcement that we are investing in this. So, yes, it is important and yes, we are aware.

Sanjay Upadhyay: And we have a good team of people also available who are skilled.

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

Arvind: First one is a follow up. Can you just indicate the kind of product reach and market expansion that you have done over last few years because given your high market shares in your target area and the kind of growth that you have achieved, it a function of new product additions or is it a function of market reach expansion also, if you can share some more light, over the last 10 years what have been the key drivers and how to look ahead?

Maulik Mehta: We have expanded capacities in many of our products. We have also seen that the domestic market, even the markets that we are in, forget domestic, why do I keep talking only about domestic, our customers have seen a healthy demand for their products which consume Deepak's products. So, as their requirements increase and our wallet shares stay the same or increase, we also find that our products are in higher demand with existing customers and new customers that come in. Now, for example, we have made investments, like I mentioned earlier in sodium nitrite, and even with the increased production that we commissioned in October, just a couple of months ago, our market share in the domestic market has increased, but it has increased marginally and that is because the domestic market itself has increased. And a lot of our customers have invested in downstream in their own capacities. Similarly, if we look at say agrochemicals, we are seeing a bullish trend with regards to demand for Deepak's products. So, whether this is in Europe, whether this is in India, whether this is in the US, there has been an increase in demand. And in many cases, the customers have actually increased Deepak's wallet share, because we have been able to demonstrate sustainability of supply pipeline.

Arvind: What I was asking you, 75% kind of market share is something which you cannot expand beyond that. It's not fair to assume that it can go up to 100%.

Maulik Mehta: That is not a fair assumption. The size of the market remains the same, because if the size of the market increases, then you are talking about 75% of an increased market.

Sanjay Upadhyay: Like phenol, for example, to elaborate, phenol when we entered the market we were at 60%-65%. Market has expanded so much that we are now at 55%-60%. So, the market is growing. There is enough opportunity available.

Maulik Mehta: So, we are at 55%. We are at a lower market share with a higher product output compared to what we had originally envisaged of 100%. We are far in excess of 100% and still we are a lower market share.

Moderator: The next question is a follow up from the line of Rushabh Shah from Anubhuti Advisors.

- Rushabh Shah:** My last question was on the phenol part. Basically, the revenue decline which we saw this quarter around was any impact on account of anti-dumping duty which was revoked last time? Just wanted to understand the reason of the decline in revenues.
- Sanjay Upadhyay:** No, there is no impact of anti-dumping duty for that. Absolutely no.
- Maulik Mehta:** Actually, the only time we remember this is when some investor reminds us that, oh, you remember that anti-dumping duty. It doesn't affect our regular business.
- Rushabh Shah:** So, was there any volume decline this quarter around versus the last quarter?
- Sanjay Upadhyay:** In what product?
- Rushabh Shah:** In terms of phenol, did we see a volume decline sequentially?
- Sanjay Upadhyay:** There was a reduction of around, but marginal, maybe 3,000 to 4,000 tonnes.
- Rushabh Shah:** Lastly, Basic Intermediates, the issue at the vendor has largely been resolved right now? The issue which we were facing at one of our vendors end, has that been resolved now?
- Sanjay Upadhyay:** We are not aware of this.
- Rushabh Shah:** The force majeure which we saw at one of our vendors end.
- Maulik Mehta:** That is not in Phenolics, that is in Deepak Nitrite.
- Rushabh Shah:** Yes, Basic Intermediates.
- Maulik Mehta:** Yes. So, the force majeure got removed. Now that is normalized as we speak. Every quarter has thrown up some interesting surprise or another which was earlier not envisaged. But the force majeure was lifted towards the end of December 2021.
- Moderator:** Thank you. Ladies and gentlemen, that was the last question. I now hand the conference over to the management for their closing comments.
- Sanjay Upadhyay:** Thank you all. Thank you so much for joining this call. In case you need any further clarification, please write to us, our investors relation team will respond to you. Thank you once again.
- Maulik Mehta:** Thank you. Please everybody, stay safe. I know that there is a tendency to disregard this wave as something which is not as significant or severe, but it is going to be significant or severe to people who are immune compromised. And always be aware that as a country we have a young population and that means that young population might have a lot of people who are not as vaccinated as many of us are. So, please take care. Please stay safe and ensure that your family is safe and look forward to talking to many of you again in the near to medium term.

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