Shree Renuka Sugars Limited
Consolidated results for Year ended 31st March 2013 Conference Call Transcript
31st May 2013

Moderator

Ladies and gentlemen good day and welcome to the Shree Renuka Sugars Q4 &FY13 Earnings Conference Call. We have with us joining today Mr. Narendra Murkumbi – Vice Chairman and Managing Director, Mr. KK Kumbhat – Chief Financial Officer and Mr. Gautam Watve – Head, International Operations. As a reminder for the duration of this conference, all participant lines will be in the listen-only mode and there will be an opportunity for you to ask questions at the end of today's presentation. If you should need assistance during this conference call, please signal an operator by pressing "*" followed by "0" on your touch tone phone. Please note that this conference is being recorded. At this time, I would like to handover the conference to Mr. Narendra Murkumbi. Thank you and over to you, sir.

Narendra Murkumbi

Good evening everyone. Thank you for joining the conference call of Shree Renuka Sugars. We presented our annual results for the 12 month period ending 31st March 2013 and would like to discuss the main features of our results and take your questions and queries. Over the last 12 months we have devoted our main efforts in stabilizing our operations and balance sheet as well as given maximum focus on the turnaround of our loss-making operations in Renuka do Brasil S/A. Wehave been able to achieve some significant improvements even though more work remains to be done. The key improvements that we have been able to effect is the increase in cane crushed in Brazil by almost 1.2 million tons to 9.5 million tons in 2012-13 and additional cane planting in the last 12 months which will further enhance the cane availability in the current season. In India, our main focus was on increasing the capacity utilization of our refining division where we had doubled the capacity utilization compared to the previous year. I am happy to say that since October 2012 we have been running our refineries at almost full capacity. The India standalone business is showing a year-on-year growth of 95% for the last quarter in terms of revenue.

The Indian outlook in terms of prices has turned more bearish than it looked three months ago primarily because the production of the previous season which has just finished has come in on the higher end of estimates and therefore prices have been muted in India. As a result, the overall EBITDA margin in the Indian operations has gone down. High production in India lead to lower sugar prices and the cane price increase throughout the country this year has therefore turned out to be higher than the increase in sugar prices. Both have increased but the cane prices have increased more than normal. Additionally, we had a lower recovery year-on-year in India which is largely due to climatical factors and effect of the stress created by drought. In Renuka do Brasil S/A we have an improved EBITDA margin for the quarter and also for the year we have reported an overall EBITDA margin of 26% for our two Brazilian companies. Our Brazilian companies are cash positive and we have not put in any additional money from the parent company in the last 12 months. The overall loss reported is about Rs. 4,888 million on account of non-cash items like depreciation and forex variation. In Brazil, we see a much better position in terms of operational performance going forward. More cane availability and higher capacity utilization should help us significantly.

In India we had a very significant policy change on 4th April 2013, which is the announcement of de-control by the Central Government. After this, virtually all marketing side controls have been dismantled. The removal of levy obligation will have an immediate impact starting 1st June 2013 because up to the 31st May 2013 the sugar industry was delivering sugar against production of the 2011-12 season. The new decision is effective for production from 1st October 2012 and that levy sugar was due from 1st June 2013 which no longer has to be supplied.. The impact on an annual basis for the sugar industry is about Rs. 3,000 crores per annum and for SRSL about Rs. 120 crores per annum as per the current difference between domestic market prices and the procurement price for levy sugar. The other changes like the scrapping of domestic sale controls, etc., are not something that can be quantified immediately in this quarter but I believe that these will make the industry significantly more competitive and market oriented. There have also been positive developments on ethanol policy, both in India and Brazil, which are pretty significant. The new Indian policy which I talked about in my last conference call was gazetted in January but the actual purchase orders have started being released only in May 2013. We have also received some orders and have started dispatches to couple of depots. However the full extent of the orders are not yet awarded.We believe that between 40 to 50 crores liters of orders will be awarded to domestic suppliers in the first round and it is likely that there will be further tenders for procurement of additional ethanol because the annual requirement starting from the mandate period of 1st July 2013 will come to about 110 crores liters per year for the country.

In our stand-alone company we have managed to reduce both our bank debt as well as our interest costs. As against an average interest cost of Rs. 100 crores per quarter in the first three quarters of the year, our fourth quarter interest cost is about Rs. 65 crores despite a high level of closing inventory which is a peak working capital requirement for us amongst all the four quarters. Despite that our interest cost has dropped to Rs. 65 crores which is due to higher availability of supplier credit and reduction of costly working capital bank loans. I would also like to say that we continue our efforts to deleverage rapidly. This includes our Brazilian subsidiaries where we believe, after two years of hard struggle, we havecorrected the problems that we suffered due to the droughts of 2011-12. We are now set up in a very positive manner to achieve a much better operational performance in the current year. With that I would like to hand it over to my colleague Mr. Gautam Watve who is going to talk about the crop outlook for this year in Brazil as well as the recent changes in the ethanol policies which make a significant difference for our revenue realization.

Gautam Watve

Thank you very much and good evening to everyone. There have been a couple of favorable ethanol policy moves in Brazil over the last quarter. One of them has been that the Brazilian government has decided to increase the blending of anhydrous ethanol with gasoline from 20% to 25%. This will increase the overall demand for anhydrous ethanol by about 2 billion liters and is very positive for the industry. The second move has been that the Government has actually allowed tax credit of R$(Reais) 120 per m^3 which converts to about USD 60 per m^3 which will go to the mills who produce ethanol. So this will not only give additional revenues to the mills but also give a lot of support in terms of equivalence when Brazilian car owners looks at using either neat hydrous alcohol or blended gasoline. On the production front, as Mr. Murkumbi said, we have had two tough years in terms of bringing the whole company back to higher capacity utilization and over the last couple of years we have been able to go from 8.3 million tons of cane crushed combined for our Brazilian entities in 2011-12 to about 9.5 million tons of cane crushed in 2012-13. We expect to reach about 11 million tons of cane crushing for the 2013-14 season, so that is an increase of 1.5 million over the last year. This is on a total capacity of 13.6 million tons, so we will be at about 80% capacity utilization for both the companies.

Narendra Murkumbi

With these opening remarks I would like to throw the floor open for questions.

Moderator

Thank you. Participants we will now begin the question and answer session. We have the first question from the line of Nirav Shah from Antique Stock Broking, please go ahead.

Nirav Shah

On the standalone numbers can you just share the broad breakup EBITDA of the sugar segment between manufactured sugar and the refining output. If I take a normalized EBITDA of around USD 30 - 40 per ton of sugar, I am getting a loss figure for the manufactured output. Also, have you taken any inventory write-down in the standalone operations on sugar?

Narendra Murkumbi

We do not give a breakup between the two. In the cane milling division the cost of cane has increased more than the price of sugar and therefore we have a very low margin and most of the contribution is from the refining segment. Secondly, our inventory costs are in linewith market prices and therefore there is no write off.

Nirav Shah

So what is the value of the inventory?

KK Kumbhat

We have a total inventory of finished goods which is more than 0.5 million tons. We will revert with the average price later in the call. (The inventory value in India and that composes inventory both at the refineries and the mills and the average price is about Rs. 30,100 per ton.)*

Nirav Shah

For RdB and RVdI what would be the EBITDA level cost of production in the current season?

Gautam Watve

Basically the cost of production is highly dependent on the yields that you get from the cane that we own. So over the last year we were able to increase the yields mainly because of planting as well as weather by about 10% from 60 tons/ha for year 2011-12 to about 67 tons/ha for 2012-13. If we look on the basis of expected yields of about 72 tons/ha for the region, we would have an EBITDA cost of production of about USD 15 cents/lb.

** The inventory value was clarified later in the call*

Nirav Shah

RVdI would still be very profitable at around slightly below USD 15 cents/lb?

Narendra Murkumbi

RVdI costs will be even lower because the yields there are predicted to be about 78 tons/ha of this year. As Mr. Gautam Watve explained earlier in RdB we expect a further improvement in yields this year from 67 tons/ha last season to 72 tons/ha this season and this is yield we are actually realizing in April and May. This cost is reckoned at USD/BRL exchange rate of about 2.05. The exchange rate has also further weakened which will further reduce the cost of production in USD terms.

Nirav Shah

On the cane availability for the Brazilian industry, UNICA estimates that there is a possibility of around 18 to 19 million tons of cane to be carried forward to the next season. Is this figure included in the 589 million tons to be crushed and is there any possibility of this 18 million tons being increased to a higher number based on the current stress?

Gautam Watve

The 590 million tons of cane crushing which UNICA estimates for Centre-South Brazil this year has used the fact that 18 to 19 million tons will get pushed over as *Bisada* (carry-over) cane into next year. Now this cane crushing is actually a function of how much it rains this year. So if it rains below normal in Brazil then we would be able to consume part of that 19 million tons of cane as well, otherwise if it rains more, like in 2009, then that 590 million tons would also be lower. So, it is not a factor of the industrial capacity but a factor of the rain days lost throughout the year.

Nirav Shah

Last question on the hedging front, we had some hedges at USD 20.5 cents/lb. Are we now planning to reduce the sugar production and maintain the production at the hedges level and focus more on ethanol or will it still be around 80% of our target sugar production level?

Narendra Murkumbi

As Mr. Gautam Watve explained earlier, we expect to crush 11 million tons of cane this season and as per the plan, against our 60% production of sugar last year, the production mix right now is around 35% and is expected to rise to a maximum of 42% this year. So based on that, maximum quantity of sugar that we would sell this year would be by utilizing the existing hedges and there would be only a small quantity which would not be covered by the hedges that we already have. The unhedged quantity would be counterbalanced by the fact that our cane payment is as per the consecana formula which takes into account the daily average New York sugar price and therefore there is an offsetting hedge against that. To that extent we will have a reduction in our cane costs also. In that sense, one can consider that we are fully hedged on the sugar side.

Moderator

Thank you. We have the next question from the line of Arya Sen from Jefferies, please go ahead.

Arya Sen

On the levy sugar, do you have any commitment of levy sugar on your refining production that gets sold in the domestic market and if so is that included in that Rs. 120 crores annual impact that you talked about?

Narendra Murkumbi

The estimate that I gave was based on the sugar production that we are going to have from October 2012 up to September 2013. Since there is a lag in levy lifting, this levy obligation would have come from 1st June 2013 up to roughly May 2014. For the estimate we had included the sugar production both from refining for Indian consumption and milling in India.

Arya Sen

Currently, is all your production from Haldia refinery being sold the domestic market or is some part of the Haldia production also being exported?

Narendra Murkumbi

Currently the Haldia refinery is marketing almost more than 90% of its sugar in the domestic market and the Kandla refinery is completely focused on exports.

Arya Sen

What is the consolidated debt figure?

Narendra Murkumbi

It is Rs. 8,426 crores.

Arya Sen

And this is as of 31st March 2013 for the Brazilian operations as well?

Narendra Murkumbi

We have harmonized the balance sheet date for all our subsidiaries right from the parent and the Brazilian subsidiary.

Arya Sen

What is the outlook on domestic planting in Maharashtra as well as the rest of the country for the next year?

Narendra Murkumbi

Last year the industry and the market were all caught by surprise by the fact that despite a big drought we still had significant production and came close to 25 million tons of sugar produced. Last year we had about 5.2 million hectares of cane planted in India and ultimately produced 24.8 million tons of sugar. So coming season, which we start in October 2013, we have at the moment a reduction in planting of 0.5 million hectares. This is not the final figure as there is a possibility that some planting will catch up, though there is very little time left. There is also a possibility that there will be a further slippage between last year and this year. It looks likethat we will be short by 0.5 million hectares to end with. The final figure should be available by end of June 2013 and that would imply a reduction in sugar production of between 3 to 5 million tons of sugar. Beyond that I do not really want to speculate, I think satellite imaging etc. estimates would be available by end of July 2013 on the total cane available, but just looking at acreage there is a significant drop in production.

Moderator

Thank you. We have the next question from the line of Achal Lohade from JM Financials, please go ahead.

Achal Lohade

On the debt number you said that it has reduced from Rs. 10,000 crores to about Rs. 8,400 crores and you said that the working capital debt is financed by suppliers credit. Can you please add elaborate a little bit on that because I see the current liability has gone up substantially by equivalent numbers ?

Narendra Murkumbi

I will ask our CFO, Mr. KK Kumbhat, to explain this to you, but in general I just want to make a point that, our revenues have gone up 50% year-on-year in India and we are doing it with virtually the same amount of capital on the balance sheet. I am looking at everything i.e. debt, current asset, current liabilities combined, we have been able to grow the business using the same amount of capital and we are generating 50% more revenue. Of course margins are lower year-on-year and that is why you do not see the full impact on the P&L. Now with that statement I will request Mr. Kumbhat to explain about the supplier credit.

KK Kumbhat

For imports we do not pay the money immediately. You get the credit for import of materials which can go as high up to 360 days. Now we do not use 360 days, we use in the range of 90 to 180 days depending on our requirement and as a result, this year there is a drastic reduction in the bank borrowings and the portion is getting compensated by the increase in the creditors.

Achal Lohade

And what is the cost for this extension?

KK Kumbhat

This actually is anywhere between 2.5% to 3% per annum.

Achal Lohade

There is also one thing that you mentioned, the other subsidiaries that is at Rs. 670 crores. Just wanted to know which subsidiaries are these because we believe that it is only Brazil and India.

Narendra Murkumbi

It is mainly short-term trading credit in Renuka DMCC against their trading turnover and it is in the same range as the previous year.

Achal Lohade

So Renuka DMCC is yet to be consolidated or merged with the parent company, is that correct?

Narendra Murkumbi

We are in the process and we expect it to take a few months but it should definitely be done in the current financial year. And lastly I want to point out that in the balance sheet we have been able to stabilize and maintain the balances on most of the heads, so there has been no expansion of the balance sheet not only on debt but also other items, similarly on other subsidiary debt it is almost the same year-on-year.

Achal Lohade

Can you please elaborate a little bit on the debt side for Brazil? Recently there was some news report that we may look at raising money through the issue of bonds, so can you please elaborate a little bit on that?

Narendra Murkumbi

As you may have noticed, we immediately issued an official denial to the stock exchange about the article. There is no question of any kind of guarantee from the parent company on any new borrowing in Brazil and neither are the current loans guaranteed there. Now in the normal course of business obviously the Brazilian subsidiary will be looking at refinancing debt which comes due. There is definitely nothing which we believe is going to be guaranteed by the parent company, so that is the clarification. In terms of the original debt restructuring, when we took over the company Renuka do Brasil S/A in 2010, the bulk of the loans had been rescheduled for three years moratorium and a seven years repayment period. Given that the entire industry is going through massive effects of drought and frost in 2011 and then in 2012 to a lesser degreewe have also gone to our banks in Brazil and rescheduled some of the upcoming term repayments which were due in the next two years in order to give us greater liquidity. We will use that money to plant more cane and that is how we have more cane crushed year-on-year for last year as well as the coming year. The process has already been completed in the last quarter. So this is the situation as far as far as debt is Brazil goes. In Renuka do Brasil S/A the debt has remained almost constant last year because of this. In RVdI we have started repayment of our debt because the moratorium period is over and the debt has reduced from about Rs. 942 crores to Rs. 840 crores.

Achal Lohade

What is the scheduled repayment obligation for the current year and next year, FY14-15?

Gautam Watve

For Renuka Vale do Ivai S/A it is about R$ 60 million and for Renuka do Brasil S/A it is about R$ 180 million.

Achal Lohade

And it is the same for FY15 as well?

Gautam Watve

Yes, similar numbers.

Achal Lohade

And how about India? Also the average cost of debt also for Brazil and India as well ?

Narendra Murkumbi

In India, last year we have repaid maturing term liabilities as well as raised more new long-term money in the form of debentures, etc. For the current year Mr. Kumbhat will have the numbers of maturing long-term loans.

KK Kumbhat

Next one year maturities in India is roughly about Rs. 625 crores which is already given in the balance sheet by a footnote and average cost here for total long-term loans we are in the range of about 8% to 8.5% for local and foreign currencies put together.

Gautam Watve

For Brazil, the cost of debt will be about 9%.

Moderator

Thank you. We will take the next question from the line of Sanjay Satapathy from Merrill Lynch. Please go ahead.

Sanjay Satapathy

In case of Brazil, are we seeing some kind of consolidation which will give us a lead indicator as to production will decline in the next season, because we are hearing that some of the mills are closing down because of financial stress?

Narendra Murkumbi

The mills that are closing down are typically in the range of 0.5 to 1.5 million tons per factory which is considered sub-optimal in Brazil, as they have high fixed costs relative to their size, and are mainly family owned and older mills. So some of them have closed down and up to 28 mills could close down in the next two years. But this phenomenon will not have a significant dent on capacity. I think the biggest positive in Brazil in the last three months is that the Brazilian Government has again re-engaged with the industry to try and boost ethanol consumption in fuel. After the expansion of sugar being much more attractive for last two years, the share of ethanol in the overall fuel consumption in Brazil had been shrinking and we have had three strong policy measures in just in the last three months after Christmas. First is the increase in the blend of ethanol, second is the tax break which is substantial and it is valid up to 2016, so we are allowed to retain local taxes of almost 12% of the value of the product and the third was the increase in the price of gasoline which makes ethanol more competitive. So all these three factors will together divert almost 4 million tons of sugar into ethanol which otherwise would have been sugar. So I feel the reduction of sugar exports from Brazil is being achieved by the expansion of the ethanol consumption domestically and this will be the trend for next year as well.

Sanjay Satapathy

What quantity of sugar production are you really focusing for Brazil for this year and next year?

Narendra Murkumbi

Despite an expansion of almost 60 million tons of cane, sugar output may rise to about 34 million tons which means an increase of about 2.5 million tons over last year.

Sanjay Satapathy

Are you worried that the corn plantation in USA is rising and that will affect the global ethanol price?

Narendra Murkumbi

The main markets for Brazilian ethanol is the domestic market and the expansion there is of the order of 4 billion liters this year while the exports to USA are about 1.5 billion liters. As I explained in the previous call the export of Brazil ethanol does not directly compete on price of corn ethanol because they go for the advanced biofuel mandate in states like California where corn ethanol is not eligible. So right now we do not see any significant bearish impact from the corn fundamentals in the USA.

Sanjay Satapathy

In India you have already mentioned some amount of decrease in sugar production, but is there a possibility that it will fall below consumption by next year?

Narendra Murkumbi

I think it will definitely fall below consumption. We have opening stock of about 7.5 million tons. So the extent of the fall in production will be significant in the way that prices move domestically. I think we definitely have a very high cost structure in North India but demand-supply estimates will be decided by the final 2 million tons of production which could be critical and it is a bit too early to speculate on the exact production number. Therefore I just restricted myself to pointing out the change in planting area and after that we have to observe how things go.

Sanjay Satapathy

But arrears continues to be high as mills are not making any efforts to pay off the arrears?

Narendra Murkumbi

Well it is interesting to see that even profit-making companies seem to have large cane arrears. I must clarify that Renuka has zero cane arrears at the moment but it does appear that many companies are having arrears despite reporting profits, so one wonders what is happening. The absolute number is very high and across the country it is close to Rs. 10,000 crores.

Moderator

Thank you. The next question is from the line of Vernon Fernandes from NVS Brokerage. Please go ahead.

Vernon Fernandes

Just want to know to what extent is third-party planting is likely to contribute to our plantation mix going forward?

Gautam Watve

Currently we have a mix of 65% of own cane and 35% of supplier cane. The plan is to try and bring this down to 50%. So we are currently working on that on a gradual manner each year and that will mean that we will be sharing the cane risk with the farmers on an equal basis.

Moderator

Thank you. The next question is from the line of Nirav Shah from Antique Stock Broking. Please go ahead.

Nirav Shah

Can you just share the performance of the Dubai-based subsidiary in terms of revenues and PAT for FY 2013?

KK Kumbhat

For the 12 month period FY 2013 RDMCC, that is the Dubai subsidiary, had a total income of Rs. 1,820 crores, EBITDA of Rs. 140 crores and net profit of Rs. 91 crores.

Nirav Shah

What is your view on again the industry asking for an increase in import duty from 10% to 30% because a lot of UP based manufacturers are asking for that, so what is the sense on that?

Narendra Murkumbi

I think sugar prices are stable over the last 12 months and from the results we reviewed for 12 listed companies, nine have made a profit so I do not see the reason for asking an increase in import duty and that is what I mentioned earlier that sometimes it seems that the cane arrears are tactical rather than real.

Nirav Shah

The global sugar prices being low, are we seeing any increase in consumption because the estimate says that it will increase by 1% this year? Last time what happened is that when prices were USD 30 cents/lb the demand was impacted.

Narendra Murkumbi

Speaking of both demand and supply, I think a lot of surplus this year is in the high cost countries like Eastern Europe and parts of Asia where the production has been primarily encouraged by two years of very high global prices and this sugar production is causing the current year surplus. Early estimates of next year surplus by both Kingsman and the International Sugar Organization are already showing a sharp reduction in the surplus and in our opinion that could even go to zero if the current trend of higher ethanol consumption in Brazil continues. I feel that we already see a very big decline in planted area of sugar beet in Europe this year for the winter and we will have a similar adjustment in high cost production areas of sugar cane in the coming 12 months because sugar cane has a longer crop cycle. So I feel for the current cycle, 2013 is the peak of the surplus and as we go forward the situation should get more balanced pretty rapidly. Now on the demand side we see a lot of the regional demand first hand in our Kandla refinery and at the current sugar prices, which are the lowest of the last 30 months, we see a very strong demand both for current consumption and restocking in most of the importing countries in the region. I think this is a similar story across the world and therefore in terms of despatches we will see a higher number this year because of the sharp reduction in prices.

Nirav Shah

If we look at the deviation from the initial estimates for all the states in their production, I think Maharashtra has played the main role in terms of actual production versus estimates. Is there a case that a lot of cane which would have been used as seed for the next season is used or that is not a thesis at this point of time?

Narendra Murkumbi

No there are two factors, one is the yield, which were protected better than normal by farmers given that the cane price was so attractive and the crop was very valuable. The value of the crop was more than Rs. 1 lakh per acre. Secondly yes, a significant amount of seed cane has got crushed this year because in some areas there is no water for maintaining a sugarcane crop for the coming season. So, while farmers have taken a lot of costs and pain to preserve the current crop until it was crushed, they are not replanting sugarcane. So both the factors are at play which I would say contribute roughly 50% each.

Nirav Shah

So Maharashtra can see at least a 20% or 30% drop in sugar production in '13-14 season?

Narendra Murkumbi

I think today is not the day to make a firm estimate but it is definitely going to be lower than last year.

Moderator

Thank you. We have the next question from the line of Arun Baid from IDBI Capital. Please go ahead.

Arun Baid

What is the current cost of landed raw sugar if we convert in our country and what kind of imports have already happened in the country in this season?

Narendra Murkumbi

The landed price today is the world price plus a freight of about USD 40 per ton and current imports to date are about 450,000 tons.

Arun Baid

And do you expect it to pick up because the difference between the landed costs and your conversion cost is significantly lower than your rated market prices, do you expect that to pick up significantly?

Narendra Murkumbi

In our refining division, on imports, there has been a margin expansion in the last two months since March because of the decline in world prices whereas we have had a stable domestic price. Hence there has been an increase in margin in the current quarter.

Arun Baid

What is the hedged quantity in Brazil for the current season and at what price?

Narendra Murkumbi

I will mention the hedged prices in R$ per ton of sugar because that is relevant finally to the P&L. Also for some of the sugar, the currency is hedged along with the USD sugar price. In RVdI we have about 150,000 tons hedged at average price of about 1000 R$/ton and in RdB we have hedged about 375,000 tons at an average price of 900 R$/ton.

Moderator

Thank you. The next question is from the line of Manish Mahawar from Edelweiss. Please go ahead.

Manish Mahawar

Next year what is the crushing target for Brazil?

Gautam Watve

The crushing target for 2013-14 year is 11 million tons.

Moderator

Thank you. We will take the last question from the line of Rahul Agarwal from VEC Investments. Please go ahead.

Rahul Agarwal

I just wanted to know on the debt repayment, the RdB repayment of R$ 180 million and India repayment of Rs. 625 crores to be repaid in fiscal 2014, when is it due? Is there a day to it or is it staggered over the year?

Narendra Murkumbi

It is staggered as most of it is the amortizing debt, so there are repayments every quarter. There are no major bullet payments anywhere. We had a similar amount last year and we do not see any problem with refinancing this debt.

With that I would like to thank all the participants for participating in today's call and thank you for your continued interest in Shree Renuka Sugars.

Moderator

Thank you Sir. Ladies and Gentlemen on behalf of Shree Renuka Sugars that concludes this conference call. Thank you for joining us.

Note: Transcript has been edited for better readability

sugar ethanol power

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Safe Harbour

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