



“Welspun Corp Limited Q3 FY17 Earnings Conference Call”

February 10, 2017



**MANAGEMENT: MR. LALIT NAIK - MD & CEO, WELSPUN CORP,
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Moderator: Ladies and gentlemen, good day and welcome to the Q3 FY'17 Earnings Conference Call of Welspun Corp Limited. As a reminder, all participant lines will be in the listen-only mode and there will be an opportunity for you to ask question after the presentation concludes. Should you need assistance during the conference call please signal an operator by pressing '*' then '0' on your touchtone phone. Please note that this conference is being recorded. Representing the Management, we have Mr. Lalit Naik – MD and CEO of Welspun Corp. Mr. S. Krishnan – CFO of Welspun Corp and Mr. Akhil Jindal – Director (Finance & Strategy), Welspun Group. I now hand the conference over to Mr. Lalit Naik. Thank you and over to you Mr. Naik.

Lalit Naik: Thank you. Good afternoon guys. I'm Lalit Naik and this is my first interaction with you after taking over as the MD and CEO of Welspun Corp. You must have seen the presentation we made in the morning. Clearly we had a tough quarter in terms of the financials. But I am sure going forward we are going to do well and this is predicated on the basis of a change in the market scenario, predicated by what is happening in US and of course overall in the Oil & Gas Industry. I will request Mr. Krishnan to take you through our presentation and then get into answering whatever questions you have. Thank you.

S. Krishnan: Thanks Lalit. Good afternoon friends. Before we start discussing the Q3 performance, please let us remind you that the due to implementation of the IndAS accounting standards all the numbers for this quarter as well as last year's relevant numbers are restated as per IndAS and the presentation and the details are there in our publication which we have sent you. But a few opening statements to explain the performance in better details.

In terms of volumes excluding Saudi, which is not consolidated under IndAS, production was around 202,000 tonnes up around 4% Y-o-Y but due to delay in dispatches sales around 163,000 metric tonnes was down to about 14% Y-on-Y. Including Saudi, the pipe production was down 22% to around 203,000 metric tonnes. That sales was down by 35% to 163,000 metric tonnes. Saudi business did not have any direct sales. They only did some tolling jobs during the quarter. The dip in volume was largely led by continued delays in the execution of some large projects.

The order book now stands just under 800,000 tonnes valued at Rs 4,800 crores. The bid book is around 4 million tonnes and a future potential project that we see over the next couple of years is around 9 million tonnes.

Coming to financials the weak volume has obviously impacted the overall profitability. On IndAS basis Q3 revenue Y-o-Y was down around 28% to around Rs 1200 crores and reported EBITDA was down around 32% Y-o-Y to around Rs 171 crores. PAT after minorities and share in associates and JVs, was a marginal loss of around Rs 4 crores versus a Rs 53 crores profit in Q3 of the last financial year FY'15.

Welspun Corp Limited
February 10, 2017

In terms of the balance sheet the lower revenue base, relatively higher business activity particular in preparation for the Q4 which is relatively higher in terms of volumes and expectations of throughput and also back-ended supplies to some of our customers has made the working capital intensity in the cycle of this quarter much higher and it stands at around 69 days versus 39 days for the last quarter, on a 12-month trailing basis. These are for the consolidated business on the erstwhile Indian GAAP. On an IndAS basis the cash conversion cycle is around 51 days which is also higher than what was the equivalent 26 days for the last quarter. Consequently, on a quarter-on-quarter basis the net debt has gone up by just under Rs 300 crores to about Rs 1,655 crores on I-GAAP basis. On IndAS basis net debt has gone up by around Rs 400 crores to just over Rs 1200 crores from what was just over Rs 800 crores as of end of September 2016.

Our commitment to conserve cash and maintain lean balance sheet remains. With no major additional CAPEX programs, the cash flow generated from the operations would largely be used to cut down debt. The debt increase that has happened in the current quarter is largely working capital. No new significant long-term debt has been raised.

In terms of the outlook of the business, we have been witnessing turmoil in global energy markets for last several quarters, it is only recently that we have seen some stability coming in and oil seems to have found a floor at USD 50/ barrel. Volatility in energy market has impacted execution of some of our existing projects as well as delayed final investment decision of some major projects. But as we speak and as Lalit indicated, the global market is more stable than before and the industry is adopting to the new normal of oil at 50+. We see a fairly positive outlook for the line pipe market in the quarters ahead. This is led by key markets. In India, the National Gas Grid has taken momentum and there are several water projects coming up across multiple states locations and this is going to see significant volume growth in the domestic business. In the medium term we expect the global demand to pick up across MENA markets and a few other markets as well.

Last but not the least is while in the last few quarters it has been very difficult in terms of revenues and particularly in terms of profitability. This year as well so far has been possibly one of the most challenging years for Welspun Corp. However, we continue to engage more closely with our worldwide customer bases, invest in technology and expand our capability. We see early signs of a turnaround in some of our major markets particularly in North America. The effect and impact of this will be more evident in the next couple of quarters and that is what gives us a little bit of confidence as we go ahead.

That is from our side. We will be happy to take your questions.

Moderator:

Thank you very much. We will now begin the question and answer session. The first question is from the line of Nirav Shah from GeeCee Investment. Please go ahead.

Nirav Shah: Sir few questions. Over the last two quarters we have seen some 60,000 tonnes of build-up in inventory. So you mentioned in your opening remarks that part of it would be some deferment in deliveries. So, is that entire thing executable will come up in the Q4 execution or how do you see that number? There is incremental inventory buildup of 58,000 tonnes?

S. Krishnan: So when you are seeing inventory, it includes inventories of raw materials as well, not just finished good. Whatever is the finished goods inventory as of end of December would largely get shipped out and billed in next quarter. But inventories in the form of coils and plates which are required, would not always be shipped out in the next quarter that could flow on to the quarter one of the next financial year.

Nirav Shah: Sir I am talking about the only difference between the pipes production and pipes sales, so that number is coming to around for 2 consecutive quarters we have seen a build-up and December and the cumulative two quarters number is 50,000 tonnes.

S. Krishnan: And in this quarter if you see, about 160,000 tonnes of sales and 202,000 tonnes of production.

Nirav Shah: 50,000 tonnes, yeah.

S. Krishnan: It is around 40,000 tonnes. This will get build in the subsequent quarter.

Nirav Shah: So that execution is relatively very smooth going into Q4?

S. Krishnan: No, these are just to clarify, what we meant slow-down is that, when a customer asks for a deferment or a delay in their delivery schedule to the extent possible we will also delay shipment of pipes and where possible also delay rolling of the pipes. But we would not be sitting on unusable steel.

Nirav Shah: Got it. Sir second question on the industry front, first in India we have seen few orders being awarded. Be it in the ERW space where one of our competitor won an order of around 130-odd crores, even on the seamless place though we are not present there but we have seen some traction. So how have we participated and if we calculate the realization on the ERW order it is coming to close to Rs 60,000 a ton. So is the pricing also now very reasonable in these orders, where do you see your participation in these order going forward?

S. Krishnan: See, you know you are right. I think there has been one such orders that has opened in the domestic space. That has been promising and we see hardening of prices in the domestic market starting with our raw material that is plates and coils and that I think is in the public domain you would have seen it over several weeks and almost couple of months now. That has also helped the domestic market in terms of line pipes. So whether it is oil & gas or whether it is water we see the markets comparatively higher prices and consequently better margins for us. We see this sustaining for some time because there is significant stress in the

domestic market on two segments. One is this gas grid in the Oil & Gas and the second is this water projects which are upwards of around 1.5 million tonnes at the immediate future across multiple states and corporations. So each of this is looking far more promising than what was the situation may be 3 months or 6 months back in terms of market.

Nirav Shah: So water you mentioned around 150,000 tonnes of opportunity and gas grid would be how much?

S. Krishnan: In the water we said is around 1.5 million tonnes is the estimated project size across multiple projects.

Nirav Shah: So kind of you can say next 12-15 months?

S. Krishnan: Yes.

Nirav Shah: And then in terms of gas grids what will be the opportunity.

S. Krishnan: That would also be in the region of more than 0.5 million, in the range of upwards of 0.5 million tonnes.

Nirav Shah: So kind of 5 lakh tonnes.

S. Krishnan: Yes.

Nirav Shah: And we are participating on these orders?

Lalit Naik: Yes, to the extent possible in terms of our technological capability. We are participating in all the oil and gas orders as well as significant portion of the water orders. So our optimism is based on the demand which is coming up and of course the fact that better pricing is being kind of facilitated due to higher input cost. So that is what it is.

Nirav Shah: My second question on the demand opportunity in USA, we believe that Dakota and Keystone order cannot present a lot of opportunity to pipe manufacturers, but how we see that pipeline from the US market going up and if you could just give us broad break up about the US market in terms of how much it is for oil pipes, how much it is for gas pipes because oil prices have recovered, where as gas hasn't recovered to that extent. So how do you see the US market shaping up in both these segment, Oil & Gas.

Lalit Naik: At this point in time the picture isn't very clear in terms of how much and the timelines. What the order has done is basically brought about a little bit of optimism in terms of the Oil & Gas pipeline industry. On the ground, the oil rig counts have increased, this will definitely lead to an increase in the OCTG demand to about 2-3 million tonnes, that is what our estimate is. And

Welspun Corp Limited
February 10, 2017

very clearly about a million tonnes out of this would be addressed by the HFIW segment where we are present through our HFIW facility from Little Rock. The potential market would be about a million tonnes in the coming days. And this would be targeted, besides us, by exporters from the other Asian countries like Korea and China besides the American players. We are optimistic that we will get a fair share of that. As far as the large cross country pipeline or trunk line projects are concerned, besides Keystone and Dakota at the moment we are not very clear about what new demand would come up and surely we will not be able to give you at this stage a clear demarcation between what is oil and what is gas. Now coming to your earlier comment that KXL and Dakota may not provide great operator or great opportunity to us that I do not agree fully with you because the assumption is that as and when they get commissioned the residual demand would still be significant and since we are contenders for both these projects, expect meaningful volumes from our point of view.

Nirav Shah: Got it sir and sir the final question is last quarter you shared some optimism on your coating facility and you getting some orders. So any further updates on that facility or in terms of how much traction you are seeing over there?

S. Krishnan: You are referring possibly to the CWC coating. The position does not change significantly, the mill information commissioning is happening as we speak and we hope to end it somewhere around this quarter or early next quarter and the order execution will start somewhere in the middle of next quarter. And as of now there are quite a few projects that are being addressed in the domestic space and elsewhere but none of this is still closed for us to be able to give an add on to the existing order book of the CWC business.

Lalit Naik: The comment over here would be beside the project which we have in hand, which as Krishnan mentioned we will start executing from the middle of next quarter. I think ONGC offers us a good prospect given the fact that they are looking at buying a significant quantity of cement coated pipes in the coming months and years. Now very clearly we will have to seek approval at ONGC which will happen as a part of our execution of the current project we have in hand for an American customer. So I presume orders will start flowing in from the domestic sector once we get the approval from ONGC who is one of the major customers.

Nirav Shah: And so, really final question. The profitability in the current order book, I mean, if we look at we made around Rs. 6,900 in this quarter and Rs. 5,600 per tonne in Q2. So should we more or less maintain around the latest quarter levels?

S. Krishnan: Well I think you are right. This quarter there is a shade under 7,000 but on a 9 months basis it is around Rs. 5,200. I think we would be in the region more or around Rs. 5000 to Rs. 5,500, but I think we will have better visibilities as we go into the next quarter because that is when we will see the early signs of the new orders and there profitability, right? As of now we see

projects possibly coming up but it is too early to make a call on the profitability of those orders that will come out of those projects.

Moderator: Thank you. The next question is from the line of Vivek Sharma from ICICI Securities. Please go ahead.

Vivek Sharma: My question is more on the demand environment, my first question. In the previous earning call you mentioned significant amount of projects, close to may be 750 KMT of orders, that are likely to be awarded by January '17, but we have not seen any major announcements. So what is the status of the same and recently we have heard a lot about Canada approving pipeline, the US clearing two large projects, even Iran is inviting investment in that space. So how do you see the demand environment from a 6-12 months perspective and what is our view on participation in the Iran project. Would we participate and what kind of business can the whole Iran thing give us?

S. Krishnan: You are right, last time we said that there are potentially orders in the region of 500-1000 tonnes which should come up for closure sometimes this quarter. You are absolutely right that none of them have really closed significant enough to make an announcement. That is also because some of them, as we talked earlier in the call, there have been delayed, there have been deferments in some of the final closure of these projects. But as we speak, most of those projects are still available and we still believe that many of them will get closed in the next 6-8 weeks and hopefully it will be reflected in our order book for the next financial year and coming back to your earlier question in terms of the announcement, you are right, while the new administration in the US has given some positive indication in terms of their preference for linepipes in Oil & Gas. We have also seen equally positive movements coming in from Canada with approving a couple of projects. So all these are large cross country mega projects and many of them are highly technologically intensive and that is where Welspun comes in as a global supplier. We believe that this will change the sentiment to invest in North America and a key driver for the global business as well. And when the sentiment to invest changes, we will see many of these projects which are part of our bid book of around 4 million tonnes, they will come back into action and some of them will get closed into projects, bids and awards.

Vivek Sharma: Can we see these orders fructifying in this calendar year? The US and Canada one.

Lalit Naik: I think you will clearly see certain projects medium-to-large size projects being awarded. When we specifically talk about those which come under Trumps Executive order I think the optimism is higher. But then they would be for residual quantities or may be a little more than what we expect. However, there are projects in Canada for example, one large size projects in Canada called Coastal Gas is expected to be awarded in the third quarter of 2017, the current year which is a large size project. We also expect that couple of players from the US like Kinder Morgan and so on, would bring back the projects, which they have shelved, back to the

table. So there will be some large size projects which will be on offer as an outcome of both the oil price going up, increase in drilling activity and support from the Trump administration for sure.

Vivek Sharma: And sir on Iran front, what is our view, how can we pan out?

Lalit Naik: So for Iran, I think we need to be cautious because while it is evident that there is latent demand in Iran to the extent of more than a million tonnes, we do not know the timing, but if I really go into the details, the earliest visibility for any kind of project in Iran is again third quarter, fourth quarter of this year. Okay, we are talking about one particular pipeline project. Our interest in Iran would be if at all, on the plates side where in we would supply some plates if there is an opportunity available to us.

Vivek Sharma: Not on the line pipe side?

S. Krishnan: Yes, just to add to what Lalit is saying, supplies of plates or supplies of line pipes will also be subject to the current sanction regime being vacated. So that is a fundamental condition for us to be able to transact in that market. And it is anybody's call how near or how far the sanctions will get vacated.

Vivek Sharma: Sir my second question is on your debt levels, while we really find it difficult to understand the debt levels going up. I can understand the working capital intensity might have gone up. What do you see the kind of debt levels towards the year-end and in next 6-8 months, will we see a deleveraging exercise further? We have done a decent enough job in the last two years, but should we feel the exercise to continue going forward or you think working capital pressure, when some of the large projects are in the pipeline, could hinder our ability to pay down debt?

S. Krishnan: Between September and December you are right, the net debt figure has gone up and has almost entirely because of short-term debt relating to the working capital ramping up for the higher volumes, throughput for the next quarter that we need to prepare for. As we said earlier on the call, whatever cash flow comes out of the business there is very limited CAPEX that we need to do. So pretty much the significant portion of the cash flow will be used to bring down the net debt and that agenda continues. There will be movements in the net debt situation more driven by working capital. On the long-term book it is only a question of realigning debt between one geography to another geography, one currency to another currency or pushing the tenures or extending the tenures or making it softer on the book or less cost intensive on the books. There is no agenda to borrow for around any project or any other purpose and coming to not as a guidance but more as an indication, we would like our net debt to be knocked off by couple of 100 crores between now and March.

Vivek Sharma: And sir that the following year.

S. Krishnan: That I think what we will do is, we are in the midst of finalizing our business plan and budget for this year and some of the developments in North America have made it far more interesting than what was the situation a couple of weeks back and we need to rework our expectations on the key market. So may be when we do our next call we will be in a better position to give you sense of what we believe would be the debt position for the next year. Having said this, not only for this quarter, for this year you have seen us being financially very conservative. Our focus on maintaining balance sheet controls, our focus on controlling leverage and our focus on net debt will not get diluted has that been for the last 3 years or 4 years for the next couple of years.

Moderator: Thank you. The next question is from the line of Vikas Singh from B&K Securities. Please go ahead.

Vikas Singh: Sir you said that some quantum of shipment got delayed this quarter. So could you just quantify how much in...?

S. Krishnan: Vikas, this volume of 40,000 tonnes is on a global book. So it is lying in multiple geographies, some of which are in transit where the term of trade with our customer are based on delivery at their side. So revenue recognition will happen on delivery side, out of which are not loads which are completely enough for our shipments. So to optimize shipments and logistics cost we will wait for a full ship load of materials to be shipped.

Vikas Singh: Sir just looking at the shipment of whatever it is, is it fair to assume that the next quarter your volumes can be significantly up from current levels?

S. Krishnan: As we said earlier, some of the delays that have impacted our Q2 and Q3 volumes that should benefit the next quarter and we believe we should be doing much better volumes next quarter.

Vikas Singh: And secondly sir looking into your total pipe sales, Saudi mill was almost shut for this quarter. So just some color on the Saudi mill whether we had some orders and how do we see execution from there, what is the kind of EBITDA generation is there, if you could throw some color on that?

S. Krishnan: Right Vikas, This quarter pretty much we did not have any full supply orders. We did some tolling jobs as we indicated on this call. We are, in the current quarter, executing some orders which will keep us engaged for most of this quarter as we speak. There are quite a few interesting possibilities in terms of projects and bids which will be relevant for the next financial year. Many of these will come up for bidding and award over 8 weeks to 10 weeks and this is what we intend to reflect in our business plan and budget for the next financial year. Having said this, this year has been one of our very difficult or challenging year in the Saudi market. In terms of volumes and particularly in terms of profit.

- Vikas Singh:** So sir, next year what kind of opportunity you see from that region?
- S. Krishnan:** There are opportunities ahead. One is the domestic market they are trying to move the oil consumption in the domestic market to gas and available oil is being moved on to the ports for export. So these are the two main drivers of Oil & Gas pipeline in the domestic market in the kingdom. Second is whole range of water supply project across the Kingdom. These are the two main segments which will drive our business and volumes in the next year as well.
- Moderator:** Thank you. We have the next question from the line of Bhavin Chedda from Enam Holdings. Please go ahead.
- Bhavin Chedda:** Few questions, first on the mix, if I am seeing your plant wise mix of 5,96,000 sales volume, I think Saudi is 16% and US is 20%. So how is the scenario of the current order book, how much of this order book is now pending at the US plant and Saudi plant. If I say 8 lakhs tonnes is the closing order book now, so out of this how much of the order is out of Saudi plant and out of US plant?
- S. Krishnan:** Bhavin, a predominant portion of this order book that you see, is to the service from India, almost about (+80%) because many of these are long seam pipe. Order book in US and Saudi is relatively weak at this point of time and we still have enough capacity and ability to take up quite a few orders and execute them over the course of next financial year.
- Bhavin Chedda:** So, just getting the details. I am seeing your slide #8, so ERW is 94,000. So does it include any of the HFIW order of the US mill or hardly there is any HFIW order as of now?
- S. Krishnan:** Not too many. I think those orders, don't move the needle. I mean, on 800,000 tonnes order book surplus of those would be not really significant in terms of volumes for the US business, if that is what you are referring.
- Bhavin Chedda:** And US mill will have a 3 lakh tonnes spiral capacity and 2 lakhs tonnes of HFIW capacity, right?
- S. Krishnan:** Generally you can say that, but HFIW has not just caution you it depends upon the mix. That is whether it is thickness and all you know the arithmetic. So if you see we have a relatively higher wall line pipe, 200 is also doable.
- Bhavin Chedda:** Coming to the bidding as of now, the live bidding. I think you somewhere said that current bid book is roughly around 4 million tonnes, right?
- S. Krishnan:** Yes.

Bhavin Chedda: Which if I am not mistaken, last conference call we were at 3.2, so has the bidding gone up in last 3 months?

S. Krishnan: There has been some projects that have come up across the few markets and that is what has increased the overall bid book to around 4 million tonnes.

Bhavin Chedda: Also, should I assume there since your press release and your comments is mentioning of a strong buoyancy in domestic market, so have we participated in few bids in domestic market which may ultimately turn into order in few weeks, because you mentioned of the very high number on the water pipeline projects in India. So have this few of the projects been already being bided in India?

S. Krishnan: Some of them, yes. Many of them at various stages of bid opening. Technically we will be able to supply to all these projects in water and oil as long it is our range of products. Commercially we may not be able to match every other vendor. So we will have the opportunity to select what makes commercial sense to us and what makes capacity sense from our facilities.

Bhavin Chedda: And sir what was the plate mill EBITDA for the quarter in 9 months?

S. Krishnan: I think it was in the region of around 60 odd crores.

Bhavin Chedda: This was 9 months?

S. Krishnan: Yes.

Bhavin Chedda: Which means quarter would be around 4-5-odd crores. So basically after three to four years for the first will miss out on the annual sales volume of one million ton what we regularly do. So again for next year I think it is too early but can we assume the way the statements have been coming from Canada and US that next year will be back to crossing that one million tonne volumes?

S. Krishnan: Well, Bhavin what you are saying sounds like music to us. We are re-engaging ourselves in detail in the business plan and budget exercise and particularly with North America as a focus and I would not be able to make a clear statement on what will be the volumes that we will end up this year. It is still too early to call, but our agenda will be to maximize volume, but more importantly to try and get more relevant volumes in terms of profitability as much as we can. As we said, Bhavin, for us has been a year of consolidation, one of the most challenging years that we have faced. So as we go to the next year we would like to see how we can maximize the benefits of this upswing in sentimental investment.

Bhavin Chedda: And sir my last question on the net debt numbers, you mentioned you are looking at 200 crores reduction may be by March, so that would be despite much higher volume possibility in

quarter four because I think there have been some rollover in the volumes in the quarter four, so your quarter four volumes would be much higher than the last two quarters. So despite that you would be able to reduce the net debt number?

S. Krishnan: That is a very good question Bhavin, which also means that we need to push our sales teams and others to collect what we are selling and typically what happens is what we sell in January and what we bill in early February is what gets converted into cash. Otherwise it will sit as receivables which will come in the early part of the next quarter.

Bhavin Chedda: But we are not expecting any higher debt numbers from current level now on?

S. Krishnan: I think we should be in this range.

Moderator: Thank you. Our next question is from the line of Nirav Shah from GeeCee Investment. Please go ahead.

Nirav Shah: Sir what was the plate sales volumes during the quarter?

S. Krishnan: Just under 50,000 tonnes.

Nirav Shah: Okay and plate EBITDA was you said for the quarter was how much?

S. Krishnan: 10 crores.

Moderator: Thank you. As there are no further questions, I would now like to hand the conference over to Mr. S. Krishnan for closing comments.

S. Krishnan: Thank you everyone for participating in the call. We do appreciate the keen interest that you take in our performance and we will take your observations with all humility and will try and work around that and hopefully we will come back with better results in the next quarter. Thank you so much.

Moderator: Thank you very much. On behalf of Welspun Corp Limited, that concludes this conference. Thank you for joining us ladies and gentlemen, you may now disconnect your lines.