HEG/SECTT/2023 5th June, 2023

BSE Limited 25th Floor, P J Towers Dalal Street MUMBAI - 400 001. **Scrip Code : 509631**	**National Stock Exchange of India Limited** Exchange Plaza, 5th Floor Plot No.C/1, G Block, Bandra - Kurla Complex Bandra (E), MUMBAI - 400 051. **Scrip Code : HEG**

Sub: Transcript of Earnings Conference Call on Q4 & FY23 of HEG Limited

Dear Sir/Madam,

Please refer to our Earnings Conference Call scheduled on 1st June, 2023 intimated vide our letter dated 30th May, 2023. Please find enclosed the transcript of the said Earnings Conference Call.

The said transcript is also available under the Investors Section of the website of the Company i.e www.hegltd.com.

This is for your kind information and records.

Thanking You,

Yours faithfully,
For **HEG Limited**

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Encl: as above

“HEG Limited Q4 FY’23 Earnings Conference Call”

June 01, 2023

MANAGEMENT: **MR. RAVI JHUNJHUNWALA – CHAIRMAN, MANAGING DIRECTOR AND CHIEF EXECUTIVE OFFICER – HEG LIMITED**
MR. RIJU JHUNJHUNWALA – VICE CHAIRMAN – HEG LIMITED
MR. MANISH GULATI – EXECUTIVE DIRECTOR – HEG LIMITED
MR. GULSHAN KUMAR SAKHUJA – CHIEF FINANCIAL OFFICER – HEG LIMITED

MODERATOR: **MR. NAVIN AGARWAL – HEAD INSTITUTIONAL EQUITIES – SKP SECURITIES LIMITED**

Moderator: Good day, ladies and gentlemen, and welcome to the HEG Limited Q4 and FY '23 Earnings Call organized by SKP Securities Limited. As a reminder, all participant lines will be in the listen only mode. And there will be an opportunity for you to ask questions after the managements opening remarks. Should you need assistance during the conference call, please signal an operator by pressing star then zero on a touchtone phone. Please note that this conference is being recorded.

I now hand the conference over to Mr. Navin Agarwal, Head, Institutional Equities at SKP Securities Limited. Thank you, and over to you, sir.

Navin Agarwal: Good afternoon, ladies and gentlemen. It's my pleasure to welcome you on behalf of HEG Limited and SKP Securities to this financial results conference call with the leadership team at HEG Limited. We have with us Mr. Ravi Jhunjhunwala, Chairman, Managing Director and CEO and Mr. Riju Jhunjhunwala, Vice Chairman; along with their colleagues, Mr. Manish Gulati, Executive Director; and Mr. Gulshan Kumar Sakhuja, CFO.

We'll have the opening remarks from Mr. Jhunjhunwala, followed by a Q&A session. Over to you, Raviji.

Ravi Jhunjhunwala: Thank you, Navin. Friends, good afternoon, and welcome to our financial results conference call for the fourth quarter and full fiscal year '22, '23. As per World Steel Association recent report, the global steel industry is poised for a demand rebound this year with a projected growth rate of about 2.3% and going forward, in 2024, the industry is expected to sustain its growth trajectory with a forecast increase of 1.7%.

These projections indicate a positive outlook for the global steel market, signalling opportunities for continued development in the years to come. In the January-March quarter, global crude steel production reached about 462 million tons, representing 0.5% increase compared to the same period of last year. Among the top 10 steel producing countries, only 2, which is China and India, saw an increase of steel production in January-March over the same period last year.

While China's production grew by 7.4%, India also increased by about 3%. On the other hand, other large steel producing countries like Japan, U.S., Russia, South Korea, Brazil, Turkey, all experienced a decline during this period. However, on a medium- to long-term basis, we see a big positive for our products as the entire world continues to focus on decarbonization and reduction of greenhouse gas emissions.

As per World Steel Association again, electric arc furnace share of steel production ex-China has gone up from 44% in 2015 to 49% in 2022, which is a substantial increase. Steel produced by electric arc furnace amidst one fourth carbon as compared to same steel produced by the blast furnaces.

We have seen several announcements by large steel companies, especially in the U.S. and Western Europe, announcing new greenfield capacity for steel production only through electric arc furnace. Out of such announcements of about 25 million tons coming from U.S. alone, which already produces 70% of its steel through electric arc furnace. Out of this 25 million tons, 7 million tons has already come on stream and the balance 18 million tons would be operational in the next 2 years, adding to further electrode demand.

Similar electric arc furnace capacities have also been announced by steel companies in EU, replacing about 16 million tons capacities from blast furnace to electric arc furnace. All this augurs well for the graphite industry. This is a very encouraging sign, especially for us at HEG, as except ours, no new capacity when electrode industry have been announced by any existing graphite player. While we are more or less ready with our current expansion from 80,000 tons to 100,000 tons in the next couple of weeks, trial runs are already at the final stage.

Out of 5 operations, which go into electrode making, 4 have been already operating for the past couple of months and the last one is more or less at the final stage of operation. And it's a matter of -- it's not a matter of months now, it's a matter of weeks. So it could be as early as next week, or at the most another 2, 3 weeks.

Similarly, China, which only produced 5% of its steel through electric arc furnace, still about 5 years ago is currently at a level of 12% and is aiming to reach 20% in the next few years. We believe electric arc furnace will grow at a CAGR of about 3% in the next decade, which would straight away translate into a substantial increase in electrode demand.

Though in the short-term, the outlook of the steel industry appears to be bearish, steel demand is still being impacted by the fear of global recession, but the medium- to long-term growth path, especially for the electric arc furnace industry, to which we cater, is very clear.

In the current year, due to current geopolitical situation, steel production is likely to be stagnant, which might impact the demand of electrodes. However, we maintain a fairly strong and unwavering belief in the medium- to long-term growth potential of the electrode industry, particularly due to the ongoing and serious decarbonization efforts by major steel making countries in the Western world.

We at HEG have been operating the single largest plant under one roof in the world with a capacity of 80,000 tons for a long time now. And with our expansion of 100,000 tons, very soon going to be in operation, we are in a very good position to take advantage of all the growth in demand for electrodes, as I just spoke about. This expansion showcases our unwavering dedication to technological innovation, placing us at the forefront of the industry with some of the best and latest equipment and technologies we have put under one roof.

We look forward to the successful completion of this project and the enhanced capabilities, as well as cost quality and cost competitiveness, which it will bring to our operations. Our extensive global market reach, which we have diligently cultivated over the past 25 years enables us to export 2/3 of our production to more than 30, 35 countries.

This long-standing presence in international markets further strengthens our confidence in HEG's ability to thrive and see opportunities in the electrode industry, which is waiting for us in the next 2, 3 years.

Now about our new subsidiary, TACC. Our new project for graphite anode is progressing well, and we are just about to start our pilot plant, which will facilitate trials, et cetera. The location has been decided. The land acquisition is under process, and we expect to complete the first phase of the project to make 10,000 tons of anode by mid-2025, exactly 2 years from now.

In conclusion, the fourth quarter and full year fiscal '22, '23 have been satisfying for us. We have achieved strong financial results. Our capacity utilization has been amongst the highest in the world, driven by our commitment to innovation, customer satisfaction and operational efficiency. We remain confident in our ability to navigate challenges and seize opportunities to create long-term value for our shareholders.

With this, friends, I pass on the floor to our CFO, Gulshan, who will take us through the financial figures. Following that, our Vice Chairman, Riju; and Executive Director, Manish, and I will be delighted to address any queries and questions that you may have regarding electrodes and graphite anode. Thank you. Over to Gulshan.

Gulshan Kumar Sakhuja: Thank you, sir. Good afternoon, friends. I will now briefly take you through the company's operating and financial performance for the year ended 31st March 2023. For the year ended 31st March 2023, HEG recorded revenue from operations of INR 2,467 crores as against INR 2,201 crores in the previous financial year.

The revenue for the fourth quarter of FY '23 was INR 617 crores as against INR 673 crores in the corresponding quarter of the previous FY. During the year ended 31st March 2023, the company delivered EBITDA of INR 729 crores as against INR 607 crores in the previous financial year. The company, on a stand-alone basis, recorded a net profit after tax of INR 456 crores in FY '23 as against INR 391 crores in the previous financial year. And on a consolidated basis, the net profit after tax is INR 532 crores in FY '23 as against INR 431 crores in FY 2022.

The company's long-term debt free and had a previous size of nearly INR 1,000 crores as on 31 March 2023. The Board of Directors has recommended a 425% of final dividend that is INR 42.50 per equity share of the face value of INR 10 each for the financial year '22, '23, subject to the approval of shareholders at ensuing AGM. To take out more questions from the participants in the detailed presentation have been uploaded on the company's website and on the stock exchange.

Now we would like to address any questions or queries you have in your mind. Thank you. Over to Navin.

Moderator: The first question is from the line of Vipraw Srivastava from InCred Capital.

Vipraw Srivastava: Yes. So my question was regarding the EAF plans coming up in U.S. So based on the annual reports, currently U.S. contributes 10% to our sales. So can we expect that number to increase in coming years?

Ravi Jhunjhunwala: You see, in the last 4 years, if you have followed our data, I mean, obviously, a lot of this data is not public. We have more or less increased our sales in U.S. by at least 2.5x to 3x. And we always had this in mind. As I said in my opening remarks, U.S. produces 70%, 72% of its total steel through electric arc furnace. And U.S. is the single largest producer of electric arc furnace steel. And obviously, thereby the single largest consumer of electrode. So we have been focusing on U.S. for a long time. And as I said, our -- we've increased our sales substantially in the last 3, 4 years.

Vipraw Srivastava: Got it. Got it. My second question was regarding the anode capex which HEG is doing. So currently, there are many companies in U.S., which are working on silicon anode batteries, which are completely free of graphite. So does that pose a substantial risk to our business because of that and some companies are also commercializing it. So if that happens, actually, it will be a big risk. So what are your views on that?

Ravi Jhunjhunwala: Riju, will you take that question?

Riju Jhunjhunwala: Yes. Can you repeat the question again, what exactly it was, please.

Vipraw Srivastava: So what I was saying was that there are companies in U.S., which are working on silicon anode batteries. So basically, these anodes are completely free of graphite and entirely made of silicon. So if that happens and commercialization occurs then that will pose a substantial business risk to our capex, right, which you are doing. So any views on that?

Riju Jhunjhunwala: So basically, I mean, what you are saying is partially correct. There is absolutely no company, I believe, today, which is working on 100% silicon as a replacement for anode.

Vipraw Srivastava: [inaudible 0:13:56] technologies, they have also commercialized it.

Riju Jhunjhunwala: So there are a lot of projects happening. But still, I think for the next 10 to 15 years, graphite anode will be the primary listing driver for the anode part in terms of any lithium-ion battery. And we are targeting really 4 business segments. So EV is only one business segment that we are targeting for the lithium-ion battery.

The second, which will require more amount of graphite per ton is the ESS space, the energy storage space, over there, again, the standardized graphite use is there for the anode side. And the third also, which is going to be a big business potential for our new subsidiary is the green hydrogen business.

Wherever there is an electrolyzer in green hydrogen business, you need this bipolar plates, which are made out of anode powder itself. So as far as the market goes, as far as the cell manufacturing goes, there is absolutely huge capacity and people today are talking about 25%, 10% mixing of silicon. All these technologies are evolving, but the basic technology will remain the graphite is an integral part of the anode side and in all the 4 business segments.

So really capacity-wise, if you ask then looking at 10,000 tons is just a conservative start, we can really go up to a much bigger level. Specially, if we have all the support that we need today as subsidies from the state government and from the central government.

Vipraw Srivastava: Right. Got it. And one final question from the graphite business. So Graftech did their con call and in there, they told that they were facing issues as far as U.S. steel companies are concerned related to inventory. So they are -- U.S. steel companies are having very high inventories. So what is HEG's assessment on ground? Do we expect that to improve in coming quarters? Or will it sustain? So any views on that?

Ravi Jhunjhunwala: No, I would not like to comment on what my competitor has said, but as I said, we have been focusing on U.S. for a very long time and our sales have been increasing year after year, and they have gone up by like 2.5x, 3x in the last 5 years, and we continue to expand our sales.

Moderator: The next question is from the line of Bajrang Bafna from Sunidhi Securities.

Bajrang Bafna: Just, sir, if you could make us understand that during the -- before the COVID, China announced that they will enter aggressively into conversion of blast furnaces into electric arc furnace and the progression was pretty slow and a lot of electrodes capacity that has come up in China even before EAF capacities getting materialize. So in last 2 years, we are also seeing a lot of dumping that is coming from China in the global market.

So what is your sense when you are saying that they will progressively grow from 11%, 12% to almost 20% over the next few years, which they have already guided. So how do you see the scenario from China side in terms of electrodes that they are dumping in the world market, whether they had slowed or when do you expect that? They'll progressively focus on their domestic market rather than the export market per se. So that will be really helpful for us to understand.

Ravi Jhunjhunwala: Okay. There are 2, 3 things I'd like to explain here. See, if you remember 2017, '18, when suddenly the export -- suddenly, the world market for electrode became absolutely crazy and the demand and everything suddenly boomed. It was on the basis that the Chinese government had announced their intention that the electric arc furnace capacity was only 5% and they said they would like to increase it to 20% in 5 years.

And to put it into perspective, China produces close to 53%, 54% of the total world steel. So that part of the world, which produced 53%, 54% of the total world steel was only producing 5% through electric arc furnace and everybody else except China, which produced 47% of the world steel was doing about 43%, 44%, 45% through electric arc furnace.

So putting that into perspective, the demand for electrodes in China is going to boom. The 5% has already become 12% in 3, 4 years' time, which is already 2.5x of what they were doing only 5 years ago. And from 12% now, they are still on the path to go to 20%, so a couple of things happened.

So as soon as those announcements were made, the existing graphite companies in China obviously had to increase capacity. They were seeing an increase in electrode demand of 4x from 5% to 20%. And at the same time, that 5% to 20%, I mean, it was a very, very difficult thing to achieve in just 4, 5 years. So it is at 12%. But that continuously grows year after year because China is also part of the world. And China is also seeing the advantages of decarbonization and that is where the electric arc furnaces came in.

Secondly, on the technology side, while we do compete with China on about 25%, [30% 0:20:29] of our production, which is the non-UHP, but on the balance, 65%, 70%, which is ultra-high power, we are still far ahead of China as far as the quality is concerned. So -- and that will continue for a long time. The gap between the Chinese quality and our quality, the technology that the rest of the world has and -- which China doesn't have will continue for quite a long time.

So we don't see any problem at all. And just again, to repeat what I just said in my opening remarks, we have not seen the kind of growth in the last 30, 40 years in the capacities of electric arc furnace. At least, I have not seen in last 35, 40 years, new capacities to the tune of 40 million, 50 million tons being added on the electric arc furnace.

And again, to put into perspective, a very simple thumb rule for 1 million tons of new electric arc furnace, you need about $1 billion of investment. So there -- if we are talking about 50 million tons, 55 million tons, which have already been announced between Europe and America, all in the last about 12 to 18 months. So we are talking about $50 billion to $55 billion of investment, which even America and Europe have not seen in this sector for a very long time.

And so in that context, our expansion, which is now more or less on stream, it's a matter of another week, 10 days, 2 weeks, is very timely. We may have to struggle for the next 6 months, may have to struggle for the next 12 months, maybe 15 months, but except us, there is no new capacities which have been announced. And we have increased our capacity of the plant from 10,000 tons to 100,000 tons in the matter of last 20, 25 years. And we have done it 3, 4 times in the past 20 years.

So with all the knowledge and all the information about which equipment to purchase, which is the best supplier for that, any brownfield expansion will take minimum 2.5 to 3 years to anybody. The equipment suppliers take 2 years to deliver equipment. So even if somebody was to announce even if there is a new -- even if there's an existing company, which announces an expansion at their existing site, we will take at least 2.5 to 3 years to build that. And we are very bullish because of whatever I just said.

So our expansion is extremely timely, and we are in a great position to take advantage of whatever new demand is occurring. And 7 million, 8 million tons of new electric arc furnace has already been established in America? And I just said, in the next 2 years, this 7 million is going to become 20 million to 25 million tons. So there is a new -- if there are new capacities to the tune of 20 million, 25 million tons of electric arc furnace, it easily translates into an additional demand of about 40,000 tons. Our expansion is only 20,000 tons.

Bajrang Bafna: Got it. That was very insightful, sir. And sir, if my understanding is right, of late, we have seen good correction in the needle coke prices as well from roughly $2,300 to $1,800. How it is going to impact our margins broadly say, in next maybe 2 or 3 quarters per se. If you could guide us, it will be helpful.

Ravi Jhunjhunwala: As electrode industry is linked to electric arc furnace. Needle coke industry is directly related to graphite industry. So just like as I said, if the electric arc furnace increases its capacity, the demand of electrode grows. Exactly the same thing if graphite electrode industry does well and

the demand for electrode increases, the needle coke demand increases. So it's a matter of -- we are very directly connected.

So -- and we saw 4 years ago when the electrode prices went crazy, obviously, the needle coke prices also went crazy. So it's a relationship of supplier and customers. For them, graphite industry is as important as for us, electric arc furnace is. So obviously, the electrode industry does extremely well and the prices start going up, it is obvious that needle coke prices will also keep going up.

Bajrang Bafna: But sir, needle coke has also got some connection to do with this EV also, not those lithium-ion batteries and all?

Ravi Jhunjhunwala: Not much. Yes, it is. I mean part of that is what you're saying is absolutely right. But like -- I mean, to tell you in a different way, I mean, for us, needle coke is a lifeline. If we don't have needle coke, we can't produce electrode, ultra-high-power electrode. But it's not the case in battery. So it is not a lifeline for them.

They may use needle coke if it is available at a particular price. But if the needle coke is not available at a particular price, they have several other options. So needle coke is one of the many raw materials, which they have an option. Whereas for us, we have no option. If we don't have needle coke, we don't have electrode.

Bajrang Bafna: So for us, sir, if I understand it right, the volume growth that is the one thing which you are anyway ascribing that is going to go up, the utilization levels are going to go up because of the additional demand which is going to be created globally. That's one. And second is this spread that you maintain between electrodes and this needle coke. So recently, we have seen the needle coke prices have corrected. Will that have some impact on our margins immediately, maybe coming into this quarter, maybe next quarter?

Ravi Jhunjhunwala: No, you see, as I said, it's very, very directly connected. If the electrode prices drop, the needle coke prices will also drop. So when it comes to margin, I mean, the margin gets corrected because of a reduction or increase in the needle coke price. And we saw this very much in 2018, '17 when the electrode prices went up by very crazy numbers, needle coke prices also went up in a similar manner, but the margin for electrodes, in fact, went up, it didn't go down.

Moderator: The next question is from the line of Bhavik Shah from MK Ventures.

Bhavik Shah: What has been the capacity utilization in the last quarter in FY '23?

Ravi Jhunjhunwala: Manish, will you take the operational questions.

Manish Gulati: Last quarter, it is about -- I mean, in high 70s, above mid-70s, I would say. That has been the capacity utilization.

Bhavik Shah: Okay. So with the new capacity coming in, what can we -- what will be like our capacity utilization going ahead in FY '24? Will we be able to absorb the -- like the market will be able

to absorb the excess supply? Or will we see any margin contraction because of the excess supply?

Manish Gulati: No. I mean, Bhavik, of course, when we add capacity, I mean, right now, of course, this first quarter has almost gone in April, May, June. So in the next few weeks, when its -- ready, so we'll start counting calling ourselves a 100,000 tons plant from, let's say, maybe July onwards. So capacity utilization for the whole year, now we are aiming or we anticipate the traditional demand to come in towards the later half of the year. That's what everybody thinks that 2024 we should see the return of demand.

But we internally think that in this year, if we count ourselves at 100,000 tons, let's say, for the whole year, we should be maybe around 7% or something. It's just our internal thing. That's our aim because we expect the market to -- the demand to come back towards the later half of the year or late last quarter, January to March '24.

Bhavik Shah: And sir, are we planning to be aggressive for the excess capacity or we'll try to maintain our margins going ahead?

Manish Gulati: I mean, of course, we are not going to go to that level that I mean, we just get more margins, of course. Our effort will be for both in a balanced way that we have time for market to absorb the tonnage and at the same time, taking care of the margins as well, and we're not going aggressive either ways.

So it just is very balance because market would need some time for the additional capacity to get absorbed. And we have not be very hasty about it. That's about 100,000 tons. So we are not aiming to sell all of that 100,000 tons. We'd rather go gradually, slowly and wait for the demand to rise and then the capacity to get naturally absorbed.

Bhavik Shah: Right, right. And sir, regarding the new capex which has been announced in anodes, what kind of technology collaboration or expertise will we need? And will it be in-house or are we looking at some partnerships?

Manish Gulati: I will have our Vice Chairman answer this.

Riju Jhunjhunwala: Most of the technology is to be standard and the most important technology as far as this is concerned, which is graphitizing the product, that is something that is only like HEG and some other companies present in the graphite electrode space can have, because that particular thing of graphitizing anode is probably more complicated than graphitizing our graphite electrode itself. So that -- I mean, with our rich experience of the last 40 years in that particular segment, we have a huge competitive advantage as far as that particular side of the technology is concerned.

The rest of the technology is pretty standard, and we are trying to match the kind of best in the world along with the best in cost. So it will be a mixed hybrid. It would not be like one EPC contract. It will be a hybrid mix of Indian machinery, some Chinese machinery, some European ones, and then the Acheson furnaces, which we will develop ourselves in India with HEG profile inside this.

Bhavik Shah: Okay. And so what kind of revenue and margins are we expecting from the anode business.

Riju Jhunjhunwala: So I mean, I can't really talk about the revenue and margin, but let's say, 10,000 ton plant even at an average of around $9,000 to $10,000 per ton should be your revenue. And the margin is really 2 years down the line, what they will be, what they won't be, given whatever the raw material prices is, competition is, demand is everything. So we have assumed a reasonable at least a 25% operating margin in this particular business.

Bhavik Shah: Okay, sir. What has been the sense in the 2 months regarding the price of graphite electrodes and needle coke? Like how has been they moving? And how do you see them in the next quarter?

Manish Gulati: Price is under pressure, which is very natural for it to be in this year of 2023. There are some marginal correction in needle coke prices also and electrode. So going forward, since needle coke contracts are being done still quarter-by-quarter and electrodes are also being booked still, let's say, quarter-by-quarter or maximum 6 months, we hope, and we expect maybe needle coke suppliers should do some more correction. They have already corrected a bit, but more is expected from them.

Moderator: Our next question is the follow-up question from the line of Vipraw Srivastava from InCred Capital.

Vipraw Srivastava: Yes. So what I wanted to know is that as far as the European market is concerned, so what is like I just wanted a ballpark figure, how much the Europe contributed to our volume -- sales volume?

Manish Gulati: As a total of furnace sales, it will be between let's say, about 9% to 10% or something.

Vipraw Srivastava: Right. And there was some issue in previous quarters regarding Turkey. They were facing some volume issues. So anything on that line or how is it faring right now?

Manish Gulati: It's definitely better than the past quarters because Turkey is one country where they are very flexible of steel making, they are quick to reduce, they are quick to come. So we are seeing some positive signs and rise in production in Turkey also.

Vipraw Srivastava: Okay. And one last question. So as far as the [inaudible 0:34:54] contracts are concerned, so there was a time when we were signing 6-month contracts. So like how is the situation now? Is it 6 months, is it 3 months? So how is it now?

Manish Gulati: It continues to be 3 months still.

Navin Agarwal: Aman, I guess no more questions. Thank you very much that was the last question in queue. As there are no further questions, I would now like to hand over the conference to Mr. Manish Gulati for closing remarks. Thank you, and over to you, Manishji.

Manish Gulati: Friends, thanks for listening to our call and thanks for attending the call. And we are very optimistic about our industry. There is no doubt about it. We can see things happening on the ground. We are seeing new and new electric arc furnaces coming up, and we are very positive about HEG being a 100,000-ton plant at one location. This is one of the most cost-competitive

plants in the world. So we hope that from 2024 onwards, you'll see a rebound in demand, and we'll be very much ready for that. Thank you so much, and we look forward to seeing you again.

Navin Agarwal: Thank you, Raviji. Thank you Riju. Thank you Manishji. Thank you, Gulshan. On behalf of SKP Securities, that concludes the conference. Thank you for joining us, ladies and gentlemen. You may now disconnect your lines. Thank you, and have a nice day.

Moderator: Thank you.