

HEG Limited

Q2&H1 FY2011 Results Presentation



Introduction

- ✦ **Leading manufacturer** and exporter of graphite electrodes in India
- ✦ One of the **lowest cost** producers of graphite electrodes
- ✦ Strong presence in value added **Ultra High Power (UHP)** segment
- ✦ Diversified **customer portfolio** - POSCO, US Steel, Arcelor Mittal and Nucor Corp
- ✦ **Graphite electrodes manufacturing plant** in Mandideep – Rated capacity of 66,000 MT being expanded to 80,000 MT per annum
- ✦ The **largest single-site graphite electrodes manufacturer in the world**
- ✦ **Captive power** generation of **77 MW** provides **reliability & self-sufficiency**



Sector Perspective

☀ **Steel production and demand expected to reach record levels**

- Growth in production primarily driven by China where usage of blast furnace route is high
- Europe and USA produce large steel volumes through EAF route; production showing gradual increase
- Rest of the World (excl-China) production also buoyant but yet to touch peak levels of pre-crisis levels of 2007-2008

☀ **Graphite Electrode production driven by steel production through EAF route**

- EAF steel production volumes witnessing recovery though away from peak pre-crisis levels
- EAF route production outlook is positive

☀ **Graphite Electrode realisations treaded soft in earlier quarters**

- Visibility of initial signs of uptick in price movement

Performance Perspectives

- ✦ **Operational performance is robust**
 - Capacity utilisation at 85-90% plus range; volume visibility for the rest of the year is encouraging
 - Capacity utilization expected to further strengthen in H2FY2011
 - Negotiations and volume commitments from customers & industry feedback supports this trend
 - Increasing sales ahead of growth in demand
- ✦ **Adequate needle coke supplies envisaged for existing capacities**
 - No major cost inflation foreseen
- ✦ **Captive power of 77 MW supporting production ramp-up and adequately covers expanded capacities**
 - 2 thermal power plants of total ~63.5 MW benefit from coal linkages
 - Hydel-power operations provide low-cost power
- ✦ **Expansion to 80,000 MT proceeding well and on schedule.**

Performance Perspectives

✦ **Financial performance considers**

- Muted graphite electrode realisations
- Lower power realisations

✦ **Financial performance is encouraging given**

- Continued steady cash flows from operations
- Healthy earnings performance despite soft graphite electrode pricing scenario and lower power realisations
- Sustained improvement in cost of borrowings

Highlights

- ✧ Revenues in Q2FY2011 improve by 10%, at ₹ 299.6 crore as compared to ₹ 273.1 crore in Q2FY2010
- ✧ EBIDTA at ₹ 64.6 crore in Q2FY2011 from ₹ 94.7 crore in Q2FY2010
- ✧ EBIT at ₹ 51.0 crore in Q2FY2011 from ₹ 81.6 crore in Q2FY2010
- ✧ EBT at ₹ 42.5 crore in Q2FY2011 from ₹ 65.4 crore in Q2FY2010
- ✧ PAT in Q2FY2011 reported at ₹ 29.7 crore from ₹ 44.2 crore in Q2FY2010
- ✧ EPS (Basic) in Q2FY2011 at ₹ 6.94 from ₹ 10.8 in Q2FY2010
- ✧ Expansion of Graphite Electrode capacities from current rated 66,000 TPA to 80,000 TPA is on schedule

Expansions – Graphite Electrodes

- ✦ Capacity expansion from 66,000 TPA to 80,000 TPA which commenced in March, 2010 is on schedule
 - Expansion anchored by revival in demand growth of graphite electrodes and is to be supported by increased demand of steel produced through the EAF route
- ✦ Expansion is expected to be completed by September 2011
- ✦ Expansion capex, by design, revised to approximately ₹ 275 crore from ₹ 225 crore; to be directed towards efficiency, productivity and quality enhancement initiatives
 - This additional investment of ₹ 50 crore is towards quality and efficiency; to generate its own payback
- ✦ Total expansion capex being funded through debt and internal accruals
- ✦ Expansion will consolidate HEG's position as the largest single-site producer of Graphite Electrodes in the world
 - Low cost, Brownfield expansion
 - Economies of scale to improve further
- ✦ Timing of capacity expansion is well positioned for the next up cycle as volume visibility is strong going forward



Management views

Commenting on the results, Mr. Ravi Jhunjunwala, Chairman and Managing Director, HEG Limited, said:

“A global economic recovery is underway and though it is very evident, we are yet to witness operations, industry-wide returning to their pre-crisis levels.

Recovery of the steel sector has been good and steel production through the EAF route has also been on an uptick, though the peak levels have not yet been achieved. This is still encouraging for our Company which operates in the graphite electrode industry, as the EAF route presents new opportunities for growth, through a positive volume outlook.

The initial improvement for us has come in the shape of better volumes performance, which continues to improve. The pressure on graphite electrodes pricing has eased and we now have initial visibility of price improvement. This expected increase in prices will enable us to take further advantage of the opportunities that the sector offers.

We are encouraged by the improved scenario and look forward to improved results based on our quality of production and an expected, favourable sector scenario.”



Management views

Commenting on the results, Mr. Manvinder Singh Ajmani, Chief Financial Officer, HEG Limited, said:

“I am pleased to share with you the Company’s operational salience during the quarter. The graphite electrode environment is improving, driven first by volume pick up and supported by an expected increase in realisations trajectory. Though realisations in the quarter under review have been muted, our performance is expected to show stronger improvement in value when the current contracts are honoured, and as we enter new contracts with prices revised upward.

In the power division, we saw higher level of generation, given the full utilisation of the second thermal power plant. Muted merchant power realisations, maintenance shutdown of the first thermal power plant and delayed hydel-power operations put some pressure on performance of Power Division. Going forward we expect continued stable performance from the Power Division.

The current results have been achieved in a subdued economic scenario, and going forward, as the sentiment improves, we aim to further improve our operational performance and endeavour to match that with delivering higher returns.”



Financial performance – A review

Revenues:

- ☀ Revenues were higher by 10% at ₹ 299.6 crore in Q2FY2011 on the back of higher sales volumes of graphite electrodes and higher power generation
- ☀ Visibility of improved volumes in H2FY2011 will support higher proposed capacity utilization rates

Particulars (₹ crore)	Q2 FY2011	Q2 FY2010	Shift (%)	H1 FY2011	H1 FY2010	Shift (%)
Gross Revenues:	344.6	305.8	13	606.3	561.4	8
Net Revenues:	299.6	273.1	10	521.8	505.3	3

Financial performance – A review

Total Expenditure:

- ☀ Needle coke prices remain stable; Other raw material costs were marginally higher
- ☀ Power and fuel costs higher on account of higher captive power
- ☀ Interest cost has reduced by 47%, due to higher proportion of low cost borrowings and lower working capital costs

Particulars (₹ crore)	Q2 FY2011	Q2 FY2010	Shift (%)	H1 FY2011	H1 FY2010	Shift (%)
Total Expenditure	239.5	179.3	34	402.6	326.9	23
<i>(Increase) / Decrease in Stocks</i>	(9.6)	28.2	NA	(69.7)	17.3	NA
<i>Consumption of Raw Materials</i>	142.4	84.2	69	290.7	171.6	69
<i>Power & Fuel (Net of Interdivisional purchases)</i>	20.7	12.0	73	36.1	26.8	35
<i>Staff Cost</i>	10.5	9.9	6	20.7	19.5	6
<i>Other Expenditure</i>	75.6	45.0	68	124.6	91.9	36

Financial performance – A review

EBIDTA:

- ☀ EBIDTA stood at ₹ 64.6 crore from ₹ 94.7 crore
- ☀ Margins in Q2FY2011 muted on account of lower realisations in both graphite electrodes and in power (merchant sales portion) and increase in expenditure

Particulars (₹ crore)	Q2 FY2011	Q2 FY2010	Shift (%)	H1 FY2011	H1 FY2010	Shift (%)
EBIDTA	64.6	94.7	(32)	123.6	180.8	(32)
EBIDTA Margins (%)	21.6	34.7	NA	23.7	35.8	NA

Financial performance – A review

- ✦ Q2 FY2011 Profit Before Tax at ₹ 42.47 crore as compared to ₹ 65.37 crore last year
- ✦ In Q2 FY2011, the Company reported a forex gain of ₹ 4.96 crore

Particulars (₹ crore)	Q2 FY2011	Q2 FY2010	Shift (%)	H1 FY2011	H1 FY2010	Shift (%)
PBT	42.5	65.4	(35)	77.0	121.5	(37)
PAT	29.7	44.3	(33)	56.3	86.1	(35)
PAT Margins (%)	9.9	16.2	NA	10.8	17.0	NA
EPS (Basic) not annualised	6.94	10.78	(36)	13.14	21.0	(37)
EPS (Diluted) not annualised	6.94	10.64	(35)	13.14	20.7	(37)

Segmental results – Graphite electrodes

- ✴ Revenues in Q2 FY2011 were higher by 14% at ₹ 293.7 crore as compared to ₹ 257.9 crore due to increase in sales volumes
 - Higher volumes driven by revival in steel production through the EAF route
- ✴ Q2 FY2011 PBIT at ₹ 45.3 crore from ₹ 72.1 crore
 - Margins reflect moderation in realisations
- ✴ Order booking continues on an average of rolling 3-6 month basis
- ✴ Needle coke booked for the whole year at fixed prices and sufficient needle coke is available for current year

Particulars (₹ crore)	Q2 FY2011	Q2 FY2010	Shift (%)	H1 FY2011	H1 FY2010	Shift (%)
Revenues	293.7	257.9	14	502.4	470.4	7
PBIT	45.3	72.1	(37)	79.2	132.1	(40)
Return on sales (%)	15.4	28.0	NA	15.8	28.1	NA
Capital Employed	617.0	576.6	7	617.0	576.6	7

Segmental results - Power

- ✧ Revenues in Q2FY2011 increase by 19% to ₹ 45.3 from ₹ 38 crore on the back of higher generation
- ✧ Earnings performance influenced by
 - Subdued merchant power realisations
 - Routine, annual maintenance shut-down of 30 MW thermal power plant
 - Delay in resumption of operations of the hydel power plant; operations have since stabilized with sufficient water reserves in the catchment area
- ✧ 3 power plants under operation with a total capacity of around 77 MW
 - Two thermal power plants at Mandideep (30 MW+33 MW) – provide cost-effective and dependable power supply throughout the year; coal linkage received for thermal power plants support operations
 - Hydroelectric power plant at Tawa (13.5 MW)

Particulars (₹ crore)	Q2 FY2011	Q2 FY2010	Shift (%)	H1 FY2011	H1 FY2010	Shift (%)
Revenue	45.3	42.3	7	92.8	80.3	16
PBIT	4.7	9.3	(49)	14.0	22.7	(38)
Return on sales (%)	10.4	22.0	NA	15.1	28.3	NA
Capital Employed	242.9	216.8	12	242.9	216.8	12

In summary

☀ **Graphite Electrode volume outlook remains encouraging**

- Trend is encouraging
- Capacity utilisation to improve
- Customer enquiries are strong
- Increase in production through the EAF route continuously rising with strengthening steel demand; HEG volume growth ahead of demand trend

☀ **Graphite Electrode price outlook is improving**

- Initial uptick visible; to reflect in performance with a time lag

☀ **Cost outlook stable**

- Needle coke as key raw material is stable; though other raw material costs have increased
- Lower finance costs to augment earnings

In summary

☀ **Performance outlook is positive**

- Volume growth is visible.
- Price stabilisation/improvement to support higher returns
- Benefits from price effect expected to accrue over coming quarters; volume reflection is immediate

☀ **Model remains strong and robust**

- Major cost advantages as HEG is the largest single site producer of graphite electrodes
- Healthy relationships with raw material suppliers
- Self sufficient and reliable power capacities
- Impressive long term relationship with customer base

☀ **Fresh expansion to 80,000 MT per annum to augment production ahead of demand uptrend**

- To augment performance once implemented



Disclaimer

Statements in this document pertaining to future status, events, or circumstances, including but not limited to statements about plans and objectives, potential product characteristics and uses, product sales potential and target dates for product launch are forward-looking statements based on estimates and the anticipated effects of future events on current and developing circumstances. Such statements are based on management's current expectations and are subject to risks, uncertainty and changes in circumstances, which may cause actual results, performance or achievements to differ materially from anticipated results, performance or achievements. HEG Limited is under no obligation to (and expressly disclaims any such obligation to) update or alter its forward-looking statements whether as a result of new information, future events or otherwise. The Company may, from time to time, make additional written and oral forward looking statements, including statements contained in its filings with the regulatory bodies and reports to shareholders



About HEG Limited

HEG Limited, a listed company of the LNJ Bhilwara Group, was established in 1977 in technical and financial collaboration with Societe Des Electrodes Et Refractaires Savoie (SERS), a subsidiary of Pechiney of France.

HEG Limited currently operates a 66,000 MT graphite electrode plant at Mandideep, near Bhopal. The company has earlier invested ₹ 725 crore between 2002-09 in upgrading graphite electrode production capacity and setting up its own captive power plants.

The Company also operates three power generation facilities with a total rated capacity of about 77 MW. The hydroelectric power plant at Tawa near Itarsi, District Hoshangabad (Madhya Pradesh) has a rated capacity of 13.5 MW, while two captive thermal power plants located at Mandideep (Madhya Pradesh) have rated capacities of 30 MW and 33 MW respectively.

HEG Limited is a part of the ₹ 5,000 crore LNJ Bhilwara Group, which is a diversified conglomerate with business interests in power, graphite electrodes, textiles and IT services sector. The Group has 5 listed companies and wide range of stakeholders.



About Graphite electrodes

Graphite electrodes find their biggest industrial use in Electric Arc Furnaces (EAF) used in steel plants to melt steel scrap. The demand for graphite electrodes is therefore sensitive not to steel prices but to steel production volumes through the EAF route, which accounts for 31% of the world's steel production.

Graphite electrodes are manufactured using a closely guarded technology which is available with only 7-8 manufacturers globally. Globally USA, Europe, Middle East and South America have an EAF share of over 60%, 40%, 80% and 60% respectively. HEG Ltd., being one of the lowest cost but high quality producers of graphite electrodes, exports over 80% of its production.



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