NEOGEN
CHEMICALS LTD.

February 20, 2023

BSE Limited Department of Corporate Services Floor 25, Phiroze Jeejeebhoy Towers, Dalal Street, Kala Ghoda, Fort Mumbai 400 001 **Scrip Code No: 542665**	National Stock Exchange of India Limited Listing Department, Exchange Plaza, Bandra Kurla Complex, Bandra (East), Mumbai – 400 051 **Company Symbol: NEOGEN**

Sub.: Q3 9M FY23 - Earnings Conference Call Transcript.

Dear Sir/ Madam,

With reference to the captioned subject, please find enclosed herewith the Earnings Call Transcript of the Company's Q3 9M FY23 Earnings Conference Call held on February 13, 2023.

The transcript is also being uploaded on the company's website at https://neogenchem.com/financial-performance/ .

Kindly take the same on your record.

Thanking you,
Yours faithfully,
For Neogen Chemicals Limited

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KANANI

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Encl: As above

Neogen Chemicals Ltd.

Q3 FY23 Earnings Call Transcript

February 13, 2023

Moderator:	Ladies and gentlemen, good day and welcome to the Neogen Chemicals Q3 FY'23 Earnings Call. As a reminder, all participant lines will be in listen-only mode and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing '*' then '0' on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Nishid Solanki from CDR India. Thank you and over to you, sir.
Nishid Solanki:	Thank you. Good evening, everyone and welcome to Neogen Chemicals Q3 FY'23 Earnings Conference Call for Analysts and Investors. Today, we are joined by senior members of the management team, including Dr. Harin Kanani – Managing Director, Mr. Anurag Surana – Director and Mr. Ketan Vyas – Chief Financial Officer. We will commence the call with opening thoughts from the Management Team, post which we shall open the forum for 'Question and Answer' session during which the management will be addressing queries of the participants. Before we commence, I would like to share our standard disclaimer. Certain statements made or discussed on the conference call today may be forward-looking statements. The actual results may vary from these forward-looking statements. A detailed disclaimer in this regard is available in Neogen Chemicals Q3 FY'23 Earnings Presentation, which has been shared. I would now like to invite Dr. Kanani to share his perspectives. Thank you and over to you, sir.
Dr. Harin Kanani:	Thank you Nishid. Good evening, everyone and welcome to our Q3 FY'23 Earnings Conference Call. We published our Q3 financial results and subsequently, the earnings presentation over the weekend. I hope you were able to go through them. I will be sharing the performance overview, key developments and strategic insights, while our CFO, Mr. Ketan Vyas will share the financial highlights for the period under review. Q3 of the current fiscal year was an eventful period for us. Not only did we demonstrate a robust financial performance, but also undertook several strategic initiatives to further strengthen our business model across both existing as well as Lithium-ion battery chemicals' space. I will share some of the key fine prints of this development in just a bit. First, on the financial performance side. We reported 40% gains in revenue in Q3 FY'23 with solid profitability with EBITDA increasing by 27% and profit after tax growing by 40%. As a result of our relentless efforts of having higher planned throughput with increased focus on value-added portfolio based on incremental capacity is available. This was achieved despite impact of continued high inflation in some of the key input costs, especially prices of lithium, which stood elevated during

the period under review. Having said that, we were able to pass on these cost pressures to our customers, thereby protecting the absolute EBITDA.

In Q3 FY'23, we registered 30% gains in organic chemicals revenue, while growth in inorganic chemicals stood at 85%, which was steered by a mix of realization improvement and volume expansion. The demand trajectory continues to be favorable and we are capitalizing on the incremental opportunities emerging in the sector.

Our scale up in advanced intermediates and custom synthesis manufacturing is progressing well, and as expected, we are taking up more complex assignments that require multiple steps, thereby leveraging our process expertise and manufacturing infrastructure to deliver customized solutions. The objective is to further elevate the performance trajectory of high margin value-added portfolio within the business mix by utilizing our competent R&D capabilities.

During the nine-month period, we have added 8 new customers across various geographies and industries. With this we are now engaged with more than 39 customers in this custom synthesis and manufacturing segment. Overall, we are working on 23 products with combined revenue potential of Rs. 2,100 crore with further pipeline and new enquiries flowing in.

Now, let me take you through some of the major developments in this quarter. First, I will update you on some of the existing CAPEX initiatives. With regard to the expansion of specialty organic chemicals capacity by 60,000 litres or 60 m3, we are glad to have commissioned 15,000 litres or 15 m3, while remaining 45,000 litres will come up by September 2023. We have a total reactor capacity of 466,000 litres or 466 m3 in organic chemicals.

Our expansion of inorganic chemicals capacity from 1,200 MT to 2,400 MT in Dahej, which amounts to 30 m3 reactor capacity in the existing inorganic MPP is in progress, and we are on track to commission this by May or June 2023.

Within battery chemicals, the new capacity of 400 MTPA or 92 m3 reactor volume for manufacturing of specialty lithium salts and additives for electrolytes, will be commissioned by June 2023.

Lastly, as you may know, we have announced CAPEX for building a pilot plant to manufacture 250 MT of electrolyte at Vadodara facility. This will now come at Dahej SEZ facility and based on expected demand we are enhancing this capacity to 1,000 MT, which will be ready by August/September 2023. All these initiatives will start contributing to our revenues in a phased manner from FY’24 and will peak out in FY’26.

Moving on to the second key development, we are setting up a wholly-owned subsidiary of Neogen Chemicals Limited, that will accommodate battery chemicals business of the company. This was executed after numerous internal discussions and considerations.

The key reasons of this are, battery chemicals business requires a high-volume setup with different CAPEX and OPEX as compared to legacy business. This business requires different kinds of skill sets and expertise across functions, and we would like to take advantage of the lower corporate tax rate of 15% for newer corporates.

Now, the third development. In line with robust demand environment for battery chemicals in FY'25 and beyond, the board has approved expansion of the electrolyte capacity to 5,000 MT, which will be operational by June 2024, followed by specialty lithium salts capacity of 1,000 MT which is about 232 m3 of reactor volume, which will be operational by June 2024.

The board has also approved further greenfield expansion of electrolyte and specialty lithium salts at a new site for dedicated battery materials. This will include an additional 5,000 MT of electrolyte capacity, making the total installed capacity across sites, 10,000 MT and an additional 1,000 MT of specialty lithium salts, making total installed capacity about 2,000 MT, both of which will be operational by September 2025. It is expected to meet the incremental demand arising from FY'26/FY'27. These projects, when commissioned, will add to revenues from FY'25 and will peak out by FY'26/FY'27.

The overall CAPEX for all the new projects will be close to Rs. 450 crore and will be funded by a mix of debt and internal accruals. While the debt levels will increase with this expansion, the debt-equity will continue to remain below 1.25x as guided earlier. These CAPEX initiatives will significantly contribute to our earnings from next financial year. At a consolidated level, our goal is to attain more than 30% revenue compounded annual growth rate, translating into Rs. 2,000 crore to Rs. 2,250 crore of revenue by FY'26 or FY'27. This compares to Rs.487 crore top line achieved in FY'22.

I am immensely pleased to outlay our growth plan and let me assure you that our teams will work tirelessly and judiciously to achieve that. Neogen is anticipated to experience a substantial increase in its financial performance and demonstrate its proficiency in manufacturing to clients worldwide. An optimistic outlook for demand and India's position as a desirable manufacturing centre, will increase the market size and attract additional customers throughout the supply chain. That ends my opening thoughts.

I would now request our CFO, Mr. Ketan Vyas, to share the financial highlights for the period under review. Over to you, Ketan.

Ketan Vyas: Thank you Dr. Harin. Good evening, everyone and welcome to our Q3 and 9M FY'23 Earnings Call.

I will now take you through the key financial highlights. Please note, that these are on standalone basis and based on year-on-year comparison.

In Q3 FY'23, revenues grew by 40% on a year-on-year basis to Rs.186.3 crore and in nine months FY'23, it grew by 46% year-on-year to Rs. 482.3 crore. The growth was boosted by the increased utilization at plants which was aided by firm demand in crucial end-user industries. The company had started to see positive results from the efforts around scaling up its high margin on advanced intermediates and custom synthesis manufacturing business as highlighted by Dr. Harin.

Organic chemicals saw a growth of 30% year-on-year at Rs.136 crore in Q3 FY'23, whereas inorganic chemicals jumped 85% year-on-year at Rs. 50 crore. In nine months, FY'23, organic chemicals saw growth of 23% year-on-year to Rs. 326 crore and inorganic chemicals grew by 137% year-on-year at Rs.157 crore.

The domestic and export mix for Q3 FY'23 stood at 47% and 53%, respectively. EBITDA increased by 27% year-on-year at Rs. 30.1 crore in Q3 FY'23 and 32% year-on-year at Rs. 79 crore in nine months FY'23. Despite the persistent inflation in some raw materials and utilities, robust EBITDA was attained through effective management of the product mix. The company faced a rise in certain costs, such as, employee expenses, which aligns with the management’s plan to enhance the workforce across various departments.

PAT performance for Q3 FY'23 improved by 40% year-on-year at Rs.14.7 crore and in nine months FY'23, it enhanced by 23% year-on-year to Rs. 35.7 crore. The increase in profit after tax demonstrated our operational efficiency which was marginally impacted by high depreciation resulting from the additional new capacities and surge in finance costs caused by rising interest rates.

Those were the key financial highlights. I will now request the moderator to open the forum for Q&A session. Thank you.

Moderator: We will now begin the question-and-answer session. The first question is from the line of Mihir Damania from Ambit Investment Advisors. Please go ahead.

Mihir Damania: My first question is: you alluded that we are looking to fund the entire Rs. 450 crore of CAPEX by debt and internal accruals. Do you want to give a break up of how we are going to fund the entire Rs. 450 crore? An indication would be really helpful. Just a follow-up on that. Are you also looking to raise additional capital to fund this Rs. 450 crore of CAPEX?

Dr. Harin Kanani: Thank you for your question.

Based on our projections and numbers that we have looked at, for this Rs. 450 crore, the capital which we had raised in last financial year would be sufficient in terms of our equity. Approximately, the banks normally fund 70% to 75%. So, we would utilize maximum funds from the bank. So, somewhere between 70% to 75% of the Rs. 450 crore will be funded through bank term loans. We are also requesting banks for a longer maturity and longer moratorium term loan considering that the business is growing significantly well, and so far, we have received a positive response. The balance will be funded through our own internal accruals. A part of the equity which we had raised last year, which we had kept aside in the form of investment and financial products will be brought in, and together we will be funding the equity portion of the Rs. 450 crore.

Mihir Damania: What would be the anticipated payback for the CAPEX of Rs. 450 crore that we are doing or what would be the internal return on equities on the said project?

Dr. Harin Kanani: When the CAPEX is fully utilized by FY'27, our ROE and ROCE will stand much above 20%, is what we are projecting.

Mihir Damania: Would this CAPEX be ROE-accretive with the current business?

Dr. Harin Kanani: Yes, because it would be more or less similar, because even existing at full utilizations, once the business is stabilized, it would be like a 20%-plus. So, currently in the electrolyte and lithium salt business, what we have seen is that if we are making the salts ourselves along with the electrolyte, it looks almost similar to our existing business, at least in our projections and that is what we have taken. We have taken similar asset turns and we are taking similar kind of operating margins as well. Again, as I have said in previous call, this is a new industry and is for the first-time being established in India. As it gets established, we will have a better picture. But, at least, currently, in our models and based on whatever we have looked at – pricing, investment and internal cost structures, we feel that we should be able to get at least similar asset turns as well as similar margins on investment.

Mihir Damania: Do we have any firm orders or something of a guarantee of sort, which gives us the confidence of achieving the Rs. 2,250 crore of revenue?

Dr. Harin Kanani: From this Rs. 2,000 crore to Rs. 2,250 crore, about Rs. 1,000-odd crore is coming from our regular business. When we look at our pipeline and the incremental demands of our customers, we are fairly confident that our existing business can easily earn up to Rs. 1,000-Rs. 1,200 crore, let us say by FY'26/FY'27.

Now, when it comes to the battery business, what gives us the confidence in this is that we have worked with both, international customers for lithium salts, as well as Indian customers for their electrolyte requirement. Several of these customers have started evaluating Neogen samples and some of them have given very positive feedback that, the first samples submitted by us meet majority of their criteria. This is for both, our electrolyte as well as international salt customers with whom we have worked. So, I think together, this has given us the confidence to basically continue the journey that we had started.

We already discussed the initial trial investment, which we had already planned - the 250 MT of electrolyte, which we are now revising to 1,000 MT and the salt of 400 MT. Looking at the timelines which are required for India from our customer side, we have decided to basically take the decision and based on the feedback received from customers and with their plans getting more and more clearer, we have decided to go ahead with our CAPEX plans.

Moderator: Next question is from the line of Saurabh Kapadia from Sundaram Asset Management. Please go ahead.

Saurabh Kapadia: This project, as of now, what I understand is that we do not have a firm contract from a customer on electrolyte capacity. However, according to you, when can we get the correct number of customers for electrolytes and whether it will be one customer, or would there be two or three customers? What are you looking at?

Dr. Harin Kanani: Thank you for your question. We are working with almost 15 potential customers for electrolytes within India and maybe a couple of customers outside as well. Several of these customers are starting by 2024; especially those who are part of the PLI Scheme need to start, and some others also will start by 2024. Therefore, we need to be ready by at least end of 2023 to take care of their initial requirements. So, that is why we have projected initially to increase the capacity from 250 to 1,000 MT, followed by an immediate increase of that 1,000 MT to 5,000 MT hopefully by June 2024, which will take care of their FY'25 requirement and early FY'26 requirement. Some of the customers have already approved our samples in their phase-I trial. The next approval will be once the pilot facility starts. We need to start the pilot facilities from where we can submit the samples and then we can start more commercial supplies to them from FY'25. Similarly, as I explained on the salts side also, the customers have already approved our R&D samples, and once the pilot facility starts, by June or so, they will also start approving the samples.

Saurabh Kapadia: The firm contracts will be from post the pilot facility once the product gets approved?

Dr. Harin Kanani: Yes, after the pilot facility beyond June to December period. Before that, we may get some conditional contract. So, the contract will be approved or like we may have some conditional contracts, but they will be subject to final qualification of the final plant.

Saurabh Kapadia: Also, if you can give some color in terms of how the margin profile will be; also, how the working capital cycle could be for this new business?

Dr. Harin Kanani: The margin profile that we are expecting at an EBITDA level, is at least the same as what we have, that is, 18.5%, +/-1%. This is the bare minimum we are currently considering. We are considering this when we are making from, let us say, starting from lithium carbonate and making the salts ourselves and then we are making the electrolyte. If we are doing the whole thing, the minimum margin we should be getting is this much. If we are able to get a better margin, we will of course try for that. It will depend upon how much value we are able to add and how the competitor landscape looks like. So, this is on the margins.

In terms of working capital cycle, we hope, because this will be fewer products and fewer customers and more long-term business, from a working capital cycle point of view, it should be significantly better as compared to our existing multi-product multi-customer organic business. We believe the working capital cycle would be better and this is what we have presumed in our models.

Saurabh Kapadia: Where do we stand in terms of working capital improvement on our existing business?

Dr. Harin Kanani: In absolute terms, our working capital utilization and our inventory remain more or less similar to what it was at a six-months level, but our revenues are increasing. So, if you are looking at it from a number of days point of view, the working capital cycle is improving. Let us say by next quarter, it will improve further. We stand by what was our original view that by FY'24, we want to come down to networking capital cycle of around 120-125 days and then beyond FY'24 we will look at further improving this.

Moderator: The next question is from the line of Archit Joshi from B&K Securities. Please go ahead.

Archit Joshi: The first is a clarification. I could not hear the number that you said about the CSM business. Did you by any chance say that the potential of CSM business is Rs. 2,100 crore or is it for the total potential that we are envisaging after the battery chemicals?

Dr. Harin Kanani: The number which I mentioned in the call as Rs. 2,100 crore refers to all the molecules which are currently under development. We are currently at 23-24 molecules which are at various stages of development – something which is in R&D, something which is in pilot, something which is in our first trial run. So, the total value of that is around Rs. 2,100 crore.

Archit Joshi: In due course of time upon considering the waiting period and once it gets approved, any direction that you are looking at with respect to achieving any milestones or when this will be realized?

Dr. Harin Kanani: This is at R&D level and this is the total potential of these molecules. So, depending on how successful is the R&D and how much percentage of them succeed. This will finally determine how much is realized. This is basically the pipeline that we have. When we go from Rs. 480 crore last year, to, say, Rs. 1,100-Rs. 1,200 crore revenue potential, what we are saying is by FY'25/FY'26 ; so that is the healthy pipeline we have. Now, some of it may even replace some of the existing molecules if the demand or the margin profile were to change. So, this was just to give an idea of what is the pipeline. It does not mean that exactly all of that will get converted.

Archit Joshi: Sir, currently at what run rate, what annual number will we be looking at only in the CSM business, I think, which is largely on the agri side? Is there a meaningful change that we are seeing with respect to all these molecules in the pipeline and the R&D stage. Are the application areas increasing or any color on that?

Dr. Harin Kanani: I think in terms of application areas, I already gave a little bit of additional information in the last call – that we are also seeing interest from flavors and fragrance areas as well as another area like the specialty chemicals industry, which is non-agri, non-pharma. So, for both of these we are seeing more interest coming in and that continues.

In terms of CSM percentage, our target was that by FY'24, we wanted to achieve 20% of our revenues coming from the CSM business. So far, currently in this year, we are at about 15% number. We are getting close to that and have received several further, initial first commercial orders which we are planning to execute, between now and June. Depending on that, we feel that this will add further. Plus, we are trying to work with the existing customers with their increasing demand. Hopefully by next year, as we had planned, we will reach at least Rs. 700-750 crore on a standard lithium price, with today's lithium price might become somewhere close to around Rs. 800-850 crore with at least 20% contribution coming from CSM. That was our target and we stand by that target.

Archit Joshi: Just one more question on the battery chemicals CAPEX that we have announced. The greenfield expansion that you are planning which as per the presentation, will most likely be commissioned in FY'26, and the total revenue target that we are looking at is Rs. 1,000-1,200-odd crore, only from the battery chemicals division. Would it be fair to assume that after we have commissioned the 5,000 tons plant in electrolyte and another 1,000 tons for specialty lithium salts, that there will be some leeway in terms of ramping up that capacity going into say FY'27 or FY'28? Is there a number that we are looking at in FY'27/FY'28? Also, with the contribution coming from capacity that we will commission in FY'26 or for now, are we just looking at Rs. 2,000 crore in FY'26/FY'27?

Dr. Harin Kanani: What we have said so far is, first of all, in the battery materials, we have only assumed India electrolyte demand currently. Of course, we keep the international demand as a backup, but we have not taken any significant number from that into our projections. We have also said that the capacity which you just said, would peak by FY'27. So, we will be fully utilized by FY’27. This is based on the clarity that we have and this is the minimum we feel we need. As we go further, as we talk to more customers and as the customers’ requirements crystallize, and as we keep signing contracts, if there are opportunities beyond this in electrolytes, depending on what market share we are able to get, we may have to further increase our capacity.

For sure, we will have to increase capacity beyond FY'27/FY'28, as we get into FY'30, when the overall demand is expected to be around 100,000-250,000 MTPA. So, with this capacity which you said, we will have capacity of only 10,000 MT. So, by 2030, we will definitely need more and depending on the market share even by FY'27/FY'28, we may need more. But this is the bare minimum that we need. And it is just keeping in mind this additional capacity which we may require beyond this, as well as our initiatives for salts in the international market may work. The cathode material requirements may also work.

So, that is why, to consider this as an opportunity, we felt the subsidiary having its own space and maybe having a greenfield site would be beneficial. That is why the board is currently considering if this can be done at a greenfield site, especially once we have taken care of the initial requirement of the next two years. Afterwards, in parallel, we can get the greenfield site ready and then that becomes the main site for our battery chemicals.

Archit Joshi: But, how easy or difficult is it to ramp up these capacities, because I can see that in FY'25, we will have a 5,000 tons plant in place, which will be a brownfield expansion, and then we will have 5,000 tons from a greenfield expansion, and we are looking at Rs. 2,000-odd crore potential in FY'27 or FY'26 at earliest. So, is it that once it gets done.

Dr. Harin Kanani: No, sorry, just to clarify that Rs. 2,000 crore number is both, battery and regular molecule together. So, for the regular demand, we have already made most of the investments, and the remaining ones will come in the middle of next year.

Archit Joshi: So actually, not the Rs. 2,000 crore number but the Rs. 1,000-1,200 crore number that we have talked about only from the battery chemicals division. So, my question was how easy or difficult it is to ramp up these capacities? Because as I said earlier, in FY'25, we are looking at a brownfield expansion of 5,000 tons and then immediately a year after that, we will have 5,000 tons more. So, all in all, with these 10,000 tons in place, we will be able to achieve this Rs.1,200 crore number. So that will happen in the same years instantly. Is this understanding, correct?

Dr. Harin Kanani: What will happen is the greenfield and the brownfield will run in parallel, because the greenfield will take a little longer time. Some of the things like site development, etc., will be happening in parallel. So, the 1,000 MT that we are doing is in the existing plant with very limited modifications. So, that will come first. Then in parallel, in our existing facility, we will do a brownfield for 5,000 tons. In parallel to that, we will also increase the salts capacity, from 400 MT to 1,000 MT. All these will come at our Dahej site, because this is where the majority of our lithium chemistry and the expertise currently are. In parallel, we will start working on the greenfield. That is why we have made all the announcements together, because some of this may run in parallel and not one after another. Yes, it will be a little bit of a challenge, but we feel that with what we have been doing in preparing for this, for the last one and a half years, we are now fairly well prepared to be able to achieve this timeline.

Moderator: Next question is from the line of Anirudh Shetty from Solidarity Advisors. Please go ahead.

Anirudh Shetty: My first question was on the Rs. 1,000-Rs. 1,200 crore revenue potential that we see from our battery chemicals business. Of that, how much would be from salts that we will be selling to third-party customers? I believe that a majority of the salts capacity will be used in-house. So, my second question around this is that, why are we not investing more aggressively in salts for international opportunities, especially given the pace at which EV is growing globally at much faster rate than it is in India at this point in time?

Dr. Harin Kanani: The way we have currently thought is that if we are using 10,000 MT, then, it will require somewhere around 1,200 MT to 1,500 MT of salts itself, and then remaining 500-600 tons would be available to us. But, for now, we do not want to commit ourselves that so much will come from electrolytes and so much will come from salts. We are three years away and we are just starting. As the business will develop, we will keep evaluating, we will see how the mix develops and how much comes from salts and how much from electrolytes.

As I have said in my previous call, in terms of strategic advantage, in terms of moats, when we think of India electrolyte demand, we feel we have the maximum number of moats or the strategic benefit or the value-add. Right now, when we are working with electrolytes, we have advantage of local market, thus being able to take care of logistics. We have some benefits over China.

Now, if we are targeting a non - Chinese international market, we are in direct competition and it is a head-to-head comparison. I mean, China has a clear scale advantage over us, whereas the only thing which we have is that we can be China Plus One. Other than that, so far, we are at a catching up phase in the international market. That is the reason why our primary focus remains on domestic electrolyte demand. We keep exploring international salts and we have got positive feedback. However, at least at this point in time, it is our plan-B or a second source.

As we go forward, once our trial production starts, we do commercial supplies, we understand our cost structure as compared to the Chinese how much of a difference there is and also the willingness of customers to be able to pay a premium over China for a China Plus One or a supply security kind of a strategy; that is when we will have a better idea of how much further investment, we would need for the salts demand for the international market.

There are many moving parts here. The capacities which we have announced are the capacities, which we feel we barely need to take care of for India's demand and we need to get started on that to meet the customers' timelines. That is the announcement we have made for now. As our pilot facilities start, trial production starts and as we keep getting more customer feedback, that is when we can keep revising our plan further.

Anirudh Shetty: My next question is on the margin profile for the battery chemicals business. I remember in one of the past calls, you had mentioned that on the innovation curve, the organic specialty would be higher than the electrolyte and the salts business. So, what would explain the margin profile would be similar for this new business? The second question is within electrolyte and salt, is there a difference in the margins that one would make if you sell these salt directly to a third-party customer?

Dr. Harin Kanani: When we are looking at our salt business, it is similar to making a simple lithium salts. It is just as when we made bromine derivatives and then we went on to make advanced intermediates and then maybe making advanced intermediates for innovator which is the CSM business. Ii is almost like that, in the sense that we have to first make basic lithium salt from lithium carbonate - of course, the purity requirements are much higher. Then we have to make lithium salt, which will be a little two-stage, three-stage kind of a reaction. It also has its own stringency in terms of purity, it has its own stringency in terms of moisture control and other impurity control requirements, and also some of the handling challenges of these materials. And then you are also doing a value add and making electrolyte out of that, which adds another layer of complexity and customization for each individual customer.

So, when we are doing all three together, we feel that it is similar to basically making bromine derivatives, making advanced intermediates and then doing CSM on an OEM basis. So, that is why we feel it has a similar margin profile. We have also looked at it from a cost point of view, the reactor volumes versus business point of view and it looks similar.

That is why we are hoping that we will at least get similar margins. That is, the bare minimum that we are looking at. Depending on the criticality and customization required by the customer, if we are able to add further value and the competitive scenario, we may try to get a bit of margin there. But, at present, in our models, we are using similar margins as our current target, which is 18.5% +/-1%. In our models to be more comfortable, we are using 17.5% as a base. As the business develops, the right numbers will emerge.

Anirudh Shetty: If the margins are similar, then should not the return on capital employed for this business be higher in scale, because like you mentioned, the working capital days are much tighter over here, and I believe in lithium, the asset turns also tend to be better. So, if everything goes as per plan, could not this be a ROCE business for us?

Dr. Harin Kanani: Two parts – the asset turns that we have seen are similar because this has the other complexity of moisture control and very high purification requirements, etc. So, ultimately the asset turns are something similar to that of organic production which we have seen based on whatever we can see now. But, yes, working capital cycle could be better, and on those terms, on a ROCE level, we could have a separate business. But, we can have an improvement over our existing organic business. For now, at least, let us consider similar margins and returns. They should be 20%-plus ROE and ROCE level.

Anirudh Shetty: In our existing business, with our current run rate, we could probably do around Rs. 600-650 crore within this year and the revenue potential by 2027 is around Rs. 1,050 crore. So, that translates to anywhere between 13% to 15% kind of CAGR. Given the opportunity that we have in this business and the China Plus One tailwinds and scope for more value add, is 13% to 15% a conservative number or do you think that the opportunity is much larger and the growth could be higher than this as we make further investments along the line?

Dr. Harin Kanani: I think this is just based on investments which we have done so far. As Dahej is stabilizing, we are seeing a lot of customer visits to our site. We have seen several pharma, agro, aroma and other industry customers also come in and show a keen interest in working with Neogen Chemicals for these new projects. Some of them are also discussing fairly large project volumes. Right now, our target is how we can have single molecules between Rs. 50-100 crore or Rs. 100 crore plus as a single molecule. We are seeing several projects come in which kind of meet this criteria. We remain hopeful there, but the number that we have shared is based on our current existing CAPEX, which we have already announced. Beyond that, as I said, we feel that we will max out by FY'25, and maybe FY'26/FY'27 if we might require further capacity; so, for that we may have to do further CAPEX in FY'25 or FY'26 depending on how the business develops.

Moderator: The next question is from the line of Noel Vaz from Union Asset Management. Please go ahead.

Noel Vaz: Just had one question relating to CAPEX. Rs. 450 crore is the total CAPEX. Exactly how do we see it being phased out over the next five or six years? Also, you had mentioned regarding the CAPEX itself that, in case the demand is much higher than expected, then accordingly we would have to make changes also. If that were to happen, then how will that exactly happen and within the next two years would you see another revision to this growth?

Dr. Harin Kanani: In the next financial year, we are increasing the 250 MT to 1,000 MT of electrolyte capacity, and then in parallel, we are also building a facility which can increase this up to 5,000 MT which will come by June 2024. This is the first part. In parallel, we are working on capacity, which will come online by June 2025. We do not have a year-wise numbers which we can share at present, but, yes, we do have it in our internal models. But we wanted to further fine-tune it before we give you a year-wise breakup of the CAPEX. But, based on that, you will see that initially we are just doing 1,000 MT, 1,000 MT becoming 5,000 MT, and then the 5,000 MT is again doubling. So, the CAPEX will come when we are setting up a greenfield and when we are doing the doubling part, which is basically coming online by FY'26. So, you will see significant CAPEX happening on that line in FY'24 and FY’25. This is on the CAPEX breakup.

Also, as I explained, yes, this is the bare minimum demand that we see and we are quite confident that we can achieve this number through several customers. But as I said, we will be able to give more clarity on whether this is sufficient or whether, we need more salt or more of the electrolytes, etc. That kind of slight adjustments we will have to do. We will be able to do this, maybe 6 months or 9 months down the line once our pilot facility starts and more approvals start coming in from our customers. Then we can give more clarity. If required, based on that, our FY’25 and FY’26 CAPEX plans can be fine-tuned.

Noel Vaz: So, quite simply put, based on the offtake that you would be getting at the pilot plant, then definitely we will get a much clearer picture as to what the demand scenario would be and we will get a much clearer idea of the whole demand scenario.

Dr. Harin Kanani: Yes. Because a little bit on this side, the demand is a bit more fluid as compared to our bromine derivatives and pharma business. That is the reason why we felt having a separate subsidiary gives a very clear view of how the operations are shaping up and how the changes are taking place.

Noel Vaz: Just one last query. Regarding the revenue guidance, is this assuming full utilization or this is like 80% utilization? What is the best way to think about it?

Dr. Harin Kanani: Basically, the guidance whenever we give is considering 80% utilization of our facility.

Moderator: The next question is from the line of Yash Shah from Investec. Please go ahead.

Yash Shah: Sir, my first question was regarding our capacity on formulation and salts. We can see that we will be increasing our capacity in tandem, which will be basically 20% of the salt capacity for the formulations. I wanted to understand from you that how much of the demand will be captive consumption and how much will we have to procure from outside – the electrolyte salts for the formulation?

Dr. Harin Kanani: Most of the salts will be made in-house. In fact, we have slight excess over and above what is required for internal consumption. Let us say, depending on the formulation, a 10,000 MT electrolyte facility would need somewhere between 1,000-1,500 MT of salt. Against that, we are planning a 2,000 MT. We always have a little bit of a buffer because the lithium salt reaction takes a bit of a longer time. So, it is always good to have a slight overcapacity there. If at all you have an additional electrolyte requirement, you can quickly do the electrolyte and be able to serve your customers at a shorter period of time and the additional capacity can always be used to target international demand.

So, at least the way that we have taken it, most of the lithium salts we should be able to make ourselves. However, there are many new additives, the main electrolyte salt and then there are some speciality additives that we need to take. Usually, specialty additives in terms of volume are not much and new additives keep coming all the time. So, some of the additives we will be making ourselves and some additives – since they are specialized ones – we may have to buy it from Japan or Korea where it has already been established till we make them on our own. The majority of the salts should be made in-house. Only a small quantity of some specialized additives might be bought till they are required at a scale where it makes sense for us to make them ourselves.

Yash Shah: That was going to be my next question. Do we intend to sell the additives as well, to the third-party customers? If my understanding is right, we do not intend to sell them, right?

Dr. Harin Kanani: We make salts whenever we have excess capacity available. Even additives if we make ourselves, we would be happy to sell them as well if we have excess capacity available.

Yash Shah: Sir, my next question was about our inorganic segment. The traditional lithium salt business which has been performing extremely well this year. Can we expect a similar kind of growth to continue in the 4th quarter and in the year ahead and in FY'25? And also, if you can provide some kind of commentary on the prices of lithium?

Dr. Harin Kanani: Prices of lithium, as we have shared earlier, as compared to the standard lithium price what has been there for many years, they have been between 6x to 8x of whatever is the usual lithium prices. So, they are significantly on a higher side. When you are comparing last year versus this year, a significant portion of that is also because of this price increase. When you go a year forward, yes, as we have explained to you, we are increasing our Dahej facility, and over the next 2 to 3 years, we also expect that that facility would be fully utilized. If the lithium price remains the same, you may see a 40% to 50% increase over the next 2 to 3 years. In terms of percentage what we are seeing is 85% and stuff like that, a significant portion of that is because of the higher lithium prices.

Next year, we will maintain the same level and then show further volume increases. On an absolute value term, whether it remains the same or it might even drop if the lithium prices start going down. What we are estimating is that when the dust settles and when lithium demand-supply is balanced, it might be 2x or 3x of what were historical lithium prices. That transition when it will happen, that is very difficult to predict. Will it happen in 2 years, will it take 4 years, or will it take 6 years to reach those levels is very difficult to predict. That is why lithium price remains a bit of a question mark, but at least from what we have heard, it is not going down to the previous level for sure. Even when it settles down, it will be 2x or 3x of what were the historical lithium prices. It might happen anytime between next 2 to 4 years. Volume-wise, we expect the volumes to see the additional 1,200 MT which we are adding, which will give us additional volumes over the next 2 to 3 years, but value-wise, it is a bit uncertain depending on how the lithium prices behave.

Yash Shah: Last question from my side would be, in the previous quarter, we had mentioned that we added about 5 customers on the CSM side on the flavors and fragrances, which had a revenue potential of Rs. 200 crore; wherein some of our projects had moved from pilot stage to the commercial stage. Have we already started supplying to them in the current quarter?

Dr. Harin Kanani: Whatever has moved from pilot to commercial stage, we have started supplying. Some we will be supplying in Q4 of this year. We did supply something last year, something this year. The aroma ones are still under discussion. The flavors and fragrances ones are still under discussion. They have not yet commercialized, but we are hoping that in the next financial year, we will see some revenue contribution coming from them.

Yash Shah: So, we remain on track with the 20% contribution from the CSM business by FY'25, right?

Dr. Harin Kanani: By FY'24. Yes, that is the target.

Moderator: The next question is from the line of Nitin Tiwari from YES Securities. Please go ahead.

Nitin Tiwari: Sir, my question is a clarificatory one on the CAPEX side. The Rs. 150-crore CAPEX that we had announced in the existing business, is that completely over or what percentage of that CAPEX is over? Secondly, is that Rs. 150 crore out of Rs. 450 crore in new businesses that we have announced? Thirdly, if not, then, does that Rs. 450 crore cover both the phases of battery electrolyte plant expansion?

Dr. Harin Kanani: Your first question is about how much of Rs. 150 crore we have done. As I said in my opening remarks and in the investor presentation, 50 m3 out of 60 m3 in organic capacity has already been commissioned and the remaining 45 m3 we are expecting to complete by September. On the lithium capacity increase, we expect most of the reactors to be in place by March. Anytime between March and May is when we are targeting for full commercialization of that. The third part of the Rs. 150 crore was lithium salt trial production. This we will be completing by June.

Of the Rs. 150 crore, we have already spent somewhere around Rs. 50-odd crore, maybe a little bit more than that. Ketan would have that number. But that is where we currently are in terms of the total CAPEX which we have done.

Your second question was, is the Rs. 450 crore in addition of this Rs. 150 crore? Yes, this Rs. 150 crore is separate. Rs. 450 crore is for the additional CAPEX which is basically to increase the Rs. 250 MT to 1,000 MT and then 1,000 MT to 5,000 MT, increasing the salt first from 400 MT to 1,000 MT and then another 1,000 MT and another 5,000 MT at a greenfield site. So, together, this will be Rs. 450 crore CAPEX and it includes both the phases.

Nitin Tiwari: Does the Rs. 450-crore CAPEX also include the cost of land at the new site which you have not declared or is it excluding the cost of land that you would have to acquire?

Dr. Harin Kanani: Yes.

Nitin Tiwari: Is it excluding the cost of land?

Dr. Harin Kanani: No, it includes the cost of the land.

Nitin Tiwari: So, let me summarize this. For 10,000 tons of electrolyte and 2,000 tons of salt, the entire CAPEX requirement is Rs. 450 crore.

Dr. Harin Kanani: Yes.

Nitin Tiwari: Can you break it up in terms of how much would be required for the salt capacity and how much for the electrolyte capacity?

Dr. Harin Kanani: Currently, because of confidentiality reasons, we do not want to share the breakup of this. Please give us some more time when we are comfortable sharing the breakup.

Nitin Tiwari: Lastly, any comments on the lithium deposits found in Jammu in India. What is your take on that? Would that work to bring the prices down or how do you see it evolve?

Dr. Harin Kanani: We are very happy with this development. We are sure that as the world progresses further, more such deposits will be found. Because, originally if we look at the situation from 3 years ago or 4 years, we already had identified a lot of deposits as compared to what the world needed. If you just think of India also, it required hardly 2,000-3,000 MT of lithium. So, nobody was motivated enough to look hard (for such deposits). Now, I am sure the entire world is looking hard (at finding such deposits) and I am happy that in India, we have already found a deposit and hope there will be more such deposits will be found. Because, previously, people were just not looking hard enough because the demand was not much.

It would not help us immediately because I personally believe that there is a lot of work still to be done to understand the exact composition. They have an estimate on the quantity, but what is the commercial viability of that? We are also still trying to find out the exact composition, concentration, what are the other minerals, and how the separation would work. We keep our fingers crossed and we are still trying to find more. But I do not think this alone will solve the lithium price issue, but overall, I personally feel that ultimately demand and supplies will catch up. There is a lot of lithium capacity being added the world over.

So, over a period of 3-6 years, the lithium price and the demand-supply will match up and the prices should become closer to what they were. As I answered in my previous call, it might be 2x or 3x that of the historical average just because some of the new resources which are being found and their processing cost is much higher and the royalty which one has to pay to the Government is also much higher. Therefore, it will never go back to the historical level unless there is a very strong demand crash or something of a path-breaking, new innovative technology. But it will be lower as compared to what it is. It is just difficult to predict when.

Moderator: We will take our last question from the line of Sabyasachi Mukerji from Centrum Portfolio Management. Please go ahead.

Sabyasachi Mukerji: The first question is, if you can explain the reason behind the gross margin dip during the quarter both, on QoQ basis as well as YoY basis?

Dr. Harin Kanani: It is just a function of both the lithium prices as well as the product mix in the current quarter.

Sabyasachi Mukerji: You have been saying that we are increasing our CSM mix, which I believe, is of higher margin and which was reflected in the gross margins in Q1 and Q2. Then sequentially has there been any other thing than lithium prices or the bromine prices were very high or something like that or any other reason?

Dr. Harin Kanani: Between CSM projects also, there are some projects which are of longer duration and have different gross margin profiles. It is again just a product mix difference between these molecules.

Sabyasachi Mukerji: In the long term, you would stick to around 45% to 46% of gross margin that we intend to do? Will that remain intact?

Dr. Harin Kanani: What I had explained earlier that we used to be like 40% +/-2% historically and now we expect 42% +/-2%, so between 40% and 44% on a stable basis. That is the way so far, we have seen. At least till FY'24, we expect that to be the case. Sometimes we may have a slightly higher margin but more or less, right now, the way the prices look like we expect to be in this range unless lithium prices change dramatically

Sabyasachi Mukerji: Next is on the electrolyte capacity that we are putting up. The 10,000 MT and the salt, largely almost 1,200-1,500 MT, will be internally consumed. Largely if I do a broad math, 10,000 MT yields Rs. 1,000 crore of revenue. I know this is not easy but then broad crude math of 1 MT yielding Rs. 1 million. So, 150,000 MT of potential capacity that India will need by 2030. Does it reflect that it is probably a Rs. 15,000 crore market size that we are looking at and then probably we would be having a bare minimum of 25% kind of a market share or more than that? Is that the way we are looking at it?

Dr. Harin Kanani: That is why on purpose, we have still not said how much 150,000 MT means. Again, this is a mix of salt and electrolyte. These are the capacities, and as I said, not all can happen together. We would still not want to comment on the exact price and the exact market size. We would like to wait till at least some few contracts are signed or there is better clarity in terms of how this business develops in India. So, please allow us time till then.

Sabyasachi Mukerji: This Rs. 2,000-2,250 crore guidance for FY'27 at peak utilization, these are, I believe, at stable prices, and on top of that if I do the 18.5% or 18% EBITDA margin, you are looking at a Rs. 350-360 crore of EBITDA by FY'27. Is the math correct?

Dr. Harin Kanani: We wanted to keep tracking what is stable lithium price and what is normal lithium price. For now, the current price looks like the price is going to stay for the next 2-3 years. That is why when we gave the revenue projection, it is more keeping in mind the current lithium prices.

Sabyasachi Mukerji: You believe that whatever we are doing, that is,16-16.5% margin, that will probably inch up to again probably 17.5-18%, or 18.5% by the time we reach the Rs. 2,000-2,250 crore by FY'27, right?

Dr. Harin Kanani: If the lithium prices remain the same, then it might be, again, a little bit on a lower side, the way you are seeing it. I will have to do the exact math that how much lithium will contribute and it will be somewhere around 16.5% to 17.5% in that region. And yes, with a stable lithium price, it will be somewhere around 18.5% to 19% in that region. So far, in our business if we do the lithium price correction, we have been able to depend on how stable lithium as well as the currency (will be) or how stringently we do the correction, we are again in that range of 18.5% to 19% EBITDA. This year also, we had targeted about Rs. 110 crore EBITDA, and with the run rate that we are at, most likely we should be able to overshoot the Rs. 100-110 crore target which we had kept for this year. We should be overshooting beyond Rs. 110 crore.

For most specific like EBITDA level targets, etc., my request is let this business develop a little bit and then as we are closer to the years, we will keep giving you guidance on what the EBITDA looks like, what the lithium price looks like. This is just to kind of give you an approximate idea on what kind of revenues we can generate and what kind of CAPEX which we are planning which we wanted to give today.

Sabyasachi Mukerji: Last question if I can squeeze in. The greenfield capacity for the battery chemicals, I believe, would be mostly domestic focused and hence probably the site will not be in Dahej or in some other place. Is my assumption correct? Have you finalized the land?

Dr. Harin Kanani: You are right. It will be largely domestic and so it will not be in the SEZ. That is correct.

Moderator: Ladies and gentlemen, that would be our last question for today. I now hand the conference over to the management for their closing remarks. Thank you and over to you.

Dr. Harin Kanani: Thank you all the participants for joining the call. I hope we were able to address your queries. If you have any further questions, please feel free to reach out to our Investor Relations team, CDR India, and we will address them. Thank you once again. Stay safe. We look forward to connecting with all of you again in the next quarter.

Moderator: Ladies and gentlemen, on behalf of Neogen Chemicals Limited, that concludes this conference. Thank you all for joining us and you may now disconnect your lines.
