Punj Lloyd Limited

Investor/Analyst Conference Call Transcript
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Moderator Ladies and gentlemen good day and welcome to Punj Lloyd's Q1 & FY15 results conference call. As a reminder all participant lines will be in the listen-only mode. There will be an opportunity for you to ask questions at the end of today's presentation. 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. Vinay Krishan Sood – Head of Investor Relations at Punj Lloyd Limited.

Vinay Sood Good afternoon ladies and gentlemen and welcome to Q1 FY15 earnings conference call. Joining us today on the call are members of our senior management team Mr. J P Chalasani – Managing Director and Group CEO, Mr. Luv Chhabra – Director Corporate Affairs, Mr. P N Krishnan – Director of Finance, Mr. Pardeep Tandon – CEO B&I, Mr. Atul Jain – CEO Pipeline & Tankages, Mr. Arun Sharma – COO Power, Mr. Shantanu Karkun – President & CEO B&I. I believe you have received the investor communication along with the results. Just to recap, the current order book stands at Rs. 21,164 crore, revenue for Q1 stands at Rs. 1,122 crore and EBITDA at negative Rs. 244 crore.

Before we begin, I would like to mention that some statements made during this call may be forward looking in nature and disclaimer to this effect has been sent to all with the conference call invitation. I would also like to emphasize that while this call is open to all invitees it may not be broadcasted or reproduced in any form or manner. We can now begin with the questions.

Moderator Participants we will now begin with the question and answer session. We have the first question from the line of Saket Kapoor from Maple Vyapar Pvt Ltd.

Saket Kapoor My question is with respect to the interview given by Mr. J P Chalasani that was telecasted on CNBC TV a few months ago anchored by Shereen Bhan. In the interview Mr. Chalasani had very categorically stated that the debt level of the company would be 40% lower from the peak that it is at today.

So, are we heading in that direction? Also, looking at the balance sheet of the company what sort of restructuring is needed or are we adequately capitalized to ride the infrastructure boom that may happen with a very strong government at the helm?

J P Chalasani If you have heard that interview in detail, I mentioned about the source of funding which we expect for debt reduction. There are two main areas; one is non-core asset monetization – the sale of barges and Medanta stake monetization. The second part, the focus areas for the company today, is to recover our claims. As we had mentioned last time, that when we had taken stock of every single project which we have handled till now and whatever claims we have lodged, the amount is close to Rs. 10,000 crore. But based on our internal estimates even on a conservative basis we expect Rs. 3,000 crore to be recovered. So this Rs. 3,000 crore from claims settlement plus barge sale plus the Medanta stake monetization together would give us adequate funds and even if we pump part of this back into operations, we see our reduced debt levels at around Rs 4,000 crore. Unless we reduce the financing cost, the amount of hard work done in improving the profitability of the projects would go towards paying the interest. Therefore it is necessary for us to bring down our debt in order to improve our bottom line.

With respect to the second part of your question which is whether we are in a position to capture the expected boom in infrastructure sector. My answer is yes. In my opinion for an EPC company, the only capital we need to go ahead and do these projects are the people, organization and processes. At the top management level we have added significant strength; we had mentioned last time that we have setup a new procurement team, which is now fully established and we are seeing the results of that. Mr. Shantanu has joined us as the new CEO for our building and infrastructure division. We are going to have a new President and CEO joining for power division in a week's time and we are getting a new chief financial officer to assist Mr. Krishnan. We have just appointed a president for contracts and new business initiatives who has also joined. So we have strengthened our management team and we are now strengthening our systems and processes. Therefore, I think this is what makes us ready to capture new business. That is what is important for our EPC business.

Saket Kapoor Down the line what should we expect in terms of revenue as in the first quarter the revenue booking has been dismal and very less to state anything about it. What sort of order execution should we expect going forward? Whether it is the strengthening of the management team and the other aspects which you are trying to implement, what should be the run-rate going forward?

J P Chalasani I slightly differ with you on dismal revenue booking, as at consolidated level we have done about Rs. 1,500 - Rs. 1,600 crore of revenue. So I do not think that is dismal. Yes, it is significantly less compared to what we had clocked earlier. But having said that, we are now at a stage where the existing set of projects are tapering off and the new set of projects are beginning to take off. I think this year performance might remain flat as to what it was in the previous year. The revenue should pick up in the following year.

Saket Kapoor What corrective measures are you taking to address the revenue issue?

J P Chalasani First thing is we need to know the reasons for lower revenue. Then we need to know what corrective measures are required or to what extent they are required. As I had mentioned, if you look from the point of view of claims, we have accumulated claims of huge amount of money. Also, some of the claims like ONGC are taking years to get resolved. One of the things which we consciously decided in the company is that we cannot continue to have a system where we keep working and settle the claims at the end of the contract period. If there are bottlenecks while we are executing the project we want to escalate those bottlenecks at that point of time and see that we settle them during the contract period rather than waiting for it. To cite an example from this quarter, one of the reasons for the shortfall in revenue is on account of a project called poly-silicon project in Qatar which is one of the very large projects which we are executing. We did have a set of issues with the client. The team including the CEO, who is also present on the call, took a view saying that it is better to settle these issues at this stage rather than continuing and subsequently facing an issue. So we reduced our progress substantially and told the client that we have to settle it. So now we have signed a settlement agreement with them and are moving ahead with full speed this quarter starting in July. But in the last quarter because of this, the revenue compared to the target had a shortfall of about Rs. 350 crore. That is because we wanted to escalate the issue and get it resolved. That is one big hit we had in the last quarter. Myanmar is the second example where the work on oil pipeline is almost complete and gas pipeline has just been put to use between Myanmar and China. Once the subcontractor's bill of about Rs. 250 crore comes in, we could start recognizing that into revenue. Third project which we did in a similar way like QSTec was Hout project in Saudi, which is an offshore project. We have officials who are now across the discussion table with them and we are trying to resolve the issue so that we can go full tilt towards reducing the Rs. 140 crore shortfall in target. Myanmar was Rs. 250 crore, Polysilicon was Rs. 350 crore. One of the projects which really impacted us was the GSPC project where we had to revise our profit margins due to some claims of subcontractors which we went through in detail and recognized those claims. So because of the revision in profit margin we booked earlier, we reduced our revenue. Just these four items put together itself is around Rs. 900 crore. That is the major reason why we see shortfall at the standalone level. In fact if you look at the consolidated level the shortfall is slightly less. We are at Rs. 1,600 crore at consolidated level compared to Rs. 2,359 crore in the last year. So currently, we are predominantly working with the understanding, that the issues should be settled as they arise rather than deferring them. Therefore, this is not something where a corrective action needs to be taken for increasing the revenue. But then obviously in future also if you face issues in the set of projects then we would hold on there and try to get them resolved.

Saket Kapoor We got clarity on the revenue part but how is our bottom-line going to shape up? You are having the capacity to execute this project. But what about the bottom line because at the end of the day it is the bottom-line that matters to all of us?

J P Chalasani Absolutely. I had mentioned earlier that instead of chasing top-line we want to chase bottom-line. On the EBITDA side of it, if you look at the difference between the previous quarter and this quarter, in the last quarter we had positive Rs 285 crore and this time it is negative Rs 240 crore. In GSPC we took a hit of about Rs 145 crore. We have accomplished about Rs. 100 crore of cleanup of the projects which were very old and were still lying in the balance sheet for various reasons. We have just cleaned up many of those small projects which are not part of the order book backlog but they were still figuring there. As we all know, Sabic has a £5.3 million pounds undisputed amount. As it is an undisputed amount which we have also agreed to, on a conservative basis we have booked that in the balance sheet. That is about Rs. 54 crore. The last aspect is because turnover itself is low; almost about 55% of the previous year, EBITDA will come down because revenue is slow. To sum it up these are the four major reasons for why your EBITDA is low – Sabic, GSPC, old projects cleanup and the turnover being low.

Saket Kapoor What was the issue with GSPC?

J P Chalasani GSPC we had to revise our profit margin by Rs145 Cr.

Moderator We will take the next question from the line of Inderjeet Singh Bhatia from Macquarie.

Inderjeet Singh How much exposure we have to Libya? We have been taking orders as late as second half of last fiscal year. Also, now as the Government of India has officially given a recommendation to Indians to leave that country, what is our asset base? What is the kind of debt that you have taken for those projects? So any details on that would be helpful.

J P Chalasani The current order book that we have in Libya is roughly about Rs. 7,800 crore. Till about three weeks back, the entire escalation happened. As we had mentioned last time, we have been working on one of the projects which is the Arada Project. In fact in this quarter we have billed some $3-4 million for Arada Project but in the last 3-4 weeks our interest was mainly to safeguard our people and our assets. So, currently we have put suspended animation on the whole Libyan operation. We are just taking care of our assets and our people. In fact we are evacuating as many persons who want to come back, but the core team still remains there. We have taken a wait and watch approach for Libya. Having said that, there is no loan taken on Libya project. So therefore that issue does not exist.

Inderjeet Singh What would be the value of assets that we have deployed?

J P Chalasani We have plant & equipment worth $14 million.

Inderjeet Singh Any unbilled revenues?

J P Chalasani Total outstanding is about LYD 275 mn, including claim which was agreed for about Euro 70 million.

Inderjeet Singh In the opening comments we mentioned that we have large amount of funds which are stuck with the Government and I think the number quoted was close to Rs.10,000 odd crore.

J P Chalasani No. I did not say the claims are with Government. It was mentioned that the total claims which we lodged with all our clients across the globe is Rs 10,000 crore and our own internal estimate on a most conservative basis is about Rs 3,000 crore of this should be recovered.

Inderjeet Singh And how much of that is in India especially to Government because India would mostly have the Government part.

J P Chalasani The major portion in India is ONGC.

Inderjeet Singh And what is the status of that arbitration and the whole process?

J P Chalasani The OEC, not arbitration is the outside expert committee and the last meeting they had was on Saturday, 2nd of August. The hearings are now completed, so we expect the OEC to give their report. They said that they will try to do that by the middle of September.

Inderjeet Singh And what is the kind of escalation clauses available if either sides do not agree to that report?

J P Chalasani We can go back to Arbitration.

Luv Chhabra I think in the case of Hira we should clarify that originally we had gone to arbitration. Then at the suggestion of ONGC we took the OEC route. So our arbitration is in suspended animation.

Moderator Our next question is from the line of Pritesh Chedda from Emkay Global

Pritesh Chedda In our interaction we discussed that we are working on the operations side of the company and somewhere in the call also you pointed out that there is a disconnect between the scale of revenue and the scale of operations. What efforts have been put on the operations side in terms of managing it better and when do the benefits actually start flowing? Should the benefits be a function of just higher revenues or the benefits can also come in terms of better management?

J P Chalasani I think the benefits have started flowing in some projects where we are in a position to show them. For example, one of the things if you remember we spoke about is for an EPC company, basically what you can do to improve your margins significantly is in 'E' and 'P'. The 'P' that is the procurement portion is what we have worked on in the last four months. We have completely centralized procurement. We have a very senior level team put in position called central procurement team not just in India but they operate from different parts of the world. For example, even the Shell Marina project which we just concluded, all the contracts which were awarded, we had seen the benefits. But then what you are seeing is the result on an overall basis and are not able to appreciate the benefits that are accruing because of these changes. Right now we have a set of projects which are delayed or are working on an extended time period. So there are profit margins getting reversed. I expect such projects to close by the end of this financial year. We also have a lot of good projects which are under progress today, like Shell Marina project, Jamnagar project, IOC Paradip, CPCL project, QSTec project and few other projects. They will continue to add to our top line and bottom line. But some projects will get completed this year and the new set of projects, whether it is the Kuwait project or the Brunei LNG or the pipeline including the MN Road project which would take off. Therefore, you will gradually see the improvements. Today, we are seeing at the project level but at the overall company level we will be able to see it as we move ahead. But obviously all of you would expect it at the company level, as at the individual project level it does not really make a visible impact. That would happen gradually.

Pritesh Chedda Are there any chances for cutting the operation cost in the process? So one way is basically you align it better and you manage it better. Are there any areas where specifically the cost can be cut?

J P Chalasani One is the procurement cost. The benefits we can get in procurement are already evident. Secondly, in the current year we have given ourselves a target of reducing the overheads at different levels. We put ourselves at a target of 10% reduction at all levels, i.e. at the project, at the vertical and at the corporate level put together. In the first quarter we did achieve the target. In fact we achieved a little more than 10% overheads cut. Whatever the overheads we cut, it can be said that it will benefit the bottom-line. Thirdly, we started looking at the project implementation methodology much more closely. We have our project management side including manpower optimization. That is where we have got a couple of external agencies getting embedded into us and working in three or four projects now. So they would work with us and also come up and articulate the areas where we can actually further do better project management and reduce the cost, these are the different steps we have initiated for this program. Some of them are still in the process while some of them we have already started implementing. I think these things as we move ahead we will see gradual results.

Pritesh Chedda So, if I understand FY15 will actually be a year where you get away with older projects, whatever it be in terms of providing for it or getting it executed and on the other hand even try and manage the operations better. Now because you have a certain quality of revenue being booked or certain provisions being made in FY15, the benefit of the new project execution and the operations management should be visible in FY16?

J P Chalasani In fact I have been on record and wherever I meet people I have been saying that my personal target and then my team's target is that at the end of this financial year we will be on ground and become visible to people and people will become visible to us and then we start the growth thereafter.

Pritesh Chedda The numbers which were given out by you with respect to the revenues which have been hit on the HOUT project in Saudi, are there other projects where revenue has been hit?

J P Chalasani One is shortfall in revenue in the following projects – QSTec project, poly-silicon project in Qatar, Myanmar, Hout and GSPC. In the follow-up question of the gentleman which was on profitability on EBITDA, I spoke about Sabic, GSPC, cleanup of Rs. 100 crore and turnover itself having come down to that extent and proportionately EBITDA is be down.

Pritesh Chedda How about the cost there? Costs have been booked or the projects were stalled, so there is no cost and there is no revenue.

J P Chalasani Costs were there, corresponding revenues were there and the other three items of GSPC, Sabic, and old projects cleanup is actual cost of provision being made.

Moderator Our next question is from the line of Vikas Gupta from Canara HSBC Life.

Vikas Gupta Mr. Chalasani you talked about the sale of non-core assets. Can you share with us at what stage it could be and are there any timelines for that?

J P Chalasani We always have a timeline. I think unfortunately this is one place where it pinches. We can put up a moving goal post on these two items. But as we speak the current status on the barges is that we have now negotiated the agreements except for a couple of points. I think things will reassemble after the Eid holidays and the barges have already sailed out to Abu Dhabi. Therefore, now the joint inspection is happening. We expect the documentation portion to be done at the end of August and sometime in the beginning of September is when we should see the realization of money from barges, unless any unforeseen event happens. Also, on Medanta, due diligence is going on and by the progress we expect that sometime in September we shall be able to close.

Vikas Gupta So as of now, how much will be the slow moving order book out of the current order book?

J P Chalasani As we speak today, the Rs. 7,800 crore order backlog from Libya can be put as slow moving. We do not know what happens on that. So other than that, I do not see any other significant projects which are slow moving today.

Vikas Gupta And in the current result press release it was written that there is a client who has encashed performance bond worth Rs. 170 crore. So can you throw some more light on it, what exactly it is?

J P Chalasani We have two projects in Thailand which we are doing for a company called PTT. We are doing one pipeline project and one offshore project. It is called the PCF project. On the pipeline project there were a set of issues between us and the client. We could not get it solved and finally the contract had sort of terminated and we went to court. When we went to court, the court wanted to decide whether the proceedings shall be part of administrative court or part of civil court. The issue was whether the PTT was a Government body or is it a Government undertaking. While the process is in progress, in fact the next hearing is on 8th August, they went ahead and encashed the bank guarantee. After this we approached various courts in Thailand to see whether we can get an injunction but we were not successful in the process. So they have encashed it but at the same time it is now part of the litigation along with the whole contract.

Vikas Gupta What will be the size of these two orders?

J P Chalasani $290 million was FTP and I think $130 million odd was PCF.

Vikas Gupta At what stage these orders will be in terms of execution?

J P Chalasani The second project is about 96% complete. We were about 60% complete in the pipeline project. This project is now terminated and in court.

Moderator Our next question is from the line of Jigar Valia from OHM Group. .

Jigar Valia How do we normally account for claims? I understand about 50-60% of our claims have already been booked as revenues and you gave a number of Rs. 10,000 crore which relates to claims. Can you explain how much would be a part of debtors and inventory?

J P Chalasani Whatever claims are booked, it is to the extent of wherever there is some sort of an agreement or an acceptance. Only one large claim which we booked is ONGC, about Rs. 946 crore against the last OEC recommendation of Rs. 1,100 crore.

J P Chalasani In the last quarter there was a setoff where we originally considered $97 million.

Jigar Valia So that was also booked and then we reversed $37 million.

J P Chalasani We had an offer from client of $60 million, we still think that we can go up but as the offer was for $60 million, we decided to reverse $37 million on conservative basis.

Jigar Valia On barges you have mentioned the timeline to be first week of September. On Medanta are you giving a timeline?

J P Chalasani Yes, September.

Jigar Valia Currently, how much is the total receivables, unbilled revenue and plant and machinery in Libya?

J P Chalasani Receivables is about LYD 15 million and machinery about LYD 14 million. Unbilled revenue is LYD 275 million including agreed claim of €70 million.

Moderator Our next question is from the line of Ashish Shah from IDFC Securities.

Ashish Shah You had mentioned that in a couple of projects you have reached some sort of settlement. Is there any sort of cost increase that you might have booked in these projects? Out of the four projects you had mentioned it was said that for GSPC Rs. 145 crore of profit has already been reversed. Would there be a similar outcome for the other three projects?

J P Chalasani Currently in Hout, we are talking to the client on how we settle. Accordingly, there is some progress made but it is work in progress and therefore it is difficult for me at this stage to say how much the value is. We have also put up some additional costs that were incurred. So it is in negotiation stage. On Myanmar, we said that we have done the work but the subcontractor's bills are what we need to receive about Rs. 250 crore and therefore we have not booked. The other project is polysilicon. So whatever we wanted in terms of additional cost change is now agreed on how to move ahead with the project.

Ashish Shah In the Thailand project, we now have around Rs. 562 crore. As I understand, Rs. 391 crore is the claims and Rs. 171 crore is the performance bond. So potentially if it does not go in our favor, then this is the amount that might have to be written off in the Thailand project. Is that the right understanding?

J P Chalasani Yes. But one is termination and second is the claims. We believe that we are in a very strong footing as far as the claim is concerned and therefore there is reasonable confidence. Also, irrespective of what is happening on the legal side we have maintained a good relationship with them as one project is still ongoing. I have also personally met the top management team of PTT 3-4 times in the last 3-4 months. Therefore, the idea is to settle those things amicably. We are reasonably confident. We believe that we may not reach a situation where we need to write-off.

Ashish Shah What would be your consolidated debt?

PN Krishnan The debt is to the extent of about Rs. 5,344 crore on a standalone basis. On a consolidated basis the debt is about Rs. 6,470 crore.

Ashish Shah Is there any particular reason we did not give the consolidated numbers?

PN Krishnan As per the Clause-49, we have both the options to either publish standalone or consolidated numbers. So while for the management review, we are considering the consolidated numbers but for the purpose of publishing, which also involves auditors to do a little more work it is just the standalone part we have published.

J P Chalasani But otherwise we share the numbers. As I said that in fact at the consolidated level the numbers are slightly better compared to what they are at standalone level i.e from the point of view of shortfall in performance.

Ashish Shah Could you give the other numbers too, i.e the consolidated EBITDA and the PAT numbers?

J P Chalasani EBITDA is about Rs(-238)Cr. The PAT is Rs(-443)Cr.

Moderator Our next question is from the line of Ronald Siyoni from Sharekhan. .

Ronald Siyoni I had same query regarding consolidated results. From now on you would not be publishing consolidated results. So would we be able to get the consolidated P&L?

J P Chalasani Yes, we have given you now and we will continue to give you. To the exchange we have given the standalone numbers. But if you want consolidated numbers, I will ask Vinay to share.

Moderator We have the next follow-up question from the line of Saket Kapoor from Maple Vyapar Pvt Ltd.

Saket Kapoor We have seen that the Government is putting a lot of thrust on laying down of gas pipeline and the concept of smart city. How well is our company positioned to take advantage of these forthcoming projects in these two arenas of smart cities implementation and gas pipeline project?

J P Chalasani In pipelines, we are one of the largest players. We are keenly watching every single opportunity and we will participate in each and every opportunity in the pipeline space. On the smart cities front, we are now preparing the group into how do we participate. This is part of our B&I division. Therefore, this is something which is at preparatory mode at this stage. We are deep-rooted in pipelines and it's much easier for us as we have the knowledge, experience and people. We are very keen on smart cities project and we are now working internally so that we are prepared to participate.

Saket Kapoor Previously, a lot of damage happened to our balance sheet because of erroneous projects, cost escalations and other factors. Is the management also looking for some fund raising exercise even though Mr. Chalasani has very categorically said, it is people who are going to work for EPC projects and not specifically the balance sheet size.

J P Chalasani I think right now our concentration is on enlarging the EPC business where we want to use more of the organization. But moving ahead once we stabilize ourselves then obviously we would like to play a role of a developer on some of the infrastructure projects. We are going to expand further on this front. Right now we are doing solar and a police quarter project in Delhi. These are the places where we are putting our own equity. Once we see some stabilization in the EPC business, then I think from FY16 onwards we will start looking at investing more and more into the company that is when we may need more capital.

Saket Kapoor Can we expect greater changes in the revenue and the profitability going forward for this year itself? Is this what you have categorically stated in your opening remarks that FY15 is going to be a consolidating phase and it is only from FY16 onwards that investors can expect EBITDA positive level from the company. Is our expectation correct?

J P Chalasani Last quarter and this quarter you have seen and my assumption is that from now onwards each quarter you will see a quarter-on-quarter improvement. So that is something which we can give as guidance. So if you take this quarter as a base we will keep improving on this. I had also said that some of the projects which are delayed are the projects we want to see ending at this level. So therefore we can see much broader positive results in the coming year.

Moderator Participants that was the last question. I now hand the floor back to the management for closing comments.

J P Chalasani We are open to share the numbers at a consolidated level because we have done that for our management review. Therefore, there is no second opinion about that. The other message is the same which I just said in my commentary, that we are currently strengthening our team, our processes and we are seeing some results in the projects which are moving ahead on that basis. But on an overall basis you will start seeing the improvement on quarter-on-quarter basis as we move ahead. I have been on record saying that the opportunities in India would start materializing only from Q3 of this year. So we are right now getting ourselves prepared because we feel that B&I is one area where we think that there are going to be opportunities. Power is again we expect that the opportunities in India and outside will increase so we are significantly strengthening our teams in those areas. The other one is the pipeline and tankages vertical in India is expected to pick up. So we are internally getting prepared ourselves at this stage by improving our current set of processes and operations and be prepared for capitalizing the opportunities which are likely to come.

Luv Chhabra I would just like to add to what Mr. Chalasani has said on defense. I think this Government has placed a lot of emphasis on indigenization of the Indian armed forces defense procurement. As all of you know we have made an investment in a fairly sophisticated defense manufacturing unit at Malanpur in Madhya Pradesh where we are already doing subcomponents and assemblies for some of the defense PSUs and defense departments. So for example, we have made fuel panels for the Sukhoi. We are doing the machining for the combustion chamber for the Mig aircraft. We are doing the casing for the advanced light helicopter for HAL. So we now believe that unlike what we saw in the previous five years of UPA II, this Government will give a lot more emphasis to buy and make India programs. And we are ideally positioned for those programs having a good engineering set up, having a very strong manufacturing base and I think in the next 3 to 4 years we hope that you will see Punj Lloyd as a pretty strong contender in all land systems and may be some of the aviation related component and sub-assemblies in these programs and we have already started bidding for some of the large programs. Hopefully we will see success in the next couple of quarters.

J P Chalasani Those are the concluding comments and we once again want to thank each one of you and Vinay and his team are available for any further specific clarifications you need.

Moderator Ladies & gentlemen on behalf of Punj Lloyd's Limited that concludes this conference call.