

Morganite Crucible (India) Limited
Morgan Advanced Materials
Molten Metal Systems
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Aurangabad - 431 136,
Maharashtra, (India)

Transcript of the Investor Meet held on July 15, 2022

Attendee:

Mr Aniruddha Karve – Managing Director MMS
Mr Hanumant Mandale – Chief Financial Officer
Mr Rupesh Khokle – Company Secretary
Mr Nirav & Ms Saloni – Molecules Ventures

Mr Rupesh Khokle: Hello Ms Saloni & Mr Nirav, nice to meet you. Mr Aniruddha Karve will be joining soon. I request you to keep your questions specific so that we can answer within timeline.

Mr Aniruddha Karve: Good Afternoon everyone.. Apologies. I am slightly late to join the call. I hope everything is good at your end.

Ms Saloni: Thanks for giving us the time now.

Mr Aniruddha Karve: Before starting the discussion, please tell us about ourselves and about your firm.

Ms Saloni: Thank you, Sir. And you know for it I'm a managing partner of Molecule. We are SEBI registered PMS and private equity managed firm and we got a license in May 2021. For the PMS, our focus is purely on the small cap and mid cap and on the market. Since last one year we have been looking at capital goods industries. We are kind of seeing clear signs of CapEx revival and we have been evaluating complete into that particular theme and that is how we got interested in Morganite, and Saloni been looking at the company for a couple of weeks now and that's all she was trying to reach you guys. And I think she'll take it over on the Q&A side.

Mr Aniruddha Karve: OK. Thanks for the introduction.

Ms Saloni: Thanks. So my question that is divided into couple of parts like it's product related, what the company does followed by industry related questions, for those working in that activity question, then I'll reach to company specific and then some few drivers and monitors with regarding to come.

Mr Aniruddha Karve: OK.

Ms Saloni: Please explain about the crucible business, what are they used in? basically ferrous industries, non ferrous industry. Who are the end user customers? So just a basic understanding about the company.

Mr Aniruddha Karve: OK, fine. Let's start with that. So I'll give you a bit of an introduction on the company structure as well, sort of holding side, OK. So you must have done your research. You know that there's a couple of entities that hold 38.50 and 36.50 shareholding in MCIL totalling 75% of Morgan holding. We Morgan Advanced Materials are about £1.1 billion materials, Advanced Materials group, and there are five verticals, 5 business verticals within Morgan and molten metal systems which I run is one of them. Molten Metal system makes Crucible like you observe foundry products and other things, but this is how the company started actually in the UK back in 1856. So we are the original business of Morgan. Of course, now the company has grown over and about the principles product line, a lot of advanced ceramics and carbon type of products. So we have electrical carbon seals and bearings, thermal, technical, ceramics in addition to MMS. So more to metal systems is a global business. We will operate worldwide. We trade in more than 120 countries, most of which is done through our distributor partners because our end market is fairly fragmented and therefore the cost of serve is best realized through distribution. People can keep the entire portfolio and on stock and feed the market as required. Crucibles, you know, basically what is used for melting and holding aluminum, copper, zinc, gold, any metal, any nonferrous metal primarily, OK, so not iron, steel though we have a few possible that go into our meeting, but mostly known for non ferrous metal. Yeah, you got a question.

Ms Saloni: So why is that that the group was only used in non ferrous?

Mr Aniruddha Karve: Yeah. So the the melting temperature of iron and steel are over 1600 Celsius. OK. And at that, at that temperature, they require what are called insulating refractories. So the material that can withstand that temperature and hold the properties at that temperature are a separate group of materials. And we have some of that exposure, but where we specialize as a non ferrous melting, which where the melting temperatures are typically somewhere between 500 Celsius to, let's say 1200 so the what we called. Our sister Company, which operates in India. They operate as a Murugappa Morgan thermal ceramics. But this is the thermal ceramics business. They supply a lot of the linings for the iron and steel business, so they take care of that portion while we take care of the non ferrous market and speak about non ferrous markets or anywhere where there's a non ferrous metal being melted or transferred or somehow processed. We are present and that because driver that you will end markets would be well first one is aluminum. Aluminum primarily goes into automotive applications. So you look at you know engine chassis. You know the panel and so on. So if you look at the way we roughly break down our business about 60% a little bit more than that. So about 60-70% of our product ends up in an aluminum melting and holding a casting application and about 2/3 of that is going into the auto industry. Right. So our exposure to the auto directly or indirectly is about 50%, fifty, 55%, right. Then you have other automotive aluminum applications, those for white goods for instance, you're washing machines are refrigerators microwave, that kind of thing. So that aluminum casting that go into that, there are lots of other industrial applications meter boxes valve bodies, things like that that also take a look in casting. So 2/3 of aluminum casting go into auto. Want to go into other white goods and industrial application and that for us is roughly about the same now where we are seeing increase user volume minimum is very high purity aluminum used in semiconductor. So this is you know Taiwan, China, Japan type of thing and we are starting to now we started establishing a presence in that market in 2009-10 but it was very initial because they're the contamination requirements are super critical. Don't drop your room and I'm so they don't want any pick up from the Crucible and so on. So we are starting to grow the business now, but that's out of our Chinese entity primarily not our Indian one, not mcil. So that that you have proper and brass, which is really driven by construction because you have a lot of illnesses and things like that.

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We have a certain segment of our crucibles that go into the copper and brass segment about 15% if I remember correctly. That's that's going into copper and brass then we have precious metals, OK, precious metals means anything from your jewellery that make earrings. They use small groups of both. So melt the gold and pour into a mould or other jewelry to the big mines like Anglo American Barack. You know, Rio Tinto, Rand refinery, they use our crucibles in refining gold in the mine sites.

So you got majority in aluminium second largest segment is probably there's a tie between precious metal and copper and brass alloys. And then you have finally you have zinc oxide which is a very specialized application where they distillate. But it does still from zinc and that is used in tires. It's used in paint. It used in cosmetics like your foundation and so on. We have a pretty large exposure to aluminium and therefore auto. Our products actually go into sort of huge range of industries and we have some big names that are customers, right. So you've heard of the Ferrari Formula One team, right, they use crucibles to melt aluminium to make their engine blocks for the Formula One racing cars, Rolex, the watches, the all of the cases of the watches are made in Morgan reusable statue of Unity in Gujarat. Part of that process in Morgan Crucible, the Big Shivaji statue of Maharashtra in Aurangabad which is you know where by the so you can tell that we have a fairly large a lot of some defence applications as well but not very, very much where the aluminium is used that we would have that. So we have a fairly diversified end market portfolio though we are tilted to auto towards auto and on the auto side I will give you a couple of trends that we are really watching one is. The aluminium content per vehicle keeps going up because people want a lightweight, so people are getting away for a lot of stamp, stamp welded assemblies and into aluminium castings, which is good for us.

The other thing is on the EV side. So when you look at what you wanna transition to, EV comes what we see is that the amount of aluminum in the car will go up, but there would be less castings. OK. So I'm casting is our main boundary is a main end market. So what we are trying to pivot to is, OK, what does that mean for us? Extrusion industry sheet, metal foil, that kind of thing. Uh, I'm not. I'm not aluminum side. And how can we participate? So that's future growth areas for for us. So that sort of gives you a breakdown for 95% plus of our revenue comes from the crucibles themselves. Then you have other foundry products which are handling to thermo couple sheets and just very specialized stuff that is used in the melt shop of foundry.

That requires contact with molten metal, so anywhere where there is a contact with high temperature metal where you require erosion resistance, right the metal flows by the product it should not erode away or it needs to be resistant to chemical attack fluxes and things like that. That's where our product performed the best. In iron and steel like I said, thermal ceramics handle that because it's gonna requires a whole different range of materials and properties.

Ms Saloni: In the value chain apart of the casting process, so I need to understand that how are they replaceable and like what is the replacement cycle of possible? how often it is consumed and the handling part. I tried to search about that if it gets mishandled, it needs to be replaced right away. So how often does it occurs?

Mr Aniruddha Karve: Yeah, So we have a range of that, OK. So I'll give you an example on the extremes. So we have automotive customers like Toyota. They were very stable user product, so you rarely ever. It's like and we will price it according to the value proposition that we offer, right.

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And there am I audible or is it the poor network?

Mr Rupesh Khokle: We just lost for a couple of seconds.

Mr Hanumant Mandale: Yeah.

Mr Aniruddha Karve: OK. like I was saying, you know, a company like is Toyota use the Crucible very carefully. They have good foundry practice and there we could. We could see depending on the application, accountable lasting anywhere between six months to even up to 12 months, OK. And we can typically in a customer like that we can price the value proposition. So if it's obviously going to give them longer operating cycles then we will price for that because any time you have to change the Crucible you have about three to four hours of downtime and the bonus has to be shut down.

Everything else should be removed, the Crucible removed and put a new one in there. And then on the other side, you have questions metal people like the your Jewellers who will use the Crucible only once they won't reuse it. Because when they melt the ball, they put a lot of chemicals in it and they attack the Crucible and you know it can't be reused. So you got anywhere between single use application for things like precious metals to one year long in automotive aluminium casting. So it really varies about what you're melting and how the customer uses it also.

Ms Saloni: The other places for automotive using must be around a year or two.

Mr Aniruddha Karve: No, it is the extreme end. I would say more like a 6 to 9 month like and wherever melting is done, in the Crucible with the chemicals that are added, obviously the life comes down because the chemicals attack the wall. So there you would see one month, two months of cycles, you know 400. So whenever they're melting, they'll measure the life in charges, not time. So how many, batches of metal can they melt in that principle? And we'll typically see 400 batches, which might take one or two months to do.

Ms Saloni: One of the ER, this was mentioned that the company has around 42% market share in that case. So just to understand on the industry side, if you think. So what would you say is presenting other players to start making their own? Because from general observation, the industry seems quite unorganized. So just to help us understand, is this the capital intensity part, is this a complexity? Is this the kind of application specific to automotive that prevents a lot of players that uses in the?

Mr Aniruddha Karve: No, I mean the real trick in this business is the material formulation. Right. Because the rest what we call the recipe and to formulate these things like, if you look at our range of crucibles.

They more or less use the same inputs, it's just how you proportion them to get the properties you want. That makes a difference. The other thing is the coatings and the Glazers that we put on top the protect the Crucible. Those are big differentiators, so our IP is more of a trade secret kind of IP, so it's formulation and so on that is what you need to succeed in the business. Is it horribly capital intensive? No, I mean I mean much more I mean like our forging or stamping plant.

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A lot more capital intensive than our business, so it's not hugely capital intensive. The barrier to entry are two things in my opinion, not having the right formulations which will take years to do to really fine tune I mean we have local competitors that make Crucible. So because of our strong distribution network we were able to reach at the market in almost every segment and customer. So we have a lot of local competitor in India who make one product line. While we make multiple. And others don't have not enough investment in R&D. So we're the only one that report aside, we would like to put aside percent of our sales and you know, keep refreshing formulations.

So people get people in copy of formulation that are snapshot. They can take. One of my employees for leave and sort of start his own company making that. But we keep constantly changing, right. And therefore as long as we can do that, we can control, maybe we're still gonna lose a bit of it, but the price sensitive customers are our biggest problem, right? So when somebody comes along and offers close enough Crucible at 20% discount, then yes, but then the other thing we find is Technical Support is lacking, right? So Crucible can fail. It's a ceramic product if you misuse it, it fails and we have that reach to the market in terms of our distributor partners, their technical staff, our technical staff and therefore we can address, help our customers address those technical issues much better than any competitor can. The other global competitor which operates under different brand also in other line of business whereas we try to focus mainly on our product portfolio, customer services and branding though we have a lot of local competitors, we have competitors in China, we have competitors in India, we have competitors in Brazil. And I think the key there is again reached to market and formulation.

Ms Saloni: In India the competitor are the largest or second largest in terms of market share.

Mr Aniruddha Karve: So depends on which data you look at, what at what point of time. We are certainly number one in most cases, OK, there might be months where for SQL might get a big order and they might outsell us, but I think over the long run based on everything we see, we are the market leader. And there are certain segments that we prefer to play in. Obviously, the more technical organized segments, the unorganized segment need Crucible and there are parts that don't over ones or weeks or do that. But the margins there aren't that great. So eventually as we see the global outlook change, we may choose to exit some non best profitable segments in the Indian market and therefore you might see a number sort of go up and down, but everything will be done with the global view and to make sure we maximize profitability and ability to reinvest in the business as well.

Ms Saloni: So, Sir, can you really say that, your revenue sort of is linked entirely to how the auto cycle in general performs?

Mr Aniruddha Karve: I mean, if you look at the breakdown the business, you would come to that conclusion, right? So certainly you leave aside 2020-21 because that was just a it was an aberration from all aspects of the business. But what we typically see, yes, we have exposure to auto, no doubt right around the world. We have exposed but typically what we find is we have enough exposure to the precious metal, spare of things. So normally what happens is you know, autos tend to grow up in a recession and there's a slowdown, there's sectionally outlook.

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That is about the exactly the same time when the gold price typically tends to rise because you know the money moves from the investing in stocks and bonds to go into more to gold or other stable asset and then therefore exploration and refining activity rises as well with gold. So typically and it's not a one for one, but typically we can if there's a massive slowdown auto we can offset most of it with precious metal sales going on now. Auto is one of the things that I found over the last couple of years that our sales in the aluminium segment are not very well correlated to the number of vehicles being produced and the other they are the factor that's driving that disconnect is the fact that the aluminium content per vehicle is also keeps increasing. So even if you produce less cars in total, the amount of aluminium process for those tasks still keeps going up. So we still see a little bit of buoyancy from that.

Ms Saloni: Over the past couple of years if you see growth was single or double digit growth however all of the sudden in the last two years the growth is sort of quoted. So anything specific driving any, any specific reason for that, any specific statement from the industry and that is driving that change in the base of sales that happen?

Mr Aniruddha Karve: There's a couple things that we made a pretty significant investment back in 2017, 2018, & 2019. So if you go back to history, we amalgamated and simplified the structure. We actually have two sites in India, so the Diamond Crucible site is Mehasana Gujarat and they have this one and about so starting 2017, we embark on a sort of plan to simplify structure, make it combine the two factories so we can utilize our capacity more effectively, we can offer.

As we went through that process we found our ability to service some higher margin markets, some more attractive markets go up at the same time right. The work we did around simple restructuring, simplifying, consolidating capacity and bringing all the focus into our roundabout and saying OK how do we maximize the assets now we don't know assets now.

And the other thing is also, we'll be constantly keep looking at, segments around the world for us in Aurangabad is not just to serve as the Indian market. It's a service to MMS Market globally so we did pick up quite a bit of business in the precious metal space in other part of the world over the last couple of years that has come in which is that brought us fairly decent margins because we're looking to increase our presence in some of other global area as well. There's a bit of that going on. So we're looking at the markets and saying well, what can we.

Ms Saloni: Talking about the same thing, which is that the capex spent is around Rs 40 to 50 crores in the last 3-4 years. But if I look at the gross block of fixed asset only around Rs. 20 or 25 crores has capitalised. The rest is still in capital working for this. So might I ask what is stuck in the twig?

Mr Aniruddha Karve: Yeah, I think it's just mostly the peripheral work so the operation CapEx has been spent and we are utilizing that. There was a lot of work that we had to do on the outside to get compliant with things with the new gas storage regulation, safety regulation, we had to put in additional backup capacity for diesel generator, for our LT substation, these kind of infrastructure, things that actually got delayed due to COVID. So in theory, we should have spent all of that by the end of 2020, but because of regulatory restriction, we couldn't get some of the certifying agencies on site, so we can't fully capitalize it until they give us the completion certificate or their request to operate. A lot of the capital work in progress that you see is just delayed projects on the infrastructure side that need to get done.

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And I think we are mostly all the way through you know waiting a couple of completion certificates something that but that CapEx should be wrapped up in a year.

Ms Saloni: What was the existing capacity and after shifting your old plant to Aurangabad and its utilisation?

Mr Aniruddha Karve: The consolidation was aimed at a couple of areas. One was, reducing the overhead burden because we essentially running two plants and making the revenue of one. We wanted to get some of that inefficiency out. The overhead burdens of it slimmer on the business, the capacity combined capacity is now about 20%, roughly higher than if you look at the individual total of the two factories. And that's driven really by being able to utilize common processes.

We are currently running at about 70% capacity. We have some local bottlenecks that we need to break because obviously we run multiple processors in the factory and then some of them might get constrained. But overall capacity utilization is around 70%, which means we have room to grow.

We could get to the certain revenue level how can we break some of the local bottlenecks and enable us to fully maximize that capacity we have? And secondly, what the global market outlook is, because we see a lot of headwind in the global market.

In the long run, I think we are still OK. I I'm not concerned about the long term viability of the what we could see a bit of a choppy ride in the next few quarters, but that's mostly market driven.

Ms Saloni: You're running at 70% capacity. What is the optimum utilization for you after 20% increment after the shifting. Which CapEx part is yet to come. So post that how much improvement can be assumed or not or capacity and they?

Mr Aniruddha Karve: The operational CapEx is already done, there were the some of the CapEx is left if more infrastructure and getting some other safety standard upgraded and so on. So I'd say the majority of that 20% is already realized now that we have some local.

Now what we have seen is like a first, local bottlenecks somewhere within the processes that we have constraint. We can't scale up based on the demand profile of the market so we're working on those. Now we have to look at the post pandemic market scenario and what we want to supply out of India. We anticipating small expansion CapEx for operational improvement as we're finding is the overall capacity is fine. We are just constrained on certain product lines because they all flow through the plant differently and we may have to put in some money to enhance those specific outputs which will give us overall maybe not as much capacity because you take one from the other in a sense on shared process. But it will allow us to meet to align our capacity to more the market demand based on what the product lines can make so.

Ms Saloni: What is percentage of crucible with other foundry products?

Mr Aniruddha Karve: The Crucible is our basic revenue and like I said, if you look at today's revenue profile, about majority of our revenue is coming from Crucible and remaining from the others what we call foundry products. We look forward more for growth profile and it's tied to the overall metals market and you'll probably grow at industry CAGR GDP as well 3.5% percentage globally, India's faster.

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But you know globally we've seen some of that going but foundry products what we find is while some of them are not scalable in the sense that you're never going to need millions of these things, there are certain ones which like I said feed the non casting market in aluminium so like extrusion, the foil, the sheet metal, that sort of market we're looking at and we have earmarked that for a faster growth. Now clearly that starting from a very small group base. So even if you get major growth in those things, you're not going to see a material impact on revenue, not at least for the next two or three years. But that is sort of our if you want to call it a diversification plan away from Crucible. So we know our material can provide the technology solutions in that space.

Ms Saloni: Reason behind low margin in the past in 2019-20?

Mr Aniruddha Karve: Mr Hanumant Mandale CFO will address this question.

Mr Hanumant Mandale: Yeah, definitely. I think I would like to definitely will provide the feedback. In fact, I would also like to do deep dive and will come back to you.

Mr Aniruddha Karve: I'm quite bullish on margins for the business. Of course, we have tremendous inflation, especially in gas and mineral based raw materials. So graphite, silicon carbide, so on. We have been, reasonably successful at passing on the inflation to our customers, reasonably successful India. They had a slow start. We always get tremendous pushback from the market when we try to raise prices here, but eventually I think we're getting that through so.

About Auto sector commentary , I think you see the government obviously pushing more EV. So you'll see some of that and that that will drive possibly a change out transformation in people, give up their old vehicles. We see obviously much quicker penetration of EV bikes than cars, but eventually when you get the charging infrastructure in place and all the conditions start to come right, I don't know if the government were coming with the benefit scheme etc. You'll see some EV penetration which drive auto sales where people give up their own vehicles which they would not have normally.

But in general, I think volume growth in the Indian auto industry from what everything we can see looks positive and the same applies for Southeast Asia. It's a huge region, there's 100 million people, a lot of them are getting out of the poverty space for overpowered line. And the middle class and so on. We look forward a lot of demand for that in different segments. In the developed markets, Germany, China, US, you might get a little bit flat. But that I think we see the auto growth in India & Africa as a lot of people are exporting cars to Africa, and Southeast Asian market. In general we think we have positive momentum and like I said, it's not just also number of cars being made, it's also how much aluminium is being used in the car.

Ms Saloni: Any impact on raw material prices due to inflationary pressure?

Mr Aniruddha Karve: From leading in leading indicator standpoint, the metal prices and minerals prices, almost all of our inputs cost has increased And then LPG is normally indexed to the Brent crude price. We follows the Brent crude price because when you look at the way our contracts are structured with BPCL HPCL, they are in indexed to sort of the input cost of raw oil and therefore that if you watch those two then, then you have a fairly good idea of how much information you might be seeing. The other thing obviously for packing purposes corrugated board like a lot of Crucible are packed in. Further, increase in packaging material and other overheads also putting pressure on the manufacturing cost.

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Ms Saloni: The last quarter we have extreme moved in the commodity. How have we managed that?

Mr Aniruddha Karve: We were a little bit late to the realization that we need to manage it. So we look at Q4, which is already public though. So I think the margins in general held fairly well because the product makes it so on and that's why I think in Q1 we'll get a little bit of a hit on margins. But as I said since the last post Diwali last year, we started looking very carefully about how the inflation profiles are hitting us and what actions we need to take to pass through these increases to the customer. So some of those will come do now. OK. So the way we've managed it for the most part as well.

Ms Saloni: What is the size of the crucible industry?

Mr Aniruddha Karve: The crucibles only I think the market size globally £200 million which is expected growing at about a 5% CAGR and foundry market where we are focusing on degassing rotor look another big market in terms of revenue.

Ms Saloni: So going forward, in terms of the growth that you mentioned, because it's a niche market and going at a steady pace, that would surely come from your new capacity, right?

Mr Aniruddha Karve: Yeah, it's a diversification of product code for you getting into new markets and then of course leveraging the capacity to take share globally. We can take share globally with the right profile of product made in India that allows us to with arbitrage of course of the labor, technology that we have here and focus in the market to get maximum benefit out of that mostly from exports.

Ms Saloni: Along with some technical questions and some numbers that I might require, I'll mail it.

Mr Aniruddha Karve: Yeah, please share the other questions on e-mail, we would be happy to answer those

Ms Saloni: Thank you so much, Sir.

Mr Rupesh Khokle: Thanks for your participation and if there are no other questions we end up this meeting with vote of thanks to Mr Aniruddha Karve Sir.
