UNIFI Capital

THE GREEN FUND

QUARTERLY REVIEW – FEBRUARY 2019

In our previous newsletters, we wrote to you about interesting trends in various sectors within the Green Fund and how such trends could lead to a positive impact on not just the environment but also on earnings growth in the times to come. In this note to you, we are sharing performance of various portfolio companies in quarter 3 of financial year 2019.

I Recycling: The various sub-segments within recycling include – lead, glass and refractory recycling.

a) Lead Recycling: The fund is invested in Exide Industries and Gravita India and both the companies have a runway of initiatives that will help them to grow earnings in the coming years.

   Gravita India is India's largest responsible recycler of lead metal. The informal recycling of lead is particularly inefficient in terms of lead losses and it causes significant environment degradation. Also, lead mining uses large amounts of energy and environmental resources. Responsible lead recycling using appropriate technologies with adequate environmental compliance is the only solution. We continue to stay invested in Gravita as lead metal is the most critical raw material in a lead acid storage battery and about 90%+ of global lead consumption is out of recycled lead. The company's revenue grew by 27% YoY and 4% QoQ in Q3FY19 due to rise in lead sales volume. However, its operating profit declined sharply due to multiple one-offs – a) high cost unhedged inventory in system, b) low lead metal recovery from battery sourced through a new customer empanelment, c) increase in mix of domestic revenue as compared to exports and d) teething issues at their new plant in Chittoor. The company has taken measures to address these issues and we expect profitability to improve in the coming quarters. Incrementally, Gravita's two new lead recycling facilities in Ghana and Tanzania are on schedule to be commissioned by April 2019. This would add 15,000 tonnes to overall capacity and contribute to volume growth in FY2020.

   The other investment in lead recycling**, Exide Industries,** manufactures batteries by sourcing close to 40 per cent of its lead and lead alloy requirements through recycled lead. The company supplies lead acid batteries to diverse segments like auto OE & aftermarket, telecom, inverter, UPS, e-rickshaw and for various industrial requirements. In Q3FY19, its revenue/profitability grew by 10%/2% YoY respectively due to growth in auto replacement market in spite of slowdown in auto OE sales. We like Exide given a) the growth in auto replacement market, b) benefit of lower lead price in coming quarters and c) the company's focus on technology up-gradation to improve market share and profitability.

b) Glass Recycling: The fund is invested in a Gujarat based container glass manufacturing company, **Haldyn Glass** which reported good performance. 50% of the raw materials used in the manufacturing of container glass is broken glass (called cullet). Glass cullet is a valuable raw material as it saves vast amounts of virgin raw material, in addition to saving a large amount of energy that is otherwise required to manufacture glass. As per experts, glass can be recycled 6-7 times. Led by volume and price increase, revenue grew by 47% YoY and 9% QoQ. As a result of positive operating leverage, profitability improved by 97% YoY. The business environment continues to be good for container glass manufacturers as visible in financial results of peers in industry and we continue to remain invested.

c) Refractory Recycling: Refractories are a consumable in the manufacturing process of iron, steel, aluminium and cement. The fund is invested in India's largest manufacturer of refractories - **Orient Refractories**. The company utilizes used refractories (from plants) in their manufacturing process which accounts to about 25-30% of their raw material mix. RHI AG (2nd largest globally) acquired 69.6% in Orient in April 2013 and recently, the parent company RHI has announced consolidation of its Indian businesses by merging its unlisted companies in India with Orient. This is a powerful step in right direction and helps in synergizing for better scale and growth. The company continues to report strong volume growth through introduction of new products which is leading to market share gains.

II Alternative Energy: This fund has exposure to **Petronet**, India's largest gas re-gassifier. Driven by both, Government policy as well as lower cost to the consumer, gas consumption in India continues to grow steadily. The company's Q3FY19 results were in line with our expectations. While their Dahej regasification terminal operated at 103% utilisation in Q3FY19, the Kochi terminal operated at 8% utilisation. The next phase of growth for the company would come once the Kochi-Mangalore pipeline has been laid which is scheduled to be commissioned by June 2019 and commencement of incremental capacity of 2.5 MT at their existing facility in Dahej, Gujarat. Both of these growth drivers are expected to contribute from H2FY2020.

The fund has exited its investment in **Indraprastra Gas**. The trigger for this portfolio transaction was Delhi government's draft policy on electric vehicles (EV). The policy clearly sets targets to move towards EV and the first introduction would happen for public transportation. Currently, buses in Delhi are fuelled through CNG and these would be moving towards EV. The draft policy also incentivises 3-wheelers and cabs who move to EV from CNG. As 75% of Indraprastra Gas' revenues come from CNG in the Delhi belt, we expect its sales volume to peak out in near future.

III Energy Efficiency & Emission Savings: The fund has an exposure to this segment with investments in (a) India's largest industrial steam turbine manufacturer - Triveni Turbine, (b) India's largest coastal shipping services provider – Shreyas Shipping & Logistics Ltd, c) India's only manufacturer of advanced carbon material for lithium-ion batteries - Himadri Speciality Chemicals and d) KPIT Technologies – provider of auto engineering solutions for electric and hybrid vehicles.

Triveni Turbine continues to retain its dominant market share in less than 30 MW industrial turbine segment. These turbines are used for non-conventional sources of generating power by either using a by-product or heat generated in the course of a manufacturing process. The company's product order booking in the domestic sector has been 40% higher in 9MFY19 as compared to the corresponding period of previous year. In the international market, their products are mainly used for the renewable segments such as waste-to-energy and sugar co-generation and the order intake continues to remain healthy. As a measure to hedge the company's performance against business cycles, it is increasing its exposure in aftermarket segment, which now forms 27% of overall sales in 9mfy19. The company's Q3FY19 profitability grew by 19% due higher steam turbine sales both in domestic and export market and growth in aftermarket segment.

The fund's investment **in Shreyas Shipping and Logistics** continue to benefit from government's push for movement of goods through waterways. It is being observed that the shift of cargo from road and rail to costal waterways is happening. The average growth rate of cargo moved through coastal waterways was only 1.4% between 2009-10 and 2013-14. This has increased to 14.2% during 2014-15 and 2017-18 period. There was a decline in recent financial performance of company due to rise in bunker fuel cost. However, fuel cost have started declining and as a % of revenue have fallen by 1.7% in Q3FY19 as compared to Q2FY19. We expect profitability to improve further in the coming quarter due to further decline in fuel cost. The company reported healthy top line/operating profit growth of 1%/20% QoQ respectively.

The fund recently took exposure to **Himadri Speciality Chemical Ltd's** as its business model is well integrated across all its product segments, not just enabling good environmental practices, but furthering its margin proposition. Over the next 12 months, the company is entering an integral part of the green value chain, via supply of advanced carbon materials which is a key raw material in manufacturing "anode" that is used for Lithium Ion Batteries. Consumption of Lithium Ion Batteries are growing at the rate of > 20% CAGR world over and the current supply chain is a tightly controlled one, on grounds of technology as well as capability. As one of few producers of anode material through the coal tar route, Himadri is expected to benefit from the exponentially rising demand.

The company has delivered well on all operating parameters in Q3FY19. It reported growth in profitability by 20% YoY and 14% QoQ.

KPIT Technologies is another recent addition to the fund and it is a play on automotive embedded electronics space. This segment focuses mainly on CASE – Connected, autonomous, sharing and electric vehicles. There is an increased thrust on CASE not just due aesthetics but also due to various emission regulations. Embedded system is also an important part of power train of an electric or hybrid vehicle. Currently 40% of company's revenue come from auto embedded products. The company also had exposure to IT services business which got demerged recently. The fund exited its exposure in IT services business.

IV Water Infrastructure: The sub-segments within water infrastructure include – Ductile Iron Pipes and Micro Irrigation.

a) <u>Ductile Iron Pipes:</u> The fund is invested in two of India's largest Ductile Iron (DI) pipe manufacturers– **Tata Metaliks** and **Srikalahasti Pipes**. The demand for DI pipes continues to be robust and this industry is growing at rate of 12% p.a. Both our investments reported strong volume growth in DI pipe sales. The prices of key raw material for these companies – cooking coal and iron have been soft recently and we expect the benefit of this lower cost should reflect in coming quarters.

b) <u>Micro Irrigation:</u> The fund is invested in a Mahindra group company – **EPC Industrie**, which supplies micro irrigation products. EPC Industries

reported strong Q3FY19 performance with profitability growth of 50% YoY. We continue to remain positive on the micro irrigation sector as the penetration level in India is just 5%, thus offering huge scope for growth. EPC Industrie is also looking to set up a plant in Coimbatore to reduce logistics cost and cater to southern market.

V **Safe Chemicals:** This segment includes exposure to Sudarshan Chemicals, which is a manufacturer of organic pigments. The fund is also invested in Galaxy surfactants, which is a manufacturer of oleo chemical-based surfactants.

Sudarshan Chemical's recent financial performance was impacted due to raw material cost inflation and investments made towards new growth drivers. These investments include hiring of senior marketing professionals and towards new product launches in the high performance organic pigment segment. This is a temporary transition phase which the company is passing through and we expect revival in coming quarters as most of these investments have already been completed.

Galaxy Surfactant which is a manufacturer of oleo chemical-based surfactants reported a higher revenue mix from speciality business as compared to its core performance surfactant business in Q3FY19. The company is focusing on new markets to compensate for the loss of volume in its sales to Egypt. Ten new target countries (mostly Africa) and 25 new clients have been acquired in the last 9 months. India business is doing well with 13% volume growth with the home and personal care segment doing very well. Over the mid to long term, as urbanisation and premiumisation play out in developing countries like India, the specialty component will gradually increase and lead to margin expansion. In the short term, the mass market performance segment will continue to drive the revenue growth.

Financial Details of Portfolio Companies

(Rs. in Cr)	Sales		Operating Profit		PAT		Debt	Equity	D/E Ratio	ROE
Company	**Q3FY19**	**9MFY19**	**Q3FY19**	**9MFY19**	**Q3FY19**	**9MFY19**	**H1FY19**	**H1FY19**	**H1FY19**	**FY2018**
Petronet LNG Limited	10,097	30,011	847	2665	565	1717	720	10057	0.07	23%
Orient Refractories	200	561	34	94	21	65	-	330	-	30%
Sudarshan Chemical Industries Ltd	348	1,067	37	148	14	63	231	563	0.41	20%
Gravita India Ltd	305	903	10	47	1	19	237	201	1.20	25%
Triveni Turbine Ltd	211	600	36	111	23	72	-	474	-	22%
Exide Industries	2497	7,990	313	1,036	155	558	-	5784	-	19%
Shreyas Shipping and Logistics Ltd	157	465	19	52	13	24	150	264	0.57	34%
Haldyn Glass	62	165	7	18	3	9	3	141	0.02	12%
Tata Metaliks Ltd	546	1,561	75	226	40	118	210	149	0.71	57%
Srikalahasti Pipes Ltd	397	1,089	65	149	31	82	212	1196	0.18	15%
Galaxy Surfactants Ltd	680	2,081	82	258	42	134	359	815	0.44	26%
EPC Industrie Ltd	77	186	7	12	4	6	10	141	0.07	4%
Mahanagar Gas Ltd	753	2069	239	672	148	412	-	2230	-	24%
Himadri Speciality Chemical	587	1794	133	399	84	235	538	1555	0.35	17%

Note: a) Financials of KPIT technologies are not shown as company recently underwent demerger. b) For Sudarshan Chemicals, Haldyn Glass, Exide and Shreyas Shipping and Logistics – standalone figures are shown.