

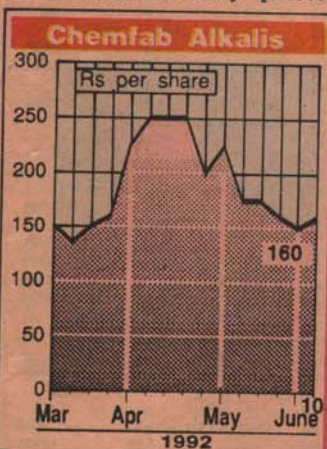
Chemfab: where have all profits gone

Hemindra Hazari

CHEMFAB Alkalis mainly manufactures caustic soda, which accounts for 76 per cent of its sales. The company's other products; chlorine, hydrochloric acid, sodium hypochloride and hydrogen are related to the manufacture of caustic soda.

It was the first company in India to introduce the power saving ion exchange membrane cell technology.

In the Indian caustic soda industry 79 per cent use the conventional mercury process



while only 10 per cent use membrane cell technology and the remaining 11 per cent uses diaphragm technology. The caustic soda industry is currently performing well as supply is falling short of demand.

The Chairman's statement and the Director's Report in the company's 1991-92 annual report are littered with contradictions. The Chairman, states, "there has been a lower production due to fluctuation in power supply," while according to the Director's Report, "during the year under review the production of caustic soda lye was higher at 14,026 tonnes." The production schedule for 1991-92 reveals a 2 per cent increase in capacity utilisation to 85 per cent which is low for the industry. In the power and fuel consumption detail reveals only a 0.2 per cent decline in electricity units purchased in 1991-92 compared to 1990-91. "Fluctuation in power" would have resulted in a more drastic

decline. In the Director's Report for 1991-92 foreign exchange earning are stated at Rs. 1.85 crores while in the schedule to accounts it is Rs. 1.31 crores. No explanation is provided for these discrepancies and the auditors have chosen not to comment on it. The auditors lack of observation is glaring as the Director's Report is an integral part of the annual report to shareholders which is duly certified by the auditors.

For 1991-92, although turnover increased by 30 per cent, profit after tax declined by 36 per cent. Caustic soda turnover in 1991-92 increased by 21 per cent over 1990-91. The increase was

The increase in transport also appears unnatural considering total volumes sold only increased by 4 per cent and combined with fuel hikes does not justify a 119 per cent increase in transport and handling. The quantum of salt which is the main raw material increased by 33 per cent while the cost price per tonne of salt marginally increased by 2 per cent. In 1990-91, 1 tonne of salt produced 1.26 tonnes of output while in 1991-92, 1 tonne of salt produced only 0.98 tonnes of output. The profligate wastage of the major raw material appears to be another anomaly considering that the plant uses the sophisticated

per cent in 1990-91 to 15 per cent in 1991-92. Management has failed to effectively utilise the ploughback.

The management has further inflated the profit by capitalising Rs.69 lakhs on scientific research and adding it to plant and machinery. The company also follows a liberal costing policy by including depreciation in the value of the finished goods, thus further inflating profits.

In 1991-92 the company exported Rs. 1.85 crores worth of caustic soda and appeared content in contributing its share "of earning precious foreign exchange." However what is not mentioned is that in 1991-92 the company had a "precious" foreign exchange outflow of Rs 2.99 crores, netting remittance of Rs. 1.14 crores.

Power is a major cost in the caustic soda industry. It is noteworthy that although the electricity tariff increased by 20 per cent from Rs. 0.83 in 1990-91 to Rs.1.00, the company's power to sales declined from 24 per cent in 1990-91 to 21 per cent in 1991-92. Electricity consumption per tonne of electro chemical production declined by 2.3 per cent from 2,610 KWH in 1990-91 to 2,550 KWH in 1991-92.

In a capital intensive industry the company with a capacity of 16,425 tonnes per annum (tpa) has a small equity base in 1990-91 and 1990-92 on only Rs.2.94 crores and the lowest debt to equity at 0.8:1. In 1990-91, Sree Rayalseema with a capacity of 31,416 tpa had an equity of Rs.7.74 crores and a debt to equity to 3.6:1, Punjab Alkalies with a capacity of 37,059 tpa had an equity of Rs.10.12 crores and a debt to equity of 1.3:1 and Modi Alkalies having a capacity of 51,560 tpa had an equity of Rs. 17.91 crores and a debt to equity of 2.1:1. Chemfab Alkalis can therefore easily finance an expansion through debt and equity.

The caustic soda industry performed well in 1991-92 as caustic soda prices increased considerably and there is no reason why sophisticated units like Chemfab Alkalis which has a small equity base, a favourable debt to equity ratio and low power costs should declare such lacklustre results. □

FINANCIAL HIGHLIGHTS

	31-3-92	31-3-91	% Change
Sales	20.80	15.89	30.90
Other income	0.32	0.36	-11.11
Operating profit	5.00	4.87	2.67
Interest	0.67	0.64	4.69
Depreciation	2.60	1.86	39.78
Taxation	0.38	0.25	52.00
Net profit	1.35	2.12	-36.32
Equity capital	2.94	2.94	—
Reserves	6.05	4.31	40.37
Total capital employed	16.18	13.06	23.89
Dividend (%)	25.00	20.00	—
Earning per share (Rs)	4.59	7.21	—

mainly due to a 14 per cent rise in sales realisation to Rs. 8,600 per tonne, while quantity sold increased by a modest 7 per cent which was made possible by a high opening inventory from last year.

Profit margins in 1991-92 came under pressure mainly due to increase in overheads. Overheads to sales increased from 26 per cent in 1990-91 to 33 per cent in 1991-92. The cost increase is not due to operations but more due to accounting. Stores and spare parts increased by 124 per cent, transport and handling charges by 119 per cent, miscellaneous expenses by 77 per cent, repairs and maintenance of machinery by 40 per cent and raw materials by 35 per cent.

The increase in maintenance and spare parts in abnormal considering the modernity of the plant and there is no report of the plant being overhauled or having suffered a mishap.

membrane technology and the company did not experience any major power shortfall compared to 1990-91. The unjustified increase in costs which has no operational causes reflects poorly on the management.

In order to cover up the increase in overheads the management has changed the method of depreciation in 1991-92 and therefore have inflated profit after tax by Rs.42 lakhs. Adjusted depreciation therefore increased by 40 per cent.

On the reduced and adjusted profit after tax of Rs.1.35 crores the company increased the dividend by 5 per cent to 25 per cent. Payout therefore nearly doubled from 28 per cent in 1990-91 to 54 per cent in 1991-92. Although dividend has nominally increased, as a percentage of net worth it has remained constant at 8.1. From the shareholders perspective, growth has reduced sharply as return on net worth declined from 29.2