



“Escorts Limited Q2 FY'17 Earnings Conference Call”

October 27, 2016



MANAGEMENT: **MR. RAVI MENON – CEO, ESCORTS AGRI MACHINERY**
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MR. DIPANKAR GHOSH – CEO RAILWAY PRODUCTS DIVISION & ESCORTS AUTO PRODUCTS
MR. BHARAT MADAN – CFO, ESCORTS LIMITED
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MODERATOR: **MR. DEEPAK JAIN – IDFC SECURITIES LIMITED**



Escorts Limited
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Moderator: Ladies and Gentlemen, Good Day and Welcome to Escorts Limited Q2 FY17 Earnings Conference Call hosted by IDFC Securities Limited. As a remainder, all participant lines will be in the listen-only mode, and there will be an opportunity for you to ask questions after the presentation concludes. If 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. Deepak Jain from IDFC Securities Limited. Thank you and over to you, Mr. Jain.

Deepak Jain: Thank you, Aman. Good evening. On behalf of IDFC Securities, I welcome to the Escorts Limited Q2 FY17 Result Conference Call. I also take this opportunity to welcome the management team from the Escorts Limited. Today we have with us Mr. Ravi Menon – CEO - Escorts Agri Machinery; Mr. Ajay Mandahr – CEO, Escorts Construction Equipment; Mr. Dipankar Ghosh – CEO Railway Equipment Division & Escorts Auto Products; Mr. Bharat Madan – Chief Financial Officer; Ms. Jyoti Khatuka – Head (Treasury) along with the Investor Relations Team at Escorts.

We would start the call with a brief opening comment from the management followed by a Q&A session. Before we start, I would like to add that some of the statements that the management makes in today's discussion will be forward looking in nature. At this point, I would request Mr. Madan to make his opening remarks. Over to you, sir.

Bharat Madan: Thank you, Deepak. Ladies and Gentlemen, a very good evening to you all. Thank you for joining us on the second quarter earnings call for financial year 2017. A snapshot of Company's quarterly performance is as follows:

Turnover at Rs. 995.3 crores against Rs. 818 crores last year, up by 21.7%, led by volume growth in both Tractor and Construction Equipment businesses. Tractor volumes were up by 35.4% to 15,482 tractors as against 11,438 tractors last year same quarter. Construction Equipment volumes up by 18.3% to 724 machines, against 612 machines last year same quarter.

EBITDA at Rs. 62.5 crores against Rs. 26 crores last year, up by 140%. EBITDA margin now stands at 6.3% versus 3.2% last year same quarter ended September 15th. The major reason for increase in EBITDA margin is 105 basis points reduction in the material cost from 69.1% to 68.06%.

Finance cost went down by Rs. 1.6 crores to Rs. 9.6 crores as compared to quarter-ended June 2016. The total debt outstanding as of September 2016 is Rs. 252 crores, down from Rs. 360 crores in March 2016 because of reduced working capital during the season. PBT before exceptional item stands at Rs 43.7 crores, up by 296% against Rs. 11.03 crores last year same quarter. There is an exceptional item of approximately Rs. 3.9 crores in the quarter on account of VRS of 25 employees.

The Company reported a PAT of Rs. 31.3 crores versus 9.8 crores last year, up by 219.7%. PAT margin now stands at 3.14% versus 1.2% last year in quarter ended September 2015. EPS is reported at Rs. 2.62 against Rs. 0.82 last year same quarter.

Now, moving on to segmental business performance:

Starting with the Agri Machinery business, domestic tractor industry volumes grew by 27.5% to 1.35 lakh tractors as compared to 1.06 lakh tractors last year same quarter. Our domestic volumes went up by 35.3% at 15,284 numbers against last year 11,293 in quarter ended September. Industry in our stronger market North and Central grew by 16.5% whereas industry grew by 46% in the opportunity markets of South and West.

Our domestic market share stands at 11.3% in quarter ended September 2016 against 10.6% last year same quarter. We had gained market share across 9 states out of 12 states. EBIT margin in EAM stands at 9.4%, up by 247 basis points against 6.9% last year, primarily due to material cost reduction initiative and higher volumes. This quarter we also have one-time expenses on consulting cost on completion of the material cost reduction Project “Shikar” which is non-recurring item.

The market response for the newly introduced modules in the Powertrac and Farmtrac brand has been positive and encouraging. And our market share increased from 10.4% to 11.4% in 41 HP to 50 HP categories in first half of this year. We expect domestic tractor industry to grow by 14% - 15% in current fiscal. We will grow in line with the industry.

Coming to the Construction Equipment business:

Industry grew by 27% in Q2 FY17 with respect to last year corresponding quarter. All major segments like Earth Moving, Material Handling, and Road Construction have seen a positive movement. Our Served industry which is Backhoe Loaders, Pick ‘n’ Carry Cranes and Compactors went up by 3.1% in quarter two. Backhoe Loaders have been the biggest gainer in quarter two with growth of 36% followed by Cranes that grew by 22% and Compactors grew by 7.2% in quarter two.

Our total volumes of manufactured and traded products went up by 18.3% to 724 machines in quarter ended September 2016, against 612 machines in last year same quarter. In Pick ‘n’ Carry our volumes have grown by 7%, mainly led by low end hydra range. A positive swing of 121 basis points on quarter-on-quarter is seen in EBIT margin in Q2. We have introduced a new Brute Power Jungli 4x4 Backhoe loader with our own Escort engine making it more fuel efficient with respect to peers. Going forward, we expect that construction equipment industry will continue to grow at 15% to 20% CAGR growth for next two to three years and we will be launching new innovative products variance to cater to the growth.

Now, coming to the Railway division:

Revenues at Rs. 60.1 crores quarter ended September 2016 flat versus that of last year same quarter. EBIT margins is at 12.8%. This quarter margins are affected primarily due to adverse product mix. Order book for this division stands at approximately Rs. 110 crores, which will get excited in the next six to seven months.

Bogie Mounted Brake System called BMBS fitment order of 115 quantities is executed in first half of this fiscal, and for Axel Mounted Disk Brakes first trial order from two sets has been completed 18 months field trial and other trial for complete range are expected to start soon.

Lastly, on the Auto division we have divested OEM and export business of Auto Product division to Badve Engineering Limited Pune as a part of planned strategy reorientation of the business. Currently we are in transition phase and transition will be completed in Q3 this year.

Now, I request the moderator to open the floor for Q&A session, please.

Moderator: Thank you very much. Ladies and Gentlemen, we will now begin with the question-and-answer session. We have the first question from the line of Rakesh Jhunjhunwala from Rare Enterprises. Please go ahead.

Rakesh Jhunjhunwala: Sir, one question I had is, how much was fixed that is one-time payment that you have made?

Bharat Madan: See, the impact in this quarter will be about Rs. 6 crores.

Rakesh Jhunjhunwala: That is a non-recurring item?

Bharat Madan: That is a non-recurring item. So, if you look at the margin in the tractor business, there is a decline of about 2% sequentially. One of the major reason obviously is in the volumes, there is a bit of seasonality in Q2 normally the volumes are low, so it is about 900 tractors lower than compared to the first quarter. Also, in addition the spare parts sale which has gone down by almost Rs. 22 crores, so I think about Rs. 17 crores all you got is volume decline in Q2 compared to Q1 and this one-off cost of consulting. So these two put together we got about 2% decline in the margin on tractor business.

Rakesh Jhunjhunwala: What is the Rs. 17 crores you said?

Bharat Madan: Rs. 17 crores on account of volume drop in Q1.

Rakesh Jhunjhunwala: How is October fairing for the industry?

Ravi Menon: The October scenario from the market is looking very positive. And the industry as a whole expects fairly strong closure of the month in the range of some 80,000 plus units for the industry as a whole.

- Rakesh Jhunjhunwala:** And what was it last year?
- Ravi Menon:** Last year would have been around 14% lower than that, 14% to 15% lower.
- Rakesh Jhunjhunwala:** And do we expect the gain in market share?
- Ravi Menon:** It is very early to say that because what happens is there are some auspicious days and as the month closes there are some suppliers who push tractors into the market. But given what we know today, I think we will probably gain marginally.
- Rakesh Jhunjhunwala:** Second question I had is in the heavy machinery division, I mean the volumes have gone up but the losses have not been reduced, so any comment on margins and when can we expect a breakeven?
- Bharat Madan:** In the construction you are saying?
- Rakesh Jhunjhunwala:** Yes.
- Bharat Madan:** Construction, I did mention in the last concall also that breakeven levels at the current mix is about 300 to 325 machines in this business. Last quarter we did about average 240 machines a month and in fact in H2 we will be able to get to that number, so the volumes are looking up. And normally H2 is stronger season months for the construction equipment industry. So we are expecting it will be doing 300 plus average in the second half, so we should be looking at about a breakeven level that is being there for construction business in the second half.
- Rakesh Jhunjhunwala:** And you have introduced some new products there, some new differentiated products, how are they fairing? Have we introduced some new differentiated products?
- Ajay Mandahr:** Yes, we have introduced. We have introduced the new Backhoe with indigenous engine coming from Escorts, test monitoring has been done for those 25 units and it's probably very good and we expect the momentum to come from that product.
- Rakesh Jhunjhunwala:** So we will only make money next year? So we will make money next year hopefully?
- Ajay Mandahr:** Yes, sure.
- Rakesh Jhunjhunwala:** And in your Railway Division, what is the prospectus there?
- Dipankar Ghosh:** Railway Division, actually what has happened a few of coupler and big tenders were not decided in Q2, so we had a flattish quarter? We expect that Q3 and Q4 would be far better than what we have now in the Q2. And our new products, we have got some major orders for the new product which is BMBS; we have just started pushing them into the market. And similarly

your Axel Mounted Disk Break also now we have got orders which we are now actually pushing to the railways. So we hope to see a good traction out there.

Moderator: Thank you. We have the next question from the line of Raghunandan from Quant Capital. Please go ahead.

Raghunandan: Given the strong sales in the first half, we have seen a 22% growth, is there a case for increasing outlook for the full year towards 20% from the earlier 12% to 15%?

Bharat Madan: So, like we mentioned, so quarter two normally, see in this case October was very high retail month we started right from day one, so a lot of inventory build-up actually happened in Q2 since a lot of push was there from the manufactures to the dealers, so the inventory build-up was high. So that is why the 22% sort of growth rate is not a sustainable number on a full year basis, so that correction I think will happen in Q3. So we will be having a more sustained number, we still feel we are somewhere around 14% - 15% sort of growth on a full year basis for tractor industry.

Raghunandan: Realizations are lower QoQ for tractors, is it due to higher share of Powertrac series, can you share the mix? And also, can you throw some light on new products to be launched?

Bharat Madan: So, mix this time has been slightly negative. So like I said the Powertrac has actually gone up and Farmtrac has slightly gone down with a swing of about 6 basis points between the two compared to corresponding quarters last year. So, this time it is about 62% - 38% mix on the Powertrac and Farmtrac.

Raghunandan: And anything on the new products in the tractor side?

Ravi Menon: I think we do not have any major new product coming in, but I expect that we will have one haulage tractor which we will launch in probably two months from now. And there is another good initiative which we are taking on the Farmtrac side, but I think we would probably give you a slightly better detailed explanation in the next call.

Raghunandan: And the haulage tractor will be under the ALT series, sir?

Ravi Menon: It will be a part of ALT series at higher HP point.

Raghunandan: And my net query was to Ajay sir, what would be the areas of focus going ahead?

Ajay Mandahr: Yes, going ahead the area to focus will be basically big cranes and backhoe that we talk about, the Jungli that we have launched and exports, this is basically a function of realization, for realization we have to change in markets.

Raghunandan: Realizations are lower quarter-on-quarter which means that there were a higher proportion of lower tonnage cranes, does this lead to an increase in breakeven volumes?

Bharat Madan: Like we mentioned, so breakeven has already moved up so at the current mix the breakeven level today is about 300 to 325 machines. So that breakeven is the result of big changes that have happened, so we are selling more of high end cranes and lower cranes where the margins are pretty low compared to what we were selling earlier which was higher build of same cranes. So like Ajay mentioned, the focus going forward will be more to sell more high contribution products which is more on the cranes and focus more on the export markets where the margins are better.

Raghunandan: Auto products division, sir, had losses of close to Rs. 6 crores, can you elaborate a little on the losses because they seem to be higher.

Bharat Madan: So, one of the key reasons there is the drop in the sales. If you look at the turnover has almost gone 50%. Now what are the reasons behind the since we are in a transition phase to the new buyer, so all our customers' orders are getting transferred to the new buyers, so as a result there is a less order execution that is happening at our end. So we expect to complete this entire transition within this Q3, hopefully in November we will be able to consummate this transition. So then the reporting of this numbers on bought out product after Q3 will most probably stop. So this is one of the key reason why the top-line has gone down and the loss exactly gone up temporarily.

Raghunandan: And the impact of inventory write-off has it come in this quarter or is it likely in the second half?

Bharat Madan: No, it will be in the second half only. So when the transition gets completed only then we can do that thing, so it will happen in Q3 most probably.

Raghunandan: And sir I missed the number on the growth and opportunity and the weak markets, I mean basically weak markets and strong market, can you share that number again?

Bharat Madan: Yes, so in the quarter we mentioned the strong market has grown by 16.5% growth in the strong market in the quarter and 46% growth in the weak market of south and west.

Moderator: Thank you. We have the next question from the line of Chintan Modi from Motilal Oswal. Please go ahead.

Chintan Modi: Sir, as we can see that the south and west region has grown by almost 46%, so incrementally it is becoming very critical for us to have a good amount of presence over there. Can you share like the step that we have taken, how things have moved in first half compared to the base first half?

Ravi Menon: So let me give you some specific examples so that it clears the issues. So, we are looking at markets of Maharashtra, Gujarat and then the South. So if you look at specific markets, let's start with AP which is one of the markets where we have not been very strong. So if you include the number in September, our share in that particular month has gone up to almost 8%. Now in the quarter we are closer or lower than that but we are close to about 6% in the quarter. One state which we have to do some good work is Karnataka where we are low in sales, but across these regions, Maharashtra, Andhra and Karnataka we are adding dealers. So, for example in Andhra Pradesh we have added around four very strong dealers, both including AP and Telangana. In Maharashtra where we are weak in the Western Maharashtra regions we have already had three dealers, which are also going to fetch us some good returns. Some good work we have done in the northern part of Karnataka where we have added I think one or two dealers who are reasonably strong. And then in the state of Gujarat where we were weak in the Southern Gujarat markets, that is also an area where we have strengthened the addition of dealers. So that is something as a whole I suppose answers your question.

Chintan Modi: And in terms of products anything specific that is moving in the region for us?

Ravi Menon: So what we have done is we have got one flagship product called Euro 50 which is moving very well in not only these markets but all across India. And then there is another product from the FP stable which is called the FT Smart which is also doing very well to be very specific on the products.

Chintan Modi: And secondly, we were also planning to separate the dealership for FT and PT in the northern part of the regions, so there also if you can share how things have shaped up in this first half compared to last year?

Ravi Menon: Okay. So we have done this activity almost in the entire part of the northern region, barring one state where we have to yet do that. But other than that most of Northern India is now in a separate channel situation.

Chintan Modi: Sorry, I did not get that.

Ravi Menon: So I will just repeat what I said. In the northern part of India, barring one state, we have now created separate channels for the two products lines that we have. And we are working in that one part of that state to reconstruct the channel network.

Chintan Modi: And I missed your outlook for second half in the tractors business, if you can just share that.

Ravi Menon: Are you talking of industry or are you talking of the company?

Chintan Modi: The company level.

Ravi Menon: It is very difficult to hazard a guess because the industry is close to 300,000 tractors at the end of first half, 298,000 is the accurate number. Typically, the second half I think in my mind would be slightly lower, we might end up the year with around, maybe to hazard a guess, somewhere around 570,000 units, or a little bit more than that maybe. So, if you put share of ours, we are running for a share of maybe between, maybe if you say 11% then I think you have the mathematics.

Chintan Modi: And is it typically that in the second half the northern markets generally picks up compared to the southern market?

Ravi Menon: We have seen it, and if you look at our product mix the way it grows, we see a surge in the FT which is stronger in the northern markets. So I think your analysis is bang on.

Chintan Modi: So that should basically convert into good numbers since we have a good amount of presence in the northern market, is that a right way to look at it?

Ravi Menon: Yes, that is right because the Punjab, Haryana markets have not been doing well so far, and so has Rajasthan. But what we are seeing is an upsurge in Rajasthan right now which is one of our strong active markets and there is a robust growth in UP which is largest tractor market in the country. So if you put all that together, I guess we should see better numbers.

Moderator: Thank you. We have the next question from the line of Mayur Malik from Anand Rathi. Please go ahead.

Mayur Malik: I just wanted to understand what is happening on the VRS side. So you mentioned that for Q1 you have retired 50 people and for Q2 you retired another 25. I thought the target for the entire year was around 500-odd. So do we believe that the third quarter and fourth quarter will typically the bulk of VRS coming?

Bharat Madan: No, so for this year there is no target of 500 numbers, this year there is a settlement due with the union so we will not do any major VRS this year. So any VRS will happen only after the settlement, that basically was for next year. So next year the employees we are targeting are for the auto product division which we had divested, so there is a blue collar which needs to be addressed so that is what we are doing. So there the number closer to 100 odd number which will happen, it is about 18-20 crores sort of cost on a full year basis because VRS will be there.

Mayur Malik: So when is this wage settlement typically due?

Bharat Madan: The negotiations are on, so hopefully by the end of this year we would be conclude on that. So when VRS will happen after that only, next year.

Mayur Malik: So typically that should come only in FY18 and FY19?

- Bharat Madan:** That is right.
- Mayur Malik:** And the second thing was, while you mentioned that because of the change in mix your average realizations seem to be lower on the tractor side, another Rs. 6 crores am I reading right, Rs. 6 crores is the consultancy fee, right?
- Bharat Madan:** That is right.
- Mayur Malik:** So those two will typically be the reasons for these lower operating margins?
- Bharat Madan:** No, so there are two. One is the volume also, compared to Q1 the margins have gone down, so in Q1 the volumes were higher. So it is not only tractor but also the related business of spare parts also the volume dropped in Q2 because it is a non-season quarter. So because of the volumes impact we said that the loss was about Rs. 17 crores in the bottom-line on the EBIT margin for tractor and Rs. 5 crores to Rs. 6 crores is the consulting cost which is the one-off cost in this quarter. So these two account for 2% margin in the tractor business this quarter.
- Mayur Malik:** And on the staff cost just one thing, typically right now whatever you convert to VRS typically goes as extraordinary, so it is not part of the regular staff cost?
- Bharat Madan:** That is right.
- Moderator:** Thank you. We have the next question from the line of Mitul Shah from Karvy Stock Broking. Please go ahead.
- Mitul Shah:** Sir, my question is pertaining to ancillary segment. By what time or by which quarter you expect revenue to be completely zero and no losses will come from that segment?
- Bharat Madan:** So it is likely to be Q3 we will complete the transition, so from Q4 you will not see these numbers getting reported on auto product division.
- Mitul Shah:** And even the balance part of the ancillary which you were earlier thinking of retaining that will also go away?
- Bharat Madan:** Yes, that is more for liquidation of inventory. So the business which is not getting transferred will gradually get liquidated. So we will try to liquidate it as far as possible, but it is not a very amount, a very small business will be there and we are merging that with the spare part division of tractor business. So there will not be separate reporting for those numbers, it will be very small in amount.
- Mitul Shah:** And sir my second question is on the railways side, out of this Rs. 110 crores order book what would be the quantum from the new product side?

- Dipankar Ghosh:** Out of this Rs. 110 crores, actually Rs. 45 crores to Rs. 50 crores would be from the new products side.
- Mitul Shah:** And what was this number a year before or how these new products are ramping up?
- Dipankar Ghosh:** The new products are shaping up well, I mean just to give you the new product, and last year the total year was around at Rs. 11R.5 crores or Rs. 12 crores, this year we are expecting around Rs. 45 crores to Rs. 50 crores.
- Mitul Shah:** And any further new launches or this would be enough to get the targeted revenue?
- Dipankar Ghosh:** We are also launching some new brake electronics also, that we will launch in Q4. And parallelly there are few more things which we had launched, but since they are in the free trail mode we are not telling about the commercial action, it will take actually six months to one year for the commercial action. But we have launched few new products also.
- Mitul Shah:** And sir my last question is on the tractor side outlook, for FY18 generally whenever it is observed that good monsoon which has an effect of one, one and a half year positive starting with the lag effect of one quarter to two quarters, so it should translate into very strong number for FY18. What is your outlook for 2018 and just if you can give some breakup or some highlight on the region wise growth prospects?
- Ravi Menon:** We can take it in two steps, we expect this year to close at somewhere 570,000 to 580,000 units and while it is very difficult to be very accurate on this, we still think that a strong double-digit growth is possible. Now, what exactly that number would be is something which I think it will be very speculative to answer. The other changes which I see are, we see the northern markets, Punjab is growing at negative 10%, Haryana is negative 2%, and Rajasthan is negative 3%. So I feel that this will get probably corrected in the next quarter. And thereon I think these markets will also see positive growth in FY18.
- Mitul Shah:** This south and western regions will continue growing like 30% - 40% kind of numbers?
- Bharat Madan:** I am not sure of that because if you look at it, AP today is 69%, Karnataka 37%, Tamil Nadu 72%. So the basic effect will definitely kick in the next year and I do not think we will be seeing those type of growth, they would probably in high double-digit growth still.
- Mitul Shah:** Okay, because those are our weak markets so our growth may not be matched with the industry if this will continue south and...
- Ravi Menon:** I think that next year we would be in a slightly different position in many of the markets, especially on the channel front. So, I guess even if we get to 30% growth we should also be taking growth close to that or higher than that actually. Because even today with this kind of growth we are gaining share.

Moderator: Thank you. We have the next question from the line of Prashant Biyani from JHP Securities. Please go ahead.

Prashant Biyani: Are we expecting any write-off in the auto ancillary division in Q3? If yes then how much could be the quantum of that?

Bharat Madan: See, there will be some write-off which will happen, but to quantify at this point of time is difficult. So till the time transaction gets completed and we know how much assets are transfer to the buyer which will be on that particular cutoff date when all approvals are in green, so only at that time probably we will be in a better position to answer, but you will see that impact coming in Q3 definitely.

Prashant Biyani: And regarding the tractor division, why are these southern markets growing so fast over the last couple of years? Is it because penetration levels are low there, because deep down some of the states I guess have not received so much of rainfall this year seeing the water reservoir levels in the southern region.

Ravi Menon: Okay, let me give you two examples to illustrate the point. Take the case of Tamil Nadu, three years ago Tamil Nadu was hardly selling around 1000 units in a year primarily because of drought and the fact that there was no electricity in the rural areas, so today that number has almost tripled. Take the case of AP, if you look at the last two or three months there has been almost a doubling of the numbers. So for example, if August - September was 2000 and 4000, October was around 4000 and it is expected to be around 8000 this month and so on and so forth. So, there was a base effect and plus the fact that the rains have come in after two continuous years of drought.

Prashant Biyani: Have we seen any, means though AP is growing but we have heard the news of large farm tracks being converted into city kind of areas. So do we expect any loss because of the conversion of land from agri to commercial or industrial?

Ravi Menon: No, it is actually the other way round. Because when you see this kind of a movement happening you also tend to see tractors getting into commercial use. So it is actually helping the growth of tractors because tractors also have a good percentage in the commercial segments. Having said that, I think the government of both Andhra and Telangana are creating a lot of these water catchment areas, so there is a lot of work which is being in that area where again tractors are being used. So at least in these two states we see a fair amount of growth happening.

Moderator: Thank you. We have the next question from the line of Chirag Shah from Edelweiss. Please go ahead.

Chirag Shah: Sir, just a question on industry pricing scenario and the cost pressures that are building up. So what kind of, first on the cost side what can we expect in terms of pressure?

- Ravi Menon:** You are talking about tractors or...?
- Chirag Shah:** Yes, I am talking about tractors.
- Ravi Menon:** The estimated increase at the end of March 2017 from our side is expected to be in the range of about Rs. 9,000 per unit.
- Chirag Shah:** Okay, so it would be around 1.5% to 2%?
- Ravi Menon:** If you take an average of about 5.2 lakhs per unit, you have the numbers.
- Chirag Shah:** So, this is from your perspective and would you be able to pass on because this should not be that difficult to pass on the cost given the demand scenario?
- Ravi Menon:** You have asked me a very difficult question, but nevertheless I think what we have done is whatever we have seen so far we have been able to do so. But going ahead we will have to look at the industry dynamics to be able to give you a very accurate answer.
- Chirag Shah:** And how have been the cost pressures in Q/H, have there been any similar cost pressures and price hikes been done or...?
- Ravi Menon:** If you look at what happened in the industry, there were price hikes which were taken in and around August.
- Chirag Shah:** And that would be how much roughly?
- Ravi Menon:** I mean, different players are doing different things, I do not think it is a right thing to comment on others.
- Chirag Shah:** So it would be around 1% or it would be substantial?
- Ravi Menon:** so I think it will be 1% or slightly lower than 1% I would say.
- Chirag Shah:** But that was not necessary because of cost pressures right, it was more of an opportunistic because of demand cycle?
- Ravi Menon:** No, there are two things. One is that if you look at the way it moved quarter-by-quarter, the first quarter saw deflation to the trend of about close to Rs. 1,300 but it picked up to around approximately Rs. 4,000, I do not know the exact number, close to Rs. 4,000 in the second quarter. So pricing was based on both and on the deflation which happened and the expected inflation...

Moderator: Thank you. We have the next question from the line of Sameer Deshpande from Fairdeal Investments. Please go ahead.

Sameer Deshpande: Regarding the tractor prices, you mentioned that there was a marginal price increase in Q2 of Rs. 3,000 - Rs. 4,000. And you mentioned that it will be increased because Rs. 8,000 to Rs. 9,000 in second half?

Ravi Menon: No, what I said was that the exit estimate at this point in time is Rs. 9,000 plus, that is an estimate. Now will that exactly happen is something which depends on many factors, so it is very difficult to hazard an accurate guess on that.

Sameer Deshpande: So it is not exact, and with cost structure do you see the raw material prices which were there in Q2, are we comfortable with that or the prices have gone up in this segment?

Bharat Madan: So, as I said the prices have got down surely, the first quarter we saw some deflation which was there in Q2, now already the inflation has reduced, especially the prices of tier have moved up significantly. Then Q2 and Q4 we expect the steel prices continue to strengthen because of MIP being introduced. So we expect that the inflation will stop, has already stopped. So what you see is the inflation is coming, so if you are talking about price increase, it is linked to the inflation. So how much we will be able to pass on, it will depend on how the competition responds and how much inflation we see on the commodity prices going forward.

Sameer Deshpande: Because we actually in the last conference call it was being mentioned that we will like to have about 11% margins on our agri business, tractor sales, that is agri business we will have a segment margin of about 11%. Now this time it has come down to 9.4%, you mentioned some reasons, it is okay. But if those reasons are not there is it likely we will revert back to about 11% in the third quarter and fourth quarter?

Bharat Madan: Yes, so one of the key reason was the volume, if volume does not take off obviously the margins would not be there. So the volume is a major driver there and second was the one-off cost, consulting cost which obviously is a non-recurring item which will not be there going forward to that extent. So yes we expect still on a full year basis we still maintain our guidance of double-digit margin for tractor business, now whether it is 11% or 10% or it is 12% we would not know, but it will be in the low double-digit margins on a full basis, looking at those numbers we foresee and we estimate as of now for the industry and for our volumes.

Sameer Deshpande: And in construction equipment, despite the rise in volumes we are not in a position to cut our EBITDA losses to zero yet.

Bharat Madan: So like we mentioned, we have got a breakeven level and at a mix of 300 to 325 machines, so last quarter we did only about 205 machines average. So we are far below our target numbers into the volume. But having said that, normally quarter two is a very weak quarter for construction equipment industry, with the rain season the construction activity more or less

does not happen. So the pickup will happen really from October onwards, we expect the numbers in H2 in construction will be in the positive range, it will be probably 300 plus average in a month and we should be able to hit the breakeven level in H2.

Sameer Deshpande: So, actually we have Mr. Ajay I think the new person joining as a CEO of that division recently, so can we know what is his view about the construction equipment business?

Ajay Mandahr: Business is good, the industry is good, and industry has shown a really good growth. It has shown the growth and our view is we can expect some 14% to 15% increase over this year in the market volumes. But the major volume growth is going to come in backhoe. So, for backhoe also we are ready with some products, we have to do our network, we have to sort out something in the network and once we are able to do that probably the numbers will flow in. Plus, on the safe crane side we have couple of product launches and we are getting a good response. If you ask me, that market is not very big and we are commanding lion share in that. And with further new products coming in we probably would dominate this market. And as Madan said, H2 should be right quarter for EBITDA.

Sameer Deshpande: Yes, normally after the monsoons which industry should pickup and currently the trend is about 15 - 20% in volumes overall in the industry.

Ajay Mandahr: Yes.

Sameer Deshpande: So we hope to turnaround in the second half?

Ajay Mandahr: Definitely, we are positive about it.

Sameer Deshpande: Let us hope you come as a CEO and now you will be in a position to turn it around, because we are waiting for it for about last two, three years for the things to happen.

Ajay Mandahr: Time is back.

Sameer Deshpande: And last question, it is regarding our bank balances, we have around some Rs. 270-odd crores, some Rs. 200 crores and some Rs. 67 crores-odd and we have the debt of about Rs. 210 crores - Rs. 220 crores. So, are we not in a position to swap the debt with the cash available? Because the yield on our cash is not going to be higher than 6% to 7%, debt cost must be in the range of about 11% to 12%.

Bharat Madan: So if you look at the cash and bank balance, there are two components there. So there is escrow account money which is about Rs. 118 crores which is sitting on the balance sheet. Now this is related to the hospital business sale which happened way back in 2005, so that money is not accessible to us so that is under escrow account so that will probably get released and the litigation around that on tax part is over, so this is one disclosure which we already have in the annual report. And the balance is Rs. 100 crores is the liquidity which we are

keeping for contingency purposes. And today if you look at our borrowing cost on working capital, we have been able to issue commercial papers to even doing ordinate funding there and the borrowing cost actually is coming down significantly. So, today we have been able to manage the borrowing of a working capital at pretty lower rates. So we do not see there will be any risk on that front, it is better to maintain some liquidity on the business rather than keeping all the loans at this point in time. But yes, the liability will continue to be there for some time.

Sameer Deshpande:

So that escrow account we are not in a position to do anything for that?

Bharat Madan:

No, so there is pending litigation which is related to that, so till the time the litigation gets resolved that money cannot be released to us.

Sameer Deshpande:

So are we trying to expedite it in a way?

Bharat Madan:

Well, it is not in our hand. So it is clearly with the department with the court and how the court moves.

Sameer Deshpande:

And regarding VRS, we mentioned that this time 25, last time we had 50, so in this year we expect to have another VRS of about 25 - 30 people going forward?

Bharat Madan:

Yes, so the scheme is on. So I think something will get spilled over in Q3 also, so we expect about 100-odd people should be there in full year.

Moderator:

Thank you. We have the next question from the line of Raghunandan from Quant Capital. Please go ahead.

Raghunandan:

Just one clarification, any pricing action by Escorts so far? Like in August when the industry participants took the price hike that we also participate?

Ravi Menon:

Yes, we have taken a price hike slightly with ahead of the competition, though a few days before them.

Raghunandan:

And what was the quantum, sir, roughly?

Bharat Madan:

1.5% price increases have taken at that time.

Raghunandan:

And agri exports, how is the outlook there sir?

Ravi Menon:

So if you look at what we have been doing, we have been on double-digit for most of the year in terms of billing. But if you look at the last three months we have gone from 100 to 135 and this month we expect to get about 185 numbers. So we should be on track to keep the annual numbers which we have projected. Also if you want more details, we can always provide it to you separately.

- Raghunandan:** And sir like between Powertrac and Farmtrac, like roughly can you give what would be difference in the margins?
- Ravi Menon:** I cannot give you an accurate thing, but I would assume it to be in the range of about Rs. 20,000 I would say.
- Raghunandan:** On the railway segment, what is the outlook for the full year revenue growth and margin expectation?
- Dipankar Ghosh:** Full year revenue growth we would target something around 230, 240 and for the margin we are confident that we should be around 14% to 15% EBITDA.
- Moderator:** Thank you. We have the next question from the line of Nitesh Sharma from Philip Capital. Please go ahead.
- Nitesh Sharma:** Sir, one quick question. You highlighted that you have launched new backhoe loaders with indigenous engine, so any thought process in terms of what sort of cost savings we are looking at because of using indigenous engines in your construction equipment products?
- Bharat Madan:** This is a four-wheel drive backhoe loader which has been launched to really benchmark against the competition. So I think cost wise this is better as we have been introducing our own engine, so that is one of the synergies we were looking forward to. So most of the irrigator earlier were getting agri outsourced from third party, so now we are trying to integrate both the backend operation for tractor business and construction business. So, definitely we have cost advantage there in terms of introducing our own engine but we will see how the product really picks up in the market.
- Nitesh Sharma:** And are we looking at replicating the strategy of using indigenous engines to across all the products in construction equipment segment?
- Bharat Madan:** We are already using like transmission, we are supplying for all the cranes, so it is going from tractor side. We are also doing engines for some of the cranes right now and this is the backhoe which has been introduced with 75 HP engine and there is plan to introduce higher HP engine also in the other backhoe category. So yes, the integration is on, so our idea is to do as much as we can for both in tractor business and construction business.
- Moderator:** Thank you. We have the next question from the line of Viraj Kacharia from Securities Investment Management. Please go ahead.
- Viraj Kacharia:** Most of my questions have been answered, I just have one question. When you talk about us only manufacturing engine for some of the transition equipment which we produce, we already now started doing it for backhoe loaders. Whom were we supplying before, if you can provide some idea?



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- Bharat Madan:** Whom we were sourcing these from?
- Viraj Kacharia:** Yes.
- Bharat Madan:** There are multiple of buyers, so Kirloskar was there, Simpson was there.
- Moderator:** Thank you. We have the a follow-up question from the line of Mitul Shah from Karvy Stock Broking. Please go ahead.
- Mitul Shah:** Sir, my question is related to the assets like land and buildings remaining with us after this hiving off the entire auto business. Now any strategic plan for usage of that?
- Bharat Madan:** So, we will look at other options for the business growth across all segments, as of now there is nothing concrete because right now for certain period same space will be used by the new buyer for six to nine months and they will operate from the same facility. So once they vacate the facility, at that time probably we will look at what alternate use we can put this land building to.
- Mitul Shah:** So even from Q3 it will take six to nine months this party will use those?
- Bharat Madan:** That is right.
- Moderator:** Thank you. Ladies and Gentlemen, that was the last question. I would now like to hand the floor over to Mr. Deepak Jain for closing comments. Thank you and over to you, sir.
- Deepak Jain:** Special thanks to the Escorts Management for being on the call. And thanks everybody for taking time out for this. Wish everybody a Very Happy Diwali. Before I hand this over to Mr. Bharat Madan. Over to you sir, for closing remarks.
- Bharat Madan:** Thank you, Ladies and Gentlemen, for being patient on this call. For any feedback and queries feel free to write in to us at investorrelation@escorts.co.in. You can also logon to our website, www.escortsgroup.com for earning releases as well as other details and this transcript will be available on our website after sometime. You can now download our Investor Relation App from Google Play store and Apple iTunes for updates. You can visit our social media pages for the latest company news, developments, etc. We will meet again in next quarter. Wishing you all a very Happy Diwali. Thank you very much.
- Moderator:** Thank you very much. Ladies and Gentlemen, on behalf of IDFC Securities Limited, that concludes this conference. Thank you for joining us and you may now disconnect your lines.