



## “Ashok Leyland Q3 FY2018 Earnings Conference Call”

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**Moderator:** Ladies and gentlemen, good day and welcome to the Ashok Leyland Q3 FY2018 earning conference call, hosted by Emkay Global Financial Services. As a reminder, 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. Should you need assistance during the conference call, please signal an operator by pressing “\*” then “0” on your touchtone telephone. Please note that this conference is being recorded. I would now like to hand the conference over to Mr. Raghunandhan from Emkay Global. Thank you and over to you Sir!

**Raghunandhan:** Good afternoon everyone. I would like to welcome the management and thank them for giving us this opportunity. We have with us today, Mr. Gopal Mahadevan, The President Finance and Chief Financial Officer and Mr. K.M. Balaji, The Vice President, Finance. I would now hand over the call to Mahadevan for his opening remarks. Over to you Sir!

**Gopal Mahadevan:** Thank you Raghu. I hope you can hear us all. Good morning everyone. Thank you very much for the interest in Ashok Leyland and taking time out for our investor call. I have Balaji also joining in. I am calling from London and Balaji is dialing from Chennai. I will just give a quick highlight and then hand it over for the questions.

I think one of the most important things that I just wanted to share with you is that, as you all know the industry seemed to have turned the corner in Q3 and the demand that was there in Q3 was unexpected.

You will remember in Q1 2017 the total industry volume was about 32% lower than the same period last year and even in September, I spoke that TIV on a cumulative basis was lower than last year by at least about 7%, but now as we speak in Q3, the total industry volume has been 9% higher in absolute numbers but if you were to really compute it in terms of tonnage and the number of axles, I believe that industry is moving towards higher tonnage vehicles and we possibly have seen a growth of about 70% in tonnage terms in Q3 over last year.

Ashok Leyland itself has grown about 41% in volume in the current year. We did about 31437 units as opposed to 22344. Our market share for the quarter on SIAM declared basis was 33.4% as opposed to 33.7%. It is marginally lower by about 0.3%, but on a cumulative basis, our market share is 33.8% as opposed to 32.6%. So, we are about 1.2% higher than last year.

I think this exemplifies the iEGR solution that the company has embarked on aside of the SCR solution that the company could also provide, has helped us in this growth. IEGR has been very well accepted in the market. iEGR is doing well in all the tonnages and we are happy that we have been able to help customers to have a product whose total cost of ownership is lower than what competition can offer.

In terms of revenue for the quarter, we are 58% higher and in terms of PAT, if you were to look at it for the quarter, we have been at about 178% and our EBITDA for the quarter was 11.1%. A total debt for the first time in the history of the company in December quarter has been negative

at Rs.543 Crores, but frankly while I am not going to celebrate on this, because there has been lot of customer advances that came in December in anticipation, not in anticipation but more for requirements to be fulfilled, but as we move forward, I think our working capital all I can tell you is that our working capital is very well in shape and I believe that we would be at about six to eight days, which is best in class in the industry and we continue to post double-digit margins despite the price impact of raw materials, I think steel prices continue to escalate while we have been possibly the one player who has been revising prices quite regularly, we have done that in April with a 12% - 13% price increase and I think a lot of people were concerned that we seemed to have taken prices up while the rest of the competition did not, but we had to do it because the new move from Euro 3 to Euro 4, the cost has gone up.

The second point was in July and subsequently in November also we did make some marginal price increases because there was raw material cost push effect which was needed to pass on, but of course, we have continuously been working on our costs and all of this has culminated in a EBITDA of 11.1% for the quarter and the most important thing which I should possibly mentioned at the beginning of the call there were two things.

One is something, which is very close to my heart, is I think the Deming Prize Ashok Leyland the Hosur plant got. We are the only commercial vehicle manufacturers in the world to have got two consecutive Deming Prizes. Last year we had it for Pantnagar facility, this year we are having it for Hosur. This kind of exemplifies the efforts that the company is taking in and getting its quality up consistently.

The second most important thing of course this is a special quarter for us because this possibly is the highest Q3 volume ever in the history of the company and possibly is the highest ever revenues in the history of the company as well. I will hand it over to Emkay for the floor for questions.

**Moderator:** Thank you very much. Ladies and gentlemen, we will now begin with the question and answer session. We take the first question from the line of Jay Kale from Elara Capital. Please go ahead.

**Jay Kale:** Thanks for taking my question and congratulations on a great set of numbers. Sir, my first question is on the demand side. Are you seeing in the last few months, the economic activity-led demand also pickup or was it just to pre-buying if you can just throw kind of demand that we are seeing how sustainable it is that would be my first question?

**Gopal Mahadevan:** I think we are seeing a lot more demand. I think there are confluences of reasons frankly. The challenge that we have is putting a percentage for a factor for each of these reasons. One of the first things is in the northern states especially in Rajasthan and UP and other states as well, we are seeing the rated load legislations are coming in so which means the overload, which was happening in some of the sectors including cement and steel. Now fleet operators would need to invest in more vehicles. So, this is one reason, so very clearly this has increased demand.

Now in states like UP, the level of infrastructure spend that is happening, the activity that are happening, road building, construction, is also kind of significantly scaled up, so there is a little bit of demand push that is also one of the reasons why we are seeing the demand from fleet operations going up. We are clocking one of the highest ever in terms of road building. We are possibly doing about 24 km a day anywhere between 20 and 24 km a day and I think that is another significant factor, which is leading for the growth on the higher tonnage vehicles.

The third thing as I had mentioned earlier, but this is still to be waited and watch, I am not saying that I have got it right or something, but I think GST impact has kind of settled down. Last year we had demonetisation and then we had BS-III to BS-IV then we had GST, I think a lot of uncertainties have kind of settled down. The movement of goods between states is possibly improved. People are seeing that trucking operations, productivity are getting better, so we are seeing investments happening.

The fourth one is a lot of end customer industries, if it is FMCG, food and beverages, chemical industry, you have MNCs, a lot of them, oil companies, a lot of them are insisting that their fleet operators, supply chain partners would need to upgrade their fleet, if they need to stay relevant for the business. So, I think this is a confluence of factors, which has been driving up demand and then on the eastern side of the country, I think the mining activities have also started to take off, this has been happening over the last two quarters and that has seen a demand for tippers also going up.

**Jay Kale:** If you can just quantify the Pantnagar production and what is the status on the incentive that we did not have last quarter, if you can just highlight something on that?

**Gopal Mahadevan:** Well, I cannot share the exact incentive benefit. All I can tell you is that yes, we had, the profitability of the company has been achieved despite the Pantnagar benefit getting reduced by about 35%, but Balaji can give the reduction in Pantnagar. Balaji, can you share the production after I finish, but let us wait and watch. We have made representations to the government. I think we should see the light at the end of the tunnel, because this is a commitment that the government has made based on which investments have been made, so we have the benefits going up to March 2020, the government has promised to look at it, but we will have to wait and watch, how they react, but we have represented to the government that the investments in Pantnagar have been done based on the physical benefits that have been promised at the time of investment.

**Jay Kale:** Just one last question, if you can just throw some light on the defence part, are we seeing some slowdown in orders or how should we look at the defense portion say in the next two years in line with your expectations?

**Gopal Mahadevan:** I think as far as defense is concerned from an Ashok Leyland perspective there are two parts. There are stable orders that we have from VFJ and those would possibly continue. We are not seeing any slowdown on that but I think we also have as I mentioned to you, have about as I speak the number of tenders where we are prequalified is about 21. The revenues of that would

be anywhere between about Rs 750 and 1000 Crores. We have started executing some of them. We have got various kinds of vehicles including mine-protected vehicles or medium bullet proof vehicles, Multi Barrel Rocket Launchers, and then there are different kinds of vehicles even within them which are beyond the four-wheel drive, they could be 8 x 8, 12 x 12, etc. What I see happening in the medium term you can see a lot of reports on the defense procurement that the country is planning to do, there are also requirements from the army to refurbish their existing fleet, so I am positive about the defense business. I think there is a lot of potential that it holds for a player like Ashok Leyland who have been one of the larger logistics partner, but I think where, I am not able to put one fix on it is the exact timeline, because these are tender based businesses, so at some point in time the defense ministry would have to acquire land systems, they will have to acquire for transportation services not only for people, but also for artillery, so and we can and we have the capability to work with multiple vendors who are manufacturing artillery. So, we are building our capabilities there, and I think this is a little bit of a medium term and now quarter and quarter story, but as far as the VFJ business is concerned, it is stable.

**Jay Kale:** Thanks, and all the best.

**K.M. Balaji:** The production for the PNR in Q3 is about 11000 vehicles.

**Moderator:** Thank you. We will take the next question from the line of Pulkit Singhal from Motilal Oswal. Please go ahead.

**Pulkit Singhal:** Thanks for taking my question. Just wanted to understand, in January we have seen possibly some market share dip for Ashok Leyland in terms of numbers. Are there some production constraints out there or are you just not participating in the discounts that are happening in the industry?

**Gopal Mahadevan:** I think it is more a supply chain constraint than a production constraint, so what happens ideally would be the challenge that all of us, this is not an excuse or anything, but there is a sudden improvement in demand for 3718 lift axle vehicles and these are special vehicles. This is not just a standard chassis, so these are lift axle vehicles and then when you have higher tonnage vehicles going up, the whole supply chain system has to be worked on. So, we have had a marginal dip but if I had more vehicles, I possibly would have been able to sell, but we are trying to fix the problem because it is not just production constraint at Ashok Leyland, but it is more a supply chain constraint at the supplier's base. So sometimes, well I cannot take up specific names, but there are certain parts, which get kind of rationed between various manufacturers. So, the demand was there. I would have said that we could have possibly sold a bit more in January but there were some constraints, but one of the things that I also missed mentioning was the LCV business in my initial introduction. I think they have done a wonderful job. I think the whole LCV business is profitable now on a consolidated basis between the LCVs, companies as well as Ashok Leyland operations and I think given the current month, LCV volumes have been very satisfactory in January. Yes, please back to you.

**Pulkit Singhal:** So, at the supply for, I mean there is a supplier issue, but is that only true for Ashok Leyland or the industry itself on that 3718?

**Gopal Mahadevan:** It is for the industry also.

**Pulkit Singhal:** Can you talk about the discounting trends? I know it is high, but I mean, incrementally if it kind of stabilizing or getting better?

**Gopal Mahadevan:** It is disturbingly high. I mean there is no forcing the amount of demand to actually be discounting and we find it very difficult to digest, but we have to participate in the market to stay relevant so our strategy has been over the last four years if we have to look at it, we persistently keep raising prices and managing the net price realization because somewhere there is a satisfaction at the customer end when you get a higher discount, so we will have to raise prices and then we will have to give a higher discount and that is the basis on which we are going about it the discounts have been higher. I think the discounts are peaking. There is no reduction in the count etc. I think it has become a price game for some of the players because they want to do customer acquisition through discounting. I am not going to take any order in which I have to leave money on the table. I need to make margins. I am not saying that we will walk away from customers but at the same time it has to make economic sense for my customer, it has to make economic sense for Ashok Leyland to do the transaction, so what we are doing to make the business and economic sense for the customer is to build vehicles, and I am not selling this for the sake of this kind of a peak, but generally, I mean, we are working very hard on reducing the total cost of ownership for the customer.

**Pulkit Singhal:** Sir, lastly in a disturbingly high discount scenario, we have a pleasantly high net realization growth of 11%, now if you could just help us understand that I understand the product mix is getting better, but does this particular quarter have some higher contribution from non-truck revenues like defense or spares or something?

**Gopal Mahadevan:** No, in fact defense revenues was slightly lower so we had exports in this quarter to Ivory Coast, but I think predominantly it has been the truck mix that has helped us, so we have not had anything which is singularly responsible. So last year had a favorable impact in terms of the GST whereas we did not have the same thing in the current quarter so the profitability that we have been able to see has been for two reasons is the higher mix of products, we have somehow been able to ensure that the NPRs are slightly better. Third one is operating leverage. Very clearly if you look at it we have had a 54% or 55% increase in revenue than the PAT impact has been significantly better.

**Pulkit Singhal:** Correct Sir. Sir, let me squeeze a last one, so any demand outlook because all these factors that you mentioned in terms of demand some of them seem to be structure, so any outlook in terms of demand growth for the industry?

**Gopal Mahadevan:** The demand seems to be firm and fourth quarter is typically good but what I am not going to talk about is ratios because the last year the base effect was there, because there was a BS-III to BS-

IV prebuy that has happened, but January has not been bad, let us wait for February and March, we are reasonably positive, I had given an outlook and frankly when I give an outlook it is not like it is cut in the stone whatever visibility that we have is what we share. I had mentioned in the beginning that we possibly would see the year ending with a 10% increase in volumes; it is possible that our number will be done, because the reason is we already are there at that number. We are 9% YTD, but we must remember that Q4 of last year had a high base effect, but even with that base effect are we able to maintain a 10% growth, we will have to wait and watch, it looks like it can happen.

**Pulkit Singhal:** Thank you. And all the best.

**Moderator:** Thank you. We will take the next question from the line of Kapil Singh from Nomura Securities. Please go ahead.

**Kapil Singh:** Congrats on a great set of results. Few questions on you mentioned about operating leverage so just trying to understand what is the kind of capacity that you have and especially because Q4 you will be stretched, so from that perspective and going ahead when you look at next one to two years if this kind of a growth sustains what is the kind of peak production that the company can do? Second related to that what kind of cost escalation is required to achieve that in terms of capex or manpower cost. For example, when you go from 3Q to 4Q you may have let us say 10% to 15% higher production, does that require significantly higher manpower cost or other costs or it can be done at the same level of costs broadly?

**Gopal Mahadevan:** I think instead of letting us say answer in this way, yes, we are at about 80% or so of utilization and a lot of this, I cannot answer it in absolute terms why because the mix of production if it goes to a 3718 is different from a mix of production if it is a 27-tonner. So, it is not equivalent. So, we look at it in equivalent units. All said and done, we will have to beef up our capacity as we move forward because we are now, you know when we peer into the glass ball, what I can say is that we expect at the moment that 2018-2019 will also be a growth year because we would see a lot of infrastructure spend coming in by the government and hence we have 2019-2020 if the BS-VI implementation is going to happen, we expect that there could be a BS-VI prebuy that will happen in 2019-2020. After that in 2020-2021 we will have to wait and watch when BS-VI comes in and some of the demand will be there, but that is quite far away. This is one. The second one is yes, we will have to augment capacity. The management is fully ceased of the demand from capacity and we are already doing a lot of debottlenecking. I do not think they are going to do a big bang capacity expansion, setting up a Brownfield plant or something like that. We have facilities available. We are debottlenecking in certain areas where we believe that that would kind of release capacity. The third thing is with respect to your question on whether the fourth quarter would that be a higher incurrence of expenditure, of course there will be higher incurrence of expenditure because if the production is going to be more we will have to wait and watch, but the production overhead will be higher. I mean the sales overheads are going to be higher, but what we look at is not absolute quantum, but as a percentage to sales. As long as the variable costs as a percentage to sales is maintained or slightly lower and then after that a gross margin kind of kicks over to an operating leverage that is how you get the entire profitability

getting planned so I do not see anything of concern in terms of anything specific on production overheads or sales overheads manufacturing or I think we have well in control and we do not see any issues of that.

**Kapil Singh:** The reason why this question was because when I go from Q2 to Q3 there are very minor increase in employee cost but your revenues have seen on almost 17% to 18% increase so is this area which has largely fixed in nature at?

**Gopal Mahadevan:** Variability is very low here.

**Kapil Singh:** That is what I was trying to understand.

**Gopal Mahadevan:** Management has a done wonderful job in terms of improving the productivity of force.

**Kapil Singh:** Okay and Sir your thoughts on discounting as well have we peaked and what are kind of price increases you have done in January if at all you see you will be able to pass on increase in commodities for Q4 and going ahead?

**Gopal Mahadevan:** I will tell you I think I answered this question, but in the interest of time of all other people also, all I can say is that we do not lead discounting game but once you give a discount the customer then would say, Mr. Company X is giving discount, please tell me the price that you are going to give. So, we work with the customer on net price, we work on total cost of ownership, we have raised prices in January and again by around 1% possibly the only player to do that I am not too sure whether other players have done that. We are trying to remove the effect of the raw material price increases. It is a very, very believe me it is a very, very difficult thing to do in market where it is right to discount so to answer your question can I guarantee? I cannot guarantee but at the same time you people know me I mean very open on this issue but the basic idea of the company is to see that we keep improving our gross margin and operating leverage. I mean that is why we have had so many quarters of double-digit EBITDA margin except for the June quarter where the volumes have fallen out so then consistent on then that is the goal of the management and want to ensure that we grow the business possibly.

**Moderator:** Thank you. The next question is from the line of Chirag Shah from Edelweiss. Please go ahead.

**Chirag Shah:** Thanks for the opportunity and congrats for a good set of numbers. Two questions Gopal one on the gross margins so we have seen sequential dip in gross margins is it because of commodity cost already in PNL or is it because product mix?

**Gopal Mahadevan:** When you say gross margin can you please define it?

**Chirag Shah:** Sales minus raw material?

**Gopal Mahadevan:** Sales minus raw material cost. You are talking about sequential happen in September to?

**Chirag Shah:** Yes, Q3 over Q2 of FY2018?



- Gopal Mahadevan:** Sequentially there is no change in gross margin
- Chirag Shah:** What is the kind cost impact commodity cost is it possible to quantify to some extent what is kind of commodity cost but we have seen in what likely in Q4?
- Gopal Mahadevan:** What I can you tell that we had commodity price approximately about Rs.154 Crores.
- Balaji:** Not for the quarter, this is cumulatively for the first three quarters.
- Chirag Shah:** Does it reflect the reasonable part or large part is yet to come because many other companies have indicated that the commodity impact is not yet seen in the quarter P&L it is likely to come from Q4 onwards?
- Gopal Mahadevan:** I mean steel prices have been going up how can be they have not seen it.
- Chirag Shah:** Because the contractual arrangements are such that there is a lag effect probably for that.
- Gopal Mahadevan:** No, I mean if they are doing it, I think it is wonderful but no steel company is going to supply steel at constant prices for nine months.
- Chirag Shah:** Fair point. Second question was that market share of late we have seen on monthly basis we gain market share or lose market share incrementally, if at all, and I know you have focus on profitable market share and keeping that in my mind what all things we have to do is it more on product or is it more on distribution, is it more on internal efficiency so what will drive market share for Ashok Leyland from here on?
- Gopal Mahadevan:** I tell you this is an important question but it is like I keep telling that market share is like thermometer reading of 98.6. It does mean you're healthy, it does mean you're sick so while market share is a good thing to have. We will have to look at the entire performance of the company. Second, the network is pretty well laid out. You know that we were at about 350 points of presence about 6.5 years ago and today we are at nearly 2900+ points of presence. So, we are pan India company if you look at share of business in North, East, West and Central we are very close to about 30% somewhere around 25% and 30% so our presence is pretty pan India and now lot of network have been added non-South because we were well entrenched in the southern side. So, I do not think there are any network issues on the contrary that has been a strength for us to be posting the market share gains that we have had. The other thing I just wanted you to understand that approximately we have added 10% market share over the last five years. It is a huge number so on a quarterly basis if I see some dip and then going up coming down like you are rightly mentioned or a monthly basis I am not too worried while I do note that number I am not going to change my entire strategy based on that number. What I will be looking at in terms of product strategy or network strategy is that I will have to look at my technology strategy, am I offering correct products and what I am doing in after market, in maintenance cost etc., What I can tell you is that we are not saying that we have achieved this market share and we are happy sitting there. No, we will certainly try to grow business, but we will have to look at lot of other

aspects before we take any stand and you are right, they are deals in this quarter where I walked away from including a large account.

**Chirag Shah:** Fair point. One last housekeeping question depreciation has gone down sequentially anything over there because from Rs.141 Crores it is Rs.135 Crores?

**Gopal Mahadevan:** It is just that is why I said I mean maybe add capex in a couple of quarters it will start going up?

**Chirag Shah:** Okay fair point. This was helpful and all the best.

**Moderator:** Thank you. We will take the next question from the line of Sunil Kothari from Unique Investment. Please go ahead.

**Sunil Kothari:** Thank you for the opportunity. Congratulations for good numbers Sir. Sir, my question is this new change in this budget on import duty structure changes on auto component imports, what is your view and how it will be affected.

**Gopal Mahadevan:** We are waiting for the notification to be released to understand the impact.

**Sunil Kothari:** Are you importing anything up to now?

**Gopal Mahadevan:** Not anything significant we are not major importer at all.

**Sunil Kothari:** Sir, second point is some comments on Hinduja Finance if you can throw some light and IPO plan just now we heard?

**Gopal Mahadevan:** I am not able to comment anything on that because at the first moment we are looking it various options for it. All I can say is that the company has been doing well. It is a very good performer and we are very, very happy with the performance of the company and now that is all I can share with you.

**Sunil Kothari:** Great and Sir last question is there was a lull in the aftermarket sales and spares all these things so now it has stabilized and how it is performing?

**Gopal Mahadevan:** It is performing very well. I think about a year-and-a-half back we used to struggle to do Rs.70 Crores and Rs.75 Crores because the penetration was little lower. The team has started itself a very big task of having penetration of going up to 50% over the next four to five years. Currently we possibly at about 20% but all I can tell you is that the guys are doing wonderful job, they have now consistently clocking about Rs.100 Crores to Rs.110 Crores every month that is not one month since the beginning of the year I think since when the after-market revenues are being lower than Rs.100 Crores.

**Sunil Kothari:** Wish you good luck. Thank you.

**Moderator:** Thank you. We take the next question from the line of Priya Ranjan from Systematix Shares & Stocks. Please go ahead.

**Priya Ranjan:** Thanks for taking my question. I have two questions; one is on industry capacity at what level do you see that probably when we will see the discount will be coming off?

**Gopal Mahadevan:** Sorry at what level what will come off?

**Priya Ranjan:** If industry capacity utilization itself becomes 90% then whether you are desperate or not you will come out with the discount?

**Gopal Mahadevan:** I do not think so. I tell you it is a very difficult question to answer because I do not foresee a situation where the industry capacity will be at 90% on consistent basis. I appreciate your question, but I do not think it will be like that and secondly what happens is there are various opportunities that will come for the commercial vehicle industry also. One is I know it is not a direct answer to your question but what will have to look at some point in time we are expecting that the government should look at the cash for clunker scheme and that could possibly bring in about 5,00,000 to 7,00,000 units of demand into the system. The second one is I think as we are getting more and more technologically savvy including we have now of course got fully built vehicles coming in, fully cab vehicles of course we have added blowers coming in from January then all these are happening I think there is a lot more regulation that is helping us to consolidate production in the organized sector so there are opportunities which I see happening over the next three to four years, which will auger well for the industry but will that actually help reduce discounts, I will have to wait and watch because frankly pricing today is being used as strategy for gaining share and will have to see when that kind of strategy evolves. I am not able to put a date.

**Priya Ranjan:** My second question is on the your market share I mean it has been kind of stable plus or minus 1% but when we look at the segmental market share you have last time and you have lost the leaders 37 tonner, but you have good gain in 25 and 30 tonner in multi-axle side similarly you have lost say more into tractor trailer side but you have gained more at the lower end say 12 tonner I mean 9 tonner and all so how should we read it, is it more because the products has acceptability EGR is poor at lower tonnage vehicles?

**Gopal Mahadevan:** No. We are doing well on 41 and 49 tonners, also but what happens is that when we started, we introduced 3718 lift axle but again there is a lot of pricing involved in that so there are deals when we are walking away from 37 tonners. So, I am not going to sell below my variable cost. As far as the ICV market share is concerned, you are right and I think it is a very good observation that you have had. The ICV strategy of the company about four years ago our market share, was about 12% to 15%. Today we are at about 22% to 23% that happened because we had a very clear ICV strategy. We brought in premium product called Boss, which is doing well and in its segment its possibly unique vehicle. The second one that we did was we recently launched Guru which has been doing very well. It is rated load vehicle, three cylinder, lower cost option for carriers who are not looking at overloads and then we have just completely refurbished cab on

our other ICV vehicle also so we have seen lot more penetration coming in so what we keep doing is away we will come back with our strategy on some offering that we may have but we have had a 3718 Plus that has been launched, which is India's first vehicle with unitized wheel bearing, the only vehicle with unitized bearing. Unitized bearing it does not have to be greased at all, it is life time grease up thing and second thing we are offering is superior tyres which will offer better mileage and I think we will see a little reduction on 3718 market share but we are trying to do it little differently than I will give you Rs.50000 - Rs.1 lakh more and buy a vehicle we are not doing that.

**Priya Ranjan:** I mean now the 37 is in multi-axle side, 37 is probably I think 60%-65% of the market, which was earlier reversed, the 35% and 31% was 60%?

**Gopal Mahadevan:** So, we expect kind of a demand on 3718 in Q3 I mean this was unprecedented.

**Priya Ranjan:** Sir, one more question on this regarding that, so can we put additional axle on MAV side to get more than 42 or something, is it possible technically?

**Gopal Mahadevan:** Well I am not an engineer, but I don't think there is a possibility.

**Priya Ranjan:** Thanks. That is all from my side.

**Moderator:** Thank you. Next question is from the line of Pramod Amte from CIMB. Please go ahead.

**Pramod Amte:** Congrats on great set of numbers. Two questions, one what is the status of your BS-III inventory liquidation, how much you have done one, and second what is the mix of your recently launched SCR versus EGR in your portfolio?

**Gopal Mahadevan:** It is predominantly EGR and I think more than 90% should be that. The second one is as far as the liquidation of the BS-III to BS-IV inventory is concerned, we had about 10600 to 10700 units. I think as on date, we possibly have about 500-600 units, which are waiting to get exported, nothing more. As I said we have done a wonderful job, I mean the manufacturing guys, please understand they have done wonderful job. There was a lot of planning that was involved in terms of swapping. You know we did export about a quarter of that number, but the balance just to kind of share because you also need to understand what are the things that our team has done is to swap an engine and then put in a BS-IV engine even when production is struggling along its full capacity is an amazing feature that they have done, wonderful.

**Pramod Amte:** Second with regard to the ASP discounting trend we understand that tactically to maintain your market share, you are participating in the short-term ASP discounts, but some of the recent contracts are spreading over next two years' delivery and are they coming with the similar type of discounts that gives us substantially, how do you look at such deal?

**Gopal Mahadevan:** What is the ASP?

**Pramod Amte:** The ASP discount, average selling price discounting?

- Gopal Mahadevan:** Average selling price discount, okay.
- Pramod Amte:** No, the deals are now getting elongated with the delivery time of two years, so in that context do you see them ever coming down, it looks these deals which has not come down at all?
- Gopal Mahadevan:** Yes, I think we have kind of you know everybody is keen to discuss about the discounting. You see frankly I will tell you. We look at the problems slightly differently. I mean that not that we have solved the problem. We would not want to have discounting in this thing, so we are not leading the discounts by the way. That is known in the market. You visit the dealership then you will know who is leading the discounts. The point that comes up is, so what we have said in the market is like this, I have to give discount, it is like you want to buy a car in December, and you will get discounts. Everybody is discounting. Now it has gone on to January also, so it is prevalent in the commercial vehicle industry lot more than in the Passenger car industry, but the point that comes up is I need to look at what is my net realization and my net gross margin on the vehicle itself. I have got a net amount of fixed overheads and I have to ensure that to meet certain EBITDA targets that we have set for ourselves how much do I need to sell the thing and at what volume. So, it is a mix of the net price realization of the vehicle, the mix of the vehicles that I sell, the gross margins that I get, the gross contribution that I get on this total sale for the company, net of the fixed expenses what is the EBITDA that I will make, which will also give me an ROCE. So, it is a lot more, so we do give lot flexibility to the operating teams. We are now today disseminating information quite significantly to the front end. You know our guys in the fields to the zones, the regions, the area managers we are giving them flexibility to manage a portfolio because you win some, you lose some, but overall, we need to see two things, one is on an individual transaction I cannot make a negative contribution that is not permitted. I do not make negative contribution on an individual sale ever, unless there is a mistake, but I just saying it never happen. The second thing is, they can manage their portfolio. They can manage their customers, so there are lot customers whom we cannot afford to lose, but we may end up losing them if they are going to ask for a price, which is lower than my variable cost. I cannot do that.
- Moderator:** Thank you. We take the next question from the line of Kapil Singh from Nomura Securities. Please go ahead.
- Kapil Singh:** Sir, during your opening comments you mentioned that different business, the additional tenders won are 21 and they are about 750 Crores to 1000 Crores in revenue terms, I just wanted to understand is this the overall lifecycle revenue or this is the annualized revenue that you are looking at from these tenders?
- Gopal Mahadevan:** It is a mix of both. We have got about 900000 Crores out of which possibly the annualized revenues could be somewhere around about 550 to 600. The reason why I am not again able to answer this is if the government does not retender again they have said that they are going to retender every year, but there is a procedure is slightly more complex. Once you get into and you become L1, you can be L1 for the every year tender, but suppose the government does not, and then my annual revenues will come down. So, I do not want to state something, which is not, but

I would say that about another 500 to 600 Crores of additional revenue would easily come from this on an annual basis.

**Kapil Singh:** Currently our FY2017 or FY2018 if you can tell us what would be the defense revenue broadly in FY2018?

**Gopal Mahadevan:** I cannot, at the moment I do not give those revenue breakups Kapil, so I will have to constrain but there would I think slightly better than last year that is all I can say.

**Kapil Singh:** Second on LCVs you touched upon the profitability has improved, so we are seeing market share gains coming through almost on the monthly basis, so what is the volume target or market share target that you have here?

**Gopal Mahadevan:** Market share target, all I can tell, of course it not that we do not have it and we are doing blind. We are not doing the business blindly, but I cannot give that this is a purely internal, and if you notice we have given a market share target even for the main MHCV, but I think what the team has got is a big audacious goal. They have target that are set for them. We have just started to do this whole business dependently just about a year since we acquired the entire LCV business and I think that it has been a wonderful turnaround that has happened and I think the last month January of course is the first month in the sense where we have reached again after a longtime 4500, and then we have introduced Dost+ because we have been doing very well. It is an upgrade on the existing Dost, so we have now volume line and value line product. We still have the Dost rigid front axle for specific loads, but we will be improving the portfolio. We will be adding to the portfolio over the next may be 9 to 12 months about six variants of it and including some export variants of LSD, so I think there is a lot of promise that this LCV business hold that is all I can share at the moment.

**Kapil Singh:** Sir, profitability of the LCV business has it reached the overall company levels in terms of margins?

**Gopal Mahadevan:** Well, the gross margins are as healthy as the domestic MHCV business. Now, the trick is that getting the operating leverage of up the scale so then the EBITDA margins also start coming up to the company level. It is not very far away.

**Kapil Singh:** Sir, capex, any targets?

**Gopal Mahadevan:** LCV is going to be a very integral piece in our export initiatives also. There are markets where LCV can make even in roads.

**Kapil Singh:** Sir, capex number if you can share?

**Gopal Mahadevan:** I think Balaji said about 500 Crores this year also?

**K.M. Balaji:** Yes, it will be capex and investments if you put together then it will be 750 Crores, 750 to 800 Crores and that will be including the investments also.

- Gopal Mahadevan:** Capex will be lot lesser because we have made some investments into HFL also very recently. We may have to put in some further money, etc., but it is going to be reasonable in control. We are not going to have any big bang capex is coming like that, some investment in Optare will be there, which we have completely provided for, but we would need to have some regular investment to be done to support the company for its running expenses, but not very good significantly may be 7 million pounds or so that we have been putting on an annual basis, I am not saying from now to March, let me clarify. It is not from now to March, but on an annual basis so that may continue, but I think Optare is also kind of getting some orders, etc., Optare had this new, New Zealand order for about 114 buses that have come in and that is a 20 million order, which is going to be executed by May.
- Moderator:** Thank you. Next question is from the line of Chirag Shah from Edelweiss. Please go ahead.
- Chirag Shah:** Thanks for the opportunity again. Mr. Gopal, I had a question again defense, so as I understand there is a regular business of VFJ water browsers and then over and above that we have this new tender where we have technical qualification?
- Gopal Mahadevan:** Yes, for trucks as well as that there are some CBUs completely built units, which are done both in India and as far as exports and water browser business also.
- Chirag Shah:** So, of this new tender qualification that you indicated 21 kind of number, there is nothing much of that would be in current revenue, it is all, which will come from 20 or something like that, is it right?
- Gopal Mahadevan:** It comes on 2018-19, then 2019-2020.
- Chirag Shah:** It will start from 2019 itself and if you can help how the ramp up happened, so if that is a fixed say 500 Crores revenue every year or it will start with the lower number and it will scale up 500 Crores kind of a number for individual project, if you can help us understand so it will, how to look at this part of business?
- Gopal Mahadevan:** Because I just had a review from the Defence also as to when the government will start ordering. A lot of this is going to depend on ordering. So for example, if the ordering starts say June, July, August, then that 500 Crores number may be around 300 Crores next year and then after then ramping up to 500, but if the ordering happens say sometime in the fag-end of next year then you will have very little in the next year and then after that it will start, so at the moment, I am not able to give that visibility because until the program starts I am not able to give, believe me, if I get know about the share, but at the moment these are good estimates of what will happen. I expect that it will start, the ramp up will happen then I think we should see about 300 Crores to 400 Crores stocking of immediately in the next year. I will keep you posted.
- Chirag Shah:** The second question was on spare parts so post GST is now stabilizing, how do we see that number for us, what are the aspirational revenue that we are looking from the spare part business

because we are generally low on spare part may be compared with our peers we are still on the lower end as the contribution to overall revenue?

**Gopal Mahadevan:** I do not know whether, as per as MCV business is concerned it is low, but when a benchmark it against my own LCV business, we are low, but LCV is a new business. So, LCV penetration is somewhere around 70% whereas the MHCV penetration was about 20%. Our target is to take it up to somewhere around 40% to 50% and given other things there are so many variables when I give you this kind of statistics, but directionally if you know what we predict happens and then everything happens in the same bucket you understand you know what I mean then we would want our players revenue moving from about 5% to 6% currently to about 12% of revenue and you see we are also working on other solution business, I mean we mentioned that the basic ideas that we are looking at is how do I, that is why we have had this launch of four digital solutions that we did, one was the service mandi then we had the LEYKART, which is for ordering parts over the system itself through a website and then we have what is called as E-Diagnostics, which have started fitting those boxes by the way though the telematics system inside the truck now. E-diagnostics helps the operators to understand what is wrong with the truck, do a quick diagnostic and then there is something called as an eye alert also which we are now activating, which gives real time online information to fleet operators what is the performance of the trucks, how is the engine performing, temperature, oil consumption, air pressure, etc.

**Chirag Shah:** Thank you and all the best.

**Moderator:** Thank you. We take the next question from the line of Mayur Malik from India Nivesh Securities. Please go ahead.

**Mayur Malik:** Sir, I just wanted to know what is really happening on electric bus front, how ready are we and I heard that there were some orders that we are really coming out from the state transports, so have you really looking to do something there in the near future?

**Gopal Mahadevan:** I think there is a separate electric vehicle SBU that has been set up and headed by a very senior person and we have a technical arrangement also for swappable batteries, which possibly be showcased in the coming expo. We are just looking at that with Sun mobility and the second thing is of course see we are looking at various options. See the electric vehicle technology you must remember it is not something that has been carved out in stone, it is very much evolving. I am reminded about the solar technology that were coming in early about 5 to 6 years or 7 years ago when you had multiple options on solar technology even in you had thermal, you had PV, etc., and within PV you had so many options, so similarly what is happening is you got long range options where you have a single charger, which will take to about 200 km then you have got fast charging technologies also, which would take us to medium range, then you have swap technologies where the cost of the battery and the size of the batteries are significantly lower, but you keep swapping them for short range so we are actually plotting ourselves for each of these options because I am sure that there will long range solutions required as well as swap technology as required. So, we are very much there in our plans. We are working with on tendering for some of these state government orders and you will hear from us soon.



**Mayur Malik:** Sir, have we done tie up with anybody particularly for the lithium battery. I mean just trying to understand because what I hear is some competitors are readily 50% who have already supplied buses to a couple of State Transport Corporation so have we really delivered any vehicle so far or we are almost on that finalization stage?

**Gopal Mahadevan:** One competitor has done an experimental order, but we have tie ups, I think we have very recently also done an announcement with the company abroad for tying up with battery technology. What we are not doing is tying ourselves with one person because then you have a challenge, so we have to work for win-win situation with the potential partner to look at various options because even in lithium ion there are multiple options of batteries. Lithium ion is only a type of a battery, type of electrochemistry that is all. So, there are multiple options that are there so when we are working with Sun mobility the type of batteries that they will use is distinctly different from our fast charging battery, which is distinctly different from a long-range battery like for example, what has been used in our Optare business. So, we must remember that we have been doing electric vehicles. We have built capability in Optare also. So, we are not making some of those announcements in terms of tie up and then doing it because we are doing it a lot more quietly because the proof of pudding the vehicle on to the customer so we are very much on track on that.

**Moderator:** Thank you. We will take the next question from the line of Saurabh Kumar from JP Morgan. Please go ahead.

**Saurabh Kumar:** Sir, just two questions from my side, one is what is your outlook for the bus segment going into fiscal 2019 and second is that if you can provide the breakup of revenue for the quarter?

**Gopal Mahadevan:** Breakup of revenue will be given by Balaji. As far as the bus segment in concerned overall if you are going to look at the TIV. TIV for the quarter was lower by about 27% and coincidentally on an YTD basis also it has been so because I think a lot of state transport undertakings have not ordered and for us I am not saying we are not doing state transport undertaking, we are doing state transport undertaking. They form a very, very important component of our overall bus portfolio, but we are also focusing on the private sector and providing solutions for that. We have still to utilize the opportunity in the school bus segment, so we are very positive on the Sunshine school bus that has been launched last year, which has secured lot of positive traction. You will know that it is an India's first rollover protected front end crash protected bus absolutely safe for school children. We are also trying to see what we can do with the Oyster range of buses that has been launched in Middle East, which has been comparable in terms of fit, feel and finish and NVH with some of the global players, we have done blind testing of these buses also and nobody was able to differentiate. In fact, they thought our buses were so far superior, but having said that the focus very clearly on the entire bus strategy is to look at how do we capitalize on the fully built regulations that are coming in, how do we make deeper inroads into the private sector even as we tender for the profitability let us put it that way.

**Saurabh Kumar:** But STU order should come back next year you think?

**Gopal Mahadevan:** I think they should. I think there was a little bit of gap. There was a lot of funding that was not available. Most of the STUs are bleeding by the way. So, they do not have funds. So, in fact we have pitched some other alternative methods of even financing, but it is difficult. I appreciate from their perspective it is a government institutions that it will a little bit of time. There are works around that are possible for STUs to invest into fresh buses, so we are working with some of them.

**Saurabh Kumar:** Sir, just a breakout of revenue if you can?

**K.M. Balaji:** Revenue as far as the domestic MHCV trucks and buses are concerned, it constitutes 75% and exports MHCV constitute 10% so all these three put together constitute 85%, the rest 15% is from LCV spares, defence, Power solution business and foundries.

**Saurabh Kumar:** Thank you.

**Moderator:** Thank you. That seems to be the last question for today. I now hand the floor back to the management for their closing comments.

**Gopal Mahadevan:** Thank you very much for participating in the call. I know that there were lot of people and one hour was not sufficient. We can extend it next time onwards because I am just rushing to airport to catch the flight, but all I can tell you, ladies and gentlemen, the management is putting its best efforts in augmenting growth both in the domestic and export markets. As we are much focused on our cost, we have taken a lot of them over the past three to four year, but we are very particular about it. We will continue to hang on to our working capital because we believe that, that is the best way to do business, while we will have to invest in capex over the next three, four years, believe me they are not going to be lumpy capexes, which we are going to see that will crease our brows. Overall, it looks that 2018–2019 should also be positive. So, we are preparing ourselves for that internally. Our trust on the auto market revenues and the exports, LCV and defense, will continue. Wishing all of you the very best.

**Moderator:** Thank you very much. Ladies and gentlemen, on behalf of Emkay Global Financial Services that concludes this conference. Thank you for joining us. You may now disconnect your lines now.