"SKF India Limited Q1 2019-20 Results Conference Call"

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Moderator: Ladies and Gentlemen, Good day and welcome to the SKF India Limited Results for Q1 2019-2020 Earnings Conference Call. 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 '*' and then '0' on your touchtone phone. Please note that this conference is being recorded. I would now like to hand the conference over to Ms Mallika Apte – Head (Country Communications). Thank you and over to you, ma'am.

Mallika Apte: Thank you. Good Morning. Thank you all for joining the call today. We have Mr Manish Bhatnagar – Managing Director SKF India and Mr Anurag Bhagania – Director (Finance), SKF India on this Earnings Call.

Before I begin, I would like to mention a short cautionary statement. Some of the statements made in today's earnings call maybe forward-looking in nature. Such forward-looking statements are subject to risk and uncertainties which could cause actual results to differ from those anticipated. Such statements are based on management beliefs as well as assumption made by and on the information currently available to the management. The audience is cautioned not to place undue reliance on these forward-looking statements and making any investment decisions.

The purpose of today's Earnings Conference Call is purely to educate and to bring about awareness of the company fundamental business and the financial quarter under review. I will now hand over the conference to Mr Manish Bhatnagar who will discuss the Highlights of Q1 2019-2020 Results for SKF India. Thank you, over to you Manish.

Manish Bhatnagar: Thank you Mallika and good morning everyone who is on the phone. This is a bittersweet call for me personally only because this is Chandramowli' s last call with us, it is also his last week at SKF. We have of course Anurag Bhagania, who has joined us as the CFO. He has been here a month and a half and he will address most of the questions which in the past have been addressed by Mowli.

On behalf of everyone on the phone, I do wish Mowli all the best, but of course, we look forward to his guidance as we move forward. But with that brief introduction, you have seen the results we announced yesterday for Q1 I am sure you have gone through the numbers in great details I will not dwell upon those. We will go straight into questions and answers.

Moderator: Thank you very much. We will now begin the question and answer session. The first question is from the line of Nishit Jalan from Kotak Securities. Please go ahead.

Nishit Jalan: Sir can you can give more colour on how is the segmental performance in terms of auto OEM aftermarket in industrial segment, in terms of growth that we have seen or decline that we have seen in this quarter?

Anurag Bhagania: As you know the context for auto and overall industry as such. It has been a bit of downward spirals starting from beginning of the year. Our results pretty much reflect what is happening in the industry. Automotive, over all in terms of our total revenue this quarter makes up about 38% of our total revenue whereas industrial is about 53%. As you perhaps would have guessed automotive overall including distribution, is actually down 8% year-over-year corresponding same quarter last year, but there is a little bit of goodness remaining on the automotive distribution market which has grown about 5%, but automotive OEM is actually down about 14%.

Nishit Jalan: And what about industrial segment sir?

Anurag Bhagania: Industrial overall we have seen it is a mixed bag with about 9% growth, but there are some of the sub-verticals are actually growing faster than the rest, particularly wind which is part of our energy segment, which has had some significant growth. Railways if you compare it to the last year same quarter is not so much of a growth, but really if you compare it to the previous quarter that definitely has shown about 22% growth over the previous quarter. When I say first quarter of 2019, I am talking about January through March of 2019.

Nishit Jalan: Sir what are you sensing on the Railways freight side, have you started to see any action in terms of ordering for DFC and you being a new entrant into that segment. How are you placed in terms of getting orders in that space?

Manish Bhatnagar: We are working with all the manufacturers of freight wagons who have either won contracts for the DFC or are in the process of bidding for those. All of those builders know us well and we know them well. We have already got a couple of orders and the rest are in the pipeline. Overall as Anurag mentioned much of the Railways growth, we believe, will be driven by the freight growth in the future. And you rightly point out DFC is one part of it, but there are also other freight expansion plans for the Government.

Nishit Jalan: Sir my second question is on other expenses if I see the other expenses are down about 8%- 9% on a YoY basis, just wanted to understand is it purely driven by our cost efforts or there is some impact of lease accounting changes that we have seen under indices as well?

Anurag Bhagania: The lease accounting changes do not have a significant impact, actually to be precise, no material impact on the expenses. What you see as other expenses being down year over year is primarily a result of actions around our cost efforts. In fact, our other expenses also has an element of foreign exchange loss in the quarter which in the corresponding period prior year is actually a gain which is sitting in the other income. So, net-net yes it is a result of good cost actions and one of the biggest cost actions I would say is really control over past due receivables, the quality of receivables has started to show some signs of improvement which is why you do not have provisions for bad debts.

Nishit Jalan: Sir is it possible for you to quantify the FOREX losses that you had in this quarter?

Anurag Bhagania: The FOREX losses this quarter is about 41 million as compared to a gain of around 20 million corresponding prior year same quarter. So, the net-net change is about 61 compared to last year.

Nishit Jalan: Sir my last question is on the CAPEX plans last quarter you had highlighted that you are looking at about 100 to 150 crores kind of a CAPEX, but given the kind of slowdown that we are seeing in autos are you going slow on that and also last quarter you had highlighted that there is some localization plan also that you plan to undertake in the industrial segment, so if you can give more colour on that it would be very helpful.

Manish Bhatnagar: Yes, I think a CAPEX plans, you know we sincerely believe and I am sure you will share my belief, that the India growth story is intact the timing may be changed by couple of quarters based on what we are seeing right now. Any CAPEX we do the gains come to us after a couple of quarters which is a lag between investment and returns. So, our CAPEX plans as we spoke about in the previous quarter calls are still on track the timing may get shifted by one or two quarters depending on the line or the product, but they still remain in line with what we have spoken in the past.

Nishit Jalan: Sir any colour on the CAPEX to increase localization on the industrial segment?

Manish Bhatnagar: In our industrial segment we are always looking at plans to localize. At this minute I cannot share with you of course in terms of how much we localize by when, but certainly the trend is to localize more and more every quarter. We have done more localization in this quarter than previous quarter, we will do more next quarter etcetera that is a trend that we foresee for the future also.

Moderator: Thank you. The next question is from the line of Sandeep Tulsiyan from JM Financial. Please go ahead.

Sandeep Tulsiyan: My first question is pertaining to the individual growth rates in each of the sub segments like passenger cars, two wheelers and tractors and CVs if you can share that?

Anurag Bhagania: Sandeep by and large I think we are seeing similar trends across the different sub verticals in the automotive OEM space, but if you really want a deeper split I think cars and trucks are high single-digit early double-digits, tractors we are about a little higher double-digits degrowth as compared to last year. Overall, the entire automotive OE space is down about 14%.

Sandeep Tulsiyan: Okay so cars and trucks is high single-digit, or a double-digit decline right?

Anurag Bhagania: That is right.

Sandeep Tulsiyan: Secondly, I wanted to understand and there is two wheelers in that would be again what kind of a decline?

Anurag Bhagania: Two wheelers roughly around 14% to 15% down to be precise 14% down versus same quarter last year.

Sandeep Tulsiyan: Second question is on the Railways portfolio that we have. As in the share of freight bearings is now increasing with order on the class K bearings getting finalized, if you could just broadly help us understand the current mix between freight, non-freight and locos for SKF and how do you see this mix panning out and say in others three years' timeframe?

Manish Bhatnagar: This is we have spoken about this in the past Railways market is about and I am talking the market here is about 40% freight, 40% passenger and 20% loco. Traditionally as you know our strength has been passenger and loco. On the freight side we have had a lower share which we are now rectifying through approval of our bearing you mentioned K class etcetera. Of course someone haD asked the question earlier on the DFC tendering. So, we certainly expect the railway growth to be driven by freight. Our share in freight today is single-digits and we hope to increase it at par with what we have in the other segment. Of course, it will take time to get there, but that is our intent. We are also in the process of starting to localize some of these bearings in India. So, you will see some benefit from there too.

Sandeep Tulsiyan: My final question is towards the net working capital cycle. I did see the other income has come down which you mentioned partly you do absence of FOREX gain and also their lower cash because we did a buyback in previous quarter, but is there an element of higher working capital deteriorating our balance sheet or cash balance in any way?

Anurag Bhagania: I would not say that I think your first two hypothesis is more appropriate Sandeep the lower cash levels because of the buyback is driving lower interest income and of course the foreign exchange loss.

Sandeep Tulsiyan: One more point if I can harp on this other expenditure. You did mention there is a FOREX loss component there despite which we have shown a tremendous reduction in this particular line item, if you could help us understand the quantum of decline other than bad debt what you mentioned which has seen a material reduction over here and is it more permanent in nature or more transitory for a quarter?

Anurag Bhagania: The way you should read this is first to understand we had degrowth in the automotive space right and therefore there is a lower level of production and there is an implication to the expenses to that extent. So, we are producing 14% lower in our factories compared to last year same quarter. So, that definitely there are certain fixed cost obviously you cannot do much about, but there are variable cost which we definitely are flexing so that takes the expenses down. In addition to that, we have some more strategic actions which are permanent in nature taking cost out and some are one timers like the provision for bad debts and foreign exchange that we talked about.

Moderator: Thank you. The next question is from the line of Vimal Gohil from Union Mutual Fund. Please go ahead.

Vimal Gohil: I would just like to have some more colour on the segmental revenue if you can just highlight what has been the growth in the industrial OEM and the replacement side?

Anurag Bhagania: **T**he way we talk about our OE and aftermarket is roughly a 50-50 split between OE and aftermarket in terms of industrial. So, if you further deep dive really the energy is and particularly renewable energy has a segment is actually doing good for us, but bear in mind that it is coming of a very low base in the last year and therefore the growth looks all exciting. The good part though is, it has also grown compared to the last quarter just the previous quarter. So, there is about 23% growth over the previous quarter and about 100 plus percentage growth over the last year. By and large, I think the other segments are either flat or have marginally grown with the exception of Railways which is flat to the last year, but grown 20% over the previous quarter. Distribution is been a bit of upside for us continuously it is growing about 10% over the last year.

Vimal Gohil: Would it fair to say that the industrial OE would have in totality would have grown at about 7% to 8%?

Anurag Bhagania: That is right it is about 8%.

Vimal Gohil: Second question was on the CAPEX given the fact that you are still looking to localize more on industrials, but autos as a segment has not been firing, so what would be the absolute CAPEX number that you are looking at in FY20?

Manish Bhatnagar: Our CAPEX number typically is ballpark 80 to 120 or 80 to 130 crores a year and it is tough to give you an exact number what you will do this year, but that is the ballpark number you can take.

Vimal Gohil: Sir how has been the off take on the Hub 3 bearings been for us this quarter?

Manish Bhatnagar: The Hub 3 bearings that line as you know is fully operational. We have a couple of customers who are waiting for the bearings, we have finished the first trial run last month. We are awaiting results of that trial run testing by the OEMs and we hope to start full production sometime in this quarter.

Vimal Gohil: So, hub 3 bearing are still not getting reflected in the sales?

Manish Bhatnagar: No.

Moderator: Thank you. The next question is from the line of line of Adit Shah from Vibrant Securities. Please go ahead.

Adit Shah: We see here that we have reduced our import of raw material from our 40% around 2011-2012 to right now 20% am I right?

Manish Bhatnagar: Yes.

Adit Shah: Is there any possibility of further import substitution or is it that entire 20% will remain you cannot get that 20% raw material from within the country?

Anurag Bhagania: I would like to understand where you are picking those numbers from the imported raw material where do you see that from now?

Adit Shah: No, I am asking is it 20% right now?

Anurag Bhagania: I do not want to comment on that number, if it is not out there, but I would say our trading volumes have gone up significantly over the prior year as well as the prior quarter because of the context of our business. There is a manufacturing plant which serves mostly automotive customers and then as far as industrial is concerned we serves from our local factories. At the same time, we also import and sell that mix has gone up this quarter compared to last year at least by about 5 percentage points in terms of the mix which essentially reflects in lot more traded products both finished goods purchases and that is what is pretty much reflecting on the material cost increases too.

Adit Shah: So, what have been the driver of this increase in gross margin from the traded portion because we see an increase in the gross margin even though the traded portion has increased your gross margins have also improved, so is it that industrial aftermarket is increased or you are selling a product mix has become better?

Manish Bhatnagar: Adit I am absolutely uncertain. Mowli you would like to answer that question I do not know where those numbers are coming from.

Chandramowli Srinivasan: So, this is a factor of different things one is the mix between OE and aftermarket. Within OE again you know that there are different segments which have different price levels in the market the wind being the most competitive one etcetera. So, it is a factor of different things, currency movements have a different thing as well, price levels that we have achieved in the market is also something. So, when you compare the same quarter last year to the same quarter this year there are lot of factors that have gone into making the gross margin, as you call it, look better. However, remember that there is also selling and administration expenses which you do not see separately. So, it is not right to only compare the gross margin at this point of time. It is a mix of OE aftermarket and the split within OE of the different segments.

Moderator: The next question is from the line of Vipul Shah an Individual Investor. Please go ahead.

Vipul Shah: Can you give the contribution of service business?

Manish Bhatnagar: Vipul we do not break out services separately from our numbers we do not report it that way as a business line, but suffice it to say that and I want to be clear when you say services be on the same page what we mean by services. When I talk of services, I mean what we call rotating equipment performance services. Directionally today that business is mid-single-digit contribution to our total revenue.

Vipul Shah: And where do you see two, three years from now?

Manish Bhatnagar: I wish I had that crystal ball and I could predict the future, but my aspiration and my ambition and share by the company is to get to about early 20s.

Moderator: The next question is from the line of Rajesh Kothari from Alfa Accurate Advisors. Please go ahead.

Rajesh Kothari: Sir what is the total replacement within industrial segment, what is the growth on that?

Manish Bhatnagar: I think you just said it is about 10% in the industrial aftermarket.

Rajesh Kothari: And that is about 50% of your total industrial revenue, right?

Manish Bhatnagar: That is right.

Rajesh Kothari: And you mentioned that the traded goods components has increased significantly, can you elaborate on that because even if I look at last year full year the traded goods was close to about 800 crores compared to previous year of about 670 crores, so just trying to understand that what kind of a mix results into more traded goods- question number one. Question number two do you have gross margins little bit better on traded goods if you can give a little colour on this?

Anurag Bhagania: Rajesh I think the numbers that I look at is 41% came from traded goods same quarter last year which is now gone up to about 46% so there is a 5-percentage point improvement. Traded goods overall in terms of our revenue has grown 14% year-on-year. I do not think we are out there stating our margin levels at between traded and manufactured, but I think just by the virtue of what we do in traded we just buy, and we sell. You can assume that we cannot extract a very high level of margin there almost the entire cost of our procurement is sitting as cost of material and therefore we end up getting anywhere between 15% to 20% margins.

Rajesh Kothari: 15% to 20% you mean at the gross level?

Anurag Bhagania: That is right.

Rajesh Kothari: And what results into this kind of a significant change what the segment if it grows at higher level, then your mix will change like this?

Manish Bhatnagar: The industrial segment, if you have been following us for some time, you know a lot of our industrial products are not manufactured in the local factories. So, with the automotive sector declining as Anurag mentioned an industrial showing better growth. If we are selling more industrial, we are importing more industrial and therefore we are trading in that.

Rajesh Kothari: While of course it is very difficult to give outlook, but any early indications apart from hope which everybody of course has on second half , from your perspective how you are reading the economy?

Manish Bhatnagar: I will not give any forward guidance in SKF, but I can give you my sense of the economy and you can make your judgment from that. The automotive sector at least from our perspective based on our interaction with customers and with suppliers seems to be in the down cycle where today we do not know where the bottom is. The next trigger point for the automotive up cycle to start, if it does, is the festive season in end October early November. If we miss that trigger point it moves on to Q1 2020. On the industrial side we are seeing capacity utilization rates inch up to upwards of 75%, 76%. Historically as you know at that utilization level that is when factories start getting almost fully utilized and private CAPEX starts kicking in. So, we expect that industrial private CAPEX to kick in earlier I believe than the automotive up cycle. When that will be, I do not know it is also linked to funding, infrastructure etcetera, but in summary I expect industrial CAPEX to pick up in the next three or four months automotive little after that based on what we see today.

Moderator: The next question is from the line of Prachi Kodikal from Bay Capital. Please go ahead.

Prachi Kodikal: My question was related to Railways so I would like to understand what is our current arrangement for the railway bearing, is it similar to the industrial ones where they are importing everything and then distributing it in India?

Manish Bhatnagar: It is a combination of both- we import some, and we make some locally.

Prachi Kodikal: Earlier you also mentioned that we make 15% to 20% gross margins on the traded goods which is the industrial side, so do these margins vary depending on whether they are imported or locally manufactured by us here in India?

Manish Bhatnagar: Yes they vary.

Prachi Kodikal: And just one last question how have the export fared this quarter?

Anurag Bhagania: So, exports have been a little bit of a positive support for us if you may call it that way actually automotive has been significantly down and we are wanting to pull any opportunity from our various global operations that we have to support our production levels in the factories. Export grew about 24% year over year and 65% quarter over quarter, making up about 9% of our total revenue now as compared to what it was 5% or 7% in the previous period.

Moderator: The next question is from the line of Priya Ranjan from Antique Stock Broking. Please go ahead.

Priya Ranjan: Couple of things on industrial side. When we talk particularly on Railways when we talk about the 40-40-20 mix in terms of freight, passenger and locos and you mentioned about single-digit share in freight, so what can be your share in probably in passenger and loco side that is question number one and second is on the when you see that the passenger side also the government is trying to move towards LHB fully, so what kind of opportunity and what kind of I mean content share we can increase in that segment?

Manish Bhatnagar: I have made this comment at one to one investor meetings in the earlier conference call. I will answer your question of course Priya, but I do want to make the comment that we spend a lot of time on these calls talking of things like the Railways, Hub 3 etcetera. You have to understand that unlike some of our competitors Railways is not a big driver of our revenue of growth. I think you may be biased by what you hear from other bearing manufacturers and that is all right, but I do want to make the point that we are very diversified company across segments, across industries and so we sometimes tend to spend lot of time on things that are common to bearing companies which maybe relevant for them and not for us.

But having said that let me answer your answer on the railway side you are right government is moving from conventional coaches to LHB coaches. We have a good share in the current conventional coaches there are not necessarily adding new capacity on the passenger side but the replacing coaches. So, to that extent because we have a good position of strength on the conventional coaches we will automatically get first choice on the LHB coaches. And on the locomotive side likewise we have very good share not much change happening there, but we are well entrenched there on the freight side, I talked of earlier.

Priya Ranjan: And just on the wind side I mean I guess the order is driven by ZF for the entire industry, so when do you see this ZF thing can peak-out in terms of their ramp up or their exports from India?

Manish Bhatnagar: I can answer from our perspective only, and that is as Anurag mentioned our wind sales picking up and again I will make the same comment wind, Railways Hub-3s are not drivers of our business, but since you asked the question I will answer it. Today our wind sales is depended on export orders or gear boxes from India. Based on our interaction with our customers we see that cycle playing for at least three or four quarters more.

Priya Ranjan: And any green shoots you look into the process industry like cement, steel, etc., where you have mentioned that probably the capacity utilization rate is now inching up around 75%, 80%?

Manish Bhatnagar: I think more than just green shoots I think we are seeing clear growth in all the four industry. So, heavy industries you mentioned cement, steel, all infra-linked industries we have been seeing good performance there. That is expected to continue with the continued push towards infrastructure spending by the government.

Priya Ranjan: Between PV, two-wheeler and CV and tractors how is the automotive revenue is split at this point of time?

Manish Bhatnagar: Most of our revenue today is two wheelers and the rest is split between passenger and commercial.

Moderator: Thank you. The next question is from the line of Akshay Bhor from Premji Invest. Please go ahead.

Akshay Bhor: My question is on the automotive aftermarket growth from last quarter of 17% down to about 5%, just wanted to understand is this to do with destocking of the dealers, distributors end as it also to do with pickup in the end markets?

Manish Bhatnagar: It also a comp here Akshay, the 17% was an easier comp compared to the 5% this quarter.

Akshay Bhor: But what should be a more sustainable number to look at I mean this ideally should be a more stable business what kind of number should be?

Manish Bhatnagar: The number should be between 10% and 15%.

Akshay Bhor: Second thing is on the industrial business which is more in a high lead time business you would have some sense of next two, three quarters how you sort of look at in terms of your end markets, do you think that 10% kind of growth is more sustainable growth going forward as well?

Manish Bhatnagar: It depends on the segment and the vertical. Overall, the industrial segment we colour it with the same brush, but as you know Akshay, there are many different sub-segments in that. We believe the infrastructure led segments. You mentioned a few of those earlier on will continue to drive growth for the industry and certainly for us. We believe that the consumption led industrial segments will lag behind the infra segments. So, process industries, F&B, etc., will lag behind it and specifically on wind and Railways we have already talked about.

Akshay Bhor: Third thing on gross margins I know there is a bit of a change in the mix between industrial and autos, but have you started seeing any benefits of steel prices coming through did not sort of reflect in your gross margins in my opinion?

Anurag Bhagania: You are right you know there are some positive signals of steel price improvements in second quarter and when I say second quarter, I am talking about the quarter that we reported out. We see about 2% to 3% softening in the steel prices and maybe about 50 to 60 basis points in our material cost.

Akshay Bhor: This quarter you mean you already saw benefit of that?

Akshay Bhor: That is right.

Akshay Bhor: In your 2018-19 annual report the traded goods margin is up significantly from about 13%, 15% range that you had for up several years up to 19%, any reasons for that and is this like more sustainable, how should we read into that?

Manish Bhatnagar: Help us understand your question- point us to the annual report page number you saw this.

Akshay Bhor: I do not have the annual reports in front of me, but what I can tell you is the traded goods margins has gone up from 13% to 19% which was pretty much steady at 13%, 14% range for several years, is there a reason why that could have happened in the last year. We are looking at the gross margins.

Chandramowli Srinivasan: As I explained earlier also to your earlier questions it depends on the mix of sales that happened when it comes to traded goods and last year wind was down and we see the wind improving in the current year only not in last year. So, last year wind was much down compared to the previous year and wind is one of the parts of the total traded goods portfolio. So, when a lower margin business comes down then automatically the profitability of the other parts which remains in the pipe, they pull their overall average up that is one reason. The other reason is that in the previous quarter for the one quarter of the previous quarter the sales numbers were inflated and the cost of goods sold were also inflated because that was a the pre-GST era so you had the entire custom CV duty is sitting in your both sales and cost of goods sold whereas in the year '18-19 you had the full impact of top line and cost both not having the CV duty element. So, that also improves the margin as a percentage.

Moderator: The next question is from the line of Vimal Gohil from Union Mutual Fund. Please go ahead.

Vimal Gohil: Sir I just wanted to understand what is the reason for the flatter growth in Railways because we have been talking of lot of expansion on the freight side and lot of initiative will be taken on the Railways, so just wanted to understand why has not Railways grown on a YoY basis that would be question number one I have a follow up after that?

Manish Bhatnagar: First of all, certainly we can do a lot better in the Railways whatever the growth number is I agree with you and I am empathize with your comment that we should do a lot more. Keep in mind that we have a very good share on passenger and loco. We have a low share on the freight side so at least our growth will be driven on the freight side. On the freight side while you may think the DFC is doing well, there is good demand here and you as well as I know that DFC has been slow to take off here. It is only now in the last three or four months that we are seeing tendering of DFC wagons. So, to that extent there is a lag between the intent of the government to get into freight and expand that and actual reality on the ground which comes to us in terms of new orders. So, we are well-prepared for freight now. Our bearings have been approved by the Railways after a long process and as and when that intent becomes reality, we are well-positioned to gain share in freight and therefore expand a Railways business.

Vimal Gohil: The second question is on the traded goods you said that the traded goods in Q1 FY19 was at 41%, right?

Manish Bhatnagar: Q1 FY19 meaning just the quarter that concluded. The same corresponding quarter last year was about 41% it is now about 46%.

Vimal Gohil: So, this is despite our localization efforts to increase localization in industrials?

Manish Bhatnagar: Yes, that is right.

Vimal Gohil: But it would be largely because of the auto market slowing down? Or would my assessment be right?

Manish Bhatnagar: Rephrase the question.

Vimal Gohil: Because of the localization increasing I would have expected that the traded goods mix would have shifted towards manufacturing, but that has not happened.

Manish Bhatnagar: Yes, so you have differentiated between the absolute number and the relative number. In absolute term yes as we localize more, we sell in an absolute number, we would sell more, manufactured versus traded and that is slowing inching out and you are referring the percentage basis here with automotive slowing down the mix changes and therefore even though the absolute number goes up the mix becomes adverse.

Anurag Bhagania: And I would also like to clarify that when we say traded, we are not talking about imported. If a SKF subsidiary in India is manufacturing which is not part of the listed entity that is also traded. So, if you know, our industrial business also buys from the SKF Technologies the Ahmadabad plant which is part of the traded good.

Vimal Gohil: My next question was going to be that how much have we procured from SKF Technologies this quarter?

Anurag Bhagania: I do not have the exact numbers right now here with me, but I think that mix is improving at least for the quarter that I see there is about 30%, 40% improvement in the quarter because the focus of that factory has always been railways and winds and therefore we see an upside coming there.

Vimal Gohil: How much of our revenues or volumes would be coming in from transmission-led bearings for four wheelers and two wheelers you can put it together no problem?

Manish Bhatnagar: Most of the bearings in auto sector that we sell is on the wheel end.

Vimal Gohil: A very little is coming from the transmission ones?

Manish Bhatnagar: Let me say "little" I would not say very little but little.

Moderator: Thank you. The next question is from the line of Gautami Desai from Chanakya Capital. Please go ahead.

Gautami Desai: About 24 days of July gone and you would have them inside on the order position also, so can you comment on whether the stop is near or you know July month was slightly better than the June month so what is the trend that you are seeing?

Manish Bhatnagar: I think I will not get into specifics because we do not want to get into guidance here, but I think you read the papers as much as I do. The automotive sector continues to slow down. We have not seen any good news coming out of it in the first 24 days of July also. So, automotive being 38% of our business we are tied at the hip with the fortunes of that industry. On the industrial side we continue to see growth in line with what we have seen in the past.

Gautami Desai: But in industrial also there has been a slowdown right so my point is even on the industrial side is July month slightly better than June or is it like same or is it worse?

Manish Bhatnagar: It is not worse than the previous months.

Moderator: Thank you. The next question is from the line of Viraj Kacharia from Securities Investment Management. Please go ahead.

Viraj Kacharia: I just had one question you talked about service share being single-digits and ambition to take it to 20% or above what will drive that?

Manish Bhatnagar: What will drive the increase in share?

Viraj Kacharia: Yes.

Manish Bhatnagar: That is an easy one to answer that is really depends on the value proposition we offer to customers and our ability to sell that to customers which we are very confident in. What exactly is REP? Rotating equipment performance is nothing else, but creating value for customers through ensuring reliability, integrity and efficiency of their rotating assets. Customers frankly care less about what they are purchasing from a supplier like us, but what does they do for their asset and if we have skin in the game in terms of ensuring reliability of the asset there would be willing to share that value creation with someone like us. For example, in up time increase from 90% to 91% may seem only a 100-bps increase in uptime, but it has significant impact in terms of profitability for customers and if we are able to gain some share of that increased possibility that is what will drive our revenue increase in REP.

Viraj Kacharia: How should one understand the scale up and, in that sense, also the profitability in this because what I understand eventually we might be moving to something like more of a deferred payment or a milestone based payment kind of a model as we keep on scaling up this particular aspect?

Manish Bhatnagar: So, we have yet to clearly define what will be the exact revenue model here. We have multiple models that we are piloting right now not every revenue model is referred. Some are monthly payment models, some are deferred payment models, some are performance-based model, etc. So, that revenue model is being worked on and we will hopefully have moved to share with you soon.

Viraj Kacharia: And based on initial results or initial pilot offering which are done on the metal and cement side for example which you gave yesterday what kind of profitability this offering would have?

Manish Bhatnagar: Today it is a little lower than our current profitability, but simply because we are investing in resources to launch these services. At steady state when it does get launched fully it will certainly be higher than our current profitability of the businesses.

Moderator: Thank you. The next question is from the line of Ashi Anand from Allegro Capital Advisors. Please go ahead.

Ashi Anand: Just wanted to understand how our content per vehicle would actually move as we move from BS-IV to BS-VI and also eventually towards electric vehicles? I wanted to understand this both one for the bearing industry at an overall level and I think you had mentioned earlier that we have moved the wheel bearing paths. So, one for the bearing industry how does it happen impact and for SKF specifically?

Manish Bhatnagar: I will answer both those questions in one I will try and at least answer both in one. Whether we move from BS-IV to BS-VI or we move from internal combustion to EV the number of wheels on a car will not change. They still remain four wheels or two wheels in a two wheeler and since a large part of a business is linked to the wheel and bearing application we are less impacted by these changes than other players might be. But having said that any change in emission would also need lower friction bearings, lighter weight bearing, etc. So, to that extent we constantly need to innovate to make sure that we are supplying the bearings of the customer needs for these new transition there.

Ashi Anand: If I look at a bearing industry level would it have a larger impact especially as you are moving towards the electric vehicle would it be fair to see that the bearing industry could shrink quite significantly possibly or not so much?

Manish Bhatnagar: Well the bearing industry on the power train once you move from current bearings of the current engines of electrification of the power train, we expect the bearings to get to come down in number you are correct, but the type of bearing will change. So, we expect the industry to move towards other materials in bearings for example hybrid or ceramics bearings. These bearings are not cheaper than our current bearings. So, if the number of bearings comes down by certain number the price per bearing will go up and certainly from our perspective the value of bearings in that vehicle will not change, the numbers might change.

Ashi Anand: Would there be something similar happening on the wheel side because we are speaking to some tyre manufacturers recently and they have kind of spoken off as you moved with EV the tyre is actually making the biggest noise, so would there be substantial changes in type of wheel bearings or not really?

Manish Bhatnagar: My comment earlier on was on the number of bearings. The number of bearings are unlikely to change well pretty sure they will not change the type of bearings might change.

Moderator: Thank you. The next question from the line of Chirag Shah from ICICI Securities. Please go ahead.

Chirag Shah: Sir I just had a very broad questions because whatever your commentary you have made on the concall till now seems that private sector CAPEX and infra-led CAPEX rather than consumption CAPEX will take over from here on and if that plans out probably the share of industrials will bump up in your overall portfolio, so what would trigger up putting up a capacity of industrial bearings itself in India rather than getting it imported or trading it from your sister concerns?

Manish Bhatnagar: I think irrespective of what is happening today or what will happen tomorrow, infra consumption etc., our stated strategy or stated goal is to localize industrial bearings as much as possible of course you realize that industrial bearings are very different from automotive bearings. In automotive bearings you produce one SKU and you produce a separate channel and you produce millions of them and it gets pumped out in the OEM with no problem. On the industrial side the assortment is much wider, the volumes are much smaller, so one has to take a look at projections by segments, by SKUs to see what we will localize and what we will trade that exercise is always ongoing and as and when we forecast that a volume for a certain type of industry or SKU warrants localization we will do that as we have been doing in the past.

Ashi Anand: If you can just quantify as in which say segment particularly X, Y, Z grows his revenue grow or his visibility is up by 4x or 5x or probably the revenue of the industrial segment per se goes up to 3,000 odd crores from 1,500 crores then the plant would be visible, sir any such kind of figures that you have in mind?

Manish Bhatnagar: Yes for example we have one segment what we internally called Drives which is pumps, motors and gear boxes. These typically need, and if you are familiar with bearings, what we call DGBB Deep Groove Ball Bearings. These are smaller bearings small DGBB then medium DGBBs. We certainly expect those to get localize faster then let us say larger bearings where the volumes are not that large.

Ashi Anand: And sir what would be the target for your industrial bearing localization say over next three years?

Manish Bhatnagar: I don’t want to give you a target for three years I can certainly point you and this is public information for SKF globally the mix of industrial and automotive is 70-30. I am not saying we will get there in two or three years I am giving you the global SKF breakup of industrial automotive.

Moderator: The next question is from the line of Achala Kanitkar from Birla Sunlife. Please go ahead.

Achala Kanitkar: I just wanted to understand what would our current capacity utilization be now in auto and industrial?

Manish Bhatnagar: Mid-60s.

Achala Kanitkar: And what were they last year?

Manish Bhatnagar: A little higher than about two or three points higher.

Achala Kanitkar: In autos as well sir?

Manish Bhatnagar: I am talking autos only because most of our production in India is for autos.

Moderator: Thank you. The next question is from the line of Priya Ranjan from Antique Stock Broking. Please go ahead.

Priya Ranjan: Just couple of things one is on the raw material side you mentioned that there is a steel price correction and it has been reflected in the RM benefit as well, so what about the pricing I mean do you see that because of the correction in steel prices in the market do you see pricing behavior of customers is going to change and you will be kind of pressured for lower price realization going ahead I mean and what kind of price reduction can happen in different segments?

Manish Bhatnagar: Let me rephrase the question are you saying that when the steel prices start softening will we expect customers to push back at us on prices?

Priya Ranjan: Correct.

Manish Bhatnagar: Customers will do their job they will push back at pricing with a steel prices go up or go down anything can happen that is part of their job. Our job and our sales teams job is to ensure that we get better realization for our efforts. So, it is a constant discussion, negotiation back and forth between our customers and us.

Priya Ranjan: My second question is on the Railways if I look at your approved plant from the Railways side I mean many of the plants are located outside India on the different class of bearings, so with the SKF Technologies do you see I mean that change in terms of the approved plant where you can import or where you can supply to the Railways is going to change drastically?

Manish Bhatnagar: When you say you can see most of the approved plants are outside India what do you mean by that?

Priya Ranjan: I mean typically railway also it is not only the supplier they also approve the plants and from where you can buy.

Manish Bhatnagar: But where did you get this information from?

Priya Ranjan: So, it is from railway.

Manish Bhatnagar: So, typically, in the past our Railways business has relied on our European plants for supplying in the country. The Railways also have a rule, I am paraphrasing here, I think is called the golden rule or something similar to that which basically means if the same company has a similar bearing in a plant outside India, the time for approval of the plant in India when they start making the same bearings is short circuited. So, one does not go through the full two year development cycle, but the cycle becomes much smaller. So, our SKF Technologies plant has now been approved as a replacement plant for the bearings that we have supplied from our Italy plants. That journey will keep continuing.

Priya Ranjan: And in terms of I mean has the government finally decided on the because in the K-Class bearing lot of developmental vendor status is still there I cannot see that, it is a non-conditional vendor status has yet come in?

Manish Bhatnagar: I am rephrasing your question . Is your question that has a government approved bearing manufacturers for K-Class?

Priya Ranjan: Yes. So, as of now everybody is on the developmental vendor status, nobody has got the non-conditional vendor status?

Manish Bhatnagar: Yes, and that goes back to my previous comment we keep talking about freight and DFC, etc. DFC and freight are also very tightly linked to K-Class bearing. So, you are right a lot of the vendors in India are still in developmental status and that will change hopefully very soon, but we will not see that freight from its become reality till all these things happened.

Moderator: The next question is from the line of Shyam Sunder Sriram from Sundaram Mutual Fund. Please go ahead.

Shyam Sunder Sriram: Sir you have been mentioning that when Railways are not major growth drivers for us, if you can just help us understand within the industrial how much is the broad contribution of wind, railways, steel, cement some broad ball park numbers that will help us appreciate your comments that you made earlier?

Manish Bhatnagar: SKF India as a whole the entity we are talking about wind is about 5%, railway is about 7%.

Shyam Sunder Sriram: And steel and cement sir?

Manish Bhatnagar: Steel and cement would be I do not have the exact number, but it would be around 10% to 12% each.

Shyam Sunder Sriram: And this would include the aftermarket as well is it?

Manish Bhatnagar: Yes.

Shyam Sunder Sriram: So, the aftermarket growth that we have been seeing that is primarily led by this steel and cement demand and the other infra related sectors is that right understanding?

Manish Bhatnagar: The aftermarket demand is driven mainly by industries where capacity utilization is higher than the rest.

Shyam Sunder Sriram: Such as.

Manish Bhatnagar: Certainly, cement for example, certainly steel.

Shyam Sunder Sriram: On the exports you mentioned we have seen very strong growth this is of course in our earlier comment you also said wind has been doing very well from an export perspective, so our export pie is at this point of time will be more of industrial wind-led pie, how will be the mix be there?

Manish Bhatnagar: I want to make couple of comments when we say exports from SKF India and when we say wind exports, we are talking different things. When we say wind exports it is selling to customers in India who are then assembling products for export from India at their end. That is not our export. What we are talking of the growth in exports is exports from the Indian factory of SKF India to other factories of SKF outside India; which is primarily automotive.

Anurag Bhagania: And that pie since you asked that question is about 9% of our total revenue number for this quarter.

Moderator: Thank you. The next question is from the line of Amar Maurya from. Alfa Accurate Advisors. Please go ahead.

Amar Maurya: In railways sir what would be your share of locomotives and passengers?

Manish Bhatnagar: It is higher than our share in freight.

Amar Maurya: So, like in freight we have single-digit.

Manish Bhatnagar: It is higher than single-digits.

Moderator: Thank you. Ladies and gentlemen due to time constraint that was the last question. I would now like to hand the conference over to Ms Mallika Apte for closing comments.

Mallika Apte: Thank you. On behalf of SKF India I would like to thank you all for joining us today in this earnings call. Should you have any other questions for the management please reach out to me with an email mallika.apte@skf.com. This is also mentioned in the invitation that was shared. Thank you again for joining and have a great day ahead.

Moderator: Thank you. Ladies and gentlemen on behalf of SKF India Limited that concludes this conference. Thank you for joining us and you may now disconnect your lines.

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