“SKF India Limited 2016 Year-Ending Earnings Conference Call”

May 30, 2017

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Moderator: Good day, ladies and gentlemen and welcome to the SKF India Limited 2016 Year-Ending Earnings Conference Call. As a reminder, all participants' 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 phone. Please note that this conference is being recorded. I now hand the conference over to Ms. Bibhabaree Biswal – Lead Corporate Communications at SKF India Limited. Thank you and over to you, ma'am.

Bibhabaree Biswal: Good afternoon everyone. Thank you for joining the call today. With us today we have Mr. Shishir Joshipura, Managing Director - SKF India Limited and Mr. Chandramowli Srinivasan , Director- Finance for SKF India Limited. I will now handover the phone to Mr. Shishir Joshipura to share the brief updates of the results. Over to you, sir.

Shishir Joshipura: Good afternoon and welcome to our first 12 months' year ending in March 2017. This was a very, very interesting year and as we all know was actually the hallmark event was the demonetization which actually played out full in the last quarter of the year. And we have at the back of that I think we still managed to get on a year-on-year basis 11% change in sales and operating income change of 16%. I think that is reflective of the efforts that we have undertaken. But clearly the momentum that was built during the year in 2016, I think demonetization did put some kind of brakes on that and I think coupled with the fact that we are going to have a GST roll out very soon.

In short term businesses are going to see some difficulties that they may have to churn out but overall in the long term I think we will start to see growth come back. I would be happy to receive your questions and provide clarifications and answer as the case may be.

Moderator: Thank you very much. We will now begin with the question-and-answer session.

The first question is from the line of Raghunandhan from Quant Capital. Please go ahead.

Raghunandhan: My first question was on the revenue mix for FY17. Sir, can you please share the revenue mix for FY17?

Chandramowli Srinivasan: Actually we are not so much I am sorry to say but we are still not so much on the 2016-17 kind of calendar year, we are still on quarter-by-quarter. So I will give you for the Quarter 1 2017. So our automotive business is about 40% for the quarter and exports which is primarily automotive is 9%. So if you add those two together you could say automotive is 49% and industrial is 51%.

Raghunandhan: And within the auto?

Chandramowli Srinivasan: Within the auto out of the 40% one third is aftermarket and balance is OEM and within the OEM you could say it is sort of almost equally between four wheelers and two wheelers.

Raghunandhan: And within the industrial, sir?

Chandramowli Srinivasan: Within the industrial OE is about 28% out of the 51% and the aftermarket is 24% out of the 51%, yes 27% and 24%; yes so almost little bit slightly higher on the OE side.

Raghunandhan: Understood sir. Can you also share the traded versus the manufactured mix?

Chandramowli Srinivasan: So for the quarter the traded is 41% and manufactured is 59%.

Raghunandhan: So traded has decreased as I remember the last quarter?

Chandramowli Srinivasan: That is right. In the immediate preceding quarter, it was 45% and 55% now it is 41% and 59%.

Raghunandhan: And last year, sir?

Chandramowli Srinivasan: Last year for the full calendar year was 44% traded and 56% manufactured for the full calendar year 2016. If you are comparing with Quarter 1 of last year then it was same, 41%, 59% same.

Raghunandhan: I mean for the March ended quarter the raw material cost has increased despite as you said, the share of trading has come off and even the Euro has appreciated whether there were any benefits of the Euro appreciation in the quarter?

Chandramowli Srinivasan: Well, actually it has changed marginally it is about 64.8% is our raw material cost if I add the excise duty also and it was 64.1% in the same quarter last year. That is as a percentage of sales. So that also depends heavily on the mix within the sales and some raw material cost increases we have started to see of course because steel prices have started to strengthen. So it is a mix issue as well as some increase in cost, yes.

Raghunandhan: And sir, any forex losses or gains in the quarter and in this line item?

Chandramowli Srinivasan: Yes it is very, very marginal. We had a small gain of Rs. 13 million against loss of Rs. 14 million in the same quarter last year. That means Jan-March 2016 was a loss of Rs. 14 million, this quarter it is a gain of Rs. 13 million.

Raghunandhan: An in which item does it reflect sir, other expenses?

Chandramowli Srinivasan: It could be in other expenses or other income because this is a bit of a problem for us, it does not remain consistently in one line every quarter depending on where it is and then the March quarter is always the balancing quarter so it sorts of skews it. I would like to see the other income and other expenses, these two lines taken together for any analysis because it just keeps shifting from one quarter to another and the March quarter is always a problem because it is a balancing quarter between the full year and the three quarters declared already.

Raghunandhan: My next question was to Shishir sir. Sir, which segments have performed strongly or weakly in the current quarter and what are the directional outlook you are seeing, what could be the drivers of revenue growth ahead?

Shishir Joshipura: Raghu, I lost the part of your question can you please repeat that?

Raghunandhan: Sir, which segments have performed strongly or weakly in the current quarter?

Shishir Joshipura: So we have seen for us especially the segments of car and trucks have done very, very well. We have also seen very strong growth for our industrial OEM businesses which is non-energy sector, I am not talking of the renewable energy other than that, railways has done very well for us. So railways, industrial OEMs we have seen trucks and cars these are four big segments that have done very, very well for us.

Raghunandhan: And sir, like on the railway segment specifically I mean how much is it contributing currently and how do you see the ramp up going forward directionally or if you can throw some more color in terms of what could be the expected revenues in FY18?

Shishir Joshipura: Raghu, in our case, one particular segment because our product line is so widely distributed, one particular segment would remain in the 6%, 7% of the total revenue range and that does not change much unless and until others do not grow and that is the only segment that grows. But that does not happen because our growth comes from multiple segments. So railways has been part of that growth story. And it has been at about 6% of our overall revenue.

But when I compare it to say this time last year then it shows me a decent growth over a period of time which was at that time around 4%, 5% of our overall sales mix and is about 6%. So from 4% to 6% is a decent shift as far as the railway business is concerned. And going forward also we expect railways to continue to be a very strong segment for us on different dimensions and I would not hazard a guess on what will be our revenue out of that particular segment. But it is important that we stay equally bullish on railways going forward as well.

Raghunandhan: Sir, can you share the CAPEX for FY18?

Shishir Joshipura: So as I had said in the past as well that we are likely to see a significant change in our CAPEX profile going forward so we are expecting that as we move forward we will be almost doubling our capital layout compared to our previous three years average over the next three years. So that is the broad plan that we can give to you.

Raghunandhan: And what could be the broad breakup of the CAPEX sir, expansion, new products how will it be distributed?

Shishir Joshipura: It will be a mix of both of course there will be new product lines which will call for new CAPEX but also expansion in capacity which will probably play it out on the latter half of the three-year period that I talked about and the initial first one and a half years it will be more around introduction of new product lines.

Raghunandhan: And what would be the utilization currently, sir?

Shishir Joshipura: So, we had mentioned this in the past that looking at our utilization level we believe that there is still a 20% headroom available for us to grow and I think now we have reached a stage where we are at about 10% headroom more to grow from the current status. Of course there could be some particular product line where the balancing may be required ahead of others, but on an average basis the 20% additional capacity is now down to 10%.

Moderator: Thank you. The next question is from the line of Nishit Jalan from Kotak Securities. Please go ahead.

Nishit Jalan: Sir, why do you mention on CAPEX or you are looking to double your gross block in next three years?

Chandramowli Srinivasan: No, I said that we will double our expenditure on CAPEX side compared to the previous three years average in the next three years.

Nishit Jalan: So previous three years average would be around Rs. 40 crores to Rs. 50 crores, right?

Chandramowli Srinivasan: Yes, so that will double.

Nishit Jalan: So you will do around Rs. 80 crores to Rs. 100 crores?

Chandramowli Srinivasan: Yes.

Nishit Jalan: Okay that is fine. Sir, just wanted to understand on the status on the third-generation bearings order that we have received. Have we started, have you commissioned the line, have you started delivering to the customer?

Chandramowli Srinivasan: We have commissioned the line but the deliveries as the process runs will start only on 1st of July. So that is when the commencement of the commercial deliveries will happen. In the meanwhile, the way the automotive industry goes so that samples and test runs and general audit and stuff that is going on. So we are now ready for it and it will start rolling in July.

Nishit Jalan: Okay. Sir, on the railways front you mentioned that you have done very well and it will continue to be a strong driver. Is it the traditional passenger railway segment that is growing for us, or is it that we have entered into the freight segment so that is the one which is driving growth for us?

Chandramowli Srinivasan: So the fact is that we have entered freight segment where we were not present so that is obviously contributing to the growth. But we are also growing equally strongly in the passenger side.

Nishit Jalan: So is it fair that the existing segments would also be growing in double-digits?

Chandramowli Srinivasan: Well, I cannot speak for the Railway Ministry.

Nishit Jalan: But I am saying your existing segments like passenger segment that is also growing?

Chandramowli Srinivasan: Yes that is what I am saying so I mean the indicators are that when things run in normal fashion, as India starts to modernize the railway network it will move in that direction that is what should happen.

Nishit Jalan: But right now, it is not growing in double digit, is it?

Chandramowli Srinivasan: No, it is growing currently. I am saying in future I do not know in the sense that it depends on what is the capital outlay for the Railway Ministry, I mean that is something that I cannot comment on.

Nishit Jalan: Sir, lastly last question from my side. I think you had mentioned sometime back that there are some pinion bearings for M&HCV that you have kind of received an order. So that has already started coming out in numbers?

Chandramowli Srinivasan: Yes, that has started. So as you can see the truck segment which was negative as an industry was negative in the quarter we have one of our strongest growth segments in that industry in the last quarter.

Nishit Jalan: Sir, is it something that in trucks we see a lot of imported bearings from Chinese players also coming in and has this kind of slowdown especially post demonetization or can it slow down further after GST?

Chandramowli Srinivasan: I hope so but it becomes difficult for other players to sell. But having said that I think what is important is we have decided that we will let the performance speak, so as we partner the industry for performance enhancement of their product lines. I think that is where we start to get the differentiation and then we do not have to worry about bearings from anywhere because then we have work on a customized solution for them like the pinion bearings that you mentioned earlier and that should continue to help us bill further.

Moderator: Thank you. The next question is from the line of Kunal Bhatia from Dalal & Broacha. Please go ahead.

Kunal Bhatia: Sir, just wanted to understand at the moment in case of railways what is the addressable market which we have in passenger as well as freight for SKF? And where do you see that growing because just wanted to understand are these new orders straight from the metro rail all that coming to you as well?

Chandramowli Srinivasan: So let me try and speak. So there are two segments for Indian Railways and Metro being the third one. Metro is the third segment. So two segments are passenger and there was a long distance passenger haul and the freight, okay. Traditionally we have been present and we have been very, very strong with the passenger segment of Indian Railway but as I had mentioned earlier as well, that we have also started to offer now products for freight application and it has gone through a process, it is a three-year process that you have to go through.

So if you ask me addressable segment of the freight side, we are still at only about 10% of the freight side that we are allowed to address. But that is changing, so between now and next 12 months that 10% will go to 100% of segment we can address because otherwise by law we cannot participate for more than 10% of the quantities that they buy for freight because the three-year period has to pass. So sometime next year this 10% will at least allow us to compete for the full scope. Today we cannot compete even if we have the best prices, the best product we can get only get 10% of the share. That is the way the rule is.

On the metro side, as metros are being built for those what do I call as, those bogies which will get built in India or will have a requirement of Made in India content, obviously we are bidding for that. In some of the initial metro rails, the whole thing has come imported from outside. But now for example for DMRC we are there is a Korean company that is building the bogies and we are supplying the bearings from here to Korea and from there they will get fitted and come back here.

So it depends on the contractor for the railway, for the metro train who gets the OEM, who gets the bids to make the train and what is their manufacturing model, that determines how we will move forward. For example, on the other hand on Indian Railways GE has got into as you know GE and Alstom it is the PPP route for making locomotives and we already have signed the contract with GE now for supplying bearings over the next ten-year period, yes.

Kunal Bhatia: And in terms of the size, how big would be the Indian Railway part if you could differentiate in the passenger and freight in terms of numbers?

Chandramowli Srinivasan: So roughly the Indian Railway market is of the order of Rs. 1,000 crores in a year. And then within that I think 40% is passenger and 60% is freight.

Kunal Bhatia: And in terms of freight we have already reached the 10%?

Chandramowli Srinivasan: Yes, so this is the year when we will be 10%.

Kunal Bhatia: Sir, and also just one clarification. In terms of industrial you have mentioned in the revenue mix it is 51% of the revenue mix in this quarter. So out of that you mentioned OE and aftermarket, if you could please repeat those numbers, sir?

Shishir Joshipura: OE is about 28% and aftermarkets is about 24%.

Chandramowli Srinivasan: 27% and 24%, 27% for OEM business and 24% for distribution business.

Kunal Bhatia: Okay so this 27% of the overall, right?

Shishir Joshipura: No, But Yes within 51% the break up is 27% and 24%.

Kunal Bhatia: 27% and 24% okay got it. And sir, just also I missed out on the part. In terms of as you mentioned Rs. 1,000 crores is for the Indian Railways how much is it for metros?

Chandramowli Srinivasan: No, metros are not such a huge segment and as I said it depends on the business model that is being followed by the main OEM as to whether they make in India or they have made in India content requirement and stuff like that.

Moderator: Thank you. The next question is from the line of Jeetu Punjabi from EM Capital Advisors. Please go ahead.

Jeetu Punjabi: I thought the numbers were great in the context of the environment. A couple of questions. If we were to look in a post GST world what kind of do you see things accelerating and within your portfolio which are the sectors you see doing better and which ones are you not so confident about?

Chandramowli Srinivasan: So Jeetu, the way I look at the post GST so assuming that once it is stable regime, people have settled down to the new laws, they know how to work etcetera, etcetera. So in a steady state environment what I expect that this would do is one, very clearly by design it must put some kind of breaks on to the counterfeit business you know because that is very much on the cash side of the dealing and obviously the tax laws will discourage that kind of a thing to happen. So that is in the whole supply chain of that part. So counterfeit business would clearly be under some kind of say pressure and they should reduce their presence, that is one thing that I expect will happen.

The second thing that I see happen is also I think it will build shall I say a pan India market for products as opposed to very small regional or local markets for our products. So we can see because it will also facilitate three-year movement of goods. So that should also drive some of the activities you know in terms of driving availability of the product lines and reducing inventory levels, improving competitiveness. So that is the second dimension that will happen, that we will be I clearly see some kinds of competitiveness being built both on account of the time that will be saved but also on account of the fact that now with one tax country you can afford to have lesser number of inventory points as compared to before.

So those are two big impacts that I see. Other than that, sectorally the unorganized players whether they are counterfeit or not, unorganized players also will see some pressures because obviously the tax law is not friendly to unorganized, it is asking people to be part of the system. So if they become part of the system then some of the what should I say the leverage is that they hold today because of the unfavored trade practices, that will all go away. So those are three things that I see should happen.

Jeetu Punjabi: Right and would you be more confident of the autos and the railways going into post GST world or?

Chandramowli Srinivasan: Yes, I think that is my personal view is that it will not matter.

Jeetu Punjabi: Okay then the other question is what kind of behavioral elements are you seeing in your opening comments you said that you are related to GST being a bit of nervous period for industry. What kind of behavioral elements are you seeing in the market in this period?

Chandramowli Srinivasan: So I think one of the key issue is that for whatever reasons, the lack of information, or lack of understanding or understanding the inter connectivity between various issues, or connecting the past practices to the new change practice in the new regime multiple reasons. I think what is going to happen is that people right now are saying should I not defer my buying if I can because it is only a matter of few days to first of July rather than buy it now because if I buy on 1st of July I do not have to worry everything is crystal clear.

But if I buy it within June or May then are things clear or not, what will happen to my stock, what will happen to my inventory, what will happen to tax treatment of the input tax credit. So there is some ambiguity on that account so that is one behavior that we see some uncertainty and some saying the best way to deal it is to just postpone the purchases into the next quarter. That is just one thing that we see. Second is also I think people are also beginning to understand that they need to get used to the fact that the transactions they will have to be done in an organized part of the system way rather than off the book transactions.

So that is also driving some behavioral change in the distribution networks in the retail networks because now they are getting ready to or they are beginning to understand what it means to transact in an official sort of way. So that is the second thing that I clearly see happen. I do not see any other major issue. So if you said the actual end user or actual OEM was buying, I do not see any changes in their behavior, it does not matter.

Jeetu Punjabi: And one final question. I mean you talked about your CAPEX program moving up substantially. Can you just tell us what is the motivation behind that, is it headquarters saying we need to do it or is it you guys saying we need to integrate better and we need to get newer products and the entire chain better ready for the new world. Where is that coming from is my question?

Chandramowli Srinivasan: So Jeetu, one thing is the headquarters never say we should do it. They always say why we should do it. So it is my job is to justify. I think it is very simple, I think we are clearly looking at ensuring that we are prepared for our growth, we are ready to meet the results that were outcome of our growth so that our customers are able to see the end result which is in to then product delivery and so we are obviously we have to take a map of what our capacities are, where are we with respect to what is required to be done.

And then plan the CAPEX for two accounts one is that we need to have a new product line for which I cannot produce from my current infrastructure or second is that I have the infrastructure but that is full so therefore I need additional capacity. So these are the two things that are driving us. So the innovation led, new product introduction and the deeper inroads with the customers for the same product lines.

Moderator: Thank you. The next question is from the line of Raghunandhan from Quant Capital. Please go ahead.

Raghunandhan: Just wanted to understand has procurement started under the dedicated freight corridor project can it significantly increase revenues for us in the railway segment over the next three years. How are you seeing that?

Chandramowli Srinivasan: So, I would say some initial quantities are being contracted now but these are what I would call as testing quantities from an engineering perspective. So they are trying to see whether changing some specifications will help them to increase the tonnage on the freight corridor but there is no lock, stock and barrel buying for DFC yet. So these are initial days but I think as we go forward if the final direction is that we want higher speed trains which can carry higher tonnage, then obviously the procurement will go in the direction of that and so I think I would had mentioned in couple of calls ago that current buys for E Class bearings in that will shift to a K Class bearings and we see some initial quantities of K Class coming but I am sure that three years down the line we will see more of K and less of E.

Raghunandhan: And are we also participating in that locomotive orders for GE?

Chandramowli Srinivasan: Yes, I did mention that earlier that we have just signed a contract with GE on a ten-year basis for the supply of bearings for the locomotive that they will produce.

Raghunandhan: Can you quantify sir, how big that opportunity can be for us over the life of the contract or on an annual basis how big can it be?

Chandramowli Srinivasan: It could be I mean it depends at what speed GE will make and how many number of locomotives they will produce per year etcetera,, etc., but we are looking at something like Rs. 300 million opportunity.

Raghunandhan: Rs. 300 million annual opportunity?

Chandramowli Srinivasan: Yes, not that in an over the period of the contract.

Raghunandhan: Okay Rs. 300 million over the period of the contract?

Chandramowli Srinivasan: Yes.

Raghunandhan: And sir, on the GST part, do you see any inventory unwinding with dealers, distributors in the near term because of the confusion or the uncertainty and are we taking any steps to compensate them for any tax losses or I mean how are you seeing that to help them for a smooth transition?

Chandramowli Srinivasan: So one thing is that yes there are some distributors quite a few of them who are now destocking if I can use that word. They are destocking from so they are not buying new stocks as I was mentioning earlier, they would rather buy it on 1st of July rather than buy it on 30th June and so on. So that is just one clear action that is happening. The second is you know we have always believed in doing all transactions with our distribution network and they know that in an absolutely uniform and transparent manner. So we have no such case that we will give them invoice which is without excise duty and with excise duty, we do not do any of that stuff.

So for us it has been a very, very clean transaction right through. So there is no need for me to go forward and say I will compensate you for something or I will give you some money in return. We are not doing any of that stuff. We are very clear for us it is business as usual. On the tax law scene in 1st of July we will become compliant to that on 1st of July.

Raghunandhan: Understood. Last quarter you had shared in some numbers in terms of the growth across segments like cars, trucks and tractors had grown at 30% whereas two wheelers had grown at 9%. I request you to share these details for the current quarter?

Chandramowli Srinivasan: Yes, to compare to the same quarter last year cars have grown for us by 30% though the industry grew by about 9.5%, 10%. Trucks for us grew by about 42%; tractors grew by about 8% and two-wheelers grew by about 4% when the industry actually was down by 2%.

Raghunandhan: And aftermarket, sir?

Chandramowli Srinivasan: Aftermarket this quarter was compared to the same quarter last year down by 11% but that is mainly because of the demonetization effect which we got out of I would say sort of only in the month of March. I mean Jan was very slow, February slightly better, by March we had sort of recovered.

Raghunandhan: Understood, and on the industrial OEM and replacement can you share the growth?

Chandramowli Srinivasan: Industrial OEM grew by about 22% in total and distribution grew by about 6%.

Raghunandhan: Any growth number you can share on railways?

Chandramowli Srinivasan: Yes, railways grew by 65% compared to the same quarter last year.

Moderator: Thank you. The next question is from the line of Basudeb Banerjee from Antique Finance. Please go ahead.

Basudeb Banerjee: Sir, as you mentioned every year in your annual report sir what was the industry growth for bearings this year and what is the size of the industries as of now and what is the change in market share?

Chandramowli Srinivasan: It is roughly about Rs. 9,000 crores is the value for the market for the bearings in India and our share I have put roughly at about 27%.

Basudeb Banerjee: Now what is the change year-on-year?

Chandramowli Srinivasan: I mean there may be half a percentage point favorable change for us. Nothing as shattering but half a percent point market share is decent enough.

Moderator: Thank you. The next question is from the line of Laxmi Narayan from Catamaran. Please go ahead.

Laxmi Narayan: Couple of questions. First is on a full year basis what has been the growth across segments because you mentioned that quarter 1, can you just help me understand on an annual basis, 12 months?

Chandramowli Srinivasan: Laxmi, I do not yet have, I have not really cast my numbers on a full year basis because we still run our business really on a calendar year basis not so much on the financial year basis.

Laxmi Narayan: Yes, on the calendar year basis I am just looking for directionally if you look at 12 months Jan to December of 2016 what has been our, you have that number readily or I will take it later?

Chandramowli Srinivasan: I can tell you in total we grew by about 7% last year. That means calendar year 2016 compared to calendar year 2015. So I think segmental I will give it to separately. You will have to just call me back.

Laxmi Narayan: Okay. And you mentioned just for the previous question that on quarter-on-quarter there has been healthy growth. Now which and you mentioned that aftermarket grew minus 11%. Now when I look at your turnover it has grown by around 7% odd, right and all of them had like really large high double-digit growth. So which actually kind of pulled you down apart from aftermarket?

Chandramowli Srinivasan: Sorry, you are comparing us with the same quarter last year, right?

Laxmi Narayan: Because you just gave the quarter-on-quarter number?

Chandramowli Srinivasan: No, I have given year-on-year. I did not give quarter-on-quarter.

Laxmi Narayan: Yes, Jan to March 2017 versus Jan to March 2016 you gave.

Chandramowli Srinivasan: Okay so we grew by 11%. And within that we grew in cars by 13% and trucks by 42% and tractors by 8%. In two-wheelers by 4%; in industrial markets by 14%. And aftermarket automotive de-grew by 11%. And then exports also grew by 29%. So all-in-all we still grew by 11% totally.

Laxmi Narayan: And in terms of your distribution reach, your end distribution points that you add more aftermarket distribution for both auto and industrial broadly what is the number like?

Chandramowli Srinivasan: So I would say that in terms of number so two level of distribution. So one is the primary distributors for us in an industrial market we have added about say 10% points in terms of number of outlets that have gone up in compared to a year ago.

Laxmi Narayan: Which is primary industrial?

Chandramowli Srinivasan: This is primary industry and this almost a similar number on the primary automotive side as well. On the secondary side for industrial market there is a retail network for industrial market we have almost grown by 25%, our retail network and on the other hand on the VSM side we have reached to about 16,000 odd retailers out of the total 25,000 that are registered with us.

Laxmi Narayan: What is this second program you mentioned it is VHM or something, I did not get it?

Chandramowli Srinivasan: VHM is the vehicle aftermarket so on the automotive side.

Laxmi Narayan: And you have reached 16,000 retailers?

Chandramowli Srinivasan: Yes.

Laxmi Narayan: And what is that 25,000 you mentioned?

Chandramowli Srinivasan: So 25,000 is the retail network that we know of and 16,000 is the one that transact with us out of that.

Laxmi Narayan: Okay and that 25,000 itself is, is it kind of growing or is it like fairly stagnant?

Chandramowli Srinivasan: No, so the way this retail network works is there would always be some people, retail network is reasonable volatile. So some will drop out, some will join in. So it is important to know the full universe and then make sure that out of that how many you want active. So of those 16,000, 17,000 that on a normal basis remain active. We would probably say that with a half of them we have direct contact. So that is the way it works. Whereas the other half is through our distribution network but with.

Laxmi Narayan: So you build to the primary and the primary will build to these retailers?

Chandramowli Srinivasan: That is correct.

Laxmi Narayan: And the demand generation is done by you or by the primary distributors?

Chandramowli Srinivasan: No, it is different stocks in different market. So industrial market is a joint effort where we will generate and they will generate. On the automotive side is more their generation but we do all the marketing activities for them to connect them with mechanics so create mechanics connect program and stuff like that. So all that is taken care by us.

Laxmi Narayan: And you mentioned in the previous question sometime back on the railway thing. You mentioned Rs. 1,000 crores is the total market fit in to a 60% to freight and 40% to passenger. And you said we are strong in passenger so far. And again, passenger again splits into the high-speed passenger cars like the Rajadhanis and Shatabdis and then you have I think you mentioned something called

Shelton bearings or something, right. Now where are we dominant on I mean where is our large chunk coming from is it from the Rajadhanis and Shatabdis or?

Chandramowli Srinivasan: So Laxmi, generally higher performance means SKF that is the way it moves. So all these new trains that you are hear about now Tejas which runs between Mumbai and Goa and the one that run for Agra the Gatiman one they all run on our bearings. So they are 200 kilometers one. Higher the speed, better off AR.

Laxmi Narayan: Okay and on the passenger thing which you mentioned that around 6% of your revenues so assume it is around Rs. 170 crores, right. Now on that how much is coming from freight for you broadly?

Chandramowli Srinivasan: Freight is not much right now. Freight is a very small number for us. The most of it is passenger right now.

Laxmi Narayan: Okay and in freight you would do across the class bearings, right both TRV, CRV?

Chandramowli Srinivasan: Yes.

Laxmi Narayan: All you will be doing?

Chandramowli Srinivasan: Yes.

Laxmi Narayan: And that market which is essentially the entire Rs. 600 crores market is up for grasp and I believe that if I put those together your additional capital expenditures will be predominantly going in line with the railway, right that would-be majority I believe, right?

Chandramowli Srinivasan: No sorry, I did not get your question actually?

Laxmi Narayan: So you mentioned that you will be getting into railway freight bearings in a big way. Some 10% of addressable to almost 100% over the next one year?

Chandramowli Srinivasan: Yes.

Laxmi Narayan: And also mentioned that the incremental capital expenditure over the next three years would be double that of?

Chandramowli Srinivasan: So for railways the CAPEX is already there, it is just that it takes three years to get approved. So we have to put up the capacity and then it is a three-year cycle to go to the full scale.

Laxmi Narayan: Yes, I was thinking that the incremental capacity you are adding.

Chandramowli Srinivasan: No, the CAPEX is already there, I just need to get it through the full capacity and the tender side.

Laxmi Narayan: So only after that you can even go for tendering?

Chandramowli Srinivasan: Yes, plus the fact that the railway investment is in the other subsidiary not in the listed company.

Laxmi Narayan: And the incremental capacity which you mentioned some Rs. 80 crores per year you have to do, which are the specific things you have in mind, what type of bearing which you have?

Chandramowli Srinivasan: We have mentioned in the past as well so third generation bearing for cars that is one channel we have established. Now it will go for expansion as well. Then we will have it for so normal than TRDs the medium DGBBs in the entire range the current range that we serve the market as I was saying that one is the innovation that is when we come up with the new kind that we cannot make on our existing machinery. It may be a TRD or CRB that does not matter.

But if I cannot make it on my present assortment or it is full then I need to put additional capacity or I may have a higher volume requirement because of higher share of business from some customers or higher spread of an application. Then we need to it expand in that direction. So existing product lines but I have no more capacity to produce them and therefore I will expand.

Laxmi Narayan: And any kind of when you mentioned the next generation bearings but any India innovator, India product you have actually done for passenger cars or anything in the last one year or so any?

Chandramowli Srinivasan: For cars?

Laxmi Narayan: Cars or any like because just trying to understand your innovation pipeline?

Chandramowli Srinivasan: So that way there is many. So we have a complete range of bearing housings that are introduced out of India complete range for bearing housings which are actually now we will also start to step it in the export market for those product lines. So that is housing and accessories so that is one complete product line out of India. Then we are also working on a very unique product that SKF has on offering which is a hub unit but it is a tapered hub unit. So that is not something which is available with anybody else.

So that is something that will now go to the automotive market and it is already spreading a very, very wide acceptance from the customers. So that is another product line that will come out of India and go to it is currently for Indian customers but it can even go outside later on. So that is the second one.

We have the pinion bearing that was mentioned earlier that we have offered to the commercial vehicle segments. So that is the third example. So there are many.

Laxmi Narayan: Okay and one last thing. I have been hearing some good things related to the Defense procurement and some of the trucks that are being built in the factory in Bangalore they are looking for Defense trucks lot of things which are foreseeably going for Make in India. And the procurement authorities in Defense have to prove that this product cannot be Made in India hence and importing. Now all those things we will see Defense as your important priority and what have been done there?

Chandramowli Srinivasan: So Defense is an important segment for us. But as you probably know the Defense procurement cycles are long and for different reasons that they have different requirements for prototyping and testing and stuff like that and with the PPP program that they have served with the three private sector players Tatas and L&T and I think Bharat Forge so we know that that is a program underway we are very much part of it. In fact, I cannot tell you the names and details because my lips are sealed but yesterday only we have received a contract for supplying bearing for a very, very important application under this program.

Moderator: Thank you. The next question is from the line of Shraddha Seth from Edelweiss. Please go ahead.

Shraddha Seth: Sir, just two questions. Wanted to understand has the traction on the industrial side come off from the previous two quarters because as you mentioned the mix in the traded side has reduced on a year-on-year as well as on QoQ basis. And also, you mentioned industrial has grown at 14% from I assume it used to be growing at 20% for the last two quarters. So just wanted to understand where have we seen this traction coming off in the industry?

Shishir Joshipura: Some seasonality in total at railways, banks, etc., which is part of our industrial segment. But we do not see any change. In fact, I think Mouli did mentioned that on the OEM side it is still at near 20% growth on a QoQ basis, on a YoY basis for industrial OEMs. The distribution business was not to the extent that the vehicle aftermarket had got impacted but definitely to some extent it was impacted on account of the demonetization in the last quarter.

So that also slowed it down and pulled it a little bit. We did see an absolutely slow January so all have started recovered from February, March and in April recovered even further. So that is what we saw. So mix of little bit of impact of demonetization on the distribution business. But otherwise I do not see any slowdown at all.

Shraddha Seth: So industrial OEM does continue to grow at a double digit?

Shishir Joshipura: Yes.

Shraddha Seth: And just secondly, wanted to understand the exports as you mentioned it was a very healthy 29% growth. So how was it for the full year and how are we seeing the traction there?

Shishir Joshipura: Yes, this quarter our exports were very good. As a full year last year, it grew by only 3%. When I say last year means calendar year 2016 over calendar year 2015. But this year first quarter has been very good. Help by recovery in the automotive market in the western world because a lot of our bearings go to the automotive market in the west. But also by some new markets in Asia for us. So we have started to now put out some more bearings made by our Indian factories in to Asian market. So both these put together exports are showing good traction.

Moderator: Thank you. The next question is from the line of Vipul Shah from Sumangal Investments. Please go ahead.

Vipul Shah: My question is on regarding traded side. So what is the source or what is our sourcing strategy for traded products? And is it comes entirely from SKF?

Shishir Joshipura: Yes, when we say traded product it is just that is made by an entity which is not SKF India Limited but it is within the SKF Group. I mean I would not say this is like 100% true but this is 99.9% true so maybe there is a small amount.

Vipul Shah: Okay, so whatever products which are not.

Shishir Joshipura: For example, if we sell some grease, etc., which obviously we do not make but.

Vipul Shah: And regarding sir, railways I think you have commented that railway business is a separate 100% subsidiary. Have I understood you correctly or?

Shishir Joshipura: I said was that the manufacturing for railways bearing, the bearings that railways need is in our other subsidiary which is another group subsidiary which is not part of SKF India.

Vipul Shah: Okay so you will source them from them and supply to railways?

Shishir Joshipura: That is correct we source them and supply.

Moderator: Thank you. The next question is from the line of Kunal Bhatia from Dalal & Broacha. Please go ahead.

Kunal Bhatia: Sir, just wanted to understand you have mentioned about few new bearings one is you have mentioned about the housing and accessories and the hub unit tapered bearing and also about the pinion bearing which you are putting on the M&HCV. Just wanted to understand including these and the innovative bearings how many of these are manufactured and what percentage would be traded?

Shishir Joshipura: All of these are manufactured in SKF India.

Kunal Bhatia: All of these are manufactured in SKF India?

Shishir Joshipura: Yes.

Kunal Bhatia: So sir, in terms of the third generation bearing which we have for the four-wheelers even those are manufactured in SKF India?

Shishir Joshipura: Yes.

Kunal Bhatia: And sir, what kind of if you could just give some sense on what kind of expansion are we looking in the case of those bearings?

Shishir Joshipura: So I mean this is obviously market driven and as you can know you know that in automotive word I mean I will have to be getting a contract now for producing it two years down the line. Because when the car platform is completely ready etcetera. So it depends on how that moves on which piece. So we already have the first contract as I mentioned from Maruti and now we also have the next one from Tata. So we are moving in that direction.

Kunal Bhatia: Sir, but right from the time when this third-generation bearing has started have we put in any additional capacities or this would be the first time when we are?

Shishir Joshipura: This is the first capacity for third generation.

Kunal Bhatia: And will it be higher than the previous capacity?

Shishir Joshipura: No, so this is the new capacity. I did not have the third generation bearing at all in India with me. Now we are putting the first facility and then we will get a suitable expansion down the line.

Kunal Bhatia: Okay so at the moment you are sourcing it?

Shishir Joshipura: No, we are not sourcing it. We are not selling it at all.

Moderator: Thank you. As there are no further questions, I now hand the conference over to Ms. Bibhabaree Biswal for closing comments.

Bibhabaree Biswal: Thank you very much all of you for participating in today's call. In case you have any further questions, you can write to me at bibhabaree.biswal@skf.com. Have a great day. Thank you.

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