# Cummins India Limited

## Quarter One Earning Conference Call, 2017-18

## August 4th, 2017

**Anant Talaulicar:** Good morning, ladies and gentlemen. I would like to convey the results of the April through June quarter to you this morning. Sales at 1388 crores grew 5% compared to a year ago and 12% sequentially. Domestic sales grew 10% compared to a year ago and 6% sequentially. So, we continue to see good domestic strength. Exports, unfortunately are 5% lower as compared to the same period last year. However, they did see a 31% bump sequentially. However, I would like to caution that one data point does not make a trend and we have not declared victory in terms of robustness in the global marketplace here. Although, we think that the situation has certainly bottomed out. Net profit before tax excluding the extraordinary gain that we saw because of a real estate sale of our Viman Nagar property which was 56 crores, so, excluding that one time factor which was non-operational, our operational net profit before tax grew 2% as compared to the same period last year. Again, profitability continues to be buoyed down based upon the exports decline. However, the company saw good leverage sequentially. So, based on a 12% sales growth sequentially, we saw 17% growth in the bottom line. Going forward, we feel good about the state of the domestic economy. I'm also happy to relate that the GST transition has gone relatively smoothly for the company that is on the back of incredible amount of good work done by the team. And we have not seen any material impacts. And, even though, there was some impacts obviously because of our customer transition issues. I think over the quarter, we do not expect to see anything material impact, the company as far as the GST transition that is a really good news. And, you know, what that means is, hopefully going forward, the company should start benefitting from the various structural changes that will come about in the Indian economy as a result of this massive indirect tax reform. We continue to be cautious about exports outlook. And overall, I would continue to maintain my guidance for the full year, for the fiscal year which was 5 to 10% growth in domestic revenues and flat to down 5% in terms of exports outlook. So with that I will open it up to your questions. Thank you.

**Moderator:** Thank you, sir. Ladies and gentlemen, at this time should you wish to ask any questions, you may please press "0" and then "1" on your telephone and wait for your name to be announced. Yeah. We have the first question from Mr. Charanjit Singh from B&K securities. The line is unmuted. Please proceed.

**Charanjit Singh:** Hello, sir

**Anant Talaulicar:** Good morning.

**Charanjit Singh:** Good morning, sir. Sir, if you look at the quarterly numbers, so there has been an, you know, increase in the staff cost on a y-o-y basis. Sir, can you, you know, help us understand, one is the staff cost increase and other is, you know, how has been the, you know, raw material impact? And do we see these, you know, factors continuing going forward?

**Anant Talaulicar:** Yes. So, the staff people cost have increased in the quarter. And there are couple of factors that are driving it. One is, of course, the annual merit cycle that we go through. But, in addition to the normal merit cycle which tends to be in the, approximately 8% increase range, we've had an increase in our annual variable pay out accrual. So, based upon, you know, relatively strong performance, we expect that by the end of the year, we will be paying annual variable incentives to our employees which are at a higher level as compared to last year. So, that has been another factor that's played out. And the third factor is, our long term settlement which is a three year contract which unionise employees on the shop floor. Although, three things kind of came together in the quarter, that should level out going forward to, you know, at least staying somewhat flat I would say, but that's really what's going on. But, no doubt, the employee cost as a percent of revenues have gone up by a point as you have noted. And, you know, essentially growing the company's top line will eventually bring it down to the same level as it was last year.

**Charanjit Singh:** uh-huh.

**Anant Talaulicar:** Approximately...

**Charanjit Singh:** But then your absolute level, it will remain at this level or it will go down?

**Anant Talaulicar:** On an absolute level, it will remain at this level.

**Charanjit Singh:** Okay, sir. And sir, on the raw material front, how do you see the trajectory going forward? We have been, you know, trying to bring in lot of cost cutting initiatives and bring in on the foot-print also of the engine and all those initiatives. But, how do you see with the increasing pricing pressures in the high KVA segment and, you know, the trajectory on the overall margin front and the gross margins?

**Anant Talaulicar:** Yeah. So, looking ahead in terms of our margins, I expect that we should be able to hold the margins going forward. And, you know, there is some upside to the margins, anyway, between 1 to 1.5% is what I would project by the end of this fiscal year. That could be an upside.

**Charanjit Singh:** Okay, sir. And this is the last question. Sir, if you can please help us with the break-up of different segments on the industrial automotive numbers.

**Anant Talaulicar:** Okay. So, basically when you look at our domestic side, what we saw was the, the power gen business was 370 crores. The industrial business was 200. Auto essentially, we don't have any revenues and, you know, we are out of that business. And distribution, we are at 340 crores. And then, there is the excise portion now which is approximately 85 crores.

**Charanjit Singh:** Okay, sir. And sir, within the power gen, what was the break-up of low KVA, mid and the high KVA, sir?

**Anant Talaulicar**: In terms of the low KVA in power gen, that was approximately 40 odd crores, mid range was about 120 crores, heavy duty was 20 odd crores and high horse-power was about 185 crores.

**Charanjit Singh:** Okay, sir. Sir, that's all from my side. Thanks a lot for taking my questions.

**Anant Talaulicar**: Welcome.

**Moderator:** Thank you, sir. The next question is from Mr. Ravi Swaminathan from Spark Capital. The line is un-muted.

**Ravi Swaminathan:** Hi, sir.

**Anant Talaulicar**: Good morning.

**Ravi Swaminathan:** Sir, I had a few...yes good morning, sir. Sir, in the exports market, apart from Africa and Middle East, are we seeing some sense of recovery in other markets or is it like still the, directionally things are still remaining weak there, say China, US and other countries?

**Anant Talaulicar:** Yeah, what I would say is that Middle East and Africa, clearly down. And all the other markets are relatively flat. You might see some ups and down quarter-to-quarter but overall when I look at longer term trends, it's flat, it's a flat picture.

**Ravi Swaminathan:** Okay. And, with your commodity prices, like, crude stabilising, are you seeing any pick-up in the other countries?

**Anant Talaulicar:** Not really, no.

**Ravi Swaminathan:** Okay. Okay. And coming to the domestic market, we have seen something like 18 to 20% growth in the industrial business. Is this growth kind of sustainable, in the sense that was there some kind of pre-buying in earth moving equipments related to GST that had happened during this quarter and that might not turn up in the next few quarters or how is it?

**Anant Talaulicar:** You know, we feel generally good about the industrial side of the business. Quarter-on-quarter again, there will be some puts and takes that go on. So, for example, you know, we do see that the compressor segment in our industrial business, which is generally the water well rigs, is still in a depressed state, you know, so as compared to historic sales, and it's going through a cyclical down turn which we think has bottomed out. But construction, you know, clearly has improved as you've seen in recent times. However, you know, there will be, like, you know, there is, generally this quarter, we expect now, this I'm talking about the July quarter, is likely to be somewhat flat to down based upon, just the monsoon impact and some impact due to possibly GST. But, overall I would say when you look at it from a fiscal year basis, you know, we feel good about the prospects of our industrial business. And we should be able to grow it in the double-digit grades.

**Ravi Swaminathan:** Okay, okay. Sir, and the employee cost I had one more clarity, you told, 120 crores run rate for every quarter, next three quarters will be there, that is what you had mentioned, around 120 crores of employee cost?

**Anant Talaulicar**: Yes.

**Ravi Swaminathan:** Okay. And, okay, got it, got it. And in terms of gross margins, sir, with the rising rupee in exports, how is it that it is likely to play out? Do we have an pricing arrangement with our parent with Respect to exports? How does it work?

**Anant Talaulicar**: Yeah, we do actually. We do have a pricing arrangement with the parent where, you know, within a certain band there are no changes and then beyond the band, there is a sharing arrangement that takes place.

**Ravi Swaminathan**: So, with the rupee moving from, say, around 67, 68 levels to say, 64.5 levels, will it break up band limit? How does that work?

**Anant Talaulicar**: It will, it will bring it down to some extent. It's not going to be very material, I don't think.

**Ravi Swaminathan**: Okay, okay, got it. And sir, in terms of exports break-up, can you give between low HP, MHP, HT and HHP?

**Anant Talaulicar**: Okay. So, basically, when you look at low horsepower, there was approximately 70 crores. The mid-range was approximately 110 crores. Heavy duty 30 crores. High horse power of about 165 crores and the rest was fair parts of approximately 25 crores.

**Anant Talaulicar**: Okay, sir. Thanks. Thanks a lot.

**Ravi Swaminathan**: You're welcome.

**Moderator:** Thank you, sir. The next question comes from Mr. Venugopal from Bernstein. The line is un-muted.

**Venugopal:** Hi. Sir, thanks for the opportunity. Sir, on the export thing, I wanted to understand, again a very similar question is, what is the rupee dollar rate at which the export pricing is set with the parent company? And within that could you also give us some understanding of what makes you continue to have a weak outlook on export? Is it that you seeing certain end markets remaining weak and what is the extent of visibility you have on that? That's your first question.

**Anant Talaulicar:** Okay. So, basically when I look at, to your first question, rate is pegged at 64.6 right now for dollar. Okay, so, that is really what we are seeing flow through the PNL. And as I said, you know, there are substantial movements in the rate as compared to that, then we make pricing adjustments. Now, on the other part of it, your question which was related to exports outlook, as I look at rents, I'm not looking just at a quarterly number because that can be misleading. But, as I look at 4 or 5 quarters across each one of our geographies, I'm not seeing any substantial change in the demand picture, except that, clearly Middle East and Africa has come down, I would say, statistically come down and it has come down based upon the fact that, at today's or even the last few, let's say months of oil prices, you know, lot of those countries cannot make money on that commodity and they are struggling in terms of liquidity et cetera. That is what I scribe it to. The rest of the world, I would say, yes, you know, we are clearly seeing now, not declines but growth, the US is growing slightly, right, 2% whatever, Europe is about the same. China is growing at a lower pace but certainly growing. So, my view is that, you know, things have bottomed out pretty much and they could improve. All I'm saying is, I'm not willing to declare victory yet. I'm taking of more cautious outlook. But it looks like things are bottomed out and will improve over a period of time that is where I'm coming from.

**Venugopal:** Sure, sir. Sir, my second question is more to do to with the discussions couple of quarters back on the K19 engine range where you might think of, you know, sort of shifting manufacturing from CIL to CTIL, more from a cost optimization perspective, where are we on that in terms of a deficient? And number two is, is there any other high horse power range engine which you currently manufactured which you think is appropriate to shift it out there for cost reasons?

**Anant Talaulicar:** There is no plan by the way, maybe, a mis-communicate. There is no plan to outsource the K19 engine that will continue to be made within CIL's manufacturing facility of Kothrud. And there are no other plan neither of any substantial shift in outsourcing either.

**Venugopal**: Okay.

**Anant Talaulicar**: What I was referring to was, more that, we are looking to actually bring cost down of certain products and also up rate certain products. Up rate being that, from the same carcass, we will get more power output and therefore, on a rupee per kilowatt basis, we will improve our profitability. That's really where I was coming from.

**Venugopal**: Okay, because earlier there was a discussion that, you know, the 10 engines which, whatever, the facility from US which was shifting to CTIL, you would probably think of shifting some from CIL and then outsource it from there, you know, because it will be better cost reposition because the facility is older while CTIL1 will be newer et cetera. So, that was the discussion earlier about a couple of quarters back.

**Anant Talaulicar**: No, no, there might be some miscommunications but certainly, you know what we are seeing right now, all these demand in power gen that is based upon K19 et cetera, that is going to continue within the CIL legal entity.

**Venugopal**: Sure, sir. Thanks a lot.

**Anant Talaulicar**: Welcome.

**Moderator:** Thank you, sir. The next in the queue is Mr. Sandeep from JM Financial. The line is un-muted.

**Sandeep:** Yeah. Good morning, sir.

**Anant Talaulicar**: Good morning.

**Sandeep:** Sir, my first question is on the domestic HHP just in sales current demand scenario and the competitive intensity outlook because, you know, we've been constantly mentioning that pricing for these gensets has not been able to recuperate after the CPCB-II implementation which is kind of having an impact on the overall profitability. I just want to get your comment as to how the pricing has moved in the last two years after CPCB-II. And has there been any recent pricing action on those products?

**Anant Talaulicar:** Yeah. So, in general, price competition intensity has been very high. And, you know, we in general, the trajectory of pricing has been downwards in the last two years post CPCB-II, of course, we have increased it but then we could not sustain those increases and we brought those prices down. So, that is where it's at. In terms of very recent activity, for example, even in this calendar year, January through, you know, June time frames, also we have taken some selective price reductions. There have been price increases in other segments but overall there has been no net price impact that has depressed profitability the way I would put it.

**Sandeep:** Alright. So, it's basically you are saying it's not had an impact on profitability although prices are down.

**Anant Talaulicar:** Correct. So, while we have selectively addressed some price corrections, in other cases, we've increased it et cetera. So, on net no impact.

**Sandeep:** Alright. And, sir, my second question was on the status of the Tax Centre Construction where we are investing jointly with the parent company, fraud of 1000 crores and nearly 500 crores is going to be invested from, I mean, it's India, what kind of, what is the current status on construction of same? And what kind of impact will it have on the profitability employee cost structure and so on?

**Anant Talaulicar:** Right. So, you know, we are very excited about that project and in fact, I toward that facility yesterday and it's almost ready, okay. So, I would say that by the October time frame, in that quarter certainly, we will see people occupying that facility. So, we are at that stage now. So, almost done. In terms of the capital investment, that falls onto CIL legal entity, we've almost floored most of it. If you look at it from a full fiscal year picture, there will be about a 170 crores impact to our capital this year, this fiscal year. And a lot of it is flowing as we speak and has already flown in the first quarter too. So, but if you look at the full year, that's the last piece of it which is approximately 170 crores out of that 500, 600 crores whatever approximate amount, the total spent basically that we had planned for. So, you know, again in terms of going forward as you know, CIL, the way the arrangement works, CIL is essentially the landlord, you know, they have invested in the civil part, the facility part, but the inerts of the facility are being funded by the parent. So, we, the CIL legal entity will continue to benefit from the rentals that will come out of that landlord role I would say. And then more importantly and strategically far more importantly, the engineers from CIL will occupy that facility along with engineers from the parent company. By the way, also Indians, of course, you know. They will be collaborating very well together. And while 70% of that work is focussed on global activities which is really developing futuristic technologies for power trains, you know, the benefit of that will certainly flow through two CIL based upon that close collaboration and co-location. So, I would say, the strategic benefits of an... I can't quantify but you know, there will be very significant in terms of CIL's competitiveness in the domestic market place, long-term.

**Sandeep:** Right. And sir, my last question is towards, basically we've shutdown two manufacturing units in the last financial year but if you look at the annual employee count in the annual report, it's still remain similar to the year before that. So, how should we look at this since there is no reduction in the overall employee count on an overall company basis?

**Anant Talaulicar:** So, the way you should think about that is, you know, while we have reduced the employees who are operating in those two facilities, we have actually increased employees, not necessarily at the shop floor level but we have increased employees in the professional ranks based upon the growth that we are already seeing as you know, in the last couple of years, Certainly, in the domestic side and will continue to believe, we continue to grow and for that we have to make the right people investments also. So, that is the way to think about it. It's an investment. You will see the returns in terms of growth in the top and bottom line.

**Sandeep:** Right, right. Alright. And just one book-keeping question, if you can share the tax portion of these sale, on the gain of sale of asset that you have recorded in this quarter.

**Anant Talaulicar:** So, the approximate tax rate for that transaction should be taken as about 22% on that gain that we saw there, that 56 crores.

**Sandeep:** Uh-huh. So, excluding that, I think the tax rate has gone significantly up in this quarter. Has there been any changes because it was around 30% over the last 3, 4 quarters?

**Anant Talaulicar:** Yeah. So, essentially, you know, it was running at about this 19, 20%. Now, you have taken it up to 20. We are accruing this year at 22% based upon two factors. One is that we expect our lower sales of exports as compared to past which means of course now, your tax benefit is lower. And secondly, the R&D tax deduction, if you recall that used to be 200%, the government is phasing out over a period of time. And this fiscal year that should be more like a 150%.

**Bhavin Mitlani:** Got it. Thank you so much for taking all my questions.

**Anant Talaulicar:** You are welcome.

**Moderator:** Thank you, sir. The next question comes from Mr. Venkatesh from City Group. The line is unmuted.

**Venkatesh:** Sir, very simple question. If I look at the engines that you have sold in this quarter, can you give a rough break-up, how many of those engines have actually got made in Cummins India and how many of it has either come from say, a Cummins Inc entity or Simpsons, something like that. How much of this is make and how much of is it buy in the current quarter? Is there a last break-up?

**Anant Talaulicar:** I can't give you the numbers. I don't have that in front of me. However, the way to think about it is, when you look at the low horse power, that is largely outsourced, okay, essentially that is outsourced. So, because those engines, CIL buys from our sister company Tata Cummins and buys from our vendor, Simpsons. All the others, you know, which is anything above; approximately 200kva, you could say, are made within CIL. So, that's approximately, the way to kind of think about that.

**Venkatesh:** Okay. Now, this Simpsons, is that a Cummins Inc entity or is like a completely third party?

**Anant Talaulicar:** No, Simpson is an independent company, is part of the amalgamation group. It is based in Chennai. We've had a very long relationship with them, that's span about over a decade. And, so they are a very close partner of ours. I now have, actually some volume break downs for you. So, if you look at the quarterly numbers in terms of revenue and this is just looking at our power gen, by the way, doesn't include the industrial and so on. But essentially, you know, we sold about 6300 units of products in the power gen segment. And out of that, about 2800 is what we call low horse power but then if you can add on the mid-range which is also outsourced to Tata Cummins, that's approximately another 2000, it's about 4000, almost 5000 is outsourced because volume of these small engines is much larger as compared to the volume of mid and high horse power engines, heavy duty and high horse power

**Venkatesh:** Okay. Now, if we go back in time, maybe one or two years, would the make component be much higher in Cummins vis-a-vis today?

**Anant Talaulicar:** No, not really because, you know, even in the past, Simpsons and Tata Cummins was still making the base engines. The only difference was that these engines were being bought by CIL and brought into a CIL facility, specifically Pirangur and the facility at Phaltan. And CIL was doing some value add, okay, so it was doing what we call, some up-fit. And now, we have chosen to even outsource that up-fit portion. So, you could say that the proportion of that value add has also been outsourced now but essentially to benefit CIL legal entity in terms of overall cost structure.

**Venkatesh:** Okay. See, sir, all these questions are basically to try and figure out for like, two quarters now we've had very gross margins on the lower side, I mean both fourth quarter and third quarter gross margins are very similar. Now, these are significantly lower than what it was one year back or two years back. So, if you look at it from an overall perspective, what exactly is causing this? Is it because you think raw material prices has gone up? Is it because the rupee dollar exchange rate, there is a problem? Is it because of competition you've not been increase prices? Or is it got to do with the fact that the way you are doing value added change over the last couple of years? So, that is what we are trying to find out.

**Anant Talaulicar:** Okay. So, I think you'll have to just take my word for it. Over time, hopefully the data will prove it to you. But our sourcing strategy has had no impact, okay, no impact in terms of depressing the profitability that you are referring to. If anything, it is going to be a helpful phenomenon. Too early to call. Now, the real factor that is going on which have been declaring is our mix of products, okay. So, essentially what I mean by that is, the products that are profitable are seeing a lower demand currently as compared to a year ago. And products that are seeing a higher demand right now as compared to a year ago have relatively lower profitability. And we are the company, are fully committed to addressing that issue so that we become a lot less, you know, what can I say, we've become more impervious to those kinds of shifts in the product mix.

**Venkatesh:** Okay. Sir, one additional question: You gave these break up of sales, when you give us the breakup of sales segment wise, did you give it on a gross sale basis, is it possible to give it on a net sales basis because the numbers don't seem to be adding up, the power generation...

**Anant Talaulicar:** So, basically the numbers I gave you was based upon a net basis, excise separately. I quoted excise at 79 crores is what you probable have seen, that is the excise number but I've given the numbers net of that.

**Venkatesh:** See, because what you have given, that adds up to around 910 crores which is higher than the domestic sales, net of excise, so that is why I was asking you.

**Anant Talaulicar:** No, but there is some miscellaneous also in that, so, you know, you can factor that out, whatever.

**Venkatesh:** Okay.

**Anant Talaulicar:** It's lost in the shuffle. I'm not giving you the very number down to the last penny, by the way.

**Venkatesh**: Okay, okay. And you said there is no auto sales, why is that, because we had it till the fourth quarter, what happen suddenly in this quarter?

**Anant Talaulicar**: Essentially, if you've been following our, you know, calls here, you know, we used to sell to one OEM called Asia Motor Works and they have run into some sort of financial issues, so the demand there has not been there. And also, we were selling to Volvo Eicher and they have chosen the strategy of now using their own engine as they have entered BSIV arena. So, essentially, CIL is out of the auto business.

**Venkatesh**: Okay, okay. Thank you very much, sir. All the very best.

**Anant Talaulicar**: You're welcome. Thank you.

**Moderator:** Thank you, sir. The next question comes from Bhavin from Axis Capital. You may please proceed.

**Bhavin:** Good morning. Could you help me with the break-up of the industrial segment like you have been giving earlier like compressors, construction equipment and mining, etc.?

**Anant Talaulicar:** Compressor has been approximately 40 crores. Construction has been approximately 95 crores. Mining is approximately 20 crores. Rail is approximately is 45 crores and then there are some miscellaneous which adds up to 200 odd crores of industrial sales.

**Bhavin:** One observation is we have been seeing that mining sales have been subdued. We are seeing a significant growth in the construction which is understandable given the building activity. Any view on this because, correct me if I am wrong, this is relatively more profitable than the construction segment?

**Anant Talaulicar:** Yeah. So, here is the way to think about that. Post the Modi government, once the Modi government took over, they cleared all the environmental rubbish that was going on, jetstopped the mining activity; and now we are seeing some very good robust mining activities happened. But having said that there are no fresh allocations that have taken place. But the good news for us Cummins is that we are seeing the benefit of that in our distribution business unit in terms of parts and service. So, that is really good. That is good activity happening in the mines and they stopped importing coal and things of that nature.

Now in terms of fresh equipment tenders coming out from the mines, they are starting to come out but is not very robust I would say. So, that is part of the issue you are seeing here – fresh tenders, which is what you see in the industrial business. So, they tend to be lumpy. There will be a quarter wherein you will see a good demand and then you will see less demand. So, this is the nature of mining. There are, of course, competitive activities also. So, players like Caterpillar, Komatsu who are bringing their own engines of course and are trying to compete hard with the local manufacturer which is **Bemmal** that we are the partner of. So, there is that competition also playing out in this whole mix of what is happening in that market.

**Bhavin:** Understood. Second is, I mean just a clarification on the earlier use because K19 was anyway expected to be in CIL, Kothrud, as you rightly said. In one of your presentations, it was mentioned that QSK19 which is a different product, that was contemplated, not decided, to be manufactured at the Phaltan plant from the US. So, that decision was not taken. You mentioned that it could come to India or it can go to China. So, any update on that QSK19, not about K19.

**Anant Talaulicar:** Right. So, the QSK19 product is the one that we will be manufacturing at a Megasite. Okay? So, it doesn't impact CIL legal entity.

**Bhavin:** Okay. So, it will be by CTIL?

**Anant Talaulicar:** Correct, CTIL. That is right. Now to the extent that there is demand domestically for the QSK19, then CIL will certainly sell it at the domestic market place and enjoy the benefits of those profits, but not manufacturing.

**Bhavin:** Okay. I understood. Second part of Power Gen is wWhen we speak, your peers said and in the industry we see that the a good part of growth in the power gen has been led by the data centres which actually demand a significantly higher rating of the engine, and these are the QSK60 which we buy from CTIL. So, is that the mix you are saying because that is relatively new product and lower indigenization and so hence the margin and this stage is lower.

**Anant Talaulicar:** I think to try and simplify that would not be accurate. I think you have to look at it in the broad mix of all of the products. Of course, I am not free to disclose to you which are more profitable, which are less profitable. That gets into competitive issues.

**Bhavin:** Understood that. Lastly, on the export front and on the high horse power, when we look at the parent results, we see significant growth coming back into mining and oil and gas segments and you mentioned that high horse power segment has again started to reborn in a smart way. So, do we see that maybe in the coming quarters? Will we see a pick up in the high horse power while LHP may take some time but HHP will now after the decline in the LHP?

**Anant Talaulicar:** Yes, I would say so. I would say so that we should start seeing some of that impact on CIL. So, there should be up side. Exactly when, I could not tell you because we have not seen it. Right now it is not evident in the very short term.

**Bhavin:** Okay. That 100% plus growth that we just talked about in the parent call in the mining, oil and gas segment is not America. It is not seeing a rub-off impact as yet on CIL?

**Anant Talaulicar:** That is correct.

**Bhavin:** But will it be with a lack of a quarter or so?

**Anant Talaulicar:** I have no idea. We have not seen that kind of an input yet. So, I really don't have a picture.

**Bhavin:** Okay, fine. Thank you so much for taking my questions.

**Anant Talaulicar:** You are welcome.

**Moderator:** Thank you, sir. The next question we have is from Ms. Renu Vaid from IIFL. The line is unmuted.

**Renu Vaid:** Hi, Good morning, sir. Sir, on the gross margins, you did motioned that that we expect to maintain a margin for the entire year with the likelihood of upside of 100 to 150 bids. The increase in your view will be driven by what elements? Will be cost, product, or any specific actions that you have taken?

**Anant Talaulicar:** It will be based upon cost. That's what I was referring to. We are continuing to execute strong measures around cost control and value engineering. So, we have a programme. We call it ACE (Accelerated Cost Efficiency). It is a time tested one. It was kicked off in 2005 and continues to give us significant benefits and helps us offset the downward pressures that we continue to see in the market place. So, that is what I was referring to. We are also working on the product designs themselves to operate them. So, essentially the same engine putting out more horse power or kilowatts. And essentially that gives us a way to derive more revenues from the same product at the same cost level or even lower cost levels. So, the net result of all that is an improvement in margins. So, it's all cost based.

**Renu Vaid:** Right. And this excise of operating on certain knots of engines, can you share with respect to which particular category does this pertain to or any particular range of products?

**Anant Talaulicar:** Generally, it is in the high horse power categories. That's what I would say. I am talking about 500 KVA and above and is where our focus is right now.

**Renu Vaid:** Okay. Sir, on competition, what has been your sense? Have you seen the pressures easing in the past few months or you think the pressure that we had seen in the last couple of years are likely to sustain and increase further?

**Anant Talaulicar:** I don't see any easing. I do see competitive intensity sustaining in the future. Having said that, I think the Cummins actions, all of the comprehensive we are taking around the four-piece of marketing, I think, are putting a lot of pressure on competition. You probably see publicly also in the case of listed players. And we will continue to stay on course.

**Renu Vaid:** Correct. Sir, one more question. If you can just share with respect to the overall growth outlook, if you see the industrial segment, it continues to be a strong growth in construction. Even this quarter, there is almost kind of 50% growth y-o-y. So, do we see these numbers inching to higher double digit levels of 25-30% growth? In the medium term outlook, if you can share on this segment?

**Anant Talaulicar:** As I have said, you know, the industrial segment, we should see even better growth rate as compared to power gen over the long haul. I am not talking about one quarter and so on because that continues to yoyo. But if you look at it from a fiscal year perspective, my prediction is that the industrial business will grow above that guidance level. I gave you power gen will grow in the guidance range I gave you, etc. That is my outlook.

**Renu Vaid:** Sure, sir. That's it from side. Thanks and all the best, sir.

**Anant Talaulicar:** You are welcome. Thank you.

**Moderator:** Thank you, ma'am. So, the next question you have is from Mr. Abhishek from Deutsche Bank. Your line is unmuted.

**Abhishek:** Thank you for the opportunity. Sir, two questions: one on the railway side, you've seen, you know, as per the annual report you've picked up market share in the DEMU segment. With railways efforts to electrify their lines, would you see this kind of demand continuing, that's one. And secondly on the power gen side, HHP business has remain kind of flattish, what is the outlook or in terms of enquiries on the data centres that you see or is there any other segment which is also contributing to growth there?

**Anant Talaulicar:** Okay. So, you know, the railway electrifying actually is a good news item for us, because we actually supply the electricity on the trains. Our engines are not only used for propulsion purposes, something I would like to clarify, we actually supply the entire generator sets, that then power the railways. And sometimes that power is even used for traction purposes through traction motors. So, you know, this is where we are at. So, we are not concerned. In fact, if anything reach the railways as a continuing opportunity for CIL in the medium and long-term, obviously because it's one of the ministries that is, I would say, transforming very radically and quickly as compared to many others on the back of really good leadership on the part of Mr. Prabhu. So, you know, their action on growing capacities, their action on growing speed, their action on growing safety, their action on the use of alternate fuel, their action on emissions; all of this is positive as far as Cummins is concerned. And we are looking to partner even more deeply with the railways.

**Abhishek:** Right, on the data centres part, the HHP and power gen..

**Anant Talaulicar:** Yeah. So, you know, when we look at our HHP segment and as we look at, you know, the data centres to your point, even when we look at it from the last few quarters, I would say, realty has also been one that is buoyed up our demand for HHP gensets. So, now, that could be due to some of the policy thing that are happening including RERA etc cetera, right. So, but that has been the factors that even that has been a segment that has certainly gone in our favour. As we look ahead and as we look at the kind of the enquiry levels in the marketplace, healthcare is another one, you know. So, that's a, I would say that's going to be a sustaining one because again, given the fact that prosperity levels are improving in the country. Sometimes, those have a downside of people becoming more sick physically. So, I think healthcare is going to be a segment that, you know, we see good demand levels coming from. And even retail, because, you know, consumer demand generally is doing pretty well in the country from what all I can tell. And so that leads to good retail demands, so that's mall and things of that nature. So, that's where I see the action.

**Abhishek:** That goes into HHP or the mid-range ones, sir?

**Anant Talaulicar:** No, this goes in, I'm talking about HHP, right now.

**Abhishek:** Okay. And your mid-range has also seen good amount of growth, you know, over the year, last few quarters I would say. So, what is driving that exactly?

**Anant Talaulicar:** I would say the same things that we just talked about earlier. And in addition I would only add that, you know, infrastructure investments, so these are things like roads, also benefit mid-range because, you know, they are used for road construction. The generators actually are there to power road construction activities. There are stone crusher application also that we seeing good demand in, that impacts generator sales positively.

**Abhishek:** Thank you. And, you know, if I can sneak in one more strategic question, we are reading globally that a lot of data centres are now moving to the solar based installations or maybe hybrid installations for power consumption. Additionally, recently railway has also, you know, initiated certain racks with solar panels on the roof top. Would you consider that as a threat or you know, anyways, the back-up will be required and hence the diesel engine will be sold?

**Anant Talaulicar:** Yeah, exactly, exactly. So, let me just be very clear that Cummins doesn't consider any new technology as a threat. We actually would like to embrace and work on all new technologies which is what we are doing, I think, in our global calls. You would hear our global chairman talk about these things. We are actually making some specific plays in other areas like in automated power trains as well as electrification. All of those activities are going on within Cummins. We just trying to make sure, you know, that we also protect our share holder's interest which I'm sure you would appreciate of trying to improve our core business while we invest in some of these emerging technologies.

**Abhishek:** Thank you. And all the very best, sir.

**Anant Talaulicar:** Thank you.

**Moderator:** So, the next question we have is from Mr. Bhargav from Ambit Capital. You may please proceed.

**Bhargav:** Yeah. Good morning, sir. And thanks for the opportunity.

**Anant Talaulicar:** You're welcome.

**Bhargav:** Sir, just one clarification that, you said that in railways, the gensets are actually used to power railways. So, I mean, just pardon my ignorance, but just wanted to check why wouldn't they sort of power it from the overhead line, why would they need a genset to power the railways?

**Anant Talaulicar:** Well, they do both, you know. So, they do depend on the grid, right, for powering the railways but they also use generators to power, you know, internal light etc rails, sometimes for traction purposes. So, they use a multitude of technologies to do this, just based upon grid availability and reliability and all of those kinds of factors.

**Bhargav:** Okay. And second question is, sir, if you look at your industrial business, we've seen a very strong growth over the last two years but alongside that we've seen some softness in the gross margins as well. So, just wanted to check that whether the industrial business margins would be slightly lower as compared to the blended company level margins or how does that works?

**Anant Talaulicar:** No, I don't think so, you know, it doesn't work that way. Actually, we have to get down into product specific granular detail to understand that better. And obviously, that is not something I'm prepared to share publicly. But overall, I would not make those kind of assumption around industrial or power gen et cetera.

**Bhargav:** Okay. And lastly, sir, you did mention that your parent is essentially trying to work on new innovations in terms of catering to renewable base applications. Would you want to highlight what is Cummins India doing on that front, sir, to sort of diversify the business?

**Anant Talaulicar:** Well, see the thing is Cummins India, you know, has been working for, on straight vegetable oils, on mixers of various kinds of fuels. So, this is something that we've been doing for long period of time. Produce a gas is another one. And, but frankly just like all other alternate technologies where there is a lot of hype around them, the actual action on the ground and certain profitable action is not present. So, we are essentially, the way to think about it is, between our parent and Cummins India, we are playing in all of these things and creating options for ourselves, for entry appropriately, at the right period of time. That is the way I would like you to sort of think about this, you know, obviously, you want to make sure that whatever we do leads to profitable growth, you know, over the long haul.

**Bhargav:** Okay, sir. Thank you very much and all the best.

**Anant Talaulicar:** You're welcome.

**Moderator:** Thank you, sir. The next question we have is from Mr. Ankur from Motilal Oswal. The line is unmuted.

**Ankur:** Yeah. Good morning, sir. Just a question on your exports; and, you know, when I read your annual report, you've spoken about new opportunities on the export front, you know, on two things; one is on supply of machine components and also on the 14 litre engine for marine application. So, if you could just talk about, you know, the potential revenues which could accrue from these two plus, you know, is the parent looking to, you know, outsource any further engines to CIL, here, you know.

**Anant Talaulicar:** Yeah. So, basically, you know, when we look at the products that you quoted right now that have been mentioned in the annual report, we are really talking about machine components such as connecting rods et cetera that we are supplying to our parent, in fact, plants as well as the N14 for marine applications. Now, again, in the big scheme of things, frankly, I couldn't quantify to you what exactly this is going to mean. It will help our overall exports basket which, as you know, right now, is still in a flat to down scenario. It will help but I could not quantify specifically what this could mean. But not, I would say, not very material.

**Ankur:** Okay, okay. And sir, just a second question on the domestic power gen business. Right now, what we understand is that both, you know, some of your peer, KOEL, Mahindra, you know, they have taken some price hike to kind of offset, you know, the higher RM cost prevalent with last few quarters. So, is Cummins thinking on similar lines as well? If something, you could share on those lines.

**Anant Talaulicar:** See, we have an ongoing process that our teams look at and they are constantly in touch with market pricing. And we make adjustments that are suitable all of the times. So, like I was saying, you know, there are specific notes that are corrected pretty much on an ongoing basis. So, that's all I can say at this stage.

**Ankur:** Great. Alright, sir. Thank you so much and best of luck.

**Anant Talaulicar:** You're welcome. Thank you.

**Ankur:** Yeah.

**Moderator:** Thank you, sir. The next question comes from Pulkit from Goldman Sachs. Please proceed.

**Pulkit:** Yes, sir. Most of my questions are answered. Just one question after the finish of CapEx for this year, regarding the tax centre, next year, what should be an approximate number that we should be building in for capital expenditure?

**Anant Talaulicar:** Well, in fiscal year '19', I think, you could look at the step down and it will be somewhere in the 200 to 250 crores range.

**Pulkit:** Okay. Thank you, sir.

**Anant Talaulicar:** Welcome.

**Moderator:** Thank you, sir. The next question we have is from Sreenath from Motilal Oswal. The line is un-muted.

**Sreenath:** Yeah. Good morning, everybody.

**Anant Talaulicar:** Good morning.

**Sreenath:** My question is regarding again Cummins tech centre. You said that CIL will be receiving rentals at being the landlord. Is that the only revenue, was screen from this investment?

**Anant Talaulicar:** Not at all. In fact, see, a tech centre is not a profit generating activity...

**Sreenath:** Yeah, exactly.

**Anant Talaulicar:** per se, right. So, CIL will benefit from the products that it designs and develops in that tax centre.

**Sreenath:** Sure

**Anant Talaulicar:** And you'll see that in the revenues. So, that's where it's at, right.

**Sreenath:** No. So, I was speaking more from the direct line of revenue, that immediately, as soon as it gets commissioned, the direct line of revenue will be the rental.

**Anant Talaulicar:** That is correct.

**Sreenath:** Okay. So, there is no R&D charges which the parent will be paying CIL for?

**Anant Talaulicar:** No, no, not at all. Each legal entity takes care of its own expenses.

**Sreenath:** Right. Okay. So, can you give us a sense of the yield on this investment which we should expect by way ?

**Anant Talaulicar:** It should be better than non-treasury, about 8% or so.

**Sreenath:** 8% or so?

**Anant Talaulicar:** Yeah. We had brought in external auditors and they did a survey of market rates and et cetera. And we've gone by the rate wise. Obviously, the dependent members, the board et cetera, will get concern about those kind of things. So, we make sure that we are doing everything that is absolutely, you know, above board and honours the regulations.

**Sreenath:** Right. We should build in say, 8%...

**Anant Talaulicar:** Yeah.

**Sreenath:** before tax.

**Anant Talaulicar:** Yes, yes.

**Sreenath:** Yeah, okay. Thank you very much.

**Anant Talaulicar:** Okay. I think, we will take one more question.

**Moderator:** Certainly, sir. The next we have is Nilesh from Macquerie. The line is un-muted.

**Inder:** Thanks for the opportunity. This is Inder here. My question is on the exports given the weakness that we are seeing in this some of the markets. Can you give us a sense on what is the geographical mix? Have you seen the worst of the declines that we had to see in this, some of these key markets like Middle East, Africa?

**Anant Talaulicar:** What I would say is, first of all is, I don't think we've seen the worst in the low horsepower side.

**Inder:** Okay.

**Anant Talaulicar:** I do think, probably seen the worst in the high horsepower side. That would be one broad statement I'll make. You know, I could be proved wrong but this is my best view of the scenario. And then, when we look at it regionally, all our exports put together, I would say, the areas where we see the most struggle right now is in Africa and the Middle East. All the other seem to have stabilized and, you know, likely to, I would say, grow over a period of time.

**Inder:** Okay. Any number as to what is the contribution of Africa and Middle East in the exports and what was this number in percentage around a year back?

**Anant Talaulicar:** Well, you know when you look at Africa and Middle East, you know, they have significant, in terms of overall exports. So, somewhere, I would say in the 20% category is where they are at.

**Inder:** Both put together?

**Anant Talaulicar:** Both put together..

**Inder:** Okay. Thanks a lot.

**Anant Talaulicar:** Okay. You're welcome. So, will close with that now in the interest of time. And I do appreciate all of the good questions that have been raised and I hope I've been able to, you know, appropriately address them. So, in closing, I just like to say that, we are as Indians in a fortunate place. I do believe that despite, you know, some of the issues, we have a relatively far more responsible government which is focussed on trying to find the right balance between economic growth and the environment. Cummins certainly is benefitting from this government's policies. So, we support, you know, these policies, you know, strongly. And so, the domestic side of our business, I would say, will continue to see good growth. And on the export side also, I think, we have seen lastly the worst of times and over a period of time, we should start seeing improvements. We are very well positioned as a company because we have leading market positions based upon all the technology investments that we've been making over the last, over 50 years in India and about a 100 years globally. And so, we will continue to stay focussed on improving our competitiveness, our cost structure, our productivity levels. We have a very, very strong diverse and stable leadership team that is committed to this entity success. And, you know, you should count on performance that is above market and above what our competitors can do. So, with that, thank you very much for your interest in Cummins India Limited.