



Q3FY13 Earnings Conference Call

August 14, 2013

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MR. GVR MURTHY – CEO, ESCORTS CONSTRUCTION EQUIPMENT
MR. LALIT PAHWA – CEO, ESCORTS AUTO PRODUCTS
MR. DIPANKAR GHOSH – CEO, ESCORTS RAILWAY PRODUCTS
MR. BHARAT MADAN – CFO, ESCORTS AGRI MACHINERY
MRS. JYOTI KHATUKA – HEAD OF TREASURY FUNCTIONS OF ESCORTS GROUP
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MR. RAJEEV DASS – VP, CORPORATE AFFAIRS AND COMMUNICATIONS

Moderator

Ladies and gentlemen good day and welcome to the Q3 FY13 Results Conferences Call of Escorts Limited. As a reminder for the duration of the conference all participants' lines will be in the listen only mode and there will be an opportunity for you to ask questions at the end of today's presentation. Should you need assistance during the conference call you may signal for an operator by pressing "*" and then "0" on your touchtone telephone. Please note this conference is being recorded. I would now like to hand the conference over to Mr. Raghavendra Jaipuria from Perfect Relations. Thank you and over to you, sir.

Raghavendra Jaipuria

Good afternoon and thank you for joining us on Escorts Q3 FY13 Results Conference Call. Today we have with us Escorts Ltd. senior management represented by Mr. S Sridhar – CEO, Escorts Agri Machinery; Mr. Murthy – CEO, Escorts Construction Equipments; Mr. Dipankar Ghosh – Business Head-Railway Products; Mr. Lalit Pahwa – CEO Escorts Auto Products; Ms. Jyoti Khatuka – Head Treasury; Mr. Bharat Madan – CFO Escorts Agri Machinery; Mr. Saikat Mukhopadhyay – CFO, Escorts Construction Equipment and Mr. Rajeev Dass, VP, Corporate Affairs and Communication. We will start the call with a brief opening remarks from the management followed by an interactive Q&A session. Before we start I would like to add that some of the statements that we make today will be forward looking in nature. At this moment I would now request Mr. Rajeev Dass to make his opening remarks. Thank you.

Rajeev Dass

Ladies and gentlemen on this evening of our 67th Independence Day, warm greetings to all of you and welcome you for joining us on Escort Ltd Q3 and nine months FY13 earnings conference call. We will take you through the operating performance at the group level and division wise before opening the floor for the question and answer session. Ladies and gentlemen this quarter the company has delivered significant results on the back of a focused product strategy, operational efficiency, costs and rationalization and sales growth. At the group level Q3 revenues are correspondingly up by 16% and sequentially up by 17.5% as compared to Q2 FY13. Tractor volume stood at 19,518 in Q3 FY13 versus 16,083 in Q3 FY12 which represents a growth of 21.4% as against 14,764 in Q2 FY13 an increase of 32.2%. We have also done better on a nine-month basis too with a growth of 7.7% versus last year. This overall improvement in the results is due to measure taken; material costs stood at 71.7% in Q3 as compared to 73.2% in Q3 FY12 and 72.2% in Q2 FY13, a significant improvement both on sequential and on corresponding basis. EPS for the quarter stood at Rs. 4.89 as compared to Rs. 1.57 in Q3 FY12 and Rs. 3.14 in Q2 FY13, on a nine months basis EPS stands at Rs. 10.4 as that of Rs. 4.25 last year. Profit after tax was up by Rs. 39.8 crores to Rs. 58.3 crores in Q3 FY13 as compared to Rs. 18.5 crores in the same period last year, sequentially also it was up by Rs. 20.8 crores from Rs. 37.5 crores in Q2 FY13.

I would now like to turn to Escort Agri-Machinery division with a small snapshot. The growth seen this time was higher than expected on account of a good monsoon across the country along with higher minimum support prices for crop and favorable government initiatives. Key states that supported this growth are Andhra Pradesh, Madhya Pradesh, Chhattisgarh and Rajasthan. We remain strong in Northern India as well as North-Western India as before. We are committed to continuously upgrade our portfolio and with this regard we plan to launch improved version of our existing products in the coming quarters. The Ferrari tractor launched earlier this year saw a

heartening response from professional farmers and we now begin to see sustained demand emerging from this product. In order to expand our reach to customer Escorts has continued to expand its dealer footprint across the country, this has also resulted in a favorable business performance at an overall level.

Focusing on the profitability strategy, the company took two price hikes in the calendar year, once in February and then again in May, backed by response of its new product and enhanced dealer network. This was contrary to the discounting which other players resorted to and continued to do so in the last two months as well. We continue to diversify our offerings within the agri-division by initiating an entry in crop solution space, within this we will provide crop centric mechanization services in the coming future. Historically, this quarter has been strong for us and we were able to capitalize upon this opportunity by initiatives as discussed above. We believe that innovative products catering to the needs of the customer, enhanced network and service along with the operational discipline which the management has initiated will help us increase our foothold in this segment in the year ahead as well.

I would now like to turn to our construction equipment business. We are all aware of the challenges and the repercussions faced in this construction industry in the form of a slowdown, regulatory restrictions and the upcoming elections uncertainty, we continue to invest in product and product development and continue our focus in rationalizing working capital management. Macroeconomic headwinds have impacted our growth this quarter as we sold 718 units versus 1,138 units last year and 1,113 units in the previous quarter. We have initiated a number of actions to enrich our product profile, streamline our sales and marketing network and initiated several areas of value addition, value engineering which we hope we will result in a better performance in the months ahead. We hope that the recently set deadline by the Prime Minister's office for projects in key sectors of railways, roads and power will provide the much-needed push in this sector and this is the key to the growth of infrastructure business in India and we look forward to a much more healthier management of the infrastructure **economy** in the months ahead.

Turning to the railway division, the order flow from Railways continues to remain subdued. There has been no finalization of wagon orders from the board in 2012-2013, also no major tenders have been floated for the coupler business so far. At Escorts we are developing products for new generation rolling stock as we have seen a decline for the older generation rolling stock taking place. The Escorts, air brake system for the bogie mounted brake systems have been performing well in the fields since the last seven months and the commercial benefits will begin to accrue post the approval which we shall receive in the middle of 2014. The performance of the railway products have been satisfactory in this quarter with the income of Rs. 54 crores the growth of 37% versus the corresponding quarter and 18% sequentially. At the EBIT level stands at 10.1% which has expanded significantly by 247 basis points sequentially and by 803 basis points on a corresponding quarter to quarter basis. Our order book for this division has on 31st July stood at Rs. 51 crores which will get executed in next quarter.

Turning to the Escort auto product business, the automobile sector is reeling under the pressure of very high interest rates, diminishing spending, labor problems and regulatory burden which has led to sluggishness of the auto component manufacture like ours. Suppliers to medium and heavy commercial vehicles and passenger vehicles have been impacted the most. In order to brace the slowdown, Escorts Limited will focus on high margin products and customer segments to enhance profitability along with the increased focus on cost rationalization which has already helped reduce the material cost which is a major input for us. Income from this segment stood at Rs. 37 crores compared to Rs.44.3 crores in Q2 and Rs. 42 crores in Q3 though we did see a positive string of 73 basis points in EBIT margin in the nine-month period.

Our continued focus on operational efficiency and profitability along with increased volumes, better product mix and cost rationalization has led to an improvement at the EBITDA level and margins too. When compared to percentage to sales we have improved upon our raw material cost, employee expenses and other expenses, this has helped our margin expand by 256 basis points on corresponding basis and 246 basis points sequentially. Discipline on external funds has led finance cost to come down when compared on a year-on-year basis and quarter-to-quarter basis to Rs. 20.2 crores.

We at Escorts continue to focus on profitability, operational efficiency along with identifying and catering the needs of our customers with the new innovative products which will help us carve out a niche in the sectors we are present in and this will be supported by enhanced network and quality servicing to increase our foot holding and position.

Ladies and gentlemen now I would like to open the floor for questions to our management.

Moderator

Participants we will now begin with the question and answer session. We have our first question from the line of Jay Kale from IDFC Securities, please go ahead.

Jay Kale

Wanted to understand from you what would be the revised growth outlook for tractor industry for this fiscal starting from April to March 2014 and what are the chances of fair bit of moderation in demand going forward?

S Sridhar

Our operating period is October to September. I just want to bring in one degree of caution, this you would have seen even in the month of March everybody in tractor industry was projecting a bleaker picture and suddenly this quarter you see industry hitting 26%, this is because the October-December quarter was around 4% growth, the second quarter was -1% growth and then we have hit 26% growth, the reason for quoting this is it is very difficult to make projections on what will happen in the future, having said that since we have faced a flat industry for almost 2 years the revival is here to stay, this is the first confirmation I would like to make based on our assessment. Second is the projection of what should be the industry growth, since the industry is almost growing with 26% growth rate which means that this financial year is growing at 10% it is very safe to assume that the next years industry that is October to September industry also to grow at the rate of 10% to 12% kind of a growth rate, this in my view is a reasonable assumption.

Jay Kale

What could be the possible upside or the downside risk to this particular growth in terms of any development which are closer to election which can really drive the growth upwards?

S Sridhar

Since you're mentioning about elections, the first thing happens with elections are the money floats, lot of liquidity in the system, lot of expenditure happens, this also triggers a lot of growth, this we have faced election after election not only for tractors generally for automobiles and all other consumer durables. Whatever is happening now is the reverse, the market is tight and the liquidity are being tightened, so the election related signals are nowhere near to see. Having said that monsoon is a big plus and the customers are seeing better monsoons, this has put the sentiment on the hype. Second is the minimum support price, since the support price is sustaining and also the sentiment being high because of monsoon, there is a big advantage on the consumer mindset side. On consumer side so far there is no big evidence of coming out of the way to support, that is why 10% to 12% growth is a very realistic expectation for the next financial year.

Jay Kale

So there could be some upside risk to this number, if there is some government support which comes in?

S Sridhar

It can be on the downside as liquidity is tightened, you will see not only cars but trucks and bikes in the market gets crippled, it is anticipated because in my previous experience on the bike sector and other thing is that if liquidity gets tightened the whole industry's growth goes for a toss.

Jay Kale

If you can just throw some light on the state wise growth or the key states, not one quarter but the quarter so far till September, how has the growth been and which states have started to come back in the green. You mentioned about a few states doing extremely well, if you can just quantify to the top five performing states and the states which in are laggard at this point of time?

S Sridhar

We cannot talk on the basis of a particular quarter because some of the states are doing well on a year-on-year basis for almost 18 months in a row. States like Madhya Pradesh and Rajasthan, they have been continuously doing very well, and the good thing is almost all the states are showing positive signs except few belts like Karnataka, Tamil Nadu and maybe part of Maharashtra, overall the country seems to be growing which is a good sign. We expect a aggressive growth possibly from the South and West in the states like Andhra and Maharashtra, the big growth will come from there because of two reasons, their basic infrastructure like credit and money are generally very good and these are the states which had also suffered because of poor monsoons for the last one or two years. We should expect going forward that the Southern and the Western zones to do very well otherwise the whole of the India is almost on a revival mode.

Jay Kale

If you can throw some color on your balance sheet in terms of what is your current debt, what you have in the books and what is the kind of debt repayment roadmap or the kind of target what you aim to have by end of this fiscal and the end of the next fiscal?

- Bharat Madan** We have close to Rs. 400 crores of debt on the balance sheet, roughly in terms of repayment we have Rs. 70 crores to Rs. 80 crores of repayment happening every year.
- Jay Kale** So Rs. 70 crores to Rs. 80 crores, can't we pay on higher terms, can we repay the debt much faster given the kind of buoyancy what we are seeing in the business?
- Bharat Madan** Will take a call as and when the performance happens, so based on that we can take a call and always do that.
- Jay Kale** Any plans of any divestments or something like that?
- Bharat Madan** There are fresh CAPEX also happening and new projects are under way, so in terms of overall debt situation even if we paid there will be fresh borrowings also happening so overall I think we would still remain in the level of Rs. 300 odd crores.
- Moderator** Our next question is from the line of Rishikesh Chopra from India Capital, please go ahead.
- Rishikesh Chopra** Although the last year numbers were quite good but there were concerns about the inventory buildup, so what is your take on that?
- S Sridhar** This is especially to Escorts you are asking?
- Rishikesh Chopra** Yeah.
- S Sridhar** We have not been building inventory, in the last two years we were the first to drop the inventory that means that after Quarter 1 2011, we were the first to sense a downfall and we immediately corrected our inventory situation. So as far as our inventory with the dealer, it is a very stable inventory which is minimum required and that is what is being built. It is a very steady state inventory neither less nor more.
- Rishikesh Chopra** If you can give me a number, what is the change from last quarter to this quarter in your inventory?
- Bharat Madan** We remain in the level of 10 to 12 weeks. That is the norm and this includes the advances that the dealer gives to the customers, so we remained in that range only. In the last quarter it was the similar level and in this quarter also we are not anticipating any change in the level.
- Rishikesh Chopra** There has been a concern that there is no MRP on tractor, Ministry of Heavy Industry they are going to come up with the notification, so are you planning to put an MRP on the tractor?
- S Sridhar** Maybe we are not aware, but the current situation is it still continues to be a highly intense competitive situation; nobody sells on MRP everybody is selling on a discount, this really does not alter the situation as on today.

- Bharat Madan** But the issue is also on the transparency that the ministry is trying to really put on the manufacturers, and from our perspective and many players in the industry are also doing it. We are advertising retail prices in the market in the newspaper and even the NBFCs who are financing the tractors, there is an MRP which is already shared with those NBFC's and therefore information is already available. So it is not that there will be any issue of non-transparency, but yes from Ministry's perspective if it comes it is not going to effect the industry as such.
- Rishikesh Chopra** Are you providing any current discount on the tractors like as Mahindra & Mahindra is giving Rs.40,000 discounts per tractor?
- Rajeev Dass** No, we do not have a strategy to do any of that.
- Moderator** Our next question is from the line of Nishant Vyas from ICICI Securities, please go ahead.
- Nishat Vyas** My first question is in the farm equipment segment, could you give us some kind of detail outlook as to what is the crop solution business that you are trying to venture into and what is the strategy and how are you building up on increasing your portfolio towards the farmer?
- S Sridhar** First and foremost the crop solution story is a long-term strategy, long term meaning anything beyond three years and above, three years to 10 years outlook. What we're trying to do is, generally all the manufacturers sell equipment that goes with the tractors that is the emphasis like the rotavator that go with the tractor, in our case what we have done is we start adapting at the crop level, and this is what we call it as crop centric solution. For example first crop what we have adapted is paddy, this itself will call for around 9 to 10 equipment to give a complete solution, we also have tied up with various best manufacturers in the world for those kind of machineries we adapt and then be given it to the customer to experience it, this is a very different way of doing it. The initiative was started two years back, now there is 80% perfection in terms of the exact solution we are offering to the customers, this will lead into various modifications in machines. Depending on the market demand we will start manufacturing it, collaborate it, and give solutions to the individual customers on a lease basis not in terms of owning it, so there is a host of actions around the crop solution but the entire action in the minimum time. We will see a tangible result only after three years so nothing should be expected immediately.
- Nishat Vyas** Is my understanding correct; will your trading component of the business increase because of this?
- S Sridhar** Trade in terms of?
- Nishat Vyas** Because you will not be producing these products, the other equipment that you do not produce will have to purchase and sell it at a trading margin, is that correct?
- S Sridhar** Yes, that will also be there.
- Nishat Vyas** So affectively that will be effectively a margin dilutive to the core business?

- Rajeev Dass** You can say that but that will be very temporary phenomena before the indigenization program kicks in and all of that happens.
- Nishat Vyas** But that would be at a later stage obviously because of the start it will be more of a trading portion, right?
- S Sridhar** First thing we will not be making a lot of money. The size of the crop equipment is so small the players who are operating there are all making big money, in the correct situation the business has to explore in terms of not 10 times it has to explore in terms of 100 times and on the later stage the money should be made. The crop solution as the subject itself is under survey we are just scratching the surface, the technical answer to the question is you will make money but it is **just** scratching the surface since it is on the evolution stage. It is to make a significant impact to the bottom line in three years onwards and not in the short-term.
- Nishat Vyas** In terms of dealer network, could you tell me what is the current dealer network and what is the target for the next two years?
- S Sridhar** In the dealer network we already have around 700 dealers, we have also added 200 dealers and then deleted 80 dealers in the last two years. Our main aim is not only appointing the dealer but also bringing in the right quality of dealers, like emphasis is on the right quality of the dealer and also a territory like South and West will become a focused territory. With the kind of products that we are launching, this will go hand in hand. Just by appointing a dealer the assumption of selling more, is an incorrect assumption so we will be doing as a package act.
- Moderator** We will take the next question from the line of Amitabh Sonthalia from SKS Capital and Research, please go ahead.
- Amitabh Sonthalia** Just a couple of quick questions one is on your latest shareholding post restructuring, just required a clarification on what is the direct stake of the management and what is the breakup in terms of treasury stock and other stocks held this part of the employees benefit trust etc?
- Bharat Madan** The shareholding breakup is given every quarter to the stock exchanges, in the last June also we have intimated to the stock exchange.
- Amitabh Sonthalia** I just want to understand what is the management view on the current promoter holding in terms of direct holding versus indirect holding and what would be the direct holding of the promoters and indirect holding?
- Bharat Madan** The total shareholding for the promoters is 42% that includes the share held under the trust.
- Amitabh Sonthalia** Who are the ultimately beneficiaries of that trust?
- Rajeev Dass** Escorts Ltd is the beneficiary of that trust.
- Amitabh Sonthalia** The company itself?

- Rajeev Dass** The company itself is the beneficiary and the independent directors who are the trustees on the board or who are the trustees of this trust call the shots on this. If you really look at the holding that the promoters have, it will be in the region of 8% or 9% and the balance is of the trust that has been created on the treasury stock.
- Amitabh Sonthalia** So 9% is a promoter holding
- Bharat Madan** 30% odd is the Trust and balance 11% to 12% is the promoters.
- Rajeev Dass** Those are the ballpark numbers.
- Amitabh Sonthalia** So the question was, essentially as you said Escorts Ltd is the beneficiary of 32% odd trust holding it is effectively treasury stock? Effectively when a company owns its own shares or the company is effectively the beneficiary it's kind of like treasury stocks?
- Bharat Madan** That is our intention it is right.
- Amitabh Sonthalia** So treasury stocks will also be minority shareholders and the promoters in equal proportion let's say to the extent of promoter holding of 10% out of this 30%, so promoters effectively hold 12% of the company?
- Rajeev Dass** I think, ballpark, yes, I think it is around that number.
- Amitabh Sonthalia** So what is your view on that, how is the promoter interest aligned with that of minority shareholders then with a low holding in the company and in the past also you have done a fair bit of restructuring to further dilute the minority shareholders?
- Bharat Madan** We can discuss this off-line as this call is for discussing Financial Results
- Amitabh Sonthalia** In terms of the treasury stocks what is the long-term solution, I mean, in management's opinion remain the way it is?
- Bharat Madan** Treasury stock was created to avail any opportunity which may arise in the future on M&A front when we can use this stock at that point of time. It will also depend how the company performs going forward, what is the value we have in that stocks and what opportunity comes our way. We will take a call going forward based on that, maybe in the next 4-5-10 years.
- Amitabh Sonthalia** But at the moment in the foreseeable future there is no intention of the management to increase their stake into the company directly or otherwise?
- Rajeev Dass** That is right.
- Moderator** We have a next question from the line of Arvind Sharma from Citi Group, please go ahead.

Arvind Sharma

Looking at your agri-machinery products in segmental results, there has been a significant uptake in terms of margin my question was what is driving these margins, is it mix pricing or cost pressure and what are the cost pressures scenario right now and how do you think it will shape up going forward?

S Sridhar

If you compare some 6 quarters back or two years back it was around 6% that is the kind of margins we were making. We are currently at 10% maybe for the nine months and maybe at 11.5% for the quarter, so to that extent we have almost closed to near doubling up our EBIT margins. The way we have done is in a way generics we squeeze a lot of cost structure, also we talked about the increasing of our pricing, so when nobody has increased the price from the last six months or eight months we went ahead and increased by Rs. 9000. Rs.2000 in the month of February and another Rs.7000 in the month of May, Rs.9000 is a pretty sharp price increase we took, this is the first action. And also when the competitors are reducing the price by Rs.40,000, we have not responded to it. In fact, we were even letting our market share go by 0.2% or 0.3% but not resulting into actions like responding to the pricing pressure imposed by competition. How exactly we have achieved this, you would have seen the cost compression through material cost and other things we have been already discussing in pricing power. Whichever category we are operating like C category which is the largest category, 30% of our segment is from C category which is around 35 to 40 horsepower category, in this segment 50% of our volume mainly will be coming from a model which is the very high priced model for the segment which we call 439 DS+ this is a most expensive model and that model contributes around 50% of our volume. In other words it is not only our explicit strategy to target the E and E+ category for leadership, within the high-volume category also our models are priced very high and we will stick to that. Profitability is our obsession; this is the demonstration of the route what we're taking. Now when the industry is reviving there is an opportunity for everybody. Those who want to target the largest number or those who wants to target market shares can target whereas Escorts wants to target the profitability and that the plan to move forward. The direct benefit is in terms of margins, indirect benefit is in terms of imagery. For us these two are most important guiding principles and this is the way we will proceed further.

Moderator

Our next question is from the line of Silky Jain from Nirmal Bang Securities, please go ahead.

Silky Jain

Can I get the CAPEX plan for the company for this particular year as well as FY14?

Bharat Madan

This year we are expecting the year to end with the CAPEX of roughly Rs.100 crores and a similar number for next year also Rs.100 to Rs.120 crores, i.e. all our businesses put together.

Silky Jain

You were talking about the HP wise distribution of tractors so is it possible that we get the percentage as in how much is in 30 to 40 or 40+ and 50+ HP tractors?

S Sridhar

This we should access through TMA only.

Rajeev Dass This Tractor Manufacture Association puts out these numbers, right now it is not on my table but I can e-mail this to you.

Silky Jain If you could tell us how much were the sales for the Ferrari and farm track executive?

S Sridhar The Ferrari is targeted not on the mass segment because a compact tractor or 25 HP tractors are the wine yard tractors. The price what Ferrari charges is nearly double that of the nearest competitor for example Kubota or any other model, so we will double the price. The important thing is the kind of an imagery rub off that it creates for Escorts because our objective is to bring in many such brands which will be giving this kind of an imaginary rub off on leadership. Now our plan of a Ferrari model is to sell something like a 100 in a year, we have already exceeded 50 kind of a number. Right now I think the customers are put on a booking and this is the kind of a response we have received. That means the target number of 100 in a year what we wanted to set out, it looks like we will be exceeding those kinds of numbers.

Silky Jain This 100 target was for the calendar year?

S Sridhar Escorts financial year.

Moderator Our next question is from the line of Sameer Deshpande from Fair Deal Investments, please go ahead

Sameer Deshpande The results are really excellent and the company seems to be on a very good vibrant growth momentum and particularly our agri-machinery business and as our conference calls progressed for last 3-4 times, I have seen the lot of things which the initiatives the company has been taking resulting in good profits and the segment margins for agri-machinery 11.65% which is really worth congratulating you all people for the effort and despite the tremendous competition prevailing and the industry trends which seems to have changed for the better now, I think, we have capitalized well on that. So my question is our total volumes last year were some 57,000-58,000, this year we expect to do around 10 to 12% so we will be something like 65,000-66,000 may be in volumes, this still constitutes only 55% of our capacity utilization. And secondly we also have diesel engines which we use in our tractors that diesel engines spare capacity is also substantial, so how are we planning to use these spare capacities because when these spare capacities get used by even 10% or 20% our margins really crossed 10% or 11% for the entire blended margins, particularly agri-machinery can grow substantially and other also, kindly elaborate on that?

S Sridhar We have certain guiding principles for our company. First and foremost, the demand, we should not chase the capacity, utilisation of capacity is not the obsession, this is in our view in yesterday's model, create capacity and then utilize capacity and take that as a basis for creating profit in our view is not the correct view, so first is we will generate a demand and the profitable segments, sustainable demands (and those kind of demands creation is what we will create) and the capacities will chase the demand not the vice versa. The reason for mentioning this is, this is the way Escort will proceed in the future not the way we have operated in the

past. This would mean that the current capacity may be relevant or may not be relevant because when I'm saying not really relevant is because the kind of a product you will be needing is a very high technology, different kind of product with a different fits and finish, different Italian designs what we are trying to introduce or tomorrow it is a product like Ferrari if the volume support which we can even assemble, so what is most important is our aligning with highly profitable future segments, this is what we are going to do. As far as engine capacity is concerned due to the excess capacity in the market and so much of competition intensity, the pricing pressure is immense, so even in engine area where we do not see that kind of margin with a 10% or 11% margin we do not participate in those kind of competitions. These are all certain internal discipline we have brought in among ourselves and then we will start looking forward where there is a space, non-competing space, profitable space that will become our governing principle and we hope with the industry moving further, there is enough space to reasonably utilize the capacities the way we wanted to grow in the market.

Moderator We have a next question from the line of Riken Gopani from Infina Finance. Please go ahead.

Riken Gopani Just wanted to understand more on the Agri business margins, one is given the kind of strong volume growth, the leverage on the other expenditure doesn't seem to have come, and the other expenditure is grown almost like 35% YoY, if you could highlight what are the various pressures that you have seen their and what improvements can be seen going ahead?

Bharat Madan On the cost side you yourself said that the volumes have gone up, so all the variable cost in the systems also go up with the volumes. When you look at the cost going up by 30%- 35% that is also because the volumes have gone up. If you look at cost as a percentage to sales, overall cost whether it is personnel cost or it is selling and administration cost both have come down.

Riken Gopani What I meant is that there should have been some leverage that you could have got on the other expenditure with such a large volume expansion?

Bharat Madan That leverage is best represented in EBIT margins, which have gone up by about 3%.

Rajeev Dass Last quarter it was around 8% to 8.5%, current quarter we are looking at 11.5% plus, so you have seen the cost management and easily 1% to 1.5% may be little more will be on account not to mention the raw material cost management which is where the initiatives has borne a lot of fruit, a lot of work is happening there since that is the largest chunk of cost in any case.

Riken Gopani How are you seeing the raw material scenario panning out and have we seen most of the improvements come through or you see further improvements and any internal exercises that should further help you improve on the raw material side?

S Sridhar One is to see external situation. Number two, how do we internally improve the processes and how do we work? As far as internal goals are concerned we have much steeper goal to cut down the material cost for existing products, that is a part of our three-year plan, for example around 71.5% where we are today we wanted to reach 68% this is a goal as I said we have to

work on it. Lot of initiatives on this, just in time and in massive inventory reduction, a lot of things are going on. Also the fact is the overall industry is not doing well, so that is also giving us an advantage, both together is the benefit what we are deriving.

Riken Gopani

The other question is to understand what has happened on the export side, what proportion of our tractors are now exports and what is the outlook there?

S Sridhar

In exports, all that we have done in the last one and half years is to set our house in order when domestic business is concerned. We are very clear on which segment to operate, which to product offer at what price point and how exactly it is happening. Still markets like Andhra Pradesh and Maharashtra we are yet to crack, so there is an agenda for India is what you set in place. As far as exports are concerned, the strategy level working was started two quarters back, today we are fairly clear on what should be our approach. Having said that between the approach and realization it is still a one year away from me that means at least we will take 4 to 6 quarters in terms of what will exactly happen. Now having said that if you were to have some insider view of what exactly is our export strategy, you are most welcome on our Germany conference in November 11 where we will unveil global strategy for Escorts Agri-Machinery Division.

Rajeev Dass

It is very significant event and we invite you there. Hanover Agri Techniqua on 10th November to 16th November is where we will afford ourselves the opportunity of unveiling our global platform and our global brand connect. Most welcome to come and visit our press conference and our product display and our visibility on our Europe and North America strategy.

Riken Gopani

The other point is also on the railway side just wanted to get your thoughts, there has been a significant improvement in terms of both top line and the margins, if you could highlight how would the next year pan out in this division and is this improvement sustainable?

Dipankar Ghosh

Yes, this improvement is sustainable but we will not see any major increase out there because we have launched few new products but as you would appreciate our railways goes for a 18 months validation period so most of our new products are in the validation cycle, we expect them to actually be commercialized only by end of 2014. We would not see a major upstart for the railways but yes, going forward we see a very bright future for our railway division.

Moderator

We have a next question from the line of Bharat Gyani from Sharekhan. Please go ahead.

Bharat Gyani

I just wanted to get a flavor on your regional mix, how it was three years back and how it has been today, like the southern market the market share was less, so if you could just give me a flavor on your regional market share as of today?

S Sridhar

Six year to eight years. In the regional mix there is no change, we are predominantly a North based company, the weak spots remain as South and West, this situation has not changed for past 6 to 10 years yet. Our market shares and those zones are something around 3% or 4% as against 14% or 15% approximately in the area where we are strong, this are the gaps today.

Having said that, now that we have to start making some money we should expect action may be from next year onwards; this is again a three year action plan. What did not happen for 10 years or 20 years cannot happen a few quarters and few years. All that what I am confirming is the way we have put product strategies in place, slowly start anticipating market strategies also to be put in place starting with one or two states from the next financial year onwards.

Bharat Gyani

If I could get a mix as our strategy is targeting the higher HP range, just wanted to know on what is our contribution of the overall volumes from the above 40 HP space now and how was it say 2 to 3 years back?

S Sridhar

We have some A, A+, B, C, D, E, E+ this categories goes in tractor industry but within that E and E+ category it is considered as an end-higher end category. In fact, the E category for example Escorts average market share is 20%, E + category we are almost around 5% to 6% so our explicit strategy is to become a leader in these two categories over a period of three years, this is what we have been disclosing. Our internal target if I had to say is to touch around 33% market share in this E and E+ category within three years, this will give not only the money but also the kind of imagery rub off what we are looking for. Another important categories, we have talked about is C category, C category is another area which contributes close to 27% to 30% of a market share. Within this category which ever portfolio which Escort is presenting which we call power track and others, 50% of our portfolio is the most high-priced portfolio within the C category, this is the way we target markets and then we develop it.

Bharat Gyani

I just wanted to get a sense about the market shares, can you provide the overall proportion of the Escorts volumes what would E and E+ category currently contribute in terms of your overall volumes, just a mix?

S Sridhar

50%.

Bharat Gyani

50% is currently contributed by E and E+ category. What was this proportion 2 to 3 years back? Just a ballpark number.

S Sridhar

Should be around 17 to 18% return. If you look at it historically, means 15 years back, we had a market share of around 40%-45% in this category. It was our category, we lost it to the many of the multinational, now the claim has become steep because for sometime we were not doing well, now we have to claim back and re-claim what was our rightful market share once upon a time that was objective of 33% approximately of a market in three years.

Moderator

Our next question is from the line of Basudeb Banerjee from Quant Capital. Please go ahead.

Basudeb Banerjee

If I look at your fixed cost per unit on a QoQ basis, specifically if I take staff costs and other expenses as the fixed cost broadly remaining non-variable, your EBITDA per unit saving QoQ is around 29,000 which is somewhere around more than 5% of sales, so one can see that it contributed significantly to the margin as volume moved up 14,700 to 19,500. Coming to the July volume which was around 4500 and if that kind of sub-5000 run rate continues for the

coming quarters so overall volume coming back to say March quarter territory, how can one assess the risk that is cost per unit will go back to March quarter levels and margins will again go back to the square ones?

Bharat Madan

Coming specifically to manpower number, with the regular workers whose average wage is Rs 40,000 per month, we can achieve certain level of production volume, when the volume goes up we hire casual labour whose average cost is Rs. 10,000 per month. So I would say when the volumes go up you will get those synergies, you will hire casual labour and the average manpower cost per tractor will go down but when you go back to the same level of numbers then obviously that cost will again go back.

Basudeb Banerjee

So now where do you see the volumes broadly in the coming few quarters post the good set of monsoon is now?

S Sridhar

As I said, this is a huge guess when we are making it as an industry, we said 10% to 12% of a growth rate for the next financial year is a reasonable assumption. You can expect Escort as I said we wanted to be choosy on which segments we want to participate on what we want to do, broadly you should expect us to be on par with the industry.

Basudeb Banerjee

If I look at your quarterly interest outgo, it is somewhere around Rs. 20 crores and as per your March balance sheet your short-term borrowings and long-term borrowings, combined was somewhere around Rs.400 crores- Rs. 450 crores it signifies cost of debt significantly high, am I missing out somewhere?

Jyoti Khatuka

This is the total Finance Cost, what you are comparing is the interest cost on the borrowings and the number Rs. 21 odd crores is the total finance cost, it includes non-funded utilization like LC or DC or my bank charges also, so a comparison in net to net if you take Rs. 400 crores of borrowing and you compute the interest cost that will appear to be very high, it is not a true comparison.

Basudeb Banerjee

So how much of this Rs. 20 crores quarterly is allocable to the long-term

Jyoti Khatuka

Borrowing cost you can assume term borrowing is around 13.5%.

Basudeb Banerjee

And any short-term debt in the other current liability line item of your balance sheet?

Jyoti Khatuka

That would be the debt repayable in next one year is taken as the current liability.

Basudeb Banerjee

How much is the quantum?

Jyoti Khatuka

It would be something around Rs. 80 crores.

Moderator

We have our next question from the line of Mahantesh Sabarad from Fortune Equities. Please go ahead.

Mahantesh Sabarad This pertains to your vast margin improvement demonstrated in tractors this quarter. I know you have discussed this in part and explained that it is primarily the price increase on tractors that has contributed to this improvement. But with 10 to 12 weeks of stocks that you seem to have right now, is there an oncoming discounting pressure, number one, and secondly, what are the material costs pressures that you are witnessing, there seems to be virtually no increases on the material cost front?

Bharat Madan On the stock side with dealers, what we said was that 10 to 12 weeks of stock with the dealer also includes advances. In tractor industry there is a unique trend where the customer is advanced a tractor and based on that more or less the sale has already happened, the only thing is that it not treated as a closed sale. The total 10 to 12 weeks' inventory also includes such advancing which happens in the tractor industry. So the dealer gives advance tractors to the customers without invoicing but practically that sale is already closed, so most of the advances actually turn into the retail sales, with a 90%+ success rate. So that inventory is already sold and today practically the dealer has physical inventory of only four weeks which is not a huge inventory at all and is a normal trend for us. Therefore on the stock side we don't see a pressure coming in for discounting because of that reason.

Mahantesh Sabarad And what is if there is a default on those advances, does that fallback on Escorts as a company or the dealer absorbs it or the financier of the dealer absorbs it?

Bharat Madan Dealer gives tractor to the customer and normally take their land paper or other mortgage papers from the customers, so the chance of default is very very low that is why I said success rate for that advances converting into retail is 90% plus.

Mahantesh Sabarad 10% NPA is still very large number?

Bharat Madan 10% advances is a normal trend in the industry which is already happening, there is nothing new which is going to happen now.

Mahantesh Sabarad So in short you are suggesting no discounting pressure is being seen ahead?

Bharat Madan Not in our case at least, we can't tell about the industry what their inventory levels are. But atleast that's not the case with us.

Mahantesh Sabarad What is the raw material cost pressure for you?

Bharat Madan As of now because of the slowdown in the overall Auto industry we are not facing any pressure from any suppliers. Also we don't foresee a pressure is next 6 to 9 months unless things really go out of sync and suddenly demand picks up. As of now we don't see those pressures coming in and building up.

Mahantesh Sabarad The other query I had is that based on the segmental results that you have provided and assuming that the agri-revenues pertains to tractors alone, then the average realizations seems to have dropped sequentially, so from 5,12,000 odd to about 5,06,000 odd per tractor?

- Bharat Madan** It is around Rs.6000 drop because of the product mix and there is a corresponding decrease in the material cost also.
- Mahantesh Sabarad** No, that doesn't seem to be the case because your EBIT per tractor has vastly improved. On an incremental sales, when I go sequentially, the new tractors that you seem to have sold for the quarter is at an average of Rs. 4,88,000 which is far lower than what your average rate is. So that means the mix has apparently deteriorated and yet you have seen a substantial increase in EBIT margins, so somehow can't seem to understand this?
- S Sridhar** Let me explain this, we have talked about two things on pricing power. One, we have said we will target segments like E and E plus. The second one, which I have stated earlier is the largest segment, the C category, it is 30% of the industry and within that also I said we introduced a model which contributes 50% of our portfolio is a high-priced model within that industry. The highest priced tractor in the large segment C category belongs to Escorts today that also gives you a lot of money, I cannot put out the precise money, there is a huge improvement in what we call power track kind of a brand which is 439 DS plus kind of a model, so this model even though this is not a E or E plus category but a C category model but the margins have shot up.
- Mahantesh Sabarad** The price positioning or the premium positioning that you are taking on this particular model will give you what kind of advantage, Rs.10,000 advantages or is it Rs.50,000 advantages?
- S Sridhar** That I don't want to disclose but it is substantial.
- Mahantesh Sabarad** That brings me to the question that is this positioning going to remain sustainable because the competitors will come in with their own models there to take an advantage?
- S Sridhar** That is the challenge of being in business, nothing is static everything will get questioned. Having said that people have got certain approach, philosophy or a guideline what they have. Somebody targets overall volume; somebody targets only the profitable slice within the segment, somebody will target the E or E plus segment, MNCs have a different way of approaching subject. There is a unique position for each one of this company and we said Escorts will target the profitable slice within the segment and this is our way, this is what we said is the way we are governed by. Hopefully the same thing you may not hear from Mahindra, which may be targeting a very different cup of tea. So each company has got their own way of approaching business and this is why you would profitability will remain as our obsession for some more years to go.
- Mahantesh Sabarad** Just wanted to understand are you suggesting that for the next three years you would continue to maintain 11%-12% kind of EBIT margins on tractors?
- S Sridhar** Certainly that is not our target, our target is to move up further and further. Whatever we are discussing now is all in public domain. One and half year back itself we said in a period of three years or four years we will touch something like 15% EBIT margin and now what you're

seeing what quarter after quarter is the movement towards it. Now we are only giving you the rational of how we are moving but otherwise the management objective is to reach something like 15% EBIT margins in two years from now.

Moderator We have the next question from Sunil Jain from Nirmal Bang Securities. Please go ahead.

Sunil Jain My question relates to your construction division, the sales have come down drastically, no doubt the environment is not so great in this particular segment. But how do you see this going forward, how much more downfall can we see from here and how are we planning to keep protect ourselves to what is happening in the market?

Saikat Mukhopadhyay We feel the market from here till the general elections looks to be pretty static at this point of time and the number that currently we're doing is the bottom hopefully. Though our reading says that the current volumes will continue till announcement of the elections and from there onwards things will gain momentum.

Sunil Jain Is there any cost-cutting possible because the EBIT margins in this particular division have come quite low this time?

Saikat Mukhopadhyay If you compare it from the last financial year we did have significant achievements in variable as well as the fixed cost reduction. We will continue to optimize our costs and you can compare it from a year-on-year basis our costs have come down and the major part of it is under control.

Sunil Jain About another segment that is auto ancillary, no doubt we have seen some improvement in the last two quarters, but this quarter again the pressure has come back. Can you throw some more light on our strategy for this?

Lalit Pahwa The auto OEM industry and therefore the component industry has seen one of the toughest year in the last decade. Infact industry leaders are saying they have never seen such a bad year in recent history, so you have to see our performance in that backdrop. We have been holding onto our top line in fact, improving a little and also the bottom line. So as soon as the industry turns around, there will be a significant upside, both in the top line and bottom line.

Moderator Our next question is from the line of Kiran Chedda from Value Quest Research. Please go ahead.

Kiran Chedda If I heard correctly you set the industry is growing at about 26% in the tractors?

S Sridhar We talked about Q3, this is one quarter excess, previous quarter it was -1%.

Kiran Chedda But our sales seems to have grown only by 21% so where is the disconnect?

S Sridhar No disconnect, this is our choice.

- Kiran Chedda** We have grown slower than the industry?
- S Sridhar** Of course, if it is so let it be. We want to pick and choose on the segment and on the slice where we wanted to grow. If not certain price we participated in certain segments, we wanted to grow in that way, this is what has happened, so that is our approach.
- Moderator** Our next question is from the line of Viraj Kacharia from Securities Investments. Please go ahead.
- Viraj Kacharia** My question is on agri-business, we have three plants and now we are operating out of two plants. So what is your view on the third plant, are you trying to monetize it, if you can just provide some color on that.
- S Sridhar** Right now what we're doing is from the point of view of waste elimination, duplication elimination, movement elimination. We are trying to bring in highest productivity level with a lot of emphasis on outsourcing; this is an obsession with which we are doing. Now what to do with the plant, we will decide on what more to do. There are a lot of opportunities knocking at our door, what kind of possibilities, what kind of other businesses which are aligned to agriculture, opportunities are there but we will take it as and when we are ready for it. So as I said many experiments are on, certain things are close to completion, certain things are under preliminary stage. So how to use this is still one year away but for now the consolidation as a means of reducing unnecessary cost in the system is an approach we're taking.
- Viraj Kacharia** For the crop solution, are you trying to move further into the agri-value chain or offer different products, what is the company looking at?
- S Sridhar** Generally the tractor manufacturer take the approach of putting the tractor in the centre and then decide on the equipments which will go with tractors, this is the way they all sell their equipments. In our we put the crop in the centre, for example we put paddy in the centre and see there are 10 set of equipments that will help the paddy and this is what we call end to end solutions, it is from tilling to the level of bailing, harvesting there are lot of equipments are this, Now we are amassing this total solutions through various collaborations, various arrangements so that the customer can experience a complete mechanization experience. Having said that, today we are almost one and half years old and still have three years to go before we make a meaningful impact on our balance sheet.
- Moderator** Our next question is from the line of Kaushik Poddar, KB Capital Markets. Please go ahead.
- Kaushik Poddar** Whatever I heard from you people it seems the tractor division will be only the driver for profitability, do you agree with this comment?
- Rajeev Dass** well it depends. Significantly, we would have to say yes for the near term only, till we see the improvement in the infrastructure side and on the auto component side.

- S Sridhar** Let me have a little more. Within that agri- machinery you would have realized strategy is our ace, we know how to take this thing and then crack it otherwise this kind of magical jump of something like as low as 4% to 5% EBITDA becoming 12% EBITDA in two year is impossible, the similar thought, the similar idea is being exercised in our infrastructure division, maybe they will take a couple of years but the direction is not very different. So what we are perfecting in one division is what we should expect for other division. In terms of time, of course they are lagged by one and a half to 2 years. A similar impact of what you seeing in the tractor division can be expected in the construction equipment too with a lag time of one and half to 2 years.
- Kaushik Poddar** So does that mean that you're looking at a premium positioning in other sectors as well?
- S Sridhar** I think you have guessed it rightly so, but the way we are talking about the tractor division is because it's seized, frozen, and practiced so we are sharing with you.
- Kaushik Poddar** Absolutely, we can see the results. So what you are saying that the same kind of premium positioning strategy will play out probably three to four quarters from now?
- S Sridhar** But only thing is that we cannot disclose more, but one can anticipate a similar maneuver in the construction equipment as well.
- Moderator** We have our last question from the line of Nishant Vyas from ICICI Securities.. Please go ahead.
- Nishant Vyas** I wanted the utilization levels in the other than agri businesses?
- Rajeev Dass** Other than farm you are talking about capacity utilization?
- Nishant Vyas** Yeah, capacity utilization levels?
- Saikat Mukhopadhyay** ECE right now we would be doing about 50% or so.
- Nishant Vyas** In the railway equipment business?
- Dipankar Ghosh** Railway equipment business we are somewhere in the range of 50% to 60% utilization. But we are expecting new products to kick in which we have already introduced to railway and are under the product validation and evaluation stage. So next year or so we should be able to take it up much higher.
- Nishant Vyas** Also had one last question on the tax rate what do you see for the annual basis, what kind of tax rate should we kind of envisage for the company and maybe for next year also? And do we have any tax benefits that we are availing?
- Bharat Madan** We have the R&D benefits which we get in tax plus whatever carried forward losses are there, But you can take 20% to 22% as the effective tax rate for this and next year because the tax

benefits which you get in R&D expenses that is a 200% rebate and in the March quarter we got two years benefit since the approvals came from the government only in the March quarter so that is why our tax rate there was negative actually. Going forward we are assuming this effective

rate of 20-22% will continue.

Moderator

Participants that was the last question. I would now like to hand the conference over to Mr. Rajeev Dass for closing comments.

Rajeev Dass

Ladies and gentlemen we thank you for being with us today. To put it on a lighter note we have exciting times ahead and for all our businesses but let me on behalf of Escorts Ltd and our senior management team assure each and every one of you that you are more than welcome to reach us for any queries, information that you would like or you would like to visit our plant or you would like to have a greater understanding on our unfolding strategy across our four businesses, you are more than welcome to reach me or come down to Faridabad at any time and having said that I once again on the half of Escorts, thank you for your patient listening and for a time and all the very best for coming Independence Day.