"Escorts Group Q2 Conference Call"

May 4, 2011

MODERATORS: **MR. O.K. BALRAJ**
MR. ROHTASH MAL
MR. VIKRAM SINGHAL
MR. K.K. VIJ
MR. HITESH GOEL

Escots Group
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Moderator: Ladies and gentlemen, good day and welcome to the Escorts Q2 conference call hosted by Kotak Securities Limited. As a reminder, for the duration of this conference, all participant lines will be in the listen-only mode. There will be an opportunity for you to ask questions at the end of today's presentation. If you should need assistance during the conference call, please signal an operator by pressing "*" and then "0" on your touchtone phone. Please note that this conference is being recorded. At this time I would like to hand the conference over to Mr. Hitesh Goel, thank you, and over to you sir.

Hitesh Goel: Thank you. I would like to welcome the management of Escorts for Q2 results conference call. Today we have with us Mr. O.K. Balraj Group CFO Escorts, Mr. Rohtash Mal Executive Director Agri Machinery, Mr. Vikram Singhal Executive Director Engineering Division, and Mr. K.K. Vij Executive Director, Construction Equipment. Now I would like to hand over the call to Mr. O.K. Balraj for initial remarks and then we can open the floor for Q&A.

O.K. Balraj: Thank you Hitesh. First of all let me thank Kotak Securities for undertaking this responsibility and on behalf of Chairman and JMD and other board of directors of Escorts I welcome you all for this Q2 results conference call. Thank you for sparing your time, I trust you have all gone through the numbers published yesterday. I think some of the newspapers have also carried the results. The way we will proceed with this conference call is as follows, first I will give you a brief synopsis of the performance of the company as a whole, along with me are the three business heads Mr. Rohtash Mal of agri division, Vikram Singhal of engineering, which is automobiles and railways and also Kanwal Vij, the CEO of fully own subsidiary, Escorts Construction Limited.

I will take you through the published results line by line. If you have gone through the numbers we will start with sales first. Sequentially, the sales have gone up by 7.5% that is from 827 Crores in the last quarter to 889 Crores this quarter. Also on a year-on-year basis we have grown up by 32% that is from 671 Crores last year to 889 Crores. A major part of the growth has come from the tractor business, as you know tractor is about 85-90% of our business. Major part of the growth in business has come through tractor sales and the automobile engineering division also has started showing growth in sales.

Now on the expenses side, on the material cost front you would have seen sequentially there is an improvement. This is partly due to the substantial price revision, which we undertook in our tractor business in the month of March and also through a series of cost compression measures, which the division has been doing. Also on the automobile business, we have started getting better margins than last year, together we have been able to reduce the material cost on sequential basis although on year-on-year basis, there is still a 4% difference, but now the trend has been reversed, hopefully we will be able to end up with last year number may be marginally higher than that. Main reason for the material cost increase as you know is steel and rubber, while steel has started to become stable, rubber prices are still increasing. We are taking all measures to see how we can pass on this cost and also bring it out with better results. On the personnel cost front you will find a marginal increase in absolute values on a year-on-year basis that is because of the annual increments and also we had the wage settlement last year, there has been also marginal increase in number of employees hired. All these put together is responsible for the absolute increase in numbers although as a percentage to sales we have been able to peg the personnel cost at the same level of last quarter.

Now at EBITDA level, we have been able to reverse the trend. On a sequential basis the EBITDA has gone up by 1.2 % again due to the price increases we did in March and on a year-on-year basis it is still a minus figure of 3%, but hopefully with this increase in March and also with cost compression measures we should be able to come out with better results in the coming quarters. Interest and bank charges, there have been a marginal increase in borrowings, the Darby loan which we took last year on an absolute basis, the interest cost has gone up by 3 to 4 Crores, but there are certain repayments also coming up and hopefully we should be able to end the interest at an annual figure of below 15 Crores.

On the taxation front, as you know, analysts who have been following our performance for the last two quarters, they know that we had done restructuring last year and I have told most of the analysts that restructuring also has a great tax planning motive and we were able to get the RBI approval for that write off of the old bad debts about 117 Crores, which has given us a net benefit of 38 Crores. After getting this approval in early March, we went through our provisions. We found that we have been making the usual provisions pending this approval, so we were able to reverse all that provision that has increased the net profit from 4.1% to 7.1%, so this has helped us bring out better results than last year and also on a quarterly basis we have shown substantial improvement in our margins. On the CapEx front, as a company we are planning some investments in debottlenecking, R&D, increasing capacity of certain products and the likely amount which we will spend over the next three years is about 160 Crores. The financial closure of this is over, part of the amounts have been drawn. The expansion is going as per schedule and a substantial part of the expansion also is R&D,on which we are planning to take tax advantages, so I have summed up the performance of the company as a whole. Now we can move into the question and answer session. If there are any specific questions concerning the company we will answer, specific questions concerning the divisions, the divisional business heads are here, we can answer that also.

Hitesh Goel: Can you please tell us what is the price hike taken in this quarter and also if I see the average realizations, it has come down on a quarter-on-quarter basis? Was their a one-off in the sales last quarter if you can dwell on that?

Rohtash Mal: I got the first half of the question. Mr. Goel, we took our first price hike this quarter on March 1st against an average industry level which was close on to 12,000 or 12,500 we took hike of almost Rs. 16,000 weighted average across the board, this coincided with the launch of our new product range called the Jai Kisan series, which also was brought into the market in three states at the same time. What is your second part of the question please?

Hitesh Goel: Basically if I look at the average ASP basically on the agri machinery side, there is a dip on the reported numbers on a quarter-on-quarter basis, why is that?

Rohtash Mal: We actually increase prices, so effectively I do not see an average realization drop; on the contrary I see an increase because this price increase essentially is a net increase. May I inquire which number you are referring?

Hitesh Goel: Basically if you see the segment revenue last quarter the agri machinery revenue was 773 Crores, this quarter it is 818 Crores.

Rohtash Mal: This could well be on account of the closure of the Tanzanian order, all the revenues pertaining to training cost etc. came in differentially over these two quarters. If I were to remove these lines of revenue which are actually a part of the revenue for the Tanzanian order then the net increases are of the order of magnitude that I suggested to you, which are equivalent to the price increase.

Hitesh Goel: I also wanted to ask on the order component side now that you have reduced the losses in this quarter quite a bit so what is happening there. When can we expect the break even in that business?

Vikram Singhal: As far as auto components are concerned what I had mentioned last time was that we will break even in Q4 of this year, our financial year, and we continue to maintain that we are very clearly moving into that direction and largely the reasons why we have improved our Q1 is because of price increases, the OEM that we supply to as well as we have got price increases in the after market, so that has contributed. We maintain that we will be breaking even in Q4.

Moderator: Our first question is from the line of Amit Vohra from PCS Securities Ltd. Please go ahead.

Amit Vohra: Good morning sir. we joined late in the call, so I would like to know what is the quantum of increase of tractors we have done and are you concentrating anymore increase in the next couple of months because steel prices as you said probably are a little bit stable but rubber prices is a cause of concern and generally can u give us the guidance for the next six months.

Rohtash Mal: Your question pertains to what price increases did we do in the quarter primarily effective March 1st we increased our prices on a weighted average of 16,000 rupees, this as I said a short while ago is consistent with the launch of the new series of tractors called the Jai Kisan series, a new re-branded and retooled version marked to application, so that is the quantum that you queried about. As far as the next price increase is concerned yes we are actively calibrating another one keeping in view the cost increases that we have faced in the last quarter and are likely to face in the current quarter. Your point that steel prices have stabilized, does not really show the rate of increase of steel prices has gone down, so I do expect cost increases coming out of steel however and of course rubber is the one that is really on fire and other metals also copper, aluminium, some of them impact us, so to your point yes we are calibrating and anticipating price increase in the next 45 to 6o days.

Moderator: Our next question is from the line of Abhir Pandit from Parag Parikh Financial Advisory Services Ltd. Please go ahead.

Abhir Pandit: My questions are related to the construction equipment division. I wanted to know the outlook for the construction equipment division for the next one year.

K.K. Vij: The outlook what we are looking forward is roughly about close to 35% more than what we did last year, although the construction equipment industry is not growing much, the government spending is not there, you must have been reading it now there is a news item which is coming that the government is not right now basically able to give the tenders for road construction. That is where the basic construction equipment demand is there. Nevertheless with the latest RBI policy, which has come yesterday that lending to NBFC have been stopped. We have to see how to really take care of this issue in the market because majority of the NBFC finance these machines and if the lending from the banks to NBFC stops this is going to have an effect on overall financing of the construction equipment machine.

Abhir Pandit: Also I wanted to know has the increased competition since I believe everyone from the MNC to many Indian companies also are entering this phase.

K.K. Vij: Competition is increasing in this sector. The demand is going, as per the pundits of the market they talk about by 2014-2015 the market will be double from what it was in 2009 and 2010. There will be still enough pie of the cake available for everyone to survive.

Abhir Pandit: Could you give me order book or anything you have for the next six months?

K.K. Vij: I would not like to share this.

Abhir Pandit: My last question would be what would be the capacity utilization currently?

K.K. Vij: We are right now at a capacity utilization of 85% and there is already a declaration made by our joint Managing Director that we are investing 50 Crores in next two years for enhancing the capacity to almost 100%.

Moderator: Our next question is from the line of Mitul Ashwath from Barclays. Please go ahead.

Mitul Ashwath: Just looking at your numbers, just wanted to get sense on the profitability of the overall company in terms of margins, some sort of guidance for the rest of the year and do you see some improvement in the margins going forward, as you mentioned you have taken some price hikes and you are taking some even in the future, also wanted to get a sense with this latest round of interest rate hikes do you see softening of demand on the tractor side?

O.K. Balraj: Well in terms of profitability all I can say at this point is I wont be able to give you an exact number, for example I can't tell you what will be my PAT on sale, all I can say is that the trend of continuing to look at our cost closely, look at opportunities to reduce cost then also when raw material increases or happening as Rohtash has said that we have been quite aggressive in taking pricing decisions, so we are hopeful that we will be able to protect and grow our margins although I wont be able to give you any specific number.

Rohtash Mal: Apart form the price increase, I think fair price increases do defray cost while in a comparative scenario it is important to be looking at compressions. We have had some significant result for the past two years on managing compression of our cost, which is why over these few years our profitability has grown, there is more head room available and what I am saying is that we are now launching yet another exercise on compression, which will take us upwards in terms of profitability, EBITDA to sales etc. So in summary two vectors of effort, one of course price is determined by the market, though not completely so and a new series of tractors, refurbished and therefore the ability to gain prices beyond what market otherwise gives on a commodity basis, those efforts are in the pipeline, as I suggested we had a series of new launches in March, at the end of this month we are launching another series on the Powertrac side in the areas of Gujarat, Maharashtra and Rajasthan, so that is on the side of gaining more revenue from the same cost and as I said on the other side this month the launch of a very large company wide exercise on shrinking costs across the board.

Mithun Ashwath: Thanks and just wanted to get an outlook on growth in terms of tractors in light of increased interest rates, do you see some sort of a slowdown in the growth.

Rohtash Mal: As a cost effect relationship I personally believe that this will not make an impact. If you were to see the rate increase even if as the hands on the customer it comes out to merely a percent. Now for a seven-year tenure, on a ticket size of 3.5 lakhs it will probably end up on an EMI difference of a few rupees a month. I do not believe that this difference in the EMI will cause any decision changes in respect of demand, more so the demand in my opinion will remain strong because of a variety of reasons, (a) the crop is looking good, the recent crop, even though it has been delayed for a while but the volumes are looking good and the newspapers are full of great reports on queues outside the procurement center. Second, the forecast on the monsoon has been good. Thirdly, as I suggested on the last conference call I believe that was a shade under three months ago I expected the government to up its deployment on agriculture to over 425,000 to 450,000 Crores. I admit I was wrong. On the negative side, we actually got 475,000 Crores as deployment. Nevertheless all the macro factors in terms of agri-growth are in position, rate **is** available. The tractorization of India is low, so on the demand side I do not expect any impact of this rate hike on demand and the other factors are in any case well in position to take care of the current outlook.

Moderator: Thank you. Our next question is from the line of Ramnath Subramaniam from Golden Sachs Asset Management; please go ahead.

R. Subramaniam: Good day to all of you and thanks for taking my call. My question is to Mr. Rohtash Mal. Sir, on the back of this 16,000 odd price increase you have taken in the month of March, where do you see the margins for the tractor business in the next one or two quarters given that we have been able to probably offset some of the cost increases with this price increase and if this Tanzanian order is completed on the topline specifically where can we probably expect margins on tractors from hereon?

Rohtash Mal: I will attempt to answer it to the best of my ability in the shortest possible time. As you may have noticed that on a Q2 to Q2 basis or on a sequential basis there has been an improvement. This particular price increase that was taken on the 1st of March, actually we had thought of taking it earlier. As I mentioned in my last conversation with you 2-2.5 months ago, we wanted to align this to the launch of a new range of tractors, otherwise that could cause too much confusion in the market. Had we sort of taken it at that point in time, this percentage would have looked much better, however we need to measure it on a quarter-to-quarter basis, so couple of things is happening in respect of prices and realization i.e. contribution. #1 is that with the new range one launched in March and the other coming up later this month, we expect to re-rationalize our prices and therefore contribution upwards, #2 on the side of cost alone, raw material cost I expect to be calibrating price increase in the next 45-60 days perhaps a shade earlier and thirdly as I mentioned just a short while ago, we are launching our third phase of our cost management and cost compression exercise aimed across the board, not necessarily at raw material, an attack on overhead cost, an attack of fixed cost de-fixing some fixed cost and so on, so I do expect our EBITA margins to be smartly moving up. It would not be proper for me however to give forward looking numbers.

R. Subramaniam: The only question related to that is as you mentioned the price increase that came in March is something which you had indicated that you could be doing somewhere in February itself and that took almost one month and then probably to get it across would probably be April 1.

Rohtash Mal: No, that is not the case, you are dead right we were delayed by a month and it does happen when you are dealing with about 9 or 10 new product variants getting the engineering and the getting the entire thing dead right almost to the day, you know there are some slippages. I admit we could have done better by about 30 days but that was the delay that had to be taken. We would not allow our product to go into the market just because we had given a date. We really wanted to make a big wave with this, which we succeeded in, and the second range of products comes in now this month. So as far as the delay is concerned what is the second after that question if I may inquire.

R. Subramaniam: I think the other part was that how does competition react to such price increases, because when we take a price increase and we are significantly lower down the order in terms of the market share in terms of the first and the second player, how do they react to this and how confident are you that another price increase in the next 45 days or so can happen?

Rohtash Mal: As it turns out there are a couple of facts that stare at us in the face. Number one, the fact of cost increases. Given the efficiency relative efficiency of our buying systems we also have a window into competition. So therefore we also know what kind of cost enhancements they are seeing, we have a pretty good, market intelligence cell that watches our cost and relative costs across the industry, so the first fact is we do know how we are doing in terms of efficiency of buying. Number 2, if you take into account the last one year, another factor that comes into mind is how smartly are you growing in your strength areas or indeed how strongly are you growing in areas that you are not so strong in and as you watch your own numbers and the gains in the market shares, relatively small that they might be you also gain confidence that your product line has been well accepted. Number 3, when you do come up with a new product range with another range to follow it does give the dealership system and the company itself the confidence to take a decision that these price increases will be accepted; on one plane a price increase of about Rs.14,000 in an economy that is inflating at 10%, does amount to a momentary increase of about 3%, so you do look around into all these four factors to gain some sensibility as to how much you should increase and at what time and of course comforted by the fact that inside the house itself efforts are underway to contain cost. So it is a thin line I admit, but that is where our confidence comes from. My confidence in the future actually emanates from the same factor with one more addition that we are launching yet one more of compression exercise and we are coming up with yet one more series of launches.

R. Subramaniam: Over the last 1-1.5 years, we have been betting on the fact that as capacity utilization on the stated capacity for tractors starts inching up, obviously the gross contribution margins has to see a significant change given that we have a very old depreciated plant in that sense, that is point number one. Second thing is now this price is coming through the Tanzanian order impact over, we straight away have to benefit out of this huge capacity utilization improvement that comes through, so can we be confident or rather get some confidence from the management that this should definitely aid in the next couple of quarters by way of improved EBITDA margins?

Rohtash Mal: None of these factors are a standalone. Capacity utilization as it goes up obviously has to infer increased profitability in the sense that a lot of your revenues rather contribution margins go straight to the bottomline. So there is an arrow that goes up on that side. There is another arrow that goes down that is called raw material and its inflation and inflation in personnel cost etc., which in any case is part of some inflation levels. Third, the Tanzania order is not a stand alone order, these are orders for example we have done some in Ghana, we have done some in Tanzania, Mozambique, Madagascar, so these are institutional orders, and there are more in the pipeline. What we do not know is when the next one or rather precisely when the next one will emerge, so there is a series of cross factors, some that gave more to the bottom line, some that detract from the bottom line and we have got to manage each one of them individually. To your summary question which said in total will the EBITDA margin go up, my sense is they will and smartly so. For example let me just share with you on a standalone basis in a month when you raise prices even in an inflationary situation your EBITDA margins go up upwards of 11.5%, 12%, 12.5%, so as more costs kick in and blended EBITDA to sales kind of settles down to 9.5% to 10%

which is significantly better than where we are today, so in summary yes you can look forward to higher EBITDA margin based on the reasons that I outlined just a short while ago.

Moderator: Thank you. Our next question is from the line of Rashi Talwar from Demeter Advisors. Please go ahead.

Rashi Talwar: How is the demand side behaving because obviously from all other auto companies we are kind of hearing about some softness in demand and footfalls being low etc.?

Rohtash Mal: Firstly I will give you numbers that pertain to the fiscal year, not ours but the equivalent of the government financial year and then I will address this same thing in the manner of the last half and indeed the last quarter, so it will give you a sense of 365 days, 180 days and 30 days. In the last one year the tractor sales in India grew from 403,000 to 483,000, the exact increase is 19.7%. If I look at the half-to-half the market position remained about the same 19.5% to 20.5%. In the last quarter, the position is again 19.6% to 19.7%. Some of the numbers that were being thrown around over the last one year, there were 20% increase, 35% increase, these are random data points that are picked up in the press seemed to indicate that the whole place was on not fire but an inferno, that was not the case, on a more sober analysis the market grew by about 19.5% to 20%, now to your point that would this mean that some demand would kind of slowdown, it has been on fire for a long-time, a couple of logic points and a couple of emotional ones. The logic is that all the factors of agri growth are in position as I have been saying for a long time. In fact there is nothing really that should stop the agri mechanization sector, so on a macro level all the things are in position. What we do need to worry about is how we are going to manage the price cost equation in order to see that our profit grows at a similar pace, so in summary what I would say in response to your question, I on the emotional side, I certainly hope that there is no deflation, I do not see it happening, but there could be blips of the kind. For example a blip that says in the Rabi season which is just getting over, our harvest has been absolutely at record levels. As I mentioned a short while ago in front of the procurement centers you have reports of queues of trolleys and trucks waiting, but you do see a dust in the wind that says well the harvesting got delayed by 15 days, 30 days, that is not likely to make an impact demand will shift for one month to the next, but that is about all that is going to happen and the El-Nino effect which is the forecast which comes in April for July monsoon seems to suggest a probability level of about 93%, 94% that the monsoon will be better than normal, so macro factors in position, some gusts of wind here and there I say late harvest therefore a pick up 15 days later, but overall healthy.

Rashi Talwar: Therefore you feel taking another price increase in 45 to 60 days will be comfortable?

Rohtash Mal: Let me not anchor that decision only on market growth, there are factors beyond market growth, let us for a minute have an argument about growth rates 20% versus 10%, let us go by the 10% growth rate just for argument sake and only for a moment, if I have 10% growth rate and I have got a new range of products and in parts of the country where we were weak, we are getting strong and I recognize that in 13 areas out of 19 areas we have made gains in to other people's territory, I will feel more confident to take on a price increase. Do remember that Escorts has an unsaturated upside whether you take it on the EBITDA to sales side or indeed in our proportional share in the industry, which I would say our rightful share of the industry is 20% or more, so therefore on that emotional note saying rightful share and the logical note that I mentioned earlier my confidence is that we should be able to take it and this confidence also comes from the fact that in the last many prices we have been firstly ahead of competition, we were the number three player but the first one to press a price increase, number two, if they talk about price increase of Rs.10 we are ahead at Rs.11, and that is out of weighted average it does not go model to model but that does give us the confidence to be able to stick our necks out on this one and having stuck our neck out many more times let us face it, we have not really been penalized by the market, on the contrary we have been lauded.

Rashi Talwar: I am not sure whether you gave you any numbers of ECEL?

O.K. Balraj: We have not given any numbers.

Rashi Talwar: Could I get the numbers please?

O.K. Balraj: I have the six monthly numbers here vis-à-vis the full weight and the comparison with the full last 12 months. Sales has increased by 35%, last 12 months we had a sale of 575 Crores against that we have made a sale of 380 Crores which is about 35%. On the profitability side, EBITDA level, we have increased EBITDA compared to last year by 1%, last year our EBITDA to sales was 3.4%, it has gone up to 4.5%, even the PAT also has increased by 1%, 2.3% was the last year number and this year for six months we have recorded 3.4%.

Moderator: Thank you, our next question is from the line of Chetan Vora from Edelweiss Securities. Please go ahead.

Chetan Vora: Good morning Sir, just wanted to know how much volumes we have done during this quarter?

Rohtash Mal: 17,672 tractors. You take the number at 17,672 and then you will find the realization. Just a second, I will try and solve this problem, 556 and 17,000; it appears that this includes an export figure of 556 tractors. What we are talking about 17672 is the domestic sales.

Chetan Vora: So the total in the sales number both the numbers will be included?

O.K. Balraj: It is a total sale, total is 17,672 including exports.

Chetan Vora: Because the balance sheet what the number what I have got from your side is 17,473 plus exports 556 what I get the number is 18,000. So what is the number actually Sir?

Rohtash Mal: 17672 including exports. Are you saying there is an error of 200 odd tractors in this?

Chetan Vora: The error is of somewhere around 300 units and because of that there is a sequential decline in realization of 4%. The tax rate even after I give the credit for these bad debts written of the effective tax rate comes to 12.2% of PBT, now why is that tax rate is so low?

O.K. Balraj: Let me tell you, our accounting year is October to September, the tax year is April to March, so the tax credit which we have taken here are the tax provisions which we have done in excess of the requirement over the last fourth quarters, on 118 Crores of old receivables we got an approval from Reserve Bank because these are foreign receivables. The effective saving is 38 Crores, so we have provided in excess of that in the earlier month because till you get this approval you cannot provide less tax, so once we got it we did the entire calculation backwards and we realized we have provided 33 Crores extra and that is the one which you find as returned back.

Rohtash Mal: I have got the answer to the query of Chetan and that is if you take out the revenue pertaining to Tanzania which came in various forms like training costs, we even talked about the reduction in average realization answered by the fact that it will take away the Tanzanian revenue in terms of training cost etc., on a sequential basis, the earlier point that I made that realization have gone up rather than the other way round.

Chetan Vora: So what will be the volume relay, if the volume is 17,762 then we see a sequential rise, but if the volume is 18,009 the number that is with me, can we see a sequential deal so the question mark is on the volume part?

O.K. Balraj: We are confirming that the volume is 17672 Chetan.

Chetan Vora: On the tax part, the negative tax is right now 33 Crores even if I write it back as 38 Crores it comes to a positive of 5 Crores, now 5 Crores on a PBT of 41 Crores is 12% it is very less even after adjusting for your tax credit, I have taken a 33% tax write back so if I add that 38 Crores to your negative 3 Crores I get a number of 5 Crores on a PBT of 41 Crores now that is a tax rate of 12%, I just wanted to know how such a low tax rate, am I missing something?

OK Balraj: This 33 Crores includes deferred tax credit of 10 Crores also, basically the reversal is only of 23 Crores.

Chetan Vora: Even if I write it back by 38 Crores still my tax rate comes for 12% effective tax rate?

O.K. Balraj: Well we have another two months to go in the current year where we will have to provide the real rate of 30%, so on a 12-month basis you will find effective rate around 20-22%.

Chetan Vora: Because we do not have any incentive on the tax haven zone, the tax will be lower at 20-22%?

O.K. Balraj: You please remember we have got a substantial write back, at 115 Crores.

Chetan Vora: After adjusting that what would it be?

O.K. Balraj: On an annualized basis for guidance purposes for your model, you can take a 22% effective rate.

Moderator: Our next question is from the line of Bharat Gyanani from Asit C. Mehta investments. Please go ahead.

Bharat Gyanani: Sir if you could give me the CapEx guidance for FY 2011 and FY 2012?

O.K. Balraj: We have a total CapEx of about 165 Crores over the next three years which includes 2010-2011, 2011-2012 and 2012-2013, out of this about 50 Crores have been spent and going forward before end of September we might be ending up spending about 75 to 80 Crores, the balance will be spent over the next two years and a substantial portion of this also will come as R&D investments and these CapEx are for debottlenecking, capacity build up and then also ancillary.

Bharat Gyanani: My other question is to Mr. Rohtash Mal, we have seen initiatives off late by the market leader Mahindra has recently entered in to micro irrigation, and do we have any strategic plan to enter that space?

Rohtash Mal: There are a lot of initiatives which are in the baking stage, we should be announcing them in the course of the next period, I cannot commit when, just like in a market everybody takes initiatives some which come in front and some which have to counter we are exactly in the same position, so yes there are some serious different vectors of strategy under discussion and I do hope that they will become more public shortly as they get to a fully baked situation.

Moderator: Our next question is from the line of Amit Kasat from Standard Chartered. Please go ahead.

Amit Kasat: Sir just wanted to share what was the spill over of Tanzania order, the export order in the current quarter and if so, what is the amount that is in the revenue process and the volume process?

Rohtash Mal: 25.5 Crores in Q2, 64.4 in Q1.

Amit Kasat: Can you just give me what was the volume in Q2 on the Tanzania order?

Rohtash Mal: 183 units.

Amit Kasat: Similarly on the raw material front because there is a lot of attachment which Tanzania order wanted to have, what is the absolute amount in terms of raw material which is excess for this order, incremental because there were lot of fitments which you had to put, there is a lot of bought out?

Rohtash Mal: Against the 25.5 Crores the net material cost is 21.2 and against 64 it was 49.4.

Moderator: Our next question is from the line of Kaushal Maroo from Religare. Please go ahead.

Kaushal Maroo: Can you tell me what percentage of your agri machinery business revenues comes from implements and other business, non-tractor businesses?

Rohtash Mal: At the moment, the percentage is an interesting 0%, however we have sold a total of or being responsible for a total of about 1100 units implements for various kinds, the way it has been done so far is that we have asked our implement manufactures to directly bill our dealers and the mining and engineering which we have done beforehand we have timed it up with our tractors and selling it as combo units, so far we have ceded the market with this volume and so far deliberately we have not taken a cut or a margin out of this. Going forward as this momentum gains strength, there will be a margin which will be obtained from this business. This turnover, because of various taxation angles is not being parked through Escorts Limited but in future as tax rationalization happens or as other opportunities open up we will park this through our book bearing a margin.

Sachin Relekar: The other question is on auto ancillary business, this time we see an uptake in our revenues, and so is this because of acquisitions of some new customers more supplies to existing customers?

Vikram Singhal: Basically the improvement in the margin over the previous year has been on the basis of price increases that we managed to get from our OEM. We are in the process of new business as well as new products in the coming two quarters through the auto component business.

Sachin Relekar: On quarter-on-quarter basis our revenues have increased by 50%, so there should be some portion because of higher supplies to existing OEM?

Vikram Singhal: The supplies to OEM as well as price levels.

Sachin Relekar: So at these current revenue run rate will be able to make margins to the tune of negative 5% that we are making, the revenue run rate is maintained?

Vikram Singhal: The first objective is break even on this business and we will do in Q4.

Moderator: Thank you. Our next question is from the line of Sourav Das from Sundaram Mutual Fund; please go ahead.

Saurav Das: My first question pertains to the agri machinery division. I am not able to tie up the realization. I am just working with the numbers. Last quarter you mentioned agri machinery had 773 Crores of revenues of which 60 Crores pertains to Tanzania order and you had volume of 16633 units. If I take up the 60 Crores I get a realization of 4,29,000 rupees. In this particular quarter I have 817 Crores as revenues and you just mentioned that I have to take out 25 Crores on account of Tanzania, if I take that out I reach to a number of 4,49,000 rupees per unit, so there is a sequential increase of 20,000 rupees while the price hike has been effective only in March and that is for 16,000 rupees, so I am not able to tie how this increase in realization has happened on a sequential basis?

Rohtash Mal: Here are the causative factors, #1 there is a positive product mix in fact from quarter to quarter that is almost about 5 Crores, second there has been some revenues received from Tanzania on the training cost etc., would actually bore zero cost, taking both these out, these will happen if we marry each other, if anybody is interested I will get this reconciliation carried out and send it to you. I would like to point out that in the increase in revenue there has been, this we did not point out earlier, there has been an increase in the enrichment of product mix to the extent of 4.38 Crores, so the linearity that you might see between realizations deflated for this will and does reconcile these numbers.

Saurav Das: If you can give us a sense that we have been undergoing a lot of initiatives in the southern part of the country for increasing our market share, so what was that in the previous quarter and what it is now and what do you see going forward in that market?

Rohtash Mal: Thanks I was hoping somebody would ask that question, we have seen almost a 2.6% increase in market share in the South and we are not stopping here, the various initiatives that are in the pipeline #1 I spoke about in the last conversation with you and that was pertaining to a new organization structure that we have put in position headed by a very senior guy and we are further building the organization there, #2, we have a new basket of products which have been now tested and are ready for launch. These are products for wetland application. There are products with cyclic reduction, then there are which are differentiated and application lead to the kind of cultivation that happens there, so that is the product side, thirdly on the dealer side there were and are gaps. We are closing those gaps, we are appointing some high-quality dealers in to those gaps, so sum total of all this plus a lot of organizational energy behind it will certainly shift this percentage up. I am very confident that next time we speak, I should be speaking of another increase in our market position in the southern area.

Saurav Das: This 2.6% increase takes our market share up to in South India?

Rohtash Mal: We will put it together. Andhra Pradesh accounted for 0.2, Karnataka 0.8, then Tamil Nadu 2.1, so that kind of reconciles them.

Saurav Das: What I was alluding to is what the current market share is; we have increased the market share by 2.6%?

Rohtash Mal: If I blend this together we are currently running about 5.5%, we have a nice headroom of them.

Saurav Das: One more question on our higher ASP strategy and you just mentioned there has been a positive product mix and I think we have three ranges, Escorts, Powertrac and Farm Track, if you can just give us a broad sense of what is the break up of sales and volumes in these three segments?

Rohtash Mal: Look it is primarily Powertrac and Farmtrac. I also urge you please not to distinguish too much between the two kids of the same family but the proportion between Powertrac and Farmtrac is like 56:44. As far as high horse power tractors are concerned we have just developed a new four cylinder 55 horsepower which with the turbocharger intercooler can pull up to 75 horsepower, we are looking for some products to be built around this engine. As I mentioned a new range of Powertrac is going to be launched this month, I hope you were on the conversation a little earlier, so that should kick in at the end of this month and we are also now prototyping some even higher horse power tractors.

Saurav Das: Four cylinder as a proportion of the total portfolio would be more than 15% now?

Rohtash Mal: Just hold on, we will give you the exact number, about 8%

Saurav Das: In terms of our capacity I do know that it is 1 lakh capacity but between 4 and 3 do you need to reconfigure and do you think you have adequate four cylinder capacity?

Rohtash Mal: Yes, part of the investment that Balraj spoke of earlier is not merely to rebalance our assembly capacity, our money is going to the machine shops to take care of changes in product configuration and you used the word rebalancing, I think that is the right way to look at it, because the way capacities are normally computed, you take a per day capacity and multiply it by so many days, say 330 a year and you arrive at a figure. In an industry like ours rebalancing has to be far higher because our peak capacity will be in excess of 100 or 1000 units but the throughput capacity often times is lower, so you need to rebalance it by way of throughput rather than peak output.

Saurav Das: And then the seasonality factor?

Rohtash Mal: Absolutely.

Saurav Das: My next question is to Mr. Balraj , you are expecting a 15 Crores odd interest outgo for the year and we are through with 10 Crores already, so are you alluding that we have just a 5 Crores outgo for the balance of the year.

O.K. Balraj: Yes, we have some repayment of existing term loans that are going to happen in the next six months and if the interest rates does not change much between now. I do not know the impact on credit policy, whatever calls are made to my banks I do not see much of a difference, but then you cannot, between next six months there could be a revision, if that thing happened I think our target is to restrict interest to maximum 15 to 16 Crores.

Saurav Das: Because I see almost 300 Crores of loan and 212 Crores of cash sitting on the books, so I was just wondering that why do we have such a high cash level or is it just a closing figure so it distorts the picture?

O.K. Balraj: It is not a closing figure, we have surplus cash which if you see in the last few quarters balance sheet also you would have found that number. We keep the cash and going forward I would like to maintain the figure of 16 Crores for interest.

Saurav Das: Because even if I take a 8 to 9% rate on the 300 Crores.

O.K. Balraj: You should not take 300 Crores because part of the 300 Crores is cash credit limits which fluctuates and second is some of the term loans which we are seeing gets repaid about 30 to 40 Crores of repayments are due between now and September, so on that I do not have to pay interest. It is my estimate, about 16 Crores we should be able to close.

Saurav Das: Last year we had an investment of 130 Crores in to ECEL, if you can just give us a sense because I was going through the gross block of ECEL and that itself is 130 Crores.

O.K. Balraj: The investment in ECEL is not on gross block from Escorts side, it is to repay the Darby convertible debentures and preference capital which we had, you know Saurav if you remember correctly we had brought out the Derby Holdings before maturity.

Saurav Das: So this is for that.

O.K. Balraj: It is an investment. The Darby money originally was used to invest in fixed assets, so ours was the case of refinancing and put it in Escorts books.

Saurav Das: Right now what are the capacity units in ECEL for the backhoe loaders?

K.K. Vij: We have invested in to a capacity of about 50 numbers per month; we have now realigned the total system right now to 100 numbers per month although without much of investment, how we are investing the money in the next two years which the overall capacity of ECEL machines from 6000 to 12000 per year.

Saurav Das: 6000 which includes the pick and carry.

K.K. Vij: Pick and carry, backhoe loaders, compactors, basically the main categories what we produce. We are likely to increase almost about 100% in next two years time and in today's situation although my throughput capacity is much higher than my installed capacity; whatever we are producing is moving out, there is not much in finished stock, so there is all the need for us to now immediately invest in to expanding our capacity.

Saurav Das: So are we doing something like a 100 units on the backhoe side?

K.K. Vij: Well we are restricted by certain suppliers of the main aggregates which are MNC companies, so we have done roughly about 75, I think in the month of June we should be first time crossing 100 numbers. Capacity is not an issue constraint now.

Saurav Das: On the pick and carry side do you see any movement because anecdotally the infrastructure space is not doing well?

K.K. Vij: If you see these six months, what we have done in pick and carry we are almost about 27% more as compared to last year, quarter to quarter we are more by almost 22.7% between first quarter and second quarter and we have gone beyond our installed capacity in producing pick and carry machines today.

Saurav Das: So what are the sales on an average monthly basis on pick and carry?

K.K. Vij: On average we are touching 400 plus now against last year we had about 275 or 290 machines.

Saurav Das: We would be having something like a 40-45% market share?

K.K. Vij: Well in pick and carry my market share, I am the leader still maintaining from the very beginning with 54% market share although the competition has gone up, has been in part because of high rise of commodities of steel price, but nevertheless I think we as a market leader this is a premium product we have been able to maintain our position in the market, so we still look forward, there is still scope of growth in pick and carry which we are now planning to do so in the coming six months time.

Saurav Das: Just one last thing on ECEL again, on the margin side, at 85% of capacity utilization we are clocking something like 4.5, so do you think that going forward as we expand capacity it is tough to improve margins from here?

K.K. Vij: No, it is not tough to improve margin here because if you see my majority that is 64-65% of the topline right now coming from pick and carry to machines where the margins are very low which is highly competitive, it has become a commodity rather than a machine, now whatever expenses are taking place are taking place on high end machines, we are going in for a very high capacity machine which are 15 tonnes, 16 tonnes, 18 tonnes, 23 tonnes also backhoe loaders. The improvement in the margin even over the first quarter versus the last quarter by 2% although six months to six months it is only 1%, basically the product mix and we have gone in to the focus owing to the higher contribution and higher value product in the market so my basic expansion in investment is more going in to the higher products and the pick and carry machines. If I am able to do this investment that and able to position this capacity utilization my EBITDA margin percentage would double.

Moderator: Our next question is from the line of Basudeb Banerjee from Quant Broking. Please go ahead.

Basudeb Banerjee: Thanks Sir for taking my question. You gave the break up of Tanzania revenue of 25.5 Crores this quarter and 64.4 Crores in last quarter, what were the corresponding tractor units in these two quarters? 183 units was this quarter I suppose you said?

Rohtash Mal: It was 233 in the last quarter and this quarter it is 183.

Basudeb Banerjee: Sir if you see the quarterly other expenditure figure it has been moving up quite steadily and even from few quarters tractor volume on a quarterly basis has been more or less the same, so can you highlight which are the variable factors affecting the other expenditure part?

Rohtash Mal: First of all the tractor volumes quarter-on-quarter has always increased, it was never the same.

Basudeb Banerjee: Other expenses till Q3 FY 2010 is more or less in the same region even this quarter but if you see Q3 FY 2010 the other expenditure was 95 Crores and this quarter it is 120 Crores?

OK Balraj: You look at it in terms of percentage to sale, percentage to sale basis is still hovering around 13%, your point is taken all I am saying is that this is an expense which goes up with sales.

Basudeb Banerjee: So what are the variable elements, because generally one can take majority being fixed element in the start.

O.K. Balraj: There are about 11 components to this cost, it is not only sales related, starts with sales expenses and the packing and freight forwarding expenses and maintenance expenses all these come under other expenses because under the guidelines you can only have three major expenditure shown for this quarterly reporting, so we club all those together, so it is basically if you look at the other expenses as a percentage to sale, even on year-on-year basis or even sequential basis it is between 13.1 and 13.3%, so there has not been any while the tractor business has been going.

Basudeb Banerjee: Do we see this part to gradually taper off to some extent.

O.K. Balraj: Not clearly, there are expenses which are connected to sales on this which grows with sales, there could be certain expenses like replacement to machinery, audit fees etc., which may not increase with sales but a majority of the expenses are sales related, it does go with sales.

Rohtash Mal: Let me come in here, the way you club expenses but to give you a sense of variability of expenses versus nonvariability, now for example if you were to take manufacturing expenses, as a percentage it has come down over the years but overall it would go up because there is a huge amount that is related which is variable in nature and that is related to the volume of production, if however you take something like sales expenses, now the moment you launch, brand new series of tractors obviously these are shown as expenses on the P&L, your advertising, promotion etc., actually it is in nature of an investment expense, as your volumes go up which go up from quarter to quarter by almost about 3000 units the variable cost is freight and the rate of freight, so let me put it like this, overall percentage in all these are declining, there is a very strong focus as adjust in part on variability and fixability of expenses and the fixabilities are under attack, variables are being controlled.

Basudeb Banerjee: Can you share the magnitude of one time expenditure for the Jai Kisan series launched this quarter?

Rohtash Mal: 8 Crores between these two and we had made provisions; we took higher price increases and also kept aside a buffer in those price increases for these expenses, so this will be a onetime expense.

Basudeb Banerjee: Should we prepared for again a drastic margin worsening in Q4 of this year compared to last year like 400-500 bps difference happened because of that one quarter accounting?

O.K. Balraj: Can you clarify that please?

Basudeb Banerjee: Last FY 2010 Q4 if you see that several numbers were clubbed in Q4 accounted only in Q4 rather than getting evenly distributed so should we expect similar kind of accounting in FY 2011-2012?

O.K. Balraj: You are referring to the director's fees and managing director's remuneration. Royalty is something which is paid on a monthly basis, royalty is not clubbed in fourth quarter, you are wrong there, second is in terms of the director's fees and remuneration, that is an expense which you can forecast only when the full year profits are down and this is normally calculated as a percentage of profits as per the Companies Act, we disclose it in the balance sheet also, so that is an expense which I cannot spread out through the quarters. My auditors will not agree and it is not proper to do it also, so as you know the profits when we enter the quarter we will be able to arrive at a debt figure and therefore that trend will continue in this quarter also.

Basudeb Banerjee: What was the April month volume?

Rohtash Mal: We had a total of almost about 5600-5700 deliveries.

Basudeb Banerjee: Including exports?

Rohtash Mal: Yes more or less including exports.

Moderator: Thank you Mr. Banerjee, due to time constraint that would be the last question. On behalf of Kotak Securities that concludes this conference.

O.K. Balraj: Thank you Shifa and on behalf of Escorts I also thank you for all the assistance for this call.