



“Escorts Limited Q2 FY-19 Earnings Conference Call”

October 31, 2018



MANAGEMENT: **MR. BHARAT MADAN – GROUP CHIEF FINANCIAL OFFICER, ESCORTS LIMITED**
MR. SHENU AGARWAL – CHIEF EXECUTIVE, ESCORTS AGRI MACHINERY
MR. AJAY MANDHR – CHIEF EXECUTIVE, ESCORTS CONSTRUCTION EQUIPMENT
MR. DIPANKAR GHOSH – CHIEF EXECUTIVE, RAILWAY EQUIPMENT DIVISION
INVESTOR RELATIONS TEAM

MODERATOR: **MR. MITUL SHAH – RELIANCE SECURITIES LIMITED**



Escorts Limited
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Moderator: Ladies and gentlemen, good day and welcome to the Escorts Limited Q2 FY19 Earnings Conference Call hosted by Reliance Securities Limited. As a reminder, all participant lines will be in the listen-only mode and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing '*' then '0' on your touchtone telephone. Please note that this conference is being recorded.

I would now like to hand the conference over to Mr. Mitul Shah from Reliance Securities Limited. Thank you and over to you, sir.

Mitul Shah: Thank you, moderator. Good evening all. On behalf of Reliance Securities Limited, I welcome you all for Escorts Limited Q2 FY19 Earnings conference call. I also take this opportunity to welcome the management team from Escorts Limited. Today we have with us Mr. Bharat Madan – Group CFO; Mr. Shenu Agarwal – CE, Escorts Agri Machinery; Mr. Ajay Mandahr – CE, Escorts Construction Equipment; Mr. Dipankar Ghosh – CE, Railway Equipment Division and the entire team of Escorts Investor Relations.

We would start the call with brief opening remarks from management followed by an interactive Q&A session.

Before we start I would like to add that some of the statements during today's discussion may be forward-looking in nature. At this point I would request Mr. Madan to take this opportunity and give opening remarks. Over to you, sir.

Bharat Madan: Thank you, Mitul. Ladies and gentlemen, a very good evening to you all. Thank you for joining us on the second quarter earning call for financial year 2019.

A snapshot of our company's quarterly performance is as follows. Turnover up by 15.4% at Rs. 1,398.4 crores against Rs. 1,211.7 crores last year lead by volume growth in both tractor and construction equipment business.

The tractor volumes went up by 3.4% to 21,039 tractors as against 20,358 tractors last year same quarter. Construction equipment volumes up by 36.9% to 1,331 machines against 972 machines last year same quarter. EBITDA is at Rs. 157.5 crores against Rs. 140.9 crores last year is up 11.8%. EBITDA margin now stands at 11.3% versus 11.6% last year same quarter ended September 2017.

Finance cost went down by Rs. 4.5 crores to Rs. 3.9 crores as compared to quarter ended September 2017. The total debt outstanding as of September 2018 is Rs. 211 crores, it has gone up due to increase working capital requirement in preparation for a festive season starting in quarter 3. PBT stands at Rs. 154.4 crores which is up by 33.3% against Rs. 115.9 crores last year same quarter.

The company reported a PAT of Rs. 102.7 crores versus Rs. 77.6 crores last year up by 32.5%. PAT margin now stands at 7.3% versus 6.4% last year. EPS is reported at Rs. 8.6 against Rs. 6.49 last year same quarter.

Now moving on to segment wise business performance. Starting with the agri machinery business. Domestic tractor industry de-grew by 2.5% at 1.85 lakhs tractors against 1.9 lakhs last year same period. Escorts' domestic volume grew by 3.7% at 20,553 units against last year's 19,817 tractors. Industry de-grew by 3.5% in Escorts' strong markets where in opportunity markets industry de-grew by 6.2%.

In line with our Vision 2022 direction we have gained market share across all major states. Our domestic market share now stands at 11.1% in quarter ended September 2018 which is up by 70 basis points as compared to corresponding quarter of 10.4%. The EBIT margin in Escorts Agri Machinery division stands at 14.7% against 13.7% last year primarily due to our operating leverage and cost reduction initiatives.

We unveiled India's first autonomous concept tractor in collaboration with our technology partners. This partnership within the technology partners will help the company to develop a range of farm machines with electric transmission, autonomous applications, remote vehicle management, database soil and crop management and sensor this credit form applications. We expect domestic tractor industry to grow by 12% to 15% in credit fiscal.

Now coming to the construction equipment business, our served industry comprising Backhoe Loaders, pick and carry cranes and compactors which went up by 41.2% in second quarter. Compactors having the biggest gains in the second quarter with growth of 85.5% followed by cranes that grew by 41.6% and Backhoe loaders grew by 38%. Our total volumes manufacture and credit products went up by 36.9% to 1,331 machines. In quarter ended September 2018 as against 972 machines in last year same quarter. EBIT margin for Q2 ended September 2018 at 0.7% as against 0.5% in the same quarter previous fiscal. Commodity prices inflation has been adversely affected margins in the second quarter in the construction business. For FY19 we expect that our served construction equipment to grow upward 30%.

Coming to the railway division, revenue at Rs. 105.9 crores in quarter ended September 2018 is up by 44.5% against Rs. 73.3 crores last year same quarter. EBIT margins were up by 375 basis points at 20% as against 16.2% last year same quarter. Sequentially margins were down due to increased share of our new products with high import content in the overall sales portfolio in this quarter. Order book for this division stood at more than Rs. 400 crores as of September 30, 2018 which will get executed in next 12 to 13 months. For FY19 we expect realization to grow at 25% to 30% over last year and in midterm at 18% to 20% CAGR.

Now I request the moderator to open the floor for question-and-answer session.

Moderator: Thank you very much. Ladies and gentlemen, we will now begin the question-and-answer session.

We will take the first question from the line of Hitesh Goel from Kotak Securities. Please go ahead.

Hitesh Goel: Sir, just wanted to get a sense on the festive season demand for tractors we are hearing in certain pockets the demand is soft. So, can you just and you have not changed your guidance so can you just give a color on that? Secondly, in unallocated EBIT it has increased quite meaningfully from Rs. 13 crores last quarter to Rs. 18 crores. So, can you just give us some sense what is happening there? And can you also talk about the royalty payout that is going to the promoters which we had fixed to around 0.5% of sales. Any change in that if you can highlight these three points?

Shenu Agarwal: The demand right now in the festive season. So, on the ground we are seeing very positive sentiments in the market. The crop prices are better than last year. The production is higher than last year. Even the estimates for the Rabi sowing are better than that of last year. There are no problems in the financing part, liquidity part. So, we are seeing that the formal sentiment is very positive. So, we hope that we will clock good amount of growth in our sales in this fiscal. For the other two questions I will pass this to Bharat.

Bharat Madan: Yes, just coming on the royalty to promoter's company so royalty remains at the same level at 0.5% , no change in the royalty policy as of now, it will continue to be at the same level. And then on your other question of the unallocated carpet overall expenses starting there is a one event which we held in September quarter which is this new product introduction platform which we do every year.

So, this time there is an event which was held at slightly major scale, the event called Exclusive on 6 September. So, the one-off cost has just come in this quarter which obviously going forward will not be there. So, overall there will not be any major change on the un-allocable costs.

Hitesh Goel: Just a clarification on demand. Shenu, can you talk about how Dussehra demand was and any regional trends that if you can share that South was better, South was strong and North in regional wise how is the trend?

Shenu Agarwal: Yes, so Dussehra and Navaratri demand was very good. Especially the first five or six days were awesome. We had ourselves grew substantially like more than 30%, 40% in that range. So, last couple of days, the last two or three days were still good not as good as the first five or six days. I have no reasons for that but I think the enthusiasm was very high and therefore most of the customers who wanted to buy they came to the showrooms at the beginning itself. But overall Navaratri including Dussehra was pretty strong for us.

After Dussehra there was a kind of lull which happens every year of course because Dussehra is kind of peak Navaratri and Dussehra peak line but the sentiment is still very, very positive. So, we are looking forward to another peak on Dhanteras and Diwali which is just coming up.

Regionally speaking yes, South did not show that much enthusiasm this time. A couple of sectors one is that there were some parts which did not have good rainfall like North Karnataka and Rayalaseema and so on. And also South was sitting on a very high pace from last year tremendous growth. And in one or two states the subsidy this year was not available was available last year. But there was no market that de-grew pretty much. So, the growth was relatively higher or lower in different parts of the country but very much overall it was positive.

Moderator: Thank you. We will take the next question from the line of Jatin Chawla from Credit Suisse. Please go ahead.

Jatin Chawla: You have shared the performance for the industry in the strong end opportunity market. Can you share the same for Escorts as well in the quarter?

Shenu Agarwal: Yes, we have the numbers, we have to pull it out. So, if you have any other question in the meanwhile you can go ahead with that.

Jatin Chawla: Yes, a related question was on your market share aspirations for the year and we have seen some gain that has come through in the first half. How are you looking at your market share for the full year?

Shenu Agarwal: In the first half YTD basis we are about 0.9% up from last year's first half and we hope to at least continue this kind of a scenario.

Jatin Chawla: So, for the full year broadly a 100 bps kind of market share gain is what?

Shenu Agarwal: Yes, it could be yes. That is right.

Jatin Chawla: And when you maintain your growth rate for the industry you are at 12% to 15%. Would it be fair to assume that this would be within the second half more front loaded meaning 3Q will be the main driver for the growth and then 4Q with a strong base we see growth slowing down?

Shenu Agarwal: That is right because Q3 would be I mean we are expecting about 18% to 20% growth in the market industry in Q3 largely this variation between Q2 and Q3 is largely because of the shift of the festive season and also because in last year in July we have a heavy Base because last year some of the sales shift is because of GST from June to July. So, that is why Q2 looks very subdued but as I said the sentiment on the ground is very positive.

It is just the shift of the season and the GST impact last year. So, Q3 should cover for that because Dussehra, Navaratri etc are in Q3 this time. Q4 you are right, Q4 was very, very high last year

and therefore the growth may not be as high as we have in Q4. But we are expecting positive growth marginally positive growth in Q4 also but substantially good growth in Q3.

Jatin Chawla: You briefly mentioned that financing availability is not an issue but just again wanted to cross check is that because you have your own captive NBFC or do you see that from other NBFCs also funding of tractors is not a problem?

Shenu Agarwal: Our captive company although we are very optimistic about it for the future but right now it is only catering to about 10% to 13% of the volume. So, our dependence is like significant on other companies and yes, but overall we are not seeing anything any liquidity crunch or any fall back from the financing companies at all. In fact, at least in the festive season they were in touch with us trying to get more and more business out of our sales and this applies to both banks and NBFCs.

So, we are not feeling any crunch on that we are reading in the media, we are not feeling that crunch at least in the rural sector. May be that we are the priority sector and they have to keep their focus on this sector in any case.

Jatin Chawla: Just one more question on the finances. So, other expenditure this quarter seems to be on the higher side. So, there is almost a 36% Year-on-Year growth as well. Any one offs there?

Bharat Madan: No Jatin, I think one of the reasons is since we were building inventory for the festive season for the oncoming season in Q3 so there is production overheads are very high in the second quarter. So, we have done almost 25% more production in second quarter to cater to the Q3 demand and we were carrying that inventory to Q3. So, obviously that impact is there on the overhead side that impact is there although your overheads are directly coming in second quarter. So, the benefit will definitely improve in the second and third quarters when the sale happens.

Jatin Chawla: And just one more question on the finances. When I look at the construction equipment business with a very stable kind of revenue Quarter-on-Quarter we have seen some decline on margins. What would you attribute that to?

Bharat Madan: So, major impact this time on the construction side is like you said our inability to pass on the inflation on the commodity side to the market. So, that has been not only for this quarter I think we have been seeing this trend happening in the last three, four quarters now continuously with the steel prices have moved significantly higher. It is one of the fact, that we have taken price increases in the last two quarters but still the price increase which has happened on the commodity side is much more than that, so much more than probably what the market is able to absorb.

So, which is the impact we are seeing on those numbers now. Hopefully going forward because we are factoring in some more price increase happening in the coming quarters so that should

address the overall number and the guidance which had given for this full year at 4% to 5% sort of margins from construction, we should be able to be very close to that.

Shenu Agarwal: Mr. Jatin, on your first question about our growth in strong and opportunity market so there is some data for you. For strong market the industry growth was 8% and our growth Escorts' growth was 14% resulting in a 0.9% market share increase. This is for H1. And for opportunity markets the industry growth was 10%. Our growth, Escorts' growth was 24% resulting in a market share increase of 1.1%. So, we grew pretty much equally well on both strong and opportunity markets. So, 0.9% market share increase in strong and 1.1% in opportunity and the market overall also was kind of equally growing. So, strong was 8% in H1 growth and opportunity was 10%.

Moderator: Thank you. We will take the next question from the line of Raghu Nandan from Emkay Global. Please go ahead.

Raghu Nandan: Sir, just on the tractor side how is the export outlook for the current year?

Bharat Madan: For the current year we had given a guidance of roughly 50% growth this year over last year. So, this quarter numbers are slightly lower because there is some order which got billed but we could not be shipped on board so that probably will shift to three quarter. But overall number wise we think we should be able to maintain there is some institutional order which is in the pipeline which we expect will get executed in third quarter or the beginning of fourth quarter.

So, overall number we are still looking at somewhere around close to 3,000 odd tractors in this complete financial year.

Raghu Nandan: And sir, like I know it is early days but how would be the outlook for FY20 tractor demand for domestic market?

Shenu Agarwal: Yes, it is actually a bit early for us to predict on 2020 next year. I think we will be in a better position to give you a good estimate post Diwali may be after the festive season has panned out. So, may be in the next call we can answer that.

Raghu Nandan: I mean there are some concerns in the market that now that three years of strong growth has been there next year and also recently that evolving El-Nino conditions and stuff is there and generally when the El-Nino comes in the effect can stay anywhere between 9 to 18 months. So, given these concerns do you think like tractor demand can still be on the positive side or do you think there is a probability it can go to the negative that is where I was coming from?

Shenu Agarwal: Yes, I understand. See the first monsoon predictions will start coming in around March next year so I think we will be in a better position to estimate the effect of next year monsoon for the next year industry at that point in time. But right now what we are looking at the ground in terms of most of the macro factors.

We think that we will definitely have a positive momentum in the industry at least until Q1 of next year. And as I said beyond that is it is too early to say right now. We will have to wait for some more information to be able to predict for rest of the year. But until Q1 we see a very positive momentum.

Raghu Nandan: Coming to the quarterly numbers there is an increase in realization for tractors on a Quarter-on-Quarter basis wherein the realization has gone up by 3%. How much of it is because of the price increase and how much of it is because of the mix?

Bharat Madan: So, it is essentially because of price increase we took up. So, we took roughly 2.25% price increase in Q2 and partly also because we are executing some of the orders for the Assam Government which is under their subsidy-based scheme and there are some implements which is a non-tractor part of the revenue which are also getting added to the topline which is actually looking at impacting the realization.

So, that number itself is about Rs. 23 crores in this quarter which is what are the factor realization but overall on the tractor side other than the price there is not really major change on realization point.

Raghu Nandan: So, the Powertrac, Farmtrac what would be the mix?

Shenu Agarwal: Yes, so for H1 Powertrac is 61% and Farmtrac is 39%. This is for H1.

Raghu Nandan: And sir, on the raw material cost pressure given this 2% plus price hike has it been fully passed on in the Agri segment?

Bharat Madan: Yes, so in the agri side whatever inflation was there till Q2 we have passed it on but obviously there is further pressures now coming on Q3 also. So, maybe we will have to look at some more price increase there going forward after the festive season.

Raghu Nandan: Any sense like what kind of price increase would be required?

Bharat Madan: See roughly 1% cost pressure we are seeing happening in Q3.

Raghu Nandan: And sir, on the construction equipment side what kind of like price increase would be required going ahead and to achieve that 4% to 5% margin for the full year and would we be in a position to take it? You said that it is in the market it might be difficult to absorb the entire commodity inflation?

Bharat Madan: We have been passing on the price increases to the market but only thing is unlike in tractors where we need to pass on the price increases because this is stock and sell model and construction is typically every deal is a negotiated deal so even though you are on paper we take

the price increase but when you end up with the negotiation and setting with the competition there is some pass on which do happen.

So, we have taken price increases so far but I think it is already it is about 2% price increase has been taken in construction sector too in the last two quarters. Because we also had a lot of carry forward from the last year for the inflation part which was not getting absorbed. So, that obviously impacted us but it is not continuing. I think second half also is very good in terms of the volume growth.

So, typically your volumes should be 40% to 45% in first half and second half is 55% to 60%. So, that also gives some operating leverage and bit of the product mix if it is favorable which is what we are banking upon for the second half. We should be able to give us this margins that we are looking at.

Raghu Nandan: And sir, on the tractor side new products atom series and the 47 HP agri paddy specialist tractor so how is the sales run rate and what are the expectations ahead for these products?

Shenu Agarwal: Yes, the demand is very, very good. Actually, we have some customers lined up to buy these tractors because we cannot produce enough right now. So, we are gearing up on the production capacity and also on the supplier capacity among both atom and 45 horse power four-wheeled drive paddy special.

So, January-February-March in that quarter we have some big plans for these two models but Q3 will remain kind of it will grow the volume will grow with respect to Q2 but not significantly because of the supply side constraints.

Raghu Nandan: Can you share the volume for the last quarter Atom and Paddy Specialist tractor?

Shenu Agarwal: We do not have it right now. If you do not mind we can send you an email on that.

Raghu Nandan: Sure sir. I mean can I take the last question or I can come back in the queue for more queries? It was on the railway side. Sir, I just missed your point that sequential margin was lower because of increased share of new products is that what you mentioned sir?

Bharat Madan: Yes, that is right.

Raghu Nandan: And FY19 what kind of growth is expected in railways?

Bharat Madan: So, it is 25% to 30% on the full year basis.

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

Chirag Shah: Sir, I had a question on our industry. So, any specific inputs you can give what kind of tractors are driving in terms of horsepower mix and what kind of trends you are observing?

Shenu Agarwal: Yes, see there is no big shift in the trend really in H1 so far. There is a slight increase in the 41% to 50% and also very slight increase in greater than 50% but not very, very significant. So, for example 41% to 50% has grown from about 45.4% to about 47% and this is on the expense of 31% to 40% which has de-grown by about 1.5%, the weightage of the entire industry.

Chirag Shah: Is it because of regional mix or there is an underlying change in way of farming?

Shenu Agarwal: Yes, largely because of regional mix. Because like some higher horsepower markets have slightly grown more than with some other markets and that is why it has happened. See any fundamental change happens over a very, very long period of time. So, I mean Quarter-by-Quarter or half Year-by-Year it is very difficult to see that. So, whatever we see are slight increases of 1% or 2% is only because of the regional mix.

Chirag Shah: Second question was on the commodity side. So, what kind of pressures we are further expecting and any risk of not being able to pass on either in construction equipment or in tractors?

Bharat Madan: Yes, so like we have already mentioned I mean to say already about 3% cost increases have happened in this year and we are expecting another 1% cost increase in third quarter. So, overall we hope I think by Q4 in this bit of stability happens around that. So, in tractor obviously we have been able to pass it on so far whatever inflation management there till Q2 and then in Q3 again whatever pressure we are facing we think we should be able to take that also as another price increase after the festive season.

So, in construction like I mentioned so there is better pressure there so which we have not been able to really pass on fully to the market. So, one is the issue because of there is a log impact of passing on the inflation and second whatever inflation gets passed on also not gets fully absorbed in the market. So, both the issues are there in the construction segment which is a bit of challenge as of now.

Chirag Shah: And just one last clarification. Sir, does while you have indicated Dussehra sales impact, does the auspicious the sales are very significant when you look at this season if you look at the entire 40 days of sales is it very skewed to the festive day or it is very well spread out?

Shenu Agarwal: See overall there is buoyancy in this time because it is not just festive season because it is also the harvest season. So, there is lot of cash available in the hands of the farmers. And depending on the markets we see lot of skewness in from day-to-day depending on whether it is auspicious day or not. So, for example if we take Haryana or Punjab market there is not much belief in any particular day and it is more depends on the harvest and the cash flow.

But in some other markets like let us say Bihar or UP or even some parts of MP we see lot of skewness on particular days. So, for example like average sales on a Navaratri day for us will be like let us say about 1,100 to 1,200 tractors. And in the normal day would be about say 300 to 400 something like that. Just to give you an idea of the Q1.

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

Mitul Shah: Sir, I have two questions. One is on the tractor and other on the railway side. In case of tractor sir, we have grown we have outperformed the industry not weaker as well as strong both the markets. Our market share has improved not only purely because of the favorable geographical mix but within strong market also we are growing. So, according to you what are the key factors one or two important factor which is resulting in to this outperformance in the recent time?

Shenu Agarwal: We are just working harder than the others. Nothing else.

Mitul Shah: Basically is there any product change or are we expanding in a big way dealer expansion?

Shenu Agarwal: Yes, so this is actually a result of our strategy I mean nothing that we have done in the last few months. I mean we have been telling you that for last couple of years or more we have taken some strategic actions in the way we handle the market. So, one action is that we have separated out our Farmtrac and Powertrac distribution. Earlier we had a situation where most of our dealers were common for both the brands. And we thought that same dealer would not be able to do justice to two brands which have different meaning to customers. So, that has really helped us especially in the strong markets where the weaker brand is also giving us some growth in volume and market share.

Also South and West have been traditionally very, very weak for us and therefore we had to run several projects starting with AP and then following up with Maharashtra and Gujarat and Karnataka and now we are running a special project in Telangana right now. So, those projects are now yielding results. So, for example our AP market share would be in the regional of 6%, 7% while it used to be 2%, 3% a few years ago.

Maharashtra has also inching upwards 6%, 7% now. So, those things are helping us and that is why one of the major curse with our company was that we were growing only we will grow our market share and only one-half of the country and another half of the country we will lose. Therefore, we will see pretty much static. But the good thing is that now very consistently we are gaining market share in both the strong and the opportunity markets. And that is helping us in better volumes.

Mitul Shah: Within Agri revenues what would be the non-tractor revenue? You said implements roughly Rs. 23 crores so is there anything else sizeable and which has been growing more which is non-cyclical in nature to some extent?

Bharat Madan: No, I think just like our past revenue obviously that has also grown but those are in line with the normal growth rate what we have in the tractors too. So, parts have grown, the engines have grown so overall implement the business is also now start picking up because of the subsidy program. So, I think all these three are essentially the non-tractor revenue would get there on the the topline.

Mitul Shah: Second question is on the railway equipment side. Our margins are slowly improving and the way order book appears it appears that operating leverage will further increase in the second half. So, do you expect margin to improve sizably from here onwards with the new products and new?

Dipankar Ghosh: Actually, if you see the overall margin is pretty I mean in the Q1 it was almost like the EBIT is almost 25.3%. There was not much of an import content. Q2 we had some import content but Q3, Q4 we would be hovering in the range of the whatever 16%, 17% it will be difficult to maintain 25.3% whatever we had in Q1 because we have lot of import contents as a part of the tendering, as a part of the approval process we have to push in some of the new products which have import content which we are confident that by next year we should be able to get our local break systems also approved. Once we do that then it will again stabilize and it will again be improving.

Mitul Shah: So, do we follow any hedging for that?

Dipankar Ghosh: Hedging actually we do not follow. It all depends upon the how the tenders come we have to do that. And as I said that these are few tenders which we have already won and we have to as a regulatory we have to supply this with the particular import content built in.

Bharat Madan: So, this is not really the effect of Forex, Mitul. I think what Dipankar is trying to say because we have high import content so the margins from the input initially are going to be low and we are virtually working at a margin of 8% to 10% in the new product compared with a normal gross margin of 14%. So, that margins will improve gradually as you localize those content.

So, it is not just Forex impact which is happening it is an overall import content is high in that particular material which is what is leading to the lower margin. But as we grow further so obviously there will be localization which will happen which will further improve the margin. So, again as a 12 to 18 months' time we should be able to localize that content and you probably will fall in line and then you can see the margin improvement happening again.

Mitul Shah: And sir, last question on the construction equipment. What is your outlook for next year?

Ajay Mandahr: The industry is talking about maintaining 10% to 15% growth kind of situation even though this is the election year. Expect it to 10% should be the growth.

Moderator: Thank you. The next question is from the line of Deep Shah from Motilal Oswal Securities. Please go ahead.

Deep Shah: Couple of questions. First is on the side of Shenu. You mentioned you guys are having special products in the opportunity markets like Southern and Western. So, if you can elaborate which are these initiatives and how these help us gaining more business in that sense?

Shenu Agarwal: Yes, I think I need more time kind of to explain you about these initiatives but broadly speaking this is mainly a mix of focus and creating a lot of energy in those markets. So, what we do is instead of going to the market full hog what we do is we select a few districts or blocks or micro markets where our products and our distribution is the best and then we focus on that and try to raise the market and try to develop some brand acceptance in those markets.

And once we have done that for let us say six months or so we develop a very good amount of positivity in the rest of the broader market. So, that is roughly kind of the approach that we have taken. So, for example in Telangana we are running a project and Telangana has about 25 or 28 districts and we have selected 6 districts in which we are doing something special in terms of our offering and in terms of our distribution network etc.

So, that is what we normally do as an approach. But I will be very happy to make a detailed presentation to you when an opportunity arises.

Deep Shah: Second question is on the Escorts credit penetration I mean if you can elaborate more on the geographical leverage etc how has been the progress in this quarter as compared to last quarter that will be helpful?

Bharat Madan: I am sorry quarterly data we do not have on that right now but I can give you generally kind of more of broader answer on this. So, we have a quarterly and a monthly plan for expansion. Also a plan for penetration within the same dealership or within the same area where Escorts credit is operating. So, we are very much on the mark on geographical expansion.

So, we are already in about 9 or 10 states as of now and by end of next calendar year our aim is to be in about 80% to 90% of our dealerships. And as we have now the overall penetration is roughly, I think about 12% to 13% as our overall sales or client sales right which we want to take up to about 30% by end of the next calendar year. And on both accounts we are pretty much on the mark.

Deep Shah: And last question is Bharat, if you can elaborate on cost control benefits. So, how much it must have contributed to margins this quarter roughly?

Bharat Madan: The cost side I think our indication is I think it will be closer to 0.75% to 0.9%. I think it is about 90 basis points you can say. I think it is coming both from a combination of manpower cost and material cost initiatives. So, both put together I think what has led to this improvement.

Moderator: Thank you. We will take the next question from the line of Shyam Sundar Shriram from Sundaram Mutual Fund. Please go ahead.

Shyam Sundar Shriram: Sir, typically tractors are used for commercial applications as well as agricultural purposes. How was the commercial usage now holding up we are hearing of some restrictions and registration of tractors for commercial purposes and in some states with model code of conduct coming in to place. We are also hearing some commercial applications coming down. With this context how are you looking at commercial usage of tractors over the next six months panning out?

Shenu Agarwal: Yes, so on the ground we are not feeling any pressures like this from the commercial side also. Of course commercial is very, very sporadic and very political and in different parts of the country I mean different things keep on happening. So, for example South Bihar mining will open up one day and will close in three months and all that stuff keeps happening. So, we have to be just agile and we have to just know where the demand is coming from and be there at the right time.

But other than that we are actually seeing lot of momentum in our commercial or sales for commercial purposes, commercial uses. Right now, there are lot of markets which are doing very, very well on the commercial side. So, we have not seen any concern on that so far.

Shyam Sundar Shriram: So, you do not see that has any threat going over the next six months if at all something changes on the ground?

Shenu Agarwal: I think it will be for positive actually until the election at least.

Shyam Sundar Shriram: Sir, recently M&M launched a slightly underpriced product under the Trakstar brand. So, which geographies are more amenable for these lower priced tractors? Will this lead to a market size expansion in the sense that our new customers who have never bought and first time buyers may come in to the market and related to that is this a threat for us?

Shenu Agarwal: I do not think, I think our brand is a much more stable brand it is around for 70 years now. Trakstar is a very new brand and you know that tractor industry is a very matured industry. It is not very easy to display its incumbents in any market. So, it will take a long time for Trakstar to prove itself. I mean I do not want to comment on what their strategies etc but I think even if it is something formidable it will take a lot of time.

Moderator: Thank you. The next question is from the line of Navin Kumar Duggal from Nanolia Financial Advisors. Please go ahead.

Navin Kumar Duggal: My question is on the tractor side. In earlier calls you mentioned that the shift is happening towards the lower HP tractors. So, how is the progress going on that side?

Shenu Agarwal: Yes, see as I was explaining earlier on this call that see there are some fundamental difference changes that are happening which require larger tractors to be used. But that kind of a shift is very, very slow in India and only over a period of 5 to 10 years you can actually see that there is some significant movement across the horse power segments. Most of the quarterly or even yearly shifts that we see are the result of the regional mix.

So, for example in Southern MP there is in Indore belt penetration of higher HP tractors and if that market goes up then of course we see a shift on even the all India numbers. So, I think if you are just looking at H1 sales which is about 1.5% shift from 31% to 40% to 41% to 50% that is largely because of that and not because of any fundamental changes that had happened in the last six months.

Navin Kumar Duggal: The second question is on the construction equipment side. What is the localization content there I mean import content?

Bharat Madan: So, in construction the overall content I think in the manufacturing what we do is not much it is only the excavator business which we have started or the trading business which we are in where we importing the products like we have recently tied up with Doosan for example for excavators and earlier we were doing distribution for forklift truck and high-end cranes. So, those are the products which are today imported.

So, actually there we got exposures in terms of the FOREX risk. Otherwise on the local manufacturing side there is not much. I think overall our company level is less than 2% of the import content.

Moderator: Thank you. We will take the next question from the line of Sakshi Mahant from India Nivesh. Please go ahead.

Mayur: This is Mayur. Just wanted to know what are the current inventory levels in the system that is with us or dealers and distributors?

Shenu Agarwal: Okay inventory level is high as compared to normal and that is that is again very normal for the festive season. And we are in the middle of the festive season so we are still about 8 days away from Diwali. So, we are maintaining high stock as the industry is right now. And of course we will do some correction in this month and some of more correction next month after Diwali is over.

Mayur: Because we have done some channel checks and they were suggesting that yes, as usual the festive inventory is high but we are also getting some signals that demand so far has been a little lull and they are anticipating that probably in the next one week, 10 days we should have some strong demand. So, in case that happens then I am sure it is business as usual but for some reason if the demand really does not come back then do we expect a significant production cut to correct this inventory?

Shenu Agarwal: No, see that question is actually I think a little bit hypothetical because we are only about 7, 8 days to Dhanteras and Diwali. And we have a very strong IT based system of managing our sales pipeline. So, we have a very good idea what are we going to sell on Dhanteras and Diwali because we have the leads we categorized the leads in to different categories.

We are in touch with these leads already. Many of them have deposited some booking amount with us. So, we cannot expect a huge surprise now. So, we are in a good position. We would not give you any surprise on stock situations.

Moderator: Thank you. The next question is from the line of Aksh Vohra from Praj Fincorp. Please go ahead.

Aksh Vohra: Sir, just wanted a clarification. You mentioned 10% to 15% tractor growth for this fiscal or for next fiscal?

Shenu Agarwal: No we said 12% to 15% for this fiscal.

Aksh Vohra And what would be the outlook for next fiscal? You had mentioned around 7%, 8% I think so that stands?

Shenu Agarwal: No, we did not mention anything. So, we just said that we are seeing a positive momentum at least until Q1 of the next fiscal. And post that there are lot of factors that are to be seen and we will be in a better position may around in Q4 to give you a better or any number actually on the next full year.

Aksh Vohra And on construction equipment what are the target EBIT margins that we are looking forward for like not for this fiscal probably from a medium term perspective?

Bharat Madan: So, if you look at our Vision 2022 document we have given a direction for a high single digit margin on the construction side. So, it will be roughly 8% to 9% sort of margin which we think we can stabilize this business at.

Aksh Vohra Do we see traction coming in from next fiscal year that the margins can move forward or it is still will take some time to get to say 4% to 5% kind of EBIT margins?

Bharat Madan: So, 4% to 5% is the guidance which we had given for the current fiscal year. So, honestly if you exit the year with that sort of margins for next year we expect things should only look better from this. So, it will be gradually increase obviously it is not a single year we shift to the 8% to 9% growth but that I said is the Vision 2022 number what we are talking about. So, it is still three years to that. But average realization which we are working is to improve the margin basically in this business.

Aksh Vohra Sir, lastly on how this industry cycle works for construction equipment? We have seen a very long dull cycle and we have come up with a great base effect and we are growing at a good

number. But how sustainable is this kind of growth we are looking for from 2 to 3 years perspective?

Ajay Mandahr: Actually, if you look at the growth last two years has been phenomenal in terms of the industry growth. I think the growth will be of not that quantum when we look at 35%, 40% kind of growth that is something which is not sustainable for long. So, I think the question is on completion of the project or delivery of the projects which are on. Some big tournament is also happening on the project side. So, I think from next year onwards the number increase of 10% to 15% if we look at in this industry will be there and that will continue for another three, four years I think or may be more.

Aksh Vohra Have we seen any market share increment in construction equipment division in this first half?

Ajay Mandahr: Yes, we have improved our market share in the core sector that is pick 'n' carry sector. That too in a particular sector the contributions are good. We have achieved close to 70% market share in safe crane. So, we are concentrating more on the segments which give us money. So, that is the attention that we have taken now.

Moderator: Thank you. We will take the next question from the line of Sameer Deshpande from Fare Deal Investments. Please go ahead.

Sameer Deshpande: I would like to know whether we have started selling this farm implements and are we getting any contribution from that in a meaningful way?

Bharat Madan: Look the implements which you talked about actually is part of the order which we got from Assam Government for under the subsidy-based scheme. So, that comes as a packet so it is not something which we have started manufacturing and also it is something that we are trading activity which we have funneling along with our tractor and supply in to the government.

So, you cannot look at margin in isolation so it is a bundle deal So, yes on the overall basis the margins in the overall program are lower than probably what you make in the normal case and that it is operation but the volumes are likely to be better there.

Sameer Deshpande: And now with this increase in raw material prices which you have passed on in most of the cases and you may pass on going forward. Do we expect to maintain a margin for the entire competitor on 12% plus going forward?

Bharat Madan: See we have given our initial guidance of about 100 basis points improvement in the margin on the overall full year basis until the first half we had a very low base so that is where we are seeing a good traction have been on the margin front. But in the next two quarters the base structure is very high. So, but we are still seeing our guidance so I think we should be able to be somewhere around that between 11.5% to 12% range.

- Sameer Deshpande:** And this Tadano joint venture which we had for the higher range of cranes when it will start the activity?
- Bharat Madan:** So, likely to be from December. So, right now in the process of setting up the company and getting all the consensus and approvals and registration in to place. So, hopefully by end of November we should have everything in place. So, we will start commercial production from December onwards.
- Sameer Deshpande:** From December that is from new year you may start the production for the January 2019 onwards?
- Bharat Madan:** Yes, you can say that. That JV will start manufacturing.
- Sameer Deshpande:** We have 50% there?
- Bharat Madan:** Yes, we have 49%.
- Sameer Deshpande:** And what is the reason for this higher other income of Rs. 22 crores?
- Bharat Madan:** So, this is basically since we have cash on the balance sheet so it is the investment which we have done with the income coming from the investment on those mutual funds and the investment categories so this is the credit which we give to the dealers to the channel partners so that the interest income is based on that. And there are also exceptional items like Forex gains on the export front. So, income has come in related to this.
- So, just about Rs. 4 crores, Rs. 5 crores is in the exceptional income which is coming out of this MTM equivalent on the investment income which may not be the recurring one because it is giving that trend situation on the debt market like the NBFCs. So, but I think the real number you can say is Rs. 15 crores to Rs. 16 crores sort of other income possibility will be there in each quarter on an average basis.
- Sameer Deshpande:** Rs. 15 crores to Rs. 16 crores will be a normal?
- Bharat Madan:** Yes, normal level which we will have.
- Sameer Deshpande:** And wage revision we were going to undertake in Q2 have we done that?
- Bharat Madan:** So, Q2 it is not wage reason so it is still a normal appraisal cycle for the managerial staff for the white collar employees which we follow from July to June. So, that increase obviously has happened from 1 July. For the blue-collar employees for the wages part the settlement is due in next year not his year. So, it will be in 2019 second or third quarter. So, that process obviously will start next year. So, it has no real impact as of now.

Moderator: Thank you. We will take the next question from the line of Raghu Nandan from Emkay Global. Please go ahead.

Raghu Nandan: Sir, just can you share for this JV with Tadano how much is the investment from Escorts side?

Bharat Madan: See we have 49% partner there and 51% is in Tadano. So, the initial capital requirement will be I think close to Rs. 60 crores, Rs. 70 crores which in a longer period we are looking at say 8 to 10 years cycle it will be somewhere around Rs. 150 crores to Rs. 200 crores investment. The requirement which will come. But initially we are going to start with Rs. 60 crores, Rs. 70 crores sort of capital.

Raghu Nandan: So, out of that Rs. 60 crores, Rs. 70 crores, 49% will be from Escorts?

Bharat Madan: That is right.

Raghu Nandan: And sir, like coming back to the festive season. Starting from Navaratri to Diwali what is your internal expectation what kind of growth are you looking at versus the last year festive season?

Shenu Agarwal: Navaratri to Diwali?

Raghu Nandan: Yes.

Shenu Agarwal: I will have to talk to you separately on this. I will give you some numbers separately on Navaratri to Diwali.

Raghu Nandan: And sir, like within tractors what will be the share of non-agri tractors and what would be the growth in the first half of the quarter that is commercial or non-agri what would be the kind of you said the momentum is strong currently in the market?

Bharat Madan: See right now see this season is actually largely the agri season. Of course, commercial sales happen but commercial sales as a percentage goes down during this season. I mean that is very, very normal. So, because there is a harvest and lot of people, lot of farmers have money coming in right now and therefore all these additional sales or seasonal sales is largely because of the agri sector.

So, once we enter in November-December-January period then you will see as a percentage commercial sales will start rising again because at that time there will not be many farmers who will be in the market to buy tractors.

Raghu Nandan: And broadly what will be the share, sir?

Shenu Agarwal: It is very, very hard to say but normally when we are asked, we do say that in our estimates the tractors that are used also for commercial purposes is about 40%. We think there are hardly any

tractors that are used solely for commercial purposes. I think that number is very, very low. But tractors which are significantly used for commercial purposes in addition to agri is about 40%.

Raghu Nandan: And for the current year would you say the growth will be in double digits in this segment?

Shenu Agarwal: Yes, we are already given an estimate a few months back of 12% to 15% growth in the industry for the current fiscal and right now.

Raghu Nandan: That is for the commercial segment?

Shenu Agarwal: For the commercial segment I think that growth should be in the range of about 15% to 20%.

Raghu Nandan: And sir, can you share what is the share of traded products in construction equipment?

Shenu Agarwal: It is only about less than 3% in terms of volume. So, value wise it will be higher but in volume terms less than 3%.

Moderator: Thank you. Next question is from the line of Supratim Basu from Americorp Capital. Please go ahead.

Supratim Basu: Apologies if you have answered this before but just looking at the presentation could you tell me why your debt has gone up from Rs. 50 crores to Rs. 211 crores?

Bharat Madan: See this is the working capital basically because you are really sitting in the offseason month and we are building inventories for the high season months which was happening in this time in Q3. And since obviously we have capacity issues because we were almost running at a peak capacity level for last three months now.

So, we were not able to really push the numbers in the season time and the production is required so we had to build that inventory. So, it is a temporary situation so in Q2 the working capital has gone up but in Q3 we will see this traction happening back. So, by the end of Q3 you will see that things will be back to the normal.

Supratim Basu: So, both Rs. 91 crores plus Rs. 99 crores would be working capital?

Bharat Madan: Yes. Term-debt is down to roughly about Rs. 20 crores. So, balance is all working capital.

Supratim Basu: And so, this will get wound down by the end of the year?

Bharat Madan: Yes, so again like I said it is basically depending on the season obviously by March again the season start. So, normally the cash situation is good. So, March to June is a good cash flow period for us. So, that trends are obviously for us therefore 7 to 8 months with the cash flow is very positive but 3, 4 months where we need the working capital so it is there.



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Moderator: Thank you very much. Ladies and gentlemen, that seems to be the last question for today. I would now like to hand the conference over to Mr. Bharat Madan for his closing comments.

Bharat Madan: Thank you ladies and gentlemen for being present on this call. For any future enquiries feel free to write in to us at investorrelation@escorts.co.in. You can also log on to our website www.escortsgroup.com for our earnings releases as well as the other details and the transcripts will be available on our website after sometime. You can visit our social media pages for latest company news, developments, etc. We will meet again in the next quarter. Thank you very much and a very good evening.

Moderator: Thank you very much. Ladies and gentlemen, on behalf of Reliance Securities Limited, we conclude today's conference. Thank you all for joining us and you may disconnect your lines now.