"CEAT Limited 4QFY15 Results Conference Call"

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Moderator: Ladies and gentlemen, good day and welcome to the CEAT Limited 4QFY2015 results conference call hosted by Macquarie Capital Securities Private Limited. As a reminder, all participant lines will be in the listen-only mode. There will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during this conference call, please signal an operator by pressing * and then 0 on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Amit Mishra from Macquarie Capital Securities. Thank you and over to you, Mr. Mishra.

Amit Mishra: Good afternoon everyone. It is our pleasure to host CEAT Limited post results conference call and thank you very much all of you for participating on it. To represent the company, we have with us Mr. Anant Goenka – Managing Director and Mr. Subba Rao – Chief Financial Officer. I would now like to hand over the call to the management for opening comments and then we will open the call for Q&A. Over to you sir.

Anant Goenka: Thanks Amit. So good afternoon everyone and a warm welcome to CEAT's Investor Call. This is Anant Goenka – Managing Director and I have here with me Mr. Subba Rao – our CFO. Thanks once again for your interest and I will briefly take you through our results and a few parameters relating to our results after that we can have questions.

Some information on our year-on-year results: So CEAT India registered a growth of 1.5% in revenue terms and 4.8% in volume terms. Raw material prices have come down by around 10% on a year-on-year basis and some of this benefit was passed on in the OEM or large part of it was passed on in the OEM and export segments. Natural rubber prices along with crude related raw materials have continued to soften even after this quarter and we do expect the full benefit to even further reflect going forward in the next quarter or quarter and a half. The 4.8% volume growth was mainly on account of growth in the replacement segment while OEM in exports had flat volume growth. The passenger segment has continued to grow well for us with growth levels at over 20% on average. This includes passenger car radials, utility vehicle radials, two and three-wheeler tyres. On a quarter-on-quarter basis, CEAT India registered a 4.6% revenue growth with volume growth of about 6.7%. In terms of each segment, replacement in OEM grew at about 9% and 15% respectively, however exports registered a decline of 11%. Raw material was lower by about 3% from quarter 3 to quarter 4 and softer raw material prices have helped gross margins to improve on a quarter-on-quarter as well as year-on-year basis. Overall in FY2015, we experienced a steady growth in both domestic OEM and replacement tyre market and we have added new OEMs like Yamaha and Renault recently to our portfolio which will be certainly very beneficial going forward.

Going forward a little bit on the outlook, a few key things on the project front that we are looking at India expansion plans are on track in fact a little bit ahead of schedule and we hope to start our production at Halol for passenger car radial cars very shortly. Our Nagpur plant is also very much on track, work on the plant has begun, and should be ready towards by the end of the year. Our project in Bangladesh however is quite delayed. There are some problems we have had with respect to land acquisition out there. We have acquired the land but there are issues that we are having out there and work has unfortunately not begun. So there is a quite a large delay there. We are still waiting and watching for this issue to get cleared.

On the raw material front as I shared, we expect rubber prices to stay around current levels. Crude prices have softened quite a bit towards the large part of last year and we expect that further benefit to come going forward. Going forward, we are quite positive overall on the economy and we expect steady growth in both domestic OEM as well as the replacement tyre market. So overall we feel quite positive on growth with a lot of changes happening in the economy on mining, etc. I will now hand over the call to our CFO, Mr. Subba Rao who will talk about a few key financial parameters.

Subba Rao: Thank you Anant. Ladies and gentlemen, good afternoon. I would present the financial primarily focusing on the P&L account and balance sheet analysis. Coming to the P&L account, again I would divide it into 2 parts, one is quarter-on-quarter analysis and again the whole year analysis for the entire 12 months. Let me just touch up on the gross margins for the quarters. On year-on-year basis, the gross margins expanded by 650 basis points to 41% and on quarter on sequential basis, it is about 50 basis points. EBITDA quantum grows by 17% year-on-year to 187 crores and on sequential basis by about 2%. The margins have expanded by 170 bps year-on-year to 12.8%, however on sequential basis, they marginally come down by 20 bps. Profit before tax has expanded by 270 bps year-on-year to 9.2% to 135 crores. However on sequential basis, the PBT margins have slightly come down by about 20 bps and for the whole year for the 12-months period, gross margins have expanded by 330 bps from 38.6% from 35.3%. EBITDA quantum rose by 3.5% to 681 crores. The margins, however, came down slightly by about 10 bps to 11.8%, will explain the reasons for this slight reduction in the margins during Q&A.

The finance cost has come down by 23% from 172 crores to 132 crores largely due to reduction in the borrowing cost and also the hedging cost. The PBT on whole year basis, again the profit before tax as the percentage of the sales has expanded by 90 bps to 8.2%, that is 472 crores for the year. On balance sheet front, debt equity has come down to 0.46 times from 1.14 times. Debt-to-EBITDA has come down from 1.8 times to 1.1 times, we are almost at 1:1 in the debt-to-EBITDA. EBITDA-to-interest has moved to 5.2 times from 3.8 times indicating excellent coverage of the serviceability of the debt. Return on Equity and ROCE for the year stands at 26% and 25% respectively which compares very well with the competition.

On Sri Lanka JV front, our Sri Lanka JV revenue has declined 13% sequentially and year-on-year basis by 10%, however EBITDA rose by 23% year-on-year to 23 crores from 18 crores earlier and EBITDA margins also grew 610 bps from 16.6% to 22.7% on year-on-year basis. Again on full year basis for the whole 12 months, EBITDA margins expanded by 230 bps to 23.1% and EBITDA quantum grows by 8% to 102 crores. I pause here my presentation and we will again take up any queries and any clarifications in the Q&A session. Thank you. We will open the Q&A.

Moderator: Thank you very much sir. Ladies and gentlemen, we will now begin the question and answer session. We have the first question from the line of Basudeb Banerjee from Antique. Please go ahead.

Basudeb Banerjee: A few questions, one if I see your FY2014 balance sheet and FY2015 balance sheet, there was a huge increase in working capital last year, and again this year, there was a huge reduction. So can you throw some light on this huge volatility in terms of working capital as such?

Subba Rao: End of last year, we had such a buildup of both raw material as well as finished goods to meet certain contingencies and we reduced those higher limits to the normal limits in the current year. We have in fact released close to about 120 crores of working capital during the course of the current year despite a higher volume as compared to the last year. So that is why it is just paring down the higher volumes of some strategic stock ups, primarily in the finished goods and raw material.

Basudeb Banerjee: In terms of receivable deals also it seems on the lower side?

Subba Rao: Yes, slightly but the receivables continued to be largely the same, year-on-year basis.

Basudeb Banerjee: Next question is sir in your standalone P&L this quarter, both your staff cost and other expenses seems to be on the higher side. So can you quantify how much of the other expense was for World Cup Campaign and why this staff cost was higher and how much is for the IPL related expense which should come in Q1?

Subba Rao: Yes, overall there are about 4-5 expenses which were out of tune for various reasons the last year. If you look at the revenue, revenue has gone by 5%. Most of the expenses ideally should go up in the same tune but for certain specific reasons, say for example salary has gone up by 21% as compared to the last year primarily because of the wage revision and once in 3 years, we go through the workers wage revision that has come in this year. So that is the reason for this and second reason because of the reduction in the interest rate, the provisions on account of gratuity and leave encashment, as the interest rates goes down because there is a future discounting, so we have to make higher provisions. That is about 23 crores. So these are the two reasons why because of which the salary cost for the year has gone up by 21% and we also have significant part of our production sourced from outsiders. So the outsourcing cost also have gone up by 40% by about 87 crores which again is primarily about 25% is the volume growth and 15% is on account of the rate revision. So again periodically, we keep adjusting the outsourcing cost so that 15% is the additional burden that we have taken because of the periodical rate revision. The freight also has gone by 20% which is again 40 crores. This is the structural adjustment because of the mix changer. Perhaps this would continue though we are going to take a keen look at the breakup of this expenditure and try to pare it down during the current year. The sales variable cost has gone up significantly by about 40 crores and the repair is also because of the safety issues, we had to carry out such an extraordinary repairs which are nonrecurring in nature though they may partly recur but last year was a focus area on the safety front and we significantly carried out the repairs which again, the repairs were higher by about 50%, the quantum being 18 crores and advertisement is an investment, we continue to invest. So again it is about 35% higher as compared to the earlier year. In terms of the quantum, it is about 25 crores higher. So in the aggregate, these 5 expenses have resulted in 230 crores for the year. So even if you take say half of it or more than half of it as normal and other half as abnormal, about 150 crores is extraordinary expenditure which we incurred during the course of the current year which is unlikely to recur in the following years. So this is a major reason why some expenses look higher than usual.

Basudeb Banerjee: Sir about the IPL expense which should come in Q1?

Subba Rao: IPL expenses, yes will come in Q1 but this is over a period of 3 years at a rate of about 10 crores per year. Yes, the entire amount of 10 crores but it will be phased out. So we incur something in the current quarter, something in the next quarter. So there is an overall budget for the year.

Basudeb Banerjee: So 10 crores per year. Okay that is not much material and last question sir, Mr. Goenka said that already bulk of that PCR brownfield expansion in Halol is over and so what is the pending CAPEX in coming 2 years for Nagpur project and other brown field projects?

Subba Rao: Nagpur project is 420 crores. Substantially, it is not incurred yet except some small amounts that has been spend on the land. Yes, this much what we can say. Bangladesh project, we already know that there is some kind of delay because of certain land issues. So both on account of Halol Phase-II PCR project as well as Nagpur. PCR also we have not spend completely. Still there is a significant apex that is outstanding that we would incur some of it post commissioning of the operations also and the 420 crores of Nagpur close to both the projects put together over the next 18 months we must be spending about 800 crores of kind of capex.

Basudeb Banerjee: That 800 crores include the maintenance CAPEX also?

Subba Rao: No, maintenance CAPEX, the run rate is about 80 crores per year.

Basudeb Banerjee: Sir last question. Post this recent increase in the Chinese radials into the market, what is the present CV bias tyre utilization for CEAT and any change on a sequential basis?

Anant Goenka: It is around 80%-85% kind of levels.

Basudeb Banerjee: Nylon truck, nylon tyre and was there any reduction in last 1 or 2 quarters because of this Chinese increase in market shares?

Anant Goenka: So there has been a lot of Chinese inflow into the market but I will say that overall sales have been flat.

Moderator: Thank you. Next question is from the line of Arjun Khanna from Principal Mutual Fund. Please go ahead.

Arjun Khanna: Sir just to carry forward the earlier question in terms of bias utilizations. You mentioned exports of ours were down, could you help us what are the key reasons for it, was it largely currency driven?

Anant Goenka: Yes, it is a mix of currency, depreciation of currencies of key markets Brazil, I think Nigeria etc. that was one. In part also a lot of the exports that we do are of truck bias tyres and LCV bias tyres. Now radialization is happening all over the world. So as a result of that there is a shift towards radials. So that is one second reason and third is competition from Chinese tyres as well. So as raw materials prices are coming down and I do believe that overcapacity in China, what happened is US has put in an import duty for Chinese tyres. So China is having a big impact on competition around the world. So these are 3 large reasons why exports are down.

Arjun Khanna: Sir in the sense then how do we look at our Bhandup facility going forward?

Anant Goenka: Bhandup is still overall utilization, it is about 230 tonnes per day capacity and it is still running at about 200 tonnes per day. It is pretty recently utilized for anything, any thought on I guess may be coming to closure or things like that. So we are still at about over 85% capacity utilization. So we are going to aim towards continuing to see how long we can stretch this level of utilization.

Arjun Khanna: Fair enough. My second question is in terms of two-wheeler pricing? Have we seen any impact there at all?

Anant Goenka: In the replacement market, there has not been any change in pricing at this point of time. With OEMs, lot of them we have price formula, so that goes down as raw material prices come down.

Arjun Khanna: Sure, fair. In terms of our new capacity, would it largely be driven for replacement or we would be looking at incremental OEM share?

Anant Goenka: For two-wheeler?

Arjun Khanna: Yes, two-wheelers.

Anant Goenka: For two-wheeler, a large skew of it is going to be towards scooter tyres because scooter segment has grown very fast and our capacity was skewed towards from the market which was maybe 3 years old. So there is a big shift towards scooter becoming a much larger share of the two-wheeler business. So we are able to a large share of business for scooter but the mix is going to be approximately something like 50%-60% replacement market about 30%-40% OE market and about 10% exports.

Arjun Khanna: Just to understand sir, would scooter margins be similar to say that the motor cycle margins?

Anant Goenka: Yes.

Moderator: Thank you. The next question is from the line of Puneet Gulati from HSBC. Please go ahead.

Puneet Gulati: Can you give some more color on what kind of capacity Nagpur is going to throw up and your Halol project and what is the amount that you will capitalize during the year?

Anant Goenka: The Nagpur capacity is going to be about 10 lakh tyres per month and motor cycle combined. Today capacity is about 10 lakh tyres. So this will be about between 10 and 12 lakh tyres. It will take about a year, year and a half from say quarter 4 of next year or quarter 4 of this financial year to ramp up. So approximately 2 years from now to reach its full capacity so that is from the Nagpur plant.

Puneet Gulati: And 420 crores capitalization from this?

Anant Goenka: That is right but entire capitalization will not happen during the course of the current year between both projects Halol and Nagpur, we must capitalize around 650-700 crores because some payments, some equipment will continue to arrive post commissioning of the operation because the ramp up will take time and some incremental capex will take place thereafter.

Puneet Gulati: And on Halol?

Anant Goenka: Halol is largely going to be a passenger car and UV radial plant. That is going to have a capacity of about 5 lakh tyres in total and it is about 120 ton per day capacity out of which a small capacity is truck radial about 10 tonnes per day and 110 tonnes per day is passenger car and UV tyres and that should be ready in about a quarter from now.

Puneet Gulati: How much CAPEX have you spent on that and how much more you need to spend?

Anant Goenka: That is about 650 crores CAPEX in total.

Subba Rao: Yes, would have spent about 200 crores kind of because large part of the machinery is still to be paid for, but by December, most of it would have been spent.

Puneet Gulati: That is when you will capitalize all at one go.

Subba Rao: No, it is a progressive capitalization. Everything, entire 650 will not get capitalized in one go. So June-July would be commissioning the operations as Anant has said and partly will capitalize about 400 crores, we will capitalize by that time and balance would be progressively spent.

Anant Goenka: There is also some machinery which will come over the course of a, little bit even over a year from now. So, some of that will take time as well. So it is planned that we will phase it out because demand, we will may not be able to fully utilize it on day #1.

Puneet Gulati: So by December how much capacity would you be able to add out of the 5 lakh?

Anant Goenka: Very broad numbers, I think maybe about 1 lakh.

Puneet Gulati: By December only 1 lakh and then over next year, you will take it to 5 lakhs.

Anant Goenka: We would be there but there will be in a way new manpower running the machinery, it will be machines which are not yet fully 100% operational to its high speed cycle time**,** all machinery is not in. So these things, generally the ramp up of a plant takes about a years' time, year, year and a quarter, in this case it may be a little bit over a year because of the machinery also and the planning is such that we are phasing out the entire investment.

Puneet Gulati: So by December end, what will be your total PCR capacity?

Anant Goenka: Currently it is about 3 Lakh including PCR and UVR. I think it will be 3 lakhs tyres today which is up 4 lakhs by December, I mean 1 more lakh by December.

Puneet Gulati: Right and then all the way to probably 8 by next December or March 2017?

Anant Goenka: That is right.

Moderator: Thank you. The next question is from the line of Ashutosh Tiwari from Equirus. Please go ahead.

Ashutosh Tiwari: Sir can you please share in this year how much is the ad spend as percentage of total sales?

Anant Goenka: How much is ad as the percentage of total sales?

Ashutosh Tiwari: Yes and how it will move within next year?

Anant Goenka: It is approximately 1.5%-2% type levels. Going forward also it will be along similar lines as the percentage. So it will go up but we may take it up slightly more, maybe a little bit around 2% or so.

Ashutosh Tiwari: Regarding tubeless tyres in two-wheelers, a lot of ads are coming on TV right now. So how much in the current two-wheeler market, what percentages of that and how the realizations of tubeless tyres in two-wheeler different from normal tube tyres?

Anant Goenka: So I will take your last question first. Basically tubeless tyres as mentioned in the ad really what it helps out on is if there is a puncture while you are riding, it will help you go to the final destination before the air comes out. So you can travel a few kilometers comfortably with the tubeless tyre. Second is that the tyre does not burst or it is not a puncture which can cause a risk so to that extent it is also a safer tyre. So to that extent tubeless is far more beneficial than tube type and approximately I would say 40% or so of the market is tubeless. I can get back to you on the exact number of what the market tubeless to tube type share is?

Ashutosh Tiwari: What is the pricing difference between the tubeless tyres and the normal tyres?

Anant Goenka: I think, a tubeless tyre would be approximately the tube type, the tube as well as the tyre price.

Ashutosh Tiwari: Sorry, I am not getting it.

Anant Goenka: So if you add the tube and tyre price that should be same price as the tubeless tyre.

Ashutosh Tiwari: There is no difference between the prices of whole.

Anant Goenka: Not much.

Ashutosh Tiwari: And what was the volume growth in different segments in the current year?

Anant Goenka: Largely on the commercial vehicle segment it has been flat and as I shared on the passenger side, we have grown quite well at over 20% type of growth rates led by the motorcycle, scooter category which has grown by over 30%-35% level.

Ashutosh Tiwari: Currently you said the capacity is 10 lakhs tyres per month.

Anant Goenka: That is right.

Ashutosh Tiwari: And that will be going up to 12 lakhs tonnes per month as the maximum.

Anant Goenka: That will be an additional 12 lakhs tyres. So it will go from about 10-11 today to about 22.

Ashutosh Tiwari : No, I am talking about this year. I think the Nagpur expansion will come up only by the end of the year. So this year, how much room you will have to in terms of volume growth?

Anant Goenka: This year what we are doing is we are adding some outsource capacities. In some way, we are also adding capacity probably up to about, I would say the adding capacity is about 2 - 2.50 lakhs tyres from our in a way current sources and new sources excluding Nagpur plant.

Ashutosh Tiwari: So to that extent we could see the overall volume growth in the current year?

Anant Goenka: Yes, also over the course of the last year, there was some volume growth. So if you look at for example, quarter 1 over quarter 1 that growth should continue. Quarter 1 of last year was not at 10 lakhs. So quarter 1 of last year may have been at about 8.5 lakhs. I am giving you very broad numbers. Today we are at 10 and then so 8.5-10, there will be clearly some growth even in quarter 1 to quarter 1.

Ashutosh Tiwari: Sir my last question is two-wheeler capacity per se, if you look at currently, the demand supply is kind of matching up in terms of peak season, there is shortage also of two-wheeler tyres in the market. That is what we get from channel interactions but now that you are expanding you are doubling your capacity in March I think other players are also expanding, not in that same fashion, how the market would be say 1.5 year down the line, will the pricing power will remain there or do you think that some pricing competition can come through capacities are on the higher side?

Anant Goenka: One is that the market has grown very well in the last 3-4 years even during the down turns, we have seen scooter growing at over 20% and motor cycle also growing at about 7%-8%, and OEMs also have grown very well. So that impact will now come in the replacement market going forward. OEM growth on the other hand maybe a little subdued because of the challenges we are facing in rural economy, bad rainfall, etc. So rural economy has gone through a fair amount of pain in the last 4 months and that may continue going forward for some time, very difficult to say but that can continue. The OEM demand may be a little subdued but replacement I think will be very positive and replacement is where we make all the money. So very difficult to say how pricing power will remain but the good thing is that, yes there are less players here in this market and therefore competitiveness is a little lower, actually investing in the brand a fair amount, so to that extend our brand equity, we believe is stronger than anyone else. Perhaps MRF is the one which is of course doing well.

Ashutosh Tiwari: Sir what would be the import of two-wheeler tyres in India as of now? I think it had also gone up last year.

Anant Goenka: I will not be able to give you a number but yes, there has been a fair amount of import of two-wheeler tyres.

Ashutosh Tiwari: But is it due to price differential or it because there was shortage of tyres in the market?

Anant Goenka: No, in fact generally Chinese tyres has been going all over the place in all categories and to that extent even two-wheeler tyres had made its foray into India.

Moderator: Thank you. The next question is from the line of Sachin Kasera from Lucky Investments. Please go ahead.

Sachin Kasera: First question is regarding this two-wheeler tyres. You mentioned that you ended the year with around (+10) lakhs a month and you started with around 8.5 and that you are hitting some 2 - 2.5 lakhs through debottlenecking. So just for our clarity purpose, can you just give us some ballpark sense as to what is the type of extra volume growth that you can have in two-wheeler because you have been growing more like 30%-35% in this segment. What is the maximum volume growth you can have in FY2016 in two-wheeler in terms of the production?

Anant Goenka: I would say about clearly at least 20% minimum.

Sachin Kasera: 20% and in terms of the passenger car, if I heard it right you said at the Halol plant is currently at 3 lakhs and the capacity expansion will take it to 8 lakhs sir?

Anant Goenka: Yes.

Sachin Kasera: And this current 3 lakhs is at full capacity or the existing one also has some scope for improvement?

Anant Goenka: The existing one will have scope of about 7%-8%. So 3 lakhs is the capacity. We would be at about between 250 and 280 type somewhere around that range. So that can grow by 10% now and then you will have the further expansion which will kick in from quarter 2.

Sachin Kasera: This would have also progressively improved over the four quarters. So we may started a little lower from where we are on the Halol passenger also and be at the level at which we are today?

Anant Goenka: A little bit.

Sachin Kasera: So it is fair to assume that if demand is there in two-wheeler and passenger car both we should be able to do around 20% volume growth this year also?

Anant Goenka: Yes, we are keeping our finger crossed.

Sachin Kasera: Second question is regarding we had taken an approval to form a 100% subsidiary and we were looking to do something on the specialty tyre side. Can you update us what is the progress on that front?

Anant Goenka: As of now it is still at an early exploratory phase. We have not yet taken any final decision. So it is still we are exploring. Yes, we did create a subsidiary and that is done but we are still at a stage where we are further evaluating the market, understanding demand-supplies and looking at things like that.

Sachin Kasera: When can we expect some clarity, maybe end of this year?

Anant Goenka: Yes, certainly before the end of this year.

Sachin Kasera: Sir second question is regarding export, you mentioned that because of multiple 2-3 challenges, currency, Chinese, and another things, the export market is facing pressure. So first of all was there any pressure in terms of we have to take certain price correction and because of which was there any impact on the profitability of the export business in the current financial year?

Anant Goenka: Yes, substantially. So we had to pass on nearly most of the raw material benefit that we have got in the export category. So to that extent there has been substantial price corrections on the export side. What was the other question?

Sachin Kasera: No, so I was asking what has been the price correction that we have taken in and was the EBITDA margin export business this year lower than last year despite raw material prices being lower than last year?

Anant Goenka: I would say it is at least at par if not, it could be a little bit lower also.

Sachin Kasera: What is the thought process of the company strategy because it has now been I think 4-5 quarters since we have started to feel the pain in the export market and from what I understand at one point of time, export was the most profitable segment for us and it still continues to be around 18% of our revenues. So what is the company strategy to overcome the challenge that we facing on the export front?

Anant Goenka: Yes, you are absolutely right. So one is that there is clearly a structural change happening at industry level on the export front and by that I am saying is primarily in the case of bias tyres. So I do not see that resolving. What we have to do going forward is make sure that we are able to sell more and more of our radial tyres whether it is truck tyres or whether it is passenger car and motorcycle tyres, those are the tyres we can start selling to the export market which will resolve sales. So I do not believe there is too much opportunity on efficiency or better selling, etc., that will substantially take up sales. It is more going to be that we need to change our product mix towards more future products like radials.

Sachin Kasera: In that case sir, we again have a problem in the sense already our bias plant which is primarily Bhandup and Nashik are operating at lower capacity utilizations and if we were to change our mix in export more towards radial, so they would again and this primarily because there are old plants and they are in the city locations, they have high fixed costs. So in a way it again increases the problem of high fixed cost that we face in both the plants?

Anant Goenka: So what I am saying is that looking at where we are today, I do not see bias sales going down much further. We are already at quite low levels. In my view that correction should largely happen, now we have to look towards increasing sales in the radial side and a lot of the data that I am sharing of 85% utilization, etc., is coming out of what is the situation today after the exports drop that has happened.

Sachin Kasera: But you mentioned that going forward, we will have to probably increase. Currently sir what is the share of radials in the total export, is it a very small number?

Anant Goenka: It is not a very small number. It would be at least 35% or so, I cannot say exact but it will be at least 30%-35%.

Sachin Kasera: You see that we need to take it to say 60%-70% over the period of 3-4 years to be able?

Anant Goenka: Yes, that shift has to happen. Now the market is also shifting.

Sachin Kasera: Yes sir that is where my query is coming from that if you were to increase the share of radial from 35-70 in exports, the surplus capex that will be left over because the domestic market is also seeing a trend towards utilization. So how do we sell the surplus capacity in the bias?

Anant Goenka: Might be over the next 4-5 years, there will certainly be a rationalization of the two plants. So at that time, you will have to see what do we do with the excess capacity that exist in these plants between the two plants but I would say in the 2 years, maybe there is nothing else that, I do not see anything, any action needed to be taken in 2 years' time. The budgets that are being taken on, that can we do some increase in capacity of making some two-wheeler tyres or industrial tyres or things like that. Those are types of tyres we continue to move towards but it is only very incremental in nature in our older plants in both tyres and things like that.

Sachin Kasera: In case of Bangladesh you mentioned there has been quite a bit of delay and we are still not started the construction of the plant, are you still hopeful of being able to resolve it or we may have to look in terms of evaluating our Bangladesh proposal afresh?

Anant Goenka: No, I would say we are still hopeful. I would give it about may be 3-4 months' time. Yes, I cannot give a commitment that in a months' time or so, it will be resolved but all efforts are on to resolve it.

Sachin Kasera: In Sri Lanka this year, the revenues are a little lower compared to last year, any specific reason for that?

Anant Goenka: So in fact the market itself has been very challenging in terms of growth rate. GDP growth has been low, markets has been very challenged. So largely for that reason and the second is to a certain extent, we also had a little bit of an issue with our two-wheeler suppliers in Sri Lanka. So we outsource some of our two-wheeler capacity within Sri Lanka where there was some issues then we stopped purchase from that two-wheelers supplier. We have now replaced that with our own capacity but nearly from November all the way till March, there was a substantial drop of our two-wheeler sales within Sri Lanka. So that will get resolved with our own capacities coming in.

Sachin Kasera: Couple of balance sheet questions, one the CFO mentioned that approximately around 150 crores of expense that we incurred this year could be of extraordinary nature and may not recur. Is that understanding correct?

Subba Rao There is a guestimate say for example of the salary every year it will not go up by 21%. So this year, it has gone up by 21%. Outsourcing cost, it has gone up by 40% while the volume growth is 25%. It should proportionately go up by the volume increase. Freight has gone up by 20% whereas the volume growth is about 4.5%. There is a structural adjustment of this. Repair again it has gone up by 50%, every year it does not go by 50%. So this is the guestimate, it could be plus or minus some change could be there, so 20 crores but yes, substantially it will not recur. It cannot reach every year 250 crores, 230 crores we will not spend on this kind of items.

Anant Goenka: Just to clarify what we are saying here is that you will not see this kind of inflation going forward but it is not that the expenses that were incurred were one time and therefore we will get reversed or will not happen in FY2016. I would say that out of this possibly 10-15 crores maybe one-time which will not happen again.

Sachin Kasera: Just to follow up on this itself, normally in terms of most internally when we see the conversion arrangements, typically the conversion cost go down with a type of volume increase we see but in our case for example, even with a 25% volume increase, we had to give a 15% higher conversion cost especially when in the last one year, the inflation has been pretty subdued. So is there any formula to which we are linked and that is why we have to give away this type of price increase on the conversion cost?

Anant Goenka: No, there is no real formula. You are absolutely right but because we have to make sure that our vendors were happy, profitable, etc., as well, so we wanted to make sure that they are getting fairly paid as well. So we looked at that adjustment from that perspective as well.

Sachin Kasera: Secondly on the freight, the last year if we see the diesel cost have come down quite a bit and quite a bit of in fact our reporting a reduction in freights, so in that scenario, a 20% increase in freight looks a little on the higher side. So can you just experience what exactly has happened which has transpired into such as steep increase in freight cost for us?

Subba Rao: In the freight, there are 2 elements. There is a fixed cost, there is a variable cost. Variable cost is relating to the diesel. This is approximately about 30%-40% of the overall freight cost. So the freight cost do not proportionately go down in proportion to the diesel price changes. That is one factor. Second we have been selling more and more of two-wheeler tyres. The same way say 10 tyres of two-wheeler would be equally to one tyre of say for example truck tyre but the volume it occupies is, the 10 tyres of two-wheelers, it occupies much larger space. So then you have to incur higher freight cost because of the volume increase, it is not the weight increase. So this is another structural change that has been happening. But these are two reasons.

Sachin Kasera: We have seen the debt-equity improving quite substantially this year, are we also looking at sort of rating upgrade because of which there could be some further improvement on the interest cost front this year?

Subba Rao: In fact the rating has gone by 4 notches over the last 2 years. We are again planning to submit based on the audited balance sheet, we are trying to submit for 1 more revision. Let us see what is going to happen but we are hopeful that even today one of very reputed minister was saying that yours is AA quality balance sheet, not just a simple A+ which we have currently rated it.

Sachin Kasera: How much was the reduction in interest rates for us because of the rating upgrade in the last financial year sir?

Subba Rao: See the banks once they lent whenever you go for a reset they would be very miserly to reduce the rate of interests. RBI has cut 50 basis points and banks have not passed much on this rate cuts. So the banks have been very tardy in passing on the rate cuts but to what we are planning to do is to go for the replacement of the long-term loans where we have paying (+11%) with a bond issuance. So with this what we are exploring, we are just taking the board approval, we are sending it for the shareholders' approval.

Sachin Kasera: How much could be the arbitrage by doing this, that we could probably?

Subba Rao: It could be a little more than a percentage.

Moderator: Thank you. Next question is from the line of Nikhil Deshpande from Sharekhan. Please go ahead.

Nikhil Deshpande: Sir in addition to your 10 lakh capacity, what would be the outsourcing capacity we would be having for two-wheeler tyres?

Anant Goenka: So currently everything we produce is all outsourced. The entire additional capacity coming in so currently as part of debottlenecking and small capacity expansion, about 2 lakhs additional outsource will happen over the course of this year, but the entire Nagpur capacity coming in of about 12 lakhs tyres will be inhouse.

Nikhil Deshpande: So say 2 years down the line, we would be slightly more than 50% inhouse and 50% outsource?

Anant Goenka: That is right.

Nikhil Deshpande: Sir and what would be the industry growth for two-wheeler tyres this year?

Anant Goenka: Industry growth approximately, industry in replacement market or OEMs?

Nikhil Deshpande: Replacement market.

Anant Goenka: Replacement would be at about 10%.

Nikhil Deshpande: So we would have gained substantial market share over there.

Anant Goenka: Yes.

Nikhil Deshpande: What would be our market share in two-wheeler tyres now?

Anant Goenka: We do not have data. So I cannot give you a very clear data. So the data that we have would be I can give you a ballpark estimate of about 25% between scooter and motorcycle?

Nikhil Deshpande: Sir what would be two-wheeler tyres? How would be the split between OEMs and replacement for CEAT specifically?

Anant Goenka: I think it will be about 60% to the replacement and 40% to OEMs.

Nikhil Deshpande: Sir is there any industry representation going on for antidumping duty on Chinese tyres and could you update over there?

Anant Goenka: So it is too early to say antidumping duty has just been removed for, this is for truck right you are talking about?

Nikhil Deshpande: Yes, truck.

Anant Goenka: It just come off in early or middle of February. We are working towards it. I think the industry body is working towards being how we can get or curb damage that has been done to the industry. I think it will take some time though.

Nikhil Deshpande: So there is a review in process or how is it?

Anant Goenka: So we have to put in our request to the government which is in progress.

Moderator: Thank you. Next question is from the line of Sonal Gupta from UBS Securities. Please go ahead.

Sonal Gupta: Sir I just to want you again coming back to this question on industry, can you also give this split in terms of two-wheeler, what is the sort of volume growth have you seen for the full industry and what is the split in terms of industry volumes of replacement move here?

Anant Goenka: Yes, the industry as I said would have grown by approximately 10%.

Sonal Gupta: That would be the replacement market right?

Anant Goenka: Even the OEM would have grown by somewhere between 5.

Sonal Gupta: OEMs is 8%.Yes, right so.

Anant Goenka: If you look at, the first half has better growth. Second half, the OEM has shown nearly negative growth or key OEMs have shown 0 to negative growth kind of levels. So that is one. In terms of overall industry breakup, it would be approximately 50:50 between OEM and replacement.

Sonal Gupta: Sir what would be your market share on the passenger vehicles, UV plus car together?

Anant Goenka: It could be somewhere around approximately 10%.

Sonal Gupta: This is just replacement or this is overall?

Anant Goenka: This would be replacement.

Sonal Gupta: Do you have any OE share as well?

Anant Goenka: OE would be a little bit lower somewhere around 6%-8% kind of levels.

Sonal Gupta: And again would you have a split on for the passenger vehicles into OE and replacement?

Anant Goenka: I think passenger would be slightly higher towards replacement. So it would be something like 60% or so with replacement, 40% OEM.

Sonal Gupta: Sir going forward what is the outlook on exports given that challenges that you mentioned, do you still see a decline going forward or you think that things will stabilize at current levels?

Anant Goenka: In my view, I think exports could see a little bit of further decline going forward in the shorter term. Long term, I think once our capacities are up, then we should see some positivity in terms of overall exports. So up means we are talking about with Halol coming in and with two-wheeler coming in, so I do not see an increase coming in from increased bias sales. You can see minor increase but not much more so that whatever we have can go up by 7%-8% with bias but really looking at a longer term, you need to grow 10% at least say year-on-year and that growth will come into radial tyres which we have to wait for our capacities to come in.

Sonal Gupta: Sir you mentioned in the beginning some markets like Nigeria and some other markets which saw currency depreciation, which are the major markets for you other than say the Sri Lanka and stuff?

Anant Goenka: Brazil, UAE, Indonesia, and Nigeria. These will be the key markets.

Moderator: Thank you. Next question is from the line of Mayur Milak from Anand Rathi. Please go ahead.

Mayur Milak: Just a quick take you mentioned that you have to pass on most of the benefit of the rubber to the export market and typically you did mention that some of it also goes to the domestic OEs. So what I am trying to just understand is going forward if you are actually expecting the rubber prices to soften further, so you expect that further despite making much margins this you will have to pass it on to the OEs?

Anant Goenka Yes, so in the OEs with at least about say 60%-70% of our OE customers, we have formula-based pricing. So to that extent that has always got passed on and will continue to get passed on and if there is a raw material price increase, you can get it and on exports, it is more the competitive nature which we have to keep evaluating and right now it is extremely competitive and therefore that price also gets passed on. So Chinese for example, are selling tyres below our raw material price. So that extent it is very difficult to compete.

Mayur Milak: Sir typically do you import natural rubber? What would be that content?

Anant Goenka We would be importing nearly 65%-70% of natural rubber today.

Mayur Milak: Alright so for your total consumption, you import around 70%?

Anant Goenka It really depends. I depends on the market, pricing, quality, availability, all of those things. So it could vary from I would say even 20% import up to 70% import.

Mayur Milak: So for FY2015, this number has been up to as high as 70%?

Anant Goenka No, I would not say that. I would say that it has varied. I would say depending on the tapping season, etc., it would really vary but it would be somewhere maybe as high as even 50%-60% in certain months.

Moderator: Next question is from the line of Disha Seth from Anvil. Please go ahead.

Disha Seth: Sir just wanted to know that in two-wheeler market shares, we would be second to MRF. So MRF would be approximately how much?

Anant Goenka: I do not have the exact information but I mean surely over 30%.

Disha Seth: Then third would be TVS in replacement

Anant Goenka: I think so yes.

Disha Seth: I just wanted to see the difference between the first and the second and sir all the two-wheeler gaining market share is because of Falcon capacity going close down because market is just growing by the 10% and we all are growing by?

Anant Goenka: In part yes.

Disha Seth: Yes and sir going forward on margins, do we expect an improvement because raw material is almost stable or because of ad and everything we would.

Anant Goenka: No, I think some benefit of raw materials still have to trickle in because a lot of the material that we use are oil-based product and that by the time oil comes down, then that get passed on to carbon black or tyre cord players and then that or synthetic rubber, that impact will then come in to us going forward. So I think there is still some scope of raw material price reduction in quarter 1.

Disha Seth: Sir for sales growth for the coming two years, what would be the revenue target like growth target?

Anant Goenka: We do not have any target.

Disha Seth: Like if we have grown around 5% so it would approximately grow like around 10% if the market.

Anant Goenka: We are more optimistic now about the market. A lot of good things are happening at an economic level, we are seeing good things on MHCV demand. So overall we are more optimistic than we were. In principal, we do not give any guidance.

Moderator: Thank you. Next question is from the line of Nikhil Deshpande from Sharekhan. Please go ahead.

Nikhil Deshpande: Would be our truck bias capacity across plants?

Anant Goenka Total bias capacity across plants?

Nikhil Deshpande: Yes.

Anant Goenka: Including outsourcing, it would be about 600 tonnes per day approximately.

Nikhil Deshpande: What would be inhouse?

Anant Goenka: So this includes outsource. If you look at only inhouse, it would be about 450 tonnes per day.

Nikhil Deshpande: Sir and if given a scenario with some extra investment, is it possible to convert this to a two-wheeler or something like that?

Anant Goenka: It is a possibility, yes.

Subba Rao: On expenses front, I would like to stand corrected on 150 crores figure that I have gave earlier. It is a kind of very rough estimate if not this expense, something else would come in. I did not mean that so 150 crores would be the saving out of this in the following year.

Moderator: Thank you sir. The next question is from the line of Ashutosh Tiwari from Equirus. Please go ahead.

Ashutosh Tiwari: Yes sir if you want to convert our bias capacity into radial capacity or specialty tyres, what kind of capex could be there in that?

Anant Goenka: If you want to convert bias to?

Ashutosh Tiwari: Radial or say speciality tyres?

Anant Goenka: So it depends. So if you are converting to a radial, it would be nearly like a fresh investment. A very large investment of possibly 4-5 crores per tonne whereas normal radial investment maybe 6 crores per tonne type thing. For specialty again depends whether you are doing cross ply, bias, and what are the sizes of presses that you currently have? You need to change presses. It will be a little lower than the radial but it depends on what is the inherent capacity that is there right now.

Ashutosh Tiwari: Any ballpark number, how much it could be if say if you want to convert it into bias specialty tyres only for mining tyres.

Anant Goenka: Bias specialty tyres or radial specialty tyres?

Ashutosh Tiwari: Bias.

Anant Goenka: Bias would be possibly around 3-4 crores per tonne.

Ashutosh Tiwari: Sir out of our current sales, how much would be coming from sales in the mining tyres in India?

Anant Goenka: Total off-highway tyres would be about maybe 6%-7% of our sales.

Ashutosh Tiwari: 6%-7%?

Anant Goenka: Yes, not mining I am talking about all off-highway tyres?

Ashutosh Tiwari: How much of this would be related to exports out of 6%-7%?

Anant Goenka: About 50%.

Ashutosh Tiwari: Do you think that because of the revival in mining segment in India, you could sell more tyres over there. Do you see that there could be one driver for OHT tyres per se.

Anant Goenka: Yes I think that will be a certainly a good opportunity. We have seen a negative growth in off-highway tyres in the year gone by. So we do have the capacity that is left and mainly it has gone down because OEMs have shown much lower growth and replacement is also looking like a challenge, has been looking. So I think with this revival or with the change coming in the next 6 months to 1 year time, we are optimistic about this.

Ashutosh Tiwari: And the exports, like export essentially how much would be bias and how much would be radial. You said 60% is roughly bias?

Anant Goenka: Yes.

Ashutosh Tiwari: Is it you are seeing pressure across the geographies that you supply or there are certain geographies where it is more.

Anant Goenka: So we are finding more pressure on category like bias category.

Ashutosh Tiwari: No sir, I mean to say that when you are selling bias tyres, it would be different geography like South East Asia and other market as well, so are you seeing…?

Anant Goenka: China is there everywhere.

Ashutosh Tiwari: Roughly how would the pricing of the Chinese radial tyres would be different from your bias tyres. So that be even lower than bias tyres you supply or it will be in the same range?

Anant Goenka: As I said China is lower than our raw materials. So it does not matter whether that is a cross ply or radial tyre?

Moderator: Thank you. Ladies and gentlemen that was the last question. I now hand the conference over to the management for their closing comments.

Anant Goenka: So thank you very much for your interest in the call and look forward to touching base once again in next quarter.

Amit Mishra: Thank you sir. It was a pleasure to have you on the call and thank you all participants, thank you.

Moderator: Thank you very much members of the management. Ladies and gentlemen on behalf of Macquarie Capital that concludes this conference call. Thank you for joining us and you may now disconnect your lines.