"Mahindra CIE Automotive Limited Q1FY16 Results Conference Call"

July 28, 2015

MANAGEMENT:	**MR. HEMANT LUTHRA – CHAIRMAN, MAHINDRA CIE AUTOMOTIVE LIMITED** **MR. K. RAMASWAMI – MANAGING DIRECTOR, MAHINDRA CIE AUTOMOTIVE LIMITED** **MR. SANJAY JOGLEKAR – CHIEF FINANCIAL OFFICER, MAHINDRA CIE AUTOMOTIVE LIMITED** **MR. VIKAS SINHA – VICE PRESIDENT, STRATEGY, MAHINDRA CIE AUTOMOTIVE LIMITED** **MR. PEDRO ECHEGARAY – EXECUTIVE DIRECTOR, MAHINDRA CIE AUTOMOTIVE LIMITED** **MR. K JAYAPRAKASH – CFO - FORGINGS DIVISION, MAHINDRA CIE AUTOMOTIVE LIMITED**
MODERATOR:	**MR. NISHANT VASS – EQUITY RESEARCH ANALYST - ICICI SECURITIES LTD**

Moderator: Ladies and Gentlemen, Good Day and Welcome to the Mahindra CIE Automotive Q1FY16 Results Conference Call hosted by ICICI Securities. 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 the conference call, please signal an operator by pressing '*' then '0' on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Nishant Vass. Thank you and over to you, sir.

Nishant Vass: Hi! Good Afternoon, Everyone. Thanks for joining us for the Mahindra CIE Automotive Conference Call. From the management side, we are represented by Mr. Hemant Luthra – Chairman, Mahindra CIE Automotive; Mr. K. Ramaswami – Managing Director, Mahindra CIE Automotive; Mr. Pedro Echegaray – Executive Director, Mahindra CIE Automotive; Mr. Sanjay Joglekar – CFO, Mahindra CIE Automotive; and Mr. Vikas Sinha – Vice President, Strategy, Mahindra CIE Automotive. Now, I would like to hand over the call to the management for their initial remarks and then we can have the Q&A. Thank you.

Hemant Luthra: This is Hemant Luthra – Chairman of the company. I believe many of you have to go to another call, so I am not going to take too much time. We are quite pleased with the fact that despite the slowdown which is affecting the top line in India, the consolidated results are still looking much better, and in fact, that is an improvement in normalized EBITDA (without one time costs) on a consolidated basis from 10.1% to 11% which is a huge nice jump, and the same thing is reflected at the EBIT level. The strategy of putting Europe in place is working nicely. The strategy of keeping the costs in India down till the market starts to recover is working even better for which KR and his team and Romesh and Pedro must take credit and even in places like MetalCastello which we were discussing last time is how we are turning Italy around and how we are turning Germany around, there is a significant improvement. So, I am going to turn it over to you for questions and obviously, we may not be able to give you any forecast or what is happening in the future, you can see the trend, Q1F16 is better than Q1F15 and Quarter-on-Quarter also we are doing much better. Back to you people for questions.

Moderator: Thank you. Ladies and Gentlemen, we will now begin the Question-and-Answer Session. The first question is from the line of Akshay Saxena from Credit Suisse. Please go ahead.

Akshay Saxena: My first question is on the India business. In the first slide of your presentation, you have alluded to supply starting to new model launches to the customers. Can you elaborate which have been the key models? I guess one of them will be the new LCV by Mahindra. What are the other ones? Also, you have mentioned new orders being finalized in Castings, etc., Can you talk about these order wins? Are we seeing any traction from some new customers whom we were not serving earlier?

Sanjay Joglekar: Maybe we can request KR and thereafter to Pedro Echegaray to talk about this.

K Ramaswami: We are talking of several businesses and Mahindra CIE now as opposed to one or two businesses, now we are talking of Forgings, Stampings, Foundry and Composites. If you look at major customers like Tata Motors and Mahindra, whatever they are planning to introduce there are several models which Mahindra is planning to introduce, Tata Motors have already introduced a few models. In most of these introductions, we have been identified as source for supply, be it Stamping, be it Casting, be it Forgings. In the case of Casting, we are also looking at one or two major customers in the Turbocharger Housing segment to be more specific where we are very close to bagging orders.

Akshay Saxena: So, these will be new customers basically?

Hemant Luthra: One will be new customer, Mahindra, Tata Motors are already existing customers. So it will be existing customers - new products, and existing products - new customers.

Akshay Saxena: If I also look at your standalone business there was a gross margin expansion of over 250 basis points on a quarter-on-quarter basis. That is from 4Q to 1Q. So, how much of this is on the account of commodity benefit? Is it the case that you have to pass on the commodity price movements to OEMs with a lag and hence there will be some bit of reversals in the next quarter as you pass on the recent fall in commodities steel, etc.,?

Hemant Luthra: Again, it varies from business-to-business. In case of Casting, there could be a quarterly lag but it may not be true for Forging and other businesses. But, it is kind of everything mixed in the total results. So, if you are talking about lag, there may not be a significant lag in terms of total, but with respect to Casting, there would be a lag because it is adjusted on a quarter-to-quarter basis.

Akshay Saxena: So, what was the reason for the large gross margin expansion on quarter-to-quarter…?

Sanjay Joglekar: Different people define gross margin differently, so…

Akshay Saxena: Basically, raw materials to sales have come down; in Q4 was 54%, this quarter was 51.5%.

Sanjay Joglekar: Are you doing it after deducting inventory change?

Akshay Saxena: Yes, from fourth quarter to first quarter.

Sanjay Joglekar: JP, are you there?

K Jayaprakash: There is a reduction in raw material prices and like KR explained there would be a lag of a quarter, therefore, there is some benefit flowing in, in this quarter.

Akshay Saxena: And this should sustain as long as commodities are at the current prices, this level of gross margins should sustain, is that correct?

Sanjay Joglekar: At some point of time, Sanjay here, it will be passed on. Raw material cost, you cannot keep on having a continuous benefit in the pricing from customers.

Hemant Luthra: The skill is to see how long you can delay it.

Akshay Saxena: Also, moving on to the Europe. So, can you give some color on the truck market outlook? Today only I see that numbers that June were released and there was a 32% growth in every truck for the month with volume growth at 20% for the full quarter. So are you seeing signs of the same in your business with improving order book?

Pedro Echegaray: The situation in Europe continues improving slowly. I do not think we can assume this rate will continue in the future. Definitely, it will continue growing for both passenger cars and commercial vehicles but definitely not at this rate, our expectations is that steady growth will continue in both markets.

Vikas Sinha: To the first part of your question, what are those photographs that we have put up, this is for the new model launch since most of them have Stamping parts, there is a new model launch for Mahindra, so you know that.

Moderator: Thank you. The next question is from the line of Raghu Nandan from Quant Capital. Please go ahead.

Raghu Nandan: On the cost side, there was a cost item of €5-6 million which had to be taken due to severance package for workers in Jeco plant. Has that been factored or would subsequent quarter see an improvement in margins?

Sanjay Joglekar: As you know, Jeco, we had factored about €3 billion in the quarter Jan to March. Now, at present the discussions are going on. There will be of course additional hit but what has been decided is that when we come very close to the conclusion then in that quarter we will take that hit and of course we will disclose it like we did it in March.

Raghu Nandan: Sir, on the quarterly consolidated financials, the euro translation for the current quarter was at 72 leading to translation losses versus last year. Can you give us a broad sense of what has been the volume growth and what has been the fall in realizations for European business if possible?

Sanjay Joglekar: If you see like Jan-to-March quarter, the translation was about 78 and now it is 70, so it is about 10% less. If you see the difference in the number in volume is not very large. And Vikas Sinha…?

Vikas Sinha: So, if you take consolidated minus subsidiary for the last quarter Q4F15 and consolidated minus subsidiary for this quarter Q1F16 and then you take 77.31 and 70.2 you will see that in euro terms we have grown from approximately €124 to €131 million.

Raghu Nandan: You had said that cross-selling and those opportunities are continuous process. So if you can give an update as to like how you are looking at that particular opportunity? Also, if you can throw some light broadly on the demand scenario on new products, new customers, both for India business and global business and generally how do you see that directionally for both the businesses, that could be helpful sir? You already alluded to a part of it in the initial answer. If you can throw some more to elaborate it would be helpful sir.

Vikas Sinha: In terms of new customers which we have talked about in the past, we are of course in talks with a lot of them, some of them have been mentioned on the first page of the presentation. So that process is ongoing. Pedro Echegaray, if you can hear us, in terms of the new customers that we have talked about, non-M&M, non-Tata in India, is there anything further that we should add?

Pedro Echegaray: I cannot give you names or a specific projects, but yes, we have made a significant progress with two North American OEMs in India and we expect in the near future to be able to confirm this for the new customers.

Vikas Sinha: That was as far as new customers is concerned. New products, KR has already talked about in response to the Akshay's question that we are well represented on the new models of Tata Motors and Mahindra and also for turbocharger housings we are developing a new customer. So, along with these two new North American OEMs, this is really what is happening of the new products and new customer side.

Pedro Echegaray: What I would like to complement here even though if he is not a new customer but I think it is a significant achievement for us, it is the high content per vehicle that the new Mahindra Jeeto vehicle has which most of the body parts are standby Mahindra CIE now a new Zaheerabad plant as well as all the gears from the gear box has to ply it 100% from Mahindra CIE, and the latest news is that their vehicle is being a market success. So we expect also revenue growth in the next quarter because of the ramp up of these production.

Vikas Sinha: Since Pedro Echegaray has mentioned it, if you look at the photograph on the first page of our presentation, it gives you the cabin body and the cargo body which is made by our Stampings division.

Moderator: Thank you. The next question is from the line of Priya Ranjan from Systematix Shares. Please go ahead.

Priya Ranjan: Just on the Casting crankshafts are for GM or export?

Vikas Sinha: We will not confirm that.

Priya Ranjan: In terms of outlook for domestic market, since Mahindra will be launching a couple of new models in their UV division and the tractors is now looking at bottoming out, so, can we see some kind of meaningful growth from Q2 or Q3 onwards?

Hemant Luthra: I think you should go with whatever Pawan Goenka has been saying and will say at Mahindra AGM, Meetings and post results conference call in a couple of days, I think publicly he has made many statements, saying that we are optimistic about Q3 and Q4, and with the monsoon coming in your guess is as good as mine. The only thing that you should remember is that there are two things that are going on – one is increased share of wallet from Mahindra without becoming more dependent on Mahindra than we already are. So therefore, what Pedro said about acquiring new customers is important but also getting a greater share of wallet from Mahindra is also important which means basically we have to grow the business quite substantially because the philosophy is that we have to bring down our dependents on Mahindra and Tata in any case. But if the volumes go up, we want to reduce our percentage of our business with them, we do not want to reduce our absolute volume of business with them.

Sanjay Joglekar: So, we will diversify and increase more customers.

Hemant Luthra: Also, I think what needs to be recognized is that this is not a commodity business, in the sense that if a customer requires you to develop a new part, by the time you do your approval and the PPAP approvals and so on, it takes a while before it settles in and therefore the process of how much should be made in India, how much should be made in Europe, how much should be made in Spain, it is an ongoing process and results appear in 6-8 months after you start the process. So, just hang in there, be patient, but the logic is that there is only one Forging company worldwide as far as CIE is concerned and that is Mahindra CIE. So, there will not be any conflict of interest and moving stuff around to maximize profitability.

Vikas Sinha: To your question on Mahindra & Mahindra and Tata Motors growth rate, we are talking about all the numbers put together except Two-Wheelers i.e. Tractors, UVs, LCVs, Cars etc. if you look at Q3, they had declined by 13.6%, if you look at Q4, they have declined by 7.5%, if you look at Q1 of this financial year they have declined by 2%. So you are seeing that there is a gradual improvement in the production at our main customers and we do hope and we believe that this is going to get only better.

Priya Ranjan: And then, I guess you were doing some kind of Automation in Domestic Forging as well for which the one line automation was supposed to come in FY16. So, is it on track or it has already started in the numbers?

K Ramaswami: We are planning to automate one line. It is partly activated already but for the line to get in full swing, we are having active discussions with various people and taken some actions in some areas. So it is being done in phases and it is on stream.

Priya Ranjan: Recent wins since last quarter presentation, Daimler, Linamar, etc., so when can we start seeing those numbers…?

K Ramaswami: In terms of Daimler Trucks, we already have some numbers incorporated in the actual numbers. Linamar… as and when the volume keeps going up, they just put up a plant and they started pie and it should kind of ramp up in next quarter and the quarter afterwards.

Priya Ranjan: On the Jeco, when can we expect the conclusion of the final settlement, etc.,?

Sanjay Joglekar: What we had initially estimated was by end of September, so maybe end of September, October, we will know.

Moderator: Thank you. The next question is from the line of Nalin Shah from NVS Brokerage. Please go ahead.

Nalin Shah: I have two questions: One is that as it appears from the standalone versus the consolidated figures, that is more or less Indian market to overseas included, if it is in 30:70 kind of a ratio, will it remain in the similar fashion for the times to come or gradually even the local domestic business also can grow and the mix can change? Second question is since there are too many different companies, too many different facilities, product lines, can we have some idea about what is the kind of the capacity utilization at which the entire company is operating or other words, at a full capacity what is the kind of top line one can expect from this company?

Hemant Luthra: Let me just give you a quick answer to the first part and then ask Sanjay and Pedro Echegaray to fill in a little bit more detail. No, it is not the intent of us to have the Indian operation at this level. The intent is that we have been caught in a situation where the market has slowed down, so we are cutting cost. And as soon as the market starts to come back, the benefit of those costs that KR and Pedro Echegaray have put into place will leverage the bottom line quite significantly. Second thing I think I mentioned to you on the call the last time that the strategy is that we have a presence in low cost Latin America, we have a presence in parts of Europe, that are low costs which includes Spain, Lithuania and yes of course we have Germany, but Germany is giving us the technology and access to Daimler. We now have a presence in low cost India and there is a small presence in Russia, there is a small presence in China and we are looking at growth opportunities for Asia. I am not letting any secrets out of the bag, it is on the CIE website which you are more than welcome to visit, is that CIE expects to spend something like €250 million over the next couple of years for allocating to Mahindra CIE growth in organic and inorganic ways. So you will see a greater presence moving into Asia. As far as the top line is concerned, I would not use the word 'too many plants' I would say that there are many plants and that is an advantage because these plants that are spread all over the world, is useful because it gives you flexibility of being near the customer of having the overhead of 5,000 people in one plant. So, I would say that it is nicely spread all over. To go plant-by-plant might be difficult but I think if your question is related to CAPEX, I think there is a headroom all over the company for maybe about 25% growth without having to incur significant CAPEX.

Nalin Shah: So overall company without significant CAPEX another 25% top line can grow, which is currently at on a consolidated basis going to be… if my estimate is correct around Rs.5500 crores?

Hemant Luthra: I have to qualify this because the way you qualify this is that if we have Forgings capacity, we may not need to increase Forgings capacity, but if we want to increase margins and we want to increase our machining capacity, there will be pockets. So I do not think it is fair to use the number.

Moderator: Thank you. The next question is from the line of Mahesh Bendre from Way2Wealth Securities. Please go ahead.

Mahesh Bendre: On a YoY basis, in the last quarter, European cars and commercial vehicles sales have grown anywhere between 7% to 9% but our sales have declined by 6%. Is it possible to share the reason for this?

Vikas Sinha: Yes, you are right, there has been a decline on quarter-on-quarter but please do not look at it quarter-on-quarter, simply because there was some inventory correction that has happened. So, if you look at from H1 calendar year 2014 to H1 2015 you will see that we have grown anywhere 6% to 7% and the market has also grown around 8% on a H1 to H1 basis. Unfortunately, our growth has got divided; in Q4F16 we grew by 23%, while now we have declined by 6%. So, if you take an overall thing in that fashion, you will get that we are very much close to the market. There has been an inventory correction essentially which is causing this dichotomy.

Hemant Luthra: Also, not to get on to specific because it is not the policy to declare the thing about specific plants, but just like I was saying about MetalCastello, the turnover has been quite special because we have not just made it a gear company, we are now making a machining company. You may actually have a conscious policy of saying "I will cut out those customers that do not give me the margin that I need" And even if I mean that means that I will reduce the top line. As long as the bottom line on the residual customers in absolute terms and percentage terms certainly is greater than the bottom line that was there before, it is a conscious policy.

Mahesh Bendre: Sir, going forward, is it reasonable to assume that we will be able to grow along with the market in Europe territory?

Hemant Luthra: I would be very disappointed if between CIE and Mahindra and all other good stuff that we are doing all across the world we should not be able to grow the market, our intention is obviously always be to beat the market and that is how the team stock options are measured, how much are they beating the market.

Mahesh Bendre: In Presentation, we have mentioned about Mahindra Forgings Europe that the Phase-I action for turnaround has been completed and Phase-II action on optimizing the products line has begun. So what actually we are planning to do and when do you think these efforts are going to get reflected in the financials of our company?

Sanjay Joglekar: Sanjay here. Phase-1 was mainly focused on the internal operational improvement. By and large completed, but ongoing it has not come to an end. And about Phase-II, what we talked about the examination plant-by-plant about the product margins, etc., customer margins cost, and the closure of Jeco was announced in February by transferring the production of plant at

Jeco to other plants within Mahindra Forgings Germany. Now likewise, we will be analyzing the plant-by-plant, means at the moment we are not really envisaging the closure of any plant, but if anything comes up eventually we will let you know. Secondly, the outsourcing activity was also a part of Phase-II and outsourcing more of a low technology, operations or even machining, that has started but maybe it could take another probably six months' time to materialize the full effects of that.

Moderator: Thank you. The next question is from the line of Hitesh Goel from Kotak Securities. Please go ahead.

Hitesh Goel: Sir, I just wanted to dwell more upon the standalone margins. You said the gross margin mostly improvement has come through from the raw material benefit, but you also said that in coming quarters you could see passing on these benefits to the customer. Can you please allude on this a little more and give us a sense of how do the margins improve going forward if revenue growth could be pretty significant with new products coming in?

Hemant Luthra: Before I ask KR to jump in, I just want to qualify. There is no automatic passing on of benefits of raw materials to customers. Their purchasing department and our marketing department are in a constant battle. There are some products like Stamping, where you have a formula which says that there is a conversion cost and therefore we will give you certain yields and therefore if your raw material cost falls and therefore the top line might fall, but I do not think it affects the margin. There are other products in which if the customer does not give and ask the benefit of rising electricity prices, we do not necessarily have to give him the benefit of fall in commodity prices. So, it is not as if there is a handout that is waiting to be dished out to the customers. And with that qualification, I let KR answer the question that you have asked.

K Ramaswami: Let me explain the impact or what we need to pass back to the customers…I think this question is raised time and again. If you look at the last six months, there has been impact not only on raw material while there is a softening of material prices, there have been several increases, for example, the power cost has significantly gone up. So we go back to the customers and talk about the impacts that we have had to incur against the benefit that we had in raw materials, and with some customers we are successful, and with some customers we are still negotiating and with some customers we are not. So, it is a combination of everything. While there is a system of automatically indexing on price, you cannot do it for ever, as Sanjay was explaining we need to pass this back at some point in time. Now, going forward, I think we are in a stage while our revenues have not increased in the last quarter, mainly because of market condition, we have done a lot of home work to make sure that our margins are improving despite the various cost escalations that are taking place. What it means is that we have set ourselves a platform where if there is a growth and that growth will come from whatever new businesses that we are looking at and also more importantly, on the conditions of market in India and if it starts growing, there would be a significant improvement in margins, but I cannot say how much will be the growth and so I cannot predict any of these numbers but only say that we are sitting in a platform of fairly efficient cost controls and so increase in revenues would probably result in increase in margins as well.

Hitesh Goel: What would be the fixed cost to sales in your standalone business broadly?

K Ramaswami: I will ask JP to…

K Jayaprakash: Our fixed cost all put across, we would be around 15%.

Sanjay Joglekar: JP, are you talking about fixed cost including depreciation?

K Jayaprakash: Yes, staff cost to sales is 12%, so that is purely fixed, in other expenses there will be fixed plus variable.

Sanjay Joglekar: JP, do you readily know this breakup between other expenses fixed to variable? You can tell him flat.

Hitesh Goel: I will take it that offline. My second question is on the European operations year-on-year. In Europe, can you please tell me what is the growth in the Euro terms and revenues in this quarter?

Vikas Sinha: As the previous question talked about in Q1F16 there is a drop in euro terms because Q1F16 to Q1F15 is at the same euro rate; so that was 131 in Q1F16 to about 139 in Q1F15 in million euro terms. But again in response to the earlier question, we had pointed out that it is best to look at H1 of this calendar year to the H1 of the previous calendar year and then you will see the same growth is in line with market growth.

Hitesh Goel: So basically the top line has dropped, even from fourth quarter of FY15 to 1QF16 but EBITDA has gone up.

Sanjay Joglekar: EBITDA has gone up into subsidiaries year-on-year, just it is MetalCastello the MFE and of course there is a marginal improvement in CIE Forgings; CIE Forgings already at a higher margins, so improvement is marginal there.

Hemant Luthra: Just in order to pass on to the question, if you are running at an EBITDA which is north of 15%, I am not going to give you specific numbers when you talk about marginal improvement and you are talking it in Europe, that margin improvement also take some serious effort to happen.

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

Aditya Sundaram: If you could help me to my first question could you please provide me the saleable tonnage that you all have done on an entity basis for FY15 and maybe Q1FY16?

Sanjay Joglekar: It is a really very difficult to do it on the basis of tonnage because all products are not measures in tonnage terms.

Aditya Sundaram: Maybe the Forgings business then at least Europe if you can give me some clarity on that?

Sanjay Joglekar: I think we by and large talk about the capacities also in terms of revenue.

Vikas Sinha: This is something difficult for us to answer simply because of the wide variety of product mix that we have in Europe especially. In Europe, we have approximately 300 product categories. So it would be very difficult to correlate revenue figures and tonnage figures. That is the reason why we encourage our analysis in revenue terms and I think Hemant has already pointed out that there could be an upside of 25% overall in revenue terms and that is more or less is applicable in all portions of Mahindra CIE. So that is the way we need to look at it.

Hemant Luthra: The number has not been pulled out of the air. It is at peak around the period just before the Lehman crisis. Now, the issue is if you keep doing the same volume at the same margin which was not optimal at that time or do you sacrifice a little bit of the top line and therefore when I was talking about 25% I think it will be on the basis of a sensible acceptance of orders which give us headroom of 25% as I said earlier over and above the capacity.

Sanjay Joglekar: Just to clarify, if MFE is running at about €250 million in Germany, what Hemant said, 25% is absolutely right, I think in the current situation the capacity could be measured around €300-325 million during the current product mix and the pricing levels.

Aditya Sundaram: Sir, my next question is in terms of the turnaround at our Big Press. Do we see any further headroom there at MFE at the Schoneweiss facility?

Sanjay Joglekar: I already explained, it is not only a question of Big Press because Schoneweiss is just one of the companies and the Big Press what we found is a low hanging fruit because it was performing very badly, there has been a 50% improvement that the number of parts are now 21,000 per month which were earlier 14,000 per month. I would say it is reaching close to its capacity but now all around the plant, since Schoneweiss is in elsewhere the improvements are going on. Big Press is just about 20% of MFE capacity.

Hemant Luthra: We like to keep quiet about this because it is not a great thing to announce. But, those people who did not think that such a turnaround could happen as Sanjay has described, yes, some action has been taken so that their contracts have not been renewed. Therefore, you will find that a change of attitude also helps how the performance is going forward. I am not throwing about the about the fact that some contracts have not been renewed, but they had. It was a necessity to keep the change of attitude consistent all over the company.

Aditya Sundaram: I was going through CIE Automotive Presentation and I do know that in Europe there are very different end user segment, but I did see that Forgings business there recorded a margin of about 17% in EBITDA terms, though I know we are still to reach the 14% target that we have. Do you think this HCV segment could actually be a possibility catering to this particular end-user segment in Europe, do you think we could actually make those margins is there a possibility is all I am asking?

Hemant Luthra: I am also telling you that given KR's skills it is a possibility.

Sanjay Joglekar: In Europe, if we see it additionally, MFE had hit EBITDA margin of 12%, it has never gone to 17% or 16% in the past. So, what we are putting modestly is our first aim is first try hit what was already achieved and then of course the next step is if some other Forging companies in the group are 15-16% why not this but we will address it later. I would not put it on table at the moment.

Aditya Sundaram: My basic question was, is this a possibility for the HCV segment or is it only very specific to the Passenger Vehicle segment where you can make such margins?

Hemant Luthra: I am going to answer it differently. Yesterday, we reviewed internally the results by segment; what is it that is happening in Gears India, what is happening in Machining Europe, what is happening in Forgings Europe. All that I can say is that we are all alpha males who are highly competitive and therefore, I do not think KR is going to accept within that is lower than what Europe can produce. The way MFE is organized, each of the people also looks after specific plant and they all got P&L responsibilities, but what we are trying to do which you must remember is that the whole logic of this merger has been, let us look at the collective profitability of Mahindra CIE and not individual plants. If it means that a particular plant in Germany has to sacrifice a certain volume so that Spain can produce it at a lower cost and therefore increase the overall profitability of Mahindra CIE. That is something that will take priority. A guy is saying that "I am sorry, I am not going to move some parts from here to there because I want to do something." So, the huge advantage that you are seeing here is one forging company, one consolidated results and that is what I wanted to point out that do not just focus on one particular plant because we are all collectively looking at how to maximize the overall profitability.

Moderator: Thank you. The next question is from the line of Gagan Thareja from Comgest India. Please go ahead.

Gagan Thareja: First question pertains to the sales for the quarter in India. You reported 3% drop. Your two major customers overall volume drop is 2% odd. Is it correct to presume that for balance customers your sales drop is higher?

Vikas Sinha: It is more or less in line, there are of course we have a lot of businesses like Magnetics and Composites which really do not cater to our traditional auto customers in Stampings, Gears, Forgings and Castings. This small difference is because of changes on that side.

Gagan Thareja: Because the logical assumption is that apart from these two major customers, the rest of the market size has grown in volumes. So why would then your share of the pie decrease?

Sanjay Joglekar: It could always depend on which product we are supplying to which customer, whatever the schedule in the one quarter. I would not read too much into it, let us see one or two quarters and then we will be able to make out better.

Gagan Thareja: My second question is again pertaining to sales but this is on European business. The European Automotive agency numbers for heavy commercial vehicles 16 tonne trucks for the quarter is fairly high I think 20% YoY as someone pointed out. That is almost 40-45% of your European sales I would presume or probably even more. If that is the case at least in euro sales should your European sales not have actually reported a reasonable growth because you had a cushion of very good market growth in your largest business?

Vikas Sinha: Let us clarify again; please look at it from H1 to H1 rather than Q1 to Q1.

Gagan Thareja: I think the inventory issue that Vikas Sinha pointed out pertain to the PV segment and not…

Vikas Sinha: No, it is for overall. Frankly, the inventory thing, correction is more for the CV segment rather than for the PV segment, because that is where the variations happen much more. So I would say if you look at the H1 2014 to H1 2015 you will see an approximate market growth of 8% to 9% if you take the overall weighted average of Cars and UVs and for us the market growth is around 7%, of course, you also have to realize in the subsidiary revenues there is a little bit of reporting of MetalCastello and Mahindra Gears India also. That makes a difference. It is not purely European numbers.

Gagan Thareja: The third question is purely a book-keeping question. On Page #9 in the Presentation, EBITDA without one-time gains and losses for consolidated entity is up 4% whereas without one-time gains and losses is up 52%, the entire adjustment obviously is pertaining to depreciation and amortization, if you could just explain that to me?

Sanjay Joglekar: While you are partly right, I would like to qualify that this Q1F15 if you see it is a pro forma, we really did not have this kind of merged numbers which we have worked out and there could be some grouping differences, but yes, overall depreciation and the amortization has reduced, there are a couple of reasons that one, if you may recollect that in the European companies, we had taken a hit by devaluating the fixed assets so that the future depreciation reduces. So, that is one of the major reasons and somewhere the estimation of the life of the asset, all this was done at the merger time. There have been some kind of differences in the non-operating income as well. For this purpose, if you look at the yearly number, that would be much better to make a guess. For some more time to come, this Q1 numbers there will be quarterly adjustments and as I said it is only a pro forma, it may not be exactly right to make judgment at least below EBITDA, to EBITDA we are fairly sure.

Gagan Thareja: My last question again pertains to some accounting doubts. When CIE reports, EBITDA margins tend to be north of 14% but at EBIT level their margins are around 7-7.5 or 8%. When we say that Mahindra CIE's margins have scope for improvement and they can go up to the comparable 14%, 13% with whatever improvement in efficiency and operating leverage and scale is possible, are we therefore looking at a similar EBIT as what CIE reports or are we looking at a like-for-like increase in Mahindra CIE's EBIT which would mean that MCIE's EBIT margin should ideally be higher than that of CIE's when MCIE's EBITDA reaches 14%?

Sanjay Joglekar: It is like this. I cannot state in the way you are stating because it becomes a purely futuristic financial guidance. But, what we have been saying is that with the improvement in the market in India, and the efforts already taken for cost reduction, plus when we expect the new products and new customers to go, our aim is certainly to increase the EBITDA margins and then the Indian EBITDA margins then certainly be probably more than 14-15% over a period of time. It is CIE's stated goal to have EBIT margins of about 9-10% and we were also aiming to reach that level. Currently, I think we are at about 7%.

Gagan Thareja: Lastly, is it possible to give any idea of inventory days and receivable days, tables for the quarter and how do they compare QoQ or YoY?

Sanjay Joglekar: I would not be able to give days and all that but we generally talk about net working capital and net working capital at the standalone level is by and large the same at about 7-8% of the sales and consolidated net working capital…if you might have seen the March results published in SEBI, I think it is almost nil and it continues to be so. That is because of the European company, there are longer payment terms with some suppliers as well as factoring without recourse has been done.

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

Jinesh Gandhi: My question pertains to EBITDA margins. Can you give margins for three main operating businesses – CIE Forgings, Spain, Mahindra Forgings, Europe and India?

Sanjay Joglekar: Indian margins are of course available but rest of the things our request is for you to look at Europe holistically, and at the moment I cannot discuss what is not in the public domain.

Hemant Luthra: Somebody else from the call has picked data from somewhere, I do not know where. So, if it is out there in the public domain, do point it out to us and we will then be able to comment on it but I think you can deduce it from the annual report and we are targeting that all parts of the business get to the highest margin that is possible. I have already qualified by saying that if three plants do 14-15 or 16% whatever your colleague refer to, and one of the plants is less than that, then we have to bring it back up to the best that it is ever achieved, this is our old Mahindra philosophy, that is the first step and I think you can see that there is a headroom as I said for alpha males to compete with each other provided the overall profitability of the system keeps going up.

Jinesh Gandhi: Coming back to standalone business, considering that from coming quarter onwards we will see further benefit of new launches of our key customers, effectively there should be a reasonable top line growth, should that in turn impact our EBITDA margins?

Sanjay Joglekar: It is difficult to make such statements at this stage, let that revenue come. You will see it in results for that, but generally speaking, as Hemant clarified a few times already that whenever we are looking at new business, we are looking at a new business with good margins.

Jinesh Gandhi: In terms of our European business we have seen that margins per se on a quarterly basis are pretty volatile. Is there any seasonality or just to do with the mix?

Sanjay Joglekar: If you are talking about last year when restructuring was going on, then obviously, the numbers will not be comparable. What you can see now is you can take it more or less sustainable and our efforts will be on to improve the same.

Jinesh Gandhi: Would it be fair to say our first phase of restructuring is over and 1Q would be largely reflecting benefits of that?

Sanjay Joglekar: Largely, yes.

Jinesh Gandhi: In terms of the Phase-II restructuring of optimizing product and capacity, what is the timeline which we are looking at, by when can we see benefit of that coming through?

Sanjay Joglekar: It will be an ongoing process because while making operational improvements it is significantly in-house, the other steps also include a lot of outside agencies. As I indicated that some steps which are already taken like Jeco closure or some outsourcing of low technology, machining, would take about 6-months' time, beyond that as and when more and more steps are being taken, we will keep you updated.

Jinesh Gandhi: Are we also including shifting out of the low value added items to other entities like to Spain doing more value-added items that Germany?

Sanjay Joglekar: Again, I will refer to Hemant's statement that the objective of the group is to improve the consolidated results.

Jinesh Gandhi: Sorry, my question was whether it is part of Phase-II, obviously, overall we will be looking at that but in Phase-II…?

Sanjay Joglekar: Exactly. So, in order to improve the consolidated results, if steps are necessary to do such a thing to shift some products from one place to other place, it can be vice-versa, that will be done.

Hemant Luthra: Also, some human psychology here which takes two partners who has got the integration program going so well and whose respective market cap has increased by a figure of 2.5x and 4.5x in less than 2-years. There is a real positive feeling inside the company. But, there are of course human beings**.** So, if you tell some human being in Germany, that in order to improve the overall profitability, you cut 200 people and move those jobs to India, people are not automatons, there are some human being, there are some human emotions involved and so on, and therefore it takes a little bit longer than turning a switch on and off. We have reached a point where everybody has enjoyed the benefit of seeing how the market cap has increased. We have reached the point where we have been able to show them that which are the exporting companies of automotive components from India, how they make the margins, how much margins are in India, how much in Europe, and we have yesterday taken a proposal which hopefully we will get approved from the board and the shareholders about some marginal ESOPs that need to be given to motivate people. People are going to be motivated by taking an ownership of the company. I do not want to jump the gun because the shareholders may shoot this thing down and therefore I do not want to say anymore, but anything that is to be required to be done to motivate people to look at the company holistically including ESOPs is being considered. You will find, yes, there is some little bit of resistance, somewhere it will go away by showing them, dangling the carrot of collective ownership by showing them and dangling the carrot of how much you have beaten the market. So there are many measures that need to be taken when you integrate 14 companies across 4-different countries and we are conscious of that and we are doing it.

Moderator: Thank you. The next question is from the line of Priya Ranjan from Systematix Shares. Please go ahead.

Priya Ranjan: Just one more clarification; I think the residual stake which was there for Mahindra Gears and Transmissions has been transferred to the company, so now it has become a 100% subsidiary of the company. So here on it will be part of the consolidated or will be part of the standalone?

Sanjay Joglekar: It was a part of the consolidated already because it was 77%-owned anyway, but it has not been merged into MCIE. It will continue to be the part of consolidated.

Priya Ranjan: You have also mentioned about the amount that you have paid for that. So, kind of valuation that you have done for that it is around 5x, 6x EV/EBIT or something like that, I do not know.

Sanjay Joglekar: This is always done with an independent valuer.

Hemant Luthra: Just as a strategic input to you, theoretically, there is no restriction in merging the Gears business or practically there is no difference in merging the Gears business with the rest of the company. The issue is that do you incur the cost now or do you incur the cost when some other let us say acquisition takes place at some point in the future as we push our growth plans along and therefore do not have to do the whole process of merging two companies and so on more than once. So last time around we have merged four-five companies in one shot. Next time we make some acquisitions we will do Mahindra Gears and also in the same way.

Priya Ranjan: At this point of time, what will be your net debt?

Sanjay Joglekar: Net debt is almost in the similar range like March was around Rs.1400 crores.

Priya Ranjan: Any thought, Hemant, on merging the residual Forgings business of CIE going forward probably because the net debt-to-EBITDA will most likely be lower than the 2x by FY16?

Hemant Luthra: We have always said CIE has four mantras – one is 15% EBITDA, 10% EBIT, 20% ROC and cash flow being equal to more than 50% of EBITDA. All this is towards maximization of shareholder value and market cap which you have seen happen again and again. Now, let us say the choice comes that we have a CIE company in Brazil and China Forging company. And about the same time, our choice comes to acquire something else and merge it with Mahindra CIE. Priority should be kept to what? The internal company can always be done because it is completely under our control. If we are buying an external company which is a third-party company, should we handicap the balance sheet of Mahindra CIE by adding a little bit more debt and diluting with the number of shares or something by taking on Brazil Forgings, Mexico Forgings. So it is always going to be optimization. If I do not see anything in the horizon, yes, that is a possibility. If I do see something in the horizon which we certainly do, I think we are going to give priority to strengthening the business and we can always bring those companies into the fold, it is part of the understanding with CIE in any case.

Priya Ranjan: In terms of geographically also, since you talked about the acquisitions and all, so it will be more of India-driven or more of Asia-driven?

Hemant Luthra: I have already said that on a call if you were there on the beginning, CIE in its presentation to the investors on I think 25th of April which is available on the net, they said, they are going to allocate €250 million to India and Asia for growth and that is the kind of allocation that they have got. The challenge is for us to find companies which would meet all the criteria of adding value to Mahindra CIE. And yes, Asia-focus, we are already looking at stuff and ideally, it would be somebody who can give us an entry into Japanese OEMs, ideally it would be somebody who will give us some capacity in Thailand, Indonesia, we are not averse to have capacity in Japan, ideally, from our potential partner it would be somebody who might want our capacity in Latin America and if he wants that capacity in Latin America he can take some of our capacity there and give us some capacity in Asia. So, all of that is work in process.

Priya Ranjan: Whatever you have been doing that or CIE has been doing like Plastics, these will be defined within the businesses of the operating units like Gears, Stamping, Forgings, beyond that you are also looking at…?

Hemant Luthra: Why not? Again, there is a strategic answer. They are very strong with Forgings technology, they are very strong in Aluminum, they are strong in Plastics, we will do that. But supposing, our great opportunity comes along which has a great future which is outside of the traditional strengths, but still can leverage of the India growth story of going finally up to 5-6 million cars instead of the couple of million that we do today and CIE technology. I do not think we are restricting ourselves and saying that forever and ever till kingdom come we are going to be doing only Forgings and Castings. In fact, what I want to state on this call…I do not know how many of you listening, but it is a public statement, if you see European competitors and if you see North American competitors which were the giants, whether it was Ford's Visteon or General Motors' Delphi or you see the Renault, Peugeot, French automotive component company Faurecia they were all based in high cost Europe and maybe high cost North America, and yes, they may have been some presence in Asia but not very much. Now, you got a beautiful entity called CIE plus Mahindra CIE alliance which is an low cost Brazil, low cost Mexico, low cost Spain, low cost Lithuania, low cost India, low cost China, low cost some parts of Russia, low cost Poland. Could it be the next global automotive component company? Would we learn from Pawan Goenka as the automotive head? And he says that, Hemant, I want partners who can do R&D, I want partners who can take on my design risk for component because I have to focus on creating the compact SUVs of the world. I have to focus on crash and safety which is mandated by the National Highway Authorities, I have to focus on getting green because I need the fuel efficiency. While I am doing all this, can you design systems for me?" And that is why we see that is a strong company with a strong balance sheet could actually be a partner to an OEM rather than a supplier. A partner in the sense that the Japanese people make their supplier as partner and not a supplier in the American sense of an adversarial relationship. So, I would point you to an excellent article that has been written as a preface, I am not talking about ICICI's estimate of where the value of this company will head, but an excellent article which is a preface of that article says that in the future will the OEMs and auto components guys not be adversarial but would they be partners.

Moderator: Thank you. Ladies and Gentlemen, that was the last question. I would now like to hand the floor over to the management for closing comments.

Hemant Luthra: I have made the closing comments. I will ask Vikas Sinha who is our Strategy Head, Sanjay CFO, KR, who heads the business, to handle the closing comments. I have made mine. Thank you very much.

Sanjay Joglekar: I would only say that thanks to all of you for taking interest and asking questions. It is educative for us also and we will keep on providing the information transparently within the legal framework.

Moderator: Thank you. Ladies and Gentlemen, on behalf of ICICI Securities, that concludes this conference. Thank you for joining us and you may now disconnect your lines.