



“Endurance Technologies Limited Earnings Conference Call”

February 9, 2017



MANAGEMENT: **MR. ANURANG JAIN – MANAGING DIRECTOR**
MR. RAMESH GEHANEY – DIRECTOR & COO
MR. MASSIMO VENUTI-DIRECTOR & CEO
ENDURANCE OVERSEAS
MR. SATRAJIT RAY- DIRECTOR & GROUP CFO
MR. VIKAS MAHESHWARI-HEAD TREASURY &
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HOST: **MR. ASHISH NIGAM – AXIS CAPITAL**



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Moderator: Ladies and gentlemen good day and welcome to The Endurance Technologies Limited Q3 FY17 Earnings Conference Call hosted by Axis Capital Limited. As a reminder, all participants' lines will be in the listen only mode and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing '*' then '0' on your touchtone telephone. Please note that this conference is being recorded. I now hand the conference over to Mr. Ashish Nigam from Axis Capital Limited. Thank you and over to you Sir.

Ashish Nigam: Good morning everyone. This is Ashish Nigam from Axis Capital, welcome to the Q3 FY17 Results Conference call of Endurance Technologies. From the management team, we have with us Mr. Anurang Jain - Managing Director, Mr. Ramesh Gehaney – Director & COO, Mr. Massimo Venuti - Director & CEO Endurance Overseas, Mr. Satrajit Ray - Director & Group CFO and Mr. Vikas Maheshwari - Head of Treasury and Investor Relations. I will now hand over the call to Mr. Jain for his opening remarks post which we can have Q&A. Over to you Anurang.

Anurang Jain: Thank you Ashish. I am Anurang Jain Managing Director of Endurance. Let me first brief you on the two and three-wheeler industry for the first nine months of 2016/17. The two-wheeler industry sales including both domestic and exports grew by 7.33% mainly due to domestic demand which grew by 10.04%, while the exports de-grew by 9.7%. Exports continue to face challenges from Sri Lanka, Africa and South American countries who are the largest importers of 2 & 3 wheelers. Out of the total 2 wheeler industry sales, scooters continue to grow faster than bikes; scooter sales including exports grew by 15.91%, whereas motor cycle sales including exports grew by 2.84%. Three-wheeler sales de-grew by 14.8% mainly due to a sharp decline in exports which de-grew by 34.76% and domestic market grew by only 1.88%. In Europe, the passenger car sales grew by 6.3% in the first nine months of the year, as you all know in our overseas operations in Europe 85% of our sales comes from the passenger car sales. On the Financials, let me briefly touch upon the 3rd quarter first and then for the first nine months' period. As far as the 3rd quarter is concerned, the company's total income including other income, excluding excise duty grew by 2.7% to Rs. 13,276 million and our consolidated Profit after Tax grew by 13.5% to Rs. 743 million. Consolidated EBITDA grew by 7.3% to Rs. 1842 million. Consolidated EBITDA margin grew from 13.3% in the previous year to 13.9% of quarter 3 of 2016-2017. As far as the consolidated PAT margin is concerned, it was 5.6% which grew from 5.1% from quarter 3 of 2015-2016. As far as the first nine months are concerned of this financial year, company's total income, including Other Income, again excluding excise duty grew by 7.7% to Rs. 42,293 million and the consolidated Profit after Tax grew by 12.4% Rs. 2468 million. Consolidated EBITDA grew by 12.1 % to Rs. 5857 million. Consolidated EBITDA margin grew from 13.3% to 13.8% as compared to the first nine months of 2015-2016. Consolidated Profit after Tax margin grew from 5.6% to 5.8% as compared to the first nine



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months of 2015-2016. Aftermarket sales from India Operations grew by 20.5% to Rs. 1544 million. Exports from India grew by 24% to Rs. 1189 million. The exports largely comprise our aftermarket department exports and the export of castings. Detailed financials are available with the stock exchanges and on the Endurance website. I would also like to share certain other points with you. In the first nine months of the current financial year Bajaj Auto share of business on consolidated sales was down at 38% compared to 42% in the previous year, therefore we lowered our dependence on Bajaj Auto. There was sizeable growth of business with Honda two wheelers at 37.4%, Royal Enfield at 28.6% and overseas we grew with Daimler, General Motors and the Fiat Chrysler group. As you know we are setting up for Hero Motor Corp a new plant at Halol in Gujarat for the 100% requirement of front forks and shock absorbers. The land acquisition is still in process and we are planning to start this plant in the last quarter of 2017-2018 but I am happy to inform you that the Halol plant of Hero has already started, this month they are already reached a level of 500 vehicles a day and we have already started supplying to them both the front fork and shock absorbers from our Waluj Plant. Our new machining plant in Germany which is catering to Daimler has started on 10th January 2017. As far as our 26-acre vehicle testing track is concerned, it is progressing well and we should be ready by early 2018, this will help us to strengthen our target of giving first time right products to our clients. I would also like to inform you that we have recently acquired another 2 acres of land attached to these 26 acres which has made it now 28 acres. The recent demonetization has affected our growth in India in the third quarter. Generally, the third quarter of every financial year is the weakest but this has further compounded a problem. We believe that this is only a postponement of demand and not a cancellation. However, it is not possible for us to say when normalcy would return but we are definitely seeing an improvement from January 2017 onwards. This is important for us as you know 80% of our India business is for two wheelers and 12% for three wheelers, so therefore we are quite optimistic that this improvement is taking place. So, with these opening remarks I would like to invite questions from everyone. Thank you.

Moderator: Thank you. Ladies and gentlemen, we will now begin with the question and answer session. The first question is from the line of Puneet Gulati from HSBC. Please go ahead.

Puneet Gulati: If you can give some more color on how you are able to demonstrate such strong growth in the aftermarket sales and also from the exports segment?

Anurang Jain: Yes, see what we have done is, in fact as far as I had mentioned earlier the aftermarket sales have grown by 20.5%. As far as the export countries are concerned, we have opened up new countries of Argentina, Dominican Republic, and El Salvador in this year plus we have increased our sales in countries like Honduras and Peru. We are planning next year to open new countries of Chile and Bolivia also. So, there is a penetration as well as firstly it is an expansion in the existing countries as well as penetration into new countries which have a large amount of two wheeler and three wheeler sales. Secondly as far as India is concerned, we have of course, we

have boost up our aftermarket department I would say the staff, the people and this is a continuous process and they are penetrating tier 3 and tier 4 towns, so that is why you see the growth to be so good. So, we have grown 20.5% in spite of a tough quarter 3 which has also affected the aftermarket but this of course as I said remains a major focus area for us for the company, I mean the aftermarket.

Puneet Gulati: Just a little bit of clarification; the two numbers that you shared, Rs. 1554 million aftermarket sales is only India aftermarket sales right?

Anurang Jain: No it is both, India as well as overseas.

Puneet Gulati: So, there is a kind of overlap in the number that you shared Rs. 1189 million as exports from India?

Anurang Jain: Yes. So when I said Rs. 1189 million, it was both for export of castings as well as for aftermarket, so there is an overlap you are right.

Puneet Gulati: Secondly on your supply for Hero, are there some loss that you could be incurring because you are supplying from Waluj, instead of being next over to Hero and do you see opportunity for a much bigger margin expansion once your plant starts in Q4?

Anurang Jain: See actually the understanding is that the freight is being paid by them because that is an understanding because they also appreciate that we cannot start the plant immediately as the land allocation which has been done by them only, through the concerned agency which is GIDC in Gujarat. So as is in process, they also understand and they are paying for the freight, so there is no loss to us. As far as the plan is concerned, their plan is to reach 2600 vehicles a day by the last quarter of 2017 - 2018 and 6500 vehicles a day by 2018 - 2019. I believe the scooters form about 1900 of this 6500 by 2018 - 2019, so that is a plan for Hero. So right now till our plant comes up in the last quarter of 2017 - 2018, we will be supplying from Waluj and we have the capacity for the same.

Puneet Gulati: Okay and you would be able to ramp up to 6500 with them by FY19 as well?

Anurang Jain: Yes because for a 6500, the new plant will come up in the last quarter of 2017 - 2018 and from this plant we will service the 6500 ultimately.

Puneet Gulati: So in one year ramp up is a realistic possibility?

Anurang Jain: Yes of course, in fact we have done in the past and there is no problem at all because we have a very strong set of suppliers and we have done this in the past, we have done it for HMSI's plant



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which we have in Vithalapur catering to their largest scooter plant in the world making 1.2 million scooters, so we scaled up very fast within 4, 5 months. We scaled -up to almost 4400 scooters a day, so that is no problem for us.

Puneet Gulati: Lastly just on the financial side, if you can give more color on why the tax rate was so low this quarter?

Anurang Jain: So I will request Satrajit Ray, our Director & Group Chief Financial Officer to talk to you on this.

Satrajit Ray: Actually the right way to look at it is, to look at the YTD tax rate nine months but there has been tax gains by way of higher R&D spend this year and last year our CSR spend up to the nine months' period was high, so all these taken into account leads to the kind of ETR that we have.

Puneet Gulati: And is that likely to continue in the fourth quarter as well?

Satrajit Ray: Yes I mean whatever is your YTD ETR, it is normally our tax rate would go anything between 27.5% to 28.5% in that range and the last time also, in last quarter's call I had said that our tax rate would be between 28% and 28.5%.

Puneet Gulati: So that 21% which was in Q3 for Standalone should come back to 27% sometime in Q4?

Satrajit Ray: Yes, that is right, it is higher than that.

Moderator: Thank you. We take the question from the line of Nakul Malakala from Samaira Capital. Please go ahead.

Nakul Malakala: Sir two questions; number one I mean just want to get a sense of regarding ABS, how far have you reached in the last three months that the last call, how is that development progressing from your end? I know you guys were seaming up or partnering up with European companies, so just wanted to gauge the progress in that front?

Management: We have already signed a MoU with one of the companies and we hope to reach an agreement with them latest by March 2017. In the meantime, we have got another proposal from another company which we are also exploring but that is just at the back of the mind but we hope to get this started by March 2017 and immediately get started.

Nakul Malakala: Would you have any knowledge on how your price to the OEM would be versus the Continental or a BOSCH?



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Anurang Jain: No, I mean it will be very difficult to say that because we really do not have the pricing of the competition but in general I can only say that companies like Bosch and Continental definitely enjoy high prices because these are technology leaders in the Auto component field. And our strategy always has been to give a similar product at an economical price, so that is our strategy going forward. I can share this with you.

Nakul Malakala: And one another question, so what you are doing with Germany plant I think that has been commissioned in January of this year, when can we see the ramp up taking place and you know reaching 90% to 100% utilization levels, how much time do you think it will take?

Anurang Jain: I will request Massimo Venuti to speak to you on this.

Massimo Venuti: So we started the new machine plant in Germany in the second week of January with the production of one part we are doing to do for Daimler, which is a new part that we acquired more or less one and half years ago with the total volume of 625,000 per year. A portion of this volume is produced in Italy and a portion in Germany. We will reach the regime of this product in 2017, and this will allow overseas operation to increase the turnover with Daimler. So far, we have increased the total income with Daimler of more or less 30% compared to the previous year.

Moderator: Thank you. Next question is from the line of Aditya Jhavar from Investec Capital. Please go ahead.

Aditya Jhavar: Our German plant has got commissioned in this quarter, so any impact of startup call should we expect on Q4 margins of the European business?

Massimo Venuti: We expect to continue more or less with the same trend of the previous quarter. The new plant will allow businesses overseas to increase the volume for sure in the next year because of the new space available but we have to be able to take new profitable business in order to use in the best way this new space. In this moment, the market in Germany is stable compared to the previous month and so we expect for the next three months the same level of volume of the previous quarter.

Aditya Jhavar: If you can give some outlook on the European business, both Germany and Italian business separately in terms of new order wins or the growth outlook that you are looking for, for the next year?

Massimo Venuti: For the next year, I do not know which will be the future but frankly speaking my opinion the feeling is to maintain a stable market in 2017, as compared to 2016. In the last nine months the European market grew 6.5% and we perform a 10% more compared to the previous year mainly



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due to the new businesses acquired in the last 3 years, 4 years or so; the new car registration in Germany and Italy are performing very well, mainly Italy frankly speaking. In the last nine months Italy grew more or less 13.9% as compared to the previous year and Germany only 4.6%. It is true that the last quarter the increase in Italy was 10.7% and in Germany was more or less stable, (negative for 0.3%) but we are optimistic due to a recent progress in Germany. In Italy, in January the Italian market closed with 10% increase as compared to the previous year and 2% in Germany. So for this reason I think that forecast could be more or less stable for the next month.

Aditya Jhavar: So my next question is for Anurang, if you can share the share of business that Endurance enjoys with Hero and Honda as we speak?

Anurang Jain: See as far as Honda is concerned, we have crossed 10%, same with Royal Enfield and as far as Hero Motor Corp is concerned, it is I mean because in this year we will do about Rs. 65 crores which is hardly about 1.6%, 1.7% but with the supplies going for Neemrana of suspension where we have 50% share of business for suspension parts and with Halol now starting, you know we have already started 500 a day. So I think this should increase the business and in the second half for Hero we are starting both the clutch and the CVT. I mean because these are the very advanced stage of clearance and so we hope that the Hero business because the largest growth we are expecting is in the Hero business because the base is very low. So I would say that as far as Hero is concerned, still small at 1.6%, 1.7%. HMSI and Royal Enfield have crossed 10% of our share of business.

Moderator: Thank you. We take the next question from the line of Ashwin Shetty from Ambit Capital. Please go ahead.

Ashwin Shetty: Couple of questions; how do you see the CVT opportunities?

Anurang Jain: Huge opportunity because as you know the scooter market is growing three times you know the motorcycle market; you have seen it in the first nine months of this year. And it is very important for us to enter the CVT market; we have the technology both the product and the process technology from **Adler** which is Italian company. They have been our partner right from 2001 and that is the reason because of this technology our CVT is like almost cleared at Hero and we hope to start in the second half of the next financial year. And similarly, we have got clearances to go ahead, with the introduction of CVT it will take about one year, one and a half years with even HMSI and Yamaha. So this is a huge opportunity because the base we have to supply more and more products for scooters, so we are growing faster now. So for us it is a very high focus area.



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- Ashwin Shetty:** And can you just tell us about the CAPEX plans for the next two years, how are you seeing CAPEX?
- Anurang Jain:** See what I had mentioned earlier is we want to our budget is about Rs. 275 crores in India and about €15 million overseas, I mean that is the kind of plan we have, which could change looking at the opportunities which are there but that is the plan going forward.
- Ashwin Shetty:** So this Rs. 275 crores are the annual figure, is it?
- Anurang Jain:** Annual figure.
- Ashwin Shetty:** And there is a factor in anything related to ABS?
- Anurang Jain:** Yes, it does.
- Moderator:** Thank you. The next question is from the line of Rohit Sinha from Asit C Mehta. Please go ahead.
- Rohit Sinha:** Just want to know that any plan you are looking to add to entering into the four wheeler segments and any contribution you are looking to improve in the domestic business from the four wheelers?
- Anurang Jain:** As far as the four wheeler is concerned, our presence is mainly in the aluminum casting space. So we are definitely going to keep looking for opportunities for supply of castings for, say passenger cars where the volumes are bigger, we are always on the lookout there but right now our major focus is for exports. So for example, exports I can share this with you that this year Exports to Getrag are expected to be Rs. 78 crores, we want to go to Rs. 150 crores say in the next financial year because we already have the orders for it but these orders are one at least one and a half years' earlier, so we are focusing on the four wheeler. Now this is to Getrag transmission which is a supply to ford motor company and recently for their plants to Mexico, UK and in France. So we are focusing more on these products because they are large, the margins are better and we also get an export incentive on this, a small export incentive. So for us exports of casting makes a lot of sense. So our focus on the four wheelers space is more there because as you know we believe in profitable growth, it is very important for us. So our target for the passenger cars is mainly in the aluminum castings in here.
- Rohit Sinha:** What normal time it takes to add a new customer in your portfolio, all auditing period and all that things if you kind of consider?



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Anurang Jain: See first it depends who is approaching, in case of Hero Motor Co-op Corp, they approached us for our technology, so that was immediate, that was fast, but then when we have approached like Honda it took us five years to get in. We were trying from 2000, in the year 2000 it took us five years till 2005 to get the business with them. So it depends case to case, so there is no period I can tell you.

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 our standalone business; we have seen a reasonable reduction in our RM cost on vis-à-vis second quarter. Any reason for this RM cost to come down considering the commodity cost inflation and how sustainable this would be?

Anurang Jain: See what happens is that we have understanding with our suppliers because one is, we have like a back to back pricing model, unless we get a price increase or reduction from the customer, we do not pass it on. That will happen after almost I would say 15 years to 20 years of dealing with these suppliers, so there is a lot of trust amongst selves. We have an Endurance vendor association where we interact on any interface losses, so we have a very strong supply group which is supporting us. At the same time, we have a year on year based on business, so we get some lower prices or at the same time we have understandings based on the share of business if it changes, there also we get some better prices. So there are lot of initiatives which have been taken with the vendors for which we are able to, whether it is sustainable next quarter of course that would be our goal but see it is a factor of what we can get prices we give to our suppliers and that is what we get from our customers. So it is a factor of that, so in third quarter we could do it well and I would say very well. So you see the RMC standalone is come down to almost 63.8%, so it depends quarter to quarter what increase you can get from your customer which is normally quarterly or six monthly and what we pay to our suppliers. So it is a factor of that.

Jinesh Gandhi: And are we seeing commodity cost inflation now reflecting in our P&L or that is yet to happen?

Anurang Jain: No because see most of the materials are a pass on to the client, so we do not get much affected by that and that is a very good system which is there in this industry that quarterly or six monthly you pass on the major increases, of commodities that is a good understanding we have, you know good base, we have a very transparent costing structure with a clear cut bought out materials, what is the raw material price for each, so it is a very transparent way of functioning.

Jinesh Gandhi: Sure but that cost inflation is now coming through or I mean from OE perspective are we getting a pass through?

Anurang Jain: Yes, we are.



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- Moderator:** Thank you. The next question is from the line of Ashish Nigam. Please go ahead.
- Ashish Nigam:** Sir if you can just talk about our average content per bike and how does it changes when supplying to premium bikes like KTM and the new Bajaj Dominar.
- Anurang Jain:** See the thing is if you know Bajaj we were at around 15% to 16%, I am saying on an average our content per bike 15% to 16% of what they buy is bought out is our content per bike. Right now if you talk about HMSI and the other customers because it is second and third, the HMSI and Royal Enfield, Royal Enfield is also about 16% to 17%. As far as HMSI is concerned, we are not catering in a big way to all their plants, it is mainly to the 3rd and 4th plants which are the newer plants in the last 3-3.5 years, so all I can say is, it is very difficult to put a percentage on the average, of course we can compute it but our focus has been always to get large share of business in our product segments, one is introduction of the new products like CVT and Clutch and brakes where we are not present and to get high share of business for our casting and suspension, which with HMSI we have got, with Hero we are getting both for Neemrana which was a new plant opened 3 years ago as well as the Halol plant where we are 100% share of business, so with this automatically the content per bike will increase. So, our focus is to be honest not so much on content per bike that is an outcome, our focus is try and keep increasing our share of business in all our four products segments and that is what we are striving out to do.
- Ashish Nigam:** And sir secondly how receptive are OEMs to new suspension technologies like mono shock and when do we expect scooters to go entirely towards front fork?
- Anurang Jain:** In fact, they are very open. In fact, I cannot share everything but we are already working with customer's based on their request for different types of front forks for scooters, for motorcycles. Whether it is economical or whether it is high-end. Because we have the technology with White Power, Austria we have the technology for very high-end forks including the inverted forks. As well as we have given for the HMSI NAVI as very low cost economical mechanical front fork. So ultimately our R&D is doing a lot of innovative things in a product segments to give them a good value add for the products we supply. Looking at the requirements could be right from a hydraulic shock absorber, to an oil & gas shock absorber, mono shocks with a side canister or it could be right from a mechanical front fork to an inverted front fork where the price can be 10x. So we are offering various things which we have already done in the past and there are new things on which we are already talking to them and you will see these products come out in future years.
- Moderator:** Thank you. We take the next question from the line of Rakesh Jain from Asit C Mehta. Please go ahead.



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Rakesh Jain: my question is regarding the European business, in terms of Fiat Chrysler what is the contribution as on December 2016?

Anurang Jain: Are you talking about consolidated basis?

Rakesh Jain: Yes,

Anurang Jain: Its 15.9%.

Rakesh Jain: And European?

Anurang Jain: If I take only Europe it is 51.1%.

Rakesh Jain: So how do we see it moving forward in the next two years and are we adding any new clients?

Anurang Jain: We are adding. Let Mr. Massimo Venuti answer this question.

Massimo Venuti: Chrysler is one of the most important customers that we have in Europe but as you know more or less 85% of our overall business is with five different customers. We have all the main German customers so we don't want to enter with new customer. The strategy of Endurance in Europe is to maintain for sure the focus with these five customers of which, in Germany – BMW, General Motor, Daimler, Volkswagen.. In our portfolio we have not Japanese customers so, sooner or later, probably we will try to find a solution but this depends also from our industrial foot print. We are in Italy and Germany where as you know the Japanese potential customer have not plants. The strategy is to maintain the focus with these 5 top customers. 85% of our business is with them and we want to continue to focus on them.

Moderator: Thank you. We have a next question from the line of Nishanth Vass from ICICI Securities. Please go ahead.

Nishanth Vass: Sir structurally I just wanted to understand considering the fact that our new focus business or let us say growth business segment should be say transmission and brake side. So from a geographic foot print basis in terms of manufacturing for the customers and though we are trying to enter on the other customers other than Bajaj, over the next three to five years, what is your thought process in terms of plant expansion near to the customers in India or do you think in these segments you don't need to set out customer centric plants to get higher share of business?

Anurang Jain: What I would like to tell you and I will just share some example with you. It depends on the size of the business because when you set up a new plant it involves investments. The investments in machine and all is one part but the main challenge is investment in people, to get the right

people to invest in them because ultimately your quality will not change whether it is exiting plant or new plant so they expect the best. And quality requirements are going up every year. So the way we see it is you must have heard we are consolidating plants also. In fact, we have 18 plants, which have already given it in the media to the stock exchanges, we are consolidating plants to 17. But once the Halol plant starts in the 4th quarter of 2017-2018 again we will back to 18. So the question is of the economies of scale. It should make business sense to start a new plant. So yes, for transmission and brakes depending on the size of business if it entails a new plant we will do it. So for example, when HMSI started initially with suspension for the third plant in Narsapur in 2012-2013 we said we will supply from Aurangabad because we have the capacity though they gave us 100% share of front forks but the shocker and casting was at that time a lower percentage. So they agreed that we supply from Aurangabad but when HMSI gave us 80% share of business for suspension and 65% for castings for the plant in Vithlapur which was near Ahmadabad and then we put up our Sanand plant. They insisted on a new plant. It makes sense to us. It gave us economies of scale. So we put a new plant. Same thing we are doing for Hero and Halol because they have given us a 100% of business, we are ultimately going to 6500 vehicles a day it does entail a new plant and then it makes sense. So ultimately it should make business sense and we should be able to make good margins only then we set up new plants otherwise we prefer existing plants.

Nishanth Vass: Sir hypothetically speaking if we gain higher share business from other Honda plants or other Hero plants, we would be open to setting up Greenfield facilities?

Anurang Jain: Of course.

Nishanth Vass: On the point somebody asked on the ABS the CAPEX that 275 crores domestic, ABS related CAPEX is more on technology or in terms of actual?

Anurang Jain: I think it will be quite similar, both the technology as well as the capital equipment investment will be similar. The technology will not happen in the first year; it will happen over a period of years while the investments in the capital equipment will of course happen in first year itself.

Moderator: Thank you. That was the last question. I now hand the floor over to Mr. Ashish Nigam for this closing comments.

Ashish Nigam: Thank you. On behalf of Axis Capital thank you all for joining the call today and thanks again to the Endurance Management for give us the opportunity to host the call. Have a good day every one.

Moderator: Thank you. Ladies and gentlemen on behalf of Axis Capital Limited that concludes this conference. Thank you for joining. You may now disconnect your lines.