"Mahindra & Mahindra Ltd Q3 FY17 Earnings Conference Call"

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MODERATOR: **MR. MIHIR JHAVERI – RESEARCH ANALYST, EMKAY GLOBAL**

Moderator: Ladies and Gentlemen, Good Day and Welcome to the Q3 FY17 Results Call of Mahindra & Mahindra Limited, hosted by Emkay Global Financial Services. As a reminder, all participant lines will be in the listen-only mode. And there will be an opportunity for you to ask questions at the end of today's presentation. Should you need assistance during the conference call, please signal for an operator by pressing '*' then '0' on your touchtone phone. Please note that this conference is being recorded. I would now like to hand the conference over to Mr. Mihir Jhaveri – Research Analyst of Emkay Global. Thank you, and over to you.

Mihir Jhaveri: Good evening, everyone. I would like to welcome the management and thank them for giving us this opportunity. We have with us today Dr. Pawan Goenka – Managing Director; Mr. V.S. Parthasarathy – Group CFO, Group CIO; and other Senior Management personnel from M&M, including IR team.

I would now hand over the call to Mr. Parthasarathy for his opening remarks. Over to you, sir.

V.S. Parthasarathy: Thank you. I extend a very warm welcome to those who are attending this call. I will share a glimpse on the economic scenario along with financial snapshot for Q3. After my comments, Pawan will share overall performance of M&M.

Before I share financial results, let me take you through some quick macroeconomic updates. The big one was Union Budget with disciplined fiscal target, focused on conservative and effective spending and giving an environment to stimulate growth, without even giving any big stimulus. So it is more like our policy of guiding without guidance. So it is stimulating without giving stimulus. Budget emphasizes on building more on initiative already taken. Overall, very positive for growth. But the big impact will come when the initiatives are kicked off at the ground level.

Demonetization, we see mixed impact of demonetization on Indian economy. This is a bold step, and we welcome the step taken by the Government for the larger good of nation. We may see some short-term pains and you will see it in the volumes and financials of this quarter. GST is a big decision being finalized. Broad decisions are already taken, so everything is go. The specifics need to be decided, and we hope that it is decided in time for a July implementation.

Manufacturing growth has been sluggish for the last few quarters. However, November IIP grew at 5.7%. We may see some uptick in manufacturing sector. We hope to see the demonetization impact slowly reduce and the impact on the economy over next year begin on even to a positive deal. Overall, on the global economy, picking up in terms of growth across in spite of quite a bit of problems starting with Brexit and other such incidents.

Now let me talk about M&M and our financials for Q3 of FY17. I will talk about M&M plus MVML.

We had 21.9% higher volume in tractors. However, auto was lower by 7.7% volume. Net revenues overall, therefore, grew by 1.2% versus Q3 of FY2016, Rs. 10,587 crores versus Rs. 10,464 crores in the previous year. EBITDA was flat at Rs. 1,449 crores, previous year was Rs. 1,451 crores.

PBT was lower by 4.4% at Rs. 1,124 crores, versus Rs. 1,158 crores of Q3 of FY2016. The above, I wanted to point out, included last year a large amount due to Haridwar excise benefit being there. Therefore, the last quarter benefit was available and it was significant around Rs. 200 crores. We have started to have a new IPS, as we call it, our Industrial Promotion Scheme, which benefits us by Rs. 26 crores this quarter. However, the impact is Rs. 201 crores last year versus Rs. 26 crore this year. So that is a big delta, which has been overcome in many sense to get the OPM at similar level as last year. PAT at Rs. 801 crores is lower by 5.7% as against Q3. That is overall an exceptional income, which is by and large neutral Rs. 17 crores on M&M plus MVML level. You see higher amount of exceptional income in M&M, which is for sale of some shares in subsidiary companies and some impairment provision, net-net it is broadly zero impact on the bottom-line.

Segment revenue and result: Auto, total volume lower by 7.7% as I said, and revenue Rs. 6,359 crores, lower by 8.3%. Segment results, Rs. 452 crores profit this year as compared to Rs. 714 crores last year. FES grew handsomely by 22%. Revenue is higher by 20%, Rs. 4, 281 crores versus Rs. 3, 561 crores last year. And FES segment results at Rs. 746 crores, 35.6% higher versus previous year of Rs. 550 crores.

In terms of subsidiaries, key performance. Tech Mahindra had a stellar quarter, Rs. 856 crores, a growth of 14% versus sequential, and a 30% growth versus the previous year. MMFSL had a group profit of Rs. 12 crores, it has been a tough quarter based on demonetization. MHRIL at Rs. 36 crores and MLDL at Rs. 35 crores, grew 15% and 48% respectively versus previous year same time. So, all these subsidiary companies did very well, listed companies did very well in this quarter.

That brings me to the end of my portion. Let me now hand over to Pawan for his comments.

Pawan Goenka: Thank you, Partha. And good afternoon, everyone. I want to start off with the subject that may be on top of your mind, which is demonetization. What was the effect, where we are, and where we think things will be back to normal?

So, I will talk about the automotive industry and the tractor industry. And what we have seen is, if you look at November and December as sort of peak of demonetization, and January as the beginning of recovery, and if I was to compare the growth rate in the first seven months of the financial year to the growth or de-growth in the two months of November-December, what we find is that the least affected sub-segment was our passenger vehicles where the effect was about 10%, and the most affected segment was tractor and two wheeler, where the effect was as much as 30%. Just to underline again, I am comparing the growth rate that was there for the first seven months versus what happened in these two months. So what that tends to tell us is that the effect of demonetization was perhaps higher in the rural area, because two wheeler and tractor sales are driven by rural; and perhaps lower in the urban area because passenger vehicles are driven more by urban.

If you then look at January as a recovery month, we find that the cars and UVs, passenger vehicles that is, have almost fully recovered. In fact, the growth in January was higher than the first seven months growth. The tractor recovery is partial, the two-wheeler recovery is partial, in fact, very small. And the commercial vehicle recovery is somewhere in between. And therefore, our assessment is that the fastest recovery that has happened in cars brings cars kind of out of demonetization effect, and we also think that by end of March, as the Finance Minister said in his speech during Budget, by end of March or early April, demonetization will be fully behind us. We are also finding that the switching over to digital economy, switching over to digital transaction, bank transaction is happening perhaps faster than any of us would have thought, especially in rural areas where the rural folks are slowly but surely are switching over to digital economy.

Now what will be the effect of this on the growth rates for the financial year is the next question that you will have on your mind. So just taking tractor first, last quarter we had talked about a potential 20% growth in the tractor industry for the financial year. Because of what has happened in the last two, three months and what we think will happen in the next two months, we are pegging the growth in this quarter, current quarter at 8% to 10%, making it overall about 16% -17% for the industry full year. If you look at passenger vehicles, our estimate is that we will see a double-digit growth, 11% - 12% for the whole year, right now we are at about 9.6% and we should cross 10% is what we are estimating. If you look at light commercial vehicles, we would remain in positive territory, but probably in single-digit. And the small commercial vehicle, which is sub-one ton, is something where we will probably just about get even to last year's volume. Three wheeler is a segment that perhaps most hurt by demonetization, and we do not think that three wheeler will come into positive territory during this year. So that is the overall effect of demonetization and what it will do to overall growth for the year.

Just focusing a little bit again on the Union Budget that Partha had touched upon briefly. What we clearly see in terms of what impacts our business the most is that there is a good thrust on rural development and infrastructure, that continues, which will be very good for our farm business, for tractor business, micro irrigation business, and also has a positive effect clearly on the automotive spaces or segments that Mahindra is most present in. Continued support for electric vehicles we have seen in the budget. What we would have liked to see more would have been focus on Make in India, and clearly reduction in corporate tax for all corporations, not just for MSMEs.

So, if I go to tractor performance during the quarter three, that is October - December period, it was our best quarter in terms of market share with 44% market share in the quarter, highest ever. Obviously, helped with very good numbers in October where we had as much as 60% growth in that month. Even in spite of subdued growth in November and December, we had overall very good numbers of growth for tractor, helped by Yuvo, which is doing very well as we talked about last quarter also. Right now, the industry YTD January is at about 18.2% growth and YTD January Mahindra is at about 23.5% growth with a market share of 43.4%, which is an increase of 1.9% over last year, YTD January.

For automotive, the effect of demonetization has been on many segments as we talked about earlier. Passenger vehicles are up only about 1.8%, but UVs are up 20.3%, I am talking about the industry. And UV growth is driven by the new launches, Brezza, Innova Crysta and to some extent, KUV and TUV. And right now, UVs' share of passenger vehicles is at the highest ever, at about 25%, that is one out of four passenger vehicles sold in India now is a UV.

Commercial vehicles are down, small commercial vehicles. Two wheelers are down. For Mahindra, the total volume in the quarter was down by 8.3% for overall and 11.8% for passenger vehicles. Export was marginally up during the quarter, but overall 13% up for the year in nine months.

Q4 outlook, I have talked briefly about it already, so I would not repeat that. But again say that urban recovery is almost complete, rural recovery is happening. And by end of March we expect it to be completed. The sowing in rabi crops is very good, it is about 6% higher than last year. The food grain output of kharif has been extremely good, more than what we had thought three months ago, 9% up compared to last year. And therefore, overall farm situation is good, except of course the fact that during these two months, the perishable goods prices had crashed and that did affect the revenue for the farmers. Very good water reservoir levels also at 101%, perhaps the highest that we have seen in three or four years.

We have talked about the tractor industry in detail. Commodity prices are likely to firm up, starting this quarter and going into the next quarter. The BS-IV norms that will happen on 1st of April, that clearly will have a price impact more so on heavy commercial vehicles than on passenger vehicles, and therefore we would expect to see some pre-buying happening in the heavy commercial vehicles.

Just talking about inventory, because that is always a question on your mind, let me first say that on the tractor side. Our inventory is just about where we want to be, we like to keep about 60 day inventory within our plant and dealers in tractors, and we are marginally lower, 60 days right now. On the automotive side, our inventory at the end of December was the lowest that we have seen in the last five or six quarters, at the level of about 52 days, 53 days, dealer and plant combined, maybe two or three days higher than ideal, which would have been about 50 days. So we are pretty well placed in inventory both in auto as well as tractor.

Cost increase or selling price increase, we have seen approximately 1% increase in material cost on an average basis up to December, and we have tried to pass on most of it in selling price, both in tractor and auto.

Just a little bit about the launches, because you may have some questions on that. I am more or less repeating what I had said last quarter, with only one new additional input, that is the U321 product which is an MPV, this is something that I had not said last time. So it is an MPV product, this is a product designed in our technical center in Detroit using American engineers, by and large American engineers and will be manufactured in Nashik. That is an announcement that we have made today, we have announced that we will be investing Rs. 1,500 cores in Nashik and Igatpuri combined for manufacturing U321 product. Then we have the S201 product that I talked about last quarter, which is based on which is based on Tivoli, and that will be launched in second half of FY19.

On the tractor side, we will have variants of Novo and Yuvo coming up over the next 12 months. We have a new tractor platform that will be coming up middle of this year, and a new platform from Swaraj division that will also be happening middle of this year.

A bit on SYMC, we have concluded the calendar year, which is the financial year for SYMC on December 31. The results of the last quarter are not yet announced, therefore I can only talk up to third quarter. We had a volume growth of 7.7%, getting to about 156,000 volume, which is the highest that SsangYong has seen I think since 2002. There was a revenue growth comparable to volume growth, 8.8%. Nine months that is ending September quarter, SsangYong was in positive PAT of KRW 38.7 billion, which translates to Rs. 226 crore positive PAT at the end of nine months, against Rs. 474 crore loss previous year. So the nine months are profitable. In fact, every quarter of the calendar year, the first three quarters has been positive for SsangYong. So in some sense, we have turned around and looking now to have positive profit and growth from here on.

New product launches for SYMC. Just like for Mahindra, we will see a new product every year. Y400 will be launched in May, this is a new large SUV. Q200 will be launched in early 2018, which is a pickup. And another new products will be launched in May 2019 from SsangYong's stable.

Mahindra Electric, a lot of activity happening, not much in terms of volume growth yet but a lot of interest that is coming from government of India, a lot of interest coming from fleet operators, and therefore we should be seeing some kind of large ramp up happening in electric vehicles anytime soon. It could be this quarter, it could be next quarter, but soon.

Two M&As that I just want to briefly mention, that have been announced and you are all aware of it. One is, we have acquired 75.1% stake in HİSARLAR, and this is a Turkey based company into cabins, agricultural machinery and farm mechanization equipment. This is just about in the process of the transaction getting completed. The other one was on the grapes where we had purchased a company called OFD, which is a Netherlands based company, we have acquired 60% of stake in that company, and that transaction has been completed.

So that completes our formal presentation from Partha and me. Now, we will leave it open for any questions.

Moderator: Thank you, sir. Ladies and gentlemen, we'll now begin with the question-and-answer session. Our first question is from the line of Kapil Singh from Nomura. Please go ahead.

Kapil Singh: Sir, my first question is on the investment that we are doing in Nashik of about Rs. 1,500 crores. So, could you help us understand what is the kind of capacity we are creating there and what all does this Rs. 1,500 crore include?

Pawan Goenka: So, our capacity increase in Nashik will be about 50,000 vehicles, from 160,000 to 210,000. What was the second part of the question?

Kapil Singh: Sir, what all does this Rs. 1,500 crore include?

Pawan Goenka: So, as we always include in any investment, we have the intangible expenditure on the product development. We have all the tooling sets are developed either at our plant or in supplier plants in Maharashtra. We have investment in Igatpuri plant for engine, investment in Nashik plant for all the capacity additions, as well as dies, fixtures that we will do.

Kapil Singh: And sir, is U321 a global product or it is more focused for India?

Pawan Goenka: U321, we certainly see that it will have markets outside India. Our first launch will be in India and then we will be looking at markets outside. This is a true MPV, a true MPV designed like an MPV and not like an SUV. And the focus is on movement of people and it is not an SUV vehicle.

Kapil Singh: And secondly to Partha, just one question. Could you give some guidance on tax rate given the merger taking place for the two-wheeler business, in light of that?

V.S. Parthasarathy: Two things, first from the P&L point of view and second from a cash flow point of view. The two-wheeler demerger has been announced into M&M, subject to the court order, is being done for strategic and operational reasons. The consequence of the strategic and operational initiative being concluded would mean that the effective tax rate for next year would be about 4%. However, according to IndAS, any tax credit that received goes into the balance sheet as part of the reserves, so that it does not come and give you a P&L benefit. So that is an accounting way of looking at the demerger.

The second is the cash flow way. In the cash flow side, you know that we are on MAT. So on cash basis we have been on MAT for the past number of years, and for the next two or three years, we will continue to be on MAT. So this two wheeler will continue to help us with that, but even without two wheelers we would have been on MAT next year and the year after, okay. So from a cash flow point of view, you can take 21.22%, which is the cash tax rate.

Kapil Singh: Sorry, that is for FY17 as well?

V.S. Parthasarathy: Yes. So cash basis we are in MAT this year, we will in MAT next year.

Kapil Singh: And on P&L basis?

V.S. Parthasarathy: P&L basis, what happens is that this year we are about 27.5% effective rate, next year we would not have two benefits which we have this year, which has already been announced two years back and now that will not be available as deduction. First is 32AC, which is the 15% benefit we used to get on all R&D expenses, so that will not be there. The second is, whatever R&D expenses that we incurred, we were getting 200% weightage deduction, from next year onwards, we will get 150%. So both these put together, the 15% not being available and the second part is the 200% to 150%, the effective tax rate will go up about 4%. So EBITDA is 27.5% this year, the P&L tax rate should be about 31% - 31.5% next year. This is a double whammy effect that the current budget has had that they have taken away the exemption that we had, but there is no top-line tax rate reduction towards 25%. So we will have that kinds of rate. But luckily for M&M, for us what is real is the cash tax rate or MAT rate which is at 21.5%.

Moderator: Thank you. Our next question is from the line of Amyn Pirani from Deutsche Bank.

Amyn Pirani: My first question is again on the Nashik investment. First of all, I just want to check this Rs. 1,500 crores will be spent over what timeframe? And is it within the Rs. 10,000 crore rolling guidance that you gave on your investment?

Pawan Goenka: Answer to the second question is, yes, it is part of the Rs. 10,000 crores. If you would recall, last year we had announced an investment of some Rs. 4,500 crore in Chakan Phase II, that is currently going on. We have already invested part of it in KUV and TUV, and more will be done over the next four - five years. This investment we expect to be completed in about three-year timeframe, though the timeframe available to us to make this investment is about eight years. From effective 2016 to eight years is what available to us, but we expect to complete this in about three years.

Amyn Pirani: And so the launch of the product would be also within a three year timeframe, I am assuming?

Pawan Goenka: That is right. In fact, launch of U321 will be in the next, I would say, 12 months. And it is not all Rs. 1,500 crore will get invested in that, there will be more investment happening beyond U321.

Amyn Pirani: And just to recall in terms of the launches, so this year we just have the gasoline variants being launched for Scorpio and XUV?

Pawan Goenka: No, that is not correct. We have not announced everything that we will be launching. All the launches announcing is not right for us, we announced two things. So the thing that we have announced is a petrol launch, as we said, we announced the U321 launch. The other things in terms of refreshes that we have not announced.

Amyn Pirani: And just on the results itself, so while you understand that the automotive margins on a YoY basis would have been hit because of the benefits going away, but is that the only reason why the margins on a YoY basis are down, or is there some other reasons in terms of discounting or any other reason that we can think of on the automotive margins?

Pawan Goenka: Let me take a crack at it and then perhaps Partha can add. The margin down and the effect of Haridwar almost matches. But then there are lot of other factors, some of which are plus, some of which are minus, which cancel each other out. So therefore, one can think of it as an effect of Haridwar because every quarter we will have some pluses and some minuses, and they balance out. You want to add anything?

V.S. Parthasarathy: Two or three things actually. First is that let us start from the below, depreciation and amortization, I am talking about segment results, depreciation and amortization is about 100 basis points higher as compared to the previous year. This is because all the product launches which have happened, the amortization is coming on and the revenue is not going up, means I have lesser revenue to to adjust this. Therefore, if you see, depreciation as a percent as amortization, it would have gone up by 100 kind of basis points, so that impact.

Second is, fixed cost is very much under focus and control. But that is personnel cost alone, assuming only increment is the increase, but the revenue de-growth is there in Q3. So you will see percentage to revenues, fixed cost as a percentage to revenue going up. These are two impacts. When you come to the gross margin, the only impact that you can take is that last year, Haridwar, and this year positive IPS and to some extent, so it was just to give quantum, last year impact is Rs. 200 crore minus and we have got a positive Rs. 26 crores on account of IPS II. The balance is what you get reflected in gross margin. Other things cancel each other out each other and therefore it is not going below the line.

Moderator: Thank you. Our next question is from the line of Sahil Kedia from Merrill Lynch. Please go ahead.

Sahil Kedia: I have questions regarding the farm equipment business. You said that there are two launches that are taking place as far as new platforms are concerned, while your market shares are already very high. I just wanted to get a sense of how confident are we of further gaining market share this year? That was number one.

Number two, when we look at your farm equipment revenue, and I know this is probably not the right way of doing it, and we divided by the total volumes to come with realization, it seems that the realizations have fallen down. Is it right to say that that is largely because the non-tractor sales of all other equipment, etc are now a smaller portion of total revenue given that volumes are up?

Pawan Goenka: So in terms of average realization, agri is not included So last year, agri revenue was in M&M Limited, this year agri revenue is outside. And therefore if you divide the number of tractors you will get that effect, because agri revenue was in the order of Rs. 600 crores - Rs. 700 crores last. Quarter will be about one-fourth of that so Rs. 175 crore - Rs. 200 would be agri revenue that is out. So that is one factor. I think that is pretty much about it that will have and the segmented account of farm includes our engine business, which is part of that segmented account, includes the construction equipment business that is part of that segmented account, and therefore if you simply took the top-line divided by number of tractors, you will probably not get the right figure. Fundamentally, nothing much has changed in terms of model mix. It is not that we have a lower revenue or lower ticket price shift in the model mix. If anything, we have sold more Yuvos this year compared to last year. Yuvo is higher priced than the vehicle and then tractor at places. What was the other question?

Sahil Kedia: No. My first question was on market share. Consenting that you have two new platforms coming up?

Pawan Goenka: Yes, market share. See, when we have a 44% market share for us to say that we will gain more is a statement. Everybody will want to gain a market share. The reason one launches new products is not necessarily just to gain market share, but even to protect market share in today's competitive world. You have to constantly keep running, if you stand still then you will lose market share. So clearly, we strive to gain market share, but so does everybody else, and everybody else is also launching new products, improving their products, improving their marketing and sales activity, all of these things. Internally, of course, we do plan to raise market share. But in tractor industry, as you have seen in the past, in a given year you will never see a huge departure of market share of any player. Maybe 1% more or 1% less, but you would not see a huge departure of market share of any player.

Sahil Kedia: One more question if I may, how has spares done this quarter from other companies and calls that have happened, it seems that spares were impacted quite significantly due to demonetization. Can you just give us a quick color across both auto and farm?

V.S. Parthasarathy: On a very broad level, I did not see an impact, maybe because the spread in terms of both the dealer and the bazaar channel. I have not seen that kind of impact, but because you made a specific statement that I am just asking my people to check if there is anything that I find, then I will revert to you. Otherwise, you can take generally we were okay.

Just one quick thing on the earlier question that you had, which is in terms of revenue. Broadly if knock off this agri and even divided by numbers, though it is not the pristine way, Rs. 300 crores you take out for agri revenue for the quarter, that is what that is... sorry nine months, Rs. 300 crores. Rs. 100 crores a quarter you knock off, you should get the trend to be okay. But we can confirm once again that there is no tractor drop.

Moderator: Thank you. Our next question is from the line of Pramod Amthe from CIMB. Please go ahead.

Pramod Amthe: Two questions. One, since your two wheeler business is about to get merged, will you give us some color in terms of last quarter what was the run rate in terms of top-line EBITDA, or nine month, how is the performance financially?

V.S. Parthasarathy: Topline?

Pramod Amthe: Sales, EBITDA, some trends so we can relate into fourth quarter numbers …..

Pawan Goenka: We will not be able to share two-wheeler financials on this call.

V.S. Parthasarathy: The question I have registered, you are asking the question from that how do I plan for next year. So let me think about it.

Pramod Amthe: Not only next year, if I am not wrong, even the fourth quarter or…

V.S. Parthasarathy: Yes, I understand, we will think about that and come back to you.

Pramod Amthe: And second, with regard to the MPV development, this is to Mr. Pawan Goenka. It seems this is the first development you are doing through your US tech center versus your historical developments in India. One, how are the cost differentials in terms of development cost and this Rs. 1,500 crores what you talk about includes the development cost? And second, what is the benefit of going there and doing it? Is it the speed-to-market, or what all you derive benefit versus disadvantages?

Pawan Goenka: So, first just to answer the previous question on spares, YTD January our spare volume is 12% higher than last year. I do not have figures for the quarter, but YTD January it is 12% higher than last year, auto and tractor combined.

V.S. Parthasarathy: So we can stay with this that overall we have not seen any negative impact yet.

Pawan Goenka: Okay. So the question is on investment impact of doing development in Detroit and what is the value of doing it in Detroit. So, investment impact is only to the tune of the salary differences between India and Detroit. In terms of the investment that we have to make in tooling, in prototyping, we have tried to maintain maximum prototyping work happening in India, a little bit happens in US but mostly in India, and therefore the impact there is not very large. I cannot quantify that if the same development was fully done in India, what it will be. But it is not a day and night difference. It is a small increment, but not a day and night difference. The reason for that is that it is not a turnkey development done by USA, it is where we use our engineers here in MRV working with the engineers in USA. In fact, we have about 110 engineers working in US, not all of them are deployed on this one project. And therefore, we probably have 50 - 60 fulltime people working on U321 development, and rest of the work is being done here in India.

Second, when you talk about the benefit of doing it in the USA. Detroit clearly is a place where maximum automotive engineering knowledge is available. While we could have hired two or three or four people to come and work here with us in Chennai, but we cannot bring 100 people to work here in Chennai. And we probably will not have as much options of that talent pool that may be willing to move to India. And therefore, we decided that it is best that we go there rather than try and bring people here and establish a technical center, which will help and work with our engineers here in MRV. So it is not being done in isolation by those people, it is being done in cooperation with people here in India with constant travel happening back and forth, constant video conferences, audio conferences happening, and then able to get the best of both worlds in terms of not having a significant cost impact of development and yet be able to get the benefit of expertise available in Detroit area.

Moderator: Thank you. Our next question is from the line of Binay Singh from Morgan Stanley. Please go ahead.

Binay Singh: My question is basically on the product cycle only. How different or what kind of product improvements are you seeing when you are developing a product overseas in Detroit versus what we have seen from Mahindra in the past? And the second question is, Tivoli has done very well in Korea against strong competition, and now we are talking a product on Tivoli's platform in India. Will it be sort of a compact SUV and is this also getting developed in Detroit, can you talk a little about that?

Pawan Goenka: So second question first. The product which we are calling S201 is based on Tivoli platform and developed jointly between engineers at SYMC and engineers in MRV, Chennai. And so it is a joint effort of these two. Though I cannot give you any more details about the product, but based on Tivoli platform, it cannot be much bigger or much smaller than Tivoli. So you can kind of conclude from this.

The improvement on the product, I think, you just wait and see. When the product is launched you will see. It is not that we are not able to do right products here, but when we do products here, in the past we had to work a lot with consultants outside. And by doing product development in Detroit, we have our own people doing product development working with the team here. So, the joint effort does two things, it builds the engineering expertise of Detroit into our products and also helps to sort of ramp up the expertise of engineers here at MRV. But the products like XUV for example, Scorpio for example, Xylo, all of these have been done completely by our engineers with help from consultants outside. So it is not like suddenly you are going to see something that is totally different. It is just a degree that you will see difference. In some areas, there will be improvement perhaps based on Detroit ability, but wait and see until the product comes out.

Binay Singh: And sir just lastly, on your existing product portfolio…

Pawan Goenka: Sorry, I just want to clarify one more thing on this that if you look at any products that we have launched, from Scorpio onwards, you would see that in every new product launch there will be some improvement that you will have either in the design, either plug some gap and interior finish and so on, ride and handling, fuel efficiency. So it is sort of a learning curve that we are going through and we are now into our fourth cycle of product launches, the first cycle was the Scorpio cycle, the second cycle was the XUV cycle, Xylo - XUV, third cycle was what we did in FY16. And what we will start with U321 will be the fourth cycle. And with the fourth cycle we are pretty much getting to a level where we have the expertise at a level that we need to be to be able to do global product development and launches equivalent to global launches.

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

Chirag Shah: Sir, I have a question on raw materials. You indicated that cost pressures have built up in this quarter. Can you just elaborate on that, how much is the impact visible and how much is left out in that sense? And what kind of pricing action you have taken to counter that?

Pawan Goenka: Again, what is yet to come time will tell, we only make kind of an estimate. If I was to a little bit more precise about it, we think that steel prices will go up, cold-rolled steel prices will go up. We think that natural rubber prices will go up, we think that plastic prices will go up, polypropylene. Probably the forging steel, pig iron and lead will remain roughly where it is. That is our looking into a crystal ball, but it depends on too many other factors, so we do not know where we will end up.

Chirag Shah: So the steep increases that we have seen recently, will we see the impact in the Q4 or it will be in next year quarter one? So we will have some lag effect, right?

Pawan Goenka: Yes, so the steep increases have happened in the last three quarters. We' have gone from high-30s to high-40s, that means almost 25% increase. We do not expect to see such steep increases, but we think it will continue to increase somewhat.

Chirag Shah: And a related question, because when I look at your gross margins, RM to sales sequentially, despite a significant improvement in tractor volume as the percentage we have seen a negative impact on RM to sales. So, is it because of demon where discounting activity or support activity had gone up and that is the reason? It has gone up from 61.1% to 68.6%, raw material to sales as a ratio.

Pawan Goenka: Again, a lot of factors go on to it. To draw a conclusion from that one number is very difficult. Because for example, you have spares which is not a small amount, almost every quarter it is Rs. 500 crore that is part of revenue, the contribution margins are different in spares. You have incomes coming from oil royalty, you have incomes coming from accessory sales, you have IPS income that is coming in, which is also part of the revenue. Last year, agri was part of that Powerol income is coming into that. So it is very difficult to draw a conclusion. And typically as you know the tractor has higher contribution margin than auto, so when tractor will go up, then there will be a different effect on material cost if tractor share is higher. So we have all the detail worked out, but obviously we will not be able to discuss that with you. But, if I was to look at a product to a product, not a product mix to a product mix, if I look at a product there is not a significant change in contribution margin.

Chirag Shah: This was slightly perplexing, because our mix has been favorable tractor results sequentially, but RM has gone adverse for us. And I just had one last question on spare parts, if you can help us understand…

Pawan Goenka: We are not look at sequentially. Partha has been saying this for many, many years that please do not look at data sequentially, sequential data is very misleading because there is lot of seasonal effect that happens. So look at data wise.

Chirag Shah: Just a follow-up on spare parts, between auto and farm, can you indicate broadly what is the ratio, how much is the spare parts revenue coming from auto and from farm on annualized basis or something like that?

V.S. Parthasarathy: Once again, can I go back on the previous one and then let's take spare parts. Your question is, mix should have shown improvement in margin, correct?

Chirag Shah: Yes, gross margin actually.

V S Parthasarathy: Gross margin. And I told you that I look at year-on-year, but if I look auto year-on-year and tractors year-on-year for the quarter, I said to you before, some other question was asked and I said that tractor year-on-year there is a small improvement in margin. Auto, there is a dip in margin, but if I adjust for the Haridwar impact, in fact it is slightly better, both individually as a sector. The combination is what the output is. So Chirag, broadly from a point of view, I did not see a margin impact year-on-year.

Coming to spare parts, margins are similar whether it is for auto or tractor and I think fungible from our perspective and you do not want to go to breakups.

V.S. Parthasarathy: I have to say that auto is more than tractor. Whether it is 51/49 or 60/40 or 70/30, I would not tell you.

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

Sonal Gupta: Just a couple of questions. One is, what is the sort of price increase you've taken from January? And then, if you could just talk about also what has been the acceptance of Bolero Power Plus?

V.S. Parthasarathy: So, January price increase was about 0.7% for auto. So auto is about 0.7% and 1% is for tractor, but that is for the year, not for January. I think in January we took no price increase, it is about 1%. So about similar, percentages are about similar, 0.7% for auto and similar number for tractor in January. Overall, we have taken YTD December 1% increase in tractor and 1.7% in auto.

Sonal Gupta: And sir, what is the response you've seen for the Bolero Power Plus? I mean, do we see sort of arresting the decline on the Bolero volumes?

Pawan Goenka: Yes. Bolero Power Plus has done extremely well for us. It is a product that has very good value proposition because, as you know, this is up sub-4 meter, so that allows us to give a better value to the customer. It has a three-cylinder engine, which is a very powerful engine, sub 1.5 litre. And overall performance, fuel efficiency, NVH, ride comfort, everything is improving. So Bolero Power Plus has done very well and it has certainly helped us to revive the overall Bolero volume. Having said that, I also want to add that the whole Bolero, the pre-Power Plus, is refusing to die, we continue to get good volume out of that. And right now our volume is roughly half and half between Bolero Power Plus and Bolero.

Sonal Gupta: And sir just on the LCV side, could you tell us what would be the impact of BS IV, what sort of price increase we should see on this?

Pawan Goenka: On the passenger vehicle segment, the effect of BS-IV on pricing will be of the order of Rs. 15,000 - Rs. 20,000. Finally, what pricing we will do, we already have the BS IV available in the market in almost all cases, so you can compare BS-III and BS-IV and you will know the difference, and it is about Rs. 15,000. The same difference will continue post March 31 when we go all BS-IV. As far as trucks are concerned, the heavy truck, where we do not have any BS-IV, there you will see a fairly large impact. My guess right now, we are still working out the final pricing, my guess right now is that you will probably see of the order of Rs. 1.6 lakh price increase, which is 7% - 8% of the selling price, and therefore it is a fairly large impact.

Sonal Gupta: And LCV is the same, right, Rs. 15,000 to Rs. 20,000?

Pawan Goenka: LCV will be similar in the Rs. 15,000 - Rs. 20,000 range, which is currently available. Currently, we are selling LCV both in BS-III and BS-IV.

V.S. Parthasarathy: So, just to get one kind of this, Chirag asked this question, so I just wanted to kind of respond. And this will also say why quarter-on-quarter is not a great one, year-on-year should be looked at. Last year if you do the corresponding Q2 - Q3 comparison for auto and Q2 -Q3, you will see Q2 to Q2 is similar percentage, Q3 to Q3 is similar percentage. But in both cases, Q2 margins for auto is better than Q3, both years. So it must be some mix that goes into rural, to holiday time, etc. So without trying to double guess, just saying that trend-wise, look at year-on-year, we will be able to answer better and you will be able to understand better.

Moderator: Thank you. Our next question is from the line of Jinesh Gandhi from Motilal Oswal.

Jinesh Gandhi: A couple of questions from my side. First is, we have seen a reasonable reduction in other expenses on YoY basis, is there any one-off or just totally cost control-led reduction?

V.S. Parthasarathy: So, just to give that other expenses equal to our total fixed expense, and I told you two things, if I were to break this up broadly into my variable and fixed, the variable has gone in line with the volume, so no surprises there. In fixed expenses, we have been kind of looking at how we can be at similar levels as last year, therefore the cost control and the containment program has worked and that what you see. Last year, Q2 was also slightly on the higher side, sorry, Q3 was slightly on the higher side, so that also helped the comparison. But if I give you one answer, it is cost control.

Jinesh Gandhi: And second question pertains to, any reason for increase in interest cost on QoQ basis has debt numbers increased materially?

V.S. Parthasarathy: So, again your question quarter-on-quarter?

Jinesh Gandhi: Right.

V.S. Parthasarathy: Yes, we took some new debt.

Jinesh Gandhi: And sir lastly, what was the accumulated losses in two-wheeler business?

V.S. Parthasarathy: Accrued losses in two-wheeler is indeed about Rs. 2,000 crores. Accumulated losses in MTWL?

Jinesh Gandhi: Yes.

V.S. Parthasarathy: Sorry, they are all telling me to amend that statement to Rs. 2,500 crores.

Jinesh Gandhi: Rs. 2,500 crores?

V.S. Parthasarathy: Yes.

Moderator: Thank you. Our next question is from the line of Yogesh Aggarwal from HSBC.

Yogesh Aggarwal: Just one question, I missed in your prepared remarks, you mentioned tractor outlook of 8% to 10% in the fourth quarter. Is there some initial outlook guidance for FY18 as well, like you mentioned for the car industry?

Pawan Goenka: Right now, no. We probably will be able to do it in April - May only. The reason is that we are still trying to figure out how the quarter will end. Normally by now we would have had an estimate, but because of demonetization we are still not able to do a full assessment. So, we probably will have to wait till till the end of March before we can do a full assessment. But what I can say however is that we are expecting a decent growth. It is not a situation where we say that we have had good growth this year and therefore not a good growth, because I think I had mentioned in this call earlier that in spite of the 17% growth, we would still be 50,000 tractors less than the peak year that we had about four years ago. So just to get to peak year, we will have to grow 10%.

Yogesh Aggarwal: But obviously, a lot will depend on monsoons as well I guess?

Pawan Goenka: Obviously, it will depend on monsoon. But again, we have always said that one bad monsoon is not very bad, two bad monsoons are really bad and three bad monsoons, I do not want to think.

Moderator: Thank you. Our next question is from the line of Arvind Sharma from Citi. Please go ahead.

Arvind Sharma: My first question would be on TUV and KUV. How is the trend, how has the impact of demonetization been on these two models? And second question would be more on the results, can you give some more details on the exceptionals, both for M&M and M&M plus MVML? Thanks.

Pawan Goenka: So both KUV and TUV, after a very good start, did slow down a little bit for a variety of reasons. Not the least of that was the fact that there is this whole uncertainty about diesel vehicles about this time last year because of the Supreme Court ban that was put in. And therefore, TUV being only diesel and KUV being diesel and petrol both, but Mahindra being more known for diesel adversely affected our growth in KUV and TUV. Slowly, the confidence is coming back, both in the product as well as in the diesel situation and we would see volume increase month-on-month both on the KUV and TUV. So therefore, I would say both are on the mend in terms of volume.

V.S. Parthasarathy: Yes on the exceptional items in M&M, because of sale of certain investments there was an exceptional income, and I think if you had this exceptional income in the order of Rs. 364 crores in M&M. There is an impairment of two wheelers which has been taken. So that is when you add M&M plus MVML, that impairment is to the extent of Rs. 347 crores. If you take and net these off, at a PBIT level, the exceptional income is Rs. 17 crores that is broadly.

Arvind Sharma: Any details on what investments were where we booked profit?

V.S. Parthasarathy: One of them is sale of Sona, Mahindra Sona shares, and the other is certain other investments that we sold, which is an inter-group transfer to the investment company.

Moderator: Thank you. Our next question is from the line of Ashish Nigam from Axis Capital.

Ashish Nigam: My question was on tractors. How has the share of financing been in tractors? How much was it before demonization and how much is it now?

Pawan Goenka: We do not have any specific data on it, but intuitively I would say that there is not a major impact that has happened and major change that has happened.

V.S. Parthasarathy: The more problem was around how the margin money, cash impacted, how the margin money will be given. And people have found both financing and non-financing solutions for it.

Ashish Nigam: We do not have a rough indication of how much is cash purchases in tractors, is there something you can share?

V.S. Parthasarathy: Very, very small. If you talk about 100% cash purchase, it was a very small percentage for tractor. I do not have a figure, but it is negligible.

Ashish Nigam: And just on a related note, you mentioned that we are 10% away from the peak of tractors in the cycle, but holistically, how do you look at tractors? Is there some kind of cycle that you believe it follows, and if so, which stage of the cycle we are in?

Pawan Goenka: Yes, there is a cycle. Normally you will see a year or two year of dip after three or four years of growth, if you go back last 15 - 20 years. And this year is sort of beginning of the growth cycle. So, unless monsoon plays a spoilsport, we should see a growth cycle in the year.

Ashish Nigam: I will just see if I can squeeze one more. Dr. Goenka, there is some confusion whether this emission norm deadline is on production or on registration, what are your thoughts on this?

Pawan Goenka: Thank you for asking that question. Some confusion is perhaps an understatement of the day at least, if not the month or the quarter. See, the regulation is very clear, there is no sort of uncertainty or vagueness on what is regulation. Regulations say that after March 31, 2017, we cannot produce BS-III vehicles. The regulation does not say that we cannot sell BS-III vehicles. In fact, we have talked to the Ministry after this confusion arose again, and Ministry has confirmed that that is the intent and that is the regulation, that is the rule of the law, and that is the law of that land. It is not first time, every time the BS emission norms have changed, it has been like that that manufacturing date is the date that determinants the end of the previous BS norm and the beginning of new BS norm. It is not only in India, every country in the world follows that. Unfortunately, confusion is being created. We are spending a lot of time running around trying to get this settled. I know it will finally get settled because the law of the land is very clear. But is it is a confusion that is being caused, and I must say it is unnecessary confusion that is being caused.

Moderator: Thank you. Our next question is from the line of Raghunandhan from Quant Capital.

Raghunandhan: Many of my questions have been answered, just one query. The gasoline models of XUV and Scorpio, earlier in one of the calls you had said, by end of FY17 for XUV and starting of FY18 for Scorpio, that stays, right sir?

Pawan Goenka: So we would be launching XUV gasoline very soon. I think it will happen next quarter, XUV. Scorpio, we will do after we see the response to XUV. But frankly, the fact is that in this segment, the customer demand still is predominantly diesel and there is very little demand for gasoline. So we will launch XUV, then we will see when we launch Scorpio. We are ready with it, but launch date we will decide.

Just going back to the previous question, I want to add one more thing. It is impossible for us to control inventory to end all the BS-III model inventory by any such date. It is not just a question of number of days of inventory, it is also aging of inventory. And you know very well that every manufacturer will have some vehicles that are aged as much as six months or more, and therefore there is no way they are going to stop sale of older emission and norms on a single day, they can only control manufacturing and cannot control sale.

Raghunandhan: Sir, just continuing on the same question, would there be any process like the dealers will have to declare their inventory to the respective RTOs and then they will be allowed to sell from April onwards?

Pawan Goenka: There is no such regulation, again. However, if the authorities see it fit, we have no problem in doing so, because it is reasonable to ensure that there is not a buildup of inventory that is being done just to be able to have a higher stock BS-III so that we get advantage post March 31. What we have assured everyone that our inventory levels at the end of March 31 will be similar to what it has been March 31 last year. And if somebody needs to audit it, we are open to it, but there is no such requirement or law as of now.

Moderator: Thank you. Ladies and Gentlemen, that was our last question. I now hand the conference over to Mr. Jhaveri for closing comments.

Mihir Jhaveri: I would like to thank the management once again, thank you all for the call.

V.S. Parthasarathy: Thank you, everyone.

Moderator: Thank you very much, Members of Management. Ladies and Gentlemen, on behalf of Emkay Global Financial Services, that concludes today's conference call. Thank you all for joining us and you may now disconnect your lines.