"Mahindra & Mahindra Q2 FY20 Earnings Conference Call"

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Moderator: Ladies and gentlemen, good day, and welcome to Mahindra & Mahindra Limited Q2 FY20 Earnings Conference Call hosted by Yes Securities Limited. As a reminder, all participant lines will be in the listen-only mode and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing * then 0 on your touchtone phone. Please note this conference is being recorded. Certain statements on this conference call with regard to our future growth prospects are forward-looking statements, which involves a number of risks and uncertainties that could cause actual results to differ materially from those in such forward-looking statements.

I now hand the conference over to Mr. Amyn Pirani from Yes Securities. Thank you and over to you, sir.

Amyn Pirani: Thank you. Good evening, everyone. I would like to welcome the management of Mahindra & Mahindra and thank them for taking out time for this call. We have with us today Dr. Pawan Goenka - Managing Director, Mr. V. S. Parthasarathy - Group CFO and Group CIO as well as other senior management, including the IR team.

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

V. S. Parthasarathy: Thank you, Amyn. On behalf of M&M Limited, I extend a very warm welcome to everyone on this call. I will share some key updates on economic environment along with financials for Q2 F '20. After my comments, Dr. Goenka will talk about overall performance of the company.

First, let me briefly talk about some macroeconomic updates. It has been a tough quarter for the global economy. As per IMF, 2019 will witness the global growth at just 3%, a drop from their previous estimate, and also as compared to 3.6% previous year. This will be the slowest rate of expansion since the 2009 recession.

China grew at 6% this quarter, down from 6.2% last quarter. The growth is expected to reach 5.5% by 2024. The U.S. is expected to grow at 2.4% in 2019, down from 2.9% in 2018 and further expected to decline to 2.1 in 2020, an election year. The global economy continues to face risks led by ongoing trade wars and geopolitical issues. Crude oil prices could see a downward bias in the coming months, as global oil inventories rise during the first half of 2020. This quarter has been challenging for India as well. But when I do a page turn on India, you'll see that the Indian economic scenario is picking up slowly.

The first highlight is the above normal rains, with monsoon 2019, ending at 110% of LPA, highest surplus in the last 25 years. Given uneven distribution and unseasonal rains in October, there might be some short-term negative, but overall, monsoon augurs well for the rural economy. High reservoir levels and good moisture content in the soil is likely to positively impact Rabi output.

Inflation remains low. CPI is estimated to continue to average at 4% in FY '20. WPIs are 0.3%, a 3-year low. Commodity prices remain range-bound amidst global slowdown. The festive season has brought some cheer. In October month, M&M had the highest ever retails in a month in automotive and highest ever deliveries (in a month) in tractors. If the momentum continues, we'll see good traction in the coming months.

Now let me share the financials for Q2 F 20 for M&M plus MVML. In a tough and turbulent environment, the domestic automotive segment de-grew by 21.5%. However, happy to share, we improved our overall market share in the auto industry. More on this will be covered shortly. In tractor, sales de-grew by 6.4%. But again, happy to share that we improved market share as compared to Q2 F '19. Net revenues of 10,935 crores, EBITDA of 1,541 crores. OPM margin at 14.1%. PBIT at 1,791 crores and PBT at 1,758 crores before EI, and PAT at 1,355 crores.

If you look at the comparison versus previous year, you will see there is a drop, but this is consequent to the volume and the revenue drop. On the income tax side, for M&M Limited, we are under process of evaluating if and when do we move to the new tax regime. The decision will be taken in due course. And hence, this quarter, it reflects the old rate of tax. In MVML Limited, we have moved to the new tax rate in this quarter, and the numbers will reflect that. There is no EI this quarter. And last year, there was an EI for 138 crores. And therefore, the comparisons will appropriately show that.

Let me quickly go to Q2 segment financials. Auto segment had a revenue of 6,893 crores, lower by 18.4% versus the previous year. The drop in EBITDA has been similar to the drop in revenue. We have maintained our OPM at 12.6%, which is similar to the previous year and is sequentially higher by 20 basis points as compared to Q1 F 20. This has been achieved through a robust cost focus and material cost management. The depreciation and amortization figures were higher due to new launches and the volume saw a contraction leading to higher D&A charge as a percentage to revenue. Accordingly, segment results at 397 crores showed a higher drop of minus 40% versus previous year 664 crores.

FES segment revenue at 3,631 crores, lower by 10% against previous years. At a segment level, the OPM for farm equipment sector was 21.3%, which is 50 bps lower, but sequentially higher by 40 bps and at 21%. You could call that it's an industry best-in-class. Segment result at 702 crores lower by 13.7% versus last year.

Now let me come to the consolidated results. At the consolidated results, our net revenue was 24,150 crores with a de-growth of 7.6% over the previous year. In terms of segment results, the consolidated PBIT was 823 crores, which is 49% drop over previous year. The degrowth at consolidated level is primarily due to loss of SYMC in this quarter. For the same reason, you would have seen a loss at the consolidated automotive segment level as well.

Now coming to key sector. Our company results, Tech M posted a profit of 1,124 crores, delivering 5.6% Y-o-Y growth. Mahindra Holidays from a loss last year turned to a profit of 24 crores this quarter. Other companies Mahindra Finance, Lifespaces and Logistics reported a healthy profit, though year-on-year, they also showed stress.

Overall, I have to summarize by saying the following. We not only held on, but marginally improved the OPM on a sequential basis in spite of the volume drop. We have shown Q-o-Q improvement in OPM since Q3 F 19, from 13.2% in Q3 F 19, 13.5% in Q4 F 19, 14% in Q1 F 20 and 14.1% this quarter. This has been possible due to benign commodity, astute cost management and margin focus. This is in spite of negative operating leverage. In other words, we are all geared and ready to excel further when the growth momentum returns. We have best-in-class margins in both automotive and tractors. We always kept financial prudence in mind. We continue to operate at negative debt equity ratio at net level. We have maintained the internal discipline throughout in terms of inventory and cash management. So while the quarter has been tough, the environment has been tough, I can dare say that our business model has been both resilient and tough.

Now I request Pawan to give his comments.

Dr. Pawan Goenka: Thank you, Partha. And I start with the last sentence that Partha has said. That if I were to summarize the quarter for Mahindra, the quarter 2, I would say that in a continued difficult industry scenario, M&M has performed reasonably well. And I hope that at the end of this call, you would come to the same conclusion. The reason we say that, that kind of covered by Partha.

Gain in auto industry market share, gross margin improvement of as much as 1.7% in auto, EBITDA 12.7% maintained; for tractor, gain of 1.5% in market share, which is a huge gain; and gross margin improved by 0.4% and just a marginal drop of 0.6% in EBITDA, still having EBITDA of almost 22% that we believe is the best in the industry. PBIT, of course, is hit hard because of lower volume, both in tractor as well as automotive. October, though we are talking primarily quarter 2, but I must mention that October has been a very pleasant month for the whole industry across almost all the companies. We have, as Partha said, highest ever retail in both auto as well as in tractor. The auto inventory is lowest ever, at both dealer point as well as plant level. And we are probably about 5,000 to 6,000 vehicles short where we would have liked to be. Tractor inventory, we are roughly at a level where we would like to be. maybe 1000-1500 further reduction will happen over the next 2, 3 months.

The overall industry scenario remains weak. In fact, in case of auto, somewhat weaker than it was in Q1. And in case of tractor, somewhat better than what it was in Q1. Economic slowdown; the rural income; the monsoon, both the good, bad and ugly; the tight credit conditions; the reported reduction not been passed on to the customer. All of these are things that carried forward from quarter 1 into quarter 2, in spite of some very good initiatives that were announced by the Finance Minister; post the budget on July 5th.

There's also a postponement of buying decision, that's happening. Earlier, there was an anticipation of GST rate cut. Now that is not there anymore. There is uncertainty over BS-VI norms. What will happen is still, in spite of clarification by the Finance Minister, still there is uncertainty in people's mind. And people kept waiting for better schemes and discounts in the month of September, for the month of October.

If I look at overall industry scenario, and you'll probably have these numbers, that the passenger vehicle is the lowest in 21 quarters. Heavy commercial vehicles is lowest in 23 quarters. First time in 15 years that 2 consecutive quarters had all segments of industry degrowing. PV drop of 29%, HCV drop of 66%, tractor degrowth of 9.8%. 3 consecutive quarters of degrowth. All of these are obviously a matter of concern as far as industry is concerned, and we are all hoping that what we saw in October is not just a 1-month thing. It will carry forward and indicate some sign of bottoming out and turning up for the better.

Now in terms of forecast going forward, it is a very dangerous game now to forecast anything. But we do think that the UV segment will probably see a positive growth in the second half because of 3 or 4 new products that have been launched, namely Seltos, Hector, Venue, XL6 coming up, Triber and all of these will help to grow the UV volume. The PV industry degrowth, therefore, will slow down in H2, from about 23% in the first half to maybe about 5% in the second half. In the CVs, we don't see much of an uptick happening from the first half, what we saw 25% degrowth probably will continue because this has to do with the loan availability, which still is not sort of going up rapidly.

In the tractor area, I had said the 0% to minus 5% in the last quarter. I will have to take it down, because we had expected the previous quarter Q2 to be minus 5% and turned out to be about minus 10%. And therefore, right now, our estimate is that we probably will be having the industry at 7% to 8% degrowth overall for the year.

EV is gaining momentum. The October month, we retailed almost 2000 vehicles, including 1,300 of e-Alfa and about 700 or 600 of Treo and about 150 of e-Verito. And I do believe that this at least was not a blip and we would expect to see a continuing growth in the volumes of all-electric vehicles that we sell. So that's sort of what I want to do as an opening statement. I'm sure you'll have a lot of questions about various things that we have not talked about and few things that we have talked about. So we should now open up for any questions.

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

Kapil Singh: Congrats on a good set of results and also improving outlook, which brings some respite. Dr. Goenka, I have 2 questions. Firstly, I want to know how you think about the UV business over the next 4 to 5 years. In the last 4-5 years, we have seen market share loss for various seasons. What is the company doing different to grow either in line with industry or ahead of industry, whatever your ambitions are? That's my first question.

Dr. Pawan Goenka: But why don't you ask the second question also.

Kapil Singh: Okay. Yes. Maybe it might be linked. So second question is on the emission side. I want to know what is your thought on BS-VI, What kind of impact will BS-VI have on the diesel mix, especially in SUVs for above 1.5 litres? And will it be advantage diesel when we move to CAFE or there are technologies like hybrid, for example, which could negate that advantage? So that's the second question.

Dr. Pawan Goenka: Okay. So frankly, I think that given how the mix of UV and passenger cars is changing, the UV market share is, in some sense, losing meaning because now UVs are one-third of the passenger vehicle and just about half of passenger cars. And if you have to remove the sort of small hatch, the UV may, in fact, be larger than passenger cars. So while, for a long time, we kept worrying about losing market share in UV, now we really look at what is happening in the passenger vehicle and where we are in the passenger vehicle. So thankfully, in passenger vehicle, YTD, 2 quarters in last year, we have an increase in market share from 7.2% to 7.8%, I think, is what we have. And as you know that every month somebody is launching a new UV, new players are coming. Just in the last 1 year, we had 2 new brands that have come into the UV segment. And if you look at the products that are lined up for launch, not just in India, but globally, predominantly, only UVs are getting launched or SUVs are getting launched. And therefore, I think we need to probably stop worrying about the UV market share and focus more on passenger vehicle market share. UV makes sense when UV was only 16%, 17%, 18% of passenger vehicle. Now perhaps it is immaterial.

The BS-IV to BS-VI, my view is not different than what I had expressed before, that 1.2 litre, that is for a compact hatchback or compact SUV like KUV100 the diesel will disappear. For 1.5, the ratio will probably reverse. Today, it maybe 60-40 in favour of diesel, it might become 60-40 in favour of petrol. And for above 1.5, I believe that in SUV or UV segment, the penetration of gasoline, probably will not be very high. It won't be zero. Those who have petrol vehicles will get 10%, 15%, 20% petrol penetration, but it will not be a 50-50 kind of number is our estimate. Having said that, as you are aware, that all new products that we will be launching, we'll have both diesel and petrol option. Because we don't know what might happen at any given point of time by regulatory restraints or because of pricing, and that shift may happen very quickly to gasoline.

If you look at globally, and since I know Korea very well, in Korea, which was like India, predominantly diesel has had a fairly quick change to gasoline. And the XUV300 size vehicle, now are almost 75%, 80% gasoline only 25%, 20% diesel. And we will have to prepare for that scenario in India, though, as you yourself pointed out that for CAFE or CO2 emission, diesel does have a distinct advantage. And at least, I don't think that even after BS-VI, without government incentive hybrid would be more cost-effective than diesel to meet CO2 requirement. I think the diesel still will continue to be advantageous, though there are companies that believe differently.

Kapil Singh: Just a follow-up. Even if you look at the PV market share, I mean, could you just highlight what are the things we are doing which are different from what has happened in the last 4, 5 years, either in terms of product cycle, will it be more stronger or product quality, which are the key areas which will help the company outperform?

Dr. Pawan Goenka: So Kapil, that's pretty clear. I mean, basically, it's all game of what product you launch at what price. And we have been fairly active in launching new products. We had 3 product launches in the last financial year, and we will have 3 product launches, these are brand new product starting fourth quarter of next year, that is first quarter of next calendar year to maybe about 5, 6 quarters. And these are nicknamed W501, W601 and Z101. Most of you have your own sort of understanding of what these mean, but I won't tell you officially what they mean. And in addition to that, we have electric vehicle portfolio coming up S110, which is electric KUV will be launched in Q4 F20 followed by what we call internally C100, which is a last mile connectivity, electric vehicle, sort of a different concept than anything which is existing today, which we will launch somewhere around second or third quarter of FY '21 followed by the S201 electric that is XUV300 electric, which will be sometime probably in second quarter, first quarter of FY '22. And then we have bunch of refreshes that are happening. So I must tell you that even though we are going to be talking more about passenger vehicle market share, but our thrust other than electric vehicle will primarily remain on utility vehicles or CUVs, SUVs, and all the products that we have in the pipeline are in CUV and SUV space.

Moderator: Thank you. We have a next question from the line of Pramod Amthe from CGS-CIMB. Please go ahead.

Pramod Amthe: Couple of questions. One, how has been the festival for LCVs? And do you see more visibility there as compared to other segments of recovery?

Dr. Pawan Goenka: Okay. So for Mahindra, pretty good, except, let me qualify that, in the SCV segment what we call small commercial vehicle segment, we have crossed 50% market share after some time, we used to be 50% 2-3 years ago. We had dipped down to about 45% or 46%, now we are back to 50%. This is segment up to 3.5 tonnes. That is including our Pick-Up, our Supro, our Jeeto in that segment, right? That's very good for us to get back to the 50% market share. Pick-Ups are doing very strongly. We had 22,000 retail in the month of October, which is the highest ever retail for Pick-Ups. And our Jeeto and Alfa is growing in volumes compared to what we had last year this quarter, and in fact constantly growing. As you probably know that we now have a different vertical within auto division to just cater to the small commercial vehicles. The LCV segment has done well for us, LCV meaning up to about 7 tonnes, where we have increased our market share now to 9.5% from what used to be about 7.5%. And in the truck segment, that is 25 tonnes and above, we are still at about 4.7%-4.8% kind of market share. But obviously, you know that industry is so depressed that the volume for all the players is very small.

Pramod Amthe: Okay, sure. And the second one is with regard to diesel moving towards BS-VI. What is your understanding in terms of fuel availability and rollout for the same? Is that a hindrance for you since you already demonstrated that you are ready with products. But considering the timelines, would it be a challenge to introduce the same before March 31?

Dr. Pawan Goenka: So this is a scenario that we have to plan for multiple things happening, okay? What is committed by oil industry is that from April 1, Pan-India, we will have BS-VI fuel, and we are talking only diesel fuel because gasoline doesn't matter. BS-VI and BS-IV, there's not much difference. What is committed in April 1, 2020, there will Pan-India diesel fuel. However, that does not help us because we cannot not be selling BS-VI vehicles before April 1; we have to become 100% BS-VI from April 1. Therefore, as the industry has been saying that we need to have diesel BS-VI fuel across India at least I would say, 6 to 8 weeks before 31st March deadline. We will start shipping BS-VI vehicles from January, we probably cannot sell it till after the fuel becomes available and we can hold stock only for 2-3 weeks. We cannot just be holding stock and dealership without selling for more than 2-3 weeks. Therefore, it becomes very important for us for a smooth transition that we get BS-VI fuel from February 1. SIAM is in dialogue with the petroleum ministry and with the oil-producing companies to see what can be done. They are well aware and sympathetic to our concern. At the same time, they are saying that technically it is very difficult for us or almost impossible for us to move it sooner than April 1. So it is kind of a no solution situation that we are in. We are hoping that there will be some kind of intervention that might be done by government of India to resolve this problem. It is a genuine problem. It's not about anybody looking for extra time or anything like that, it is a genuine problem. Everybody understands that you cannot be switching over from BS-IV to BS-VI overnight. It will have to be ramp-down and ramp-up, which requires 2 months, 3 months that kind of timeframe.

Moderator: Thank you. We have next question from the line of from Raghunandhan from Emkay Global. Please go ahead.

Raghunandhan: Sir, I just wanted to understand, any comments you can make on Jawa, how has things panned out so far? And how is the ramp-up happening?

Dr. Pawan Goenka: Before we talk about Jawa, I just want to go back to the question that Pramod had asked. And point out that almost all automakers now have made their plans on when BS-IV will stop. So it basically defined the cutoff BS-IV volume so has Mahindra, and we will now work according to that plan. Even if the demand becomes higher, it will be almost impossible for anyone to increase the number of BS-IV vehicles that we have planned, and we will work with that plan. Coming back to Jawa, I thought it will be best if we had Anupam, who is managing that business, the CLPL business to answer that question. So, we will be inviting him to come in towards the end of the call. And any other question that might come up on Jawa, he will try and answer for you.

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

Binay Singh: My question is with regard to changes in powertrain. As we move to BS-VI, for small commercial vehicle do you see are they moving away from diesel to CNG, either CNG 3 wheeler or small commercial vehicles on the CNG side?

Dr. Pawan Goenka: This was a question that we had debated very hard about a year and a half ago to know whether the cost increase, that will happen for small commercial vehicle would justify continuing with diesel engine. And we had concluded that we cannot for sure say that diesel will become out of fashion with the BS-VI. Though I must say that we have stopped production of Jeeto passenger vehicle, and the reason we have to stop production is that the safety requirements that have come into a vehicle of that size, requiring ABS, requiring airbags, which is a very low power intra-city vehicle and the BS-VI emission norm coming in would have added almost 33%-34% to the cost of the vehicle. And therefore, we decided to get out of passenger side because it was getting hit by both safety as well as emission norms. But as far as the load side is concerned, which will only have the emission norm hit, we will continue with that. Right now, we don't know for sure how the demand will change because the cost impact will be significant, because of the cost increase on a very small base. And therefore, we are preparing for other scenarios if diesel goes down, but we are not stopping diesel at least now.

Binay Singh: And what are these other scenarios?

Dr. Pawan Goenka: Meaning petrol, CNG and even electric. Like for example in three-wheeler, it is my belief that within 2 to 3 years, you would see most three-wheelers become electric. And we obviously have a very strong presence in electric 3-wheeler with Treo as well as with e-Alfa Mini.

Binay Singh: On the electric 3-wheeler side, like if you see cost of running for electric is quite compelling versus CNG. But at the same time, we have seen a very rapid CNG network expansion across India happening. So how do you see in that context because CNG availability will also rise a lot. So, do you see that like this electrification of 3-wheeler may not happen because CNG will became very widely available?

Dr. Pawan Goenka: No, I don't think that will happen. It's possible that CNG and electric will coexist. But I cannot see electric not happening.

Binay Singh: So, these 2,000, like 1,800 electric 3-wheelers that you sold in October, are these mainly sold in metros? Because this is the marketplace where CNG is already available. Just to get an idea.

Dr. Pawan Goenka: The primary markets for these are, I may not have all the markets in the mind, but primary markets for these are Delhi, Lucknow, Patna, Kolkata. So basically, North belt and East belt, up to Kolkata. So those are the primary markets. These are metros. These are not non-metros where they are getting sold. And I do not know how the CNG availability is in all these markets. Delhi, of course, is very big. I think Kolkata also has good CNG. But I don't know whether Lucknow and Patna also have good CNG. So, it is not like CNG versus electric. The operators probably are finding that electric works quite well and many of them are moving to electric.

Moderator: Thank you. We have a next question from the line of Joseph George from IIFL. Please go ahead.

Joseph George: My first question was in relation to the discounting in the Diwali period. Could you give us a sense of how it was compared to last year Diwali and the entire festive? And related question is whether that had continued post Diwali? I think related to that is also whether there was aggressive financing during that festive season and whether that has continued post Diwali?

Dr. Pawan Goenka: Just a little addition to the previous question that in our case, we have electric, we have diesel and we have CNG. So, we are covering 3 bases, and we will have to prepare ourselves for any business. In fact that is what is making a little difficult for all automakers, because what will pan out 3, 4, 5 years from now is anybody's guess. And almost everyone is prepared for all scenarios, all multiple scenarios to ensure that they are not left high and dry. Coming back to discounting during festive season, in case of Mahindra, if you look sequentially, that is from Q1 towards the end of Q2, we probably had about Rs. 3,000 to Rs. 4,000 more per vehicle in discounting. And if you look at year-on-year, it's only about Rs. 1,000- Rs. 1,500 more than last year Diwali. So, we have not really gone overboard in discounting and that you will see from the maintaining gross margin that we talked about earlier, in fact, improving gross margin. If we had done heavy discounting that wouldn't have been possible. I cannot speak for the industry, you would probably have the data better than I do, but this is what it is for Mahindra. As far as finance rate is concerned, Mahindra has worked with financiers during the Diwali season, Diwali and Navaratri both, to have good aggressive schemes. But we have not done any major subvention of financiers to get those schemes because financiers also probably had little bit of room available with the repo rates going down, which have not yet been passed on. So, I think in the Diwali season, they have opened that up and passed on that benefit to the consumer. I do not know if that is continuing into November. But I do know that discounts have been withdrawn to some extent, back to what normally it is in November. And as you know very well that in December, they come back because of year end. So, November, probably, the low discount season and December will probably again be high discount season. Now again, each automaker will make their own call on what they want to do. But at least temporarily, all the heavy discounts that were there for festive season have been withdrawn.

Joseph George: Okay, just a continuation of that, when the commentary from various OEMs came in during these result season, the sense we got was all of them saw good Y-o-Y growth on a like-to-like basis in the festive season. I think the commentary from you was also similar. But do you share any enthusiasm in terms of that growth or that positivity continuing in the coming months? Or do you think there was some amount of bunching up of sales in the festive season because of discounts, because of financing etc. which may not give you the confidence to say that there's a full turnaround in the industry?

Dr. Pawan Goenka: So, there's certainly an optimist in me who thinks that this is the beginning of the up cycle, and therefore, we should see a positivity going forward. Now having put the optimist aside and I will start looking at data and rationalize the data, October had at least 2 reasons for very good retail. One is that bunching up of the festive season, both the Navaratri and Diwali, the 5 days of Diwali and 8 out of 10 days of Navaratri were in October, which very rarely happens to get so many festive days in one month. And therefore, the increase in retail was partly because of that, partly because of heavy discounting that has been done by many players in the industry, and partly also because, I think, finally, it is dawning up on people that BS-VI will mean heavy price. And therefore, we might as well buy BS-IV and might as well do it when the discounts are high in a Diwali season and not wait for last quarter. Then in the last quarter, depending on the stock that manufacturers have, discounts may totally disappear. And I think that is also helping. So, this portion, this last item will continue probably till 31st March. But the first and second was a specific thing for the month of October. Now when I talk to our sales people, both in the auto and tractor side, auto people do think that there will be better 5 months than what they had thought on 1st of October, okay? And therefore, they have slightly improved their forecast for these 5 months. That is under certain Mahindra auto people. Mahindra tractor people think that what we have seen in this month may spill over a little bit in November because of flood situation in many parts of the country, and therefore, deferment of purchase and also because the harvest being late, and therefore, the farmers' income being late. And therefore, we'll probably see some uptick in the month of November. But December, January will be slow as it normally is. And then there is a very good optimism about February and March. So that's what we need to watch out now. Somewhat mediocre November, I'm talking tractor now, slow December and January, and very good February and March.

Joseph George: That's very helpful. And just lastly, if I could have a couple of questions to the Jawa question bank and it's addressed later, one, whether you have already ramped up to the 5,000 per month number that was indicated earlier. And second, some color on the upcoming launches, please?

Dr. Pawan Goenka: First one, I can answer, yes. Second one, we'll wait for Anupam to come.

Moderator: Thank you. We have a next question from the line of Gunjan Prithyani from JP Morgan. Please go ahead.

Gunjan Prithyani: Just 2 questions from my side. Firstly, on the SsangYong, I recall you, you guys had mentioned that we are looking at some of the cost controls. But if I look at the SsangYong performance, I think the losses have further widened there. Could you provide some insights as to how we should think about SsangYong because markets still there is pressured and seeing high competitive intensity?

Dr. Pawan Goenka: Yes. So, let me take a little time on the whole SsangYong situation because I think it will be on minds of many of you. So there has been a significant sudden change in SsangYong's performance in the last 2 quarters. If I go to first quarter there on calendar year, first quarter of 2019 calendar year, they did very well. The losses were lower, our margins were better. And we were expecting that this year may, in fact, turn out to be a profitable year. But the next 2 quarters, that is April quarter and July quarter have been very challenging for the company. And there are many reasons why that has happened. First is that, overall, the economic slowdown and the resultant slowdown in global automotive industry has affected many of the export markets of SsangYong, some because of just the economic situation and some because of various extraneous circumstances. For example, Iran, because of sanctions, we had to stop; Egypt because of an FTA with Europe, SsangYong exports became expensive; Western Europe because of very heavy CO2 penalty that is getting imposed became very expensive. So those are the reasons on export. On the Korean side, the Korean industry has slowed down, automotive industry has slowed down. Even though, in 9 months, still SsangYong has managed to outdo the market slightly, okay? And as a result of slowdown as it happens everywhere, it's happening in India, the variable expenses that is cost of selling has gone up substantially. And then in Korean market, I mentioned that earlier also, there's a very sudden shift that has happened in the gasoline-diesel ratio. So that has also made an impact because SsangYong, like Mahindra, is more diesel-dominated than gasoline-dominated. But though they now have, just like Mahindra, new gasoline engines that are getting launched. And finally, I would say that the overall result of this on the total cost base has been significant and because leveraging is very high. The D&A in case of SsangYong is significantly high with the higher development cost that we have there. So that's the current scenario. Now the question is, what happens in future? What happens going forward, how do we correct it? There are a bunch of things that we are doing right now. The biggest bucket of that is obviously material cost reduction and the team there is working very hard to see how we will be able to knock out maybe 2%, 3%, 4% out of material cost. And then we also need to see avenues of getting new volume in export market. And again, there are many possible markets that are being right now explored to try and try and get that. So the team is working hard on turning around the volume scenario that we have. And on that basis, getting back to, let's say, profitability or if not profitability, at least, 2 digit kind of loss rather than 3 digit kind of loss.

Gunjan Prithyani: Okay. So, if I look at the last 9 months or the 3 quarters, you said that the losses have been closer to about, I think, 1,100 crores. So, this should substantially come down according to you with these initiatives which are underway if I look at next year.

Dr. Pawan Goenka: No, I don't think that happens in fourth quarter or that is the quarter starting now, but we should start seeing some positive outcome of that starting next quarter, that is January quarter and then April quarter.

Gunjan Prithyani: Okay. And on the farm-subs, I see that at least we are not seeing those substantial losses that we saw in last couple of quarters. So, is that something which is now stabilized and all those one-off inventory related write-offs that we've taken in U.S. tractor, that is behind, right?

Dr. Pawan Goenka: Yes, you're absolutely right. As we had said, I think 3 calls ago that we had a significant onetime inventory correction that we had done. And if I look at this year compared to last year, we have increased retail volume. We have increased our market share. We have increased our billing volume, and we have significantly reduced dealer stock, in fact, lower than what we had planned in terms of dealer stock right now. And so this year, as I had said last time also, that time also, this year is a year of kind of getting back on our feet after significant onetime pricing that we had done, and we will stabilize, and then we probably will have a turnaround year next year.

Gunjan Prithyani: Okay. And just last question on tractors. You did mention that at least Rabi crop outlook is looking good and there is at least optimism in the industry. Would you be able to share any outlook for next year, at least even if let's assume the monsoon, we don't know about next year, but water reservoir levels are reasonably in good shape. So, is it fair to say that the industry can turn into positive growth next year as per your assessment at the moment?

Dr. Pawan Goenka: It's very early for me to make a comment on next year. Normally, we do that assessment at the end of third quarter, the beginning of fourth quarter, when we start getting the first level of monsoon forecast. But as you have pointed out, that next year, probably monsoon will not be a very big factor because we have very good soil conditions going in, very good reservoirs going in and, therefore, monsoon probably will not be a very big factor next year. And if I was forced to make a guess today, I would say that the next year would be a positive year. But I cannot say anything more than that for the time being. I think in the next call, we probably will have better view on some kind of number that I can give you as to what the growth would be.

V. S. Parthasarathy: Just one question that you had asked, which is around, you said about 1100 crores of SsangYong. I think if you look at Q1 PAT, it was about 300 crores slightly more, 307 or something. Q2 was about 600 crores, yes. So Q2 is higher than Q1, but it is in that range. And PBIT, which goes into segment results have similar figures, yes. So, 300 and 600 for Q1 and Q2 cumulatively.

Gunjan Prithyani: So, I was going at calendar year, but no worries, I got the numbers.

Moderator: Thank you. We have next question from line of Jinesh Gandhi from Motilal Oswal. Please go ahead.

Jinesh Gandhi: My question pertains to the gross margin improvement that you've seen in this quarter. What are the key drivers for that? I missed your explanation.

Dr. Pawan Goenka: So, 3 things that contributed to it. The biggest contributor was the commodity price benefit that we got. And commodity prices, I don't have precise number with me, but they dropped more than 1% during the quarter. So that's number one. Number two is the selling price increase. We did take and the industry took a selling price increase during the 2 quarter, I don't know precisely the exact timing. But during the 2 quarters, we have taken as much as, I think, about 1% price increase in that 1 quarter. And about 1% commodity price reduction. So that certainly has helped us tremendously. And then after that, the model mix was more favorable in terms of profit margin, and that has also added. The 3 factors together has given us the 1.7% increase that we talked about. And in terms of tractor, similar thing. We had a price increase. We had a reduction in material costs, and that has then led to the increase that we talked about.

V. S. Parthasarathy: And you're talking about EBITDA margins or gross margins?

Jinesh Gandhi: Gross margins.

Dr. Pawan Goenka: But the important thing is that if you go below gross margins and look at the details that we have shared, you will find that our fixed cost even in absolute terms is lower than last year. And that has really been a remarkable effort put in by the team because of the low volume to really watch the fixed cost and keep it below last year in fixed term level or in fixed cost level is something that has therefore helped. Otherwise, on percentage, our fixed costs would have been much higher than what it is now. Since we have 20% degrowth in revenue, the fixed cost percentage goes up automatically.

Jinesh Gandhi: Sure. Second question pertains to the festive season where we have seen highest ever retails. But any sense on how much the UV segment grew festive to festive and in tractors, a similar growth number?

Dr. Pawan Goenka: I think tractor festive to festive was about the same, give or take 2% up or down, about the same. Tractors, I think it's roughly the same as last year festive season. In the automotive, if I look at September, October together, I think there's a retail growth of about 20%. You see, we can't even compare right now because we have to look at up to November, up to last year Diwali. Okay, there are various numbers being shown to me, so I would rather not answer. We'll try and work that out precisely. And if it's done before the end of the call, I will come back and tell you that..

Moderator: Thank you. We have next question from the line of Priya Ranjan from Antique Stock Broking. Please go ahead.

Priya Ranjan: One is on, there is a lot of talk also on the emission-based GST rate. So, what's your thought on that? And is it feasible, given the context?

Dr. Pawan Goenka: Well, there are lots of talks and lots of such things. So, I don't think that we should even worry about that. Let something come in draft notifications, then only we will talk about. There are talks about fuel efficiency-based GST, talks about emission-based GST, talks about rate-based GST. So, I would not put too much sort of thrust on that for the time being.

Priya Ranjan: So, do you see that the current level of GST or the current way of measuring GST is going to change in some other form?

Dr. Pawan Goenka: It's always very risky and disruptive to change the way of imposing GST. And the reason I say that, it takes industry several years to align to that. And if something is done arbitrarily, then it suddenly creates winners and losers because of that decision. The sub-4 meter that came in India and 1.5 litre and 1.2 litre that came in India many years ago, I don't know, 7 years, 8 years ago, at that time, there were no 1.5 litre engines. And the whole industry has now developed 1.5 litre diesel engine and a 1.2 petrol engine. And everybody is now doing 3,995 millimetre cars. It will be very unfair that suddenly we have a very different way of measuring GST because all the investments that have been made to align with the law of the land will be out of the window. So, while the GST rates could be changed, I think the method of imposing GST, in my view, should remain the same. It's not a question of whether I agree with one way or agree with a different way. It's just a matter of that we have enough substance happening, enough things changing constantly. Let's not change the way we measure or the way we impose GST.

Priya Ranjan: The second question is on the UV side. So, we are already at around 34%-35% of the overall passenger vehicle market. So, do you see that like in Europe and other geographies, so are we moving towards 50%-60% of the market?

Dr. Pawan Goenka: I don't know about 50%-60%, but we certainly are moving towards, still we have not stabilized. What I mean by that is still I see the UV growth to be higher than passenger vehicle growth. And therefore, the UV segment or UV share will continue to go up.

Priya Ranjan: But I mean, just coming back to your own assessment of around 5% degrowth for entire industry, so how much you have considered, say, normal UV growth and the others?

Dr. Pawan Goenka: I think I mentioned or I may not have mentioned that we expect for the second half, the UVs to be in the positive territory and passenger cars to continue to be in negative territory. And therefore, in the second half, again, the ratio of UVs to passenger cars will go up.

Priya Ranjan: So I mean, do you see yourself in some advantageous situation going ahead based on that?

Dr. Pawan Goenka: As I mentioned to you earlier that the UV passenger car distinction now has become less meaningful. And we really look more at passenger vehicle as a segment and not UV as a segment. Of course, all our products are UV products. And therefore, when there is more demand for UV or more preference for UV, that's good for us. But at the same time, all new launches are UV launches also. So, competition also is going up in this UV segment.

Moderator: Thank you. We have next question from the line of Sonal Gupta from UBS. Please go ahead.

Sonal Gupta: Sir, just continuing on that question. I mean like you've said like you expect second half passenger vehicle growth to be a decline of only 5%. This is, I mean, in context of if you look at obviously on wholesale terms, industry still has seen October to be negative, right? And you do have the BS-VI transition where you're saying that it's not possible to stock a lot of BS-VI into the dealers. So, should you see the underlying retail improving so much that you will be only at minus 5% for second half?

Dr. Pawan Goenka: I said the PV will be lower than last year. What I've said is the UV will grow. Did I put a number? Okay. So, I said minus 5%. Look, frankly, to pin down a number right now for industry growth - degrowth is very hard to do. And directionally, what I can say is that UVs will be positive. Passenger car will probably be similar to what it was in the first half. Therefore, overall, PVs, passenger vehicles, will be better, it is minus 5%. Whether it will add up to minus 5% or not, I will have do the math once again. And I cannot really say a specific number. There are too many unknowns, too many uncertainties, therefore, impossible to pin down a number. I'll go back to the question that you asked about the retail growth. So, in tractor, retail was about degrowth actually, degrowth of a little over 4%. And in automotive, there was a 23% growth in retail last season to this season. Now keep in mind that the reason auto industry was in such a huge jam for the last 12-13 months was because of last Diwali. Last festive season, there was a sudden drop in retail. And that's the reason everybody having built and sits on retail, normal retail had excess inventory. And it's taken almost up to this month, October month to come back to where the inventory should be. And going into November now, almost every player barring 1 or 2 is very comfortable in terms of where the inventory levels are. And therefore, the retail growth of

23%, just shows that we are probably back to the normal festive season from a very bad festive season that we had last year.

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

Dr. Pawan Goenka: And one more thing before Chirag comes in that our estimate is that the industry has grown about 14% or 15% in auto in retail.

Chirag Shah: I have one question on cash flow. If I look at the half yearly cash flow statement, September operating cash flow seems to be far lower than what, so is there a seasonality involved in? Or is there anything specific into it?

V. S. Parthasarathy: You are talking about standalone or consolidated?

Chirag Shah: M&M plus MVML?

V. S. Parthasarathy: M&M plus MVML, right?

Chirag Shah: Around 145 crores.

V. S. Parthasarathy: Yes. So, I think you're right. There is a seasonality involved in it. We were in September, this is still September? Yes. So, we have taken into account that we are building up for season. October end, this would have come down majorly than you will see in Q3 the cash flow normalizing. There is a second reason for the abnormality because the production cut happens along with the demand cut, so that tail end impacts faster the creditor, so we would have much less creditors than we normally have. That would also again normalize when it comes to end of next quarter. So, these 2 things would drive this up. And I would tend to see that there are a little bit higher capital requirement this year as compared to previous because many of the government schemes under which we sold vehicles and tractors also the cash flow coming in slightly lower. But we hope by Q3, you'll see in Q4, so you will do 2 things. Q3, we will report back on this issue specifically, Chirag on a qualitative basis, and Q4, you'll see the cash flow. Yes, but I think it will normalize.

Chirag Shah: And just one question, if I can squeeze, on SsangYong. So, if you look since we have acquired SsangYong, we have been going through phases of profits, losses, profit, losses, how do we look at a business like SsangYong, which is, in a sense, a low growth economy in that sense. Is this a normalized trend that, in up cycles, you will see profit, and in down cycles, you will see losses. Is this a normal way of looking at business?

Dr. Pawan Goenka: That should not be. But see, frankly, it comes down to the stabilized volume that we can get through. And I have said this before in some call that SsangYong needs a volume of approximately 140,000 vehicles to be at the EBITDA positive level and a volume of about 155,000 to be PBT positive. Right now, we are short of that in this year. We were roughly about 143 or 144 last year, so we were EBITDA positive and PBT negative. And if you're able to get to 155 which will require us to grow export because in domestic market, we are at about 105 or thereabouts. And given where the Korean market is, to go substantially higher than 105 is going to be very difficult. And maybe 105 can become 110, 112, but that's about it. We will have to focus on export market and get roughly 40,000-42,000 volume from export for us to become PBT positive. Once we reach that level, then we can be consistently PBT positive. And to get that, we need to develop a couple of very good markets, and we are working on that. And if we get couple of good markets with consistent, 8,000-10,000 volume to us, then we would be in good shape. Before Anupam comes in just going back to that minus 5%, so this is based on a calculation of about 10%, growth in UV in the second half and about 12%, 13% degrowth in passenger car in the second half and taking a 2:1 ratio passenger car and UVs which will lead to a minus 5% for passenger vehicle.

Moderator: Thank you. So, we have next question from the line of Kumar Rakesh from BNP Paribas. Please go ahead.

Kumar Rakesh: I had only one question to Dr. Goenka. I want you to pick your brain on how you're planning to meet the emission challenges on 2 fronts. I understand there's push and pull, one coming from the BS-VI which can potentially reduce your diesel mix? And the second coming from CAFE norm which would need a higher diesel mix to reduce your CO2 emission. What I understand, that your response is to move swiftly towards electric vehicles over the next 2-3 years before the much tougher CAFE norm kicks in from FY23. Would that imply you're your overall profitability of the automotive division at least will start coming down as you shift towards more electric powertrain to balance these two emission norms. And is my understanding of your response to these 2 emission norms correct?

Dr. Pawan Goenka: So, this is not a simple question to answer though you have partly answered yourself that, yes, I believe that the way to meet CAFE norm in my belief will be electric. Though there are many who will say that the way to meet the CAFE norm will be hybrid. So, they are 2 different camps, as you know we have. Now on electric, if I was to go with the profitability that we have today, then your conclusion is correct that it will have an impact. But this is not the profitability that we would have once the electric volume becomes reasonable. Right now, as I said earlier that we are selling 150 or so of E-Veritos. Now if you're going to sell 150 vehicles a month, then obviously, you're going to have very heavy cost. But if we get to selling say 2,000, 2,500, 3,000 E-Veritos, that will have a significant impact on reducing cost. So, in terms of making the electric vehicles viable for the consumer, we don't need to go too much lower than where we are, maybe 5% lower cost, 10% lower cost will be sufficient. In terms of making it fully profitable for us, we will have to reduce costs further which will happen automatically partly because of the battery cost going down with time and partly because of overall cost going down when volumes go up.

Kumar Rakesh: Understood. So, it's a long process. Over next 2-3 years, gradually we'll move to that level. But during that transition, we could see some impact…..

Dr. Pawan Goenka: Well, see, I don't think so because, as I mentioned earlier, that for most of the vehicles that we have, our large portfolio will probably remain largely diesel for the short to medium term. And also keep in mind that the IC engine technology both for gasoline and diesel is not standstill. Every new generation of engine that we do has a higher fuel efficiency than in the previous generation engine and as I have already mentioned that we are doing a completely new range of engine, 2 litre and 2.2 litre gasoline and diesel which will be more fuel efficient, therefore, lower CO2 than the engine that we will replace.

Moderator: Thank you, sir. We have the last question from the line of Sahil Kedia from Bank of America. Please go ahead.

Sahil Kedia: I have a quick question. Can you help us understand that in the automotive margins, how much is the loss coming from the truck losses because we can see that you guys are doing a lot of cost reduction. But how do we quantify the loss on the truck side, considering how the volumes have come off so much? And also if you can give an update on the MVML merger, please?

V. S. Parthasarathy: So, we've been talking to you about truck that our MTBD what was earlier called is moving through EBITDA breakeven and then will be completely breakeven. This was all predicated on a normal curve of the volume growth within industry which fell more than 50%. And in some segments even as high as 70% reduction in volumes. This has taken a slightly backseat. I think we will wait for one more quarter for it to normalize. I think according to every segment where we are planning cost reduction and by the way, the 12.7% EBITDA margin of auto sector includes MTBD and includes the truck. And therefore, it's factored into the EBITDA margin which is same as last year. And as I told you, best-in-class for the industry. However, if you look at MTBD separately, I think we are where we were, yes, close to EBITDA breakeven, but still quite not there, yes?

Sahil Kedia: So, the losses you're saying have not widened on year-on-year despite the fact that the industry volumes have come off so much because...

V. S. Parthasarathy: Losses have not widened or narrowed. I would say we still are on the path to EBITDA breakeven, okay?

Sahil Kedia: Partha, sir, if we could request for you to give a little bit more granular color on this.

V. S. Parthasarathy: I'll do

Dr. Pawan Goenka: Anupam, 2 questions for you on Jawa. One is how is Jawa doing, general question. And second is what is the product pipeline?

Anupam Thareja: Sure. I think it is a general question, how is Jawa doing. I said I am just going to give a quick update from the past to right now and then we can take it from there. So I think as all of you might remember or recall that we showed our engine September '18, launched the bike in November 15 last year. We closed the booking on 25. I think we had 2x the number which we had in our business plan, but we estimated the ramp up, we estimated the general requirement and we gave a 9-month period. After November, we went on unreasonable almost an audacious plan of launching 100 dealers in 100 days in 83 cities. By March, we completed that. We had 103 dealers in 83 cities. We started delivering bikes in April. We gave a few hundred for test rides, for meet the rides, for regulatory approvals and few to the customer. May onwards, we started ramping it up. As promised, we delivered all the online bookings by September 19. Though I must admit that we were a little delayed on our dual channel and the reason for that is dual was introduced or agreed to be introduced midway, given the customer demand. Also, I am happy to tell that by end of October, by Diwali we completed all the dual demand which was promised before the online booking was closed. And today, some models, we are delivering as in December last year. In terms of production and production ramp-up, I think we are very happy the way it's actually it is shaping up. There were a few hiccups from the part side. I think we are pretty much over that. Now, I think we have stabilized our model variant colors. And I think we would be able to deliver bikes faster than we were and the customers are happy. In terms of our future, we have access to 3 brands, we have Jawa, we have Yezdi, and BSA. Given the fact that the demand was higher than what we expected, we decided to delay the launch of Perak which we already showed on November 15, because I think our response mainly was to fulfill the demand which was slightly ahead or rather ahead of our expectation. As you can see, we had planned lower, the demand was higher. But given the fact that we had to satisfy the customers, we are focusing on delivering that. But very soon, we will have launches in the other categories. We are in the classic categories. Here the number of models is not important. It's actually how we can create the buzz around currently what we have. That answers the questions which were asked. Anything else or Pawan how do you want to take it?

Pawan Goenka: Thank you, Anupam. So, I think we have concluded.

Sriram Ramachandran : So thanks a lot for everyone participating in this call. And so with this, I hand it over back to Amyn. Amyn, back to you.

Amyn Pirani: Thank you to the management for taking out time for the call, and thanks a lot to all the participants for coming on the call. Moderator, we can now end the call.

Moderator: Thank you very much, sir. Ladies and gentlemen, on behalf of Yes Securities, that concludes this conference call. Thank you for joining with us, and you may now disconnect your lines.