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The Listing Department,
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Bandra (East), Mumbai-400051.
NSE Symbol: VARROC

The Manager – Listing
The Corporate Relation Department,
BSE Limited
Phiroze Jeejeebhoy Towers,
Dalal Street, Fort,
Mumbai-400 001.
BSE Security Code: 541578
[Debt: 975062]

Sub: Transcript of Investor / Conference Call pertaining to Unaudited Financial Results for the quarter and half year ended on September 30, 2024

Dear Sir/Madam,

Please find Transcript of Investors / Conference Call held on Wednesday, November 13, 2024, in respect of the Un-audited Financial Results for the quarter and half year ended on September 30, 2024.

This is for your information and records.

For Varroc Engineering Limited

Ajay Kumar Sharma

Digitally signed by Ajay Kumar Sharma
Date: 2024.11.18 21:13:51 +05'30'

Ajay Sharma
Group General Counsel and Company Secretary

Encl: a/a

"Varroc Engineering Limited
Q2 and H1 FY '25 Earnings Conference Call"
November 13, 2024

DHRUV JAIN: **MR. TARANG JAIN – CHAIRMAN AND MANAGING DIRECTOR – VARROC ENGINEERING LIMITED**
MR. ARJUN JAIN– WHOLE-TIME DIRECTOR AND CHIEF EXECUTIVE OFFICER BUSINESS-I –VARROC ENGINEERING LIMITED
MR. DHRUV JAIN – WHOLE-TIME DIRECTOR AND CHIEF EXECUTIVE OFFICER OF BUSINESS II –VARROC ENGINEERING LIMITED
MR. K MAHENDRA KUMAR – GROUP CHIEF FINANCIAL OFFICER –VARROC ENGINEERING LIMITED
MR. BIKASH DUGAR – HEAD INVESTOR RELATIONS AND FINANCE CONTROLLER BUSINESS-II–VARROC ENGINEERING LIMITED

MODERATOR: MR. ADITYA JHAWAR – INVESTEC

Moderator: Ladies and gentlemen, good day, and welcome to Q2 and H1 FY '25 Earnings Conference Call of Varroc Engineering Limited hosted by Investec Capital 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 after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing star then zero on your touch-tone phone. Please note that this conference is being recorded.

I now hand the conference over to Mr. Aditya Jhawar from Investec. Thank you, and over to you.

Aditya Jhawar: Yes. Thank you. Good evening to you all. From Varroc Engineering, we have with us Mr. Tarang Jain, Chairman and Managing Director; Mr. Arjun Jain, Whole-Time Director and CEO of BD1; Mr. Dhruv Jain, Whole-Time Director and CEO of Business Unit II; Mr. Mahendra Kumar, Group CFO; and Mr. Bikash Dugar, Head, Investor Relations and Finance Controller of Business-II

We'll start with the call with a brief opening comments from the management followed by Q&A session. I would now like to invite Mr. Tarang Jain for the opening remarks. Thank you, and over to you, Tarang.

Tarang Jain: Thank you, Aditya, and thank you, team Investec for hosting the call, and a good evening to everyone who has joined the call. To start with the India GDP growth for Q1 of FY '25 was at 6.7%. This was lower than the earlier projections given by the RBI and lower than the growth levels of the previous few quarters. While urban consumption is down, rural consumption has been improving during the financial year, which also reflected in the good growth seen in the 2-wheeler industry.

During Q2 of FY '25, the 2-wheeler and 3-wheeler segments registered good growth; however, the passenger cars and the commercial vehicles remain challenged on a year-on-year basis. 2-wheelers grew by 12.5%, 3-wheelers grew by 6.3%, passenger vehicles de-grew by 0.7% and the commercial vehicles de-grew by 13.3%. However, on a quarter-on-quarter basis, we saw a growth in almost all segments other than commercial vehicles due to the early festive season. The 2-wheelers grew here by 6.8%, 3-wheelers grew by 29.3%, passenger vehicles grew by 5.7% and the commercial vehicles de-grew by 5.2%.

De-stocking by dealers before Euro V plus and lack of growth driven by lower consumption is impacting the European and the American 2-wheeler market. In the ASEAN region, the growth was largely driven by low-end segments and the premium segment continues to struggle for growth in this region.

During quarter 2 of FY '25, the company has registered a revenue of INR20,808 million with a growth of 10.3% year-on-year. The India business reported a growth of 13.4%. The profit before tax of the company was at 4.4% for quarter 2 FY '25 due to the positive operating leverage seen in the India operations. The consolidated profitability remains impacted by de-growth in the overseas businesses, R&D spending and overseas operations for future growth.

On a quarter-on-quarter basis, the company reported improvement all around. The revenue on quarter-on-quarter grew by 9.6%. The EBITDA margin improved by 60 basis points and the PBT margin by 150 basis points. The company's balance sheet continues to strengthen along with improvements in the return ratios. The net debt of the company in H1 FY '25 reduced by INR1,554 million and net debt to equity has reduced to 0.5x at the end of H1 FY '25 from 0.64x at the end of FY '24.

The absolute net debt figure is INR8,273 million. The annualized return on capital employed at the end of H1 FY '25 stood at 19%. The capex spend in H1 FY'25 was INR1,030 million. The capex spending in H2 FY '25 will increase, driven by the need for additional SMT lines for electronics and the increased EV capacity needed.

We are also investing in land in southern and western part of India for future growth. As indicated earlier, we are working on various initiatives to drive cost reductions across several categories of costs with special focus on fixed costs. Some of these measures have already started showing impact on our bottom line, but most of them will fully get reflected by Q4 of FY '25.

We have also rationalized headcount levels across businesses and functions. We continue to look at avenues to make the organization more lean, nimble, and agile and to increase speed in decision-making.

The order book for H1 FY '25 continues to remain healthy, and we continue to build the order book in both India and the overseas business. In H1 FY '25, we have achieved net new business wins with annualized peak revenues of INR6,046 million. The order book from EV models constitutes more than 37% of these wins. In the first half, we added various new-age technological advanced product portfolios in our business. We started the production of integrated starter generator and soft-touch door panels for Mahindra, whereas we won business for battery management systems for electric vehicles, thus further increasing our content in the electric vehicle space. We also won business for interior ambient lighting from a global player, which helps in increasing our offering for 4-wheeler vehicles.

We will continue to innovate by further strengthening our engineering capabilities streamlining our operations to further cost reductions and working capital optimization. Our endeavour will remain to expand our presence through focused products to drive sustainable growth and deliver value to our shareholders.

Beyond business, we continue to focus on various ESG aspects to make the organization more sustainable. We have published our first sustainability report, which can be accessed on our website. Our efforts towards giving back to society is also being recognized. The Kham River restoration in Aurangabad was recognized by the WRI Ross Centre for Sustainable Cities as 1 of the top 5 finalists globally for their prestigious award. This project also received globally recognized prestigious award that is The St. Andrews Prize for the Environment.

With this, I will now ask MK, our Group CFO, to walk you through the presentation and give more insights into the financial performance. We've uploaded the investor presentation to the stock exchanges as well as on the website. Over to you.

Mahendra Kumar: Thank you, Tarang. Good evening, everybody. Let me take you through the highlights. Most of these points have been highlighted by our Chairman already. Basically, we had a revenue growth of 10.3% in Q2, but India business registered a strong growth of 13.4%. Profitability was at 4.4% at PBT level during Q2 versus 3.9% last year. EBITDA came in at 9.7%, marginally lower from 9.9%, which you saw last year.

The net debt reduction journey continues. So we brought it down to INR827 crores now by end of last quarter. In terms of lifetime orders, the cumulative H1 FY '25 lifetime orders were INR32.5 billion, which has the potential of annual peak revenue of INR6 billion. And more than 37% of this business is related to the EV vehicles.

The other highlights, of course, our Chairman covered already. I just want to bring your attention to the new products, which we listed out here. These are the 4 new products which we are working on, and which are going to give us the future growth potential, which is basically the interior ambient lighting, soft door touch panel, battery management system and ISG, which is integrated starter generator.

Going to the next slide, which is about the industry trend. We really see the trend by segment. Year-over-year, 2-wheeler grew by 12.5% during second quarter. Three-wheeler also registered a growth of single digit, 6.3%. Passenger vehicles and commercial vehicles had a de-growth. Passenger vehicle de-grew by 0.7% and a commercial vehicle by 13.3%.

However, on a quarter-over-quarter basis, 2-wheelers grew by close to 7%, 6.8%; 3-wheeler by strong 29.3%; passenger vehicle grew by about 5.7% and commercial vehicle had a de-growth. EV 2-wheeler volumes on quarter-over-quarter grew by almost 74%. So those are the highlights. In terms of H1, again, 2-wheelers grew by about 15.8%, 3-wheeler by 7.6%, passenger vehicle by 2.4%.

Coming to the financials. The 10.3% growth in top line we talked about already. So this resulted in a 4.4% PBT for us. Our Indian operations, of course, grew by 13.4%. The profitability, of course, registered a significant growth compared to sequential quarter compared to Q1, the PBT went up by 62% and compared to the same period last year, the PBT went up by about 23%.

So these are the significant growth numbers which we could see in the profit level. And if you really look at the H1 in total, all of you know that in Q1, we had some challenges in terms of the overall growth. So H1 growth came in at about 7.8%, PBT at 3.7%, more or less similar to what it was last year. Indian operations in total, of course, grew by about 12.4%. On the next slide, we talk about the consolidated ratio on the balance sheet numbers. The net debt came down to INR827 crores, equity of INR1,640 crores. Some of you may remember that about 2 years ago after the divestment, it was the other way, we had debt of close to INR1,500-plus crores. So, it actually now shifted the other way. So that's a significant development. Net debt to equity is now very comfortable at 0.5%. Net debt to EBITDA is at 1.11% based on the annualized EBITDA level. The return on capital employed is also strong at around 19%.

The next slide, we gave the revenue breakdown. We gave the breakup by business unit and also by segment and customer and geography. By segment, if you really, 75% comes now -- comes from 2-wheelers and 3-wheelers now. And India's revenue is close to about 88% of the total. Bajaj revenue, of course, strengthened from 40.6% to 45.3%, mainly because of the increase in EV business.

On the new lifetime order win, of course, we discussed this already, it's about INR32 billion, giving us INR6 billion of annual peak revenue potential. The lifetime revenue or breakup if you really see, 2-wheeler and 3-wheeler constitute about close to 46% of the total. And Bajaj at 47%. And interestingly, the EV part of the overall order intake is close to 37%.

In the next couple of slides we explain what these new products are all about. And then finally, we also gave some pictures of the new or additional capex, which we are going to spend basically for growth. We're going to invest in SMT lines to take the numbers from 10 to 15 to basically meet our demand for electronics. We're also expanding an existing plant to cater to the additional demand of EVs. And we are also acquiring land, both in south and also in the western part of India to further strengthen our relationship with a couple of OEMs to cater to their requirements.

So that's broadly what it is. In the subsequent slides, of course, we explain each business separately. So let me stop here, and then we can take questions. Thank you.

Moderator: Thank you very much. We will now begin the question-and-answer session. We'll take our first question from the line of Arvind Sharma from Citi.

Arvind Sharma: First question would be on the gross margin in this quarter was slightly on the weaker side quarter-on-quarter, so any specific reason for that?

Arjun Jain: Yes, I think there is a couple of reasons. I think, firstly, in IMES, we've had a change in our sales model to the customer, which has contributed to the gross margin fall. And then further, there's been a level of mix impact. And there are also some resin-related lags in our RM pricing or in resin-related RM pass-through lag.

Arvind Sharma: Got it. So is it going to stay at these levels or going forward, there could be a normalization, like an improvement in gross margin?

Arjun Jain: So the resin will, of course, normalize, but the notional impact in IMES due to the sales model to the customer, that is here to stay. But that does not impact the bottom line per se, it's only notional in the gross margin...

Mahendra Kumar: There's no impact on the absolute numbers. It is only the percentage which will look different.

Arvind Sharma: Got it. The second question would be on your outlook going forward, which segments are the ones where you believe that there could be significant growth?

Tarang Jain: So I think what we see in Q2 is the programs that we had already -- or the businesses that we had already SOP'd and in particular, in EV are now seeing volume expansion, which is starting to flow into our revenue. And I think that is a trend that will only continue and strengthen. Further, the order book that we have declared, I think the program launches are also now taking place. So, this is really across segments, across 2-wheeler and passenger car both.

And I think that's also reflected in some of the business wins and SOPs that we've talked about even in terms of new technologies. So I would say it's a mix. I would say it's a mix between 2-wheeler and passenger car. But yes, I think the order book is translating into -- the order book translates into real revenue now. But if you talk about the segments, of course, as you know, lighting is a very big segment all around.

So lighting will, of course, see with its 2-wheeler and 4-wheeler lighting will see a strong growth. Also on the plastic molding side, whether it's 2-wheeler and the 4-wheeler side. And like what Arjun mentioned, the EV side will see a growing momentum. All the EV powertrain and non-powertrain parts for 2- and 3-wheelers, especially we will see also quite a high growth in electronics in general.

So therefore, we were looking also earlier at investments coming in next year. But we had to prepone some of the investments for our EV motors as well as for a lot of the electronics. So we are now preponing a lot of the capex in this regard now to at least 6 months earlier. So which is a good sign for future growth.

Arvind Sharma: Got it, sir. And just if I may ask on the tax part, tax rate was quite high. So any specific reason for that in this quarter? And what should be the normalized tax rate for second half and FY '26?

Mahendra Kumar: Yes. So there are a couple of reasons here. One is, of course, on some of these overseas businesses where we are actually incurring some losses, we haven't recognized the deferred tax asset as of now because we need to see the turnaround to actually get that confidence and give that confidence to the auditors. So once we do that, that will get corrected. But otherwise, it is the normal thing only. Going forward, the stable effective tax rate could be in the range of around 25-27%.

Moderator: We'll take our next question from the line of Aditya Jhawar from Investec.

Aditya Jhawar: Yes. A few questions here. On the new business wins, for example, the BMS order win, can you talk a little bit more about it? Did you mention it is for M&M, number one?

Arjun Jain: No. It's for 2-wheeler customers.

Aditya Jhawar: This new BMS win is for a 2-wheeler customer. So if you can -- Arjun, if you can elaborate whether it's a new-age OEM, existing customer incumbent, and how do you see volume ramp up on this?

Tarang Jain: It is an existing customer. So it is an order, and it will be quite a large volume going forward, but it's from an existing customer.

Aditya Jhawar: Okay. Okay. Fair enough. Similarly for this interior in-built lighting order win, if you can talk a little bit about, is it a domestic customer, overseas customer? And how do you see it ramping up? Do we need to set up a separate facility or will it be catered by existing facility?

Tarang Jain: So this, I think Dhruv will explain, but this is, of course, for our overseas business is for our overseas electronics plant in Romania. And it is from an American customer, but I think maybe Dhruv you can elaborate a little bit on that.

Dhruv Jain: Yes. So I think just to add to what my father just said. So this is for a North American EV customer, and this would be serviced out of our romania electronics plant. And we're expecting the SOP in 2026.

Tarang Jain: Any major capex or anything over there in this regard?

Dhruv Jain: Yes., so there will be no major capex and in terms of any specific capex, this is also reimbursed by the customer.

Aditya Jhawar: Okay. Okay. Fair enough. And Tarang, you mentioned that there is some acceleration in capex that you have planned in the second half of the year. So for FY '25, what would be the total quantum? And directionally, if you can talk about what would be the capex in FY '26 as well?

Tarang Jain: So basically, I think we had given a guideline, and we were trying to also obviously be more careful on the capex, milk our existing assets. So we have given a guideline of INR200 crores.

But I think seeing this that we are investing now and including on the land also, so this could go up to this year INR260 crores, INR270 crores. And next year also, I think definitely, we would try to see that it is around INR200 crores, but it could also, depending on the growth and we are quite aggressive now on new sales wins, so there, again, it could go up to INR260 crores, INR270 crores next year also because we don't want to lose any opportunities in the marketplace at present.

Aditya Jhawar: Okay. Okay. Fair enough. And 1 question for MK. Clearly, I think debt reduction is going as per plan, very, very encouraging to see that. So is there any target in mind for second half of the year and you have set a target for debt for FY '26?

Mahendra Kumar: Yes. I mean, internally, we have aggressive targets, but I think we should end this year with maybe around INR700 crores to INR750 crores is what is possible. But we are trying to do something more than that also, but certain things need to fall in place.

Aditya Jhawar: Okay. Okay. Fair enough. Final question to Arjun. Arjun, if you can talk a little bit about this new product of integrated starter motor? What kind of order visibility we have and engagement with customers? And how do you see volume ramp up? Is it one customer, multiple customers you're engaging with on this product right now?

Arjun Jain: So for one customer, we've already SOP'd 2 models, and we have business wins from a further customer as well. And I would say we are engaged in discussion and really prototyping activity with 2 more customers.

Aditya Jhawar: Okay. And if you can give some colour on whether it is incumbent, existing customer, new-age customers?

Arjun Jain: So, this is essentially an integration of the Magneto, the starter motor, and the RR. So these customers are generally the traditional OEMs. And all that -- we supply the, let's say, older version of technology to practically every OEM in the country. So everything is through an existing OEM only.

Tarang Jain: But just to elaborate, I think, let's say, Arjun is talking about at least engagement with 4 customers, and we've already SOP'd with 1 and other 3 also will happen going forward.

So 2 for us -- I mean, so 2 could be -- you could say, could also be a partial replacement where we are already supplying magnetos and starter motors and RRs, but to an entirely an additional business where we don't supply a magneto or a starter motor or RR. So 2 will be totally additional. So that will give us an additional revenue stream, and it won't be a replacement.

Aditya Jhawar: Okay. Okay. Fair enough. My final question, Tarang, is there any update on arbitration proceedings in China? And was there any arbitration costs that we have incurred in this quarter?

Tarang Jain: So I think the arbitration costs, firstly, is minimal because all this arbitration is now kind of closed. Now we are just awaiting the final kind of this thing -- the verdict from the tribunal in Singapore. And in fact, it has been delayed.

But now, what we understand is that hopefully, this month itself, before the end of the month, we should be able to get a verdict, or it could spill into probably December. But in any way, in any case, we have been told it is not -- it will not pass December 31. But the signs are that we could get it at an early date now. And once that is done, there will be a lot of clarity on China, how to move forward in a more clear manner.

Moderator: We'll take our next question from the line of Vijay Pandey from Nuvama.

Vijay Pandey: Congratulations on successful quarter closure. I have 2 questions. One was on the order book. So after the presentation, the order book or the new order book points to INR22,000 crores in revenue in FY '27. So is it like your expectation? Or is it like a lifetime orders -- like how should we think about it?

Tarang Jain: So this is not INR22,000 crores. This is INR22,000 million.

Moderator: Sorry, sir, can you speak a bit louder, please?

Bikash Dugar: It's not INR22,000 crores. It's INR22,000 million. So it's INR2,200 crores. And the way to read that -- Exactly. And that is the annual incremental over the FY '24 closure level. So it's not lifetime, it's annual.

Vijay Pandey: Okay. Okay. Okay. There was one more thing I wanted to check on the luxury part. You said in your opening remarks that the luxury in ASEAN is on a weaker side. How much should we think about like in terms of revenue or in terms of exposure, is it less than 10%? Is it around 5% or -- if you can give a bit of idea on that, that would be helpful.

Bikash Dugar: So the overseas business, as you know, for 2-wheeler lighting is less than 5%. And out of that, when we talk about Piaggio, the customer who is into this luxury 2-wheeler segment, they contributes around 50% of our sales. So that segment is getting impacted because the sales in the ASEAN region of the luxury scooters are less as compared to the mass segment vehicle sales. So it's overall less than 2%, 3%.

Moderator: Next question is from the line of Vishal S from Svan Investments.

Vishal S: Congrats on decent set of numbers. Sir, my question is regarding the top line increase we have seen quarter-on-quarter from INR1,900 crores to INR2,100 crores, which is a healthy growth. But in terms of other expenses and employee expenses have remained to the similar levels of the last quarter. So just wanted to clarify, is this a one-off benefit here and gradually going forward, next quarter, there will be an increase from here on? That is my first question, sir.

Mahendra Kumar: Yes. So in terms of other expenses, in Q1, we had certain professional consultancy expenses, which have come down now. So it should more or less continue at this level as a percentage of revenue. And then employee expenses, yes, it should only get better.

Vishal S: Okay. Sir, my next question is regarding our share of business from Bajaj. If you see year-on-year, it has grown almost around 23%, 24-odd percent. But except for Bajaj, the other customers, it has remained almost on a flattish trajectory year-on-year. So how do we see this going forward? Because when I see the order book and the trajectory has been increasing, the share of non-Bajaj is close to around 52%, 53%, and this has been every quarter in the presentation, which you published, it has been increasing. So when this number will start reflecting on the overall top line?

Arjun Jain: So from a timing perspective and especially given how dynamic the market has been, I think it's hard to, let's say, predict an exact FY when we will see some dramatic change in the Bajaj percentages. And even if we look at the business win ratio, Bajaj is a significant portion of that. So today, I think the way we think about it is the business win and the execution of the business win is far more important than really the customer split. And based on timing, based on how different markets perform, whether it's 2-wheeler ICE products, 2-wheeler EV products, how different subsegments in the market perform, how passenger car performs, those percentages can change significantly.

Mahendra Kumar: Yes. And also -- it's also because the EV content is pretty high. And as EVs become more and more prominent, obviously, the Bajaj percentage will go up. So it's not because we have started taking less from others, generally because of the change in the EV penetration, correct?

Vishal S: Okay. I was coming to this question because I just needed a clarification whether there has been some market share loss, one, or there has been some deferment or delay in the new launches from the non-Bajaj customers, which has resulted in this flattish trajectory. Just that clarification I wanted from you.

Arjun Jain: There is no market share loss for sure. I think -- but again, like I said, right, it's a timing topic, right? If you look at this quarter, our sale into EV models is 12%, right, which is materially higher than -- materially higher than any quarter before that. Now of course, a large portion of that goes to Bajaj, which means that their weight in our mix increases. Tomorrow, for example, if passenger car starts to do better, we'll see maybe a reduction in that -- maybe we'll see a reduction in the Bajaj weight. But directionally, this is a mix that -- this is a mix that will broadly -- if market continues to perform the way it is, it will stay and it will evolve in line with the percentages that we are forecasting based on our business wins. But tomorrow, 2-wheeler EV dramatically increases in size, of course, the Bajaj weight will become bigger.

Vishal S: Perfect, sir. Sir, my last question is regarding -- just wanted to clarify, INR700 crores debt you mentioned for FY '25 as a target, is it the number of net debt or gross debt?

Mahendra Kumar: Yes, net debt. It can be better also, but there are certain things which need to fall in place. We need to also collect some government incentives and all from the government. So if all that falls in place, it can be better than that. But as of now, to be on the safe side, that's the target we are mentioning.

Moderator: We'll take our next question from the line of Iqbal Khan from ICICI Prudential Life.

Iqbal Khan: Sir, just wanted to understand from your order win perspective, around 37% odd is from EVs, right? So can you please elaborate on what all products is there? And what is the market size of those products? And how much is Bajaj or how much is non-Bajaj or it? Yes. So just wanted to get more clarity and sense on this EV products, new order wins?

Bikash Dugar: When we say EV customers, so these are also -- we spoke about the interior lighting business, which we have won from U.S.-based EV 4-wheeler player. That is one thing. Then there are 4-wheeler customers in India also, especially for their polymer parts, they'll be supplying them starting this year. So that is also there. And yes, there are incumbent 2-wheeler EV players to whom we'll start supplying BMS. So that is also part of this.

Iqbal Khan: All right. And sir, just 1 last. About the net debt, you mentioned that INR700 crores, INR750 crores of net debt by the end of this year, is this what I heard is correct?

Mahendra Kumar: Yes, yes, that's right.

Iqbal Khan: It will be from your internal cash generation, right? I mean, nothing of -- or is there any other way you're planning to reduce it?

Mahendra Kumar: No, no, it's through internal generation only.

Moderator: We'll take our next question from the line of Jai Prakash an Individual Investor.

Jai Prakash: My question to the management is that since March 2018, last 4 years, there was no reward for the individual investors despite there is a growth in your top line as well as your bottom line also, whether you have any discussion or you are focused on the rewarding the investors, there is no dividend, there is no buyback, anything? That is my question.

Mahendra Kumar: Yes. Thanks for the question. So as of now, like how we communicated earlier also, we are first focusing on strengthening the balance sheet and reducing the debt. At the same time, we are also giving importance to growth. So these 2 happen anyway, the benefit will flow to the investors indirectly in terms of the value enhancement. But having said that, yes, at some point in time, we will discuss this at Board level on when to declare dividends, and we will start that.

Moderator: Next question is from the line of Pawan from Geojit PMS.

Pawan: Just a couple of questions. One, with more and more EV business, how should you think about margins for this part of the business? Is it different from the existing business.

Mahendra Kumar: It's more or less similar to the existing business. It won't be very different.

Pawan: Okay. So from current levels, how should you think about margins for next, say, 1 or 2, 3 years?

Mahendra Kumar: Well, we don't give that kind of guidance, but definitely, the operating leverage should definitely help us as we continue to grow our business, particularly in the EV segment. So that itself should help us. On top of that, we are also looking at various cost reduction initiatives like how our Chairman explained in his speech. Most of these will start showing results from Q4 onwards. So it should get better from the current levels. That's where we would like to stop.

Pawan: Okay. And in terms of revenue growth, sir, if you could give any colour going ahead?

Tarang Jain: See, revenue, our stated position is definitely our effort is that we want to be at least 6% to 8% more than the market growth. We understand that, that's not happened at the moment so far. But I think going forward, that is the direction we have that -- because we place the most importance to revenue growth. So growth is definitely on top of our minds besides the other initiatives we are anyway taking. So this is something we will keep driving. And we are seeing a good amount of success also when it comes to new business wins and engagement with various customers.

Mahendra Kumar: Again, please don't take it as a future guidance. Yes, and one more thing we would like to remind all of you is we also talked about the overseas challenges, which will take some time to stabilize.

Pawan: Almost 85%, 90% of the business is domestic. So sir, I mean, my question is that whatever orders we've won in last, say, few quarters, does it give a visibility that we can achieve this industry higher -- 6% to 8% higher than industry growth for FY '26?

Mahendra Kumar: Yes, it does.

Moderator: We'll take our next question from the line of Rohan Vora from Envision Capital.

Rohan Vora: So just one question was the capex that we've preponed. So some colour on what are the products where we are seeing interesting demand trends? And what is the current capacity utilization for those products around that?

Arjun Jain: So like we've declared, the capacity constraints we face are on electronics and in particular, PCB assembly. This goes into many products, right? So it practically goes into maybe half our sales. So that is where we need to drive capacity expansion, and we're driving significant capacity expansion there. And the other one is in terms of the EV product lines, where we are -- where we also now feel -- where we also now face the need to expand capacities.

Yes. I'm sorry. And the third one is in terms of painting, in particular for the Northern region.

Tarang Jain: For the Northern customers.

Rohan Vora: Understood. Understood. And sir, in case of PCB assembly, so what is the current utilization and how long can the current capacity support before the new capex comes in?

Arjun Jain: So at this point, for PCB assembly, we are fully utilized, which is why we are driving the capacity expansion.

Moderator: We'll take a next question from the line of Vijay Pandey from Nuvama.

Vijay Pandey: Just wanted to check on the -- if you could give us an idea about the content for EV and ICE for your products

Tarang Jain: Sorry, can you repeat the question?

Vijay Pandey: If you can give an idea about -- Yes. If you can give a little bit of idea on the content per vehicle -- for electric vehicles and ICE given such a big order from electric vehicles?

Bikash Dugar: In 2-wheelers, if you look at -- if I compare the EV models with 125 cc vehicle, so the content on an average with our incumbent customer -- incumbent customer in 2-wheeler ICE for 125 cc, it will be around INR4,000 to INR5,000 per vehicle, whereas for EV, it will be around INR25,000 to INR30,000 content per vehicle. So that's around 5 to 6x of the ICE content.

Vijay Pandey: Okay. And -- but the margin is broadly similar for both EV and ICE components?

Tarang Jain: Yes. Comparable, yes.

Moderator: We'll take our next question from the line of Nishant from Geojit.

Nishant: Sir, firstly on -- I think in Q1, you mentioned about some startup costs related to the new plants that were coming up in Maharashtra. So could you just help us understand, I mean, where are -- I mean those costs still reflected in Q2 and how they would be going ahead?

Arjun Jain: Yes. I think we are at a place of far more stability now versus Q1. However, of course, there is always room for improvement across all operations. But yes, I mean, in all seriousness, we are definitely past the initial startup costs now.

Nishant: Okay. Any number that you could put around I mean what percentage?

Mahendra Kumar: No, we don't give those specifics. As Arjun pointed out, it's getting better certainly.

Nishant: Okay. And secondly, I think there was some notional impact on gross margin that was mentioned earlier by Arjun. So could you just expand a little bit? I mean, I didn't get that part clearly.

Arjun Jain: So the notional impact is so previously in one of our foreign plants, we were selling x material. Earlier material was supplied by the customer. So, the revenue recognition was only the value addition which we were doing. However, that the customer has changed the model now. So the material cost is now once again a part of the price as we are procuring the material.

Mahendra Kumar: So earlier, we were only getting the conversion cost. Now both material is part of the cost, and the corresponding revenue is also part of the revenue.

Tarang Jain: This is only for one of our major customers for one of the major customers in that plant, the forging plant.

Mahendra Kumar: So it's the arithmetical impact. Both numerator and denominator.

Nishant: Sorry, so that had some negative impact on our gross margin?

Mahendra Kumar: Yes. It's purely arithmetic. Both numerator and denominator if they go up by the same number, you will have some impact on the percentage.

Nishant: Okay. Okay. Fair enough. And lastly, sir, if you just help me with what would be our average interest rate on the debt side?

Mahendra Kumar: Right now, it's around 9%.

Moderator: We'll take our next question from the line of Shridhar Kallani from Axis Securities.

Shridhar Kallani: Kindly pardon me, I was a little late to join the call. On the EBITDA front, on the stand-alone basis, we can see that we have almost clocked 11.4%, 11.5%, but on a consol basis, it is lower than 10%. Now I understand that there was some gross margin impact on your international business. Just wanted to understand if there is anything else that has impacted the margins in the European business? And what steps are we taking to improve the same? This is my first question.

Mahendra Kumar: Yes. I think Arjun explained it earlier, maybe you weren't there at the time. So there are 2 factors here, which happened. One, of course, there was some change in the mix of businesses, plus there was also some lag in recovering some of the inflation cost in terms of input cost, which should get corrected over a period of time. The second part is the arithmetic part, which we just explained.

Shridhar Kallani: Okay. Understood. So currently, the EBITDA margin is, I think, in low single digits for your European business?

Mahendra Kumar: So I think we should look at it at the consolidated level. So consolidated level gives the right picture. It should get better going forward.

Shridhar Kallani: All right. And on the tax front, you had mentioned that this is a onetime deferred tax expense, right?

Mahendra Kumar: No, no, no. See, the deferred tax asset, which we created end of last year will have to be recognized or taken to the P&L every quarter or every month rather. So that is the impact which you see in the deferred tax line item. On top of that, where we are losing money or where we're incurring loss in some of these overseas operations, we haven't recognized the tax benefit on those losses as a deferred tax asset because that requires a strong confirmation that the future is going to be highly profitable to recover those losses. So once that confidence comes in, we will certainly recognize that particular asset also. So right now, it's on a conservative basis.

Shridhar Kallani: So the auditors have disallowed recognizing the DTA because of low visibility? Is the understanding correct?

Mahendra Kumar: No, it's not disallowing or anything. We also did not take it because we also wanted to see that positive news coming in, and then we'll start recognizing it.

Moderator: We have a question from the line of Pravin from Kotak Securities.

Pravin: I just have one question. So in the notes, it mentioned that the company received an order from GST for appropriation of GST dues, right, to the tune of INR63 crores -- yes, I was just referring to the footnote that the orders that you got from GST, right, pertaining to GST dues. If you can throw some colour while the company is planning to contest for the penalty and interest rate in the core, but what will be the likely impact in 3Q?

Mahendra Kumar: We don't expect any near-term impact here because the base duty has been paid already, so that is settled. The dispute is only about the interest and the penalty. And this is an industry-wide issue. It's not just -- not pertaining to us alone. So there is a classification confusion, which got created because of the inadequate explanation in the tariff courts, so which is being contested by many participants of the industry. So we will take the legal recourse for this. And once that issue is settled, this will get settled. But we don't see any immediate or near-term impact because of this.

Pravin: Okay. But the INR63 crores, whatever is paid, it will be recognized in the third quarter, right?

Mahendra Kumar: No, no, that is already done. I mean it is basically the GST, which we are recovering from customer and customers are taking credit. So there's nothing to be further recognized on the INR63 crores. It's only the interest on penalty, which is under discussion.

Moderator: We'll take our next question from the line of Ashwini Agarwal from Demeter Advisors ·LLC.

Ashwini Agarwal: Regarding the earthmoving equipment and construction machinery business, you had hoped for an improvement in the outlook there. Are you seeing any green shoots there?

Mahendra Kumar: Can you please repeat it? I couldn't hear you.

Tarang Jain: We lost you in the beginning.

Ashwini Agarwal: I'm saying is that one of your European subsidiaries has an exposure to earthmoving equipment and the construction machinery business, right?

Tarang Jain: That's right.

Ashwini Agarwal: Are you seeing any improvement in the outlook there because you were hoping to see some turn there?

Tarang Jain: Yes. So here with this company, we are definitely very strongly engaged for getting more business from them. There are large customers. So the discussions are on there, and we are hopeful that we will win some more business on an immediate basis. So those discussions are on with this customer already. And we are hoping that we are able to win some additional business from this customer.

Ashwini Agarwal: Okay. But nothing visible right now?

Tarang Jain: Nothing has been clarified. We know what is possible, and that's what we are discussing on, but it is confirmed, we are not -- we cannot say anything.

Moderator: Ladies and gentlemen, we'll take that as the last question for today. I would now like to hand the conference over to management for closing comments. Over to you.

Tarang Jain: So thank you once again to all for joining this call and for your continuing support. See you again in the next quarter.

Moderator: Members of the management team. On behalf of Investec Capital Services, that concludes this conference. Thank you for joining us, and you may now disconnect your lines.