Varroc Engineering Limited
Regd. & Corp. Office

L-4, MIDC, Industrial Area
Waluj, Aurangabad 431 136,
Maharashtra, India

Tel + 91 240 6653700
Fax + 91 240 2564540

email: varroc.info@varroc.com
www.varroc.com
CIN: L28920MH1988PLC047335

VARROC/SE/INT/2023-24/96 November 10, 2023

The Manager- Listing
The Listing Department,
National Stock Exchange of India Limited
Exchange Plaza, Plot No. C/1, G Block, Bandra-Kurla Complex,
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, 2023

Dear Sir/Madam,

Please find Transcript of Investors / Conference Call held on Tuesday, November 7, 2023, in respect of the Un-audited Financial Results for the quarter and half year ended on September 30, 2023.

This is for your information and records.

For Varroc Engineering Limited

Ajay Kumar Sharma
Digitally signed by Ajay Kumar Sharma
Date: 2023.11.10 17:33:30 +05'30'

Ajay Sharma
Group General Counsel and Company Secretary

Encl: a/a

"Varroc Engineering Limited

Q2 FY '24 Earnings Conference Call"

November 07, 2023

MANAGEMENT: **MR. TARANG JAIN – CHAIRMAN AND MANAGING DIRECTOR – VARROC ENGINEERING LIMITED**
MR. ARJUN JAIN – WHOLE-TIME DIRECTOR – VARROC ENGINEERING LIMITED
MR. MAHENDRA KUMAR KARUMANCHI –CHIEF FINANCIAL OFFICER – VARROC ENGINEERING LIMITED
MR. BIKASH DUGAR – HEAD INVESTOR RELATIONS – VARROC ENGINEERING LIMITED

MODERATOR: **MR. BASUDEB BANERJEE – ICICI SECURITIES LIMITED**

Moderator: Ladies and gentlemen, good day and welcome to Varroc Engineering Limited Q2 FY24 Earnings Conference Call hosted by ICICI Securities. 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 this conference call, please signal an operator by pressing star then zero on your touchtone phone. Please note that this conference is being recorded.

I now hand the conference over to Mr. Basudeb Banerjee from ICICI Securities. Thank you and over to you, sir.

Basudeb Banerjee: Thanks, Neerav. Good evening, all participants. Thanks to Varroc Engineering Management for giving us the opportunity to host the call. We have with us the senior management represented by Mr. Tarang Jain, Chairman and Managing Director of Varroc Engineering, Mr. Arjun Jain, Whole-Time Director, Mr. Mahendra Kumar Karumanchi, CFO, and Mr. Bikash Dugar, Head Investor Relationship. So I'd like to hand over the call to Mr. Tarang Jain for his initial comments. Over to you, sir.

Tarang Jain: Yes, I'm Tarang Jain here. Good evening to everyone and I thank ICICI Securities for hosting this call. To start with, the geopolitical situation in Europe and the Middle East has created uncertainty in the global business environment. The interest rates may come under pressure if inflation goes up further due to a spike in oil prices. Despite these uncertainties in the global markets, we see a resilient and a growing economy in India. The Indian economy has sustained its growth momentum in FY24 so far.

Though urban demand has already picked up well, we're expecting the rural demand will also pick up with the current festive season. The automobile production in India during Quarter two FY24 grew on a year-on-year basis for most of the segments. The passenger vehicles grew by 5.6%. Three-wheelers registered a strong growth of 19.16% and commercial vehicles grew by 8.8%. Only the two-wheeler segment has de-grown by 1.5% as the early festive season helped Q2 during last year.

Sequentially, that is quarter-on-quarter, we have seen growth in all the segments.The commercial vehicles have grown by 7.9%. Passenger vehicles have grown by 12.7%. Three-wheelers by 33%. And two-wheelers saw a growth of 13.6% on a quarter-on-quarter basis as Q1 is generally a sluggish quarter.

In terms of operations in Q2 FY24, we continue the journey of improving operational and financial performance. Revenues from operations grew by 3% on a year-on-year basis to INR18,868 million despite a weak growth in the overseas markets due to the holiday season in Europe. The reported PBT for the quarter was INR739 million which includes profit from a joint venture of INR80.6 million.

Our balance sheet has strengthened in half-month of financial year 24 as we pulled ahead some of the debt reduction initiatives to Q2 and reduced our net debt significantly by over INR2,714 million and a net debt to equity ratio to below one time. Our debt servicing ability has also improved as net debt to EBITDA is now at 1.35 times compared to over 2.13 times at the start of the financial year. The annualised return on capital employed for the first half of 24 is around 23%.

We continue to win the trust of the customers as they are awarding more business. This is reflected in the new order win. In first half of financial year 24, a new lifetime order win is INR36.0 million. In Q2 of FY24, we have added three new customers for supplying components to the EV models. In the quarter, we also won business from two customers for supplying components related to the EV powertrain. These new orders will enable us to strengthen our presence in the EV component space. Our revenue from supplying to EV players in Q2 of FY24 was approximately 4.4% of our overall revenues. Our effort to increase our technical capability was further enhanced in half-month of FY24 as we filed nine patents in India and one overseas.

As you might have noted from our submissions to stock exchanges, we also signed agreements to procure power from renewable energy sources to tune off over 36 megawatts DC annually for consumption in the states of Maharashtra, Karnataka, and Tamil Nadu. We will continue to look for more such opportunities in the near future.

We continue to enhance our engagement with OEMs and showcase our ability to deliver advanced technology solutions at affordable cost to them. We are also working on various other efforts like capacity utilization, prudent capital allocation, and cost reduction across the board to make our business more robust.

With this, now I will ask MK, our group CFO, who will walk you through the presentation which is already uploaded on our website and submitted to the stock exchanges also.

K. Mahendra Kumar: Thank you, Tarang. Good evening, everyone. This is Mahendra. So let me take you to the highlight slide in our presentation, which is slide number four. As our chairman explained, the year-over-year revenue growth was about 2.9%. Maybe this was partly moderated by the early Diwali which we had in Q2 of last year. So the revenue closed at about INR1,887 crores.

In terms of profitability, we are continuing the profitability journey. We are close to about 10% EBITDA or about 3.9% in terms of PBT. The absolute PBT was about INR74 crores. Balance sheet has been significantly strengthened. You may recollect that in our earlier discussions, I mentioned that in H2, we will be able to reduce debt significantly. But this time, we actually could pull ahead most of that to Q2 itself, taking advantage of the higher revenue so we could do more of factoring. And similarly, the higher realization from the sale of divestment last year, which we realized in the month of July, that also helped us.

So with that, we could actually reduce debt by close to INR300 crores compared to what it was one year ago. So with this, the net debt equity comes down to below one, or 0.94 to be precise, and net debt to EBITDA is at 1.35. Business wins, of course, our chairman touched upon already. In H1, if you see the total business won, it was like close to 36 billion. We also added three more new OEMs to the EV segment.

And in terms of the EV revenue percentage of total, it's about 4.4%, which should actually grow based on the new orders which we won recently. And like how we explained earlier, we are focusing more on cost reduction, and one of the areas is energy saving. Previously, we mentioned that we are actually tying up with a few firms to source more of renewable energy. So those things are in place now. There are still a few more things to come, but we are still working on them.

Going to the next slide about the industry, the two-wheeler industry grew by 1.5% year-over-year, and it actually grew by 13.6% on quarter-over-quarter. Passenger vehicle grew by 5.6% year-over-year, and sequentially by about 12.7%. So we still need to see what kind of impact all these geopolitical developments will have on the economy and the industry going forward. But we are hoping that the festival season should help us to some extent in Q3 also.

Going to the next slide, which is about the consolidated financials for Q2. So like how we explained earlier, 3.9% was the PBT in Q2, which is up by 2.2% compared to same time last year. And you might have noticed that the interest costs actually went up compared to the previous quarter. That's partly because we prepaid some of the high-cost loans during Q2. That should actually help us in the future, plus the higher factoring, discounting also is something which we actually consciously did it to repay the debt. So those are the main reasons. Going forward, we are hoping that this interest cost should come down in the coming quarters.

The next slide, we give the overall H1 picture, like how we explained earlier. We are always aiming for a faster PBT growth compared to revenue growth. So you see that H1 to H1, if you really see the revenue grew by 6.4%, the EBITDA grew by 21%, and then PBT was almost like three and a half times. So we are hoping to continue this kind of improvement journey going forward with a heavy focus on growth as well as cost reductions.

Then in the next slide, we give the details of net debt. We are close to INR1,000 crores now in terms of net debt as of 30th September, INR1,006 crores to be precise. So the net debt to equity ended up at 0.94, and net debt to EBITDA at 1.37, growth was 23%. And coming to the revenue breakdown, more or less similar to what we showed earlier, the overall two and three wheeler revenue comes to about 71% of the total, and about 15% of the revenue outside India compared to 85% within India. And the outside India revenue was also partly impacted because of the holiday season in Europe and other markets.

In terms of the order win, about 36 billion in the lifetime business wins in H1, and interestingly you may see that nearly one-third of that actually is in the EV space now, which is an encouraging trend for us.

So that's it from our side. We are now happy to take questions.

Moderator: Thank you very much. We will now begin the question and answer session. The first question is from Aashin from Equirus. Please go ahead.

Aashin: Hi, thanks for the opportunity. So, my first question is regarding margins. So, we have margins on a quarter-on-quarter basis that remain flat at 9.9%. So, could you help us explain how do we plan to go to the 11%, 12% margins going forward? And what sort of a margin do we expect for the next two to three years?

K Mahendra Kumar: Yes, so, thanks for your question. Mahendra here. First of all, we don't give this kind of guidance going forward, but I'll broadly tell the direction which we're planning to take. Definitely, revenue growth plays a role, and the related operating leverage should actually help us to a large extent. Because in most of our businesses, our capacity utilization is only around 60%, 65% level.

So, without incurring any extra costs or additional investment, we should be able to scale up our revenues in most of the areas. So, the operating leverage should help us. On top of that, we are also working on various actions towards improving contribution margins. In the next couple of years, we have certain targets internally we are working on.

Energy is one of those areas which I mentioned earlier in my presentation. But there are also certain other areas that we are working on. Plus, a continued focus on fixed cost control is another area. We just want to ensure that fixed cost doesn't grow in line with the revenue. Our internal target is to ensure that it grows at a much lower pace than the revenue growth. So, that should also help us in terms of bigger improvement in the overall margins.

And going forward, we'll be monitoring the businesses for performance based on PBT, not so much on EBITDA. So, when it comes to PBT improvement, the interest cost reduction will also help us. Because that is already close to INR1000 crores. It should come down further in the coming year or so.

So, that should enable us to reduce the interest burden. Plus, the capex control also is going to help us in terms of reducing the overall depreciation burden in the coming quarters. So, with all this, we're expecting that the PBT level should be reasonable to good improvement in the coming quarters or coming years.

Aashin: And sir, you said that you've added a few new customers on the EV side. Could you please highlight what sort of business things have been done and which are the key product areas that we are seeing good?

Arjun Jain: So, within the EV product line that we have, our focus is really on the EV powertrain, which is the motor and the motor controller. And also on our connectivity devices. And the businesses we have won are around the powertrain.

Aashin: And sir, about the customers, which you've added?

Arjun Jain: So, we can't reveal the exact names of the customers. But, one is a domestic startup, who is not yet started production, but we expect to start soon with our powertrain. And the other is an export customer on a much larger capacity powertrain.

Aashin: And sir, lastly on the profitability of the EV product side. So, given the fact that now claim to subsidy has been reduced, do we see any impact of that on our profitability? Given the fact that OEM might want to pass on that to the vendors?

Arjun Jain: I think our OEMs are very mature buyers of products, especially from us. So, again, I can't comment on OEM strategy. They also have replacement benefits in place i.e. PLI, instead of fame. But, in our view at least, our pricing with respect to EV product line is sustainable. And we expect that that trend will continue.

Aashin: Okay, thank you sir. I'll join back.

Moderator: Thank you. Next question is from the land of Akash Gopani from Investec. Please go ahead.

Akash Gopani: Hello. Thank you for the opportunity. Taking forward that EV question, can you highlight what would be the timeline when we can see this revenue flow into our console operation? And any tentative timeline pertaining to when can we see this revenue reach peak in our EV revenues?

Arjun Jain: Okay. So, I think the first thing to say is in terms of reaching peak, I think it's much harder to comment. I think it depends. There's a lot of variables around OEMs reaching their peak needs. From the standpoint of when we could expect to start seeing revenues coming in, I would say within 12 months. We've always been fairly consistent in terms of saying that our products are ready, our platforms are ready, our manufacturing lines are ready, which means we should be able to ramp up very quickly. And I think that's why OEMs like us. So, within 12 months, we could expect to start seeing revenues.

Akash Gopani: Okay. And early, would it be right to assume that the ASP for this product would be somewhere around 15,000?

Arjun Jain: I cannot comment on specific segments, but yes, I mean, it will be significant.

Akash Gopani: Okay. Got it.

Arjun Jain: And the larger the power drain, the higher the price point, of course.

Akash Gopani: Got it. Okay. Coming to the non-EV business side, over there also, we have seen sharp increase in order book. So, any significant order win or breakthrough in OEM, which the company has been able to do over here? Or any increase in share of business with particular OEM we are seeing over here?

Arjun Jain: I mean, today we are present really across the entire two-wheeler segment and we're present with multiple customers, even in the passenger car and the commercial vehicle segment. So, of course, we report EV separately in terms of businesses for multiple different reasons, but I think the rest, I would say, is really just par for the course. We keep driving penetration, we keep driving improvements.

Within that, if I had to call out certain technology products, even for an IC engine, we would have an integrated starter generator, for example. So, I think that would maybe be a highlight, but most of it is just normal sales growth, normal sales wins in the capacity that we have available already.

Akash Gopani: Okay. Got it. And lastly, any comment on the lighting revenues, decline in Q-o-Q, which we have seen, any particular reason? Is it pertaining to European operations?

Arjun Jain: Yes. So, like we said earlier, Europe has shut down for summer holiday in this quarter. So, that would definitely be a primary driver. The other thing also is that, I would say with India, I think, we've been supplying at peak capacities for a lot of the OEMs. So, we'll have little bits here and there, etcetera, but I would not say that that is a major contributor.

Akash Gopani: Okay. Thank you and all the best.

Moderator: Thank you. Next question is from line of Vishals from Svan Investments. Please go ahead.

Vishals: Thank you for taking my question, sir. Sir, I have a question regarding the top-line growth, seems to be muted over the last few quarters, if you see. So, what are the measures you are taking to push the growth? Any guidance you can share in terms of the top-line growth which you can give? And you were always focusing on the content per vehicle increase. So, any light you can provide, roadmap in that terms going forward?

Tarang Jain: Of course, as we said before, we generally don't provide guidance for the future. From a top-line growth perspective, I think we do expect, generally the cycle for most customers is that SOPs generally take place post-Diwali. We have a fair amount of launches that will take place post-Diwali. But really, I think from a top-line growth perspective, in the spaces that we want to be in, we have a healthy order book and revenues will come.

Vishals: Okay. So, perhaps this is why, if we see your vehicle-wise growth, numbers which you have reported, two-wheeler business has grown by 4%, whereas overall volume in two-wheelers has grown by 15% on Q-on-Q basis. So, the growth in the two and three-wheeler segment has remained muted. This is because maybe some outgoing platforms and we are waiting for the new platforms to come in and that may kick in the growth. Am I understanding right in that regard?

Tarang Jain: I don't think we have any outgoing platforms per se. But of course, our largest customer has de-grown to a certain extent, quarter-over-quarter, which definitely impacts us. But I think if we think about it again from the perspective of our content per vehicle and where we are seeing volumes grow in the market, we do have significant content per vehicle, which is something that will keep panning out over time.

Further, again, like we stated, from an overall growth in revenue standpoint, we do have revenue that comes from Europe, both in two-wheeler as well as from IMES, for example, which is forging. Which, yes, in this quarter, there is a summer holiday, which impacts sales to a certain extent.

Vishals: Okay, okay. Sir, any guidance you can give in terms of your capex spend? So, for the half year, you have spent around INR116 crores. What will be the full year capex for this financial year?

K Mahendra Kumar: Yes, Mahindra here, we may spend maybe another INR100 or below INR100 crores in the second half.

Vishals: Okay, okay, okay. Thank you for taking my question. I will call you back. Thank you.

Moderator: Thank you. Next question is from line of Shubham Jain from NV Alpha Fund. Please go ahead.

Shubham Jain: Yes, sir, my question is regarding the comments made by Mr. Kumar on the decreasing interest cost and increasing our PBT margins. Can you please tell me on, indicatively, as of now, we are paying INR200 crores interest cost per annum. What should this interest cost start looking at going on incrementally over the next few quarters?

K Mahendra Kumar: Yes, so, we don't want to give exact number, but like what I explained earlier, we have close to INR1000 crores of debt left now in terms of net debt. Plus, we typically do discounting of receivables for about INR500 crores at any point in time. So, based on this, we can broadly work out what should be the future cost. There could be some working capital swings in Q3. We are working on various initiatives. So, there may be some temporary disturbance during Q3. But going forward, once we reach end of the year, I think it should stabilize and it should come down based on the levels which I indicated just now.

Shubham Jain: Sir, so, at what level of net debt to EBITDA, today it's at approximately one time, at what level of net debt to EBITDA will you be comfortable to stop doing this factoring and incurring this excess interest cost?

K Mahendra Kumar: Yes, so, we target to bring it to about half. That's what we are aiming for. But it may take some time. It may not happen immediately. It will take maybe a year or more to actually get to that level.

Shubham Jain: Okay. And what is the factoring cost interest? So, INR500 crores you said is factoring. So, what is the cost on that approximately?

Management: It's cheaper than the debt cost. It's anywhere between 8% to 8.3% per annum.

Shubham Jain: 8% to 8.3% per annum. So, this is off balance sheet. So, you pay 10% to 12% on INR1,000 crores and you pay 8% on INR500 crores. Is that right?

Management: No. The debt interest is around 9% now. So, we also do some interest. The interest cost on loans is about 9% now. We recently renegotiated some of the rates with the lenders based on the inflows which we got recently. So, the average cost has fallen

Shubham Jain: That will be visible in the next quarter or so?

Management: Yes. It should be visible going forward. Like what I said in Q3, there are so many things which are moving around. You may not see a big swing or big reduction in Q3. But going forward in the medium to long term, you should be able to see this kind of reduction.

Shubham Jain: Okay. And second question from my side, sir. We see that your depreciation as a percentage to Gross Block is slightly on the higher side as compared to other auto ancillary companies which again suppresses the PBT margins. Any comment on that? Have you studied this as compared to other auto ancillary companies?

Management: Yes. See, it depends upon the kind of -- what we call the mix of assets we have also. If we are talking about this particular quarter, we also took some kind of accelerated depreciation on some of the overseas assets just to keep the books neat and clean. So, that impact may be there, maybe until end of this year.

And thereafter, once we actually control the capex spending in relation to the depreciation that we are incurring, slowly the depreciation burden should come down in the coming quarters and years.

Shubham Jain: Okay. Awesome. Thank you so much, sir and all the very best, sir.

Management: Thank you.

Moderator: Thank you. Next question is from the line of Darshil from Crown Capital. Please go ahead.

Darshil: Good evening, sir. Thank you so much for taking my question. Some of the questions have been answered. Just one broad-based question, sir, in terms of macro environment, what kind of feelings are we getting? Are we seeing that there is now going to be accelerated growth or how do we see the environment as? And also in terms of our seasonality, so would it be fair to say due to Diwali, our H2 will be higher in terms than H1? Will that be a fair assumption, sir?

Tarang Jain: See, I think for us, we definitely feel that our H2 revenues will be more than the H1. Largely, see, what we see that the Indian market, we still see a growth in the Indian market compared to the market globally, where the sales growth is quite subdued even now. And today, we are also hoping that, that in a two-wheeler entry level also see some traction in this season.

So overall, we still remain bullish, on the growth here. And there's also the elections which is coming up, and we do see that consumption should be there. Consumption should go up also because of the forthcoming elections. Yes, there could be maybe some impact depending on this new war which has started, on the oil prices, which could be inflationary in nature for India also.

But overall, we remain optimistic and bullish, where the Indian market is concerned, which gives us today more than 80% of our revenues. So, we do see a better second half compared to the half one, from the point of view of our revenues growth.

Darshil: Okay. Thank you, Tarang sir. So, would it be fair to say, it could be around 55%- 45% in terms of H2- H1 or it could be even higher in terms of pure seasonality?

Tarang Jain: I can just say, it will be better. We don't know, but it will definitely be better. Okay.

Darshil: Okay, sir. And sir, this one question in terms of, I agree, we cannot give guidance, but in terms of qualitatively, do we see that, are we, in terms of our revenue, are we stuck in a band of revenue and that will get accelerated as the market improves or any statements, maybe not exact guidance per se, but then do we see that, okay, we'll be able to cross the INR1,800 crores- INR2,000 crores of revenue that is possible over the next year, in the quarters coming by? Again, not a firm guidance, but maybe like, are we stuck in a range, which is finally now we'll be able to open up and, come swinging? Will that be a fair way to look at it?

Tarang Jain: I would say, in fact, explicitly not, right? I think in many ways, right? I mean, if you think about the last few years, our focus has always been two-wheeler, three-wheeler. And that has not been growing industry, but we have still been able to drive significant growth as a result of very content-focused strategy.

And that is something that continues to play out. So, as EV increases in sales and volumes, and especially as our customers ramp up, as stories around premiumization, urbanization, etcetera, also continue to pan out, we will only see growth. We will only, I think, we are one of the first to really benefit from, the growth in revenue that takes place.

So, to put it simply, I don't think we're stuck in a band. In fact, we are in a very good place Where, if we compare half to half, H1 of last year and H1 of this year, the industry has de-grown, the two-wheeler industry. But as a matter of fact, we've still grown by 6.5%.

Darshil: Correct. I think that, and so it's just like, no, in terms of our growth, we don't see any risk or challenge, right? Except for maybe some war-like situation. Other than that, we don't really see any kind of risk, right?

Tarang Jain: No.

Darshil: Okay, perfect, sir. Thank you so much for all the answers.

Moderator: Thank you. Next question is from the line of Sachin Kasera from Svan Investments. Please go ahead.

Sachin Kasera: Yes, hi. Congrats on a good set of numbers. Just one question. The strong order wins that we have reported. So, when should we start to see the benefit of that? More of H2 of the current financial year, or a little more of a FY '25 financial?

Tarang Jain: This will be FY '25. And it will be the second half.

Sachin Kasera: Second half of FY '25?

Tarang Jain: Yes

Sachin Kasera: Okay, so 12 months from now. That's when we start to see the real benefit of this strong order wins that we had recently?

Tarang Jain: Yes, which we have just reported.

Sachin Kasera: Okay, got it. Thanks.

Moderator: Thank you. Next question is from the line of Prateek Poddar from Nippon India Asset Management. Please, go ahead.

Prateek Poddar: Yes, sir. A couple of questions. One is, maybe you could just touch upon, when you see Q-o-Q growth, as reported in your presentation also, across vehicle classes, it's quite strong, right? While Y-o-Y, you have outperformed, on a Q-o-Q basis, the revenue growth looks quite muted relative to the automotive production growth of India on the two-wheeler side be three-wheeler

And in fact, even the largest customer on a Q-o-Q basis has grown. So, I'm not able to reconcile as to why have these grown at 4% this quarter?

Tarang Jain: Yes, so the largest customer has only grown by 2.7% Q-o-Q.

Bikash Dugar: So, the two-wheeler industry has grown by 13.6%, but the largest customer, two-wheeler volume, their production number has only grown by 2.6%. So, as earlier stated by Tarang, sir, and Arjun, it's better to look at H1. And H1, we have grown by 6.5%, whereas the two-wheeler industry has only de-grown by 0.2%. And the new businesses for SOP are going to start in the second half of this financial year. And as we stated earlier, we remain confident that, we'll do better than the industry growth.

Prateek Poddar: Okay. The other is, when I look at your employee cost, very sharp accretion. In fact, it is something which has detracted your operating leverage on a Y-o-Y basis as well as on a Q-o-Q basis. Just curious, why did that happen?

K Mahendra Kumar: Yes Prateek, so a couple of things happened. One, we had some one-time good news in Q1. That's one of the reasons. The second reason is, we also are trying to change the composition of the workforce. We recruited some GETs and also some workforce at the entry level, which should actually give us benefit going forward in the long run. So, that's another reason.

Tarang Jain: Yes, but we remain conscious going forward on all fixed costs.

Prateek Poddar: So, just to double-click on this changing of composition which you are doing, is it in anticipation of the additional orders which are yet to be executed and then we'll see the operating leverage? Is that the way I should think about it? So, you are building capacity for future growth, but the capacity is built at a lower cost because you have hired entry-level graduates, etcetera?

K Mahendra Kumar: Yes, that is one reason. Secondly, we are also re-skilling considering the growth prospects, we have.

Prateek Poddar: Okay, got it. I think one of the participants did ask and you did say that by H2 FY 2025, we'll start seeing the new order book being executed. What time frame is this? In the sense, when you have won these new orders, in what time frame would you execute? Like, is it three years or 18 months, two years?

Arjun Jain: Again, Prateek, every customer and every program will generally have different development timelines. You know, passenger car development timeline is generally longer than a two-wheeler development timeline. Within passenger car, within two-wheeler, within commercial vehicle, different customers have different philosophies. So, it's hard to put an exact number on it without actually explicitly delivering revenue guidance. But, like we said, I think FY '25 is when we expect a lot of this will go into manufacturing.

Prateek Poddar: Sure. And the new orders which you have won, these are not replacement orders. These are over and above your legacy business, if you really do, right? So, these are essentially filling up of capacities which will drive operating leverage. Is that a fair understanding?

Tarang Jain: Yes, absolutely. We don't report any replacement numbers at all. These are only new orders win.

Prateek Poddar: Okay, fantastic. Last question. When you look at your largest customers, they've been quite vocal, at least in this conference call, about new product launches on the EV side, be it two-wheelers, as well as scaling up their three-wheeler EVs. Is it fair to say that their scale-up, the content for vehicles in the EV, for them would be far higher than our base business, and that would drive operating leverage or that would drive revenue growth for us once their three-wheeler and two-wheeler EV business starts becoming more popular or starts gaining traction?

Tarang Jain: Yes, I think that is definitely fair to say.

Prateek Poddar: And would you have 100% share of business over there with them?

Tarang Jain: No, I think platform by platform, model by model, it will vary.

Prateek Poddar: You are the pre-dominant customer supplier over there. That's a fair understanding?

Tarang Jain: It will always be significant. Some products, we could be a single source, but in some products, there would be a sharing of business.

Prateek Poddar: Got it, sir. And, sir, just correct me on the interest cost, a bit puzzling, right? You called out debt interest cost, you called out factoring cost. When I do the math and when I analyse your interest cost, it doesn't add up. How is that? Because, look, you have INR200 crores of interest cost. You said INR1,000 crores of net debt at 9% interest, that's INR90 crores. INR500 crores of factoring cost at, again, 8.3%, that's INR40 crores. So, INR90 crores plus INR40 crores should be, whatever, INR130 crores versus INR200 crores. Can you help me understand, where is this INR70 crores additional coming from?

K Mahendra Kumar: Yes, so there are also things like the lease interest, which is part of that. Plus, there are bank charges. Plus, there are things like repayment cost, which we paid this time to get rid of some of the high cost debt. So, if you analyse all this, it may actually work out to be that number. But going forward, some of these may not repeat.

Prateek Poddar: What's the lease cost? Maybe you can just call out that.

K Mahendra Kumar: This is the interest component of the leases that we have.

Prateek Poddar: Yes, I understand that. What's the lease cost, like, per quarter?

K Mahendra Kumar: I don't want to give the exact number, but you can broadly work out the difference. And the second thing you need to keep in mind is, this is like net debt versus gross debt, right? We also have about INR200 crores- INR250 crores of cash, which we'll scale down going forward. So, you need to apply this on the gross debt also.

Prateek Poddar: Understood. And what is this foreign exchange gain pertaining to?

K Mahendra Kumar: Yes, so it has both operating and non-operating parts of it. Operating is simply the restatement of these export receivables and all. Non-operating is relating to these loans and advances which we gave to our overseas subsidiaries and the businesses which we have there.

Prateek Poddar: Can you call out the non-operating one, please, if it's possible, sir?

K Mahendra Kumar: Broadly, I can say 50-50.

Prateek Poddar: Okay, fantastic. Thanks and best wishes for the future. Thank you.

Moderator: Thank you. Next question is from the line of Piyush Gandhi from Cognizant Capital. Please go ahead.

Miyush Gandhi: Hi. Thanks for taking my question. Sir, would it be possible to quantify the impact of European shutdown in this quarter? In terms of revenue, how much would we have missed?

Tarang Jain: Yes, it's difficult to – I mean, we don't want to reveal that kind of breakup between overseas and India. But you can broadly say that for nearly more than a month, most of those businesses were closed for holidays.

Miyush Gandhi: Okay. And would it be fair to assume, given the shutdown, the margins or probably EBITDA would be far lower, I mean, for this quarter, again, versus the previous quarter?

Tarang Jain: Yes, obviously, because that revenue was not there, but costs would continue.

Miyush Gandhi: Okay. So next quarter, maybe once the business comes back to normal, there is some tailwind from that part of the business that can come through.

Tarang Jain: Correct.

Miyush Gandhi: Would it be possible to quantify the impact of, falling raw material prices on our top line? I mean, we've seen in the whole of one year, both the metal part of the business and the plastics part of the business would have seen some deflation in the products. So that would have been passed on, right? So, I mean, just trying to understand, what is the underlying growth versus the inflation deflation that hits our top line?

K Mahendra Kumar: We can broadly say maybe it's close to 1.5% to 2%.

Miyush Gandhi: Okay. So it's not very large. It's not that large as such?

K Mahendra Kumar: Correct.

Miyush Gandhi: Fair enough, sir. And in this quarter, particularly because of this shift in festive season, that would also have had some impact on our top line growth, right?

K Mahendra Kumar: Correct.

Miyush Gandhi: Any number that you would like to put it?

K Mahendra Kumar: How do we estimate this? Difficult to put a number to it.

Miyush Gandhi: No, the whole idea of asking these questions is to understand the underlying, top line growth, because we've been in this 1800, 1850, 1900 range for the last three, four quarters. And we were actually hoping given this is the biggest quarter for us, this quarter would have been a little better on the top line front. So that's why I'm trying to understand where is the miss coming from? That was the underlying thought process?

K Mahendra Kumar: No, I understand. I understand your question. It's difficult to quantify it is what we think.

Bikash Dugar: Look at the annualized number. You should look at how much we have done in the last four quarters and compare that to the previous four quarters number. If you analyse the numbers, then you will see that we have significantly grown.

Arjun Jain: Again, I would also say, I think if you compare H1 of this year to H1 of last year, we have grown. To be honest, I think as a result of semiconductor challenges that took place through, 2022 or basically FY23, some of the revenue last year was a little bit maybe lopsided. But if you look at the half overall, the only real difference is the impact of the festive season. But we've still been able to drive a level of growth.

Miyush Gandhi: Fair enough. I may be completely wrong on this and pardon me if I'm wrong, but if I recollect properly, our domestic lighting business, we were supposed to start on a plant and we were supposed to, in-house, in-source the entire LED light production. Is that already happened or I'm reading something wrong?

Arjun Jain: No, so we had already in-source. So we had not got any outsourced lighting production even last year. We are starting a new plant. In fact, it is partially started already. And I think that ramp up into, from the old plant into the new plant will continue. But it is not an in-sourcing activity that is taking place. It is a location move that is taking place because unfortunately, in the old plant, we ran out of space.

Miyush Gandhi: And how much more capacity would the new plant have? Because you also mentioned in one of the answers that we are running out of capacity on the lighting side business?

Arjun Jain: So I would say space more than capacity. But yes, we have the ability to, I mean, we have the ability to add 40% more volume.

Miyush Gandhi: Okay. And just one last question. Any update you would like to share on what is happening in the China business? We were in an arbitration procedure with them?

K Mahendra Kumar: Yes, so both the approaches are continuing. The arbitration proceedings are continuing. On the other hand, the discussions with the partner on split are also progressing well. It may take maybe a little more time to actually conclude. So in any case, we are assuming that this should actually come to an end before end of this financial year.

Miyush Gandhi: Okay. Thanks. That's it from my side.

Moderator: Thank you. Next question is from Vignesh Iyer from Sequin Investments. Please go ahead.

Vignesh Iyer: Congratulations, sir. And thank you for the opportunity. I just wanted to know, after the prepayment of this debt, what would be our now cost of debt as of after this prepayment is done?

K Mahendra Kumar: Yes, that's what I was answering in the earlier part of this discussion. You can roughly say 9% is the average cost of debt right now across maturity. Plus factoring is anywhere like 8% to 8.3% is what we are incurring.

Vignesh Iyer: Okay. But can we, I mean, as a part of the India statement, I understand that you have to show interest cost. But as part of the notes, can we have that bifurcation shown for better clarity as to what is your regular part of the interest and what is prepayment or bank charges, if any, that is getting debited under interest?

K Mahendra Kumar: I mean, this is a one-time thing. It's not that every quarter we are going to have and there is no requirement of India that we have to give this separately as a disclosure. But this is a one-time thing which should not happen going forward.

Vignesh Iyer: Okay. I mean, because there is some discounting charges as well, right? That is a recurring nature?

K Mahendra Kumar: That will continue because that is the cheapest source of financing for us. That is the last one to be taken out.

Vignesh Iyer: Absolutely. Yes, that's all from my side. Sir, thank you. Thank you.

Moderator: Thank you. Next question is from the line of Abhishek from Dolat Capital. Please go ahead.

Abhishek: Thanks for the opportunity. Sir, we have seen a strong growth in the polymer business in this quarter. So have you owned any new business in this segment and how is the outlook ahead?

Arjun Jain: Yes, so polymer in general, right? Across whether it is moulded plastics, painting, seats, air filters, I think we have one new business which goes into production. We continue to win business as well also. So, again, that growth is driven by a combination of, let's say, businesses that have been executed for the past year. In some places, we also have, let's say, higher content, especially on topics like painting. And also in some places, maybe a level of natural growth from the OEMs.

Abhishek: Okay. And, sir, how much difference in the cost of discounting of recievables versus loan cost and how much benefit we get? And what is the normal payment term you give to the customer usually?

K Mahendra Kumar: Yes, I think I answered this earlier in the call. The debt fees are around 9% and factoring is somewhere between 8 to 8.3.

Abhishek: And how much is the normal payment terms to the customer? How much normal payment terms you give to the customer?

Tarang Jain: Payment terms, of course, vary from customer to customer. The large part of the customers is in the range of about 30 to 45 days. And then there are also certain customers in the range of 60 days and up. We're trying to rationalize that. But yes, you can say average, maybe around 45 days.

Abhishek: Okay, sir. Thanks.

Moderator: Thank you. Next question is from the line of Rohan Pasad from Renaissance Investment Managers. Please go ahead.

Rohan Pasad: Hi, sir. So, again, my question is on growth. So, if I look at your largest customer, H1 to H1, revenue growth is something like 17%? So, isn't it better to look at revenue to revenue growth versus volume growth and considering that our growth is just about 6%. So, could you explain this?

Tarang Jain: Sorry, I'm not clear what exactly is the question. Are we saying that we have grown more with our...

Rohan Pasad: So, I think your largest customer, Bajaj, has grown, H1 revenue has grown at 17% I'm not talking about volume, I'm talking about revenue. And we've grown at about 6%. Even Hero has grown at 4.5%. So, in that context, our revenue growth appears to be on the lower side, H1 to H1, I'm comparing. Or maybe that's not the right way to look at it.

Tarang Jain: Yes, it's hard for us to comment on customer value or revenue growth. I mean, of course, the pricing strategies, I think that is best to speak with them. I think from a supplier perspective, looking at the volume and comparing their volume growth with what is our revenue growth, I think it makes a lot more sense.

Rohan Pasad: Can you actually repeat, what is the capex you're planning for this year and next year?

K Mahendra Kumar: Capex?

Rohan Pasad: Yes.

K Mahendra Kumar: Capex, we must spend about another INR100 crores or so in H2.

Rohan Pasad: And how much have we done in H1?

K Mahendra Kumar: It's close to about INR110 crores or INR113 crores.

Rohan Pasad: And should we expect a similar number for the next one, two years?

K Mahendra Kumar: Yes, it should be around INR200 crores or thereabouts.

Rohan Pasad: And just trying to work out your cash flow, so there should be any meaningful change in the working capital cycle that we have as of now?

K Mahendra Kumar: Should not be, it should only get better is what we are trying. In between, there could be some ups and downs, but going forward as a trend, it should not get worse than what it is right now.

Rohan Pasad: Okay, okay, okay, great. So, we think net debt next two, three years should be good on free cash flow generation for us?

K Mahendra Kumar: Yes, yes.

Rohan Pasad: Great, great. Thank you.

K Mahendra Kumar: Again, it's not a guidance, but that's what we're aiming for.

Rohan Pasad: Yes, so basically, what I'm trying to understand is that, I mean, with about INR1000 crores debt, we should be max two years, we should be net cash.

K Mahendra Kumar: Yes, ideally, yes. I mean, yes, it should be maybe even early perhaps, but anyways.

Rohan Pasad: Thank you, sir. All the best.

Management: Thank you.

Moderator: Thank you. As there are no further questions, I will now hand the conference over to the management for closing comments.

Tarang Jain: So, thank you all for joining the call. And I would again like to reiterate that we will continue to drive profitable growth, be prudent on our capital allocation, and focus more on free cash flow growth and also on the cost reductions. Thank you once again.

Moderator: Thank you very much. On behalf of ICICI Securities Limited, that concludes this conference. Thank you for joining us. You may now disconnect your lines. Thank you.