"ELGi Equipments Limited Q3 FY2018 Earnings Conference Call"

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Moderator: Ladies and gentlemen good day and welcome to the ELGi Equipments Limited Q3 FY2018 Earnings Conference Call, hosted by Asian Market 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 telephone. Please note that this conference is being recorded. I now hand the conference over to Mr. Kamlesh Kotak from Asian Market Securities. Thank you and over to you Mr. Kotak!

Kamlesh Kotak: Thanks Karuna. Good afternoon everyone. On behalf of Asian Markets, we welcome you all to the 3Q FY2018 earnings conference call of ELGi Equipments Limited. We have with us today Mr. Jairam Varadaraj, Managing Director representing the company. I request Mr. Jairam to take us through the overview of quarterly results and then we shall begin the Q&A session. Over to you Sir! Thank you.

Jairam Varadaraj: Thank you Kamlesh. Good afternoon ladies and gentlemen. Thank you for being on this call and it is my pleasure to spend this time with you. As per our normal process I am going to take you through our consolidated results for the quarter compared with the performance of previous year same quarter. At a sales level we have increased by 25% from 3325 million to 4154 million. At EBITDA level we have increased by 71% from 278 million to 474 million. I run the normal reconciliation as usual. By virtue of the increase sales we should have had a higher EBITDA to the extent of 370, but our material cost is higher in this quarter compared to the previous quarter and that has taken away close to 26 million. So in spite of that our EBITDA should have been 621 million whereas we have done 474 and the biggest incremental cost that has taken away this EBITDA is man power cost that is increased across the world, but the biggest chunk of increase has happened in India, so other than that our costs are pretty much under control within normal levels. So this is at the consolidated level. I will rely on your specific questions to talk about any details on the financial numbers. I will spend a little bit of time talking about the overall business scenario what led to this growth, so I will split this up into India and the rest of the world.

As far as India is concerned, we have had growth across all the verticals of our business. Our industrial compressor business has been good, but the biggest growth came from our construction and mining in terms of percentage the biggest growth was in construction mining. We have grown in the railways, but not anything significant. We have grown in our aftermarket as well again not as much as our budget, but we are moving ahead. So overall India's performance has been good across all the business verticals. I believe that there is emerging confidence in the economy, even though large projects are still pending, large projects by that I mean power and steel. Balancing capex investments are beginning to happen and we have seen the result of that in our performance as well, so I expect this kind of cautious optimism to take us through the fourth quarter as well, as well as take us into next year. Barring any major political developments or policy changes or economic impediments I expect 2018-19 to continue to move on the same trajectory as what we have seen in the last two quarters and what we expect in the fourth quarter as well.

As far as international is concerned, as usual I will start from where the sun rises, which is Australia or us at least. We have done well in Australia, we are continuing to grow, we are profitable and we expect to see some good initiatives there in the coming years. Southeast Asia has been a bit of a challenge so far; it is marginally better than last year, but nowhere near the targeted numbers. I have explained India to you.

Moving onto the Middle East. Middle East has been a challenge, but things are beginning to pickup now, so I think the fourth quarter should be better for Middle East and 2018-19 should be better. Specific countries in Africa are doing well, we will have to wait and see what happens, but it is not a strategically keen market for us. Europe has done very well for us both Rotair products sold worldwide as well as ELGi products sold by Rotair in Europe they have done well for us.

America continues to be strong for us; we are growing our business on all the verticals that we are operating in, in America. Brazil has been a challenge though the economy seems to be coming back. We have done a reasonably good job of ensuring that we are not losing any money, but sales has been lower than last year. We expect the next year to be better, the economy seems to be picking up and there is overall optimism, the elections around the corner and there will be a better economic situation. So this is really the summary of our performance geographically, so I will stop at this point and I will rely on your questions to take this call further. Thank you.

Moderator: Thank you very much Sir. Ladies and gentlemen we will now begin the question and answer session. Ladies and gentlemen we will wait for a moment while the question queue assembles. Thank you. The first question is from the line of Ravi Swaminathan from Spark Capital. Please go ahead.

Ravi Swaminathan: Congrats for a good set of numbers. Just wanted to know from a domestic perspective you told that construction and mining are seeing decent amount of pickup, what about the other sectors, you told that steel yet to see a pickup, but if the demand from these industries start picking up will it move the needle materially for ELGi and will it drive the next leg of growth for us, what is your view on this?

Jairam Varadaraj: It is not going to significantly alter our topline, but there will definitely be a reasonable contribution from the steel and power segment if they start reviving, but I do not expect power to revive because there is just too many stressed assets that are lying around, even in steel with all these delinquent assets being auctioned, the profitable steel companies are probably looking at acquiring assets rather than greenfield auction.

Ravi Swaminathan: But how much would steel and other industries are, other industries would be contributing towards the revenue for us, the ballpark and infra how much it would be any sense that can be?

Jairam Varadaraj: Infra is too broad definition Ravi because airports are also infra, but we do not contribute much to airport, roads and dams are the main areas where our portable compressors go, so I do not want to get into the specifics of what they contribute. We are not a business where any one industrial vertical has a substantial contribution to our topline, so we play across all, so the health of all the industries are critical for us to have that kind of a full 100% performance capabilities and we need all the industries firing.

Ravi Swaminathan: In terms of market share do you get a sense that we would have one market share, would the market have also grown at the same pace or slightly lower?

Jairam Varadaraj: That is a million dollar question Ravi. I am sure my competitors are going to be listening in on this call after it is posted on the website. I think they should tell me whether we have done better than them.

Ravi Swaminathan: Got it and moving onto international, so basically US a lot of capex activities expected, do you see this growth sustaining for the next two to three years in US and can it contribute majorly to the growth for ELGi?

Jairam Varadaraj: There are mixed opinions about the sustainability of the US economy, so it is a little difficult, I am not an expert in terms of what are the dynamics that the Federal Reserve has already started increasing the interest rates, so they are worried about inflation, they want to cool down the economy, but there are so many things happening there, it is difficult for us to really predict, but **(inaudible 11:16)** our starting point is so small and the market is so big. The economic growth is important, but is slightly less relevant for our future in the US.

Ravi Swaminathan: So irrespective of the growth there we can keep growing is what you are saying?

Jairam Varadaraj: Yes that is the reasonable assumption Ravi.

Ravi Swaminathan: But the team is in place now, fully stabilized there post decline we had seen?

Jairam Varadaraj: After the disruption that we had from our competitors that team has been rebuilt already, but we are in the process of expanding the team because we have got some new initiatives looking at.

Ravi Swaminathan: Got it and one small question on bookkeeping number, what would be ELGi's branded sale outside India, so basically compressor sale what could be the growth there?

Jairam Varadaraj: You mean compressors with the brand ELGi?

Ravi Swaminathan: Yes, correct.

Jairam Varadaraj: I do not have that number in front of me Ravi.

Ravi Swaminathan: And one more thing these consultancy charges, which we had hired in the domestic market, are those charges over or get over?

Jairam Varadaraj: They are over as of Q3; there would not be any more charge on Q4.

Ravi Swaminathan: Quantum?

Jairam Varadaraj: We have specifically said that we will not disclose that Ravi with a consultant.

Ravi Swaminathan: Thanks a lot Sir.

Moderator: Thank you. The next question is from the line of HR Gala from Finvest Advisors. Please go ahead.

HR Gala: Just wanted to know this super performance of 25% revenue growth in Q3, is it due to because FY2017 Q3 would be relatively weak because of the demonetisation as far as India is concerned?

Jairam Varadaraj: No, I do not think so because if you look at Q2 to Q3, there was not much of a drop and demonetisation was a very temporary blip for us and we are in capital goods we are not in a business where cash was a big component in our value chain, so I would not say that growth is because of a weak Q3 of last year.

HR Gala: So it is basically a growth across all the geographies as you indicated.

Jairam Varadaraj: Right.

HR Gala: Sir can you help us with this nine months number of 1143 Crores, how much is domestic and how much is international?

Jairam Varadaraj: 1100, which one are you talking, 1143? India is about 7072 and the rest of the world would be about 4300.

HR Gala: That is millions?

Jairam Varadaraj: Yes.

HR Gala: Now Sir talking about the long-term growth perspective we have been aiming to double the sales by FY2020 how are we placed as far as the M&A opportunities that we have been looking at for the past few years?

Jairam Varadaraj: We have identified specific products and specific geographies that we want to focus on and we have just initiated the search process for inorganic growth opportunities in these key markets, but we are tempering that whole process because we need to first have a strong leadership team in place before we venture into inorganic opportunity and that is the lesson we learned from our past inorganic growth. As we speak we are in the middle of putting that team together. We hope that in the next three to four months' time, at least in the key markets we will have all the resources in place to be able to pursue this opportunity.

HR Gala: Subject to that happening organically do you think that about 15% to 20% type of revenue growth as we have achieved in nine months would be sustainable organically?

Jairam Varadaraj: I am optimistically cautious on this. We think that 2018-19 could be at least minimum we should be able to do 15% without any inorganic growth opportunity, but if everything is status quo nobody interferes with economic functioning then we should be fine.

HR Gala: I think that we will come to know on February 1, 2018 how much interference?

Jairam Varadaraj: Exactly.

HR Gala: Thank you very much and wish you all the best.

Moderator: Thank you. The next question is from the line of Ranjith Sivaram from ICICI Securities. Please go ahead.

Ranjith Sivaram: Congrats on good set of numbers. Just wanted to check this 15% growth, which you are talking is in the consolidated or the standalone?

Jairam Varadaraj: Consolidated.

Ranjith Sivaram: In standalone if you can help us like what kind of growth we are expecting?

Jairam Varadaraj: I think like we said cautious optimism we are saying both would be pretty much. We are looking at the rest of the world growing at around 17% and domestic growing between 14% and 15%.

Ranjith Sivaram: Any more issues in terms of overseas where we will see the margins being impacted or growth being impacted or you feel that most of the operations in all these geographies have been stabilized, do you foresee any?

Jairam Varadaraj: I think there are two aspects to it. One is the present stage of the price and cost structure. I think that is pretty much stabilized and there are marginal opportunities may be to increase prices and marginal opportunities to reduce cost, so those are I would say business as usual improvements year-on-year. The other is the country level risk where we have been struggling two areas where there is a continuing kind of challenge one is China and the other one is Brazil. China we have consciously taken a decision two years ago that we will scale down the extent of our operations, but we will not exit China because we know that it is the largest compressor market in the world today, but it is a very different and complex market we need a completely different strategy. At the moment a geographical focus in terms of building out our business globally is not in China; therefore, we want to stay in a hibernated situation, we want to remain in China and even while we do that we want to go back to the drawing board and build a product strategy, which will give us the right to win in China. So till such time there will be some challenges, we will have to fund the Chinese operations and there could be some marginal kind of write offs that we need to take, but nothing significant. As far as Brazil is concerned, we are growing, we have stopped making the losses, we have restructured the business, so I do not see any charge coming on account of Brazil in the future, but when Brazil can start contributing healthily to a bottomline is something that we have to wait and see.

Ranjith Sivaram: Okay and in terms of our focus geography where last analyst meet also you mentioned we will be trying to inorganically buy some like dealers or some kind of like patterns kind of companies, so which geographies we will be looking at for that?

Jairam Varadaraj: Our primary focus is Europe, America and India is the high priority geographies for us. The second level priority is Australia, Indonesia and Thailand. So these are the areas where we will be looking various opportunities.

Ranjith Sivaram: Lastly just wanted to understand after now GST is over, so are we seeing that we were all expecting some shift from unorganized to organized, so is it very early for that or we seeing some kind of?

Jairam Varadaraj: No, we are not seeing any change I think everyone has kind of gotten used to it, got adjusted to this process.

Ranjith Sivaram: Thank you so much.

Moderator: Thank you. The next question is from the line of Richard D'souza from SBI Mutual Fund. Please go ahead.

Richard D'souza: Congratulations on a good set of numbers. Sir just wanted to understand when you did is the international subsidiaries have done very well in this quarter I think the growth was somewhere around 27% and margins have expanded quite a bit now is this something sustainable and I mean where do you expect the ideal margins to rest there?

Jairam Varadaraj: No I think this is sustainable.

Richard D'souza: Just wanted to understand the growth, which we have seen in your international subsidiaries whether it is sustainable going ahead and the margins are especially where do you see them settling down?

Jairam Varadaraj: I think the growth rate certainly for Q4 and most certainly for 2018-19 is sustainable with our international subsidiaries and especially Europe and US. On margins I do not see any big pressure on margins at this point in time. We should be able to sustain these levels as much at operating level, but if there are specific initiatives that we are planning to run that is separate I mean that is like at project level.

Richard D'souza: When you look at the structure of the results for the international subsidiaries it seems that you have crossed tipping point and your margins basically you have covered your fixed cost and incremental everything is going into margins so you got right way to look at it?

Jairam Varadaraj: Yes absolutely.

Richard D'souza: Thank you and my second question is that you mentioned in the concall about strengthening your leadership and when we look at your employee cost basically your international subsidiaries the cost has flattened out for employee expenses, but in 3Q your domestic wages were up 23%, so was that due to new hiring or any specific reason?

Jairam Varadaraj: We have increased our headcount as part of our various market initiatives. We have also moved compensation partly towards and this I explained in the last concall. We are moving compensation towards the market level we still have some ways to go on that, but we are not doing it one big jump and we are not doing across the board, we are doing it very selectively, but I expect that the pressure on people cost to remain for the next few years at least.

Richard D'souza: Okay Sir so the way the cost of mood does it means that for the international geographies you are adding domestic people to the work?

Jairam Varadaraj: This is for certain initiatives that we ran, which we started almost one-and-a-half years ago that we have been.

Richard D'souza: Okay so you are having hiring international people for international market?

Jairam Varadaraj: Absolutely.

Richard D'souza: Thank you and wish you all the best.

Moderator: Thank you. The next question is from the line of Aditya Bagul from Axis Capital. Please go ahead.

Aditya Bagul: Congratulations on an excellent performance. Sir the first question would be on the plan laid out by the BCG, you have mentioned earlier that you have implemented this plan domestically over three quarters ago, would it be possible for you to share the broad contours of the same?

Jairam Varadaraj: Aditya I do not want to talk about the results that I have emanated from that specific initiative that is comparatively too sensitive, what I can say is our presence in the market is improved, our engagement with customers especially in the aftermarket has been very good and that is beginning to show in our revenue growth in our aftermarket, so overall I think we had looked at returning the money spent on this whole project within one-and-a-half years and I think we are on track for that.

Aditya Bagul: Just a followup on that. Would it be fair to assume that most of the new employee additions would have been towards the front end at least domestically?

Jairam Varadaraj: I would not say that I mean I would say it is about 50:50. We have also invested quite a bit in our backend in terms of our technology function and some of our operation's functions so I would not say that all of it went to the front end.

Aditya Bagul: Sure Sir that is helpful. Sir coming to your technology you mentioned in the previous analyst meet that you had introduced the revolutionary oil free compressors, which you could manufacture probably the cost of normal lubricator compressor and what could be the status on that and when would it be rolled out?

Jairam Varadaraj: It has already been rolled out for validation. We have got machine running in the field, we have a detailed plan worked out. We are hoping the global launch will be probably in 2019, but India launch will be probably in the second half of this calendar year.

Aditya Bagul: Great Sir. That is quite useful. Sir one last question on the bookkeeping side. What would be the net debt position as on December and what would be your deleveraging plans given that we have some inorganic ambitions?

Jairam Varadaraj: Well on net debt as of December was about Rs.180 Crores. We expect the debt position to be around Rs.115 Crores by March 2018. In October, November and December we kind of built some strategic inventory because there was a regulation pertaining to efficiency standard of motors that the government had kind of announced with a very short notice, so before our vendors could actually gear up to get those certifications done we are in anticipation built some types of inventory, so subsequently the government had kind of extended the deadline so that was an inventory that we had, which is being liquidated, so I am very sure that we will be able to bring it under control by March, so that is why I am optimistic it will be in the neighbourhood of about Rs.115 Crores by March. Earlier we had given a commitment or plan that we will be debt free by September 2018. Give or take quarter I think we should be on target to make that happen. This is business as usual, but if many of the inorganic opportunities that we are engaged with if they kind of mature into a transaction level those would be additional that I mean I cannot quantify that now.

Aditya Bagul: Sure Sir. That is quite useful. That is it from my end. Thank you so much.

Moderator: Thank you. The next question is from the line of Vipul Shah from Sumangal Investments. Please go ahead.

Vipul Shah: Congratulations for very good set of numbers. Sir my question is which of the international subsidiaries are struggling and what are our plans to turn around them?

Jairam Varadaraj: I just explained Vipul, there are two subsidiaries that we are under pressure one is China and I have explained what is the strategic reason why we are continuing into stay in China and we have a longer term view. The other subsidiary, which is not losing money, but it is not contributing profits to the extent that the others are is Brazil and we have done a good job in containing the losses, there are no losses anymore in Brazil in spite of variation in the exchange rate, but we expecting that 2018-19 would be a better year because economy is expected to be better.

Vipul Shah: My second question is would it be possible to give spares and service income on a 12-month basis?

Jairam Varadaraj: I would not like to split the verticals to beyond this level Vipul.

Vipul Shah: No, it is perfectly fine Sir. Thank you very much and all the best for the future.

Moderator: Thank you. The next question is from the line of Sunil Vijay from Spark Capital. Please go ahead.

Raghavan: Congrats for the good set of numbers. I had couple of questions. First question is basically demand showing slight chains of pickup and what about the pricing scenario Sir given this compressor market is fairly concentrated, so can you talk about what was **(inaudible 31:37)** about the pricing scenario at your end customers?

Jairam Varadaraj: I do not think we have added any price pressures nor have we done any significant improvement in price realization that is what you are talking about.

Raghavan: Okay. It still remains, as buyers market is the right understanding?

Jairam Varadaraj: No absolutely. There is no sellers market; we have never had sellers market in compressors.

Raghavan: Sir my second question is we have been investing in gross block over the last four or five years if I asked without any incremental investments in your gross block what sort of revenues you can do organically considering basically we have wider range of products compared to the last cycle?

Jairam Varadaraj: No, it is not that we have not done incremental investment to our gross block. We have not made any significant breakthrough kind of investment like we did when we set up a new facility, but every year we are incrementally balancing our capacity so right now we have enough capacity to grow close to 30%-40%.

Raghavan: For example our 2011 if I go back to last cycle where is when we peaked our asset terms where we did close to 4.5 times of asset terms, which is currently reading as close to 2.5 times. Is it fair to assume that considering we invested quite a bit of capacities over the last five years and with more wider range of products, is there a scope for this asset terms to improve to more than 4.5 times?

Jairam Varadaraj: You got to look at the complexion of the investment. We set up two big investments that we have made, which reduced the asset term were a new campus and the foundry. Neither of them is going to increase contribute directly to the topline, they are all basic infrastructure that is required to conduct the business, so that is like a step increase in the asset base, which is fundamentally required to conduct the business. So productivity of productive assets in terms of sales is continued to keep improving even during that period.

Raghavan: Thanks. Sir without any incremental investment you are saying 30%-40% kind of growth possible organically?

Jairam Varadaraj: No, we balancing investment that we do on a year-to-year basis, which is not significant.

Raghavan: Understood. Thanks Sir. All the best.

Moderator: Thank you. The next question is from the line of Vivek Sethia from Stewart & Mackertich. Please go ahead.

Vivek Sethia: Congratulations on good set of numbers. I had just two questions with you. The first one being can you give us some idea about the market share that you hold in the air compressor market and automotive equipment?

Jairam Varadaraj: I wish I knew that number because it is such a complex number to arrive at because in India we do not have a consolidated publication of all the sales made by the competitors, so it is very difficult for me to estimate, but if somebody puts a gun to my head I will say it is probably 30%.

Vivek Sethia: In the compressor market right?

Jairam Varadaraj: Yes.

Vivek Sethia: And Sir in the automotive equipment?

Jairam Varadaraj: I would say about 40% to 45%.

Vivek Sethia: In the next two to three years where do you see the company like what future plans do you hold for the company?

Jairam Varadaraj: We want to grow and we think that Indian economy is at a stage where it will facilitate growth for us and we think that, that is reasonable to expect. We have got good presence now and key international markets and we believe we will grow well in those markets, so that is basically our plan.

Vivek Sethia: There is increase of about 84, 85, 86 million in other expenses, is that attributable to some specific extent?

Jairam Varadaraj: Which number you are looking at, you are looking at consolidated?

Vivek Sethia: Yes Sir consolidated.

Jairam Varadaraj: Consolidated other expenses. I have to come back to you on that I do not have the breakup of that with me, but part of it could be also the increase in our fixed cost in across the board, across the world, in Italy, eight years in the Gulf and in US. We have also got some increases in some variable cost as a consequence of increase sales so I do not have the breakup between the increases in other cost between variable?

Vivek Sethia: Basically due to expansion in some small countries like or in the countries, which you are trying to expand it is due to those that other expenses which you say?

Jairam Varadaraj: No see other expenses have a variable component and fixed component. So variable is moved, as a percentage variable cost is not increased so that is under control, so I do not have the breakup of that between those two elements.

Vivek Sethia: Thank you so much.

Moderator: Thank you. The next question is from the line of Vinod Chari from Dolat Capital. Please go ahead.

Vinod Chari: Congratulations on the quarter. Just to continue with that market share question the previous participant asked 30% is your market share and how was the rest of the 70% split between Ingersoll-Rand or an Atlas, Copco and say Kirloskar?

Jairam Varadaraj: I have no idea. You need to ask them.

Vinod Chari: Secondly in the opening remarks you made that you said that there is a growth across verticals including industrials are there any specific industries that you are seeing growth or is it again much more broad-based?

Jairam Varadaraj: I think it has been across the broad all industrial verticals have been quite poised except for certain segments like I said power and steel and all the big projects.

Vinod Chari: Sir this demand that you are seeing on the construction and mining side if I have to do capex read through or is it more of ground level execution happening or is also combination of execution plus new orders coming in I mean new capex happening?

Jairam Varadaraj: No, it is both. If you look at road construction, they are all contractors, the orders on them has gone up, their investment in equipment have gone up and that is resulting in our sales just as an example.

Vinod Chari: You are seeing some ground level viable in the new orders also that is happening?

Jairam Varadaraj: Yes.

Vinod Chari: Sir finally when you said 15% growth expectation and you have mentioned that your international business is going to grow faster than India, when do you see this reversing when do you see India like growing faster and faster?

Jairam Varadaraj: Since I do not control the finance ministry and economic management of the country. I again only say that things are left as they are and no disruptions happened, I think that India has the potential to have a significantly larger GDP growth, but you got understand India is only one country for us the rest of the world may be another 50 countries. So once we ignite a growth engine in the rest of the world, India's growth cannot compete with that in terms of contribution to the total.

Vinod Chari: Fine Sir. Thanks a lot.

Moderator: Thank you. The next question is from the line of Kirthi Jain from Sundaram Mutual Fund. Please go ahead.

Madan Gopal: This is Madan from Sundaram. Congrats on good set of numbers. Sir I just wanted one data point. Can you give us rough idea of what will be infra as a mix towards and how much it has grown year-on-year?

Jairam Varadaraj: I do not know how you define infra?

Madan Gopal: Something to do with our road construction, railways those kinds of areas other than say general engineering or a manufacturing setup?

Jairam Varadaraj: It is still for me to split that up Madan, but like I said railways has grown, but it is not a big number, it is a single digit growth whereas it is a double digit growth on a road construction business and general other road and dams and other construction.

Madan Gopal: Anything that we get participation for urban transportation something like metro construction and those kinds of areas?

Jairam Varadaraj: We are not homologated yet into the electrical multiple units that are supply because they are all coming in from global tenders and international players who have not yet with whom we have not homologated, it is a long process and right now we have not engaged in that process. So our market share on the metro segment is very, very low. Our presence in railways is more on the intercity and the goods railways.

Madan Gopal: But you see this as an opportunity the metro side?

Jairam Varadaraj: We do see, it is an opportunity we are working towards, we are trying to figure out what would be the best way to get ourselves homologated, so it is a long process, so we are waiting to see how to do that.

Madan Gopal: Great to see good numbers coming and giving confidence to capital goods sector. Thank you.

Moderator: Thank you. The next question is from the line of Aditya Singhania from Enam Holdings. Please go ahead.

Manish Goel: Very congratulations on excellent set of numbers. Thank you so much. Sir couple of questions on our new products basically oil free screw compressor, which is at the oil compressor price. So for us will it probably, technically we are already there with the product on oil free, but with this product do you think that our addressable market will expand both in domestic and international will it make a change?

Jairam Varadaraj: Absolutely because right now there are oil free compressors that are both oil free screw as well as oil free piston. Now the oil free screw cannot compete with the oil free piston because of the price, and the oil free cannot compete with the oil free screw on efficiency. There are two different set of products are straddling, these two applications under the oil free markets. Our product can serve both very effectively, so to that extent there will be an expansion of our opportunity rather than the market.

Manish Goel: So ideally today what would be the price differential in terms of if we probably want to take an average roughly for both categories?

Jairam Varadaraj: I do not understand your question.

Manish Goel: What I am trying to say is that if probably you are giving the new product that for a lubricated compressor what would be the price differential and on other side if you are probably substituting for a low price product like oil free piston where you will probably give more efficiency, so ideally for a customer what would be the cost saving preposition Sir?

Jairam Varadaraj: I still do not fully understand your question.

Manish Goel: Where I am coming from Sir is that today you are offering a product oil free screw compressor at a price of a lubricated compressor, so today what would be the price difference Sir between these two?

Jairam Varadaraj: Between oil free screw and oil lubricated piston?

Manish Goel: Yes.

Jairam Varadaraj: It could be anywhere between double to 250 tonnes, 200 to 250% for oil free screw.

Manish Goel: Okay, basically 2 to 2.5, so this ideally according to you will be in terms of market openings would it be possible quantify what would be the size of this market?

Jairam Varadaraj: We have not done that yet Manish. We know the size of the oil free market, which I do not want to share in this column, but we do know the size of the piston compressor also, we need to put it altogether in a global context and arrive at the opportunity set, but we are really going after in phase I we will go after the current oil free market and that will be our focus and that itself is a big enough opportunity for us.

Manish Goel: And you are probably launching it in second half of the calendar year this year?

Jairam Varadaraj: Yes.

Manish Goel: On the headcount, which you mentioned that probably before we do acquisition we would probably look to improve our headcount in the key operating market, so basically is it largely international markets?

Jairam Varadaraj: Yes. Our acquisition like I told you it is in our focused area. There is really new acquisition opportunity for us.

Manish Goel: Sorry I meant international, so we would be ideally looking for acquisition in terms of having a better market penetration that is how we should basically to have a better front end?

Jairam Varadaraj: Right and there could be certain product extensions, which we are not present in, which we need to have control over, but not in the core compressor business, but product extension.

Manish Goel: So ideally Sir when you do acquisition it will come with set of peoples, so like to kind of preempt and build a team ahead of that and then probably also have another team, so just wanted your thoughts on that?

Jairam Varadaraj: No, an acquisition is part of a largest strategy for a particular region, so you need a leadership for that region in place to be able to integrate and manage that acquisition.

Manish Goel: I thought that you are probably looking to build larger sales and marketing team as well.

Jairam Varadaraj: No that will be an incremental business decision; it would not be a strategic.

Manish Goel: To clarify Sir you said the growth momentum would be maintaining Q4, so would it be 25% revenue growth or 15% for the nine months?

Jairam Varadaraj: Q4 is always a big quarter for companies, to grow 25% over the few quarters a little difficult.

Manish Goel: Yes, because last year Q4 was quite decent, and I missed on one question on the team building, so will it involve a large cost impact say probably six to eight months down the line?

Jairam Varadaraj: For the specific initiatives that we are going to run, there will be a cost impact we still do not know what those initiatives are, we have not finalized and we have not costed them, but that will be a project. I will come back at the appropriate time at the call I will talk about it, but overall people like cost increase for the current headcount itself is going to go up, we are going to increase incrementally headcount as we grow our business both in India and rest of the world and in specific countries like geographies like for instance in Europe. In America, we have organization by virtue of having been present there now for almost five years. In Europe, we have only the road tyre organization, we do not have European organization right, and so we need to build that leadership at that level.

Manish Goel: And last question Sir basically our historical PBT was Rs.48 Crores in Q2 FY2011, so hope we cross that number in Q4 Sir?

Jairam Varadaraj: Which one Manish sorry I did not get.

Manish Goel: Of Rs.48 Crores PBT in Q2 FY2011 hope that we cross this in the coming quarter Sir It is just my hope. Thank you so much Sir. Thanks a lot.

Jairam Varadaraj: You are remembering too many things.

Manish Goel: And look forward to meet you Sir. Thanks a lot.

Moderator: Thank you. The next question is from the line of Eshit Sheth from Anvil Research. Please go ahead.

Eshit Sheth: Thank you for taking my question and congrats on a good set of numbers. There are couple of questions. One is that you highlighted that we had certain raw material pressure in this quarter basically, was it a lot to do with the product mix also, which led to increase in raw material cost as a percentage of sales?

Jairam Varadaraj: I did not refer to raw material cost, I was talking about inventory with specific material that is why the inventory went up. The change from quarter-to-quarter on material cost percentage is purely a product mix thing, there is no fundamental shift in our contribution margin.

Eshit Sheth: Okay and say for example with steel prices actually rising from January onwards, are you confident to hold on to your raw material cost as a percentage of sales in the coming quarter?

Jairam Varadaraj: We are not seeing any big pressure on that, we should be able to manage it.

Eshit Sheth: Because what we are seeing is that since the international business has grown at a very steady pace of 20% plus ideally with higher contribution we should have seen higher actually EBITDA basically?

Jairam Varadaraj: But that is what has happened if you look at our international business about five years ago the consolidated EBITDA used to be around 6%, now the difference between the standalone and consolidated EBITDA is only about 1% or 1.5%.

Eshit Sheth: Sure.

Jairam Varadaraj: One is we had some unexpected cost and revenue losses, all that is behind us, we have cleaned it up. Now those entities are growing and we are beginning to see the results of the growth in the bottomline.

Eshit Sheth: Okay, Sir and you highlighted something on a staff cost where you said that for the next few years staff cost is going to be on the higher side, so do we expect the staff cost with the annual wage revision and the employee addition that you are talking about in terms of the leadership for our develop market, do we expect the staff cost to be pricing at the rate of 12%, 13% every year or will it be less?

Jairam Varadaraj: I do not know what the percentage growth is going to be year-on-year, but what I can say is depending upon our talent levels in India based on what market levels are we have a significant gap like I explained. We did some part of the gap correction and the gap this year we will continue to do that over multiple years we cannot afford to do it one shot. So how it is going to get converted it into a percentage increase in a given year is something that it is too early for me to predict. On the other hand internationally we need to build out the organization in line with our strategic priorities that we have identified for ourselves and strategic initiatives that we need to kick off, but I believe that these are all going to be temporary investment that may temporarily distort the percentages in the P&L, but in the long term we will just get normalize, not even long term, medium term.

Eshit Sheth: Okay that is great to hear. Sir one question I had also was on the new product range that we were talking about the oil free, which will be launched in second half of CY2018, I understand we are trying to reduce the gap between the traditional oil free and lubricated compressor, but will we have the same kind of contribution margins for the new products that we launch?

Jairam Varadaraj: Absolutely.

Eshit Sheth: That is all from my side. Good luck.

Moderator: Thank you. The next question is from the line of Kirthi Jain from Sundaram Mutual Fund. Please go ahead.

Kirthi Jain: In the opening remarks you had highlighted that some of the cost elements have got increased and impacted our profitability, are those negative factors starting to reverse like say we have been able to take price hikes?

Jairam Varadaraj: I did not mention anything about cost increase in my initial.

Kirthi Jain: No, you told that in the earlier opening reconciliation you have told that some of the cost like staff cost increase had not come or say material cost increase might not have come EBITDA would have been that much right Sir?

Jairam Varadaraj: No I said that we are fine; we add only manpower cost increase. Our EBITDA the gap between what we should have been and what we did was about 140 million of which close to 40 million is variable cost and close to 85 million is because of people cost increase.

Kirthi Jain: Okay.

Jairam Varadaraj: So people cost increase is a biggest shift in the ratios.

Kirthi Jain: Sir as activity level this has been picking up across various industries, is our fair consumptions are also increasing Sir or improving?

Jairam Varadaraj: Yes like I said the aftermarket business has grown that has grown it could be much higher, we are working on it and that is one of the initiatives that we ran with BCG, so it is beginning to gain some traction.

Kirthi Jain: Thanks a lot Sir.

Moderator: Thank you. Ladies and gentlemen this was the last question for today. I now hand over the floor back to Mr. Kamlesh Kotak of Asian Markets Securities for closing comments. Over to you Sir.

Kamlesh Kotak: Jai just wanted to understand couple of points. Do you want to touch upon water well and Centrifugal as a segment?

Jairam Varadaraj: Water well like I said, we have in our earlier calls I have said that we are regrouping and we are getting back into the market and that those are beginning to show some good results. Kamlesh I do not want to talk about specific numbers, but only to say that we are beginning to move ahead as per our plan. Centrifugal is still in our development phase, our prototypes are running machines, the two frames that we have developed, they are running, they are running with absolutely no issues at all, but we have now also started working towards building a front end organization, which will start focusing on the sale in India because we had to get the product ready, now that we are ready we are going to do that.

Kamlesh Kotak: By when we expect it to launch Sir?

Jairam Varadaraj: There is no launch really Kamlesh because we have already sold a few machines. This is about really going expanding our presence in the market. We will do that during 2018-19 we will start implementing.

Kamlesh Kotak: Okay and Sir just wanted to know understand this nine months number you gave about revenue in India and overseas, do you have the number for the same period last year?

Jairam Varadaraj: I do not have it in front of me. I gave you the total, India, last year was.

Kamlesh Kotak: Out of 9976 total.

Jairam Varadaraj: India was 6356 and the other one is 3600.

Kamlesh Kotak: Thank you. On behalf of Asian Markets we thank everyone for joining for the call. A special thank to Mr. Jairam and his team for providing the insight about the company's business and financial performance. With that we conclude the call. Any closing remarks Sir?

Jairam Varadaraj: I think it seems to me that if you do well the call last longer.

Kamlesh Kotak: That is true Sir and I think we are leading the entire cap good speck also in terms of the performance.

Jairam Varadaraj: Thank you Kamlesh.

Kamlesh Kotak: Thank you.

Moderator: Thank you very much. Ladies and gentlemen on behalf of Asian Markets Securities that concludes this conference call. Thank you for joining us. You may now disconnect your lines.