"Larsen & Toubro Limited Q3 & 9M FY 2017 Earnings Conference Call"

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MANAGEMENT: MR. R. SHANKAR RAMAN
CHIEF FINANCIAL OFFICER AND MEMBER OF THE BOARD
LARSEN & TOUBRO LIMITED

MR. YVS SRAVANKUMAR
EXECUTIVE VICE PRESIDENT: ACCOUNTS AND TAXATION
LARSEN & TOUBRO LIMITED

MR. MANISH KAYAL
ASSISTANT GENERAL MANAGER
INVESTOR RELATIONS, LARSEN & TOUBRO LIMITED

Moderator: Ladies and gentlemen, good evening, and welcome to the Larsen & Toubro Limited Q3 & 9M FY2017 Earnings Conference Call. 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 any 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. R. Shankar Raman -- CFO and Member of the Board. Thank you and over to you, Sir!

R. Shankar Raman: Thank you. Good evening, everybody, Shankar Raman here. You may find that surprising that I have surfaced on this call, not to get worried. Except that colleague, Mr. Arnob Mondal, who handles this call is indisposed today. So, I have joined the call to compensate partially what he could have contributed to the call.

I have also sought the help of my senior colleague**,** YVS Sravankumar -- who is Executive Vice President, In-charge of Financial Reporting and Taxation to join us. So, we are three of us in the call myself, Mr. Manish Kayal who is helping us from the Investor Relations team and Mr. YVS Sravankumar.

The sequence of the call would be that I would request Manish Kayal to make a quick presentation of what we have uploaded and then it can be followed up by Q&A. To the extent they relate to broader matters, I would be happy to respond. If there are some details which can be answered on the call between me, Mr. Sravankumar and Manish we will answer and if there are items which are of clarification nature and sub details we can take that offline.

I intend to close the call in 60 minutes' time from now. So, kindly do not repeat questions and I would appreciate if you can restrict your questioning to something that are of broader in nature. Any clarifications required, we are always available offline. Over to you Manish.

Manish Kayal: Thank you, Sir. Good evening, Ladies and Gentlemen. I am Manish Kayal from the Investor Relations Team. I hope everyone on the call have downloaded the presentation which was uploaded on our website.

So, let us start with the disclaimer slide #2. I will consider this as read. However, I would like to highlight key points here. Firstly, as you would all know that we make some forward-looking statements which may or may not materialize and second there are some risk and uncertainties related to these forward-looking statements which would go in direction that we may not have anticipated.

We go to the next slide on presentation outline. Presentation is spread into three parts: Performance Highlights, Performance Summary and Segments & Key Subsidiaries.

Next slide #5 pertains to Performance Highlights. This quarter has been mixed for L&T. Order inflow has seen a decline and revenue has witness muted growth. However, we are happy that few of our businesses have performed better and led to EBITDA growth of 19% YoY and recurring PAT growth of 39% YoY during the quarter.

Next slide #7 pertains to group level order inflow and order book. We have managed to bag fresh orders close to Rs. 35,000 crores this quarter and the decline in order inflow was due to muted domestic capex and delay in awards.

On the international market, order inflow witnessed 10% growth and this was mainly led by B&F, Heavy Civil, and Hydrocarbon segment. Order book remained more or less the same at Rs 2,58,600 crores and within that the international jobs contributes 29% as compared to 27% last year.

Next slide #8 deals with Group Performance, sales, and cost. Revenue growth has been muted for the quarter and like in Q2, Q3 also faced execution bumps in some of the domestic jobs which could have provided higher growth had there been smooth execution of the jobs.

International revenue is again coming to the rescue which grew faster than domestic revenue on strong execution in Infrastructure and Hydrocarbon segment. The international revenue grew by 9% for Q3FY17 YoY and 15% for the 9MFY17 YoY.

MCO expenses which is Manufacturing, Construction and Operating Expenses decreased by 2% this quarter on account of operational efficiencies in Hydrocarbon, MMH, and Heavy Engineering Businesses. As you know our Hydrocarbon and Heavy Engineering Businesses have been showing good margins this year. SG&A expenses during the quarter is higher due to higher provisioning in our Financial Services Business.

Next slide #9 pertains to Group Performance Summary. EBITDA has seen higher growth in this quarter despite muted revenue growth. Overall EBITDA grew by 19% which is due to margin improvement of 140 bps YoY. This is on account of margin improvement in few businesses which we will deal with in the respective business slides.

I would like to again remain you that, margins in our business are non-linear if seen on Q-o-Q basis and those are not indicative of long-term trends if considered in isolation.

This year we have registered lower interest charge on better fund management. Depreciation is higher and it is on account of asset value restatement of a Retail Mall upon monetization. Taxes for the quarter reduced on account of Deferred Tax adjustments and higher tax free dividend income.

Under "Share in profit / loss of JVs and Associates", as explained on earlier con-calls, we are consolidating the net profit and losses of few of our JVs and associates like road concessions, Forgings, MHPS JVs, etc. on equity method basis which means we consolidate at the PAT level under the new IndAS reporting standards. Further break-up to this side is given as an annexure to this presentation. IDPL concessions have witnessed lower losses this quarter, MHPS JVs performance was stable whereas, Forgings continues to contribute losses.

Net Profit has grown by 39% YoY and this was on account of operational efficiencies and turnaround in few of the businesses that we have observed this year.

Next slide #10 deals with Group Balance sheet. This slide is mainly for informational purpose. But there are few key points to note. Current Investments are now at a level of around Rs. 11,961 and the increase is mainly due to the inflow of cash that we have received from the IPO of L&T Infotech and L&T Tech Services during the year. And the other item that I would like to highlight here is our working capital has shown further improvement and currently stands at 21% of TTM sales versus 22% that we have reported in 1HFY17 results.

Next slide #11 deals with Group Cash Flow. This quarter again, we have witnessed robust operational cash flows of close to around Rs. 2,700 crores. Out of the total, around Rs. 1,000 crores have been contributed by reduction in net working capital. So, this is in line with our strategy of progressively reducing net working capital through tighter control, upfront business decisions and pulling back execution if necessary in case working capital increases in some of the projects.

If you see, our operational cash flows is sufficient to cover our fixed asset capex requirement for the quarter. Net borrowing is also lower for the year compared to previous year.

Next slide #13 gives you an overview of the businesses that we operate in and the composition of those businesses. Suffice to say that we have nine externally reported segments.

Next slide #14 deals with Segmental Breakup of Order. This slide is mainly for reference purpose and it shows that the infrastructure segment still accounts for bulk of the order inflow as well as unexecuted order book.

Share of Hydrocarbon business in total order book has increased this year which is due to robust growth in the order inflows witnessed in this segment.

As pointed out earlier, please note that revenues of Services business and other products businesses are grouped under order inflows as their sales arise from very short cycle order inflows.

We will now move to the next slide #15 on revenue breakup for 9MFY17. This slide is for reference purpose and there is not much of the change in the revenue mix. Better execution in international jobs led to increase in its total revenue from 35% in quarter two to 36% in Q3.

With that, we move to the next slide #16 on Infrastructure. Infrastructure remains our largest reportable segment and the revenue growth in this quarter has been moderate. Revenue has grown by 6% in Q3 and 7% for 9M. There are some overall readings that can be derived from the sales number which are: The execution environment is still not very robust though it has not deteriorated either and there are few projects where revenue was muted mainly due to regulatory clearances and clients slides issues that RSR mentioned in the Press Conference. Jobs in international market are progressing satisfactorily and according to schedule.

Despite challenging execution conditions, margins in the Infrastructure segments has improved this quarter. It improved from 7.2% to 8.3% in Q3 YoY. Heavy Civil and Power T&D businesses has witnessed better margins during Q3 and that has helped the overall margins. Cost reduction & design optimisation initiatives also helped margin improvement.

Next slide #17 deal with Power business: Revenue declined during the quarter mainly on account of lower order book and tapering revenues of Bangladesh Gas Projects as evident from the share of international revenue. Major portion of the Bangladesh jobs was completed up to the period ending Q2FY17 and hence, lower revenue in this quarter. Margins are affected because of higher proportion of cost jobs during the quarter.

I would like to point out here is that we do not consolidate the financials of MHPS JVs which gets consolidated at the PAT level.

Next slide #18 deals with Heavy Engineering business. Revenue growth is impacted by lower order book and the stage of execution of orders. Cost and time overruns has impacted the previous year margin and this year we have seen improved margins both in PPN business and Defence & Aerospace business.

Next slide #19 deals with Electrical and Automation Segment. Revenue growth in this business was impacted on muted industrial activity. However, our ESP business, which is the Electrical Standard Product business and C&A, which is Control & Automation Business, registered good growth during the quarter. Operational efficiencies led to margin improvement from 11.1% in Q3FY16 to 15.7% in Q3FY17.

Next slide #20 deals with Hydrocarbon segment. Higher revenue growth in Hydrocarbon segment is mainly due to strong project execution on our international and domestic jobs. Margins improved on operational efficiency, execution progress and the close out of legacy jobs.

Next slide #21 deals with IT & Tech Services Segment. As you know these companies are separately listed and they have declared their results about a week back. You could find a detailed presentation on their website and they have also conducted their quarterly conference call recently. I would only like to highlight the strategic perspective, which is that these companies are focusing on mining the existing clients, analytics and automation. I believe the rest of the slide is self-explanatory. And as I said earlier, one can find further details on their website.

Next slide #22 deals with "Others Segment". This is a residuary segment and comprises of businesses like Construction and Mining Equipment, MMH (Metallurgical and Material Handling business), Valves, Welding, Realty and finally the Shipbuilding business.

Weak industrial demand and low capacity utilization has continued to hamper the business environment for this segment. You would have seen that there is revenue growth of 4% during the quarter and that was due to strong execution pick up in MMH segment partially offset by muted growth in other segments. We have observed lower offtake in Construction and Mining Equipment and realty business. Shipbuilding business is impacted due to delayed Defence ordering. Higher margins in MMH business and lower losses in the Shipbuilding segment helped margins for the overall segment.

Next slide #23 deals with Developmental Projects Segment. To give you an overview this segment mainly constitutes Hyderabad Metro, Port and Power Development. Revenue was impacted due to lower construction revenue recognized in Hyderabad Metro and we also had maintenance shutdown of Nabha Power Plant that we observed in this quarter. Disputes related to receivables impacted the margins for this segment. Other developmental projects which are Road Concessions and Kudgi Transmission Line are getting consolidated at PAT level as per our new IndAS reporting.

Next slide #24 deals with L&T Finance Holdings. This is a separately listed company and we have presented the I-GAAP numbers here because this is what they have reported in their financial results few days back. However, for consolidating purpose, we consider IndAS financials. The strategy of the company is to improve ROE and to bring it to the top quartile of the industry by 2020. We have seen that improvement coming already this year. The ROE improved from 9.29% in Q3FY16 to 12.8% in Q3FY17.

Loans & Advances grew by 10% even in this difficult quarter and the MF business AUM (Asset Under Management) also witnessed robust growth of 40% YoY.

We also have few slides in the annexure, which we would request you to see.

And with that, I end the Presentation and handover the call back to RSR. Thank you.

R. Shankar Raman: Thanks, Manish. And I think we can start with questions.

Moderator: Thank you. Ladies and gentlemen, we will now begin with the Q&A Session. We take the first question from the line of Renu Baid from IIFL. Please go ahead.

Renu Baid: Reasonably good result, despite execution headwinds. Firstly, I wanted to understand the impact of demonetization and tardy pace of domestic execution. How are you seeing things improving post December or rather say for this calendar year and what gives you the confidence that we will be able to see reasonable domestic execution pick up happening across segments in the coming 12 months to 15 months.

R. Shankar Raman: It is very hard given the nature of our business to pin point variance in revenue based on demonetization. It has been a sudden disruption and it has taken few weeks for readjusting our own processes to deal with this. Our business is largely B2B and very less consumer facing. The only area where we were directly affected was in Toll Road Concessions business where we are required by the government to shut operations for 23 days and we lost close to Rs. 100 crores of revenue during the closure. Of course, there has been some efforts from the government on compensation the developers which we will know in due course. So, the headwinds on execution is not only due to demonetization. It could have a certain element impact but there are other larger elements at work as well that we deal with while executing the job. For example, when you win large projects there is a certain presumption about the pace at which the Right Of Way (ROW) would be made available, availability of clearances, utility shifting, etc. Many times we find that we have to co-ordinate between several agencies and most of them government to get the path cleared for us to execute those projects. We continue to find that the ROW issues continues to be a challenge. Things are getting better because the government wants to move ahead but action it is taking more time than what it ought to. That is one aspect why execution is delayed.

The other aspect is the entire issue of liquidity. Today, because of the market conditions a client may not want to complete the project on time because there is no motivation for him to time to market. This is due to residential apartment projects where the bookings have slowed down partly due to demonetization, partly may be due to the expectation that the price levels will correct, etc. Consequently, if the booking slows down, the cash flows to the developer slows down and hence, the payment to the construction company slows down. Wherever we sense such a situation we also proportionately slow down our execution to avoid piling up working capital for the benefit of sales. So, that is the second aspect.

The third aspect is many of these infrastructure projects are financed by commercial banks and considering the baggage of bad loans, disbursement clearances by the lenders engineers has been very time consuming, it has not been rapid as we use to see during good old days of 2008-10. So, that is adding to the delay process.

And forth, because of clients own working capital management, client tend to stagger the payment cycle if they are allowed by the contract. But assuming that we settle on a contract with all the terms and conditions, there is an effort to make sure that the cash flows comes in time.

So, given all of this, the hindrances to execution are multiple. So, we cannot wish them away because they are ground realities. So, we try to weave around all of these obstacles and move forward.

I am using your question to make another point. At the beginning of the year we guided for 12% to 15% revenue growth. We have about 6% growth for 9MFY17. Given that we normally run a very hefty fourth quarter both in terms of order inflow and revenue, we believe that the revenue growth for the year could be around 10%. This downward revision is after considering the environment in which we are operating.

Renu Baid: Sure. And sir, the second question is on the development projects we have seen loss is being booked primarily because of provision done on receivables. So, are these receivables largely related to Nabha Power and if possible, can we quantify what is the kind of provisions undertaken here?

R. Shankar Raman: The matter is subjudice. Hence, it becomes a little difficult to be very vocal about the quantum. But accounting prudence does demand that we recognize some of these slow-moving receivables and make appropriate provisions. So, we have done that in the course of this year and as the matter gets resolved in the court we would be far more clear as to what could be the impact because ultimately if something is disputed it could go in your favor, it could go against you, it could go somewhere midway, it all depends on how the interpretation of the court lie in this matter. So, at the moment, good to recognize that the receivables may not be 100% recoverable but exact quantum I think we will have to wait for few more quarters. My sense is it will take anywhere between three months to six months for us to get some clarity around this matter. And it is not likely to be very destabilizing as we see it now.

Moderator: Thank you. We take the next question from the line of Aditya Bhartia from Investec. Please go ahead.

Aditya Bhartia: Sir, our revised revenue and order flow guidance of 10% still kind of bakes in a fairly strong fourth quarter while you did mention that fourth quarter tends to be a fairly large quarter for us. But specifically, fourth quarter last year was a very-very strong for L&T. In that respect, are you seeing things improving and therefore that is something is driving this confidence?

R. Shankar Raman: Even if we don't build in delta improvement over the pattern, in the last few years Q4 has been contributing between 30% to 40% of the yearly revenues. So, I do believe that even if we were to perform at similar level 10% revenue growth for the year should be achievable. So, we are not really building in that delta at the moment. We are just extrapolating the pace at which we execute work in Q4 to arrive at the revised guidance of 10%.

We would be very surprised if we don't hit those levels because it has been fairly carefully assessed situation. But as they say we actually live and die where there are certainties in our business so, at the moment, the intent is to reach there and we will keep talking to you depending on how we progress.

Aditya Bhartia: Understood, sir. And sir, what could have been the sales consideration for Seawood's mall and why is it that we have taken impairment charge related to the same? Is it related to the mall only or is it related to commercial offices as well?

R. Shankar Raman: No, Aditya, it is only mall. I think the idea around Seawood is this project is a delayed project and the clearances have taken enormous time. I think we in way a paid the price for being a pioneer in doing Transit Oriented Development (TOD). If you look at the government documents, the number of stations identified for exploitation this way are many. So, the opportunity even in government's mind is compelling. But the ability of the local corporations and municipality to convert all of this into rapid clearances and approvals is still a challenge. We can hold on to this asset. We have completed the asset, we have progressed which is typical of L&T wherein we have completed the project whether it is financially rewarding or not, because that is one stigma we would like to avoid under all cost. So, we have completed certain aspects of this projects and the mall is ready. The station is getting built up and there will be some more entertainment zones in mall on top of the station that is coming in. And the commercial space is not completely exploited. So, there could be a Phase II and a Phase III to this project. What we have exited is Phase I and we have done this only to release our capital.

We have been speaking about the need to improve ROEs that can happen partly by releasing capital which are invested in areas which are not very productive and reinvest them in areas which are better. So, exiting mall even at the cost of some impairment we thought is a prudent decision and that is a reason why we have done this. Cash on hand today is far more valuable to us than compared to a potential upside on a mall few years down the line. Also, it is all linked to Airport if you know the Navi Mumbai Airport and we are not yet clear when this Airport will actually take shape. And this project was done in conjunction with such a development because it is fairly close to that potential new Airport. With the kind of uncertainty around the airport, we thought it is best to monetize.

Aditya Bhartia: Understood, sir. And sir, money in respect of this has been received and could you tell us what was the sales consideration?

R. Shankar Raman: The money is not yet completely received because there are few transaction related documentation that needs to be done. But the firm arrangement has been made and we are almost virtually recovering the cost that we have incurred in the asset.

Moderator: Thank you. We take the next question from the line of Sumit Kishore from J.P. Morgan. Please go ahead.

Sumit Kishore: Sir, we heard your comments on weak execution particularly in domestic infrastructure and the reasons thereof. Could you also give some qualitative color on how the margin profile of these orders are likely to pan out given the delay in execution? So, do the liquidity constraint, delay in getting clearances also weigh on margins going forward?

R. Shankar Raman: I think there are two buckets to this. One is projects which are struggling to progress as per schedule and there are projects which are proceeding as per schedule. It is a combination, it is unfair to place the whole thing onto lack of progress. Now on projects that are progressing well, we have been able to get the benefit of softer input cost over the past 24 months or so and hence been able to price them better. And secondly, I think we have also try to optimize the execution methodologies that we employ. As a company, we have been focusing more on automating the processes, we are focusing more on productivity, site management, shifting the cost to less cost zones, etc. Just a case in point is what we were executing in Middle-East, a lot of cost that we were incurring in supporting those projects in Middle East, we have shifted it back to India where we have a cost advantage. So, a combination of things, essentially focused on better cost management has led to improved margins on jobs that are progressing well. If the portfolio had only these jobs possibly we could have even seen a much better margin profile than what has emerged. These are getting pulled back because of jobs which are struggling a bit on execution and hence the smoothness with which we commission a site and complete the job is missing whereas snatches of commissioning, decommissioning, commissioning, etc., and the work disruption does have costs which are not completely reimbursed. So, to that extent the margin gets muted by these. But net of all of this, since we have been able to achieve the cost gains and productivity improvements, we feel confident that the projects which are progressing, we would be able to hold on to these margins.

In fact, we have guided for a 50-basis points improvement in EBITDA margins Ex-Services businesses for FY17 and I think we are on course to achieve that.

Sumit Kishore: Okay. And a couple of data related questions. Could you quantify the provisioning towards disputed receivables in Development Projects segment? And what was the bottom-line impact due to disruption of toll collection, you said Rs. 100 crores what is the bottom-line impacted to what extent?

R. Shankar Raman: Actually, if you see in toll projects, there is very little operating expenditure of 10% - 12% of revenue, the rest is depreciation and interest. So one can say that around 85% of the toll revenue could have a bottom-line impact in terms of PBT, tax is anyway a common adjustment. So, at the top-line Rs. 100 crores and may be at PBT level Rs. 80 odd crores could be the impact on account of stopping toll collection.

We have provided about Rs. 100 crores for the disputed receivables in DP Business and as I mentioned to an earlier query the adequacy of this will get determined as we move forward in the judicial matter.

Sumit Kishore: Thank you so much. And is the guidance for order inflow of 10%?

R. Shankar Raman: On Order Inflow, we are at 3% YoY growth for 9MFY17 and looking at the pipeline of jobs where we are L1, we think that we should be able to do about 10% order inflow growth for the year v/s 15% guidance at the beginning of the year. The slippages are not account of lost orders, they are on account of projects which are deferred. So, it is a bit of guessing game as to how much of that fall into Q4 and how much of it will fall into subsequent quarters. But the opportunity spectrum remains the same. It is just the challenge around the timing of them being awarded which is causing this kind of volatility to the estimated numbers.

Moderator: Thank you. We take the next question from the line of V. Balasubramaniam from Citi Research. Please go ahead.

V. Balasubramaniam: Sir, few questions on the stake sell. You were supposed to sell stake in the roads business to the CPPIB and Kattupalli Port to Adani Port. What is the status of these divestments? And when do you think this will get completed is my first question.

R. Shankar Raman: Okay. Let me take the second part of your first question. On Kattupali Port, the matter is before NCLT which is National Company Law Tribunal. We had filed our demerger application because the Port and the Shipyard are in the same entity so we have to demerge the port before they can be monetized. So, the demerger application has been transferred from High Court to NCLT which we have done, because the government came in with this new legislation saying that all the demerger application will be handled by NCLT. So, this has cost us some time delay because it is disruption to the process and we are still working towards closing the transaction by the end of the year. The commercials are already agreed upon with the buyer. It is just that the fine prints, in terms of approvals and necessary clearances by concerned authorities like pollution control board, etc. that we need to figure out. Hopefully, in the next 2 months, we should make progress on that. But at least there is no uncertainty around concluding this transaction.

In so far as the road portfolio is concerned, CPPIB had subscribed to the Compulsorily Convertible Preference Shares (CCPS) of the company and we have several dates on which the investor can exercise the option to convert. CPPIB has not so far exercised that option. There are further dates coming up in 2017-18 maybe they would choose to convert on one of those dates. The conversion and hence the sell down of equity in IDPL will happen on those conversion dates.

V. Balasubramaniam: Okay. Is there an option of Canadian Pension Fund not at all to convert?

R. Shankar Raman: No, it is compulsorily convertible.

V. Balasubramaniam: Okay. The second question is on Shipbuilding subsidiary and the Nuclear Forgings subsidiary which are making losses. The expectation was that on the Shipbuilding subsidiary there would be either the Submarine order or the Landing Platform Dock (LPD) order which could help turnaround the business. But it seems like government timelines keep getting extended and we do not hear anything about it now. If you could give an update on what exactly is happening to those potential orders which were supposed to turnaround the Shipbuilding business. And also how do you plan to deal with the losses in the Nuclear Forging business?

R. Shankar Raman: While outcome is still uncertain in terms of the Defence orders on the Shipbuilding, there are lots and lots of activities that is happening beneath the surface. I think there is active discussion that are happening with several stakeholders in so far as those orders are concerned. The stakeholders are foreign countries, Defence PSUs and private sector yards. So, the government has to make up its mind as to which configuration they would like to follow and on what terms. Because the price points that they anticipate in each of these alternatives are very different. So, the decision-making process is consuming time and adding to uncertainty. The Shipbuilding has been built citing these opportunities what we have been so far getting are orders like offshore petrol vessels, etc. which are reasonably small-sized orders in the context of the yard capacity. The LPD could be the big one. There is an Floating Dock order which is under execution which is reasonably sized. But the defining orders is going to be the types of LPD , Submarines, etc. We are hopeful that the ordering will happen. However, with every passing quarter, it seems one quarter closer. So, let us see, how it pans out. Let me tell you that the Shipyard asset is very strategic to L&T. We spend close to Rs. 100 crores a quarter in maintaining this facility and this is something that we just cannot abandon it. So we are continuing to hold it, we believe it has long-term benefit. We may have touched this segment ahead of time but I guess, we have to pay the price for being a bit of pioneer in this area.

Regarding Forge Shop, the entire economic scenario has changed dramatically with the dip in oil prices. The pricing for Forged components for Hydrocarbon sector have completely melted and makes it a bit unviable. There is excess capacity at almost all the global forge shops and they are running empty. So, consequently limited opportunities are getting consumed and also at the same time more and more countries are beginning to look at little more inward. There is a lot of clamor for in-sourcing of some of these parts. I wish India had done this few years ago, because all the Nuclear Forge that NPCIL was importing we could have possibly helped built through JVs in India itself. Though late, but NPCIL has now realized that we need to do something in domestic markets. The fortunes of Nuclear Power is beginning to look up because they are proceeding now with ordering from the Kudankulam Nuclear Power Project (next phases) and we think one or two of the other projects in Andhra Pradesh and Gujarat will move forward in the near future. Consequently, this Forge Shop would begin to get orders. At the same time, the order inflows will not be completely adequate to keep this facility busy. We also need to get some forging order for Defence equipment's. We do believe as and when the government takes the call for privatizing the Defence manufacturing, the Forge Shop will be a periphery beneficiary of this policy shift. So, we are reworking the revenue configuration and positioning ourselves for this opportunity. And hopefully by the time government is ready to place these orders the Forge Shop should be ready to reap benefits of these opportunities. We spend about Rs. 50 crores a quarter to support the facility in the meanwhile. But we do think that it has some hope over the next 2-3 years for it to breakeven and not put pressure on the consolidated results of the company.

V. Balasubramaniam: Okay. Sir, one last question from my side. The two businesses one is the internal real estate, your own land in which you are developing real estate that contributed almost Rs. 500 crores to your consolidated profit last year. And as you mentioned residential bookings have started slowing down. Does it not worry you that even though you might have projects, you might not have sufficient offtake to support that business over the next year or so? And secondly, if you could give some update on Hyderabad Metro when the first phase will get commissioned and when we will start seeing the numbers in the P&L? Thanks.

R. Shankar Raman: The strategy for real estate is more broader than the need to support the top-line or bottom-line. As we shifted a lot of our city centric factories and workshops to more cost-efficient zones, these real estates were available for commercial monetization. While there is a program in phases to monetize lands that we have in Powai, Chennai, Bangalore and likewise, there is not going to be an element of desperation to push product in the market. The land available is pretty large and is capable of being divided into phases gives us the flexibility to phase our offering in conjunction with the market sentiment. We never have been pricing our projects as elite. These are not very expensive projects. If I take Mumbai for example, I think there are projects where developers are charging anywhere between Rs. 7 crores to Rs. 10 crores per accommodation. These are premium or elite projects. L&T's offering is in to affordable category for the mid-segment of the market. We do believe that the investment momentum in the mid segment is going to be driven by the need to own homes and reduction in the interest rates for housing loans, etc. So, this is a space we would like to actually measure and move and not flood the market with unsold inventory. So, it is going to be a bit up and down in terms of how much it can contribute to the consolidated numbers. But if we look at it from a 10-year perspective between today and 2025 there could be a steady flow of profitability.

Whether it is going to be a steady flow of Rs. 500 crores or Rs. 300 crores or Rs. 700 crores I think the market sentiment will drive this. Also, the new Real Estate Regulations (RERA) actually favor developers who are institutions. To that extent, if there is a revival in real estate market, I do expect companies like L&T Realty to benefit because (a) the mortgaging process and the loan sanctioning process becomes better; (b) the client gets far more assured about cost quality, delivery timelines etc.

Now, moving to Hyderabad Metro, as you know it has been one of the largest projects that we are executing and it has gone through its own twist and turns by factors partly foreseen and partly unforeseen. State segregation, and other issues are not projected in advance and while we execute the project, we try to deal with each one of these issues as they get served. I must tell you that the project is about 70% complete today. There is only one way for L&T to move forward in this project and that is to complete it. The whole issue is on the time overrun and hence, the cost overrun. There is a good enough case for the government to acknowledge that the delay and hence, the cost increases are not due to L&T's own execution issues. There were several instances where because of governmental action we have to stop progress. So, we have made our case. One development over the last 6-7 months, has been that the government is far more engaged both at the Centre and State level, the most over the last four years. And they all view this project as important landmark. They cannot let this project fail, it is too big to fail. We are hopeful that between the Central Government viability gap funding, the State Government support and our own execution for the residuary part we should be able to close the project. The original schedule was June 2017 on which we have sought extension and informally, we do believe that we will get that extension. Normally, the government like to notify regarding extension at the nick of time. So, I do expect that in a few months down the line we will formally receive the extension. If we were to commence the projects all in one go, it will go all the way to the second half of Calendar 2018. We could well consider starting this in a phased manner but that decision is still not yet made because of all the discussion surrounding the total cost.

Moderator: Thank you. We take the next question from the line of Venugopal Garre from Bernstein. Please go ahead.

Venugopal Garre: Firstly, what is the proceeds from the Seawood's Phase-I divestment in terms of cash flows?

Secondly, IDPL road divestment, I could not understand the structure of that. We are aware of the compulsorily convertible share. But is that it or there is a further inflow required there?

And thirdly, what are the other monetisable assets you are looking for this year? Also, is Hyderabad Metro every monetisable as per the regulatory documents? So, these are my questions on the divestments.

R. Shankar Raman: Seawoods, we have not got the cash yet. So, in the subsequent quarter or subsequent quarters depends on the documentation completion and as and when this transaction is completed this cash flows will be evident in our statements. The cash flow that you have with you for 9M FY17 does not include Seawoods.

On your second question, CPPIB has brought in close to Rs. 2,000 crores will get converted into equity at some point in time and it will address the risk share that we were seeking to achieve in that platform. As a part of the business, the idea of the platform is to generate returns so, we constantly look at how the capital is employed. If some of the assets can be monetized and recirculation of the capital is possible, we would certainly do it. But the idea of monetization is more to recycle the capital for better returns rather than exit that space. CPPIB and L&T are in very close discussions around all of this.

On your third question, Hyderabad Metro is monetizable but at the right time. I think we need to make sure that we remove the uncertainty around the project to make the asset a little more predictable for potential investors.

On other assets, there are a few assets that are definitely monetizable. In the past, you have been seeing us monetizing small businesses which are profitable but subscale. So, that process will continue because thanks to much part of this 80 years being in license Raj, we have commissioned our businesses where we were allowed to commission. So, such of those had to be stream lined then in the context of the next 15 to 20 years, we need to be present in business which are globally scalable. So, in that context, this monetization in small measures will happen but that will not impact the overall numbers much, it is more to release the bandwidth of the management.

In the near future, there are bigger assets like Nabha Power which we would like to sell. However, there are some disputes and matter is subjudice as said earlier. We would like to plug those disputes before going to the market.

Venugopal Garre: Second question on orders, could you tell us the size of L1 positions at this juncture? And secondly the weak real estate market does it really impact your thought process on Parel Phase-II and Powai Phase-II projects? And thirdly, if you could get an idea of pipeline at this juncture for the fourth quarter?

R. Shankar Raman: We normally do not speculate on the L1s because L1 is a matter of comfort for us that there is visibility. But suffice to say there is a bit of good quantum of projects which are awaiting to be awarded and that will form part of that big Q4 that we normally talk about.

Secondly, in terms of weak real estate, I think the sales in Parel has come down. Fortunately, in Powai we do not have much inventory. We have not received the clearances for the subsequent Phase in Powai project. So, what is typically unsold in Phase-I are those ground level flats which normally are sold at the very end of a project. So, Powai does not have much inventory. Parel has some inventory but I think, because of the general sentiment, people are deferring their decisions. But my belief is, it will settle down. We will hold on to the prices because in the first place we were not overpriced.

We expect the demand to return. Subsequent phases in Parel will happen upon getting clearances.

Venugopal Garre: And sir, the 4Q pipeline?

R. Shankar Raman: If I just add the pipeline between what we have bid and where we are well-placed and where RFPs are in the process of being submission, I find Rs. 70,000 crores to Rs. 80,000 crores worth of orders. Now, how much of that will go in our favor and how much of that will fall in the subsequent quarter, is difficult to assess but we don't see shortage of opportunities. We are frustrated about the time it takes in terms of decision making around these opportunities.

Venugopal Garre: This Rs. 70,000 crores, Rs. 80,000 crores excluding L1 positions, right?

R. Shankar Raman: I told you, I do not want to speculate. Since, you said what kind of visibility I see in Q4, let me put it this way, if Gods were to be very kind to us we can have all the Rs. 80,000 crores.

Moderator: Thank you. We take the next question from the line of Inderjeet Bhatia from Macquarie. Please go ahead.

Inderjeet Bhatia: My first question is on this working capital. Now we have seen working capital improving tremendously this year. Between revenues and working capital, what kind of balancing act you are trying to do because working capital has already improved by more than the 2% target that we set out for this year. Can you please give more color on the tradeoff between working capital and revenues.

R. Shankar Raman: Inder, it has been a tough balancing act, because I think both are important in their own perspective. But very clearly, the call is to improve the capital efficiency and if working capital is getting built up because of the client's inability to pay on time that is a strict no-no in current conditions. But if working capital is increasing because of certain scheduled contract milestones we still go ahead and do this. Thanks for acknowledging that we have done some hard work and improved on the working capital front but the big quarter is ahead of us now and Q4 is normally a large quarter. So consequently, we have to wait for the big quarter to play out before we can actually open the Champagne bottle.

Inderjeet Bhatia: Okay. My second question is on the Middle East. In the past, we got positive on Middle East and then later curtailed back and then again we have started to take more orders in Hydrocarbon space in Middle East. So, can you just run through what is the thought process of management regarding Middle East at this point of time?

R. Shankar Raman: Yes, Middle East is going to be 25% of our pie as a broad strategy. Now, this stepping up & stepping down, etc., is very sectorial. In some seasons, we find thrust to infrastructure investment increasing so, you find that we participating in those bids a little more strongly than Hydrocarbon. Hydrocarbon took a pause and in a way, it was fortuitous because we were going through a period where we are closing out difficult jobs. We did not want to be distracted by tempting opportunities around that time. The decline in oil prices coincided with that and that took the distraction away from the Hydrocarbon plate and we were able to focus and close jobs and that is partly reason behind Hydrocarbon revival. But having said that, Infrastructure and Hydrocarbon are two areas where Middle East will continue to invest. We need to get very selective in projects that we pick and we need to get top class in execution. So, these are the two things that we are trying to achieve while participating today. In the earlier round, we got a touch carried away and we bid for projects simultaneously, spread ourselves too thin and the learnings out of that is to consolidate and bid for target projects and stay focused. So, Middle East continues to be an important area and within that Infrastructure and Hydrocarbon.

Moderator: Thank you. We take the next question from the line of Nitin Arora from Aviva Life Insurance. Please go ahead.

Nitin Arora: Sir, just a small doubt on this provisioning which you have taken in the depreciation line item, is it possible to quantify the amount and how should we look at your numbers of depreciation on a quarterly basis?

R. Shankar Raman: Rs. 270 crores is the amount we have taken as impairment that is clearly one-off. So, the rest will be following into a model pattern.

Nitin Arora: With respect to the order pipeline which was asked by Venu that is about Rs. 70,000 crores to Rs. 80,000 crores the best-case scenario you are looking at this point. But what is the broader strategy in terms of the capex when we see it is largely happening more in the Roads, in the T&Ds, Defence still not picked up yet. So, how are you looking to place yourself for the next year because we are growing in terms of our E&C top-line as well at a very big number as well as on the order intake side, so how you are looking to place your orders part?

R. Shankar Raman: See, despite all these uncertainties and difficulties we have close to 1 lakh crores of order in the nine months' period. It appears to me if I look at last few years the company's base level of ability to win at opportunities in the space in which we operate somewhere lies between. 1.25 lakh crores to 1.5 lakh crores. The delta needs to be provide by large ticket programs like the Airport program, Inland Waterway Program, extension of Dedicated Freight Corridor program, second Airport in Bombay, Trans Harbor Link, etc. These are the projects which will provide the momentum to take the company from one level of order wins to the next league. But today, we are looking at every opportunity be it big and medium and we find that there are more medium opportunities and big opportunities and in any case small opportunities we don't focus on. So, I would think that we are doing well given the limitation of the way the project business works and the capex cycles are going. We are not able to breakthrough and just move to the next league that I think is sometimes are factors beyond our control. But optimism continues that India needs tremendous amount of investment over the next 10 years if it wants to be anywhere near consistently growing economy. And if you look at investments in India we stand head and shoulder above any other next competitor in terms of technical skill and ability to marshal the resources required. We have remained financially sound despite all these difficulties. We might have opinions and expectations and disappointments around what the number ought to be and it is also true that we are punching below our weight in terms of what we can achieve as an organization. But we tend to be positive and I think at some point in time India will crack this code and sooner the better for us. If I look at next 10 years, I continue to remain very optimistic in this space in which we are occupying.

Nitin Arora: Can you share percentage of Defence out of the pipeline numbers of Rs. 70,000 crores to Rs. 80,000 crores?

R. Shankar Raman: May be about 15% could be difference out of this, approximately. It all depends, it is a big guessing game.

Moderator: Sure. We take the next question from the line of Charanjit Singh from B&K Securities. Please go ahead.

Charanjit Singh: Sir, in the buildings and factories segment, we have seen a significant dip in execution in Q3. So, just trying to understand what would be the quantum of dip and do you see this getting more severe going forward in Q4?

R. Shankar Raman: Okay. See, as things move normally and if we had not seen these dips possibly another Rs. 500 crores of top-line would have been possible. And I am saying this in the context of anyway certain difficult environment that is existing. So, anywhere between Rs. 500 crores to Rs. 600 crores could have been the difference on account of this additional slow down.

Charanjit Singh: Okay. Sir, but exactly in which kind of projects you are seeing this kind of slow down, are there institutional projects also slowing down?

R. Shankar Raman: These are residential largely, the elite buildings that we are executing has seen slow down. We are not very much into mass housing. The affordable homes, the progress is project specific.

Charanjit Singh: In the Power segment, we are running a lower order backlog. So, what is the outlook because if we look at the CEA report which talks about a very muted pipeline of thermal power projects in the near to medium term. So, how do you see this segment?

R. Shankar Raman: It is going to be a tough segment because the capacity outruns the addition every year. We have close to 25,000 MW of capacity per annum and we are ordering out around 8,000 MW. So, every competitor quotes a winning price which is why we find that the prices of the power plants are declining and hence the profitability. So, the issue is I think we will have to get strategic with that opportunity. There are a few projects where let us say because of our either competence or understanding of the lay of the land or the customer we can be at our competitive best. There are some projects which are fraught with the danger of progress and completion there we need to be very careful. So, in a sense you will find that these projects which are far and few are getting distributed among the various players. No single player has actually accumulated multiple orders, one goes to BHEL one goes to Doosan, one goes to L&T it has been distributed this way. I expect this to continue for some more time until government actually gets the demand back and for that they are getting schemes like UDAY operational and the TRANSCOs will have to get financially more solvent to be able to afford purchasing the capacity that is getting created. NTPC continues to invest but they are the lone investor and they are also investing at a pace which is very-very measured. So, next couple of years until manufacturing picks-up, until we as a country and community believe in consistent power but paid-for power, where we move away from populism of free power. If we work in tandem with the viability of the generating units, viability of the distribution units and public policy being in supportive of all of this, I think the Power sector will look up. So, it is going to be another hard grind for the next 2 years according to me for Power sector.

Moderator: Thank you. We take the next question from the line of Bhavin Vithlani from Axis Capital. Please go ahead.

Bhavin Vithlani: So, one question on the BOT. You highlighted about Rs. 100 crores losses because of demonetization but when I look at the profitability the losses from Rs. 150 crores a quarter has actually fallen to about Rs. 100 crores in the third quarter so, if you could help us with this?

R. Shankar Raman: Last year if you recall we have made provisions for some of the Sri Lankan project that we were pursuing and the project was not moving well and we wanted to actually check-out so we had done that.

We had also done some refinancing of road projects which meant restating the effective life of the project because the depreciation that we provide on the project is directly connected to the revenue and during refinancing the future revenues are restated based on current experiences. So, all of that meant we have to take a certain one-time knock in the P&L of the previous year and those are absent in the current year.

We also surrendered two projects i.e. Chennai-Tada and Pimpalgaon-Nasik, which were contributing to book loss in the past year and since we have surrendered we have stopped accruing the effect of those projects as well in the current period.

Bhavin Vithlani: On the Hyderabad Metro while you did mention about potentially starting it on a phase manner there was a news article last week where the Phase-I and Phase-II which is 56 kilometer is almost near in completion so, if you could give some timeline on commissioning.

R. Shankar Raman: I had answered this earlier in the call that we have an option of commissioning it in phases or we have an option of waiting out until the last bit of the track is completed. So, the timeline is between June 2017 to Dec 2018. We have not yet taken a call as to whether we will do segmental launch because all of this has to do something with the overall commercial negotiation which we are having with the government both State and Center. But then we are very close. It is in between this period that we are talking about that the project you will hear directly from us has having launched or otherwise.

Bhavin Vithlani: Okay. And last question is when I look at the Infrastructure segment we have seen about 2% growth in the order backlog and we have been targeting double-digit growth. So, are we expecting a pick-up in the execution going forward?

R. Shankar Raman: See, order book we do not target growth. What we target is obviously the order inflow and the revenues and order book is a consequence. So, in periods where the order inflow and the sales are flat, the order book also remains to be flat. We are targeting 10% revenue growth and 10% order inflow growth for FY17. The 10% revenue growth is where the hindrances about execution headwinds are involved, we do think that these are resolvable issues. For example, we got an order for Mumbai Metro the underground packages in South Mumbai. There are public interest litigations that are already being spoken about. So, being found competent financially & technically and getting the order is one, we also have to deal with large community stakeholders. So, the projects are very sensitive to all of these especially those projects which you do in crowed metropolis.

R. Shankar Raman: Thank you very much and we are open to receiving mails and calls outside of this call and in the interest of time I need to call time on this. Thank you very much for participating.

Moderator: Thank you. Sir, do you any closing remarks to give?

R. Shankar Raman: Well, all that I want to say the prospects continue to be very attractive. The Company's competencies are well lined up to these prospects. We do hope that the time loss in getting all of these programs implemented reduces going forward and processes are timely adhered to, the company looks forward to a period of very-very robust growth both in terms of top-line and bottom-line and we seek all your good wishes.

Moderator: Thank you. Ladies and gentlemen, on behalf of Larsen & Toubro Limited, that concludes this conference. Thank you for joining us and you may now disconnect your lines. Thank you.