



ñCEAT Limited 3QFY13 Results Conference Callò

February 7, 2013

MANAGEMENT: **MR. ANANT GOENKA– MANAGING DIRECTOR, CEAT**
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MODERATOR: **MR. ASHVIN SHETTY – ANALYST, AMBIT CAPITAL**



*CEAT Limited
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Moderator: Ladies and gentlemen, good day and welcome to CEAT Limited's 3QFY13 Results Conference Call hosted by Ambit Capital. As a reminder for the duration of this conference, all participants' lines will be in the 'listen only' mode and there will be an opportunity for you to ask questions at the end of today's presentation. Should you need assistance during the conference, please signal an operator by pressing * followed by 00 on your touchtone telephone. Please note that this conference is being recorded. I would now like to hand the conference over to Mr. Ashvin Shetty from Ambit Capital. Thank you.

Ashvin Shetty: Good afternoon, ladies and gentlemen. On behalf of Ambit Capital, I welcome you all to the 3QFY13 earnings conference call of CEAT Limited. CEAT is today represented by Managing Director, Mr. Anant Goenka and Chief Financial Officer, Mr. Manish Dugar. Without spending any further time I would like to hand over the call to Mr. Goenka for his opening remarks and then we can start the Q&A session. Over to you, sir.

Anant Goenka: Thanks, Ashvin. Good afternoon and a very warm welcome to CEAT's quarterly investor call. I am Anant Goenka, M.D. of CEAT and with me I have Manish Dugar, our CFO. Thank you very much for your interest in CEAT and I will briefly take you through the results and key parameters related to the results.

3Q has been a positive story for the company, primarily because volumes have gone up and raw material prices have come down. On a sequential quarter basis, there has been a 4% increase in volume across segment. Exports volumes have grown by about 11% QoQ while Replacement and OE and have grown by about 2%. On the raw materials side, NR prices have softened to about Rs175 per kg during the course of 3Q. And also we have seen a softening of prices across other raw materials which led to a decline in average RM cost by about 3.8% QoQ.

As we shared in the past conferences that UVR is one of our key product segments. I am happy to share that we launched our UVR ad campaign which was very well received by our customers and we have been able to convey the brand message to the target audience very strongly.

We have also announced recently our expansion plan in Bangladesh where we have entered into a joint venture with A K Khan & Company, one of the most-reputed business houses of Bangladesh. We are now in the final stages of purchasing the land for the proposed plant and we have begun seed marketing activities to build the brand which will be ramped up in the next few months.

As we had shared in the last call, we also gave VRS to our employees in Bhandup plant in the beginning of 3Q and, to this effect, we have given VRS to about 188 employees, paying a total of about 13.7 crores, which is reported as an exceptional item.

Going forward we expect the demand scenario to continue to be challenging. The OEM segment is looking like a big challenge. Macro demand drivers are looking to be pretty weak at this point of time; however, raw material prices have also come down, and we expect margins to continue to be strong going forward.

I will now hand over the call to Manish Dugar who can take you through the key financial parameters.

Manish Dugar:

Good afternoon, everyone and thanks, Anant. I will take you through the consolidated financials then the standalone financials of CEAT India and the financials of our joint venture in Sri Lanka. On a consolidated basis, net sales for the quarter stood at 1,239 crores which is up 13% on a YoY basis and which is 2% growth on a QoQ basis. Profit before tax on a consolidated basis was 32.6 crores after charging the VRS expenses of 13.7 crores and the making a payment of gratuity of about 6 crores to the employees who took the VRS. Keeping in line with our philosophy of reducing leverage through operational efficiency and tight working capital management, I am happy to report that we have been able to reduce our debt to 1.7 ratio of equity at an absolute figure of 1,257 crores from 1,350 crores just about two quarters back. This is despite the investment we made in Bangladesh, the regular capex, the VRS payment and the increase spending that we have in advertising which is primarily an investment for building the brand.

CEAT India in 3Q on a standalone basis delivered a revenue of 1,195 crores, registering a growth of 14% over 3Q of last year and an operating profit before tax of 25.1 crores compared to 3.5 crores of last year. On a sequential basis, the revenue was up by 2.6% driven by volume growth of 4% and a negative contribution by price and mix primarily on the realisation side of 1.5%. EBITDA percentage rose from 6.7% to 8.5% on a QoQ basis. The primary contributor to increasing PBT from 4.1 crores to 25.1 crores and EBITDA percentage of 6.7% to 8.5%, despite the expenses on VRS, gratuity on the VRS employees, increased ad spends and no dividend income from Bangladesh in this quarter versus 5 crores of dividend income in the prior quarter was primarily, as mentioned by Anant, was the 3.8% reduction in RM cost, and increased volume of sales. It is good to see that the growth in revenue is not just on a particular segment but it is across segments on QoQ as well as on YoY basis. There was reduction in interest cost because of, one, reduction in cost of funding and secondly, due to reduced levels of debt. All of these were partly offset by the impact of mix on realisation, although that mix contributed to a better profitability because it was primarily in the segments where we deliver higher profits.

Coming to Sri Lanka JV, operations reported a profit before tax of 14.6 crores on net sales of 102 crores and EBITDA margin improved to 17.1% from 13.6% in 3Q of last year.

With this, I now invite questions from you and we will be happy to answer them.

Moderator:

Thank you. Ladies and gentlemen, we will now begin with the question-and-answer session. The first question is from the line of Nishit Jalan from Nomura Securities. Please go ahead.

Nishit Jalan: I have got a question regarding your raw material cost. Can you throw some light as to what was the raw material cost average rubber price in this quarter and in last quarter?

Anant Goenka: Average rubber price was somewhere about Rs175 per kg roughly in 3Q.

Nishit Jalan: And what was it in 2Q?

Anant Goenka: 2Q was around Rs190 per kg.

Nishit Jalan: And currently, have you seen further reduction in rubber prices, like what are the prices currently that you are getting?

Anant Goenka: Rubber, as of today, stays at about Rs158 per kg but it has been pretty stable between Rs158 and Rs165 over the past two months time.

Nishit Jalan: All these prices are the Natural Rubber Board prices or your consumption prices?

Anant Goenka: This is our approximate consumption prices prevailing over a period of time. This is the ex-Cochin price but it was the weighted average based on our buying.

Nishit Jalan: For example, when the Rubber Index is at 160, what will be the consumption cost in that CEAT will incur?

Anant Goenka: It will be approximately the same amount, right. Rs1-2 up/down.

Manish Dugar: But just to explain that a bit, I think to some extent, it is dependent on inventory levels and how much is the mix of Imports and Domestic. So one cannot necessarily say it will be exactly that but if domestic prices are lower than the import prices and we do not have any inventory of opening stock of imported rubber then it should be in line with the Board prices.

Nishit Jalan: But what I wanted to understand was like you will incur some freight cost or some cost over and above the cost at which the rubber is showing in the index, right?

Manish Dugar: Yeah, that is called typically landed cost. What we shared with you is not the landed cost.

Nishit Jalan: That is the ex-Cochin cost, right?

Anant Goenka: That is right.

Nishit Jalan: What would be the broad range basically, the difference between this cost and the landed cost?

Manish Dugar: It should be anywhere around Rs15 to 20.

Nishit Jalan: And that will be primarily freight? What are the key cost head?

- Anant Goenka:** It would be freight and taxes.
- Nishit Jalan:** If rubber stays around current levels, do you see a further margin expansion in the fourth quarter or in the coming quarters?
- Anant Goenka:** 4Q should be better. Going forward, depending on how we are able to behave with respect to our selling prices, if we keep selling prices at current levels, then I think things should be better and rubber stays the same.
- Moderator:** Thank you. The next question is from the line of Srinivas Rao from Deutsche Bank. Please go ahead.
- Srinivas Rao:** Two questions. First, if you can throw some light on, you mentioned the demand environment is challenging. I mean, obviously, we can also see that reflected in the OEM numbers. But any sort of a commentary you could give on the Replacement demand; is that also dramatically slowed down? That is the first question. And secondly, as in the past cycles do you expect the Replacement demand to actually start or come before the actual OEM numbers start to show up?
- Anant Goenka:** Replacement demand has come down, I would say replacement demand is nearly flat. As I shared with you on a QoQ basis, replacement has grown by about 2%. So it is as good as nearly flat. 0 to 5% is the kind of growth that we are seeing. We expect this to continue going forward for some time. There are a few things. Even you have a slow down in mining activities which has had some impact. Slowdown in OEM demand has had an impact. Your overall macro economic situation with respect to your petrol prices, diesel prices going up, and interest cost getting affected. So all of this has had an impact on demand. Now, I do not see these things changing for the next four to six months in my view. It is only after that post some news with respect to investment in infrastructure, positive steps by the government, overall investment climate, mining, power, all of those things changing, I think demand should pick up. These things will take time in my view.
- Srinivas Rao:** As in the past does the replacement demand tend to kind of come before the actual OEM demand starts to improve?
- Anant Goenka:** No, in my view, it is very often the other way round. Generally, OEM demand picks up and replacement has an effect post a certain amount of time after that. So, OEM demand is really looking to be at a very low point at this point of time. Things are not looking good. I would say even going forward for the next couple of months or three months on the OEM front except for certain categories like utility vehicles and scooters, all the other segments are looking to be quite a challenge.
- Srinivas Rao:** And finally, the Tyre industry has been a big thrust towards radialisation of the Truck and Bus Tyres. Where do we stand today as an industry and CEAT as a company?

- Anant Goenka:** In the Commercial Vehicles segment, we are about 18-20% radialised, and it has gone up by about I would say 4-5% over the last one year. Radialisation is continuing, in my view.
- Srinivas Rao:** And in your case, what is your break-up of radial versus the normal bias tyres?
- Anant Goenka:** About 15%.
- Moderator:** Thank you. The next question is from the line of Srinath Krishnan from Sundaram Mutual Fund. Please go ahead.
- Srinath Krishnan:** If I look on a sequential basis, your realisations have declined. Is it more due to mix change or more of discounting that is happening at this point of time? And the second question is on capacity. You have been speaking of putting up the Bangladesh plant. So when is that expected to come up in the capex required from our side? And then in the current Halol capacity production, per day capacity, has it improved?
- Manish Dugar:** So far as the realisation is concerned, there has not been any price action. There has been some discounts which has been passed on to the customers but there has not been any pricing action so to speak. So what drop you see in the prices is primarily because of a change in the mix because of the OEM revenues going up significantly as compared to Replacement and Exports. So far as Bangladesh is concerned, like Anant mentioned, we have just signed the joint venture agreement as we are in the process of buying the land and only somewhere around last quarter of the next calendar year is when we expect the commercial production to commence.
- Srinath Krishnan:** And current capacity sir for us at this point of time?
- Anant Goenka:** Current capacity total or Halol?
- Srinath Krishnan:** Total and Halol.
- Anant Goenka:** Halol is currently at about 110 tonnes per day kind of production, and it will peak to 140 tonnes per day in about six months time. Right now, it is not a capability issue, it is more on the demand side that things are looking slow which is hampering production at this point of time. So Halol is ready to ramp up to at least about 120 tonnes per day in a short period of time. Overall capacity continues to be roughly the same with Halol ramping up. Assuming Halol is at about 140 tonnes per day plus 250 for our Bhandup plant, 200 for Nasik and about 170 tonnes outsourced. So I think it comes to about something like 600-700 tonnes is our total capacity. Bangladesh capex will be somewhere around 270-280 crores total.
- Srinath Krishnan:** If I have about 600 tonnes per day and for quarter it is about 54,000 tonnes total, but the volumes which you have given about is 53,000 tonnes. This does not include the outsourced figure, is it not or does that include for 3Q?
- Manish Dugar:** The sales will include outsource, the 600 tonnes per day that we spoke about; it will include outsourced.



- Anant Goenka:** 250 plus 200 plus about say 140 plus 170; it is about 750 tons per day. We are not operating at 750 tonnes per day. We are operating at about 85-90% capacity. So our capacity is slightly higher. We are operating at say 650 tonnes per day.
- Moderator:** Thank you. The next question is from the line of Basudeb Banerjee from Quant Capital. Please go ahead.
- Basudeb Banerjee:** A few questions. For the nine months to date, what is the attributable PAT from the Sri Lanka JV?
- Anant Goenka:** Our PBT is at about 40 crores. PAT would be say at about 33-34 crores roughly in nine months.
- Basudeb Banerjee:** That is the attributable PAT?
- Manish Dugar:** It is the consol financials, half of 32 crores has been included. So, 16 crores in the consol financials would be attributable to the Sri Lanka JV.
- Basudeb Banerjee:** So nine months, 16 crores PAT to date?
- Manish Dugar:** Yes.
- Basudeb Banerjee:** And second, what is the consolidated net debt as of today?
- Manish Dugar:** 1,257 crores.
- Basudeb Banerjee:** And what has been the reduction QoQ?
- Manish Dugar:** Two quarters back, this number was 1,350 crores.
- Basudeb Banerjee:** And down the line, what do you see the trend of debt repayment happening with the decent margins and somehow you can say bottoming out of volume?
- Manish Dugar:** Our focus continues to be on reducing the leverage. We are ensuring that other than essential capex, we do not spend on anything except for maybe things like advertisement. And so far as the Bangladesh investment is concerned, keeping in mind the planned investment required for Bangladesh, we expect that we should be able to continue seeing a reduction in debt levels, at least the same rate or kind of quantum that we had seen currently if not more.
- Basudeb Banerjee:** And last question, when do you see the pricing discipline in the industry going down the line in the next few months because the demand is in a very bad shape, to date not much of price cuts but you foresee any major price cuts in the coming months?
- Anant Goenka:** Very difficult to say. So even at current price levels if you look at pure EBITDA margin they are kind of not very high if you compare to other industry. Very difficult to say how

competition will react, what will happen. In my view, there could be discounting in certain category but overall if rubber prices do not go down then, I would say it is actually very difficult to give you an answer on that what will happen.

Moderator: Thank you. The next question is from the line of Surjeet Arora from Prabhudas Lilladher. Please go ahead.

Surjeet Arora: I have two questions on Sri Lanka JV. One is for the nine months period, what was the top-line for Sri Lankan operations?

Anant Goenka: Top-line was INR 300 crores.

Surjeet Arora: What was the tonnage in terms of sales?

Anant Goenka: About 12,000 per tonne.

Surjeet Arora: And my second question if I look at 3Q and compare it on a YoY basis for Sri Lankan operations your top-line has declined by around 8% but your volumes have grown by around 9%. So the realisation per kg, which is going down on a YoY basis, is it because of product mix or is it because of some pricing pressure you are seeing on the Sri Lankan operations?

Anant Goenka: It is mainly because of Exports actually. In terms of tonnage, you are exactly right on what you said. So, Exports give much lower realisation and the domestic market there has degrown substantially. So our domestic sales have de-grown there quite a bit but our Exports have gone up. The overall tonnage has been strong but value has gone down because of lower realisation in Exports. So, it is a market mix issue.

Surjeet Arora: What would be the Export proportion as an overall mix in Sri Lanka?

Anant Goenka: About 35%.

Surjeet Arora: One last question on your debt. You said debt was around 1,257 crores, and this includes your working capital also, the short-term debt also, right?

Manish Dugar: No, this is only the long-term debt and the project financing.

Surjeet Arora: What will be the working capital debt as of December?

Manish Dugar: On an overall basis because we take security deposit from our suppliers, if we net that off it actually will not be very significant. I can just get back to you with that number.

Moderator: Thank you. The next question is from the line of Ashutosh Tiwari from Equirus. Please go ahead.

- Ashutosh Tiwari:** My question is out of this 15% volume growth that you have shown basically, what was the OEM growth rate and replacement was how much?
- Anant Goenka:** OEM growth was much higher, 58% growth we have seen in the OEM segment, and whereas the Export would have grown by about 15% and replacement by about below 5%.
- Ashutosh Tiwari:** And what led this strong OEM growth? What are the contributors mainly?
- Anant Goenka:** We have entered into a lot of OEMs. We have grown well with Hero MotoCorp. We have entered into Bajaj after a long time, we also added more OEMs like Royal Enfield and we have grown with Tata Motors. So overall we have had good growth in a lot of our customers with the OEM.
- Ashutosh Tiwari:** And in terms of replacement demand industry-wise what kind of replacement demand are we looking at say Truck segment and the two-wheelers basically?
- Anant Goenka:** The overall demand situation has been very weak in the past nearly eight to nine months. So I do not see that going looking to be much better going forward. As I shared a little earlier, in my view, growth will be somewhere between 0% and 5% in the replacement segment going forward for the next four to six months.
- Ashutosh Tiwari:** What was the case for the last nine months basically?
- Anant Goenka:** Very similar situation. So growth has been nearly flat between again 0 and 5% kind of growth in the Replacement segment.
- Ashutosh Tiwari:** So with this kind of lower growth rate, because your margins for rubber are going down, so are you not seeing any discounting or pricing action by other players ?
- Anant Goenka:** What has happened is raw material prices actually came down quite sharply in a short period of time from October to November. Say rubber had inched up to Rs185 per kg to Rs190 per kg in a very short time. So, what has happened is that some material that was bought at that time was still getting consumed nearly on the way up to end of November or so. So maybe been a month and a half since actually we have been consuming the lower cost raw material. Some amount of discounting has begun in those categories where clearly supply is much higher but overall price reduction has not happened.
- Ashutosh Tiwari:** And as of now how much forward booking rubber not in terms of inventory, but your forward contracts and all?
- Anant Goenka:** Generally, we do forward booking to the extent of what we export. Historically, because imported raw materials has been cheaper than domestic raw materials, generally rubber what I am talking about. So, generally, we have been doing forward booking to the extent of the amount we export that is about say 20% to 22%. However, in the past few weeks, international

prices have been going up and domestic prices have been coming down. So it is no longer making sense to import any rubber. So we might not look at importing going forward.

Ashutosh Tiwari: So in terms of forward booking you are saying that it is quite low right now? Because in the last con-call you mentioned that two-three months booking was thereé .

Anant Goenka: It is for two-three months, not full month. I say two months, then for the next two months, we will be getting 20% rubber or other raw materials would be booked because the rest of it then you have to pay duty and then duty paid becomes more expensive than domestic.

Ashutosh Tiwari: Overtime basically you think that the disparity between say imported and domestic prices should actually be normalised. I mean, how do you see that basically because everybody is reporting much more over the last two-three months basically now that the benchmark prices are much higher? So maybe over time domestic prices will catch up with the benchmark prices globally?

Anant Goenka: The domestic prices are just a little bit lower. So international prices are say at about Rs160-163 ex-Cochin whereas domestic prices are at about Rs158-159. So it is nearly the same. In my view domestic prices should generally be higher because there is a duty component that comes in for imported rubber. So I would say that in my view I believe domestic prices will go up and exceed international rubber prices over time.

Manish Dugar: Surjeet, just to respond to your comment on the total debt level, including the working capital debt, the number against the Rs1,257 crores is close to Rs1,640 crores.

Moderator: Thank you. The next question is from the line of Jaineel Jhaveri from JNJ Holdings. Please go ahead.

Prashant Sarkar: This is Prashant Sarkar from JNJ Holdings. This is a question to the promoter basically. Basically, today your market cap is about 375 crores. Your book value is more than Rs200 and you have already made 110 crores PBT in the first nine months and assuming you made the same about 46 or 50 crores, so you are around 150-160 crores PBT for this year before extraordinary items. So there is available at around less than 2.5 times PBT to market cap. So I am just asking is, would the promoters not be interesting in buying back or doing some kind of a buyback either in an individual capacity or by the company?

Anant Goenka: This is something which I think is a call where we have taken some warrants, etc. So that is something which is part of what we keep doing over a period of time.

Manish Dugar: I think you would have seen us active in increasing our stake over a sustained period of time and promoters do believe strongly in the stocks and your observation is correct.

Prashant Sarkar: That is why I told that, this is the kind of valuation what are you getting at, 5,000 crores manufacturing company available at 370 crores market cap with nearly 150 crores PBT for this year, would the promoters not be interested in buying at least? Some thoughts from your side.

Anant Goenka: No, we have been increasing our shareholding. Last year we did raise it by about 4-5%.

Prashant Sarkar: So you are actively considering that?

Anant Goenka: That is right.

Ashvin Shetty: A couple of questions from my side. We discussed about a lot of pricing discipline on the replacement side. Any pressure you are witnessing on the OEM front or generally how is your arrangement with the OEM on pass-throughs?

Anant Goenka: With some OEMs, there is a formula-based system that does exist and very often it is on regular negotiations. So they will say that "Okay, raw materials prices have come down. So time to give us a discount". So, they are depending on each OEM. And yes, there is pressure from them to cut prices and that could very much happen in the next quarter or so.

Ashvin Shetty: International prices, what I believe is from the Rubber Board prices which we get is currently around Rs175 per kg, domestic prices around Rs158 or so. Why this anomaly? What is suppressing the domestic prices or what is actually leading to international prices actually going up, anything on that front?

Anant Goenka: I think domestic prices are at about Rs160-165 per kg if I remember right. I think \$3.3 per kg kind of pricing. And yeah, there is a difference at this point of time. What my guess as to why this has happened is overall demand has been down within India. Supplies, the output has been pretty strong with respect to growth tapping of rubber, etc. This is the peak season at this point of time. And internationally there has been some positive news with respect to the US recovery that has happened. China bouncing back or positive news on the China front. So all of that is perhaps having some impact. If you would ask me I would not have guessed that international prices would exceed domestic prices but this is what my guess is why it has happened on international pricing being higher than domestic.

Ashvin Shetty: Any possibility of domestic prices actually inching up towards that?

Anant Goenka: In my view, that generally should happen because there is a custom duty for imported rubber. So if there is a custom duty or domestic prices, generally should be higher which has been the case over the past two years. So it is only about 2.5 years ago or so I remember domestic prices being lower than international prices. So in my view, longer-term domestic prices should be higher.

Ashvin Shetty: Finally, on the competitive intensity, we expect in the next medium term like two years, there will be a lot of players actually entering the segment. How is CEAT actually gearing up to meet this in terms of for example, revving up the distribution network, etc.? What are the company's plans?

Anant Goenka: Yes, you have the large players, the MNCs coming in, in the next year-and-a-half or so; Bridgestone, Michelin, etc., is what we hear they are planning to come in. That I believe will

intensify competition. What we are planning to do is substantially focus on a few select categories like two-wheelers, utility vehicles and perhaps not specifically very aggressive on the commercial vehicles front where competition is going to be at the highest. Also, we are going to be focusing on our core strength which are going to be towards the B-Class and C-Class towns where our brand equity is very strong and we will continue to invest in our distribution network coming out with new products, focusing on smaller-sized tyres for commuter passengers and focusing on an overall message of giving excellent grip to the customers. So we want to capture that mindshare of the customers and these are the few things that we are focusing on to make sure that we have our strong share even when competition comes in.

- Moderator:** Thank you. The next question is from the line of Satish Kumar from Kotak Mahindra Bank. Please go ahead.
- Satish Kumar:** My question is on this Bangladesh project. You just shared the project cost would be around 270 crores. I wanted to know the source of funding for this project.
- Manish Dugar:** The project is funded in equity and debt and 33% will be equity and 67% will be debt. It will be in the ratio of shareholding by the joint venture partners.
- Satish Kumar:** So the debt has already tied up?
- Manish Dugar:** We are in the process of working on that and we still have time because given the project plan we believe that the first draw of money from the loan funds will not be required before August or September of 2013. So we are in the process of tying it up.
- Moderator:** Thank you. The next question is from the line of Srinath Krishnan from Sundaram Mutual Fund. Please go ahead.
- Srinath Krishnan:** If I look at your specialty business, it was around 5% of sales in FY10; it is about 8% now. Where do you see the segment moving and approximately what are the margins that you make because you are converting some portion of your cross ply capacity to specialty tyres?
- Anant Goenka:** On the specialty front, we are seeing actually tough times currently because we do export a good number of our tyres to Europe where there has been substantial slowdown in trading activities in ports, mines, etc. So actually the last year has not been a good year with respect to the specialty business. Going forward, we are planning to convert very small nearly negligible capacities to specialty. So you will not see much change in specialty; you might see a little bit of growth because of this change but I would say barely 10-15 tonnes per day type capacity that we are looking at changing from truck, bus, bias to specialty capacity.
- Moderator:** Thank you. The next question is from the line of Vishal Saraf from SBI Mutual Fund. Please go ahead.



Vishal Saraf: Just wanted to understand for this Bhandup plant, the VRS amount we have been giving for last two quarters. So how many employees we would have laid off?

Anant Goenka: About 188.

Vishal Saraf: This quarter number or cumulative until now?

Anant Goenka: This is the number which was the only VRS we have done in this financial year.

Vishal Saraf: And overall what would be the total employees there, and is this VRS payment likely to continue going ahead?

Anant Goenka: This is quite a routine VRS that we do and the total employees number would have come down from approximately 1,800 to 1,600 employees with this VRS. It could continue going forward, but we do not have any specific numbers in mind yet. So it could continue to between 200, 300 kind of employees per annum.

Vishal Saraf: So fourth quarter are we again likely to see some number?

Anant Goenka: No.

Vishal Saraf: And this 1,600 number is just the Bhandup employees strength?

Anant Goenka: Yes.

Vishal Saraf: And we plan to switch off from Bhandup, is there any timeline to that?

Anant Goenka: No, there is no timeline to Bhandup closure or anything like that yet.

Manish Dugar: We do not have a plan to close Bhandup as of now.

Vishal Saraf: And you also mentioned some 8 crores payment towards gratuity for these employees. So, the 13 crores amount includes that 8 crores or that is on top of this 13 crores?

Manish Dugar: Typically, when you do a VRS, the cost that is shown as an exceptional item is the actual pay out. Gratuity is something that is already in the books provided. The only thing that happens is when you make that payment you certainly have a shortfall in your corpus and hence you get a hit on your P&L for the excess gratuity that you have to provide. So if you see the people cost, you will see that the employee cost has gone up significantly and that is the explanation for people cost going up. That does not form a part of 14 crores.

Vishal Saraf: And that is how much?

Manish Dugar: Close to 6.5 crores.

- Vishal Saraf:** Also wanted to understand how the realisation would have moved in various segments over the last two-three quarters or say YoY numbers?
- Anant Goenka:** Realisation has come down a little bit from 2Q to 3Q and this as Manish had shared earlier was because of our market mix we have increased our sales quite substantially in the OEM segment while replacement has kind of remained stagnant. So OEM generally the pricing is lower. So our realisation has come down because of that and secondly there has been a small amount of discounting that has happened in some category. So both those have resulted in realisation drop.
- Vishal Saraf:** But within segments, OEM customers are the ones who get possibly the first benefit of price reduction or increase. So what kind of price reduction would have happened in OEM?
- Anant Goenka:** We have not taken any price drops in OEM.
- Vishal Saraf:** So the discounts we are mentioning is more into the replacement market, is it?
- Anant Goenka:** Replacement in certain category, yes.
- Vishal Saraf:** But like you said OEM customers is more of a pass-through for rubber. They would be also seeing rubber price and our average rubber costing. So are we likely to finalise some pass-through to them with a lag effect and hence we can see some cost reduction for the second quarter and the third quarter coming for us?
- Anant Goenka:** Yes, you could see some further drop in realisation with respect to OEM customers because rubber prices have come down and yes, there is a good chance that they may look at negotiating and having a price drop.
- Vishal Saraf:** But that could be only prospectively or have we already provided some amount for retrospective price reduction that you may give them?
- Anant Goenka:** Nothing in 3Q, if at all anything could come in Q4. But generally it would happen prospectively only.
- Vishal Saraf:** And broadly can you share what kind of price reduction you would have seen or the discount level you would have seen on a blended average basis in the replacement segment?
- Anant Goenka:** I am not sure if I have that number but it would be certainly less than 1% on an average. So in a certain category that would be say 2% or 3% kind of discount but that would be in a category which is less than 10% of our total sales, just as an example. So net-net it would be less than 1%.
- Vishal Saraf:** On the entire replacement market?
- Anant Goenka:** On everything, yes.

- Vishal Saraf:** And do you see that increasing, say, January onwards like we have already seen further 10% rubber cost reduction for us compared to the blended average for us?
- Anant Goenka:** There is no plan yet. Very difficult to say if competitioné .
- Vishal Saraf:** As of now you would not have taken. You already close to 1.5 months past.
- Anant Goenka:** No, nothing has been taken yet.
- Vishal Saraf:** And looking at the current average rubber cost of Rs157, 158 in the domestic market, and I believe our rubber cost was Rs175 you mentioned for 3Q, right?
- Anant Goenka:** That is right.
- Vishal Saraf:** So if say rubber stays at this level then again we will see a 10% kind of reduction in rubber cost for us on a sequential basis. Is that the right number to assume?
- Anant Goenka:** Not really 10%, but yes, there should be some improvement in rubber pricing, you are righté .
- Vishal Saraf:** Like you said there is Rs18-20 of freight, etc., also included. So for us to look at the trend, is it 174 compared to 157 or we need to compare it with some other numbers?
- Anant Goenka:** 174 compared to about 160, I would say, maybe 163, because it depends, maybe in December if rubber prices were at, say, 163, 164, as I said, today is 157 or 158, but it has been at about 160 to 165. So whatever we procure at 163, 164 in December, we would be consuming in January. But the number is right. You would be comparing 175 with 163 or whatever, that type of a number. I think I would like to correct freight. I think the freight and tax quantity might be slightly lower. It would be something like between 10 and 15 rather than 15 and 20.
- Vishal Saraf:** Also how is the realisation on the export side been? A lot of variables there, rupee depreciation and otherwise overall general demand scenario?
- Anant Goenka:** Export realisation has been very strong, at least our contribution has been strong because of the rupee situation. So at 54-55 kind of level export realisation has been strong. Yes, we have had to give some discounts because realisation had gone pretty high, but at this point of time Exports is very attractive.
- Vishal Saraf:** Can you give some indication of per kg realisation in INR terms or dollar terms for export market?
- Anant Goenka:** I won't be able to give you the exact numbers.
- Manish Dugar:** The numbers typically are in dollar terms, but you will see some softness because the dollar has now moved to 53.5 from the 55-55.5 level, but again export is a little more complicated than domestic given that it is a mix of some 50 countries and hence it is difficult to give one dollar

realisation number. It will vary significantly depending on whether you send to Indonesia or to Bangladesh or to Brazil.

Vishal Saraf: So if you could give us some indication how profitability in Exports market would have moved? Are we benefiting from the rupee depreciation?

Anant Goenka: Yes, certainly. So actually export is at least 5-7% more effective than other categories or than say even the replacement category.

Vishal Saraf: So as of now Exports have become more profitable segment is it?

Anant Goenka: Yes.

Vishal Saraf: And we have already been seeing the last three quarters share of Exports increase say from 20% of sales to 23%. Is this sort of realisation or are we seeing better volumes there and is the trend likely to continue?

Manish Dugar: Volume growth in Exports has actually not been very attractive. This year we have grown by about 16% on year-on-year for last quarter, but overall export tonnage has actually remained a little bit slow at this point of time. So a large amount of the growth is coming because of value itself.

Moderator: The next question is a follow-up from the line of Jaineel Jhaveri from JNJ Holdings. Please go ahead.

Jaineel Jhaveri: Just a couple of questions more. Basically, this quarter margin is about 8.9%. With continuous fall in rubber prices, do we see the fourth quarter to be substantially better in terms of operating margins?

Anant Goenka: Yes, fourth quarter should be better in terms of margins. I do not know whether substantially better or not, but it should be a little bit better.

Jaineel Jhaveri: Could it be 10-11% because you are already nearing 9%?

Anant Goenka: So that could be a little bit better. You can see the rubber prices have come down. So to that extent it should be a little bit better.

Jaineel Jhaveri: What about the other raw materials prices like carbon black, etc.?

Anant Goenka: Yes, most other raw materials have also come down. Carbon black has actually remained little bit flattish, 1-2% kind of growth in carbon black, but others have kind of gone down. Synthetic rubber has gone down by about 7-8%, fabric has come down, but rubber has come down a fair amount as well.

Jaineel Jhaveri: So basically next quarter definitely you are seeing an improvement in margins from this quarter?

- Anant Goenka:** There should be.
- Jaineel Jhaveri:** Are you expecting some sales growth or it would be flattish?
- Anant Goenka:** There could be some very marginal growth. So if you look sequentially our growth has been about say 2-3% QoQ and because of being the year end, a little bit because of seasonality, we can see some little bit of a better quarter in 4Q than 3Q. I am not talking on YoY growth, but sequential quarter growth.
- Jaineel Jhaveri:** So you are expecting slightly better sales with the better operating margins?
- Anant Goenka:** Yes.
- Jaineel Jhaveri:** And one more last question, any formal dividend payout policy formulated by the company.
- Anant Goenka:** Not really, that is decided by the board. There is no fixed quantity or anything that is decided on dividend.
- Jaineel Jhaveri:** So you have not finalised the payout policy, but roughly I mean what is the track record of paying? Last year you made about Rs5 and you paid 1, so it is about 20% payout. So should we expect that kind of number or it should go up?
- Anant Goenka:** I do not have an answer on that. I think it is a board decision. So I think perhaps you could just look at the past few years trend and may be assume that it will be something along those lines.
- Moderator:** The next question is a follow-up from the line of Srinivas Rao from Deutsche Bank. Please go ahead.
- Srinivas Rao:** Just one question. You mentioned in your outlook that you would like to focus on two-wheelers and UVs and kind of not compete hard on the commercial vehicles. Will that have an impact on your profitability that is margins because our understanding is that margins would be lower in two-wheelers and UVs as compared to CVs, that is not the case?
- Anant Goenka:** No, that is not the case at all. In fact commercial vehicles have the lowest margins. So that is part of the reason why we would be focusing on these categories.
- Srinivas Rao:** Alteration in the product mix between doing a truck-bus tyre versus a two wheeler tyre or a UV tyre, does that have an impact on capacity levels or any other associated cost?
- Anant Goenka:** From the cost side, yes, these products require more advertising and brand plays a bigger role and that is why we want to play out there because we can clearly demonstrate value and eventually command a premium. So at this point of time for example even in motorcycle tyres our pricing is the highest in the market and nearly 3% to 4% higher than the second highest. So that is one part of it. The second part of it is on the capacity side. Currently, we have set up a new plant in Halol which is ramping up. So that will help us with respect to the UV volume

increase over the next few months. And on the motorcycle side, we have an outsourced partner who is ready to take up capacities to as high as 30-40% increase over the next one year as well. So capacities are pretty tied up for strong growth in the next year, year-and-a half.

- Moderator:** Thank you. The next question is from the line of Silky Jain from Nirmal Bang. Please go ahead.
- Silky Jain:** Sir we would like to know what is our current market share in the two-wheeler market?
- Anant Goenka:** Our current market share should be approximately around 18% or so.
- Silky Jain:** Sir it has remained flat broadly on the QoQ basis. If we see in the last quarter also it was around 18 to 19%.
- Anant Goenka:** Yes, it would be somewhere around the similar range at this point of time. Actually market data over the past few months has been a little difficult to gather, and so it is very difficult to give exact quantities. Over a period of time we will be able to give you a better update in the next quarter. It is more because of a lack of data at this point of time that I am not being able to give you a very clear answer on this.
- Silky Jain:** So have we seen some improvement if we cannot quote in percentage terms but on an absolute basis, we are seeing some improvement in the market in the two-wheelers?
- Anant Goenka:** Yes, last year same quarter, our motorcycle sales have gone up by 25% in volume terms whereas the market has actually remained nearly flat or de-grown in a way. I would say that clearly our market share has gone up and based on our calculations it has gone up, in my view, by about 4% to 5%, but I am not able to give you an exact number because market data is not very easily available on this.
- Silky Jain:** And sir one more thing what will be our capex guidance for FY13 and FY14, like broadly you said for the Bangladesh plant, like how much would be in FY13 and 14 if you can give.
- Manish Dugar:** Our normal capital expenditure Silky is in the range of 50 to 60 crores per year and we expect it to remain in similar range outside of the Bangladesh investment.
- Silky Jain:** Sir you mentioned that you have witnessed some increase in carbon black prices, and so primarily this was because of the safeguard duty, which was imposed on carbon black from China. This was purely due to that reason or some other reason?
- Anant Goenka:** No, our pricing in carbon black is generally fixed with respect to a formula. So it generally follows a certain index. I would agree with you there is enough advance licence that a lot us have where we can look at still purchasing on a duty free basis.
- Silky Jain:** So we do not see a significant impact happening due to the imposition of this duty on raw material cost.



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- Anant Goenka:** Not right now yes. Because we can still procure duty free from low-cost country like China because we have advance licences.
- Silky Jain:** Okay apart from China do we import from any other countries as well?
- Anant Goenka:** No, I think only China, in my view.
- Silky Jain:** Okay sir another question was like one of our competitors was talking about having a production cut. So like are we also looking on the same terms like we are witnessing an overall slowdown? So are we looking out for some production cuts may be in FY14?
- Anant Goenka:** Yes, so production cuts have been pretty much quite a norm at this point of time. So we do take production cuts once in a while and so say in a quarter 3, 4, 5 days a month, we have to shut down a few plants. So that does happen. We are operating at about 85 to 90% capacity utilisation.
- Silky Jain:** So we do not see any significant downsizing. We would be operating at the same levels or like may be we can see some downsizing from here, may be 75 to 80% of capacity utilisation.
- Anant Goenka:** I don't think so. I think it should be at the current level.
- Silky Jain:** We are very much comfortable in maintaining the current momentum?
- Anant Goenka:** We would prefer the higher capacity utilisation, but I guess this is the market situation at this point of time.
- Moderator:** Thank you. The next question is from the line of Basudeb Banerjee from Quant Capital. Please go ahead.
- Basudeb Banerjee:** Yes, a few questions sir. As you mentioned that 270 crore of Bangladesh investment that is the full investment from your side I suppose.
- Manish Dugar:** Basudeb, this is Manish here. 270 to 280 crores is the total requirement, which is to be contributed by both the partners. It is not just CEAT India's contribution.
- Basudeb Banerjee:** But sir in the press note, which you put on the BSE around \$67 million, and so if I take 70% of that and so it comes out much higher from CEAT's perspective.
- Manish Dugar:** So you know the variation could be because of potential expansion that we would have included in that number. Currently, what we have signed off, which we are executing on adds up to 270 to 280 crores.
- Basudeb Banerjee:** So we should take 70% of 270 as CEAT's contribution?
- Manish Dugar:** In the immediate future yes and of that 70%, 33% will be equity and the balance will be debt.

- Basudeb Banerjee:** And sir, two more things I might have missed out, your staff cost was up almost 10% quarter-on-quarter. Anything special behind that?
- Manish Dugar:** Yes, so you know the VRS that we did the pay out for VRS was 14 crores, but the side effect of that was that we had to pay out the gratuity against those 188 employees, which was about 6.5 crores. And after that gratuity payout because of the actuarial valuation we had to reinstate the corpus of the gratuity amount and that came in as an impact on the people cost. So the primary reason for the people cost going up is because the gratuity payout happened; however, the actuarial valuation led to close to 12 crore provisioning on gratuity which normally in a year is about 3 to 4 crores.
- Basudeb Banerjee:** And for how many quarters, sir, this VRS scheme will continue?
- Manish Dugar:** This was done and closed. This 13.5-14 crores is the total cost and we are not expecting anything more beyond this.
- Basudeb Banerjee:** And next thing is sir as mentioned earlier you were undergoing a project with McKinsey. What is the update on that and what kind of costs you have incurred this quarter on that?
- Manish Dugar:** So the cost that we are incurring is same on a quarter on quarter basis, and so there is no incremental cost this quarter over last quarter. It is the same number. From a benefit perspective as Anant was mentioning, we have clearly seen Halol ramping up in terms of production from 70 metric tonnes per day to close to 105 on average and on few days we have seen 125 and actually the discussion is now more on how to get volumes and sales rather than how to get the production up.
- Basudeb Banerjee:** So this 13 crore increase in other expenditure is primarily because of the ad campaign for SUV tyres?
- Manish Dugar:** That is right.
- Moderator:** Thank you. The next question is from the line of Ashutosh Tiwari from Equirus. Please go ahead.
- Ashutosh Tiwari:** Your export portion, what is the product mix actually and you are catering to which segment mainly?
- Anant Goenka:** The products mix in Exports, largest sale in Exports is in the LCV segment followed by truck-bus bias and truck-bus radial and then you have the specialty tyres, which is the balance amount. Thus, specialty means your mining large off-road tyres.
- Ashutosh Tiwari:** Okay, 7% specialty is completely exported?
- Anant Goenka:** No, about 60% would be exported.

- Ashutosh Tiwari:** And that is mainly catering to the mining only or farms also.
- Anant Goenka:** Mining, majority port mines, and some amount is farms.
- Ashutosh Tiwari:** Okay, in those markets, are you seeing some pricing pressure or pricing is kind ofé ..
- Anant Goenka:** We are seeing overall demand to be low at this point of time rather than pricing pressure. In Exports generally they look at a quality product and if your product is of good quality they are not so price conscious.
- Ashutosh Tiwari:** But because rubber prices have fallen so much in those markets also, but haven't you seen any pricing pressure over the last six months or last three months?
- Anant Goenka:** Yes, we have taken some price cuts overall in Exports depending on the country and depending on the nature of growth in each country. So, Africa has been growing well and we have been less generous on price cuts there whereas Europe has seen a higher drop in sales.
- Ashutosh Tiwari:** Higher drop in the selling prices or volume sales?
- Anant Goenka:** And as a result some amount in selling prices also.
- Ashutosh Tiwari:** And sir normally how is the replacement pricing different from OEM pricing in India?
- Anant Goenka:** There is a pretty decent difference between the two. So OEM pricing is at a much higher discount than replacement pricing. In terms of percentage, it really depends on category to category and that is very difficult to say. It can vary from anything from 2-3% discount to about 10% difference.
- Ashutosh Tiwari:** In case of truck-bus, what is the discount?
- Anant Goenka:** I think it could be about 5 to 7% or so.
- Moderator:** Thank you. The next question is from the line of Nidhi Singhania from Kotak Mahindra Bank. Please go ahead.
- Nidhi Singhania:** Sir, I just wanted to check that as you mentioned that the Bhandup plant currently is at a capacity of 250 tonnes per day and you have been declaring VRS also. What production levels do you expect the Bhandup plant to continue? Also, any plans to shift because of the higher production cost at the Bhandup facility? Do you have any plan to shift that production to some place else or any plans of developing the Ambarnath land?
- Anant Goenka:** Bhandup is a 250 tonne per day capacity. We are currently operating at about 215 to 220 tonnes per day capacity. It is clearly our largest plant at this point of time giving us a revenue of over 1,500 crore. So until a new plant is not put up, we cannot move out of Bhandup. There is no plan to set up a new plant at this point of time in India. So we are planning to continue with Bhandup

for now. I agree with you that it is relatively higher cost location because it is an old plant, but it is a very large plant and we are not looking at closing it at this point of time.

Nidhi Singhanian: Sir, no plans of any other facility developing in India?

Anant Goenka: Not yet. No we have acquired some land in Ambarnath a few years ago, but we have not yet taken a call to move or anything at this point of time.

Moderator: Thank you. The next question is a follow-up from the line of Vishal Saraf from SBI Mutual Fund. Please go ahead.

Vishal Saraf: Sir just one more clarification, the employees reduction in Bhandup that is more on account of lower operating levels or there is better operating efficiencies and mechanisation.

Anant Goenka: Yeah it is because of lower operating levels plus the productivity of the plant is low. So we would be looking at improving our productivity in the plant. We had excess manpower there and we would like to bring it down and over time you have people who want to retire because of medical condition, etc. So, we offer them the scheme that they are welcome to retire and take a VRS.

Vishal Saraf: We are now at 215. If you go back to 250, do we need more employees or we will be able to continue with the similar number?

Anant Goenka: We will be able to continue. We might need a few additional contract workmen, but we don't need to recruit permanent workmen necessarily for this job.

Vishal Saraf: And the difference in the cost of two would be very high, is it? Can you give some number?

Anant Goenka: The difference between the two could as high as Rs 20,000 per person per month.

Moderator: Thank you. Ladies and gentleman that was the last question. I would now like to hand the flow back to Mr. Ashvin Shetty for closing comments.

Ashvin Shetty: On behalf of Ambit Capital, I would like to thank the management of CEAT for giving us an opportunity to host this call. I will also like to thank all the participants for joining in. Thanks.

Moderator: Ladies and gentlemen on behalf of Ambit Capital that concludes this conference call. Thank you for joining us and you may now disconnect your line.