"CEAT Limited
Q2 FY2019 Earnings Conference Call"

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Moderator: Ladies and gentlemen good day and welcome to the CEAT Limited Q2 FY2019 Earnings Conference Call hosted by Elara Securities Private Limited. As a reminder, all participant lines will be in the listen-only mode. There will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing "*" then "0" on your touchtone telephone. Please note that this conference is being recorded. I now hand the conference over to Mr. Jay Kale from Elara Securities. Thank you and over to you, Mr. Kale!

Jay Kale: Thanks. Good evening and welcome to all the participants for the CEAT Q2 FY2019 post results earnings call. From the management we have with us Mr. Anant Goenka – Managing Director, and Mr. Kumar Subbiah – CFO of CEAT Limited. I would like to hand over the call to the management for their opening remarks followed by the Q&A. Over to you Sir!

Anant Goenka: Thanks Jay. Good evening and a very warm welcome to CEATs Earnings Call. I am Anant Goenka, Managing Director and I have with me our CFO, Kumar Subbiah. I will give you an update of Q2 earnings update followed by financial commentary by Kumar after which we will be happy to take questions.

For Q2 FY2019 our standalone revenue from operations grew by about 2.6% on a quarter-on-quarter basis and 13.6% on a year-on-year basis, which was at 1718 Crores. The standalone EBITDA margin was at 9.1% with 167 Crores and PAT was at 4.4% at 75 Crores.

Revenue across all markets registered strong growth on a year-on-year basis. OEM exports as well as replacement markets all are showed strong buoyancy. On the volume front on the standalone basis our growth was at 12.4% on a year-on-year basis and 1.4% growth on a quarter-on-quarter basis.

With respect to raw materials our prices went up by about 3.5% on a quarter-on-quarter basis and 4% on year-on-year basis and on the pricing front we took on an average of price hike of 1.7% across products and BUs during Q2. We have further taken a price hike of approximately 4% in our two-wheeler segment as on October 15th and approximately 2% price hike in the truck radial segment.

A few other highlights for the quarter was that we partnered with FC Torino which is the football club based in Turin, Italy for two years. This deal will help strengthen our brand presence in Europe where we have recently launched our passenger car radial tyres.

Our Nagpur facility was awarded the British Safety Council Sword of Honour during the quarter, reflection of our focus on safety in our plant. On the OEM front, we started supplying tyres to a new OEM on the two-wheeler side, which is Cleveland Cycle Work. It is a premium US bike manufacturer and we have gained entry into their Ace Deluxe Model.

With these updates for the quarter I now hand over our call to our CFO, Mr. Kumar Subbiah.

Kumar Subbiah: Thank you Anant. Ladies and gentlemen, greeting of the day. I will present before you the key financials.

Our Q2 consolidated net revenue from operations grew by about 2.8% quarter-on-quarter and by about 15.2% year-on-year and stood at 1755 Crores. The growth was both on account of volumes and price.

Our consolidated gross margins witnessed a drop about 1.2% largely on account of higher raw material prices. Increase in raw material prices was higher and it has partly offset by increase in prices and favorable mix.

Our consolidated EBITDA stood at 9.4% for Q2 a contraction of about 118 basis points sequentially. Our EBITDA was impacted largely by increase in raw material prices and increase in employee cost during the quarter. Our employee cost was sequentially up by about 22 Crores partly on account of increase in salaries during our annual pay cycle in July. Addition of employees at our new factories predominantly in Nagpur and also a long-term settlement, which involved payment to workmen retrospectively at two of our factories Bhandup and Nashik.

Our other expenses were higher primarily on account of higher level of production activities at the factories. Though our advertisement expenses were down sequentially but on year-on-year basis were higher as we ran extensive campaigns with KBC and during the India, England Cricket Match Series.

Our consolidated net profit for the quarter stood at 63 Crores in Q2 a sequential decline of about 11.7% has a decline in EBITDA had an impact on PAT. We maintained tight control on our cash flows during the year, a continuation of what we did in the last year. We took several initiatives to reduce our working capital that helped to reduce our working capital by about 141 Crores in the first half of the year and that includes about 40 Crores in quarter two of the year. Our debt equity remains healthy at 0.34 on consolidated basis and at 0.28 on standalone basis.

With this we will now open the Q&A. Thank you.

Moderator: Thank you very much Sir. Ladies and gentlemen we will now begin the question and answer session. The first question is from the line of Amyn Pirani from Deutsche Bank. Please go ahead.

Amyn Pirani: Good afternoon. Thanks for the opportunity. My first question is actually on the price hike that you mentioned. So this two-wheeler price hike of 4% can you help me understand is an industry phenomenon now or this is something that you only have done unilaterally?

Kumar Subbiah: No, I think we took a small price hike sometime in September unilaterally, but October I do understand that there could be others who have taken price increase.

Amyn Pirani: This does mark a departure from what we had seen for most of the last 12 months so it is a positive departure if I can say that.

Kumar Subbiah: Yes, it is a departure.

Amyn Pirani: Secondly on the overall price hikes in the other segments can you help us understand what is the cumulative price hikes that you have taken in trucks as well in passenger vehicle from the beginning of the year?

Kumar Subbiah: Yes, approximately we have taken a price hike of about 5% say on a year-to-date basis across all categories, quite well divided equally across most categories so given between truck and passenger and two-wheeler, I would say not more than say 0.5%, 0.6% variation. So, it is somebody's at some categories at 4.2%, somebody is at some categories at 5.5%, 5.6%, so approximately 5% YTD, which means have today that is not only September in but including October as well.

Amyn Pirani: That is helpful. Secondly on the employee cost the deviation that was mentioned, can you quantify how much was the retrospective number, which may not be a recurring number going forward?

Kumar Subbiah: Yes, I think about 7 to 10 Crores would be a onetime cost that we incurred some of it is retrospective, some of it is relating to some onetime bonus kind of expenditures that was there.

Amyn Pirani: Just lastly obviously your debt management has been quite impressive but as year-to-date, what is the capex that you have already done for the year and what is the guidance for the full year now?

Anant Goenka: Far we have incurred about 440 Crores in the first half of the year; our guidance for the year is about 1300 to 1500 Crores.

Amyn Pirani: That remains I think more or less about what you had talked about earlier?

Anant Goenka: Yes in the past, in the earlier quarters we have indicated 1500 to 1700 Crores and now we would like it to be 1300 to 1500 Crores.

Amyn Pirani: Thanks for the opportunity. I will come back in the queue.

Moderator: Thank you. The next question is from the line of Chirag Shah from Edelweiss Securities. Please go ahead.

Chirag Shah: Thank for the opportunity. One can you help us understand the cost pressures going ahead how do you look at from here on?

Kumar Subbiah: Primarily raw material cost we do expect that to continue to go up over the next three months. I would say approximately about 1.5% increase in our raw material prices every month for the next three months so that is approximately for between 4% and 5% increase in RM till end of December after that things should stabilize because this is at current crude prices.

Chirag Shah: So this is largely because of crude prices because the rubber is largely stable?

Kumar Subbiah: Crude and rupee.

Chirag Shah: Crude and rupee, okay. This is a reasonably steep jump actually fair point. Second question is on the can you just indicate how is the replacement demand looking because there are lot of news flows that festive demand at the OEM level is reasonably weak, but how is the replacement demand at ground level?

Anant Goenka: No we are quite optimistic about demand situation. I think growth will continue to be strong in my view and so we are quite overall positive across categories to see good growth. We have been seeing it for the last few quarters and it appears from the market that demand is strong.

Chirag Shah: So can we expect this double-digit volume rate to sustain?

Anant Goenka: Yes, for the short-term for sure long-term tough to say but I think things are looking good. We also have our truck radial capacity that will come on stream towards the latter half of this year so with some of that also coming on stream double-digit growth should be possible.

Chirag Shah: I was just coming to that radial plant so can you just explain the ramp up any changes in that because it is coming up stream in the last quarter and in terms of ramp up how do you look at it?

Kumar Subbiah: So no change in our expectation in terms of ramp up or timelines. We are largely on track. Plant is I think in a good shape near about 90% completion and I would say by Q4 of this year we start seeing volumes coming in. The total capacity is about 80000 tyres per month capacity from this new plant and it will take about a year and a half to reach full capacity. So like any plants maybe we will start off with somewhere around I do not know the exact numbers, but somewhere around 3000 to 5000 tyres initially which will ramp up I would say by 3000, 4000 tyres every month but I can get back to you with the exact details later, but between say year and a half we should reach full capacity.

Chirag Shah: This is helpful. Thank you.

Moderator: Thank you. The next question is from the line of Jinesh Gandhi from Motilal Oswal. Please go ahead.

Jinesh Gandhi: My question pertains to the RM cost in this quarter so Q-o-Q if we see it has been pretty stable as percentage of sales so is it largely because of the price increases or this will also mix benefit which we have seen in this quarter?

Kumar Subbiah: RM cost as a percentage has moved up last quarter versus the previous quarter and partly offset by price increase partly by favorable category mix and there is still a gap between RM cost increase and price that led to drop in margins.

Jinesh Gandhi: Second question pertains on the capex side so while you gave update on the TBR capacity are we on track for the PCR capacity and OTR as well?

Kumar Subbiah: Yes so with respect to TBR capacity we expect as again we are on track on our PCR capacity. We will be sometime in the first half of next year maybe around July or so we should expect our passenger car capacities to start coming on stream July, August kind of time period and OTR we have not yet commenced the second phase of expansion so the first phase is ramping up but the second phase is something, which we will start investing in shortly that project also has not yet begun. We are still in the closure of the final planning stages, but we are currently at about that capacity is about 33 tonnes per day capacity we will take that up to 100 tonnes per day.

Jinesh Gandhi: So effectively what would be our total capex between FY2019, 2021 given that there has been some change here as well?

Kumar Subbiah: See I am going to give you a number relating to CEAT standalone. I could tell you our plants for specialty. We had indicated about 3500 Crores as our capex and till date we have spent above 550 Crores and balance and during the course of this year maybe we will spend around 1300 Crores that I had indicated earlier and our earlier projection was 1500 Crores standalone this year and another 1500 Crores next year so that 1500 to 1700 we would like to make it to 1300 and 1500 and the balance would be spent next financial year. In addition to that we also we have approved about 500 Crores for our CEATs specialty where we do not expect any significant amount of capex outflow during the current year depending on how we ramp up our phase I maybe we may spend some portion of it in the next financial year. I am not able to quantify but there could be something that we would be spending on CEAT's specialty in the next financial year.

Jinesh Gandhi: So that 3500 Crores remains for next two years effectively?

Kumar Subbiah: Yes it will be little less than 3500 in the next two financial years if you add up maybe it will come to 3100 Crores balance would be in the year 2021-2022.

Jinesh Gandhi: Thanks and all the best, I will come back in queue.

Moderator: Thank you. The next question is from the line of Nishit Jalan from Kotak Securities. Please go ahead.

Nishit Jalan: Sir firstly on capex if we see that your, have you cut down the capacity on the TBR plant because earlier you were talking about our 200 tonnes per day capacity but now given the quantum you are saying it seems to be about 160 tonnes per day capacity so any change in plans over there?

Kumar Subbiah: No. There is no change maybe it is exactly the same 200 tonnes per day, which is equal to about 8000 tyres. There could be confusion that our current capacity is about 40000. So you may have assumed we may have said 120000 tyres total. Today our capacity is about 80 tonnes per day.

Nishit Jalan: Sir how come your capex you have cut down if you have not basically cut down and because but I understand you mentioned earlier was that there will be 1200 Crores capex on TBR plant and you are saying that the plant will get commissioned in 4Q and you have incurred only 440 Crores capex in the first half. So I just fail to understand will we expect to incur significantly higher capex in the next three to four months how should we look at it?

Kumar Subbiah: Till date we have spent about 550 as I mentioned. Some part of it we spent in the last financial year also and when we start the plant we would not be spending all of the capex. So as we ramp up the downstream capex would get spent. So till date I said approximately about 440 Crores is what we have spent but we are still indicating a forecast of about 1300 to 1500 Crores. So there is something more to be spent in the next two quarters.

Nishit Jalan: Sir on your specialty tyre business the quarterly revenue generates would be about 20 Crores is it the right number?

Kumar Subbiah: Quarterly run rate on specialty tyres in terms of revenue.

Nishit Jalan: The CSTL yes in terms of revenue.

Kumar Subbiah: There are two parts to which one is our bias business, which we have been doing for some time, and we have the radial business. Radial business is still under ramp up at this point of time so I will say it is a little bit on the lower side if you just look at radial but if you look at truck ply plus bias it will be relatively higher maybe about 100 Crores a quarter kind of.

Nishit Jalan: Because when we look at your consolidated minus standalone revenues now we get about 35 odd Crores on a quarterly basis, so this 35 Crores would largely include the radial tyre facility under the CSTL?

Kumar Subbiah: No these 35 Crores are buyers plus radial both put together.

Nishit Jalan: So there is only 70 Crores right the difference for the first half.

Kumar Subbiah: I will come back to you. I think we will take this question again.

Nishit Jalan: Sir because why I ask this question is, is the revenue ramp up on the new radial tyre facility as per your expectations or you have faced some headwinds and you think that it was below your initial expectations and because of which also you are looking to delay your next phase of expansion in the CSTL?

Kumar Subbiah: No. I would say that yes our ramp up is slightly slower than what we are expected but we are not delaying it is largely because we were waiting for monsoon to get over we could not start off the new project usually project we will start only post monsoon period so we are just working on our plants if at all there is a delay it have not more than one month in terms of our own plan.

Anant Goenka: I will just respond to your question on specialty approximately their turnover is about 170 and out of that about 135 Crores is what we supply from CEAT to CEAT Specialty that is bias tyres so balance amount is what they have their profits.

Nishit Jalan: Radial is only 35 Crores in the first half.

Anant Goenka: 35 Crores include some amount of their profit as well on bias tyres it could be little less than 35.

Nishit Jalan: Sir one final question if I you mentioned I think the standalone revenue growth is 12.5% right?

Anant Goenka: Yes.

Nishit Jalan: Then basically if I look at the Y-o-Y realizations are up by about 1% and on sequentially the realizations are up only 0.8% and despite that the RM cost is largely flat on a RM cost of sales is largely flat on a sequential basis so was there any benefit of low cost inventory or you think that your sourcing was at lower prices and because of which there was low RM cost inflation in this quarter which can go up in the subsequent quarters?

Kumar Subbiah: See I just want to clarify on RM cost the after that maybe Anant would respond on other question that you ask. As a practice it appears when we arrive at RM cost we take material consumed and if there is any difference between opening finished goods inventory and closing finished goods inventory, we reduce it from the consumption, that is the way RM cost is worked out maybe that is why some confusion on what the gross margin is also all about. If closing in finished goods inventory is more than the opening finished goods inventory indirectly it means that production is more than the sales. So when we arrive at closing finished goods inventory and the difference between closing and opening the value of closing finished goods inventory would not only include materials but also would include other direct cost relating to that. So during the quarter, Q2 we held more finished goods inventory by end of Q2 compared to opening inventory and that portion includes them nonmaterial portion also. Actually raw material prices moved up between Q1 and Q2 in terms of rupees per kg by about 2.5%, but it is not clearly visible to you in the way we normally look at RM cost as a percentage of turnover is because the difference in finished goods inventory value also includes the nonmaterial portion.

Nishit Jalan: Thank you Sir.

Kumar Subbiah: But what was your first question, I think was to Anant in case you want to repeat it?

Nishit Jalan: No, I think that was the main question that what I try to understand whether we have realized the cost pressures or whether we have basically it will come in the future so what you are indicating is that because of the absorption cost accounting basically the a part of RM fixed cost is getting deducted from RM cost because of which RM cost is looking lower right?

Kumar Subbiah: Absolutely so therefore we have to look at right gross margin I would say the gross margin decline in Q2 by about 1.2%.

Nishit Jalan: But these entire thing does not have any impact on EBITDA per se right?

Kumar Subbiah: No it does not have an EBITDA impact because it gets absorbed between sales and EBITDA but the right way of calculating EBITDA is this.

Nishit Jalan: Thank you.

Moderator: Thank you. The next question is from the line of Arvind Sharma from Citi Group. Please go ahead.

Arvind Sharma: Good evening Sir. Thanks for taking my question. My only question is that the price hike that you have taken in October will they more than offset the raw material cost pressures especially a crude pulls down and so it is possible to see any margin expansion going forward or is it just in line to negate the cost pressures which we believe would be there in the coming quarters?

Kumar Subbiah: I think it will help certainly to negate some of the past. I think we need to take more price increase between November and December to equate for further price increases on raw material that we are expecting as well.

Arvind Sharma: Sir just a followup to it is the pricing environment as an industry conducive enough to pass on these price hikes?

Kumar Subbiah: Difficult to give an answer on that. I think the good thing is volume growth has been positive so that is the only indication that I can feel that there should be but tough to say.

Arvind Sharma: Thank you so much.

Moderator: Thank you. The next question is from the line of Basudeb Banerjee from Ambit Capital. Please go ahead.

Basudeb Banerjee: Congrats for a decent set of numbers. Just wanted to understand out of your volume growth how much was the two-wheeler volume growth in first half and this quarter Sir?

Kumar Subbiah: We would not be able to share that information. Category wise we do not share the volume growth numbers.

Basudeb Banerjee: Sir in this quarter in between the Kerala floods there was surge in rubber prices significantly though it has normalized down again. So is there any risk of the lag effect of that natural rubber price inflation in the coming quarters?

Kumar Subbiah: No, not really there has been rubber prices has been quite stable and usually the domestic prices have generally followed in what prices of global commodity prices. So rubber should not have any adverse impact. In fact it has been quite stable all through the time, maybe for a period of 10 days it went up by say Rs.5 or something but should not have any impact on going forward rubber prices.

Basudeb Banerjee: Last question Sir your assessment of how radialization is panning out at replacement level?

Kumar Subbiah: Yes, radialization continues to happen. I will say that we are somewhere around 45% to 50% level of radialization in the truck segment today so approximately between 2% and 5% per annum is what we are seeing in terms of radialization every year.

Basudeb Banerjee: Sir in specifically in replacement market because OEMs are anyhow on the higher end of radialization so how it is?

Kumar Subbiah: That is right. I am talking particularly about replacement. OEM side of course is somewhere around 75%, 80% radialization so that is I am talking about replacement itself.

Basudeb Banerjee: Thanks.

Moderator: Thank you. The next question is from the line of Siddhartha Bera from Nomura Securities. Please go ahead.

Siddhartha Bera: Thanks for the opportunity. Sir on the revenue growth side I just wanted to understand slightly better in terms of that revenue growth in the truck and bus segment has been quite strong in the first half so with more TBR capacity coming up in the last quarter is it fair to assume that your truck and bus mix will continue to inch up even from these levels?

Kumar Subbiah: Yes, I would say that certainly truck, bus after say January, February onwards we will see increase sales from there. There is enough demand so we will see higher growth there, but in the meantime our two-wheeler capacity also has been ramping up. So we expect two-wheeler as a mix maybe we will see and initially not much impact for the sake of first three, four months after that as we reach higher numbers in truck radial truck will go up a little bit and then again in July onwards July, August onwards you start seeing PCR sales. So the mix should not see a major change, but yes the volume growth will be high on truck radial once we start ramping up that capacity.

Siddhartha Bera: Can you please also indicate what has been the growth in the bias truck and bus bias segment and we have also seen a sharp decline in the LCV and some segment revenues in the first half so how one should look at these segments going ahead?

Kumar Subbiah: I think all segments have been pretty robust so there is no one segment I would say that really stands out for stronger growth. In fact overall we have seen strong growth across the board because there has been a general strong demand on the commercial vehicle side whether it is OEM demand or replacement demand some amount of duty antidumping duty impact, some amount of overall positivity base effect so net-net even in the bias segment has seen strongly demand I would not say bias has been slower; however, going forward we expect radial growth space to continue to outpace bias that has been done over the last few years, but particularly last six months buyers has grown well.

Siddhartha Bera: Thanks a lot.

Moderator: Thank you. The next question is from the line of Nitesh Sharma from Phillip Capital. Please go ahead.

Nitesh Sharma: Thanks for the opportunity. My first question is on the two-wheeler segment October price hike of 4% seems to be pretty steep so what has changed all of a sudden in the industry because the competition and competitors remain the same so where does this confidence comes from that 4% will be easily absorbed and passed on by the all the players?

Kumar Subbiah: No I can say high time that there is a fair amount of raw material price appreciation while we did see that happen in to a certain extent in truck and passenger after that so I will close two-wheeler happened at a delayed time so with raw materials inching up the phase it was a matter of time that raw material side we had to take price increase and the fact that few other players have taken and given confidence that it is happening at an industry level and not just at a one company level and therefore the confidence is higher that it will stay.

Nitesh Sharma: And on the currency hedging front I wanted to understand what is your hedging strategy and what is the realization in terms of exports how much you realized during this quarter?

Anant Goenka: Not sure, whether it will be able to share what we have realized on exports but our hedging strategy has been we are very conservative here all our capex we hedge 100% of our exposure once we finalize our agreement in case of raw materials also the largely exposure hedge our import exposure.

Nitesh Sharma: So it is on annual basis?

Anant Goenka: No as and when the transactions happen, we immediately follow it up with hedging of that exposure.

Nitesh Sharma: And can you help us understand utilization levels across segments?

Kumar Subbiah: Sorry.

Nitesh Sharma: Plant utilization level segment wise?

Kumar Subbiah: No, plant utilizations as I said has been pretty strong I way close to 85%, 90% difference is that some of these capacities are ramping up and therefore I say that utilisation is high. For example, Nagpur has not reached full capacity from a manufacturability perspective. So to that extent one from a demand side things are fully utilized, from a production side they are still certain amount of small capacity still left to be ramped up similarly I had shared that we have there are some amount of debottlenecking happening so out of what could be supplied we are fully utilized out but on the manufacturing side there is still some upside that will left to be further extracted from our plant. Going forward we expect bias truck to be reduced. I think there has been a large amount of demand because of duty etc., that is imposed but I think truck bias utilization will go down overtime.

Nitesh Sharma: The two-wheeler front have you received any indication from the OEMs to reduce offtake because festive demand has been weak or any indication from the OEMs to reduce the production or offtake?

Kumar Subbiah: Not yet.

Nitesh Sharma: Thank you very much.

Moderator: Thank you. The next question is from the line of Suraj Chheda from IIFL. Please go ahead.

Joseph George: Thank you this is Joseph from IIFL. I had a couple of questions. One was on the two-wheeler segment profitability. Now what we always understood in the past was that two-wheeler segment has been higher compared to the other segments of course if not quoted numbers but given the pressure that we have seen in terms of pricing in the two-wheeler segment could you just give us a subjective assessment of how much margins in the two-wheeler segment has come down has it come down by maybe half or something like that and now it seems to be a bottoming out given the price hikes that you have taken some color on that?

Kumar Subbiah: Yes, I think I would not be able to share the numbers or anything with you but broadly I do agree with you that relative to other categories two wheeler was more profitable now it has come down to a certain extent.

Joseph George: Had it come down to similar levels as say truck and bus?

Kumar Subbiah: No I think we have seen even company to company so for us our strength is more on the passenger side so we feel that our profitability is stronger on the passenger means passenger car and two-wheeler than on the truck side. So generally margins for us in these categories are higher.

Joseph George: The second question that I had been could you give us a sense of what the amount of interest that was capitalized in the quarters given that you are in a capex phase?

Kumar Subbiah: Can we get back to you on this?

Joseph George: Sure yes. Thank you.

Moderator: Thank you. The next question is from the line of Ronak Sarda from Systematix Shares. Please go ahead.

Ronak Sarda: Thanks for the opportunity. Couple of questions, one was the XLO norms, which were increase and now we are hearing RTOs have passed the norms. So any ground level anecdotes, which you can share, has that how has that changed the truck tyres usage pattern assuming the same old trucks are crying new load and also on the OEM side how has the tyre schedules changed, or is it like business as usual?

Kumar Subbiah: Yes, I think the nomenclature has undergone some change so earlier we used to be having a 1020 as our main selling tyre has been now changed to a metric pattern; however, our tyres were always okay for selling maybe 20%, 25%, 30% even more than that overload so to that extent our tyre there is no technical change that has happened in our tyre, but it does has a change that over time since 20 inches the main there can be a shift over time towards 22.5 inch kind of tyres over time. So nothing to be done at this point of time but it does indicate more global alignment of Indian tyre sizes.

Ronak Sarda: On the replacement side?

Kumar Subbiah: no this is replacement as well, but any impact at this point of time. In short-term there were neither much impact on a demand side nor anything major on the technological side, but over time I think we will have to work towards higher inch sizes.

Ronak Sarda: What I also meant to ask was whether the tyre life has come down if they are carrying extra load or you are saying that because your tyres were already made to carry higher tonnage it has not been impacted the life of tyres as such?

Kumar Subbiah: No major impact that we are seeing as such. It also remains a much regulation strength had come in towards making sure overload is not coming in so too many other factors that are there, today first state is not tracking down on over load then nothing changes. If states are tracking down then there will be some impact that yes now legally people are allow increasing their load by 20% so no really major impact that we see.

Ronak Sarda: Second question is I am sure you are tired of answering this question, given the current scenario both on demand side and let us say competition side and the capex plan which you have and the industry has what is in your sense the peak debt which CEAT would have let us say on FY2020 or FY2021 basis and are you still comfortable with that number?

Kumar Subbiah: Yes I think our peak debt equity that we would be comfortable or just about aiming for would be a 1:1 debt equity so once it reaches that kind of level or reaches that kind of level we would try obviously visibility then we will try and limit our debt or control our debt at that point.

Ronak Sarda: But can you highlight absolute debt number not the debt to equity because that can change?

Kumar Subbiah: No not really at this point. I think that we shared our capex kind of details so that is where there can be a minor adjustment here and there to accommodate our risk appetite but broadly we are on plan.

Ronak Sarda: But if things do not improve much or if they worsen are you open for an equity raising or dilution as well or will you rather postpone or delay the capex?

Kumar Subbiah: I think that will take a call when the time comes. We would not like to make a decision on that right now.

Ronak Sarda: Thank you.

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

Ashutosh Tiwari: Sir in our truck sales what would be the mix of radial and bias currently 35% sales comes from truck and bus?

Kumar Subbiah: Out of truck within truck bus for us it is about 75% bias, 25% radial.

Ashutosh Tiwari: In the two-wheeler segment we were targeting earlier to increase our market share in the OEMs basically how is the progress over there and currently what is the mix in the two-wheelers of OEM replacement?

Kumar Subbiah: Overall we are seeing very strong traction for our tyres and OEM as well as the replacement side. We are there with each and every OEM with strong share of business with them ranging from 20% going up to even 50% with the number of OEMs so we are in a very strong position with our OEMs. We are happy where we are and I will say in fact we are in a position where we are finding once again supply to be a little bit of a constraint. So we need to look at a quick ramp up or increase in capacity of two-wheeler tyres.

Ashutosh Tiwari: Nagpur plant what is your traction there currently?

Kumar Subbiah: Traction there is today is at approximately 100 tonnes per day.

Ashutosh Tiwari: The difference it is 120 right?

Kumar Subbiah: Yes, also on the manufacturing side constrains rather than demand constraint.

Ashutosh Tiwari: Sir lastly on the debt side we have 943 Crores of debt currently out of which this also include dealer deposit?

Kumar Subbiah: No it is only debt.

Ashutosh Tiwari: And what part of this is currently getting capitalized on which we are not paying the interest?

Kumar Subbiah: A small portion. Our debt level has more or less remain the same if you compare March versus September the amount of interest capitalized is very small I think there is someone else are also asked about it maybe in the last quarter of 5, 6 Crores worth of interest would have got capitalized approximately.

Ashutosh Tiwari: But 943 Crores is roughly say 100 Crores per year and then we are paying almost the Nagpur was 13 Crores in that payment only right?

Kumar Subbiah: No, see approximately about 20 to 22 Crores is the outflow at CEAT standalone basis and another 3, 4 Crores is CSTL so that is the way we incur interest and if you look at our debt level what you see is as of end September but average debt for the quarter was little lower at least 100 Crores lower.

Ashutosh Tiwari: But if we are doing 13 Crores of interest in the last quarter right same quarter, 13 Crores?

Kumar Subbiah: The last quarter was 19 Crores.

Ashutosh Tiwari: That is on consolidated level and standalone is 13 Crores.

Kumar Subbiah: Only towards September it went up.

Ashutosh Tiwari: Thank you.

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

Nishant Vass: Thank you for the opportunity. Sir first I wanted to understand on the working capital side you said obviously you have done strong control on that, could elaborate more on what you have done to kind of control this and what can we see possibly for the rest of the year?

Anant Goenka: If you really look at it in all three key elements of working capital we have managed to improve and in case of raw materials and finished goods, raw materials there is reduction between March and September maybe to a tune of about 50 Crores or so. In case of finished goods towards end

September we ended up holding little more inventory so therefore there is not much of an improvement between March and September though it improved in June. Receivables overall in terms of number of days has improved and even on creditor there has been increase through better payment terms, we are managing, as the material comes only when it is required you end up having more liability in your books, so all three elements that we are focusing today. In addition to that we have few things also we did, we brought in some efficiencies in GST so all the accumulations we were able to utilize, we had managed to utilize large part of the export licenses, these are all sitting in other current assets and then amount of money it lying in transit okay we also brought down significantly between March and September so multiple measures many small, small measures added up to this 140 Crores of working capital reduction in between April and September.

Nishant Vass: So for the second half and the remainder of the year can we expect an incremental number on this?

Anant Goenka: No, I do not expect anything increase in working capital and even last year we managed to bring our working capital down by about 105 Crores or so unless there is a need for us to hold little more inventory of either raw materials or finished goods or if our sales activity increases in absolute terms there could be some change but in terms of number of days we do not expect it to deteriorate in the second half of the year.

Nishant Vass: Sir second question was on the other expense side you had highlighted earlier in your comments that there were costs that were sitting due to higher manufacturing activity which you all say alluded to on the and you are explained in the gross margin bit so could you quantify that amount?

Kumar Subbiah: Quantify other expenses is it?

Nishant Vass: No the expense related was on the increased manufacturing activity for the finished goods that was not sold but produced?

Kumar Subbiah: I would say about 14, 15 Crores is on account of increase in manufacturing activity.

Nishant Vass: Considering if that was not the case next quarter would probably reverse itself?

Kumar Subbiah: No, see that benefit has already come through in the form of higher finished goods.

Nishant Vass: Right, so that the gross margin this would kind of cancel each other out that benefit on the gross margin.

Kumar Subbiah: Yes.

Nishant Vass: Sir on the add expense just wanted to understand generally we see a decline on the ad expense I do not know quarter one to quarter two basis because of the IPL but again we have some things that we have done this quarter how should we look at ad expenses have we seen a structural increase on this on the company side and are we spreading out the cost more evenly or how should we look at it?

Kumar Subbiah: Yes we are spreading out the cost to a certain extent. We have found that the expenses for IPL have generally gone up so we have moved out of IPL and are looking at other areas of expenditure not that we moved out from strategic time out that is still there with us but we used to do campaigns at IPL advertising during the IPL seasons. That is what we have stopped and we are looking at other avenues for that advertising budget that we are looking at. So the increase in Q1 would have generally been a little lower than the previous year and that hence would have moved to the other quarter so we are advertising during the KBC, which is what we are incurring in Q2.

Nishant Vass: So as a percentage to say is one should not expect a meaningful change per se is that right?

Kumar Subbiah: No, you should not expect.

Nishant Vass: So and a house keeping question obviously you gave the change in commodity on a per kg basis could we have also the basic commodity cost like the NTCS as carbon block synthetic and crude?

Kumar Subbiah: Approximately there has been an increase in most crude and crude derivative product generally natural rubber has remained quite benign, but the other that will over out 15% increase on a year-on-year basis.

Nishant Vass: This would also include carbon black in the same percentages?

Kumar Subbiah: That could be higher, but I am just saying at least to 15% increase we have seen in the crude derivative products, carbon black would be 20% plus.

Nishant Vass: I am just trying my luck here now that you have done some price increase and obviously the industry has seen a big change on that side where do you see once you have also doing increasing at in-house manufacturing vis-à-vis outsourcing so what can we directionally look at it in the next 12, 15 months where do you think say the margins on the EBITDA could be for us just on a broad directional sense from the company?

Kumar Subbiah: We do not give guidance really.

Nishant Vass: No I know, but I am just trying to test my luck, would you be able to come back to the previous numbers that we have seen if the industry pricing scenario improves?

Kumar Subbiah: I would not be able to share and give you any numbers.

Nishant Vass: Thank you.

Moderator: Thank you. The next question is from the line of Sunita Kamat from Motilal Oswal. Please go ahead.

Sunita Kamat: Sir could you give us an update on the PCR debottlenecking activity that we were undergoing?

Kumar Subbiah: Yes. We are making positive inroads on that so we have taken up our capacities by about 10% to 12% on a quarter-on-quarter basis approximately. We have another about 10% opportunity to go, that I expect to happen sometime to happen say sometime by December, January onwards.

Sunita Kamat: Effectively for FY2019 our PCR sales have a scope of about 8% to 10% kind of an increase in this year right.

Kumar Subbiah: On a year-on-year basis you are saying PCR has gone up?

Sunita Kamat: On a year-on-year basis yes.

Kumar Subbiah: Yes, as I said we would not be able to share that data but yes as I said that from whatever we work and using we have been able to debottleneck about 10% and I think another 10% chance for debottlenecking which we are working on and that will come by December and January.

Sunita Kamat: Second question could you give us some light on how the replacement growth has been at an industry level in the first half of this year?

Kumar Subbiah: Industry data we would not be having to that extent usually say we get ATMA data at a much later time, so industry data is still not available for the first half.

Sunita Kamat: Thank you.

Moderator: Thank you. The next question is a follow-up from the line of Siddhartha Bera from Nomura Securities. Please go ahead.

Siddhartha Bera: Thanks for the opportunity again. Sir two housekeeping questions; if I see your consolidated tax rate it has consistently remained at close to 40% in the first half of this year so why is this from the higher side and what do we expect going ahead it will be?

Kumar Subbiah: No, see tax I think that way if you look at the standalone basis our standalone tax has come down by about 2.5% over first quarter. In first quarter we took the impact of change in income tax cess that happened in the last budget. On a consolidated basis because CSTL has incurred losses so therefore there is no tax shield there and one of our subsidiary companies also Rado Tyres also incurred losses so therefore you would not get that benefit of tax shield when you arrive at the consolidated number but if you really want to see the progress that way to look at it is our standalone that has moved down from over 35.6% to 32%.

Siddhartha Bera: So the standalone tax rate should remain at least 32%, 33% levels?

Kumar Subbiah: Yes that is true in that range.

Siddhartha Bera: Our other income also I believe has been slightly lower is it that the dividend from Sri Lanka has been on a slightly lower side this year and or is it something else?

Anant Goenka: Yes it is true.

Kumar Subbiah: That is right.

Siddhartha Bera: Thanks a lot.

Moderator: Thank you. The next question is from the line of Chirag Shah from Edelweiss Securities. Please go ahead.

Chirag Shah: Thanks for the opportunity again. Just one clarification on the employee cost you indicated there are some additions on our Nagpur plant if it possible to quantify how much that could be. So that could be a recurring for another two quarter's still Nagpur plant starts production?

Kumar Subbiah: No, the best way to look at it is that Anant clarified in the beginning what is the one time cost which is about 7 to 10 Crores that is what I think you need to take out to find out what would be the recurring cost.

Anant Goenka: The recurring cost increase includes other things your normal increment that are there, worker long-term settlements is that everything inclusive is what we are incurring is the balance amount and Nagpur.

Chirag Shah: Nagpur is the part of the balance amount. I was just wondering how big that Nagpur chunk is and just a clarification on this tyre change you indicated but had the OEMs gave you an indication when the new change new tyre they would be requiring because they are indicating a rollout of new truck to happen by now in that sense so is there an indication coming from them that there is new tyre for changes in the and some might change the existing tyres?

Anant Goenka: No, there is no change on the tyre from a technical perspective. It is only in the nomenclature so the tyre plate where the name comes instead of 1020 there will be 195 ETR 20 or whatever that will come on so that is the place change that can be done at any point of time.

Chirag Shah: This is helpful. Thank you.

Moderator: Thank you. The next question is from the line of Vijay Sarthy from Anand Rathi. Please go ahead.

Vijay Sarthy: Thank you Sir. Basically I just want to understand what is the current operable capacity in two wheeler, three wheeler today and how much have slated to go in the next two years and then we also plan to add more on two wheeler side? That is one question second by that happening what will happen to our outsourcing is there an agreement with the supplier to get it down it will be helpful.

Kumar Subbiah: The way we look at our two-wheeler capacity is to always augment our current capacity so even the outsourced capacity that we have we do not plan to bring it down. Demand long-term demand we plan to add capacity assuming that our outsourcing will continue in the longer-term as well. So we are not going to bring that down. Today we have a capacity of about 2 million tonnes of tyres alluded over that per month.

Vijay Sarthy: Sorry Sir I did not hear you 2 million.

Kumar Subbiah: Today's capacity is about 2 million tyres per month.

Vijay Sarthy: And that is likely to go up by how much by FY2020?

Kumar Subbiah: At least another million tyres.

Vijay Sarthy: And we have another set of capacity increase beyond that right?

Kumar Subbiah: No this is what we are saying is that going to be about we are going to increase our capacity by about a billion tyres over the course of the next year, year and a half time. When we compare it, it is too early to say yet we have not decided on any other expenses.

Vijay Sarthy: Continuing on what is generally rub-off effect in your two-wheeler and PC what is your assessment if you can help us understand?

Kumar Subbiah: There are couple of rub-offs that happen one is both our brand dependent so with respect to advertising, visibility, I think one advertising rubs off on the other that is one second is on the channel side there is a fair amount of overlap of channel so whatever distribution that we are able to increase our channel presence in that has some amount of rub-off effect. These are the two major impacts that are there at one complementary the other.

Vijay Sarthy: Basically so the put point I am trying to understand if you have every one tyre that you sell today on OEM, for every ten tyres that you sell in OEM today how much of that gets replaced with your own tyre in your first replacement that is what I wanted?

Kumar Subbiah: Approximately 30% or so.

Vijay Sarthy: 30% in two wheelers.

Kumar Subbiah: Yes.

Vijay Sarthy: How much would that be in PC Sir?

Kumar Subbiah: Little bit lower I would say about 30% to 40% in two-wheeler slightly lower in PC.

Vijay Sarthy: Sir it is curious is not that low given that we have solid brand image and we have done it for last five years given our own?

Kumar Subbiah: It is not behavior right so these are the consumers who just say what is there just put it, kind of mindset. So then the others I am not saying the others do not put our brand but the others something irrespective of whichever brand is there about 30% consumers if they are happy with the product they will say that you will just put whatever I got with the OEM.

Moderator: Thank you. The next question is from the line of Arvind Sharma from Citi Group. Please go ahead.

Arvind Sharma: Thanks again. On the TBR end TDP is side of truck and bus tyres as TBRs gain more prominence and TDP go down so I believe replacement cycle for TBRs is much stronger so does the revenue/profitability on a TBR account for or more than a offset the increase of elongation in the replacement cycle over the longer-term?

Kumar Subbiah: It is difficult question to answer because I think the profitability varies from time-to-time but overall TBR profitability is and should be higher than truck bias profitability because the product is clearly a superior value proposition versus the truck bias tyre but looking at the long life of the vehicle I would say that I get just at an margin level truck radial profitability should generally be better than bias in the longer-term.

Arvind Sharma: Sorry for repeating but if you could just repeat that 3000 Crores capex in terms of what you are planning for FY2019, 2020 and 2021 and you answered it but just once again please?

Anant Goenka: See out of 3500 we have spent at lower 500 already and during the year little lower 400 so capex estimate for the current year is about 1300 to 1500 Crores and next year would be approximately about 1700 Crores that is the projection and 500 Crores beyond that everything is standalone it does not include CSTL.

Arvind Sharma: Thank you so much.

Moderator: Thank you. The next question is from the line of Jayesh Chandragupta from JM Financial. Please go ahead.

Jayesh Chandragupta: Good evening Sir. Sir one of the players in the two-wheeler space is offering significant promotion schemes of five-year unconditional warranty and one year free replacement and he is targeting close to one-fourth of the distribution network at CEAT so do we see some competition over here what kind of response do we have?

Kumar Subbiah: No, I think that is part of life right everyone looking at becoming leaders in each of their respective categories so to that extent we would also continuously fighting for us distribution is our strength. I think it is very difficult to replicate what we have done. In addition brand is an investment that we have been doing for a long time. We have been in the country for 60 years and advertising has been strong continuously at least for the last eight, ten years on the two wheeler side we have been strong so I think it is difficult for somebody to catch up or we also look at on the product side that our product should continuously be superior because everyone keep coming out with new products with new promises so these are some of the efforts that we work on to make sure that we maintain and improve our market share for us two-wheeler is a very important category so somewhat may we will do whatever investments needed to win in this category.

Jayesh Chandragupta: Sir so but we are not thinking of any kind of promotion scheme right like similar to the other player in the two-wheeler space.

Kumar Subbiah: I am not sure specifically but I think say consumer schemes here and there keep running say sometimes we have a new SKU that you launch you want the consumer to try it out and you may run a scheme but no we will not look at discounting in the form of scheme. If there is a discounting of price change then we will take a price decision but a scheme is a scheme, which is meant for a temporary period which is meant for trial basis and not for discounting that is how we do it.

Jayesh Chandragupta: Sir one more question in terms of commercial vehicle space what kind of industry guidance are we still looking at the commercial vehicle space after getting some clarity of axle norms now?

Kumar Subbiah: No, there should be no impact on tyre demand so I think overall demand is quite positive we are seeing nearly what commercial vehicle have grown by what 40% I think on a year-on-year basis while last year was the low base. Similarly if we look at other players or industry growth has been very strong 30%, 35% plus on the tyre side while that growth will taper down because of the base effect of last year being more on the first six months but demand is still relatively strong what we hear is Tata Motors, Ashok Leyland all well utilized on the truck side.

Jayesh Chandragupta: Thank you Sir.

Moderator: Thank you. Ladies and gentlemen this was the last question for today. I now hand the conference over to Mr. Kale for his closing comments. Over to you Sir!

Jay Kale: Thanks for joining the call everyone and thank you CEAT Management for giving us this opportunity. Have a good evening.

Moderator: Thank you. Ladies and gentlemen on behalf of Elara Securities Private Limited that concludes this conference call. Thank you for joining us. You may now disconnect your lines.