SONA BLW Precision Forgings Ltd. (Sona Comstar)

Q2 FY22 Earnings Conference Call Transcript
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The webcast recording and the presentation referred to in this transcript are available on website of the Company and can be accessed on the following link:

https://sonacomstar.com/investor/investor-presentations

Kapil Singh: **Slide 3:**

To take us through Q2 FY22 results and to answer your questions, we have with us Mr. Vivek Vikram Singh - MD & Group CEO, Mr. Kiran Manohar Deshmukh - Group CTO, Mr. Vikram Verma - CEO of Driveline Business, Mr. Sat Mohan Gupta - CEO of Motor Business and Mr. Rohit Nanda - Group CFO. I will now handover the call to Mr. Vivek Vikram Singh for his opening remarks and the presentation. Over to you Vivek.

Vivek Vikram Singh: Thank you Kapil and good day everyone. On behalf of Sona Comstar, I would like to welcome all of you to the earnings call of what has been in terms of the financial metrics, our best quarter yet.

Slide 6:

We will begin as usual with our vision, which we have tweaked a little bit after we have some excellent feedback from one of our new public shareholders and because we are a Company with a global customer base, global presence and global competition, we have modified our vision from India's most respected and valuable auto technology Company to one of the world's most respected and valuable auto technology companies.

Slide 7:

Our story is a testament to that long-term vision. We started small but with an unbeatable technology advantage of precision forming, which has allowed us to grow at nearly 50% CAGR in the first 12 years. In the next phase our growth moderated to a CAGR of 10% but we improved our EBITDA margins to 25%, while adding differential assemblies in the new product.

Our third phase was truly transformational. We massively expanded our export business, our customer base as well as the product portfolio. We also started our EV journey here in 2016 with gears for electric cars and later vertically integrated upwards into making a full final drive assembly. We also did a fairly value accretive acquisition of Comstar and this along with our fantastic organic growth, helped us achieve over 32% CAGR growth in the last 5 year phase. All this while simultaneously increasing our EBIDTA margin to nearly 28%.

While our 4th phase begins now, I would like to highlight that in our 22 years journey, we have grown at an incredible rate of 36% while always sustaining excellent EBIDTA margins, and at any phase in our story we have exceeded the industry growth rate by many many times.

Slide 8:

Yes, our values, our results rest on the foundation of our values of integrity, vitality, agility, and frugality, and by staying true to our value system, we hope to continue delivering strong results on all three - growth, margins and returns like we have so far.

Slide 9:

We feel that we have managed to build quite a unique business by having these three things, large EV revenue shares, good scale and high growth, while achieving and maintaining remarkable financial performance. I touch upon each of these three aspects in the context of our first half and latest quarter in the next three slides.

Slide 10:

First, we begin with EV, our BEV revenue share has increased to 21% in H1 from 13.8% in FY21, our EV revenue in absolute terms has grown by 223% to over Rs. 220 crore in the first half. It also gives me great pleasure to report that in the last quarter we have added three new EV programs, 2 from existing customers and 1 from a new customer. With this, we have reached now 20 EV programs, 7 of these are in serial production as compared to 5 in the last quarter, while 13 are in the order book.

These three new programs cover three different products, a differential assembly program for a compact electric passenger carmaker in Asia, who is also a new customer. Strategically this is a very important win and I'll elaborate upon this and the importance of this in the later slide. We've also got a differential gears program for an existing North American customer, where the ultimate customer is a large North American passenger vehicle maker. And lastly the third one which is a P.M.S.M. Motor program for an existing electric two - wheeler customer in India.

Slide 11:

Now we come to the Net Order Book. At the end of Q2 this stands at Rs. 13.6 thousand crore or nearly $1.8 billion. For people who are joining for the first time, this is the aggregate value of the next 10 years revenue from all programs that are yet to commence or are still ramping up, minus the impact of all programs that will reach end of life hence, the net value. I want to clarify that when we say order book, we do not include running programs that are already in production, so, this is over and above our current revenue run rate.

The order book is obviously dynamic and in Q2 since we consumed orders worth 16 billion and one new order worth 12 billion on a net basis, there is a reduction of 4 billion. Although what everyone has to understand is that this is now on a much higher base rate of running revenue versus last quarter. If you see a growth, a lot of this growth has come because we have consumed this order book because industry growth rate has actually been negative, so, this is our growth. Now of course, we want new order intake, and it always is much higher than orders consumed each year. But this is, as you would understand, hard to predict or manage on a quarterly basis because order wins are discrete and unevenly distributed events. So we've had quarters where we've added a 40 billion to the order book and also where we've added nothing at all to the order book. A full year in our opinion is a much better time frame to measure and monitor new order intake. However, because this is just our second quarter, we thought we will be completely transparent and share it live as we go along.

Another highlight on this is the EV part of the order book, battery EV or plug-in hybrid as a percentage that has increased from 57% at the end of Q1 to 58.5% at the end of Q2, and because our existing EV revenue share is also increasing in this quarter to 22%, the proportion of revenue from the EV should continue increasing over the next few years.

Slide 12:

Third, I come to our financials. So, first quarter, like I said at the onset, this was the best quarter yet. We grew our revenue, EBITDA and PAT by 52%, 24% and 22% respectively. That we have achieved this despite strong headwinds on semiconductor shortage globally, material price increases, freight costs increase and frankly each and every input costs facing inflation these days, this really highlights the resilience of our business. I'm afraid though that these headwinds will persist through Q3 and Q4, and the auto market as well as margins will continue to remain under pressure from these factors. But as promised to you whenever we talked before between 26% to 29% is how we've kept and always talked about our EBITDA depending on input price variance. To also to note our BEV revenue grew by 143% and it has reached 22% underlining the pace of electrification in an otherwise very slow or almost negative growth automotive industry.

Slide 13:

For me, the H1 numbers are more important because they reflect an ongoing business and I'm proud to report that we have managed to more than double both our revenue as well as net profit over H1 of last year.

We had a healthy 27% EBITDA margin for the first half and over 15% PAT margin while our returns continue to be best in class.

Even more important than financial growth, we have managed to improve our global market share in both differential gears from 6% to 6.4% and in Starter Motors from 4.6% to 5% in the first nine months of calendar year 2021, which is a phenomenal rate of expansion from a global perspective.

Slide 14 &15:

Now, victories are only meaningful if they're achieved on our priorities and not on an ever-expanding need for more without focus or reason or purpose. So now on to our four medium term priorities:

- Electrification,
- Global market significance,
- Diversification,
- and lastly technology; which is how innovative companies, like us, survive and thrive over time.

Slide 16 & 17:

In our last call, I had spoken about how in the driveline business, we were focused on the performance and high-performance segment of electric passenger car market, basically 100 kilowatts upward. With our latest order win, that I spoke about of a compact car differential assembly business, what it has done is now we can address the entire passenger cars space, including the small and mid-segment BEVs from 50 Kilowatt upwards. What this does is allows us to supply our gears, differential assemblies, and final drive assemblies to a much wider market. Earlier, it was only US, Europe and China which were relevant end-markets. Now we have a relevant product offering to cater to the emerging small car EV markets in Asia and India as well.

Now coming to the motor business, the motor businesses core strength has always been making lower voltage motors with high power density and performance. We have extended the strength to making traction motors and motor control units for electric 2 and 3 Wheelers. And we've already been fairly successful in the Indian market where we are supplying to 2 of India's top five electric 2-wheeler makers. The longer term aim here for motors will be to keep moving upwards along the power access and get into traction motors for hybrid and battery electric passenger cars as well.

Slide 18:

Now this focus on EV has yielded good results and while our revenue share has grown 16 times in the last 2.5 years to reach 21%, in absolute revenue terms, the growth is even more impressive at 25 times. And looking at the fact that 58.5% of the order book is EV, this segment will continue to be the fastest growing.

Slide 19 & 20:

Now, onto market share and we continue to increase our market share globally in both product groups and continue to also hold a dominant position in the Indian differential gear market.

And if you were to look at it, the biggest reason for our growth in this quarter is indeed our market share growth because if you look at the industry, there is a degrowth in virtually every segment. In fact, the global auto industry had its third worst quarter of sales in the last three or four years. And our two biggest markets, Europe and North America had their second worst quarters of sales, preceded only by the covid impacted quarter, which was worse. So, if you look at our performance against this backdrop and context, hopefully it would appear even more remarkable, and this is what is translating into financial growth as well.

Slide 21 & 22:

Now coming to diversification, we begin with revenue cut by power train, two things to point out, the two secular themes increasing BEV share and the reciprocal trend of our exposure to ICE also reducing on every period growing from 35% in the FY19 to 19% at the end of H1 this year.

Slide 23:

Moving to geography, I think we are getting into a much more balanced revenue mix with U.S. Europe Asia and India, almost all becoming nearly equal contributors to revenue, and this mix will definitely change from quarter to quarter depending on the performance of these four economies, their end markets and much more critically our customer's performance in these end markets.

On product diversification, we are happy to report that our journey from components to subsystems and systems is proceeding well. Our revenue share from differential assemblies has grown from 5.6% in FY20 to 24% now in H1. And the second notable point here is the revenue share of ICE Starter Motors, which is there, is declining every period.

Finally, the last one, the one mix that is unchanged. our vehicle segment diversification. The one notable thing here is that the India CV demand is starting to gradually pick up and we can expect that in the medium term it could be an additional lever of growth.

With that I will turn the call over to our Group CTO, Mr. Deshmukh to discuss our approach to technology. Over to you sir.

Mr. Deshmukh: **Slide 24:**

Thank you, Vivek. Good evening, ladies and gentlemen.

Slide 25:

Tony Seba and the RethinkX team found across diverse fields that once a tipping point is reached, it takes a new technology 15 years to go from nothing to being dominant. During the same period, the old technology is decimated, catching the incumbents by surprise. This rule has repeated for over 200 years for products as diverse as fabric dyes, car tires, nails, cameras, to cars vs. horse carts. It is our firm belief at Sona Comstar, that the tipping point of electrification was last year, and in 15 years or by 2035 ICE engines would be reduced to a negligible global market share.

Slide 26:

This rule happens due to a casual feedback loop led by three actors: the Governments or the regulators, the financial markets, and the consumers. Government supports subsidizes the cost of the adoption of new technology and lowest investment risk. Capital markets reward new technologies with higher valuation multiples and lower cost of capital, thereby attracting more incumbents to switch to the latest technology. The consumers start getting more variety, better prices and better performance, creating more and more demand. The exact reverse of this starts happening to the old technology players, we have already started seeing this in motion with electric vehicles and investors as usual are ahead of the curve helping accelerate distressed.

Slide 27:

During the last quarter's earnings call, Sona Comstar's technology roadmap, which is fully aligned with this trend, was presented. Such roadmaps are for the long term, and they don't change in a few months unless of course there is a significant disruption in society. Our strong belief in the electrification of mobility dates back to 2016 when we focused on the emergence of EVs, acquired Comstar and developed products to meet the needs of electric vehicles. Today, we supply a variety of products for electric passenger cars, electric 3-wheelers and electric 2-wheelers and we will continue this journey and make more products to support the electrification of the drivetrain.

Slide 28:

Traditional methods of business excellence are so far focused on optimizing costs and cost efficiency. Today's businesses need to be steadfast in the volatile, uncertain, and complex world, while also being efficient. Recognizing this, we embarked in our Industry 4.0 journey with the vision to use technology to achieve a delicate balance between the efficiency and the resilience. We implemented various initiatives to digitalize our factories to make our operations smart.

While our strategic intent drove these initiatives, their scaling up was possible only if we had able, competent, and skilled employees. To develop digital fluency and build advanced skills of our managers, engineers, and executives we partnered with NASSCOM to roll out the FutureSkills Program. Conceptualized and constructed by NASSCOM and supported by MeitY, the program aims to upskill our employees to face digital revolution across multiple functional areas.

In the future we will work with NASSCOM to develop content suitable for the shop floor employees to bring digital literacy among the frontline associates.

I would now hand it over to Rohit to cover the financials.

Rohit Nanda: **Slide 29:**

Thanks Mr. Deshmukh, a very good day to you all. It's my pleasure to share our second quarter and H1 results where we are reporting the best-ever Revenue, EBITDA and PAT numbers for the Company.

Slide 30:

We'll start with the slide on the first half results.

Vivek has already given you a snapshot of revenue Ebitda and PAT numbers for H1. So I'll focus largely on the key factors affecting these numbers.

Our revenue growth for this period was diversified across all geographies, product categories and powertrains though the highest growth was seen in our focus areas of BEV in powertrain and Systems i.e Differential Assemblies in the product categories.

EBITDA margin at 27% had a positive impact from operating leverage and product mix at 2.5% and 3.8% respectively. Despite price passthrough, RM cost increase has reduced margin by 3.7% due to arithmetic effect. It's important to understand how this arithmetic effect works. Therefore, we have made an illustration to explain it.

Slide 42:

In this illustration, we have assumed a base selling price of ₹100 for a product with the material cost of Rs. 45. In case of an illustrative 15% increase in the RM cost, both the selling price and material costs go up by the same amount. As you can see, there is no impact on absolute margin. But the margin as a % drops by 3.5%.

Slide 30:

An adverse impact of 3.7% in a similar way has come on our EBITDA margin due to this arithmetic effect.

Besides this, RM cost increase, not having a pass-through arrangement had an additional impact of 2.1%. Last year first half EBITDA margin also had 2.1% higher forex gain because of which the last year's first half EBITDA margin looks to be a bit on the higher side.

PAT margin at 15.7% was higher compared to the last year's H1, because depreciation and interest as a percentage of revenue have gone down by nearly 4%. H1 of current year had also had a one-time effect from exceptional income on account of reversal of IPO expenses, nearly 1% post tax impact on the PAT margin.

Slide 31:

Now let me walk you through the Y-o-Y comparison of our second quarter numbers.

We will begin with revenue. Our revenue for the second quarter was Rs. 5.86 billion with a Y-o-Y growth of 52%. Our BEV revenue grew by 143% to Rs. 1.24 billion, constituting 22% of our total sales. Our revenue grew in all geographies, but for North America which was lower by 14%, mainly because of the higher impact of chip shortage on some of our North American customers.

On the EBITDA front, it grew by 24% to Rs. 1.54 billion wherein EBITDA margin was 26.4%. There was a positive impact of 1.2% due to operating leverage. Similar to the last slide, the arithmetic impact of the RM cost pass through was 3.7%. RM cost increase without corresponding pass through plus the product mix impact, had an adverse impact of 1.7%. Besides this, EBITDA margin in the comparable quarter last year was higher by 2% due to forex gain.

Moving on to the PAT for the quarter, it grew by 22% to Rs. 882 million with a PAT margin of 15.1%. Lower finance costs during the quarter helped in an improved margin transmission between EBITDA and PAT.

Slide 32:

Now let me take you through quarter-on-quarter comparison for the second quarter of FY 22.

Our overall revenue grew by 17% on a quarter-on-quarter basis while BEV revenue grew by 28%. We saw revenue growth across all geographies on a sequential basis. Our global market share in Differential Gears and Starter Motors continue to grow and stood at 6.4% and 5% respectively, based on the nine months of the calendar year, indicating that we continue to grow faster than the market.

Our EBITDA for the quarter grew by 11% on a sequential basis compared to the previous quarter where the EBITDA margin was lower due to product mix and increasing the RM prices. We expect inflationary pressure on the input cost of RM and services to persist at least in the near term.

On the profit after tax front, our Q1 PAT included exceptional gain on account of reversal of IPO expenses with an approximate post tax impact of Rs.100 million, compared to the adjusted PAT for the first quarter we had a growth of 22% in profit after tax. Depreciation and finance as a percentage of revenue was lower and has helped in to improve transmission of profit margin between EBITDA and PAT.

The financial performance of the Company needs to be appraised in the context of continuing inflationary pressures on input costs, supply chain challenges and fading effects of monetary and fiscal support globally.

Slide 33:

Now onto the cash flows for the half year, major sources of cash inflows for the first half happened: the EBITDA of Rs. 2.93 billion and the proceeds from the primary issue to the tune of Rs. 2.94 billion. In terms of the deployment or outflow of the cash flow, we used Rs. 2.6 billion for the loan repayment. Capex spending was Rs. 1.47 billion, and there was an increase in the working capital to the tune of Rs. 559 million. Besides this, there are tax payments of Rs.462 million. On the whole, there is a net equal of Rs. 395 million in the cash position, plus the treasury investments of Rs. 513 million which were made during this period.

While we are on the cash flows, it's fair for me to provide an update on our estimated capex outflows in the current year. Against our earlier estimated number of Rs. 6.5 billion this year, the revised estimates are now around Rs. 4.5 billion. This change is mainly on account of logistical constraints faced by our Capex vendors, pushing out nearly Rs. 1.8 billion of cash outflow to the next financial year. A large part of it was skewed towards the last quarter of the current year in any case. Further, there is a reduction of about Rs.150 million in capex due to efficiency improvements. It's important for me to add that this shift in cash flows is not expected to have any negative bearing on our overall expansion plans.

Slide 34:

Moving on to the key ratios, I will start with the ratio of value addition to the employee costs, which has improved to 5.7 times compared to 5.2 times last year. As I explained last time also it is calculated by dividing material margin with a total employee cost and is used by us internally as one of the key operating metrics. Higher numbers implies operating leverage working more favorably relative to the comparable period.

Our return on capital employed was nearly constant at 34.7% as compared to last full year. Improvement in the annualized EBITDA has had a corresponding increase in the capital employed and therefore the ROCE is nearly constant.

Return on equity stood at a healthy 31.4%, though it was lower than 36.4% reported for the last financial year. And that is mainly because of expansion of the equity base following our primary issue of Rs. 300 crore, which we have used to largely pay off the long term debt of the Company.

Coming on to net debt to EBITDA ratio. Net debt of the Company is now negative after we've paid down our long-term debt and therefore, net debt to EBITDA ratio has also turned negative.

In terms of the turnover ratios, the working capital turnover and fixed asset turnover ratios have improved to 3.9 and 4 times respectively due to higher growth and revenue as compared to the growth in both net working capital and net fixed block.

With this we come to the end of the quarterly earnings presentation, and I will now hand the proceedings back to Vivek.

Vivek Vikram Singh: Thank you, Rohit. I think we can head straight to Q&A, I don't think there's much more I have to add.

Caihua Chan: Okay, thank you very much. To all participants online, currently we are in the Q&A segment. If you have a question, you may use the raise hand function icon located at the bottom right of the WebEx page. We will unmute your line and prompt you to speak and you may also choose to type your question in the Q&A box, and we will address it accordingly. Thank you.

The first question will be from Mr. Nitin Arora of Axis Mutual Fund. Nitin, your line is unmuted, please go ahead thank you.

Nitin Arora: The first question is again, you know, on the point which we discussed last quarter also and you said that you know, our endeavor is to outperform the market and you know the kind of demand which is coming from the electric vehicle despite chip shortage, we will try to do better and that you have grown even on quarter-on-quarter basis you have grown significantly despite the issues. Here the question is that, when we look at the kind of transition which is happening in the market, you stated in your opening remarks that electrification, you know every region, can you throw some light more just to understand the supply chain once more on the chip shortage side. How is it still very confident to outperform and do better and supplies would not be impacted. The kind of demand which is coming from the electrification side. If you can talk about that first and then I have two more questions.

Vivek Vikram Singh: Perfect. The supply chain continues to remain a problem, the chip shortage is real. This is why I said if you guys look at the numbers of the overall world industry, just step back and look at it. It is the third worst quarter in the last five years. And that's the data I looked and it maybe even longer. Europe and US are really badly hit. Will it continue? Yes, I think it will continue. Why I was confident even last time about our growth was because we were growing more from new orders. So, let's say existing run rate was you had 100 rupees of business, that 100 I knew was going to 90 but I had 30 of new business coming. That's why, I was confident of going to 120. I don't think it's improving any time soon. When there are many more people more suited than me and more knowledgeable than me, who can comment on when finally, the chip shortage will end, but not any time soon is our estimate and our assumption while we are working. Will electrification continue? I think electrification is continuing because of all of this. While the chip shortage persists and you have higher times to wait anyway, a lot of people can switch their demand and wait for the electric vehicle. So, I think electrification is inevitable, immutable, irreversible. So that's going to continue. How we fair is connected being to B2B2C player, it is connected to how our customers perform and how they manage to overcome the chip shortage issues. So, while in the short term there could be fluctuations even with us. In the medium term we will always be much-much ahead of the industry. If you look at the industry growth rate in US passenger vehicle, Europe passenger vehicles, these are our important markets, right? All of them have seen a double-digit de-growth while we have grown by double digits. So, that I can promise you that we will always be far better than industry growths. But if overall industry again has the same issue, we are not unaffected, we are part of it and we will remain affected because even if we can make our parts and supply that, no car can be sold 99.9% complete. So, my parts will just sit in inventory, if any one person in the supply chain is affected.

Nitin Arora: This answers my question, thank you. Just dwelling more onto it because you had some client addition and as stated in the call in starting, I'm not trying to get into any client names or client specific things. I know you don't take those questions. The question is more from the penetration point. When six months back when China was 13% of EV suddenly becomes in six months 22% of the EV. The question here is that do you see in massage you know because of this even Europe is growing very significantly when we look at the numbers, is it more of an aberration or because in the last six months there is no new model launches which has come in the electric part, it's more of the existing models which is going and taking the electrification numbers higher. So, when in the next 2-3 years, the way luxury car makers are trying to launch the model of the EV in the next 2-3 years' timeframe, you know, just from a longer term, I'm asking this question to you 2-3 years. Again, not taking any client specific name, could we see some more client additions here from a luxury side, for you?

Vivek Vikram Singh: Okay, yes, is the short answer. We've already got, I think now a fair number of customers. Prateek can you just take us back to BEV slide which has the number of programs and customers? Perfect. So, Nitin, this is already 11 customers in three years. We will have many more customers just because of the pipeline we have and many more new entrants. There are a lot of people who still don't have a significant EV model or a significant born electric platform. I mean some of the car makers have retrofitted, I would say for the lack of a better word for existed models with a battery electric vehicle powertrain. When they design some vehicles from scratch, they will come in and we will add more and also to be noted now right now my revenue if you saw five programs were what were only ramped up last quarter now it's already seven. When these 13 come in, the revenue will also become far more diversified across many customers. And it includes some of the major current automakers also just that their programs haven't started yet, and I hope that in 2022-23 a lot of big programs will start.

Nitin Arora: This is helpful. I'll come back to Vivek in the queue and thank you so much for answering this.

Vivek Vikram Singh Thanks Nitin.

Caihua Chan: The next question is from the line of Mr. Satyam Thakur from Credit Suisse. Satyam, your line is now unmuted. Please go ahead.

Satyam Thakur: Thanks for taking my question. So first question to Vivek, as you have talked about that, your first set of BEV customers on the differential sideway were performance EV customers and now you are trying to go down the curve and get more into mass market EV as well and you have had one order win from Asia, but just trying to understand the dynamics how that differs there because with the performance BEV cars, we know in what you did really well; the differentiation in terms of your ability to deliver high torque applications, right. So, does the appreciation for that differentiation really go down as we go down to the mass market and what will that manifest into, will that manifest into lower margins?

Vivek Vikram Singh: Hi Satyam. Good to hear from you and a very good question and I know that the last phrase you used is the crux of your question. But I will still answer the technical part of it also. Yes. Just because a customer of ours makes a smaller sized vehicle or a lesser priced vehicle, it doesn't mean that they don't want to give their customers our consumers, the car drivers a better, more kicky driving experience, you know, a more torque car. So, they are focused, and this Asian customer wants to make a really high torque zippy application. It just doesn't have to be EV for the sake of it. It should be a battery electric vehicle, which is also fun to drive, high performance while being smaller. Right. What is important for us is to deliver. Like we keep saying more torque per gram. Now keeping the constraints of a smaller car in a smaller package in mind, can we deliver a differential assembly which delivers that higher torque while not costing a lot. And doing it at the margins that we were used to. So, to answer the last part, No. This would be equivalent margin to all our battery electric differential assembly projects that we are doing, same. And that is the trick right to try, you can always get market share by lowering price. Without sacrificing price by designing the product to be more efficient, the materials to be more efficient, the gear design to be more efficient that you are using less, hence it costs less.

So, you are not reducing price by sacrificing a profit but you are reducing price by reducing cost of manufacturing, which is why this is very key for us and it is an important win because it opens the door to a lot many automakers who don't have the, you know, the luxury EV offering only. Most of the car market is actually geared towards the hatchback, compact or small sedan space. So, it allows us far greater access. Now we can access, I would say the middle of the pyramid as well.

Satyam Thakur: Thanks Vivek, thanks for that. And, if I can just also get an update on what's happening in our effort to win BSG customers and so far we've still not won an order, if I am correct. So what's delaying this? Is there some challenge, I mean covid driven challenges or some other issues? And if you could also share an update how many customers, we are in discussion with at what stage?

Vivek Vikram Singh: Sure. So, I request Sat to take it but overall, no new win. If there was, I would have reported it. Sat over to you.

Sat Mohan Gupta: Yeah, thanks Vivek. We are working with a few customers both in Europe and in Asia. And generally, it's a very technology driven component of the assembly. It has its own a lead time for testing and validation, so we are engaged with right now around four customers and the discussions are going pretty well. So, at the right and appropriate time as Vivek said we will inform you on further development.

Satyam Thakur: Okay, thank you for that. And lastly one question for Rohit, if I may. So, on margin front, our margins slipped a bit while topline performance was very good, margins slipped a bit, and especially if I back out what the implied Comstar margins would have been, you know, consolidated minus standalone kind of. So that seems like Comstar margins might have slipped to as low as 20%. So is that ballpark correct estimate? And secondly, you know, I mean, how do we improve from here? Because from Comstar side we don't have a pass-through arrangement or an opportunity to take a price hike or something. And so how does the margins start improving, especially given traction motors potentially could be a bit more margin dilutive is the sense one has.

Rohit Nanda: So ballpark, I think the number sounds okay. And the number that you spoke about. Now see in terms of margin we have already explained. So, in case of, even the motor business also, there are both kinds of cases, so we do have material pass through for copper, in case of many customers, we do have a price pass through for aluminum. So steel is the only commodity where we don't have any pass through. So, there are two types of impact which has come on the margins on the motor business side, like I explained for the overall console numbers, one is the arithmetic impact wherein in spite of the price pass through there is a drag on the margins because of the arithmetic effect. And the second is the genuine impact on the margins because of increasing the RM prices. So that's why we did mention that because of the strong RM prices, the margins were sort of under pressure in the last quarter.

Vivek Vikram Singh: Yeah, and to add to what Rohit said, Satyam, the real thing there, the real loss is actually only about 2%. The rest of it is actually just math what Rohit showed you. That because the base changes and the extra money that you get as reimbursement for material price increase, goes sits in your denominators. So, the percentage changes, but it's not real. On how much did you make in absolute terms remains the same. So the 2% is the actual drop. It's not as high as one would imagine. Material prices will cool at some stage, but when, I can't predict and it will come back, as it does. We have seen in the last six years, many of these cycles. That's why I keep saying it fluctuates; second, the second part of it, when you're looking Y-o-Y last year we had unusual actually, highly unusual forex gains which was in our favor and artificially inflated those margins at that point. I think also because we do mark to market accounting of forex where in every quarter we actually look at the value of all our forex (inaudible) and there is more fluctuation quarterly basis. But the real drop is actually 2%.

Caihua Chan: The next question is from the line of Mr. Shyam Sundar from Sundaram MF. Shyam your line is now unmuted. Please go ahead.

Shyam Sundar: My first question is if we look at our geography mix, clearly China has done exceedingly well quarterly. So, I mean without taking any name there, what's exactly happening from our supplies to China and how do we think of this going forward? That is the first question.

Vivek Vikram Singh: Hi Shyam, good to hear from you. One, we have actually added China and all of Asia, rest of Asia to one thing called Asia, just for a comparison because we were doing a very strange thing saying North America and Europe which were two continents and then suddenly saying China, which is a country. So, we put that, but you're right. A lot of the growth has come from that segment mainly because if you look at it relatively, China has de-grown the least amongst all three major car markets. There is no other real reason. So, if everyone was 100 and if everyone dropped by let's say 20% North America dropped by Europe, dropped by 15% and China dropped by only 2%, relative proportion in the mix goes up, that's all that happened. There is no new, no new win or no new major program that ramped up in this quarter, it's a relative shifting of revenue.

Shyam Sundar: Okay, okay I think there is some shift in terms of classification, I think I misread.

Vivek Vikram Singh: What we did. RoW was a bigger chunk which was also actually almost all Asia, because if you look at these continents Asia, Europe, and North America, and we take India out of Asia of course there is not much left in the automotive world, there is just UK and South America which is 1% of our revenue, but biggest part of Asia is China and will continue to be China.

Shyam Sundar: Sure, thanks for that. So, I think my other question on the margin I think was answered in the prior question. The last one, if you have to think about 17% sequential sales growth, what would have been approximately volume vis-a-vis realization increase? Realization was it like 3.7-4% that we have also spoken about in the margin sections? Just trying to get the split between volume and realization that we got in the topline.

Vivek Vikram Singh: Sorry, I did not understand, Shyam.

Shyam Sundar: Okay, revenue growth on a sequential basis was up almost 17% at the console level. Just trying to understand how it would have been split volume and realization increases that you would have got because of the commodity pass through, that's all.

Vivek Vikram Singh: Good question. I can't answer it just yet. It would require some clever thinking because volume I have to think about gears volume, assemblies' volume, there will be so many products, it will be hard to do. But you're right, there is a bit of what we call empty sale. Empty sales are basically nothing that you've got because steel prices increase or copper price increase, you just got the pass through, right? And that is empty. I could say that would be a percentage, which is why actual EBITDA margins in that sense has not gone down that much, it just looks optically because there is some empty sales. By how much, I can't answer but I will get back to you on this one. Actually Shyam, I will answer that, what Rohit said 3.7%. So, 3.7%, is that increase which is the math part of it.

Rohit Nanda: Vivek but that is not on a sequential basis because second quarter we didn't have a price increase, there was only some pass through. So actually between first and second quarter there is no empty sales, I mean the terminology you used so to say and in terms of volume, I think it's a bit tough because there are three products or four products we are looking at and clearly here you can see the BEV revenues have grown faster than the rest of the revenue so that's a different unit of sale as compared to..

Vivek Vikram Singh: Current, part realization won't make sense because even within one type of product there will be hundreds of SKUs with different pricing. Actually, there are products in gears for example, there is a gear which is Rs. 45 and there is a gear which is Rs. 4,500, so very hard to figure that bit out.

Caihua Chan: The next question is from the line of Mr. Nitij Mangal from Jefferies. Nitij, your line is now unmuted. Please go ahead.

Nitij Mangal: Hi, good evening and thanks for taking my question. I wanted to understand what are you doing on the Starter Motor side differently that's helping you gain market share? I think the differential gears are better understood but on starter motors seems to have gained over the last few years. So, what's really driving that?

Vivek Vikram Singh: Hi Nitij, good to see you again. Sat do you want to take this and speak a little bit about the differentiating factor or USPs of our Starter Motors?

Sat Mohan Gupta: See Nitij, for starter motor it is the power to weight ratio and also the durability cycle, which we are offering to our customers and most of the growth happened in a segment where both are, very critical for the vehicle. In addition to that, we're also giving a very good advantage to OEM's on the temperatures handling and our starter motor can handle up to between minus 40 degrees, 220, 140 degrees. So, these are the advantages we are offering as our standard package to the OEMs. Though other tier 1s would ask for the premium on as far as the pricing is concerned but we are offering these as our USP. The other factor which contributes for us is the response to the concerns or response to the customers on their applications. So, we don't just give our standard Starter Motors. We worked with OEMs, and we give them application specific solutions. So, these are the, some of the advantages we are offering and that's helping us to win businesses.

Nitij Mangal: Thanks very much and just quickly, can you share what are you utilization levels in both gears and motors?

Vivek Vikram Singh: So, gears at the end of first half around 75%, assemblies well very close to 100%. In differential assemblies, the demand supply keeping us on our toes. I think in the motor business, for the Starter Motor settlement, it will be between 55 to 60%. There we had installed a fairly high amount of capacity, 2-3 years ago so we have that available.

Caihua Chan: The next question is from the line of Mr. Jinesh Gandhi from Motilal Oswal. Jinish, your line is now unmuted. Please go ahead.

Jinesh Gandhi: Vivek, continuing on the question of capacity. The starter motor capacity which we had put 2-3 years ago, can that be, is it fungible between Starter Motors and Traction Motors? How does it work?

Vivek Vikram Singh: Sat do you want to take that?

Sat Mohan Gupta: Sure, these are the two different products and it's some of the equipment's you can use it, but primarily these are the assembly lines. So, these are more specific to Starter Motors and the EV motors. But within Starter Motor you can, I mean, you can produce a different type of starter motors. It can range from 1KW to 2KW. So, in that sense, it's fungible. But between two product line, it's very difficult.

Vivek Vikram Singh: Yeah, and to after that Jinesh, the motor business, both traction motors as well as starter motors is not that CAPEX intensive compared to the gear business for around Rs. 600 of investment, you get about Rs. 3,000 revenue on starter motors. So 1 is to 5 you know, Rs. 1 capex, Rs. 5 revenue. So, because it's an assembly business, right, so it's a lesser capex.

Jinesh Gandhi: Right. And with respect to the traction motors, particularly on the 2-wheeler side, how well are we geared up for any substantial ramp up in the Indian market?

Vivek Vikram Singh: Great question. Actually, it's taking us by surprise, the speed at which the ramp up is happening. I think that is one of our key operating things that we look out for. So, Sat, how much is our BLDC capacity right now?

Sat Mohan Gupta: Today we are at 150,000 units a year and we are in the process of setting up an increase in the capacity to 400,000 units, both BLDC and PMSM.

Vivek Vikram Singh: So, Jinesh we are quite ahead because you know, each vehicle only requires one, and last year it was only 25,000 and we were at that time 100,000 capacity. So, we were quite ahead in terms of capacity than what the industry was. But looking at the fast rate of growth, we are staying ahead of you know, the demand curve.

Caihua Chan: The next question is from the line of Mr. Keshava Bharadwaj. Keshava, your line is now unmuted. Please go ahead.

Keshava Bharadwaj: I have a couple of questions. One is when will the Government announce PLI schemes, so it will start adding to the bottom lines? That's one question. And the second question is, I recently saw a tweet from you on the new factory setup being brought up. So, how long will it take for that, and what would be the main components that you would be producing in that?

Vivek Vikram Singh: Thank you, Keshava. Thank you for following me on Twitter. I didn't even know anybody saw those tweets. But yeah, so the factory we are building is in Chakan. It will be a plant where we'll make differential gears and differential assemblies. We also have an existing small plant in Pune that we will be shifting to this large plant. It is our largest plant yet at 10 acres, should start getting operational. Vikram, you want to take that one on when and what the plans are, Vikram?

Vikram Verma: So this, the new plant, we are targeting by the end of March or April, which should be in production. But this will be, the first phase will be to shift our existing, as Vivek explained, our existing Pune plant is actually a very small plant which is overflowing and then we are shuffling some businesses and redistributing our volumes from Gurgaon, which we are sending all the way to South and West. We'll be redistributing and creating more space in Gurgaon because as the volumes are ramping up, we need more space to set up in Gurgaon. And while we will expand in Pune to cater most of the South and the West. Of course, we have a differential assembly business and we will grow the differential assembly business for the Indian domestic, for the West & South. That's our overall plan.

Vivek Vikram Singh: Thanks Vikram. And on PLI, Keshava, we have applied, we don't know whether our application will get accepted and we will get enrolled and when the money comes. I think the scheme clearly says that FY22 - 23 will be the first year of when they will evaluate and the payment of the cashflow, the payout from the scheme is I think is in FY 23 - 24. So yeah, we don't know any more than what is already out there in the public domain and what has been announced by the Government. We will apply and what will happen to our application and the certainty of getting any incentive is unknown at this moment.

Caihua Chan: The next question is from the line of Mr. Naresh Suthar from SBI life Insurance. Naresh, your line is now unmuted. Please go ahead.

Naresh Suthar: First question is regarding BLDC. You said about this capacity being increased from 30,000 to 4 Lakhs. So, I just wanted to understand the timelines regarding that and whether we already have order visibility, or we will be, we are currently in discussion, and we'll be having those orders along when we get ready with this capacity.

Vivek Vikram Singh: Sure. So, one Naresh, we already have 150,000 capacities, not 30 and we already, like I mentioned, we are already supplying on three motor programs to two customers in 2-wheelers and one in 3-wheelers. Yes, we are in discussion with, Sat can take this on how many, but quite a few number of potential customers. But that's not anything to think about because only when you have confirmed purchase orders does it becomes real for us. But, Sat, do you want to throw some more light on how BLDC is shaping up?

Sat Mohan Gupta: Yeah, both the products, BLDC and PMSM motors are shaping up pretty well. We are in discussions with more than 15 customers, having a pretty good volumes forecast. As far as the capacity is concerned, I think we will be ready by the first quarter of FY23 with the 400,000 capacities. So, we are targeting May-June of next year where we will be having the capacities. And we are assuming that I mean in that period we will have a pretty good customer base and the products.

Naresh Suthar: Understood. Second question again on margins, you have many things clarified already, but again, sequentially if I see the gross margins and one of the comments you highlighted that there was no price increase, from quarter to quarter we have taken. So, I assume then everything is volume quarter to quarter the sales growth, the gross margin dip there means the raw material inflation has not been passed on, so is it right understanding and how much, I mean after that I want to understand the raw material index, how much it has gone up after that also, so that cumulatively how much is still to be pass through.

Rohit Nanda: Yeah. So, if we look at the sequential slide, Prateek can you please go there, Q-o-Q comparison. So, basically there is a slight fall in the margin on a sequential basis and like we have said it's actually a mixed impact of product mix and also there was some delayed price increase pass through to our vendors which has impacted us in this quarter. So, although there is no increase in the RM prices as such but there is a slight impact which has come in this quarter because we could manage to delay the price increase pass through to our vendors to this quarter. And to answer you other question actually, I think April was the last when the steel prices actually were increased.

Vivek Vikram Singh: Apart from that everyone should remember there's also freight, which has gone up by many times not percentage. It has gone up by many times, freight rates.

Rohit Nanda: Yeah, 4-5 times

Vivek Vikram Singh: Yeah and being an exporter you have to absorb those. Operating leverage and because we are growing, we are able to absorb those and keep the margins where they are. Otherwise, it is a very inflationary environment.

Kapil Singh: Hi Vivek, can I take a couple of questions from you two as well?

Vivek Vikram Singh: Yes sir. Why not.

Kapil Singh: One question has come that was there any RoDTEP benefit for H1 in the reported numbers?

Vivek Vikram Singh: No.

Kapil Singh: Okay.

Vivek Vikram Singh: So, Kapil this is what Rohit meant by in his very broad statements like line of you know, removal of fiscal and whatever benefits that the regulators. Actually, till last year, and this is one of the things I wanted to highlight, that last two years, a lot of things have been gone. MEIS is gone, RoDTEP was supposed to come and help bridge that gap for exporters, it has not. We used to be in the GSP regime with the US when we exported to the US, that benefit is gone. We are not on that list anymore. So, there were a lot of incentives available to exporters in general which are all gone, which is why I keep maintaining that the fact that we are still between 26-29 is quite remarkable after all of these things have gone away.

Kapil Singh: Got it. One more is from Priya Jay. Can you shed some light on collaboration with Nexus IRP on magnetless Motors? What is the expense incurred due to the same and projected ROI?

Vivek Vikram Singh: Okay. I'll ask Mr. Deshmukh to answer that but the projected ROI is not something we have calculated or will calculate. To be honest, if innovation is subject to the whims of ROI alone, there will be no innovation in the world, something that doesn't exist, how do you calculate the market of that? If we all became people who judge every innovative step by just measures of how much money it will return, there will be no innovation. I mean there is a very good book called Innovator's Dilemma that'll guide everyone to, and the classic mistake that big companies make when they look at new products or new innovations like a magnet-less motor is this, what is the size of the potential market? Market is not big enough, let's not do it. What is the IRR, what is the ROI? We have not, if we had been that kind of Company to be honest we would have never made the drive assembly for EVs. At that time when we made it in 2016 there was no market. So, that I can assure you we will not be that Company. So, we have not and will not calculate it. What is the expenses and status, Mr. Deshmukh, you can brief everyone on it.

Mr. Deshmukh: The difficult part of the question Vivek has answered. Well, the electric motors that we make, and everybody makes have got magnets and especially for the high efficiency motors which go into drive applications. These magnets are made from rare earth metals and this material comes from China or 75% or 90% of this comes from China. So, two problems, one is that it has to be imported from China and because of geopolitical reasons the prices fluctuate so you can't be sure about when the prices will go up. Over the last 10 years, these prices have gone up and down by as much as three times. Second problem is in a typical motor, the cost of these magnets, especially magnets, high performance magnets of this rarer type, costs anywhere from 20% to 45% depending on the type of motor and configuration, etc. So, it's a big chunk of the cost. What we are trying to do with IRP with the Israeli partner is co-develop an electric drive motor, initially for 2-wheeler, 3-wheeler applications which will not have magnets. So, once we develop a motor of that type and good progress has happened so far, but right now it is in very early stages of development. We hope to complete this in the next 18 months. When that happens, when we realize that we will get a big cost reduction, we will be free of uncertainties of the magnet cost and therefore we should be able to get more market from customers. Ultimately, the benefit of this will go to our customers and to the entrances. I hope I answered your question.

Vivek Vikram Singh: Thank you sir. I mean, it is worth doing because like Mr. Deshmukh said it makes the product lighter, more certain, less polluting because neodymium mining is a very polluting activity and eventually makes the electric vehicle cheaper for the end consumer, hence it pushes the boundaries of electrification and creates more market, which is why it is worth doing and we will do it. First, we will make the product, if we do succeed, then we will look at how much market, how much the capex would be behind it, etc.

Caihua Chan: The next question is from the line of Mr. Mahesh Bendre from IDBI Capital. Mahesh, your line is now unmuted. Please go ahead.

Mahesh Bendre: On capital expenditure you said that this year we reduced it from 6.5 billion to 4.5 billion. So, will this capex go to next year?

Vivek Vikram Singh: Yes, most of it. I think Rohit mentioned that about Rs. 15 crore was, we have found a more efficient way. So Rs. 15 crore is reduced permanently, but rest of it will just shift by one quarter each.

Mahesh Bendre: So what could be the number next year on capital expenditure?

Rohit Nanda: So Rs. 180 crore is what is shifting from this year to next year. And I think the original plan for the next year was around ballpark Rs. 150 crore. So that's where we are as all. Now. Obviously with new order wins and all this can change.

Kapil Singh: Thank you team, due to time constraints, this was the last question that we could take. I would like to thank the management of Sona Comstar for taking out time. I know we had a bit longer than what was expected, thanks to all team. I'll hand over Vivek in case there are any closing comments.

Vivek Vikram Singh: No, nothing. Thanks. Thanks everyone for attending, giving us your valuable time, attending our earnings call and showing interest in us and in our story. We are committed to building a long-term business while ensuring continual alignment and transparent dialogue with our shareholders. Should you have any further questions or need any clarification from us please feel free to reach out to us or to CDR India. Thank you once again and see you next quarter.

Caihua Chan: Thank you. Thank you everyone for your time. You may not disconnect from the call. If you have any questions, you may email it to us and then we will pass it to the management accordingly. Thank you.
