



“CEAT Limited Q3FY15 Earnings Conference Call”

February 6, 2015



**MANAGEMENT: MR. ANANT GOENKA – MANAGING DIRECTOR –
CEAT LIMITED**

**MR. SUBBA RAO – CHIEF FINANCIAL OFFICER –
CEAT LIMITED**

ANALYST: MR. ASHVIN SHETTY – AVP – AMBIT CAPITAL



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Moderator: Ladies and gentlemen, good day and welcome to the CEAT Limited, Q3 FY 2015 post results conference call hosted by Ambit Capital. As a reminder, all participant lines will be in the listen-only mode and there will be an opportunity for you to ask questions at the end of today's presentation. Should you need any assistance during this conference call please signal an operator by pressing '*' and then '0' on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Ashvin Shetty from Ambit Capital. Thank you and over to you Mr. Shetty.

Ashvin Shetty: Thank you. Good afternoon ladies and gentlemen. On behalf of Ambit Capital I welcome you all to the Q3 FY 2015 results conference call of Ceat Limited. Ceat is today represented by Mr. Anant Goenka, Managing Director and Mr. Subba Rao, Chief Financial Officer. Now, I would like to hand over the call to Mr. Goenka for the opening comments and then we can start the Q&A session. Over to you, sir.

Anant Goenka: Good afternoon and a warm welcome to the Ceat quarterly call. I am Anant Goenka, Managing Director and I have with me here Mr. Subba Rao, our CFO. Thanks a lot for your interest in Ceat and I will give you a brief update on the results and key parameters. Ceat registered a negative 1.5% revenue growth on a year-on-year basis largely because of some lower pricing and mix but on a volume basis we were flat. Raw material prices have come down quite well over the past year by nearly 10%. The benefit in part has been passed on little bit to the OEM segment as well as the export segment. In the replacement segment we have largely been able to be quite in control but in December and January there has been some amount of price drops. Natural rubber prices have further declined this quarter and crude prices have also come down quite well in the last quarter and we expect some more benefits to reflect in the coming few months in the next quarter and quarter and a half time going forward.

There has been flat volume growth mainly on account of decline in exports which has actually shown a negative growth of over 10% while on the domestic segment we have seen around a 5% growth. Passenger segment which are our focus areas like motorcycles, passenger cars and utility vehicles continue to grow well and they have grown well over 20%. On a quarter-on-quarter basis we registered a marginal revenue decline of about 1% and very similarly flat volume growth. Exports have grown by about 6% while OEM showed a decline of about 7% on a quarter-on-quarter basis whereas replacement has shown some marginal growth. Raw material prices were lower by around 5% and softer RM prices have improved gross margin both on a year-on-year and quarter-on-quarter basis.

To sum it up, I would say this quarter has seen a flat volume growth but margins have improved largely because of raw material prices as well as improved product mix. Going forward on the raw material prices, rubber prices have softened a fair amount and we expect to continue to remain around current levels. Crude prices have also come down and we expect that benefit to come forward as I said and going forward we expect overall good growth both in the domestic



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OEM segment as well as replacement segment. I now hand over the call to Mr. Subba Rao who will take you through the key financial parameters.

Subba Rao:

Thank you Anant. Ladies and gentlemen, good afternoon. We have already included detailed financial analysis in the presentation circulated to you. I will just take you through the highlights of the financials. The gross margin being the difference between the net sales and material cost have expanded by 590 basis points to 40.5% year-on-year basis and by 210 basis points on sequential basis. Though the revenue has registered a marginal decline by 1.3% which we see as an aberration the EBITDA quantum rose by 16% year-on-year basis to 183 Crores and by 4.5% on sequential basis. The margins also have expanded by 190 basis points year-on-year to 13% and by 70 basis points on sequential basis.

Finance cost for the quarter has come down by 11 Crores year-on-year basis and by 4 Crores sequentially largely due to reduction in the borrowings and lower interest rate. Average interest rate has come down to 10% from 11.1% on a year-on-year basis. Profit before tax to net sales has expanded by 250 basis points to 9.4% year-on-year basis to 132 Crores in absolute terms and by 63 basis points sequentially. EPS has grown to 23.73 from 18.62 year-on-year basis and from 22.9 sequentially on expanded capital. Following the 400 Crores QIP, the company's net worth has gone up to 1,637 Crores from 1,119 Crores year-on-year basis. The book value correspondingly per share has gone up to Rs406 from Rs283 year-on-year basis. Consolidated debt stood at 882 Crores from 958 Crores sequentially and 1,115 Crores year-on-year basis. Long-term debt equity ratio is 0.2 times while total debt equity has come down to 0.5 times from 1.1 times year-on-year basis. Debt to EBITDA stands at 1.2 times and EBITDA to interest significantly moved up to 5.9 times for the quarter up from 3.8 times year-on-year basis. Return on equity and return on capital employed for the quarter stands at 22% and 23% respectively.

On Sri Lanka operations front the revenue has declined by 5% sequentially; however, it has grown by 1% year-on-year basis. EBITDA margins grew by 480 basis points from 19.7% to 24.5% year-on-year basis. With this I conclude my presentation and invite questions.

Moderator:

Ladies and gentlemen, we will now begin with the question and answer session. The first question is from the line of Chirag Shah from Edelweiss. Please go ahead.

Chirag Shah:

Thanks for the opportunity. First question is you highlighted that in replacement market also you had passed on some of the benefits, just wanted to understand what is driving this cut and who is playing the spoilsport in the industry? That is the first question. How one would look at you passing on the benefit in the replacement market because commodities prices are going up we are not able to raise the prices in the industry and now we are not willing to retain even in the replacement market?

Anant Goenka:

Thanks Chirag. Largely, what has happened is we have been able to retain prices quite well over the last two years. Raw material prices have reached quite a low level if you were to compare what has happened in the last two years and we expect a further decline going forward. So I think



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there is a point at which competitive pressures start getting felt. I would not like to highlight on who has gone about giving first price cut and then who has followed by. Generally there has been competitive pressure which has caused price drop. So while there has been a price drop, on the other hand, raw material prices are expected to further come down. So net-net the industry has benefited a fair amount with the recent raw material reduction that has happened in the last two year's time.

Chirag Shah: What would be your average rubber price and going forward Q4 pricing for the quarter on an average basis?

Anant Goenka: I would not be able to share with you exact numbers but rubber has been prevailing at about 120-130 rupees per kilo ex-Cochin for the last quarter whereas other raw material prices nearly the balance half are all crude-based products and they all start getting passed on after sometime because for example carbon black, the first impact will be felt by the carbon black manufacturers and then it get passed on usually about 2.5-3 months after that. So items like that, that impact will come in going forward. We all know how much crude has come down, so to that extent the balance raw material will also get affected. We do expect a good reduction in raw material prices from Q3 to Q4 also.

Chirag Shah: You also expect rubber prices to correct from here?

Anant Goenka: No. I don't think to. I think rubber prices are today at between 125 and 130 rupees per kilo. I don't see any change happening. Unless there is some external government action which one can never predict say for example there is an increase in duty or anything like that very difficult to say. One more thing I would like to add is that there have been a lot of petitions to the government on the fact that there is a pressure to reduce prices and that too has had some impact on price drop by the All India Tyre Dealer Federation or other tyre-consuming industry.

Chirag Shah: But is it fair to assume that the price drop scenario is actually for the time being at the current raw material basket level or not necessary?

Anant Goenka: One can never predict that, we have no idea that there would be a price change in December or January, so nobody can predict that. I do hope that it has come to an end but I can never say.

Moderator: The next question is from the line of Sachin Kasera from Lucky Investment Managers. Please go ahead.

Sachin Kasera: Good afternoon Mr. Goenka and congratulations on a good set of numbers. Basically if you could just quantify what is the type of price correction you have seen across various segments both in terms of OEM as well as replacement and across categories, is it like equal across two wheelers and CVs or is it different across segments?



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Anant Goenka: For example OEM there has been no price drop. There are certain OEMs where we have commodity linked pricing that has been getting passed on even about year ago, year and a half, beyond the formula there has been no price drop at an OEM level and so we have linkages with commodity pricing with many of them, which is a continuous process that has been happening. On the replacement side there has been a price drop, sometime around early or middle of December and that will save approximately overall about 2 percentage points in December, about a 0.5% in January, similarly in LCV about 1-2% between both the two periods. Farm has also seen about a 2-3% between both the periods. So these are the key categories, so largely between commercial vehicle and farm we are seeing some price drops, so it has not been across the board, across all SKU but it varies on SKU level but this has been mainly in the commercial segment.

Sachin Kasera: What about passenger cars and two-wheelers sir?

Anant Goenka: No, not really.

Sachin Kasera: My second question is regarding that you are going to put another 60 Crores in subsidiary especially tyres, if you can elaborate a little on that what exactly is the thought process?

Anant Goenka: We have got a board approval for this. I mentioned a couple of times earlier that we are quite interested in this area. We are still working out the modalities and we have still not finalised any plans but it is an area we are interested in. So I would like to keep that on hold for now and if we take a final decision we will make an announcement at that point of time.

Sachin Kasera: Because we have I think now taken almost approximately 110 Crores that is a reasonably large sum of money from our balance sheet point of view.

Anant Goenka: We have the board approvals that we have got, so we will take a call at the right time and let you know.

Sachin Kasera: Any timeframe by which we can expect some clarity in the next 3-4 months or is it going to take much longer?

Anant Goenka: We will provide you with some clarity in the next couple of months.

Sachin Kasera: Another question on the volumes, you mentioned that volumes were flat; these are the sales volumes but what about the production, because my presumption is that the volumes in two-wheelers would have grown as you mentioned which means that was the production at our own plants is down, is that a correct assumption?

Anant Goenka: It is not as much a matter of production, what has happened is there are two or three trends in the industry which have been a challenge. One is exports as I shared, there has been challenges that are coming in exports, tremendous competition from Chinese tyres in other countries; Chinese manufacturers are supplying tyres at below raw material prices which is making it very



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challenging. I do believe this is not sustainable and there will be some impact on Chinese manufacturers going forward in the form of closure of factories etc., is what I expect to see but this is something that is being felt as a result of competition.

The second is radialization, in exports again, we were selling largely bias supply tyres which is produced across the industry in India; now radialization is happening all around the world, so the demand for those tyres is going down. So as you replace them with radials net-net you don't see an increase, as radial goes up, bias goes down. These numbers therefore largely remain flat or see very low growth - that is the challenge we are facing in exports. On the domestic side there is some challenge, largely the industry has totally seen a huge drop in demand. It is on the OEM side as well as replacement side and that has had some impact on volumes, so we have seen a slowdown on truck bias in domestic as well as tractor in bias and exports overall we are seeing a slowdown so that is net-net and nullifying the positive growth we are seeing in two-wheeler and passenger car.

Sachin Kasera: If I understand correctly the more profitable segment which is basically passenger cars and the two-wheeler there we are seeing growth also and not too much of pressure on prices whereas exports and CV anyway the profitability is a little lower, we are having volume as well as margin pressure, is that understanding correct?

Anant Goenka: Exactly.

Sachin Kasera: Just a followup, you mentioned that certain OEMs have tie-ups in terms of passing through the raw material prices so do we have to pass on the entire benefit because we will also have some other conversion cost related which may have gone up. So how does it exactly work, the formula, with the OEMs regarding the passthrough of raw material prices when they go up or down?

Anant Goenka: They may vary customer to customer but broadly they are linked to raw material pricing so there is a certain index that is calculated based on the formula that is used in the tyre and it is largely linked to that and then sometimes as an exceptional basis if there is a need to change the formula we negotiate that.

Sachin Kasera: I am just trying to understand how do we get compensated for the increase in cost other than raw material, so raw material as I mentioned is a passthrough when they go up or down but I am saying there are also other costs for us associated other than raw material, do we get a passthrough for them or they remain more or less static over a period of time?

Anant Goenka: I don't have a 100% answer on this but I think those remain static, so there are efficiency improvements on the other hand and there is an inflationary impact and therefore as I said that raw material linkage is there but on balance items, I think presumably asking things like fuel and manpower and things like that those items I don't think there is a linkage but I can get back to you on that.



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Sachin Kasera: Because if we see the reported numbers, costs other than your raw material have gone up, so in case we pass on the benefit of raw material to the OEMs we would still have taken some impact on the margin despite lower RM because while the RM cost has been passed off, the other costs remaining static or going up and we don't get any benefit of that, margins could have been impacted there...

Anant Goenka: It is a very valid point. I will get back to you on that because I think it varies from customer to customer. I don't know the exact formula.

Sachin Kasera: Just, if you can update us with the status of the Bangladesh plant, what is the status and when do we expect commercial trials?

Anant Goenka: Bangladesh plant has been delayed by about three months or so largely because of some challenges we have had in the land, there were some issues with the forest department that we have had out there and therefore not been able to work on the land. We did start again on January 1 after about 2.5-3 months closure of work, so I would say we are still about 10 months away at least.

Sachin Kasera: Has there also been any impact on the project cost because of this delay?

Anant Goenka: Not really.

Sachin Kasera: What about the progress on the Indian expansion of both the two-wheeler as well as Halol expansion?

Anant Goenka: Halol expansion is coming along well. We are perhaps even a little bit ahead of schedule in Halol and we expect sometime by July or so the plant to be ready. On Nagpur we are going well on track; we expect within a year sometimes by Q4 of next year for the plant to be operational. So both these plants are moving along very well.

Sachin Kasera: You said Q4 of FY 2016, is that correct?

Anant Goenka: Yes.

Sachin Kasera: One last question regarding the financials if I see the current assets they have gone up quarter-on-quarter by roughly around 400 Crores from 1,640 to 2,047, I presume a large part of that is because of the cash that you have received or is there some sharp increase in debtor or inventory?

Subba Rao: You are right it is because of the QIP cash.

Sachin Kasera: So the debt which you are reporting which is 882 that is net of cash?

Subba Rao: No, that is gross of cash.



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- Moderator:** The next question is from the line of Rohit Gupta from JM Financial. Please go ahead.
- Rohit Gupta:** Hi Anant, congratulations on a good set of numbers. Couple of questions from my side, the first is when you just look at different segments where there has been a price cut and maybe it is dominated more in the CV and the farm and not more in PV and two-wheeler would you attribute this more to pressure from customer or is it just competition pressure where one kind of starts off and others have to follow suit because the players are frankly the same right?
- Anant Goenka:** It is largely from competition.
- Rohit Gupta:** Why would you think this would not be repeated across other segments maybe a PV and a two-wheeler because the players are the same?
- Anant Goenka:** I have not said, it can be repeated, it has just not happened until now. It could very much happen.
- Rohit Gupta:** In terms of just the next 12 months I would assume most of our plants are running at pretty much full capacity at this point in time?
- Anant Goenka:** Our radial capacities are fully utilized. Our two-wheeler capacities are quite well utilized. It is only the bias capacities which have slightly lower utilization. It is also at about 85%.
- Rohit Gupta:** If I just look at the next 12-month trajectory for both the topline as well as the net income would it be fair to say the topline would grow if at all marginally if there is a slight mix improvement but the PAT trajectory might be moving in a positive direction because of some of the raw material advantages we might have?
- Anant Goenka:** No, I think growth can come along still well. As I said our Halol plant will be on stream from July, our Halol expansion, so from July onwards you will find that new capacity of passenger car and utility vehicle tyres coming on from them. We have also expanded our capacity of outsourcing in two-wheelers from about 10 lakh to 12 lakh tyres and if you are looking at say FY 2015 June-July of production that would have been maybe at about 8.5-9 lakh tyres. So you see another 20% high growth potential in two-wheeler etc., so in my view in these categories you can see overall good growth whereas in my view on the margin side very difficult to say how raw material prices etc., pan out. So I would be a little bit more cautious and say that margins could be a little bit under pressure because of the current price cut but besides that it should be at the current level not very different.
- Rohit Gupta:** How would the raw material, I think it is difficult to kind of predict how prices for natural rubber and crude would move but in terms of our sourcing how would these contracts be in terms of both crude as well as natural rubber?
- Anant Goenka:** For crude etc., we are largely indexed, for example for carbon black, nylon tyre, which are all crude derivative products are all linked to certain pricing, the only difference is there is a little bit



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of a lag whereas in the case of rubber etc., rubber is largely spot buying and there is some amount of inventory or inventory coming in on high seas if they are imported. So to that extent there is another delay of about 2 months I would say by the time that impact comes in.

Rohit Gupta: Would it be fair to say that a reasonable part of the benefit for natural rubber would have already come in this quarter whereas for crude it might be out?

Anant Goenka: Natural rubber has not gone down from Q3 to Q4. But for crude it would probably play out in the next quarter or maybe the next couple of quarters.

Moderator: The next question is from the line of Ameen Pirani from Deutsche Bank. Please go ahead.

Ameen Pirani: Good afternoon, thanks for taking my question. My question is on the pricing, I think given the fact that raw material have declined for such a long time I think the price cut may not be as severe at this stage but my question was that as and when the cycle turns how do you think the industry is placed competitively in order to pass on those raw material price hikes as and when that happens unlike what happened in the last up-cycle?

Anant Goenka: Very tough question. Very difficult to predict how the industry is going to react. I can just give you a guess what I feel could happen. Initially if there is uptake in raw material pricing within a certain level, say I am just giving broad numbers say up to 5% there may not be any reaction by industry but beyond that I do hope or there could be some price increases but very difficult to say really what will happen. The call is that what is your view on raw material? In my view I am quite bearish on raw material prices even going forward. I think they will continue to remain low. I am extremely negative on the outlook for China which is the biggest impact for commodity including rubber and with that I feel global commodity prices or at least rubber particularly will continue to remain low. The only thing that will take rubber up is government action if they were to take, Indian government action, if they were to take increase import duty on rubber or things like that which nobody can predict.

Ameen Pirani: Right, understood. Sir, coming back to the China issue in India, as I understand and please correct me if I am wrong there is an antidumping duty on truck radial but on passenger radial I think Chinese imports form a significant proportion of volumes, is that a correct assessment?

Anant Goenka: Yes, that is right. I do believe there has been an antidumping duty on passenger car radial imposed but I can confirm that back to you. This could have happened in the last 20 days but I can confirm and get back to you on that.

Ameen Pirani: But you don't see much risk from China dumping tyres into India at this stage?

Anant Goenka: No. They have about a market share of 10% in passenger car and I don't see it getting worse than that.



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- Ameen Pirani:** Okay, fair enough, sir, just coming to the OEM profitability obviously we do realise that OEM margins are significantly lower than replacement and obviously there is a passthrough based on formula but structurally over the last 2-3 years would you say that OEM profitability on its own has improved? Do the OEMs realize that they may need to give you better pricing for the investments that you need to make or has it remained stable over the last 4-5 years?
- Anant Goenka:** No, they have not realized that yet, so I think that remains largely the same but there are ways where you can look at better pricing which is things like making sure you co-develop tyres with them to get a large share of business and there are ways of doing that where you can get it at competitive advantage. So there is no industry structure change that has happened but each company has to figure out its own way of doing that. For example if you co-develop a tyre right in the beginning there is possibly a better chance of getting a higher margin because you have been involved from day one whereas if there are already three established suppliers and you are the fourth one who has to get it you will get in based on pricing that is the only leverage that you have which will allow you entry.
- Moderator:** The next question is from the line of Ashutosh from Equirus Securities. Please go ahead.
- Ashutosh:** This Ashutosh here. My question is you mentioned that there are some price cuts, in the truck bus segment is there a price cut in the radial tyres or is it limited to only bias tyres?
- Anant Goenka:** Largely in the bias category, maybe a little in the heavier side, mostly in the bias category.
- Ashutosh:** Few months back there was shortage of two-wheeler tyres in the market but I think off late there is some ease off has happened so how is the situation right now of two-wheeler market?
- Anant Goenka:** There is still a little bit of shortage but I agree with you, it has eased off quite well.
- Ashutosh:** You mentioned that your capacities have increased from 10 lakh to 12 lakh tyres, when did this come through?
- Anant Goenka:** It is still under way, it has not happened yet. It will happen over the course of the next 4-5 months. We are maybe producing about 10.5 lakh tyres right now, so it will go up to about 12 lakh over the next few months.
- Ashutosh:** Any colour on what other players are doing in the two-wheeler segment, what are your expansion plans?
- Anant Goenka:** No. I would not have any idea on that.
- Ashutosh:** We also hear from the market that definitely they are not price cuts in the passenger car segment directly but there are schemes on and off going on so what is your comment over there?



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- Anant Goenka:** There could be some schemes here and there but those are things which are temporary, so usually schemes do not run for more than two months or so and that continuously happens, so that happens all the time. It would have been happening maybe three months ago, it maybe happening six months ago but those are tactical calls taken by the company.
- Ashutosh:** Sir my question is that in the truck and bus segment because of increasing radial tyre truck industry also definitely the capacities right now players have would become redundant over time, so is that leading to the pressure in the market and that is why the price cuts have come through and if that is true we can see more such actions in the future also?
- Anant Goenka:** I think prices have come down largely because of raw material prices coming down but I agree with you clearly there is a trend that there will be over-capacity in truck bus bias and margins there could come down going forward because utilisation levels are low but very difficult to say that yes the price cut has happened because of this. In my view price cut has happened more because in general raw material prices have come down.
- Ashutosh:** Any threat you see from Chinese tyres in India because in India also the price differential between the Chinese tyres and domestic tyres are quite high especially for a taxi owner and all basically they are kind of shifting tyres, is that correct?
- Anant Goenka:** I would say there is no increased threat from China. Yes on the passenger car side they do occupy a pretty decent market share of about 10% or so but I don't see any change in the last couple of quarters or so.
- Ashutosh:** My last question on the raw material cost, you mentioned that the crude derivatives cost is likely to come down in the coming quarter, so to what extent basically you can see the gross margin benefiting from the same?
- Anant Goenka:** I think raw material prices could come down, crude is about 40-50% of our raw material basket that will come down maybe by 6-7%, so maybe about a 3-4% drop in raw material prices overall or 3% or so roughly.
- Moderator:** The next question is from the line of Nikhil Deshpande from Sharekhan. Please go ahead.
- Nikhil Deshpande:** Good afternoon sir, are you seeing increasing radialization picking up in CV space or is it still normal?
- Anant Goenka:** Radialization is happening but the pace is continuing to be at current level, so radialization is around 30% today, 29-30% kind of level.
- Nikhil Deshpande:** But do you see a tipping point for the sector or something like that your bias may be obsolete faster than what you expect?



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- Anant Goenka:** The tipping point generally is about 15%, so we have crossed that tipping point about a year and a half ago. It took about 10 years to reach 15% and then about 3 years or 2 years to reach from 15 to 30%, so we have crossed that tipping point.
- Nikhil Deshpande:** So in the next two, three years where do you see radialization?
- Anant Goenka:** It could go up to about 50% levels in three years.
- Nikhil Deshpande:** Now, at your Halol you have not invested in if I am not mistaken in the TBR segment; you are only in the PCR segment you had invested?
- Anant Goenka:** Yes.
- Nikhil Deshpande:** Do you require TBR capacity going forward?
- Anant Goenka:** No, we are taking a call to play more and more on the passenger side, while there could be a shortage in capacity of truck radials we are choosing not to play in that segment.
- Nikhil Deshpande:** So you will want to maintain TBR levels at today's production. Okay, sir in the media interaction the CFO was talking about shortage in the two-wheeler capacity currently also, is it still there or how is it?
- Anant Goenka:** It is very much there. At an industry level it has eased off a little bit but clearly there is a shortage in two-wheeler, we could easily sell another 20-30% if we had that production capacity.
- Nikhil Deshpande:** So after the 12 lakh you were looking at further two-wheeler side?
- Anant Goenka:** Yes that is in our new plant in Nagpur that will still take about 10 months to come up. We feel quite confident of utilising that going forward by then.
- Nikhil Deshpande:** But you may see some constraint till the Nagpur plant comes on steam?
- Anant Goenka:** Yes. We will be able to grow because as I said that last year at the same time we were supplying about 8 lakh tyres now we are selling about 10.5 lakhs and this can go up to about 12 lakh during the course of the year. So we will see growth of 15%-plus levels even during the course of the year but there is clearly a lost opportunity because of lower capacity at this point.
- Nikhil Deshpande:** But do you see anywhere you losing market share because of this?
- Anant Goenka:** No, we are growing faster than the industry.
- Moderator:** The next question is from the line of Akshit Gandhi from Aviva Life Insurance. Please go ahead.



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- Akshit Gandhi:** I just had one question, I am reconfirming, you said exports had a 10% volume degrowth while domestic had a 5% volume growth, is that correct?
- Anant Goenka:** Yes.
- Akshit Gandhi:** So that if I back work it that means exports contributes around 33% of your volumes and domestic is 67% of volumes right?
- Anant Goenka:** No, export is about 20% of our volume and domestic is about replacement is about 55% and OEM is about 25%.
- Akshit Gandhi:** If I look at the last nine months where the volumes have grown at a slower pace versus that your other expenses have grown at a far faster pace and certain things in the other expenses would have been variable cost, so what is the reason for this high growth?
- Subba Rao:** Couple of expenses has gone up particularly the wages for long-term settlement with increase in wage cost. It happens once in three years through a long-term settlement, thereafter year on year basis it is only marginal costing will be there. This is one factor, second is because of the production shift, we are moving towards the two-wheeler which is smaller tyres, the bigger tyres occupy less space and for the same weight smaller types occupy much larger space so as the transportation cost, logistic cost would increase which is called sales variable cost. These are the two significant costs that have increased, otherwise normal other cost like your employee cost will keep growing but we need to clock higher volumes to absorb this cost; progressively this will happen.
- Akshit Gandhi:** One thing on the freight side which is an important part of your other expenses with the diesel prices falling should we expect certain benefit over there?
- Subba Rao:** They are automatically indexed to the diesel prices but not the entire freight cost, so freight cost has two elements the fixed as well as variable, the variable part which is about 30% of the total freight cost that gets indexed to the fuel cost which keeps coming down based on the fuel cost movement.
- Akshit Gandhi:** Lastly the cash which you raised through QIP what kind of yield should we estimate on that because now that would start coming in other income?
- Subba Rao:** For the current quarter we have realised about 1.7 Crores which is approximately about close to 7-8%. All this money has been invested in the liquid mutual funds.
- Moderator:** The next question is from the line of Ayush Agarwal from ICICI Bank. Please go ahead.



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Ayush Agarwal: Good evening sir and congratulations on a good set of numbers. I have one question, seeing the recent decline in crude oil prices can we expect increase of percentage share of synthetic rubber in tyre manufacturer?

Anant Goenka: That is very difficult to do. You cannot switch around raw material to a large extent so you can make a change of 1% here and there in the product mix but generally all our products have very well-defined technical specifications which cannot be really changed around too much.

Ayush Agarwal: So, the share will remain at around 70:30, 70 in favour of natural rubber and 30 in favour of synthetic rubber.

Anant Goenka: Yes, roughly.

Ayush Agarwal: Sir, what are your expectations from the forthcoming financial budget because I believe all the major tyre manufacturers have put a wish-list saying that the import duty should be increased from the current 10% to 20% to stay off competition from cheaper Chinese imports?

Anant Goenka: Right, what about that.

Ayush Agarwal: Sir actually one news also came like in case of auto tyre dealers manufacturers they have also put forward a wish-list saying that the 10% import duty should be waived off, so what is your take on that?

Anant Goenka: What should be waived off, can you repeat?

Ayush Agarwal: Tyre Dealers Association have also put forward a wish-list saying that the current import duty of 10% should be waived off mainly to check the unfair and exploitative behaviour of the domestic tyre industry.

Anant Goenka: Basically this is clearly an inverted duty structure that exists right now. There is an import duty on rubber of 20% and import duty of tyres from 0 to 7% or so, now this is absolutely opposite of Make In India, if the government wants to do this Make in India then you have to think of a favourable non-inverted duty structure, so that is the reason, it makes more sense to manufacture outside of India and supply into India right now because you can get cheaper rubber and you will be able to supply it at lower price. So I don't think it makes any commonsense to reduce import duty of tyres.

Moderator: The next question is from the line of Ajay Shethia from Centrum. Please go ahead.

Ajay Shethia: Thanks for taking my question, a couple of questions from my side. First is if you can just help us how has the pricing differential between radial tyres and bias tyres over the last few years and also if you can sort of indicate how has been the movement in terms of profitability on the radial tyres because I assume that earlier indication was that radial tyres are not as profitable but giving



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the trend that radialization is picking up how do you see that changing or how it has changed over the last two or three years?

Anant Goenka: I think roughly radial tyres are about 15% or so higher price than bias tyres. They are also about 15% more in weight, so net-net I say margins are not very different between truck bias and truck radial tyres even now, things have not changed too much yet. Profitability is roughly the same but I do agree that in the longer term radial tyres should be more profitable, that just makes a lot more commonsense, because it is a better quality tyre, much better value add to the customer.

Ajay Shethia: So at what penetration level do you see that margins could be significantly at a respectable level?

Anant Goenka: Tough to give a number.

Ajay Shethia: Second thing what is your market share on the two-wheeler side and how it has moved over the last two years?

Anant Goenka: On two-wheeler side we have been doing well, we have been growing at 20-30% CAGR for the past few years; the market share has gone up sharply about three, four years ago we were at about 11-12% we are now very broadly around 25% kind of market share in the replacement segment but numbers are very broad because data is not very easily available right now.

Ajay Shethia: How has been the traction on OEM side or it is only on the replacement?

Anant Goenka: OEM side also we have done very well; our market share there would be somewhere between 20 and 25%.

Ajay Shethia: How would be the split in terms of the market share across other players if you can just help us out?

Anant Goenka: Difficult to give numbers but largely the other players are MRF, TVS.

Ajay Shethia: Any sense in terms of where MRF and Ceat would be, just a rough number if you can?

Anant Goenka: I would not have MRF numbers specifically, certainly higher than 30%-plus.

Ajay Shethia: Sir is there a significant difference in terms of capex in terms of tonnes per day on the radial side and on the bias side?

Anant Goenka: Yes nearly one-and-a-half times more expensive for radial tyres.

Ajay Shethia: What would be the normal thumb rule in terms of setting up one capacity per day?

Anant Goenka: It varies product to product depending on size of plant; there are too many factors that would affect it.



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- Ajay Shethia:** Is it fair to assume that it would be closer to around 5-6 Crores tonnes per day?
- Anant Goenka:** Yes.
- Ajay Shethia:** Okay and that would be one-and-a-half times higher for radialized as compared to bias?
- Anant Goenka:** Yes, say for example for us we are investing about 110-120 per day capacity and putting a little bit over 600 Crores, this is for radial, so roughly 6 Crores per tonne or so for radials and therefore 4 Crores per tonne for bias.
- Moderator:** Next question is a followup question from the line of Sachin Kasera from Lucky Investment. Please go ahead.
- Sachin Kasera:** Can you just tell us exactly what has been our strategy on the export market because you mentioned that there has been some degrowth in the volumes, we have also reduced prices to meet the Chinese and if this thing continues from the Chinese side what is going to be the strategy in the medium term?
- Anant Goenka:** Can you repeat the question.
- Sachin Kasera:** You mentioned on the exports front there has been some pressure on the volumes and you also mentioned that some of the Chinese are selling below raw material cost, if this scenario continues what is going to be our medium-term game plan and secondly have we also taken any price reduction because of this competition from Chinese in the export markets?
- Anant Goenka:** Yes we have taken price reduction and we have been doing so for the last year and half. Also, exports is one segment where we continuously taken price reduction but going forward I don't see this continuing. You cannot have any business sustaining for so long at such low prices. In my view I don't see it sustaining, it can sustain for three months, four months but I don't see that working out plus yes they are creating problems but I feel there is clearly a segment for them also. So there are clear buyers who say I want Chinese tyres, clearly people who say I want only Bridgestone and Goodyear and so on and some people who clearly say that okay we want a mid kind of value segment which could be the other players.
- Sachin Kasera:** Cumulatively how much will be the price cut we would have taken in exports and how much in the last quarter itself in exports?
- Anant Goenka:** I won't have a number specifically but it would be largely aligned to the raw material price drop that has been there.
- Sachin Kasera:** In a sense most of the drop in raw material would have been passed on as far as export market is concerned?



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- Anant Goenka:** Maybe about 70% or so would have been passed.
- Sachin Kasera:** Secondly was there a differential trend in the replacement market between the passenger segment or the commercial segment in the sense was the growth rate in the replacement market in volume terms better in passenger segment vis-à-vis commercial in the last quarter?
- Anant Goenka:** Yes. At least for Ceat the passenger car segment has grown much better than the commercial segment.
- Sachin Kasera:** I am talking more on the industry perspective?
- Anant Goenka:** Industry I would not exactly the details at a replacement level which one has grown in the last quarter.
- Sachin Kasera:** Because as you mentioned in one of the previous queries last part of the price cuts have come on the commercial segment and on the passenger side we have not seen too much of pressure as of now, I was trying to understand whether that is more a function of the fact that the growth is much better on the passenger side than on the commercial side and that is why the pressure is more on the commercial side.
- Anant Goenka:** Data is not very easy to get on replacement. OEM we get the data because we know how much each manufacturer has produced, replacement is very dependent on economic data and things like that. In my view, passenger car segment may have grown a little bit better because we are not seeing enough economic activity growth even in India, overall mining, etc., still continues to be a challenge. Industry growth is still a challenge. So overall I think passenger may have grown better.
- Sachin Kasera:** Just one followup on this new two-wheeler plant that is coming up. You mentioned that, that will almost double our capacity. Assuming the current healthy growth rate in the two-wheeler market that would still mean that in the next two, three years, we are looking at substantial market share gain in both domestic and OEM or are we also going to start looking at the export market for the two-wheeler?
- Anant Goenka:** Largely we are looking at domestic replacement and OEM but yes we will start exporting with the new capacity coming up but majority will come in for the domestic market.
- Sachin Kasera:** Any sense how long will it take for you maybe to reach full capacity in the new two-wheeler plant?
- Anant Goenka:** I would say a year and a half.
- Moderator:** Ladies and gentlemen, that was the last question. I would now like to hand the floor back to Mr. Ashvin Shetty. Thank you and over to you Sir.



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Ashvin Shetty: Thank you. On behalf of Ambit Capital I thank you all for joining the call. I also thank the management for giving us this opportunity. Thank you and good bye.

Anant Goenka: Thank you.

Moderator: Thank you Sir. Thank you members of the management. On behalf of Ambit Capital that concludes this conference call. Thank you for joining us and you may now disconnect your lines. Thank you.