



“CEAT Limited Q2 FY17 Earnings Conference Call”

**November 08, 2016**



**MANAGEMENT: MR. ANANT GOENKA – MANAGING DIRECTOR**  
**MR. MANOJ JAISWAL – CHIEF FINANCIAL OFFICER**

**MODERATOR: MR. NISHANT VASS – ICICI SECURITIES**



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**Moderator:** Ladies and Gentlemen, Good Day and Welcome to the CEAT Limited Q2 FY17 Earnings Conference Call hosted by ICICI Securities Limited. As a reminder, all participant lines will be in the listen only mode and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the 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. Nishant Vass from ICICI Securities. Thank you and over to you, sir.

**Nishant Vass:** Thank you, Janis. Hi, good afternoon everyone. Thanks for joining us today for the CEAT Limited Conference Call. From the Management side, we are represented by Mr. Anant Goenka – Managing Director and Mr. Manoj Jaiswal – Chief Financial Officer.

Without further ado, now I would like to hand over the call to the Management for their initial remarks.

**Anant Goenka:** Thanks, Nishant. Good evening, everyone, and a warm welcome. I am Anant Goenka and I will briefly share with you our results and a few key parameters relating to our results before opening up for questions.

Some data on our year-on-year analysis:

We registered a 5.7% net sales growth on a year-on-year basis, driven mainly by volume growth of 13.2%. Price and mix resulted in a negative 7.5% impact on growth. Raw material prices were largely lower by about 5% and the growth that came about 13% was mainly on account of strong growth in the key areas of focus, which is the passenger segment, key areas of scooter, motorcycle and passenger car have all grown by over (+25%) growth levels. Commercial vehicles on the other hand resulted in negative growth and exports continued to show positive growth, nearly at 20% growth.

Margins have declined a little bit, largely due to price cuts taken over the last year and raw material prices have not gone down to that extent, so that has resulted in a little bit of impact on our gross margins.

On a quarter-on-quarter basis, our CEAT India's net sales showed negative growth of 2.9%, this is largely due to seasonal factors where quarter two is weak sales season in comparison to quarter one.

A few highlights for the quarter:

I am happy to share that we launched our Puncture Safe Tyres for bikes, this is a first in India. These are tyres which have a special coating of gel on the inside which protects the tyre and prevents air locks in the case of the tyre getting punctured. We also launched the low rolling resistant fuelsmart series of tyres for passenger cars which enabled significant fuel savings for



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end users. For the Puncture Safe Tyre we have applied for a patent and it is truly a unique innovation that we feel very proud of. It is currently launched on a pilot basis and will launch over time on an all India basis once all the learnings of the launch have been incorporated.

We continue to strengthen our association with cricket by signing a four-year bat endorsement deal with cricketer Ajinkya Rahane. We also collaborated with Mahindra Adventures for hosting seven of the most challenging expedition and drive through one of the most difficult terrain of the country.

On the distribution front, we recently launched CEAT Bike Shoppes. A new format of CEAT shoppes exclusively for the two-wheeler segment. This will be a one stop solution for two-wheeler owners, including superbikes encompassing all types of tyre related services.

Going forward, we expect steady growth to continue. The continued focus towards two-wheeler segments and passenger segment will continue and new capacities that are expanding will result in continued high growth in these segments. Also, the new capacities we expect to mitigate any increase in input cost that may come going forward.

I will now hand over the call to Manoj Jaiswal, our CFO, who will talk to you about some of the key financial parameters.

**Manoj Jaiswal:**

Thank you, Anant. Ladies and Gentlemen, good evening. As highlighted in the previous quarter, we have adapted IndAS from the beginning of financial year 2017. One of the key changes under IndAS is company's investment in Sri Lanka JV is accounted using equity method which was earlier consolidated using proportionate consolidation method.

I would now present the financials, primarily focusing on the P&L account and the balance sheet analysis. Our gross margin have contracted by 130 basis points from same quarter last year to 42.3%. EBITDA at Rs. 194 crores has grown marginally by 1% year-on-year, while quarter-on-quarter it has declined marginally by 1%. The margins have declined by 60 basis points year-on-year to 13.7% while remained at similar levels on a quarter-on-quarter basis. While we continue to invest in strategic areas of our business, we have been able to strengthen our balance sheet as well. Our long-term credit rating is upgraded to AA from AA- by CARE ratings.

Consolidated debt as on 30<sup>th</sup> September stood at Rs. 770 crores from Rs. 681 crores in the previous quarter and Rs. 654 crores as on the same date last year. On year-on-year basis, debt-equity remains at 0.3 levels, debt-EBITDA stood at 1.0 versus 0.9 and ROE and ROC net of tax stands at 20% and 14% respectively.

An update on Sri Lanka JV – On a year-on-year basis, revenue grew by 3% and volume growth of 1.5%. EBITDA margins stood at 21%.

With this, we are now open to question-and-answer session. Thank you.

- Moderator:** Thank you. Ladies and Gentlemen, we will now begin with the question-and-answer session. We have the first question from the line of Chirag Shah from Edelweiss. Please go ahead.
- Chirag Shah:** Sir, two questions I had. One was on the capacity ramp up, if you can just help us, what is the kind of effective capacity addition that has happened for the quarter and the road ahead? How the ramp up will look like?
- Anant Goenka:** So, capacity ramp up, we have two capacities coming up, one is our Nagpur plant capacity which is for two-wheeler tyres, today we are at approximately for say end of quarter two we were at about 2 lakh tyres per month in our Nagpur plant. This is eventually going to be an 11 lakh tyre capacity. So we are at about close to 20% out there.
- Chirag Shah:** So 11 lakh per month?
- Anant Goenka:** 11 lakh per month is our total capacity of Nagpur. So we are currently at 2 lakhs.
- Chirag Shah:** And by when we will reach 11 lakhs?
- Anant Goenka:** By around June quarter two of next year.
- Chirag Shah:** And would it be right to assume the ramp up would be like 2-odd lakhs coming every quarter, two to three lakhs, is that the right way of analyzing the ramp up?
- Anant Goenka:** That is right. So that is with respect to Nagpur plant. Halol plant is going to be 120 ton per day capacity. So this should be fully completed also in about quarter one or so of next financial year. We are currently at about 69 metric tons. So we are just over 50%, 60% capacity utilization.
- Chirag Shah:** And again, the ramp up would be in a symmetrical manner, so every quarter some capacity will be added?
- Anant Goenka:** Exactly.
- Chirag Shah:** Second question was on your raw material cost. So, is the impact of higher raw material rubber prices etc, commodity cost visible in the quarter or how should one understand the results from that perspective?
- Anant Goenka:** Yes, so from quarter one to quarter two raw material prices have gone up by about 3%.
- Chirag Shah:** The basket has gone up by 3% for you?
- Anant Goenka:** That is right. What has happened fortunately is that while we had anticipated in April there was a sudden surge in domestic raw material pricing, internationally raw material prices did not go as much and there were different type of rubber, for example block rubber and sheet rubber etc.

So block rubber which is largely international had not gone up to that extent, we were able to take advantage of that. And rubber in a way started to come down to a certain extent as well as we had expected sometime by June - July time period as well. So, in past there were some impact of increased raw material, but net-net I would say it did not go up as much as we had expected to go up. Carbon black for example, etc, came down to a certain extent.

**Chirag Shah:** So this inflationary pressure should continue in Q3 also or how should one look at the ensuing quarters?

**Anant Goenka:** So, I think now what has happened is that natural rubber has begun to further come down a little bit, not going back to the extreme low levels, I would say it had gone down to about Rs. 100 per kg in February, or Rs. 100 - Rs. 110, now it is at about Rs. 120 - Rs. 125 which is lower than that Rs. 140 - Rs. 145 it had gone up to. So, it has come down to a certain extent natural rubber, on the other hand synthetic rubber has begun to go up. But net-net at an overall basis I would say raw material for the next couple of quarters should be at similar levels.

**Chirag Shah:** In that case, how should one look at the industry pricing scenario? Because there are lot of news flow that there is a risk of aggressive pricing, given the capacity that are coming up, especially in two-wheelers and in cars. If you can throw some light, your understanding of what kind of capacities are coming up, it would be really helpful.

**Anant Goenka:** So, two-wheeler capacities, while I believe a lot of players have announced new capacities coming up, setting up capacities takes quite some time. The capacities that do exist in the market at this point in time which people can leverage is a very small capacity, maybe barely, my guess is at a broad level of maybe 50,000 tyres per player kind of levels, maybe a little bit up and down. So, if people are setting up their own capacities, while announcements have been made, it takes about a year for new capacity to come in and then another six - eight months or a year to ramp up, depending on the size of the capacity, etc. So I do not see any specific pressure either on two-wheeler or on passenger car at this point of time. There has been some pressure on the truck bias segment where there has been a little bit, maybe 1% - 1.5% price cut, but we have taken some price increases, in fact in the last couple of months, maybe last three months on the two-wheeler and passenger car space.

**Chirag Shah:** And can you quantify how much, broadly?

**Anant Goenka:** It could be between 1% and 2%.

**Chirag Shah:** And it would be an industry phenomena or...?

**Anant Goenka:** This is just us.

**Moderator:** Thank you. We have the next question from the line of Jay Kale from Elara Capital. Please go ahead.

**Jay Kale:** Sir, my first question was regarding your other expenses in standalone as well as consol. We have seen sharp decline sequentially from Q1 to Q2. So just wanted to understand what would have lead to that, any expenses which have not been booked this quarter and it is just a normalized kind of a trend? If you can just answer that, I will come back for the next question.

**Manoj Jaiswal:** Just to explain that, we had a huge upswing of advertisement cost last quarter due to IPL. And that has been a moderation because IPL as an event was a quarter one event and that has been a cause for significant reduction in terms of the expenses that we make. But there are other, of course there are other small variant but the major chunk of the deduction that you would see is on account of advertisement cost and IPL.

**Jay Kale:** Okay, which is booked in Q1?

**Manoj Jaiswal:** Yes.

**Jay Kale:** Sir, and my second question was regarding the two-wheeler and the passenger vehicle volume growth outlook. We understand with our capacities coming in and our distribution network we expect to outgrow the market, but any kind of a trend of what growth of two-wheeler tyre industry is the market looking at in the next two years and for the passenger vehicle industry what would be the market growth and then maybe players would fight in between that?

**Anant Goenka:** So, I would say at an industry level two-wheeler is looking quite positive, especially with very good volumes coming in, economy looking quite positive. Scooter is growing at 20% plus levels, the automobile demand for scooters in quarter two, YTD scooter growth is at 20% plus, nearly 13% growth for motorcycles. So this is the kind of growth, if that is happening in the OEM segment. Second hand scooters is anyways growing at between 15% and 25% over the last three years. Motorcycle similarly is growing well with good monsoon, I see comfortably over 10% to 12% growth from the replacement segment coming in as well as OE segment overall. On the passenger car side, not maybe as high but I still think that there is more positivity in the growth segment, particularly in the UV segment because of the new launches that are happening from Breza to KUV, BRV, so many new CSUVs, actually the SUV auto segment has grown by nearly 40% in the last year. in this quarter I would say on a year-on-year basis. So that is growing well, passenger car is growing at about 5% - 6%. So net-net if you take passenger and UV together, it would be growing at about 10% or so. So, growth levels in both these categories in my view are quite positive at a market level.

**Jay Kale:** And have they been accelerating say in the last one or two years, the replacement markets specifically or has it been broadly similar and we have been outperforming, but has the market growth accelerated say from 8% to 9% to say 11% - 12% for the replacement market?

**Anant Goenka:** Yes, I think so. So, I would say last year was a very mixed year, you had lots of months where there was flat growth or maybe minor negative and then a few months of positive. So it was kind of half, half divided. This year is a more positive year in general, you see lot more positive

growth months with 10% - 12% kind of growth levels. And this is all market level data that I am sharing, not CEAT data here.

**Moderator:** Thank you. We have the next question from the line of Ashutosh Tiwari from Equirus Securities. Please go ahead.

**Ashutosh Tiwari:** Sir, firstly, we are growing at 30% in both two-wheeler and four-wheeler and I think for a very long time and we probably now have weak base also. So what is driving this growth, I mean is it the expansion of your distribution network or something else, I just wanted to understand that part.

**Anant Goenka:** I think on the two-wheeler space it is clearly, some of it is because of expansion of two-wheeler, we have supported that with increased capacities, investment in brand. So all of it combined, I think new products coming out. So two-wheeler has been really an area of focus which has resulted in good growth, the market has also been supportive particularly this year, scooter market has grown very well. So I would say two-wheeler because of all round initiatives, but I would say particularly distribution has been one area that we have been focusing on. On the four wheeler space, our market share is relatively low even now. So I think the base itself is quite low, there is enough potential for growth. And again, we have been focusing on three or four areas, we have come out with new ranges of tyres, we have been upgrading our product to a certain extent, we have entered a few key OEMs like Renault Nissan, we have been supplying the Kwid which has done extremely well. So, four wheeler side I would say is a little bit of a low base impact. While we have been growing well in the last two three years, I would still say that we still have huge potential on the four wheeler side.

**Ashutosh Tiwari:** Yes, it is true on four wheeler side the base is low, but on two-wheeler side coming back, I mean, in terms of distribution how well we are penetrated as of now and how much scope is there pan-India?

**Anant Goenka:** So, in distribution I would say still a lot of scope because as we grow you can keep penetrating further and further, so we were earlier looking at it at a district level of presence, so out of 600 districts or 620 districts we are now there in over 95% of the districts. But over time we will be going into smaller and smaller population towns, so from district level we will be looking at town level, 25,000 population, 10,000 population, going to the next and next level in terms of our presence. And so therefore I would say the potential still is large in terms of our reach and serviceability.

**Ashutosh Tiwari:** And what would be your mix in terms of OEM replacement in two-wheelers and the market share basically over there?

**Anant Goenka:** Sorry, OEM and replacement market share in two-wheeler?

- Ashutosh Tiwari:** Sir, in the two-wheeler sales for you how much is coming from OEM and how much is coming from replacement? And secondly, how much market share we have in each category?
- Anant Goenka:** Approximately 60% to 65% comes from the replacement segment and about 30% - 35% from OEM and our market share would be somewhere between 27% to 32% approximately.
- Ashutosh Tiwari:** In both the segments or replacement only?
- Anant Goenka:** It is slightly lower on the OEM and higher on the replacement.
- Ashutosh Tiwari:** And sir, any clarity on anti-dumping duty, I mean how do you see the chances of that?
- Anant Goenka:** No idea, so we have pitched to the government but we still are waiting to hear, I think this petition had gone to the government nearly a year and a quarter ago, so it has been a long time. Usually other governments at least come back in maybe three months or they take interim action, but it has been a long time, so we are just waiting and watching out here.
- Ashutosh Tiwari:** And you said that you have taken price increase of 1% to 2% in cars and two-wheelers. Has there any prices change happened which happen in truck segment for you?
- Anant Goenka:** No, in the truck bias segment we have taken a small drop in pricing, maybe by about 1% or 2% or so.
- Ashutosh Tiwari:** And how is the demand for truck tyres specifically right now, how is the market at the industry level?
- Anant Goenka:** I think quarter two was slightly low, but I would say again there is some positivity with respect to demand in the last month, month and a half time. But earlier on in quarter two there was a slight drop in commercial vehicle. But related to passenger cars it is low, but I would still say that in the recent month, month and a half we are seeing some positivity in demand.
- Ashutosh Tiwari:** In truck segment overall?
- Anant Goenka:** Yes.
- Ashutosh Tiwari:** Sir lastly, if you look at the interest cost, I declined on a Q-o-Q basis despite the fact that the debt level is higher for March. So, what is relating to that?
- Manoj Jaiswal:** So, the reason is largely because if you see our debt it is largely towards the CAPEX and project and as and when we are retiring the old debts which was around the capitalize assets, there are some movement of interest that is happening. So it is largely on account of some of those capitalization happening due to new projects versus old projects getting released due to the fresh cash flows, and hence you would see the interest movement accordingly.



- Ashutosh Tiwari:** So, we have around Rs. 735 crores of debt on a standalone basis, so how much of that is still getting capitalized basically?
- Manoj Jaiswal:** So in terms of numbers, around half of it would be effectively capitalized and half of it would be in the P&L.
- Ashutosh Tiwari:** And sir, we also have around Rs. 316 crores of dealer deposit, how much interest we pay over there?
- Manoj Jaiswal:** As per the policy we pay close to 9%, but there various clauses and conditions around it. So a straight answer would not be a clear answer, it depends on few things on which the interest is paid, around 9%.
- Ashutosh Tiwari:** Sir, then this quarter seems very low in terms of interest cost, so how do we see it going ahead over the coming quarters?
- Manoj Jaiswal:** So you would see the similar range as and when we expand, the capacity that is getting ramped up, new loans would come in and new capitalization would happen. If you look at the CWIP, if we split that out you will be able to take the trend. But as and when the loan increases the trend would be similar, I do not think there will be any kind of a significant variation in the trend going forward.
- Moderator:** Thank you. We have the next question from the line of Basudeb Banerjee from Antique Finance. Please go ahead.
- Basudeb Banerjee:** A few questions. One, if I see our overall raw-mat basket in March quarter, around Rs. 196 and broadly it has only come down subsequently in June quarter and broadly flat in September quarter. So in between your rubber moved up all the way from Rs. 100 to Rs. 140 and again Rs. 140 came down to sub-Rs. 120 levels. But overall your raw-mat basket seems to be pretty steady despite all those dynamics. So, can you explain how to look at this down the line? And why there has not been any sharp up-move or down-move in your raw-mat basket?
- Anant Goenka:** Yes, so as I shared earlier what had happened is that around the time of possibly the last quarterly call, what happened is that raw material had shot up quite substantially contrary to our expectation from, and particularly the natural rubber had gone up from about Rs. 110 to Rs. 140 or so. While we had expected it to come down but till about end of May it continued to remain at similar levels because of substantial drought in South India. So this is domestic, ex-Cochin natural rubber price. The block rubber which is largely international rubber had not gone up to that extent and so the gap in pricing between block and sheet rubber was quite high. You can also substitute sheet rubber by using block rubber to a very large extent. So to that extent, international buying helped in making sure that the impact to us was not of to the magnitude of Rs. 110 to Rs. 140 levels, but it was relatively lower levels. In the meantime, once monsoon started to come in, output increased a little bit and as a result even domestic prices started to

come down. And therefore from about August onwards we further saw a slight drop and right now we are in the peak tapping season, so even domestic prices are today at about Rs. 120 per kg or so levels. So that is how natural rubber has moved. We expect natural rubber to continue to remain at current levels going forward. On other raw materials, I would say particularly one area where there has been some increase, because of crude going up earlier in the month of October, etc particularly, we expected synthetic rubber to go up. If there can be a little bit of impact or increased synthetic rubber, but crude has come down in the last week, 10 days time. So, net-net I think there can be some impact on increased synthetic rubber but the drop that has happened on natural rubber will also mitigate the impact. So, net-net I would say there is not expected to be any dramatic impact on raw material going forward. I mean, it can go by Rs. 2 - Rs. 3 here and there but not any major impact.

**Basudeb Banerjee:**

And second thing sir, as you said a few questions back, just wanted to understand that more better. The capacity coming up in highly competitive segment like PV, though you have been growing at a very good pace on a low base of your business, presently at 25% you are growing. So, when capacity is ramping up how should one foresee there is just capacity coming up and in a year's time one should look at the growth so that the capacity reaches full utilization, both in the incremental capacity from Halol or two-wheeler from Nagpur, whereas the industry as you said is barely growing by 10% to 12%.

**Anant Goenka:**

Right, so I would say, first if I were to take Nagpur, despite the increased capacity that has come in from Nagpur, our stock out levels are quite high. I do feel that we will continue to utilize Nagpur as it ramps up and in fact if at all we find a situation where demand is exceeding supply, we will be able to look at increasing our distribution efforts, etc at this point of time because of shortage of supply we are not going very strong on increasing our distribution network to that extent. So, net-net I think we are quite confident about utilization of the two-wheeler space. Also, the new capacity that we have setup is largely skewed towards scooter tyres where there has been a higher growth. So, I feel that our utilization levels will not be a problem. On the OEM side also there are certain OEMs where we have had to limit our supplies to them just because of shortage of capacity. And exports is one area where we have not focused at all, we do very minimal export of two-wheeler. So there are enough markets and opportunities for us to utilize our two-wheeler space. So, I expect, as we ramp up, our utilization levels to continue to remain at 100% level. On the passenger car space we are also seeing a positive situation where supply is short despite us reaching 60% capacity utilization levels. So, in my view demand and supply will go hand in hand and I do not see much of a situation where utilization levels will be low.

**Basudeb Banerjee:**

And sir, why suddenly this export jumping up, it is clearly because of base effect or some new supply markets per say?

**Anant Goenka:**

Mainly because of base effect. We have seen some negative growth in the last two years in exports. So to that extent it is a relatively low base, I would say that while we have grown by

20%, it is still lower than what our original exports used to be maybe two, three years ago. So, net-net I would say that it is largely low base.

**Basudeb Banerjee:** And sir, even now any plans to expand TBR capacity as of now because that is one of, you can say, non-focused area of your business, though bias from industry perspective it is non-focused but everybody is doubling capacity in TBR demand, everybody is running at full. So any focus on that are or down the line you are thinking?

**Anant Goenka:** Not yet. I would say in terms of expanding capacity. But we have just launched our new range of tyres about two months ago, this is by the name of Wind Series of tyres. We are pretty excited about the launch, market is quite positive and accepted the product well. So, let's see how demand for his picks up and we will take a call at a later time. But at this point we are not planning to do any expansion on TBR.

**Basudeb Banerjee:** And sir last thing, I missed out, you said 1% price cut in bias you took, which month sir?

**Anant Goenka:** In October first week or so.

**Moderator:** Thank you. We have the next question from the line of Deep Shah from SBICAP Securities. Please go ahead.

**Deep Shah:** Thanks, my question has been answered. Thank you.

**Moderator:** Thank you. We have the next question from the line of Mayur Milak from Anand Rathi. Please go ahead.

**Mayur Milak:** Just a couple of questions. One, you mentioned that while you have seen almost a 13% increase in volumes and mix of price and product has actually given you a 8% kind of decline. So broadly if I look at your presentation it says your mix is similar, so just trying to understand, is this broadly only majorly towards price decreases?

**Anant Goenka:** Yes, most of it is price decrease, there is nothing else. The only other area is that while our products mix from our product side is improving, our sales in the OEM segment has also grown faster which is slightly lower realization. But I would say 80% to 90% of this is because of price drop.

**Mayur Milak:** And we saw the series of price drop last year, so typically the base effect should continue in Q3 as well I do want to believe, while Q4 should look typically as complete volume growth?

**Anant Goenka:** No. So we took a price drop all the way up till April of this year. So there can be a gap between volume value growth going forward till quarter one also.

- Mayur Milak:** And one thing on your capacity, so you are saying that your Nagpur two-wheeler capacity is typically 2 lakh per month currently, you are running full capacity at this point and you are ramping it up?
- Anant Goenka:** Yes.
- Mayur Milak:** Similarly, Halol is 120 ton is what you target by Q1 and currently it is 69 metric per ton. Now, broadly if I have to, as an analyst there is a serious disconnect between ton and quantity in the entire industry. So it is very difficult to judge, is there some way to measure as to how much ton can be converted into quantity or vice versa on similar lines. So if I have to look at your capacity, one plant is in tons and the other is setup in numbers, so how do I look at the whole thing in total?
- Anant Goenka:** Yes, absolutely. Fair point. So, the reason we spoke about tons between the expansion of the Halol includes some truck radial capacity also. So it is about 10 tons of truck radial that we are doing where the weight of the tyre is about 55 kg per tyre and about 110 tons is passenger car and UVR where the weight of the tyre can again vary between 6 kg - 7 kg to about 10 kg, whereas in the two-wheeler space the weight of a tyre is about 3 kgs. So broadly if you convert the kgs into the product mix that we are looking at, you would get the tonnage. Since in two-wheeler there is a little bit less variation on the weight while motorcycle and scooter is between 2 kg and 3 kg, here since it included some truck radial, we share that in tonnage.
- Mayur Milak:** Alright, this was helpful. And just one last thing on the market share. So, seem to have definitely improved your market share in the two-wheeler space. Now this is despite JK now also announcing coming into this segment. Now what I am trying to understand is, what is your market share in the passenger car segment particularly?
- Anant Goenka:** Yes, our market share in the passenger car segment would be around 8% to 9%, UV would be around 14% - 15%.
- Mayur Milak:** And this includes both the OE and replacement taken together?
- Anant Goenka:** Replacement.
- Moderator:** Thank you. We have the next question from the line of Shyam Sunder Sriram from JM Financials. Please go ahead.
- Shyam Sunder Sriram:** Sir, our RM cost per ton has largely remained steady QoQ. Given that natural rubber supply typically is maximum in November to January period, what is our outlook on the natural rubber prices, will it decline from the current levels or do you expect it to stay at the current levels?
- Anant Goenka:** Again, difficult to hazard a guess. But I would largely say it should be at similar kind of levels.



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**Shyam Sunder Sriram:** Sir I Sri Lanka, our EBITDA margins seemed to have dropped sequentially, any outlook on that space?

**Anant Goenka:** No major dramatic change between quarter one and quarter two, I mean in terms of operations or any specific action that we have taken. Maybe, it could be some amount of drop in exports that have happened which may have had some minor impact. But nothing else has really changed in Sri Lanka.

**Shyam Sunder Sriram:** Any update on our CSTL specialty tyres?

**Anant Goenka:** Yes, the plant is on track. We expect to be ready sometime by end of quarter four, maybe first few tyres rolling out in March - April kind of time. Commercial production possibly in May or so, maybe by quarter one. A few test tyres may come out by end of quarter four.

**Moderator:** Thank you. We have the next question from the line of Amin Pirani from Deutsche Bank. Please go ahead.

**Amin Pirani:** My first question is actually on the volume growth, I might have missed it. What was the volume growth for this quarter?

**Anant Goenka:** 13.2%.

**Amin Pirani:** And secondly, my question was on your two-wheeler and passenger vehicle market share. So you embarked on this strategy almost at the same time around four to five years back and while on the two-wheeler we have seen significant traction, you have added lot of distribution as well, on the PV side it has been relatively slower. So is it just a function of distribution or have there been other factors, is that segment more competitive, is there a product gap, could you help us understand that?

**Anant Goenka:** Yes, so when we embarked on this journey we did not look at the passenger segment, we looked at the UV segment primarily. So on the UV side we have seen growth market share from about 7% to about 14% - 15%. But not to the extent of success we have seen in the two-wheeler segment. Whereas the passenger car segment is something that only now we are beginning to focus on where we hope to look at a similar kind of growth going forward. But I would say focus on passenger car segment to that extent has come about only in the last year or so.

**Amin Pirani:** And again the strategy will be to do a distribution, I mean, is distribution the gap you think?

**Anant Goenka:** So, I would say here it was a mix of capacity because our capacities are fully utilized. I would also say that I agree with you that it is more competitive because we have many more players in this segment. And strategy will be to really look at everything, whether it is brand or whether it is products, everything.

- Moderator:** Thank you. We have the next question from the line of Siddharth Vora from Religare Capital Markets. Please go ahead.
- Siddharth Vora:** Anant, just one question regarding the recently announced GST rates, if you think tyres will be slotted between 18% or 28%, what will be your view, how it will impact things?
- Anant Goenka:** We are hoping 18% but we do not know what will happen.
- Manoj Jaiswal:** No, we are still waiting for the schedule to come to understand what rate it would be. Because there is an industrial product which is slated at 18% and there is cars that is slated at 28%, so we are trying to debate. But at this moment we do not know exactly how it will be. But if you look at effective tax to the end consumer today, it will be in the range of, depending on GST in various states, it would be in the range of 25% to 27% - 28%. So to that extent it will vary from consumer segment to consumer segment.
- Siddharth Vora:** Correct, but still at 28% you will be comfortable enough as well?
- Manoj Jaiswal:** We will like it to be 18% or 12%.
- Siddharth Vora:** In terms of our ad spends which are down this quarter, do we expect them to pickup in Q3 - Q4, or what are our plans ahead?
- Anant Goenka:** There can be a slight increase in Q3 from quarter two, but largely no major change. I would say that on an overall basis maybe a 20% growth on a year-on-year basis. So on average for the year I would say you can take a 20% growth from FY16 to FY17.
- Siddharth Vora:** And initially you said that price increases you have taken at around 1% to 2%, was that currently that will be for Q3 or you meant at Q2?
- Anant Goenka:** We took at it in the latter half of Q2, mostly between say August to October period.
- Siddharth Vora:** And if I am not wrong, you had taken a 1% to 2% price hike in the Q1 as well around April - May?
- Anant Goenka:** April - May we did not take, I think maybe early June we took a small price increase. But I would say, yes, maybe about 1% or 1.5%.
- Siddharth Vora:** Both the quarters you have had 1.5% kind of a price hike?
- Anant Goenka:** Yes. But I would say net-net, taking everything into account it would not be more than 2%. So it is not 1.5% plus 1.5%, it would have been 2% in say two-wheeler earlier on and then 2% in PCR or so.

- Siddharth Vora:** And only a price cut in bias which was taken in October?
- Anant Goenka:** Yes.
- Siddharth Vora:** And Anant, as you mentioned, there is a strategic play between domestic and international rubber prices over the way you can use block rubber or sheet rubber. Can you just say what is the maximum split, how you can play around, so 50:50 or 60:40?
- Anant Goenka:** Yes, you can use a large component of block rubber, so it depends. So certain companies can nearly substitute or use a very large share of shift. So it really depends on the price gap and difference. Also, what happens is when you look at international buying, internationally buying there is a lag of about three months whereas domestically you can get it in a shorter period of time, maybe 20 days to a month's time. So there is a little bit of forecasting also that comes into play. So it has a large gap say of Rs. 15 per kg between domestic and international, you may take a call that will domestic come down to that extent going forward to match international. So there is a little bit of smart buying that has to be done based on this, but largely a large part can be substituted between the two.
- Siddharth Vora:** So, currently in terms of our natural rubber requirement it will be 50:50 but in domestic and international?
- Anant Goenka:** Again, you can do 80% domestic 20% international or you can do even as much as 60% - 65% international and 30% domestic. So as I said, the fungibility is quite high between the two.
- Siddharth Vora:** And going forward, in terms of our interest cost as well we expect it to be at current levels or slightly higher, that will be fair enough as a view, correct?
- Manoj Jaiswal:** Yes, it will be in the current level but there will be some incremental loan that would come in as and when the project is coming up, very marginal, and to that extent there will be shift but it will not be significant change from where it is.
- Moderator:** Thank you. We have the next question from the line of Sudipto Saha from Crisil Research. Please go ahead.
- Sudipto Saha:** So, I have two questions. The first one is regarding commercial vehicle segment. I understand that CV segment business has been challenging, please request to understand how has been Q2 volume growth YoY and how has been H1 volume growth YoY?
- Anant Goenka:** So, Q2 has at least for domestic segment largely some amount of negative growth between, OE has shown at least on a quarter two basis a slower growth on a year-on-year basis, replacement has been a little bit flattish. So, net-net about between 0% to negative 5% kind of growth on the commercial vehicle side.

**Sudipto Saha:** And my second question is on utilization level. I want to understand what is your current capacity utilization level for TRB and PCR segment?

**Anant Goenka:** So, PCR would be fully utilized. On the truck radial space, about 85% or so.

**Sudipto Saha:** And for bias segment, truck and bus bias?

**Anant Goenka:** Truck and bus bias maybe about 80%- 85%.

**Moderator:** Thank you. We have the next question from the line of Bharat Gyanani from Sharekhan Ltd. Please go ahead.

**Bharat Gyanani:** Just wanted to understand, I mean, just to get a sense in the tyre industry what would be the share of unorganized players, if any? And the potential impact of GST once the rates get finalized. So just wanted to get a sense of understanding of how the unorganized players are there in tyre industry?

**Anant Goenka:** Unorganized players it would be a very small share, I would not even know the number but it would be less than 3% to 5% for sure. By unorganized I am talking about unknown Indian domestic players, say unbranded players or things like that. But tyres is a high CAPEX industry, so to setup a plant you need to put in a minimum of Rs. 200 crores - Rs. 300 crores kind of thing. So it is difficult for an unorganized player to come into this. Therefore, maybe even less than 2% - 3%. Whereas Chinese players are of course a very large share. So while they are technically organized but it is coming in on an ad-hoc basis through dealers and distributors and so on.

GST, I would say that overall there will be a positive impact. One is the larger impact that we will see with respect to transportation in this range, trucks moving hopefully more freely, less waiting in toll nakas, etc. to that extent efficiency of trucks, utilization should go up. With respect to financial impact to CEAT, it should be also overall positive. We pay an octroi component on the raw material coming in through our older plants, that will hopefully we know will get absorbed, so to that extent that octroi saving will be there. And then there are some input tax credits that we are not able to avail in the current environment which we will be able to. So net-net financially we expect a positive impact. The rate itself, whether it will be inflationary or deflationary with respect to the rates carved out, depends on whether it is going to be 28% or 18% what will come in we do not know yet.

**Bharat Gyanani:** And sir, also I have one query on the share. While the share of Chinese players in the CV market, especially in the replacement now stands at about 30% to 35% or so, but what is the share of Chinese players in the passenger space, I mean, if you have some idea on passenger vehicle and two-wheelers both?





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- Anant Goenka:** Yes, approximately somewhere between 15% and 20%, a little bit less, maybe about 15% and 18% in the passenger car space. This is just a very broad level, gut level data that I am sharing, it may be off by 5% or so. The other is on two-wheeler, maybe even a little less.
- Moderator:** Thank you. We have the next question from the line of Mahesh Bendre from Way2Wealth Securities. Please go ahead.
- Mahesh Bendre:** Sir, last two quarters we have reported a double-digit volume growth, given the new capacities that are going to ramp up over next few quarters do we think we will be able to maintain this double-digit volume growth over next three to four quarters?
- Anant Goenka:** Yes, we are quite hopeful about that. So capacities, as I said again, in the two-wheeler space we are only at about 2 lakh out of 11 lakh tyre capacity, so there is still a long way to go. And here also in the passenger car space also we are at about only 60% ramped up. So there is still some way to go which will all come into effect in the next one year's time, so we are quite confident of double-digit growth in at least next two, three quarters.
- Mahesh Bendre:** And sir, in terms of margins. Last nine quarters our operating margins have been quite stable, they are in double-digit. So do you think this will be sustainable margins going forward?
- Anant Goenka:** That is where our efforts are on towards, making sure they are sustainable and they go up. So really it is all about, I mean, one is we need to see how raw material move, second is that we are continuously moving our product mix towards the passenger segment. So these are the two factors that will play in margins but we are hopeful that margins will continue to remain at at least current levels.
- Moderator:** Thank you. We have the next question from the line of Romil Jain from Quantum Advisors. Please go ahead.
- Romil Jain:** Sir, just one question, the growth that we have seen in the personal mobility segment, two-wheeler, PV, UV, just wanted to understand that is there more of undersupply and hence more of demand or we are gaining more market share from maybe organized players as unorganized very small?
- Anant Goenka:** So I think demand as I said is picking up by about 10% whereas we are growing at possibly around over 30% type of growth. So we are getting market share somewhere.
- Romil Jain:** So more would be coming from market share gains from already existing players I would assume, right?
- Anant Goenka:** Yes.

- Romil Jain:** The other question is, just wanted a breakup of your CV sales between bias and radial, how much that would be? And in terms of capacity also, in CV how much would be bias and radial?
- Anant Goenka:** So, breakup between bias in radial in CV space would be about 75% bias and 25% radial.
- Romil Jain:** This is capacity, right?
- Anant Goenka:** No, sales. Capacity also will not be very different because utilization levels are not very different, maybe a little bit, I would say largely over time it will only grow in the radial space because I do not expect bias growth to be higher at least in the longer term.
- Romil Jain:** So just wanted to understand that whatever bias capacity we have, would it be fungible to a radial capacity or it is a larger proportion of your entire CV capacity so what are we going to do with it?
- Anant Goenka:** So bias is not fungible to radial, we can move some into some other types of bias tyres only. So there can be some shifts, but if at all, there will be very small shifts in comparison to the entire capacity. For example, if we have a capacity of say 400 tons per day or 350 tons per day, we can move maybe about 10 tons or so here and there, not much more than that. So rest of it will show negative growth going forward.
- Romil Jain:** And just one more last question, going forward since on a totality basis we are getting about 64% - 65% sales from the replacement segment, so OEM has shown definitely a good growth so going forward in next two years do we see the replacement growing further from here from the 64% - 65%?
- Anant Goenka:** No, I do not think so. So, I think that over time this current ratio could continue or OEM could grow a little bit higher also going forward.
- Romil Jain:** So this is as our strategy to grow more on the OEM side?
- Anant Goenka:** No, generally the mix in the passenger segment is about 45:55%, 50:50 at an industry level. So we are a little bit more skewed towards the replacement sales segment. So what I am saying is that I do not see much more growth in replacement as a mix happening, while overall both will grow. But I would say that this is a mix we are happy with and we will try and maintain this.
- Romil Jain:** And FY16, our total rubber basket import would be how much and domestic would be how much, let's say FY16 or maybe first half of this year?
- Anant Goenka:** Very much keeps varying, so certain markets it is a very different from month-to-month.
- Romil Jain:** So it depends in terms of pricing, where we are getting cheaper pricing or something like that?

- Anant Goenka:** Yes.
- Moderator:** Thank you. We have the next question from the line of Chirag Shah from Edelweiss. Please go ahead.
- Chirag Shah:** Just a clarification, first is, 30% volume growth is in tonnage I presume?
- Anant Goenka:** Yes.
- Chirag Shah:** Second, I was just going through your distribution network data and I see that in H1 there is a slowdown in the addition of network, so how are we looking at it, have we reached most of the places or as you highlight more of capacity? Then what is the ideal number over next three years that you would like to present?
- Anant Goenka:** Yes, so the data that we shared was on our district level reach. So our district level means India has some 620 districts, now we have reached some 615 districts or something, a large number of districts. Now, beyond that you cannot grow beyond the number of districts, so therefore you have to go to the next level of looking at present. So what we will do is we look at data of town for example, now a district will have certain population, so if you go to the next level, population town and there we will be looking at larger levels of growth. So, for example 25,000 population town as I said earlier in the call, we will look at increasing our presence towards saying that let's look at 90% penetration in 25,000 population. Once you reach that, we will be looking at possibly a smaller population. So that is how we will be looking at increasing our distribution.
- Chirag Shah:** Sir, on an average would it be fair to assume a 10% increase in reach is what can happen?
- Anant Goenka:** No, I think there can be much more. Difficult to measure as a percentage I would say, but I would say there is a huge potential for further distribution. Because if you look at it at a village level, what India has 6 lakh villages or something, maybe our penetration in villages maybe just at about 1 lakh villages, I do not know the number but I am just saying at a hypothetical level it maybe at about 1 lakh. So that kind of potential is very high.
- Chirag Shah:** Because ideally the question that keeps on coming is this 30% growth that we are seeing, how much of that is distribution lead and how much is sustainable growth. I think that that is where the question I presume all of us are trying to understand, that is why this question I asked.
- Anant Goenka:** Yes, I think I would just suggest that you can look at it from a market share perspective. So what kind of market share, how do you see the market growing and what kind of market share do you see us looking at being able to reach. And to that extent that is where I would say that growth will possibly slowdown based on that achievable market share, but I leave it to you how you do your analysis.



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- Chirag Shah:** And what would be your aspirational market share in passenger car segment, combined UVs plus cars combined, its 14% - 15% or you would be looking to set a higher number?
- Anant Goenka:** So we do not look at it at a combined level. So we would look at it certainly we would like to be amongst the leading players in this category, but we do not have, I mean it is difficult to combine market share at a passenger level, all combined there is a certain market share.
- Chirag Shah:** So the focus is on UV market share separately and passenger car market share separately, that is the correct way of understanding?
- Anant Goenka:** Yes, cars, scooters, motorcycle, each of them would be different.
- Chirag Shah:** And second is on this distribution network, this 4,500 dealers. So again, that number may not necessarily increase, there would be sub-dealers and sub-franchisees that could go up, right?
- Anant Goenka:** Yes.
- Chirag Shah:** Which you may not be actually sharing across also in terms of your presentation details?
- Anant Goenka:** Yes.
- Chirag Shah:** So the 4500 dealer number is not the right number to focus on in terms of how your distribution is going up, is that right understanding, correct?
- Anant Goenka:** Yes. In fact mechanics, small mechanics, etc that have it. So we may not have all of that data as well, these are certain number of dealers that we directly service.
- Chirag Shah:** And this number is not likely to go significantly, 4,500-odd number that we have?
- Anant Goenka:** No, it will not.
- Chirag Shah:** And just one out of curiosity question, I have seen this British Safety Council Award, now why do we need to have an award from British Council Safety, so it is from what perspective we have it?
- Goenka:** Yes. So it is largely from the perspective of making sure our own plants follow a high level of environment, health safety standards. So, it is primarily a sign of manufacturing excellence and focus on safety within our plants. While we try and make roads safer and make our products safer, we have to be safe at home and practice it where we work. So making sure that our workers in the plant, our associates are all safe, we have to be at a certain level. So therefore the level of safety practices that we have are very high and therefore the British Safety Council decided to recognize this effort. So that is the only thing that is there.



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- Chirag Shah:** It is not a prerequisite for export markets, there is nothing of that sort, its voluntary?
- Anant Goenka:** No, that is right.
- Chirag Shah:** And last question on off highway tyres, you indicated that we would be ready from Q1 of next financial year, how do you think the ramp up of this business will be because it is a new segment in a sense you are entering. So if you can help us understand how much time, how different is the customer acquisition or the distribution model over there versus the normal export business that you have?
- Anant Goenka:** So, we have just setup a very small capacity, initially of 40 tons per day. This over time we will take it up to at least 100 tons per day for the second phase of expansion that will be there. So I say quite confident of utilizing this capacity in a short period. We already have a distribution network in place where we are selling off-highway bias tyres, so we have relationships with customers in Europe, in the US and so we are selling those. We just need to increase the range to radial which will come in from this new plant that is there.
- Moderator:** Thank you. That was our last question, I now hand the conference over to the management for their closing comments. Over to you.
- Anant Goenka:** Thank you very much for your time and your interest in CEAT. We look forward to staying in touch. Do let us know if there are any questions that we may have missed out on and we will catch up again next quarter same time.
- Moderator:** Thank you. On behalf of ICICI Securities, that concludes this conference. Thank you for joining us and you may now disconnect your lines.