Earnings Conference Call

Q2 FY2018

December 19, 2017

Management:

Mr. Akshay S Pitti – Vice Chairman and Managing Director

Mr. N R Ganti, Director

Mr. N. K. Khandelwal, President (Corporate Resources) and CFO

Moderator: Ladies and gentlemen, good day and welcome to Pitti Laminations Q2 FY2018 Earnings Conference Call. 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. Please note that this conference is being recorded. Joining us today on this call are Mr. Akshay S. Pitti – Vice Chairman and Managing Director; Mr. N. R. Ganti – Director and Mr. N. K. Khandelwal – President (Corporate Resources) and Chief Financial Officer.

Before we begin, I would like to mention that some of the statements made in today's call maybe forward looking in nature and may involve risk and uncertainties. For the list of such considerations, please refer to earnings presentation. I would now like to hand the conference over to Mr. Ganti. Thank you and over to you sir.

N. R. Ganti: Thank you. I would like to start by providing an overview of the prevailing macroeconomic condition followed by financial and operational performance during the recently concluded quarter including key highlights of our strategic and operational initiative. Index of industrial production growth slowed in September to 3.8% from a 9 month high in August. The impact of GST and unfavorable base effect resulted in a marginal contraction in IIP. Despite this, mining output increased by 7.9%, electricity generation by 3.4%, while manufacturing sector increased by 3.4% in September 2017. Even from a global perspective, growth sentiment remains positive. Global economic growth is projected to grow at 3.6% in 2017 and 3.7% in 2018. Going forward, marginal recovery in manufacturing output, strong consumer demand and implementation of structural changes particularly in India will reflect in the growth momentum over the medium to long term.

Moving to our performance for the quarter, total volume remained almost flat year-on-year at 4,540 metric tonnes, domestic volume for the quarter was 3,616 metric tonnes, decline of 8.5% year-on-year, while export volume surged by 48.8% to 924 metric tonnes compared to the same period last year. Decline in domestic volume is mainly driven by shipment delay on account of limited clarity on GST during the first 15 days of July 2017. Stator frame demand increased more than twice to 250 units in Q2 FY2018 compared to 110 units in Q2 FY2017.

Net revenue from operations for the quarter increased by 25.8% year-on-year to Rs. 84 crores. Growth was supported by price realization due to better product mix and raw material inflation. In terms of sales mix, domestic sales accounted for 73% of the total sales and remaining 27% was contributed by exports. Domestic sales for the quarter improved by 38.2% year-on-year to Rs. 60.6 crores. Export sales for the quarter was Rs. 22.7 crores, an increase of 2.8% compared to the same period last year. The other operating income accounted for Rs. 0.6 crores. Our EBITDA for the quarter increased to Rs. 12.3 crores, up by 53.1% on a year-on-year basis. This increase was driven by better operating efficiencies and favorable product mix. EBITDA margin for the quarter was 14.7%.

Hiring for new plant 4 coupled with annual increments increased our employee cost by 27.5% year-on-year. However, the revenue ramp up for the plant 4 shall happen progressively. Profit after tax was Rs. 3.3 crores, an increase of 238.8% from the same period last year, with the PAT margin of 4%.

Further, taking into consideration the overall business dynamics, we remain comfortable with our current leverage profile. As of 30th September 2017, our total debt was Rs. 198.9 crores which included Rs. 68.1 crores of long term debt and Rs. 130.8 crores of short term debt. Cash and cash equivalents for the quarter was Rs. 18.2 crores resulting in a net debt position of Rs. 180.7 crores. The net worth of the company was Rs. 118.8 crores at the end of the quarter. As of September 30th 2017, we had a conservative leverage profile with total debt to equity ratio of 1.25 times. Total debt to equity ratio is adjusted for quasi equity, that is loan from promoters of Rs. 40.3 crores has been considered to be quasi equity. Based on projection, the long term debt shall be around Rs. 30-35 crores within next two years.

Our strategic initiatives of shifting Pune facility to Aurangabad is in completion stage. We have completed trial production and operations are expected to begin soon. The plant will have machining and laminations capabilities. At plant 4 Hyderabad, we have started commercial production in the month of August 2017 and it is expected to pick up momentum in H2 FY2018. This facility will be utilized mainly for machining activities. Furthermore, as mentioned earlier, we have started commercial production for GE India as part of Indian Railways project end of last year and it has gained momentum during H1 FY2018. It is expected to contribute meaningfully during this year. Also, we are pleased to announce that we are in the advanced stages of smaller laminations order for Crompton Greaves. Our sample has been approved and commercial production will start as soon as the Aurangabad plant is operational. Overall, it has been highly encouraging to see the company's performance during the recently concluded quarter. Given Pitti Laminations has steered all the turbulences behind it, this has further enhanced our brand equity and reinforced our market position globally. Presently, the company has a robust order book and a good visibility of order for next 4 to 6 quarters.

As stated earlier, we are more focused on machining and value-added business. Our product already goes into heavy electric vehicles and we are working on the lighter version. This is a high potential market for unleashing further growth in long term.

We would now like to open the floor now for an interactive question and answer session. Thank you.

Moderator: Thank you very much. Ladies and gentlemen, we will now begin the question and answer session. The first question is from the line of Giriraj Daga from KM Visaria Family Trust. Please go ahead.

Giriraj Daga: Couple of questions and clarifications. First, what was the GE revenue during the second quarter? How much we have recorded?

Akshay S. Pitti: We normally do not share customer wise revenues.

Giriraj Daga: In the last quarter we gave Rs. 13 crores in the first quarter.

Akshay S. Pitti: That was exports mostly.

Giriraj Daga: Rs. 13 crores of GE exports or I believe that was the total number?

Akshay S. Pitti: Total GE revenue was Rs. 25 crores. Rs. 22 out of which was exports and Rs. 3 crores was domestic.

Giriraj Daga: This Rs. 25 crores is the first half or second quarter number?

Akshay S. Pitti: Second quarter.

Giriraj Daga: Okay. My next question is related to, if I look at the domestic realization, obviously it is going up quarter-on-quarter. I understand that was the GE business coming in which is a high price better mix product business. So, that is likely to sustain from here. My question is that, last quarter if you say that we did about Rs. 13 crores from that Rs. 50 crores of business, so ideally now we should be stabilizing on this realization for the domestic market. So is that the right number and current realization should be sustainable or were there any one-offs in the second quarter, we should go back to first quarter?

Akshay S. Pitti: You mean per tonne realization?

Giriraj Daga: Per tonne realization, which I understand year-on-year it is driven by the GE also, primarily GE business, or you look at the Q-o-Q also it is about 3-4% higher from 1,62,000 to 1,68,000.

Akshay S. Pitti: Correct. We will keep improving on two counts. One because the GE India loco order that we had bagged two years back is now coming into production for the concurrent supplies. So as the quantity keeps increasing for the domestic GE business, which is currently pegged at Rs. 3 crores for the last quarter, this will increase to Rs. 50 crores per year. So as this will increase, your per tonne realization will improve for the domestic business. But certain chunk of the domestic realizations increased in current quarter is attributed to raw material price increases.

Giriraj Daga: And export realization if I see, there is very sharp drop. Year-on-year though it is a big 32% drop, on the quarter-on-quarter it is a 15% drop while the volume is same. So has the product mix deteriorated to that extent or what will explain this?

Akshay S. Pitti: It is a level of value add. Earlier we used to supply more of the core dropped stator frame type of business to the export market, that is now going to be domestic end of GE. So the Rs. 3 crores that we have done for GE domestic, it is the same product. So our business terms at GE is ex-works**.** So whatever they want they can either take to their domestic facility or to the export facility. So it is a pure incidence of them taking more of the value-added product for the domestic unit rather than their US and Mexico units.

Giriraj Daga: But the realization drop is very sharp, actually it appears that. Rs. 246 compared to Rs. 289 in the Q-o-Q and last year it was Rs. 354.

NK Khandelwal: The lamination supplied is more than the stator frame. As Mr. Akshay said, it is the value-added product versus the plain lamination supplies. So in particular quarter when the lamination supplies are more and value-added product will be less, the average realization will be skewed to lower per ton realization and if in a particular quarter, when the stator frame or value-added product business is more and lamination business is less, that time it will show a higher average realization.

Giriraj Daga: Understood. You are maintaining the guidance of FY2018, 18,000 domestic and 4,000 export, tonnage wise?

Akshay S. Pitti: Yes, currently confident of maintaining that number.

Giriraj Daga: Okay, and last thing in that, like you mentioned about the Aurangabad facility starting revenue and you also mentioned about the Crompton order. So if you can just throw more light on the timing of when they will be start showing in the revenue and what will be the peak revenue from this facility?

Akshay S. Pitti: See, Aurangabad facility is basically consolidation of multiple facilities that we had. We had a Pune facility which we have shut down. We have two facilities in Hyderabad, one of which we have shut down. So that is what is moving to Aurangabad. So in terms of peak revenue that is realizable by Aurangabad plant, it is going to be the overall revenues of the company which was earlier plus some incremental revenues because of capacity enhancement. So it is not like if we say Aurangabad revenue, you can realize the peak revenue of Rs. 400 crores, that is going to be an addition to our historical performance. Half of the historical performance is already part of the Aurangabad facility. That is one part of it. Aurangabad facility will probably go into commercial production first week of January. It is fully ready, we are waiting for the last regulatory approvals from the pollution control board, it is just a formality that we have to wait for. Sample production has been started and successfully tried out. Commercial shipments would probably start from first week of January. As far as the Crompton order that Mr. Ganti was talking about, this the foray from the company into the small laminations market basically appliances for ceiling fans, table fans, coolers, ACs, so on and so forth. So we have just started with Crompton with their ceiling fan business and we hope to expand this with other clients in various appliances businesses. As a potential revenue, I think for the first year we are conservatively estimating it to be about 1,200 tonnes for the year, valued at about Rs. 10 crores and then let us see how it goes from there. Once we are more confident of doing the smaller lamination in bulk production, we will probably expand that business further.

Moderator: Thank you. We have the next question from the line of Kaustav Bubna from SKS Capital and Research. Please go ahead.

Kaustav Bubna: So on this Crompton Greaves deal that we have, foray into the white good segment, just wanted to understand, who is supplying these small laminations to them before because they obviously needed this before, not like they suddenly need this. So what competition are we dealing with and what is our capacity in this segment compared to the total market size. So I am trying to understand that can our current supply meet whatever demand that we are rejecting and then how much in the future, what are the plans in this and how much we are aiming to increase capacity and whatever?

Akshay S. Pitti: So firstly on the incumbent suppliers to Crompton Greaves fan division, as you know Crompton has separated their consumer goods business and the industrial business and sold the consumer business off. So earlier Crompton used to have the in-house facility to make these laminations which has stayed with Crompton industrial and not moved to Crompton consumers. So now they want to start a completely different supply chain which is independent of the erstwhile Crompton. So we would be replacing Crompton's in-house capacity.

Kaustav Bubna: This is for consumer?

Akshay S. Pitti: Yes. Consumer never had in-house capacity. The industrial unit which is based out of Ahmednagar used to have the lamination facility which used to make the laminations of Crompton consumer. So now when the consumer division is sold off, they want to start an independent supply chain of Crompton. So that is where we are coming into the picture.

Kaustav Bubna: And you have also spoken about taking to Havells about a similar type of deals, so who do they currently get this lamination from and how do we plan to encroach on Havells in the future**?**

Akshay S. Pitti: We have not spoken about Havells. We are saying that once we move into Crompton then we will have a wide market open because Havells may expand, so does Bajaj, so does Yash Fans, Usha Fans and the basic design of the component is similar. So once we have this expertise, for us the possibilities are limitless in the white good sector.

Kaustav Bubna: What is the total addressable market for us?

Akshay S. Pitti: The white goods market will be more than 150,000 tonnes per annum.

Kaustav Bubna: Okay. And who is currently supplying to these people, like Yash Fans, Havells, Bajaj?

Akshay S. Pitti: See, quite of bit of it is imported from China, Singapore, Thailand. Quite a lot used to be done in-house with ancient technologies which are now being moved out to a proper and professional supply chain rather than try to do everything in-house. So it would be a combination of replacing in-house capacities and import substitution.

Kaustav Bubna: Are we the only organized player to do this in India?

Akshay S. Pitti: No, I wouldn't say that we are the only organized player to do this in India. There are smaller lamination manufacturers than us, who are trying to get into this who are in the organized space.

Kaustav Bubna: Okay. So on the debt side, your long term debt is doubled, just want to understand what is this debt taken for, is this for the Capex only or what is this increase in long term debt for and what is the long term debt reduction guidance?

Akshay S. Pitti: I think the long term debt has peaked as of now. I mean, this quarter would be I think the peak of our long term debts since all our Capex just concluded and year-on-year I think our total long term debt would reduce by FY2020. We estimate it to be about between Rs. 30 -35 crores by FY2020.

Kaustav Bubna: And is it all Indian debt or is there any foreign debt too?

Akshay S. Pitti: I mean, mix of both.

Kaustav Bubna: So what is your total interest rate, interest cost. Your interest rate on your total debt?

Akshay S. Pitti: It will be about 8% on an average.

Kaustav Bubna: Okay. And so you managed to deliver 4% net profit margins, just trying to understand what is the extent of this margin, I mean since GE orders have still not started picking up and eventually if we do get Alstom order, then the realization will be higher in that segment plus moving into the Aurangabad plant etc. can all improve our margins. So by FY2020, where could we see, any indication on net profit margins or margins in general EBITDA?

Akshay S. Pitti: At EBITDA level, I would estimate us to reach somewhere around 16-16.5% by FY2020.

Kaustav Bubna: Okay. And since your long term debt will be reducing, your finance cost will also reduce, I mean how do we see our net profit margins, any guidance or any indications?

Akshay S. Pitti: I think I will prefer, I am more comfortable giving a guidance on EBITDA level because when you talk of the net level, then the depreciation will kick-in. I sitting here, off hand I cannot say how the depreciation will be in 2020. I mean, it is simple financial math, but sitting here I don't want to try and catch that.

Kaustav Bubna: But could we say above 5%?

Akshay S. Pitti: Definitely it would be above 5%, but where it would be, I cannot tell you, right now. Probably next call I will come more prepared for this question.

Kaustav Bubna: And on the Alstom deal, have we got any further?

Akshay S. Pitti: We are in discussion with them. For couple of parts we are in final stages of negotiation, for the rest, it will still take some time.

Kaustav Bubna: Well, this would be a smaller deal than GE, but same timeline or will it be a smaller timeline also?

Akshay S. Pitti: Timeline is slightly extended. GE is moving very fast on this and Alstom is going to probably import the first 200-300 locomotives from their European facilities and then start manufacturing in India.

Kaustav Bubna: No, what I mean is the timeline of the deal. So we have a 10 year deal with GE, right?

Akshay S. Pitti: Yes, so the timeline of the deal would be similar, but for us the shipment could start probably 3 years later than GE because in the initial part of the order, Alstom will service it from the European facility. It is not very clear yet from their side.

Kaustav Bubna: Okay, fine. But they are leaning to our side, right because even they have a structural change, they are not shutting off their internal production.

Akshay S. Pitti: So they are definitely leaning towards us.

Moderator: Thank you. We have the next question from the line of Shashank Kanodia from ICICI Securities. Please go ahead.

Shashank Kanodia: So sir, Akshay sir, just wanted to get a flavor, but how is the export demand because we have been hearing there is some clamp down by GE global because of slowdown in the global locomotive space. So how is the demand traction in the export front from GE?

Akshay S. Pitti: GE for us is not just locomotive. It has a multitude of products including mining, off highway vehicles, marine, oil and gas exploration, so it is a combination of products and end markets for us. In the locomotive space, we are definitely seeing a contraction, especially for the North American Railways. But on the global electrical diesel locomotive front, we see GE barring quite a few orders in various parts of the world including Egypt, South Africa, India, so for us the going is still good, as far as the locomotive business goes.

Shashank Kanodia: Okay. So right now we are clocking a run rate of around 1,000 tonnes per quarter. So we expect the same run rate for the rest of the year?

Akshay S. Pitti: Yes, we had estimated about 4,000 tonnes for this year for exports. So we are kind of holding that guidance.

Shashank Kanodia: Okay. So what about next year?

Akshay S. Pitti: Next year, we see it improving slightly maybe to 5,000 to 6,000 tonnes. That would be the exports. See, I want to make a correction here. Earlier when we used to talk of GE, we used to talk of exports. When we say GE today, we talk of GE in the world, including India. Earlier GE didn't have a facility in India, now they have. So for us, realizations are same whether it is export or domestic.

Shashank Kanodia: Right. Sir domestically we will be supplying to GE India which is basically for diesel locomotives, right?

Akshay S. Pitti: Not only diesel locomotive, we supply components to them for their windmills, we supply components for them for oil and gas, stationary power, various things.

Shashank Kanodia: So domestically how is the demand scenario for our product profile and what is the volumes that you were targeting for this year and next year?

Akshay S. Pitti: With respect to GE or with respect to all customers**Shashank Kanodia**: All domestic market in total.

Akshay S. Pitti: See, domestic market, we are very bullish. If you see our projection, we have given about 18,000 tonnes of laminations we are targeting for the current year which is about 2,000 tonnes more than previous year.

Shashank Kanodia: So which means we would be doing something like 5,000 tonnes for the rest of the two quarters each?

Akshay S. Pitti: Yes. It may be slightly lower because we have some disruption of shifting our facility from Pune to Aurangabad. So that will cause a little bit of disruption in our sales which we will make up in Q4.

Shashank Kanodia: So which segments are you seeing demand traction domestically?

Akshay S. Pitti: I think all segments. Across all segments, including power generation. Wind power is slightly down as of now. But apart from that, I think every other segment we are seeing good growth.

Shashank Kanodia: Secondly sir on the margin preference, so we have kind of very sharply improved margin trajectories. So we are now at 14.5-15% odd, so what is the sustainable range that you see, going forward that we can safely assume?

Akshay S. Pitti: You are talking about EBITDA margin, right?

Shashank Kanodia: Yes.

Akshay S. Pitti: So Q1, we are about 13% and this quarter we are about similar 13-14%. So I think we see this margin profile continuing and like I mentioned by 2020, we see about 16-16.5% EBITDA margin possible given the change in product portfolio and the overall increase in business volumes.

Shashank Kanodia: We have never clocked something like 16% ever in our history, right, given that we have been supplying stator frame in the past as well, that too in highly lucrative export markets. So what gives us confidence that we can drive such high margins?

Akshay S. Pitti: See, it is not just stator frames or product profile. It is also the sheer volume. So this year we are targeting Rs. 380 crores of turnover. Our all time high turnover is Rs. 420 crores, at which time we had about 14.5% EBITDA and by 2020 we see ourselves going past Rs. 420 crores obviously to somewhere around Rs. 600 crores revenue. So the higher operating leverage will give us higher EBITDA.

Shashank Kanodia: True. So sir, what kind of volumes are we targeting for FY2019, in the domestic market?

Akshay S. Pitti: FY2019 is still some time away for us to finalize our budgets. We can discuss that probably in Q4.

Shashank Kanodia: Okay. And sir, any flavor on the order book as of now?

Akshay S. Pitti: No, I think the order book like Mr. Ganti said, remains strong. We see the GE order continuing to give us some additional revenues in this year and probably the full revenues from next year as originally planned. Apart from that, all other sectors are growing, we just hope that the wind power sector kind of comes back and gives us additional boost this year.

Shashank Kanodia: Okay. And sir for the GST front, so our product profile gets classified under 18% tax rate or is it something different?

Akshay S. Pitti: It is 18% tax rate. Some of the products which go to windmill earlier used to be exempt, now they are under the 18% tax rate as well.

Shashank Kanodia: Okay. And previously we used to pay roughly the same rate, right, excise duty plus VAT?

Akshay S. Pitti: Excise duty plus VAT used to work out to roughly the same and excise duty plus CST would work out something little lesser than that. But now when the taxes are fully modvatable, so it is an added advantage for the customers and the disadvantage that we used to have being in Hyderabad for our domestic market has kind of disappeared because the CST would now be modvatable.

Shashank Kanodia: True. Sir in this quarter have we increased the investment in Pitti Castings because your investments shows around Rs.1.5 crores of increasing investment. So is it largely because on account of Pitti Castings or something else?

Akshay S. Pitti: Revaluation only, it is as per IndAS.

Moderator: Thank you. We have the next question from the line of Ketan Karane from Global Advisory Research. Please go ahead.

Ketan Karane: I have a set of few questions. How are we looking at the volume growth in Q4, as Akshay just mentioned that there will be disruption in sales because of transfer from Hyderabad to Aurangabad. So what are the volume we are looking consolidated, I don't want export, just volume wise what are we looking at in Q3 and Q4?

Akshay S. Pitti: In Q3, I think we will lose about 20% kind of a number because we are shifting from Pune and Hyderabad. So we will lose 15 days of production from each of the facilities. So we are trying to minimize that, we still have couple of days left in this quarter. We are trying to make that number up, but unfortunately I see it to be slightly down maybe as much as 15% in top line terms.

Ketan Karane: So it is volume I am talking and not revenue? Am I correct?

Akshay S. Pitti: I am talking of both. It is interlinked.

Ketan Karane: The 3,825 tonnage we will be doing.

Akshay S. Pitti: Something like that.

Ketan Karane: But in Q4, what are we looking at. You told that we will make up in Q4, so?

Akshay S. Pitti: Q4 we should be definitely making up in terms of topline. Because see stator frame orders will be significant and we will be trying to push them out in Q4. In terms of tonnage, anywhere around 6,000 tonnes.

Ketan Karane: Okay. So can we continue this 6,000 tonnes for FY2019 or would it be shrinking again because of constraints you may have?

Akshay S. Pitti: See, it won't be constraints that we have, it would be primarily because of the 6,000 tonnes would be purely that some of the production that we have done in Q3 will be shipped out in Q4 because of the changeover and the approval of the pollution control board coming because till that comes we cannot start shipping from our Aurangabad facility. We cannot do commercial invoicing.

Ketan Karane: Can we do, means what will be the guidance for FY2019, if I were to look at? As we have already capacity of 36,000 now which would be more modern and more workable? So, can we look at 24,000 or more than 24,000 tonnes per annum?

Akshay S. Pitti: I am more comfortable giving that number sometime in Q3-Q4, but if you want to extrapolate, you can extrapolate domestic to about 20,000 tonnes and exports to about 6,000 tonnes.

Ketan Karane: So that is around 26,000 tonnes.

Akshay S. Pitti: Yes.

Ketan Karane: So we should be able to do 26,000 tonnes and I am just extrapolating as you said, so this 380 crores turnover what we are targeting this year, so would it be turnover accretive also as we are moving to value-added products more than… So what are we looking at turnover, if you have some internal budget which have just, on a ballpark figure, I am not asking you to, as you mentioned your budgets are not done totally, so around Rs. 600 crores or Rs. 550 crores would be a right figure to just take for my guidance, for my view?

Akshay S. Pitti: I think it is better we discuss at Q3 conference call because we are still finalizing, it is very premature for us to give this number.

Ketan Karane: Okay. I just want to know what kind of volume growth are we looking at in FY2019 and FY2020 and what kind of revenue are we looking at, just which is the budgeted one and one more thing is, the EBITDA margin seem to be going up, other participant also told and you also told that around 16.5% would be stabilized margin by 2020. Is it possible that we may see better margins much more earlier than FY2020?

Akshay S. Pitti: See, it all depends on how quickly your customers start taking the product from us, which is meant for the higher value-added level. So if they start buying that product from tomorrow, you will see the improvement tomorrow, but based on our current order inputs and visibilities and forecast from the customers, we see that kick-in sometime in end of current year 18, so you will see the full impact in FY2019 and FY2020.

Ketan Karane: So that is the year when we should be seeing, I think then your view will be fully utilizing the capacity as far as I understand, I am making a wild guess over here, but it is an educated guess I am making for myself because…

Akshay S. Pitti: We would not be fully utilizing the capacity at all. See, in our business we can never utilize the full capacity.

Ketan Karane: Yes, I know because you can only utilize 80% of your capacity.

Akshay S. Pitti: 75-80%.

Ketan Karane: So would you be, means as what you have said that, will it be possible for you to expand the capacity with minimum additional Capex or you will require another Capex. As far as I understand from the talk, you should be doing another Capex to enhance the capacity by December 2018 or something like that.

Akshay S. Pitti: I don't foresee that happening, because as you know in our industry, the incremental capacities are very easily added at a very low cost.

Ketan Karane: So that is why I wanted to know what would be the additional cost if you just expand it by 50% or something like that. Just I want a ballpark figure if you expand it net.

Akshay S. Pitti: 50% is huge. If I have to expand it maybe 10-15% you are like small incremental capacity…

Ketan Karane: Let us say 20% capacity expansion then.

Akshay S. Pitti: Probably about Rs. 20-25 crores because the infrastructure is already there. The Aurangabad plant we have made in such a way that the overall space that we have is capable to do far more than what we are doing right now.

Ketan Karane: And just one of the last question before I come back again, what kind of order book we have besides GE and with GE. So are there visibility of the next 3 years order books with us or next 2 year visibility is there with us?

Akshay S. Pitti: See, for the Indian railways contract with GE, we have a visibility for 10 years.

Ketan Karane: Yes, that is Rs. 500 crores, I think if I am not wrong?

Akshay S. Pitti: Yes. Apart from that, we typically get a forecast of one year from them.

Ketan Karane: Okay sir. For the next year, what kind of order we are looking at?

Akshay S. Pitti: Next year order book, they will go by calendar year. Calendar year is just ending now. So we get their forecast for the next calendar year in January.

Ketan Karane: Okay, so in Q3 only you will be able to tell.

Akshay S. Pitti: Yes.

Ketan Karane: One more last question before I come back, will this GE order, what you are saying Rs. 50 crores per annum from next year fully for this year also, I don t know how much it will be? Will it be possible to shrink the time if GE requires the orders to be completed much more earlier?

Akshay S. Pitti: Definitely, we have already shrunk this time. If you see, it is stated to start from calendar year 2018. The very fact that we have started supplies in Q1 of current fiscal, we have already kind of pulled it in by one year.

Ketan Karane: Yes, because I was just picking one of these days, one of the Ministers who is also handling Railways happens to be my colleague when I was doing CA. Also, they were talking about shrinking this time to a much greater extent and the GE Chairman recently was on CNBC, also was telling the same thing. The Diesel locomotive order needs to be shrunk over a period of next 5 years only and not 10 years. That was the kind of indication they were talking. So is it possible to do that kind of thing?

Akshay S. Pitti: See, if the customer requires it, then we will definitely follow the customer. In our industry there is nothing that we can do. Whatever the customer requires we have to do.

Ketan Karane: Because they have categorically said that in next 5 year we want to complete this order. That Chairman of GE himself told who is the global Chairman, not even Indian Chairman.

Akshay S. Pitti: See, so far no such…

Ketan Karane: I agree, nothing would have been conveyed or something, but these are the things which are being talked. This is the projection of the government, they want to complete in next 5 years. Mr. Piyush Goyal who is the Minister of Railways has categorically stated twice, thrice on this point, when he went to Bihar also he said it recently. Just I am making a case for that kind of… Are we geared for that kind of capacity utilization immediately?

Akshay S. Pitti: Strictly speaking if we have to pull it down to half, then it will be difficult, it will require further investment. But if you have to advance to 10-15% or 20% that kind of buffer you always keep. This is advancing by double, like you are trying to shrink the timeline to half.

Ketan Karane: Yes, I know that.

Akshay S. Pitti: That kind of thing would require investments as and when there is any update from GE on that ground, then we will keep a….

Ketan Karane: I just want to, when I come back just can I have a ballpark figure on turnover we would be estimating in FY2019, just? Thanks, I will just come back again on the phone line. Thank you for the answers.

Moderator: Thank you. We have the next question from the line of Prabhash Anand, an Individual Investor. Please go ahead.

Prabhash Anand: Just in the line of previous participant, I just wanted to understand that electrification of railway route, 42% has already been done, so how this trend will impact our expected business from GE, Bihar located plant?

Akshay S. Pitti: I don't think it will have any impact of that. This is a diesel electric locomotive. So electrification does not really impact this. This is for freight. This is not for passenger railway. The other order that we are discussing with our client Alstom is for passenger rail which is the electric rail, not a diesel electric. In either of the two, our product goes the same. Like it is the same traction motor for both the product.

Moderator: Thank you. We have the next question from the line of Giriraj Daga from KM Visaria Family Trust. Please go ahead.

Giriraj Daga: Just a couple of follow-up. Like our export revenue is primarily GE business, right?

Akshay S. Pitti: Primarily GE, GE dominant.

Giriraj Daga Okay, because you mentioned Rs. 22 crores and total was also Rs. 22.7 crores only, so it is primarily like 97-98% or even 100% is GE only.

Akshay S. Pitti: Yes.

Giriraj Daga: And has that been trend for the last many quarters?

Akshay S. Pitti: See, that is a historical fact with the company.

Giriraj Daga: First domestic realization looks very high, even if we assume that GE is only 3 crores in the domestic revenue, okay? The second point is that, then it has also led to the higher EBITDA margin overall for the company with the gross margin has grown up to almost 75,000 per tonne and EBITDA margin at 27,000 per tonne which is historically high levels for us. I am looking at last almost 20 quarters now.

Akshay S. Pitti: I didn't understand how you have bifurcated that.

Giriraj Daga No, the gross margin will be EBITDA of the total company.

Akshay S. Pitti: Yes, and you are dividing that by the total tonnage?

Giriraj Daga: Total tonnage.

Akshay S. Pitti: So, that is also to do with not just GE, right? You are focusing this point on the GE domestic business, apart from GE also we do the value-added stuff like core dropping stator frame for Emerson machining.

Giriraj Daga: The idea of asking is that the realization number has started going up only from the fourth quarter onwards. I am talking about the domestic realization, it was 1,13,000 in the third quarter, then 1,41,000 in the fourth quarter, 1,62,000 in the first quarter and 1,68,000 in the second quarter. So by the time our GE that locomotive contract started, that number has started moving up. So what is the coincidence that it happen in such a manner?

Akshay S. Pitti: No, it is not just GE, that is what I am trying to say. It is just coincidental that the GE India's order has kind of started at that particular point of time. Apart from that, the company has also started supplying value-added assemblies to various other customers including Siemens, Emerson, Cummins at different value add levels. So it is not just plain vanilla laminations, it is assembled laminations, it is various different things which bring the total revenue. We report in tonnage terms because that is why so to speak an equalizer for all. On the base tonnage, you can do a different level of value add.

Giriraj Daga: Understand. Just to get the underlying thing clear, there is no one-off in any of the last quarter number?

Akshay S. Pitti: No, not at all.

Giriraj Daga: All are recurring numbers.

Akshay S. Pitti: Yes. See, I mean the product mix will change. What I am again and again trying to say the product mix will change. Today, Siemens is say buying one type of lamination with fully assembled and some kind of machining on it. Tomorrow if they get a different kind of order from their client, they may just buy the lamination because that may not require the same type of value addition. Nothing is ever one-off. It is repetitive. But the quantum of each particular item in the product mix will change from quarter-to-quarter and month-to-month also. We have similar kind of realization level continuing. We see a more value-added product profile going forward than plain vanilla laminations.

Giriraj Daga: Understood. That is quite happening. Second, like what would be the share of GE from the domestic market like, and why I am asking this question will be, how it will impact our working capital also?

Akshay S. Pitti: See for domestic business, if GE's rate will not really impact our working capital because that will be transferring of some of the international business to the domestic plant.

Giriraj Daga: So we will not be cutting down on like freight, as I said lead distance time, travel time…

Akshay S. Pitti: That will just help a little bit, maybe what 40 days to that extent.

Giriraj Daga: Yes, but 40 days is a large number, right?

Akshay S. Pitti: Yes, but the quantum division gets shifted from their American and Mexican facility through India is very small. See, what will be for GE India loco was never ever going to the US and Mexico plant. It is the altogether new business that they have got, right, which GE has got and we have got. So it is a new business for India. So it is currently going to their Indian plant is some part of the Indian Railways contract and some part of the global requirement which we doing as a trial case. So that small Rs. 2-3 crores, we will get a little bit of reduction which is not very significant.

Giriraj Daga: Okay. Understood. What will be sort of first half Capex and what is the full year guidance on Capex on FY2018 and FY2019, if you can throw?

Akshay S. Pitti: More or less finished all the Capex in this H1. For FY2019, we are not having any guidance on Capex. It maybe just small Rs. 4-5 crores kind of maintenance type of CAPEX.

Giriraj Daga: What was the first half Capex we incurred?

NK Khandelwal: Total Capex by the end of the year would be about Rs. 130 crores **in** FY2018.

Giriraj Daga: And you have mentioned about like FY2020 revenue of Rs. 600 crores just a thought process number. What kind of volume we are targeting that level?

Akshay S. Pitti: Somewhere around 27,000-28,000 tonnes of lamination with a very high level of value addition.

Giriraj Daga: Okay. I understood. Because you are expecting that the value addition should increase by almost 20% from here also because last quarter your realization was Rs. 180 and you are targeting overall about Rs. 220 kind of a number?

Akshay S. Pitti: Yes.

Moderator: Thank you. We have the next question from the line of Shashank Kanodia from ICICI Securities. Please go ahead.

Shashank Kanodia: So some color on the infusion of funds from the promoter group, in terms of pure equity?

NK Khandelwal: Presently it has come by way of unsecured loan only.

Akshay S. Pitti: It is pending conversion from some formality with stock exchange. I think it should get completed by March.

Shashank Kanodia: Okay. So what is the quantum that the promoters are looking at infusing the funds?

NK Khandelwal: Totally it has come which we have in the note also, about Rs. 40.6 crores has come from the promoters as unsecured loans.

Shashank Kanodia: Okay. So this entire quantum you tend to convert into the equity, right?

NK Khandelwal: Yes, part of it will be in the equity, part will be the share warrants which will be subsequently converted.

Shashank Kanodia: Okay. Any price range at which the stake will get converted?

NK Khandelwal: We had originally estimated somewhere in early 2017 that we may allot it up to 90 or as per SEBI Guidelines. At that time, 90 looked to be a fair enough estimate. Today I think that is also gone due to time lapse in approval process. So let us see how the Board further decides.

Shashank Kanodia: Okay, you are mentioning Rs. 90 a share?

Akshay S. Pitti: We had estimated it to be up to 90, sometime in early 2017.

Shashank Kanodia: Right, sir what it the prevailing scrap prices in the domestic market?

Akshay S. Pitti: For our kind of scrap, we get a slightly lower realization because it is unconcentrated scrap. It is very loose, I don't know the word to use it, it is not very dense.

Shashank Kanodia: So will it be just something like Rs. 25-27 a kg kind of a thing?

Akshay S. Pitti: About Rs. 2.5 less than the prevailing scrap rate for heavy melting, as they call it. If you see Metals and Minerals Review, there is a magazine which publishes the rate. Typically if you try to historically benchmark it, we realize about Rs. 2- 2.5 less than that.

Shashank Kanodia: Okay. So last realized scrap value for us would be how much realization?

Akshay S. Pitti: About Rs. 22.

Shashank Kanodia: Rs. 22 a kg?

Akshay S. Pitti: Yes. Ours is ex-works and without any credits. So when you talk of Rs. 25, that is obviously with some kind of credit and delivered with loading and unloading. The rate that we quote is ex-works, cash on delivery.

Shashank Kanodia: Sir, there is also some increment in terms of net working capital cycles, right? So reduction, both in terms of debtors and increase in creditors. So what is sustainable net working capital cycle that you are looking at, so is there any concentrated effort to reduce that?

Akshay S. Pitti: See, most ideal working capital cycle for us would be about 150 days. Beyond that, we would see how we can reduce it. The only way we can reduce it is by either offering our clients, some kind of discount for early payment or kind of factoring the bills, which both come at a cost. So at current turnover, we are comfortable with that leverage profile. Going forward as the turnover increases, probably we will have to you know kind of do some kind of bill factoring or some kind of cash discount because we will not be able to get that kind of working capital limits going forward and also the debt leverage will become very high which is not viewed kindly by investors.

Shashank Kanodia: Okay. And on the debt fund, you said that it is almost sitting at the peak, right?

Akshay S. Pitti: Long term debt is sitting at the peak.

Shashank Kanodia: Okay, so FY2019, in terms of absolute debt how do you see the trajectory going forward?

Akshay S. Pitti: See, like I just mentioned a minute ago that as the turnover increases we will have to strike a right combination of cost and debt. We will have to start some kind of factoring of receivables or some kind of cash discount to clients and strike a sweet spot to manage the debt. As of now, we have not targeted that. You can expect about 150 working capital days for the projected turnover of FY2019.

Moderator: Thank you. We have the next question from the line of Sunny Agarwal from PNB Investment Services Limited. Please go ahead.

Sunny Agarwal: What is the opportunity we see because of this electric vehicle segment, both on lamination and motor side?

Akshay S. Pitti: See, let me give you a background on this. Today we already supply lamination for traction motors for heavy vehicles. For off highway vehicles, which are powered by diesel electric technology for traction, we already supply laminations and motor frame assemblies for these products. Now we are trying to expand that into the electric vehicles for passenger and mass transits, say buses and so on and so forth. So we are exploring the opportunities. We are in touch with couple of people who are manufacturing these motors. So as it develops, we will let you know.

Sunny Agarwal: Okay. But opportunity phases will be humongous, far higher than the existing opportunity which we see, I mean on the heavy vehicle as well as on the passenger vehicle. So I believe the opportunity on passenger vehicle that will be far higher than the heavy vehicle side.

Akshay S. Pitti: Definitely, it all depends on how quickly the electric vehicle is kind of popular in the world and in India as well. So as of now the percentage of the electric vehicles on the road is very small and we don't see that increasing in the near term as well. So as and when that market develops, the opportunity will be huge. Definitely we are one of the leading suppliers of laminations and laminations are required in every electric vehicle. So we are already in touch with people who are manufacturing these motors for electric vehicles, so that we position ourselves well as and when this technology gets picked up.

Moderator: Thank you. We have the follow up question from the line of Kaustav Bubna from SKS Capital and Research. Please go ahead.

Kaustav Bubna: Just wanted to get a sense, because these numbers according to me aren't adding up. So you know I just wanted to know if you are being conservative because you are already doing 14.5% EBITDA margin and your GE order, domestic is only Rs. 3 crores, plus you are saying that you will see a very high level of value-added products in your 28,000 tonnes expected volume in FY2020.It seems like it has been based on what you are saying and the EBITDA target you have given and since you have been little conservative. Is that right, is that your approach in general?

Akshay S. Pitti: There are two points. Firstly, we have been slightly conservative, not very conservative. Secondly in the next 2 years, we see our operational cost increased, like there will be a significant increase in manpower cost, you have already seen that in Q2, our employee cost is up 27% and as we keep going for the value-added component, the employee cost will go up because there is no outside material that you are procuring and putting into the component. The value add has been done by our labour. So we will have a significant increase in overhead cost. So that will kind of eat up little bit of the number that is not adding up that you are saying, that

16.5% but you are projecting, probably you are seeing 1.5%-2% kind of a difference. So that will get eaten up by higher employee cost. So we are trying to factor that and you know be conservative and say it today.

Kaustav Bubna: Okay, fair enough. And just also on your revenue opportunity of Rs. 600 crores, just wanted to understand whatever actually taken into this because your opportunity in general from a domestic perspective and the changes that are happening in this country is massive because of whatever you may attribute it to, but this electric vehicles and shift to the B2C model which can be huge too because that market is huge. So what is we see, I mean that could amount to way more than Rs. 600 crores of revenue. Now what is Aurangabad facility doesn't have enough capacity to cater to this, let us say this sudden huge demand comes into a lapse. Then if you put yourself ahead, how would you see, also one year down the line you will see, or 1-2 years down the line you see position improving. So you know you will be able to increase Capex through your internal approvals and so how do we see, if we get this opportunity to a lapse, how do we see Capex plans or expansion in general?

Akshay S. Pitti: I think with the Capex matched out today, as time goes by, the term loan would get repaid and we will have again the headroom to borrow further and there will be internal accruals as well to fund any opportunity that comes our way. As far as the revenue potential goes, like you rightly observed, Rs. 600 crores is a very low number, it can grow much higher. But we are again not trying to simply chase the topline, we are trying to be balanced in our approach for protecting good EBITDA margin and having a decent size turnover. The appliance business as everyone knows is going to be a lower margin business. So we don't want to kind of weigh into that very heavily. We want to keep it at a certain percentage of our sales. We don't want to try and chase the turnover target and then you know compromise our bottom-line.

Kaustav Bubna: So I know this is a tough question, but just to get a broad perspective, out of this Rs. 600 crores of revenue that are projecting in FY2020, could you somehow give us a broad sectorial breakup as to where your revenues would be coming in the domestic market, out of the Rs. 600 crores of revenues. Could you somehow give us a broad range of sectoral breakup like x amount of percent from wind, x amount from auto, x amount from industrial?

Akshay S. Pitti: At a broad level, I would say about Rs. 75 crores would come from the locomotive business. About Rs. 100 crores to Rs. 150 crores would be exports which should again be into some form of mining of highway Oil and Gas Locomotive. That would be one segment. Apart from that, about Rs. 50 crores-60 crores would come from white goods or equivalent to white goods. When I say equivalent to white goods, I mean like medium sized motors which are not really for industrial use but they are not even for like domestic use. They are somewhere in between. The rest of it would come from power generation and by power generation I mean wind, hydro, thermal and stationary power like DG Set and industrial. Now the mix between these things I cannot today give you.

Kaustav Bubna: And this is also you have not shown this Rs. 600 crores are not accounting for any electric vehicles?

Akshay S. Pitti: No, not at all. I mean it would be insignificant to even talk about it. In the next 2-3 years in India, electric vehicles, even though there is a significant excitement, I think the technology does not exist.

Kaustav Bubna: Well, that is the future to basically something…

Akshay S. Pitti: Yes. Electric vehicle is 5-year and beyond kind of horizon.

Kaustav Bubna: And are we on track?

Akshay S. Pitti: For any significant revenue, let me qualify that by saying for any significant revenue.

Kaustav Bubna: I know. Then we would obviously have to do incremental Capex over that opportunity if it never came up.

Akshay S. Pitti: Yes.

Kaustav Bubna: But one more question is that, on this merger that we are doing, is everything going fine. I know it is tough to say, but from the time we last spoke that means last conference call to now…

Akshay S. Pitti: No. We have discussed that. We are looking for M&A in a space which is suitable to us.

Kaustav Bubna: No, I mean about the merger of Pitti Castings.

Akshay S. Pitti: No, there is no talk of merging Pitti Castings.

Kaustav Bubna: Okay. There is no talk and what about the acquisition?

Akshay S. Pitti: For acquisition, like we said last time that we are still looking for an opportunity. If the opportunity arises in a good space, we will look at it.

Moderator: Thank you. We have the next question from the line of SK Goenka from YG Commercial Private Limited. Please go ahead.

SK Goenka: My question is actually regarding the tonnage for Q3 and Q4, we have done about 9,500 tonnes in the first half and 6,000 is what we said is likely to be done in the fourth quarter. And you said you also would want to maintain the target of 22,000 for the year. Is that right? Actually that will mean the third quarter to be very high.

Akshay S. Pitti: No, 6,000 for domestic for fourth quarter.

SK Goenka: No, so on an overall basis, 9,500 is what we have done in first half combined domestic and exports.

Akshay S. Pitti: Yes.

SK Goenka: And for the year we were guiding for about 22,000 for the year, full, domestic and exports.

Akshay S. Pitti: Yes, 18,000 and 4,000.

SK Goenka: Yes, so about 22,000. So that leaves us with about 12,500.

Akshay S. Pitti: Yes.

SK Goenka: Then we said 6,000 domestic only for the fourth quarter you meant, is it?

Akshay S. Pitti: Yes. Let me summarize it this way. We have done about 7,500 tonnes in domestic and about 1,500 tonnes in exports. So Q3 we are seeing these shipments to be lower because of our shift from Hyderabad and Pune to Aurangabad. So we would be making up our domestic tonnage by shipping out the materials which we will not be able to ship in the month of December and January. The reason for the disruption is to firstly we are uprooting the capacity in Pune and Hyderabad and transferring it to Aurangabad and apart from that, we are not able to do commercial invoicing over there because we are still awaiting our consent for operation from the pollution control board which was expected shortly. So whatever is this inventory build up, we will be liquidating it in Q4. So in terms of shipments, it will be in Q4, the domestic shipments.

SK Goenka: Okay, the overall guidance of 22,000 shipment billing will continue for the year?

Akshay S. Pitti: We are estimating it to be continuing. Maybe it may have a 3-4% or 5% kind of variants which is normal. So it may be about 21,000 to 22,000 somewhere in that range. But domestic about 18,000, we are still confident and we are holding that guidance.

SK Goenka: Okay. See another question is about the margins. So we are at about 14.1% in H1 of this year. You expect this to be at least this or slightly better for the full year as well in FY2018?

Akshay S. Pitti: It would be similar.

SK Goenka: Okay, because we were talking about a better value mix, so I thought it may improve in the next two quarters, thereby improving it by a few basis points or whatever.

Akshay S. Pitti: The value mix will significantly start improving from January onwards and as the India loco order kicks-in in full volume. So Q4 you will see a significant improvement.

SK Goenka: Thank you. I have got one more question. In the earlier presentation, we read about the capacity of the company to be increased to about 50,000 tonnes over a period of time, lamination capacity. Currently we are at about 36,000 is what we saw from the presentation. So do you have any roadmap for that because you said that on the Capex side you have already capped out, so how is this plan to be achieved, I mean if I am reading it correctly?

Akshay S. Pitti: No. We have not said 50,000. See, we are trying here 36,000, out of which about 75% to 80% is utilizable capacity. Once we kind of near 30,000 tonnes-32,000 tonnes of operating level, we will look at a further Capex.

SK Goenka: Okay. No, I think I read in the June presentation, maybe there was an error or mistake in that, that you planned to increase it to 50,000 tonnes over a period of time. Anyway, thank you very much.

Moderator: Thank you. Ladies and gentlemen, that was the last question. I now hand the conference over to Mr. N. R. Ganti for closing comments. Thank you and over to you sir.

N. R. Ganti: Thank you for participating so actively. Any further doubts, please do reach out through Churchgate Partners. Thank you.

Moderator: Thank you very much. Ladies and gentlemen, on behalf of Pitti Laminations Limited that concludes this conference. Thank you for joining us and you may now disconnect your lines.

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Note: This transcript has been edited to improve readability

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